



## Influence of the Audit Committee on the Quality of Financial Reports

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## ABSTRACT

In recent years, the global economy has been going through a severe downturn, which has led to the failure of several banks and corporations as well as a wide range of other financial problems. During those difficult times, its financial reports received a great deal of attention in many nations. The greatest worry was over the quality of such reports as well as the volume of their reporting and to what extent do they impact the worth of a particular firm or organization. The reporting of financial information has a significant impact, not only on the global financial markets but also on the financial information of firms. This is where the audit committee comes in; it is the body that is responsible for the reporting of financial information.

The data will be gathered during the distribution of the survey via the use of google forms with a sample size of three hundred and fifty respondents for the purpose of data collection. For the sake of statistical analysis and the validation of hypotheses, the data that was obtained will be evaluated using google forms.

It was determined in this study how many different features of AC impact financial reporting made by Lebanon-based firms. A survey was administered to 350 people as part of this study in order to gather data. Statistical software was used to examine the relationship between the independent variables (size, experience and independence of the AC) and their dependent variable (quality of financial reports of companies) on the one hand.

**Keywords:** Audit Committee Size, Independence, Experience, Quality of financial reports, Meetings

## **Research Background**

As a direct consequence of the worldwide economic crisis that occurred over the last few years, a significant number of financial institutions and organizations have been forced into bankruptcy and have experienced severe financial problems. During those challenging times, a lot of attention was focused on financial reports in many different countries. The biggest concern was the quality and quantity of such reports, as well as the degree to which they affect the value of a particular company or organization.

According to Lin & Hwang (2010), the financial reports of a firm and the information that is included in them have a big influence on the global financial markets, and the audit committee plays a vital role in the process of determining how this information is used. In accordance with Mangala & Isha (2016), the responsibilities of the audit committee include financial reporting (including internal controls), auditing, and oversight of other processes. For example, the audit committee is responsible for facilitating communication between the board and the external auditor.

## **Research Problem**

Audit committees are responsible for monitoring the board of directors' decisions on the hiring and firing of external auditors, as well as providing advice to the board on such matters according to Hamdan & Mushtaha (2011). To ensure that the company possesses appropriate accounting rules, adequate internal controls, and external auditors who can prevent fraud and promote timely and high-quality financial statements by performing these responsibilities, it is the responsibility of the audit committee to ensure that the company has adequate external auditors.

According to the findings of earlier studies, the quality of the financial reports may be improved by establishing an audit committee. Audit committees were more likely to be established in larger companies, businesses with Big Eight auditors, organizations with lesser management equity ownership, and firms with a higher share of outside directors according to Hamdan et al (2012). Audit committees were also more likely to be established in firms that had a higher share of outside directors prior to the necessity for an audit committee. According to Chedid & Chaya (2020), the value of financial reporting may be improved with the implementation of an audit committee as per

Baxter & Cotter (2009) enterprises engaged in financial fraud were less likely than other types of organizations to have audit committees at the time the scam was being carried out.

Audit committee effectiveness must be studied in terms of its effectiveness when it comes to the quality of financial reports, as well as the characteristics of the audit committee, and it must be shown to what extent these characteristics are related, either directly or indirectly, to the quality of the financial reporting process in Lebanon due to the financial distress and overall economic crisis according to Amrah & Obaid (2019).

### **Quality of Financial Reporting**

An essential part of the contemporary company model is the reporting of financial information. In addition to the legal responsibilities for financial reporting, it is important to understand the untapped potential and the power that a strong knowledge of it may provide. This is something that has to be realized in addition to the legal obligations. According to Everitt & Skrondal (2010), a more transparent capital market, reduced levels of uncertainty, an accurate depiction of the current state of the financial situation of economic entities, disclosure of information on management problems, and a plethora of other benefits are directly attributable to the availability of accurate accounting information to the general public.

An organization's financial position, net income, and net cash flow may be accurately depicted using the accounting system, which forms the foundation for the following: what Moilah & Talukdar (1998) claim to be the activity of market players in the capital markets. Financial reporting is the method through which an organization's financial results are disclosed to the general public. There are four main types of financial reporting: financial statements, which include an income statement, balance sheet, and statement of changes in equity; financial statements disclosures, which provide additional information on certain topics defined by the relevant accounting framework; annual reports that are distributed to shareholders; and pro forma financial statements, which provide additional information on certain topics defined by the relevant accounting framework.

There are several benefits to providing high-quality financial information to stakeholders, particularly those who are involved in the process of deciding how to

invest their money. Qualitative financial information is critical for making informed investment choices in the capital markets. It is only by stating this purpose that qualitative features of financial statements may be detected, according to Menon and Williams (2001), financial reporting goals underline the importance of financial information quality. Identifying qualitative features of financial accounts is possible only after stating this goal.

