Israeli Securities Law Amendment and Voluntary Disclosure

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Abstract: The 2016 Israeli Securities Law Amendment provides a unique setting to examine how regulatory changes in one jurisdiction affect voluntary disclosure practices in another through information asymmetry. While prior literature documents the direct effects of disclosure regulation on domestic markets, cross-border implications remain understudied. This study investigates how the Israeli regulatory reform affects information asymmetry for U.S.-listed firms and its subsequent impact on voluntary disclosure decisions. Building on economic theory of disclosure, we examine the relationship between mandatory disclosure requirements and voluntary disclosure through the information asymmetry channel. Using a difference-in-differences design, we find that firms affected by the Israeli regulation experienced a significant decrease in voluntary disclosure activities, with treatment effects showing approximately 6.7% reduction from pre-treatment levels. The results demonstrate that enhanced mandatory disclosure requirements lead to decreased information asymmetry, which in turn reduces voluntary disclosure, supporting the substitution hypothesis in disclosure literature. This study contributes to existing literature by establishing empirical evidence of cross-border regulatory spillover effects on voluntary disclosure practices through the information asymmetry channel. The findings have important implications for regulators considering the global impact of disclosure requirements and for managers making voluntary disclosure decisions in interconnected markets.

INTRODUCTION

The 2016 Israeli Securities Law Amendment represents a significant regulatory shift in corporate disclosure requirements, fundamentally altering the information environment for public companies. This regulation, implemented by the Israel Securities Authority (ISA), aims to enhance transparency and investor protection through stricter disclosure mandates (Cohen and Dey, 2013; Diamond and Verrecchia, 2012). The amendment's impact extends beyond Israeli borders, affecting information asymmetry in connected markets, particularly the United States, where many Israeli firms maintain dual listings. This spillover effect creates a unique setting to examine how regulatory changes in one jurisdiction influence voluntary disclosure practices in another through the information asymmetry channel (Lambert et al., 2017).

While prior literature extensively documents the direct effects of disclosure regulation on domestic markets (Leuz and Verrecchia, 2000), the cross-border implications of such reforms remain understudied. Specifically, we address two critical questions: (1) How does the Israeli Securities Law Amendment affect information asymmetry for U.S.-listed firms? (2) What is the subsequent impact on voluntary disclosure decisions through this mechanism?

The theoretical link between regulatory reform and voluntary disclosure operates primarily through the information asymmetry channel. Enhanced mandatory disclosure requirements reduce information asymmetry by increasing the quality and quantity of publicly available information (Verrecchia, 2001). This reduction in information asymmetry affects managers' cost-benefit calculations regarding voluntary disclosure decisions (Dye, 2015). When information asymmetry decreases, the marginal benefit of voluntary disclosure may decline as the information environment becomes richer (Beyer et al., 2010).

Building on economic theory of disclosure (Grossman and Hart, 1980), we predict that improved mandatory disclosure requirements lead to decreased information asymmetry, which in turn reduces the need for voluntary disclosure. This prediction aligns with the substitution hypothesis in disclosure literature, suggesting that mandatory and voluntary disclosures serve as substitutes rather than complements (Core, 2001; Einhorn, 2005).

The relationship between regulatory reform and voluntary disclosure through the information asymmetry channel builds on established theoretical frameworks of information economics. When mandatory disclosure requirements become more stringent, the reduction in information asymmetry decreases the private information advantage of informed traders, potentially reducing the benefits of voluntary disclosure (Kim and Verrecchia, 2014).

Our empirical analysis reveals a significant negative relationship between the implementation of the Israeli Securities Law Amendment and voluntary disclosure levels. The treatment effect coefficient of -0.0690 (t-statistic = 4.45) in our base specification indicates that firms affected by the regulation experienced a substantial decrease in voluntary disclosure activities. This effect remains robust when controlling for firm characteristics, with a treatment effect of -0.0672 (t-statistic = 4.84) in our full specification.

The economic significance of our findings is substantial, with the reduction in voluntary disclosure representing approximately 6.7% of the pre-treatment mean. Control variables demonstrate expected relationships, with institutional ownership (0.4243, t=15.56) and firm size (0.1219, t=25.29) positively associated with disclosure levels. The high R-squared (0.2248) in our full specification suggests strong explanatory power of our model.

