

UC Berkeley

UC Berkeley Electronic Theses and Dissertations

Title

How Do Firms Mitigate Conflicts Among Creditors During Bankruptcy?

Permalink

<https://escholarship.org/uc/item/29g9w1w4>

Author

Hwang, Jinsung

Publication Date

2023

Peer reviewed|Thesis/dissertation

How Do Firms Mitigate Conflicts Among Creditors During
Bankruptcy?

By
Jinsung Hwang

A dissertation submitted in partial satisfaction of the
requirements for the degree of
Doctor of Philosophy
in
Business Administration
in the
Graduate Division
of the
University of California, Berkeley

Committee in charge:

Professor Panos N. Patatoukas, Chair
Professor Sunil Dutta
Professor Omri Even-Tov
Professor Xi Wu
Professor Kenneth Ayotte

Summer 2023

© 2023

Jinsung Hwang

All rights reserved

Abstract

How Do Firms Mitigate Conflicts Among Creditors During
Bankruptcy?

By

Jinsung Hwang

Doctor of Philosophy in Business Administration

University of California, Berkeley

Professor Panos N. Patatoukas, Chair

The aim of my research is to understand how firms alter their debt structure and accounting policy in response to strengthening some creditors' rights. To this end, I examine the impact of the Anti-recharacterization law, which enhances the rights of securitization creditors, on firms' debt concentration and financial reporting. By considering the conflict of interest between creditors during bankruptcy, I find that the legal reform leads firms to concentrate their debt structure (e.g., by using fewer types of debt or contracting with fewer creditors) in order to mitigate creditors' coordination costs in bankruptcy. This effect is more pronounced for firms experiencing financial distress, with low re-deployable assets, poor disclosure quality, and high accounts receivable. Additionally, firms' financial reporting becomes more conservative after the reform in an effort to compensate other creditors and improve their chances of recovering their claims to prevent coordination failure in bankruptcy. This effect is more pronounced for firms in financial distress, with high re-deployable assets, and high accounts receivable. Overall, my results highlight how firms attempt to mitigate the risk of creditors' coordination failure in bankruptcy.

Table of Contents

1. Introduction.....	1
2. Anti-Recharacterization Statute in Bankruptcy	8
3. Research Design	10
3.1. Data.....	10
3.2 Propensity score matching.....	11
3.3 Methodology.....	12
3.4. Measure	14
3.5. Identifying the SPV	17
4. Empirical Results.....	18
4.1 Descriptive Statistics	18
4.2 Trend in SPV use.....	18
4.3 Visual Examination and the Parallel Trend Condition	19
4.4 Debt Concentration and Anti-recharacterization.....	19
4.4.1 Debt Contract and Anti-recharacterization	20
4.4.2 Anti-recharacterization, Debt Structure, and Distress Risk	21
4.4.3 Anti-recharacterization, Debt Structure, and Asset Redeployability	22
4.4.4 Anti-recharacterization, Debt Structure, and Accounting Quality	23
4.4.5 Anti-recharacterization, Debt Structure, and Account Receivable	24
4.5 Financial Reporting Policy and Anti-recharacterization	24
4.5.1 Anti-recharacterization, Accounting conservatism, and Bankruptcy Risk	26

4.5.2 Anti-recharacterization, conservatism, and Asset redeployment	27
4.5.3 Anti-recharacterization, conservatism, and Account Receivable	28
5. Conclusion	29
References.....	30
Appendix 1.....	34
Appendix 2.....	36
Appendix 3.....	37
Table A1	56
Table A2	57
Table A3	58
Table A4	59
Table A5	60
Table A6	61
Table A7	62
Table A8	63
Table A9	64
Table A10	65
Table A11	66
Table A12	67
Table A13	68
Table A14	69
Table A15	70
Table A16	71
Table A17	72

Table A18	73
Table A19	74
Table A20	75
Table A21	76

List of Figures

Figure 1. The proportion of SPV over Time	40
Figure 2. The parallel trend of Debt Concentration (HHI) over time	41
Figure 3. The parallel trend of Conservatism (Timely Loss Recognition) over time	42
Figure 4. The parallel trend of Conservatism (Timely Loss Recognition) over time	43

List of Tables

Table 1	44
Table 2	45
Table 3	46
Table 4	47
Table 5	48
Table 6	49
Table 7	50
Table 8	51
Table 9	52
Table 10	53
Table 11	54
Table 12	55

1.Introduction

There has been a considerable amount of research conducted on the effect of creditor protection on financial development and economic growth. Many studies, including those by La Porta et al. (1998), King and Levine (1993), and Beck et al. (2000), have found that ownership protection, particularly in credit markets, can promote financial development by decreasing the cost of borrowing. This is believed to be due to the ability of creditors' rights to enable creditors to effectively enforce their contracts. However, some research in the area of bankruptcy has suggested that creditor rights may be excessive and result in post-bankruptcy inefficiencies, such as a liquidation bias (as seen in the work of Aghion, Hart, and Moore (1992) and Hart et al. (1997)). Given these mixed findings, it is important to consider how far the law should go in protecting the interests of creditors.

The Anti-recharacterization law (AR law) strengthens the rights of certain creditors, specifically those who lend money to firms through Special Purpose Vehicles (SPVs). Under this law, secured creditors who lend through SPVs can seize collateral with greater certainty in bankruptcy. However, other creditors do not have this same ability. According to Chapter 11 of the US Bankruptcy Code, secured lending collateral is subject to an automatic stay, which can delay or prevent creditors from repossessing the collateral. Prior to the implementation of the AR law, assets owned by a firm's SPV were not subject to the automatic stay due to the bankruptcy-remote nature of SPVs, unless the court recharacterized the assets transferred to the SPV as a loan rather than a true sale. Recharacterization could occur during Chapter 11 proceedings if the court determined that the collateral was essential to the originator's operations during the restructuring process. However, as recharacterization became more common, there were lobbying efforts by the banking and securitization industries to prevent it (Kettering, 2008). To address this issue, some states passed anti-recharacterization laws that limit judges' ability to recharacterize collateral pledged through SPVs as assets of the company in Chapter

11 bankruptcy proceedings. Therefore, the AR law enhances creditor protection by allowing secured SPV creditors to repossess their collateral without the constraint of the automatic stay when a firm files for bankruptcy.

I examine the impact of the Anti-recharacterization law (AR law) on firms' debt structure and financial reporting policy. The AR law serves as a positive exogenous shock to the rights of securitization creditors (those who lend through Special Purpose Vehicles) in bankruptcy proceedings. By improving the control rights of these creditors, the AR law may increase the risk of creditor coordination failure due to conflicts of interest among creditors during bankruptcy. In my study, I investigate how firms respond to this risk by altering their debt structure and financial reporting policy. Specifically, I seek to understand how firms attempt to mitigate the risk of creditors' coordination failure through these means.

In this study, I first examine the relationship between firms' debt structure and creditor coordination failure in bankruptcy, which can be caused by conflicts of interest among creditors. In perfect markets with rational investors, the Modigliani-Miller model (1958) suggests that a firm's value would be insensitive to its capital structure. And this model assumes that bankruptcy is costless and does not impact a firm's capital structure. Since then, several researchers have sought to incorporate the concept of bankruptcy costs into the capital structure framework, but there is still ongoing debate about the relevance of these costs to firms' debt structure.

One of the objectives of optimizing debt structure is to minimize bankruptcy costs. Aghion et al. (1992) argue that a major obstacle to debt financing is the collective enforcement problem that can arise from coordination failure among creditors in bankruptcy, which is driven in part by conflicts of interest among different claim holders. Conflict among different groups of debt holders can also impact capital structure (Welch, 1997; Bris and Welch, 2005; Hackbarth and Mauer, 2012). Firms with higher expected bankruptcy costs may benefit from specializing in borrowing from a single lender in order to reduce

coordination costs, while firms with lower expected bankruptcy costs may choose to diversify their debt by borrowing from multiple creditors in order to take advantage of lower debt costs. Bolton and Scharfstein (1996) formalize the idea that an optimal debt structure should minimize expected bankruptcy costs. They propose that firms with low credit quality can maximize liquidation value by borrowing from a single creditor, while firms with high credit quality can minimize the likelihood of default by borrowing from multiple creditors. However, it is unclear how improving control rights for certain creditors, such as SPV creditors, affects creditors' coordination and how this increased conflict of interest impacts firms' optimal debt structure. In this study, I examine how empowering SPV creditors, who become the most senior debtholders, affects firms' debt choices.

The increased control rights of SPV creditors, as granted by the Anti-recharacterization law, may lead firms to concentrate their debt structure in order to mitigate the potential coordination failure among creditors during bankruptcy. This is due to the fact that the other existing debt becomes subordinated, and the balance sheet may become skewed towards riskier assets, potentially increasing the risk of default and expected loss for other creditors. The use of multiple debt types may also increase coordination costs among creditors, which may be priced into the market by sophisticated investors. To address these potential bankruptcy costs, firms may choose to concentrate their debt structure.

The results of my study indicate that firms respond to a legal reform that strengthens the rights of securitization creditors by concentrating their debt structure, likely in an effort to mitigate creditors' coordination failure during bankruptcy. This effect is particularly pronounced in firms that are experiencing financial distress, have low re-deployable assets, poor disclosure quality, and high levels of accounts receivable. These findings suggest that strengthening creditors' rights can have significant impacts on firms' debt structures and highlight the importance of considering the potential consequences of such legal changes.

It is predicted that firms with a heightened probability of default will be particularly concerned with the issue of creditors' coordination failure. Thus, it is expected that such firms, characterized by a high risk of bankruptcy, will be more inclined to concentrate their debt structure in an effort to reduce creditors' coordination costs in bankruptcy. The bankruptcy risk was measured using a z-score, and the results indicate that the impact is more pronounced for firms with a high level of distress risk, as indicated by a low z-score. The aim is to minimize the costs associated with bankruptcy.

Asset redeployment plays a crucial role during the bankruptcy process, as the re-deployability of assets can significantly impact the recovery rate for creditors. Kim and Kung (2016) establish that firms possessing high re-deployable assets exhibit higher recovery rates, which is desirable as it enhances the ease of agreement among creditors, who expect to recover their collateral with a high degree of probability. On the other hand, firms with low re-deployable assets will face more conflict between creditors, as it becomes difficult for creditors to recover their claims, and they are more likely to be involved in the restructuring process, which increases the likelihood of disagreement among creditors. As a result, firms with low re-deployable assets are more likely to incur creditors' coordination costs and to concentrate their debt structure in an effort to mitigate such costs. In this research, the industry asset re-deployability measure, as established by Kim and Kung (2016), was utilized. The results indicate that the effect of the law is more pronounced for firms with low re-deployable assets.

