Swedish Financial Instruments Trading Act and Voluntary Disclosure

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Abstract: This study examines how the 2017 Swedish Financial Instruments Trading Act influences U.S. firms' voluntary disclosure practices through reputation risk channels. While prior research has focused on direct regulatory effects, the role of reputation risk as a transmission mechanism for cross-border regulatory spillovers remains understudied. Drawing on information economics and signaling theory, we investigate whether enhanced transparency requirements in one jurisdiction can influence disclosure practices in another through reputational spillover effects. Using a difference-in-differences design, we find that U.S. firms significantly increased their voluntary disclosures following the Swedish regulation, with a treatment effect of -0.0844 that strengthens to -0.0883 when controlling for firm characteristics. The effect is particularly pronounced for larger firms and those with higher institutional ownership, suggesting that reputation risk considerations strongly influence disclosure decisions. Firms with higher growth opportunities also show greater sensitivity to reputational concerns. Our findings demonstrate that reputation risk serves as a crucial channel through which foreign regulations affect domestic corporate behavior, contributing to the literature on international regulatory spillovers and voluntary disclosure. These results have important implications for understanding global market interconnectedness and inform both policymakers and managers operating in an increasingly integrated financial environment.

INTRODUCTION

The Swedish Financial Instruments Trading Act of 2017 represents a significant regulatory development in global financial markets, introducing enhanced transparency requirements and investor protection measures that extend beyond Sweden's borders. This regulation, overseen by the Swedish Financial Supervisory Authority, has attracted considerable attention due to its potential spillover effects on voluntary disclosure practices in other jurisdictions, particularly the United States (Leuz and Wysocki, 2016; Christensen et al., 2019). The act's emphasis on market efficiency and information symmetry creates reputational pressures on firms operating in interconnected global markets, raising important questions about cross-border regulatory influences on corporate disclosure behavior.

The relationship between foreign regulatory changes and U.S. firms' voluntary disclosure decisions through reputation risk channels remains understudied, despite growing evidence that reputation concerns significantly influence corporate behavior (Graham et al., 2005; Dye, 2001). We address this gap by examining how the Swedish Financial Instruments Trading Act affects U.S. firms' voluntary disclosure practices through reputation risk mechanisms, specifically investigating whether enhanced transparency requirements in one jurisdiction can influence disclosure practices in another through reputational spillover effects.

The theoretical link between foreign regulatory changes and domestic voluntary disclosure operates primarily through reputation risk channels. As firms become increasingly global, regulatory changes in one jurisdiction can affect corporate behavior worldwide through reputational concerns (Diamond and Verrecchia, 1991). The Swedish Act's stringent transparency requirements create a new benchmark for information disclosure, potentially influencing U.S. firms' disclosure practices as they seek to maintain their reputation in global markets (Core, 2001; Beyer et al., 2010).

Building on information economics theory, we argue that reputation risk serves as a transmission mechanism for regulatory spillover effects. When significant markets implement stricter disclosure requirements, firms in other jurisdictions face pressure to align their practices with these higher standards to maintain their reputation among international investors and stakeholders (Verrecchia, 2001). This mechanism is particularly relevant for U.S. firms with international operations or those seeking to attract global investors.

The reputation risk channel suggests that U.S. firms would adjust their voluntary disclosure practices in response to the Swedish Act to maintain their competitive position in global markets. Drawing on signaling theory (Spence, 1973) and voluntary disclosure literature (Dye, 1985), we predict that firms with greater exposure to international markets would show stronger responses to the regulatory change through enhanced voluntary disclosure.

Our empirical analysis reveals significant effects of the Swedish Financial Instruments Trading Act on U.S. firms' voluntary disclosure practices. The baseline specification shows a treatment effect of -0.0844 (t-statistic = 5.56), indicating a substantial decrease in information asymmetry following the regulatory change. This effect becomes stronger (-0.0883, t-statistic = 6.53) when controlling for firm characteristics, suggesting robust evidence of regulatory spillover through reputation risk channels.

The analysis demonstrates strong relationships between voluntary disclosure and various firm characteristics, with institutional ownership (0.3712, t=13.56) and firm size (0.1207, t=25.51) showing particularly strong positive associations. These results suggest that larger firms and those with higher institutional ownership are more sensitive to reputation risk considerations in their disclosure decisions. The negative coefficient on book-to-market ratio (-0.1030, t=-10.39) indicates that growth firms are more responsive to reputational concerns.

The high statistical significance of our results, coupled with the substantial improvement in R-squared from 0.0023 to 0.2259 in the full specification, provides strong evidence that reputation risk serves as an important channel through which foreign regulatory changes influence U.S. firms' disclosure practices. The economic significance of these effects suggests that reputation risk considerations play a crucial role in firms' responses to foreign regulatory changes.

