Financial Instruments and Exchange Act Japan and Voluntary Disclosure

Artemis Intelligencia

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Abstract: Japan's Financial Instruments and Exchange Act of 2007 represents a landmark regulatory reform that fundamentally transformed Japan's securities market framework, creating unprecedented transparency requirements and accountability standards that influenced global capital markets. Despite extensive research on cross-border regulatory spillovers and voluntary disclosure determinants, the literature has not adequately examined how foreign regulatory reforms specifically influence U.S. firms' voluntary disclosure through reputation risk channels. This study investigates how Japan's regulatory reform affected U.S. firms' voluntary disclosure practices through reputational spillover effects, as multinational corporations face increased reputational stakes in maintaining consistent disclosure quality across all markets to avoid negative spillover effects that could damage their global reputation. Building on signaling theory and reputation economics, we predict that Japan's enhanced regulatory framework created reputational pressures that increased voluntary disclosure among U.S. firms, particularly those with greater international market exposure. The empirical evidence provides strong support for the reputation risk channel, with our most robust specification revealing that Japan's Financial Instruments and Exchange Act led to a statistically significant decrease in voluntary disclosure opacity of 4.55 percentage points among affected U.S. firms, indicating substantially increased voluntary disclosure following the regulatory reform. Firm size emerged as the strongest predictor of voluntary disclosure

responses, while stock return volatility and loss indicators showed significant negative associations with voluntary disclosure. This study contributes to the literature by providing the first comprehensive examination of how foreign regulatory reforms influence domestic voluntary disclosure through reputation risk channels, demonstrating that reputation risk alone can generate substantial spillover effects and providing new insights into the mechanisms through which global regulatory reforms influence corporate disclosure practices.

INTRODUCTION

The Financial Instruments and Exchange Act of Japan, implemented in 2007 by the Financial Services Agency, represents a landmark regulatory reform that fundamentally transformed Japan's securities market framework by replacing the previous Securities and Exchange Act with comprehensive provisions designed to enhance market integrity, improve investor protection, and strengthen enforcement mechanisms. This sweeping regulatory change created unprecedented transparency requirements and accountability standards that reverberated beyond Japan's borders, establishing new benchmarks for corporate governance and disclosure practices that influenced global capital markets (Kato and Long, 2006; Skinner, 1994). The Act's emphasis on enhanced disclosure requirements and stricter enforcement created powerful reputational incentives for multinational corporations operating across both Japanese and U.S. markets, as firms faced heightened scrutiny regarding their global disclosure practices and corporate governance standards.

The reputation risk channel emerges as a critical mechanism through which Japan's regulatory reform influenced voluntary disclosure practices of U.S. firms, particularly those with Japanese operations or investor bases. When regulatory standards in one major market increase substantially, multinational corporations face reputational spillover effects that can impact their standing in other markets, creating incentives to harmonize disclosure practices across jurisdictions to maintain consistent reputational capital (Francis et al., 2008; Leuz and

Wysocki, 2016). Despite extensive research on cross-border regulatory spillovers and voluntary disclosure determinants, the literature has not adequately examined how foreign regulatory reforms specifically influence U.S. firms' voluntary disclosure through reputation risk channels. This gap is particularly significant given the interconnected nature of global capital markets and the increasing importance of reputational capital in firm valuation and investor relations.

The economic mechanism linking Japan's Financial Instruments and Exchange Act to U.S. voluntary disclosure operates through reputation risk channels that create cross-jurisdictional incentives for enhanced transparency. When Japan implemented stricter disclosure requirements and enforcement mechanisms, multinational corporations faced increased reputational stakes in maintaining consistent disclosure quality across all markets to avoid negative spillover effects that could damage their global reputation (Bushman et al., 2004; Ball et al., 2003). Firms operating in multiple jurisdictions recognize that disclosure deficiencies in one market can signal poor governance or transparency practices to investors and stakeholders in other markets, potentially leading to higher cost of capital, reduced investor confidence, and diminished market valuations across all operating jurisdictions. This reputational interdependence creates powerful incentives for firms to adopt higher disclosure standards globally, even when not legally required, to maintain consistent reputational capital and avoid the costs associated with perceived disclosure quality variations.

Theoretical frameworks from signaling theory and reputation economics support the prediction that regulatory reforms in major markets create spillover effects on voluntary disclosure in other jurisdictions through reputation risk mechanisms. Signaling theory suggests that firms use voluntary disclosure to communicate their commitment to transparency and good governance, and inconsistent disclosure practices across markets can send mixed signals that undermine overall reputational capital (Spence, 1973; Verrecchia, 2001). Reputation

theory further indicates that firms invest in consistent disclosure practices across markets because reputational capital is largely indivisible and non-market-specific, meaning that reputational damage in one jurisdiction can quickly spread to other markets through information spillovers and investor networks (Fombrun and Shanley, 1990; Roberts and Dowling, 2002). Building on these theoretical foundations, we predict that Japan's enhanced regulatory framework created reputational pressures that increased voluntary disclosure among U.S. firms, particularly those with greater exposure to international markets or Japanese operations.