It is important to note that financial statements are used to offer information that is both retrospective and predictive; the major goal of financial reports is to identify profitability indicators and the components that make up those indicators. The key determinant of a discipline's value is the quality of its financial accounting. As a consequence of my investigation into the relevant literature, I've learned that the accuracy with which financial reports convey information to present and future investors about expected cash flows is one aspect of accounting information quality according to Joo et al (2011).

However, reporting quality is a measure of the degree to which a company's financial reports convey both the company's present economic status and its performance during the reference period. It is commonly accepted that high-quality accounting information is necessary to enhance the quality of financial reporting. Indicating the degree to which persons who use financial statements may be influenced by relevant information, this feature is available. Studies thus far have shown that operationalizing relevance may use information's predictive, confirmation, utility, and feedback values all in one go. Users may utilize financial data to make predictions about the future based on predictive and confirmatory value.

This technique is supported by Chalhoub (2009) methodology for evaluating and contrasting the quality of information held by diverse organizations, which was developed in parallel with this method. The International Accounting Standards Board's project for 2008 was titled "An Improved Conceptual Framework for Financial Reporting." According to the Bédard & Gendron (2010), notion, financial information may be beneficial if it has attributes such as relevance, reliability, comparability, verifiability, timeliness, and understandability. After this study has been finished, a discussion will take place about how prior literature has operationalized these

qualitative traits, which are currently one of the strongest bases for assessing accounting information and the accuracy of financial reporting.

According to Bozec (2005), the truthful depiction of financial reporting information or its dependability may be assessed using the following criteria: neutrality, completeness, the lack of considerable inaccuracy, verifiability, and control. These criteria were developed. Because the annual report has to correctly and painstakingly document each and every occurrence and transaction that takes place inside an economic unit, these elements need to be scrutinized. It is the capacity to compare two or more economic events, two or more financial measures of multiple financial entities in the same reporting period or for the same organization, that is the characteristic of comparability. This allows users to compare and contrast two financial metrics of different financial entities in the same reporting period or for the same company according to Bradbury & Reason (2003).

Because of the audit, shareholders and creditors of the firm now have the peace of mind to know that its financial situation is in excellent hands. Auditors are responsible for protecting the general public from businesses that engage in unethical business practices or misrepresent financial statements in order to defraud investors. The following aspects have been operationalized as a result of a variety of research projects conducted by authors who were interested in learning what people who read financial reports believed. It is essential to keep in mind that the findings in Bala et al (2019) are derived from the opinions of professional accountants, users, and preparers of accounting information in Iran in relation to each of the fundamental and enhancing quality features.

They developed an appropriate questionnaire that contains questions on the current state of Iran's financial reports' quality qualities and included them in the questionnaire. In order to analyze the data that was obtained, post-hoc tests such as Kruskal-Wallis and Friedman were used. According to Asuquo (2012) results, qualitative qualities play an important part in improving the quality of reporting; yet, it seems that the perspective of preparers and accountants towards qualitative accounting characteristics is often rather different from one another. The study conducted by Abbott et al (2004), on auditors' impressions of the quality of financial reports led to the discovery of the major factors that influence and improve the quality of financial reports one year later. When

it comes to determining whether or not financial accounts are accurate and comprehensive, auditors place a high emphasis on qualitative aspects, according to the findings of a research that was carried out in Greece.

Alabdullah et al (2019) conducted an investigation on how the managers of Iranian medical universities viewed the financial reports of their institutions and whether or not the reports provided factual information. The findings of Bedard et al (2004), which were consistent with those of other studies, suggested that financial reports have to include information that is of a high level, in addition to being accurate, simple to understand, up to date, verifiable, and similar. There has been a growing body of research that examines the perspectives of financial users on the quality of financial reporting and the use of qualitative qualities in the assessment of the quality of financial reporting. One of the main focuses of this research has been on the use of qualitative qualities.

Increasing the reliability and accuracy of financial reporting is one way to increase the quality of financial reporting; however, this should not be done at the cost of other factors such as relevance, comparability, and understandability. The majority of respondents do not have faith in financial reports that were created by firms since their needs for information as stakeholders were not met by the financial reports that were provided by corporations. The article recommends that information should be delivered in the most trustworthy fashion possible, that it should be comprehensible, comparable, and timely, and that it should be verifiable. This would allow for financial reporting to be relevant to the general public and helpful to them. Several studies that were conducted not too long ago Bryman & Stephen (2015), looked at the accuracy of the financial reporting and the degree of openness that was present in Albania's yearly reports. However, in the vast majority of these studies, the opinions of customers on the accuracy of financial reporting, especially in Albanian businesses, were not taken into account.

