

Legal Environments and Accounting Information Comparability

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The dramatic rise in global investment activities increases the demand for more comparable accounting information across countries. The literature suggests that legal environments affect accounting information comparability: firms from common law jurisdictions have higher information comparability than firms from code law jurisdictions. This study examines whether information comparability improves when firms from code law legal jurisdictions are listed in common law jurisdictions. Specifically, we test whether firms from China, a code law jurisdiction, improve their information comparability by listing in Hong Kong, a common law jurisdiction. After controlling for firm-specific characteristics, we find that listing in Hong Kong by Chinese firms actually led to lower comparability.

INTRODUCTION

Over the last two decades, globalization of financial markets has increased the demand for more comparable financial information. This has led to the creation of the International Accounting Standards Committee (IASC), the predecessor of the International Accounting Standards Board (IASB) (Camfferman and Zeff, 2007). Today, over 130 countries and all major stock exchanges in the world have either adopted or allowed the use of International Financial Reporting Standards (IFRS) in an attempt to enhance cross-country comparability of financial information for efficient capital allocation.

Several studies have examined whether the widespread adoption of IFRS has led to improved cross-country information comparability (Barth et al., 2012; Bartov et al., 2005; Bradshaw and Miller, 2008; Hung and Subramanyam, 2007; Gray et al. 2009; and Yip and Young 2012). These studies generally conclude that the adoption of IFRS improves information comparability. Furthermore, the literature suggests that accounting information comparability is also affected by the legal environment. For example, Barth et al. (2012) and Yip and Young (2012) document evidence indicating that the cross-country comparability of financial information is higher for firms from common law jurisdictions than that for firms from code law jurisdictions.

This study extends the comparability literature by examining whether firms from code law jurisdictions can improve their financial information comparability by listing in a common law jurisdiction. Specifically, we examine whether Chinese companies improve their information comparability by listing in Hong Kong. We choose to focus on Chinese companies listed in Hong Kong because China is a code law jurisdiction whereas Hong Kong is a common law jurisdiction (Ball et al., 2000; Ball et al., 2003; Eccher and Healy, 2003; He et al., 2011; Leuz et al., 2003). In addition, there are a large number of Chinese companies listed in Hong Kong, which enables us to conduct sound statistical analysis.

The comparability measure used in this study was developed by De Franco, Kothari, and Verdi (2011) and was subsequently used in several comparability studies (Barth 2012; Francis et al., forthcoming; Yip and Young, 2012). We first calculate comparability scores for Chinese companies listed in Hong Kong (the H-shares) by forming firm pairs of Chinese companies listed in Hong Kong (the H-shares) and Hong Kong companies (the HK-shares) matched by industry and size (hereafter referred to as H-HK pairs). We then calculate comparability scores for Chinese companies listed in China (the A-shares) by forming A-HK pairs (i.e., A-shares and HK-shares). Since Chinese companies listed in Hong Kong (the H-shares) and their counterparts listed in China (the A-shares) use the same accounting standards (i.e., IFRS converged standards) during the sample period and face virtually the same economic, political, social, and cultural environment except where they are listed, any significant differences in information comparability are likely attributable to the listing variable.

While studies have shown that firms from common law jurisdictions have higher information comparability than firms from code law jurisdictions, there are neither empirical evidence nor readily available theory regarding whether information comparability improves when firms from code law jurisdictions are listed in common law jurisdictions. Two related theories regarding cross-border listing in accounting literature are the bonding theory and the signaling theory. Both theories would predict higher information comparability when Chinese companies are listed in Hong Kong.

Using 117,125 pairs of data for the test period of 2010 to 2012, we find the mean and median comparability scores for H-shares are only marginally higher (and statistically insignificant) than those for A-shares. After controlling for firm-specific characteristics that may affect comparability, we find that, contrary to the predictions of the bonding theory and the signaling theory, comparability scores are significantly lower for Chinese companies listed in Hong Kong than their counterparts listed in China. The results are not sensitive to firm-level characteristics, correlations across firms and over time in our panel data, alternative comparability measures, or potential self-selection bias.

This study contributes to the IFRS comparability literature. To the best of our knowledge, we are the first to investigate IFRS information comparability for firms from code law jurisdictions listed in a common law jurisdiction. While the comparability literature suggests that firms from common law jurisdictions have higher information comparability than firms from code law jurisdictions (Barth et. 2012; Yip and Young, 2012), our findings indicate that comparability does not improve when firms from code law jurisdictions are listed on stock exchanges in common law jurisdictions. To the contrary, we find listing in Hong Kong by Chinese companies led to lower information comparability. Given the continued interest of firms from less developed, code law jurisdictions seeking to list on stock exchanges in common law jurisdictions, our findings have direct policy implications in that they suggest that securities regulators and stock exchanges need to improve their regulatory and enforcement actions on foreign issuers for the benefit of investors.

