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ABSTRACT

Accounting scandals and concerns about the quality of financial statements have led to many calls for improved audit committee effectiveness. Prior research indicates that audit committee independence is positively related to effective oversight of the financial reporting process. Unfortunately, prior research has not provided an answer as to how much independence on the audit committee is enough. This is an important unanswered question because while Section 301 of the Sarbanes-Oxley Act of 2002 (SOX) currently requires all listed companies to maintain an audit committee that is 100 percent independent there has been much debate regarding easing the SOX requirements for smaller and foreign companies. In this paper we examine whether the regulatory requirements of a completely independent audit committee are necessary to obtain the monitoring benefits related to audit committee independence that have been documented in prior literature. Our results suggest that the benefits of audit committee independence are consistently achieved only when the audit committee is completely independent. These results provide support for the SOX requirement of 100 percent independent audit committees.

Keywords: Audit Committee; 100% Independent; Auditor Changes; GC Reporting

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