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The Effect of Campaign Finance Laws on Electoral Competition
Evidence from the States

by Thad Kousser and Ray LaRaja

Executive Summary

Congress is now considering new regulations on campaign finance. Although their goal of preventing corruption or its appearance is important, those restrictions may reduce the competitiveness of elections.

Many states have enacted regulations on campaign finance, including limits on how much can be given to political parties. A close analysis of those state limits shows that restrictions on how much parties can raise and contribute to their nominees hinder the ability of candidates, especially those in close races, to raise money. Such restrictions do not hurt incumbents as much as they do challengers, since sitting lawmakers can attract more money from interest groups and individual donors. State regulatory limits on parties reduce the vote totals of challengers, thereby reducing the competitiveness of elections.

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Regulations on campaign finance, such as those of the McCain-Feingold and Shays-Meehan bills now before Congress, seek to prevent corruption or the appearance of corruption in the political process, but a consequence of such regulations may be a reduction in the competitiveness of elections. This analysis looks at the effects of campaign finance regulations on the competitiveness of state elections.[1] We address two central questions: First, what impact do campaign finance laws have on the flow of political money to campaigns? Second, what is the impact of that money on election outcomes?

Recent studies in political science suggest that weakening the role of parties in campaigns might undermine electoral competition. While interest groups and individual donors tend to favor incumbents, parties give more than expected to challengers because they want to maximize their share of seats in a legislature.[2] Pursuing that goal efficiently leads parties to contribute to challengers in competitive districts if the challengers have a chance of winning.[3] Interest groups, in contrast, often seek influence over policy through lobbying legislators; accordingly, they prefer to give money to incumbents who will likely win and return to the legislature.

These findings suggest that if parties are constrained in how much they can raise or spend, serious challengers will be penalized the most. Some studies of congressional elections[4] indicate that any loss of campaign funds will hit challengers especially hard at the polls, compounding the problems caused by limits on party contributions.

There is no single system of political regulation in state legislative elections. For instance, 24 states impose limits on how much money individuals can contribute to party organizations, and 23 set caps on party contributions to campaigns. We use a broadly representative sample of 15 states[5] to show how different campaign finance laws can influence which candidates raise money and who wins votes. This approach allows us to examine how the variation in state campaign finance laws affects political competition.

We begin by describing the various limits on political contributions in effect at the state level during the 1996 elections and linking them to overall patterns in fundraising. Taking account of other relevant factors, we then analyze the effects of laws on how much money individual candidates in contested districts raised. The second stage of the study focuses on districts where an incumbent ran, gauging the impact of campaign dollars on the vote totals garnered by both incumbents and challengers.

We find that limits on how much parties can raise and contribute to their nominees hinder the ability of candidates, especially those in close races, to raise money. Moreover, those limits do not penalize incumbents as harshly as they do challengers, since sitting lawmakers can attract more money from interest groups and individual donors. Most critically, these fundraising obstacles, which can be attributed to regulatory limits on party activity, reduce challengers' vote totals.

Campaign Finance Regulations in the States

One way American states set the rules of the electoral game is by enacting fundraising laws. A state can choose any combination of the following:

- a limit on party donations to candidates,
- a limit on contributions to parties,
- a limit on interest group[6] donations to candidates, and
- a limit on individual donations to candidates.

To evaluate the effects of those regulations, we assembled data on campaign contributions, campaign finance laws, and electoral conditions.[7] We then divided the contribution data into three categories that closely (but not perfectly) parallel the targets of campaign contribution limits:

- party contributions: donations from traditional party committees, and money provided by caucuses;[8]
- interest group contributions: interest group money and donations from "interested individuals," that is, individuals who have been identified as belonging to particular organizations or occupational categories;[9] and
- small individual contributions: individuals who give too little to be required to list their names and occupations.

To control for the size of legislative districts and make comparisons across the states possible, we transformed contributions into dollars per thousand residents in each legislative district.[10] We selected the 15 states listed in Table 1 because they display wide variation in campaign finance laws (the explanatory factors of interest in this study). Table 1 provides an overview of regulations and elections in the sampled states. The organization of Table 1 reflects the degree of regulation, from least restrictive to most restrictive, with loosely regulated states at the top.