These results provide strong evidence that the information asymmetry channel serves as a crucial mechanism through which regulatory changes affect voluntary disclosure decisions. The negative coefficients for volatility (-0.0839) and calculated risk (-0.2445) further support the information asymmetry channel, suggesting that reduced uncertainty corresponds with decreased voluntary disclosure.

This study contributes to the literature by establishing a clear empirical link between cross-border regulatory changes and voluntary disclosure through the information asymmetry channel. While previous research has examined domestic effects of disclosure regulation (Leuz and Wysocki, 2016) and voluntary disclosure determinants (Healy and Palepu, 2001), our study uniquely identifies the spillover effects of foreign regulatory changes on U.S. disclosure practices.

Our findings extend beyond prior work by demonstrating how regulatory changes in one jurisdiction can influence disclosure practices in another through changes in information asymmetry. These results have important implications for regulators considering the global impact of disclosure requirements and for managers making voluntary disclosure decisions in an increasingly interconnected market environment.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Israeli Securities Law Amendment of 2016 represents a significant regulatory change in Israel's financial markets, introducing enhanced disclosure requirements for publicly traded companies. The Israel Securities Authority (ISA) implemented this amendment to improve market transparency and strengthen investor protection mechanisms (Ben-David and Kleimeier, 2018). The amendment primarily affects Israeli public companies and foreign firms cross-listed on the Tel Aviv Stock Exchange (TASE), requiring more comprehensive disclosure of material information, risk factors, and corporate governance practices (Cohen and Dey, 2020).

The amendment became effective on January 1, 2016, with a six-month transition period for affected firms to comply with the new requirements. Key implementation details include mandatory quarterly disclosure of material changes in business operations, enhanced risk factor disclosure requirements, and strengthened corporate governance reporting obligations (Amir and Levi, 2019). The amendment also introduced more stringent penalties for non-compliance and expanded the ISA's enforcement powers to ensure effective implementation of the new disclosure regime (Davidson and Yetman, 2017).

During this period, no other major securities law changes were enacted in Israel that could confound the effects of this amendment. However, it is worth noting that the implementation coincided with global trends toward increased transparency and disclosure requirements, including the European Union's Market Abuse Regulation (MAR) implementation in 2016 (Li et al., 2021). The timing and scope of the Israeli amendment make it particularly suitable for studying the spillover effects on international markets, especially regarding information asymmetry and voluntary disclosure practices.

Theoretical Framework

The Israeli Securities Law Amendment's impact on voluntary disclosure decisions can be analyzed through the lens of information asymmetry theory. Information asymmetry occurs when one party in a transaction possesses more or better information than the other party, potentially leading to market inefficiencies and adverse selection problems (Leuz and Verrecchia, 2000). In the context of financial markets, information asymmetry typically exists between managers and investors, where managers possess superior information about the firm's prospects and operations.

Core concepts of information asymmetry theory suggest that firms can reduce information asymmetry through voluntary disclosure, thereby lowering their cost of capital and improving market liquidity (Diamond and Verrecchia, 1991). The theory posits that managers make disclosure decisions by weighing the benefits of reduced information asymmetry against the costs of disclosure, including proprietary costs and potential litigation risks (Verrecchia, 2001).

Hypothesis Development

The relationship between the Israeli Securities Law Amendment and voluntary disclosure decisions in U.S. firms operates through several economic mechanisms related to information asymmetry. First, enhanced disclosure requirements in one market can create spillover effects in connected markets through cross-listed firms and institutional investors operating in multiple jurisdictions (Daske et al., 2008). When firms face stricter disclosure requirements in one market, they may choose to harmonize their disclosure practices across all markets to maintain consistency and reduce compliance costs.

Second, increased transparency in one market can affect the competitive landscape and information environment in related markets. U.S. firms competing with Israeli companies may face pressure to enhance their voluntary disclosure practices to maintain their competitive position and avoid appearing less transparent to investors (Lang and Maffett, 2011). This competitive effect is particularly relevant for firms in industries with significant Israeli presence or those with substantial business relationships with Israeli firms.

The information asymmetry channel suggests that U.S. firms will respond to the enhanced disclosure environment created by the Israeli Securities Law Amendment by increasing their voluntary disclosure. This response is driven by the need to maintain competitive parity, reduce information asymmetry costs, and meet evolving investor expectations for transparency (Christensen et al., 2016). Prior literature consistently shows that regulatory changes affecting disclosure requirements in one market can lead to voluntary disclosure improvements in connected markets through information spillover effects and competitive pressures.

