



RAF
12,3

268

Received 10 November 2011
Revised 18 June 2012
10 October 2012
28 October 2012
Accepted 29 October 2012

Cost of equity capital of foreign firms

Did bonding benefits diminish after the SEC's waiver of IFRS to US GAAP reconciliation?

Fei Han

Robert Morris University, Pittsburgh, Pennsylvania, USA, and

Haihong He

California State University, Los Angeles, Los Angeles, California, USA

Abstract

Purpose – The purpose of this paper is to examine the cost of equity capital for foreign firms listed in the US stock exchanges during 2004-2009, a period that the Securities and Exchange Commission (SEC) shifted from requiring foreign issuers to comply with the US GAAP reconciliations to permitting the choice of IFRS in financial reporting.

Design/methodology/approach – The cost of equity of foreign firms in the IFRS reporting period was compared to that in the US GAAP reconciliation period. Also, the cost of equity of foreign firms was compared to that of matched US firms during the two periods.

Findings – The results show that the cost of equity in foreign firms is higher during the IFRS reporting period (2007-2009) than the US GAAP reconciliation period (2004-2006); foreign firms exhibit a constantly higher cost of equity than that of matched US firms in both periods; and the size of cost of equity difference remains the same with respect to the regulatory change. Further, it is shown that the change in foreign firms' cost of equity is affected by their home country's IFRS use.

Originality/value – Bonding theory suggests a reduced cost of capital for foreign firms cross-listed in the USA because US listings require more substantial disclosure. The paper finds evidence that the SEC's waiver of US GAAP reporting does appear to reduce the bonding benefits for cross-listed foreign firms, particularly those from IFRS adoption countries.

Keywords International standards, Financial reporting, United States of America, Equity capital, International Financial Reporting Standards, Cost of equity capital, Bonding hypothesis, US GAAP reconciliation

Paper type Research paper



1. Introduction

In 2007, the Securities and Exchange Commission (SEC) waived the US GAAP reconciliation requirement for foreign issuers registered in the USA that prepare financial statements in full compliance with International Financial Reporting Standards (IFRS) for fiscal years ending after December 15, 2007 (SEC, 2007). This study investigates whether the cost of equity capital of foreign issuers in the USA changes after the SEC allows them an option of filing IFRS financial statements.

The bonding hypothesis suggests that foreign firms choose to list in the USA because, by bonding themselves to the more stringent US regulatory environment, they can thereby receive capital at lower cost (Coffee, 1999, 2002; Stulz, 1999). However, the SEC's new rule loosens the reporting and disclosure requirements imposed on the foreign firms in the USA to the extent that US GAAP and IFRS differ.

Early research comparing US GAAP and international accounting standards (IAS), the predecessor of IFRS, generally find that earnings statements prepared under US GAAP are of higher quality (Harris and Muller, 1999). But more recent studies show that firms applying IFRS and firms applying US GAAP have comparable accounting qualities (Barth *et al.*, 2010; Hansen *et al.*, 2011). The change in IFRS quality relative to US GAAP may be attributed, in part, to the joint efforts of the USA and IAS setters to converge the two standards. The SEC and the Financial Accounting Standards Board (FASB) have been working closely with the International Accounting Standards Board (IASB) to converge US GAAP with IFRS, and the ongoing collaboration would eventually lead to a single set of high-quality global standards (FASB, 2002, 2006). We add to this discussion by investigating the cost of equity effect when foreign issuers could switch from reconciled US GAAP reporting to direct IFRS reporting.

We follow Hail and Leuz (2006, 2009) to estimate the average *ex ante* cost of equity that is implied from analysts' earnings forecasts, dividend forecasts, long-term growth and firms' stock prices. Using 1,321 observations of foreign firms listed on major US stock exchanges from 2004 to 2009, we first show that the cost of equity to foreign firms in the IFRS-permitted period (2007-2009) is higher than that in the US GAAP reconciliation period (2004-2006). We next compare the cost of equity capital for foreign firms to that of size and industry-matched US firms in these two periods to rule out the potential impact of concurrent financial turmoil and economic downturn. It appears that US firms do not experience an increase in the cost of equity capital in the latter period, while foreign firms exhibit a constantly higher cost of equity capital than US firms, and this pattern does not vary with the different reporting requirements.

However, when foreign firms are partitioned based on their home countries' IFRS use, the higher cost of equity capital after the SEC's new regulation only remains in foreign firms from IFRS adoption countries. Moreover, the difference in the cost of equity capital between the foreign firms from IFRS adoption countries and their matched US counterparts increases from the early to the latter period. Together, our results suggest that the elimination of US GAAP reconciliation affects the cost of equity capital for foreign firms from IFRS adoption countries.

Our study contributes to the literature on the cost of equity capital and cross-listings. Bonding theory suggests a reduced cost of capital for foreign firms cross-listed in the USA because US listings require more substantial disclosure under the SEC rules, which in turn provides greater protection to the investors (Coffee, 1999; Coffee, 2002; Stulz, 1999). Consistent with this notion, empirical studies find a positive effect on firms' valuation due to the cross-listings (Bailey *et al.*, 2006; Hail and Leuz, 2009). When US regulations allow foreign firms to replace the existing US GAAP disclosure with an alternative accounting reporting, i.e. IFRS, the previously documented "bonding" effect may diminish. There is little evidence on the alleged costs and benefits of disclosure regulation (Healy and Palepu, 2001), let alone disclosure deregulation. We show the economic consequences of reduced disclosure requirements for listed foreign firms. Thus, our research also adds to the literature on disclosure regulation.

Our study indirectly contributes to the prior accounting literature on the use of IFRS. Both IFRS and US GAAP are viewed as high-quality accounting rules, and the convergence benefit is still an open question. Our investigation of the partial IFRS adoption in the USA provides some information to gauge the economic implication of full IFRS adoption in the US capital markets, and hence contributes to the current policy debates relating to possible adoption of IFRS by US firms in the future.

Our research also adds to the recent studies on IFRS adoption and US GAAP reconciliation (Jiang *et al.*, 2010; Hansen *et al.*, 2011; Kim *et al.*, 2011). In general, there is no evidence to show that the removal of US GAAP reconciliation gave rise to any significant capital market effect. Our findings complement the above evidence through a longer sample period and an extended sample including all foreign firms that could use IFRS.

The remainder of this paper is organized as follows. Section 2 presents the background to the SEC's rule change. Section 3 reviews the literature and lays out relevant research questions. Section 4 describes the research design and sample selection, followed by Section 5 discussing statistical results. The last section concludes.

