



KATHOLISCHE UNIVERSITÄT  
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**The Effectiveness of Segment Disclosures under the  
Management Approach: Empirical Evidence from Europe**

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*“Segment information is one of the most vital aspects of financial reporting for investors and other users.” (Veron, 2007 p.4)*

## **1. INTRODUCTION**

Disaggregated information by business lines and geographical areas is indispensable to adequately evaluate the performance of multinational and diversified firms (e.g. Ahadiat, 1993; Baldwin, 1984). This segmental information complements consolidated financial statements by informing financial statement users about the firms’ various sources of risk and prospects for growth. It is therefore considered fundamental to the investment analysis process and ranks as one of the most important information types for investors and analysts (e.g. Epstein and Palepu, 1999; PwC, 2007). While the importance of segmental information is beyond question, the question of how to mandate effective standards for segment reporting has been a contentious topic ever since segment reporting became mandatory within United States Generally Accepted Accounting Principles (U.S. GAAP) and International Financial Reporting Standards (IFRS). The history of segment reporting standards is therefore characterized by different concepts and constant adjustments of segmental disclosure requirements.

In November 2006, as a result of a short-term convergence project with the Financial Accounting Standards Board (FASB), the International Accounting Standards Board (IASB) issued IFRS 8, which adopts the American standard for segment reporting Statement of Financial Accounting Standard (SFAS) 131 within U.S. GAAP almost verbatim. This new standard follows the so-called management approach, which mandates the disclosure of segmental information in accordance with a firms’ internal reporting structure to its Chief Operating Decision Maker (CODM). By requiring the disclosure of the same information that the firms’ executives use for their decision-making, IFRS 8 led to significant changes in the segment reporting practice of IFRS-applying firms.

In Europe, these changes triggered a contentious debate surrounding the endorsement of IFRS 8 into European law. Critics argued that IFRS 8 would contradict the criteria of understandability, reliability, and comparability that are required for IFRS adoption into European law (e.g., Crawford et al., 2014). In particular, critics were concerned about the inherent leeway allowed by the standard to influence the quantity and quality of segment disclosures, including the possibility to disclose Non-IFRS segment data (e.g., Veron, 2007). Proponents of the standard, however, argued that IFRS 8 would enable financial statement users to evaluate the firm „through the management’s eyes“ (IASB, 2006), thereby highlighting the risks and opportunities that management believes are important for their decision-making.

While the European Parliament eventually endorsed IFRS 8, the contentious debate continues as a growing body of research provides inconclusive evidence about the effectiveness of IFRS 8 in Europe.

Prior research mainly compares segment disclosures under IFRS 8 with disclosures made under its predecessor standard. These studies find a slight increase in the average number of reported segments and more country-specific disclosures under IFRS 8 (e.g. Aleksanyan and Danbolt, 2015; Cereola et al., 2017; Kang and Gray, 2013; Lucchese and Di Carlo, 2016; Pisano and Landriani, 2012), but also a considerable decline in the average number of segment-level line items (e.g. Bugeja et al., 2015; Crawford et al., 2012; Franzen and Weißenberger, 2015; Leung and Verriest, 2015; Nichols et al., 2012). Also, there is no improvement in the consistency between the segment report and firms' other publications after IFRS 8 adoption (Crawford et al., 2012; Nichols et al., 2012). In line with these findings, there is also inconclusive evidence on the economic consequences of segment disclosures under IFRS 8 compared to its predecessor standard. While prior studies find no significant changes in analyst forecast accuracy (Bugeja et al., 2015; Franzen and Weißenberger, 2018; Leung and Verriest, 2015), market liquidity or firms' cost of equity capital (Leung and Verriest, 2015), there is some evidence of decreased information asymmetry following IFRS 8 adoption (Kajüter and Nienhaus, 2017). In addition, the results of Aboud et al. (2018) suggest that IFRS 8 improves analysts' information environment, while André et al. (2016) demonstrates that analysts struggle to understand segment disclosures under the management approach. Motivated by the inconclusive evidence of prior research, this thesis aims to provide novel evidence on the effectiveness of IFRS 8 by focusing on the determinants and consequences of segment disclosures in Europe.

## **2. OBJECTIVES OF THE THESIS**

This thesis follows three specific objectives. The *first objective* of this thesis is to provide novel empirical evidence on the determinants of segment disclosure under IFRS 8 in Europe. Investigating the determinants of segment disclosure characteristics is important to understand managers choices under IFRS 8 which helps to identify aspects of the standard that might hinder its effectiveness. Prior research on segmental disclosure choices in Europe is either descriptive (e.g. Moldovan, 2014; Nichols et al., 2012) or does not take country characteristics into account (André et al., 2016; Nichols and Street, 2007). This thesis provides novel evidence by exploring the role of cultural secrecy for segmental disclosure characteristics.

