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Effective Audit Committee and Financial Reporting Quality: the Mediating Effect of Audit Quality: Evidence from KSA

Abstract

The purpose–This study aims to examine the mediating effect of audit quality on the relationship between the effective audit committee and financial reporting quality.

Design/ methodology/ approach– The research uses multiple regression analysis to test the relationship between the effective audit committee and financial reporting quality. The sample consists of 77 non-financial firms listed on the Saudi stock market between 2014 and 2021.

Findings – Empirical findings show that studies on effective audit committees and financial reporting quality displayed mixed results. The study findings indicate that audit quality has a mediation effect on the relationship between audit committee characteristics (more oversized Audit Committee, financial expertise, frequent meetings, gender diversity, independent members) and financial reporting quality. The study findings indicate that a change in audit committee effectiveness brings a change in audit quality, and a difference in audit quality brings a shift in financial reporting quality.

Practical implications– This study has important implications for regulators and policy-makers to address the conflict between insiders and outsiders by promoting a higher standard of financial reports. The study also may be useful to investors, aiding them in financial decision-making and helping all stakeholders understand and trust the fairness and quality of financial information. In addition, it helps to understand the role that an effective audit committee plays in external audit quality and financial reporting quality. Finally, the study also contributes by bringing a new perspective on how external audit quality engages in monitoring by requesting financial reporting quality.

Originality/ value – The main contribution of the current paper is to examine the audit fees (audit quality) as a potential mediating variable between the effective audit committee and financial reporting quality.

JEL Classification G40, M41, M42

Keywords: Effective Audit Committee, Audit Quality, Financial Reporting Quality

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لجنة المراجعة الفعالة وجودة التقارير المالية: الأثر الوسيط لجودة المراجعة دليل من المملكة العربية السعودية

ملخص البحث

تهدف هذه الدراسة إلى فحص التأثير الوسيط لجودة المراجعة على العلاقة بين لجنة المراجعة الفعالة وجودة التقارير المالية. وتم استخدام تحليل الانحدار المتعدد لاختبار هذه العلاقة وذلك لعينة من 77 شركة غير مالية مدرجة في سوق الأسهم السعودية خلال الفترة من 2014 إلى 2021. وقد توصلت الدراسة إلى أن جودة المراجعة لها تأثير وسيط على العلاقة بين خصائص لجنة المراجعة (لجنة مراجعة أكبر حجمًا ، وخبرة مالية ، واجتماعات متكررة ، وتنوع بين الجنسين ، وأعضاء مستقلين) وجودة التقارير المالية، حيث تشير نتائج الدراسة إلى أن التغيير في فعالية لجنة المراجعة يؤدي إلى تغيير في جودة المراجعة، وأن الاختلاف في جودة المراجعة يؤدي إلى تغيير في جودة التقارير المالية. هذه الدراسة لها آثار مهمة على المنظمين وصانعي السياسات وتخفيض تعارض المصالح بين الداخليين والخارجيين من خلال تعزيز مستوى جودة التقارير المالية. قد تكون الدراسة مفيدة أيضًا للمستثمرين، حيث تساعدهم في اتخاذ القرارات المالية ومساعدة جميع أصحاب المصلحة على الفهم والثقة في نزاهة وجودة التقارير المالية . بالإضافة إلى ذلك ، فإنها تساعد على فهم الدور الذي تلعبه لجنة المراجعة الفعالة في جودة المراجعة الخارجي وجودة التقارير المالية. أخيرًا ، تساهم الدراسة أيضًا في تقديم منظور جديد حول كيفية مشاركة جودة المراجعة الخارجي في المراقبة من خلال طلب جودة التقارير المالية. وتعد المساهمة الرئيسية للدراسة الحالية هي فحص أتعاب المراجعة (جودة المراجعة) كمتغير وسيط محتمل بين لجنة المراجعة الفعالة وجودة التقارير المالية.

الكلمات المفتاحية: لجنة المراجعة الفعالة - جودة المراجعة - جودة التقارير المالية

1- Introduction

The bankruptcy of many major international firms, such as Enron and WorldCom, led to decreased confidence in the quality of financial reports and audit quality. Therefore, corporate governance emerged with internal and external mechanisms to regulate the relationship between management and stakeholders. Audit Committees have an essential role in ensuring the integrity and transparency of financial reporting. The financial reporting process consists of different elements that provide financial information to different parties. The role of management is to be responsible for operational processes that create shareholder value. The role of the Board is to determine the executive management's strategy and business decisions and follow up on appropriate policies and systems to control business. The external auditor's role is to express an independent and impartial opinion on the representation of the financial statements prepared by management and approved by the Board of Directors. The Audit Committee provides an internal corporate governance mechanism – a sub-committee of the Main Board of directors that coordinates between these groups. Moreover, providing a primary focus for discussions with internal and external auditors enables both sets of auditors to boost their independence. A written charter helps the audit committee and others to understand its role and responsibilities and is an essential starting point.

Financial reports are essential for managers to communicate a firm's performance and governance to external investors. Financial reporting quality has been an issue of debate for several years, and it has received significant attention from regulators and researchers (Hermanns, 2006). Therefore, high-quality financial reporting is essential because it significantly affects stakeholders' financial decision-making. The agency theory assumes that the audit committee's primary objective is to protect the shareholders' interest from management opportunism. This required hiring independent auditors to provide their independent opinions on the truth and fairness of the companies' financial reports. Therefore, an external audit can be considered a comple-

mentary method to monitor processes that can improve financial reporting quality.

Under the Saudi Governance Regulations and their last amendment in 2021, according to the Saudi Governance Manual, the general assembly of each company is the one that forms an audit committee, among which there must be at least one independent member, and none of its members must be executives. Furthermore, the number of its members should not be less than three and no more than five, and one of them is a specialist in financial and accounting affairs. In article 55 of the Saudi Governance Manual, the Audit Committee verifies the integrity of the financial reports by expressing a technical opinion on whether the financial reports are fair, transparent, and understandable. On the other hand, the Audit committee examines audit reports and notes on the financial statements and expresses its views thereon.

Several previous studies focused on the relationship between the characteristics of the audit committee and the quality of financial reports (e.g., Lin et al., 2006; Kusnadi et al., 2016). On the other hand, some focused on the relationship between the audit committee and auditing quality (e.g., Ali et al., 2018; Sultana et al., 2019). However, due to the recent financial scandals, investors' confidence in the audited financial statements has decreased. Therefore, the research problem stems from the discrepancy in previous studies' results in determining the audit committee's impact and the audit's quality on the quality of financial reports. In addition, the research problem also appears from a lack of a study conducted in the Saudi environment. Therefore, the current study will answer the following questions:

- 1- Is there an impact of the audit committee's effectiveness on the audit quality of companies listed on the Saudi Stock Exchange?
- 2- Is there a direct impact of the audit committee's effectiveness on the quality of financial reports in firms listed on the Saudi Stock Exchange?