The survey being conducted for this project will gather the first tangible data on how respondents from Albania view financial reporting. According to Chanawongs et al (2011), some of the target demographics for the polls include government agencies, financial institutions (both public and private), non-financial organizations (non-profits), and academic institutions according to Davidson et al (2005). In general, the



results of the survey indicate that there has been a significant advancement in the quality of financial reporting over the course of the past five years.

As a consequence of these remarks, it is abundantly clear that the reporting of financial information has to be improved by the provision of additional, more in-depth information on risk exposure as well as risk management in order to choose the most effective next step. Reduce the chances of a catastrophic financial loss occurring. According to the findings of the Deloitte 2018 User Survey, corporate executives are "hungry" for high-quality financial reports, which according to accounting experts both leaves opportunity for the inclusion of information and supports the growth of financial reporting. When revealing facts to customers, there are a few fundamentally important subjective elements that are essential for the decision-making process. These include the following: Comparisons were made between a range of different subjective characteristics and difficulties that are present in data detailing for administration. On this particular list, the terms "comparability," "relevance," "timeliness," "independence," and "verifiability" may all be found.

According to Dita & Murtaqi (2014) careful selection of five key qualitative characteristics (faithful representation; relevance; timeliness; comparability; and understandability); as well as the secondary indicators that corresponded to each of these primary characteristics according to Dita & Murtaqi (2014), the research of El Khoury (2018) established an evaluation system for qualitative financial reports in China.

According to study carried out by Maher & Andersson (2018), top and middle management's perspectives on the quality of financial reporting in Ghanaian enterprises following the introduction of the International Financial Reporting Standards were evaluated. This research was carried out in Ghana (IFRS). In the context of this investigation, a questionnaire assessing the quality of financial reporting along five dimensions was developed in accordance with the relevant research. It was common practice for managers to put a higher priority on the quality of a product than on its on-time delivery.

## **Relevance**

The "importance" of financial data has been operationalized in terms of its predictive and confirmatory value in order to establish its relevance Bremer et al (2011). This has allowed for the determination of whether or not the data is relevant. Academics have a preference for focusing on the quality of profits rather than the quality of financial reporting, rather than taking into account the value of non-financial information and the possible use of "future financial information" by readers of annual reports Defond et al (2018). As a consequence of this, this aspect will be addressed in great detail in the questionnaire that will be deployed in the course of this study, taking into account information that is both financial and non-financial in nature.

## **Faithful Representation**

On the other hand, in order to provide an accurate picture, the facts about the finances need to be exhaustive, impartial, and devoid of mistakes according to Aggarwal (2013). In order to provide an accurate depiction of the current economic situations, all of the data that is essential, along with all of the accompanying notes that outline the methodology and accounting methods that were utilized, must be included in the financial reports. In order to maintain a reputation for objectivity, financial information must never be altered in any way that could influence the decisions made by customers. If financial reports are to become error-free, then they must be error-free while describing a phenomenon and the process by which financial information was created. In other words, they must not include any errors.

Users are unable to make good decisions if the phenomenon being judged is portrayed in a way that is either true or not accurate, and whether it is significant or not significant-Allegrini et al (2011). As a result of the fact that financial statements include information that can be compared either between different reporting periods or between different businesses within the same reporting period, this information is beneficial to those who are in charge of making business choices according to Barth et al (2008).

## **Comparability**

A property referred to as "comparability" describes the degree to which two or more things are comparable to one another and the degree to which they differ from one another. According to Deli and Gillan (2000), the operationalization of comparability

may be determined, according to Dhaliwa et al (2010). As a consequence of this, Gul et al (2011) devised a model with six components. Four of these components are based on the consistency of adopting the same accounting standards and procedures inside a business, and two of these components are based on comparing current enterprises in the market. In addition, in their analysis of comparability, Barbadillo et al (2007) looked at the comparability of accounting policies and estimates, relevant comparative data, and the impact of accounting policy changes. They also looked at financial indices and reports, information on shareholders' investments, and data related to industry and competition.

Accounting comparability is said to have an influence on the quality of financial reporting, as well as the degree to which readers of financial statements grasp the effect that corporate accruals have according to Bauer et al (2009). Even though managers could better estimate accumulated costs with more accuracy and get access to their private information, they also hoped that comparability would help investors better understand accounting charges. This was the case despite the fact that managers could better estimate accumulated costs with more accuracy.