The aggregate figures show that campaign finance laws affect the source of a candidate's funding. In states with loose regulations on political contributions (Colorado, Idaho, Illinois, and Utah), parties provide candidates with an overall average of 23 percent of their funds while interest groups and affiliated individuals provide 67 percent of funds (Figure 1). In contrast, in states with limits on all kinds of contributions (Kansas, Kentucky, Ohio, and Wyoming), parties provide only 15 percent of candidates' funds, and interest groups and affiliated individuals provide 76 percent (Figure 2).

Even though the playing field may appear leveled by laws constraining all types of donors, parties and the types of candidates that parties back (i.e., challengers) suffer the most from limits. This difference may appear marginal. However, in a state in which very few districts are competitive, this small difference in party control of funds might make a big difference in races that are potentially close.

Estimating the Effects of Contribution Limits

We need not be content with these aggregate numbers. We also examined the impact of contribution limits on challengers and incumbents in different types of races. We analyzed donations to 2,234 candidates,[11] all of whom ran for contested seats in the legislative houses listed in Table 1 during 1996.[12] Using measures of the electoral conditions in each district, we estimated econometric models that explain the variation in how much a candidate raised from party donors, interest groups, and individuals.

To predict contribution subtotals, we used a number of explanatory factors. Reports by the Federal Election Commission[13] and the Council of State Governments[14] list the contribution limits enacted in each state.[15] To estimate the expected tightness of races we looked at past party performance (during the 1992 and 1994 races) in legislative districts.[16] We computed the average spread between the major parties in contested races and subtracted that value from the major party vote to measure the tightness of races. We also used a party's history in the district to estimate a candidate's probability of winning, reporting the proportion of the two-party vote that the candidate's party had won in elections since the 1990 redistricting.[17] We identified incumbents by comparing prior session legislative rosters[18] with ballot choices and then recorded how each candidate fared in 1996.[19] Finally, we controlled for the legislative chamber in each race, the percentage of contested races for the chamber, district size, the candidate's party, and whether or not the candidate held a leadership post within the legislature.

With these factors measured, we then estimated multivariate regressions designed to isolate the effect of each variable, holding all others constant. The results show that the general lessons from the political science literature hold in state elections. Table 2 gives the results of one model that predicts how much candidates raised from parties and party caucuses.

Parties and challengers suffer the most from limits.

Table 1
Sampled States, by Campaign Finance Regime

	Percentage of Contributions from				Percentage of Races Uncontested	
Contribution Limits	Parties	Interest Groups	Individuals	$ per 1,000 residents	House	Senate
			Loosely Regulated States			
No limits on giving to candidates or to parties						
Colorado	20	74	6	365	72	68
Idaho	24	65	11	656	50	63
Illinois	29	54	17	2,563	73	55
Utah	20	75	5	336	61	57
			Moderately Regulated States			
Limits on giving to candidates from interest groups and individuals; no limits on giving to parties						
Utah	20	75	5	336	61	57
Michigan (House only)	17	83	0	566	99	-
N. Carolina (Senate only)	11	72	17	441	-	48
Alaska	26	58	16	3,407	85	60
Limits on giving to candidates from parties and interest groups; no limits on giving to parties						
Oregon[a]	6	79	15	375	82	60
Limits on giving to candidates from parties, interest groups, and individuals; no limits on giving to parties.						
Georgia	17	63	20	520	42	41
Maine	30	56	14	599	91	91
Tennessee (Senate only)	24	57	19	785	-	81
			Tightly Regulated States			
Limits on giving to candidates from parties, interest groups, and individuals and on giving to parties from individuals						
Wyoming[b]	12	87	1	543	55	40
Limits on giving to candidates from parties, interest groups, and individuals and on giving to parties from interest groups and individuals						
Kentucky[c]	12	65	23	601	55	84
Kansas	12	77	11	610	66	83
Ohio[d]	24	74	2	520	89	100

Sources: Contribution limits from Federal Elections Commission, *Campaign Finance Law 98: Chart 2-A: Contribution and Solicitation Limitations*, 1998, http://www.fec.gov/pages/Chart2A.htm, and Council of State Governments, *The Book of the States, 1996–1997* (Lexington, Ky.: Council of State Governments, 1996). Average contributions from National Institute of Money in State Politics.

