

Corporate Governance and the Informativeness of Accounting Earnings: The Role of the Audit Committee

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Abstract

Policy makers around the world have focused on corporate governance reform since the Asian financial crisis and scandals in the United States such as the Enron debacle. In particular, policy makers have focused on the establishment of independent audit committees to improve investor confidence in reported accounting information. In a sample of East Asian companies, we find that the negative relation between concentrated control and earnings informativeness that was documented prior to the Asian financial crisis persists in a more recent period, even though many corporate governance reforms have been adopted since the crisis to improve financial disclosure. We do, however, find that earnings informativeness is strengthened by both fully independent audit committees and audit committees with a majority of independent directors with accounting financial or legal expertise. In addition, the increased reliability that is associated with these audit committee characteristics appears to more than offset the detrimental effect that is associated with concentrated control. The results in this paper suggest that an emphasis on audit committee independence alone may not be enough to enhance earnings informativeness. Instead, focusing on both complete independence and the financial or legal expertise of independent directors who are appointed to the audit committee may be a more fruitful way to increase investor confidence in accounting information, especially when ownership is concentrated.

Keywords: Corporate Governance; Ownership; Earnings Informativeness; Audit Committee