AUDIT COMMITTEE CHARACTERISTICS, REGULATORY CHANGES AND FINANCIAL REPORTING QUALITY IN IRAQ: SOME LESSONS FROM SOX ACT

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—Abstract—

This study aims to examine the impact of audit committee characteristics such as audit committee size, audit committee meetings, audit committee independence, and the financial expertise of audit committee on the quality of financial reporting in non-financial firms operating in Iraq. In addition to that the study also examines the direct and moderating role of regulatory changes at the nexus between audit committee characteristics and quality of financial reporting in the context of non-financial firms in Iraq. The particular focus of the study is on the implications of Sarbanes-Oxley Act in Iraq. For this purpose, the author selects 170 organizations as the study sample which comprises a total of 850 firm-year observations. For further analysis, only 575 organizational-years observations are included. The multiple regression model is used to analyze this data. Referring to the resource dependence theory, results indicate that characteristics of an Audit Committee are highly resourceful, which leads to enhancement of the financial reporting quality because of the expertise, greater skills, and shared experiences.

The regulatory changes also appear to be a significant direct and intervening factor in the relationship between the characteristics of an Audit Committee and reporting quality in the non-financial firms of Iraq.

**Keywords:** Audit Committee, Sarbanes-Oxley Act, Financial reporting, Iraq

JEL Classification: G30, G32

1. **BACKGROUND**

Financial reporting is the upshot of the economic performance of a company which is accessible to the general public. The basic objective of financial reporting is to apprise stakeholders of information pertaining to financial performance of the company. Financial statements are the most integral part of financial reporting. With the help of financial statements, an organization makes itself capable of projecting its financial positions and financial upshots to the users. In order to make rational decisions, financial statements are utilized by the financial analysts (Yahaya et al., 2017). As a rule, no financial statement should be prepared in a way which could mislead the user intentionally and deliberately (Jehu, 2018). Financial statements are generally incorporated by managers for misleading investors and manipulating their understanding through earnings management about the value of the firm (Lo et al., 2017). This act, of managers misleading stakeholders or trying to affect effect contractual results that depends upon shown accounting numbers by manipulating the financial reports is referred to as earnings management (EM) (Abner et al., 2017b; Lo et al., 2017). The present study discusses EM as the opposite behavior of financial reporting quality (FRQ) in terms of reversibly exchanged contexts as higher the EM, the lower the FRQ and vice versa (Christensen et al., 2017). The reliability and reliance elements of accounting earnings serve as the basis for the quality of financial reporting (Christensen et al., 2017). Therefore, the relevance of accounting earning of any company to the stakeholders is extremely important because the stakeholders’ trust depends on it. In financial statement, due to its assistance in direct allotment of the resources in capital market, accounting earnings is considered as a crucial element. Several creditors and investors use this summarized financial information of company’s performance (Goh et al., 2019).

If the earnings are dependable they are considered as relevance earnings and if a system works according to expectation then it is referred to as a reliable system (Závodný, 2021). Yet, in order to determine EM, quality of earnings is considered as a crucial factor (Závodný, 2021). Therefore, the efforts put by management for making permanent discrepancies of incomes even, may result in lowness of earnings quality. Additionally, it is observed that the companies show accruals so that they may pose a substandard performance or they may hide a good performance so that they could retain it (Passos, 2020). Therefore, the opportunities provided to the managers for choosing accounting
 approaches are exploited by them as they also exploit the knowledge they gain about the company and evaluate a befitting approach with the business economics through which accounting numbers are prospected to have a significant increment (Abner et al., 2017a). Thus, for the sake of improvement in the reporting system, there is a requirement to employ a certain method to maintain reliability and relevance. In order to assist stakeholders, a corporate governance system has been developed by lining up the interests of managers and investors, and through bringing the improvement in reliability of the financial statistics and element of genuineness regarding procedure of financial reporting (Inua, 2018). External auditors and AC are some of the main elements of the corporate governance procedures. Therefore, it is emphasized by Agency Theory that it should be made sure that the agent is acting in the favorable interests of the stakeholders. AC is completely authorized to keep an eye on financial reporting systems, though the BOD is present for observance of the managerial activities (Gardi, 2021b). Therefore, overall responsibility of results due to the imprecise financial reporting is concerned with the AC including SEC action and lawsuit (Gardi, 2021a). In order to deal with the preferences of the managers about approximating the accounting numbers, AC has been discussed in this study as it is considered as an integral part of corporate governance practices (A.A Zaid et al., 2020). The primary aim of AC is to improve FRQ by increasing the quality of audits. Additionally, in corporate governance mechanism, external auditors play a crucial role in boosting the legitimate protection of external stakeholders (Bala et al., 2019). They are responsible for mitigating the conflict between the principal and the agent by ensuring that the reporting system is error-free and financial reports are precisely prepared without any material manipulation, reducing the chances of illegitimate reporting practices and fraudulent activities. Different researches have focused on the role of AC regarding monitoring management (Ali C. Akyol, 2020; Ashraf et al., 2020a; Ullah et al., 2017). In order to escape from any errors and losses of the reputation emerging from lawsuits, it is affirmed that independent members of AC need to have a higher quality of audit. It has been discussed by Ali C Akyol (2020) that governance is only improved by the proficiency of AC regarding financial experiences yet quality of financial reporting is improved through broader financial skills. However, as Gardi (2021a) affirms the legitimate experts of AC act as the checker instead of being an indicator of financial reporting quality. Ashraf et al. (2020b) and Oussii et al. (2018) contend that for the purpose of reduction in EM, the proficient members having financial accounting expertise are considered crucial and, ultimately, quality of financial reports gets to be improved. Furthermore, it has been discussed by earlier researches that the greater the quality of audit, the greater is the reliability of the financial reports which would ultimately leads greater assurance and protection for investors (Khanh et al., 2018). Therefore, to improve the reliability of the financial reports, audit quality is also considered as an integral part of corporate governance mechanism along with the monitoring management practices (Khanh et al., 2018). For an auditor to be irrelevant in case of appearance and mind is the key factor for having a greater quality of audit.
Therefore, the independence of auditor is confirmed by AC; which boosts up FRQ. In order to protect the investors, for the surveillance of reliability of financial reports and auditing mechanisms, AC alone would not prove to be enough (Khanh et al., 2018). According to the prior literature, the external audits and internal governance can be used as proxies for each other which shows that no complementary input is required by the external audits if the internal control system is strong. Although, their suggestions are not empirically verified (Ullah et al., 2017). From yet another perspective, it is proposed by earlier studies that external audits and internal governance carry a complementary impact with higher audit quality always leading to a better system of internal governance (S. Hasan et al., 2018; Khanh et al., 2018).

2. LITERATURE REVIEW

Financial reporting is perceived as a dual activity as those who prepare financial reports make them vulnerable to the users, and furthermore, these stakeholders expect to implement those financial reports in making economically benefitted decisions. The fundamental aim of financial reporting is that these financial reports are relevant to the firm, which is important for the stakeholders, in order to help them make valuable decisions as investors. To overcome this obligation, the financial reports are responsible for presenting information pertaining to the resources of the company, the company’s resource subscriptions, company dealings as well as limitations to making changes in organizational behavior. The reason behind this is that broadcasting financial information is an important way for the management to highlight important aspects of the governance and financial performance of a company to the capital providers (A. Habib et al., 2018). Therefore, it is crucial to develop a higher quality of broadcasting of economic information for ensuring resource allocation, investment and credit decisions for bringing up market productivity, as it affects the stakeholders’ decisive capability. Since most of the people take support of financial evidences for disclosure of the information, that is why FRQ holds an important role in investment portfolio (A Habib et al., 2018). Alam et al. (2019) define FRQ as “the accuracy of the financial reports with which the information of performance of a company’s operations is communicated, especially the cash flows of the company which are means of informing the shareholders”. According to the definition of FRQ provided by Herath et al. (2017), it is said that; FRQ is the extent of accuracy of integral and fair disclosure of financial accounts focusing on the fundamental performance and financial condition of a company. Therefore, FRQ is contemplated as a complete and clear revelation of economic performance through which the users are not prone to deception (Shankaraiah et al., 2017). It has been postulated by Agency Theory that, due to the fact that investors are required to be protected because of difference of interests between the managers and the investors, since the investors and managers acts on separate agenda which ultimately leads to poor fulfilment of owner’s interests (Kyere et al., 2021). To reduce this element of uncertainty, the serves of external auditors are engaged to ensure a better and unbiased
examination of financial reports of a company. Monitoring procedures can involve these stages so that the quality of financial reporting improves and at the end would lead to the enhancement of owner’s trust on the performance of the company and a confidence would be built on corporate repute reflecting securities (Masum et al., 2019). The principal-agent cost and discrepancies would be reduced due to the broadcast of financial information. The uncertainty issues in the financial reports would decrease through a more high-quality financial reporting system and therefore the agency cost will see a reduction. IT bears to note there is no agreement points of scholars and practitioners on what elements constitute FRQ. It is observed that Shankaraiah et al. (2017) affirm that AC members, auditors and management are striving to define FRQ properly. It has been previously advocated that the transparency and clarity in the information disclosure system and financial evidence’s quality are proximal to each other. There is no point on which various scholars could mutually agree to define and explain transparency or quality. Therefore, the quality of reporting is a preconception and is not aligned with the accounting criteria and benchmarks. Moreover, other traditional factors, e.g., the legal structures, the existence and enforcement of laws of investor protection and ethics regarding disclosure and corporate governance, also impact the supply and demand of financial reporting. Prior research focuses on the conservative side of accounting quality, that is, the extent to which losses are transformed into the income aptly. It is crucial to study FRQ beyond the perspective of conservatism as it is a multidimensional and substantial perspective (Campa, 2019).

Among the main elements of corporate governance, Audit Committee is considered to be a crucial one (Wahid et al., 2020). Therefore, the primary aim of AC is to keep significant surveillance over the financial reporting system of a company. The reliability of the financial reports is protected through improvements in the internal controls and external auditing system to fulfil their responsibility of surveillance. AC has been defined by Hasan et al. (2020) as; AC is a crew of members who are chosen by the board of directors to be responsible for maintaining the independent view of the auditors. AC is defined by The Liu et al. (2020) as a body identified by and included in the associates of the board of directors of a corporation which has a goal of examining the accounting and financial reports of a corporation and auditing the company’s financial reports. The fundamental purpose behind development of AC is to inspect the board of directors and enhance the audit quality of a company. The discriminant features of board of directors in checking and monitoring the decisions made by the managers about the broadcast of financial information is referred to as AC (Firoozi et al., 2016). Hence, it has been affirmed that international professional bodies, government authorities and regulatory agencies consider the AC as means of enhancement of financial reports’ transparency and reliability (Ahmad et al., 2018). There are three classifications for AC which encompass formation of AC effectiveness of AC (Khanh et al., 2018) and characteristics of AC (Buallay et al., 2018b; Kjærland et al., 2020; Oussii et al., 2018). The present study holds more relevance in relation to characteristics of AC which have a significant
impact on financial reporting quality. Therefore, it is important to study the characteristics of AC which influence FRQ and this perspective has not been discussed in the previous researches (Ahmad Haruna et al., 2021). Furthermore, AC is taken as an independent construct as it is considered effective in the domain of corporate governance surveillance process which has an important role in judgement of decision of the managers in the approximation of the accounting numbers.

2.1 Sarbanes-Oxley Act (SOX) of 2002
For many past years, improvement and betterment to boost the quality of accounting and audit is being kept in practice (Ahmad Haruna et al., 2021). However, the need for a stronger financial reporting system has emerged since Enron in 2001 and other 40 corporations faced blackout. Uncertainties and weaknesses of corporate governance became noticeable among the U.S. SEC registrants with the activation of the clauses of the Sarbanes-Oxley Act (SOX) in 2002. There was a model shift in the management obligations and the responsibilities of the auditors became more extensive, as stipulated under SOX. Due to several clauses of SOX, which focused more on improving internal control systems rather than financial reporting procedures, there was a great impact on SEC registrants and public reporting companies’ accountants. Disclosure and analysis of internal control system is specially linked by SEC registrants to Section 404 of SOX in order to develop a better financial reporting environment. The clauses of this section stipulate that it is the responsibility of the management to examine if the financial reporting standards are maintained and if any error is present. This investigative effort on the part of the management also enables the firm to stay abreast of certain weaknesses and any insufficiencies in the internal control system in addition to the fact that the firm becomes more capable, with the help of disclosure and examination of internal control, to set aside the resources to maintain the internal control (SEC 2003). In a similar manner, it has been observed that SOX removes the perceived risks to the independence of the auditors, ultimately increasing their independence. Establishment of a quasi-governmental agency in this regard is referred to as the Public Company Accounting Oversight Board (PCAOB). The responsibility of this agency is to strictly check the external auditors and impose a heavy penalty if any contravention of law is observed. Additionally, some particular non-audit activities are forbidden by SOX, which should not be performed by any authoritative auditor. For any auditor who does not abide by the law and is responsible for misdoing in the company by demanding extensive broadcast of financial information is liable to an inflexible and strict penalty. Internal control systems of the client should be clarified by the authoritative auditors. When the surveillance increases, there is an inflexible punishment and a mediator requirement, in a rising conflict, which reassures that there is enough reliance on auditors and the rights of capital providers are safeguarded (Hamdan, 2020). Along with it, there is a beginning of corporate governance initiatives due to SOX clauses across the world, also involving the Manual of Corporate Governance in Ghana 2002, South Africa’s King Report on
Corporate Governance 2002, the review of UK Combined Code of Corporate Governance (CCG), the Malaysian CCG 2002 and Iraq CCG 2003. There is a serious censure over passage of SOX. Critics, neglecting the advantages, are more focused about the argument which passed expeditiously that it is “driven by political convenience”, and no real-time issue was discussed which resulted in the collapse of financial reporting procedures (Choudhary, 2018a). Many others suggest that it is overly expensive, and the benefits do not balance the incurred cost.

2.2 The Influence of SOX on FRQ/Audit Quality
Most existing research focuses on the effect of newly imposed regulations over the quality of financial reporting process and strength of the internal control. Few of the studies which encompass; (El Mahdy et al., 2019; Liu et al., 2020) investigate reaction of market toward SOX. However the following studies had their focus on the cost; (Aljaaidi et al., 2021; Lee et al., 2019). The studies conducted by (Manahipor et al., 2017) investigate the impact of Section 404’s on other SOX provisions’ aspects on FRQ. Whereas, Hamdan (2020) examines the influences of SEC demands and SOX as these two measures of conservatism should be certified by the CEOs and CFOs of the company: first; financial statements on the magnitude EM and second, the stock returns’ coefficient of a company. Findings obtained by contrasting optional accruals regarding the two spans of time indicate to a decline in the magnitude of EM. Additionally, dissimilarity among the earnings coefficients for companies bearing positive stock returns and the companies having negative stock returns show an increment in conservatism in the after-SOX period. In general, the findings of Hamdan (2020) describe that financial statement quality increases. Complementary evidence has been generated by doing a “quasi experiment” to segregate other concurrent events, based on the results obtained, it can be claimed that reported earnings conservatism increases by promulgation of Section 404. It has been examined by Choudhary (2018a) that reported accruals’ quality succeed to the obligatory revelation of deficiency in internal control and external auditor clarification. It has been suggested on the basis of the findings of the present study that those companies which impart internal control deficiencies and get uncertified audit suggestions after the promulgation of Section 404 show a decrease in the magnitude of the absolute value of discretionary accrual as compared to that period in which the weakness is first revealed. Findings show that internal control weakness’s disclosure proved to be beneficial for market competitors. In parallel to this, Mardessi et al. (2020) investigate the magnitude of discretionary accrual relevant to after-SOX time span by incorporating real earnings management and accrual earnings management. Even though, in alignment with the prior researches, Mardessi et al. (2020) report that for the after-SOX time span, a decline in accrual earnings management is observed; whereas, there is an increment in real earnings management for the same time span. The results of (Mardessi et al., 2020) demonstrate a more fascinating affirmation, due to SOX, advising the management to swap towards more expensive and tougher to
determine earnings management methodology referred as the real earnings management methods.

3. HYPOTHESES

Referring to the resource depending theory, it is believed that size of Audit Committee is highly resourceful, which leads to enhancement of the financial reporting quality because of the expertise, greater skills, and shared experiences of the Committee (S. R. M. Musallam, 2018). It might be an important reason of arguments presented by previous studies that size of AC significantly impacts management capacity to monitor. Hasan et al. (2020) confirm this through their finding that there exists a negative association between size of AC and EM and in case of U.S. companies, it has a positive association with financial reporting quality. From this perspective, it could be expected that increment in AC size would lead to reduction in earning manipulation, consequently improving the corporate FRQ. Few recent researches support the negative association between DA and AC. Previously mentioned arguments affirm the findings of Kasih et al. (2017) as they project the part of service period of director in the independence and effectiveness of Audit Committee. It has been demonstrated by their findings that there is a significant negative relationship between size of AC and EM. Thus, it can be observed that EM can be mitigated if the size of AC is larger. Moreover, research investigate AC characteristics and discretionary financial disclosure in the premises of Indonesian companies. Findings for the study indicate that AC size holds a significantly positive effect on the discretionary disclosure of financial information. In a recent study by Ahmad Haruna et al. (2021), it is shown that there is a significantly positive relationship between accounting conservatism and size of Audit Committee. Furthermore, it is affirmed by Ismail et al. (2017) that a company’s income smoothing behavior keeps a negative association with AC size. Hereby, an illusionary description of creative accounting is supported which is practiced by corporations. Researches of Bala et al. (2019) which have been conducted in Iraq claim to advocate the significant negative relationship between AC and EM. Thus, the findings are affirmed from the previously mentioned argument which demonstrates that there is a significantly negative relationship between discretionary accruals and size of AC. EM is effectively reduced if the size of AC is larger i.e. there is a greater number of AC members. However, the primary postulate of agency theory proposes that smaller the boards, the greater the monitoring mechanism and the easier the process of decision making (Marsidi et al., 2018). It has also been proved by recent empirical studies that the greater the size of AC, lesser would be EM and higher would be quality of financial reporting (Bala, 2019). Moreover, as indicated by significant negative association between AC size and EM, as a result of a greater size of AC, FRQ is enhanced. Therefore, corresponding to resource dependence theory, it is anticipated that there is a negative linkage between AC size and EM but there is a positive linkage of AC with FRQ. The reason behind this is, larger AC would be having broader experiences shared among themselves as compared to the
smaller size of AC. Therefore, making it obvious that a larger size of AC would be more capable of mitigating EM. Thus, aligning with the prior arguments, this study proposes that:

**H1: There is a positive relationship between AC size and FRQ of the listed companies in Iraq.**

It has been postulated by the Signaling Theory that if a corporation is seeking to increase the number of non-executive board of directors, then the owners may believe that the investors’ protection is high and corporate governance is stronger in the case of that particular corporation. It has been observed in the findings of prior researches that an independent Audit Committee has a strong impact in terms of reduction of managers’ opportunist behaviors and thus FRQ is enhanced due to AC (Kjærland et al., 2020). The illusive perspective has been supported that in reporting of earnings, the smoothing of income is totally unacceptable. It has been affirmed by their findings that if there is greater involvement of an independent AC, then the probability of fraud reduction through smoothing income is lowered. Furthermore, this argument is strengthened by Ismail et al. (2017) as they affirm that there is a significant negative association between an independent AC and income smoothing in Malaysian Companies. The impact of AC attributes on EM regarding Indonesian corporations has been examined by Bala et al. (2021). It is found in the present study that there is a positive significant relationship between independence of AC and real EM. Lately, financial reporting quality and AC characteristics of Kenyan listed companies are investigated, and a negative relationship is found between the independence of AC and FRQ. The prior mentioned argument is advocated by (S. Hasan et al., 2018) after finding a negative relationship between DA and AC. Conversely, how corporate governance plays its part in reducing the misbehavior of management in Thailand is examined. Results of their research demonstrate a positive association but the relationship is deemed to be non-significant which shows that the management may behave in an adverse or unethical way. Thus, these arguments affirm few researches that AC exerts a stronger effect on restatements and DA (Surbakti et al., 2019). Thus, it has been demonstrated that higher the independence of AC on the board, higher would be the accruals and there would be greater probability of restatement of earnings. Poretti et al. (2018) affirm that there would be higher market reactions to the earnings proclamations if the members (independent directors) of AC of a company are higher in ratio. It is further explicated that the weaker institutions can boost the reliability of their earnings proclamations if the AC are authoritative and independent. Furthermore, it is found out that there is a significantly negative relationship between AC and DA. Jerry et al. (2018) conduct their research in Iraq, describing that the FRQ in the oil companies are being enhanced by the independence of AC. Additionally, from this study it has been affirmed that the enormity of working capital accruals is reduced through an independent AC. It is contended by
Jehu (2018) that FRQ is increased and earning manipulations are reduced when AC is independent. Lately, Poretti et al. (2018) put forward an argument that there is a positive and significant impact of AC independence on FRQ. Ali C. Akyol (2020) stress that there is a significantly negative relationship between AC independence and DA. Thus, it can be claimed that due to the presence of independent AC members, FRQ is boosted up. Being aligned with the Signaling Theory, it can be said that if a corporation is seeking to increase the number of non-executive board of directors then the owners may believe that the investors’ protection is high and corporate governance is stronger vis-a-vis that particular corporation, ultimately, improving the financial reporting quality (Nassir Zadeh et al., 2018). Thus, it can be proposed that:

**H2: There is a positive relationship between Audit committee independence and FRQ of the listed companies in Iraq.**

With regard to the Agency Theory, it is argued that the Audit Committee members are motivated for considerable and meaningful meetings through which financial reporting quality and monitoring system see improvement. It has been affirmed by the prior studies that higher the frequency of audit committee meetings, lower will be the requirement to restate earnings. This is because, the audit committee when coordinating with internal auditors, can results in upgradation of the information about the auditing and accounting problems (Ullah et al., 2017). Similarly, some arguments are made by Buallay et al. (2018b) that due to the higher frequency of AC meetings, FRQ is enhanced and there is a significant reduction in DA. Conversely, results of insignificant associations of AC and DA have been produced by other research studies (Ahmad et al., 2018). From another perspective, it has been observed that there is a significantly positive relationship between the AC meetings’ frequency and EM, higher EM is a resultant of frequent AC meetings. Moreover, the promptness of financial reporting and effectiveness of AC from the perspective of Indonesia has been studied by Nassir Zadeh et al. (2018). Based on the results, it has been claimed that with more frequent meetings and effectiveness of AC, the time required form audit gets reduced to report. Lately, quality of Audit Committee and financial reporting quality in India has been studied by Shankaraiah et al. (2017). Their findings demonstrate that there is a negative and significant influence of AC on FRQ substituted by DA. Nassir Zadeh et al. (2018) also confirm this by examining whether governance practices hold any impact on EM of Islamic banks. Results of the study prove that there is a negative association between permissive loan loss and Audit Committee. Moreover, Shankaraiah et al. (2017) conduct a study in Iraq which demonstrate that AC meetings hold a significantly negative effect on discretionary loan loss provisions, meanwhile contending that in Iraq listed corporations, real EM increases due to the frequency of AC meetings. Impacts of AC characteristics and financial reporting quality in Iraq listed companies are studied. Results demonstrate that frequent AC meetings have a significantly positive relationship with FRQ. The same has
also been advocated by Shankaraiah et al. (2017) suggesting that both of the constructs share a significant positive association. Furthermore, the impact of frequent AC meetings on EM from the perspective of Iraq listed companies is studied by Velte (2017). It is found out that in Iraq listed corporations, AC meetings have negative relationship with EM. Thus, it can be affirmed that AC effectiveness and activeness can be a reason behind enhanced FRQ. Hence, it can be deduced that FRQ and monitoring management is improved through frequent AC meetings. Therefore, this study proposes that:

**H3:** There is a positive relationship between audit committee meetings and FRQ of the listed companies in Iraq.

In regard with Resource Dependence Theory, development of resources is the purpose of AC, and encompassing those experiences and skills which make a firm capable of achieving competitive edge specifically related to financial reporting quality. AC expertise and skills are considered as a crucial driver of a firm to achieve its strategic goals and an integral part of corporate governance (Ahmad Haruna et al., 2021). The agency issues emerging due to the opportunist behavior of managers are reduced through provision of adequate monitoring. In different subdivisions of AC expertise, financial accounting expertise holds a crucial position. It has been studied and mentioned in the previous literature that those firms which incorporate a higher ratio of financial accounting experts in audit committee are more likely to reduce the fraudulent activities and make the monitoring process more efficient, ultimately improving FRQ. In one past study, it has been affirmed that practice of restatements of earnings is mitigated by accounting experts in AC. Meanwhile, it has been suggested by S. R. Musallam (2018) that level of EM is reduced by the accounting experts of AC and they can ultimately enhance FRQ. Arguments are presented by Ali C Akyol (2020); S. R. Musallam (2018) Ashraf et al. (2020b) and Bala (2019) that financial reporting quality is boosted up through accounting expertise on AC. Moreover, it has been affirmed by Hasan et al. (2018) that DA of a company is restricted by accounting expertise on AC. Likewise, it is contended that the monitoring system becomes more effective when there is a larger ratio of financial experts on AC and accounting conservatism is improved when there is strong governance mechanism. Arguments made by Bala et al. (2021) state that there is a significantly positive relationship with financial accounting skills with real EM. Findings of Bala et al. (2021) are supported by the prior mentioned arguments; they investigate the linkage of fraudulent activities with AC attributes. Thus, the results show that there is a negative relationship between financial fraud and financial accounting experts. It has been demonstrated that those firms in U.S. which have a higher proportion of financial accounting experts in AC are more likely to avoid and escape financial frauds. Thus, the dependence theory postulates state that the AC accounting experts prove to be vigilant financial experts who enhancing the monitoring capacity of AC (Abubakar et al., 2021; S. R. Musallam, 2018). The reason behind this is; accounting
expertise is much more relevant to AC attributes as compared to others, as ‘best practices’ suggest that the AC is responsible for the missions which requires greater extent of accounting refinement (Ali C Akyol, 2020). Therefore, it can be claimed that if there is a higher proportion of accounting experts in AC then there would be a greater probability of fraud detection. Consequently, leading towards the enhancement in FRQ through AC. Thus, the study proposes that:

**H4:** There is a positive relationship between Audit committee financial accounting expertise and FRQ of the listed companies in Iraq.

In the past few years, there have been a number of incidents which point to the effectiveness of financial reporting quality, and these events have resulted in the development of new initiatives to tackle the challenges in this regard. Generally speaking, regulatory enforcement regarding financial reporting auditing directs the perception of the auditors in constructing financial statements. The enhancement of financial reporting quality is the main aim of any regulatory change; it has been focused by this study that the incentives of auditors and statements’ preparers are altered if there is any kind of improvement in financial reporting quality. It is confirmed by (Abubakar et al., 2021; S. R. Musallam, 2018) suggesting that auditors are encouraged to opt those audit ways which are better for the quality and are more likely to avoid any persecution. As in, accounting bright lines involved in a rule-based reporting authority can be incorporated by the preparers and auditors to give transactions a proper structure (Ali C Akyol, 2020). And these regulations can be utilized later to escape any aggressively reporting censure. Nonetheless, auditors and preparers face the pressure of justifying their reporting selections to the regulators in case of absence of bright lines of accounting. IFRS shares a similar context because IFRS includes incorporation of professional selection and perceptions in case of choosing accounting methods and anticipations. Thus, justification of the aggressive accounting becomes burdensome. Briefly, for selecting the aggressive reporting, there is a probability of being criticized by regulators and the cost of legal actions demotivate the preparers from using such an approach. Auditors and preparers incentives have been investigated from the perspective of regulatory changes by some of the researches (Abubakar et al., 2021). The auditor’s monitoring behavior has been examined by Mardessi et al. (2020) on the basis of accounting benchmarks and robustness of external regulatory authorities. An experimental design is deployed which includes auditors and their preference of lease categorization incorporating two distinct regulatory authorities. It is reported by them that, in relation to the regulatory authorities’ strength, aggressive reporting is restricted by the auditors in addition to using a principle-based authority than under a rule-based authority. The results confirm through these conclusions, as they found out that how the robustness of internal enforcement procedures restricts the preparers under rule-based and principle-based criteria in case of aggressive reporting. It has been observed that
CFOs are not motivated to incorporate aggressive reporting under a less accurate (more principles-based) criteria than under a more accurate (more rules-based) criterion. Al-Okaily et al. (2020) posit that there would be lesser involvement of a financial statement preparer when using less accurate method for aggressive reporting. In regard with the predictions, while implementing IFRS, the financial statement preparers are not encouraged to give aggressive reporting. Moreover, Okaily et al. (2020) conduct an experiment on whether there is an impact of auditor-reporting orientation on the financial managers’ decisions regarding reporting in rule-based regimes or principle-based regimes. Generally, the results showed that any modification in reporting orientation of an auditor relevant to principles increases the quality of reporting under a principle-based regime. The studies conducted by (Abdulmalik et al., 2019; Moses et al., 2020) provided empirical evidences for affirmation. It has been reported that earning quality is enhanced by IFRS. Karami et al. (2019) suggest that the clause of SOX leading to a deep exploration of publicly listed companies and auditors, increases the independence of the auditor and thus earnings quality also boost up. It is demonstrated that deceptive alteration of financial results can be avoided by IFRS by means of transaction structuring. Deducing from the prior mentioned arguments, it is predicted that the threat of being criticized in regard to aggressive reporting and persecutions because of regulatory change may encourage the preparers to adopt better methods which may improve the quality. In regard with the Process Accountability Theory, focusing on in-depth description and cognitive struggle are practiced in the financial statements’ fabrication. There are certain accounting choices on which the auditors and preparers agree upon, which produces a sound financial statement of a company. The design of FRCN, which contributes to the set of rules for corporate reporting process in Iraq, reflect that a firm might take serious actions through its board of directors on lawless and misbehaving auditors along with their clients. The present study would stimulate them to enhance the financial statements’ quality. Likewise, the incorporation of IFRS can also lead to enhanced reporting quality (Cadot et al., 2021).

**H5:** There is a positive relationship between regulatory changes and FRQ of the listed companies in Iraq.

**H6:** The regulatory changes moderate the relationship between the size of the audit committee and FRQ of the listed companies in Iraq.

**H7:** The regulatory changes moderate the relationship between the independence of the audit committee and FRQ of the listed companies in Iraq.

**H8:** The regulatory changes moderate the relationship between the audit committee meetings and FRQ of the listed companies in Iraq.

**H9:** The regulatory changes moderate the relationship between the audit committee financial accounting expertise and FRQ of the listed companies in Iraq.
4. MODEL DEVELOPMENT

The standard equation of pooled OLS is given as follow

\[ Y_{it} = \beta_0 + \beta_1 X_{it}' + \varepsilon_{it} \]  

\[ i=1 \ldots n, \text{ and } t=1 \ldots m \]  

Where the subscript \( i \) is representing the cross-sectional dimension of variable, \( t \) is denoting the time series dimension of variables \( Y_{it} \) is denoting the dependent variables represent the dependent variable and \( X_{it} \) is denoting the set of independent or explanatory variables in the model, \( \alpha \) is a constant term, \( \beta \) is the vector of estimated coefficients and \( \varepsilon_{it} \) is the error term whose value is given by

\[ \varepsilon_{it} = v_{it} + u_{it} \]

Based on the equation 1 the econometric model of the current study will be

\[ FRQL_{it} = \alpha_0 + \alpha_1 ACM_S_{it} + \alpha_2 ACM_{it} + \alpha_3 ACM_{MM}it + \alpha_4 ACM_{FE}it + \varepsilon_{it} \]  

\[ FRQL_{it} = \alpha_0 + \alpha_1 ACM_S_{it} + \alpha_2 ACM_{it} + \alpha_3 ACM_{MM}it + \alpha_4 ACM_{FE}it + \alpha_5 REGC_{it} + \varepsilon_{it} \]  

The moderator hypothesis is accepted or rejected on the following basis i.e. if outcome of interaction term is significant or insignificant. The linear model of moderated relationship by Hair et al. (2006) is reproduced as follows:

\[ Y=Y_{it} = \alpha_0 + \alpha_1 X_{1it} + \alpha_2 X_{2it} + \alpha_3 X_{1it}X_{2it} \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots \ldots (4) \]

Where:

- \( \alpha_0 \) = Intercept
- \( \alpha_1 \)X1= Linear effect of X1
- \( \alpha_2 \)X2 = Linear effect of X2
- \( \alpha_3 \)X1 X2= Moderating effect of X2 on X1

Moderating effect of MPPI in the relationship between CRR and the funding LR

\[ FRQL_{it} = \alpha_0 + \alpha_1 ACM_S_{it} + \alpha_2 ACM_{it} + \alpha_3 ACM_{MM}it + \alpha_4 ACM_{FE}it + \alpha_5 REGC_{it} + \alpha_6 ACM_{S}*REGC_{it} + \alpha_7 ACM_{M}*REGC_{it} + \alpha_8 ACM_{MM}*REGC_{it} + \alpha_9 ACM_{FE}*REGC_{it} + \varepsilon_{it} \]  

\[ (5) \]
5. DATA
We selected 170 organizations as a sample size which comprised of 850 firm-year observations. A total of 575 organizational-years observations were included and 55 organizations with 275 organizational-year observations were discarded. The summary statistics of the sample is shown in Table 1.

Table 1: Summary Statistics

<table>
<thead>
<tr>
<th>Variable</th>
<th>Obs</th>
<th>Mean</th>
<th>Std.Dev.</th>
<th>Min</th>
<th>Max</th>
</tr>
</thead>
<tbody>
<tr>
<td>FRQL</td>
<td>575</td>
<td>.648</td>
<td>.285</td>
<td>.227</td>
<td>1.364</td>
</tr>
<tr>
<td>ACMS</td>
<td>575</td>
<td>2.7</td>
<td>3.323</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td>ACMIN</td>
<td>575</td>
<td>1.375</td>
<td>6.128</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>ACMM</td>
<td>575</td>
<td>3.192</td>
<td>5.963</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td>ACMFE</td>
<td>575</td>
<td>1</td>
<td>1.23</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
<td>REGC</td>
<td>575</td>
<td>1</td>
<td>1.345</td>
<td>0</td>
<td>1</td>
</tr>
</tbody>
</table>

5.1 Data Analysis
Panel data has been incorporated in the present study comprising two features namely; Time series and cross sectional. Various corporations were chosen for the data collection along with a significant time span, and this has been the logic behind the incorporation of Panel data. The study performs initial analysis with the correlation test. The results reported in Table 2 highlight that there was no issue of multicollinearity in the chosen study sample.

Table 2: Correlation

<table>
<thead>
<tr>
<th>Variables</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
</tr>
</thead>
<tbody>
<tr>
<td>FRQL</td>
<td>1</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ACMS</td>
<td>2</td>
<td>0.1361</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ACMIN</td>
<td>3</td>
<td>-0.1090</td>
<td>0.3088</td>
<td>1.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ACMM</td>
<td>4</td>
<td>0.1569</td>
<td>0.0104</td>
<td>-0.4533</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td>ACMFE</td>
<td>5</td>
<td>0.0139</td>
<td>0.2107</td>
<td>0.2195</td>
<td>-0.1154</td>
<td>1.00</td>
</tr>
<tr>
<td>REGC</td>
<td>6</td>
<td>0.0425</td>
<td>-0.2254</td>
<td>-0.0501</td>
<td>-0.0552</td>
<td>-0.1007</td>
</tr>
</tbody>
</table>

Moreover, the obtained data was analyzed and evaluated by inferential and descriptive statistics. The nature of the obtained data is explicated by the descriptive statistics. In order to show the linear association among the constructs, correlated was incorporated. For ascertaining the impact of AC characteristics on FRQ, the authors used the regression analysis. Although the mediating role of audit quality on the linkage between AC attributes and FRQ is also determined by regression analysis. For the purpose of enhancing the reliability and validity with respect to inferences statistics, Stata was used to do some of the robust tests. These tests comprise the heteroscedasticity, normality test, serial correlation test and multicollinearity test.
A multivariate multiple regression was incorporated by the present study which is usually implemented for the sake of modelling the relationship among a set of criterion variables and different independent variables. By following the footsteps of (Bala et al., 2021), for income smoothing on (Manukaji, 2018), the study deployed a binary logit regression as dichotomous variables (1 and 0) represent them. Although moderation effect was examined through different methods and techniques, but structural equation model (SEM) and multiple regression are mainly applied. Multiple regression was incorporated to serve the aim of this study. Multiple regression proves to be more efficient and accurate particularly handling categorical criterion variable that is why multiple regression was used in this study.

Multiple regression is accurate because estimations regarding a model can have an impact on moderation effect evaluations. That is why an option for categorical regression (logistic or probit regression) is being provided by multiple regression during the evaluations. Nevertheless, estimation techniques which are frequently implemented in SEM speculate the continuity of the observed and latent variables. Even though multicollinearity is also not contemplated. Therefore, it has been stressed by Mehmetoglu (2018) that the examination of the existence of multicollinearity, linearity, normality, and heteroscedasticity is crucial before the initiation of a moderation analysis. Various diagnostic tests were applied in order to choose the most adequate estimation methods (as demonstrated in Table 3). Firstly, for apprehending the heteroscedasticity problems in our aggregate model, the White Heteroscedasticity test was applied. The test results led to a rejection of the null hypothesis at the 5% significance level in our aggregate model, where the p-value is falling in the range of 0.0000 and 0.0020. It was evident through this result that there is a heteroscedasticity issue in the aggregate pooled model and thus it has been advised to use random effect estimates.

The results of the study indicate that the audit committee characteristics and regulatory changes had significant impact on the quality of financial reporting in Iraq. Meanwhile, the quality of financial reporting has a significant moderating relationship with the quality of financial reporting.

6. CONCLUSION
An important role is played by AC for the increment in reliability of earnings where there is a weak system to safeguard the investor and a weak system of executing accounting standards (Poretti et al., 2018). The discriminant features of board of directors in checking and monitoring the decisions made by the managers about the broadcast of financial information is referred as AC (Firoozi et al., 2016). It is observed that there is a mixed evaluation of results in studies conducted on features of AC and FRQ (Ahmad et al., 2018; Buallay et al., 2018b; Kjærland et al., 2020; Oussii et al., 2018; Surbakti et al., 2019). There has been no significant relationship found between AC characteristics and FRQ till yet in existing studies.
Previous studies have explored the association between FRQ and AC characteristics by incorporating different variables including board size, Audit Committee meetings’ frequency (Drogalas et al., 2021), independence (Kjærland et al., 2020), including women in Audit Committee and expertise relevant to Audit Committee (Bala, 2019). Thus, it has been examined by Gardi (2021b) that alterations made in the engagement of financial experts in Audit committee of the company have motivated the authors to conduct more studies regarding the association of AC and FRQ. Therefore, not only financial expertise is needed to be focused, but rather attention should also be paid on other levels of expertise such as legitimate expertise and public accounting expertise. It has been observed in prior literature that corporate governance encompasses one of the crucial elements; namely, AC attributes, as it deals with the reduction of expedient behavior of the managers and making improvements in the process of financial reporting. The research conducted shows that EM is mitigated by the establishment of AC. In a similar manner, it is contented by Bala (2019) that smooth artificial income is
remarkably reduced by the involvement of AC and a strong system of corporate governance. In a recent study Otuya et al. (2017) inspect the EM and corporate governance regarding Jordan-based companies throughout the years from, 2009 to 2013. It has been shown that FRQ is boosted and EM is mitigated due to engagement of AC. Otuya et al. (2017) affirm this and discuss how better information broadcast is done through the assistance of AC, enabling the companies to prepare financial reports with strong figures. Also, it has been studied by A.A Zaid et al. (2020) that in Iraq, there is an impact of corporate governance practices on the value of extensive income reporting. Their findings project that there is a direct and positive relationship between corporate governance devices which also encompass characteristics of AC, and the pricing of shareholders with regard to remaining comprehensive income. Moreover, Bala (2019) have investigated the impacts of AC indicators, accounting consequences and corporate value in the US. Their findings indicate that there is little participation of effective AC regarding issues of accounting, restatements and laying off the auditor after indulging in several conflicts. The impact held by 217 eminent firms of Europe regarding the effect of AC and FRQ from 2004 to 2013 is examined by Bajra et al. (2018). Their findings show that effectiveness of AC is directly associated with the financial reporting quality. There is no surprise in the preceding findings as not enough focus has been laid on the AC by the authors and the practitioners by noticing the reforms presented by the global bodies. Moreover, Abdeljawad et al. (2020) provide evidence of impact of AC enforcements and the director’s autonomy on the Chinese financial reporting. A qualitative approach consisting conduction of interviews has been used by them in 2009. Findings of their evaluation project that the basic objective for deployment of AC is to achieve conventional roles and not to ensure proper surveillance. Due to this reason, directors and AC members are not developing an environment of effective checking rather they are more indulged in conventional practices. Therefore, the AC’s effectiveness is significantly determined through the reciprocation between the input of the external auditors and AC with the assistance of official and abrupt procedures (Choudhary, 2018a). Wahid et al. (2020) advocate that for this reason, there is a dire need to conduct research on the communication of auditors with the AC members discussing the contexts of Audit Committee. Their findings further elaborate that the exposure of AC is still less than the BOD perspectives.

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