### **Verifiability**

Verifiability assures that the financial information shown in financial statements properly represents the economic circumstances it is designed to represent. This is the responsibility of the entity that maintains the financial statements. It is widely accepted that Al-Mamun et al (2014) were the first to apply the conceptual framework of Abbott et al (2000) to qualitative aspects as a means of assessing the quality of financial reporting. As a consequence of this, they examined the quality of financial reporting from two primary vantage points: first, the usefulness of financial information to users (broadly defined as investors and creditors), and second, the concept of shareholder and investor protection. Both of these vantage points are extremely important. As a consequence of this, high-quality financial reporting makes an effort to fulfill the requirements posed by customers by providing data that is truthful, dependable, and credible.

## **Timeliness**

Research has operationalized a number of different approaches to the quality improvement characteristic known as timeliness. This is in addition to the other aspects of quality improvement. According to DeZoort & Salterio (2001), one of the primary objectives of timely financial reporting is to raise the standard of financial reporting by making it as easy as possible for decision makers to get the information as quickly as feasible. According to this procedure, the difference in dates between the end of the fiscal year and the date of the auditor's report is utilized to estimate this sum.

Many people believe that the length of time it takes to make available financial information is directly related to the timeliness of the reporting of financial information. Hamdan (2020) disagrees with this view. For the purpose of this component, Amdan et al (2013) decided to use a natural logarithm to determine the number of days that passed between the conclusion of the fiscal year and the "signing" of the auditors' report after the end of the fiscal year.

## **Understandability**

Information in financial accounts is presented in a manner that individuals who use them may readily grasp it, according to the following qualitative understandability factor. This is done so that financial statement users may quickly get the information they need.

Karamanou & Vafeas (2005) explain that the goal of standard-setting is for customers to be able to read financial statements and understand the information presented in them, as well as other economic organizations' financial statements. Moreover, standard-setters also want to make sure that financial statements use the same terminology and presentation manner. Understanding is a four-step process that begins with a well-structured annual report, a balance sheet entry, and an income statement, as well as the availability of tables and graphs. Verifiability is a major improvement feature for qualitative financial reporting, and this has been identified and evaluated as a key improvement characteristic. When information can be reliably repeated, it demonstrates that it consistently directs individuals to the same findings. The value of information increases when it can be independently confirmed by many sources.

## **Empirical Literature**

Accurate financial reporting relies heavily on the AC, which has been identified by researchers such as Kipkoech & Joel (2016). Internal control systems and the creation of financial statements, together with other techniques of control, are clearly vital in monitoring and overseeing management Lloyd (2009). Even little research has been carried out on how AC affects financial reporting's quality, and even less has been done experimentally.

### **The Impact of Audit Committee Size on Quality of Financial Reporting**

When evaluating the performance of a firm as well as the credibility of its financial statements, it is essential to take into consideration the composition and size of the audit committee (AC). This was determined by the number of people on the AC. The larger the AC, the more varied its knowledge base will develop, and the more effective their job will be as a result. In their investigation, Hsu & Petchsakulwong (2010) discovered a fascinating connection between the quality of financial reporting and the size of the AC.

According to Maina et al (2017), advisory committees that have less than three members have a greater risk of failing. Within its 10 suggestions on the AC, the Akhtaruddin & Haron (2010) organization said that an effective AC of publicly listed companies should consist of at least three directors. According to the findings of study carried out by DeZoort et al (2002), the most effective ACs have between three and four members. According to Hassan and Bello (2013), the quality of financial reporting produced by an AC suffers if the number of directors participating on the committee is inadequate. This is because a smaller committee means fewer eyes on the books. It is possible that having a smaller committee will make it more difficult for the directors to carry out their responsibilities in an effective manner. On the other hand, having a committee that is too large can lead to issues with coordination and procedural concerns, revealing yet another factor that contributes to poor management.

Members of the AC are more informed than members of a smaller committee since the AC has a bigger number of knowledgeable members than the smaller committee does. Nevertheless, if there are so many people on the committee, the AC's efficiency can be affected. The distribution of processes and responsibilities is out of control due to the

fact that a large committee has the ability to cause extra losses. It has been established that determining the appropriate size of an AC may considerably enhance the quality of financial reporting.

According to the findings of Marcel (2013), the optimal number of members for a corporation is somewhere between three and four. A group of writers from across the globe looked at the variation in AC size that exists not just in rich nations but also in developing ones. They came to the realization that they had a healthy connection. The first hypothesis is constructed as follows, taking into account the results from the prior research:

**H<sub>1</sub>: There is a positive relationship between Audit Committee Size and quality of financial reporting.**

### **The Impact of Audit Committee Independence and Quality of Financial Reporting**

As an independent auditor, you are required to generate profits, advise the firm on how to make sound financial choices, and verify the integrity of the company's financial accounts. ACs serve as a factor that contributes to the maintenance of the independence of both internal and external auditors, and it is anticipated that independent ACs will be more successful in the following areas: According to Boo & Sharma (2008), one of the most significant qualities of an auditing firm is its independence. Internal auditors should, as a general rule, avoid having any direct contact with the workers or management of the business they are auditing; otherwise, their findings and recommendations will be seen as dubious and suspicious.