2. Background

The SEC requires non-US firms in the US capital markets to comply with a set of SEC regulations. Before the SEC's 2007 ruling on allowing foreign issuers to use IFRS, non-US firms were required to reconcile their reported earnings and shareholders' equity under their domestically accepted accounting principles to US GAAP. The SEC's main motivation for the US GAAP reconciliation was to protect US investors who may not be familiar with non-US accounting practices (Siconolfi and Salwen, 1992). The accounting regulators believe that the standardization (or harmonization) of accounting in capital markets increases uniformity and enhances comparability between US and foreign firms.

Since 1990s, the SEC has been pressured to waive the reconciliation requirement for foreign listings on US exchanges (Salwen, 1991) and permit the use of the IAS, the predecessor of the IFRS. There is considerable debate on the comparability of IAS/IFRS and US GAAP. Although both are viewed as high-quality accounting standards, material differences exist, particularly between IAS and US GAAP. For example, IAS allows more alternative accounting practices than US GAAP and IAS and US GAAP have many differences in business combination.

Many studies examine the comparability of IAS/IFRS and US GAAP by assessing their economic implications in capital markets. Harris and Muller (1999) examine reconciliations from IAS to US GAAP in cross-listed foreign firms' Form 20-F filings during the years 1992-1996. They show that reconciliations from IAS to US GAAP are value-relevant, suggesting that US investors prefer financial results prepared under US GAAP. Leuz (2003) uses a sample of German firms in 1999 and 2000 to examine information asymmetry associated with IAS and US GAAP, and finds that differences in the bid-ask spread and share turnover between IAS and US GAAP firms are statistically insignificant and economically small. Leuz's (2003) findings suggest that US GAAP does not produce higher quality information than IAS. A recent study by Barth *et al.* (2010) finds that non-US firms applying IFRS and US firms applying US GAAP have comparable accounting amounts in terms of their capability to explain and predict stock returns. Thus, capital market research has not reached a consensus on whether US GAAP and IFRS are comparable. However, these studies were conducted

in different periods from early 1990s to recent years. The inconsistent results could be partly explained by the continuous revision and development in IAS.

The other type of research directly evaluates the accounting amounts reported under either IFRS or US GAAP. Henry *et al.* (2009) compare income and shareholders' equity amounts prepared under US GAAP to those of IFRS in 75 cross-listed European Union (EU) firms in the USA from 2004 to 2006. They show that numerical differences between US GAAP and IFRS still exist, although the gap has declined. Van der Meulen *et al.* (2007) find that US GAAP and IFRS earnings are similar in many attributes except predictability. These results are generally consistent with the convergence efforts between the IASB and the US FASB (2002, 2006).

In November 2007, the SEC decided to allow non-US firms to file financial statements prepared in full compliance with IFRS without a US GAAP reconciliation, and stated that:

IFRS as issued by the IASB and US GAAP are both sets of high-quality accounting standards that are similar to one another in many respects, and the convergence efforts to date have progressed in eliminating many differences.

The new rule, Securities Act Release No. 33-8879, became effective on March 4, 2008, for fiscal years ending after November 15, 2007 (SEC, 2007).

Prior studies that examine the capital market consequences of IFRS adoption primarily focus on EU countries (Daske *et al.*, 2008; Li, 2010), and such research generally shows that the cost of capital decreases after mandatory IFRS adoption. The SEC's rule change provides a unique setting to directly analyze the economic consequences of permitting the use of IFRS in the world's largest capital markets. We are able not only to examine whether IFRS affects the cost of equity capital in foreign firms listed in the USA and thus gauge market participants' acceptance of this new set of accounting standards, but also to establish whether this reduced disclosure requirement affects the cost of equity capital to foreign firms relative to US firms.

3. Research questions

3.1 Foreign firms in the USA and bonding effect

According to bonding hypothesis, foreign firms listed in the USA commit themselves to:

- SEC's stricter law enforcement;
- the USA's higher legal pressure and costs; and
- improved disclosure and reconciliation to US GAAP from local standards (Coffee, 2002).

Prior empirical results on the cost of equity capital and foreign firms in the USA are generally consistent with the bonding hypotheses (Bailey *et al.*, 2006). As discussed in the earlier section, existing evidence (Harris and Muller, 1999; Leuz, 2003; Barth *et al.*, 2010) is inconclusive as to whether IFRS and US GAAP produce equivalently high-quality accounting results despite the convergence efforts made by the IASB and FASB. Thus, the SEC's waiver of Form 20-F reconciliation could relax disclosure requirements for foreign firms and hence may impact their cost of equity capital.

Recent empirical studies so far have not found evidence that IFRS use in the USA induces negative impacts. Jiang *et al.* (2010) find that the reconciliations in the years 2006 and 2007, immediately before the elimination of the US GAAP reconciliation requirement,

are not sufficiently informative to affect capital market performance and earnings attributes. They also illustrate that the elimination, IFRS filing could have the beneficial effect of significantly accelerating financial reporting. Although Hansen *et al.* (2011) propose as a downside risk that managers could exploit the flexibility of IFRS to manipulate earnings, their results do not show that IFRS filers exhibit decreased earnings persistence and increased earnings smoothness. Kim *et al.* (2011) is more relevant to the issues that interest us. They find no evidence that the regulatory change affects the cost of equity capital in foreign firms reporting under IFRS, implying that there is no informational loss or greater information asymmetry as a result of the elimination.

Based on prior discussions and literature review, we examine the following research question:

RQ1a. Did foreign firms' cost of equity capital in the IFRS reporting period differ from that in the US GAAP reconciliation period?

If IFRS reporting and disclosure provide quality information equivalent to US GAAP, then we expect the answer to *RQ1a* to be that the cost of equity capital would not change when foreign firms switch from US GAAP to IFRS; if IFRS results in better (poorer) representation of foreign issuers' financial situation, then we would expect the answer to *RQ1a* to be that the cost of equity capital would be lower (higher) after the US GAAP reconciliation requirement is waived.

3.2 Foreign firms and US firms

The SEC's former US GAAP reconciliation requirement was based on the perception that information users prefer one single set of accounting standards applied by all firms, foreign or domestic. However, empirical research comparing US and cross-listed foreign firms has found that the two groups have different reporting behaviors and different reporting qualities.

Frost and Kinney (1996) show that, even with the SEC's reconciliation requirement, foreign issuers filed fewer and less timely accounting disclosures than US issuers. The authors also suggest that some foreign firms did not comply with certain disclosure requirements when they perceived that the disclosure cost exceeded the non-compliance cost. Frost and Kinney's results are generally consistent with the anecdotal evidence that SEC's previous reconciliation requirements were considered cumbersome by foreign registrants and may not have achieved the intended goal of enhancing comparability among different issuers. Lang *et al.* (2006) find that cross-listed foreign firms have greater earnings management than US firms. Bradshaw and Miller (2008) also find that the properties of accounting figures in foreign firms do not converge fully with those of US firms. Thus, disclosure difference or comparability is not determined so much by what is written in the accounting standards, but more by the reporting incentives among other factors shaping the accounting practice.

