

Impact of Audit Committee on Real Earnings Management: Cases of Netherlands

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Abstract : Regulators highlight the importance of the Audit Committee (AC) as a key internal corporate governance mechanism. One of the most important roles of this committee is to oversee the financial reporting process. The purpose of this paper is to examine the link between the characteristics of an audit committee and the financial reporting quality by investigating whether the characteristics of audit committees are associated with improved financial reporting quality, especially the Real Earnings Management. In the current study, a panel data from 80 nonfinancial companies listed on the Amsterdam Stock Exchange during the period between 2010 and 2017 were used. To measure audit committee characteristics, four proxies have been used, specifically, audit committee independence, financial expertise, gender diversity and AC meetings. For this research, a linear regression model was used to identify the influence of a set of board characteristics of the audit committee on real earnings management after controlling for firm audit committee size, leverage, size, loss, growth and board size. This research provides empirical evidence of the association between audit committee independence, financial expertise, gender diversity and meetings and Real Earnings Management (REM) as a proxy of financial reporting quality. The study finds that independence and AC Gender diversity are strongly related to financial reporting quality. In fact, these two characteristics constrain REM. The results also suggest that AC- financial expertise reduces to some extent, the likelihood of engaging in REM. These conclusions provide support then to the audit committee requirement under the Dutch Corporate Governance Code rules regarding gender diversity and AC meetings.

Keywords : audit committee, financial expertise, independence, real earnings management

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