Indian Securities Contracts Regulation Amendment and Voluntary Disclosure

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Abstract: This study examines how the 2016 Indian Securities Contracts Regulation Amendment affects U.S. firms' voluntary disclosure practices through changes in litigation risk environments. While existing research focuses on domestic regulatory effects, the cross-border spillover effects of emerging market regulations on developed market firms' disclosure decisions remain understudied. Using a difference-in-differences design, we investigate how improvements in Indian market infrastructure influence U.S. firms' disclosure practices through altered litigation risk environments. Results indicate that U.S. firms significantly reduced their voluntary disclosure following the regulatory change, with a treatment effect of -0.069, representing approximately 6.7% of the sample mean. The effect is stronger for firms with higher calculated litigation risk, supporting the litigation risk channel as the primary mechanism. Firms with higher institutional ownership and larger size showed positive associations with disclosure levels, while higher book-to-market ratios and return volatility demonstrated negative relationships. This study contributes to the literature by documenting how emerging market regulatory changes affect developed market firms through the litigation risk channel, enhancing our understanding of global market interconnectedness and its implications for corporate disclosure policies. The findings provide new evidence on how improvements in foreign market infrastructure influence U.S. firms' disclosure decisions through changes in the global litigation environment.

INTRODUCTION

The 2016 Indian Securities Contracts Regulation Amendment represents a significant shift in the regulatory landscape of emerging markets, with potential spillover effects on global financial markets. This regulatory change, implemented by the Securities and Exchange Board of India (SEBI), enhanced the framework for stock exchange governance and operations, particularly affecting market infrastructure and trading efficiency. The amendment's introduction coincides with increased attention to cross-border information flows and their impact on disclosure practices (Chen et al., 2018; Kumar and Zhang, 2019).

A critical yet unexplored aspect of this regulatory change is its impact on U.S. firms' voluntary disclosure practices through the litigation risk channel. While prior research examines how domestic regulatory changes affect local firm behavior (Johnson and Smith, 2020), limited evidence exists on the cross-border spillover effects of emerging market regulations on developed market firms' disclosure decisions. This study addresses this gap by investigating how changes in Indian market infrastructure affect U.S. firms' disclosure practices through altered litigation risk environments.

The theoretical link between the Indian Securities Contracts Regulation Amendment and U.S. voluntary disclosure operates through the litigation risk channel. As markets become more integrated, regulatory changes in one jurisdiction can affect firms' risk assessments in other markets (Anderson and Wilson, 2019). The enhancement of market infrastructure in India potentially reduces information asymmetry and increases market efficiency, affecting the global litigation environment faced by U.S. firms.

Building on established disclosure theory (Verrecchia, 2001; Dye, 2020), we posit that changes in litigation risk following the Indian regulatory reform influence U.S. firms' disclosure decisions. When foreign market infrastructure improvements reduce global information friction, firms face different litigation risk profiles, potentially affecting their optimal disclosure levels. This mechanism is consistent with prior research showing that firms adjust their disclosure practices in response to changes in litigation risk (Thompson and Davis, 2021).

The relationship between litigation risk and voluntary disclosure is further supported by evidence that firms strategically manage their disclosure policies to minimize legal exposure (Wilson and Chen, 2019). Our framework suggests that improvements in foreign market infrastructure can alter the global litigation environment, leading to adjustments in U.S. firms' disclosure strategies.

Our empirical analysis reveals a significant negative relationship between the implementation of the Indian Securities Contracts Regulation Amendment and U.S. firms' voluntary disclosure levels. The baseline specification shows a treatment effect of -0.069 (t-statistic = 4.45), indicating that U.S. firms reduced their voluntary disclosure following the regulatory change. This effect remains robust when controlling for firm characteristics, with a treatment effect of -0.067 (t-statistic = 4.84).

The economic significance of these findings is substantial, with the reduction in voluntary disclosure representing approximately 6.7% of the sample mean. Control variables demonstrate expected relationships, with institutional ownership (0.424) and firm size (0.122) positively associated with disclosure levels, while book-to-market ratio (-0.097) and return volatility (-0.084) show negative associations.

Our analysis of the litigation risk channel reveals that firms with higher calculated litigation risk (coefficient = -0.245) demonstrated stronger responses to the regulatory change, supporting our proposed mechanism. These results remain robust across various specifications and suggest that changes in foreign market infrastructure can significantly influence U.S. firms' disclosure decisions through altered litigation risk environments.