The quality of a company's accounting information is crucial in the bankruptcy process, as it allows stakeholders to evaluate the firm's situation effectively, leading to an efficient restructuring. According to Li et al. (2020), firms with poor accounting quality tend to concentrate their debt structure to reduce coordination costs between creditors. Li et al. (2020) argue that high-quality accounting information enables creditors to make informed decisions, reducing coordination costs. On the other hand, firms with low accounting quality are more concerned about coordination costs as creditors are less likely to agree with low-

quality information. As a result, these firms are more likely to concentrate their debt structure to mitigate these costs. I used the disclosure quality measure from Chen et al. (2015), who defined it as the level of detail in the accounting line items disclosed in a company's annual report. I found the effect to be stronger for firms with low disclosure quality after the Anti-recharacterization law.

The use of special purpose vehicle (SPV) financing is more common for companies with a high volume of accounts receivable. As a result, these firms are more likely to concentrate their debt structure in an effort to mitigate the costs associated with bankruptcy. I have found that this effect is particularly pronounced for firms with high accounts receivable after the Anti-Recharacterization Law was implemented.

I have found that the Anti-Recharacterization Law results in increased coordination costs among creditors and firms respond by concentrating their debt structure. Next, I will examine the impact of the law on firms' financial reporting policies. A conservative approach to financial reporting recognizes negative economic shocks more quickly in earnings compared to positive shocks. This conservativeness in accounting results in a more rapid recognition of covenant violations following negative shocks (Zhang 2008). This enables creditors to assert control rights and preserve firm value before the debtor is unable to make payments. This also reduces agency conflicts between senior creditors, as preserving assets before default reduces the incentive for junior creditors to delay settlement in hopes of extracting value from senior creditors during bankruptcy proceedings. If a sufficient value exists before bankruptcy, then junior creditors bear the costs of losing investment opportunities and settlement costs from delay.

The study by Donovan et al. (2015) shows that creditors of firms with more conservative accounting prior to default have higher recovery rates. Previous research suggests that secured creditors tend to have better recovery rates in bankruptcy because they can exert control over the proceedings. Following the implementation of the Anti-recharacterization law, firms are more likely to use SPV financing,

putting existing creditors at a disadvantage. Hence, existing creditors may require increased accounting conservatism to enhance their recovery rates, particularly if the value of the assets securing their claims decreases. As a result, firms become more conservative in their reporting after the AR law to compensate existing creditors and improve coordination in bankruptcy.

The findings indicate that the implementation of the reform led to a more conservative approach in the financial reporting of firms in an effort to placate creditors and reduce the risk of coordination failure in case of bankruptcy. The effect was stronger for firms in financial distress, with limited re-deployable assets, and high accounts receivable.

Firms that are at high risk of bankruptcy are more likely to adopt a conservative financial reporting policy in order to compensate their creditors and reduce creditors' coordination costs. This is due to the need to mitigate the expected bankruptcy costs. To test this hypothesis, I use the Z-score to measure bankruptcy risk, and my findings suggest that financial reporting is more conservative when the bankruptcy risk is high.

Firms that have highly re-deployable assets are expected to have a high recovery rate, reducing creditors' coordination costs, according to Kim and Kung (2016). These firms are likely to receive better treatment from creditors, who expect a higher probability of recovering their collateral. On the other hand, firms with low re-deployable assets will face greater conflict among creditors over the collateral and are expected to experience an increase in these conflicts after the Anti-Recharacterization Law. To mitigate these increased costs, such firms are more likely to adopt a conservative approach to financial reporting. This paper employs the industry asset re-deployability measure as per Kim and Kung (2016) and finds that the effect of the AR law on accounting conservatism is more pronounced for firms with low re-deployable assets.

Firms that have high accounts receivable are more likely to utilize SPV financing as it is the main asset that can be transferred to

the SPV. The greater use of SPV financing by these firms puts other creditors at a disadvantage, and to compensate for the increased expected bankruptcy cost, these firms adopt more conservative accounting practices. The results of the study show that firms with high accounts receivable become more conservative in their financial reporting after the implementation of the Anti-Recharacterization Law.

This study makes several contributions to the existing literature in the fields of law and finance, creditors' rights, bankruptcy, financial reporting policy, and accounting conservatism. Firstly, the study adds to the literature that has established creditors' rights as a key determinant of credit market development by highlighting their significance in the context of the Anti-Recharacterization Law. Secondly, the study argues that strong creditor rights may not always be beneficial to borrowers, thus, providing a new perspective on the topic. Thirdly, the study provides evidence of firms' behavior in the event of expected coordination failure between creditors arising from conflicting interests, thereby contributing to the bankruptcy literature. Fourthly, the study adds to the literature on financial reporting policy by providing evidence on the benefits of accounting conservatism to debt holders, specifically, in terms of recovering control rights on collateral. Lastly, the study investigates factors associated with bankruptcy resolution, providing insight into how conservatism can be used to mitigate coordination failure among creditors.

The structure of the paper is as follows: Section 2 provides a background on the Anti-Recharacterization Law, Section 3 outlines the research methodology, Section 4 presents the empirical results, and finally, Section 5 concludes the paper with a discussion of the findings.

2. Anti-Recharacterization Statute in Bankruptcy

The process of corporate asset securitization involves the creation of a special purpose vehicle (SPV) by an originator company. This SPV is a legally separate entity from the originating company and is created specifically for the purpose of carrying out specific financing transactions. The originator company will then transfer securitization assets, such as account receivables, to the SPV. The SPV can then borrow money, either directly or through the use of a trust, and pass the funding back to the originator company. One of the key benefits of securitization financing is the feature of bankruptcy remoteness, which means that the assets held by the SPV are not considered part of the originator company's bankruptcy estate. This feature is highly valued by creditors, and as a result, the outstanding volume of asset-backed securities in the U.S. was more than \$1.5 trillion in 2019.

Asset securitization in non-financial firms is primarily focused on financing against account receivables, as noted in studies by Kettering (2008) and Lemmon et al. (2014). The outcome of receivables securitization is economically similar to a loan that is secured by those receivables. However, their main difference is that the securitization structure eliminates the constraints imposed by the bankruptcy code on a secured loan creditor, specifically the expected loss arising from the power of the bankrupt company, as debtor in possession, to obtain the use of any cash collected from the secured loan collateral. This is in line with the findings of Gorton and Souleles (2006), who highlight the bankruptcy remoteness feature of securitized debt as a key advantage of securitization financing.

In receivable securitization, the originator company transfers the ownership of collateral to a special purpose vehicle (SPV). This transfer of ownership to a legally separate entity is the underlying mechanism that causes the bankruptcy remoteness feature of securitized debt. Therefore, to maintain the bankruptcy avoidance protection, it is crucial for the securitization structure that courts treat the ownership transfer to the SPV as a "true sale" of assets and do not recharacterize it as a

secured loan. The importance of recharacterization to securitization is such that rating agencies evaluate the credit quality of asset-backed debt based on whether the transfer is going to be considered a true sale or a secured loan, as highlighted in a study by Ayotte and Gaon (2011).

Under specific circumstances, courts apply recharacterization in a securitization setting. Specifically, when courts believe that the consequences of exercising recharacterization could be in the interest of both the debtor and the general public, judges have a strong argument to recharacterize receivables' sales. Accordingly, the application of recharacterization is highly likely when a bankrupt company claims that proceeds from receivables are necessary for its successful reorganization and judges conclude that society would benefit more from the organization of the bankrupt firm than the liquidation.

To avoid recharacterization in cases where it is easily justifiable by courts, considerable legal efforts were exercised, and finally, the Anti-Recharacterization (AR) statute was enacted, entirely precluding the possibility of the recharacterization in a securitization transaction (Ketting (2010)). The AR statute gives securitization creditors the right to retain swift and complete access to SPV assets in case of the originator firm's bankruptcy, even when SPV assets are needed to support the reorganization.

Anti-recharacterization law (AR law) improves the rights of creditors in the sense that secured creditors can seize the collateral with certainty in bankruptcy. This only applies to the creditor who lends the money to the firm through Special Purpose Vehicle. (Firms can establish SPV and borrow money by putting the asset in the SPV (e.g., account receivable) as collateral) On the other hand, other creditors cannot seize their collateral (automatic stay) when the firm files for bankruptcy. In other words, AR law increases the creditor's rights in the sense that secured SPV creditors can repossess their collateral without automatic stay when a firm goes bankrupt.

3. Research Design

3.1. Data

The sample for this study was constructed by starting with all publicly traded U.S. firms in the COMPUSTAT database, and excluding financial firms and regulated utilities. Financial firms were excluded by identifying them based on their Standard Industrial Classification (SIC) codes between 6000 and 6999, and regulated utilities were excluded by identifying them based on their SIC codes between 4900 and 4999. It was also important to have information on the state of incorporation for each firm included in the sample, so only firms incorporated in the 50 U.S. states and the District of Columbia were included. Anti-recharacterization laws, which are laws that protect the true sale nature of securitization, were adopted by different states between 1997 and 2005. To take into account this variation in the adoption of the laws, the sample period was restricted to the years 1992-2010. This time frame allows including a five-year period before the first adoption of anti-recharacterization laws and a five-year period after the last adoption. All data related to debt structure, such as the type of debt and the amount of debt, was obtained from Capital IQ. The data obtained from Capital IQ was used to analyze the effect of anti-recharacterization laws on the debt structure of firms.

In order to study the use of special purpose vehicles (SPVs) for securitization financing by firms, data was collected from the firms' 10-K filings with the Securities and Exchange Commission's EDGAR database. The 10-K filing is an annual report that companies are required to file with the SEC and it provides a comprehensive overview of the company's financial performance and condition. By examining the 10-K filings, it is possible to identify if a firm has used an SPV for securitization financing. To analyze the data, a dummy variable was created which indicates whether a firm had used an SPV for financing at any point in its history. The variable is equal to one if a firm initiates an SPV at least once in its lifetime, and it is equal to zero if a firm did not use SPV financing. This variable allows to identify the firms in the

sample that used SPV financing. The data analysis shows that nearly 40% of firms in the sample utilized SPV financing at some point in their history. This indicates that a significant proportion of firms in the sample had used this type of financing mechanism, providing insights on the extent of the usage of SPV financing among the firms in the sample. Additionally, this information can be used to analyze the impact of this financing mechanism on the firms' financial performance, capital structure and other aspects.

