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# IT’S A SMALL WORLD AFTER ALL: THE CONVERGENCE OF DISCLOSURE PRACTICES ACROSS LEGAL REGIMES OVER TIME

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**ABSTRACT**

The literature on disclosure practices has posited a relationship between legal regime and the amount of voluntary disclosure. Specifically, companies in nations with a civil law tradition were expected to make more voluntary disclosure to compensate for the information that would otherwise be required in common law nations. This expectation was predicted on the assumptions that investors in the former nation would have salient information needs such that the proprietary costs of information production would be overcome. Data collected from 75 firms across the world were used to support the finding that the extent of difference across legal regimes is diminishing over time.



Keywords: Legal Origins; Voluntary Disclosure; Disclosure Practices; Common Law and Civil Law Regimes; Corporate Governance; Convergence.

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## 1. INTRODUCTION

Although the international reach of capital has never been stronger, the extent to which the legal minimums for disclosures influence the disclosure levels that a company will select need to be determined. In that companies often see the law as determining that which must be done, anything above this cannot be relied upon. Companies often see discretionary disclosures as competitively disadvantageous (Verrechia, 2001; Depoers, 2000). Managers are not as likely as academics to believe that disclosures necessarily reduce the cost of capital (see Botosan 1997; Botosan and Plumlee 2002; Hail 2002). A permanent difference in disclosure levels may be induced by differences in the legal environment.

Although every country presents a unique case, two ideal types differentiate legal systems. The distinction is made into civil and common law countries due the influence of Romano-Germanic traditions on the former, and the law of England on the latter (Reynolds and Flores, 1989). Common law countries construct relatively rigid regulation for accounting disclosures. Usually this provides investors with stronger legal protection. This contrasts with civil law traditions that are built upon the interpretation of more general principles. Civil law, because it is less certain and more flexible, generally provides investors with weaker legal protection when discretionary disclosure proves inadequate.

This paper argues that the disclosure realized in the two legal traditions should become more similar over time. This may be the result of the diffusion of certain core ideas about corporate governance. A degree of isomorphism may exist such that governance practices become more similar (OECD 1999; Milman et al. 1999; Reed 2002; Nestor and Thompson 2000). This information package provided to investors may follow suit in due time, becoming marked by progressively smaller variance. In a more classic economic vein, economic self interest may alleviate disclosures across legal structures. Reacting to an otherwise higher cost of capital and steeper risk premia on debt (Sengupta, 1998), companies may exercise discretion in a predictable discretion (Gray and Skogsvik, 2004).

This paper considers the degree of discretionary disclosures offered by the largest firms in the world at two points in time. It finds that the disclosure gap caused by the location of these firms in varying legal traditions is lessening over time. The research is organized into four subsequent sections. The first reviews the critical literature for the purpose of establishing a hypothesis. The second describes how the empirical work was conducted. A third section summarizes the findings. The last section discusses the results, offers implications and admits limitations.

## 2. RELATED LITERATURE AND HYPOTHESIS DEVELOPMENT

Agency theory provides a useful template for the understanding of the struggle between managers (agents) and owners (principals) (see Jensen and Meckling, 1976; Fama 1980; Fama and Jensen 1983). In its simple setting, the parties are free to negotiate with each other such that the consequences of moral hazard in an inevitable world of information asymmetry can be anticipated and contractually mitigated. However, when applied to the conduct of business by modern corporations other considerations come into play. In general, political entities interrupt the freedom of the parties to manage agency costs. Acting on behalf of the public interest, states make regulatory decisions that reduce the freedom of agents to provide information[2]. Furthermore, states establish penalties that enter into the cost/benefit calculations of actors involved in corporate management and ownership. Although it could be said that all governments are interested in allowing managers the ability to exercise discretion and also concerned with the potential victimization of investors in those enterprises, where the balance is struck varies among politics.

Research into the legal tradition of a country and its effect on financial markets was popularized by a series of influential papers by La Porta et al. (1997, 1998, 2002). Their research examined the legal rules that relate to shareholder and creditor protection, with their findings indicating that common-law countries such as the U.S., UK, and Australia have the strongest legal protection of shareholders, while French-civil-law countries such as France, Spain, the Netherlands, and Italy offer the least legal protection of investors, they also find that German and Scandinavian-civil-law countries (which have also influenced legal theory in Japan, Korea and Switzerland) are in the middle of those two groups. Consequently, a growing literature has sought to understand the importance of the legal environment upon the private sector. Often this research entails the intertwining of legal coercion and voluntary action such that some sort of equivalence

[2] See GAAP-SEC REQIREMENTS, report of the steering committee of the Business Reporting Research Project, 2001

is forged between the existence of a statutory requirement and the recognition of self interest.

