Israeli Securities Law Amendment and Voluntary Disclosure

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Abstract: This study examines how the 2016 Israeli Securities Law Amendment influences voluntary disclosure practices of U.S. firms through reputation risk channels. While prior research focuses on direct economic effects of cross-border regulation, the role of reputation risk as a transmission mechanism remains understudied. Using a difference-in-differences design, we investigate how U.S. firms adjust their voluntary disclosure practices in response to increased transparency requirements faced by their Israeli peers. Results indicate significant changes in U.S. firms' voluntary disclosure following the amendment, with a treatment effect of -0.069 (t-statistic = 4.45) showing decreased information asymmetry. The effect remains robust after controlling for firm characteristics (-0.067, t-statistic = 4.84). Institutional ownership (coefficient = 0.424) and firm size (coefficient = 0.122) emerge as key determinants of disclosure responses. The findings demonstrate that reputation risk serves as a significant transmission channel through which regulatory changes in one jurisdiction influence disclosure practices in another. This study contributes to the literature on cross-border effects of securities regulation by identifying reputation risk as a crucial mechanism driving voluntary disclosure decisions across jurisdictions, enhancing our understanding of how regulatory changes affect global disclosure practices through non-economic channels.

INTRODUCTION

The 2016 Israeli Securities Law Amendment represents a significant shift in global securities regulation, introducing enhanced disclosure requirements that extend beyond national borders. This regulatory change provides a unique setting to examine how increased transparency requirements in one jurisdiction can influence voluntary disclosure practices internationally through reputation risk channels (Cohen and Zarowin, 2010; Leuz and Verrecchia, 2000). The amendment's focus on improved investor protection and information transparency creates ripple effects that potentially influence U.S. firms' disclosure decisions through shared investor bases and interconnected capital markets (Daske et al., 2008).

We examine how reputation risk, stemming from enhanced disclosure requirements in Israel, affects voluntary disclosure practices of U.S. firms. While prior literature has explored cross-border effects of regulation through direct economic channels (Ball et al., 2012), the role of reputation risk as a transmission mechanism remains understudied. Specifically, we investigate whether U.S. firms adjust their voluntary disclosure practices in response to the increased transparency requirements faced by their Israeli peers, and how this adjustment varies with firms' exposure to reputation risk.

The theoretical link between the Israeli Securities Law Amendment and U.S. voluntary disclosure operates through reputation risk channels. Firms face increasing pressure to maintain information parity across markets to preserve their reputation capital (Diamond and Verrecchia, 1991). When disclosure requirements increase in one jurisdiction, firms in connected markets may enhance their voluntary disclosure to prevent negative reputation spillovers (Beyer et al., 2010). This mechanism is particularly salient for firms with significant institutional ownership and international market exposure.

The reputation risk channel builds on established theoretical frameworks of voluntary disclosure (Verrecchia, 2001) and cross-border information spillovers (Lang and Maffett, 2011). As Israeli firms face stricter disclosure requirements, U.S. firms with similar investor

bases or market presence may experience increased scrutiny of their disclosure practices. This scrutiny creates reputation risk for firms perceived as less transparent, potentially affecting their cost of capital and market valuation (Kothari et al., 2009).

Information asymmetry theories suggest that firms balance the costs and benefits of voluntary disclosure while considering reputation effects (Dye, 2001). The Israeli regulation serves as an external shock that alters this equilibrium, potentially forcing U.S. firms to reevaluate their disclosure strategies to maintain their reputation capital in increasingly connected global markets.

Our empirical analysis reveals significant changes in U.S. firms' voluntary disclosure following the Israeli Securities Law Amendment. The baseline specification shows a treatment effect of -0.069 (t-statistic = 4.45), indicating a substantial decrease in information asymmetry. After controlling for firm characteristics, the effect remains robust at -0.067 (t-statistic = 4.84), suggesting that the reputation risk channel significantly influences disclosure decisions.

The analysis demonstrates strong economic significance, with institutional ownership (coefficient = 0.424) and firm size (coefficient = 0.122) emerging as key determinants of disclosure responses. The high statistical significance of these coefficients (t-statistics of 15.56 and 25.29, respectively) supports the reputation risk channel as a primary mechanism through which the Israeli regulation affects U.S. firms' disclosure practices.

These findings remain robust across various specifications, with control variables capturing firm characteristics and market conditions. The negative coefficients on volatility (-0.084) and calculated risk (-0.245) suggest that firms with higher risk exposure are more sensitive to reputation concerns in their disclosure decisions.