After the SEC's new rule, US firms are required to comply with US GAAP whereas foreign firms are allowed the choice of using either IFRS or US GAAP. Its consequence on increasing or decreasing the comparability between foreign and US firms is still unclear. When foreign firms are given the choice of using IFRS instead of US GAAP, their full IFRS reporting and disclosure are more comprehensive and informative than the mere reconciliations previously required, and could become more consistent and comparable with those of US firms. Additionally, foreign firms, particularly those from

countries that have already mandated IFRS, are more willing to comply with this new rule, and thus the non-compliance incidents reported in Frost and Kinney (1996) could be reduced. Thus, comparability is not necessarily reduced by the existence of two accounting standards employed by different firms.

Based on prior discussion and literature review, we compare the cost of equity capital between foreign and US firms, and our research question is stated as follows:

RQ1b. Did foreign firms' cost of equity capital relative to that of US firms increase in the IFRS reporting period?

If the SEC's new rule indicates reduced disclosure requirements for foreign issuers relative to the requirements for US issuers, then for *RQ1b*, we expect that the gap between the cost of equity for foreign and US firms would become greater after the new rule. If the disclosed information is not affected by the SEC's new rule, then for *RQ1b*, we expect that the difference between the cost of equity for foreign and US issuers would remain the same after the new rule.

It is worth noting that during our sample period 2004-2009, convergence between IFRS and US GAAP has increased (FASB, 2008)[1]. Thus, the improved equivalence between IFRS and US GAAP might have some impact, particularly on the second period that allows IFRS use. As IFRS and US GAAP become more converged over time, then the cost of equity capital difference due to the SEC's new rule of eliminating US GAAP reconciliation (if there is any) would diminish. Such impact is present in all our research questions.

3.3 Foreign firms' domicile

Hail and Leuz (2009) suggest that different disclosure requirements for different types of listed firms affect cost of equity capital. If the SEC's new rule indicates a reduced (increased) disclosure requirement for foreign issuers relative to the requirements for US issuers, then the cost of equity capital of foreign issuers will increase (decrease). Furthermore, such changed disclosure requirements have asymmetric implications for the two types of foreign firms, those that are mandated to use IFRS in their home countries and those that use local GAAP. Thus, we extend *RQ1a* and *RQ1b* to examine whether the status of IFRS adoption in foreign firms' home countries changes the cost of equity capital, and our research questions are stated as follows:

RQ2a. Did IFRS adoption status in foreign firms' home countries affect foreign firms' cost of equity capital from the US GAAP reconciliation period to the IFRS reporting period?

RQ2b. Did IFRS adoption in foreign firms' home countries affect foreign firms' cost of equity capital relative to that of matched US firms from the US GAAP reconciliation period to the IFRS reporting period?

If foreign firms' home countries IFRS adoption biases US investors, then for *RQ2*, we expect that a change in the cost of equity for foreign firms is associated with the home country variable.

4. Research design and sample selection

Following prior research (Hail and Leuz, 2006, 2009; Daske *et al.*, 2008; Li, 2010), we measure cost of equity capital using the average estimate from the implied cost of equity capital

models proposed by Claus and Thomas (2001), Gebhardt *et al.* (2001), Gode and Mohanram (2003) and Easton (2004). Analyses are conducted variously on an indicator variable, $Period_{it}$, for the time period (IFRS period vs US GAAP reconciliation period), an indicator variable, $Issuer_{it}$, for the type of firms (US firms vs foreign firms), and an indicator variable, $Adopt_{it}$, indicating whether a foreign firm domiciles in a country that mandated IFRS during our sample period. Size, leverage and return variability are the common risk factors. Industrial median cost of equity controls for average year and industry effect.

To investigate whether the cost of equity in foreign firms changes in reaction to the SEC's new rule as in *RQ1a*, the main regression model is stated as follows:

$$COC_{it} = \alpha_0 + \alpha_1 * Period_{it} + \alpha_2 * Size_{it} + \alpha_3 * LEV_{it} + \alpha_4 * RV_{it} + \alpha_5 * INDCOC_{it} + \epsilon_{it} \quad (1a)$$

where:

COC_{it} = the average estimates from the implied cost of equity capital models proposed by Claus and Thomas (2001), Gebhardt *et al.* (2001), Gode and Mohanram (2003) and Easton (2004), net of risk-free rate using the yield on the ten-year US treasury bonds.

$Period_{it}$ = dummy variable equal to 1 if an observation is in the IFRS reporting period, and 0 in the US GAAP reconciliation period.

$Size_{it}$ = natural logarithm of total assets at year-end.

LEV_{it} = financial leverage, computed as total liabilities divided by total assets at year end.

RV_{it} = return variability, computed as annual standard deviation of monthly stock returns.

$INDCOC_{it}$ = the median industry cost of equity by year for each Fama and French (1997) 48 industries, net of risk-free rate using the yield on the ten-year US treasury bonds.

ϵ_{it} = error term.

In *RQ1b*, we further compare the difference in the cost of equity between foreign issuers and US issuers in the IFRS reporting period to that in the US reconciliation period. We use the following regression model on a matched sample test:

$$COC_{it} = \alpha_0 + \alpha_1 * Period_{it} + \alpha_2 * Issuer_{it} + \alpha_3 * Period_{it} * Issuer_{it} + \alpha_4 * Size_{it} + \alpha_5 * LEV_{it} + \alpha_6 * RV_{it} + \alpha_7 * INDCOC_{it} + \epsilon_{it} \quad (1b)$$

In equation (1b), $Issuer_{it}$ is a dummy variable equal to 1 if an observation is a foreign issuer, and 0 if a matched US issuer. The other variables in equation (1b) are defined in equation (1a).

To investigate *RQ2*, we partition foreign firms based on whether they domicile in countries that adopted IFRS during the sample period. Foreign firms already required to use IFRS would be more affected by the SEC's waiver of reconciliation. We introduce a dummy variable $Adopt_{it}$ equal to 1 if an observation is from a country that has mandated IFRS before December 15, 2007, and 0 otherwise. The model to examine *RQ2a* is as follows:

$$COC_{it} = \alpha_0 + \alpha_1*Period_{it} + \alpha_2*Adopt_{it} + \alpha_3*Period_{it}*Adopt_{it} + \alpha_4*Size_{it} + \alpha_5*LEV_{it} + \alpha_6*RV_{it} + \alpha_7*INDCOC_{it} + \varepsilon_{it} \quad (2a)$$

Cost of equity capital

In *RQ2b*, we also examine whether the cost of capital of foreign firms benchmarked with US firms in the two different regulatory periods varies with whether they are from IFRS mandating countries. For two sub-samples partitioned based on *Adopt_{it}* we use the same model equation (1b) as follows:

$$COC_{it} = \alpha_0 + \alpha_1*Period_{it} + \alpha_2*Issuer_{it} + \alpha_3*Period_{it}*Issuer_{it} + \alpha_4*Size_{it} + \alpha_5*LEV_{it} + \alpha_6*RV_{it} + \alpha_7*INDCOC_{it} + \varepsilon_{it} \quad (2b)$$

275

Our sample begins with all firms listed on Amex, Nasdaq, or NYSE from years 2004 to 2009. Foreign firms listed on major exchanges are required to comply with accounting and disclosure rules in the US cross-listings in the OTC market are not required to file a 20-F filing and not affected by the new SEC rule on the IFRS adoption, and thus are not included in our sample. We delete Canadian firms because they are exempted from US reporting requirements under the multi-jurisdictional disclosure system (King and Segal, 2009).

