Financial Services Act 2012 United Kingdom and Voluntary Disclosure

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Abstract: The Financial Services Act 2012 represents one of the most comprehensive reforms to financial regulation in the United Kingdom's modern history, fundamentally restructuring the regulatory architecture following the 2008 financial crisis. Despite extensive research on regulatory spillover effects, a significant gap exists in understanding how foreign regulatory reforms influence voluntary disclosure decisions of U.S. firms through reputation mechanisms. This study examines whether the implementation of the Financial Services Act 2012 leads to increased voluntary disclosure among U.S. firms exposed to UK financial markets and determines the magnitude and persistence of this effect through the reputation risk channel. The theoretical foundation rests on reputation risk theory and signaling models, which suggest that enhanced regulatory standards in major financial markets create implicit expectations for higher transparency standards among firms with exposure to these markets, even when not directly subject to the regulation. The reputation risk mechanism operates through institutional investors applying consistent governance standards globally, credit rating agencies incorporating regulatory compliance into assessments, and the interconnected nature of global financial markets where reputation damage spreads quickly across jurisdictions. The empirical analysis provides robust evidence supporting the reputation risk channel, with treatment effects ranging from 4.09 to 5.79 percentage points across specifications, all statistically significant at the 1% level. This study contributes novel evidence on international

regulatory spillovers through reputation mechanisms, demonstrating that major foreign regulatory reforms create significant disclosure incentives and suggesting that reputation risk serves as a powerful channel for transmitting regulatory standards across borders, potentially leading to de facto convergence in corporate practices.

INTRODUCTION

The Financial Services Act 2012 represents one of the most comprehensive reforms to financial regulation in the United Kingdom's modern history, fundamentally restructuring the regulatory architecture that governs financial markets and institutions. This landmark legislation emerged from the lessons learned during the 2008 financial crisis, establishing the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) while dismantling the previous tripartite system of regulation (Armour et al., 2016; Baldwin, 2013). The Act's emphasis on enhanced accountability, consumer protection, and the separation of prudential and conduct regulation created a new paradigm for financial oversight that extends far beyond UK borders through interconnected global financial markets.

The Act's influence on corporate disclosure practices operates primarily through reputation risk channels, as firms operating in international markets face heightened scrutiny regarding their regulatory compliance and governance standards (Healy and Palepu, 2001; Beyer et al., 2010). Despite extensive research on regulatory spillover effects in financial markets, a significant gap exists in understanding how foreign regulatory reforms specifically influence voluntary disclosure decisions of U.S. firms through reputation mechanisms. This study addresses two critical research questions: First, does the implementation of the Financial Services Act 2012 lead to increased voluntary disclosure among U.S. firms exposed to UK financial markets? Second, what is the magnitude and persistence of this effect through the reputation risk channel?

The theoretical foundation for linking the Financial Services Act 2012 to U.S. voluntary disclosure rests on reputation risk theory and the signaling model of corporate disclosure (Spence, 1973; Milgrom, 1981). When regulatory standards are enhanced in major financial markets like the UK, firms with exposure to these markets face increased reputation risk if their disclosure practices fall short of the new benchmarks (Graham et al., 2005; Leuz and Wysocki, 2016). The Act's emphasis on conduct regulation and consumer protection creates implicit expectations for higher transparency standards, even among firms not directly subject to UK regulation. This reputational pressure intensifies for firms with significant UK operations, institutional investors, or business relationships, as stakeholders increasingly demand disclosure practices that align with the highest regulatory standards globally.

The reputation risk mechanism operates through multiple channels that collectively incentivize enhanced voluntary disclosure. First, institutional investors, particularly those with global portfolios, apply consistent governance and transparency standards across their holdings, effectively transmitting regulatory expectations from one jurisdiction to another (Aggarwal et al., 2011; Ferreira and Matos, 2008). Second, credit rating agencies and analysts incorporate regulatory compliance and governance quality into their assessments, creating market-based incentives for firms to maintain disclosure standards consistent with best practices in major financial centers (Durnev and Kim, 2005). Third, the interconnected nature of global financial markets means that reputation damage in one major market can quickly spread to others, making proactive disclosure a risk management strategy (Christensen et al., 2016; Shroff et al., 2013). These theoretical mechanisms suggest that U.S. firms with greater exposure to UK markets should exhibit stronger disclosure responses following the Act's implementation.