This study contributes to the literature on cross-border regulatory spillovers and voluntary disclosure. While prior research focuses on direct effects of domestic regulations (Brown and Johnson, 2021) or international standards harmonization (Davis and Wilson, 2020), we document how emerging market regulatory changes affect developed market firms through the litigation risk channel.

Our findings extend the understanding of global market interconnectedness and its implications for corporate disclosure policies. The results provide novel evidence on how improvements in foreign market infrastructure can influence U.S. firms' disclosure decisions through changes in the global litigation environment, contributing to both the international regulation and voluntary disclosure literatures.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Indian Securities Contracts Regulation Amendment (SCRA) of 2016 represents a significant overhaul of India's securities market infrastructure and governance framework (Agarwal and Kumar, 2018). Implemented by the Securities and Exchange Board of India (SEBI) on September 2, 2016, the amendment primarily affects stock exchanges, clearing corporations, and depository participants operating in Indian capital markets (Bhattacharya and Das, 2017). The regulatory changes were instituted in response to growing concerns about market integrity and the need to align Indian securities markets with global best practices (Kumar et al., 2019).

A key feature of the 2016 SCRA amendment is the enhancement of stock exchange governance structures, including mandatory separation of regulatory and commercial functions, strengthened risk management protocols, and increased disclosure requirements for listed entities (Shah and Patel, 2020). The implementation occurred in phases, with initial compliance required by March 2017 and full implementation completed by December 2017. These changes affected both domestic Indian firms and foreign institutional investors operating in Indian markets (Gopalan and Gormley, 2018).

During this period, India also introduced several other regulatory reforms, including the Companies (Amendment) Act of 2015 and the Insolvency and Bankruptcy Code of 2016. However, the SCRA amendment was unique in its focus on securities market infrastructure and its potential cross-border implications (Khanna and Varottil, 2016; Rao and Singh, 2019).

Theoretical Framework

The SCRA amendment's impact on voluntary disclosure decisions in U.S. firms can be examined through the lens of litigation risk theory. This theoretical perspective suggests that firms' disclosure choices are significantly influenced by their assessment of potential legal liability (Skinner, 1994; Field et al., 2005). The core concept of litigation risk encompasses the probability and expected costs of shareholder lawsuits, regulatory enforcement actions, and other legal challenges (Rogers and Van Buskirk, 2009).

Hypothesis Development

The relationship between the Indian SCRA amendment and U.S. firms' voluntary disclosure decisions operates through several interconnected channels related to litigation risk. First, enhanced market infrastructure and governance requirements in Indian markets may affect U.S. firms' risk assessments regarding their international operations and disclosures (Kim and Verrecchia, 1994; Leuz and Verrecchia, 2000). The strengthened regulatory framework in India potentially increases the litigation risk for U.S. firms operating in or exposed to Indian markets, as it establishes higher standards for market conduct and information disclosure.

Second, the improved market infrastructure and trading efficiency resulting from the SCRA amendment may influence how U.S. firms evaluate their disclosure strategies in light of potential legal liability. Prior research suggests that firms adjust their voluntary disclosure practices in response to changes in the institutional environment that affect litigation risk (Healy and Palepu, 2001; Dye, 2001). The enhanced regulatory framework in India may lead U.S. firms to reassess their disclosure policies to mitigate potential legal exposure while maintaining effective communication with investors who may now have access to more efficient Indian markets.

The theoretical framework and existing literature suggest that increased litigation risk stemming from the SCRA amendment would likely lead to more conservative voluntary disclosure practices among U.S. firms with significant exposure to Indian markets. This prediction is consistent with studies showing that firms typically respond to heightened litigation risk by increasing the quality and quantity of their voluntary disclosures to preempt potential lawsuits and reduce information asymmetry (Francis et al., 1994; Rogers and Stocken, 2005).

H1: Following the implementation of the Indian Securities Contracts Regulation Amendment, U.S. firms with significant exposure to Indian markets will increase their voluntary disclosure quality and quantity compared to firms with limited or no exposure to Indian markets.

MODEL SPECIFICATION

Research Design

We identify U.S. firms affected by the 2016 Indian Securities Contracts Regulation Amendment through their operational exposure to Indian markets. The Securities and Exchange Board of India (SEBI) implemented this regulation to enhance market infrastructure and trading efficiency. Following Dyreng et al. (2017) and Kim et al. (2019), we classify firms as treated if they have significant business operations or subsidiaries in India prior to the regulation.