[a]This limit is lifted if an opponent's campaign raises more than $10,000 from personal funds and family contributions combined. Council of State Governments, p. 181.

[b]Wyoming limits contributions from individuals to parties but does not restrain PAC-to-party contributions. No other states in our sample make a distinction between individual and PAC soft money.

[c]Since party-to-candidate giving in Kentucky is limited to $10,000 or a match of what a candidate raises, in our multivariate analysis we code this limit as being absent.

[d]Interest groups (PACs) can contribute unlimited amounts to candidates.

Figure 1
Distribution of Contributions in Loosely Regulated States

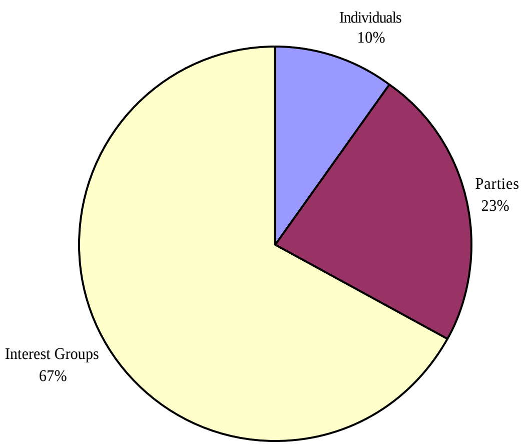
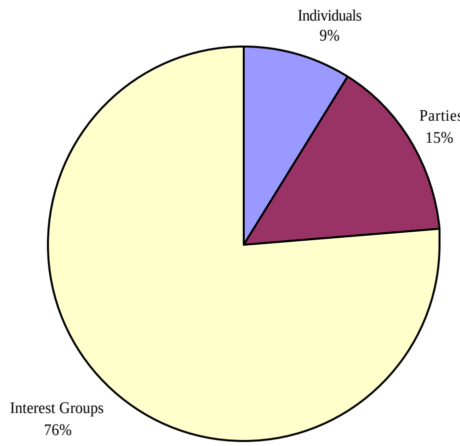


Figure 2
Distribution of Contributions in Tightly Regulated States



Our finding that parties give more to challengers than to incumbents is consistent with findings of previous studies.[20] Still, this "challenger bonus" is relatively small ($46 per thousand residents) and only narrowly achieves statistical significance. More impressive are the declines in party and caucus contributions in states that restrict party fundraising and party contributions to campaigns. A limit on how much parties can raise from individuals[21] costs candidates an estimated $620 per 1,000 residents, while a party-to-candidate contribution limit decreases their fundraising by $500.

It is important to note that the effect of those campaign finance laws is large for candidates in competitive districts. An "interaction" between the laws and the tightness of a race shows that limits on parties do not affect people in safe seats, who raise less from parties anyway. Contribution limits prevent parties from concentrating their resources on a few close races, as do laws that stop parties from raising large war chests. When party budgets shrink and party money must be spread across more candidates, serious challengers lose the most.

Although we did not report them in Table 2, we estimated similar models of contributions from interest groups and individuals.[22] To maximize their access to policymakers, these donors give more money to incumbents, controlling for other factors. Interest groups contribute an extra $251 per thousand residents to incumbents, who raise on average $47 more from individuals than challengers do. Nominees with a greater likelihood of winning also attract a bonus of $4 from interest groups for every additional percentage point of the vote that their party has captured in the past. While more money goes into competitive races, this effect is not as large here as it is for party giving.

Limits on PAC-to-candidate contributions display a puzzling positive effect on the amounts raised by candidates from those donors. Candidates appear to raise $309 more from interest groups and "interested individuals" when PAC donations are capped. That effect is counterintuitive, although nominees can turn to other interest groups or individuals when one PAC or person has given the maximum (an option they do not have when their party reaches its limit).

Parties give more to challengers than to incumbents.