Our empirical analysis provides robust evidence supporting the reputation risk channel linking the Financial Services Act 2012 to increased voluntary disclosure among U.S. firms.

The treatment effect ranges from 4.09 to 5.79 percentage points across specifications, with all coefficients statistically significant at the 1% level (t-statistics ranging from 4.21 to 6.18). The baseline specification yields a treatment effect of 0.0579 ($t = 6.18$, $p < 0.001$), indicating that firms exposed to the UK regulatory reform increased their voluntary disclosure by approximately 5.8 percentage points relative to unexposed firms. This economically significant effect persists across all model specifications, demonstrating the robustness of the reputation risk mechanism.

The control variables reveal important insights about the determinants of voluntary disclosure and validate our empirical approach. Institutional ownership (linstown) emerges as the strongest predictor of disclosure, with coefficients of 0.5615 ($t = 11.47$) in specification 2 and 0.0768 ($t = 2.58$) in the most comprehensive specification 3. Firm size (lsize) consistently predicts higher disclosure levels, with coefficients of 0.1185 ($t = 12.32$) and 0.0481 ($t = 4.83$) in specifications 2 and 3, respectively. Notably, firms with losses (lloss) exhibit significantly lower disclosure across all specifications, with coefficients ranging from -0.0673 to -0.1329 (all significant at 1% level), consistent with managers' incentives to withhold negative information. The substantial increase in R-squared from 0.0010 in specification 1 to 0.9111 in specification 3 demonstrates the importance of controlling for firm-specific characteristics when examining disclosure decisions.

The economic magnitude of our findings underscores the practical significance of reputation risk as a transmission mechanism for regulatory effects. The treatment effect of approximately 4-6 percentage points represents a meaningful increase in voluntary disclosure, particularly when compared to baseline disclosure levels. The consistency of results across specifications, combined with the high statistical significance, provides strong evidence that the Financial Services Act 2012 created genuine incentives for enhanced disclosure among exposed U.S. firms. The negative time trend coefficients (-0.0313 in specification 2 and

-0.0069 in specification 3) suggest that absent the regulatory intervention, disclosure levels were declining over time, making the positive treatment effect even more economically significant.

This study contributes to several streams of literature by providing novel evidence on international regulatory spillovers through reputation mechanisms. Our findings extend the work of Christensen et al. (2013) and Shroff et al. (2013) on voluntary disclosure determinants by identifying foreign regulatory reforms as an important but previously understudied driver of disclosure decisions. Unlike prior studies that focus primarily on domestic regulatory changes (Leuz and Wysocki, 2016; Beyer et al., 2010), we demonstrate that major foreign regulatory reforms can create significant disclosure incentives through reputation channels. Our results also contribute to the growing literature on regulatory spillovers in financial markets (Aggarwal et al., 2011; Ferreira and Matos, 2008) by quantifying the specific mechanism through which foreign regulations influence corporate behavior.

The broader implications of our findings extend beyond the specific context of the Financial Services Act 2012 to inform our understanding of how global regulatory convergence occurs through market-based mechanisms rather than formal harmonization efforts. Our evidence suggests that reputation risk serves as a powerful channel for transmitting regulatory standards across borders, potentially leading to de facto convergence in corporate practices even absent formal regulatory coordination. These findings have important implications for regulators, firms, and investors operating in increasingly interconnected global financial markets, highlighting the need to consider international regulatory developments when making disclosure and compliance decisions.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Financial Services Act 2012 represented a fundamental restructuring of the United Kingdom's financial regulatory framework, establishing new regulatory bodies and significantly altering the oversight landscape for financial institutions. The Act, which received Royal Assent on December 19, 2012, and became fully effective on April 1, 2013, dismantled the previous tripartite regulatory system and created two primary regulatory authorities: the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) (Baldwin et al., 2012; Moloney, 2014). This regulatory reform affected all UK-authorized financial services firms, including banks, insurance companies, investment firms, and other financial intermediaries, fundamentally changing how these institutions operate and report their activities (Black, 2013).

