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Russian Accounting System: Value Relevance of Reported Information and the IFRS Adoption Perspective ☆

Oksana Kim

Department of Accounting and Business Law, Minnesota State University, Mankato, MN, United States

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Abstract

In this paper I perform an empirical investigation into the value relevance of information reported by Russian public firms from two distinct perspectives. First, I document that prior to 2011, investors relied on information incorporated in the book value of equity. The value relevance of reported earnings, however, is different for "growth" versus "value" stocks. Second, I document that Russian leading firms listed on the London Stock Exchange that report in accordance with IFRS produce more value-relevant reports compared to their local peers that report under the Russian standards. This suggests that the mandatory IFRS adoption in Russia that will be completed by 2015 is likely to result in improved information quality.

JEL classification: M41; M48
Keywords: International Financial Reporting Standards (IFRS); Russian Accounting Standards (RAS); Value relevance; Accounting quality

1. Introduction

This study examines the value relevance of information reported by Russian public firms from two different perspectives. First, the study shows that for Russian firms that were listed on two national stock exchanges prior to 2011, investors relied on information incorporated in the book value of equity, while the evidence with respect to reported

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E-mail address: Oksana.kim@mnsu.edu.

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earnings is mixed. This outcome is due to differences in volatility and reporting incentives for "growth" versus "value" stocks, and the latter report more value-relevant earnings. The documented evidence is based on almost the entire period of existence of the Russian stock market — from 1995 to 2010.

Second, in 2011 the Russian government signed off on the IFRS adoption procedure for gradual transition from the Russian Accounting Standards (RAS) to IFRS by 2015. The study examines the value relevance of information for the sample of Russian firms listed on the London Stock Exchange (LSE) that report under IFRS and the sample of leading firms listed locally that report under RAS. The results indicate that information produced by IFRS-reporting firms is more value relevant, which suggests that adoption of IFRS is likely to result in improved information quality. This outcome, however, is contingent upon creating proper incentives for firms to adopt IFRS, which includes upgrading market infrastructure, revising stock exchange regulations, and rigorously enforcing the IFRS reporting regime (Ball, Kothari, & Robin, 2000).

This study is motivated by the fact that the Russian stock market is currently undergoing a number of fundamental innovations, including adoption of IFRS, a merger of the two national exchanges, and revisions in the listing and corporate law that are collectively aimed at strengthening the position of the Russian market. The empirical evidence of this study that is based on the pre-reform period of 1995–2010 should be considered as a benchmark for evaluating the innovations that will change the Russian market dynamics. The success of these reforms is to be assessed after 2015, when Russia fully adopts IFRS.

The global convergence of accounting standards through adoption of IFRS is expected to decrease information processing costs, thus facilitating the inflow of Foreign Direct Investments (FDIs) and increasing the scope of cross-border mergers and acquisitions (Amiram, 2012; Chen, Ding, & Xu, Working paper; Marquez-Ramos, 2011). Prior studies also documented that uniformity in accounting standards is likely to minimize within-country negative information externalities, leading to enhanced comparability and higher reporting quality (Ball, 2006; Barth, Landsman, & Lang, 2008; Barth, Landsman, Lang, & Williams, 2012). Therefore, one of the incentives for emerging countries to adopt IFRS is to encourage domestic and global investors to commit greater capital to a national stock market system.

Accordingly, the commitment to adopt IFRS in Russia is largely explained by the country's unprecedented need for FDIs. In 2011, the national government announced ambitious plans to invest 1.5 trillion USD in modernization of the Russian economy, an amount that is almost three times higher than the average Gross Domestic Product (GDP) of the country over the past decade (The World Bank, 2011). Successful implementation of the plan will manifest in a strong need for foreign investments, which have remained stubbornly low (The World Bank, 2012). The global investment capital, nevertheless, is a limited resource, for which Russia has to compete with other emerging nations.

This study contributes to the empirical literature in two important ways. First, the study extends the emerging markets stream of literature. The case of Russia provides unique research settings to examine the capital market development process in a country that was the leader of the Soviet Bloc in the recent past. Russia committed to modernizing its national accounting system during the period of transition from the central planning system to the market economy. Over the past two decades, the country was able to develop the