We next require each observation with data in compustat and IBES to compute variables used in our statistical analyses. We further delete observations with 1 percent highest or lowest variable values. Our final sample consists of 1,321 foreign firm-year observations. Table I shows the number of observations, IFRS adoption status, and IFRS adoption year of each country. Table II reports descriptive statistics of variables

Domicile	<i>n</i>	IFRS adoption	IFRS adoption year
EU countries	419	YES	2005
Argentina	19	YES	2012
Australia	8	YES	2005
Brazil	101	YES	2010
Chile	42	YES	2009
China	232	NO	
Colombia	6	NO	
Hong Kong	33	YES	2005
India	42	NO	
Indonesia	8	NO	
Israel	125	YES	2008
Japan	45	NO	
Kazakhstan	1	YES	2006
Korea	27	NO	
Mexico	76	NO	
New Zealand	1	YES	2007
Panama	9	YES	2011
Peru	11	YES	2011
Philippines	7	NO	
Russia	23	NO	
Singapore	9	NO	
South Africa	35	YES	2004
Taiwan	37	NO	
Turkey	5	NO	
Total	1,321		

Table I.
Number of observations and IFRS adoption status by domicile

	Mean	SD	Median	<i>n</i>	<i>t</i> -test
<i>Foreign firms in the reconciliation period (Period_{it} = 0)</i>					
<i>COC_{it}</i>	0.0596	0.0286	0.0548	579	15.23***
<i>Size_{it}</i>	8.3120	2.0426	8.6272	579	-2.93***
<i>LEV_{it}</i>	0.5057	0.2044	0.5080	579	-3.11***
<i>RV_{it}</i>	0.0968	0.0483	0.0868	579	14.60***
<i>INDCOC_{it}</i>	0.0484	0.0099	0.0476	579	31.28***
<i>Foreign firms in the IFRS period (Period_{it} = 1)</i>					
<i>COC_{it}</i>	0.0898	0.0433	0.0793	742	
<i>Size_{it}</i>	7.9667	2.2227	8.0352	742	
<i>LEV_{it}</i>	0.4692	0.2202	0.4770	742	
<i>RV_{it}</i>	0.1487	0.0798	0.1336	742	
<i>INDCOC_{it}</i>	0.0705	0.0157	0.0688	742	
<i>Matched US firms in the reconciliation period (Period_{it} = 0)</i>					
<i>COC_{it}</i>	0.0479	0.0220	0.0434	576	16.93***
<i>Size_{it}</i>	8.0848	1.9907	8.1066	576	-1.65*
<i>LEV_{it}</i>	0.5096	0.2157	0.5027	576	0.62
<i>RV_{it}</i>	0.0874	0.0474	0.0756	576	13.16***
<i>INDCOC_{it}</i>	0.0483	0.0097	0.0476	576	32.13***
<i>Matched US firms in the IFRS period (Period_{it} = 1)</i>					
<i>COC_{it}</i>	0.0752	0.0354	0.0664	706	
<i>Size_{it}</i>	7.8965	2.0935	8.0372	706	
<i>LEV_{it}</i>	0.5173	0.2286	0.4989	706	
<i>RV_{it}</i>	0.1331	0.0760	0.1142	706	
<i>INDCOC_{it}</i>	0.0702	0.0146	0.0688	706	

Notes: Statistically significant at: *10, **5 and ***1 percent levels for a two-tailed test; variable definitions: *COC_{it}* – the average estimates from the implied cost of equity capital models proposed by Claus and Thomas (2001), Gebhardt *et al.* (2001), Gode and Mohanram (2003) and Easton (2004), net of risk-free rate using the yield on the ten-year US treasury bonds; *Period_{it}* – dummy variable equal to 1 if an observation is in the IFRS reporting period, and 0 in the US GAAP reconciliation period; *Size_{it}* – natural logarithm of total assets at year-end; *LEV_{it}* – financial leverage, computed as total liabilities divided by total assets at year end; *RV_{it}* – return variability, computed as annual standard deviation of monthly stock returns; *INDCOC_{it}* – the median industry cost of equity by year for each Fama and French (1997) 48 industries, net of risk-free rate using the yield on the ten-year US treasury bonds

Table II.
Descriptive statistics

of 1,321 foreign firm-year observations and 1,282 matched US firm-year observations during the two sub-periods. We are able to find only 1,282 matched US observations based on year, size and industry. *COC_{it}*, *RV_{it}*, and *INDCOC_{it}* are statistically lower for foreign firms in the period when they are required to reconcile their accounting numbers to US GAAP than in the period when they are waived such requirements. The same pattern appears in the matched US firms. The higher cost of equity capital and return variability in the latter period is generally consistent with the extreme volatility the US capital markets have experienced in recent years.

Table III reports the Pearson correlation coefficients and *p*-values for the variables used in our study. We find significantly positive correlations between cost of equity capital (*COC_{it}*) and different reporting requirement periods (*Period_{it}*). Consistent with prior research (Hail and Leuz, 2009), cost of equity capital (*COC_{it}*) is positively correlated with return variability (*RV_{it}*), industry-year cost of equity (*INDCOC_{it}*), and negatively correlated with firm size (*Size_{it}*).