3- What is the direct and indirect impact of the audit committee's effectiveness on the quality of financial reports through external audit quality in companies listed on the Saudi Stock Exchange?

Therefore, the current study aims to examine the mediating effect of audit quality on the relationship between the effective audit committee and the financial reporting quality.

The remainder of the current study is organized as follows. **Section 2** discusses the appropriate proxies of financial reporting quality. **Section 3** covers the literature review and hypotheses development. **Section 4** provides data description and methodology. The results and discussion are shown in **section 5**. Finally, **section 6** summarizes and concludes the current study.

2- Financial reporting quality: background and measurements

Several studies (e.g., Imhoff, 2003; Biddle & Hilary, 2006) used many concepts to express financial reporting quality within the framework of the qualitative characteristics of the information mentioned by the Financial Accounting Standards Board (FASB) in concept No. 2 in 1980. Some have addressed the quality of financial reports under accounting quality. The concept of accounting quality is a broad concept related to the accounting profession, starting with the preparation of accounting and auditing standards and passing through the professional practice of preparing and auditing financial statements, and ending with the product of this process, which is the financial report (Sharawi, 2017). Some studies indicated the quality of financial reports under the quality of accounting standards, which is linked to producing useful information for decision-making (Sharawi, 2017). The quality of accounting standards represents their ability to produce reliable and relevant financial information for making decisions.

On the other hand, Verleun et al. (2011) indicated that the quality of accounting information is an ambiguous concept, as there is no agreement among researchers on a single concept. Moreover, this concept is linked to different interpretations in the minds of its users. On the one hand, some have

addressed the quality of financial reports under earnings quality. However, on the other hand, researchers have almost unanimity that the quality of financial reports starts from earnings quality (Sharawi, 2017).

It is clear from what was mentioned above that there are several measures of the quality of financial reports. Most of the studies focused on three measures: the degree of earnings management, accounting conservatism, and the quality of accruals (Martínez-Ferrero, 2014). The first measure of financial reporting quality is earnings management, considered the inverse of financial reporting quality. The greater earnings management, the lower the information quality and the lower the earnings quality (Raman et al., 2013). The second measure of financial reporting quality is the accounting conservatism which reflects terrible news for the firm more rapidly than good news. The third measure of financial reporting quality is accruals quality, used in several studies (e.g., Dechow and Dichev, 2002; Martínez-Ferrero, 2014).

The current study will depend on Martínez-Ferrero (2014) in measuring financial reporting quality by adding a current year cash flow dummy and its interaction with cash flow levels into the Dechow and Dichev model (2002).

$$\Delta WC_{it} = \beta_0 + \beta_1 OCF_{i,t-1} + \beta_2 OCF_{it} + \beta_3 OCF_{i,t+1} + \beta_4 \Delta REV_{it} + \beta_5 PPE_{it} + \beta_6 DOCF_{it} + \beta_7 OCF_{it} * DOCF_{it} + \varepsilon_{7i}$$

ΔWC is a change in working capital accruals from year $t-1$ to year t and = $\Delta AR + \Delta inventory - \Delta AP - \Delta Taxes Payable + \Delta other Assets$.

OCF is the operating cash flow; **ΔRev** is the change in revenues; ***PPE is*** Property, Plant, and Equipment; **DOCF** is a dummy variable for the negative cash flows. It takes the value one if OCF is negative and 0; otherwise, i indicate the company and t refer to the period. The total assets scale all the variables (excepted DOCF). ε is the error term. The current study will use the absolute value of the residuals from this model as a proxy for financial reporting quality (FRQ): the lower the degree of this proxy, the higher the degree of FRQ (Martínez-Ferrero, 2014).

3- Literature review and hypotheses development

The audit quality gives independent assurance of the reliability of the financial reports, which enhances the confidence and protection of investors. Therefore, audit quality improves financial reporting quality. Previous studies have adopted many proxies to measure audit quality, but no single agreed-upon measure exists (Defond and Zhang, 2014; Bala et al., 2019). The audit fee is the best measure as used by many earlier studies because it results from the demand–supply mechanism, which states that the auditor cannot increase the audit fee in exchange for additional work without a corresponding increase in the quality of the audit. In addition, many previous studies dealt with the relationship between audit quality and financial reporting quality (Alves et al., 2013; Bala et al., 2019). They showed that the higher the audit fees, the lower the earnings management would be, and thus financial reporting quality would increase.

On the other hand, Audit Committees play a vital role in corporate governance practices by supervising the quality of auditing. Accordingly, effective audit committees with appropriate expertise are supposed to improve audit quality and improve financial reports' quality (Defond & Zhang, 2014). Therefore, the higher the audit quality, the greater the reliability of the financial reports, and thus the protection of the interests of investors and other stakeholders.

Some previous studies have indicated that internal governance and external auditing mechanisms can be a partial substitute for each other, which indicates that better internal control leads to lower audit fees (e.g., Hay et al., 2008; Hogan et al., 2008). However, some studies differ from the above and consider that internal governance and external audit mechanisms are complementary, which means that strengthening internal governance mechanisms is linked with a higher quality of audit (Hay et al., 2008; Bala et al., 2019).

The demand for the audit effort increases by paying more audit fees as a result of the increase in the audit scope required by the audit committees to improve audit quality. Thus, the selection of the Audit Committee (as an inter-

nal governance mechanism) for the external auditor (an external governance mechanism) complements each other to reduce earnings management and improve financial reporting quality). On the other hand, effective and efficient boards of directors with independent directors require high-quality audits to protect their reputations. Thus, effective audit committees can require a higher quality of audit, which will improve financial reporting quality (Alves, 2013).

According to the second view, effective audit committees achieve better oversight, produce better audits, and pay higher fees. Several studies have dealt with the relationship between the characteristics of the audit committee and audit quality. If the audit committees are large, members with financial experience and independent members, and they meet continuously during the year; thus, Bala et al. (2019) had expected that audit quality could play a role as a mediating variable that could be affected by the audit committee, which in turn enhances financial reporting quality, as this means that any change in the audit committee will lead to a change in audit quality, which leads to a change in financial reporting quality.

