



The valuation properties of earnings and book value prepared under US GAAP in Chile and IAS in Peru

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Abstract

The worldwide trend toward integration of capital markets heightens the debate on whether international accounting standards (IAS) and US generally acceptable accounting principles (GAAP) are equivalent accounting regimes for cross-border listings. The Securities and Exchange Commission (SEC) operates from the premise that IAS falls below the threshold and mandated reconciliation from IAS to US GAAP. A major concern is that reconciling the IAS accounting numbers to US GAAP when the underlying contracts are formulated based on IAS results in assessment noise in the Ndubizu and Wallace [Ndubizu, G.A., Wallace, R.S., 2003. Contracts valuation assessment noise and cross-border listing of equities on US and UK stock markets. The International Journal of Accounting 38, 397–420] sense. We examine the valuation properties of US GAAP in Chile and IAS in Peru in which contracts and their representation in the financial statements are based on the same GAAP to minimize the likelihood of assessment noise. We find that earnings and book value are value relevant in the two accounting regimes. However, US GAAP as applied in Chile is more value relevant than IAS

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applied in Peru. The results are robust to alternative specifications, including controlling for cross-sectional and inflation-induced scale effects present in level regressions, tax–book alignment, and other country-specific factors. Further, the results of the study provide evidence that US GAAP is more timely, conservative, and informative about the expected future normal earnings for loss firms than IAS in emerging economies.

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1. Introduction

We examine the valuation properties of accounting earnings and book value of equity derived from contracts and financial statements prepared under US generally accepted accounting principles (GAAP) in Chile and international accounting standards (IAS) in Peru for the period 1995–1999. In both countries, the home GAAP is used to formulate contracts with stakeholders and to translate contracts into assets, liabilities and equity in the financial statements. The joint use of the home GAAP in contracting and financial reporting minimizes the likelihood of assessment noise in the [Ndubizu and Wallace \(2003\)](#) sense. Because of the cultural and institutional connection between contracts and the home GAAP, the value relevance of the contracts depends on whether the home country's GAAP maps cultural and institutional components of contracts into financial statements. The failure of the home GAAP to capture and reflect the cultural and institutional components of contracts in financial statements is referred to as assessment noise ([Ndubizu and Wallace, 2003](#)), which is value irrelevant.

Although US GAAP and IAS appear to be exogenously determined in Latin America, they are used in contracting with stakeholders and in translating the contracts into financial statements in Chile and Peru, respectively. Therefore, we presume that assessment noise is less likely in our research settings. The results of the study provide evidence of the superior value relevance of US GAAP over IAS in emerging economies.¹

The Chilean GAAP is generally in line with accounting principles prevailing in the United States ([Price Waterhouse, 1994a](#)). The main difference from US GAAP is that price-level restatements are mandatory in Chile ([Price Waterhouse, 1994a](#)) but voluntary in the United States under SFAS No. 89. Therefore, we refer to the accounting rules in Chile as the US GAAP regime. In

¹ Because of resource constraints, emerging economies tend to adopt either IAS or US style GAAP for both contracting and financial reporting. Therefore, our results may be applicable to other emerging countries.

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