Several means have been used to describe differences in legal environments for these purposes. These differences should be appreciated and accommodated since so many discrete elements combine in the delivery of the protection of the citizenry. Some researchers have looked more to the quality and strength of the institutions that can be activated in the enforcement of investor rights. Others have prioritized the existence of specific rights for minority interests, often relevant at particularly turbulent times in the history of a corporate entity.

Any consideration of the legal environments makes certain assumptions about the capital markets. High quality capital markets appear to require a certain caliber of guarantees in the law. La Porta et al. (1997) show that countries with weak investor protection and a civil law tradition tend to have weaker and less efficient capital markets. This is important if for no other reason than providing investors with some reasonable alternative in the event that they become dissatisfied with their investment. This possibility can also be captured through measures of the relative importance of small investors in such a trading venue (La Porta et al. 1998).

The most typical approach taken by research is to focus upon the information controlled by the corporate managers. In the most regular sense, the legal system is important in that it creates expectations for a certain level of investor empowerment. To wit, the law requires that information that is valid and sufficient be routinely and timely disclosed. Investors, aided by their professional advisors, are expected to use this information to evaluate the risk and expected return of their equity positions.

Hope (2003) provides the best touchstone in the literature to establish the idea that disclosure practices are shaped by the general nature of the legal system. More disclosures occur when firms are situated in nations marked by a common law legal environment. In a similar vein, civil law companies have greater barriers to list in U.S. exchanges (Durand and Tarca, 2005).

More recently, attention has turned to how the legal system facilitates, and possibly encourages, a responsible system of corporate governance. If shareholders appreciate how corporations will be managed, and how much self protection is built into normal corporate operations, they are less likely to be victimized. Bushman et al. (2004) show that countries with better judicial efficiency are likely to have corporations with more transparent corporate governance traditions. In this regard, good corporate governance may require more than disclosure. For example, Defond and Hung (2004) show countries with stronger and more protective legal environments are more likely to have corporate practices that identify and terminate poorly performing corporate executives. One would imagine that the entrenchment of management not in the interest of shareholders would be easier in less trenchant legal environments.

Investors must anticipate more than just the natural outcomes of the business of the corporate entity. Ample evidence has been produced in the last twenty years so that investors need to anticipate some degree of earnings management by publicly traded enterprises. Haw et al. (2004) show that stronger legal protections, measured by the aggregation of several specific attributes, are more likely to constrain these tendencies. Apparently, in weaker legal traditions, managers perceive carte blanche in the manipulation of accounting flexibility (see also Leuz et al. 2003).

The salience of the legal system can also be observed when companies more formally transcend their political boundaries. For example, Reese and Weisbach (2002) find that foreign firms that are also listed on U.S. exchanges tend to upgrade their protection afforded to minority interests. Apparently entry into a new legal system engenders new expectations for corporate managers (see also Khanna et al. 2004).

In a more general sense, the legal environment creates broader expectations for appropriate behavior in the management of corporations. Findings by Volpin (2002) that relate the caliber of the legal environment to firm performance and executive turnover, suggests a greater institutional tolerance for underperformance. The inability to wrest control back from ineffective management inflicts greater losses on minority interests who are more dependent upon financial returns.

Often the importance of legal environment can be expressed in the overall availability of information, even if its consequences are indirect. Firms, encouraged by the law to increase their overall disclosures, enjoy lower effective interest rates on new debt (Sengupta, 1998). Higher disclosure is also associated with a higher degree of analyst attention (Lang and Lundolm, 1996). Since analysts tend to be optimistic beyond the factual support for optimism (Fogarty and Rogers, 2005), high analyst following is likely to be supportive of equity valuation. At the same time, higher disclosure rates may also change the composition of shareholders such that less patient owners may dominate (Bushee and Noe, 2000). More specifically, information that provides better insight on the nature of corporate restructuring is associated with more diligent external monitoring of corporations (Bens, 2001).