The study will focus on some of the characteristics of the audit committee as follows:

1- Audit Committee Size

The size of the audit committee is represented in the number of its members, and it is one of the important factors that help the Committee achieve its goals. Regulations and rules related to corporate governance usually specify the minimum size of the audit committee without specifying the maximum, leaving this to each company to determine the necessary number in light of its circumstances and the extent of its need for the services of the Committee. There are mixed results in the impact of the size of the audit committee on audit quality and the quality of financial reports. Some studies support the small size of the audit committee because it provides consistency and commitment and increases its ability to monitor, follow up, and communicate with all parties, whether management, external auditor, or Board of directors

(e.g., Carcello and Neal, 2000). However, some studies indicate that the large size of the audit committee is more effective because it allows for evaluating the role of the external auditor and helps the Board of directors by presenting recommendations that support the independent Board of directors to improve audit quality (e.g., Turley and Zaman 2004). Therefore, the first study hypothesis can be formulated as follows:

H1: Audit committee size positively affects financial reporting quality through more audit quality.

2- Audit Committee Independence

The independence of the members of the audit committee is one of the most important conditions for the Committee to achieve its goals because the availability of independence reduces the opportunity for management to influence the work of the Committee, which enables it to reduce the opportunistic behavior of management and improve the financial reporting process. In order to achieve the independence of the members of the Audit Committee, it is necessary that Audit Committee members be non-members of the Board of Directors, or that they be non-executive members, and that there is no direct or indirect relationship between the members of the Audit Committee and the executive members of the Board of Directors. Members of the Audit Committee are responsible for overseeing the preparation of financial reports. Thus, it may have a conflict with the management. On the other hand, the emphasis on independence makes the committee members express their opinions freely. Each Board of Directors understands how "independent, but the Board of directors should inform shareholders of the Board of Directors' approach to the independence of its directors and members of the audit committee and the criteria on which it was based. Several studies indicated that the independent audit committee reduces fraud and misrepresentation in financial reporting, which improves audit quality (e.g., Bedard et al., 2004; Rainsbury et al., 2009).

Therefore, the second study hypothesis can be formulated as follows:

H2: Audit committee independence positively affects financial reporting quality through more audit quality.

3- Frequency of Audit Committee meetings

The activities of the Audit Committee are expressed through the number of meetings held by the Committee during the year, and corporate governance rules and regulations specify the minimum number of such meetings during the year without specifying the maximum number. Regular meetings by members of the Audit Committee allow for reviewing and discussing the information on time. It is best to schedule these meetings well before the appropriate board meeting. The arrangements must correspond to the critical stages of financial reporting, external auditing, and internal audit cycles, which often means at least four meetings per year as decided by the Chairman of the Audit Committee. Some professionals point out that in the case of an annual financial report, it may be appropriate to schedule two meetings – the first two weeks before the report is issued to ensure sufficient time to address critical issues; and the second immediately before the release to review the final figures. Therefore, the third study hypothesis can be formulated as follows:

H3: The frequency of audit committee meetings positively affects financial reporting quality through audit quality.

4- Audit Committee financial experience

The experience of the audit committee means the extent to which there are members of the audit committee who have experience in the financial and accounting aspects. The availability of this Characteristic in the audit committee is necessary to achieve its goal, given that some of the responsibilities entrusted to the Committee are of a financial or accounting nature and need to be carried out effectively. Some suggest that every member of the audit committee should be financially literate – that is, he should have the ability to read and understand primary financial statements. According to the Saudi

Governance Manual, at least one member with financial and accounting experience must be among the members of the Audit Committee. The member may gain this experience through previous employment in finance or accounting, a professional qualification in accounting, or similar experiences, such as being a senior employee with financial control responsibilities or an auditor for a listed company. The audit committee should have more than one person with financial experience so that the responsibility for financial reporting does not fall on one person. The entire audit committee is responsible for financial reporting, regardless of whether only some members have financial experience. Therefore, the fourth study hypothesis can be formulated as follows:

H4: Audit Committee financial experience positively affects financial reporting quality through more audit quality.

5- Audit committee members' gender diversity

Numerous corporate governance guides worldwide call for the inclusion of women in corporate strategic decision-making to enrich entities. Some studies have found that firms with female members are more willing and committed to board activities than male directors, which leads to better board behavior and effectiveness. Among the reasons for gender diversity in the Board of directors is that women are more moral and law-abiding than men. Thus, having women as members of the audit committee will enhance the quality of financial reporting. Several studies dealt with the impact of gender diversity in the audit committee on the quality of financial reports. Some studies found a positive association between gender diversity in the audit committee on the quality of financial reports (e.g., Gul et al., 2007; Wahid, 2019). In contrast, some studies have found that women members in the audit committee negatively affect financial reports' quality (e.g., Ud Din et al., 2021; Zalata, 2022).

Therefore, the study hypothesis can be formulated as follows:

H5: Audit committee members' gender diversity positively affects financial reporting quality through more audit quality.

6- The effective audit committee

Several studies explored the audit committee's effectiveness. The audit committee's effectiveness was measured by the effectiveness of one of its characteristics or by creating an index of these combined characteristics (Sharawi, 2018). Some studies have designed an index to measure the audit committee's effectiveness, such as Sharawi (2018). This index consists of characteristics: the Committee's independence, its financial experience, the committee size, the number of its meetings, the Committee's responsibilities, and its submission to the Board of Directors' report. Sharawi (2018) also designed an index that includes six characteristics of the audit committee: committee size, its independence, the number of its meetings, the independence of the committee chair, the financial experience of the Committee, and gender diversity in the Committee. This study indicated that the effectiveness of audit committee characteristics as a whole is better than the effectiveness of each feature separately. Therefore, the study hypothesis can be formulated as follows:

H6: The effective audit committee positively affects financial reporting quality through more audit quality.

Figure 1: illustrates the relationship between the independent and dependent variables through the median variable.

