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The Relationship between Audit Committee Characteristics and Earnings Management among Jordanian Listed Companies: Proposing Conceptual Framework

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Abstract
In a capital market where financial reports are a key feature of communication with respect to public firms' performance and financial position, as is well known, one of the objectives of a company's corporate governance system is to ensure the quality of that company's financial reporting. Accounting earnings are more reliable and of higher quality when managers' opportunistic behavior is reduced using monitoring systems. One specific area of concern is the monitoring function of the audit committee on earnings management. This paper proposes a conceptual framework that investigates the role of audit committee characteristics (independence, size, activity, and financial expertise) on earnings management using a sample of all industrial companies listed on the Amman Stock Exchange (ASE). Evidence from prior studies suggested that audit committee takes over the board function to oversee the firm's financial reporting process. The audit committee's role vital in monitoring the company's operation and internal control system with the aim of protecting the interest of the shareholders. In regards to earnings management, this paper views earnings management as opportunistic earnings. The current study argues that the firms with effective characteristics of audit committee are less likely to allow earnings management because opportunistic earning's cause uncertainty about the economic value of a firm.
Keywords: Audit committee characteristics, earnings management, financial reporting quality, Jordan.

1. Introduction

The end of the 1990s and the beginning of 21st century have witnessed a series of corporate accounting scandals across the United States, Europe and East Asian (e.g. Enron, HealthSouth, Parmalat, Tyco, WorldCom, and Xerox). At the core of these scandals was usually the phenomenon of earnings management (Goncharov, 2005). Studies on earnings management are becoming the subject of many recent researches in financial economics. Moreover, it has been a great and consistent concern among practitioners and regulators and has received substantial consideration in the accounting literature (Ali Shah et al., 2009).

Based on agency theory, issues associated with the separation between ownership and control will lead managers (agents) to act in an opportunistic manner by increasing their personal wealth at the expense of the owners (principal) of an organization (Jensen and Meckling, 1976). Therefore, opportunistic earnings management practice produces less reliable accounting earnings, which do not reflect a firm's true financial performance. Earnings management is likely to reduce the quality of reported earnings and its usefulness for investment decisions through the selection of accounting methods and treatments that serve the managers' interests rather than the ones that reflect the truthful financial position of the firm, thus reducing investor confidence in the financial reports and obscures facts that stakeholders ought to know (Loomis, 1999).

According to IASB Framework for the Preparation and Presentation of Financial Statements, the objective of financial statements is to provide value-relevant information to the external and internal parties of the organization. It is widely believed that accounting earnings information provides relevant and useful information to investors and other decision markets. Especially, the market efficiency is based upon the information flow to capital markets. When the information is incorrect, it may not be possible for the markets to value securities correctly. Hence, earnings management may obscure real performance and lessen the ability of shareholders and investors to make informed decisions. However, accounting earnings are more reliable and of higher quality when managers' opportunistic behavior is reduced using monitoring systems (e.g. Wild, 1994; Dechow et al, 1996).

In the wake of recent financial failures of some large companies resulting partially from accounting manipulation has raised serious questions about the role of different monitoring devices presumed to protect investors' interests and control managerial opportunistic behavior. Thus, as part of corporate governance, the audit committee has recently become of prominent importance in corporate governance (Zhang et al., 2007; Anderson et al., 2004); due to it plays an important role at overseeing the quality of the financial reports, and at acting as a deterrent to management override of controls and management fraud (Carcello and Neal, 2000, Whittington and Pany, 2003).

This paper proposes a conceptual framework to investigate the relationship between audit committee characteristics (audit committee independence, size, activity, and financial expertise) and earnings management among industrial companies listed on ASE. The remainder of the paper is organized as follows: Introduces the background of the study in section 2. Literatures review in section 3, the conceptual framework and hypothesis development presented in section 4. Summaries and concludes this paper in section 5.