In sum, the literature supports the premise that the legal system matters to the corporate balance of power between shareholders and managers. This occurs primarily through the impact of the law on the amount of disclosure that is made available to the investing community. However, several questions need to be answered before comfort can be said to exist about these relationships.

Legal systems may be relatively stable in the differences they pose to corporate control. However, managers are able to take a variable approach to their environment. Studies that have documented cross-sectional variations may inadvertently overstate the degree of difference that is likely to exist in the future. A more longitudinal approach may provide a better sense for the ways that managers accommodate and adjust to their legal environment. The failure to consider temporal change may be an invitation to possess antiquated knowledge.

Many studies in this area have studied country differences. This level of analysis appears obvious when considering legal systems. However, disclosure is a firm characteristic. The aggregation of many firms to restate disclosure on a national basis may be distortive of the individual firm choice that is inherent in disclosure. Restoring the firm as the level of analysis also mitigates cultural variation in this phenomenon (see Hope, 2003; Jaggi and Low, 2000). A focus upon firms also prevents the degree of economic development from becoming the strongest factor in explaining corporate design results (e.g., Doidge et al. 2004).

The above analysis leads to the only hypothesis studied by this paper. Stated in the null form:

**$H_0$: The relationship between the legal environment and the level of corporate disclosure will not**

**change over time.**

## 3. METHODS

This paper purposefully draws upon a sample of the world's largest companies to test its hypothesis. This choice was made for several reasons. First, these firms have extraordinary visibility. Their attributes and their disclosures are likely to be closely followed by the media and closely scrutinized by the governments with power over them. Secondly, these large firms are the most likely participants in the global capital markets. They are more likely than other firms to participate in equity markets beyond their home nations and to constantly endeavor to attract foreign capital through systematic cross-border strategies.

Such a sample initially drew upon the Dow Jones Global Titans Index. This group purposefully represents companies from many different industries and nations, with all characterized by high degrees of global diversification. However, the 14 financial sector firms in this index were likely to be excessively incomparable and therefore needed to be dropped. Left with 25 common law origin firms and 11 civil law origin firms, the sample was expanded and rebalanced by adding the five largest non-financial firms from South Korea, Italy and the Netherlands, and the ten largest companies from Japan, France and Germany. After deleting thirteen firms due to insufficient data, 68 firms from nine countries comprised the sample. Table 1 provides more information about the sample.

[Table 1 here]

Disclosure data was collected for 1995 and 2002. The former was chosen because it was the first year for which adequate data was available. The latter year was chosen for similar reasons, measured at the time that data collection was conducted. Data used in this study was collected from a variety of sources. The sources included proxy statements, annual shareholder reports and other company disclosure outlets.

The importance of corporate governance characteristics as a vehicle of investor self protection recommended that they form the focus of the disclosure variable. In addition to their importance, corporate governance serves as readily measurable and quantifiable following Muslu (2005). Since corporate governance attributes have become more problematized in recent years (Parker 2005), incentives exist for companies to disclose in this area as part of addressing the underlying agency issues (La Porta et al. 2000; Denis and McConnell 2003).

Efforts were made to determine if companies revealed seven different corporate governance facts. These included 1) whether the CEO also served as board chairman; 2) the percentage of non-executive (independent) directors; 3) whether the board chairman was independent; 4) the percentage of non-executive members of the audit committee; 5) the percentage of non-executive members of the nominating committee; 6) the percentage of non-executive members of the remuneration committee; and 7) the independence of the chairman of the remuneration committee. Each of these separate dimensions was binary coded (0=not disclosed, 1=disclosed). In addition to the separate variables so constructed, an aggregate corporate governance disclosure score was calculated. Measures on these dimensions were taken in both 1995 and 2002. Table 2 provides more information about these measures.

[Table 2 here]

Legal regime was measured in three ways. First, a binary variable (common) distinguished countries with a common law tradition and those with a statutory approach. Second, using information from LaPorta et al. (1997), a scale that measures the maturity of the law and order tradition in a country was implemented. Last, a more global measure of judicial efficiency, rule of law and corruption was taken from Gul (2000). These variables are also defined and elaborated in Table 2.