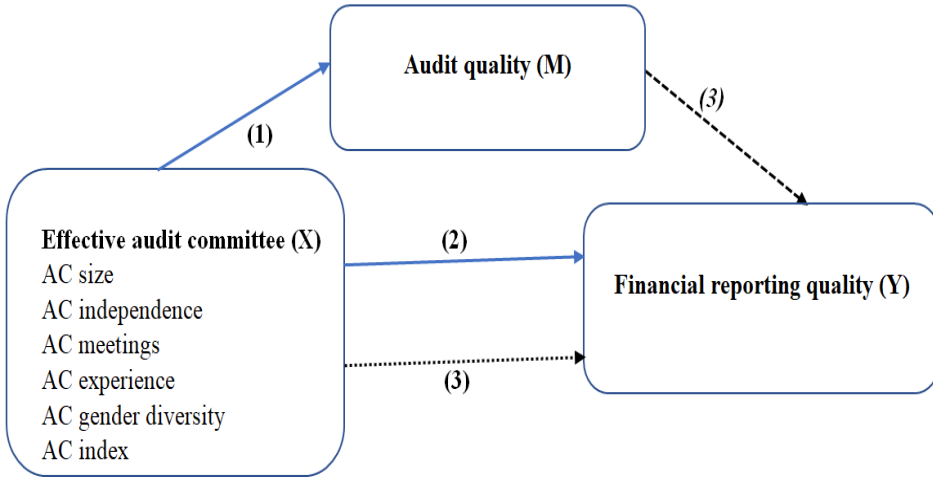


Figure 1: Proposed model

4- Data Description and Methodology

4.1 Sample selection

The current study considers non-financial firms listed on the Saudi stock markets for which all data were available. The data were collected from companies' financial reports provided by www.argaam.com. To be included in the study's final sample, a firm had to meet three main criteria: non-financial listed firms, access to a firm's complete eight-year annual reports from 2014 to 2021, and access to a firm corresponding financial data for the same period. The criteria were set for several reasons. First, Insurance firms and banks were excluded because of their specific rules and regulations. Second, the most recent years for which data were available.

Panel A of Table 1 shows the sample selection over 2014–2021. The initial sample consists of 216 Saudi listed firms. The study excludes 45 bank and insurance firms, 75 firms with missing corporate governance data (audit fees and attributes audit committee), and 19 firms with missing key control variables, giving a final sample of 77 firms with 616 firm-year observations. Panel B of Table 1 displays that 23% of the sample is derived from the Material sector, followed by firms belonging to the Food sector (10.39%), the Capital goods sector (9.09%), etc.

Table 1: Summary of the sample selection

	No. of firms	Percentage
Total firms available to be sampled	216	% 100
<i>Panel A: Sample selection</i>		
Less:		
Financial firms	45	20.83%
Firms with unavailable annual reports for corporate governance	75	34.72%
Control variables	9	8.79%
Total excluded firms	139	64.35%
Final selected sample	77	35.65%
<i>Panel B: Industrial composition of the sample</i>		
Sector	Observations	Percentage
Energy	16	2.60%
Materials	144	23.38%
Capital Goods	56	9.09%
Commercial & Professional Svc	16	2.60%
Transportation	24	3.90%
Consumer Durables & Apparel	24	3.90%
Consumer Services	40	6.49%
Media and Entertainment	16	2.60%
Retailing	40	6.49%
Food & Staples Retailing	32	5.19%
Food & Beverages	64	10.39%
Health Care Equipment & Svc	48	7.79%
Software & Services	16	2.60%
Telecommunication Services	24	3.90%
Utilities	16	2.60%
Real Estate Mgmt & Dev't	40	6.49%
Total	616	100%
Notes: Panel A contains the final sample form with robust data. Panel B shows firm classification by business sector.		

4.2 The study variables and the research models

4.2.1 The study variables

This current research investigates the mediating effect of audit quality on the relationship between the effective audit committee and financial reporting quality. The six attributes of an effective audit committee are explanatory (**independent**) variables. This study employs accruals quality as a proxy for financial reporting quality regarding the dependent variable. **The mediating** variable is audit fees as a measure of audit quality. The audit fees variable is

transformed into a natural log to help achieve data normality. Consistent with the previous studies (Sharawi, 2018; Qawqzeh et al., 2021; Larasati et al., 2019), this study controls several firms and board characteristics that might affect financial reporting quality. It uses board size, board ownership, firm size, return on assets, leverage, audit firm type, audit opinion, and industry type as the key control variables. Table 2 displays the variables of the current study and the measuring of each variable.

Table 2: the study variables and the measuring of each variable				
Variable type	Variable name	Acronym	Measurement	Supporting literature
Dependent variable			$\Delta WCF_{it} = \beta_0 + \beta_1 OCF_{i,t-1} + \beta_2 OCF_{it} + \beta_3 OCF_{i,t+1} + \beta_4 \Delta REV_{it} + \beta_5 PPE_{it} + \beta_6 DOCF_{it} + \beta_7 OCF_{it} * DOCF_{it} + \varepsilon_{7i}$	Martínez-Ferrero (2014)
	Financial reporting quality	FRQ	The study uses the absolute value of the residuals from this model as a proxy for FRQ	
Independent variables				
	Audit committee Size	AC-size	The dummy variable takes 1 if the number of members is more than three and 0 otherwise.	Sharawi (2018)
	Audit Committee Meetings	AC-meetings	The dummy variable takes 1 if the number of the meetings is more than four and 0 otherwise.	Sharawi (2018)
	Audit Committee Independence	AC-indep	Dummy variable that takes 1 if more than half of the committee members are independent and zeroes otherwise	Sharawi (2018)
	Audit committee Gender	AC-gender	An indicator variable equals one if there is gender diversity in the committee members and zeroes otherwise.	Sharawi (2018)
	Audit committee Experience	AC-exp	An indicator variable that equals one if there is more than one member of the committee who has financial and accounting experience and zeroes otherwise	Sharawi (2018)
	Audit committee Index	AC-index	Create an index to collect the characteristics of the previous audit committee from 5 items (size, independence, frequency of meetings, gender diversity, financial and accounting experience).	Sharawi (2018)
Mediating variable				
	Audit quality	A.Q.	Natural logarithm of audit fees	Qawqzeh et al. (2021)
Control variables				
	Board size	B-size	Number of the board directors	Qawqzeh et al. (2021)
	B-ownership	B-own	Percentage of members' ownership on the Board	Qawqzeh et al. (2021)
	Firm size	F-size	Natural log of the firm's total assets.	Qawqzeh et al. (2021)
	Return on assets	ROA	Return on assets(ROA) is calculated as net income before taxes and extraordinary items divided by total assets.	Qawqzeh et al. (2021)
	Leverage	Lev	Total debt/book value of total assets	Sharawi (2018)
	Audit Firm	Big4	Dummy variable that takes 1 if the audit firm is among the big four and 0 otherwise	Sharawi (2018)
	Audit opinion	A-opinion	The dummy variable takes 1 if a modified opinion is issued and 0 otherwise	Larasati et al. (2019)
	Industry type	industry	Dummy variable that = one if industrial firm, 0 if service firm.	Qawqzeh et al. (2021)

4.2.2 The research models

The mediating role of external audit quality in the relationship between the effective audit committee and financial reporting quality is tested using the mediation procedure outlined by Baron and Kenny (1986). In the first phase, the mediator (AQ) is regressed on the independent variables (effective audit committee). In the second phase, the dependent variable (FRQ) is regressed on the independent variables (effective audit committee). Finally, the dependent (FRQ) is regressed on the independent variables (effective audit committee) and the mediator (AQ). Therefore, the study formulates the following three models shown in Table 3, which display the research models:

Table 3: the research models
The first model (phase 1)
1- Audit Fees= $\beta_0 + \beta_1$ AC-size + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
2- Audit Fees= $\beta_0 + \beta_1$ AC-meetings + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
3- Audit Fees= $\beta_0 + \beta_1$ AC-indep + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
4- Audit Fees= $\beta_0 + \beta_1$ AC-gender + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
5- Audit Fees= $\beta_0 + \beta_1$ AC-exp + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
6- Audit Fees= $\beta_0 + \beta_1$ AC-index + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
The second model (phase 2)
1- FRQ= $\beta_0 + \beta_1$ AC-size + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
2- FRQ= $\beta_0 + \beta_1$ AC-meetings + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
3- FRQ= $\beta_0 + \beta_1$ AC-indep + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
4- FRQ= $\beta_0 + \beta_1$ AC-gender + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
5- FRQ= $\beta_0 + \beta_1$ AC-exp + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
6- FRQ= $\beta_0 + \beta_1$ AC-index + β_2 B-size + β_3 B-own + β_4 F-size + β_5 ROA+ β_6 Lev+ β_7 Big4+ β_8 Opinion+ β_9 Industry+ ϵ
The third model (phase 3)
1- FRQ= $\beta_0 + \beta_1$ AC-size + β_2 AQ + β_3 B-size + β_4 B-own + β_5 F-size + β_6 ROA+ β_7 Lev+ β_8 Big4+ β_9 Opinion+ β_{10} Industry+ ϵ
1- FRQ= $\beta_0 + \beta_1$ AC-meetings + β_2 AQ + β_3 B-size + β_4 B-own + β_5 F-size + β_6 ROA+ β_7 Lev+ β_8 Big4+ β_9 Opinion+ β_{10} Industry+ ϵ
1- FRQ= $\beta_0 + \beta_1$ AC-indep + β_2 AQ + β_3 B-size + β_4 B-own + β_5 F-size + β_6 ROA+ β_7 Lev+ β_8 Big4+ β_9 Opinion+ β_{10} Industry+ ϵ
1- FRQ= $\beta_0 + \beta_1$ AC-gender + β_2 AQ + β_3 B-size + β_4 B-own + β_5 F-size + β_6 ROA+ β_7 Lev+ β_8 Big4+ β_9 Opinion+ β_{10} Industry+ ϵ
1- FRQ= $\beta_0 + \beta_1$ AC-exp + β_2 AQ + β_3 B-size + β_4 B-own + β_5 F-size + β_6 ROA+ β_7 Lev+ β_8 Big4+ β_9 Opinion+ β_{10} Industry+ ϵ
1- FRQ= $\beta_0 + \beta_1$ AC-idx + β_2 AQ + β_3 B-size + β_4 B-own + β_5 F-size + β_6 ROA+ β_7 Lev+ β_8 Big4+ β_9 Opinion+ β_{10} Industry+ ϵ
$\beta_0 - \beta_{10}$ = Regression coefficients
ϵ = Error term

Following the steps used by Baron and Kenny (1986), three conditions must be fulfilled to prove the existence of the mediation process:

- 1- In the first regression, the independent variables (Effective AC) must significantly predict the mediator (AQ);
- 2- In the second regression, the independent variables (Effective AC) must significantly predict the dependent variable (FRQ) and
- 3- The mediator (AQ) must significantly predict the third regression's dependent variable (FRQ).

5- Results and discussion

5.1 Descriptive statistics

Panel A of Table 4 summarizes the basic descriptive regression variables of sample firms listed on the stock exchange of Saudi Arabia for 2014 - 2021. The results show that FRQ that represents the accruals quality has a mean value of 203.05 and a standard deviation of 923.59. The results also show that AQ. that presents audit fees as a proxy for audit quality has a mean value of 14.45 and a standard deviation of 5.92. On the other hand, Characteristics of the effective audit committee (as independent variables) the means represent the following values (0.59, 0.60, 0.67, 0.33, 0.34) for Ac-size, Ac-meetings, Ac-Indep, Ac-gender, Ac-exp) respectively and the standard deviations are (0.49, 0.42, 0.39, 0.32, 0.48) respectively. While the mean of the Ac-index represents 2.54, and the standard deviation is 1.68.

Panel B of Table 4 displays the frequencies of the independent variables, which show that the effectiveness of the independence of the audit committee represents 67.4%, followed by the effectiveness of gender diversity among members of the audit committee at 66.6%. Finally, the effectiveness of financial expertise among members of the audit committee represents 65.5%.

Table 4: Descriptive statistics

<i>Panel A: Descriptive</i>	N	Min	Max	Mean	SD
AC-size	616	0	1	0.59	0.49
AC-meetings	616	0	1	0.60	0.42
AC-indep	616	0	1	0.67	0.39
AC-gender	616	0	1	0.33	0.32
AC-exp	616	0	1	0.34	0.48
AC-index	616	0	5	2.54	1.68
FRQ	616	-1234.04	2304.23	203.05	923.59
AQ	616	9.11	15.83	14.45	5.92
B-size	616	5	11	7.68	1.81
B-own	616	0.08	0.64	0.211	0.094
F-size	616	0.5	12.0	8.06	2.40
ROA	616	-0.05	0.32	0.141	9.37
Lev	616	0.05	0.57	0.45	0.138
Big4	616	0	1	0.43	0.50
Opinion	616	0	1	0.31	0.46
Industry	616	0	1	0.80	0.40
<i>Panel B: Frequencies</i>	N	0	%	1	%
AC-size	616	268	40.9%	388	59.1%
AC-meetings	616	265	40.4%	391	59.4%
AC-indep	616	214	32.6%	442	67.4%
AC-gender	616	219	33.4%	437	66.6%
AC-exp	616	226	34.5%	430	65.5%

Notes: This table shows summary statistics (minimum, maximum, means, standard deviations, and frequencies of the variables in the regression models (dependent, independent, mediating, and control variables).

5.2 Correlation analysis

This study conducts collinearity diagnostics to ensure the lack of multicollinearity among the independent variables. Two tests were performed: the pairwise correlation matrix among the independent variables and the variance inflation factor (VIF). According to Kennedy (2008), if the correlation among the independent variables is greater than or equal to 0.80, a multicollinearity problem is assumed to exist. As displayed in Table 5, the Pearson correlation coefficients are relatively low, and there are no correlations between the variables that can reach 0.80. This indicates that multicollinearity is not a problem for the sample.