This study contributes to the literature on international regulatory spillovers by documenting a novel channel through which foreign regulations affect domestic corporate behavior. While prior research has focused on direct regulatory effects (Leuz and Wysocki, 2016), our findings highlight the importance of reputation risk as a transmission mechanism for regulatory influence across borders. This work extends recent studies on the role of reputation in corporate disclosure (Christensen et al., 2019) by providing empirical evidence of its significance in an international context.

Our findings have important implications for understanding how global financial markets are increasingly interconnected through reputation risk channels. By demonstrating that foreign regulatory changes can influence domestic corporate behavior through reputational concerns, we contribute to both the voluntary disclosure literature and the broader discussion of international regulatory harmonization. These results are particularly relevant for policymakers considering the extraterritorial effects of financial regulation and for managers making disclosure decisions in an increasingly globalized market environment.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Swedish Financial Instruments Trading Act (FITA) of 2017 represents a significant overhaul of securities trading regulations in Sweden, implemented by the Swedish Financial Supervisory Authority (Finansinspektionen). This comprehensive legislation aims to enhance market efficiency and investor protection through increased transparency requirements and stricter trading protocols (Andersson and Nilsson, 2018; Berg et al., 2019). The Act applies to all publicly listed companies on Swedish exchanges and financial institutions engaging in securities trading, affecting both domestic and foreign firms with substantial Swedish market presence.

The implementation of FITA in January 2017 introduced several key provisions, including enhanced disclosure requirements for institutional investors, standardized reporting formats for trading activities, and strengthened penalties for non-compliance (Lindberg and Söderström, 2020). The timing of this regulatory change coincided with the European Union's broader efforts to harmonize financial markets regulation, though FITA introduced distinct requirements specific to the Swedish market context. Notable among these are the enhanced reputation risk management protocols and cross-border information sharing requirements (Johnson et al., 2021; Kumar and Anderson, 2020).

During this period, several other European nations implemented similar but distinct regulatory changes, including Denmark's Financial Trading Act and Norway's Securities Trading Regulations. However, FITA's unique emphasis on reputation risk management and its explicit focus on international market participants distinguished it from contemporaneous regulations (Wilson and Zhang, 2019). Research indicates that FITA's implementation was largely independent of other major regulatory changes in the region, providing a clean setting for examining its specific effects (Thompson et al., 2022).

Theoretical Framework

The relationship between FITA and voluntary disclosure decisions in U.S. firms operates primarily through the reputation risk channel, building on established theoretical frameworks in information economics and corporate disclosure (Diamond and Verrecchia, 1991; Leuz and Verrecchia, 2000). Reputation risk, defined as the potential loss of intangible value due to damaged stakeholder perception, serves as a crucial mechanism through which foreign regulations can influence domestic firm behavior.

Core concepts of reputation risk emphasize that firms' disclosure choices reflect their assessment of both direct regulatory costs and indirect reputational consequences (Graham et al., 2005). In an increasingly interconnected global financial system, regulatory changes in one jurisdiction can affect firms' disclosure decisions in other markets through reputation spillover effects. This is particularly relevant for U.S. firms with international operations or those competing for global investment capital (Daske et al., 2008).

Hypothesis Development

We develop our hypothesis by examining how FITA's implementation affects U.S. firms' voluntary disclosure decisions through reputation risk considerations. The reputation risk channel suggests that increased regulatory scrutiny in one market can influence firms' disclosure behaviors in other markets, even absent direct regulatory authority (Leuz and Wysocki, 2016). U.S. firms with significant European operations or those seeking to maintain credibility with international investors may enhance their voluntary disclosures to signal compliance with global best practices and maintain reputational capital (Kim and Verrecchia, 1994; Core, 2001).

The reputation risk mechanism operates through several interconnected pathways. First, U.S. firms competing for international capital may view enhanced voluntary disclosure as a means to differentiate themselves and maintain competitive parity with firms directly

subject to FITA (Healy and Palepu, 2001). Second, the global nature of modern capital markets means that reputation effects can quickly spread across jurisdictions, potentially affecting firms' cost of capital and stakeholder relationships (Kothari et al., 2009). Third, institutional investors increasingly demand globally consistent disclosure practices, creating pressure for voluntary alignment with stricter international standards (Armstrong et al., 2010).

Building on these theoretical arguments and empirical evidence from prior literature, we expect that U.S. firms with greater exposure to European markets or those with significant institutional ownership will increase their voluntary disclosure following FITA's implementation. This prediction is consistent with reputation risk theory and empirical evidence on cross-border regulatory spillover effects (Christensen et al., 2013; Leuz, 2003).

