INTERNATIONAL JOURNAL OF ACADEMIC RESEARCH IN BUSINESS & SOCIAL SCIENCES

Vol 14, Issue 11, (2024) E-ISSN: 2222-6990

Audit Committee as a Corporate Governance Mechanism with the Firm Financial Performance in Saudi Arabi

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To Link this Article: http://dx.doi.org/10.6007/IJARBSS/v14-i11/23573 DOI:10.6007/IJARBSS/v14-i11/23573

Published Date: 04 November 2024

Abstract

Purpose: The aim of this academic inquiry is to investigate the relationship between the characteristics of audit committees (including independence, competence, chair independence, and chair competence) and the financial performance of firms. **Design/methodology/approach:** The current study is a conceptual paper that discusses the relevant literature on the characteristics of audit committees (AC) and provides a conceptual framework for understanding the link between AC features with firm financial performance. **Findings:** This research suggests a conceptual framework that can be applied to process FP issues of non-financial Saudi listed firms and how corporate governance mechanics such as AC characteristics facilitate firm financial performance. **Originality/value:** The uniqueness and significance of this research are derived from the scarcity of investigations that have scrutinized the correlation between the attributes of the AC and the financial performance of corporations listed in the Saudi market, subsequent to the application of the new governance code in 2018 and extending to the present day.

Keywords: Corporate Governance Mechanisms, Ac Characteristics, Firm Financial Performance.

Introduction

It is widely acknowledged that firm performance (FP) serves as a pivotal metric influencing the decision-making processes of numerous stakeholders. Academics and financial analysts, for instance, utilize corporate performance indicators to analyze comparable organizations within a defined industry or to evaluate entire industries or sectors in aggregate(Al Farooque et al., 2020). Enhancing FP has become imperative for a company's realization of the profit maximization objective. Conversely, inadequate FP will reflect management's inefficacy, ineffectiveness, and elevated risk of insolvency (Adedeji et al., 2019). Consequently, FP constitutes a fundamental issue for organizations and business professionals in the global markets, including the Saudi Arabian market, given its severe ramifications for an entity's stability, longevity, and profitability. (Al-Janad, 2021).

One of the paramount practices adhered to by publicly traded corporations in both advanced and emerging economies is the implementation of corporate governance (CG) practices to maintain the performance of companies and protect them from any collapse or fraud (Farooq et al., 2021). CG predominantly focuses on the dynamics between a corporation's executive management and its assemblage of shareholders, creditors, and board members, along with additional stakeholders such as customers, vendors, personnel, and the broader economic environment in which the corporation operates (CAM; SCGC,2017).

Implementing excellent audit committee (AC) characteristics in businesses is a key advantage of CG requirements around the world (Farooq et al., 2021; Guluma, 2021; Queiri et al., 2021 Banerjee et al., 2020). The predominant factor contributing to the failures of corporations can be ascribed to inadequacies in corporate governance standards, particularly the ineffectiveness of audit committees. The instances of financial scandals involving Enron Corporation and WorldCom in the USA, as well as Satyam, Citic Pacific, and SK Networks in various Asian nations, serve as salient examples of the collapse of corporate governance (Al-ahdal and Hashim, 2022). Likewise, in Saudi Arabia, the recent corporate failures, instances of fraud, or bankruptcies, such as those involving Saudi Paper Manufacturing, National Gas and Industrialization, AlMojil Group, Alkhodari, and Wafa, can be attributed to inadequate corporate governance practices, specifically regarding the function of audit committees within certain listed entities(Boshnak, 2021; Alfalah et al., 2022).

Consequently, numerous nations have endeavored to implement governance frameworks aimed at cultivating the confidence of stakeholders. In recent years, there has been a heightened interest among global regulators in investigating the exceptional attributes of AC members to ascertain their proficiency, as financial acumen and expertise are positively correlated with enhancing the effectiveness of the oversight of financial documentation scrutiny(Hezabr et al., 2023; Oudat et al., 2021). Most corporate governance regulations around the world require the presence of an AC that is independent and has the necessary financial knowledge. However, the degree and percentage of the AC's independence varies from one country to another. For example, countries such as the USA, UK, Canada, South Africa, and Malaysia require full independence for the AC in joint stock companies, while the Saudi Corporate Governance Code (SCGC) amended in 2017 requires that the AC have at least one independent member, and does not require the AC chairman to be an independent member (Habbash, 2022).

