

Impact of Adoption of International Financial Reporting Standards on the Canadian Stock Markets

■ Canada adopted International Financial Reporting Standards (IFRS) in 2011. There is little evidence in the accounting literature about the Canadian adoption experience even though Canada's decision to adopt IFRS meant departing from the practice of its largest trade partner, the U.S. In my research (co-authored with Professors Mark Anderson, Hussein Warsame and Michael Wright from the University of Calgary), I investigate the impact of IFRS adoption on the quality of earnings information released by firms listed on the two Canadian stock exchanges, the TSX exchange and the TSX Venture Exchange. My analysis is based on trading by both retail and institutional investors when earnings are announced.

It has been argued that IFRS is a more principles-based set of accounting standards, meaning that IFRS requires accountants to take more responsibility for providing relevant accounting information. Old Canadian GAAP (Generally Accepted Accounting Principles) placed more emphasis on the reliability of accounting information and hence relied less on the judgment of accountants. A priori, one may expect that the information content of earnings would increase for both TSX and TSX Venture exchange firms if IFRS earnings provide more value-relevant information than old Canadian GAAP earnings. As such, the increased value relevance of information provided by IFRS earnings would reflect greater emphasis on measurement of changes in net asset values based on expectations as opposed to realizations.

Consistent with this argument, my research finds that the information content of earnings under IFRS increased for TSX firms during earnings announcement periods, compared to the information content of earnings during pre-IFRS earnings

announcement periods. However, firms listed on the TSX Venture exchange, where retail investors have a greater presence, did not benefit from IFRS adoption in this manner. In fact, my evidence suggests that, due to the speculative nature of the TSX Venture exchange, investors did not rely as much on the accounting information provided during the post-IFRS earnings announcements periods as they had in the pre-IFRS periods. Thus, my findings indicate that IFRS adoption may have benefitted firms on the TSX exchange more than firms

on the TSX Venture exchange. The results of my study suggest that this reflects a greater reliance by TSX Venture investors on realized earnings information. Old Canadian GAAP emphasized the reliability characteristics of accounting information whereas more expectation-based values of net assets under IFRS may increase uncertainty of accounting information for TSX Venture investors.

Canada is unique in the world in that it has well-functioning senior and junior stock exchanges. The TSX Venture exchange is a venture capital exchange, populated largely by exploration-oriented companies

in the extractive industries and innovation-oriented growth companies, that caters primarily to retail investors. The TSX Venture exchange is a more speculative venture-oriented exchange that was formed by combining local exchanges operating in Alberta and British Columbia. Companies on the TSX exchange are typically larger, have larger institutional investor bases and are followed by analysts more than companies on the TSX Venture exchange. In fact, many of the smaller firms listed on the TSX Venture exchange have no institutional ownership. The TSX is a more traditional high-quality stock exchange regulated in the province of Ontario.

“OUR RESEARCH
CAN HELP CANADIAN
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MORE CAREFULLY
ABOUT THE IMPACT
OF ADOPTING IFRS ON
THE CANADIAN STOCK
MARKETS.”

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BIOGRAPHY

DR. SHAHID KHAN is an Assistant Professor of Accounting at the Penn State University, Berks campus. He received his Ph.D. at the University of Calgary. His research interests are in the areas of the impact of International Financial Reporting Standards on the capital markets, accounting and international capital movement, information quality, and accounting standards. His research paper has been published in *Accounting Perspectives*.

Receiving the CSIRF funding for the last two years of my Ph.D. program at the University of Calgary was one of the most critical events in my pursuit of a research career. Because of this generous support, I could focus on my research, rather than take on teaching and other research assistance work to fill the financial gap. The CSIRF funding helped me to start my career at the Penn State University. My name also appeared on the CSIRF website as one of the winners of the CSIRF scholarship which increased my visibility to future employers.

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The current debate in Canada about the need for a single securities regulator is hotly contested in the western provinces and reflects the more entrepreneurial and speculative nature of the TSX Venture exchange. Our research can help Canadian regulators think more carefully about the impact of adopting IFRS on the Canadian stock markets. Our research can also help U.S. regulators in their decision to either adopt or converge to IFRS in the future, considering that Canada's markets are similar to the U.S. markets. ■



Reference:

Khan, S., Anderson, M., Warsame, H., & Wright, M. (2015). Do IFRS-Based Earnings Announcements Have More Information Content than Canadian GAAP-Based Earnings Announcements?. *Accounting Perspectives*, 14(3), 276-302.