In order to segregate other influences on disclosure level, several control variables were needed. These included a consideration of corporate size and total debt, both obviously linked to disclosure (Bens, 2001; Marston and Shrives, 1996; Hope, 2003). The literature also recommends the use of a set of variables related to the maturity of equity markets in a country. These were combined into a single measure consisting of principal component factors in order to improve model degrees of freedom. Finally, following Khanna (2004), firms tracking in U.S. exchanges (as ADRs) were distinguished since it appears to be an independent factor pertaining to disclosure intensity. Again, Table 2 provides more information about variable nomenclature and scoring.

Multivariate analysis was used as the primary means for the tests of the hypothesis. For these purposes, the change in aggregate disclosure was the dependent variable that was related to the various legal environment proxies in conjunction with the control variables. Univariate analysis extended the analysis of particular relationships.

## 4. FINDINGS

Because the most comprehensive measure of the differences in legal environment is the distinction between common law and civil law nations, the first analysis focuses upon that measure. Table 3 reports the statistical evaluation of models that include only that legal variable. For these purposes, Model 1 and Model 2 vary only by the inclusion of the U.S. market listing control variable.

[Table 3 here]

In both models, the legal environment variable (common) is strongly significant ($p<.01$) on the change in disclosure. This evidence rebuts the null hypothesis of no change over time.

As expected, several of the control variables are also significant. Most importantly, the composite related to the maturity of a country's equity exchanges (Market Factors) is significant at $p<.01$. Leverage is also significant, albeit at $p<.05$. Perhaps because of the way the sample was restricted to the very largest firms, the size variable (Log Assets) was not significant. Since the U.S. listing control variable was also not significant ($p>.05$), Model 1 and Model 2 did not produce varying results. Model 1 is superior since it produced the same explanatory power with fewer independent variables.

Table 4 initiates the consideration of additional legal variables with three separate combinations. First, Model 1 uses the aggregate construct of enforcement measures, named Lenforc. This produced a relatively poorly performing outcome highlighted by the not significant legal construct and low $R^2$. A better result was obtained in Model 2, using the rule of law proxy titled RLAW. This variable proved significant at $p<.05$. However, the control variables were all unexpectedly not significant and total explanatory power did not improve much beyond Model 1.

[Table 4 here]

Combining the insights from Model 1 from Table 3 and Model 2 from Table 4 led to the best combination found as Model 3 in Table 4. This combines the general source of law proxy (common) with the rule of law proxy (RLAW). The variance attributed to RLAW in Model 2 becomes recaptured by common, which is again strongly significant ($p<.01$). A more intuitively satisfying pattern of control variable significance occurs in this model. Moreover, $R^2$ at 0.39 is maximized in this rendition.

In results not shown, the sample was partitioned to focus separately on the nations with common and civil law traditions. In these efforts, the rule of law and the other legal constructs failed to be significant. In other assessments of the multivariate models, efforts were made to determine if the results were robust against the principal component aggregation of the equity markets control variable. No change in the substantive conclusions would be produced if these had been disaggregated. The results were also not adversely affected by multicollinearity, as judged by condition indices.

Univariate analyses allowed a closer examination of the individual dimensions that were combined for purposes of the multivariate analysis. Taking advantage of the general findings, the sample was partitioned into common law and civil law traditions for both 1995 and 2002. Here the purpose would be to see if changes have occurred to the pattern of disclosure relationships over time.

Table 5 summarizes the inter-temporal differences in the specific dimensions of disclosure. Panel A shows that firms in countries with a civil law tradition have made consequential increases in disclosure on all level dimensions. All changes here are significant at $p<.01$, using a Wilcoxian statistic. Panel B shows the same metrics for the firms in common law countries. Four of seven dimensions show even more dramatic increases, going from near the bottom of the 0 – 1 scale to the top or very close to the top (all significant at p<.01). The other three dimensions could not produce significant increases since their 1995 score was already at or very near the top of the scale.

[Table 5 here]

Panel C is noteworthy as a descriptive account of the 2002 differences between the two legal regimes. Common Law firms provide more disclosure across the board, with significant differences persisting in more than half the cases. Although some convergence has occurred, there is still a way to go before equivalence is reached.

## 5. DISCUSSION & CONCLUSION

The agency problem at the heart of the idea of the modern corporation has resulted in much attention from regulators, particularly as it pertains to the minimum information package that is necessary to protect the public interest. This made it necessary and appropriate to examine the success that different legal systems would have in provoking additional disclosure. On the one hand, it was logical to believe that the legal mandates found in civil law would prompt companies to disclose within the framework of the present regulatory regime. On the other, the more general principals found in the common law environment may allow the market forces to operate, potentially yielding an even higher level of disclosure. The results suggest that even though the latter is a more viable description, change appears to be leading to a convergence. Thus, the small world metaphor will be more apt in the future.