2. Background

Jordan is an Arab Muslim country and it is situated in southwest Asia, at the meeting point of Asia, Africa, and Europe and a gateway to the Middle East. Jordan is a developing country with a centralized state system. It is very attractive for foreign investments, due too many reasons such as safety, political stability and its central location in the Middle East despite the on-going conflicts in the Middle East region. It seeks for afford a safe environment for its listed securities at the same time as protecting the rights of the investors. Therefore, the Jordanian government mandated the establishment of audit committees in Jordanian public shareholding companies to facilitate improving the quality of Jordanian financial reporting, the audit committee consisting of three non-executive members from the company's board of directors, two of them is independent members in the board (see The Jordanian Corporate Governance Codes (JCGC), 2009).

In view of the fact that, Jordan is one of the countries where users depend on accounting numbers intended for making decisions, it is of enormous significance to consider the area under discussion of earnings management to protect those users from being misled. Also, by reason of the lack of studies about earnings management in Jordan, So, this study intends to investigate the association between audit committee characteristics and earnings management.

3. Literature Review

Literature on earnings management mostly revolves around agency theory that proposes that managers (agent) would not work at all times in the best interest of their shareholders (principal). Where the role of management is preparing the financial statements and the role of the auditor is to audit the financial statements and evaluate internal control, the role of the audit committee is to oversee the entire process (BRC, 1999). The Wild (1994) study found that the credibility and fairness of financial reports issued by companies depends on the existence of an audit committee emerging from management councils of such companies, while Pucheta-Martínezand Fuentes (2007) found that an audit committee would be more active in the process of monitoring financial statements and limiting the differences between the management and the external auditor. This reduces the probability of the company receiving qualified opinions from the external auditor resulting from accounting errors or non-commitment to accounting standards.

A growing body of literature suggests that audit committee is as a delegate body of the board of directors charged with safeguarding and advancing the interests of shareholders (Bedard et al., 2004; Klein, 2002). The board usually delegates responsibility for the oversight of financial reporting to the audit committee to enhance the breadth of relevance and reliability of the annual report. Therefore, the audit committee has been considered as a very important monitoring mechanism of corporate governance for oversight of the company’s financial reporting process (Joshi and Wakil, 2004). Besides, the roles of regulatory and controlling authorities are mainly important in improving the market value of the firm (Agrawal and Knoeber, 1996; Bhagat and Jefferis, 2002; Dalton et al., 1999; Klein, 1998).

The audit committee is also viewed as a monitoring mechanism that can help alleviate agency problems by reducing information asymmetry between insiders (managers) and outsiders board members (Chen et al., 2008; Dey, 2008; Eichenseher and Shields, 1985; Klein, 1998; Sarens et al., 2009), since its key functions are to review financial information and control management’s conduct of affairs (Alchian and Demsetz, 1972; Fama and Jensen, 1983). In fact, the audit committee can improve the quality and accuracy of financial information (DeFond and Jiambalvo, 1991; McMullen, 1996), ensuring that the officers responsible for reporting and disclosure are more closely monitored and controlled. Therefore, as a part of the corporate governance mechanism, audit committees can play a key role in constraining earnings management and enhancing earnings quality.

In Jordan, establishing audit committees became mandatory in 1998 for companies filing with the Jordan Securities Commission (JSC), given the fact that audit committees are still a recent form of corporate governance to be employed in Jordan. In the following section, audit committee characteristics, such as independence, size, meetings and financial expertise that may be applicable in the Jordanian institutional background, are discussed for their impact on earnings management in literature review.

4. The Conceptual Framework and Hypothesis Development

The characteristics of audit committee and their relation with earnings management are integrated in one conceptual framework. Figure (1) explains the propose framework. In this conceptual framework, audit committee characteristics and earnings management are independent and dependent variables respectively. The current study thus attempts to bridge the gap by providing a basis for discerning the impact of audit committee characteristics on earnings management. Sections 4.1 till 4.4 will discuss the hypotheses that are developed from the conceptual framework.

