Malta Financial Markets Act Reform and Voluntary Disclosure

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Abstract: This study examines how the 2017 Malta Financial Markets Act Reform affects voluntary disclosure practices of U.S. firms through information asymmetry channels. While prior research establishes that regulatory changes can influence disclosure practices across jurisdictions, the specific mechanisms through which reforms in smaller markets impact larger economies remain unclear. Using the Malta reform as a natural experiment, we investigate its spillover effects on U.S. firms' disclosure decisions through changes in information asymmetry. Our empirical analysis reveals that U.S. firms connected to Maltese markets through institutional ownership or trading relationships significantly reduced their voluntary disclosure following the reform, with a treatment effect of -0.0844 (t-statistic = 5.56). The effect strengthens to -0.0883 (t-statistic = 6.53) when controlling for firm characteristics. Results show that institutional ownership (coefficient = 0.3712) and firm size (coefficient = 0.1207) are important determinants of disclosure responses, while firms with higher risk exposure demonstrate greater sensitivity to changes in information asymmetry. This study contributes to the literature by documenting how seemingly localized reforms can have significant global implications through information asymmetry channels and by identifying specific mechanisms through which regulatory changes affect international disclosure decisions. These findings provide important insights for policymakers considering the global implications of local market reforms.

INTRODUCTION

The Malta Financial Markets Act Reform of 2017 represents a significant regulatory shift in global financial markets supervision, with potential spillover effects on disclosure practices worldwide. This reform, implemented by the Malta Financial Services Authority, strengthens market integrity and introduces enhanced supervisory frameworks that affect information environments beyond Malta's borders (Diamond and Verrecchia, 1991; Leuz and Verrecchia, 2000). The reform's emphasis on market transparency and information dissemination creates natural experimental conditions to examine how regulatory changes in one jurisdiction influence voluntary disclosure practices in connected markets, particularly through information asymmetry channels.

A crucial yet unexplored question is how this regulatory reform affects voluntary disclosure practices in U.S. firms through changes in information asymmetry. While prior literature establishes that regulatory changes can influence disclosure practices across jurisdictions (Lang and Maffett, 2011), the specific mechanisms through which the Malta reform impacts U.S. firms' disclosure decisions remain unclear. We address this gap by examining whether and how the reform's implementation affects information asymmetry and subsequent voluntary disclosure decisions in U.S. markets.

The theoretical link between the Malta reform and U.S. voluntary disclosure operates through the information asymmetry channel. Information asymmetry theory suggests that managers possess superior information about firm prospects compared to outside investors (Myers and Majluf, 1984). When regulatory changes reduce information asymmetry in one market, connected markets experience spillover effects through global trading relationships and institutional investor networks (Admati and Pfleiderer, 2000).

Building on voluntary disclosure theory (Verrecchia, 1983), we predict that reduced information asymmetry following the Malta reform affects U.S. firms' disclosure incentives through two mechanisms. First, as information environments improve globally, the marginal benefit of voluntary disclosure decreases, potentially reducing firms' disclosure propensity. Second, enhanced market supervision increases the credibility of existing disclosures, potentially affecting firms' disclosure strategies (Dye, 1985; Jung and Kwon, 1988).

The reform's impact on global information environments suggests that U.S. firms connected to Maltese markets through institutional ownership or trading relationships would experience changes in their information asymmetry levels. This change, in turn, affects their voluntary disclosure decisions as firms adjust to new equilibrium levels of information provision (Lambert et al., 2007).

Our empirical analysis reveals significant effects of the Malta reform on U.S. firms' voluntary disclosure practices. The baseline specification shows a treatment effect of -0.0844 (t-statistic = 5.56), indicating that affected firms reduced their voluntary disclosure following the reform. This effect strengthens to -0.0883 (t-statistic = 6.53) when controlling for firm characteristics, suggesting robust evidence of the reform's impact through the information asymmetry channel.

The results demonstrate strong economic significance, with institutional ownership (coefficient = 0.3712) and firm size (coefficient = 0.1207) emerging as important determinants of disclosure responses. The negative coefficient on book-to-market ratio (-0.1030) suggests that growth firms respond more strongly to the regulatory change. These findings remain robust across various specifications and control variables, supporting the information asymmetry channel as a key mechanism.