Table 2
Estimated "Costs" to Candidates in 1996 Legislative Races

Change in Explanatory Factor	Predicted Effect on Fundraising from Party and Party Caucus
Candidate is the incumbent rather than the challenger	$ 71 less
Individual-to-party contributions are limited	$220 less
Party-to-candidate contributions are limited	$550 less
Number of residents in the district increases by 10,000	$ 10 less
Candidate is a top legislative leader	$882 more
Candidate is a Democrat rather than a Republican	$ 61 less
Only half of the seats in the state are contested by major party candidates, as compared to 90%	$212 less

Note: Table entries are derived from significant regression coefficients in an ordinary least squares model explaining contributions per thousand residents in a district. This model also included fixed state effects and explained 24 percent of the variation in party contributions.

The effect of campaign finance laws is large for candidates in competitive districts.

The Effect of Fundraising on Electoral Results

Do the effects of campaign finance laws on a candidate's fundraising level ultimately influence that candidate's performance on Election Day? Although many studies exploring the relationship between campaign dollars and electoral performance have been conducted on federal races, none has taken advantage of the large numbers of districts and varied regulatory regimes present in the states.

A fundamental challenge for all scholars estimating the impact of dollars raised on votes won is that both figures may be influenced by perceptions about the threat posed by a challenger, a factor that is notoriously difficult to measure. Even when past performance of the challenger's party and an index of his or her quality are accounted for,[23] we still do not have a complete understanding of how money affects a challenger's votes. This shared error most likely reflects the unmeasured perceptions of the challenger's chances. Researchers have attempted to deal with this challenge by using a technique called "two-stage least squares estimations."[24] That procedure first predicts candidate finances from factors that are not directly related to election outcomes and then uses those systematic figures—purged of their candidate-specific information—to explain vote totals.

That is the strategy we follow in our analysis. In a model not reported here, we use campaign finance laws, the competitiveness and size of districts, and state effects to predict total contributions to each candidate. We then use those predictions to explain how well the challenger performs in the general

Table 3
Effects of Fundraising Losses on Votes

If Fundraising Declines from	And the Candidate Is	Percentage of Vote the Candidate Will Lose
$1,000 to $500 per thousand residents	Challenger	1.8%
	Incumbent	1.5%
$1,500 to $1,000 per thousand residents	Challenger	1.0%
	Incumbent	0.8%
$2,000 to $1,500 per thousand residents	Challenger	0.8%
	Incumbent	0.6%

election, controlling for the strength of the challenger's party in the district.[25] We look at the 828 races in which an incumbent ran in our sample states.[26] Since previous work has shown that money has a decreasing marginal effect on votes,[27] we test a logarithmic transformation and find that campaign dollars indeed have diminishing returns. Table 3 displays the effects of changes in fundraising levels on the electoral fortunes of incumbents and challengers.

If incumbents and challengers start from the same base, their fundraising losses translate into essentially equal penalties at the ballot box.[28] Even though we find that the marginal effect of dollars on votes for each type of candidate is similar at a given level of funding, incumbent status is still important. Our earlier analysis showed that incumbents, with their higher likelihood of winning and their greater attractiveness to interest groups and individual donors, tend to raise more than challengers. Because current officeholders begin with a higher fundraising base, and because campaign dollars yield decreasing returns, any loss in contributions caused by limits on parties hurts incumbents less.

Conclusion

What does our evidence about the influence of campaign finance laws on fundraising levels and the impact of dollars on votes in state elections reveal? Linking the effects identified in both stages of our analysis, we can trace how contribution limits influence electoral results. Table 4 compares two groups of states to show how campaign finance laws can affect fundraising and, as a result, vote totals for a typical challenger and incumbent in a close race.[29] The table shows the effects of moving from a system with no contribution limits to one in which party, interest group, and individual donations to candidates are capped.

States that curtail party-to-candidate limits see quite significant decreases in contributions to both challengers and incumbents. While each type of candidate loses money, challengers face a higher penalty in the election: a loss of 2.8 percent of the vote compared with incumbents' loss of 1.9 percent due to fundraising obstacles. The difference in these effects comes from the diminishing marginal returns on campaign dollars. Even controlling for other factors, incumbents raise a bit more than challengers and thus pay less of a penalty at the polls when their fundraising declines from its higher predicted level.