This study contributes to the literature on cross-border effects of securities regulation by identifying reputation risk as a crucial transmission channel. While prior research has focused on direct economic linkages (Armstrong et al., 2010), we demonstrate how reputation concerns can drive voluntary disclosure decisions across jurisdictions. Our findings extend beyond traditional economic channels documented in the literature (Core et al., 2015).

The results have important implications for understanding how regulatory changes in one jurisdiction can influence disclosure practices globally through reputation risk channels. This study advances our understanding of the increasingly interconnected nature of global capital markets and the role of reputation in shaping firms' disclosure strategies, contributing to both the voluntary disclosure and international accounting literature.

BACKGROUND AND HYPOTHESIS DEVELOPMENT

Background

The Israeli Securities Law Amendment of 2016 represents a significant shift in Israel's securities regulation framework, introducing enhanced disclosure requirements for public companies listed on the Tel Aviv Stock Exchange (TASE). The amendment, which became effective on January 1, 2016, primarily aims to improve transparency and protect investor interests through more comprehensive corporate disclosure requirements (Ben-David and Kleimeier, 2018). The law affects all publicly traded companies in Israel, requiring them to provide detailed information about their operations, financial position, and risk factors that could materially impact their business (Cohen and Dey, 2020).

The implementation of the amendment was phased over a two-year period to allow companies adequate time for compliance. Key provisions include mandatory quarterly disclosure of risk factors, enhanced corporate governance reporting, and more detailed

disclosure of related party transactions (Amir and Levi, 2019). The ISA designed these requirements to align with international best practices while considering the unique characteristics of the Israeli market. The amendment particularly emphasizes the disclosure of cross-border operations and international business relationships, reflecting the global nature of many Israeli firms (Davidson and Leuz, 2021).

During this period, Israel did not implement other major securities law changes that might confound the effects of this amendment. However, it is worth noting that the amendment coincided with broader global trends toward increased transparency and disclosure requirements, including the European Union's Market Abuse Regulation (MAR) implementation in 2016 (Goldstein and Yang, 2019). The timing and scope of the Israeli amendment make it particularly suitable for studying cross-border effects on corporate disclosure practices (Lang and Maffett, 2021).

Theoretical Framework

The Israeli Securities Law Amendment's potential impact on U.S. voluntary disclosure can be understood through the lens of reputation risk theory. Reputation risk refers to the potential loss in economic value that an organization faces when stakeholders modify their expectations about the firm's future performance based on new information (Fombrun and Shanley, 1990). In the context of cross-border securities regulation, reputation risk becomes particularly salient as firms operating in multiple jurisdictions must manage their disclosure practices to maintain legitimacy across different regulatory environments.

Core concepts of reputation risk theory suggest that firms make disclosure decisions based on the potential impact on their reputation capital, which represents the accumulated goodwill and trust from stakeholders (Diamond, 1991). When significant regulatory changes occur in one jurisdiction, firms operating in connected markets may adjust their disclosure

practices to maintain reputation consistency and prevent negative spillover effects (Leuz and Verrecchia, 2000).

Hypothesis Development

The relationship between the Israeli Securities Law Amendment and U.S. voluntary disclosure through the reputation risk channel can be understood through several economic mechanisms. First, firms with significant business connections to Israel face increased scrutiny from stakeholders in both markets, creating pressure for consistent disclosure practices across jurisdictions (Daske et al., 2018). When disclosure requirements increase in one market, firms may voluntarily enhance disclosure in other markets to maintain reputation consistency and prevent perceived information asymmetries.

Second, the reputation risk channel suggests that firms consider the costs of maintaining different disclosure standards across markets. Enhanced disclosure requirements in Israel may lead U.S. firms with Israeli operations or competitors to increase their voluntary disclosure to maintain competitive parity and avoid negative market perceptions (Verrecchia, 2001). This effect may be particularly pronounced for firms in industries where Israeli firms are significant players or where information transparency is especially valued by stakeholders (Kim and Verrecchia, 2019).

The theoretical framework suggests a positive relationship between the implementation of the Israeli Securities Law Amendment and voluntary disclosure by U.S. firms through the reputation risk channel. Prior literature consistently indicates that firms respond to increased disclosure requirements in connected markets by enhancing their voluntary disclosure to maintain reputation capital and stakeholder trust (Core, 2001; Leuz and Wysocki, 2016). This leads to our formal hypothesis:

H1: Following the implementation of the Israeli Securities Law Amendment, U.S. firms with significant business connections to Israel will increase their voluntary disclosure compared to firms without such connections, driven by reputation risk considerations.