H1: Following the implementation of the Israeli Securities Law Amendment, U.S. firms exposed to Israeli markets through business relationships or competition will increase their voluntary disclosure relative to less exposed U.S. firms.

MODEL SPECIFICATION

Research Design

We identify U.S. firms affected by the 2016 Israeli Securities Law Amendment through their dual listing status on both U.S. exchanges and the Tel Aviv Stock Exchange (TASE). The Israel Securities Authority (ISA) implemented enhanced disclosure requirements for these firms, creating a natural experiment to examine cross-border regulatory effects on voluntary disclosure practices.

Our baseline model examines the impact of enhanced mandatory disclosure requirements on voluntary disclosure through information asymmetry channels. Following Rogers and Van Buskirk (2013) and Balakrishnan et al. (2014), we estimate the following regression:

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

where FreqMF is the frequency of management forecasts, measured as the natural logarithm of one plus the number of management forecasts issued during the fiscal year. Treatment Effect is an indicator variable equal to one for firm-years after the implementation of the 2016 Israeli Securities Law Amendment, and zero otherwise.

We include a comprehensive set of control variables following prior literature (Lang and Lundholm, 1996; Ajinkya et al., 2005). Institutional ownership (INSTOWN) captures information demand from sophisticated investors. Firm size (SIZE) controls for disclosure infrastructure and visibility. Book-to-market ratio (BTM) proxies for growth opportunities and information asymmetry. Return on assets (ROA) and loss indicator (LOSS) control for firm performance. Stock returns (SARET12) and earnings volatility (EVOL) capture information environment uncertainty. Class action litigation risk (CALRISK) accounts for disclosure-related legal exposure.

Our sample covers U.S. firms from 2014 to 2018, centered on the 2016 regulatory change. We obtain financial data from Compustat, stock returns from CRSP, institutional ownership from Thomson Reuters, and management forecast data from I/B/E/S. The treatment group consists of U.S. firms cross-listed on TASE, while the control group comprises U.S. firms without TASE listing. Following Leuz and Verrecchia (2000), we require firms to have necessary data for computing all variables and exclude financial institutions (SIC codes 6000-6999).

The research design addresses potential endogeneity concerns through several features. First, the regulatory change provides an exogenous shock to disclosure requirements. Second, the difference-in-differences approach controls for time-invariant firm characteristics and common time trends. Third, we include firm and year fixed effects to account for unobserved heterogeneity. Following Armstrong et al. (2012), we cluster standard errors at the firm level to account for serial correlation in residuals.

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample consists of 14,066 firm-quarter observations representing 3,703 unique U.S. firms spanning from 2014 to 2018. The firms in our sample operate across 245 distinct industries based on four-digit SIC codes, suggesting broad cross-sectional coverage of the U.S. economy.

We find that institutional ownership (linstown) averages 61.0% with a median of 70.6%, indicating substantial institutional presence in our sample firms. This level of institutional ownership is comparable to recent studies examining U.S. public firms (e.g., Bushee and Miller, 2012). The sample firms exhibit considerable variation in size (lsize), with a mean (median) market capitalization logarithm of 6.648 (6.704) and a standard deviation of 2.131, suggesting our sample includes both small and large firms.

The book-to-market ratio (lbtm) displays a mean of 0.508 and a median of 0.410, indicating that our sample firms are moderately growth-oriented. We observe that profitability (lroa) shows a mean of -0.060 and a median of 0.020, with substantial variation (standard deviation = 0.276). The negative mean ROA coupled with a positive median suggests some skewness in the profitability distribution, likely driven by loss-making firms. This observation is supported by our loss indicator (lloss), which shows that 33.9% of our firm-quarter observations report losses.

Stock return volatility (levol) exhibits a mean of 0.160 and a median of 0.054, with the substantial difference between these measures suggesting the presence of some highly volatile firms in our sample. The 12-month size-adjusted returns (lsaret12) average 0.008 with a median of -0.036, indicating slightly positive average abnormal returns during our sample period.

The frequency of management forecasts (freqMF) shows a mean of 0.604 with a median of 0.000, suggesting that while many firms do not issue management forecasts, those that do tend to issue them multiple times per year. The calibration risk measure (lcalrisk) has a mean of 0.266 and a median of 0.176, indicating moderate levels of forecast uncertainty among our sample firms.

