RELEVANCE OF CORPORATE GOVERNANCE IN NIGERIAN BANKS

Akinyomi, Oladele John
Department of Financial Studies,
Redeemerôs University, Ogun State, Nigeria
E-mail: delejohn21@yahoo.com

Abstract

This paper examines the relevance of Corporate Governance in Nigerian Banks. Although corporate governance is of general interests to the Nigerian public, that of the banking industry is of particular interest because of the published figures, attributes and activities of the banking institutions. Because every economy world-over has migrated to a ``money and exchange" economy, the basic instrument to facilitate exchange and lubricate international trade is money. Due to the catalytic roles of banks in any economy, their corporate governance is of prime interest to government, depositors, shareholders and the public at large. The study became necessary as a result of recent events both globally and locally in which we witnessed massive failure of large companies, including banks, which have been mainly attributed to fraud and mismanagement by Directors and Managers of such Companies. The study employed the secondary source of data on corporate governance and its application in Nigerian banks. The study revealed that poor corporate governance, poor risk management practices, inability to manage expansion, low assets quality, inadequate supervisory framework and unethical practices among top banking chiefs who gave out loans without required collateral were identified as some of the reasons for the current financial crisis in the country. The key recommendation is that the banks should be made to provide a certain minimum amount of information requirement on corporate governance.

Key Words: Fraud, Mismanagement, Directors and Banks

Introduction

Corporate governance has in recent years assumed considerable significance as a veritable tool for ensuring corporate survival since business confidence usually suffers each time a corporate entity collapses. Most of the business failures in the recent past are attributed to failure in corporate governance practices. For instance, the collapse of banks in Nigeria in the early 1990s and the recent distress of some Nigerian banks were as a result of inadequate corporate governance practices. Poor corporate governance, poor risk management practices, inability to manage expansion, low assets quality, inadequate supervisory framework and unethical practices among top banking chiefs who gave out loans without required collateral were identified as some of the reasons for the current financial crisis in the country.

It was observed by Omofaye (2009), that the various regulatory and supervisory agencies are also to be blamed for the problem. Poor monitoring by the Central Bank of Nigeria (CBN), Nigerian Deposit Insurance Corporations, Security and Exchange

Commission and the Nigerian Stock Exchange to check some of the excesses of the Chief Executive Officers has been considered factors responsible for the problem. Signs of distress in the banking sector became obvious from October 2008, when some deposit-money-taking banks became permanent clients of the Expanded Discount Window facility of the CBN an indication of a serious problem. The lead regulatory body, CBN, then directed a special examination of the 24 banks operating in the country to ascertain the extent of the problem.

The outcome revealed that non-performing loans of some banks exceeded their shareholders funds. Eight of the banks were not only insolvent - meaning that their capital adequacy was less than 10%, they were also found to be illiquid - meaning that their deposit ratios were less than 25%. To save the situation, the CBN intervened through two ways - by providing financial assistance of 620 billion naira and technical assistance, through the replacement of the affected bank chiefs with new management, with the mandate to stabilize the banks (US$1=150 Naira). Based on this background, the objective of this study is to examine corporate governance issues as they affect the current financial crisis in the country.

Methodology

Data used for this study were obtained from the secondary sources such as newspapers, magazines, journal articles, text books and the internet. The data obtained were those on corporate governance and their application in Nigerian banks.

Corporate Governance Development

Whilst there would appear to be an upsurge in the literature on corporate governance development across the globe (see Shleifer and Vishny, 1997; Demirag, 1998; Solomon and Solomon, 2004), there is still a lacuna in the literature on corporate governance development, especially in the developing world. Although some authors (Mallin & Jelic, 2000; Ow-Yong & Guan, 2000; Sarkar & Sarkar, 2000; Apreda, 2001; Hussain & Mallin, 2002; Fremond & Capaul, 2003, amongst others) provide evidence of corporate governance development in some developing countries, there is little evidence of corporate governance development in Africa, with the exception of South Africa (Yasaki, 2001) provides some evidence of the evolution of corporate governance in Nigeria, albeit within the banking sector.