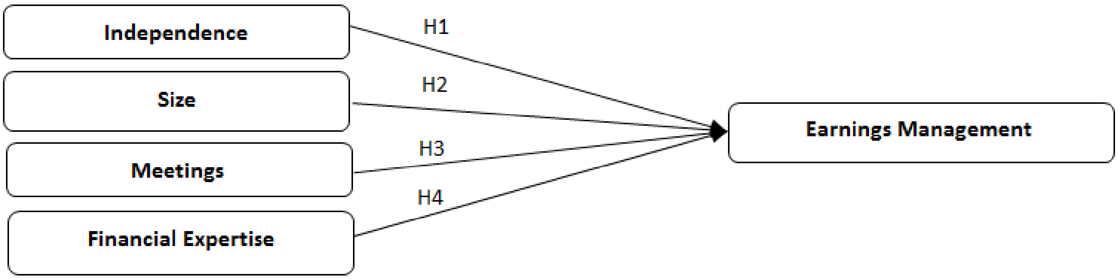

Figure (1) Audit Committee Characteristics and Earnings Management

4.1. Audit Committee Independence

The Independent Audit Committee, as a sub-committee of the board of directors, has oversight responsibility for the firm's financial reporting process. The Audit Committee provides a formal communication channel between the board, the internal monitoring system, and the external auditor, Deli and Gillan (2000) state that an audit committee serves as a reinforcing agent to the independence of internal as well as external auditor. Audit committees are expected to be more effective in the oversight of financial reporting when they are independent. Xie et al., (2003) mentioned that the more independent audit committee is argued to provide better governance compared to less independent audit committee. In literature less financial misstatements are associated with more independent audit committees (Abbott et al. 2000; Beasly, 1996; Beasly et al., 2000, Garcia-Meca and Sanchez-Ballesta 2009).

Several research studies have investigated the impact of having an audit committee on financial reporting quality. A common hypothesis is that independent audit committee directors would ensure better financial reporting and the expectation is generally supported by existing empirical evidence (Lin et al. 2006). Specifically, using a sample of 692 publicly traded U.S. firms, Klein (2002) investigates whether earnings management is related to audit committee independence. She showed a negative association between earnings management and the proportion of independent directors on the audit committee.

Furthermore, Bedard et al. (2004) investigate the effect of audit committee characteristics, namely, expertise, independence and activity, on the extent of earnings management based on a sample of 300 U.S. firms for 1996. Their findings reveal that aggressive earnings management is negatively associated with fully independent audit committees. These results support the Sarbanes-Oxley Act (2002) mandating complete independence of the audit committee. Benkel et al (2006) using a sample of 666 firm-year observations for the fiscal years 2001, 2002 and 2003. They found that higher levels of audit committee independence are associated with reduced levels of earnings management.

Additionally, Saleh et al., (2007) studied the effectiveness of some audit committee characteristics for 561 Malaysian firms in 2001. The evidence shows that the presence of a fully independent audit committee reduces earnings management practices. Using data of UK-listed companies in the fiscal years 2000 and 2002, Lei (2008) suggested that audit committee independence constrain the level of earnings management. In China, Lin et al., (2009) found that independence audit committee is associated with reduced levels of earnings management.

Recently, a meta-analysis study by Garcia-Meca and Sanchez-Ballesta (2009, p. 607), using the data of 35 empirical studies, and Kent et al., (2010) using sample comprised of Australian public companies listed on the Australian Stock Exchange in 2004. Both of them supported the notion that the independence of the audit committee constrains earnings management. Additionally, Alkdai and Hanefah (2012) found that independent non-executive directors in audit committee have negative significant relationship with earnings management by using a sample of 270 Malaysian Sharia-compliant companies during the period 2007-2009. Soliman and Ragab (2014) examine the association between the audit committee effectiveness, audit quality and earnings management practices of more active 50 Egyptian companies listed on the Egyptian Stock Exchange of the non-financial sector during the period 2007-2010. The results indicated that audit committees independence have significant negative association with earnings management.