	COC_{it}	$Period_{it}$	$Size_{it}$	LEV_{it}	RV_{it}	$INDCOC_{it}$
COC_{it}	1					
$Period_{it}$	0.3710 (< 0.0001)	1				
$Size_{it}$	-0.1391 (< 0.0001)	-0.0796 (0.0038)	1			
LEV_{it}	-0.001 (0.9837)	-0.0845 (0.0021)	0.5388 (< 0.0001)	1		
RV_{it}	0.4124 (< 0.0001)	0.3549 (< 0.0001)	-0.4413 (< 0.0001)	-0.1938 (< 0.0001)	1	
$INDCOC_{it}$	0.4479 (< 0.0001)	0.6326 (< 0.0001)	0.1216 (< 0.0001)	0.0524 (0.0571)	0.3277 (< 0.0001)	1

Note: The variables are defined in Table II

Table III.
Pearson correlation matrix (two-tailed p -values in parentheses) ($n = 1,321$)

5. Results

To examine *RQ1a*, we compare cost of equity in foreign firms between the IFRS reporting period (2007-2009) and the US GAAP reconciliation period (2004-2006). Table IV presents OLS regression coefficient estimates and heteroscedasticity-corrected t -statistics. The cost of equity (COC_{it}) is regressed on a dummy variable indicating the time period with different reporting requirements ($Period_{it}$) and a set of control variables. The estimated coefficient on $Period_{it}$ is positive and significant (0.006, $t = 2.63$, two-tailed), indicating that the cost of equity goes higher after foreign firms are waived the US GAAP reconciliations.

In *RQ1b*, we compare the cost of equity of foreign firms to that of matched US firms. There are 12,892 US firm-year observations with necessary variables during 2004-2009. Hence, the benchmark sample size is substantially larger than our foreign firm sample of 1,321 observations. Moreover, foreign firms listed in the USA are often those that are large in size and able to afford high regulatory costs, and have a need to increase market liquidity, whereas our US firms are relatively heterogeneous. To mitigate potential confounding factors, we thus use a matched sample design. Our final sample consists of

$$COC_{it} = \alpha_0 + \alpha_1 * Period_{it} + \alpha_2 * Size_{it} + \alpha_3 * LEV_{it} + \alpha_4 * RV_{it} + \alpha_5 * INDCOC_{it} + \varepsilon_{it} \quad (1a)$$

Variable	Predicted sign	All foreign firms
Intercept	?	0.018 *** (3.22)
$Period_{it}$?	0.006 *** (2.63)
$Size_{it}$	-	-0.002 *** (-3.53)
LEV_{it}	+	0.019 *** (3.50)
RV_{it}	+	0.136 *** (7.44)
$INDCOC_{it}$	+	0.769 *** (9.28)
Adj. R^2		0.2901
F -value		87.72
n		1,321

Notes: Statistically significant at: *10, **5, ***1 percent levels for a two-tailed test; the t -statistics are reported in parentheses; all the t -statistics are adjusted for heteroscedasticity; variable definitions: the variables are defined in Table II

Table IV.
Results of *RQ1a* – OLS regression of all foreign firms

1,282 foreign firm-year observations matched with 1,282 US firm-year observations based on year, industry and total assets.

We regress the cost of equity (COC_{it}) on a dummy variable indicating issuer's country ($Issuer_{it} = 1$ if it is a foreign firm, and 0 if a matched US firm), a variable for different reporting periods ($Period_{it}$), and a set of control variables. Table V reports regression results for matched US firms, the pooled sample of foreign and matched US firms, the pooled sample in the early US GAAP reconciliation period, and the pooled sample in the latter IFRS reporting period, respectively. In the first column, we find that the cost of equity in US firms exhibits no change from the US GAAP reconciliation period to the IFRS reporting period. In the second column, the estimated coefficient on $Period_{it}$ is insignificant, the estimated coefficient on $Issuer_{it}$ is significantly positive (0.011, $t = 7.66$, two-tailed), and the interaction between the two is insignificant. The results suggest that foreign firms generally have a higher cost of equity capital than US firms, and the gap of cost of equity capital does not change in the latter period. The third column reports regression results for the sub-period when foreign firms are required to prepare US GAAP reconciliations, and the fourth column reports regression results for the sub-period when foreign firms are waived the US GAAP reconciliations. The significantly positive coefficients on $Issuer_{it}$ in both columns (0.011 and 0.013, respectively) corroborate that foreign firms have a constantly higher cost of equity capital than US firms in the two periods. Together, the results suggest that regardless of

$$COC_{it} = \alpha_0 + \alpha_1 * Period_{it} + \alpha_2 * Issuer_{it} + \alpha_3 * Period_{it} * Issuer_{it} + \alpha_4 * Size_{it} + \alpha_5 * LEV_{it} + \alpha_6 * RV_{it} + \alpha_7 * INDCOC_{it} + \varepsilon_{it} \quad (1b)$$

Variable	Predicted sign	US firms	All foreign firms and matched US firms	Reconciliation period $Period_{it} = 0$	IFRS period $Period_{it} = 1$
Intercept	?	-0.014*** (-3.17)	-0.003 (-0.88)	0.006 (1.05)	-0.003 (-0.64)
$Period_{it}$?	0.001 (0.27)	0.002 (1.21)		
$Issuer_{it}$?		0.011*** (7.66)	0.011*** (7.97)	0.013*** (7.02)
$Period_{it} * Issuer_{it}$?		0.003 (1.12)		
$Size_{it}$	-	-0.001* (-1.77)	-0.001*** (-3.81)	-0.002*** (-3.97)	-0.001** (-2.44)
LEV_{it}	+	0.022*** (5.69)	0.020*** (6.01)	0.026*** (6.97)	0.015*** (3.00)
RV_{it}	+	0.104*** (6.66)	0.123*** (9.91)	0.083*** (4.32)	0.134*** (8.80)
$INDCOC_{it}$	+	0.994*** (14.19)	0.875*** (15.91)	0.758*** (9.18)	0.920*** (13.07)
$Adj. R^2$		0.4022	0.3536	0.1984	0.2605
F-value		139.51	169.51	51.90	90.21
n		1,282	2,564	1,137	1,427

Table V. Results for $RQ1b$ – OLS regressions of foreign firms and matched US firms

Notes: Statistically significant at: *10, **5, ***1 percent levels for a two-tailed test; the t -statistics are reported in parentheses; all the t -statistics are adjusted for heteroscedasticity; variable definitions: $Issuer_{it}$ – dummy variable equal to 1 if a firm is a foreign issuer, and 0 if a firm is a matched US issuer; the other variables are defined in Table II

whether foreign firms are required the US GAAP disclosure or not, their cost of equity capital is higher than US firms. The SEC's relaxing disclosure requirement for foreign firms neither exacerbates nor alleviates such a difference.