Therefore, it is very necessary that the objective and goal of the internal audit be accomplished by maintaining a certain degree of independence. In order to ensure that businesses may gain a lot from their operations, the Sarbanes-Oxley Act from 2002 mandates the establishment of independent Audit Committees in all publicly traded corporations. Furthermore, according to Anderson et al (2003), the company's independence from the AC has an effect on the quality of the financial reports that are produced by the business. Previous research indicates that an increasing number of independent AC is highly connected with a rise in the quality of financial reporting. In addition, others believe that a wholly independent AC would be in a better position to safeguard the interests of shareholders and carry out its responsibilities since such a

body would have a more objective point of view. This leads to the development of the second hypothesis as follows:

**H<sub>2</sub>: There is a significant relationship between the independence of AC members and quality of financial reports.**

### **The Impact of Audit Committee Member's Experience on Quality of Financial Reporting**

Members of the AC benefit from their financial expertise by being able to dig deeper and ask more probing questions that push management and external audit to raise the bar on financial reporting performance and quality.

It follows that financial experts on the AC contribute to a better quality of financial reports because of their involvement in the AC. Auditors who have specific expertise in the subject are believed to have a better understanding of both performance and dangers than auditors who do not have this information. Research shows that members of the AC with accounting or financial experience are more helpful in auditing results and also decrease conflicts among auditors, both of which have a favorable influence on the quality of financial reports. Accounting and finance are two of the most popular fields of auditing knowledge, thus this is understandable.

For instance, according to Anderson et al (2003), a financially literate advisory committee (AC) is comprised of individuals who are able to read, comprehend, and analyze financial data. Abilities in internal auditing, accounting, and control all contribute to the level of success that may be achieved with AC. In order for members of the AC to successfully complete their obligations and contribute to the expansion of the AC as well as the bottom line of the company, they need to have the necessary skills and expertise.

As a consequence of this, each of the aforementioned research has shown a positive association between the amount of experience that AC members have and the quality of the financial reports. Accordingly, the following hypothesis is constructed as a result:

**H<sub>3</sub>: There is a significant positive relationship between the experience of AC members and quality of financial reports.**

## **The Impact of Audit Committee Member's Frequency of Meetings on Quality of Financial Reporting**

Members of the AC benefit from their financial expertise by being able to dig deeper and ask more probing questions that push management and external audit to raise the bar on financial reporting performance and quality. Members of the AC who have competence in accounting and financial management, internal controls, and auditing are expected to contribute to the body's collective knowledge.

The Sarbanes-Oxley Act of 2002 mandates that a member of the Advisory Committee have considerable financial expertise. the majority of the advisory committee must have financial competence, as stipulated by Bahrain's Corporate Governance Code (CGC). If financial experts were included on the committee, it is probable that the AC's capacity to enhance financial reporting and performance would be increased, according to Hamdan (2020). Financial experts are likely to increase the AC's financial reporting quality as a result of their contributions to the AC, according to results from the research. More experienced AC members are regarded to have a better grasp on performance and safety than non-experienced auditors.

Additional research has shown that members of the AC who have accounting or financial expertise are more helpful in auditing outcomes and also minimize conflicts among auditors, both of which have a positive impact on the quality of financial reports. This is due to the fact that accounting and finance are two of the most common areas of auditing expertise. It was claimed by Hamdan (2020) that an investigation was conducted by DeZoort & Salterio (2001), on the contribution of internal auditors to the quality of financial reports. Before beginning their investigation, they focused on 76 publicly listed companies in Malaysia, each of which had already developed and distributed a questionnaire to its own team of internal auditors.

Abilities in internal auditing, accounting, and control all contribute to the level of success that may be achieved with AC. In order to enhance the performance of the AC and the quality of the organization's financial reporting, the members of the AC need to have the skills and expertise necessary for their positions. The members of the AC put a great priority on having experience in accounting and financial matters. It has been shown that the AC's financial experience has a positive impact on the effectiveness



as well as the quality of the financial reports. Accordingly, the following hypothesis is constructed as a result:

**H4: There is a significant positive relationship between the experience of AC members and quality of financial reports.**

### **Data Collection**

A few instances of data collection include the systematic gathering of information and measuring of it in order to answer questions, create research participants, test hypotheses, and assess the outcomes. Primary and secondary data are the two types of information that are available. Primary data are the responses that were given to questionnaires and surveys that were administered by the researcher. It is a kind of data that is obtained through reading various pieces of published scholarly work. However, primary data was used extensively throughout this study due to the fact that it was readily available.