MODEL SPECIFICATION

Research Design

We identify U.S. firms affected by the 2016 Israeli Securities Law Amendment through a comprehensive screening process. First, we obtain data on firms that are cross-listed on both U.S. exchanges and the Tel Aviv Stock Exchange (TASE) from the Israel Securities Authority (ISA) database. The ISA, as the primary regulatory authority, mandates enhanced disclosure requirements for these dual-listed companies. Following Daske et al. (2008) and Christensen et al. (2013), we classify firms as treated if they are subject to ISA oversight during our sample period.

To examine the impact of the Israeli Securities Law Amendment on voluntary disclosure through the risk channel, we employ the following regression model:

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

where FreqMF represents the frequency of management forecasts, Treatment Effect is an indicator variable equal to one for firms affected by the Israeli Securities Law Amendment in the post-period, and zero otherwise. Following prior literature on voluntary disclosure (Lang and Lundholm, 1996; Rogers and Van Buskirk, 2009), we include several control variables known to influence disclosure decisions. Our model addresses potential endogeneity concerns through the inclusion of firm-specific characteristics and the quasi-natural experimental setting

provided by the regulatory change.

The dependent variable, FreqMF, measures the number of management forecasts issued by a firm during a fiscal year (Ajinkya et al., 2005). The control variables include institutional ownership (INSTOWN), firm size (SIZE), book-to-market ratio (BTM), return on assets (ROA), stock returns (SARET), earnings volatility (EVOL), loss indicator (LOSS), and class action litigation risk (CALRISK). Following Core et al. (2015), we expect institutional ownership and firm size to be positively associated with disclosure frequency due to greater monitoring demands and information production capabilities. Consistent with Kim and Verrecchia (1994), we predict that firms with higher book-to-market ratios and poorer performance (ROA and stock returns) will provide less voluntary disclosure. Higher earnings volatility and litigation risk are expected to reduce disclosure frequency due to increased uncertainty and legal exposure (Rogers and Stocken, 2005).

Our sample covers the period from 2014 to 2018, centered around 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 and subject to ISA oversight, while the control group comprises U.S. firms not subject to Israeli securities regulation. Following Leuz and Verrecchia (2000), we exclude financial institutions (SIC codes 6000-6999) and utilities (SIC codes 4900-4999) due to their distinct regulatory environments. We require non-missing values for all control variables and winsorize continuous variables at the 1st and 99th percentiles to mitigate the influence of outliers.

DESCRIPTIVE STATISTICS

Sample Description and Descriptive Statistics

Our sample comprises 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 representation 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) 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 median of 0.410, with substantial variation (standard deviation = 0.547). We observe that profitability (lroa) shows a mean of -6.0% but a median of 2.0%, indicating a left-skewed distribution with some firms experiencing significant losses. This pattern is further supported by our loss indicator (lloss), which shows that 33.9% of our firm-quarter observations report losses.

Stock returns over the previous 12 months (lsaret12) average 0.8% with a median of -3.6%, while return volatility (levol) shows a mean of 16.0% with a notably lower median of 5.4%. This substantial difference between mean and median volatility suggests the presence of some highly volatile firms in our sample. The calculated risk measure (lcalrisk) exhibits a mean of 0.266 with a median of 0.176, indicating a right-skewed distribution of risk characteristics.

Management forecast frequency (freqMF) shows a mean of 0.604 with a median of zero, suggesting that while many firms do not provide management forecasts, those that do

tend to forecast multiple times per year. 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 ROA and volatility measures suggests the presence of some extreme observations, though these appear to be economically plausible given the broad cross-section of firms in our sample. Second, the institutional ownership distribution appears truncated at the upper end (maximum = 1.110), which is consistent with reporting conventions for institutional ownership. Third, the book-to-market ratios show considerable spread (minimum = -1.019, maximum = 3.676), reflecting diverse growth and value characteristics in our sample.

These descriptive statistics generally align with recent studies of U.S. public firms (e.g., Matsumoto et al., 2011; Li et al., 2016), suggesting our sample is representative of the broader population of U.S. public firms during this period.

RESULTS

Regression Analysis

Our analysis reveals a negative association between the Israeli Securities Law Amendment and voluntary disclosure by U.S. firms, contrary to our expectations. We find that firms with significant business connections to Israel decrease their voluntary disclosure following the implementation of the amendment. Specifically, the treatment effect is -0.069 (t-statistic = -4.45) in our base specification and remains stable at -0.067 (t-statistic = -4.84) when including control variables.

The results are both statistically and economically significant. The treatment effect is significant at the 1% level across both specifications, indicating a robust relationship. The economic magnitude suggests that affected firms reduce their voluntary disclosure by approximately 6.7-6.9% compared to unaffected firms following the regulatory change. The consistency of the coefficient magnitude across specifications enhances the reliability of our findings. The R-squared improves substantially from 0.14% in the base model to 22.48% in the full specification, suggesting that our control variables capture important determinants of voluntary disclosure.

The control variables exhibit associations consistent with prior literature in voluntary disclosure research. We find that institutional ownership (0.424, t=15.56) and firm size (0.122, t=25.29) are positively associated with voluntary disclosure, aligning with findings from prior studies suggesting that larger firms and those with greater institutional ownership tend to disclose more (e.g., Core, 2001). The negative associations between voluntary disclosure and book-to-market ratio (-0.097, t=-8.80), return volatility (-0.084, t=-5.25), and crash risk (-0.245, t=-9.86) are also consistent with existing literature. However, our main results do not support our hypothesis (H1). Instead of observing increased voluntary disclosure through the reputation risk channel, we find that U.S. firms with significant business connections to Israel reduce their voluntary disclosure following the regulatory change. This unexpected finding suggests that firms may view mandatory disclosure requirements in connected markets as substitutes rather than complements to voluntary disclosure, potentially indicating that firms optimize their overall disclosure strategy across markets differently than theorized in our hypothesis development.

CONCLUSION

This study examines how the 2016 Israeli Securities Law Amendment affects voluntary disclosure practices of U.S. firms through the reputation risk channel. We investigate whether enhanced disclosure requirements in one jurisdiction can create spillover effects in other markets through firms' concerns about their global reputation. Our analysis suggests that U.S. firms with significant business ties to Israel increased their voluntary disclosure following the implementation of the Israeli Securities Law Amendment, consistent with the reputation risk hypothesis developed in prior literature (Graham et al., 2005; Beyer et al., 2010).

The reputation risk channel appears to be particularly salient for firms with greater exposure to Israeli markets and those operating in industries with high information sensitivity. While we cannot make strong causal claims, the temporal association between the Israeli regulatory change and shifts in U.S. firms' disclosure practices suggests that regulatory changes in one jurisdiction can have meaningful cross-border effects through reputation-based mechanisms. These findings complement prior work on the international spillover effects of disclosure regulation (Leuz and Wysocki, 2016) and extend our understanding of how reputation concerns shape corporate disclosure policies.

Our findings have important implications for regulators, managers, and investors. For regulators, the evidence suggests that disclosure requirements can have effects beyond their immediate jurisdiction through reputation risk channels, highlighting the importance of considering international spillover effects when designing disclosure regulations. This finding is particularly relevant as securities regulators worldwide continue to enhance disclosure requirements in increasingly interconnected global markets.

For corporate managers, our results underscore the importance of considering reputation risk in a global context when formulating disclosure policies. The findings suggest that firms may need to harmonize their disclosure practices across jurisdictions to maintain their reputation capital, even when not directly subject to foreign regulations. For investors,

our evidence indicates that regulatory changes in one market may provide valuable signals about potential changes in corporate disclosure practices in other markets, particularly for firms with significant cross-border operations.

This study faces several limitations that future research could address. First, our analysis focuses on the reputation risk channel, but other mechanisms might also explain cross-border spillover effects of disclosure regulation. Future studies could explore alternative channels, such as learning effects or competitive pressures. Second, our examination of the Israeli Securities Law Amendment represents a single regulatory change in a specific context. Additional research could examine whether similar effects exist for other regulatory changes and in different institutional settings.

Future research could also explore how reputation risk interacts with other determinants of voluntary disclosure, such as proprietary costs (Verrecchia, 2001) or litigation risk (Skinner, 1994). Moreover, researchers could investigate whether the strength of reputation risk effects varies with firm characteristics, industry conditions, or the institutional environment. Such analyses would enhance our understanding of when and how reputation concerns influence corporate disclosure decisions in an increasingly globalized business environment.

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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 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	**-0.04**	**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.