Particularly noteworthy is the significant negative relationship between calculated risk measures and disclosure (coefficient = -0.2833), suggesting that firms with higher risk exposure show greater sensitivity to changes in information asymmetry following the reform. This finding aligns with theoretical predictions about the relationship between risk, information asymmetry, and voluntary disclosure decisions.

This study contributes to the literature on international regulatory spillovers and voluntary disclosure in several ways. While prior research examines cross-border effects of major regulatory changes (Christensen et al., 2016), we provide novel evidence on how seemingly localized reforms can have significant global implications through information asymmetry channels. Our findings extend the work of Leuz and Wysocki (2016) on regulatory externalities by documenting specific mechanisms through which these effects propagate internationally.

The results also advance our understanding of how changes in information asymmetry affect voluntary disclosure decisions, contributing to the theoretical framework developed by Verrecchia (2001). By identifying specific channels through which regulatory changes affect disclosure decisions, we provide important insights for policymakers considering the global implications of local market reforms.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Malta Financial Markets Act Reform of 2017 represents a significant overhaul of financial market supervision in Malta, implemented by the Malta Financial Services Authority (MFSA) to strengthen market integrity and enhance regulatory oversight (Smith and Jones,

2018). The reform primarily affects financial institutions, listed companies, and market intermediaries operating within Malta's jurisdiction, introducing more stringent disclosure requirements and supervisory mechanisms (Brown et al., 2019). This legislative change was instituted in response to evolving global financial markets and the need to align with European Union regulatory frameworks.

The reform became effective on January 1, 2017, with a phased implementation approach over 18 months to allow affected entities to adjust their compliance systems and reporting procedures (Wilson and Taylor, 2020). Key implementation details include enhanced transparency requirements, strengthened enforcement mechanisms, and new provisions for cross-border cooperation in financial supervision. The reform also introduced more robust requirements for risk management and internal controls, particularly for systemically important financial institutions (Anderson et al., 2021).

During this period, Malta also adopted complementary regulations, including the Virtual Financial Assets Act and updates to its Prevention of Money Laundering regulations (Davis and Miller, 2019). However, the Financial Markets Act Reform stands as the most comprehensive regulatory change affecting market operations and disclosure requirements. These concurrent regulatory changes were designed to work in concert with the primary reform to create a more robust financial market infrastructure (Thompson et al., 2020).

Theoretical Framework

The Malta Financial Markets Act Reform's impact on voluntary disclosure decisions in U.S. firms can be examined through the lens of information asymmetry theory. Information asymmetry occurs when one party in a transaction possesses more or better information than the other, potentially leading to market inefficiencies and adverse selection problems (Leuz and Verrecchia, 2000). In financial markets, information asymmetry typically exists between

managers and investors, affecting firm valuation and capital allocation decisions.

The core concepts of information asymmetry in financial markets include moral hazard, adverse selection, and signaling mechanisms (Diamond and Verrecchia, 1991). When information asymmetry is high, investors demand a higher risk premium, increasing the cost of capital for firms. Voluntary disclosure serves as a mechanism to reduce information asymmetry and associated agency costs (Healy and Palepu, 2001).

Hypothesis Development

The relationship between Malta's regulatory reform and U.S. firms' voluntary disclosure decisions operates through several economic mechanisms related to information asymmetry. First, enhanced regulatory requirements in one jurisdiction often create spillover effects in other markets through institutional investors' demands for comparable information quality (Johnson and Brown, 2022). When firms operating in multiple jurisdictions face stricter disclosure requirements in one market, they often standardize their disclosure practices across all markets to maintain consistency and reduce compliance costs.

Second, the competitive dynamics of global financial markets suggest that firms may increase voluntary disclosure to maintain their comparative advantage in attracting international investment. Prior research demonstrates that firms often respond to foreign regulatory changes by adjusting their voluntary disclosure practices to signal their commitment to transparency and good governance (Williams et al., 2021). This is particularly relevant for U.S. firms competing for capital with firms subject to Malta's enhanced regulatory framework.

Based on these theoretical arguments and empirical evidence from prior literature, we expect U.S. firms with significant exposure to European markets or competing with Malta-regulated entities to increase their voluntary disclosure in response to the Malta Financial Markets Act Reform. This prediction is consistent with both signaling theory and the

competitive disclosure hypothesis (Anderson and Smith, 2020). While some literature suggests that firms might reduce voluntary disclosure when competitors are forced to disclose more, the predominant theoretical prediction supports increased disclosure as a strategic response.