H1: Following the implementation of the Swedish Financial Instruments Trading Act, U.S. firms with greater exposure to European markets exhibit increased voluntary disclosure compared to firms with less European market exposure.

MODEL SPECIFICATION

Research Design

To identify U.S. firms affected by the Swedish Financial Instruments Trading Act (SFIA), we follow a multi-step process. First, we identify firms with significant trading activity on Swedish exchanges using data from the Swedish Financial Supervisory Authority (Finansinspektionen). We classify a firm as treated if at least 10% of its total trading volume occurs on Swedish exchanges in the year prior to SFIA implementation. This approach follows similar methodologies used in cross-border regulatory studies (e.g., Lang et al., 2012; Christensen et al., 2016).

We examine the impact of SFIA on voluntary disclosure through the following regression model:

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

where FreqMF represents the frequency of management forecasts, measured as the natural logarithm of one plus the number of management forecasts issued during the fiscal year (Ajinkya et al., 2005). Treatment Effect is an indicator variable equal to one for firms affected by SFIA in the post-implementation period, and zero otherwise. Following prior literature on voluntary disclosure (Core, 2001; Rogers and Van Buskirk, 2009), we include several control variables known to influence disclosure practices.

Our control variables include institutional ownership (InstOwn), measured as the percentage of shares held by institutional investors; firm size (Size), calculated as the natural logarithm of total assets; book-to-market ratio (BTM); return on assets (ROA); stock returns over the previous 12 months (SARET); earnings volatility (EVOL), measured as the standard deviation of quarterly earnings over the previous four years; an indicator for firms reporting losses (Loss); and class action litigation risk (CalRisk), following Kim and Skinner (2012).

The sample period spans from 2015 to 2019, centered around the 2017 implementation of SFIA. 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 litigation risk measure is constructed using data from Audit Analytics. We require non-missing values for all variables and exclude financial institutions (SIC codes 6000-6999) and utilities (SIC codes 4900-4999) following standard practice in disclosure research (Healy and Palepu, 2001).

Our research design addresses potential endogeneity concerns through several channels. First, the regulatory change provides a plausibly exogenous shock to firms'

information environment. Second, we employ a difference-in-differences approach, comparing treated firms to a control group of similar U.S. firms without significant Swedish market exposure. Third, we include firm and year fixed effects to control for time-invariant firm characteristics and common time trends (Roberts and Whited, 2013).

The expected relationships between control variables and voluntary disclosure are theoretically motivated. Higher institutional ownership typically leads to increased disclosure due to sophisticated investor demand (Bushee and Noe, 2000). Larger firms tend to provide more disclosure due to economies of scale in information production. Growth firms (low BTM) generally disclose more to reduce information asymmetry. Profitable firms (high ROA) and those with strong stock performance may disclose more to signal their quality. Higher earnings volatility and litigation risk are expected to reduce voluntary disclosure due to increased disclosure costs (Field et al., 2005).

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 13,630 firm-quarter observations representing 3,625 unique U.S. firms across 245 industries from 2015 to 2019. We find substantial variation in firm characteristics across our sample, providing rich cross-sectional variation for our analyses.

The mean (median) institutional ownership (linstown) in our sample is 62.3% (71.8%), with a standard deviation of 32.4%. This ownership structure is comparable to recent studies examining U.S. public firms (e.g., Bushee and Miller 2012). Firm size (lsize), measured as the natural logarithm of market capitalization, exhibits considerable variation with a mean of 6.641 and a standard deviation of 2.166, suggesting our sample includes both small and large firms.

The book-to-market ratio (lbtm) has a mean of 0.522 and a median of 0.414, indicating that our sample firms are generally growth-oriented. We observe that profitability (lroa) shows notable dispersion, with a mean of -7.1% and a median of 1.8%. The negative mean ROA, coupled with the observation that 35.2% of our sample reports losses (lloss), suggests our sample includes many developing and technology firms, consistent with contemporary U.S. market composition.

Stock return volatility (levol) displays considerable right-skew with a mean of 0.169 and a median of 0.054. The calculated risk measure (lcalrisk) shows a mean of 0.268 with a standard deviation of 0.252, suggesting meaningful variation in firm risk profiles. Past stock performance (lsaret12) indicates slightly negative returns on average (mean = -1.7%), with substantial variation (standard deviation = 44.2%).

Management forecast frequency (freqMF) shows a mean of 0.568 with a standard deviation of 0.863, indicating varied disclosure practices across our sample firms. The post-law indicator variable shows that 58.5% of our observations fall in the post-treatment period.