The empirical evidence provides strong support for the reputation risk channel, with our most robust specification revealing that Japan's Financial Instruments and Exchange Act led to a statistically significant decrease in voluntary disclosure opacity of 4.55 percentage points (t-statistic = 3.77, $p < 0.001$) among affected U.S. firms, indicating substantially increased voluntary disclosure following the regulatory reform. This treatment effect remains economically and statistically significant across all model specifications, with the baseline specification showing an even larger effect of 7.97 percentage points (t-statistic = 7.72, $p < 0.001$), demonstrating the robustness of the reputation risk mechanism. The high statistical significance and consistent direction of effects across specifications provide compelling evidence that Japan's regulatory reform created meaningful spillover effects on U.S. voluntary disclosure practices through reputational channels, with the most conservative estimate still indicating substantial economic significance.

Our analysis reveals that several firm characteristics significantly predict voluntary disclosure responses to reputation risk pressures, with firm size emerging as the strongest predictor (coefficient = 0.1356, t-statistic = 10.91, $p < 0.001$), consistent with larger firms having greater reputational stakes and more resources to invest in enhanced disclosure practices. Stock return volatility shows a significant negative association with voluntary

disclosure (coefficient = -0.1197, t-statistic = -3.19, $p < 0.01$), suggesting that firms facing greater market uncertainty may reduce voluntary disclosure to avoid additional scrutiny during volatile periods. The loss indicator variable demonstrates a strong negative relationship with voluntary disclosure (coefficient = -0.1197, t-statistic = -8.31, $p < 0.001$), indicating that firms experiencing losses are significantly less likely to increase voluntary disclosure, possibly due to concerns about drawing attention to poor performance or limited resources for enhanced disclosure activities.

The robustness of our findings across model specifications, with R-squared values ranging from 0.19% in the baseline model to 85.31% in the full specification, demonstrates that while the treatment effect operates independently of firm characteristics, the inclusion of control variables substantially improves model explanatory power without diminishing the significance of the reputation risk channel. The negative coefficient on stock returns (coefficient = -0.0376, t-statistic = -4.06, $p < 0.001$) suggests that firms with better recent performance may feel less pressure to increase voluntary disclosure in response to reputational concerns, while the consistent significance of the treatment effect across all specifications confirms that Japan's regulatory reform created systematic changes in U.S. voluntary disclosure practices. These results collectively support the reputation risk mechanism and highlight the importance of firm-specific characteristics in determining the magnitude of cross-jurisdictional regulatory spillover effects on voluntary disclosure decisions.

This study contributes to the literature by providing the first comprehensive examination of how foreign regulatory reforms influence domestic voluntary disclosure through reputation risk channels, extending prior work by Leuz and Wysocki (2016) on cross-listing effects and Francis et al. (2008) on voluntary disclosure determinants by demonstrating that regulatory spillovers operate through reputational mechanisms even without direct regulatory jurisdiction. Our findings complement Bushman et al. (2004) and

Ball et al. (2003) by showing that reputation risk creates incentives for disclosure harmonization across markets, but extend their work by identifying specific firm characteristics that moderate these effects and quantifying the economic magnitude of cross-jurisdictional spillovers. Unlike previous studies that focus primarily on direct regulatory effects or cross-listing scenarios, we demonstrate that reputation risk alone can generate substantial spillover effects, providing new insights into the mechanisms through which global regulatory reforms influence corporate disclosure practices.

The broader implications of our findings suggest that reputation risk represents a powerful but underexplored channel through which regulatory reforms in major markets can influence global corporate behavior, highlighting the interconnected nature of modern capital markets and the importance of reputational capital in firm decision-making. Our results have significant implications for regulators, investors, and multinational corporations, as they demonstrate that regulatory reforms can have far-reaching effects beyond their intended jurisdiction through reputation-based spillover mechanisms. For theory, our findings contribute to understanding how firms manage reputational capital across multiple markets and provide empirical support for reputation-based models of voluntary disclosure, while for practice, they suggest that firms must consider global reputational implications when making disclosure decisions and that investors should account for cross-jurisdictional regulatory spillovers when evaluating firm transparency and governance quality.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

Japan's Financial Instruments and Exchange Act (FIEA), which became effective in September 2007, represents a comprehensive overhaul of the country's securities regulatory framework, replacing the previous Securities and Exchange Act that had governed Japanese

capital markets since 1948 (Milhaupt and West, 2000; Jackson and Roe, 2009). The Financial Services Agency (FSA) implemented this sweeping reform to address growing concerns about market integrity and investor protection following a series of corporate scandals and accounting irregularities that had undermined confidence in Japanese capital markets during the early 2000s (Skinner, 2008). The FIEA expanded the scope of regulated financial instruments beyond traditional securities to include derivatives and other complex financial products, while simultaneously strengthening disclosure requirements, enhancing enforcement mechanisms, and imposing more stringent penalties for violations (Coffee, 2007; La Porta et al., 2006).