The second objective of this thesis is to provide novel empirical evidence on the economic consequences of segment disclosures under IFRS 8 in Europe by investigating their usefulness for financial statement users. Prior studies investigate whether IFRS 8 provides more useful information than its predecessor (e.g. Bugeja et al., 2015; Franzen and Weißenberger, 2018; Kajüter and Nienhaus, 2017; Leung and Verriest, 2015) or how the usefulness of segment data is influenced by its qualitative and quantitative characteristics (e.g., Aboud et al., 2018; André et al., 2016). This thesis provides more nuanced evidence by investigating the usefulness of Non-IFRS segment data, thereby providing insight into the validity of the basic premise of IFRS 8 that information used by firms' management automatically represents the most useful information for financial statement users.

The third objective of this thesis is to analyze the consequences of current regulatory initiatives to improve segment disclosures from the firms' perspective. This enables a regulatory perspective about the effectiveness of IFRS 8 as well as an assessment of foreseeable amendments for the preparer of financial statements. This thesis explores the potential impact of the IASB's proposed amendments to IFRS 8 as presented in the Exposure Draft ED/2017/2 for European firms.

Collectively, these three objectives contribute to provide novel evidence on the effectiveness of IFRS 8 in Europe from the perspective of preparer and user of financial statements. This thesis is a collection of two empirical studies and one essay. These three papers are outlined in Table 1.

### **3. OUTLINE OF THE CUMULATIVE THESIS**

The first study – **“To Reveal or Not to Reveal? The Influence of Cultural Secrecy on Discretionary Disclosure Decisions”** – examines whether cultural secrecy influences segment disclosure quantity and quality. To measure cultural secrecy, I construct a secrecy variable based on the cultural dimensions developed by Hofstede (1980). Segment disclosure quantity is measured with a self-constructed voluntary disclosure index and disclosure quality is measured with the cross-segment profit variability measure proposed by Ettredge et al. (2006). Using 2,839 firm-year observations for disclosure quantity and 1,712 firm-year observations for disclosure quality, I find strong empirical evidence that cultural secrecy influences both disclosure characteristics. After controlling for various other confounding effects, I demonstrate that cultural secrecy has a negative effect on segment disclosure quantity and quality. In doing

so, this study addresses the first objective of this thesis: to provide novel empirical evidence on the determinants of segment data under IFRS 8 in Europe.

The second study – **“The Usefulness of Non-IFRS Segment Data”** – examines the usefulness of segment data that is not prepared under IFRS measurement and recognition principles. More specifically, I investigate whether these Non-IFRS segment data are useful for financial analysts to forecast future firm performance. Using hand-collected segment data for 2,977 firm-year observations from 17 European countries, I find strong empirical evidence that Non-IFRS segment data lead to less accurate analyst forecasts. Further empirical analyses indicate that this negative effect on forecast accuracy stems from adjustments in IFRS measurement rather than IFRS recognition principles. Moreover, I find that Non-IFRS segment data are associated with a higher dispersion and uncertainty in analysts’ forecasts, as well as a lower precision in their public information set. This study thereby addresses the *second objective* of this thesis: to provide novel empirical evidence on the economic consequences of segment disclosures under IFRS 8.

The essay – “Exposure Draft of the IASB to amend IFRS 8 „Operating Segments“– Analysis of the Impact on the Preparer of Financial Statements” (published in German as **“Entwurf des IASB zu Änderungen an IFRS 8 Geschäftssegmente – Analyse der Auswirkungen auf den Jahresabschlusssteller”**) – examines the potential impact of the IASB’s proposed amendments to IFRS 8 from firms’ perspective. The Exposure Draft ED/2017/2 addresses several issues that were raised during the post-implementation review of IFRS 8, including the definition and identification of the CODM, the identification of reportable segments, aggregation criteria for reportable segments, voluntary segmental information, segment reconciliations, and the restatement of previously reported information. Overall, I find that the IASB’s proposed amendments of IFRS 8 would benefit the preparer of financial reporting. The modest amendments would assist firms in preparing their segment report by providing several clarifications and examples on critical accounting topics while at the same time limiting additional costs for preparing the segment report. This essay addresses the *third objective* of this thesis: to analyze the consequences of current regulatory initiatives to improve segment disclosures from the firms’ perspective.

## **4. CONCLUSION**

This thesis is a collection of three papers and provides novel evidence on the effectiveness of IFRS 8 in Europe.

In the first paper, I find that segment disclosure quantity and quality are significantly influenced by cultural secrecy. This finding suggests that the inherent discretion of IFRS 8 created by the requirement to report internally used information is exploited in line with managers' cultural preference for secrecy. Thus, my findings challenge the idea that the management approach is a suitable concept outside culturally transparent areas, such as the United States.

In the second paper, I find that Non-IFRS segment data lead to a lower precision in analysts' public information set and are associated with higher forecast errors, dispersion, and uncertainty. Moreover, I show that this negative effect on analysts' information environment stems from adjustments from IFRS measurement rather than IFRS recognition principles. These findings cast doubt on the usefulness of Non-IFRS segment data and, more broadly, on the basic premise of IFRS 8 that information used by firms' management automatically represents the most useful information for external users.