3.2 Propensity score matching

The study employs a technique called propensity score matching (PSM) in order to rule out concerns that the results may be driven by selection bias. The decision of a firm to initiate an SPV for financing is likely to be endogenous and firms that use securitization programs may have different characteristics from those that do not benefit from such programs. In an ideal setting, the study would randomly assign firms to treatment and control groups and then compare the consequences of the securitization program on the two groups. However, it is not possible to observe the outcome of a firm using SPVs had it not chosen to employ a securitization structure in the real world. The PSM strategy matches each firm in the treatment group (firms that use securitization programs) with a firm in the control group (firms that do not use securitization programs) that have the same likelihood of using a securitization program ex-ante. The PSM model is estimated using a probit regression, where the dependent variable is a dummy variable that takes the value of one for securitization users and zero for non-users. The control variables in the probit model include the natural logarithm of book assets, market-to-book ratio, leverage, profitability, tangibility, cash flow ratio, year and industry dummies. The matching is applied without replacement and the maximum difference in the propensity score allowed for a match is 0.01. This allows to control for the characteristics of firms that use securitization programs and those that do not, in order to obtain a more accurate and unbiased analysis of

the impact of securitization programs on firms.

3.3 Methodology

I follow an “on-off” approach in the estimation strategy because of the 2003 federal court ruling. In 2003, *the Reaves Brokerage Company, Inc. v. Sunbelt Fruit & Vegetable Company, Inc.* case dealt a blow to pledgibility. In this case, the court recharacterized the debtor’s transfer and prevented the creditors from seeking recovery after the debtor filed for bankruptcy. The importance of the case is that the court completely ignored the anti-recharacterization statute of Texas and used a federal standard to determine the nature of the sale. This specific court decision increases the likelihood that federal law will preempt state-level property rights when the debtor goes bankrupt. Therefore, the effect of passing an anti-recharacterization law at the state level shortly before or after this case law should be limited. Indeed, in the seven years following this court case, it served as a cited precedent in sixty-two other bankruptcy cases. Thus, the case created substantial uncertainty surrounding state-level safe harbors for secured lending.

According to the “on-off” approach, the “on” period includes years after a state passes anti-recharacterization laws, but before 2004. I do not include 2004 and the following years because of the 2003 federal court ruling that created substantial uncertainty around these laws. To be more specific about the treatment variable, for a firm incorporate or head-quartered in Texas or Louisiana, the “on” period consists of 1997 to 2003, whereas the “off” period consists of 1992 to 1996 and 2004 to 2009. For a firm incorporated or headquartered in Alabama, the “on” period consists of 2001 to 2003, whereas the “off” period consists of 1992 to 2000 and 2004 to 2009.

I follow Li et al. (2016) to first define the treatment variable Law as follows: Law equals 1 if the firm is incorporated in Texas, Louisiana, Alabama, Delaware, South Dakota, Virginia, or Nevada, 7 states that passed anti-recharacterization law.

I estimate a difference in difference specification as follows:

$$Y_{ijt} = a_i + a_t + b * Law_{jt} + X_{it-1} + e_{it}$$

where Y is the variable of interest of firm i incorporated in state j and year t (e.g., Debt Concentration, Accounting conservatism) and a_i is the firm fixed effect, a_t is the year-fixed effect and X is a vector of control variables. In this setting b is the difference-in-difference estimate, which captures the effect of anti-recharacterization laws on debt concentration and accounting conservatism. Because the independent variable of interest is measured at the incorporation state level, I cluster the standard error by incorporation state.

3.4. Measure

I measure the concentration of debt structure within a company using two methods. First, I adopt the approach of Colla et al. (2013) and calculate the normalized Herfindahl-Hirschman Index (HHI) across various debt types utilized by the firm. I categorize seven distinct types of debt, as outlined below. For a given firm i at the end of year t , I calculate:

$$SS_{it} = \left(\frac{CP_{it}}{TD_{it}}\right)^2 + \left(\frac{DC_{it}}{TD_{it}}\right)^2 + \left(\frac{TL_{it}}{TD_{it}}\right)^2 + \left(\frac{SBN_{it}}{TD_{it}}\right)^2 + \left(\frac{SUB_{it}}{TD_{it}}\right)^2 \\ + \left(\frac{CL_{it}}{TD_{it}}\right)^2 + \left(\frac{OTHER_{it}}{TD_{it}}\right)^2$$

CP: Commercial Paper, *DC*: Drawn credit lines, *TL*: Term loans, *SBN*: Senior bonds and notes, *SUB*: Subordinated bonds and notes, *CL*: Capital leases, *OTHER*, *TD*: Total Debt

I then normalize SS_{it} to obtain:

$$HHI_{it} = (SS_{it} - \frac{1}{7}) / (1 - \frac{1}{7})$$

The Herfindahl-Hirschman Index (HHI) is designed to have a range of values between zero and one. If a company uses all seven types of debt in equal amounts, the HHI would be equal to zero, representing the minimum level of debt concentration. On the other hand, if the firm uses only a single type of debt, the HHI would equal one, indicating the maximum debt concentration.

As an alternative measure of debt concentration, I use a dummy

variable, *Excl90*, for firm *i* in year *t*. *Excl90* is defined as follows: it takes the value of 1 if the firm acquires at least 90% of its debt from a single debt type, and 0 otherwise.

In addition to HHI, I also measure debt concentration by counting the number of different debt types in a firm's debt structure, which I label as *NUM DEBT TYPE*. *NUM DEBT TYPE* takes into account the seven distinct types of debt outlined previously, and its value ranges from one to seven. A higher value of *NUM DEBT TYPE* indicates a debt structure that is less concentrated.

To measure accounting conservatism at the industry level, I employ the measure of timely loss recognition, following the work of Ball, Bushman, and Vasvari (2008) and Wittenberg-Moerman (2008). It is believed that firms with more conservative financial reporting are less likely to report losses ex-post and that debtholders, who are common providers of collateralized capital, are more sensitive to the borrower's losses. Thus, conservative accounting practices can improve access to credit markets. Wittenberg-Moerman (2008) supports this idea by showing that firms with a higher level of timely loss recognition have lower costs for debt financing.

I adopt the industry-level calculation of timely loss recognition, as presented in Wittenberg-Moerman (2008), using Basu's (1997) method at the three-digit SIC level. This measure eliminates the risk of endogeneity, as it is calculated at an industry level. For every three-digit SIC industry-year combination in Compustat, I perform a linear regression analysis of annual price-deflated earnings (NI_{it}) on annual stock returns (R_{it} , ending three months after the fiscal year) and the interaction between stock returns and a dummy variable for negative returns (DR_{it}).

$$NI_{it} = b_0 + b_1 DR_{it} + b_2 R_{it} + b_3 R_{it}DR_{it} + u_{it}$$

TLR is measured as the sum of b_2 and b_3 . This industry-level measure

of timely loss recognition is then assigned to each firm in a given industry.

In the determination of conservatism, there has been significant discussions about the measurement biases of conditional conservatism. Dutta et al. (2021) suggested that special item is the least biased measurement of conditional conservatism. Hence, I have employed special item ($spi - xido$) divided by total assets, following the findings of Dutta et al. (2021), as the measure of conservatism.

3.5. Identifying the SPV

In this paper, a crucial aspect is to limit the sample of firms to only those that utilize Special Purpose Vehicles (SPVs) for financing purposes. Not identifying and limiting the sample in this manner may lead to problematic results as less than 50% of the total population of firms use SPVs. This is in contrast to prior studies that did not specifically identify firms using SPVs for financing and instead assumed that most firms utilized them. I have taken great care to classify and only include firms that have been confirmed to use SPVs in my sample for analysis.

To accurately identify these firms, I utilized the Securities and Exchange Commission's (SEC) EDGAR database to search through the 10-K filings of the sample firms, collecting information on each firm's use of SPVs. Adopting the methods of Feng et al. (2009) and Lemmon et al. (2012), I employed the use of a Python program to count the number of subsidiaries or affiliates listed in Exhibit 21 or Exhibit 22 with names that contain "Limited Partnership", "Limited Liability Partnership", "Limited Liability Corporation" (or their acronyms "L.P.," "LP," "LLP," "L.L.P.," "LLC," "L.L.C."), or "trust." Additionally, I searched 10-Ks for keywords such as "sale of receivable", "securitize", "securitization", "special purpose", "off-balance sheet", and "purchase program" to cross-check the firms usage of SPV for financing purposes. Through this methodical process, I was able to identify and limit the sample to only those firms that utilize SPVs, ensuring that the results of the analysis are not biased.

4. Empirical Results

4.1 Descriptive Statistics

Table 2 presents the descriptive statistics, which are adjusted for the top and bottom 1% by year using the winsorization. The average values of HHI, NUM DEBT TYPES, TLR, and Special Items are consistent with previous studies. The data indicates that debt concentration is relatively high, with an average of 70%. The number of debt types used by companies is also limited, with an average of 2.1. The average value of TLR is 0.347, which is similar to previous studies. The average value of special items is 0.246, which is a substantial portion compared to extraordinary items and discontinued operations (XIDO), suggesting that special items play a crucial role in financial reporting. The other control variables also have reasonable distributions in line with previous literature.

4.2 Trend in SPV use

In this study, the focus is on firms that finance their operations through Special Purpose Vehicles, as they are the ones most impacted by the Anti-recharacterization law. The purpose is to assess if firms' use of SPVs is substantial enough for the law to have a meaningful effect. The frequency of firms' use of SPVs is documented over time, as seen in Figure 1, and it increases from 10% to 30% from 1994 to 2010. This indicates that SPV is a common means of financing during the sample period and the impact of the law could be significant. Further, the study compares the number of SPVs used before and after the Anti-recharacterization law and finds that the use of SPVs increased after the law, implying that the law has a clear impact on firms' decisions to use SPVs. This shows that the sample size is sufficient for analysis and provides initial evidence that the Anti-recharacterization law affects firms' use of SPVs.

4.3 Visual Examination and the Parallel Trend Condition

This section presents a visual analysis of key variables to determine if they have parallel trends, which is a critical aspect of conducting a difference in difference analysis. Figure 1 shows the trend of debt concentration, with results suggesting that before the event date, both treated and control groups had a similar trend, but after the event date, treated firms had a more concentrated debt structure compared to the control group, indicating a rise in debt concentration post-event. Similarly, Figure 2, depicting the level of accounting conservatism as measured by Timely Loss Recognition, exhibits a parallel trend before the event date with a noticeable increase in conservatism for the treated firms after the event date. The same can be seen in Figure 3, which measures conservatism through the special item ratio, where it also displays a parallel trend. These findings fulfill the conditions for difference in difference regressions, thereby implying that the Anti-recharacterization law has a clear impact on treated and control firms.