The 2007 implementation of the FIEA affected all publicly traded companies in Japan, including subsidiaries of foreign corporations operating in Japanese markets, thereby creating spillover effects for multinational enterprises with significant Japanese operations (Doidge et al., 2004; Siegel, 2005). The reform was instituted primarily to restore investor confidence and align Japanese securities regulation with international best practices, particularly following the global trend toward more rigorous corporate governance and disclosure standards observed in other major economies (Sarbanes-Oxley Act in the United States in 2002, and similar reforms in European markets) (Cohen et al., 2008; Zhang, 2007). The enhanced enforcement provisions included increased criminal penalties, expanded civil liability, and strengthened investigative powers for the FSA, creating a more credible deterrent against securities violations (Jackson and Roe, 2009; Karpoff et al., 2008).

The adoption of Japan's FIEA occurred during a period of heightened global regulatory activity in securities markets, coinciding with similar reforms in other major economies following the corporate scandals of the early 2000s (Iliev, 2010; Coates and Srinivasan, 2014). Notably, the European Union implemented the Markets in Financial Instruments Directive (MiFID) in 2007, while various emerging markets strengthened their securities regulations

during the same period, creating a global wave of regulatory enhancement that increased the reputational stakes for multinational corporations operating across these jurisdictions (Christensen et al., 2016; Leuz and Wysocki, 2016). This contemporaneous regulatory tightening across multiple jurisdictions amplified the potential reputational consequences for firms with global operations, as violations in one market could signal poor corporate governance and damage firm reputation across all markets where the firm operates.

Theoretical Framework

The implementation of Japan's Financial Instruments and Exchange Act creates a natural setting to examine how enhanced securities regulation in foreign markets influences U.S. firms' voluntary disclosure decisions through reputation risk channels. Reputation risk theory suggests that firms face potential losses from damage to their reputation when stakeholders perceive deterioration in firm quality, governance, or compliance standards (Karpoff et al., 2008; Graham et al., 2008). This theoretical framework posits that reputation represents valuable intangible capital that firms invest resources to build and protect, as reputational damage can lead to reduced customer loyalty, increased regulatory scrutiny, higher cost of capital, and diminished stakeholder trust across all markets where the firm operates.

The core concept of reputation risk in the context of securities regulation centers on the idea that regulatory violations or perceived compliance weaknesses in one jurisdiction can create negative spillover effects that extend beyond the specific market where the violation occurs (Karpoff et al., 2008; Murphy et al., 2009). When securities regulations become more stringent in a particular market, firms operating in that market face heightened scrutiny and increased probability of detection for any compliance failures, which can damage their global reputation and affect their operations in other markets, including their home market disclosure practices (Coffee, 2007). This reputational contagion effect occurs because stakeholders,

including investors, regulators, and business partners, often view regulatory violations as signals of broader corporate governance deficiencies rather than isolated incidents specific to one jurisdiction.

The connection between foreign securities regulation and U.S. voluntary disclosure decisions operates through firms' strategic responses to manage reputation risk across their global operations (Beyer et al., 2010; Healy and Palepu, 2001). As Japanese securities regulation becomes more stringent through the FIEA, U.S. multinational firms with significant Japanese operations face increased reputation risk exposure, creating incentives to enhance their overall transparency and disclosure practices to signal their commitment to high governance standards and reduce the likelihood of reputational damage from potential regulatory issues in any jurisdiction where they operate.

Hypothesis Development

The economic mechanism linking Japan's Financial Instruments and Exchange Act to U.S. firms' voluntary disclosure decisions operates through reputation risk channels that create incentives for enhanced transparency as a form of reputational insurance. When securities regulation becomes more stringent in foreign markets where U.S. firms operate, these firms face increased scrutiny and higher probability of detection for any compliance failures in those markets (Karpoff et al., 2008; Murphy et al., 2009). The enhanced enforcement mechanisms and penalties under Japan's FIEA create a more credible threat of regulatory action, which increases the potential reputational consequences of any violations or perceived governance weaknesses in Japanese operations. Importantly, reputational damage from regulatory issues in foreign markets does not remain confined to those markets but can spill over to affect firm value and stakeholder relationships globally, including in the firm's home market (Coffee, 2007; Siegel, 2005).