Furthermore, multicollinearity is tested by calculating the VIF. Table 5 shows that all variables are less than 3, supporting the previous conclusion that there are no significant multicollinearity issues in the data. However, if this is greater than 3, any study must investigate this issue, while WIFs exceeding 10 are signs of serious multicollinearity requiring correction.

Table 5 Correlation matrix and VIF values

Variable	AC-size	AC-meetings	AC-indep	AC-gender	AC-exp	AC-index	FRQ	AQ	B-size	B-own	F.size	ROA	Lev	Big4	Opinion	Industry	VIF
AC-size	1																1.21
AC-meetings	.908**	1															1.23
AC-indep	.672**	.739**	1														1.13
AC-gender	0.036	0.023	.093*	1													1.24
AC-exp	0.041	0.035	.108**	.976**	1												1.45
AC-index	.766**	.780**	.747**	.599**	.609**	1											1.98
FRQ	.349**	.405**	.506**	.246**	.266**	.505**	1										1.06
AQ	.147**	.143**	.259**	.252**	.264**	.302**	.146**	1									1.41
B.size	-0.001	-0.009	0.066	0.016	0.009	0.022	0.047	0.036	1								1.01
B.own	-.144**	-.134**	-.242**	-0.033	-0.043	-.170**	-	-	-	1							1.26
F.size	-0.029	-0.042	-0.012	-0.039	-0.022	-0.041	0.022	0.008	-	0.005	1						1.01
ROA	-.081*	-.082*	-.242**	-.246**	-.241**	-.252**	-	-	-	.405**	0.047	1					1.27
Lev	-0.008	-0.022	-0.060	-0.039	-0.059	-0.053	-	-	0.035	-	-	0.071	1				1.01
Big4	-.116**	-.137**	-.190**	-.203**	-.215**	-.245**	-	-	-	.138**	0.009	.210**	0.031	1			1.08
Opinion	-.077*	-.117**	-.128**	-.143**	-.157**	-.177**	-.096*	-	-	.189**	-	.224**	0.054	.161**	1		1.09
Industry	.159**	.172**	.159**	-.294**	-.289**	-0.023	0.063	0.050	-	-	0.054	-	-	0.044	0.041	1	1.06
									0.060	.148**	0.020	0.008					

This table displays the correlation coefficients between variables and inflation factors of independent and control variables. *** p < 0.01, ** p < 0.05; * p < 0.1

5-3 Multivariate analysis

5-3-1 The effect of an effective audit committee on audit quality

Table 6 shows the model results that present the effect of an effective audit committee (independent variables) on audit quality (mediator). Adj R² as shown in Table 6 (Column1), is 25.57, and F-statistic is significant at sign. level 0.000. Therefore, these results indicate that all independent variables ex-

plain 25.57% of the variance in the dependent variable, which is statistically significant. The results reveal that the coefficients associated with effective audit committee size are positive and significant ($\beta=1.329$, $p<5\%$), implying that the large audit committee size enhances audit quality. Adj R^2 as shown in Table 6 (Column 2), is 25.45, and F-statistic is 0.000. Therefore, these results indicate that all independent variables explain 25.45% of the variance in the dependent variable, which is statistically significant. The results reveal that the coefficients associated with the frequency of audit committee meetings are positive and significant ($\beta=1.192$, $p<5\%$), implying that the repetition of committee meetings strengthens audit quality in monitoring and follow-up through the recommendations that result from these meetings. Adj R^2 as shown in Table 6 (Column 3), is 26.17, and F-statistic is 0.000. Therefore, these results indicate that all independent variables explain 27.17% of the variance in the dependent variable, which is statistically significant. The results reveal that the coefficients associated with audit committee independence are positive and significant ($\beta=2.081$, $p<5\%$), implying that increasing the number of independent committee members increases audit quality. R^2 as shown in Table 6 (Column 4), is 27.37, and F-statistic is 0.000. Therefore, these results indicate that all independent variables explain 27.37% of the variance in the dependent variable, which is statistically significant. The results reveal that the coefficients associated with gender diversity in the audit committee are positive and significant ($\beta=3.028$, $p<5\%$), implying that increasing the presence of male and female members of the audit Committee enhances the diversity of decisions and enhances the audit quality in its supervision and monitoring. Adj R^2 as shown in Table 6 (Column 5), is 28.69, and F-statistic is 0.000. Therefore, these results indicate that all independent variables explain 28.69% of the variance in the dependent variable, which is statistically significant. The results reveal that the coefficients associated with increasing members with financial and accounting experience in the audit committee are positive and significant ($\beta=3.208$, $p<5\%$), implying that increasing the financial and accounting expertise of a large number of committee members helps the Board of directors to enhance its independence. Adj R^2 as shown in Table 6 (Col-

umn 6), is 27.54, and F–statistic is 0.000. Therefore, these results indicate that all independent variables explain 28.69% of the variance in the dependent variable, which is statistically significant. The results reveal that the coefficients associated with an effective audit Committee are positive and significant ($\beta=0.850, p<5\%$), implying that the more effective the audit committee, the more robust the audit quality.

Table 6: Regression for the effective audit committee and audit quality

Variable	A				A							
	.C. size		A.C. meeting		A.C. indep		A.C. gender		.C. exp		A.C. index	
	B	P- value	B	P- value	B	P- value	B	P- value	B	P- value	B	P- value
(Constant)	36.520	0.000	36.568	0.000	35.547	0.000	34.406	0.000	34.122	0.000	33.735	0.000
B. size	0.039	0.805	0.042	0.794	0.008	0.959	0.052	0.741	0.058	0.712	0.038	0.808
B-own	-0.161	0.000	-0.163	0.000	-0.153	0.000	-0.174	0.000	-0.173	0.000	-0.158	0.000
Size	0.092	0.443	0.095	0.430	0.087	0.466	0.090	0.445	0.081	0.492	0.102	0.390
ROA	-0.390	0.000	-0.391	0.000	-0.373	0.000	-0.347	0.000	-0.347	0.000	-0.359	0.000
Lev	0.007	0.740	0.007	0.725	0.010	0.631	0.008	0.682	0.011	0.601	0.010	0.623
Big4	-1.356	0.024	-1.348	0.025	-1.220	0.043	-1.088	0.069	-1.025	0.086	-0.958	0.110
Opinion	-1.732	0.008	-1.685	0.010	-1.688	0.009	-1.593	0.013	-1.539	0.016	-1.501	0.019
Industry	0.239	0.745	0.238	0.747	0.129	0.860	1.494	0.047	1.548	0.039	0.567	0.429
AQ	1.329	0.027	1.192	0.049	2.081	0.001	3.028	0.000	3.208	0.000	0.850	0.000
F. statistic	26.00		25.85		26.80		28.42		28.877		28.66	
D-Watson	0.49		0.49		0.47		0.48		0.494		0.47	
Adj R2	25.57%		25.45%		26.17%		27.37%		28.69%		27.54%	
n	616		616		616		616		616		616	

Note: The table shows the results of the effect of an effective audit committee on audit quality. The entire sample consists of 82 firms from KSA over the period 2014-2021.