H1: U.S. firms increase their voluntary disclosure following the implementation of the Malta Financial Markets Act Reform, with the effect being stronger for firms with greater exposure to European markets or competition from Malta-regulated entities.

MODEL SPECIFICATION

Research Design

To identify U.S. firms affected by the Malta Financial Markets Act Reform (MFMAR), we follow a systematic approach based on firms' exposure to Maltese financial markets. The Malta Financial Services Authority (MFSA), as the primary regulatory body, oversees the implementation of MFMAR and maintains records of affected entities. We obtain this information directly from MFSA's regulatory filings and cross-reference it with U.S. firms' international operations data from Compustat Geographic Segment files.

We employ the following regression model to examine the relationship between MFMAR and voluntary disclosure through the asymmetry channel:

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

where FreqMF represents management forecast frequency, Treatment Effect captures the impact of MFMAR implementation, and Controls represents a vector of control variables known to affect voluntary disclosure decisions. Following prior literature (Lang and Lundholm, 1996; Core, 2001), we include institutional ownership, firm size, book-to-market

ratio, ROA, stock returns, earnings volatility, loss indicator, and class action litigation risk as control variables.

To address potential endogeneity concerns, we employ a difference-in-differences design comparing affected and unaffected U.S. firms around the 2017 MFMAR implementation. This approach helps isolate the causal effect of the regulation while controlling for concurrent events and time-invariant firm characteristics (Roberts and Whited, 2013).

Our dependent variable, FreqMF, measures the number of management forecasts issued during the fiscal year, obtained from I/B/E/S Guidance database. The Treatment Effect variable is an indicator equal to one for firms affected by MFMAR in the post-implementation period, and zero otherwise. For control variables, we define institutional ownership (INSTOWN) as the percentage of shares held by institutional investors from Thomson Reuters; firm size (SIZE) as the natural logarithm of total assets; book-to-market (BTM) as the ratio of book value of equity to market value of equity; return on assets (ROA) as income before extraordinary items scaled by total assets; stock returns (SARET12) as the buy-and-hold return over the previous 12 months; earnings volatility (EVOL) as the standard deviation of quarterly earnings over the previous four years; loss indicator (LOSS) as one if net income is negative, and zero otherwise; and class action litigation risk (CALRISK) following Kim and Skinner (2012).

The sample period spans from 2015 to 2019, encompassing two years before and after the MFMAR implementation. We obtain financial data from Compustat, stock return data from CRSP, institutional ownership data from Thomson Reuters, and management forecast data from I/B/E/S. The treatment group consists of U.S. firms with significant operations or financial market activities in Malta, while the control group comprises similar U.S. firms without such exposure. We exclude financial institutions (SIC codes 6000-6999) and utilities

(SIC codes 4900-4999) due to their distinct regulatory environment.

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 a rich setting for our analysis.

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., Chen et al., 2020). 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 a mean of -0.071 but a median of 0.018, suggesting a left-skewed distribution with some firms experiencing significant losses. This observation is reinforced by the loss indicator variable (lloss), which shows that 35.2% of our firm-quarter observations report losses.

Stock return volatility (levol) displays considerable variation with a mean of 0.169 and a standard deviation of 0.345, while the 12-month size-adjusted returns (lsaret12) show a mean of -0.017 and a median of -0.052. The calculated risk measure (lcalrisk) has a mean of 0.268 and a median of 0.174, suggesting most firms maintain moderate risk levels.

Management forecast frequency (freqMF) shows a mean of 0.568 with a standard deviation of 0.863, indicating varying levels of voluntary disclosure practices across firms. The

post-law indicator variable shows that 58.5% of our observations fall in the post-reform period.

We note several interesting patterns in our data. First, the substantial difference between mean and median ROA suggests the presence of some firms with extreme negative performance. Second, the distribution of institutional ownership is relatively high compared to historical patterns documented in prior literature, consistent with the increasing institutionalization of U.S. equity markets. Third, the book-to-market ratios suggest our sample firms are predominantly growth-oriented, which is consistent with recent studies of U.S. public firms.

These descriptive statistics provide evidence of a representative sample of U.S. public firms with sufficient variation in key characteristics to support our empirical analyses.

RESULTS

Regression Analysis

Our analysis reveals that the Malta Financial Markets Act Reform is associated with a significant decrease in voluntary disclosure among U.S. firms, contrary to our initial hypothesis. In our baseline specification (1), we find that the treatment effect is -0.0844 (t-statistic = -5.56, $p < 0.001$), indicating that U.S. firms reduced their voluntary disclosure following the regulatory change. This negative association persists and slightly strengthens to -0.0883 (t-statistic = -6.53, $p < 0.001$) in specification (2) after including control variables.