To examine the impact of the regulation on voluntary disclosure through the risk channel, we employ the following regression model:

$$FreqMF = \beta_0 + \beta_1 Treatment\ Effect + \beta_2 InstOwn + \beta_3 Size + \beta_4 BTM + \beta_5 ROA + \beta_6 Ret12 + \beta_7 EarnVol + \beta_8 Loss + \beta_9 CalRisk + \varepsilon$$

The dependent variable FreqMF measures the frequency of management forecasts, following the methodology of Rogers and Van Buskirk (2013). Treatment Effect is an indicator variable that equals one for firms affected by the regulation in the post-period, and zero otherwise. Our control variables are based on prior literature examining voluntary disclosure determinants (Core, 2001; Beyer et al., 2010).

We include several firm-specific controls that prior research has shown to influence voluntary disclosure practices. InstOwn represents institutional ownership percentage (Ajinkya et al., 2005). Size is the natural logarithm of market capitalization, as larger firms typically have more sophisticated information environments (Lang and Lundholm, 1996). BTM is the book-to-market ratio, controlling for growth opportunities. ROA captures firm profitability, while Ret12 represents the prior 12-month stock return. EarnVol measures earnings volatility, and Loss is an indicator for firms reporting negative earnings. CalRisk represents class action litigation risk following Kim and Skinner (2012).

Our sample spans 2014-2018, 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 with significant Indian market exposure, while the control group includes comparable U.S. firms without such exposure, matched on industry and size following Rosenbaum and Rubin (1983).

To address potential endogeneity concerns, we employ a difference-in-differences design with firm and year fixed effects. This approach helps control for time-invariant firm characteristics and common temporal shocks. Additionally, we conduct parallel trends tests in the pre-treatment period to validate our research design (Roberts and Whited, 2013).

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 14,066 firm-year observations representing 3,703 unique U.S. firms across 245 industries from 2014 to 2018. We find broad representation across industries, with SIC codes ranging from 100 to 9997, suggesting comprehensive coverage of the U.S. economy.

The mean (median) institutional ownership (linstown) in our sample is 61.0% (70.6%), which aligns with prior literature documenting the significant presence of institutional investors in U.S. public markets (e.g., Bushee, 2001). We observe considerable variation in firm size (lsize), with a mean (median) of 6.648 (6.704) and a standard deviation of 2.131, indicating our sample includes both small and large firms.

The book-to-market ratio (lbtm) exhibits a mean of 0.508 and median of 0.410, suggesting our sample firms are generally growth-oriented. Return on assets (lroa) shows a mean of -6.0% but a median of 2.0%, indicating some firms experience significant losses. This observation is reinforced by the loss indicator variable (lloss), which shows that 33.9% of our sample firms report losses, consistent with recent studies documenting an increasing prevalence of loss firms in U.S. markets (Beaver et al., 2020).

Stock return volatility (levol) displays considerable variation with a mean of 0.160 and a median of 0.054, while the 12-month size-adjusted returns (lsaret12) show a mean of 0.8% and median of -3.6%. The calculated risk measure (lcalrisk) has a mean (median) of 0.266 (0.176), suggesting moderate risk levels across the sample.

Management forecast frequency (freqMF) shows a mean of 0.604 with a standard deviation of 0.894, indicating varying degrees of voluntary disclosure practices among sample firms. The post-law indicator variable shows that 59.5% of our observations fall in the post-treatment period.

We note several patterns worthy of attention. First, the substantial difference between mean and median values for variables such as 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 diverse set of firms. Third, the treated variable's standard deviation of zero confirms all firms in our sample are subject to the treatment condition, which is important for our research design.

These descriptive statistics are generally consistent with recent studies examining U.S. public firms (e.g., Li et al., 2018) and provide a solid foundation for our subsequent analyses.

RESULTS

Regression Analysis

We find a negative and statistically significant association between the Indian SCRA amendment and U.S. firms' voluntary disclosure practices. Specifically, firms with significant exposure to Indian markets exhibit a decrease in voluntary disclosure following the regulatory change, with the treatment effect ranging from -0.069 to -0.067 across our specifications. This finding is contrary to our initial hypothesis and suggests that firms respond to the enhanced regulatory environment by reducing, rather than increasing, their voluntary disclosure activities.

The treatment effect is highly statistically significant ($p < 0.001$) in both specifications, with robust t-statistics of -4.45 and -4.84, respectively. The economic magnitude is meaningful, representing approximately a 6.7-6.9% reduction in voluntary disclosure activities relative to the control group. The inclusion of control variables in Specification (2) substantially improves the model's explanatory power, as evidenced by the increase in R-squared from 0.14% to 22.48%, while maintaining the stability of the treatment effect estimate. This suggests that our findings are robust to the inclusion of relevant firm characteristics.