Additionally, the SCGC, 2017 mandates the inclusion of a financial expert within the Audit Committee due to the specialized focus and interest in financial matters prevalent in most governance frameworks. Nevertheless, the Code failed to provide a precise definition of a financial expert, thereby delegating the responsibility for such determinations to individual companies. For instance, an individual possessing a Master of Business Administration may be designated as a financial expert without an assessment of their proficiency in accounting or finance, irrespective of whether they have acquired an academic or professional qualification in these fields (CAM; SCGC,2017). Consequently, this research aims to identify particular attributes of AC and analyze their correlation with the financial performance of publicly traded firms, particularly within the context of an emerging economy like Saudi Arabia.

The AC plays an instrumental role in safeguarding the autonomy and transparency of efficient reporting, which in turn enhances organizational performance and profitability (Musallam, 2020; Wahh et al., 2021). Agency theory posits that the proficiency and independence of an AC are pivotal in augmenting the reliability of the financial reporting system, thereby inhibiting management from manipulating data for personal gain (Ashari & Krismiaji, 2020; Alfalah et al., 2022). Additionally, the expertise and independence of AC members are significantly more effective in assessing the compliance processes of financial reporting, particularly concerning agency costs and issues pertaining to firm performance (Al-Hadrami et al., 2020). Conflicts between conflicts of interest between executives and the shareholders of corporations may cause enterprises to fail (Jensen & Meckling, 1976). According to the perspective of agency theorists, the proficiency and autonomy of the audit committee represent critical mechanisms for overseeing agency costs that arise from the asymmetry of information between principals and agents (Ashari & Krismiaji, 2020). Consequently, within a context characterized by uncertainty, the AC can play a pivotal role in mitigating these conflicts and assisting organizations in safeguarding their investments and enhancing their performance(Al Farooque et al., 2020; Bazhair, 2021; Farooq et al., 2021; Jensen & Meckling, 1976).

In recent times, the Saudi non-financial sector has experienced poor and downward performance. Based on the data of the Capital Market Authority (CMA), the average of financial indicators such as Return on Assets (ROA) and Return on Equity (ROE) of the non-financial sector in the Saudi CMA has fallen in recent years. The performance of Saudi nonfinancial public listed firms (SNFPLF) has steadily worsened. The observed decline in the ROA and Tobin's Q (TQ) ratios signifies a divergence in performance outcomes. The average ROA and TQ for various non-financial sectors within Saudi enterprises exhibit volatility in the FP of the SNFPLF listed on the Saudi Stock Exchange. Over a three-year span, the ROA consistently remained negative and hovered near zero across most sectors, whereas the TQ metric indicated values of less than one across all sectors, with 64% of sectors reporting figures below 0.50. Furthermore, there has been a notable increase in the number of companies experiencing accumulated losses in recent years, as illustrated in Figure 3 below. The proportion of companies that have incurred losses exceeding 20% of their capital surged by 120% from 2015 to 2019.

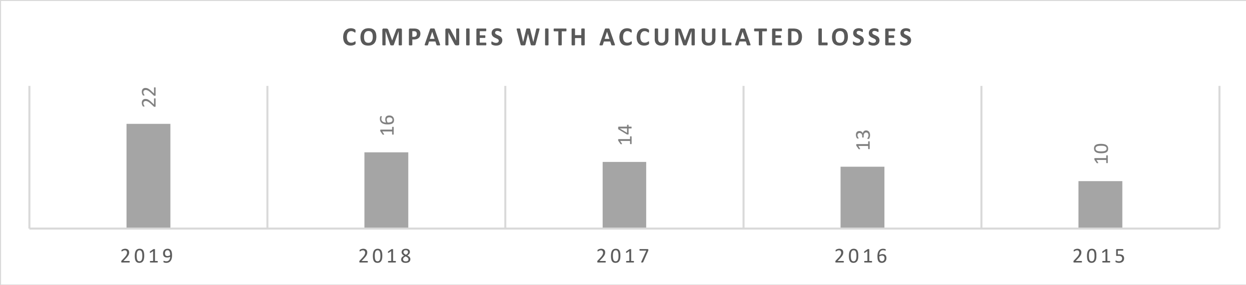


Figure 1. The number of Companies with Accumulated Losses
Source: https://cma.org.sa/Market/Documents/Companies.pdf

Moreover, an array of scholarly investigations has highlighted that the paramount factors influencing the performance of publicly traded companies in Saudi Arabia encompass the composition of the firm's board of directors, the efficacy of the audit committee, and the configuration of the ownership structure(Al-Matari, 2022; Al-Janad, 2021; Boshnak, 2021; Alawi 2019). The latest CG rule placed a great emphasis on the requirement for AC to have at least one member specializing in financial and accounting matters, as well as an independent member (CAM; Saudi Regulations on Corporate Governance, SRCG,2017). The preponderance of independent members within the AC, particularly those with specialized expertise in accounting, is critical for enhancing business performance and profitability (Musallam, 2020; Wahh et al., 2021). Nevertheless, numerous empirical studies conducted in Saudi Arabia have indicated that the correlation between the AC and FP remains contentious (Bagis and Al-Jaidi, 2020).