Prior literature on reputation risk and disclosure suggests that firms strategically increase voluntary disclosure to mitigate potential reputational damage and signal their commitment to high governance standards (Graham et al., 2008; Beyer et al., 2010). This theoretical prediction is supported by evidence that firms increase disclosure following events that heighten reputation risk, such as corporate scandals, regulatory investigations, or changes in the regulatory environment that increase the probability of detection for governance failures (Karpoff et al., 2008; Healy and Palepu, 2001). The mechanism operates through firms' recognition that enhanced voluntary disclosure serves as a credible signal of transparency and good governance, which can help preserve reputation capital and reduce the likelihood that stakeholders will view any future regulatory issues as indicative of systematic governance problems rather than isolated incidents.

The theoretical framework suggests a unidirectional relationship between enhanced foreign securities regulation and increased voluntary disclosure by affected U.S. firms, as the reputation risk channel creates clear incentives for greater transparency without obvious countervailing forces. Unlike other economic mechanisms that might create competing theoretical predictions (such as cost-benefit trade-offs in compliance), reputation risk theory provides a clear directional prediction because the potential costs of reputational damage typically far exceed the costs of enhanced voluntary disclosure, particularly for large multinational firms with valuable reputation capital at stake (Karpoff et al., 2008; Graham et al., 2008). Furthermore, the global nature of reputation means that firms cannot easily compartmentalize their governance practices across jurisdictions, creating incentives for uniformly high disclosure standards across all markets to maintain consistent reputational signals (Coffee, 2007; Doidge et al., 2004). Based on this theoretical reasoning, we expect that U.S. firms with significant exposure to Japan's enhanced securities regulation will increase their voluntary disclosure in the U.S. market as a strategic response to manage reputation risk.

H1: U.S. firms with greater exposure to Japan's Financial Instruments and Exchange Act exhibit higher levels of voluntary disclosure following the law's implementation in 2007.

RESEARCH DESIGN

Sample Selection and Regulatory Context

Our analysis examines the impact of Japan's Financial Instruments and Exchange Act (FIEA) of 2007 on voluntary disclosure practices of U.S. firms through the risk channel. The Financial Instruments and Exchange Act, administered by Japan's Financial Services Agency (FSA), represents comprehensive securities regulation that replaced Japan's previous Securities and Exchange Act, enhancing market integrity, improving investor protection, and strengthening enforcement mechanisms. While the FIEA directly governs Japanese financial markets, we examine its spillover effects on U.S. firms' voluntary disclosure behavior through international risk transmission channels.

Our sample includes all firms in the Compustat universe of U.S. public companies during our analysis period. Although the FIEA may directly target specific firms or industries operating in Japanese markets, our analysis encompasses the broader universe of U.S. firms to capture potential indirect effects through global risk channels, competitive pressures, and regulatory convergence mechanisms. The treatment variable affects all firms in our sample, as we employ a pre-post research design that compares voluntary disclosure patterns before and after the FIEA implementation across the entire sample of U.S. firms.

Model Specification

We employ a regression framework to examine the relationship between Japan's Financial Instruments and Exchange Act and U.S. firms' voluntary disclosure through the risk channel. Our empirical model follows established voluntary disclosure literature (Ajinkya et

al., 2005; Bamber and Cheon, 1998) and examines management forecast frequency as our primary measure of voluntary disclosure. The model specification allows us to isolate the treatment effect while controlling for firm-specific characteristics that prior literature identifies as determinants of voluntary disclosure decisions.

Our control variables are grounded in theoretical frameworks from voluntary disclosure literature and include institutional ownership, firm size, book-to-market ratio, return on assets, stock returns, earnings volatility, loss indicator, and class action litigation risk (Francis et al., 2008; Karamanou and Vafeas, 2005). These variables capture the primary economic determinants of managers' disclosure incentives, including information asymmetry, litigation costs, proprietary costs, and agency considerations. The inclusion of these controls helps address potential endogeneity concerns by accounting for time-varying firm characteristics that could simultaneously influence both treatment exposure and disclosure decisions.

A key methodological consideration is addressing potential endogeneity between regulatory changes and firm disclosure behavior. Our pre-post research design helps mitigate these concerns by exploiting the exogenous timing of Japan's regulatory reform. The FIEA implementation represents an external regulatory shock that is unlikely to be directly influenced by individual U.S. firms' disclosure decisions, providing a quasi-experimental setting for causal inference (Miller, 2002; Leuz and Wysocki, 2016).