At the outset, we asked whether the fears of political scientists about dampening political competition by limiting the role of parties were justified. It appears that they are. In our

Incumbents, with their higher likelihood of winning and their greater attractiveness to interest groups and individual donors, tend to raise more than challengers.

Table 4
Effects of Contribution Laws on Fundraising and Vote Totals

	Type of Candidate	Effect on Dollars per 1,000 District Residents	Effect on Challenger Vote (%)
Changing from no limits (Colo., Idaho, Ill., Utah) to limits on party, PAC, and individual contributions (Ga., Maine, Tenn.)	Challenger	–$760	–2.8
	Incumbent	–$809	+1.9

Restrictions on party activity should be weighed against the costs to political competition.

analysis of legislative elections in 15 states in 1996, we found that limits on how much parties can raise and contribute to their nominees hinder the ability of candidates, especially those in close races, to raise money. Those limits do not penalize incumbents as harshly as they do challengers, since sitting lawmakers can attract more money from interest groups and individual donors. Most critically, obstacles to fundraising, which can be attributed to regulatory limits on party activity, reduce challengers' vote totals.

These results point out a tradeoff that national reformers would be wise to consider. We recognize that political competition is but one goal of election law. Another salient goal, certainly, is to minimize corruption or the appearance thereof. Our analysis demonstrates, however, that restrictions on party activity should be weighed against the costs to political competition.

Notes

1. This analysis is based on Thad Kousser and Ray LaRaja, "How Do Campaign Finance Laws Shape Fundraising Patterns and Electoral Outcomes? Evidence from the States," Paper presented at the meetings of the American Political Science Association, Washington, 2000. That paper is available from the authors.

2. Michael J. Malbin and Thomas L. Gais, *The Day after Reform: Sobering Campaign Finance Lessons from the American States* (Albany, N.Y.: Rockefeller Institute, 1998); and Frank Sorauf, *Inside Campaign Finance* (New Haven, Conn.: Yale University Press, 1992).

3. Gary C. Jacobson, "Party Organization and the Distribution of Campaign Resources: Republi-cans and Democrats in 1982," *Political Science Quarterly* 100, no. 4 (1985): 603–25; and Paul S. Herrnson, "National Party Decision Making, Strategies, and Resource Distribution in Congres-sional Elections," *Western Political Quarterly* 42, no. 3 (1989): 301–23.

4. Gary C. Jacobson, "The Effects of Campaign Spending in House Elections: New Evidence for Old Arguments," *American Journal of Political Science* 34, no. 2 (1990): 334–62; idem, "Money and Votes Reconsidered: Congressional Elections, 1972–1982," *Public Choice* 47 (1985): 7–62; idem, *Money and Congressional Elections* (New Haven, Conn.: Yale University Press, 1980); and idem, "The Effects of Campaign Spending in Congressional Elections," *American Political Science Review* 72 (1978): 469–91.

5. We selected from the states for which electronic records of contributions are available in the centralized database kept by the National Institute of Money in State Politics. Since there is a potential correlation between states that make such data available and the strictness of their campaign finance laws, we did not randomly sample from this group. Instead, we selected states to maximize the variation in our primary independent variables, campaign finance laws. Those states mirror the rest of the nation in organizational strength of parties, ideology of residents, party control and spread in the legislature, and income and population. The institute's website is http://www.followthemoney.org.

6. We use the most restrictive law—a limit on political action committee (PAC) contributions—as our measure here. Other limits that apply to interest groups include limits on direct corporate and union giving. But because those groups often form PACs to evade such limits, we see PAC limits as the most effective obstacle to interest group giving.

7. We are grateful to the National Institute on Money in State Politics for generously providing categorized contribution data.

8. For many research purposes, this measure of party contributions will be far too "noisy" since caucuses and candidates are frequently regulated by a different set of laws than are party committees, even though they often pursue similar goals. If party laws do not apply to candidates and caucuses, then the "noise" in the measure of party contributions should not be affected by party limits. In this contribution category any movement caused by party limits comes from changes in contributions by parties themselves.