Although not much is known about the state of corporate governance in Nigeria, there is evidence of researches (Wallace, 1989; Okike, 1989), which have examined the accounting and financial reporting framework in Nigeria. Furthermore, Okike (1999) provide detailed accounts of the audit reporting environment in Nigeria.

Corporate Governance is often applied narrowly to questions about the structure and functioning of Boards of Directors, (Blair 1995:3). This view is found amongst some business school scholars and management consultants. Corporate governance can also be defined as the structure whereby managers at the organizational apex are controlled through the Board of Directors, its associated structures, executive incentive, and other schemes of monitoring and bonding. This view was reflected by his colleague, a former McKinsey consultant, in *Strictly Boardroom* (Hilmer 1993).

Corporate governance refers to the organizational framework for decision making and action taking within a corporate entity. In this regard it can be defined as the structure of relationships within an entity for making decisions and implementation. Simply put, it refers to how an organization is run, that is, how the resources of an organization are employed in pursuant to the set mission and goals of the organization. Corporate governance is not just a set of rules but also a structure of relationships geared towards establishing good corporate practice and culture.

The above definitions are summarized into one by the Report of the Committee on Corporate Governance of Public Companies in Nigeria (2003) which sees corporate governance as ñthe system by which companies in Nigeria are directed, and managers are held accountable for the performance of the organization.ò This further emphasizes the fact that the concept of corporate governance is principally on the structure of relationship within an organization which is directed at best practice in the overall interest of the organization and its owners/stakeholders. Corporate governance can also be seen as being concerned with the structures within which a corporate entity receives its basic orientation and direction. Corporate governance sets the pace that in turn determines the corporate culture of an organization on the long-run.

Corporate Governance in the Nigerian Banking Industry

The core issues in corporate governance in any country are the composition of Board of Directors, the activities/responsibilities of members, the roles of nominal directors and the use of independent auditors. The complexity and trouble with most companies including banks in Nigeria is that the directors work to the answer, mark their own examination scripts, score themselves distinctions and initiate the applause. But to the stakeholders (especially the equity owners), the excellent report sheets are openly fudged or at best engineered and indeed, the activities of boards are so varied and deceptively intractable that the more critically one looks, the less one sees. It becomes more elusive considering the corporate concept which assigns to a company, a status of legal entity with statutory rights and responsibilities separate from the owners and executives.

Further problems arise when a comparison is made between the vastly unstructured private limited liability companies in Nigeria and the public liability companies. Whereas the former is known for its simplicity and effective management, facilitating the provision of capital, encouraging business growth, inducing innovation in industry/commerce and creating wealth, the latter which is the vogue in business circles and global markets is fraught with lethargy, nonchalance and lack of personal touch due to the legal separation of ownership from management.

In spite of this legal complexity, it is often the case even in Nigeria that ownership is the basis of power exercised through the Annual General Meetings (AGM) of companies, an occasion where the shareholders wine and dine, nominate and elect their Directors who, in the conventional wisdom and legal fiction provided by Company and Allied Matters Act (CAMA) 1990 (as amended) reciprocate through accountability as mirrored in their regular reports and audited financial statements. It is true today in most developing nations and globally doubtful if the maxim of shareholder democracy is achievable in spite of the normative appeal. Particularly in Nigeria, the concept of shareholder democracy is an anachronism in that individual shareholders are hardly able to exercise any influence unless they have sufficient and dominant shareholdings. Thus, the conventional wisdom that shareholders determine Board membership and influence corporate direction is, by and large, false in spite of the constant call on shareholders by Nigerian media commentators and the various Shareholders' Associations to exercise their rights and power.

It seems that within the Nigerian context, it is only the institutional and relationship investors that appear to have some influence on Boards especially if several of them collude or act in congruence. In fairness to Boards of some blue-chip Companies (both in the real and service sectors), they go the extra mile to communicate with and carry along, their shareholders through various meetings, the array of published materials, videos of Annual General Meetings, shareholders' forums and a host of other ways to meet and question the Directors. All these communication channels simultaneously serve to maintain shareholder participation in governance as well as influence stock prices positively especially when trying to raise fresh funds for corporate capacity building.