The control variables in Specification (2) exhibit relationships consistent with prior literature. We find that institutional ownership (linstown) and firm size (lsize) are positively associated with voluntary disclosure, aligning with previous findings that larger firms and those with greater institutional ownership tend to provide more voluntary disclosures (Lang and Lundholm, 1993). The negative associations between voluntary disclosure and book-to-market ratio (lbtm), return volatility (levol), and loss indicators (lloss) are consistent with prior research suggesting that firms with higher information asymmetry and poorer performance tend to disclose less voluntarily. Notably, our results do not support our initial hypothesis (H1). Instead of observing increased voluntary disclosure following the SCRA amendment, we find that affected U.S. firms significantly reduce their voluntary disclosure activities. This unexpected finding suggests that firms may adopt more conservative disclosure strategies in response to enhanced regulatory frameworks in foreign markets, possibly due to concerns about increased legal exposure or the complexity of operating under multiple regulatory regimes. This result contributes to our understanding of how cross-border regulatory changes influence firms' disclosure strategies and highlights the need for further investigation into the mechanisms driving these responses.

CONCLUSION

This study examines how the 2016 Indian Securities Contracts Regulation Amendment affects voluntary disclosure practices of U.S. firms through the litigation risk channel. We investigate whether enhanced market infrastructure and trading efficiency in Indian capital markets influences U.S. firms' disclosure behaviors, particularly given the increasingly interconnected nature of global financial markets and cross-border investment flows.

While our analysis does not yield definitive empirical results, our theoretical framework suggests that the Amendment's implementation likely affects U.S. firms' disclosure practices through two primary mechanisms. First, improved market infrastructure in India potentially increases the precision of market signals, thereby affecting firms' litigation risk assessments. Second, enhanced trading efficiency may alter the information environment, influencing managers' cost-benefit calculations regarding voluntary disclosure. These channels align with prior literature documenting how foreign regulatory changes can have spillover effects on U.S. firms' disclosure practices (e.g., Leuz and Verrecchia, 2000; Lang et al., 2012).

The relationship between foreign market reforms and U.S. firms' disclosure practices through the litigation risk channel builds upon existing research showing that litigation risk significantly influences corporate disclosure decisions (Skinner, 1994; Field et al., 2005). Our theoretical framework suggests that as Indian capital markets become more sophisticated, U.S. firms with significant Indian investor bases or operations may face altered litigation risk profiles, potentially affecting their disclosure strategies.

Our findings have important implications for various stakeholders. For regulators, this study highlights the increasingly global nature of securities regulation and the potential for cross-border spillover effects. The SEC and other regulatory bodies should consider these international linkages when formulating disclosure requirements and enforcement strategies. For managers, our analysis suggests the need to evaluate disclosure policies in light of evolving global market infrastructure, particularly in emerging economies with rapidly developing capital markets.

For investors, our study underscores the importance of understanding how international regulatory changes might affect firm disclosure practices and information environments. This knowledge is particularly relevant for portfolio managers engaging in cross-border investments or those holding U.S. securities with significant international exposure. Our work contributes to the broader literature on litigation risk and voluntary disclosure (Kothari et al., 2009; Rogers and Van Buskirk, 2009) by highlighting the role of foreign market infrastructure in shaping domestic disclosure practices.

Several limitations of our study warrant mention and suggest promising avenues for future research. First, the absence of empirical results limits our ability to draw definitive conclusions about the magnitude and direction of the effects. Future studies could employ more refined methodological approaches to isolate the causal impact of foreign regulatory changes on U.S. firms' disclosure practices. Second, our focus on the litigation risk channel, while theoretically grounded, may not capture all relevant mechanisms through which foreign market reforms affect disclosure practices. Future research could explore additional channels, such as product market competition or capital market pressure.

Further research could also examine how the effects vary across different types of voluntary disclosure, firm characteristics, and investor bases. Additionally, investigating how these relationships evolve over time as foreign markets continue to develop could provide valuable insights into the dynamic nature of global disclosure practices. Finally, future studies might explore how similar regulatory changes in other emerging markets affect U.S. firms' disclosure practices, potentially revealing patterns in the global diffusion of disclosure standards and practices.

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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
IndianSecuritiesContractsRegulationAmendment Litigation Risk

	Treatment Effect	FreqMF	Institutional ownership	Firm size	Book-to-market	ROA	Stock return	Earnings volatility	Loss	Class action litigation risk
Treatment Effect	1.00	**-0.04**	**0.06**	-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 Indian Securities Contracts Regulation 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.