

Corporate Governance and Financial Performance: The Role of the Audit Committee in Saudi Arabia

حوكمة الشركات و الأداء المالي: دور لجنة المراجعة في المملكة العربية السعودية

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Abstract :

This study examines the impact of audit committee characteristics one of the key mechanisms of corporate governance on the performance of companies listed on the Saudi Stock Exchange, Using data from 31 non-financial firms between 2019 and 2022, and firm performance was measured by return on assets. The main variables include audit committee size, meeting frequency, independence, and members' financial expertise, with firm size and financial leverage serving as control variables, The findings reveal that audit committee independence and meeting frequency are significantly and positively associated with firm performance, whereas committee size and members' financial knowledge show no significant effect, The study underscores the importance of audit committee characteristics in enhancing governance effectiveness and improving corporate performance within the Saudi context.

Keywords: Audit committee characteristics, Firms, performance, Governance, Saudi Stock Exchange.

الملخص:

هدف الدراسة إلى تحليل أثر خصائص لجنة المراجعة بوصفها أحد آليات الحوكمة المؤسسية الرئيسة على أداء الشركات المدرجة في السوق المالية السعودية، استندت الدراسة إلى بيانات 31 شركة غير مالية مالية مدرجة في السوق المالية السعودية خلال الفترة من 2019 إلى 2022، مستخدمة العائد على الأصول كمؤشر للأداء، وتناولت المتغيرات الرئيسة حجم لجنة المراجعة، وعدد اجتماعاتها، واستقلاليتها، ومستوى المعرفة المالية لأعضائها، مع إدراج حجم الأصول والرافعة المالية كمتمغيرات ضابطة، أظهرت النتائج أن استقلالية لجنة المراجعة وتكرار اجتماعاتها يرتبطان إيجابياً وبشكل معنوي بأداء الشركات، في حين لم تظهر خصائص الحجم والمعرفة المالية للأعضاء تأثيراً يذكر، وتؤكد الدراسة أهمية خصائص لجنة المراجعة في تعزيز فعالية الحوكمة وتحسين الأداء المؤسسي في البيئة السعودية.

الكلمات المفتاحية : خصائص لجنة المراجعة، أداء الشركات، الحوكمة، السوق المالية السعودية.

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1. INTRODUCTION

Corporate governance aims to protect owners and maximize firm value by ensuring that management prioritizes the interests of shareholders, who are the key stakeholders in the survival and continuation of the firm. This is accomplished through a set of rules and principles that guide management's actions toward shareholder interests, which leads to enhanced performance and value. Numerous studies, such as one by Roy (2016), have found a positive correlation between the degrees of corporate governance implementation and enhanced firm value and performance, evidenced by rising stock prices and returns. This is because better governance promotes better administrative performance and the ability to make effective management decisions. This conclusion is also supported by several other studies (Gupta & Sharma, 2014; Mousavi et al., 2010; Rostami et al., 2016) that found a link between improved return on assets and increased company value and good corporate governance practices.

However, prior research has demonstrated that the oversight function of the audit committee is a crucial component of corporate governance and performance enhancement. The Audit Committee is tasked with overseeing the company's financial reporting system, reviewing the internal control structure, supervising the internal audit function, and communicating with the external auditor. Furthermore, the committee serves as a tool for non-executive directors to monitor management's ethical conduct and adherence to applicable legislation and corporate regulations (Dezoort et al., 2002; Rezaee et al., 2003).

It should be noted that the mere formation of an audit committee alone does not guarantee that management is not engaging in fraudulent activity or that company activities are effectively overseen. Nor does it vouch for the accuracy of financial reports. Therefore, to carry out its duties efficiently, an audit committee requires several components (Mendez & Garcia, 2007). Chen & Zhou (2007) believe that an efficient audit committee is a crucial tool for supervising the financial reporting process and ensuring the accuracy of financial reports. This is because many attributes are necessary for the audit committee to be effective, such as having the right number of members, independence, holding meetings on a regular basis, and having members with experience in finance and accounting.

As part of corporate governance reforms, companies in the Kingdom of Saudi Arabia have established an audit committee. The Corporate Governance Regulations outline the powers and necessary qualities of the audit committee to boost investor confidence in companies listed on the Saudi Stock Exchange and enhance the stock market. According to these regulations, the Ordinary General Assembly may decide to form an audit committee composed of shareholders or other individuals, provided that there's one independent member, no Executive Board of Directors members are on the committee, and the number of members is between three and five. In addition, one member is required to be a specialist in financial and accounting affairs (Corporate Governance Regulations issued by the Capital Market Authority on 14/1/2021). The regulations also stipulate that the Audit Committee bears the responsibility of overseeing the company's operations and

confirming the integrity and security of reports, financial statements, and internal control systems. The competencies delineated by the Governance Regulations include the Audit Committee's function in financial reports, internal and external audits, and compliance assurance.

For this reason, one of the most crucial things for investors to consider is company performance. According to Tambun et al. (2018), forecasting future performance and stock returns is necessary to guarantee strong returns and reduce risks. Investors, scholars, and policymakers are interested in knowing the impact of audit committee characteristics.

As a result, the current study focuses on analyzing the influence of audit committee attributes on the firm's performance in the Saudi Stock Exchange as well as the key factors contributing to the firm's performance. This is accomplished by achieving the following objectives:

- Measuring the impact of the audit committee size on firm performance in the Saudi Stock Exchange.
- Measuring the impact of the audit committee meetings frequency on firm performance in the Saudi Stock Exchange.
- Measuring the impact of the audit committee independence on firm performance in the Saudi Stock Exchange.
- Measuring the impact of the financial knowledge of committee members on firm performance in the Saudi Stock Exchange.

The significance of this study stems from the necessity to consider the financial implications and effects of audit committee characteristics. Additionally, a suitable model is required to measure and explain the determinants of firms' performance. Furthermore, emphasis should be placed on how audit committee characteristics affect Saudi Stock Exchange firm performance. The remainder of this paper is organized into five sections: the literature review and hypotheses are covered in section two; the research design and methodology in section three; the results and analysis in section four; and the conclusion in section five.

2. Literature Review

After reviewing previous research connecting audit committee characteristics to firm performance, it's clear that the findings are varied. While some studies have observed a positive or negative correlation, others have found no influence at all.

Regarding the association between firm performance and audit committee characteristics, Al-Matari et al. (2012) found a significant link between the audit and firm performance, while audit committee independence and audit committee meetings were insignificantly related. Similarly, Al-Matari et al. (2014) found no connection between firm performance and the size, independence, or meetings of the audit committee. Amer et al. (2014) proved a significant relationship between audit committee size and independence and firm performance; however, they found no significant correlation between financial expertise, meetings, and performance. Zubair (2015) discovered that the audit committee's independence and financial knowledge greatly enhanced financial

performance, but found no association between performance and the audit committee's size or frequency of meetings.

Other studies present different results. Kipkoech and Rono (2016) found that audit committee experience and size had a significant effect on firm performance. Alqatamin (2018) showed a significant positive relationship between audit committee size, independence, and gender diversity and firm performance, while experience and meeting frequency had an insignificant relationship. Ashari and Krismiaji (2019) found a positive effect of all audit committee characteristics—including independence, size, competence, and frequency of meetings—on firm performance. Bagaisa and Aljaaidi (2020) proved that audit committee size was positively associated with firm performance (ROA), but found no relationship between the frequency of audit committee meetings and performance. Abeygunasekera et al. (2021) found a significantly positive effect of AC size, AC independence, and AC meetings frequency on firm performance. However, this same study confusingly stated that it found no relationship between AC independence and firm performance.

More recently, Oudat et al. (2021) proved a significant relationship between audit committee independence, audit committee meetings, and firm performance, but found no statistical significance between audit committee financial expertise, audit committee size, and performance. Umoh-Daniel et al. (2021) found that the frequency of AC meetings, AC independence, and AC size had a significant effect on financial performance. Shamsuddin and Alshahri (2022) proved that there is no relationship between audit committee size, independence, meetings, and firm performance. Finally, Al-Jalahma (2022) found that firms with large and independent audit committees were underperforming and that the frequency of audit committee meetings had no bearing on firm performance.

Based on the literature review and the study's objectives, the following hypotheses are formulated:

- H1: There is a significant impact of audit committee size on firm performance.
- H2: There is a significant impact of audit committee independence on firm performance.
- H3: There is a significant impact of the frequency of audit committee meetings on firm performance.
- H4: There is a significant impact of the financial knowledge of audit committee members on firm performance.

3. Methods and Materials:

The study population consists of Saudi public firms listed in Saudi Exchange from 2020 to 2023. Samples for the study are selected using the random sampling method. The data is obtained from the following sources: (1) the Saudi Exchange website (<https://www.saudiexchange.sa/>); and (2) websites of sample firms; Based on the aforementioned information and the random sampling technique, 31 non-financial firms have been chosen to represent a variety of Saudi market sectors.

This study uses the model below to test the research hypothesis:

$$\text{FIRPER} = \beta_0 + \beta_1 \text{ACSIZE} + \beta_2 \text{ACINDE} + \beta_3 \text{ACMEET} + \beta_4 \text{ACKNOW} + \beta_5 \text{LOGSIZE} + \beta_6 \text{FIRMLEV} + e$$

FIRPER indicates the firm's performance and is measured by ROA, which is equal to net income divided by total assets; ACSIZE is audit committee size and is measured by the number of committee members. ACINDE is the independence of the audit committee, which is calculated by dividing the total number of independent members by the audit committee's size. ACMEET is the frequency of meetings in one year; ACKNOW is the audit committee members' financial knowledge, measured by the number of members with accounting expertise in the audit committee; LOGSIZE is the firm size and is measured by the natural logarithm of the total value of the firm's assets; FIRMLEV is leverage, which is measured by the ratio between total liabilities and total assets.

4. Results and Analysis:

Descriptive Statistics:

Table (1) provides descriptive statistics for variables; the results indicate that the mean of FIRPER is 0.11 and the STD of FIRPER is 0.13. And the mean of ACSIZE, ACINDE, ACMEET, and ACKNOW is 3.48, 0.41, 5.44, 2.41, and STD is 0.23, 0.72, 0.19, and 1.75 respectively. Having a minimum value of -0.13, 3, 0.17, 3, 1 and a maximum value of 0.58, 6, 1, 11, 4 respectively. Moreover, in relation to the control variables, the mean of the LOGSIZE, and FIRMLEV were 9.17, 0.44, and STD were 0.92, 0.23, respectively.

Table (1) Descriptive Statistics

	Minimum	Maximum	Mean	Std. Deviation
FIRPER	-0.13	0.58	0.11	0.13
ACSIZE	3.00	6.00	3.4857	.72210
ACINDE	.17	1.00	.4119	.19210
ACMEET	3.00	11.00	5.4423	1.75060
ACKNOW	1.00	4.00	2.4054	.83534
LOGSIZE	6.52	11.47	9.1749	.92258
FIRMLEV	.01	.96	.4462	.23160

Correlation Analysis:

Table No. (2) Displays a summary of the correlation results. The findings demonstrate that all correlations are less than 0.80. It complies with Gujarati and Porter's (2009) assertion that, in order to guarantee that there is no multicollinearity problem, the correlation matrix should not be greater than 0.80.

Table No. (2) Correlation Matrix

		ACSIZE	ACINDE	ACMEET	ACKNOW	LOGSIZE	FIRMLEV
ACSIZE	Pearson Corr.	1					
	Sig.						
ACINDE	Pearson Corr.	.103	1				
	Sig.	.147					
ACMEET	Pearson Corr.	-.113-	.117	1			
	Sig.	.128	.119				
ACKNOW	Pearson Corr.	.016	.366**	-.086-	1		
	Sig.	.436	.000	.195			
LOGSIZE	Pearson Corr.	.360**	.121	.053	.082	1	
	Sig.	.000	.100	.300	.199		
FIRMLEV	Pearson Corr.	.245**	.000	-.161-	.347**	.177*	1
	Sig.	.007	.497	.056	.000	.033	
**. Correlation is significant at the 0.01 level (1-tailed).							
*. Correlation is significant at the 0.05 level (1-tailed).							

Regression Model

Table No. (3) Displays the results of the regression analysis used to test the hypotheses (3) According to the results of the regression model, the model's F value is 5.245, significant at 1%%, R2adj recorded a value of 0.123. All of the model variables' VIF coefficient values fell below the critical value, proving that there isn't a multicollinearity problem between the variables.

Table No. (3) Regression Models

	B	T Value	VIF
Constant	0.328	3.958***	
ACSIZE	-0.002	-0.151	1.277
ACINDE	0.082	1.740*	1.205
ACMEET	0.012	2.678***	1.071
ACKNOW	-0.003	-0.284	1.435
LOGSIZE	-0.031	-3.459-***	1.227
FIRMLEV	-0.053	-1.339	1.471
F value	5.245**		
R²	0.152		
R²adj.	0.123		

Note: *** significant at 0.01 ** significant at 0.05 * significant at 0.1

In the model, there is an insignificant impact of ACSIZE on the FIRPER in the Saudi Stock Exchange. The ACSIZE variable is insignificant as the audit committee size is not correlated with the firm performance in the Saudi Stock Exchange. Thus, H1 is rejected.

Furthermore, there is a significant impact of ACINDE on the FIRPER in the Saudi Stock

Exchange. The ACINDE variable is significant at 10% in the model, and the positive sign of the regression coefficient corresponding to FIRPER indicates that ACINDE is positively related to FIRPER. Consequently, enhancing the audit committee's independence will boost company performance on the Saudi Stock Exchange. Thus, H2 is accepted. Additionally, there is a significant impact of ACMEET on the FIRPER in the Saudi Stock Exchange. The ACMEET variable is significant at 1% in the model, and the positive sign of the regression coefficient corresponding to FIRPER indicates that ACMEET is positively related to FIRPER. Therefore, the more audit committee meetings there are, the better the firms' performance will be. Thus, H3 is accepted.

Moreover, there is an insignificant impact of ACKNOW on the FIRPER in the Saudi Stock Exchange. The ACKNOW variable is insignificant since the firm's performance on the Saudi Stock Exchange is unrelated to the frequency of meetings. Thus, H4 is rejected.

At the 1% significance level, LOGSIZE found a statistically significant inverse relationship with FIRPER in the Saudi Stock Exchange. The regression coefficient of this variable also has a negative sign, and this implies that as a firm grows in size, its performance declines. Nevertheless, it has not been proven that there is a significant relationship between FIRMLEV, and FIRPER in the Saudi Stock Exchange.

5. Results and discussion :

The results suggest that audit committee independence and activity—not its size are the governance levers most closely associated with firm performance in the Saudi market, Descriptive indicate committees are relatively small (mean ≈ 3.49) with moderate independence (mean ≈ 0.41) and meet with reasonable frequency (mean ≈ 5.44 times), while all bivariate correlations remain well below conventional multicollinearity thresholds and VIFs are comfortably low, supporting the reliability of the regression estimates. In the multivariate model ($F = 5.245$, adj. $R^2 = 0.123$), independence carries a positive coefficient significant at the 10% level and meeting frequency at the 1% level, consistent with the view that independent, active committees strengthen monitoring, accelerate remediation, and reduce informational frictions. These patterns align with mainstream agency-theoretic expectations and with evidence from other emerging markets where board independence and diligence tend to matter more than headcount. The negative, statistically significant coefficient on firm size further suggests that, in this setting, the complexities of scale may offset resource advantages an interpretation that resonates with “diseconomies of governance” arguments for diversified or rapidly growing firm.

By contrast, neither audit committee size nor the proxy for knowledge/expertise shows a statistically discernible association with performance once other factors are controlled. The null result for size is unsurprising given the narrow observed range (3–6 members), where marginal additions may increase coordination costs without improving oversight quality. The insignificance of the knowledge proxy likely reflects measurement limitations (e.g., counts or categorical disclosures may not capture depth, regency, or relevance of expertise) and potential endogeneity (firms with weaker performance may add “experts” ex post). Leverage is also unrelated to performance in this

specification, implying capital structure is not the dominant channel once governance intensity is considered. Overall, the model explains a modest share of variation appropriate for complex performance outcomes yet the signals are policy-relevant: firms should prioritize truly independent appointments and ensure committees meet often with substantive agendas, rather than expanding membership or ticking “expertise” boxes. Future work could test robustness with richer expertise metrics (e.g., tenure-adjusted financial credentials), alternative performance measures, and designs that address reverse causality (e.g., lag structures, instrumental variables, or system GMM), and benchmark the findings against prior Saudi and GCC studies to gauge the external validity of these effects.

6. Conclusion:

This research explored the link between the attributes of an audit committee and the performance of companies on the Saudi Stock Exchange. The analysis, which drew on data from 31 firms across Saudi Arabia's key market sectors, led to three main conclusions.

Firstly, the study confirms that audit committee independence is a strong driver of firm performance; as independence increases, so too does a company's performance. Secondly, the frequency of meetings also plays a positive role, with more frequent meetings being associated with better financial outcomes for firms. Finally, the study found no relationship between firm performance and two other variables: the size of the audit committee and the financial literacy of its members.

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