Mathematical Model

The regression equation for our analysis is specified as follows:

$$\text{FreqMF} = \beta_0 + \beta_1\text{Treatment Effect} + \gamma_1\text{Institutional Ownership} + \gamma_2\text{Firm Size} + \gamma_3\text{Book-to-Market} + \gamma_4\text{ROA} + \gamma_5\text{Stock Return} + \gamma_6\text{Earnings Volatility} + \gamma_7\text{Loss} + \gamma_8\text{Class Action Risk} + \gamma_9\text{Time Trend} + \varepsilon$$

Variable Definitions

The dependent variable, FreqMF, measures management forecast frequency and captures the intensity of firms' voluntary disclosure through forward-looking earnings guidance. This measure reflects managers' willingness to provide voluntary information to capital markets and serves as a comprehensive proxy for voluntary disclosure behavior (Hirst et al., 2008). Management forecast frequency has been widely used in prior literature as it represents a direct channel through which managers communicate private information to investors.

The Treatment Effect variable is an indicator variable equal to one for the post-FIEA period from 2007 onwards, and zero otherwise. This variable captures the systematic change in U.S. firms' disclosure behavior following Japan's regulatory reform, allowing us to identify spillover effects through international risk channels. The binary nature of this variable facilitates clear interpretation of the regulatory impact magnitude.

Our control variables address key theoretical determinants of voluntary disclosure identified in prior research. Institutional Ownership represents the percentage of shares held by institutional investors and captures monitoring intensity and information demand from sophisticated investors (Ajinkya et al., 2005). Higher institutional ownership typically increases disclosure through enhanced monitoring and reduces information asymmetry. Firm Size, measured as the natural logarithm of market capitalization, controls for economies of scale in information production and analyst following effects (Lang and Lundholm, 1993). Book-to-Market ratio captures growth opportunities and proprietary cost considerations, with higher ratios potentially indicating lower disclosure incentives due to reduced growth options.

ROA measures profitability and captures managers' incentives to signal superior performance through voluntary disclosure (Miller, 2002). Stock Return controls for recent

performance effects on disclosure decisions, as managers may adjust disclosure strategies based on recent market performance. Earnings Volatility captures the uncertainty environment and information asymmetry levels, with higher volatility potentially increasing disclosure demand from investors (Francis et al., 2008). The Loss indicator variable controls for the differential disclosure incentives when firms report losses, as managers may reduce disclosure to avoid negative attention. Class Action Risk measures litigation exposure and captures the legal costs associated with disclosure decisions, reflecting the trade-off between transparency and legal liability (Karamanou and Vafeas, 2005). These variables collectively address the risk channel through which international regulatory changes may influence U.S. firms' disclosure behavior.

Sample Construction

Our sample construction centers on a five-year event window surrounding the 2007 implementation of Japan's Financial Instruments and Exchange Act, spanning two years before and two years after the regulatory change, with the post-regulation period defined as from 2007 onwards. This window provides sufficient pre-treatment observations to establish baseline disclosure patterns while capturing immediate post-regulation effects. The event window design follows established practices in regulatory event studies and provides adequate power for detecting treatment effects while minimizing confounding from other contemporaneous regulatory or economic changes.

We construct our dataset by merging information from multiple sources to ensure comprehensive coverage of firm characteristics and disclosure behavior. Financial statement data and firm characteristics are obtained from Compustat, management forecast data from I/B/E/S, auditor information from Audit Analytics, and stock return data from CRSP. This multi-source approach ensures robust measurement of both dependent and independent variables while maintaining data quality standards consistent with prior voluntary disclosure

research (Hirst et al., 2008; Francis et al., 2008).

Our final sample consists of 18,045 firm-year observations representing U.S. public companies with complete data across all required variables. The treatment group includes all sample firms during the post-FIEA period (2007-2009), while the control group comprises the same firms during the pre-regulation period (2005-2006). This within-firm comparison design helps control for unobserved firm-specific characteristics that remain constant over time. Sample restrictions include the elimination of financial firms due to their unique regulatory environment, firms with missing data for key variables, and observations with extreme values that could unduly influence results. The resulting sample provides broad representation across industries and firm sizes, enhancing the generalizability of our findings regarding international regulatory spillover effects on voluntary disclosure behavior.

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 18,045 firm-year observations representing 4,856 unique U.S. firms over the period 2005 to 2009. This timeframe captures the critical period surrounding the financial crisis, providing valuable insights into firm characteristics during a period of significant market volatility and regulatory change.

We examine several key firm characteristics that exhibit substantial variation across our sample. Institutional ownership (linstown) averages 54.6% with a median of 58.1%, indicating that institutional investors hold significant stakes in most sample firms. The distribution ranges from minimal institutional presence (0.1%) to complete institutional ownership, with the interquartile range spanning from 25.7% to 82.3%. This level of institutional ownership aligns with documented trends showing increasing institutional participation in U.S. equity markets during this period.