Despite the extensive scholarly inquiry into FP within developed nations, it still is required to be researched in the emerging business environment (Al-Gamrh, 2020; Al-Janadi, 2021; Bazhair & Alshareef, 2022; Al Farooque et al., 2020). In 2016, the Kingdom of Saudi Arabia unveiled its Vision 2030, which has precipitated a multitude of transformations, advancements, and enhancements within the corporate landscape of Saudi Arabia, particularly concerning the governance frameworks and both the financial and non-financial performance metrics of enterprises (Habibi, 2019). Consequently, the influence of certain AC attributes, such as competence and independence, necessitates further investigation in relation to corporate performance, especially within the context of the Saudi market, following the recent governance code that emphasizes the importance of these characteristics in all audit committees of listed companies (Bagais & Aljaaidi, 2020). In addition, there has been an increasing interest among global regulators in assessing the financial expertise and independence of AC members. To create best practices for regulators and practitioners in the global business arena, it is critical to understand how CG frameworks affect firm performance.

The existing body of literature concerning CG and financial performance has been characterized as contentious, lacking a unified agreement on this issue (Queiri et al., 2021). Each nation possesses distinct attributes; this assertion has been thoroughly corroborated by multiple research investigations (Queiri et al., 2021). Primarily, the investigation will make a substantial contribution to the corpus of extant literature by identifying various determinants influencing FP across diverse sectors within Asian emerging economies. This interest stems from the aim of determining whether the presence of these characteristics has any impact on enhancing the efficacy of monitoring financial records and the performance of firms (Al-Hadrami et al., 2020; Hezabr et al., 2023; Oudat et al., 2021; Wahh et al., 2021). Hence, this study needs to explore the impact of the independence and competence of the AC and its chairman on the performance of the SNFPLF.

This research has numerous sections. Following the introduction in Section 1, the literature review, hypotheses generation, and theoretical framework are presented in Section 2. The research methodology and conclusion are presented in Sections 3 and 4, respectively.

Literature Review

This section succinctly delineates the concepts of FP, CG, and the AC. Furthermore, it elaborates on the development of hypotheses, the principal theories underpinning this relationship, and the conceptual framework of this research endeavor.

Financial Performance

Firm performance defines as the organizational ability to employ the company's resources to improve the capabilities to achieve the company's goals (Bazhair, 2021). The foundation of financial performance is growth, profitability, and increase in market value (Rahman et al., 2017), and one easy method to entice investors is to provide them with larger returns. The management's effectiveness in using the firm resources is reflected in the high financial performance, which contributes to the country's economy.

It is also considered one of the most important indicators that reflect the company's profitability, clarify its financial picture, and determine its ability to compete. Thus, it is considered a crucial tool for all stakeholders to make their decisions related to this company. Previous studies (Bazhair, 2021; Boshnak, 2021; Farooq et al., 2021; Guluma, 2021; Alessandr & Cyganska, 2021) used Return on Assets (ROA) as a measure of the firm performance. ROA is the first and one of the main profitability and financial indicators which applied by investors before making their investment decisions (Alessandr & Cyganska, 2021).

Corporate Governance

Good CG is a system that addresses the responsibilities of customers, executives, commissioners, and managers. In order to achieve the fundamental objectives of the enterprise, these stakeholders advocate for competitive efficacy (Najamuddin et al., 2022). The perspective of the agency posits that superior CG is associated with heightened valuation, as numerous potential values of the enterprise are acknowledged by its proprietors rather than appropriated by management or passive investors (Dyck & Zingales, 2004).There are two types of CG mechanisms: internal and external governance (Guluma, 2021). External governance refers to a control mechanism outside the corporation, such as state legislative strategy and market restrictions. Internal governance denotes the board of directors and its associated sub-committees, which function as supervisory entities for the executive directors of the corporation (Khanchel, 2007).

In Saudi Arabia, the government identified the need to develop the country's capital market to diversify the economy and reduce its reliance on oil revenue (Bazhair and Alshareef, 2022). Thus, in 2016, Saudi Arabia launched Vision 2030, which primarily intends to change the economy from an oil-based economy to a diversified one. The document encompasses three principal themes, namely “a dynamic society,” “a prosperous economy,” and “an aspirational nation.” Moreover, a primary emphasis is placed on fostering the domestic private sector and enhancing living standards and sustainability, by proposing a series of detailed and specific objectives, such as governance reforms, the attraction of foreign investments, and the augmentation of governmental investments (Alregab, 2021).

The Saudi CMA initially promulgated regulations and guidelines aimed at mitigating future systemic occurrences following the collapse of the Saudi stock market in 2006, which experienced a substantial decline of 60% attributed to inadequate corporate governance among other factors. This precipitated the establishment of a governance code, which was optional for enterprises and initially comprised 19 articles. Nevertheless, a significant development in CG in Saudi Arabia transpired in 2017 with the issuance of a new code designed to enhance the performance of the SNFPLF post the 2006 stock market crash (Al-Faryan, 2020). This regulation was more comprehensive and obligatory, encompassing 98 articles. The primary goal of CG is to gain shareholders' trust by convincing them that the firm is working in their greatest interests, implementing best practices for integrity, and attracting as many investors from around the world as possible (Alfalah et al., 2022; Alsurayyi & Alsughayer, 2021).

In accordance with the revised CG framework of 2017, it is mandated that all publicly listed companies establish an AC as well as a remuneration and nominations committee. Nonetheless, the significance of the AC is underscored by the statutory requirement to do so under the Saudi Companies Law, which allocates an entire chapter to this committee, while the organization of the remaining committees is delegated to the Governance Regulations for Listed Companies.

Audit Committee

The AC holds a significant position within an organization and is recognized as a vital entity. It is of great importance in ensuring the sustainability of companies and protecting them from accounting manipulation (Habbash, 2022). AC is required to possess in-depth knowledge regarding the internal operations and controls of the organization in order for the owner (client) to ensure that the management (agent) works with integrity and professionalism (Alqaraleh et al., 2022; Oudat et al., 2021).

In addition, the AC is responsible for monitoring the reporting of both financial and non-financial information to reduce information asymmetry between companies, executives, and stakeholders (Appuhami &Tashakor, 2017). Likewise, the efficacy of the AC is greatly affected by the chair's role. The AC chair is responsible for disseminating important information to other committee members, management, the board, and the CFO. Relations with other relevant parties, such as internal and external auditors, are also a major part of the AC chair's responsibilities (Tanyi and Smith, 2014).

The existing body of empirical research generally suggests that firms with superior characteristics in their AC perform better due to reduced agency costs and increase more effective monitoring mechanisms (Al-Matiri, 2022; Ashari & Krismiaji, 2020; Oroud, 2019). Moreover, the principles governing CG necessitate that AC perform their responsibilities independently and maintain professionalism to ensure accurate information is recorded in the financial records (Bazhair & Alshareef, 2022; Qeshta et al., 2021). Numerous previous scholars have lauded the AC as a vital instrument for ensuring high-quality governance and enhancing financial performance (Hezabr et al., 2023; Alodat et al., 2022). The audit committee plays an important and major role in the stability and protection of the company from incurring bad consequences and financial setbacks (Ashari & Krismiaji, 2020; Oroud 2019). Bagais and Aljaaidi (2020), also stated that the audit committee exists for the resolution of any conflict of interest between managers and shareholders and in doing so the enhancement of company performance. Lastly, in a previous study by Al-Zaben (2020), on a sample of companies listed in Saudi Arabia and the United Arab Emirates, the company’s performance is better when all members of the audit committee have independence and financial and accounting experience, including the committee chairman.

The agency theory supports an AC's competence and independence to improve the credibility of the financial reporting process and prevent management from inflating data to serve their interests (Ashari & Krismiaji, 2020; Alfalah et al., 2022). Based on the agency theorist’s viewpoint, the audit committee's competence and independence are important mechanisms for monitoring agency costs caused by asymmetric information between principals and agents (Ashari, & Krismiaji. 2020).

In Saudi Arabia, the SRCG 2017, in Article 54, has defined the powers, authority and responsibility of AC in monitoring the company’s business and verifying the integrity and honesty of financial reports and internal control systems. This inevitably could lead to improving confidence in financial reports with the aim of increasing the degree of reliance on them in making sound decisions. In addition, it is the only committee that is formed by the company's Ordinary General Assembly. The amended code also stipulates that AC shall not include any executive member and the size of its shall not be less than three and not more than five members, including the committee chairman. It is the only committee in which the Board Chairman is prohibited from being a member. The committee must also include at least one independent member and one accounting and financial expert member. Lastly, the code does not require the committee chairman to be independent or has financial or accounting experience, but rather left it as guidance article that the decision-makers in the company can decide on (CAM; SCGC,2017).

Accordingly, what has been mentioned above represents the main motivations for choosing the audit committee and adopting some of its distinctive characteristics to examine their relationship with the financial performance of companies listed in the Saudi market. Therefore, examining the link of audit committee's independence, competence, chair's independence and chair's competence with Saudi companies performance has become necessary and vital.

Research Hypotheses

AC Independence

AC independence refers to the degree of autonomy and impartiality of the audit committee in carrying out its oversight responsibilities (Islam & Hashim, 2023). Ancient and current CG literature has indicated that greater AC independence is higher quality of financial information provided to the stakeholders (Abbott et al., 2003; Jesuka and Peixoto, 2021). AC independence has been discussed as part of the corporate governance mechanism that can bring various perceptions to AC discussions, thereby allowing a wider reflection of firm performance (Al- Matiri, 2022; Ashari & Krismiaji, 2020; Oroud, 2019). Despite the considerable research on the association between AC independence and firm performance, the empirical findings on this relationship have somewhat been mixed. For example, researchers such as Al- Matiri (2022), and Jesuka & Peixoto (2021), and Oroud (2019), found a significant positive relationship between AC independence and financial performance, whereas Bouaine & Hrichi (2019), found a negative association with financial performance. On the other side, Fariha et al (2021), and Al Farooque et al (2020), reveal no significant association.

In Saudi Arabia, SRCG 2017 reveals that AC must include at least one independent member, and any executive member must not be served in the AC. In light of agency theory, it posits that AC independence may enhance the monitoring ability and resource provisions to firms because of outside directors' expertise and network influence (Al- Matiri, 2022; Fama & Jensen, 1983b). Jensen and Meckling (1978), indicated that independence member is an important matter to discuss the agency problems and associated costs such they can control the opportunistic behavior of the inside directors. The AC that has more independent members, in general, deemed by agency theory to be the most effective monitoring to protect the rights and benefits of the shareholders, motivate the firms to maximize firm value based on long-term and greater transparency (Al Matiri., 2022; Al Farooque et al., 2020). Thus, the hypothesis can be stated as follows:
H1: *Audit committee independence is positively associated with firm performance.*

AC Competence
The competency of an AC can be evaluated in the number of AC members with expertise in accounting and/or finance to the total number of AC members (Bouaine & Hrichi, 2019). The proficiency of an AC may be assessed by the ratio of AC members possessing specialized knowledge in accounting and/or finance to the total membership of the A (Wahh et al., 2021). An AC characterized by a substantial degree of financial acumen and practical experience is imperative for the scrutiny and validation of essential activities of the organization, including the precision, reliability, objectivity, and integrity of the firm's financial disclosures, which are critical to the overall performance of the organization (Oroud, 2019; Ashari & Krismiaji. 2020).

The extant theoretical literature about CG indicates that the proficiency in accounting and finance among AC members significantly impacts the quality of earnings and enhances the accuracy of financial reporting, which subsequently exerts a favorable influence on the performance of the organization(Ashari & Krismiaji 2020; Dakhlallh, 2020; Wahh et al., 2021). However, this positive view is not certain, as other scholars emphasized that there is no correlation between this relationship (Bouaine& Hrichi, 2019; Qeshta, 2021). The SRCG of 2017 explicitly delineates that the AC is required to possess the necessary competencies to oversee the operations of the organization and to ascertain the accuracy and reliability of reports, financial statements, and internal control mechanisms.

The agency theory posits that in instances where discord exists between shareholders and management, it is often the case that management prioritizes its interests (Al-Matari, 2019; Jensen, & Meckling, 1976). Consequently, the duplicitous behavior exhibited by managers is primarily responsible for these conflicts of interest. To mitigate these conflicts, it

is imperative to establish a proficient AC that can ascertain the accuracy of financial statements (Ashari & Krismiaji 2020). This initiative is anticipated to ultimately enhance the overall performance of the organization. Moreover, agency theory posits that AC comprised of financially literate members who are capable of scrutinizing financial reporting significantly increases the likelihood that directors will exhibit greater diligence in monitoring managerial conduct, which in turn fosters improved FP (Wahh et al., 2021). Hence, the hypothesis can be stated as follows:
H2: Audit committee competence is positively associated with firm performance.

AC Chair's Independence
The independence of the AC chair exert a profound influence on its overall effectiveness. Independence and sufficient accounting proficiency are among the most vital attributes of an AC chair (Alodat et al., 2021). The FP of an organization may be enhanced through the contributions of an independent AC member, as posited by Alzeban (2020). Financial reporting and management oversight choices may be affected by the purview of the AC chair, who also has the power to set the topics and procedures for committee board meetings (Chaudhry et al., 2020). The AC's capacity to properly distribute its tasks is further improved by the chairperson's vital role. One can argue that for an AC to work, it requires an educated and devoted head. (Chaudhry et al., 2020).

Al-Matiri (2022), Ashari and Krismiaji (2020), as well as Al Farooque et al (2020), represent merely a fraction of the extensive body of research that has examined audit committees broadly; however, a limited number of these studies have specifically focused on the characteristics of the chairman. Research conducted by Alodat et al (2021), and Al-ahdal and Hashim (2022), has established that the independence of the AC chairperson is a critical determinant of the AC's efficiency, exerting a robust and positive influence on the performance of the firm. Conversely, Fariha et al (2021), identified a negative correlation between the independence of the chairman and corporate performance. Consequently, in light of the dearth of research in this area and the existing discrepancies regarding the nature of the relationship, this investigation seeks to provide a significant contribution to the existing literature by elucidating the degree of association between an independent chairman of the AC and the financial performance of publicly listed enterprises.

As previously articulated, the SRCG 2017 does not mandate that the chairman of the AC be an independent member, in contrast to certain governance frameworks established in other jurisdictions, including the USA and the UK. Consequently, this particular framework propels the current investigation to elucidate the impact of the chairman's independence on the operational efficacy of publicly listed corporations. Independent members, exemplified by the AC chair, play a pivotal role in addressing agency-related concerns and expenses to mitigate the self-serving behaviors of internal directors, as posited by agency theory (Jensen and Meckling 1978). According to agency theory, independent members are regarded as the most effective monitors to safeguard the rights and interests of shareholders, thereby incentivizing firms to enhance firm value through a focus on long-term objectives and heightened transparency (Jensen and Meckling, 1978; Al Farooque et al., 2020). Hence, the hypothesis can be stated as follows:
H3: Audit committee chair's independence is positively associated with firm performance

AC Chair's Competence

The competency of an AC chair can be assessed through their qualifications and experience in accounting and/or finance (Chaudhry et al., 2020). A fundamental responsibility of the AC is the supervision of the preparation of financial reporting. Consequently, in instances of inadequacy or breach in the preparation of the company's financial statements, the AC chair bears direct accountability (Al-Absy et al., 2019). To be effective and efficient, an AC requires a chair with the necessary competence to direct the committee's efforts, assure the production of high-quality "financial declaring," and manage overall performance (Alodat et al., 2023).

There exists a restricted corpus of prior research that has scrutinized the correlation between various attributes of the AC chair, such as financial background, and organizational performance (Alodat et al., 2023). Chaudhry et al (2020), have determined that the financial proficiency of the AC chair is significantly and positively correlated with the performance of the firm. Similarly, Alodat et al (2023), Al-Matari (2022), along with Gupta and Mahakud (2021), have elucidated that the acumen of the audit committee chair in the domains of accounting and finance is instrumental in augmenting organizational performance. As a result, the current study seeks to fill a gap in the literature by analysing this association, despite variances in location, kind, and quantity of samples, as well as measurement methodologies.

In contrast to the CG frameworks in nations such as Germany and Spain, which mandate that the chairperson of the AC possess experience in pertinent accounting and finance domains, the SRCG2017 does not necessitate that the chair of the committee have specialization in financial and accounting matters. As a result, this could be an essential and influential component in Saudi company success, hence the current study aims to investigate this tendency thoroughly.According to agency theory, an AC member endowed with financial and accounting expertise can mitigate agency costs through their capacity to oversee financial reporting and monitor managerial conduct, which may help improve and ensure the company's FP (Jensen & Meckling, 1976; Wahh et al., 2021). Hence, the hypothesis can be stated as follows:

H4: Audit committee chair's competence is positively associated with firm performance

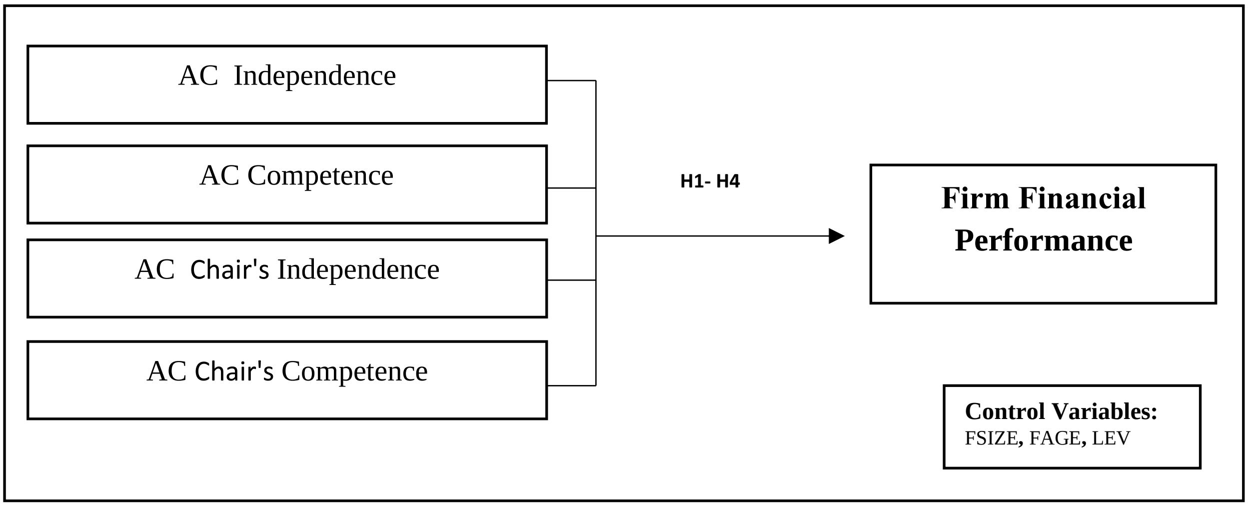
Agency Theory

The agency theory serves as the foundational framework that is arguably more suitable and sufficiently elucidates the objectives of this investigation. The agency theory is extensively utilized within the scholarly discourse concerning FP and forms the cornerstone of a considerable array of empirical studies focused on corporate performance. According to the agency theory, a misalignment of interests is present between managers, designated as agents, and shareholders, referred to as principals (Jensen & Meckling, 1976). This theoretical framework addresses the dynamics inherent in the relationship between a principal and an agent, which Jensen and Meckling (1976), assert involves a conflict of interests between managers (agents) and shareholders (principals).

In their foundational research, Jensen and Meckling (1976, p. 308) articulate that an agency relationship constitutes a contractual framework in which one or more individuals (the principals) appoint another individual (the agent) to execute a service on their behalf, thereby conferring decision-making authority upon the agent. Consequently, it is imperative to alleviate the conflicts between proprietors and their agents, which in turn enhances organizational performance. This is consistent with the fundamental tenet of agency theory, which posits that attributes of AC characteristics (for instance, independence and competence) serve as pivotal governance mechanisms that are instrumental in assisting managers to mitigate issues associated with the separation of ownership from management within corporations (Ashari & Krismiaji, 2020; Kasthury & Anandasayanan, 2020).

The Study Conceptual Framework

The conceptual framework for the study is illustrated in Figure 2. The dependent variable is firm financial performance, while the independent variables include AC independence, competence, the independence of the chair, and the competence of the chair.



Research Method

This part will address the research design, sample, method of gathering data, quantifying variables, model formulation, and data analysis

Research Design

An appropriate research design is vital for identifying the requisite data types, the methodology for data collection, and the sampling techniques to implement. Thus, the research design is critically important for achieving the research objectives (Bhatti et al., 2012). Furthermore, it can provide insights into the relationships that exist among the measured variables to clarify, anticipate, and regulate phenomena (Sekaran & Bougie, 2016). The empirical data for this investigation will be collected through a quantitative research methodology. The research design will employ an ex-post facto approach, which entails utilizing historical data to render evaluative judgments pertinent to this study. Given that the current investigation will utilize the annual reports of the SNFPLF, such an outcome is anticipated, the non-survey research design will be implemented in this inquiry due to its pertinent relevant in completing the research goals.

Population and Sampling Size

The population of interest will comprise the corporations that are listed on the Saudi Stock Exchange Market ((Tadawul). This study will encompass the timeframe from 2018 to 2023, as this period marked significant transformations within the publicly listed firms in Saudi Arabia.

Moreover, several potential implications were notably apparent. It was during this interval that the CMA promulgated the revised CG code in 2017. In that next year, 2018, it mandated that all registered corporations adhere to the principles outlined in the governance code to foster ethical conduct, transparency, accountability, and the stewardship of investors (CAM; SRCG,2017).

Consequently, the year 2018 has been selected as the focal sample period due to its status as the inaugural year subsequent to the implementation of the new regulations on CG in April 2017 for firms listed on the Tadawul. Furthermore, the sector comprising non-financial publicly listed firms contributes approximately 43.3% to the Gross Domestic Product (GDP) of Saudi Arabia.. Thus, this sector will be selected because it is appropriate to test these links among this sector and would provide a better indicator in Saudi capital markets. However, financial firms that had been listed in Tadawul have been excluded. As articulated by Bazhair and Alshareef (2022), Saudi financial institutions will be excluded from this analysis owing to their unique regulatory framework and financial reporting practices. The financial firms within Saudi Arabia are subjected to stringent regulations and utilize a diverse array of financial reporting methodologies. The year 2023 has been designated as the concluding year for this research, predicated on the availability of pertinent data. Thus, the sample size will be representative of the segment of the population that is to be examined. Accordingly, all 125 SNFPLFs spanning 17 industries that were operational from 2018 to 2023 will constitute the sample size for this study.

Method of the Data Collection

The present investigation will employ secondary data sources, as such an approach aligns with the objectives of the study and is of paramount importance to the topic being examined. According to SRCG (2017), it is required that annual reports be made accessible on the corporate website. Furthermore, organizations are mandated to retain essential records for a duration of no less than ten years. As a result, the information needed for this study will be compiled from the study sample's annual documents and financial statements. In accordance with preceding scholarly investigations, the Tadawul website, the associated data stream, and the online platforms of pertinent organizations will serve as sufficient repositories for the requisite data (Alsahlawi et al., 2021; Bazhair & Alshareef, 2022; Boshnak, 2021).

Measurement of Variables

Table 1 summarizes the descriptions, measurements, and expected indications of the study variables that reviewed studies have used.

Table 1
Measurement of study variables

Variable	Measurement	Resource
Firm performance	ROA: The net income is split by total assets.	Din et al, (2021)
AC independence	The percentage of independent AC members.	Jesuka & Peixoto (2021)
AC competence	The proportion of AC members with accounting or financial knowledge among the total number of AC members.	Bouaine & Hrichi (2019)
AC chair's independence	1 if the chair is independence; 0 otherwise	Fariha et al. (2021)
AC chair's competence	1 if the chair has accounting and finance expertise; 0 otherwise	Chaudhry et al., (2020)

Model Specification

The principal aim of this study is to investigate the influence of AC independence, and competence, as well as the independence, and competence of the AC chair on the performance of SNFPLF. Thus, the following description of the panel regression model that will underpin the investigation:

$$FP = \beta0 + \beta1ACI\mathit{it} + \beta2ACC\mathit{it} + \beta3ACCI\mathit{it} + \beta4ACCC\mathit{it} + \beta5FSIZE\mathit{it} + \beta6FAGE\mathit{it} + \beta7LEV\mathit{it} + \varepsilon i$$

Where:

FP	Firm Performance
ACI	AC Independence
ACC	AC Competence
ACCI	AC Chair's Independence
ACCC	AC Chair's Competence
FSIZE	Firm Size
FAGE	Firm Age
LEV	Leverage

Data Analysis

This research endeavor will investigate the influence of AC characteristics on the performance of publicly traded firms in Saudi Arabia, utilizing panel data as the analytical framework. Consequently, the data analysis will incorporate descriptive statistics alongside the panel regression methodology. The panel regression technique comprises both fixed effect and random effect estimations, aligning with prior research conducted by Alodat et al. (2021). Additionally, the selection of the most appropriate model for interpretation will be conducted through the application of the Breusch-Pagan Lagrange Multiplier (LM) and Hausman tests. Ultimately, the statistical software STATA has been identified as the preferred program for analysis due to its compatibility with panel data regression techniques.

Conclusion

The financial standing of the SNFPLF is markedly deficient. This condition can be attributed to the inadequate implementation of CG within these organizations. Following agency theory, the present investigation aims to explore the correlation between CG mechanisms, specifically the attributes of AC characteristics (including independence, competence, independence of the chair, and competence of the chair), and financial performance. This scholarly inquiry will comprehensively analyze the data of 125 enterprises operating in the non-financial sector during the time frame spanning from 2018 to 2022, coinciding with the announcement of Vision 2030 and the enforcement of the SRCG 2017. Therefore, it is posited that this theoretical research will yield significant benefits to all stakeholders pertinent to corporate governance and financial performance in publicly listed non-financial enterprises.

From a theoretical standpoint, the significance of this work arises from the necessity to keep up with recent breakthroughs in the notable enhancement of GC policies that drive higher company performance. Thus, the literature on CG in Saudi Arabia is minimal and continues to increase. Linking the themes of CG mechanisms, such as the competence and independence of the AC and its chair, with FP is still in the early phases of development, especially in light of the vast development of governance regulation.

From a practical standpoint, this study aims to provide valuable insights for decision-makers in the formulation of effective CG frameworks and the evaluation of the efficacy of existing structures. The relationship between CG attributes, particularly the AC, and the level of FP is a subject of significant relevance not only to the Saudi business milieu but also offers critical insights for regulators and policymakers in other Gulf, Arab, and Asian countries. In other terms, when CG practices are subjected to scrutiny, this facilitates an opportunity for governance practitioners and policymakers to evaluate the existing CG code of conduct to augment the FP of publicly listed non-financial corporations. This investigation concentrates on the non-financial sector by examining the correlation between specific attributes of AC and a singular metric of FP. Consequently, subsequent research endeavors could explore various sectors, characteristics of AC, or alternative measures of FP.

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