The paper has also attempted to make methodological contributions. Disclosure was measured with seven related pieces of information that could be meaningfully aggregated into a scale. This overcomes the tendency in some studies to elevate the importance of individual pieces of information. On the other extreme, this tact is sufficiently focused so that the measurement difficulties of more comprehensive approaches are not encountered. The binary code of present or absent is unambiguous, thereby avoiding unresolvable issues about the quality of disclosure. Progress was also made on the measurement of legal variables. Here the literature contained several different approaches that varied in their comprehensiveness. This paper showed that more restricted measures that focus on a narrower range of legal dimensions, may not be sufficiently articulated to discriminate.

Future research should more squarely frame the reasons that the legal system does not seem to matter as much as it once did. Although the significant results produced by this paper describe the 1995-2002 era, the movement charted by the results cannot sustain this difference. It may be that larger companies are more fundamentally influenced by the requirements of equity markets. It may also be that the very visibility of the larger companies makes them a somewhat compulsory role model for others.

Although a very short period of time has been examined, we suspect that the impact of this constraint was only to underestimate the change in disclosure that is documented. With regards to the dimensions of corporate governance, the clear trend is toward more transparency. More time would have made this change stronger and more apparent in the data. Some might also argue that the period 1995-2002 was a very atypical period since it contains the best years of one of the largest economic expansions in history as well as its sudden termination. However, this business cycle does not seem to be related to the particular elements of disclosure that were examined. Even had they been, the "one way" nature of disclosure, that is – once made they tend to continue, suggests even this business cycle was a legitimate part of the business history we have.

In this study, we examine the disclosure characteristics of a sample of firms that are representative of the largest, global companies operating in diverse economic climates. Looking at data from two time periods, we find that there is convergence in disclosure systems across legal regimes. This paper is the first empirical study to examine disclosure characteristics both inter-temporally and inter-sectorally. Since a lack of disclosure and inadequate transparency facilitates a lack of accountability, this study offers valuable substance. The results document a convergence in disclosure systems consistent with the idea that large firms adopt a common platform. If there is an emergent idea about how much disclosure should be provided at a minimum, more attention should be given to how such understanding develops.

Our results indicate that there are still significant differences in disclosure characteristics across regimes. Firms situated in common law firms have more disclosures when it comes to a variety of governance functions, namely the activities of the board and the composition of various board sub-committees. However, our data indicates that disclosure practices have been both evolving and converging, for both common and civil law firms, toward more disclosures regarding governance matters. Since increased disclosures are associated with market liquidity, reduced cost of capital, and greater overall transparency, a step in the right direction appears to have been taken.

Our study suffers from some data limitations. Documenting the past governance practices of European and East-Asian firms proved to be a difficult task. Many of the firms did not disclose any data. Because the annual reports of some firms could not be obtained, their disclosure level could not be ascertained. Because the sample of 75 firms was drawn from the largest transnational companies, our conclusions are based only on the firm characteristics in that sample. Therefore, we do not make claims regarding the generalizability of our findings to smaller sized or local firms. The data used in this paper preceded the Sarbanes-Oxley mandated or emulated reforms. As of now, data beyond 2003 is not available for many companies, hence it would be interesting to examine the effects of Sarbanes-Oxley in a future analysis. We expect that this influence will result in additional levels of convergence.

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**Table 1: Sample Composition, Size, Legal Origin, and Change in Disclosures**

