CHAPTER ONE

GENERAL INTRODUCTION

1.1 Background of the Study

The recent occurrences in the international corporate environment have focused the world's attention to the concerns for effective domestic corporate governance initiatives that would ensure credibility on how companies conduct business in our post-modern globalised world. The reality of corporate governance is the success or failure of incorporated companies and most importantly on the national economy vis-à-vis the increasing globalised world economy.[1]

The requirement for transparency is reflected on the obligation of financial reporting and auditing, narrative reporting, business review placed on the board of directors. All the same, corporate responsibility is meant to be captured under social and environmental reporting and sustainability vis-à-vis development reporting to be prepared and presented by the board of directors during company's general meetings.

Decision making by large companies can significantly affect the environment -the local community, the livelihood of large numbers of the people who work for the company, consumer's choice and viability of suppliers. The various groups affected by or interested in a company are sometimes referred to as stakeholders. It is because of the clear impact the quality of corporate governance of the incorporated companies' business efficacy has on the economy vis-à-vis the society at large, that it becomes more imperative to x-ray the role of the legal frameworks in corporate governance.

[1] R. Ikpeahior & H.P. Faga 'Reflection on Sound Corporate Governance For a Thriving National Economic Environment', *EBSU Law Journal*, vol. 2, No 1 (2007) p.11.

The Nigerian economy has experienced its own fair share of drawbacks as a result of the consequences of poor corporate governance. In particular, the massive failure of several banks which led to losses of an unprecedented scale both for customers and investors, as well as the economy as a whole, serves as the most potent reminder of what could happen if the principles of corporate governance are completely ignored and corporations are allowed to run wild and free, managing their affairs as they please.

Corporate organizations have become major actors in the political economy of many countries. For a continual sustenance of this, there should be a robust corporate governance and effective risk management to enhance the efficiency and healthy working of these corporate organizations. The failure or lack of the sustenance of this corporate governance and risk management in corporate organizations has led to the scale of collapses of many gigantic businesses across the globe.

Traditionally, the focus of company law jurisprudence is solely on the rules and principles that safeguard the interest of the company's members and sometimes creditors only. This is no longer the case, as many jurisdiction, including Nigeria is now taking a different approach by noticing that the way companies are run affects not only their members and creditors, but also their customers, suppliers, employees, neighbors and also the society at large. Thus, how a company is governed, and decisions made in companies and other financial institutions are a major determinant of employment levels, regional development, a significant technological change and the condition of our physical and even cultural environment.

Therefore, in the corporate world the need for proper governance and corporate governance principles assumes greater proportion because of the wide-reaching effects of the consequences of corporate mismanagement.[2] The availability of accurate or up-to-date information on company performance is of fundamental importance. In the absence of reliable accounting data, effective shareholder supervision of management is impossible.

1.2 Statement of the Problem

Corporate governance in Nigeria generally reflects system governance problems, capacity constraints and ineffective implementation of laws which have led to limited economic growth. The private sector has dogged weakness inherent in its skewed structure, poor spate of infrastructure, high cost and limited access to appropriate financing, insufficient domestic demand, low level of patronage by public sector institutions, domestic policies, environmental factors and investment floors.

Poor corporate governance will eventually lead to financial crises in corporate organizations. The problems associated with the failure of companies are not unconnected with dearth of the corporate risk management. Failure to manage corporate risk will eventually lead to failure of a company.

The enormous problems associated with corporate governance have affected the interest of shareholders in these companies. It discourages prospective investors from investing on such companies; perverts the interest of the creditor lending financial assistance to the companies affected; it affects the interests of the consumers and other stakeholders, and eventually results in an impoverished economy in Nigeria.

[2] After the Enron saga, many other big and giant companies faced similar closure.

There is modicum of legislation that seek to protect incorporated companies from failing, yet they still fail because it appears that there are inadequate modalities for the implementation or enforcement of corporate governance principles.

In view of the prevailing problems resulting from the dearth of good corporate governance and risk management, it has become imperative to properly appraise the impact of corporate governance in Nigerian. First is the problem of effective enforcement of the rights of shareholders or members whose rights have been violated by the board of directors or majority shareholders against the minority shareholders. Secondly, the lack of effective monitoring of corporate organizations by the relevant authorities has hampered good corporate governance thereby resulting in corporate failures. Thirdly, the inability of the company management to manage risk has greatly contributed to financial crisis and failure of companies. It is in the light of the above problems that we got motivated to research further on this area of law, focusing on its impact on companies and the Nigerian economy.

1.3 Research Questions

The basic goal of this research will be actualized by answering the following research questions:

i. What is the impact of corporate governance on the Nigeria community?

ii. What are the measures capable of forestalling corporate collapse?

iii. Are there enough corporate governance legislation in Nigeria or is there need for more legislation?

iv. Are there clear and adequate mechanism put in place to enforce the extant laws and codes on corporate governance?

v. How does accountability by company management to shareholders in an incorporated company impact on the society?

vi. What are workable recommendations that will enable meaningful and successful operation of corporate legal framework in Nigeria?

1.4 Objectives of the Study

This thesis is aimed at achieving the following objectives:

i. Evaluate the impact of corporate governance vis-a-viz its relevance to the national economy and socio-economic life of the people.
ii. Appraise the efficacy of accountability to the shareholders and debenture holders as a corporate governance tool, and how it has impacted on the society.
iii. Identify the measures to forestall the collapse of incorporated companies.
iv. To proffer adequate recommendations that will enable the corporate institutions to accommodate practical approaches in maintaining good corporate governance without any impediment.