This study is based on the data of Chinese companies listed in the Hong Kong Stock Exchange. To examine the generalizability of the findings, future studies may investigate the relationship between accounting information comparability and the legal environment using data from other major stock exchanges.

The rest of the study is organized as follows. Section 2 reviews the literature and develops the model. Section 3 describes the sample selection and the data. Section 4 presents empirical tests and results. The last section summarizes and concludes the paper.

LITERATURE REVIEW AND MODEL DEVELOPMENT

The last two decades have witnessed a dramatic increase in cross-border listing. Foreign registrants account for an ever-increasing portion of the market capitalization in all major stock exchanges in the world. For example, in the Hong Kong Stock Exchange, the second largest in Asia and sixth largest in the world, nine of its top ten companies in market capitalization are from Mainland China. The increasing number of foreign registrants can benefit investors in the hosting stock exchanges by providing a more diverse set of investment opportunities (Woo 2011; Obi 2006). However, investors cannot take the full advantage of such opportunities nor make proper investing and lending decisions without comparable financial information. As stated by the Financial Accounting Standards Board (FASB), “Investing and lending decisions essentially involve evaluation of alternative opportunities, and they cannot be made rationally if comparable information is not available (FASB, 1980).”

Several studies have examined the issue of comparability of financial information across countries (Barth et al., 2012; Bartov et al., 2005; Bradshaw and Miller, 2008; Yip and Young 2012). These studies generally conclude that both financial reporting standards and institutional environments affect cross-country information comparability. These studies find that the improvement in comparability is more significant for companies from common law jurisdictions than for companies from code law jurisdictions (e.g., Barth et al., 2012). To the best of our knowledge, the comparability literature has not addressed the issue of whether companies from code law jurisdictions can improve information comparability by listing in common law jurisdictions. In light of the continued interest of companies from code law jurisdictions to list on stock exchanges in common law jurisdictions, an understanding of how listing in a different legal environment may affect the information comparability of foreign registrants’ financial information should be of direct interest to securities regulators, investors, and accounting standards setting bodies.

We extend the comparability literature by investigating the effect of listing on information comparability. Specifically, we examine if Chinese companies can improve their information comparability by listing in Hong Kong. We choose to focus on Chinese companies listed in Hong Kong (the H-shares) for two reasons. First, China is a code law jurisdiction whereas Hong Kong is a common law jurisdiction (Ball et al., 2000; Ball et al., 2003; Eccher and Healy, 2003; He et al., 2011; Leuz et al., 2003). Second, there are a large number of Chinese companies listed in Hong Kong, thus providing enough data for sound statistical analysis. Since both Chinese companies listed in Hong Kong (the H-shares) and their counterparts listed in China (the A-shares) follow the same accounting standards during the sample period (i.e., IFRS) and face virtually the same economic environment except where they are listed, any differences in comparability between these two groups of companies are likely attributable to the listing variable.

Comparability studies generally use either input-based measures or output-based measures in assessing accounting information comparability (Bradshaw and Miller, 2008; Bradshaw et al., 2009; De Franco et al., 2011). When input-based comparability measures such as accounting methods are used, researchers must decide which accounting choices to use, how to weigh them, and how to account for variations in their implementation. To avoid such challenges, this study adopts the output-based comparability metrics developed by De Franco, Kothari, and Verdi (2011) and being used subsequently by several comparability studies (Barth et al., 2012; Yip and Young, 2012).

Following De Franco, Kothari, and Verdi (2011), accounting is essentially a mapping of economic transactions to financial statements. That is,

$$\text{Financial Statements}_i = f_i(\text{Economic Transactions}_i) \quad (1)$$

Where $f_i()$ represents the accounting system of firm i . Equation 1 states that a firm’s financial statements are a function of both the underlying economic transactions and how these transactions are accounted for. We consider two firms’ accounting systems to be comparable if they produce similar financial statements for similar economic transactions. Two firms i and j with comparable accounting should have similar mappings $f_i()$, such that for a given set of economic transactions, firm i would

produce financial statements similar to those of firm j . Following De Franco, Kothari, and Verdi (2011), we use stock returns as a proxy for the net effect of economic transactions and use earnings as a proxy for financial statements. Based on eight semiannual financial data, we first estimate each firm's accounting function using the following equation:

$$Earnings_{i,t} = \alpha_i + \beta_i Return_{i,t} + \varepsilon_{i,t} \quad (2)$$