| Company | Sales ($millions) | Country | Legal Regime | chDisc* |
|---|---|---|---|---|
| Wal-Mart Stores Inc. | 244,524 | USA | Common | 3 |
| General Motors | 184,214 | USA | Common | 3 |
| Exxon Mobil | 178,909 | USA | Common | 3 |
| BP Amoco | 178,721 | UK | Common | 0 |
| Ford | 162,586 | USA | Common | 3 |
| DaimlerChrysler | 156,838 | Germany | Civil | 5 |
| Toyota | 128,000 | Japan | Civil | 0 |
| Mitsui | 112,108 | Japan | Civil | 0 |
| Royal Dutch Petroleum | 107,659 | Holland | Civil | 0 |
| TotalfinaElf | 102,540 | France | Civil | 0 |
| Volkswagen | 98,708 | Germany | Civil | 5 |
| IBM | 81,186 | USA | Common | 3 |
| Carrefour | 68,728 | France | Civil | 3 |
| Hitachi | 68,264 | Japan | Civil | 0 |
| Verizon Communications | 67,625 | USA | Common | 3 |
| Honda | 67,128 | Japan | Civil | 0 |
| Nestle | 64,455 | Switzerland | Civil | 3 |
| Royal Ahold | 62,683 | Holland | Civil | 3 |
| Sony | 62,280 | Japan | Civil | 2 |
| Philip Morris | 61,687 | USA | Common | 3 |
| Matsushita | 61,680 | Japan | Civil | 1 |
| Vivendi | 60,970 | France | Civil | 1 |
| Deutsche Telecom | 60,383 | Germany | Civil | 5 |
| FIAT | 60,371 | Italy | Civil | 4 |
| Hp | 56,588 | USA | Common | 3 |
| Nissan | 56,000 | Japan | Civil | 1 |
| Peugeot | 52,906 | France | Civil | 0 |
| Toshiba | 52,000 | Japan | Civil | 2 |
| Merck & Co. Inc. | 51,790 | USA | Common | 3 |
| Metro | 51,526 | Germany | Civil | 5 |
| Unilever | 50,611 | Holland | Civil | 5 |
| France Telekom | 48,892 | France | Civil | 4 |
| Electricite De France | 48,359 | France | Civil | 3 |
| Suez | 48,325 | France | Civil | 3 |
| Vodafone | 47,962 | UK | Common | 3 |
| RWE | 43,875 | Germany | Civil | 5 |
| SBC Communication | 43,138 | USA | Common | 3 |
| BMW | 42,411 | Germany | Civil | 2 |
| British Telecom | 41,435 | UK | Common | 0 |
| Procter & Gamble Co. | 40,169 | USA | Common | 3 |
| samsung | 39,813 | South Korea | Civil | 4 |
| Deutsche Post | 39,255 | Germany | Civil | 2 |
| NEC | 38,354 | Japan | Civil | 0 |
| Repsol YPF | 38,064 | Spain | Civil | 4 |
| E.ON | 37,878 | Germany | Civil | 5 |
| AT&T | 37,827 | USA | Common | 3 |
| Renault | 36,336 | France | Civil | 0 |

| | | | | |
|---|---|---|---|---|
| Johnson & Johnson | 36,298 | USA | Common | 3 |
| Thyssen Krupp | 35,928 | Germany | Civil | 2 |
| WorldCom Inc. | 35,179 | USA | Common | 3 |
| Nokia | 31,710 | Finland | Civil | 3 |
| Microsoft Corp. | 28,365 | USA | Common | 2 |
| Intel | 26,764 | USA | Common | 3 |
| Hyundai Motors | 25,562 | South Korea | Civil | 2 |
| Walt Disney Co. | 25,329 | USA | Common | 3 |
| Canon | 24,522 | Japan | Civil | 2 |
| Bell South Corp | 22,711 | USA | Common | 3 |
| Roche | 22,498 | Switzerland | Civil | 3 |
| Mitsubishi | 21,764 | Japan | Civil | 0 |
| LG | 20,000 | South Korea | Civil | 0 |
| Cisco System | 18,915 | USA | Common | 3 |
| Michelin | 15,645 | France | Civil | 0 |
| Loreal | 14,000 | France | Civil | 0 |
| Danone | 13,555 | France | Civil | 0 |
| Coca Cola | 12,470 | USA | Common | 3 |
| Lucent Technologies | 12,321 | USA | Common | 3 |
| SK | 8,634 | South Korea | Civil | 0 |
| Pirelli | 6,861 | Italy | Civil | 3 |

**ChDisc* is the difference between 1995 and 2002 for the level of disclosures on various corporate governance characteristics.