Although corporate governance is of general interests to the Nigerian public, that of the banking industry is of particular interest because of the published figures, attributes and activities of the banking institutions. Because every economy world-over has migrated to a ``money and exchange" economy, the basic instrument to facilitate exchange and lubricate international trade is money. Due to the catalytic roles of banks in any economy, their corporate governance is of prime interest to government, depositors, shareholders and the public at large.

While government and the public want a safe, sound and stable banking industry (Umoh, 1994), depositors are more interested in the safety and returns on their deposits as well as quality of services rendered by their banks. On the other hand, shareholders (owners) are more interested in their banks' profitability, soundness and good health while the employees are interested in their sustained employment through the continued existence and profitability of their employer - banks. Given this myriad of interests, it is not surprising that the governance of Nigerian banks has become very political and volatile. Governance of any banking institution in Nigeria is centrally placed in the hands of the Board of Directors.

Given the multiplicity of interests in any bank, much is expected of the Board members, a situation which partly informs their sanctioning and approval by the Central Bank of Nigeria irrespective of what the shareholders think of any Director. To this extent, appointment to the board of any Nigerian bank differs markedly from those of other private sector corporate institutions. To satisfy the various interests, there is little argument about the responsibilities of banks' Boards of Directors which include, amongst others, the following (Conger et al., 1998, NDIC, 1991):

(a) Development of corporate vision, mission and business strategy
(b) Ensuring that a strategic planning process is in place, used and producing sound choices.
(c) Monitoring and supervising the implementation of current strategic initiatives to ensure effective results.
(d) Ensuring that the bank has the highest caliber of Chief Executive Officers and management team. In this case, the Board must find and groom the appropriate chemistry between the rare, critically important breed of internal entrepreneurs and the experienced operators to assume governance of the organization in a succession plan.
(e) Being the ultimate oversight body, it must be satisfied that adequate information, control and audit systems are in place in addition to its responsibility of corporate

compliance with legal and ethical standards imposed by the law and the banks own statement of values.

(f) Preventing and managing crisis, that is, responsibility for risk management.

(g) Must have a clear idea of how to differentiate the role of Board of Directors from that of bank management.

(h) It is the ultimate decision taker although from all practical purposes, much of the authority is delegated to senior and general management staff and in fact, amongst some new generation banks, this authority has been completely abdicated.

It is tempting, though presumptuous to examine and present a straight-jacket proposal about how a bank's Board should fulfill its responsibilities. There currently exist very scanty authoritative reports of what a Nigerian Board of Directors actually should do regarding their specific functions and tasks. The NDIC (1991) Pocket Guide only provides a ñquick and dirtyò manual. However, what can be done is to give the conceptual but feasible profile of members of Board which must be composed of people of integrity and good judgments, whose knowledge/background and experience must absolutely match the strategic demands facing the bank.

Processes of Corporate Governance in Nigerian Banks

There is no doubt that the Companies and Allied Matters Act 1990 (CAMA) places enormous responsibilities in the hands of Board members of any Company (see section 282). Similarly, the Nigeria Deposit Insurance Corporation (1991) has put additional responsibilities by spelling out the responsibilities of bank Directors. The main process of governance in Nigerian banks is three-pronged:

a) Composition in terms of competence, knowledge, experience and business network

b) Strategy in terms of organizing the board, running the Board, team work and tenure of Board of Directorsô members

c) Action in terms of responsibility, commitment, performance indicators, monitoring and evaluation

In terms of composition, the usual practice in nominating Executive Directors is to look for highly qualified and experienced people with the business connection first from amongst the staff failing which an executive search is made outside. This is common with the big and medium-sized banks. As for the new generation banks, the composition is more in favour of ownership, family relationship and cronies. In terms of organizing and running the Board, the process is first to determine the ratio of executive to non-executive Directors. In the Nigerian setting, the big banks tend to have bigger Boards than medium size banks.