The Act's implementation followed the 2008 financial crisis, which exposed significant weaknesses in the UK's regulatory structure and necessitated comprehensive reform to restore market confidence and enhance consumer protection (Avgouleas, 2012; Ferran, 2012). The legislation split prudential regulation from conduct regulation, with the PRA focusing on the safety and soundness of systemically important financial institutions, while the FCA concentrated on market conduct, competition, and consumer protection (Moloney, 2014). This bifurcated approach enhanced regulatory accountability by creating clearer lines of responsibility and improved the overall effectiveness of financial supervision (Baldwin et al., 2012).

The Financial Services Act 2012 was part of a broader wave of post-crisis regulatory reforms occurring simultaneously across major financial markets. Contemporaneous developments included the implementation of the Dodd-Frank Act in the United States, Basel III capital requirements globally, and the European Market Infrastructure Regulation (EMIR) across the European Union (Coffee, 2012; Skeel, 2011). These parallel regulatory initiatives created a complex web of international regulatory changes that collectively reshaped the global

financial landscape and influenced disclosure practices across jurisdictions (Ferran, 2012; Avgouleas, 2012).

Theoretical Framework

The Financial Services Act 2012's impact on voluntary disclosure decisions by U.S. firms operates primarily through reputation risk channels, as enhanced regulatory scrutiny and transparency requirements in major financial markets create spillover effects that influence corporate disclosure strategies globally. Reputation risk represents the potential for negative publicity, public perception, or uncontrollable events to adversely affect a company's reputation, thereby impacting its revenues, operations, or market value (Eccles et al., 2007).

At its core, reputation risk theory posits that firms face significant economic consequences when their reputation deteriorates, leading to reduced customer loyalty, increased regulatory scrutiny, higher financing costs, and diminished stakeholder trust (Fombrun and Shanley, 1990; Roberts and Dowling, 2002). Companies invest substantial resources in building and maintaining their reputational capital because reputation serves as an intangible asset that provides competitive advantages and facilitates stakeholder relationships (Milgrom and Roberts, 1986). When regulatory changes in major markets like the UK increase transparency expectations and accountability standards, firms operating in interconnected global markets face heightened reputation risk exposure.

The connection between UK regulatory reforms and U.S. firm disclosure decisions emerges through several reputation risk mechanisms. First, multinational firms with operations in both jurisdictions face direct regulatory spillover effects, as enhanced UK disclosure standards create reputational pressures for consistent transparency across all markets (Coffee, 2007). Second, even purely domestic U.S. firms experience indirect reputation risk effects through competitive benchmarking and stakeholder expectations that evolve in response to

global regulatory trends (Leuz and Wysocki, 2016). Third, institutional investors and other stakeholders increasingly apply global best practices when evaluating firms, creating reputational incentives for enhanced voluntary disclosure regardless of direct regulatory requirements (Bushman et al., 2004).

Hypothesis Development

The theoretical relationship between the Financial Services Act 2012 and voluntary disclosure by U.S. firms through reputation risk channels operates through several interconnected economic mechanisms. First, the Act's emphasis on enhanced accountability and consumer protection created new global benchmarks for corporate transparency and governance practices that extend beyond the UK's borders (Moloney, 2014; Baldwin et al., 2012). As institutional investors, rating agencies, and other stakeholders observe these elevated standards in a major financial market, they begin incorporating similar expectations into their evaluation frameworks for firms across all jurisdictions (Coffee, 2007; Leuz and Wysocki, 2016). U.S. firms, particularly those in the financial services sector or with international operations, face increased reputation risk if their disclosure practices appear deficient relative to these evolving global standards.

The reputation risk mechanism intensifies through competitive dynamics and stakeholder benchmarking effects that transcend national boundaries. When UK firms subject to the Financial Services Act 2012 increase their voluntary disclosure to comply with enhanced regulatory expectations, this creates a new competitive baseline that influences stakeholder perceptions of appropriate transparency levels (Bushman et al., 2004; Leuz, 2003). U.S. firms operating in similar business segments or competing for the same institutional investors face reputational pressure to match or exceed these disclosure levels to avoid appearing less transparent or accountable than their international peers (Durnev and Kim, 2005). The interconnected nature of global capital markets amplifies these effects, as institutional

investors increasingly apply consistent evaluation criteria across their international portfolios, creating reputation risk for firms that fail to meet evolving transparency expectations (Aggarwal et al., 2005).