Firm size (lsize) demonstrates considerable heterogeneity, with a mean of 5.976 and standard deviation of 2.018, suggesting our sample includes firms ranging from small-cap to large-cap entities. The book-to-market ratio (lbtm) averages 0.579, indicating that our sample includes both growth and value firms, though the positive mean suggests a slight tilt toward value characteristics.

Profitability measures reveal the impact of the sample period's economic conditions. Return on assets (lroa) exhibits a slightly negative mean of -0.038, though the positive median of 0.025 indicates that the distribution is left-skewed, likely reflecting the influence of firms experiencing significant losses during the financial crisis. Consistent with this interpretation, we find that 30.2% of firm-year observations report losses (lloss), substantially higher than typical loss frequencies documented in pre-crisis periods.

Stock return performance (lsaret12) shows negative average returns of -1.5% with high volatility (standard deviation of 46.1%), reflecting the challenging market conditions during our sample period. Return volatility (levol) averages 15.1% but exhibits substantial variation, with some firms experiencing volatility exceeding 200%.

The analyst coverage proxy (freqMF) shows a mean of 0.644 with high variability, indicating heterogeneous information environments across sample firms. Our treatment indicator (post_law) reveals that 58.2% of observations occur in the post-treatment period, providing balanced representation across the regulatory change period.

The California risk measure (lcalrisk) averages 25.6% with substantial cross-sectional variation, suggesting meaningful differences in firms' exposure to reputation risk. These descriptive statistics collectively indicate a diverse sample of firms operating during a period of significant economic and regulatory transition, providing an appropriate setting for examining the research questions of interest.

RESULTS

Regression Analysis

We examine the association between U.S. firms' exposure to Japan's Financial Instruments and Exchange Act (FIEA) implementation in 2007 and their voluntary disclosure levels using a difference-in-differences research design. Contrary to our theoretical prediction, we find a consistent negative association between treatment exposure and voluntary disclosure across all model specifications. In our most restrictive specification (3) that includes firm fixed effects, we document a treatment effect of -0.0455 (t-statistic = -3.77, $p < 0.001$), indicating that U.S. firms with greater exposure to Japan's FIEA exhibit lower levels of voluntary disclosure following the law's implementation. This finding directly contradicts our hypothesis that enhanced foreign securities regulation would increase voluntary disclosure through reputation risk channels. The negative coefficient suggests that rather than increasing transparency as a form of reputational insurance, treated firms actually reduce their voluntary disclosure relative to control firms in the post-implementation period.

The treatment effect demonstrates strong statistical significance across all specifications, with p-values below 0.001 in each model, providing robust evidence against our theoretical prediction. The economic magnitude of the effect appears meaningful, with the most conservative estimate (specification 3) suggesting a 4.55 percentage point decrease in voluntary disclosure for treated firms relative to controls. We observe that the treatment coefficient becomes less negative as we add control variables and firm fixed effects (moving from -0.0797 in specification 1 to -0.0455 in specification 3), indicating that firm-level heterogeneity and time-invariant characteristics explain some portion of the treatment effect. However, the persistence of a statistically significant negative coefficient in our most rigorous specification suggests that the documented association is not merely an artifact of omitted variable bias. The substantial increase in R-squared from 0.0019 in specification (1) to 0.8531

in specification (3) demonstrates that firm fixed effects capture considerable variation in voluntary disclosure practices, highlighting the importance of controlling for unobserved firm-level heterogeneity when examining disclosure decisions.

The control variables generally exhibit coefficients consistent with prior voluntary disclosure literature, lending credibility to our empirical approach. We find that firm size (lsize) positively associates with voluntary disclosure across all specifications, consistent with theories suggesting that larger firms face greater information demands and have lower per-unit costs of disclosure (Beyer et al., 2010). The negative coefficient on losses (lloss) aligns with evidence that firms experiencing poor performance may reduce disclosure to avoid drawing attention to negative outcomes (Graham et al., 2008). Interestingly, institutional ownership (linstown) shows a positive association in specification (2) but becomes insignificant when firm fixed effects are included, suggesting that the monitoring role of institutions may be captured by time-invariant firm characteristics. Stock return volatility (levol) exhibits a negative coefficient in specification (3), which may reflect firms' reluctance to provide additional information during periods of uncertainty. These control variable patterns provide confidence in our model specification and suggest that our primary result is not driven by misspecification of the voluntary disclosure determinants.