In contrast, based on data collected from the UK listed firms for period 1993 to 1996, Peasnell, et al. (2000) showed no strong evidence to reinforce the view that the existence of an audit committee influences on the extent of income increasing manipulations to meet or exceed earnings management thresholds. Evidence for Spanish companies during the period 1999–2001, Osma and Noguer (2007) test whether the existence of an audit committee is effective in reducing earnings manipulation suggest that the existence of an audit committee does not play a vital role in constraining earnings management. In the USA, Xie et al. (2003) examine the effect of some characteristics of the audit committee on constraining earnings management and found that audit committee independence is not significantly associated with reduced levels of earnings management.

Abdul Rahman and Ali (2006) using Malaysian listed firms, they found an insignificant relationship between independent audit committees and earnings management. Siregar and Utama (2008) using Indonesian companies listed on the Jakarta Stock Exchange to examine the effectiveness of some corporate governance practices on earnings management. Their sample contains 144 firms and covers the periods 1995–1996, and 1999–2002. They failed to detect a relationship between audit committees' independence and earnings management.

Moreover, Habbash (2011) found an insignificant relationship between independent audit committees and earnings management by using a sample that consists of all companies listed on the Saudi Stock Market and that covers the period of four financial years (2006, 2007, 2008 and 2009). Waweru and Riro (2013) investigate the influence of corporate governance and firm specific characteristics on earnings management by Kenyan listed companies. Using panel data of 148-firm years obtained from the annual reports of the 37 companies listed on the Nairobi Stock Exchange, the study found that independence of the audit committee is not significantly related to earnings management, although the direction of the relationship is negative.

The contradictory findings of these various studies are not surprising, because the mere existence of an audit committee, without ensuring its independence and competence, cannot assurance the efficiency of the monitoring process, or its ability to detect and reduce earnings management. In Jordan, the audit committee should be composed of at least three members among the board non-executive members; two of them is independent members in the board (see JCGC, 2009). Accordingly, based on the above discussion, the following hypothesis is developed:

H_1: The audit committee independence is negatively related to earnings management among Jordanian listed Industrial companies.

4.2. Audit Committee Size

This study also includes the size of audit committee because audit committee size can have a significant effect on the monitoring of earnings management. The size of audit committee is referred to as the number of directors appointed to be members in the audit committee, in this regard there could be small, medium and large audit committees. The Blue Ribbon Committee (BRC) report of 1999 released the usefulness of having an audit committee and recommended that an effective audit committee of listed companies should comprise at least three directors.

These recommendations reflect the assumption that size is a very important attribute of the effective audit committees (e.g.Pincus et al., 1989). Although the size of audit committee is affected mainly by the size of the company and its board of directors, if the audit committee size is too small then an insufficient number of directors to serve the committee in occurring and thus decrease its the monitoring effectiveness (Vafeas, 2005). This perhaps because small committee is not capable of fulfilling its duties efficiently as the given assignments is always increasing. Also, when a committee size is too large, the directors' performance may decline because of the coordination and process problems and hence highlight another reason for weak monitoring (Jensen, 1993; Vafeas, 2005).

The perfect average of the audit committee size is between 3 and 4 members (Abbott et al., 2004; Xie et al., 2003). Evidence from the previous suggested that the firms with large audit committee are more effective in monitoring the management. Baxter and Cotter (2009) found that quarterly earnings management is lower for the firms that have large size of audit committee. This may suggest that having a sufficient number of audit committee members increases the efficiency of its monitoring function in terms of financial reporting integrity.

The findings of prior studies for the effect of audit committee size on earnings management are mixed and inconclusive. A negative significant relationship was found between the size of audit committee and earnings management practice according to the findings of Yang and Krishnan (2005) during examine the relationship between audit committee size and quarterly earnings management in 896 US firms in the years 1996 to 2000. They found that quarterly earnings management is lower for firms that have a larger audit committee size. Lin et al., (2009) using data from Chinese firms listing in Hong Kong 2004 to 2008, found that an audit committee size is associated with reduced levels of earnings management. Moreover, Kent et al. (2010) found a negative association between audit committee size and earnings management in Australian companies. Lin and Hwang (2010), employing meta-analytic techniques to the data from nearly 48 empirical studies, also found a negative and highly significant association between audit committee size and earnings management.