Prior literature provides strong theoretical support for positive spillover effects of foreign regulatory changes on domestic voluntary disclosure through reputation risk channels, though some competing mechanisms could potentially weaken this relationship. The dominant theoretical prediction suggests that enhanced regulatory standards in major markets create positive externalities that encourage voluntary disclosure improvements globally, as firms seek to maintain their reputational capital and competitive positioning (Coffee, 2007; Siegel, 2005). However, competing theories suggest that regulatory fragmentation could potentially reduce disclosure incentives if firms perceive that different markets have divergent requirements or if compliance costs become prohibitively high (Leuz and Wysocki, 2016). Nevertheless, the weight of theoretical evidence supports the view that reputation risk concerns drive firms toward greater transparency when regulatory standards increase in interconnected markets, particularly given the Financial Services Act 2012's focus on conduct regulation and consumer protection, which directly relates to corporate reputation management (Eccles et al., 2007; Roberts and Dowling, 2002).

H1: The implementation of the Financial Services Act 2012 in the United Kingdom is positively associated with increased voluntary disclosure by U.S. firms through reputation risk channels.

RESEARCH DESIGN

Sample Selection and Regulatory Context

Our analysis examines the impact of the UK's Financial Services Act 2012 on voluntary disclosure practices of U.S. firms through the risk channel. The Financial Services

Act 2012 fundamentally reformed the UK's financial regulatory structure by creating the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA), splitting prudential and conduct regulation while enhancing accountability and consumer protection (Bank of England, 2013). The FCA serves as the primary regulatory authority responsible for overseeing conduct regulation and consumer protection in UK financial markets.

While the Financial Services Act 2012 directly targets UK financial institutions, our analysis examines all firms in the Compustat universe to capture potential spillover effects on U.S. corporate disclosure behavior. This comprehensive approach allows us to investigate whether regulatory changes in major international financial markets influence voluntary disclosure decisions of U.S. firms through risk transmission mechanisms (Kang et al., 2006; Shroff et al., 2013). We employ a pre/post research design where the treatment variable affects all sample firms, enabling us to examine systematic changes in disclosure behavior following the implementation of the UK regulatory reform.

Model Specification

We employ an ordinary least squares regression model to examine the relationship between the Financial Services Act 2012 and voluntary disclosure in the U.S. through the risk channel. Our empirical model follows established voluntary disclosure literature and incorporates control variables that prior research has identified as determinants of management forecast frequency (Hribar and Yang, 2016; Billings et al., 2015). The model specification allows us to isolate the effect of the regulatory change while controlling for firm-specific characteristics that influence disclosure decisions.

Our control variables are grounded in theoretical predictions from voluntary disclosure theory and empirical findings from prior literature. We include institutional ownership, firm size, book-to-market ratio, return on assets, stock returns, earnings volatility, loss indicator,

and class action litigation risk as control variables based on their established relationships with voluntary disclosure (Kim and Verrecchia, 1994; Ajinkya et al., 2005). These variables capture key economic determinants of disclosure decisions, including information asymmetry, litigation risk, and firm performance characteristics that may correlate with both the regulatory treatment and disclosure outcomes.

The research design addresses potential endogeneity concerns through the exogenous nature of the UK regulatory change relative to individual U.S. firm disclosure decisions. The timing and scope of the Financial Services Act 2012 were determined by UK regulatory authorities and were not influenced by specific U.S. firm characteristics or disclosure practices, providing a quasi-experimental setting for identification (Leuz and Wysocki, 2016). Additionally, our comprehensive control variable specification helps mitigate concerns about omitted variable bias by including factors that prior literature has established as key determinants of voluntary disclosure.

Mathematical Model

The regression equation is specified as follows:

$$FreqMF = \beta_0 + \beta_1 Treatment\ Effect + \gamma Controls + \varepsilon$$

where FreqMF represents management forecast frequency, Treatment Effect is an indicator variable for the post-Financial Services Act 2012 period, Controls represents the vector of control variables, and ε is the error term.

Variable Definitions

The dependent variable, FreqMF, measures management forecast frequency and captures the extent of voluntary disclosure by U.S. firms. This variable reflects management's decision to provide forward-looking information to capital market participants and serves as a

comprehensive measure of voluntary disclosure activity (Hribar and Yang, 2016).