The second step in the process is to delineate the boundary of influence of the non-executives, thirdly determine the committee system and decide which of the committees are ``no-go" areas for the nominal Directors including the Chairman. In other words the Managing Director/Chief Executive officer leads the Executive directors and the members of general management while the Chairman only leads the Board of Directors. In some cases especially in the new generation banks, the Chairman is also the Chief Executive even though there is a managing director in place.

Also, part of the process strategy is the conduct and frequency of Board of Directorsô meetings. For the old banks, the Boards of Directors meetings are quite regular (at least once in two months) and this is quite understandable given their network and total share of the market. In the medium-sized banks, the Executives hate meetings and would prefer not to have them at all so as to use the time for bank marketing.

Furthermore, the issue of the tenure of Doard of Directors today is that the big players in the banking industry have now put in place an effective and enduring tenure system based on such parameters as age, length of service and maximum number of terms on the Board. Three of the biggest banks in Nigeria have introduced a tenure system of six years with a statutory age limit of 60 years for Executive Directors and 70 years for non-Executive Directors.

In terms of actions and responsibilities, many tend to be delegated to senior and general management who do the business analysis and present recommendations to the relevant Board members for ratification with only occasional questioning for more information. But depending on the personality of the Executive Director or even the Chairman, he may get involved in more than mere ratification or approval, although their job is not to slow down the train but keep it on track.

Irrespective of the size of the bank, one common responsibility that Boards never delegate is the bank performance and its measurement because they know that this is the first concrete index with which to judge or condemn their performance at the Annual General Meetings. Within the Nigerian context however, the critical issues are not those of the processes but rather the problems of corporate governance of banks.

Problems of Corporate Governance in Nigerian Bank

A critical assessment would reveal that both endogenous and exogenous problems became institutionalized in the banking system as well as the society's core values which impinge on the good governance of banks in the 1990's and carried over into the twenty first century; such major problems include the following:

Pressure from the environment

There were two types of pressures, namely those from friends and relations and those from the underground or informal sector. On the one hand, it was usual to find friends and relations putting pressures on Board members for favours such as business contracts, employment of incompetent and sometimes unqualified personnel as well as seeking loans/advances which went sour even before approval and drawdown The other source of pressure was from business influencers who sometimes insisted on a ``price" or ``percentage rent" from a business relationship that developed between the bank and the third party Company. In this case, the agency fee (often christened as ``lubrication of the informal sector") was paid, though out of tune with the bank's core values and practices. The lessons of experience in the Nigerian environment were that these types of rent seeking quickly reduce the level of corporate governance of our banks.

Instability of contract / tenur

Everybody agrees that for any organization to be stable, the governing body should also enjoy some level of stability in the tenure system. The private sector in Nigeria in the 1990s exhibited too many sudden changes and/or dissolution of Boards of Companies even when such an institution was not government owned as long as it operated in any of the strategic sectors (petro-chemical, banking, etc). However, it must be added that since the Federal

Government divested from the banking industry in 1993, there has been a good degree of stability in the erstwhile public banks.

Instability of Board of any bank has great consequences on the bank's governance and performance. Unstable tenure tends to breed insecurity in Board members, some of whom might devise ways of quickly ``settling" themselves by engaging in fleet-footed activities. There was the real issue of waning confidence on the part of the competent and qualified men of integrity who refused to take up Board appointments for the simple reason of not soiling their names by an announcement dissolving the Board because of ``non-performance", ``declining productivity", ``uncompromising posture", ``sturbonness", and such other abrasive qualifications.

Government action

It was paradoxical that although the government through its agency, the NDIC, was interested in ensuring stability, safety and soundness of banks, their actions usually portended the opposite. This was particularly so when considering the huge amount of sovereign debts emanating from governments' direct loans/advances while also guaranteeing several others for parastatals, all of which went sour and lingered for a long time before the draconian resolution in 1998 which authorized the payment of only the principal sums. The issue here is not the succour resulting from part payments per se, but the mismatch experienced in banks' asset/liability management and the consequent haemorrhage suffered by the industry for as long as the sovereign debt lasted. In spite of the payment of the principal sums, could the question not be posed whether or not, such 100 per cent interest waiver over the huge sovereign debts contributed immensely to the demise of many of the liquidated banks?

