

ABSTRACT

Several studies on audit committee characteristics that affecting earnings quality give an inconsistent result. These inconsistencies become one of reference to start of this study. This study aims to examine the effect of independent and effective audit committee on the earnings quality in manufacturing companies listed in Indonesia Stock Exchange in 2005-2008. The effectiveness of the audit committee comprised of financial expertise, the number of meetings, and time commitment of audit committees. Earnings quality used to examine the independent and effective audit committee are earnings informativeness and earnings transparency.

The statistical methods used in this study is multiple regression. The sample selection was done by purposive sampling method. Based on certain criteria that determined by the writer, hence obtained 56 samples. In this study, earnings informativeness test was done by measuring ERC by regressing actual cumulative abnormal returns (CAR) on unexpected earnings (UE), while earnings transparency test was done by measuring the difference between the intrinsic value per share and market price per share by regressing operating cash flow per share (OCF) and earnings per share before extraordinary items (NI).

The study results show that partially with 0.05 significance level, there are the independent variables have positive and significant impact on the earnings quality effect, which is on earnings informativeness is the only interaction of EU with FINLIT. This indicates that firms with audit committees have financial expertise showed a higher ERC. On the earnings transparency is the interaction of NI with IND and NI with FINLIT showed a positive and significant influence. These results suggest that the overpricing of accruals is lower for firms that independent audit committees and financial expertise. There is no evidence that an independent audit committees have greater influence than the audit committee have financial expertise.

Key Words: *Audit Committee, Earnings Response Coefficient, Earnings Quality, Independence, Effectiveness, Financially Literate (Financial Expertise), market mispricing*