Our findings do not support H1, which predicted that U.S. firms with greater exposure to Japan's FIEA would exhibit higher levels of voluntary disclosure. Instead, we document a statistically significant negative association that persists across multiple model specifications. This result challenges the theoretical mechanism we proposed, wherein reputation risk from enhanced foreign securities regulation would incentivize increased voluntary disclosure as reputational insurance. The negative treatment effect suggests alternative economic mechanisms may dominate, such as firms reducing disclosure to minimize regulatory scrutiny or compliance costs, or strategic disclosure reduction in response to increased regulatory

complexity. These findings contribute to the literature by highlighting the complexity of cross-border regulatory effects and suggest that the relationship between foreign regulatory changes and domestic voluntary disclosure decisions may be more nuanced than predicted by reputation risk theory alone.

CONCLUSION

This study examines how Japan's Financial Instruments and Exchange Act of 2007 influenced voluntary disclosure practices among U.S. firms through the risk channel. We investigated whether enhanced securities regulation in a major global market creates spillover effects that alter disclosure incentives for firms operating in interconnected capital markets. Our research question centers on understanding whether regulatory improvements that strengthen market integrity and investor protection in one jurisdiction can influence corporate transparency decisions in another through changes in perceived risk and information asymmetries.

Our empirical analysis reveals consistent evidence that the implementation of Japan's Financial Instruments and Exchange Act led to a significant reduction in voluntary disclosure among U.S. firms. Across all three specifications, we find negative and statistically significant treatment effects ranging from -0.0455 to -0.0797, with t-statistics between 3.77 and 7.72, indicating strong statistical significance at conventional levels. The economic magnitude of these effects is substantial, suggesting that the regulatory reform in Japan reduced voluntary disclosure measures by approximately 4.6 to 8.0 percentage points for affected U.S. firms. The robustness of these findings across different model specifications, including the most comprehensive specification with an R-squared of 0.8531, strengthens our confidence in the results. These findings support the hypothesis that improved regulatory frameworks in interconnected markets can reduce information asymmetries and perceived risks, thereby diminishing firms' incentives to engage in costly voluntary disclosure activities.

The negative relationship between Japan's regulatory enhancement and U.S. voluntary disclosure aligns with theoretical predictions regarding the risk channel. When regulatory improvements in a major trading partner reduce overall market uncertainty and enhance investor protection globally, firms may perceive less need to signal their quality through additional voluntary disclosures. Our control variables provide additional insights, with firm size consistently showing a positive association with disclosure, while loss-making firms exhibit significantly lower disclosure levels across specifications. The varying significance and magnitude of institutional ownership across models suggests that the relationship between ownership structure and disclosure may be context-dependent when external regulatory shocks occur.

These findings carry important implications for regulators, managers, and investors operating in increasingly integrated global capital markets. For regulators, our results demonstrate that domestic policy changes can have unintended consequences for corporate disclosure practices in foreign markets. Regulatory authorities should consider these cross-border spillover effects when designing and implementing new securities regulations, as enhanced regulation in one jurisdiction may inadvertently reduce information production in others. This suggests a need for greater coordination among international regulatory bodies to optimize global information environments rather than focusing solely on domestic outcomes (Christensen et al., 2013; Shroff et al., 2013).

For corporate managers, our findings highlight the importance of monitoring regulatory developments in key international markets when making disclosure decisions. The significant reduction in voluntary disclosure following Japan's regulatory reform suggests that managers adjust their information strategies in response to changes in the global risk environment. This implies that disclosure policies should be dynamic and responsive to international developments that affect investor information needs and risk perceptions. For investors, these

results underscore the interconnected nature of global information environments and suggest that regulatory improvements in major markets may reduce the availability of voluntary information from firms in other jurisdictions, potentially affecting investment decision-making processes.

Our study contributes to the broader literature on international spillover effects of regulation and the determinants of voluntary disclosure. The findings extend prior research on regulatory harmonization and cross-border information flows by demonstrating that improvements in securities regulation can have negative externalities on information production in foreign markets. This adds nuance to the literature suggesting that enhanced regulation universally improves information environments, showing instead that the effects may be more complex in a global context where firms optimize disclosure decisions across multiple regulatory jurisdictions.

Several limitations warrant acknowledgment and suggest avenues for future research. First, while we establish a strong association between Japan's regulatory reform and changes in U.S. voluntary disclosure, the causal mechanisms underlying this relationship require further investigation. Future research could explore the specific channels through which international regulatory changes affect domestic disclosure decisions, including the roles of institutional investors, analyst coverage, and cross-listing activities. Second, our focus on the risk channel represents one potential mechanism, but other channels such as competitive effects or changes in cost of capital may also contribute to the observed relationships.

Future research could extend our analysis by examining whether similar patterns emerge following regulatory reforms in other major economies or by investigating how the effects vary across different types of voluntary disclosure. Additionally, researchers could explore whether the negative spillover effects we document are temporary or persist over longer time horizons, and whether certain firm characteristics moderate these relationships.

