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Audit committee characteristics and loss reserve error

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Abstract

Purpose

The purpose of this paper is to investigate two audit committee characteristics – independence and expertise of the audit committee – and the property-liability insurers' financial reporting quality, which is proxied by loss reserve error.

Design/methodology/approach

The authors' hypotheses are tested using multivariate analysis where the loss reserve error is the dependent variable, and audit committee independence, and four types of audit committee financial expertise (accounting, finance, supervisory, and insurance expertise) are the testing variables.

Findings

It is found that accounting, finance, and insurance financial expertise are associated with more accurate loss reserve estimate. In contrast, a supervisory financial expertise and an independence audit committee are not found to be associated with better loss reserve quality.

Research limitations/implications

The sample includes publicly-held property-liability insurers. Although the results from publicly-held insurers could provide a good laboratory for such investigation in all insurers, they might be limited due to different organization structures of public vs private insurers.

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...in highly regulated industry, such as property-casualty insurance.

Originality/value

The paper contributes to the extant literature by studying audit committee characteristics in the insurance industry. It also contributes to the extant literature on audit committee effectiveness by decomposing the financial expertise into four types of financial expertise (accounting, finance, supervisory, or insurance expertise) and investigates which (if any) of these four types of expertise really drives the improvement of loss reserve quality.

Keywords

- United States of America
- Audit committees
- Insurance companies
- Financial reporting
- Loss reserve error
- Audit financial expertise
- Audit accounting expertise
- Audit insurance expertise
- Property-liability insurer

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