4.4 Debt Concentration and Anti-recharacterization

In this section, I explain how AR law can increase the likelihood of coordination costs during bankruptcy and how firms try to mitigate this expected coordination failure between creditors. After the AR law, I explain why firms with SPV will suffer from the creditors' coordination failure. As SPV debt holders become to have priority on the collateral, the other existing debt holders effectively become subordinated, and firms usually put low-risk assets such as accounts receivable as collateral for SPV financing where it leads Firms' balance sheets to become tilted towards riskier assets. This will put other existing creditors at risk of claiming their collateral when the firm goes into bankruptcy. Because this may increase the risk of default for existing creditors and/or the expected loss. For these firms, contracting

with multiple creditors or debt types simultaneously can thus increase creditors' coordination costs because of the different incentives and risks each creditor has. And investors in the debt market price bankruptcy cost as the benefit of bankruptcy remote feature of SPV is lost, which investors have positively valued. To mitigate such expected costs, the company has the incentive to contract with a smaller number of creditors or use fewer types of debt type so that firms can efficiently communicate with creditors during the bankruptcy. Therefore, I argue that debt structure becomes more concentrated to mitigate the bankruptcy costs arising from the cost of coordination and the probability of default. Table 3 shows the effect of the law on debt concentration. I find that debt concentration increases and the number of debt types (i.e., lowering the number of creditors) decreases after the law. (1.5 % increase in HHI, 7% decrease in the number of debt types). This is consistent with the prediction that debt structure becomes more concentrated to mitigate the bankruptcy costs arising from the cost of coordination and probability of default after the law.

4.4.1 Debt Contract and Anti-recharacterization

This section examines how debt contracts changed after the law by looking at a change in the use of secured debt and the cost of debt. This analysis is important because it shows how creditors and firms change their view on the debt contract. For example, as creditors other than SPV creditors are put at disadvantage in terms of recovering the collateral, creditors will price in and the cost of debt will increase accordingly. And after the law, firms will have less incentive to use the secured debt as it could increase the bankruptcy cost and possibly because of the increase in the cost of secured debt. Firms have more incentive to choose their financing through SPV. For this reason, firms will be less likely to use the secured debt and the cost of debt will increase as investors that are put at disadvantage requires compensation. Table 4 shows how debt contract changes after the law. In column (1), I found that firms use 12.5% less secured debt. This is in the line with

lowering the expected coordination failure risk by contracting with a smaller number of creditors. In column (2), the cost of debt increases by 4.2%, suggesting that the debt holder price this bankruptcy cost for compensation.

4.4.2 Anti-recharacterization, Debt Structure, and Distress Risk

In this section, I show the subsample analysis. Table 3 shows that the AR law affects firms' decision on debt for the overall sample and it brings to the question of which subset of companies will have the most effect from the AR law. AR law is bankruptcy law and it is most likely that firms that face bankruptcy would care more about the implication of the law. Therefore, firms with a high probability of default will likely concern with creditors' coordination failure. I predict that firms with a high probability of bankruptcy risk will be more likely to concentrate on the debt structure to lower the creditors' coordination costs. I measured the default risk using the Altman z-score and split the sample into two by z-score. Table 5 shows that firms with a high probability of default will be more likely for firms to concentrate on the debt structure to lower the creditors' coordination cost. The effect is more pronounced for firms with high distress risk (low z-score) to mitigate bankruptcy costs and compensate creditors at a disadvantage. In columns (6) and (7), results show that the firm increases the HHI by 3.2%, 7.2% decrease in the number of debt type, and column (8), 6.3% increase in firms that concentrate their debt by more than 90%. In column (9), 2.7% decrease in the use of secured debt, and column (10), a 5.3% increase in the cost of debt when firms are facing bankruptcy risk. However, results are statistically not significant for firms with low bankruptcy risk.

4.4.3 Anti-recharacterization, Debt Structure, and Asset Redeployability

During the bankruptcy process, the main interest of creditors is to recover their collateral. Asset redeployment is important during the bankruptcy process as re-deployability can determine the recovery rate for creditors. Kim and Kung (2016) find that firms with high re-deployability assets exhibit higher recovery rates. A higher recovery rate is important because creditors can reach an agreement easily as creditors will expect to claim their collateral with a high probability. After the AR law, I expect that coordination costs increase and this cost can be mitigated if the collateral or assets in the firms can be easily in sale for liquidation, the process of agreement between creditors can be easily settled as creditors can expect to recover their collateral. Asset re-deployability is measured as industry-level re-deployability. Table 6 shows that firms with low re-deployability assets (likely to have a low recovery rate) will concentrate on the debt structure to lower the creditors' coordination cost. This is because firms with low re-deployable assets will likely have more conflict between creditors as it would be harder for creditors to recover their claim and creditors are more likely to be involved in the restructuring process, which will be more likely to cause disagreement on opinions. In table 6 column (6), results show that firms concentrate debt by 1.6%, and in column (7), 1.13% decrease in the number of debt types, and column (8), a 3.6% increase in firms that uses certain debt of more than 90%, with low re-deployable assets. In column (9) and (10), the use of secured debt and cost of debt does not change. And for firms with high asset re-deployability, results for debt concentration show insignificant results. Overall, the results are in line with the prediction that firms with a low re-deployability asset will likely experience higher coordination failure after the AR law and firms concentrate on the debt structure to mitigate such cost.

4.4.4 Anti-recharacterization, Debt Structure, and Accounting Quality

In this section, I show how accounting quality plays a role in creditors' coordination cost between creditors after the AR law. Accounting information is important during bankruptcy because interested parties can easily assess and get a better sense of firms' fundamentals when firms have high accounting quality. Li et al. (2020) find that firms with low accounting quality have a more concentrated debt structure to mitigate coordination costs. This is because high accounting quality minimizes the coordination cost between creditors by giving better quality information for creditors to understand better about the firm. After the AR law, firms with high accounting quality can provide creditors with better information regarding firms' current standing and creditors can more likely reach a consensus on the firm's restructuring plan. Following Chen et al. (2015), I measure accounting quality as a level of disaggregation of accounting line items in firms' annual reports. Table 7 shows that firms with high accounting quality will likely have lower bankruptcy costs and the effect of AR law is less pronounced for firms with high accounting quality. The results show that in column (6), firms concentrate debt by 1.6%, in column (7), 8.13% decrease in the number of debt type, in column (8), 3.4% increase in firms that uses certain debt more than 90%, with low disclosure quality. However, results are statistically not significant for firms with high accounting quality. The results are in line with the prediction that firms with higher accounting quality will suffer less creditors' coordination costs after the AR law.

4.4.5 Anti-recharacterization, Debt Structure, and Account Receivable

In most cases, the company transfers account receivable in SPV for financing and it is more likely that firms with more account receivable will be more likely to use SPV for financing. In other words, firms with more accounts receivable will have more incentive and ability to use SPV for financing. And using more SPV financing will be more likely to increase the coordination cost after the AR law and firms will concentrate on the debt structure to mitigate the cost. Table 8 shows that firms with high account receivable will be more likely to adopt more conservative financial reporting. It shows that in column (1), 3.5% increase in debt concentration, in column (2), -7.6% decrease in the number of debt types, in column (3), 2.6% increase in firms with more than 90% debt concentration, in column (4), -3.3% decrease in secured debt after the law for the firms with high account receivable. However, it is not statistically significant for firms with low account receivable. The results are consistent with the prediction that firms with high account receivable will likely have SPV financing and firms will be more likely to mitigate the bankruptcy cost by concentrating and adopting more conservative financial reporting policies.

4.5 Financial Reporting Policy and Anti-recharacterization

Given that I find that the legal reform, Anti-recharacterization Law, increases the creditors' coordination cost and firms try to mitigate the such cost by concentrating the debt structure, next I examine how firms' financial reporting policy changes after the AR law. When financial reporting is conservative, negative economic shocks are more quickly recognized in earnings than positive shocks. Conservatism accounting leads to more rapid covenant violations following negative shocks (Zhang 2008). Through timely covenant violation, creditor gain access to control rights and preserve firm value before the debtor is

unable to make required payments. The creditor can use these rights to preserve the remaining assets. Furthermore, if more assets are preserved before default, then agency conflicts between senior creditors can be reduced. Junior creditors have less incentive to delay settlement in hope of extracting value from senior creditors during bankruptcy proceedings, because if a sufficient value exists before bankruptcy, then junior creditors bear the costs of losing investment opportunities and settlement costs arising from delay.

Donovan et al. (2015) find that creditors of firms with more conservative accounting before default have significantly higher recovery rates. Prior literature suggests that secured creditors experience significantly higher recovery rates than other creditors classes in bankruptcy due to their ability to exert control over the bankruptcy proceedings. In this paper, I argue that firms are more likely to use SPV financing after the AR law and this leads other existing creditors at disadvantage. Therefore, existing creditors may demand more accounting conservatism to increase the recovery rate, especially if the expected value of assets securing their claims becomes lower. And this leads to better creditors' coordination in the bankruptcy process. I measure conservatism in two ways, timely loss recognition, and special item ratio. For timely loss recognition, it is a commonly used firm-year measure derived from the Basu conservatism model. And I used special item ratio as there has been discussion about whether measures for conservatism are biased or not and special item ratio is the least biased firm-year measure according to the prior literature (Dutta et al. 2020) Consistent with the prediction, Table 9, column (1) and (2) shows that accounting conservatism increases by 3.5% for TLR and by 6.4% after AR law. This shows that firms' financial reporting become more conservative after the law to favor the creditors where they are concerned with the low recovery of collateral.

4.5.1 Anti-recharacterization, Accounting conservatism, and Bankruptcy Risk

In this section, I show the subsample analysis to examine the impact of the Automatic Stay (AR) law on firms' decisions regarding financial reporting policies. As demonstrated in Table 9, the AR law has a significant effect on the financial reporting policies of firms in the overall sample. This raises the question of which subset of companies will be most affected by the AR law. It is likely that firms that are facing financial difficulties and a high probability of bankruptcy will be particularly concerned about the implications of the AR law. In order to test this hypothesis, I measure the default risk of the sample firms using the Altman z-score and divide the sample into two groups: firms with a high probability of default and firms with a low probability of default.

Table 10 provides evidence that firms with a high probability of default are more likely to focus on their debt structure in order to lower the costs associated with creditors' coordination failure. This effect is particularly pronounced for firms with high distress risk (low z-score), as they seek to mitigate the costs of bankruptcy and compensate creditors who may be at a disadvantage. Results in column (3) show that the TLR increases by 2.5% and in column (4) firms' use of the special item ratio increases by 12.3% when the firm is facing bankruptcy risk. However, the results are statistically not significant for firms with low bankruptcy risk. This supports the prediction that firms with high bankruptcy risk will be more likely to adopt conservative financial accounting policies in order to compensate other creditors and thereby mitigate the expected costs of bankruptcy.

4.5.2 Anti-recharacterization, conservatism, and Asset redeployment

During the bankruptcy process, creditors are primarily focused on recovering their collateral. One important aspect of this process is the re-deployability of assets, as it can greatly impact the recovery rate for creditors. Previous research, such as the study by Kim and Kung (2016), has found that firms with high re-deployability assets tend to have higher recovery rates. A higher recovery rate is beneficial as it makes it easier for creditors to reach agreements, as they can expect to recover their collateral with a high probability.