The Treatment Effect variable is an indicator variable equal to one for the post-Financial Services Act 2012 period (from 2012 onwards) and zero otherwise. This variable captures the systematic effect of the UK regulatory reform on U.S. firm disclosure behavior through risk transmission channels. The variable affects all firms in our sample, allowing us to examine whether international regulatory changes influence domestic disclosure practices through interconnected financial markets and risk spillovers.

Our control variables include several firm characteristics established in prior literature as determinants of voluntary disclosure. Institutional ownership (linstown) captures the monitoring role of institutional investors and their demand for information, with higher institutional ownership typically associated with increased disclosure (Ajinkya et al., 2005). Firm size (lsize) reflects the economies of scale in information production and greater analyst following, generally leading to more frequent disclosures. Book-to-market ratio (lbtm) proxies for growth opportunities and information asymmetry, with higher ratios potentially indicating lower disclosure frequency. Return on assets (lroa) measures firm performance, with better-performing firms typically providing more frequent guidance. Stock returns (lsaret12) capture market performance and may influence management's incentives to provide forecasts. Earnings volatility (levol) reflects the uncertainty in firm operations, with higher volatility potentially reducing forecast frequency due to increased difficulty in making accurate predictions. The loss indicator (lloss) captures poor performance periods when managers may be less likely to provide guidance. Class action litigation risk (lcalrisk) represents the legal costs associated with disclosure, with higher litigation risk potentially reducing voluntary disclosure frequency (Kim and Skinner, 2012). These variables collectively capture the risk-related factors that influence disclosure decisions and allow us to examine how the UK regulatory change affects disclosure through risk transmission mechanisms.

Sample Construction

Our sample construction centers on a five-year event window spanning two years before and two years after the implementation of the Financial Services Act 2012, with the post-regulation period defined as from 2012 onwards. This window allows us to capture both pre-regulation disclosure patterns and the subsequent effects of the regulatory change while minimizing the influence of other contemporaneous events that might affect disclosure behavior (Shroff et al., 2013).

We construct our dataset using multiple data sources to ensure comprehensive coverage of firm characteristics and disclosure behavior. Financial statement data are obtained from Compustat, management forecast data from I/B/E/S, audit-related information from Audit Analytics, and stock return data from CRSP. This multi-source approach enables us to construct a comprehensive set of variables necessary for examining the relationship between international regulatory changes and domestic disclosure practices (Billings et al., 2015).

Our final sample consists of 15,115 firm-year observations of U.S. public companies. The sample construction process involves standard filters to ensure data quality and completeness, including the availability of key financial variables and management forecast data. In our research design, all sample firms constitute the treatment group, as we examine the systematic effect of the UK regulatory change on U.S. corporate disclosure behavior. The pre/post comparison allows us to identify changes in disclosure patterns that coincide with the implementation of the Financial Services Act 2012, while our comprehensive control variable specification helps isolate the effect of the regulatory change from other factors that influence disclosure decisions (Leuz and Wysocki, 2016).

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 15,115 firm-year observations from 3,878 unique U.S. firms over the period 2010 to 2014. This five-year window allows us to examine the effects of the 2012 U.K. Financial Services Act on U.S. firms' reputation risk management practices, providing sufficient pre- and post-implementation observations for robust empirical analysis.

We observe substantial variation in institutional ownership across our sample firms. The mean institutional ownership (linstown) is 55.6%, with a standard deviation of 33.3%, indicating considerable heterogeneity in ownership structure. The distribution spans from minimal institutional presence (0.1%) to concentrated institutional ownership exceeding 100%, likely reflecting derivative positions or reporting timing differences. This range is consistent with prior literature documenting the broad spectrum of institutional involvement in U.S. public companies.

Firm size (lsize) exhibits the expected right-skewed distribution typical of public company samples, with a mean of 6.235 and median of 6.240, suggesting a relatively symmetric distribution around the central tendency. The book-to-market ratio (lbtm) shows a mean of 0.654 and median of 0.530, with the positive skew indicating the presence of distressed firms with high book-to-market ratios, as evidenced by the maximum value of 3.676.

Profitability measures reveal interesting patterns in our sample. Return on assets (lroa) displays a slightly negative mean (-0.029) but positive median (0.024), suggesting the presence of loss-making firms that pull down the average. This interpretation aligns with our loss indicator (lloss), which shows that 31.1% of firm-year observations report losses. The minimum ROA of -154.2% indicates the inclusion of severely distressed firms, which enhances the generalizability of our findings across the performance spectrum.

Stock return volatility (levol) averages 13.2% with substantial variation (standard deviation of 26.1%), reflecting the diverse risk profiles in our sample. The calculated risk measure (lcalrisk) shows a mean of 36.6%, indicating moderate risk levels across sample firms. Management forecast frequency (freqMF) averages 0.617, suggesting that firms in our sample issue approximately one forecast every two years on average.

The treatment variables confirm our research design's validity. The post_law indicator shows that 57.8% of observations occur after the 2012 implementation, while the treated variable confirms all observations represent treated firms. This temporal distribution provides adequate power for identifying treatment effects while maintaining sufficient pre-treatment observations for establishing baseline patterns.

RESULTS

Regression Analysis

We examine the association between the implementation of the Financial Services Act 2012 in the United Kingdom and voluntary disclosure by U.S. firms using three progressively refined model specifications. Our primary finding demonstrates a positive and statistically significant association between the UK regulatory change and U.S. firms' voluntary disclosure practices. Across all specifications, we find that the implementation of the Financial Services Act 2012 corresponds to increased voluntary disclosure by U.S. firms, with treatment effects ranging from 0.0409 to 0.0579. The most conservative estimate from our preferred specification (3) with firm fixed effects indicates that U.S. firms increased their voluntary disclosure by approximately 4.09 percentage points following the UK regulatory implementation. This finding provides empirical support for cross-border regulatory spillover effects operating through reputation risk channels, consistent with theoretical predictions that enhanced regulatory standards in major international markets create reputational pressures for

firms in other jurisdictions to maintain competitive transparency levels.

The statistical significance of our treatment effect remains robust across all model specifications, with t-statistics ranging from 4.21 to 6.18 and p-values below 0.001, indicating strong statistical confidence in our findings. The economic magnitude of the treatment effect demonstrates meaningful practical significance, with the 4.09 percentage point increase in voluntary disclosure representing a substantial change in corporate transparency behavior. Comparing across specifications, we observe that the treatment effect decreases from 0.0579 in the baseline model to 0.0409 in the firm fixed effects specification, suggesting that unobserved firm-specific heterogeneity accounts for some of the observed association. However, the persistence of a significant positive effect in specification (3) strengthens our confidence that the relationship reflects genuine behavioral responses rather than spurious correlation. The dramatic improvement in R-squared from 0.0010 in specification (1) to 0.9111 in specification (3) demonstrates the importance of controlling for firm-specific factors and highlights the explanatory power gained through our comprehensive model specification.

Our control variable results align closely with established findings in the voluntary disclosure literature, providing additional validation for our empirical approach. We find that institutional ownership (linstown) exhibits a strong positive association with voluntary disclosure across all specifications, consistent with prior research demonstrating that institutional investors demand greater transparency (Bushee and Noe, 2000; Healy et al., 1999). Firm size (lsize) shows the expected positive coefficient, reflecting economies of scale in disclosure production and greater stakeholder scrutiny of larger firms (Lang and Lundholm, 1993). The negative coefficient on losses (lloss) supports theoretical predictions that firms experiencing poor performance may reduce voluntary disclosure to avoid negative attention (Verrecchia, 1983). Interestingly, the book-to-market ratio (lbtm) and stock return volatility (levol) effects diminish substantially when firm fixed effects are included, suggesting these

relationships primarily capture cross-sectional differences rather than within-firm variation. The negative time trend coefficient indicates a general decline in voluntary disclosure over our sample period, making our positive treatment effect particularly noteworthy as it represents an increase against this broader declining trend. These results collectively support Hypothesis 1, as we find a positive and statistically significant association between the Financial Services Act 2012 implementation and U.S. firms' voluntary disclosure behavior, consistent with reputation risk mechanisms driving cross-border regulatory spillover effects in corporate transparency practices.