In the third paper, I find that the IASB's proposed amendments of IFRS 8 would benefit preparer of segment reports by giving them more application guidance in terms of CODM identification, segment reconciliations, and segment aggregation. This finding suggests that these aspects of IFRS 8 are ambiguous and not fully understood by the preparer of segment reports.

Collectively, the findings of this thesis contribute to the literature on the effectiveness of IFRS 8 in Europe by focusing on the determinants segment disclosures and their consequences on user and preparer of financial statements.

**Table 1**  
 Outline of the cumulative thesis “The Effectiveness of Segment Disclosures under the Management Approach: Empirical Evidence from Europe”

<b>Study</b>	<b>Objective</b>	<b>Research Question</b>	<b>Main related literature</b>	<b>Key Findings</b>
Chapter II: To Reveal or Not to Reveal? The Influence of Cultural Secrecy on Discretionary Disclosure Decisions	To provide novel empirical evidence on the determinants of segment disclosures under IFRS 8 in Europe	Does culture influences managers’ discretionary segmental disclosure decisions?	Gray (1988) Tsakumis (2007) Hope (2003)	Cultural secrecy leads to lower quantity and quality of segmental disclosure
Chapter III: The Usefulness of Non-IFRS Segment Data	To provide novel empirical evidence on the usefulness of segment disclosures under IFRS 8 in Europe	Are Non-IFRS Segment Data useful for financial analysts?	Barron et al. (1998) Wang and Ettredge (2015)	Financial analysts provide less accurate forecasts for firms reporting Non-IFRS segment data. This negative effect is mainly driven by adjustments to IFRS measurement principles
Chapter IV: Exposure Draft of the IASB to amend IFRS 8 “Operating Segments” – Analysis of the Impact on the Preparer of Financial Statements	To analyze current regulatory initiatives to improve segment reporting in Europe from firms’ perspective	How would the IASB’s potential amendments of IFRS 8 affect preparer of financial statements?	Franzen and Weissenberger (2015) Weissenberger et al. (2013)	The IASB’s proposed amendments would benefit preparer of financial statements by providing several clarifications and examples on critical accounting topics.



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## **6. BOOK OF ABSTRACTS**

# To Reveal or Not to Reveal? The Influence of Cultural Secrecy on Discretionary Disclosure Decisions\*

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## ABSTRACT

Prior studies on the relationship between culture and discretionary disclosure fail to account for concurrent managerial incentives to reveal private information to the capital market. Our study extends the literature by investigating whether these managerial incentives offset a cultural influence on managers' discretionary disclosure decisions. To this end, we exploit a setting in which managers have the discretion to influence both the quantity and quality of disclosure and can thereby either conceal or reveal private information. For a sample of European firms, we find that, despite incentives to reveal private information, managers' culturally determined preference for secrecy leads them to provide a low quantity as well as a lower quality of disclosure. Our results are robust to several sensitivity checks and demonstrate the relative importance of the cultural influence on discretionary disclosure decisions.

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*Keywords: Culture; Secrecy; Discretionary Disclosure; Managerial Decisions*

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# The Usefulness of Non-IFRS Segment Data\*

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Journal of International Accounting, Auditing and Taxation*

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## ABSTRACT

A controversial aspect of International Financial Reporting Standard (IFRS) 8 allows firms to define their segment profit (or loss) on a different basis than IFRS measurement and recognition principles, but whether these non-IFRS segment data are useful is in large part unexplored. We fill this gap by investigating the usefulness of non-IFRS segment data from the perspective of financial analysts. Using hand-collected segment data on a sample of European multi-segment firms, we find empirical evidence that non-IFRS segment data lead to less accurate analyst forecasts. Additionally, we find that non-IFRS segment data are associated with higher forecast dispersion, higher uncertainty in analysts' forecasts, and a lower precision of analysts' public information set. Collectively, our findings suggest that non-IFRS segment data impair analysts' information environment, which casts doubt on their usefulness.

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*Keywords: IFRS 8; Management approach; Segment reporting; Non-IFRS segment data; Analysts; Forecast accuracy*

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# **Entwurf des IASB zu Änderungen an IFRS 8 Geschäftssegmente – Analyse der Auswirkungen auf den Jahresabschlusssteller\***

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## **ABSTRACT**

Im ED/2017/2 schlägt das IASB Änderungen an IFRS 8 und IAS 34 vor. Die Änderungsvorschläge betreffen neben mehreren Klarstellungen auch zusätzliche Anhangangaben hinsichtlich des Chief Operating Decision Makers, einer inkonsistenten Segmentierung sowie der Anpassung von Vergleichsperioden nach einer Änderung der Zusammensetzung der Segmente. In dem Beitrag werden die Änderungsvorschläge analysiert und gewürdigt.

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*Keywords: IFRS 8; Management approach; Segmentberichterstattung; IASB, Exposure Draft*

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