With the implementation of the Anti-Recharacterization law, it is expected that coordination costs will increase. However, these costs can be mitigated if the collateral or assets of the firm are easily able to be sold for liquidation, as this allows for a more efficient agreement between creditors. In this study, asset re-deployability is measured at the industry level. Table 11 column (3) shows that the TLR increases by 6.7%, and in column (4) the use of special item ratio increases by 2.6%. This suggests that firms with low re-deployability assets (low recovery rate) will adopt a more conservative accounting policy in order to lower coordination costs for creditors. This is likely due to the fact that firms with low re-deployable assets are more prone to conflicts among creditors and are more likely to be involved in the restructuring process, which can lead to disagreements and difficulties in reaching agreements. However, the results of this study are statistically not significant for firms with high asset re-deployability.

4.5.3 Anti-recharacterization, conservatism, and Account Receivable

The study finds that in most instances, companies transfer their accounts receivable to a Special Purpose Vehicle (SPV) for financing purposes, and that firms with a higher amount of accounts receivable are more likely to use SPVs for financing. Table 12 illustrates this by showing that firms with high levels of accounts receivable tend to adopt more conservative financial reporting policies. Column (1) demonstrates a 17.6% increase in the TLR after the law for firms with high accounts receivable, and Column (2) shows a 14.7% increase in the special item ratio after the law. However, these results are only statistically significant for firms with low accounts receivable.

The findings are consistent with the prediction that firms with high accounts receivable will likely have SPV financing and that firms will be more likely to mitigate the costs of bankruptcy by concentrating their debt structure and adopting more conservative financial reporting policies. However, the results are not statistically significant for firms with low accounts receivable. Overall, these results provide insight into the relationship between firms' accounts receivable and their financing and reporting practices, and demonstrate the impact of the law on these practices.

5. Conclusion

The paper examines the causal relationship between creditor rights and conflicts of interest on a firm's debt structure and financial reporting policy. Utilizing the Anti-recharacterization statute as a natural experiment, this research aims to identify exogenous shocks to the rights of securitization creditors in order to understand the impact on firms. The findings reveal that the legal reform led firms to streamline their debt structure in order to reduce the coordination costs for creditors during bankruptcy. This effect was particularly pronounced in firms that were experiencing financial distress, had limited re-deployable assets, poor disclosure quality, and high accounts receivable. The rationale behind this is that firms with these characteristics are more vulnerable to coordination failures in bankruptcy, thus, they are more likely to take actions to mitigate the coordination costs. Additionally, the research discovered that financial reporting became more conservative post-reform as a means of compensating other creditors and avoiding coordination failures in bankruptcy. These effects were most pronounced in firms experiencing financial distress, limited re-deployable assets, and high accounts receivable. The reason behind this is that firms with these characteristics are more likely to be in a weaker financial position and are more likely to be affected by coordination failures in bankruptcy, thus, they are more likely to take actions to compensate the other creditors in order to prevent coordination failure. Overall, this study sheds light on the unintended consequences of granting more control rights to certain creditors and the associated costs for firms in terms of conflicts of interest and coordination failures among creditors during bankruptcy. The results of this research provide valuable insights for policymakers, regulators and stakeholders in the financial industry on how to design and implement laws and regulations that balance the rights of different groups of creditors and minimize the costs for firms.

References

- Aghion, P. and Bolton, P., 1992. An incomplete contracts approach to financial contracting. *The review of economic Studies*, 59(3), pp.473-494.
- Aghion, P., Hart, O. and Moore, J., 1992. The economics of bankruptcy reform (No. w4097). National Bureau of Economic Research.
- Altman, E.I., 1984. A further empirical investigation of the bankruptcy cost question. *The Journal of Finance*, 39(4), pp.1067-1089.
- Ayotte, K.M. and Morrison, E.R., 2009. Creditor control and conflict in Chapter 11. *Journal of Legal Analysis*, 1(2), pp.511-551.
- Ayotte, K. and Gaon, S., 2011. Asset-backed securities: costs and benefits of “bankruptcy remoteness”. *The Review of Financial Studies*, 24(4), pp.1299-1335.
- Ball, R., Bushman, R.M. and Vasvari, F.P., 2008. The debt-contracting value of accounting information and loan syndicate structure. *Journal of accounting research*, 46(2), pp.247-287.
- Balakrishnan, K., Core, J.E. and Verdi, R.S., 2014. The relation between reporting quality and financing and investment: Evidence from changes in financing capacity. *Journal of Accounting Research*, 52(1), pp.1-36.
- Beck, T., Levine, R. and Loayza, N., 2000. Finance and the Sources of Growth. *Journal of financial economics*, 58(1-2), pp.261-300.
- Bolton, P. and Scharfstein, D.S., 1996. Optimal debt structure and the number of creditors. *Journal of political economy*, 104(1), pp.1-25.
- Bris, A. and Welch, I., 2005. The optimal concentration of creditors. *The Journal of Finance*, 60(5), pp.2193-2212.
- Chen, S., Miao, B. and Shevlin, T., 2015. A new measure of disclosure quality: The level of disaggregation of accounting data in annual reports. *Journal of Accounting Research*, 53(5), pp.1017-1054.
- Chu, Y., 2020. Collateral, ease of repossession, and leases: Evidence

from antirecharacterization laws. *Management Science*, 66(7), pp.2951-2974.

Colla, P., Ippolito, F. and Li, K., 2013. Debt specialization. *The Journal of Finance*, 68(5), pp.2117-2141.

Donovan, J., Frankel, R.M. and Martin, X., 2015. Accounting conservatism and creditor recovery rate. *The Accounting Review*, 90(6), pp.2267-2303.

Dutta, S. and Patatoukas, P.N., 2017. Identifying conditional conservatism in financial accounting data: Theory and evidence. *The Accounting Review*, 92(4), pp.191-216.

Dutta, S., Patatoukas, P.N. and Wang, A.Y., 2020. Identifying the roles of accounting accruals in corporate financial reporting. *Journal of Accounting, Auditing & Finance*, p.0148558X211035224.

Ersahin, N., 2020. Creditor rights, technology adoption, and productivity: Plant-level evidence. *The Review of Financial Studies*, 33(12), pp.5784-5820.

Favara, G., Gao, J. and Giannetti, M., 2021. Uncertainty, access to debt, and firm precautionary behavior. *Journal of Financial Economics*.

Feng, M., Gramlich, J.D. and Gupta, S., 2009. Special purpose vehicles: Empirical evidence on determinants and earnings management. *The Accounting Review*, 84(6), pp.1833-1876.

Hackbarth, D. and Mauer, D.C., 2012. Optimal priority structure, capital structure, and investment. *The Review of Financial Studies*, 25(3), pp.747-796.

Hart, O., Drago, R.L.P., Lopez-de-Silanes, F. and Moore, J., 1997. A new bankruptcy procedure that uses multiple auctions. *European economic review*, 41(3-5), pp.461-473.

Kettering, K.C., 2008. True sales of receivables: A purpose analysis. *Am. Bankr. Inst. L. Rev.*, 16, p.511.

Kim, H. and Kung, H., 2017. The asset redeployability channel: How

- uncertainty affects corporate investment. *The Review of Financial Studies*, 30(1), pp.245-280.
- King, R.G. and Levine, R., 1993. Finance and growth: Schumpeter might be right. *The quarterly journal of economics*, 108(3), pp.717-737.
- Li, N., Lou, Y., Otto, C.A. and Wittenberg-Moerman, R., 2021. Accounting quality and debt concentration. *The Accounting Review*, 96(1), pp.377-400.
- Li, S., Whited, T.M. and Wu, Y., 2016. Collateral, taxes, and leverage. *The Review of Financial Studies*, 29(6), pp.1453-1500.
- Lou, Y. and Otto, C.A., 2020. Debt heterogeneity and covenants. *Management Science*, 66(1), pp.70-92.
- Lemmon, M., Liu, L.X., Mao, M.Q. and Nini, G., 2014. Securitization and capital structure in nonfinancial firms: An empirical investigation. *The Journal of Finance*, 69(4), pp.1787-1825.
- Patatoukas, P.N. and Thomas, J.K., 2011. More evidence of bias in the differential timeliness measure of conditional conservatism. *The Accounting Review*, 86(5), pp.1765-1793.
- Patatoukas, P.N. and Thomas, J.K., 2016. Placebo tests of conditional conservatism. *The Accounting Review*, 91(2), pp.625-648.
- Porta, R.L., Lopez-de-Silanes, F., Shleifer, A. and Vishny, R.W., 1998. Law and finance. *Journal of political economy*, 106(6), pp.1113-1155.
- Souleles, N.S. and Gorton, G.B., 2007. 12. Special Purpose Vehicles and Securitization (pp. 549-602). University of Chicago Press.
- Von Thadden, E.L., Berglöf, E. and Roland, G., 2010. The design of corporate debt structure and bankruptcy. *The Review of Financial Studies*, 23(7), pp.2648-2679.
- Vig, V., 2013. Access to collateral and corporate debt structure: Evidence from a natural experiment. *The Journal of Finance*, 68(3), pp.881-928.

Warner, J.B., 1977. Bankruptcy costs: Some evidence. *The journal of Finance*, 32(2), pp.337-347.

Welch, I., 1997. Why is bank debt senior? A theory of asymmetry and claim priority based on influence costs. *The Review of Financial Studies*, 10(4), pp.1203-1236.

Wittenberg-Moerman, R., 2008. The role of information asymmetry and financial reporting quality in debt trading: Evidence from the secondary loan market. *Journal of Accounting and Economics*, 46(2-3), pp.240-260.

Zhang, J., 2008. The contracting benefits of accounting conservatism to lenders and borrowers. *Journal of accounting and economics*, 45(1), pp.27-54.

Zhang, Z., 2009. Recovery rates and macroeconomic conditions: The role of loan covenants. In *AFA 2010 Atlanta Meetings Paper*.