Board/management relationship

The relationship between the Board and management should be mutual and complementary in order to flag the right signal to the investing and/or consuming public. At the same time, the policing role of the Board of Directors cannot be abdicated so as to ensure accountability. In theory, there is clear delineation between the functions of both but it is almost impossible to draw the real boundary line. Therefore when the Board engages in the day-to-day operations of the bank rather than policy and strategic issues, there will be role conflicts as witnessed in the ``big four" banks in the 1990s when government used to appoint Board members. The consequences of such conflicts include:

* The governance of the bank will suffer because the Board will waste their energies on operational and tactical problems.
* Rivalry will develop between Chairman and Managing Director, between Board and Management as well as between Executive Directors and other Directors whereby the executives see the non-executives as interlogers rather than team-mates and confidants. All these rivalries would lead to as many divergent opinions and behaviours as there are camps. This was the case in state-owned banks in the 1990's and carried over to the year 2000 even though such banks have been completely privatized.

Executive Chairmanship / Vice-Chairmanship

One aspect of the governance problems of the banking industry in Nigeria today is a situation where the Chairman / Vice Chairman of Board is not satisfied with his/her role as nominal Director, moderating the excesses of the Managing Director/chief Executive officer. He/she therefore takes on the role of the Executive (Vice) Chairman, a situation which could lead to abuse of power and bank mismanagement as was witnessed in the banking industry in the 1990s where the Executive Chairman could sit in judgment over his/her own activities. This observation also exposed the moral issue on the expected transparency, accountability and the police-role of the Chairman / Vice-Chairman.

Insider dealings

In a bank business, a major component in the balance sheet is the loans/advances portfolio and the occurrence of reckless approvals can easily lead to problematic governance by Board. By the provisions of Banks and Other Financial Institutions Decree (BOFID), Section 18(9) (FGN, 1991), bank Directors are expected to declare to other colleagues on the Board, their direct or indirect interests in any credit facilities being granted. The BOFID provision is to forestall conflict of personal interest with that of the bank. There is no controversy any more regarding the bitter lessons of the 1990s from the Nigerian banking industry when bank Directors influenced the approval of credit facilities to their private and/or connected companies without declaring their interests and worse still with the premonition of defaulting in payment. Furthermore, we witnessed many occasions when several companies were hurriedly floated by Chief Executives of some new generation banks for the main purpose of passing several bank businesses through such companies. The consequence of all these was that in banks with very fragile governance processes and little or lack of checks and balances, widespread distress ensued, the cost of which is huge from the perspective of public finance.

Quality of bank Directors

There seems to be a high correlation between the quality of Directors and the Board performance. During the banking boom of the post-Structural Adjustment Programme in Nigeria, it was fashionable and rewarding to be called a bank Director. Moreover, the government which then controlled the shareholding of the big players used the appointment of bank Directors for patronage. The law stipulates that bank Directors should be people of unquestionable integrity, knowledgeable with a considerable degree of experience in their professions and committed to excellence (NDIC 1991). Evidence from the industry revealed that ``unfit" persons were appointed to Boards of banks.

Apart from the fact that they did not possess the analytical background, even where they were professionally sound on paper, the society was to learn very belatedly through their professional misconduct, about their lack of integrity in spite of the so-called quality control via their appointment sanctioning by the Apex institution i.e. the CBN. The consequence was the Directors' lack of capacity to contribute at Board and Board committee meetings and at occasions when they did, such contributions were either pedestrian, below par or not relevant at all. All of these had a further consequence on the quality issues of governance and leadership by the board, a situation that further worsened the remaining fragile reputation of bank Directors irrespective of their Boards.

Conclusion

This paper is on the relevance of corporate governance in Nigeria banks. The objective is to examine corporate governance issues as it affects the current financial crisis in Nigeria. The findings from the study revealed that there are poor corporate governance practices in some of the banks. This accounts for the major factor causing the present financial crisis in the country. This becomes very glaring when one observes some of the unethical practices among top banking chiefs who gave out loans without required collateral security. Other factors equally responsible for the crisis include poor risk management practices, inability to manage expansion, low assets quality and inadequate supervisory framework

Recommendations

To ensure good corporate governance in Nigerian banks the following recommendations are made:

- The banks should be made to provide a certain minimum amount of information requirement on corporate governance. This would allow uniformity and would allow easy appraisal of the corporate governance practices.
- Banks should provide an analysis of all their non-performing debts in terms of the ages. This will provide a picture of the risk profile of the banks.
- Disclosures on Directorsô remuneration should be extensive as to provide information on who gets what and for what purpose
- Disclosures about employeesô benefits should be extensive as to show an analysis of their emoluments by category not just by number
- All banks should always provide a detailed analysis of insider-related credits according to performance.

Since the banking industry plays a vital role in the economy, it is essential to ensure that good corporate governance is in place and adhere to by the Board and Management of the various banks. This will enhance the confidence of the public in the banking industry.

References

Apreda, R. (2001). Corporate Governance in Argentina: the Outcome of Economic Freedom, Corporate Governance: *International Review*, 9, 298ï 310.

Blair, M.M. (1995). *Ownership and Control.* Washington, The Brookings Institution.

Conger, J. A., Finegold D. & Lawler III, E. E. (1998). Appraising Boardroom Performance. *Harvard Business Review*, Jan/Feb., Boston.

Demirag, I. S. (1998). Financial Systems and Corporate Governance: a Theoretical framework. In I. S. Demirag (ed.) *Corporate Governance, Accountability, and Pressures for Reform: An International Study*. London: JAI Press Inc.

Federal Government of Nigeria (FGN), (1990). *Companies & Allied Matters Decree*. Lagos, FGN Press.

Fremond, O. & Capaul, M. (2003). Corporate Governance Country Assessment: Chile. World Bank Report on the Observance of Standards and Codes, http://worldbank.org/ifa/rocs_chlcg.pdf

Hilmer, F.G. (1993). Strictly Boardroom Information**:** Australia, Melbourne.

Hussain, S. H. and Mallin, C. (2002). Corporate Governance in Bahrain. *Corporate Governance: An International Review*, 10, 197ï 210

Mallin, C. A. & Jelic, R. (2000). Developments in Corporate Governance in Central and Eastern Europe. *Corporate Governance: An International Review*, Vol 8, 43ï 51.

Nigeria Deposit Insurance Corporation (1991). Pocket guide For Bank Directors. Lagos. *NDIC Annual Reports & Statement of Accounts*, (Various issues) Lagos.

Okike, E. N. M. (1989). Extension of Information in Accounting Reports. *Nigerian Financial Review*, 2, 38ï 55.

Okike, E. N. M. (1999). A Longitudinal Analysis of the Quality of Audit Reporting on the Accounts of ListedCompanies in Nigeria Following the Indigenization of Equity Capital (1978ï 1989). *Research in Accounting in Emerging Economies,* Supplement 1, 255ï 286.

Omofaye, Boarsin. (2009). Nigerian Banks urged to Strengthen Corporate Governance http://www.afriquejet.com/news/africa-news/nigerian-banks-urged-to-strengthen-corporate-governance-2009103037283.html

Ow-Yong, R. and Guan, Kooi (2000). Corporate Governance Codes: a comparison between Malaysia and the UK. *Corporate Governance: An International Review,* 8, 125ï 133.

Sarkar, J. & Sarkar, S. (2000). Large Shareholder Activism in Corporate Governance in Developing Countries: Evidence from India. *International Review of Finance*, 1, 161-195.

Solomon, J. & Solomon, A. (2004). *Corporate Governance and Accountability*. Chichester: John Wiley and Sons Ltd.

Umoh, P. N. (1994). *The Problems of Corporate Governance in the Nigerian Banking Industry*. Lagos, Stride Associates

Wallace, R. S. O. (1989). *Accounting and Financial Reporting in Nigeria*. Norwich: ICAEW.

Yasaki, A. G. A. (2001). Corporate Governance in a Third World Country with particular reference to Nigeria *International Review*, 9, July, 238ï 253.