Under the framework of Equation 2, $\hat{\alpha}_i$ and $\hat{\beta}_i$ proxy for the accounting function for firm i . Similarly, we obtain the proxy for firm j 's accounting function, $\hat{\alpha}_j$ and $\hat{\beta}_j$, by estimating Equation 2 for firm j . The closeness of the functions between the two firms represents their comparability (De Franco, Kothari, & Verdi, 2011). To assess the closeness of the two firms' accounting functions, we first use $Return_{i,t}$ (a proxy for firm i 's economic transactions) and $\hat{\alpha}_i$ and $\hat{\beta}_i$ (a proxy for firm i 's accounting function) to predict firm i 's earnings using the following equation:

$$E(Earnings)_{ii,t} = \hat{\alpha}_i + \hat{\beta}_i Return_{i,t} \quad (3)$$

We then use the same economic events of firm i , but the accounting function of firm j ($\hat{\alpha}_j$ and $\hat{\beta}_j$) to predict firm i 's earnings using the following equation:

$$E(Earnings)_{ij,t} = \hat{\alpha}_j + \hat{\beta}_j Return_{i,t} \quad (4)$$

Given that Equations 3 and 4 are estimated using the same economic events (i.e., firm i 's returns), if firm i 's and firm j 's accounting functions are comparable, they should produce similar accounting numbers (i.e., $E(Earnings)$). Consistent with De Franco, Kothari, and Verdi (2011), Barth et al. (2012), and Yip and Young (2012), we use the average absolute difference between predicted earnings calculated from firm i 's and j 's accounting function as our comparability measure ($CompAcc_{ijt}$). Specifically, we compute $CompAcc_{ijt}$ using the following equation:

$$CompAcc_{ij,t} = -\frac{1}{8} \times \sum_{t-7}^t |E(Earnings)_{ij,t} - E(Earnings)_{ii,t}| \quad (5)$$

Following De Franco, Kothari, and Verdi (2011), we added a negative sign in equation (5) so that greater $CompAcc_{ijt}$ values indicate greater accounting comparability.

To examine whether Chinese companies can improve the comparability of their financial information by listing in Hong Kong, we first compute comparability scores, $CompAcc_{ijt}$, for Chinese companies listed in Hong Kong (the H-shares). We then calculate comparability scores for Chinese companies listed in China (the A-shares). The mean and median of all comparability scores for H-shares and A-shares are compared to see whether there are significant differences. As discussed above, since H-shares and A-shares are similar in virtually every aspect except where they are listed, any significant differences in comparability between these two groups are likely attributable to the listing factor.

While this study's settings of H- and A-shares eliminate the need to control for unobservable differences in country characteristics, the literature suggests that firm-level characteristics may also affect information comparability. Consequently, we use the following regression equation to assess the effect of listing on comparability after controlling for firm-level characteristics:

$$CompAcc_{ij,t} = \beta_0 + \beta_1 * Listing_{ij,t} + \beta_2 * Size_{ij,t} + \beta_3 * Leverage_{ij,t} + \beta_4 * MKTBV_{ij,t} + \beta_5 * CFO_{ij,t} + \beta_6 * LossProb_{ij,t} + \beta_7 * Sales_{ij,t} + \beta_8 * Growth_{ij,t} + \beta_9 * StdCFO_{ij,t} + \varepsilon_{ij,t} \quad (6)$$

$Listing_{ij,t}$ is a dummy variable that equals to one for Chinese companies listed in Hong Kong (the H-share) and zero otherwise. The other variables in the equation attempt to control for firm-level differences in firm size, leverage, market value to book value ratio, loss probability, sales, growth, and cash flows from operations. Our primary interest is the coefficient estimate for the listing variable, β_1 . A significantly positive β_1 value would indicate that the accounting information is more comparable for Chinese companies listed in Hong Kong than their counterparts listed in China.