5-3-2 The direct effect of an effective audit committee on financial reporting quality

The second model tests the direct effect of an effective audit committee on financial reporting quality. The results reported in Table 7 (Columns 1 to 6) show that AC size is positively related to accruals quality ($\beta = 6.328, p < 5\%$). This suggests that the greater the audit committee size, the higher quality financial reporting quality. This finding aligns with (Lin et al., 2006; Kamolsakulchai, 2015; Haji & Anifowose, 2016). This result indicates that many audit committees affect financial reporting quality. This result provides reasonable assurance for the requirements of the corporate governance code and stock

market regulations in KSA which determined such a number to be at least three.

Table 7 (Column 2 to 6) indicate that AC meetings is positively related to accruals quality ($\beta = 7.456$, $p < 5\%$). This suggests that the more frequent the audit committee meetings, the higher the financial reporting quality. This finding aligns with (Lin et al., 2006; Hasan et al., 2020; Hamdan, 2020). These results indicate that financial reporting quality is higher at firms having active audit committee members, as such activity provides members with sufficient time to perform their duties.

Table 7 (Column 3 to 6) indicate that AC independence is positively related to accruals quality ($\beta = 10.341$, $p < 5\%$). This suggests that the higher the number of independent audit committee members, the higher the financial reporting quality. This finding aligns with (Soliman & Ragab, 2014; Hasan et al., 2020; Hamdan, 2020). This result indicates that financial reporting quality is higher at firms having more independent audit committees. Such independence provides members with the power to express their opinion, which will appear in the financial reporting transparency and decreased information asymmetry.

Table 7 (Column 4 to 6) indicate that AC gender is positively related to accruals quality ($\beta = 5.313$, $p < 5\%$). This suggests that the greater the diversity of audit committee members between males and females, the higher the financial reporting quality. This finding aligns with (Abbasi et al., 2020; Fernández-Méndez and Pathan, 2022). This result indicates that female directors on the audit committee improved transparency in the financial information. However, improved transparency is captured by disclosing audit reports with uncertainties and scope limitation qualifications (Fernández-Méndez & Pathan, 2022).

Table 7 (Column 5 to 6) indicate that AC financial experience is positively related to accruals quality ($\beta = 5.671$, $p < 5\%$). This suggests that the more audit committee members with financial and accounting experience, the higher the financial reporting quality. This finding aligns with (Kusnadi et al.,

2016; Hasan et al., 2020). This result indicates that financial reporting quality is higher at firms with more members with financial and accounting expertise, as such expertise helps members enhance financial reporting quality.

Table 7 (Column 6 to 6) indicate that AC index is positively related to accruals quality ($\beta = 2.855, p < 5\%$). This suggests that the higher the level of effectiveness of the audit committee, the higher the financial reporting quality. This result indicates that the greater the audit committee's effectiveness, the greater the possibility of carrying out its duties. It increases accounting information transparency and reduces information asymmetry, which improves the quality of financial reports.

Regarding control variables, the results indicate no significant association between board size, firm size, leverage, return on assets, industry, and financial reporting when testing the effectiveness of each Characteristic of the audit committee. At the same time, there is a positive and significant relationship between return on assets, the industry, and financial reporting quality when there is an effective audit committee (Column 6 in Table 7).

Table 7: Regression of the effective audit committee and Financial reporting quality

Variable	(1) A.C. size		(2) A.C. meeting		(3) A.C. indep		(4) A.C. gender		(5) A.C. exp		(6) A.C. index	
	B	p. value	B	P .value	B	p. value	B	p. value	B	p. value	B	p. value
Constant	6.384	0.016	5.324	0.041	1.360	0.586	5.419	0.053	4.880	0.081	-1.690	0.510
B-size	0.214	0.266	0.230	0.221	0.059	0.739	0.233	0.238	0.243	0.215	0.209	0.241
B-own	0.020	0.630	0.018	0.662	0.057	0.140	-0.025	0.561	-0.022	0.603	0.021	0.584
Size	0.128	0.379	0.160	0.260	0.106	0.429	0.095	0.523	0.079	0.594	0.146	0.275
ROA	0.001	0.986	-0.001	0.982	0.090	0.068	0.076	0.173	0.076	0.170	0.105	0.034
Lev	0.003	0.898	0.006	0.800	0.018	0.425	0.005	0.833	0.010	0.710	0.014	0.553
Big4	-3.457	0.000	-3.208	0.000	-2.754	0.000	-3.385	0.000	-3.270	0.000	-2.308	0.001
Opinion	-0.972	0.214	-0.579	0.450	-0.741	0.305	-0.935	0.244	-0.837	0.295	-0.295	0.684
Industry	0.587	0.508	0.208	0.811	-0.013	0.988	3.537	0.000	3.646	0.000	2.037	0.012
AC	6.328	0.000	7.456	0.000	10.341	0.000	5.313	0.000	5.671	0.000	2.855	0.000
D-Watson	1.586		1.56		1.53		1.35		1.35		1.61	
F. Statistic	13.70		17.54		28.44		9.51		10.333		28.22	
Adj R2	14.85%		18.51%		27.38%		10.47%		11.37%		27.22%	
n	616		616		616		616		616		616	

Notes: The table shows the results of the effect of an effective audit committee on financial reporting quality. The entire sample consists of 82 firms from KSA over the period 2014-2021.

5-3-3 The mediating effect of audit quality on effective audit committee - financial reporting quality relationship.

Table 8 (Columns 1 to 6) reports the results of estimating Model (3) developed to capture the mediating effect of audit quality in the relationship between the effective audit committee and financial reporting quality. As highlighted in Column (1), the inclusion of variable audit fees in Model (3) allows to keep the effect of AC size on accruals quality significant but at a lower level than is the case in Model (2) ($\beta = 6.212$, $p < 5\%$). This suggests that an effective audit committee size improves the quality of financial reporting through higher external audit quality. As the presence of a sufficient number of members of the Audit Committee helps it review the external auditor's plan and verify its independence, which improves the quality of the audit process and thus improves financial reporting quality, therefore, *H1* is accepted.