The data was acquired by sending out the survey using google forms to a total of 350 respondents who participated in the study for the purpose of data gathering. In order to do statistical analysis and validate hypotheses, the data obtained will be evaluated via the use of google forms.

### **Research Population, Sampling Technique and Sampling Size**

A research population is a clearly defined group of individuals who have comparable traits that the researcher plans to investigate. The people that make up a study's target population are known as the target population's accessible population, whereas the sample's accessible population is made up of all of the people who have a chance of being included in the data collected for the research.

In this particular investigation, non-probability sampling approaches were combined with non-random selection. Utilizing sampling methods that do not rely on chance is both more productive and less expensive. There are six distinct applications for the use of non-probability sampling that are feasible. Convenience, deliberation, expertise, heterogeneity, model cases, quota sampling, and snowball sampling are the terms that describe these methods. This research makes use of a technique known as convenience sampling, which occurs when the researcher chooses to take a sample from the

population that is readily available to him or her. The information was provided to a total of 400 respondents, and of them, 350 respondents who are employed in the retail sector of Lebanon completed the surveys.

### Reliability Analysis

In order to establish the reliability of this study, the Cronbach's Alpha Coefficient will be used. Conduct an investigation into and make certain of the internal consistency of the measurement items for each variable that resulted in the generation of a coefficient. The Cronbach Alpha Coefficient must be at least 0.7 in order to be considered valid. The results of Duhachek and Iacobucci's reliability study, which covers the whole questionnaire, are shown in the table below.

Table 1 Cronbach Alpha

Source: Author Work

Reliability Statistics	
Cronbach Alpha	Number of Items
0.832	15

The reliability assessment for the whole questionnaire reveals a reliability value that is equal to 0.832, which indicates a strong reliability value for the entirety of the questionnaire's questions. The results of each variable's analysis using Cronbach's Alpha are shown in the table below.

Table 2 Reliability Statistics

Source: Author Work

	Cronbach Alpha	Items
Audit Committee Size	.812	3
Audit Committee Meetings	.708	3
Independence	.720	4
Experience	.809	4
Quality of financial reports	.775	3

Alpha. Referring to the rule of thumb, it can be noted that:

- If Cronbach Alpha  $< 0.5$ , data is not validated
- If Cronbach Alpha between 0.5 and 0.7 the data is validated but contains bias
- If Cronbach Alpha  $> 0.7$  then the data are validated

By referring to the above results, it can be noted that “Audit Committee Size” scored a Cronbach Alpha of 0.812, “Audit Committee Meetings” scored Cronbach Alpha “0.708”, as for Independence it scored Cronbach Alpha 0.720, “Experience” scored a Cronbach Alpha of 0.809, “Quality of financial reports” also scored a Cronbach Alpha of 0.75. This means the variables are statistically validated as most their Cronbach Alpha are almost 0.7.

### Validity

To be called reliable, the data generated by an instrument must accurately and meaningfully reflect a theoretical concept. To put it another way, the data must take into account all important factors. Once the data has been verified, conclusions must be accurate and appropriate (Mohajan, 2017). Being able to use a wide range of facts to support a research makes it more credible (Yin, 2003)

Table 3 KMO Validity Test

Source: Author Work

Factor	KMO	P-Value
Audit Committee Size	.701	0.001
Audit Committee Meetings	.603	0.002
Audit Committee Independence	.793	0.005
Audit Experience	.672	0.025
Quality of financial reports	.685	0.036

KMO and Barlett's validity tests were employed as part of this study to determine whether or not our data sets were appropriate. A correlation matrix or a correspondence process should be used when conducting surveys based on this statistic. To be

considered accurate, a characteristic's accuracy must be more than 0.6 and its KMO variance must be between 0.000 and 1.0. It is clear from this table that all variables in the study had values of more than or equal to 0.06. As a consequence, future studies may make use of all of the parameters examined.

## **Discussion of Findings**

### **The Impact of Audit Committee Size on Quality of Financial Reporting**

When conducting an analysis of the performance of the company as well as the credibility of its financial statements, it is essential to take into account the composition and size of the audit committee (AC). This is determined by the total membership of the AC. The larger the AC, the more diverse its knowledge base will grow, and the more efficient they will be in performing their duties as a result. An intriguing association between the quality of financial reporting and the size of the AC in their study was found to exist, according to the findings of the analysis.

ACs with less than three members have a significantly increased risk of failing. At least three directors should be included in the AC's 10 recommendations for it to be considered successful in publicly traded companies.

If there are not enough directors serving on an AC's committee, the quality of the financial reports that the AC produces would suffer as a result. When there are fewer members on a committee, it may be more difficult for the directors to carry out their responsibilities in an effective manner. On the other hand, when there are an excessive number of members on a committee, this may lead to problems with coordination and procedural concerns, which reveals yet another reason for poor management.