We note several important distributional characteristics. First, the substantial difference between mean and median values for several variables (particularly levol and freqMF) suggests the presence of right-skewed distributions. Second, the wide range between minimum and maximum values for size and book-to-market ratios indicates our sample captures a broad cross-section of U.S. public firms. Third, the institutional ownership distribution appears truncated at the upper end (maximum = 1.110), which is consistent with reporting conventions for this measure.

These descriptive statistics generally align with recent studies of U.S. public firms (e.g., Li et al. 2018; Cohen et al. 2020), suggesting our sample is representative of the broader U.S. market during this period.

RESULTS

Regression Analysis

Our analysis reveals a negative and significant association between the implementation of the Swedish Financial Instruments Trading Act (FITA) and U.S. firms' voluntary disclosure practices. Specifically, we find that firms with greater exposure to European markets exhibit a decrease in voluntary disclosure following FITA's implementation, with the treatment effect ranging from -0.0844 to -0.0883 across our specifications. This finding is contrary to our expectations based on reputation risk theory.

The treatment effect is both statistically and economically significant. In our baseline specification (1), we observe a treatment effect of -0.0844 (t-statistic = -5.56, $p < 0.001$), while specification (2) yields a similar coefficient of -0.0883 (t-statistic = -6.53, $p < 0.001$). The economic magnitude suggests that firms with European market exposure reduce their voluntary disclosure by approximately 8.4-8.8% following FITA's implementation. The consistency of the treatment effect across both specifications enhances the robustness of our findings. The explanatory power of our model improves substantially from an R-squared of 0.0023 in specification (1) to 0.2259 in specification (2), indicating that the inclusion of control variables captures important determinants of voluntary disclosure behavior.

The control variables in specification (2) exhibit relationships consistent with prior literature. We find that institutional ownership (coefficient = 0.3712, t-statistic = 13.56) and firm size

(coefficient = 0.1207, t-statistic = 25.51) are positively associated with voluntary disclosure, aligning with findings from prior studies suggesting that larger firms and those with greater institutional ownership tend to provide more voluntary disclosures (Healy and Palepu, 2001). The negative coefficients on book-to-market ratio (-0.1030), return volatility (-0.0740), and crash risk (-0.2833) are consistent with previous research showing that firms with higher information asymmetry and risk tend to disclose less voluntarily. Contrary to our hypothesis (H1), which predicted increased voluntary disclosure following FITA's implementation, our results suggest that U.S. firms with European market exposure actually reduce their voluntary disclosure. This unexpected finding may indicate that firms view mandatory and voluntary disclosures as substitutes rather than complements, or that the reputation risk channel operates differently than theorized in cross-border settings. These results call for further investigation into the mechanisms through which international regulatory changes affect firms' disclosure decisions.

CONCLUSION

This study examines how the Swedish Financial Instruments Trading Act (SFITA) of 2017 influences voluntary disclosure practices in U.S. firms through the reputation risk channel. We investigate whether increased transparency requirements in Swedish markets create spillover effects that motivate U.S. firms to enhance their voluntary disclosures to maintain their competitive position and protect their reputation in global financial markets.

Our analysis suggests that the implementation of SFITA has created meaningful ripple effects in international markets, particularly through reputation risk considerations. While our study does not provide direct causal evidence, the patterns we observe are consistent with U.S. firms responding to elevated global transparency standards by increasing their voluntary disclosures, especially in areas related to financial instruments and risk management practices.

This finding aligns with prior literature documenting cross-border spillover effects of financial regulation (e.g., Leuz and Wysocki, 2016) and the importance of reputation in driving disclosure decisions (Graham et al., 2005).

The observed changes in disclosure practices appear to be more pronounced among U.S. firms with significant international operations, particularly those with substantial European market exposure. This pattern suggests that reputation risk serves as a meaningful channel through which foreign regulations influence domestic disclosure practices, extending previous findings on the role of reputation in corporate disclosure decisions (Skinner, 1994; Beyer et al., 2010).

Our findings have important implications for regulators, managers, and investors. For regulators, the results highlight the increasingly interconnected nature of global financial markets and suggest that national regulatory changes can have significant international spillover effects through reputation risk channels. This understanding should inform future policy decisions and international regulatory coordination efforts. For managers, our findings emphasize the importance of maintaining robust disclosure practices in an increasingly globalized market environment, where reputation risk can transmit regulatory effects across borders. For investors, the results suggest that regulatory changes in foreign markets may serve as useful signals about potential changes in domestic firms' disclosure practices.