Accounting literature on IFRS information comparability generally finds comparability is higher for companies from common law jurisdictions and is lower for companies from code law jurisdictions because of latter's lack of litigation mechanisms to enforce the rigorous application of financial reporting standards (Barth et al., 2012). The bonding theory suggests that companies from code law jurisdictions with low investor protection can alleviate investors' concern by bonding themselves to a strong investor protection system through listing in common law jurisdictions with more stringent enforcement and litigation actions (Stulz, 1999; Doidge et al., 2009). In addition, the signaling theory suggests that companies with high reporting quality would choose to list on foreign stock exchanges with more rigorous reporting requirements instead of on exchanges in their home country in order to signal their higher accounting quality to investors (Huijgen and Lubberink, 2005; Lang et al., 2003; Lang et al. 2006). Both the bonding theory and the signaling theory would predict that when companies from China, a code law jurisdiction with low investor protection, list in Hong Kong, a common law jurisdiction with high investor protection, information comparability of these Chinese companies should be higher than their counterparts listed in China, other things being equal. Thus, both theories predict a positive coefficient estimate for β_1 .

SAMPLE SELECTION AND THE DATA

Our initial sample is obtained from the China Securities Market and Accounting (CSMAR) database. The test period is from 2010 to 2012. Sample distributions by year are reported in Table 1.

TABLE 1
SAMPLE DISTRIBUTION BY YEAR

Year	H-HK	A-HK	Total
2010	1370	29421	30791
2011	1660	39207	40867
2012	1803	43664	45467
Total	4833	112292	117125

H-HK is H-share and HK-share pair group; A-HK is A-share and HK-share pair group.

Semiannual data from 2007 to 2012 were collected to estimate $CompAcc_{ij,t}$ measures for each H-HK and A-HK pair. Our sample period starts in 2007 because Hong Kong adopted IFRS in 2005 while China adopted IFRS in 2007. Thus, 2007 was the first year that both A-share and H-share companies prepared IFRS-based financial statements. Using 2007 as the starting year eliminates the difference in accounting standards as a confounding factor on comparability. We exclude financial and insurance firms from the sample because they have special operating characteristics and are subject to special accounting rules and additional regulations. We also exclude firms that issue shares in both China and Hong Kong because the two sets of financial statements prepared by these firms are substantially the same. This procedure yields 117,125 pairs of $CompAcc_{ij,t}$ scores. To mitigate the influence of outliers, all regression variables in our final sample were winsorized at 1% and 99% levels. Sample descriptive statistics are presented in Table 2.

TABLE 2
DESCRIPTIVE STATISTICS

Variables	H-HK Pairs (n=4833)		A-HK Pairs (n=112292)	
	Mean	Std. Dev.	Mean	Std. Dev.
<i>Size</i>	22.855	1.396	21.597	1.200
<i>Leverage</i>	0.238	0.132	0.357	0.194
<i>MKTBV</i>	2.039	2.151	3.035	5.104
<i>CFO</i>	0.041	0.075	0.028	0.089
<i>LossProb</i>	0.186	0.191	0.227	0.207
<i>StdSales</i>	0.224	0.150	0.240	0.159
<i>StdGrowth</i>	145.900	674.689	72.928	264.103
<i>StdCFO</i>	0.065	0.049	0.072	0.056

This table presents descriptive statistics of control variables used in all regressions.

Variable Definitions:

Size = firm size, which equals to the natural logarithm of total assets;

Leverage = leverage ratio, which equals to total liability divided by total assets;

MKTBV = market value to book value ratio, which equals to market value of equity divided by book value of equity;

CFO = cash flow ratio, cash flow ratio, which equals to cash flows from operations scaled by total assets;

LossProb = loss probability ratio, which is the proportion of quarters the firm reports a loss before extraordinary items during the sample period;

StdSales = standard deviation of sales, which is calculated over the preceding eight semiannual periods;

StdGrowth = standard deviation of sales growth, which is calculated over the preceding eight semiannual periods;

StdCFO = standard deviation of cash flows from operations, which is calculated over the preceding eight semiannual periods.

Though we did not report them, the parameter estimates of accounting functions from estimating Equation 2 are substantially similar to those in De Franco, Kothari, and Verdi (2011), validating both our sample selection and comparability score estimation procedures.

EMPIRICAL TESTS AND RESULTS

Main Test Results

The primary objective of this study is to examine whether the comparability of Chinese companies listed in Hong Kong (the H-shares) differs from that of their counterparts listed in China (the A-shares). To test this, we compare the mean and median comparability scores of H-shares and A-shares. Since H-shares and A-shares are both Chinese companies and face virtually the same operational environments except where they are listed, any significant difference in comparability between H-shares and A-shares is likely attributable to listing. The results of the comparisons are reported in Table 3.