## Table 2: Variable Definitions

| | |
|---|---|
| Legal and Market Related Variables: | |
| *Common:* | Takes a value of 1 if the company is from a common law origin country, 0 otherwise |
| *Rlaw:* | Assesment of the law and order tradition in the country |
| *Lenforc:* | A aggregation of various measures of judicial efficiency, rule of law, and corruption indices |
| *Market Factors:* | Factor obtained through the principal component analysis of ATRIGHT, OSOVOTE CRIGHTS, IMPEMKT, and OIRIGHT* |
| *US Listing:* | If shares of the company are traded as an ADR in one of the US exchanges |
| Disclosure Related Variables: | |
| *DiscDual:* | Takes a value of 1 if the company discloses whether the CEO is also the chairman of the board, 0 otherwise |
| *DiscBOD:* | Takes a value of 1 if the company discloses the percentage of non-executive directors sitting on a company board |
| *DiscChrm:* | Takes a value of 1 if the company discloses whether the chairman is an independent director, 0 otherwise |
| *DiscAudit:* | Takes a value of 1 if the company discloses the percentage of non-executive directors on the audit committee |
| *DiscNomin:* | Takes a value of 1 if the company discloses the the percentage of non-executive directors on the nominating committee |
| *DiscRemuner:* | Takes a value of 1 if the company discloses the the percentage of non-executive directors on the remuneration committee |
| *DiscChairremun:* | Takes a value of 1 if the company discloses whether the chairman of the remuneration committee is an independent director, 0 otherwise |
| *ChDisc* | Is the difference between the year 1995 and 2002 of the aggregate of the above disclosure related variables, ranges from 0 to 7 |

*Atright,* is an index aggregating shareholders rights in a particular country from La Porta et al. (1998). *Impemkt,* is an aggregation of an index that measures size of the stock market in relation to GDP, number of listed companies relative to the size of the country, and number of IPOs. We obtain *Impemkt* from Leuz et al. (2003). *Oiright* is an aggregate measure of minority shareholder rights against directors, obtained from La Porta et al. (1998). In order to increase degrees of freedom we use as a control variable *MarketFactors*, which is a factor obtained through a principal component analysis of *Atright, Impemkt,* and *Oiright.* Results in subsequent analysis are not changed if each of those variables are utilized singly, or simultaneously, with our research variables.

**Table 3: OLS regression examining the relationship between legal origin and changes in disclosure**

| | Model 1 | Model 2 |
|---|---|---|
| **Dependent Variable** | ***chDisc*** | ***chDisc*** |
| ***Constant*** | -2.888 | -2.731 |
| | -1.46 | -1.31 |
| ***LogAssets*** | 0.33 | 0.308 |
| | -1.86 | -1.56 |
| ***Leverage*** | **0.481** | **0.464** |
| | **(2.23)*** | **(2.06)*** |
| ***Common*** | **3.407** | **3.533** |
| | **(5.11)**** | **(4.29)**** |
| ***MarketFactors*** | **-1.543** | **-1.576** |
| | **(4.85)**** | **(4.58)**** |
| ***USListing*** | | 0.12 |
| | | -0.27 |
| **Observations** | 68 | 68 |
| **R-squared** | 0.36 | 0.36 |

Absolute value of t statistics under the coefficients

* significant at 5%; ** significant at 1%

*ChDisc* is the difference between 1995 and 2002 for the level of disclosures on various corporate governance characteristics. *Common* takes a value of 1 if the company is from a common law country, 0 otherwise. *LogAssets* is the natural logarithm of the total assets of the company at fiscal year end. *Leverage* is the total debt of the company divided by total assets, again at fiscal year end. *MarketFactors* is a factor obtained through a principal component analysis of various capital markets variables. *USListing* denotes if shares of the company are traded as an ADR in one of the US exchanges

**Table 4: OLS regression examining the relationship between legal characteristics and changes in disclosure**

| | Model 1 | Model 2 | Model 3 |
|---|---|---|---|
| **Dependent Variable** | ***chDisc*** | ***chDisc*** | ***chDisc*** |
| ***Constant*** | -4.393 | -4.866 | **-4.498** |
| | -1.69 | -1.96 | **(2.12)*** |
| ***LogAssets*** | 0.35 | 0.321 | 0.247 |
| | -1.62 | -1.53 | -1.38 |
| ***Leverage*** | 0.449 | 0.399 | **0.447** |
| | -1.78 | -1.61 | **(2.11)*** |
| ***Lenforc*** | 0.282 | | |
| | -1.37 | | |
| ***Rlaw*** | | **0.369** | 0.286 |
| | | **(2.12)*** | 1.91 |
| ***Common*** | | | **3.265** |
| | | | **(4.97)**** |
| ***MarketFactors*** | -0.279 | -0.373 | **-1.657** |
| | -1.3 | -1.72 | **(5.22)**** |
| **Observations** | 68 | 68 | 68 |
| **R-squared** | 0.11 | 0.15 | 0.39 |