Xie et al. (2003) found no significant association between the number of directors on the audit committee and earnings management by using a sample of 282 US firms covering the period between 1992 and 1994. Likewise, Bedard et al. (2004), found no significant relationship between audit committee size and aggressive earnings management in US. Similarly, Abbott et al. (2004) found no impact of audit committee size on earnings restatement. Using the data of Chinese listed firms from 2002 to 2004 year, Zha (2006) examines the effect of the audit committee on earnings quality, it is suggested that the audit committee should improve earnings quality and broadening the size of the audit committee could increase earnings quality.

Using panel data regression for 270 Malaysian Shariah-compliant companies, Alkdai, and Hanefah (2012) found that audit committee size has non-significant relationship with earnings management in Malaysian Sharia-compliant companies. In Egypt, Soliman and Ragab (2014) using a sample of Egyptian companies. The results indicated that no significant relationship between audit committees size and the level of earnings management.

Additionally, using 97 Malaysian listed firms over the period 2002-2003, Abdul Rahman and Ali (2006) found a positive relationship between audit committee size and earnings management. Siregar and Utama (2008) argue that where there is positive relationship between earnings management and audit committee size it is attributed to efficient rather than aggressive earnings management. In Egypt, Metawee (2013) found that there is a positive relationship between the audit committee size and earnings management by using a sample from corporations listed on the Egyptian Stock Exchange from the years 2008-2010.

The audit committee size is one of the significant characteristics that contribute to its effectiveness. Thus, audit committee size can have a significant effect on the monitoring of earnings management. Accordingly, based on the above discussion, the following hypothesis is developed:

H_2: The audit committee size is negatively related to earnings management among Jordanian listed Industrial companies.

4.3. Audit Committee Meetings

Effective audit committees meet regularly to ensure that the financial reporting process is functioning properly, and therefore a well-functioning and active audit committee not only reduces earnings manipulation but also improves firm performance since it limits director interaction time (Vafeas 1999). Further, Klein (2002) suggests active audit committees as measured by the number of meetings are positively associated with audit committee independence. An important objective for an audit committee is to provide its members with sufficient time to perform their duties of monitoring their firm's financial reporting process (Lin and Hwang, 2010).

The BRC (1999) recommends that audit committees meet at least once quarterly and discuss financial reporting quality with the external auditor. The number of meetings (a proxy for diligence) is used in prior research because inactive audit committees are unlikely to monitor management effectively (Menon and Williams, 1994). In other words, the number of audit committee meetings is the only publicly available quantitative signal about the diligence of audit committees, and regulators have emphasized the need for frequent meetings of the audit committee (Raghunandan and Rama, 2007).

Previous studies suggested that firms with the higher number of audit committee meetings experience are less likely to be sanctioned for fraud as well as aggressive accounting (Abbott et al., 2000; Beasley et al., 2000). Abbott et al., (2000) found the negative relationship between meeting frequency and the occurrence fraudulent financial reporting using data 78 firms that were subject to SEC sanctions and 78 matched non-fraud firms in the period 1980 to 1996. Similarly, Beasley et al., (2000) found that the manipulation of financial reporting is not necessarily associated with audit committee meetings.

Song and Windram (2004) evaluate the audit committee recommendations of the Cadbury Committee (1992) in the UK and Blue Ribbon Committee (1999) in the US; they examine the effectiveness of UK audit committees in enhancing financial reporting. Their findings indicate that UK audit committees play a significant role in monitoring the effectiveness of financial reporting. They also found that the frequency of audit committee meetings increases the quality of financial reporting. Likewise, Xie et al., (2003) suggested that audit committees that meet regularly during the financial year are associated with effective monitoring. The more frequent they meet can constrain the levels of earnings management.