TABLE 3
COMPARABILITY SCORE COMPARISONS BETWEEN H-HK AND A-HK PAIRS

	Mean	Median	Std. Dev.
<i>CompAcc</i> (H_HK) N=4,833	-0.098	-0.045	0.164
<i>CompAcc</i> (A_HK) N=112,292	<u>-0.102</u>	<u>-0.048</u>	0.171
<i>CompAcc</i> (H_HK) – <i>CompAcc</i> (A_HK)	0.004	0.003***	0.007***

*, **, *** Denotes statistical significance at the 10%, 5%, and 1% levels, respectively.

The mean comparability score of Chinese companies listed in Hong Kong is -0.098, which is only marginally higher than that of their counterparts listed in China (-0.102). The difference is statistically insignificant. The results in Table 3 suggest that there is no significant difference in comparability between Chinese companies listed in Hong Kong and their counterparts listed in China. This evidence does not support either the signaling theory or the bonding theory, both of which predict a significantly higher comparability when Chinese companies are listed in Hong Kong.

While our settings of comparing H-shares to A-shares eliminate the need to control for unobservable differences in country-level characteristics, firm-level characteristics may still affect the cross-country comparability. To ensure that the results reported in Table 3 are not driven by the differences in firm-level characteristics, we estimate Equation 6 developed in Section 2 to assess the effect of listing on comparability after controlling for firm-specific characteristics. The regression results are reported in Table 4.

TABLE 4
REGRESSION RESULTS – OLS

<u>Intercept</u>	<u>Listing</u>	<u>Size</u>	<u>Leverage</u>	<u>MKTBV</u>	<u>CFO</u>	<u>LossProb</u>	<u>StdSales</u>	<u>StdGrowth</u>	<u>StdCFO</u>
-0.205*** (-6.56)	-0.037*** (-6.37)	0.011*** (7.03)	-0.187*** (-11.26)	0.004 (13.52)	0.091*** (6.66)	-0.205*** (-22.30)	0.012 (1.63)	0.001*** (12.02)	-0.090*** (-2.92)

Number of observations: 117,125
Adjusted R²: 0.187

*, **, *** Denotes statistical significance at the 10%, 5%, and 1% levels, respectively, two-tailed.
Variables definitions:
Listing_{ijt} = Listing is a dummy variable which equals to one if the Chinese company is listed in Hong Kong, and zero otherwise;
All control variables are defined in Table 2.

The coefficient estimate for the listing variable, β_1 , is -0.037 and is significant at 0.01 level. The result in Table 4 suggests that when Chinese companies are listed in Hong Kong, their comparability scores are actually significantly lower than their counterparts listed in China after controlling for firm-level characteristics. The findings do not support the signaling theory or the bonding theory. Instead, the evidence is more consistent with some prior studies, which suggest a reluctance of enforcement actions against foreign registrants. Since investing and lending decisions “cannot be made rationally if comparable information is not available (FASB, 1980)”, our findings have direct policy implications in

that they suggest that securities regulators and stock exchanges need to improve their regulations and enforcement on foreign issuers for the benefit of investors.

Test Results Using Two Alternative Comparability Measures

In obtaining the test results reported in Section 4.1, we have employed research designs to eliminate the need to control for unobservable country specific characteristics and added several variables to our regression to control for firm-specific characteristics that may affect comparability. This subsection reports the results using two alternative comparability measures to ensure that the results in Section 4.1 are not sensitive to the specific comparability measure used. Specifically, following De Franco, Kothari, and Verdi (2011), we compute the mean comparability score, $Mean_CompAcc_{i,t}$, for each H- and A-share by averaging its comparability scores with Hong Kong companies in the same two-digit industry group, and then use this mean comparability score as our first alternative comparability measure. Our second alternative comparability measure uses the sum of the four largest comparability scores in absolute value, $Max4_CompAcc_{i,t}$, within the two-digit industry group for each H- and A-share. The regression results of Equations 6 using the two alternative comparability measures are reported in Table 5. The results are substantially similar to those reported in Table 4 when $Mean_CompAcc_{i,t}$ is used and are stronger than those reported in Table 4 when $Max4_CompAcc_{i,t}$ is used, suggesting that our results are not sensitive to the specific comparability measure used in Section 4.1.