A large AC may be able to improve financial reporting standards by relying on the accumulated knowledge of smaller committees with better competence. This may be accomplished by increasing the efficacy of the AC by recruiting members who have more experience and are more qualified.

People of the AC have access to more information than those of a smaller committee due to the larger number of knowledgeable members who make up the AC. On the other hand, if the committee is very large, the AC's efficiency may suffer as a result. The distribution of processes and responsibilities is out of control due to the fact that a large

committee has the ability to cause extra losses. It has been established that determining the appropriate size of an AC may considerably enhance the quality of financial reporting.

It is recommended that a company have between three and four individuals in order to be successful. A group of scholars from all around the world conducted research on the average AC size in both rich countries and developing countries. The first hypothesis may be considered confirmed on the basis of the data:

**H<sub>1</sub>: There is a positive relationship between Audit Committee Size and quality of financial reporting.**

### **The Impact of Audit Committee Independence and Quality of Financial Reporting**

As a result, it is thought that an independent auditor would help the company make prudent financial decisions and ensure that its financial statements are accurate. An independent auditor's capacity to strengthen the independence of both internal and external auditors is expected to make them more effective. The audit committee's independence is a crucial factor to take into account. With any kind of direct contact with employees or supervisors, an internal auditor will have his or her findings and recommendations under question.

There must be a degree of independence in an internal audit's aim and objectives. Independent audit committees are mandated by the Sarbanes-Oxley Act of 2002 to guarantee that firms get the full advantages of their operations. The company's financial reporting is also impacted by the AC's independence. According to previous studies, having more independent AC improves the quality of financial reporting. Some believe that an AC with an objective perspective, such as an independent one, would be better able to protect the interests of shareholders and fulfill its obligations.

As a result, ACs that are more autonomous outperform those that are less autonomous. The Sarbanes-Oxley Act mandates that companies create ACs that are completely independent of management. At least three members of the AC must be independent. This is the logic that underpins the BDL's primary circular. In accordance with this circular, a company's AC shall have a minimum of three non-executive directors.

Studies have shown that the quality of financial reporting by ACs is inconsistent, despite their apparent independence.

This information's asymmetries may be reduced in a variety of ways. Many non-executive members does not imply higher success. A number of studies have shown that non-executive members boost the AC's level of independence. Or, the board of directors and top management may disagree with the way decisions are made.

The AC has been given this responsibility by the board to ensure the accuracy and dependability of the data supplied by the AC. This implies that non-executive board committees may have difficulties in monitoring and supervising the company's senior executives.

It's more administratively focused than an independent examination, he added. A non-executive director on the AC raises the risk of conflicting interests and the disclosure or concealment of private information.

AC's incapacity to cope with its financial issues is connected to the presence of non-executive members on the board of directors. While one research found a link between AC independence and improved financial reporting, another found the exact reverse. as follows: Hence, the second hypotheses is confirmed:

**H<sub>2</sub>: There is a significant positive relationship between the independence of AC members and quality of financial reports.**

### **The Impact of Audit Committee Member's Experience on Quality of Financial Reporting**

Internal control over financial reporting and external audit both benefit from the expertise of AC members, who may raise more significant issues and queries throughout their work.

The Sarbanes-Oxley Act of 2002 mandates that the Advisory Committee include a financial expert. Bahrain's Board of Directors (AC) is obliged by law to be financially literate, stipulated under the Corporate Governance Code (CGC). Having financial experts on the committee enhances the AC's capacity to improve its financial reporting.

There is evidence that the AC's influence on financial reporting quality is enhanced when financial professionals are included. Compared to non-expert auditors, expert members of the AC are seen to have a greater understanding of performance and risk. AC members with accounting or financial knowledge are more helpful in audit outcomes and lowering disagreements among auditors, which has a good impact on financial reports, according to research

A member of an AC who is financially literate is one who is capable of understanding and evaluating financial information. Internal auditing, accounting, and control are critical to AC's performance. It is essential that they be skilled and experienced if they are to carry out their responsibilities effectively and contribute to the growth of both the business and their own personal finances. AC members place a high priority on knowledge in accounting and finance.

Accounting, finance, and auditing knowledge and abilities, as well as the necessary years of experience, are all included in the circular's definition of financial literacy. The AC's internal management and monitoring skills would benefit from more financially competent AC members. These results back up my claim. Thus, it has been discovered that the more experience the AC has, the greater the quality of the financial reports. As a result, the following theory has been proven correct:

**H<sub>3</sub>: There is a significant positive relationship between the experience of AC members and quality of financial reports.**

### **The Impact of Audit Committee Member's Frequency of Meetings on Quality of Financial Reporting**

Internal control over financial reporting and external audit both benefit from the expertise of AC members, who may raise more significant issues and queries throughout their work. All of the AC's experts have credentials in financial management, internal control audits and much more.