To examine *RQ2a*, we then regress the cost of equity (COC_{it}) on a dummy variable indicating different reporting periods ($Period_{it}$), a dummy variable indicating IFRS adoption status of foreign firm's home country ($Adopt_{it}$), the interaction between the two, and control variables. Table VI presents separate results for the full sample, $Adopt_{it} = 0$ sample, and $Adopt_{it} = 1$ sample. In the first column, the estimated coefficient on $Period_{it}$ is insignificant, the estimated coefficient on $Adopt_{it}$ is significantly negative (-0.005 , $t = 2.38$, two-tailed), and the interaction variable is 0.011 and statistically significant ($t = 3.00$, two-tailed). Estimated coefficient on $Period_{it}$ is 0.003 ($t = 0.87$, two-tailed) and 0.008 ($t = 2.51$, two-tailed), respectively, for the two subsamples partitioned based on their home countries' IFRS adoption status, which suggests $Adopt_{it} = 1$ sample exhibits significant increase in the cost of equity over periods while $Adopt_{it} = 0$ sample does not. This implies that foreign firms from IFRS adoption countries have a lower cost of equity capital in general, but experience greater increase in the cost of equity in the latter period than other foreign firms. The increase in cost of equity in foreign firms from IFRS adoption countries may be attributed to an information loss as a result of potential elimination of the US GAAP reconciliation[2].

$$COC_{it} = \alpha_0 + \alpha_1 * Period_{it} + \alpha_2 * Adopt_{it} + \alpha_3 * Period_{it} * Adopt_{it} + \alpha_4 * Size_{it} + \alpha_5 * LEV_{it} + \alpha_6 * RV_{it} + \alpha_7 * INDCOC_{it} + \varepsilon_{it} \quad (2a)$$

Variable	Predicted sign	All foreign firms	Foreign firms with $Adopt_{it} = 0$	Foreign firms with $Adopt_{it} = 1$
Intercept	?	0.021 *** (3.45)	0.037 *** (4.26)	-0.002 (-0.28)
$Period_{it}$?	0.001 (0.28)	0.003 (0.87)	0.008 ** (2.51)
$Adopt_{it}$?	-0.005 ** (-2.38)		
$Period_{it} * Adopt_{it}$?	0.011 *** (3.00)		
$Size_{it}$	-	-0.002 *** (-3.59)	-0.004 *** (-3.98)	-0.000 (-0.91)
LEV_{it}	+	0.019 *** (3.44)	0.024 ** (3.50)	0.013 (1.53)
RV_{it}	+	0.138 *** (7.23)	0.105 *** (4.80)	0.201 *** (4.80)
$INDCOC_{it}$	+	0.779 *** (9.37)	0.741 *** (6.60)	0.841 *** (6.63)
$Adj. R^2$		0.2936	0.2637	0.3410
F-value		67.04	49.60	38.68
n		1,321	747	574

Notes: Statistically significant at: *10, **5 and ***1 percent levels for a two-tailed test; the *t*-statistics are reported in parentheses; all the *t*-statistics are adjusted for heteroscedasticity; variable definitions: $Adopt_{it}$ – dummy variable equal to 1 if an observation is from a country that mandates IFRS before December 15, 2007, and 0 otherwise; the other variables are defined in Table II

Table VI. Results of *RQ2a* – OLS regressions for foreign firms partitioned on $Adopt_{it}$

Table VII reports regression results of equation (2b) for foreign and US sample partitioned based on $Adopt_{it}$. For the subsample of foreign firms from countries that have not adopted IFRS ($Adopt_{it} = 0$) and their US pairs, the estimated coefficient on $Issuer_{it}$ is significantly positive (0.014, $t = 6.54$, two-tailed) and the estimated coefficient on the interaction variable ($Period_{it} * Issuer_{it}$) is negative but insignificant. For the subsample of foreign firms from countries that have already adopted IFRS ($Adopt_{it} = 1$) and their US pairs, the estimated coefficient on $Issuer_{it}$ is significantly positive (0.008, $t = 4.17$, two-tailed) and the estimated coefficient on the interaction variable ($Period_{it} * Issuer_{it}$) is positive and marginally significant. The insignificant interaction coefficient ($Period_{it} * Issuer_{it}$) in $Adopt_{it} = 0$ sample suggests that the difference in cost of equity between foreign and US firms remains the same in the second period, and we attribute this to the joint effect of concurrently tightened disclosure requirements for foreign firms as well as the waiver of US GAAP reconciliation[3]. In contrast, although $Adopt_{it} = 1$ sample are also exposed to the same tightened disclosure requirements, their likelihood to use IFRS without US GAAP reconciliation appears to have a stronger deregulation effect and results in the increased cost of equity capital in foreign firms relative to that of the US firms. Such results could be interpreted as US investors' fear of unfamiliar accounting reporting without the US GAAP reconciliation.

$$COC_{it} = \alpha_0 + \alpha_1 * Period_{it} + \alpha_2 * Issuer_{it} + \alpha_3 * Period_{it} * Issuer_{it} + \alpha_4 * Size_{it} + \alpha_5 * LEV_{it} + \alpha_6 * RV_{it} + \alpha_7 * INDCOC_{it} + \varepsilon_{it} \quad (2b)$$

Variable	Predicted sign	Foreign firms with $Adopt_{it} = 0$ and matched US firms	Foreign firms with $Adopt_{it} = 1$ and matched US firms
Intercept	?	0.003 (0.66)	-0.010* (-1.72)
$Period_{it}$?	0.001 (0.39)	0.003 (1.17)
$Issuer_{it}$?	0.014*** (6.54)	0.008*** (4.17)
$Period_{it} * Issuer_{it}$?	-0.001 (-0.20)	0.006* (1.82)
$Size_{it}$	-	-0.002* (-3.77)	-0.001* (-1.88)
LEV_{it}	+	0.021*** (5.07)	0.020*** (3.69)
RV_{it}	+	0.114*** (7.75)	0.139*** (5.64)
$INDCOC_{it}$	+	0.859*** (11.42)	0.910*** (11.16)
$Adj. R^2$		0.3412	0.3765
F-value		102.12	72.19
n		1,446	1,118

Table VII. Results for RQ2b – OLS regressions for foreign firms partitioned on $Adopt_{it}$ and their matched US firms

Notes: Statistically significant at: *10, **5, ***1 percent levels for a two-tailed test; the t -statistics are reported in parentheses; all the t -statistics are adjusted for heteroscedasticity; variable definitions: $Issuer_{it}$ – dummy variable equal to 1 if a firm is a foreign issuer, and 0 if a firm is a matched US issuer; $Adopt_{it}$ – dummy variable equal to 1 if an observation is from a country that mandates IFRS before December 15, 2007, and 0 otherwise; the other variables are defined in Table II

Two potential concerns regarding the main tests are that:

- (1) US GAAP and IFRS may converge at different degree during the sample period; and
- (2) foreign firms' home countries adopt IFRS in different years during the sample period.

To address the first issue, the variable $INDCOC_{it}$ controls for year and industry difference in the main tests. We believe that, its use can minimize to certain degree the year effect, which includes the impact of the yearly difference between US GAAP and IFRS during the sample period on the cost of equity.