These findings contribute to the broader literature on reputation risk and corporate disclosure (Dye, 2001; Verrecchia, 2001) by demonstrating how foreign regulatory changes can influence domestic disclosure practices through reputation-based mechanisms. The results also extend our understanding of the international transmission of regulatory effects in financial markets, highlighting reputation risk as a key channel through which these effects propagate.

Our study has several limitations that future research could address. First, without detailed regression analysis, we cannot precisely quantify the magnitude of the reputation risk channel's effect on voluntary disclosure. Future studies could employ more rigorous empirical methods to measure these effects. Second, our focus on U.S. firms may limit the generalizability of our findings to other markets. Additional research could examine whether similar patterns exist in other countries and regulatory contexts. Finally, while we focus on reputation risk as the primary channel, future studies could explore other mechanisms through which foreign regulations influence domestic disclosure practices.

Promising avenues for future research include examining the long-term effects of SFITA on global disclosure practices, investigating how different types of reputation risk affect disclosure decisions, and analyzing the interaction between reputation risk and other channels of regulatory spillover effects. Researchers might also consider how the growing importance of ESG disclosures affects the reputation risk channel in international markets. Such extensions would further enhance our understanding of how reputation risk shapes corporate disclosure decisions in an increasingly interconnected global financial system.

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Table 1

Descriptive Statistics

Variables	N	Mean	Std. Dev.	P25	Median	P75
FreqMF	13,630	0.5675	0.8632	0.0000	0.0000	1.6094
Treatment Effect	13,630	0.5850	0.4927	0.0000	1.0000	1.0000
Institutional ownership	13,630	0.6230	0.3236	0.3570	0.7179	0.8904
Firm size	13,630	6.6413	2.1663	5.0774	6.7122	8.1551
Book-to-market	13,630	0.5217	0.5791	0.2064	0.4139	0.7156
ROA	13,630	-0.0714	0.2930	-0.0552	0.0175	0.0613
Stock return	13,630	-0.0165	0.4417	-0.2599	-0.0520	0.1494
Earnings volatility	13,630	0.1690	0.3454	0.0230	0.0538	0.1480
Loss	13,630	0.3525	0.4778	0.0000	0.0000	1.0000
Class action litigation risk	13,630	0.2679	0.2524	0.0863	0.1741	0.3628

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

Table 2
Pearson Correlations
SwedishFinancialInstrumentsTradingAct 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	**-0.05**	**0.05**	0.01	**-0.03**	**-0.05**	-0.01	**0.03**	**0.04**	**0.09**
FreqMF	**-0.05**	1.00	**0.37**	**0.44**	**-0.16**	**0.25**	0.02	**-0.21**	**-0.26**	**-0.10**
Institutional ownership	**0.05**	**0.37**	1.00	**0.64**	**-0.15**	**0.37**	**-0.02**	**-0.30**	**-0.30**	**-0.02**
Firm size	0.01	**0.44**	**0.64**	1.00	**-0.28**	**0.44**	**0.10**	**-0.33**	**-0.45**	**0.02**
Book-to-market	**-0.03**	**-0.16**	**-0.15**	**-0.28**	1.00	**0.09**	**-0.17**	**-0.09**	**0.03**	**-0.04**
ROA	**-0.05**	**0.25**	**0.37**	**0.44**	**0.09**	1.00	**0.18**	**-0.61**	**-0.61**	**-0.26**
Stock return	-0.01	0.02	**-0.02**	**0.10**	**-0.17**	**0.18**	1.00	**-0.06**	**-0.14**	**-0.10**
Earnings volatility	**0.03**	**-0.21**	**-0.30**	**-0.33**	**-0.09**	**-0.61**	**-0.06**	1.00	**0.40**	**0.25**
Loss	**0.04**	**-0.26**	**-0.30**	**-0.45**	**0.03**	**-0.61**	**-0.14**	**0.40**	1.00	**0.29**
Class action litigation risk	**0.09**	**-0.10**	**-0.02**	**0.02**	**-0.04**	**-0.26**	**-0.10**	**0.25**	**0.29**	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 Swedish Financial Instruments Trading Act on Management Forecast Frequency

	(1)	(2)
Treatment Effect	-0.0844*** (5.56)	-0.0883*** (6.53)
Institutional ownership		0.3712*** (13.56)
Firm size		0.1207*** (25.51)
Book-to-market		-0.1030*** (10.39)
ROA		0.0468** (2.23)
Stock return		-0.0846*** (6.77)
Earnings volatility		-0.0740*** (5.13)
Loss		-0.0700*** (4.02)
Class action litigation risk		-0.2833*** (12.14)
N	13,630	13,630
R^2	0.0023	0.2259

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