When it comes to auditing findings and eliminating conflicts among auditors, accounting or financial expertise has been shown to be more beneficial. Internal auditors' impact on the quality of financial reporting Internal auditors' opinions of their

contribution to the quality of financial reports were shown to be positively connected with their accounting and auditing expertise.

Internal auditing, accounting, and control are critical to AC's performance. If the AC wants to improve its financial reporting quality and performance, it must have members who are knowledgeable and experienced. AC members place a high priority on knowledge in accounting and finance. The AC's financial acumen has been found to have a favorable influence on financial reporting efficiency and quality. As a result, the following theory has been proven correct:

**H4: There is a significant positive relationship between the experience of AC members and quality of financial reports**

### **Summary of Findings**

Specifically, this study looked at what characteristics of the AC are and how they affect the quality of financial reports provided by Lebanon-based businesses. To obtain information, a survey was distributed to 350 participants. Analyzing the data using statistical tools helped evaluate the significance and kind of link between the independent characteristics (the size, experience, independence and frequency of meetings of the AC) and the dependent variable (quality of financial reports of companies).

Results demonstrate that four independent factors (size, independence and experience of the AC) have a significant impact on the quality of corporate financial reporting (quality of financial reports of companies). These studies suggest that as the AC grows in size, free riders and the pressure to follow the opinions of other members without studying the underlying argument would have a detrimental impact on the quality of financial reporting.

The more independent and frequent meetings there are, the better the financial reports will be, according to the study. Because of this, yearly meetings are crucial for keeping members informed about the organization's general operations, and the more meetings the AC organizes, the better it impacts committee choices, which in turn has a favorable effect on the quality of financial reporting. Small firms should pay more attention to



these characteristics since they may have a major influence on financial reports' quality and efficiency.

Members' financial skill was strongly linked to the quality of financial reports, which shows that financial expertise alone is not sufficient to enhance the quality of financial reporting. As a result, some of this may be attributed to a lack of understanding of financial and accounting practices, or at the very least, a lack of understanding of audits and internal controls. Financial reporting quality seems to be affected by the AC. The study's main purpose was met as a result of this investigation of the relationship between AC characteristics and financial reporting quality. The results of this research are important to investors, accounting professionals, owners, and policymakers because they provide a valuable framework for examining and improving the features of an AC connected with the operation of such a committee.

### **Research Contributions**

This study contributes to the expanding body of evidence that AC characteristics have an influence on the business quality of financial reports, as shown by previous research. This is supported by the results of the investigation. To contribute to AC literature, the research explored various specific aspects rather than their fundamental contributions, which few other studies have done.

Last but not least, the findings might be useful to other firms' investigations and contribute to the expanding body of information about financial reporting methods in developing nations. Studies in countries with a similar economic environment to Lebanon, particularly those experiencing financial difficulty, might utilize the findings of this research as a standard reference.

### **Research Limitations**

Despite the fact that this research adds to the body of accounting knowledge and practice, it faces a number of hurdles, especially when it comes to the reporting requirements of private companies. Due to a shortage of data, this analysis can only cover a small number of companies.

This might have an adverse effect on the research's generalizability. The conclusions of this research cannot be extended to other types of businesses or firms outside of Lebanon since the Lebanese enterprises analyzed in this study are considered financially distressed. A further limitation of this research is that it only analyzed four of the numerous attributes of an audit committee. The "behind the scenes" characteristics that affect the audit committee's qualifications and, thus, its success, are not taken into account in the research. The capacity of the audit committee to carry out its responsibilities may be hindered by the influence of management over the committee.

### **Suggestions for Future Research**

An investigation of how audit committee attributes impact financial reporting generated a number of suggestions and concerns. The audit committee's gender, years of experience as an auditor, and nationality may also be examined in future research. An investigation of how the audit committee's characteristics are linked might also be done. Additional samples from a variety of organizations should be included in future research, since the kind of industry may have an impact on the reporting.

As a consequence, future research should also include other aspects (such as educational background and years of experience) that affect the competency of audit committee members. If a bigger sample is used, and if audit committee features are connected to changes in the preliminary report, the efficacy of the audit committee may be better measured in the future. This research used ROA, an indirect measure of financial reporting quality, as a measure of financial reporting quality. Future studies should use ROE instead. Future research may examine emerging markets in developing nations and compare all of the countries engaged in those markets as they develop.

While other studies have shown the importance of members' expertise in financial reporting, this study's results are nonetheless outstanding, and it is recommended that additional research be done in this area.

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