The findings (Column 2) also reveal that the coefficient associated with audit committee meetings ($\beta = 7.354$, $p < 5\%$) remains positive and significant, but with a lower level than in Model (2). This suggests that the frequency of audit committee meetings improves the quality of financial reporting through the audit quality process. Furthermore, the audit committee meetings' effectiveness helps it effectively discuss everything related to the financial reports and communicate on an ongoing basis with the external auditor, which improves financial reporting quality. Thus, *H2* is accepted.

The findings (Column 3) present that the coefficient associated with audit committee independence ($\beta = 10.246$, $p < 5\%$) remains positive and significant, but with a lower level than in Model (2). This suggests that increasing the number of independent members of the Audit Committee helps express a view of the point on the financial statements prepared by management honestly and impartially. On the other hand, it helps to independently review the auditor's plan and work, ultimately improving financial reporting quality. Thus, *H3* is accepted.

The findings (Column 4) indicate that the coefficient associated with audit committee diversity ($\beta = 5.102$, $p < 5\%$) remains positive and significant, but

with a lower level than in Model (2). This suggests that increasing gender diversity in the audit committee in light of external audit quality helps to enhance financial reporting quality. Thus, *H4* is accepted.

The findings (Column 5) show that the coefficient associated with audit committee diversity ($\beta = 5.474$, $p < 5\%$) remains positive and significant, but with a lower level than in Model (2). This suggests that increasing the number of Audit Committee members with financial and accounting expertise helps them examine financial statements before presenting them to the Board of Directors and expressing their opinions. On the other hand, the auditor's report and his comments on the financial statements are investigated, which helps improve the quality of the external audit and thus enhances financial reporting quality. Therefore, *H5* is accepted.

The findings (Column 6) show that the coefficient associated with audit committee diversity ($\beta = 2.847$, $p < 5\%$) remains positive and significant, but with a lower level than in Model (2). This suggests that increasing the effectiveness of the audit committee leads to its coordination between all parties, whether with the auditor or the Board of directors, which helps in improving audit quality, which leads to an increase in financial reporting quality thus, *H6* is accepted

On the other hand, Table 8 shows that Audit Committee independence had the most impact on financial reporting quality through a high audit quality, which adj R^2 is 27.39%, followed by the frequency of Audit Committee meetings and then Audit Committee size, which adj R^2 is 18.82% and 15.17% respectively.

The results reported in Table 8 indicate that the variable audit fees allow keeping the effects of effective audit committee significant, but at lower levels than in the previous regressions, suggesting partial mediation of audit quality.

Table 8: Regression for the mediating effect of audit quality on effective audit committee- financial reporting quality relationship

Variable	(1) A.C. size		(2) A.C. meeting		(3) A.C. indep		(4) A.C. gender		(5) A.C. exp		(6) A.C. index	
	B	p.value	B	p.value	B	p.value	B	p.value	B	p.value	B	p.value
(Constant)	3.196	0.313	2.186	0.481	-0.278	0.925	3.025	0.355	2.785	0.392	-2.007	0.500
B-size	0.210	0.273	0.227	0.228	0.059	0.740	0.229	0.245	0.240	0.222	0.208	0.242
B-own	0.034	0.419	0.032	0.441	0.064	0.102	-0.012	0.773	-0.011	0.793	0.022	0.564
Size	0.120	0.409	0.152	0.284	0.102	0.447	0.089	0.551	0.074	0.618	0.146	0.278
ROA	0.035	0.531	0.032	0.554	0.107	0.039	0.100	0.086	0.097	0.093	0.108	0.038
Lev	0.003	0.917	0.006	0.820	0.018	0.437	0.005	0.850	0.009	0.729	0.014	0.556
Big4	-3.339	0.000	-3.092	0.000	-2.698	0.000	-3.309	0.000	-3.207	0.000	-2.299	0.001
Opinion	-0.821	0.295	-0.434	0.572	-0.663	0.361	-0.824	0.307	-0.742	0.355	-0.281	0.700
Industry	0.566	0.523	0.187	0.829	-0.019	0.982	3.433	0.000	3.551	0.000	2.032	0.012
AQ	0.087	0.056	0.086	0.045	0.046	0.036	0.070	0.058	0.061	0.052	0.009	0.033
AC	6.212	0.000	7.354	0.000	10.246	0.000	5.102	0.000	5.474	0.000	2.847	0.000
D. Watson	1.568		1.54		1.53		1.34		1.34		1.61	
F. Statistic	12.712		16.185		25.71		8.77		9.463		25.37	
Adj R2	15.17%		18.82%		27.39%		10.61%		11.44%		27.11%	
n	616		616		616		616		616		616	

Notes: This table shows the results of the effect of the mediating effect of audit quality on the effective audit committee- financial reporting quality relationship. The entire sample consists of 82 firms from KSA over the period 2014-2021.

6-Conclusion

The proposed study sought to answer the empirical question about the mediating effect of audit quality on the relationship between the effective audit committee and financial reporting quality. Consistent with prior research such as Sharawi (2018), effective audit committees achieve better monitoring, produce more audit coverage, and pay higher audit fees. Larger audit committees, frequently meeting each year, composed of at least one member with financial expertise, comprising independent directors and composed of male and female, demand more significant audit efforts by engaging Big 4 auditors and paying higher audit fees (Goodwin et al., 2006). Therefore, as the Audit committee chooses the external auditor; hence, these monitoring tools may operate jointly to improve accruals quality and enhance financial reporting quality.

The fundamental prelude of this study is that an effective audit committee directly affects financial reporting quality and affects financial reporting quality

via its effect on audit quality. In particular, the study finds that effective audit committees are keener on coordinating with the external auditor, nominating the best auditor, and recommending higher fees, which ensures an increase in audit quality, which leads to improving financial reporting quality. Thus, the audit committee as an internal mechanism for governance affects the external audit as an external mechanism for governance, which is due to improving financial reporting quality.

This study focuses on the effectiveness of internal and external mechanisms in enhancing corporate governance. This research has important implications for regulators and policymakers to address the conflict between insiders and outsiders by promoting a higher standard of financial reports. The study findings may be helpful to investors, aiding them in financial decision-making and helping all stakeholders understand and trust the fairness and quality of financial reports. In addition, it helps to understand the role that an effective audit committee plays in external audit quality and financial reporting quality. The study also contributes by bringing a new perspective on how external audit quality engages in monitoring by requesting financial reporting quality.

The study has limitations as well. First, the study has focused on Saudi listed firms. Therefore, the findings may not generalize to non-listed firms. Second, the research has focused on some characteristics of audit committees and some proxies of measurements of external audit quality. Therefore, the findings may not be generalized. Future research can address whether effective risk management with higher independent committees affects external audit quality to improve financial reporting quality. In particular, future studies can investigate the moderating effect of the risk management committee on financial reporting quality.

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