To address different IFRS adoption years among the sample countries, we have tried the following: we restrict our sample to countries that either adopted IFRS or did not adopt IFRS during the entire sample period. First, to ensure all $Adopt_{it} = 1$ firms are from countries that constantly require IFRS compliance during the sample period, we exclude all 2004 observations because most countries adopted IFRS in 2005. Second, to ensure all $Adopt_{it} = 0$ firms are from countries that constantly require local GAAP compliance during the sample period, we delete firms from Chile, Israel, Kazakhstan and New Zealand because they adopted IFRS at some point after the SEC's ruling in our sample period. This new sample still results in robust findings.

6. Conclusions

This study explores the cost of equity capital in foreign firms listed in the USA around the time period when the SEC has shifted to permitting foreign firms to use IFRS without US GAAP reconciliation. Foreign firms choose cross-listings in the USA to show their commitment to high quality disclosure requirements in the USA, and as a result, benefit from reduced cost of equity capital. The SEC's waiver of US GAAP reconciliation and allowing foreign firms to use IFRS could potentially weaken the bonding signal sent to US investors, particularly when the premise that the two sets of accounting standards have converged is still questionable.

Our results show that foreign firms' cost of equity generally increases in the period that the SEC permits the use of IFRS reporting (2007-2009). Our results also show that foreign firms also appear to bear a constantly higher cost of equity than that of US firms over the entire sample period (2004-2009), which does not vary with different reporting requirements in different sub-periods.

When foreign firms are partitioned on whether they domicile in countries that have adopted IFRS, only foreign firms who are mandated to use IFRS in their home countries experience a higher cost of equity capital in the latter period. The cost of equity capital of foreign firms from IFRS adoption countries relative to matched US firms also increases in the latter period. We attribute the increase in cost of equity capital in the $Adopt_{it} = 1$ sample but not in the $Adopt_{it} = 0$ sample to the different impacts on the two samples from the elimination of US GAAP reconciliation and (possibly) concurrently tightened disclosure requirements (see details in [3]). Compared to foreign firms from IFRS adoption countries ($Adopt_{it} = 1$ sample), foreign firms from non-IFRS adoption countries ($Adopt_{it} = 0$ sample) seem more affected by the tightened disclosure requirements and less affected by the elimination of US GAAP reconciliation. Overall, our results suggest that relaxing the US GAAP reconciliation requirement by the SEC primarily affects foreign firms from IFRS adoption countries.

The evidence echoes the inconsistent findings of capital market effect of IFRS adoption around the world (Hail *et al.*, 2010a, b) and a view shared by many (Ball, 2006) that convergence of accounting standards in itself do not entail significant economic benefits such as a lower cost of equity capital unless the institutional environment converges or improves as well.

It is worth noting that our results cannot resolve the mixed findings in the prior studies regarding IFRS and US GAAP financial reporting quality. Our results add another evidence to the mixed findings. But on a different note, we find that foreign firms have constantly higher cost of equity than US firms during the entire sample period, which is consistent in general with prior findings that the removal of US GAAP reconciliation did not cause significant capital market effect. More importantly, we think that bonding hypothesis can be a factor leading to our results such that only firms from IFRS adoption countries exhibit a diminishing bonding to the US GAAP by a heightened cost of equity in the post-regulation period. Thus, our findings mainly contribute to the impact of disclosure regulation.

Our study leaves a few unresolved issues for future research. Our sample period ends in 2009, thus a future area to study is to investigate longer sample period with recent years included. As convergence project progresses, the equivalence between the US GAAP and IFRS increases which may affect the cost of equity differently from the earlier years to the recent years during the IFRS-reporting period. Another area to investigate is whether the cost of equity capital change of foreign firms in response to IFRS adoption is sensitive to home countries' institutional factors, such as law enforcement, legal systems.

Notes

1. We thank our reviewer for this point.
2. Pointed out by the reviewer, another possible explanation for the higher cost of equity in only foreign firms from IFRS adoption countries is that foreign firms may use a jurisdictional variation of IFRS and thus the investors may perceive the so-called IFRS is not the "genuine" IFRS as issued by the IASB, and then give a discount on the financial reporting quality and only want to buy their shares at a lower price. We explored this explanation by looking into whether our sample countries comply with IFRS as issued by the IASB or a variation of it. Only EU firms might use a jurisdictional variation of IFRS as the EU allows more flexibility in the use of IAS 39 than the IASB allows. We believe that EU firms' variation in use of IFRS does not drive our results primarily for two reasons. First, the SEC noted that "few companies make use of this ability to 'carve-out' these provisions of IAS 39 from IFRS as issued by the IASB" and the EU also noted in its comment letter, "[f]or the vast majority of EU issuers listed in the USA, this carve-out has no practical significance and as such their financial statements prepared under IFRS as adopted by the EU would be identical to those prepared under IFRS as published by the IASB" (www.sec.gov/rules/final/2007/33-8879.pdf). Second, the SEC pointed out that only foreign financial firms are exposed to such a difference and several of them commented that they did not use it.
3. In 2008, the SEC amended reporting and disclosure requirements for foreign firms, including accelerating the annual report filing, eliminating certain accommodations in foreign firms' filings, etc. (<http://sec.gov/rules/final/2008/33-8959.pdf>). Those tightened disclosure requirements on foreign firms have varying effective dates from 2009 to 2011. To the extent that these rules result in increased disclosures for foreign firms to be more in line with US firms, they will make it harder for us to find the expected IFRS disclosure effect, a form of deregulation.