9. The National Institute on Money in State Politics categorized contributions from individuals as interest group or industry contributions when individuals listed occupations on their contribution forms. For instance, a tire store owner's donation is classified with other contributions from the "Transportation" industry. Thus, our category should really be called "interest groups and interested individuals." To explain variation in this category, we include in our model the factors that should affect interest group donations and those that should influence individual donations. While the institute's aggregation of individuals and groups in employment sectors makes direct estimation of our separate models impossible, we can still generate reasonable predicted values of combined contributions.

10. We calculated the size of districts by dividing the state's 1996 population by the number of legislators in the appropriate legislative chamber. Population data from U.S. Census Bureau, *Statistical Abstract of the United States: 1997* (Washington: U.S. Government Printing Office, 1997). Number of legislators from Council of State Governments, *The Book of the States, 1996–1997* (Lexington, Ky.: Council of State Governments, 1996).

11. We eliminated from our analysis 10 candidates, all incumbents, who raised huge sums of money from interest groups relative to the size of their districts. Those legislators were often leaders who distributed much of their contributions to other candidates, leaving a large gap between their fundraising and spending. Because their inclusion would bias estimates of the effects of fundraising on electoral performance, we removed from our dataset the 10 candidates who raised from interest groups more than 10 times the average of $540 per thousand residents.

12. By analyzing all states in the same year, we effectively control for any national-level partisan trends that may have been present in that year. However, a time-series study covering many states as their campaign finance laws changed would be a stronger research design, and data for such a study are now becoming available online at state websites and www.followthemoney.org.

13. Federal Election Commission, *Campaign Finance Law 98: Chart 2-A: Contribution and Solicitation Limitations,* 1998, http://www.fec.gov/pages/Chart2A.htm.

14. Council of State Governments, *The Book of the States.*

15. We find that the size of contribution limits, adjusted for district size, does not significantly alter their effects on contribution levels. Consequently, we use dichotomous variables to represent their presence in our reported results.

16. Michael Barone, William Lilley III, and Laurence DeFranco, *State Legislative Elections: Voting Patterns and Demographics* (Washington: Congressional Quarterly, 1998).

17. In some districts, especially for upper houses, a seat that was contested in 1996 had never before been contested since the 1990 redistricting. Our measure of the challenging party's probability of winning these seats, zero, necessarily underestimates that party's true chances. This measurement error casts some doubts on causal inferences made from the variable's estimated effect.

18. Council of State Governments, *State Leadership Directory, Directory I—State Elective Officials 1996* (Lexington, Ky.: Council of State Governments, 1996).

19. Results from the 1996 elections for each state are available on the website of the appropriate state entity (e.g., secretary of state, board of elections, elections division).

20. Malbin and Gais; and Anthony Gierzynski and David A. Breaux, "The Financing Role of Parties," in *Campaign Finance in State Legislative Elections,* ed. Joel A. Thompson and Gary F. Moncrief (Washington: Congressional Quarterly, 1998), pp. 188–206.

21. Because there is such a high correlation between individual-to-party and PAC-to-party limits (only Wyoming limits one but not the other), we include only individual-to-party limits in our models.

22. Those models explained 40 percent of the variation in interest group and "interested individual" contributions and 38 percent of variation in small donations from individuals.

23. Donald P. Green and Jonathan S. Krasno, "Salvation for the Spendthrift Incumbent," *American Journal of Political Science* 32, no. 4 (1988): 844–907; and Jacobson, "The Effects of Campaign Spending in House Elections."

24. Alan Gerber, "Estimating the Effect of Campaign Spending on Senate Election Outcomes Using Instrumental Variables," *American Political Science Review* 92, no. 2 (1998): 401–12. See also the Jacobson articles cited previously and Green and Krasno.

25. We also include controls for the challenger's party, the legislative house, the level of legislative professionalism, and the percentage of races in the state that is contested. See Peverill Squire, "Legislative Professionalism and Membership Diversity in State Legislatures," *Legislative Studies Quarterly* 17, no. 1 (1992): 69–79.

26. The effects of contributions in races for open seats, not reported here, are the same for the nominee of the party that has held the seat and for the challenging party.

27. Green and Krasno.

28. This is consistent with the analysis of U.S. Senate races in Gerber.

29. We compute effects on a district in which the two parties captured equal portions of the vote in recent elections. All other variables are set at their means.

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