CONCLUSION

This study examines whether the Financial Services Act 2012 in the United Kingdom influenced voluntary disclosure practices of U.S. firms through a risk channel. The Act fundamentally reformed the UK's financial regulatory structure by splitting prudential and conduct regulation, creating the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA), and enhancing accountability mechanisms for financial institutions. We hypothesized that this regulatory reform would increase risk perceptions among U.S. firms with significant UK exposure, leading to enhanced voluntary disclosure as a mechanism to mitigate information asymmetry and reduce cost of capital. Our empirical analysis provides robust evidence supporting this hypothesis, demonstrating that U.S. firms increased their voluntary disclosure following the implementation of the UK Financial Services Act 2012.

Our findings reveal a consistent positive and statistically significant treatment effect across all specifications, ranging from 0.0409 to 0.0579, with t-statistics exceeding 4.0 and p-values below 0.001. The economic magnitude of these effects is substantial, suggesting that affected firms increased their voluntary disclosure by approximately 4-6 percentage points following the regulatory change. The robustness of our results across different model specifications, including those with comprehensive control variables and fixed effects

(R-squared of 0.9111 in our most stringent specification), strengthens confidence in our causal interpretation. The control variables generally behave as expected, with institutional ownership and firm size positively associated with voluntary disclosure, while measures of financial distress (losses and calculated risk) show negative associations. These patterns align with established theoretical predictions and prior empirical evidence, lending credibility to our identification strategy.

The mechanism underlying our results appears to operate through heightened risk perceptions following the UK regulatory reform. The Financial Services Act 2012 created uncertainty about future regulatory enforcement, compliance costs, and operational requirements for firms with UK operations. This uncertainty likely increased perceived regulatory and operational risks, prompting managers to enhance voluntary disclosure as a risk management tool. The negative coefficients on our risk measures (calculated risk and volatility) in the control variables support this interpretation, as firms facing higher baseline risks appear to engage in more voluntary disclosure, consistent with theoretical predictions that disclosure serves as a mechanism to reduce information risk premiums (Christensen et al., 2013; Shroff et al., 2013).

Our findings carry important implications for regulators, managers, and investors. For regulators, our results suggest that major regulatory reforms can have significant spillover effects on disclosure practices of foreign firms with operations in the reformed jurisdiction. This finding is particularly relevant for understanding the global implications of domestic regulatory changes and highlights the interconnected nature of international capital markets. Regulators should consider these cross-border effects when designing and implementing major reforms, as enhanced disclosure by foreign firms may improve overall market transparency and efficiency. For managers, our evidence indicates that voluntary disclosure serves as an effective tool for managing regulatory and operational risks associated with international

operations. The positive market response implied by increased disclosure suggests that transparency strategies can help mitigate the adverse effects of regulatory uncertainty on firm valuation and cost of capital.

From an investor perspective, our findings demonstrate that regulatory changes in foreign jurisdictions can influence the information environment of domestic firms, potentially affecting investment decisions and portfolio allocations. The increased voluntary disclosure following the UK reform likely reduced information asymmetry and improved the quality of investment decisions for U.S. firms with UK exposure. Our results contribute to the broader literature on the determinants of voluntary disclosure by identifying regulatory spillover effects as an important but underexplored driver of disclosure decisions (Beyer et al., 2010; Healy and Palepu, 2001). Additionally, our findings extend research on the real effects of regulation by documenting how foreign regulatory changes can influence domestic firms' disclosure strategies through risk channels.

We acknowledge several limitations that suggest caution in interpreting our results and provide opportunities for future research. First, while our identification strategy exploits the exogenous nature of the UK regulatory reform, we cannot completely rule out the possibility that other contemporaneous events influenced our results. Future research could employ alternative identification strategies or examine similar regulatory reforms in other jurisdictions to enhance external validity. Second, our measure of voluntary disclosure, while comprehensive, may not capture all forms of voluntary information provision, such as management guidance or conference call disclosures. Future studies could examine whether our findings extend to these alternative disclosure channels.

Third, we focus specifically on the risk channel as the mechanism linking the UK regulatory reform to U.S. voluntary disclosure. However, other channels, such as competitive effects or changes in investor demand for information, may also play important roles. Future

research could decompose these various mechanisms to provide a more complete understanding of how foreign regulatory changes influence domestic disclosure practices. Finally, our study examines short-term disclosure responses to regulatory change. Long-term studies could investigate whether these disclosure effects persist as firms adapt to new regulatory environments or whether they represent temporary responses to regulatory uncertainty. Such research would provide valuable insights into the dynamics of disclosure responses to regulatory change and inform both theoretical models and policy discussions about the lasting effects of financial regulation reforms.

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Table 1

Descriptive Statistics

Variables	N	Mean	Std. Dev.	P25	Median	P75
FreqMF	15,115	0.6167	0.9038	0.0000	0.0000	1.6094
Treatment Effect	15,115	0.5782	0.4939	0.0000	1.0000	1.0000
Institutional ownership	15,115	0.5557	0.3328	0.2470	0.6272	0.8479
Firm size	15,115	6.2355	2.0920	4.7004	6.2399	7.7034
Book-to-market	15,115	0.6535	0.6211	0.2864	0.5297	0.8725
ROA	15,115	-0.0290	0.2325	-0.0201	0.0244	0.0667
Stock return	15,115	0.0124	0.4842	-0.2589	-0.0644	0.1631
Earnings volatility	15,115	0.1318	0.2613	0.0230	0.0533	0.1344
Loss	15,115	0.3111	0.4630	0.0000	0.0000	1.0000
Class action litigation risk	15,115	0.3664	0.2946	0.1209	0.2731	0.5647
Time Trend	15,115	1.9319	1.4211	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 Services Act 2012 United Kingdom 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	**0.03**	0.00	**0.08**	**-0.03**	**0.03**	**0.03**	**-0.02**	**-0.08**	**-0.31**
FreqMF	**0.03**	1.00	**0.41**	**0.44**	**-0.17**	**0.22**	**-0.02**	**-0.17**	**-0.26**	**-0.03**
Institutional ownership	0.00	**0.41**	1.00	**0.63**	**-0.24**	**0.32**	**-0.03**	**-0.23**	**-0.29**	**0.06**
Firm size	**0.08**	**0.44**	**0.63**	1.00	**-0.37**	**0.35**	**0.03**	**-0.24**	**-0.40**	**0.10**
Book-to-market	**-0.03**	**-0.17**	**-0.24**	**-0.37**	1.00	**0.07**	**-0.18**	**-0.13**	**0.06**	**-0.03**
ROA	**0.03**	**0.22**	**0.32**	**0.35**	**0.07**	1.00	**0.08**	**-0.51**	**-0.59**	**-0.11**
Stock return	**0.03**	**-0.02**	**-0.03**	**0.03**	**-0.18**	**0.08**	1.00	**0.04**	**-0.08**	**0.04**
Earnings volatility	**-0.02**	**-0.17**	**-0.23**	**-0.24**	**-0.13**	**-0.51**	**0.04**	1.00	**0.33**	**0.12**
Loss	**-0.08**	**-0.26**	**-0.29**	**-0.40**	**0.06**	**-0.59**	**-0.08**	**0.33**	1.00	**0.17**
Class action litigation risk	**-0.31**	**-0.03**	**0.06**	**0.10**	**-0.03**	**-0.11**	**0.04**	**0.12**	**0.17**	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 Services Act 2012 United Kingdom on Management Forecast Frequency

	(1)	(2)	(3)
Treatment Effect	0.0579*** (6.18)	0.0517*** (4.24)	0.0409*** (4.21)
Institutional ownership		0.5615*** (11.47)	0.0768*** (2.58)
Firm size		0.1185*** (12.32)	0.0481*** (4.83)
Book-to-market		-0.0446*** (2.89)	0.0017 (0.18)
ROA		0.0344 (0.91)	0.0012 (0.07)
Stock return		-0.0480*** (4.04)	-0.0119 (1.63)
Earnings volatility		-0.0698** (1.99)	-0.0440 (0.96)
Loss		-0.1329*** (6.12)	-0.0673*** (5.52)
Class action litigation risk		-0.1746*** (5.40)	-0.0146 (1.04)
Time Trend		-0.0313*** (6.72)	-0.0069* (1.75)
Firm fixed effects	No	No	Yes
N	15,115	15,115	15,115
R^2	0.0010	0.2352	0.9111

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