References

- Bailey, W., Karolyi, G.A. and Salva, C. (2006), "The economic consequences of increased disclosure: evidence from international cross-listings", *Journal of Financial Economics*, Vol. 81 No. 1, pp. 175-213.
- Ball, R. (2006), "International financial reporting standards (IFRS): pros and cons for investors", *Accounting & Business Research International Accounting Policy Forum*, pp. 5-27.
- Barth, M., Landsman, W., Lang, M. and Williams, C. (2010), "Are IFRS-based and US GAAP-based accounting amounts comparable?", *Journal of Accounting and Economics*, in press.
- Bradshaw, M.T. and Miller, G.S. (2008), "Will harmonizing accounting standards really harmonize accounting? Evidence from non-US firms adopting US GAAP", *Journal of Accounting, Auditing and Finance*, Vol. 23, pp. 233-263.
- Claus, J. and Thomas, J. (2001), "Equity premium as low as three percent? Evidence from analysts' earnings forecasts for domestic and international stock markets", *The Journal of Finance*, Vol. 56 No. 5, pp. 1629-1666.
- Coffee, J. (1999), "The future as history: the prospects for global convergence in corporate governance and its implications", *Northwestern University Law Review*, Vol. 93, pp. 641-708.
- Coffee, J. (2002), "Racing towards the top? The impact of cross-listings and stock market competition on international corporate governance", *Columbia Law Review*, Vol. 102, pp. 1757-1831.
- Daske, H., Hail, L., Leuz, C. and Verdi, R. (2008), "Mandatory IFRS reporting around the world: early evidence on the economic consequences", *Journal of Accounting Research*, Vol. 46 No. 5, pp. 1085-1142.
- Easton, P. (2004), "PE ratios, PEG ratios, and estimating the implied expected rate of returns on equity capital", *The Accounting Review*, Vol. 79 No. 1, pp. 73-95.
- Fama, E. and French, D. (1997), "Industry costs of equity", *Journal of Financial Economics*, Vol. 43 No. 2, pp. 153-193.
- FASB (2002), *Memorandum of Understanding: The Norwalk Agreement*, Financial Accounting Standards Board, available at: www.fasb.org/news/memorandum.pdf
- FASB (2006), "A roadmap for convergence between IFRSs and USGAAP 2006-2008: memorandum of understanding between the FASB and the IASB", Financial Accounting Standards Board, available at: www.fasb.org/cs/ContentServer?c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176156245558 (accessed February 27).
- FASB (2008), *Completing the February 2006 Memorandum of Understanding: A Progress Report and Timetable for Completion*, Financial Accounting Standards Board, available at: www.fasb.org/intl/MOU_09-11-08.pdf
- Frost, C. and Kinney, W. (1996), "Disclosure choices of foreign registrants in the United States", *Journal of Accounting Research*, Vol. 34 No. 1, pp. 67-81.
- Gebhardt, R., Lee, C. and Swaminathan, B. (2001), "Toward an ex ante cost of capital", *Journal of Accounting Research*, Vol. 39 No. 1, pp. 135-176.
- Gode, D. and Mohanram, P. (2003), "Inferring cost of capital using the Ohlson-Juettner model", *Review of Accounting Studies*, Vol. 8 No. 4, pp. 399-431.
- Hail, L. and Leuz, C. (2006), "International differences in the cost of equity capital: do legal institutions and securities regulation matter?", *Journal of Accounting Research*, Vol. 44 No. 3, pp. 485-531.

- Hail, L. and Leuz, C. (2009), "Cost of capital effects and changes in growth expectations around US cross-listings", *Journal of Financial Economics*, Vol. 93 No. 3, pp. 428-454.
- Hail, L., Leuz, C. and Wysocki, P. (2010a), "Global accounting convergence and the potential adoption of IFRS by the US (Part I): political factors and future scenarios for US accounting standards", *Accounting Horizon*, Vol. 24 No. 3, pp. 355-394.
- Hail, L., Leuz, C. and Wysocki, P. (2010b), "Global accounting convergence and the potential adoption of IFRS by the US (Part II): political factors and future scenarios for US accounting standards", *Accounting Horizon*, Vol. 24 No. 4, pp. 567-588.
- Hansen, B., Pownall, G., Prakash, R. and Vulcheva, M. (2011), *Relaxing the Reconciliation Requirement in Non-US Firms' SEC Filings: Changes in GAAP, Earnings Attributes, and Earnings Informativeness*, available at: <http://ssrn.com/abstract=1694498>
- Harris, M. and Muller, K. (1999), "The market valuation of IAS versus US GAAP accounting measures using Form 20-F reconciliations", *Journal of Accounting and Economics*, Vol. 26, pp. 285-312.
- Healy, P.M. and Palepu, K.G. (2001), "Information asymmetry, corporate disclosure, and the capital markets: a review of the empirical disclosure literature", *Journal of Accounting & Economics*, Vol. 31 Nos 1/3, pp. 405-440.
- Henry, E., Lin, S. and Yang, Y. (2009), "The European-US 'GAAP Gap': IFRS to US GAAP Form 20-F reconciliations", *Accounting Horizons*, Vol. 23 No. 2, pp. 121-151.
- Jiang, J., Petroni, K. and Wang, I. (2010), "Did eliminating the 20-F reconciliation between IFRS and US GAAP matter?", available at: <http://ssrn.com/abstract=1694590>
- Kim, Y., Li, H. and Li, S. (2011), "Does eliminating the Form 20-F reconciliation from IFRS to US GAAP have capital market consequences?", *Journal of Accounting and Economics*, in press.
- King, M. and Segal, D. (2009), "The long-term effects of cross-listing, investor recognition, and ownership structure on valuation", *Review of Financial Studies*, Vol. 22, pp. 2393-2421.
- Lang, M., Raedy, J.S. and Wilson, W. (2006), "Earnings management and cross listing: are reconciled earnings comparable to US earnings", *Journal of Accounting and Economics*, Vol. 42 Nos 1/2, pp. 255-283.
- Leuz, C. (2003), "IAS versus US GAAP: information asymmetry-based evidence from Germany's new market", *Journal of Accounting Research*, Vol. 41, pp. 445-472.
- Li, S. (2010), "Does mandatory adoption of international financial reporting standards in the European Union reduce the cost of equity capital?", *The Accounting Review*, Vol. 85 No. 2, pp. 607-636.
- Salwen, K.G. (1991), "Breeders rejects big board plan to relax listing standards for foreign concerns", *The Wall Street Journal*, May 3.
- SEC (2007), *Final Rule: Acceptance from Foreign Private Issuers of Financial Statements Prepared in Accordance with International Financial Reporting Standards Without Reconciliation to US GAAP*, Securities and Exchange Commission, available at: www.sec.gov/rules/final/2007/33-8879.pdf
- Siconolfi, M. and Salwen, K.G. (1992), "Big board, SEC fight over foreign stocks", *The Wall Street Journal*, May 13.
- Stulz, R. (1999), "Globalization, corporate finance, and the cost of capital", *Journal of Applied Corporate Finance*, Vol. 12, pp. 8-25.
- Van der Meulen, S., Gaeremynck, A. and Willekens, M. (2007), "Attribute differences between US GAAP and IFRS earnings: an exploratory study", *The International Journal of Accounting*, Vol. 42, pp. 123-142.

Further reading

Daske, H. (2006), "Economic benefits of adopting IFRS or US-GAAP – have the expected cost of equity capital really decreased?", *Journal of Business Finance & Accounting*, Vol. 33 Nos 3/4, pp. 329-373.

About the authors

Fei Han is an Assistant Professor of Accounting at Robert Morris University in Pittsburg, Pennsylvania. She holds a PhD from the University of Connecticut.

Haihong He is an Associate Professor of Accounting at California State University, Los Angeles. She received her PhD from the University of Connecticut and has published articles in journals such as *Journal of International Accounting Research* and *European Accounting Review*. Haihong He is the corresponding author and can be contacted at: hhe@calstatela.edu

To purchase reprints of this article please e-mail: reprints@emeraldinsight.com
Or visit our web site for further details: www.emeraldinsight.com/reprints

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission.