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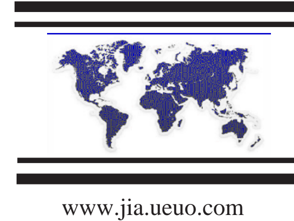

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POOR CORPORATE GOVERNANCE AND ITS CONSEQUENCES ON THE NIGERIAN BANKING SECTOR

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Abstract

The anxiety over the current banking crisis in Nigeria is understandable. This is borne out of the fact that the economic development of any country is directly tied to its banking sector. The effectiveness and efficiency with which the banks perform their intermediary roles between the surplus and deficit spending units of the economy determines to a very large extent the prosperity of any nation. Corporate governance is systematic and formalized manners of ensuring that top management represented by the board of directors do not make decision making powers occasioned by management and ownership separation to pursue personal interests at the expense of other stakeholders. This study made use of structured questionnaire to elicit responses from conveniently selected respondents comprising of investment experts, academics, banks customers, public and policy analysts with in Lagos metropolis. It was hypothesized and the study confirmed that poor governance culture and supervisory laxities were majorly responsible for the current banking crises. The study recommended an adherence to the execution of the tenets of good corporate governance in Nigerian banking sector and actions contrary to this should be dealt with appropriately by bringing offenders to book irrespective of their status in the society.

Key words: corporate governance, ownership separation, banking crises, effectiveness, efficiency, economic development

1. INTRODUCTION

The anxiety over the current banking sector crisis in Nigeria is understandable given the vital role played by the banking sector in the economic development of any nation. The banking industry plays a major intermediation role in an economy by mobilizing savings from surplus units and channeling these funds to the deficit units particularly the private enterprises for the purpose of expanding their production

capacities. The concern over corporate governance stems from the fact that sound governance practices by organizations, banks inclusive results in higher firm's market value, lower cost of funds and higher profitability (Block, Jang & Kim, 2006 & Claessen, 2006).

Eight chief executives and executive directors of some Nigerian banks were summarily dismissed between August and October, 2009 due to issues related to poor corporate governance practices. This was sequel to the conclusion of audit investigations embarked upon by the central Bank of Nigeria to determine the soundness of Nigerian banks. The release of these reports led CBN to conclude that the affected banks have acted in manners detrimental to the interest of depositors and creditors. This was at variance to the clean bill of good health earlier given to these banks by regulatory authorities (CBN inclusive) and their so called appointed reputable external auditors.

The contradictions and the resultant loss in wealth and investor's confidence have necessitated this inquiry and therefore this study, hopes to achieve the following specific objectives:

1. to determine the extent to which non-compliance with corporate governance codes by the bank executives contributed to this present crisis
2. to ascertain the extent of the regulatory authorities complicity and laxity in the present to the crises
3. to examine and evaluate the role of personal greed of executives in fostering this crises and
4. to proffer possible solutions to resolve the crises and prevent future reoccurrence

Based on the objectives and the focus of this study the hypotheses formulated were:

H1: Poor corporate governance culture precipitated the current Nigerian banking sector crisis.

H2: Supervisory laxity has significantly contributed to the current Nigerian banking sector crisis.

2. THEORETICAL FRAMEWORK

The topicality of corporate governance has manifested in diverse definitions depending on the interests and individuals involved. Cadbury (2000) defined "corporate governance as being concerned with holding the balance between economic and social goals and between individual and communal goals. The corporate governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals' corporations and society." Similar finding is expressed by Orham and Yildirim (2009).

OECD (1999) posits that corporate governance is "the system by which business are directed and controlled. The corporate governance structures specifies the distribution of rights and responsibilities among different participants in the corporation such as the board, managers, shareholders and other stakeholders and spell out the rules and procedures for making decisions on corporate affairs by doing this, it also provides the structure through which the company objectives are set and the means of attaining these objectives and monitoring performance". Corporate governance is concerned with the intrinsic nature, purpose, integrity and identity of the institution with a primary focus on the

entity's relevance continuity and judiciary aspect. Governance involves monitoring and overseeing strategic direction, socio-economic and cultural content externalities and constituencies of the institutions. According to Imala (2002) and Srivastava (2010) from the perspective of the banking sector, corporate governance involves the manner in which the business and affairs of individual institutions are governed by their board of directors and senior management with depositors standing out clearly as the most important stakeholder.

An essential feature of a corporation is the separation of ownership from management. To this end, the shareholders (owners) delegate decision making rights to managers to act on their behalf. However, this separation of ownership from control implies a loss of effective control by shareholders over managerial decisions. Thus, the primary objective of corporate governance is to attempt an alignment of the managerial incentives with those of stakeholders. This is to check the tendency of selfishness by managerial employees especially the top ones to ensure that delegated decisions making powers are not abused to the detriment of shareholders and other stakeholders.

The major elements of corporate governance are good board practices, control environment, transparent disclosure, well defined shareholder rights and board commitment. The four pillars of corporate governance are accountability, fairness, transparency and independency (Omeiza-Micheal, 2009). Weil et al (2002) concluded that although, corporate governance can be defined in a variety of ways, generally, it involves the mechanisms by which a business enterprise organized in a limited corporate form is directed and controlled. It usually concerns mechanisms by which corporate managers are held accountable for corporate conduct and performance.

Several codes have been developed as a guide to corporate governance; however, the best guide to global corporate governance was developed by the OECD. The OECD (1999) principle of corporate governance is as shown below;

i. The rights of shareholders: the corporate governance framework should protect shareholders rights

ii. The equitable treatment of shareholders: the corporate governance framework should ensure the equitable treatment of all shareholders including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.

iii. The role of stakeholders in corporate governance: the corporate governance framework should recognize the rights of stakeholders as established by law and encourage active cooperation between corporations and stakeholders in creating wealth, jobs and the sustainability of financially sound enterprises.

iv. Disclosure and transparency: the corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation including the financial situation, performance, ownership and governance of the company.

v. The responsibilities of the board: the corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board and the boards accountability to the company and the shareholders.

3. PRINCIPLES OF CORPORATE GOVERNANCE

Given the globalization of business and the need to ensure uniformity in the practice of corporate governance the world over, the Hampel Committee (1998) developed some basic principles of good corporate and sets out a code of best practices called the “combined code”. The combined code includes the following;

1. Every listed company should be headed by an effective board which should lead and control the company. The board should meet regularly and should have a formal schedule of matters reserved to it for decisions; directors should bring an independent judgment to bear on issues of strategy, performance, resources and standards of conduct, directors should receive appropriate training on first appointment and as necessary thereafter.
2. There are two key tasks at the top of every public company- running of the board (the chairman’s role and the executive responsibility for the operation of the company’s business (Chief executive’s role). There should be a clear division of responsibilities between the two roles, so as to ensure a balance of power and authority and thus avoid a situation where one person has unfettered powers of decision.
3. The board should have a balance between executive and non- executive directors with at least 1/3rd from the latter. The majority of non-executive should be independent of the management and free of business relationships that could interfere with their independence.
4. There should be a formal and transparent procedure for the appointment of directors and all directors should offer themselves for re-election every three years.
5. Levels of remunerations should be sufficient to attract and retain the directors to run the company successfully, but should not be excessive. Part of the payment of directors should be in the form of performance related element.
6. The board should use the annual general meeting to communicate with the individual investors and encourage their participation.

In Nigeria the mechanism of corporate governance are the Companies and Allied Matters Act (1990) and Securities and Exchange Commission (2003) Corporate Governance Code. These are briefly discussed with emphasis on relevant section to this study.

The CAMA (1990) requires the annual accounts reports of quoted companies to include: A statement of accounting policies; Balance sheet as at the last day of the year; Profits and loss accounts; Notes on the accounts; Auditor’s report; Director’s report; Statement of the source and application of funds; A value- added statement for the year; A five year financial summary; Group financial statements (for holding companies).

According to SEC (2003) an effective system of corporate governance provides the framework with in which board, management, shareholders and other stake holders address their respective responsibilities. The code deals with:

a. The roles of the board of directors and management
b. The role of the audit committee and
c. The right of shareholders

4. HOW COMPLIANCE ARE THE NIGERIAN BANKS TO THE PRINCIPLES OF CORPORATE GOVERNANCE?

Most analysts believed that the crisis in the banking sector is a clear manifestation of poor corporate governance practices in the financial sectors. According to Chiejina (2009) the executives had abandoned the key elements of good corporate principles of honesty, trust, and integrity, openness, performance orientation, responsibility, and accountability, mutual respect and commitment to the organization for selfish reasons. No wonder, the banks astronomical growth and all indices used to package their shares are not commensurate to economic growth and transformation. It was obvious that the core banking practices have been traded off and the most beneficial are the CEOs and their loyalists.

5. CONSEQUENCES OF POOR CORPORATE GOVERNANCE

Following the audit exercise conducted by CBN's examiners it was discovered that five of the banks had accumulated margin loans of N500 billion, among other loans, that had gone bad and eroded their shareholders' funds. The primary factors responsible for the current are laxity of control by the regulatory authorities, corruptions, inactive boards and greed on the part of the executives. The regulatory functions of the CBN to say the least have been non existent, which may be due to dearth of qualified personnel experienced in the act of bank supervision and examination. Alternatively, the bank supervisors would have been compromised to issue clean of bill reports for banks over these years.

The inability of the board of directors to effectively supervise top management of these banks has contributed more to this ugly situation. Most members of the board of these banks were composed of surrogates of the chief executives and at times chairmen. It is either they were unilaterally nominated by the managing director or the chairman who holds controlling interest in the bank as the suppliers of capital. To this end, board members have no financial contributions to the bank as their names were supplied to CBN in order to comply with statutory requirements. It is therefore imperative for such members to rubber stamp all decisions of their benefactors. After all they are friends or business associates.

6. METHODS

Participants and Procedure: The sample of study consisted of 120 respondents who were mainly investment analysts, financial experts, banks employees, shareholders and customers among others. The choice of respondents was based on their knowledge and experience in the industry. About 89 respondents finally participated in the study, which represented 71.16% response rate. Among the respondent, 41.3% was male and 58.7% female. Majority of the respondent are in the middle age which is between 31 to 40 years (56.7%). 25.3% has been working with the organization for more than 5 years and 36.6% have been working between 3 to 4 years. Majority of the respondent have First degree (55%), while those with Masters Degree are 10% and only 35% with diploma qualification.

Research Instrument: The structured questionnaire was administered to obtain

relevant information from conveniently selected respondents with in Lagos metropolis who showed interest in the subject matter. The questionnaire consisted of 20 questions in statement forms describing issues operationalised in the concept of corporate governance as it relates to the Nigerian banking sector. Responses were measured using Likert five point-scale of; strongly agree to strongly disagree. The response of the examinees are presented in Table 1.

The extent of supervisory laxity was measured through possession of relevant skills and willingness to apply those skills without compromising ones integrity. Poor corporate cultures and practices were identified, examined and operationalized as key variables that are significant in this study.

7. RESULTS AND DISCUSSIONS

The questionnaire was analyzed and hypotheses earlier formulated were tested using chi square. Results of the chi square test are presented in Table 2.

Hypothesis One

Poor corporate governance culture precipitated the current Nigerian banking sector crisis.

Hypothesis two

Supervisory laxity has significantly contributed to the current Nigerian banking sector crisis.

8. CHI-SQUARE TEST

From the result shown in table 2, where Xc_{alc} = 108.706, X_{tab} = 9.49, degree of freedom df = 4.

It clearly shows that the calculated value of chi-square is greater than the tabulated value, hence the rejection of null hypothesis and acceptance of the alternate hypothesis (H1), which states that poor corporate culture precipitated the current banking sector crisis.

While the result in table 3 also shows that XCalc = 210.634, and Xtab = 9.49, degree of freedom df = 4.

Xtab in both hypotheses is the table value of the test statistics, which is read from the standard X^2 table. It is the same for both hypotheses at 4degree of freedom and .05 level of significance since the same data that was used for analysis.

It can be inferred that the calculated value of chi-square is equally greater than the tabulated value, then the rejecion of the null hypothesis and therefore conclude by

Table 1. The response of the examinees regarding hypothesis one

	Observed N	Expected N	Residual
STRONGLY AGREE	123	61.2	61.8
AGREE	76	61.2	14.8
UNDECIDED	55	61.2	-6.2
DISAGREE	33	61.2	-28.2
STRONGLY DISAGREE	19	61.2	-42.2
Total	306		

Table 2. Results of the Chi Square test of thew hypothesis one

Test Statistics

	RESPONSE
Chi-Square [a]	108.706
df	4
Asymp. Sig.	.000

a. 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 61.2.

Table 3. The response of the examinees regarding hypothesis two

	Observed N	Expected N	Residual
STRONGLY AGREE	156	61.2	94.8
AGREE	70	61.2	8.8
UNDECIDED	35	61.2	-26.2
DISAGREE	31	61.2	-30.2
STRONGLY DISAGREE	14	61.2	-47.2
Total	306		

Table 4.Results of the Chi Square test of thew hypothesis two

Test Statistics

	RESPONSE 2
Chi-Square [a]	210.634
df	4
Asymp. Sig.	.000

a. 0 cells (.0%) have expected frequencies less than 5. The minimum expected cell frequency is 61.2.

accepting the alternate hypothesis (H2), which states that supervisory laxity has significantly contributed to the present banking crisis.

9. CONCLUSIONS AND RECOMMENDATIONS

CBN supervisory officials are judged to lack integrity and boldness in carrying out their oversight functions. Officials are known to have compromised in issuing clean of bills of health in their bank examination report. Since the bank examination department became a 'goldmine' and most sought out department, some incompetent staff have naturally found themselves there. It was also believe that most examiners' skills are outdated given the technology driven banking operations. Fagbule (2009) frankly stated that, the CBN failed just as the banks, since banking crisis are manifested by weaknesses in regulation and lax banking practices.

The study observes that the explosion in the numbers of banks and information technology has not been matched with CBN supervisory employees' skills improvement. Thus, there is the need to urgently intensify the training and retraining of these officials. Besides, the house cleansing should begin with CBN itself. To this end, this study recommends that, an internal panel should be raised by the CBN governor to identify those officials that examined and issued clean bills of health to affected banks. Thereafter, appropriate disciplinary measures should be taken against such CBN officials. This invariably will serves as lessons to other public officials with the intention of making quick riches at the detriments of the general populace. By so doing, Nigerian government will be sending the right signals to others and the world in particular that, it has zero tolerance for corrupt practices. It will equally complement the good efforts of truly rebranding Nigeria.

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