Appendix 1 Key Variable Definitions

Variable	Winsorize	Definition
<i>Firm Characteristics</i>	<i>[1P, 99P]</i>	
Profitability		Operating income before depreciation / Total assets
Dividend Payer		Dummy = 1 if common stock dividends are positive
Cash Holdings		Cash and short-term investments/Total assets
Tangibility		Net property, plant, and equipment (PPENT)/Total assets
Asset Maturity		$\text{Current asset}/(\text{Current asset} + \text{PPENT}) * (\text{Current asset}/\text{COGS}) + \text{PPENT}/(\text{current asset} + \text{PPENT}) * (\text{PPENT}/\text{Depreciation and amortization})$
R&D Expense		Research and Development expenses/Total assets
Book Leverage		Total Debt/Total Asset
Unrated		Dummy = 1 if a firm is not rated by the S&P
M/B		$(\text{MB equity} + \text{Total Debt} + \text{Preferred stock liquidating value} - \text{Deferred taxes and investment tax credit})/\text{Total asset}$
CF Volatility		Standard Deviation of quarterly operating income over previous 12 quarters scaled by total assets
Z-score		$Z = 0.012X1 + 0.014X2 + 0.033X3 + 0.006X4 + 0.999X5$; X1 = Net Working Capital/AT, X2 = Retained Earnings/TA, X3 = Earnings before interest and taxes/TA, X4= MVE/book value of total liability, X5 = Net sales/TA
Asset Redeployability		The industry asset re-deployability measure (Kim and Kung 2017)
Cost of debt (COD)		Interest Expense (XINT)/Total Debt

Size	Total Asset
<i>Debt Structure [1P, 99P]</i>	
HHI	Debt concentration
Excl90	Dummy = 1 if a firm has more than 90% of its total debt in one debt type (CP, DC, TL, SBN, SUB, CL, or Other), and 0 otherwise
NUM DEBT	Number of different debt types in a firm's debt structure.
Secured Debt	Ratio of secured debt to total debt
<i>Accounting Variables [1P, 99P]</i>	
Disclosure Quality	Level of disaggregation of accounting line items in firms' annual reports. (Chen et al. (2015))
Timely Loss Recognition (TLR)	Accounting conservatism where for each three-digit SIC industry-year in Compustat, I estimate the piecewise linear regression $NI = b_0 + b_1DR + b_2R + b_3R*DR + u$ where sum of b_2 and b_3 is conservatism measure
Special Item	Special Item/XiDO

Appendix 2
Adoption year of Anti-recharacterization law by states

State	Year Adopted
Texas	1997
Louisiana	1997
Alabama	2001
Delaware	2002
South Dakota	2003
Virginia	2004
Nevada	2005

Appendix 3.
**Delaware Asset-Backed Securities Facilitation Act (from the State
of Delaware official website.)**

§ 2701A. Title.

This chapter may be cited as the “Asset-Backed Securities
Facilitation Act.”

73 Del. Laws, c. 214, § 1;

§ 2702A. Intent.

It is intended by the General Assembly that the term “securitization
transaction” shall be construed broadly.

73 Del. Laws, c. 214, § 1;

§ 2703A. Securitization transaction.

(a) Notwithstanding any other provision of law, including, but not
limited to, § 9-506 of this title, “Debtor’s right to redeem
collateral,” as said section existed prior to July 1, 2001, and § 9-

623 of the title, "Right to redeem collateral," which became effective July 1, 2001, to the extent set forth in the transaction documents relating to a securitization transaction:

(1) Any property, assets or rights purported to be transferred, in whole or in part, in the securitization transaction shall be deemed to no longer be the property, assets or rights of the transferor;

(2) A transferor in the securitization transaction, its creditors or, in any insolvency proceeding with respect to the transferor or the transferor's property, a bankruptcy trustee, receiver, debtor, debtor in possession or similar person, to the extent the issue is governed by Delaware law, shall have no rights, legal or equitable, whatsoever to reacquire, reclaim, recover, repudiate, disaffirm, redeem or recharacterize as property of the transferor any property, assets or rights purported to be transferred, in whole or in part, by the transferor; and

(3) In the event of a bankruptcy, receivership or other insolvency proceeding with respect to the transferor or the transferor's

property, to the extent the issue is governed by Delaware law, such property, assets and rights shall not be deemed to be part of the transferor's property, assets, rights or estate.

(b) Nothing contained in this chapter shall be deemed to require any securitization transaction to be treated as a sale for federal or state tax purposes or to preclude the treatment of any securitization transaction as debt for federal or state tax purposes or to change any applicable laws relating to the perfection and priority of security or ownership interests of persons other than the transferor, hypothetical lien creditor or, in the event of a bankruptcy, receivership or other insolvency proceeding with respect to the transferor or its property, a bankruptcy trustee, receiver, debtor, debtor in possession or similar person.

It is not the purpose of this chapter to change the tax treatment of securitizations that take place pursuant to this chapter.

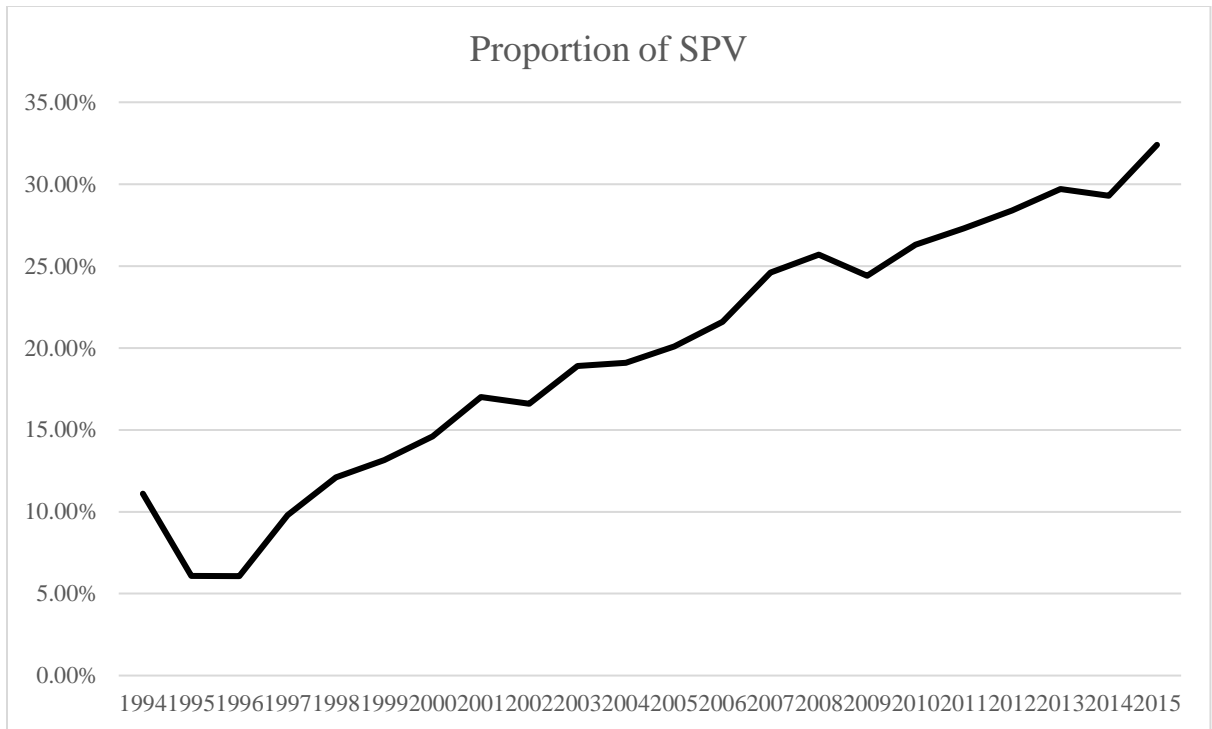


Figure 1. The proportion of SPV over Time

This figure shows the proportion of firms with SPV over time from 1994 to 2015.



Figure 2. The parallel trend of Debt Concentration (HHI) over time

This figure shows a parallel trend of debt concentration of firms with SPV before and after the passage of the law.

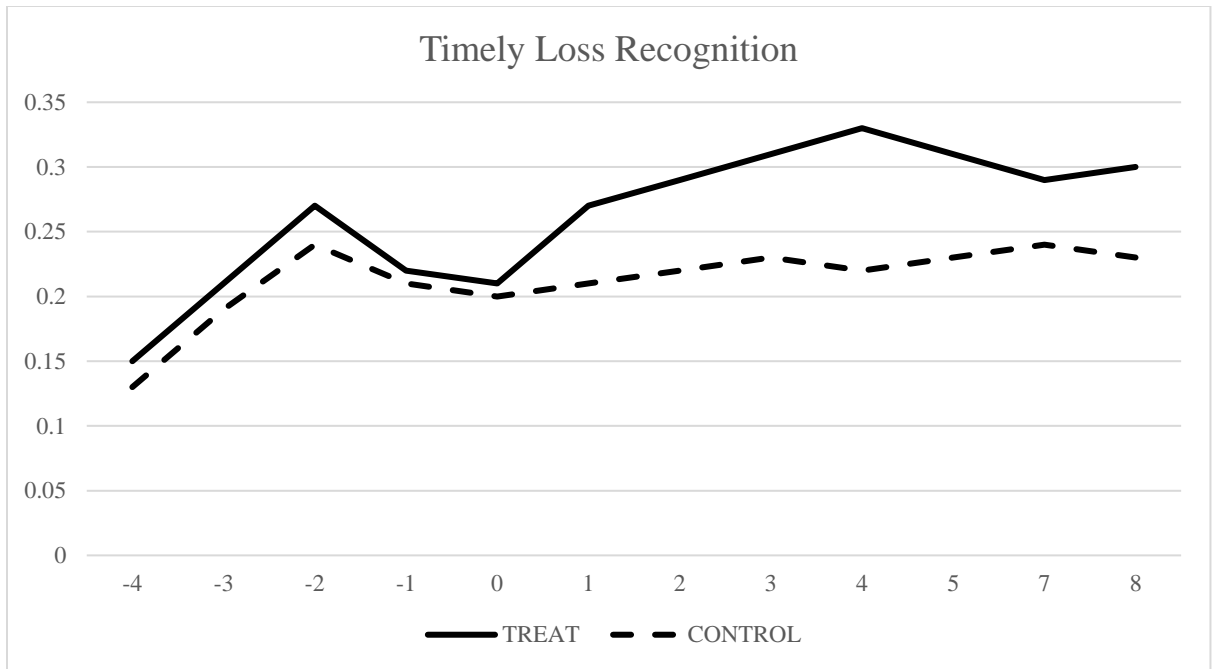


Figure 3. The parallel trend of Conservatism (Timely Loss Recognition) over time

This figure shows a parallel trend of Conservatism (Timely Loss Recognition) of firms with SPV before and after the passage of the law.