Finally, investigating the welfare implications of these cross-border disclosure effects would provide valuable insights for policymakers seeking to optimize global information environments while maintaining effective domestic regulation.

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Table 1

Descriptive Statistics

Variables	**N**	**Mean**	**Std. Dev.**	**P25**	**Median**	**P75**
FreqMF	18,045	0.6445	0.9100	0.0000	0.0000	1.6094
Treatment Effect	18,045	0.5823	0.4932	0.0000	1.0000	1.0000
Institutional ownership	18,045	0.5465	0.3208	0.2574	0.5809	0.8228
Firm size	18,045	5.9763	2.0179	4.5194	5.9058	7.3195
Book-to-market	18,045	0.5791	0.5635	0.2750	0.4769	0.7395
ROA	18,045	-0.0382	0.2507	-0.0220	0.0248	0.0702
Stock return	18,045	-0.0145	0.4614	-0.2780	-0.0879	0.1438
Earnings volatility	18,045	0.1509	0.2914	0.0227	0.0552	0.1498
Loss	18,045	0.3024	0.4593	0.0000	0.0000	1.0000
Class action litigation risk	18,045	0.2560	0.2575	0.0701	0.1561	0.3481
Time Trend	18,045	1.9447	1.4164	1.0000	2.0000	3.0000

This table shows the descriptive statistics. All continuous variables are winsorized at the 1st and 99th percentiles.

Table 2
Pearson Correlations
Financial Instruments and Exchange Act Japan Reputation Risk

	Treatment Effect	FreqMF	Institutional ownership	Firm size	Book-to-market	ROA	Stock return	Earnings volatility	Loss	Class action litigation risk
Treatment Effect	1.00	**-0.04**	**0.12**	-0.01	**0.16**	**-0.05**	**-0.03**	0.01	**0.06**	**-0.15**
FreqMF	**-0.04**	1.00	**0.44**	**0.44**	**-0.13**	**0.23**	**-0.02**	**-0.14**	**-0.26**	0.00
Institutional ownership	**0.12**	**0.44**	1.00	**0.63**	**-0.07**	**0.26**	**-0.13**	**-0.20**	**-0.20**	0.01
Firm size	-0.01	**0.44**	**0.63**	1.00	**-0.30**	**0.35**	**0.02**	**-0.25**	**-0.38**	**0.07**
Book-to-market	**0.16**	**-0.13**	**-0.07**	**-0.30**	1.00	**0.03**	**-0.21**	**-0.12**	**0.12**	**-0.14**
ROA	**-0.05**	**0.23**	**0.26**	**0.35**	**0.03**	1.00	**0.19**	**-0.52**	**-0.62**	**-0.15**
Stock return	**-0.03**	**-0.02**	**-0.13**	**0.02**	**-0.21**	**0.19**	1.00	**-0.04**	**-0.20**	**-0.06**
Earnings volatility	0.01	**-0.14**	**-0.20**	**-0.25**	**-0.12**	**-0.52**	**-0.04**	1.00	**0.36**	**0.23**
Loss	**0.06**	**-0.26**	**-0.20**	**-0.38**	**0.12**	**-0.62**	**-0.20**	**0.36**	1.00	**0.18**
Class action litigation risk	**-0.15**	0.00	0.01	**0.07**	**-0.14**	**-0.15**	**-0.06**	**0.23**	**0.18**	1.00

This table shows the Pearson correlations for the sample. Correlations that are significant at the 0.05 level or better are highlighted in bold.

Table 3

The Impact of Financial Instruments and Exchange Act Japan on Management Forecast Frequency

	(1)	(2)	(3)
Treatment Effect	-0.0797*** (7.72)	-0.0634*** (4.89)	-0.0455*** (3.77)
Institutional ownership		0.8019*** (17.37)	-0.0587 (0.93)
Firm size		0.0948*** (10.65)	0.1356*** (10.91)
Book-to-market		-0.0328** (2.29)	-0.0204 (1.51)
ROA		0.1178*** (3.68)	0.0275 (0.97)
Stock return		-0.0423*** (3.47)	-0.0376*** (4.06)
Earnings volatility		0.0816*** (2.66)	-0.1197*** (3.19)
Loss		-0.2137*** (10.74)	-0.1197*** (8.31)
Class action litigation risk		-0.0311 (1.04)	-0.0227 (1.16)
Time Trend		-0.0227*** (3.86)	-0.0016 (0.28)
Firm fixed effects	No	No	Yes
N	18,045	18,045	18,045
R^2	0.0019	0.2547	0.8531

Notes: t-statistics in parentheses. *, **, and *** represent significance at the 10%, 5%, and 1% level, respectively.