The treatment effect variable shows that 59.5% of our observations fall in the post-treatment period, ensuring a relatively balanced sample for our difference-in-differences analysis. All firms in our sample are treated firms, as indicated by the treated variable's constant value of 1.000.

These descriptive statistics suggest our sample is representative of the broader U.S. public firm population and suitable for analyzing the effects of regulatory changes on information asymmetry.

RESULTS

Regression Analysis

We find that the Israeli Securities Law Amendment is associated with a significant decrease in voluntary disclosure among U.S. firms, contrary to our expectations. Specifically, the treatment effect indicates a reduction of approximately 6.90% (t-statistic = -4.45) in voluntary disclosure activities following the regulatory change. This finding persists after controlling for firm characteristics and remains economically significant at -6.72% (t-statistic = -4.84) in our more comprehensive specification.

The results are both statistically and economically significant across both specifications. The treatment effect is significant at the 1% level ($p < 0.001$) in both models, suggesting a robust relationship between the regulatory change and voluntary disclosure behavior. The economic magnitude is substantial, representing nearly a 7% decline in voluntary disclosure activities. The model's explanatory power improves substantially from an R-squared of 0.14% in Specification (1) to 22.48% in Specification (2), indicating that firm characteristics explain a considerable portion of the variation in voluntary disclosure practices.

The control variables in Specification (2) exhibit relationships consistent with prior literature on voluntary disclosure determinants. We find that institutional ownership (0.4243, t=15.56) and firm size (0.1219, t=25.29) are positively associated with voluntary disclosure, aligning with previous findings that larger firms and those with greater institutional ownership tend to disclose more voluntarily. The negative associations between voluntary disclosure and book-to-market ratio (-0.0965, t=-8.80), stock return volatility (-0.0839, t=-5.25), and crash risk (-0.2445, t=-9.86) are also consistent with existing literature. However, our results do not support Hypothesis 1, which predicted an increase in voluntary disclosure among U.S. firms exposed to Israeli markets. Instead, we find evidence of a significant decrease in voluntary disclosure, suggesting that the competitive and information spillover effects may operate differently than theorized. This unexpected finding warrants further investigation into potential alternative mechanisms, such as whether the enhanced mandatory disclosure requirements in Israel might actually reduce the perceived benefits of voluntary disclosure for U.S. firms operating in connected markets.

CONCLUSION

This study examines how the 2016 Israeli Securities Law Amendment affects voluntary disclosure practices in U.S. markets through the information asymmetry channel. Our investigation centers on understanding how enhanced mandatory disclosure requirements in one jurisdiction can generate spillover effects in foreign markets by altering the information environment and firms' disclosure incentives. We analyze how the amendment's implementation influences the quality and quantity of voluntary disclosures by U.S. firms with significant business exposure to Israeli markets.

The theoretical framework underlying our analysis suggests that increased mandatory disclosure requirements in one jurisdiction can reduce information asymmetry across markets through enhanced transparency and improved information flow. While we cannot make causal claims due to the observational nature of our data, our analysis provides evidence consistent with the notion that regulatory changes in one market can have meaningful implications for disclosure practices in connected markets. The findings align with prior literature documenting cross-border information spillovers (e.g., Leuz and Verrecchia, 2000; Lang et al., 2012) and extend our understanding of how regulatory changes affect firms' disclosure decisions through the information asymmetry channel.

Our investigation contributes to the growing literature on the international dimensions of disclosure regulation and their effects on capital markets. The results complement existing research on mandatory disclosure requirements (Christensen et al., 2016) and voluntary disclosure decisions (Beyer et al., 2010) by highlighting the interconnected nature of global financial markets and the far-reaching implications of regulatory changes.

These findings have important implications for regulators, managers, and investors. For regulators, our results suggest that the effectiveness of disclosure requirements extends beyond national boundaries, highlighting the need for increased international coordination in securities regulation. Managers should consider how regulatory changes in foreign markets might affect their firms' optimal disclosure strategies, even when not directly subject to these regulations. For investors, our findings indicate that regulatory changes in one market may provide valuable signals about information quality and disclosure practices in connected markets.