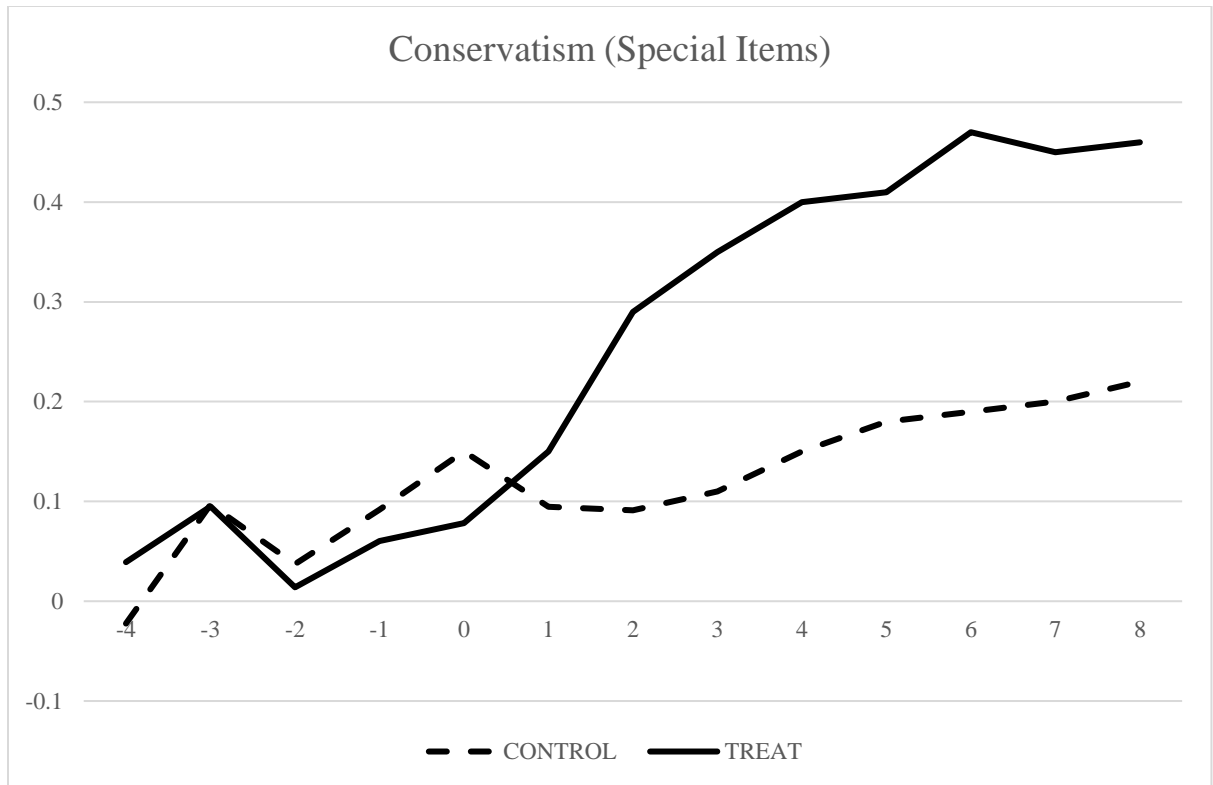


Figure 4. The parallel trend of Conservatism (Timely Loss Recognition) over time

This figure shows a parallel trend of Conservatism (Timely Loss Recognition) of firms with SPV before and after the passage of the law.

Table 1
Sample Constructure Step

N	Dif.	
347,428		
160,953	-186,475	Period 1996 - 2009
82,303	-78,650	Remove SIC 6000 - 6999 & SIC 4000 - 4999, SIC 9000 – 99999, FIC = "USA"
58,606	-23,697	Nonmissing AT, Debt, Book Leverage, AT>=1, Nonzero DEBT, 0<=Book Leverage<=1
20,300	-38,306	Nonmissing HHI and Nonmissing Controls
5,336	-14,964	Firms with Special Purpose Vehicle

Table 2
Descriptive Statistics

Variable	N	Mean	Std Dev	25p	Median	75p
Profitability	5,336	0.004	0.305	-0.014	0.089	0.148
Dividend Payer	5,336	0.239	0.427	0.000	0.000	0.000
Market to Book	5,336	1.717	1.833	0.786	1.171	1.912
Tangibility	5,336	0.253	0.228	0.077	0.177	0.357
Asset Maturity	5,336	4.304	5.978	1.321	2.402	4.690
R&D Expenses	5,336	0.063	0.136	0.000	0.004	0.063
Book Leverage	5,336	0.258	0.209	0.085	0.221	0.379
NoRated	5,336	0.737	0.440	0.000	1.000	1.000
CF Vol	5,336	0.059	0.236	0.009	0.018	0.039
Cost of Debt	5,336	0.160	0.141	0.052	0.075	0.111
HHI	5,336	0.771	0.259	0.516	0.907	1.000
Num Debt Type	5,336	2.107	1.051	1.000	2.000	3.000
Disclosure Quality	5,336	0.716	0.087	0.662	0.724	0.777
Excl 90	5,336	0.568	0.495	0.000	1.000	1.000
Secured/TD	5,336	0.134	0.299	0.000	0.000	0.035
Redeployability	5,336	0.390	0.106	0.345	0.401	0.443
TLR	5336	0.347	0.872	0.022	0.202	0.493
SPI/XIDO	5336	0.246	0.156	0.016	0.208	0.371

This table shows summary statistics of the main variables. The sample includes all Compustat firms that are incorporated in the 50 US states and Washington, DC excluding those in the financial [Standard Industrial Classification 6000 – 6999] and utility (SIC 4900-4999) industries and government sectors (SIC 9000 – 9999). The sample period spans 1992 – 2010. All continuous variables are winsorized at the 1st and 99th percentiles. Appendix 1 shows the detailed definition of variables.

Table 3
Debt Concentration and Anti-recharacterization

VARIABLES	(1) HHI	(2) Num_Debt_Type	(3) Excl 90
Law	0.015* (1.76)	-0.074* (-1.84)	0.026* (1.78)
Size	-0.005* (-1.80)	0.070*** (6.05)	-0.008** (-2.06)
Profitability	0.013 (1.31)	-0.052 (-1.12)	0.032* (1.80)
DividendPayer	0.010 (1.34)	-0.059 (-1.59)	0.014 (0.98)
Market to Book	0.010*** (8.03)	-0.039*** (-8.24)	0.018*** (7.72)
Tangibility	-0.088*** (-3.74)	0.219 (1.59)	-0.175*** (-4.40)
Asset Maturity	0.003*** (3.70)	-0.013*** (-4.48)	0.005*** (3.17)
R&D Expense	0.178*** (8.67)	-0.779*** (-8.72)	0.317*** (7.36)
Book Leverage	-0.302*** (-16.63)	1.395*** (22.00)	-0.475*** (-15.59)
NoRated	0.033*** (3.02)	-0.239*** (-5.74)	0.052** (2.51)
CF Vol	0.003 (0.32)	-0.022 (-0.57)	-0.007 (-0.37)
Observations	5,336	5,336	5,336
Adjusted R-squared	0.417	0.492	0.388
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table 4
Anti-recharacterization and Debt Contract

VARIABLES	(1) Secured Debt/AT	(2) Cost of Debt
Law	-0.125** (-2.06)	0.042** (2.02)
Size	-1.787*** (-8.75)	0.029 (0.48)
Profitability	-5.635*** (-4.26)	-1.098*** (-3.99)
DividendPayer	1.875*** (3.15)	-0.333** (-2.05)
Market to Book	0.737*** (3.85)	-0.017 (-0.47)
Tangibility	-7.250*** (-3.70)	-0.093 (-0.42)
Asset Maturity	0.150* (1.92)	-0.010 (-1.55)
R&D Expense	-10.101*** (-2.86)	0.222 (0.27)
Book Leverage	14.966*** (5.64)	-2.638*** (-6.22)
NoRated	-0.038 (-0.07)	0.112 (0.58)
CF Vol	3.609** (2.30)	0.152 (1.02)
Observations	5,336	5,336
Adjusted R-squared	0.354	0.304
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on the Debt Contract. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table 5

Anti-recharacterization, Debt Structure, and Distress Risk

VARIABLES	High Z Score					Low Z Score				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	HHI	N_Debt_Type	EXC190	Secured/AT	Cost of Debt	HHI	N_Debt_Type	EXC190	Secured/AT	Cost of Debt
Law	0.003 (0.22)	-0.057 (-0.79)	-0.001 (-0.06)	0.006 (0.64)	-0.188 (-1.11)	0.032** (2.36)	-0.072** (-2.36)	0.063** (2.25)	-0.027** (-2.08)	0.053** (2.08)
Observations	2,804	2,804	2,804	2,804	2,804	2,532	2,532	2,532	2,532	2,532
Adjusted R-squared	0.372	0.458	0.350	0.337	0.304	0.430	0.495	0.403	0.347	0.303
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by financial distress risk. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table 6

Anti-recharacterization, Debt Structure, and Asset Redeployability

VARIABLES	High Redeployability					Low Redeployability				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10) Cost of Debt
Law	0.006 (0.38)	0.018 (0.22)	0.003 (0.08)	-0.051 (-0.38)	0.023*** (2.88)	0.016** (2.51)	-0.113** (-2.61)	0.036** (2.30)	-0.100 (-0.81)	-0.008 (-0.87)
Observations	3,156	3,156	3,156	3,156	3,156	2,180	2,180	2,180	2,180	2,180
Adjusted R-squared	0.413	0.489	0.386	0.302	0.327	0.412	0.492	0.380	0.309	0.330
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by asset deployability. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table 7

Anti-recharacterization, Debt Structure, and Disclosure Quality

VARIABLES	High DQ					Low DQ				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt
Law	0.013	-0.048	0.020	-0.005	-0.056***	0.016*	-0.081*	0.034*	0.001	-0.077
	(1.21)	(-1.05)	(1.38)	(-0.59)	(-3.34)	(1.99)	(-1.98)	(1.95)	(0.12)	(-1.41)
Observations	3,846	3,846	3,846	3,846	3,846	1,490	1,490	1,490	1,490	1,490
Adjusted R-squared	0.432	0.523	0.396	0.331	0.304	0.396	0.454	0.376	0.323	0.302
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by disclosure risk. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table 8

Anti-recharacterization, Debt Structure, and Account Receivable

VARIABLES	High AR				Low AR					
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt
Law	-0.076**	0.026**	-0.033**	-0.056***	0.015	-0.035	0.013	0.001	-0.047	0.035***
	(-1.94)	(1.99)	(-2.32)	(-3.34)	(1.11)	(-1.25)	(1.12)	(1.58)	(-1.71)	(2.99)
Observations	2,936	2,936	2,936	2,936	2,936	2,400	2,400	2,400	2,400	2,400
Adjusted R-squared	0.673	0.446	0.632	0.346	0.624	0.491	0.351	0.571	0.426	0.412
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by account receivable. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table 9
Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.035*** (3.56)	0.064*** (4.36)
Controls	Yes	Yes
Observations	5,336	5,336
Adjusted R-squared	0.408	0.408
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table 10**Anti-recharacterization, Conservatism, and Distress Risk**

VARIABLES	High Z Score		Low Z Score	
	(1) TLR	(2) SPI	(3) TLR	(4) SPI
Law	0.012 (0.4)	0.054 (1.48)	0.025** (2.02)	0.123*** (4.60)
Controls	Yes	Yes	Yes	Yes
Observations	2,804	2,804	2,532	2,532
Adjusted R-squared	0.341	0.246	0.231	0.521
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism by financial distress risk. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm fixed effects and year fixed effects. Robust t-statistics in parentheses
*** p<0.01, ** p<0.05, * p<0.1.