TABLE 5
REGRESSION RESULTS – ALTERNATIVE COMPARABILITY MEASURES

Variables	<i>Mean_CompAcc</i>	<i>Max4_CompAcc</i>
Intercept	-0.133*** (-3.40)	-0.330*** (-2.71)
<i>Listing</i>	-0.034*** (-5.13)	-0.173*** (-7.81)
<i>Size</i>	0.005** (2.22)	0.016** (2.33)
<i>Leverage</i>	-0.036** (-2.28)	-0.126** (-2.41)
<i>MKTBV</i>	0.003*** (3.90)	0.009*** (4.43)
<i>CFO</i>	0.062** (2.36)	-0.220*** (2.36)
<i>LossProb</i>	-0.084*** (-9.86)	-0.229*** (-8.14)
<i>StdSales</i>	0.008 (0.78)	-0.026 (0.75)
<i>StdGrowth</i>	0.001** (2.42)	0.001** (2.35)
<i>StdCFO</i>	-0.106** (-1.96)	-0.326* (-1.75)
Adjusted R ²	0.214	0.193

*, **, *** Denotes statistical significance at the 10%, 5%, and 1% levels, respectively, two-tailed.

Regression results are obtained using OLS regression.

Variables definitions:

$Listing_{i,t}$ = stock listing dummy variable which equals to one if the Chinese company is listed in Hong Kong, and zero otherwise;

All control variables are defined in Table 2.

Test Results Using Petersen's Two-way Clustered Analysis

The results reported in the Table 4 are from ordinary least squares (OLS) regressions using panel data pooled across firms and over time. Standard errors from OLS will be consistent as long as the regression residuals are uncorrelated across firms and over time. However such uncorrelatedness is unlikely to hold in our research context because of both market-wide shocks that induce correlation between firms and persistent firm-specific shocks that induce correlation over time (Thompson, 2011). To ensure that our results are robust to simultaneous correlation along the two dimensions, we adjust standard errors for correlation across firms and over time by clustering two-way (firm and time) using Petersen's two-way clustered method. We compute covariance estimator by adding the estimator that clusters by firms to the estimator that clusters by time and subtracting the usual heteroskedasticity-robust OLS covariance matrix. Results from the two-way clustered analysis are reported in Table 6.

TABLE 6
REGRESSION RESULTS – TWO-WAY CLUSTERED METHOD

<u>Intercept</u>	<u>Listing</u>	<u>Size</u>	<u>Leverage</u>	<u>MKTBV</u>	<u>CFO</u>	<u>LossProb</u>	<u>StdSales</u>	<u>StdGrowth</u>	<u>StdCFO</u>
-0.205*** (-6.81)	-0.037*** (-5.50)	0.011*** (6.15)	-0.187*** (-5.76)	0.004 (7.49)	0.091*** (3.77)	-0.205*** (-16.96)	0.012 (0.78)	0.001*** (4.86)	-0.090*** (-1.28)
Number of observations: 117,125									
Adjusted R ² : 0.187									
* **, *** Denotes statistical significance at the 10%, 5%, and 1% levels, respectively, two-tailed.									
Variables definitions:									
<i>Listing_{ijt}</i> = Listing is a dummy variable which equals to one if the Chinese company is listed in Hong Kong, and zero otherwise;									
All control variables are defined in Table 2.									

The results in Table 6 are substantially the same as those reported in Table 4, suggesting that our results are not sensitive to correlations across firms and over time in our panel data. Although not reported, our conclusions are unaltered after controlling for potential self-selection bias using a two-stage approach. In summary, this study documents significant evidence suggesting that listing in Hong Kong by Chinese firms actually led to lower comparability of reported financial information. Given the large number of foreign registrants in all major stock exchanges, these findings should be of concern to securities regulators and investors. The findings suggest that securities regulators and stock exchanges need to strengthen their reporting regulations and enforcement actions against foreign issuers for the benefit of investors. Sensitivity tests indicate that the results are unlikely driven by firm-level characteristics, the specific comparability measure used, correlations across firms and over time in panel data, or the potential self-selection bias.

CONCLUSIONS

The dramatic increase of foreign registrants in all major stock exchanges has provided investors with more diverse investment opportunities. However, investors won't be able to take the advantage of such diverse investment opportunities without comparable financial information. This study examines if firms from developing economies with a code law legal origin and low investor protection can improve information comparability by listing in a common law jurisdiction with high investor protection. Based on the financial data of Chinese companies, we found that listing in Hong Kong by Chinese firms actually led to lower comparability than their counterparts listed in China. Given the continued interest of firms from developing countries seeking to list in major stock exchanges, our findings have direct policy implications in that they suggest that securities regulators and stock exchanges need to improve their regulations and enforcement on foreign issuers for the benefit of investors.

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