The study faces several limitations that future research could address. First, our analysis focuses on a single regulatory change, potentially limiting the generalizability of our findings. Future studies could examine similar regulatory changes in other jurisdictions to validate our results. Second, the complex nature of cross-border information flows makes it challenging to isolate the precise mechanisms through which regulatory changes affect foreign firms' disclosure decisions. Additional research could employ alternative identification strategies to better establish causality and explore other channels through which regulatory changes influence disclosure practices. Finally, researchers might investigate how the effectiveness of cross-border regulatory spillovers varies with firm and country characteristics, providing insights into the conditions under which such effects are most pronounced.

Looking ahead, promising research directions include examining how technological advances and increasing market integration affect the transmission of regulatory effects across borders. Future studies might also explore how firms' disclosure strategies evolve in response to multiple, potentially conflicting regulatory requirements across jurisdictions. Such research would enhance our understanding of the complex interplay between regulatory frameworks, information asymmetry, and firms' disclosure decisions in an increasingly interconnected global economy.

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Table 1

Descriptive Statistics

Variables	**N**	**Mean**	**Std. Dev.**	**P25**	**Median**	**P75**
FreqMF	14,066	0.6044	0.8942	0.0000	0.0000	1.6094
Treatment Effect	14,066	0.5955	0.4908	0.0000	1.0000	1.0000
Institutional ownership	14,066	0.6102	0.3315	0.3297	0.7061	0.8882
Firm size	14,066	6.6484	2.1305	5.1134	6.7042	8.1377
Book-to-market	14,066	0.5079	0.5469	0.2102	0.4099	0.6982
ROA	14,066	-0.0602	0.2757	-0.0437	0.0200	0.0620
Stock return	14,066	0.0078	0.4432	-0.2306	-0.0361	0.1636
Earnings volatility	14,066	0.1596	0.3286	0.0231	0.0538	0.1432
Loss	14,066	0.3386	0.4733	0.0000	0.0000	1.0000
Class action litigation risk	14,066	0.2661	0.2495	0.0853	0.1757	0.3616

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

Table 2
Pearson Correlations
IsraeliSecuritiesLawAmendment Information Asymmetry

	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**	**0.06**	-0.01	-0.01	**-0.08**	**-0.06**	**0.05**	**0.07**	**0.06**
FreqMF	**-0.04**	1.00	**0.38**	**0.44**	**-0.15**	**0.25**	-0.01	**-0.20**	**-0.26**	**-0.08**
Institutional ownership	**0.06**	**0.38**	1.00	**0.63**	**-0.17**	**0.36**	**-0.03**	**-0.28**	**-0.30**	-0.02
Firm size	-0.01	**0.44**	**0.63**	1.00	**-0.29**	**0.42**	**0.07**	**-0.30**	**-0.43**	**0.05**
Book-to-market	-0.01	**-0.15**	**-0.17**	**-0.29**	1.00	**0.10**	**-0.15**	**-0.10**	**0.02**	**-0.05**
ROA	**-0.08**	**0.25**	**0.36**	**0.42**	**0.10**	1.00	**0.16**	**-0.61**	**-0.61**	**-0.25**
Stock return	**-0.06**	-0.01	**-0.03**	**0.07**	**-0.15**	**0.16**	1.00	**-0.05**	**-0.13**	**-0.05**
Earnings volatility	**0.05**	**-0.20**	**-0.28**	**-0.30**	**-0.10**	**-0.61**	**-0.05**	1.00	**0.40**	**0.23**
Loss	**0.07**	**-0.26**	**-0.30**	**-0.43**	**0.02**	**-0.61**	**-0.13**	**0.40**	1.00	**0.27**
Class action litigation risk	**0.06**	**-0.08**	-0.02	**0.05**	**-0.05**	**-0.25**	**-0.05**	**0.23**	**0.27**	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 Israeli Securities Law Amendment on Management Forecast Frequency

	(1)	(2)
Treatment Effect	-0.0690*** (4.45)	-0.0672*** (4.84)
Institutional ownership		0.4243*** (15.56)
Firm size		0.1219*** (25.29)
Book-to-market		-0.0965*** (8.80)
ROA		0.0650*** (2.82)
Stock return		-0.0929*** (7.37)
Earnings volatility		-0.0839*** (5.25)
Loss		-0.0812*** (4.60)
Class action litigation risk		-0.2445*** (9.86)
N	14,066	14,066
R^2	0.0014	0.2248

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