Table 11**Anti-recharacterization, Conservatism, and Asset Redeployability**

VARIABLES	High Redeployability		Low Redeployability	
	(1) TLR	(2) SPI	(3) TLR	(4) SPI
Law	0.044 (1.45)	0.024 (1.15)	0.067** (2.24)	0.026*** (3.26)
Controls	Yes	Yes	Yes	Yes
Observations	3,156	3,156	2,180	2,180
Adjusted R-squared	0.341	0.246	0.231	0.521
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism by Asset deployability. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table 12**Anti-recharacterization, Conservatism, and Account Receivable**

VARIABLES	High AR		Low AR	
	(1) TLR	(2) SPI	(3) TLR	(4) SPI
Law	0.176** (2.16)	0.147*** (4.78)	0.126 (1.61)	0.024 (1.40)
Controls	Yes	Yes	Yes	Yes
Observations	2,936	2,936	2,400	2,400
Adjusted R-squared	0.247	0.415	0.211	0.614
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism by accounts receivable. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

**Table A1
(Delaware)**

Debt Concentration and Anti-recharacterization

VARIABLES	(1) HHI	(2) Num_Debt_Type	(3) Excl 90
Law	0.065*** (3.16)	-0.088*** (-2.89)	0.076*** (3.18)
Control	Yes	Yes	Yes
Observations	4,137	4,137	4,137
Adjusted R-squared	0.468	0.411	0.375
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table A2
(Delaware)

Anti-recharacterization, Debt Structure, and Distress Risk

VARIABLES	High Z Score					Low Z Score				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt
Law	0.007 (0.57)	-0.032 (-1.22)	-0.005 (-0.27)	0.004 (0.94)	-0.021 (-1.55)	0.042*** (3.01)	-0.061** (-2.16)	0.043** (2.50)	-0.061** (-2.12)	0.031*** (2.89)
Observations	2,277	2,277	2,277	2,277	2,277	2,040	2,040	2,040	2,040	2,040
Adjusted R-squared	0.322	0.378	0.380	0.321	0.249	0.436	0.488	0.421	0.422	0.327
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by financial distress risk. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

**Table A3
(Delaware)**

Anti-recharacterization, Debt Structure, and Asset Redeployability

VARIABLES	High Redeployability					Low Redeployability				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	HHI	N_Debt_Type	EXC190	Secured/AT	Cost of Debt	HHI	N_Debt_Type	EXC190	Secured/AT	Cost of Debt
Law	0.001	0.046	0.017	-0.031	0.033*	0.022***	-0.092***	0.067***	-0.150**	-0.048***
	(0.58)	(0.42)	(1.18)	(-1.35)	(1.94)	(3.21)	(-2.72)	(2.68)	(-1.99)	(-2.87)
Observations	2,925	2,925	2,925	2,925	2,925	1,392	1,392	1,392	1,392	1,392
Adjusted R-squared	0.440	0.421	0.234	0.319	0.311	0.324	0.413	0.435	0.313	0.439
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by asset deployability. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A4
(Delaware)

Anti-recharacterization, Debt Structure, and Disclosure Quality

VARIABLES	High DQ					Low DQ				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt
Law	0.022	-0.052	0.037	-0.002	-0.024	0.029***	-0.077***	0.015**	0.017**	-0.066**
	(1.51)	(-0.95)	(1.41)	(-1.36)	(-1.04)	(2.73)	(-2.59)	(2.22)	(2.09)	(-2.06)
Observations	3,531	3,531	3,531	3,531	3,531	786	786	786	786	786
Adjusted R-squared	0.335	0.461	0.489	0.111	0.204	0.251	0.315	0.239	0.445	0.418
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by disclosure risk. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A5
(Delaware)

Anti-recharacterization, Debt Structure, and Account Receivable

VARIABLES	High AR					Low AR				
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt	HHI	N_Debt_Type	EXCI90	Secured/AT	Cost of Debt
Law	-0.099*** (-2.88)	0.046*** (3.01)	-0.031** (-2.22)	-0.040*** (-3.78)	0.024*** (2.68)	-0.033 (-1.01)	0.021 (1.25)	0.009 (1.44)	-0.017 (-1.34)	0.001 (0.25)
Observations	2,527	2,527	2,527	2,527	2,527	1,790	1,790	1,790	1,790	1,790
Adjusted R-squared	0.556	0.422	0.509	0.299	0.412	0.244	0.294	0.439	0.219	0.405
Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure and contracts by account receivable. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A6
(Delaware)

Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.046*** (4.11)	0.074*** (5.26)
Controls	Yes	Yes
Observations	4,317	4,317
Adjusted R-squared	0.556	0.513
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

**Table A7
(Delaware)**

Anti-recharacterization, Conservatism, and Distress Risk

VARIABLES	High Z Score		Low Z Score	
	(1) TLR	(2) SPI	(3) TLR	(4) SPI
Law	0.026 (0.55)	0.022 (1.21)	0.067*** (3.12)	0.029*** (5.68)
Controls	Yes	Yes	Yes	Yes
Observations	2,277	2,277	2,040	2,040
Adjusted R-squared	0.448	0.310	0.572	0.621
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism by financial distress risk. Law is a dummy variable that equals one for firms incorporated in Texas or Louisiana after 1997, Alabama after 2001, Delaware after 2002, South Dakota after 2003, Virginia after 2004, and Nevada after 2005. All variables are defined in the Appendix. All regressions include firm fixed effects and year fixed effects. Robust t-statistics in parentheses
*** p<0.01, ** p<0.05, * p<0.1.

**Table A8
(Delaware)**

Anti-recharacterization, Conservatism, and Asset Redeployability

VARIABLES	High Redeployability		Low Redeployability	
	(1) TLR	(2) SPI	(3) TLR	(4) SPI
Law	0.057 (1.25)	0.044 (1.60)	0.081*** (3.99)	0.038*** (4.58)
Controls	Yes	Yes	Yes	Yes
Observations	2,925	2,925	1,392	1,392
Adjusted R-squared	0.440	0.371	0.621	0.575
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism by Asset deployability. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A9
(Delaware)

Anti-recharacterization, Conservatism, and Account Receivable

VARIABLES	High AR		Low AR	
	(1)	(2)	(3)	(4)
	TLR	SPI	TLR	SPI
Law	0.088** (2.16)	0.054** (2.55)	0.126 (1.11)	0.024 (1.51)
Controls	Yes	Yes	Yes	Yes
Observations	2,527	2,527	1,790	1,790
Adjusted R-squared	0.315	0.409	0.319	0.416
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism by accounts receivable. Law is a dummy variable that equals one for firms incorporated in Delaware after 2002. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A10
(Texas)

Debt Concentration and Anti-recharacterization

VARIABLES	(1) HHI	(2) Num_Debt_Type	(3) Excl 90
Law	0.015** (2.00)	-0.074*** (-2.68)	0.026** (2.18)
Control	Yes	Yes	Yes
Observations	1,908	1,908	1,908
Adjusted R-squared	0.477	0.512	0.404
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in Texas after 1997. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table A11
(Texas)

Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.075*** (5.51)	0.080*** (3.31)
Controls	Yes	Yes
Observations	1,908	1,908
Adjusted R-squared	0.410	0.303
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in Texas after 1997. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A12
(Louisiana)

Debt Concentration and Anti-recharacterization

VARIABLES	(1) HHI	(2) Num_Debt_Type	(3) Excl 90
Law	0.011* (1.71)	-0.022* (-1.90)	0.037* (1.69)
Control	Yes	Yes	Yes
Observations	1,252	1,252	1,252
Adjusted R-squared	0.391	0.333	0.296
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in Louisiana after 1997. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table A13
(Louisiana)

Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.023* (1.68)	0.051* (1.77)
Controls	Yes	Yes
Observations	1,252	1,252
Adjusted R-squared	0.312	0.526
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in Louisiana after 1997. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A14
(Alabama)

Debt Concentration and Anti-recharacterization

VARIABLES	(1) HHI	(2) Num_Debt_Type	(3) Excl 90
Law	0.008* (1.70)	-0.041** (-1.98)	0.071** (2.02)
Control	Yes	Yes	Yes
Observations	884	884	884
Adjusted R-squared	0.401	0.384	0.318
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in Alabama after 2001. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table A15
(Alabama)

Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.051** (2.10)	0.041** (2.21)
Controls	Yes	Yes
Observations	884	884
Adjusted R-squared	0.333	0.201
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in Alabama after 2001. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A16
(South Dakota)

Debt Concentration and Anti-recharacterization

VARIABLES	(1)	(2)	(3)
	HHI	Num_Debt_Type	Excl 90
Law	0.018*	-0.040*	0.016**
	(1.81)	(-1.79)	(1.99)
Control	Yes	Yes	Yes
Observations	663	663	663
Adjusted R-squared	0.417	0.492	0.388
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in South Dakota after 2003. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table A17
(South Dakota)

Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.020* (1.86)	0.024* (1.69)
Controls	Yes	Yes
Observations	663	663
Adjusted R-squared	0.299	0.330
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in South Dakota after 2003. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A18
(Virginia)

Debt Concentration and Anti-recharacterization

VARIABLES	(1) HHI	(2) Num_Debt_Type	(3) Excl 90
Law	0.059*** (2.87)	-0.099** (-2.33)	0.026*** (2.61)
Control	Yes	Yes	Yes
Observations	1,122	1,122	1,122
Adjusted R-squared	0.401	0.339	0.221
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in Virginia after 2004. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table A19
(Virginia)

Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.085*** (4.11)	0.052*** (5.96)
Controls	Yes	Yes
Observations	1,122	1,122
Adjusted R-squared	0.339	0.512
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in Virginia after 2004. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table A20
(Nevada)

Debt Concentration and Anti-recharacterization

VARIABLES	(1) HHI	(2) Num_Debt_Type	(3) Excl 90
Law	0.010* (1.85)	-0.024* (-1.69)	0.096* (1.81)
Control	Yes	Yes	Yes
Observations	592	592	592
Adjusted R-squared	0.500	0.322	0.501
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Debt structure. Law is a dummy variable that equals one for firms incorporated in Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1

Table A21
(Nevada)

Conservatism and Anti-recharacterization

VARIABLES	(1) TLR	(2) SPI
Law	0.056*** (5.50)	0.014** (2.16)
Controls	Yes	Yes
Observations	592	592
Adjusted R-squared	0.217	0.368
Firm FE	Yes	Yes
Year FE	Yes	Yes

This table shows the effect of the Anti-recharacterization law on Conservatism. Law is a dummy variable that equals one for firms incorporated in Nevada after 2005. All variables are defined in the Appendix. All regressions include firm-fixed effects and year-fixed effects. Robust t-statistics in parentheses *** p<0.01, ** p<0.05, * p<0.1.