Doubtless, the effectiveness of audit committees depends, to a large extent, upon their actual operations or activities, such as the frequency, duration, and content of audit committee meetings (Abbott et al., 2004) found audit committees that meet at least four times per year exhibit a significant and negative association with the occurrence of financial reporting restatements through using data 41 firms that issued fraudulent reports and 88 firms which restated annual results in the period 1991-1999.

Furthermore, Ebrahim (2007) examined the relationship between earnings management and activity of board of director and audit committee. He selected a sample of US manufacturing companies for two years, 1999 and 2000; results indicated there is a negative relationship between earnings management with both board and audit committee independence and he documents that this relation is stronger when the audit committee is more active. , Lin et al., (2006) found no implicit evidence to indicate that frequent audit committee meetings will restrain fraud or earnings restatement. In addition, Saleh et al., (2007) found that firms which had more knowledgeable audit committee members and held more audit committee meetings recorded fewer earnings management practices for a sample of 561 Malaysian firms in 2001. Lin and Hwang (2010) found a negative relationship between audit committee meetings and earnings management.

Lei (2008) suggested that audit committee meeting frequency shows negative association with income-decreasing earnings management. He uses data of UK-listed companies in the fiscal years 2000 and 2002. Furthermore, Soliman and Ragab (2014) found that audit committee meetings have significant negative association with earnings management. In the same context, Metawee (2013) found also that there is a negative relationship between the audit committee meetings and the earnings management.

In contrast, Bedard et al., (2004) found an insignificant relationship between the number of meetings and earnings management. Likewise, a study by Yang and Krishnan (2005) fails to found a significant association. In the Australian context, Davidson et al. (2005) Baxter and Cotter (2009), the results indicate that a greater number of audit committee meetings do not seem to reduce either earnings management or to enhance earnings quality measures. Moreover, Lin et al., (2009) found that audit committee meeting frequency is not associated with earnings management in Chinese firms.

Effective audit committees meet regularly to ensure that the financial reporting process is functioning properly, and therefore a well-functioning and active audit committee may be able to prevent earnings management, in Jordan, listing Requirements of JCCG (2009) mandate that the audit committee shall meet at least four times per year. Accordingly, based on the above discussion, the following hypothesis is developed:

H_3: The audit committee frequency meeting is negatively related to earnings management among Jordanian listed Industrial companies.

4.4. Audit Committee Financial Expertise

In response to recent major accounting scandals and corporate frauds, regulators have been increasingly concerned with the effectiveness of audit committees in monitoring corporate financial reporting. One of the significant reforms to improve audit committee quality focuses on the financial expertise of audit committee members. In 1999, BRC recommends that each member of audit committee should become financially literate and at least one should have accounting or related financial management expertise.

Knowledge in accounting and finance provides a good basis for audit committee members to examine and analyze financial information. The educational background becomes an important characteristic to ensure audit committees perform their roles effectively. Moreover, audit committees that comprise at least one financial expert have greater interplay with their internal and external auditors (Raghunandan et al. 2001). Many studies argue that audit committees members' knowledge/expertise or experience is directly associated with effective functioning of audit committees (Bedard et al., 2004; McDaniel et al., 2002; Beasley and Salterio, 2001 and DeZoort and Salterio, 2001).

DeZoort and Salterio (2001) argue that the audit committee's financial expertise increases the likelihood that detected material misstatements will be communicated to the audit committee and corrected in a timely fashion. Abbott et al. (2004) suggested that the financial expertise of the audit committee is related with a higher financial reporting quality. Choi et al., (2004) show that the presence of at least one member with financial expertise sitting on the audit committee is negatively related to the level of earnings management.

