We examine whether goodwill related disclosure, as mandated by IFRS 3 and IAS 36, reduces implied cost of equity capital (ICC) for a sample of European firms for the period 2008 to 2011. We focus on goodwill since it is a significant amount on a company’s balance sheet and it conveys current and forward looking information relevant to a firm. Additionally, the goodwill impairment tests give rise to concerns about their implementation quality. Our results indicate a mean (median) compliance level of about 82% (83%) and a high variation among firms’ disclosure levels. In depth analysis reveals that non-compliance relates mostly to proprietary information and information that reveals managers’ judgment and expectations. Furthermore, we find a negative relationship between ICC and goodwill related mandatory disclosure levels. This relationship is not only statistically but also economically significant. Thus, companies exhibiting high compliance levels experience significantly reduced ICC. These findings add knowledge regarding the economic consequences of mandatory disclosures, should have an appeal to regulators and financial statement preparers, and reflect on the IASB’s concerns to increase the guidance and principles on presentation and disclosure in the revised Conceptual Framework.

Abstract:
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