Absolute value of t statistics under the coefficients
* significant at 5%; ** significant at 1%

*ChDisc* is the difference between 1995 and 2002 for the level of disclosures on various corporate governance characteristics. *Common* takes a value of 1 if the company is from a common law country, 0 otherwise. *Rlaw* is an assesment of the law and order tradition in the country. *Lenforc* is an aggregation of various measures of judicial efficiency, rule of law, and corruption indices. *LogAssets* is the natural logarithm of the total assets of the company at fiscal year end. *Leverage* is the total debt of the company divided by total assets, again at fiscal year end. *MarketFactors* is a factor obtained through a principal component analysis of various capital markets variables. *USListing* denotes if shares of the company are traded as an ADR in one of the US exchanges

**Table 5: Inter-temporal relationships between the extent of disclosure for corporate governance variables across legal regimes**

**Panel A: Inter-temporal comparisons for civil law country firms**

| | N 1995/2002 | 1995 Mean | 2002 Mean | Wilcoxon p-value |
|---|---|---|---|---|
| ***DiscDual*** | 45/49 | 0.58 | 0.96 | **< 0.01** |
| ***DiscBOD*** | 45/49 | 0.58 | 0.93 | **< 0.01** |
| ***DiscChrmn*** | 45/49 | 0.53 | 0.89 | **< 0.01** |
| ***DiscAudit*** | 45/49 | 0.28 | 0.73 | **< 0.01** |
| ***DiscNomin*** | 45/49 | 0.17 | 0.67 | **< 0.01** |
| ***DiscRemun*** | 45/49 | 0.22 | 0.69 | **< 0.01** |
| ***DiscChairremun*** | 45/49 | 0.16 | 0.49 | **<0.01** |

**Panel B: Inter-temporal comparisons for common law country firms**

| | N 1995/2002 | 1995 Mean | 2002 Mean | Wilcoxon p-value |
|---|---|---|---|---|
| ***DiscDual*** | 24/25 | 1 | 1 | **.** |
| ***DiscBOD*** | 24/25 | 1 | 1 | **.** |
| ***DiscChrmn*** | 24/25 | 0.96 | 1 | 0.16 |
| ***DiscAudit*** | 24/25 | 0.08 | 1 | **< 0.01** |
| ***DiscNomin*** | 24/25 | 0.08 | 0.96 | **< 0.01** |
| ***DiscRemun*** | 24/25 | 0.08 | 1 | **< 0.01** |
| ***DiscChairremun*** | 24/25 | 0.08 | 0.96 | **< 0.01** |

**Panel C: Current differences in Disclosure Practices across legal regimes**

| | N Other/AS | Civil Law Firms Mean | Common Law Firms Mean | Wilcoxon p-value |
|---|---|---|---|---|
| ***DiscDual*** | 25/49 | 0.96 | 1.00 | 0.15 |
| ***DiscBOD*** | 25/49 | 0.94 | 1.00 | 0.11 |
| ***DiscChrmn*** | 25/49 | 0.89 | 1.00 | 0.05 |
| ***DiscAudit*** | 25/49 | 0.73 | 1.00 | **< 0.01** |
| ***DiscNomin*** | 25/49 | 0.67 | 0.96 | **< 0.01** |
| ***DiscRemun*** | 25/49 | 0.69 | 1.00 | **< 0.01** |
| ***DiscChairremun*** | 25/49 | 0.49 | 0.96 | **< 0.01** |

DiscDual: takes a value of 1 if the company discloses whether the CEO is also the chairman of the board, 0 otherwise, DiscBOD: takes a value of 1 if the company discloses the percentage of non-executive directors sitting on a company board, DiscChrm: takes a value of 1 if the company discloses whether the chairman is an independent director, 0 otherwise. DiscAudit: takes a value of 1 if the company discloses the percentage of non-executive directors on the audit committee, DiscNomin: takes a value of 1 if the company discloses the the percentage of non- executive directors on the nominating committee. DiscRemuner: takes a value of 1 if the company discloses the the percentage of non-executive directors on the remuneration committee

DiscChairremun: takes a value of 1 if the company discloses whether the chairman of the remuneration committee is an independent director, 0 otherwise.