DeZoort (1998, p.17) claimed that the experience of the audit committee members in accounting, and auditing is important for adequate understanding of oversight tasks. He suggested that: "…audit and internal control evaluation experience makes a difference in audit committee members' performance on an internal control oversight task. Of primary importance, audit committee members with experience made internal control judgments more like those of experts (practicing auditors) in the area than did members without experience". In addition, since the audit committee's main task is to oversee corporate financial reporting and auditing processes, its members should possess sufficient expertise to understand the issues to be investigated or discussed by audit committees (Lin and Hwang 2010). Song and Windram (2004) also demonstrate that financial literacy is one of the most important characteristics of the audit committee to monitor the quality of financial reporting.

Bedard et al. (2004) found that financial expertise is associated with a significant decrease in earnings management, where show that the presence of at least one member with financial expertise sitting on the audit committee is negatively related to the level of earnings management. In a similar way Yang and Krishnan (2005) found evidence that increased governance expertise is positively related with earnings management. In addition, Felo et al. (2003) found the percentage of audit committee members having expertise in accounting or financial management is positively related to the quality of financial reporting and the quality of the financial statement improve. Xie et al., (2003) found evidence that earnings management is reduced with audit committee members which comprise at least one member with a corporate or financial background.

DeFond et al. (2005) argue that audit committees with a financial expert strengthen corporate governance through improving the ability of the board to protect the interest of the shareholder as well as increase the value of the firm. The study found also that market participants positively react to the appointment of the audit committee with financial expertise in accounting, but there is no reaction noted for audit committees with non-accounting financial expertise.

In Malaysia, Saleh et al., (2007) some of the most important findings of the study are: the companies whose members of audit committee are distinguished for experience, financial knowledge, professionalism, in addition to frequent meetings of the committee have less practices of earnings management when compared to other companies. Additionally, Abdul Rahman and Ali (2006) supported the notion that the presence of financial experts of the audit committees constrains earnings management. Additionally, Lei (2008) found that financial expertise of audit committees constrain the level of earnings management. Further, Chang and Sun (2009) use a dummy variable for financial experts if at least one of the audit committee members possesses accounting experience. Their results indicate a marginally significant negative association between the presence of financial experts on the audit committee and earnings management.

Lin et al., (2009) found that an audit committee expertise is associated with reduced levels of earnings management. Lin and Hwang (2010) found a negative relationship between audit committee financial expertise and earnings management. In Egypt, Soliman and Ragab (2014) indicated that experience of audit committee members have significant negative association with earnings management. In the same context, Metawee (2013) found also that there is a negative relationship between the audit committee financial expertise and the earnings management.

In different words, both the regulatory concern as well as the experimental evidence suggested that having suitable experience and knowledge, mainly in accounting and auditing, is likely to improve the performance and judgment of the audit committee. The JCGC (2009) require that audit committees appoint at least one member of the audit committee has recent and relevant financial experience. Accordingly, based on the above discussion, the following hypothesis is developed:

H_4: The audit committee financial expertise is negatively related to earnings management among Jordanian listed Industrial companies.

5. Summary and Conclusions

The audit committee is one of the corporate governance tools that consist of a group of persons selected from members of the board of directors, has oversight responsibility for the firm's financial reporting process and provides a formal communication channel between the board, the internal monitoring system, and the external auditor. The ability of managers to manage reported earnings opportunistically is constrained by the effectiveness of internal monitoring such as audit committee. Activating audit committees leads to less practices of earnings management phenomenon, because an activated audit committee will restrict the different methods of earnings management phenomenon. Thus, this study discusses one of the elements of corporate governance which is audit committee characteristics.

Specifically, this paper intends to investigate the role of audit committee characteristics on earnings management among industrial companies listed on the Amman Stock Exchange (ASE). The role of audit committees in ensuring the quality of corporate financial reporting has come under considerable scrutiny due to recent high-profile earnings management cases in the world. To achieve this, four audit committee characteristics are proposed, namely, independence, size, meetings and financial expertise. In turn four hypotheses are developed to validate the hypothesis survey research will be undertaken.

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