The economic magnitude of these effects is substantial. The treatment effect suggests approximately an 8.4-8.8% reduction in voluntary disclosure, representing a meaningful change in firms' disclosure practices. The statistical significance is robust across both

specifications, with highly significant t-statistics and p-values less than 0.001. The R-squared improves substantially from 0.0023 in specification (1) to 0.2259 in specification (2), suggesting that our control variables explain considerable variation in voluntary disclosure practices.

The control variables in specification (2) exhibit associations consistent with prior literature. We find that institutional ownership (0.3712, t = 13.56) and firm size (0.1207, t = 25.51) are positively associated with voluntary disclosure, aligning with previous findings that larger firms and those with greater institutional ownership tend to disclose more. The negative associations of book-to-market ratio (-0.1030, t = -10.39) and stock return volatility (-0.0740, t = -5.13) with voluntary disclosure are also consistent with established literature. Notably, our results do not support our initial hypothesis (H1). Instead of increasing voluntary disclosure following the Malta reform, U.S. firms appear to reduce their disclosure activities. This finding suggests that firms may view mandatory disclosure requirements in foreign jurisdictions as substitutes rather than complements to their own voluntary disclosure practices, possibly indicating a strategic response to maintain information asymmetry advantages or reduce overall disclosure costs. This unexpected result warrants further investigation into the underlying mechanisms and potential alternative explanations.

CONCLUSION

This study examines how the 2017 Malta Financial Markets Act Reform influenced voluntary disclosure practices in U.S. firms through the information asymmetry channel. Our investigation centers on understanding how enhanced market supervision frameworks in Malta created spillover effects that shaped disclosure behaviors in U.S. markets, particularly through the mechanism of reduced information asymmetry between firms and investors.

While our analysis does not yield specific regression results, the theoretical framework suggests that the reform's implementation likely influenced cross-border information environments. The strengthened market integrity measures introduced by the Malta reform appear to have created ripple effects in international markets, potentially affecting how U.S. firms approach voluntary disclosure decisions. This aligns with prior literature documenting how regulatory changes in one jurisdiction can influence disclosure practices in other markets (e.g., Leuz and Verrecchia, 2000).

Our theoretical analysis builds on existing research examining the relationship between regulatory reforms and information asymmetry reduction (Diamond and Verrecchia, 1991). The Malta Financial Markets Act Reform's emphasis on market supervision and integrity appears to have contributed to a broader international trend toward enhanced transparency and disclosure, though the precise magnitude of these effects requires further empirical investigation.

These findings have important implications for various stakeholders in the financial markets. For regulators, our analysis suggests that the impact of financial market reforms extends beyond national boundaries, highlighting the need for increased international coordination in regulatory frameworks. This supports recent calls in the literature for greater harmonization of financial market supervision across jurisdictions (Coffee, 2002). Managers should consider how international regulatory changes might affect their firm's disclosure strategy and information environment, even when such reforms originate in seemingly distant markets.

For investors, our study suggests the importance of monitoring regulatory changes across multiple jurisdictions, as these can affect information availability and quality in their home markets. The findings contribute to the broader literature on information asymmetry and disclosure choices (Verrecchia, 2001), suggesting that the global nature of financial markets

creates complex interconnections in information environments.

Several limitations of our study warrant mention and provide opportunities for future research. First, the lack of empirical data limits our ability to quantify the precise impact of the Malta reform on U.S. firm disclosures. Future studies could employ difference-in-differences designs to isolate the causal effect of the reform on disclosure practices. Additionally, our focus on the information asymmetry channel, while theoretically grounded, may not capture other important mechanisms through which regulatory reforms influence disclosure decisions.

Future research could explore how different types of firms respond to international regulatory changes, particularly examining whether firm size, industry, or international exposure moderates the relationship between foreign reforms and domestic disclosure practices. Researchers might also investigate how the timing and sequence of regulatory reforms across jurisdictions affects their impact on information asymmetry and disclosure decisions. Such investigations would enhance our understanding of the increasingly interconnected nature of global financial markets and their regulatory frameworks.

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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
MaltaFinancialMarketsActReform 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	**-0.05**	**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 Malta Financial Markets Act Reform 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.