1.5 Research Methodology

In this research work, we adopted a doctrinal approach hinged on analysis, comparative study and appraisal. This research involves a vast collection of data. We deployed the analytical method to espouse the corporate governance models applicable in different economies. In using the comparative method, we were able to comparatively discuss the tenets and principles of corporate governance as well as the relative implementation and enforcement of the available legislative framework on corporate governance in various jurisdictions. We also used appraisal method to discuss the impact of corporate governance in comparable economies. The method of data collection is basically the use of primary materials like statutes, international treaties, and secondary sources like textbooks, dictionaries, journals and newspaper articles, conference papers, seminar papers, law reviews as well as law reports

of different sorts, and works of varying authors on the topic and related topics drawn from the internet.

1.6 Significance of the Study

The significance of this study lies in determining the extent to which good corporate governance has aided in combating corporate collapse and mismanagement in the economic sector. It further highlights the impact of corporate governance on the Nigerian socio-economic milieu. This work will enable the general public to embrace the prevailing economic realities and appreciate the relevance of implementation of ethical principles and the enforcement of legislative framework on corporate governance. It will also serve as a veritable guide to the judges in the dispensation of the sacred judicial function judicially and judiciously particularly on the issues that border on corporate governance and administration of companies.To the board of directors and other members of management team, this work will assist them to further appreciate the importance of corporate governance and risk management in companies and financial institutions and the need for change of attitude on how the business of a company is handled. To other stakeholders and the general public, this work will educate them on the pivotal principles of corporate governance and risk management and the resulting consequences of not observing the principles of good corporate governance. It will also provide a robust opportunity for business to strive thereby enhancing the concept of corporate governance and how to effectively manage risk. Above all, this work will provide the government of Nigeria, her agencies and all the relevant stakeholders in the various sectors of the economy with feasible ideologies that will enable them come up with sound policies and modalities for implementing them, and that will encourage and sustain the growth of our economy and the development of our Nigerian community.

1.7 Scope of the Study

This research work is basically on the impact of corporate governance on the Nigerian community vis-à-vis the historical development of corporate governance. In the course of this research, reference will be made to the concept and jurisprudence of corporate governance in other economies and jurisdictions such as the United Kingdom, United States and India with a view to drawing their corporate governance improvements to bear on the Nigerian economic growth and development.

1.8 Literature Review

1.8.1 Theoretical Framework

Since the discussion of corporate governance is a theoretical exposition of more practical affairs, one observes that there is no general consensus on the classification of corporate governance models. The approaches to the subject vary according to the ideological inclinations of the various authors who have written on it. For instance Ajaogwu[3] classifies corporate governance according to the variety of capitalism found in a given jurisdiction. According to him, emerging market models are represented by India, Malaysia and Thailand, while the Anglo Saxon model is represented by South Africa, Mexico and Hong Kong.

The Corporate Governance Group on the other hand identifies alternatives which *inter alia* include the Japanese Kiretsu Model, the Corporate Governance model in communist China, South Korea, Sweden and Italy.[4] Despite the multiplicity of classifications, the outsider and insider based models, because of their comprehensiveness, have been adopted for the purpose of the analysis in this research. There are two core features of the corporate form which underlie the outsider model of corporate governance.

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[3] F. Ajaogwu, *Corporate Governance in Nigeria: Law and Practice* (Lagos: Centre for Commercial Law Development (CCLD) (2007) pp. 27-29.

[4] Governance Model/Corporate Governance, available at: www.corporategovernanceoup.word.press.com, accessed on 10/11/2013.

According to Parkinson, the first is investor ownership which implies that shareholders, as residual claimants, have significant rights of control over their companies.[5] These rights include the right to alter the memorandum and article of associations of their companies; the right to authorize an increase or reduction in its capital and issuing of new shares, and the purchase or redemption of the company's shares, the right to call for the winding up of company and the right to sanction the payment of dividends (depending on the article of association). Kraakman identifies the second as delegated management, which implies that shareholders generally exercise this control indirectly, by participating in the selection or removal of directors or their closest equivalents in closed companies.[6]

On the insider based model, essentially, the question is whether mere shareholding can be equated with ownership. Dallas sees a company as a marketplace where various constituencies contract for their own protection. [7] According to Fama, ownership of capital should not be confused with ownership of the firm.[8] Each factor of production in the firm is owned by somebody. The firm is just the set of contracts covering the way receipts from outputs are shared among inputs. The insider based model favours the management of a company and limits the influence of shareholders as mere investors who are kept from wielding undue influence on the affairs of the company.

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[5] J.E. Pakinson, *Corporate Power and Responsibility, Issues in the Theory of Company Law*, (New York: Oxford University Press, 1993), p. 163.
[6] R.R. Kraakman *et al, The Anatomy of Corporate Law: A Comparative and Functional Approach*, (Oxford: Oxford University Press, 2004) p. 33.
[7] L.L. Dallas, Two Models of Corporate Governance: Beyond Berle and Means, (1988), cited by J.E. Pakinson, *op. cit*., p.163.
[8] E.F. Fama, Agency Problems and the Theory of the Firm, (1980), cited by J.E. Parkinson, *op. cit*, p. 178.

1.8.2 Conceptual Framework

The term ‘corporate governance’ is uniquely complex and multi-faceted. It has been looked at and defined variedly by different scholars. Jayashree[9] defines it thus:

> Corporate Governance when used in the context of business organization is a system of making directors accountable to shareholders for effective management of the companies in the best interest of the company and the shareholders along with concern for ethics and values. It is the management of companies through the board of directors that hinges on complete transparency, integrity and accountability of management.

Oyejide and Soyibo[10] view corporate governance from two perspectives viz: a narrow one in which it is viewed merely as being concerned with the structures within which a corporate entity or enterprise receives its basic orientation and direction, and a narrow perspective in which it is regarded as being the heart of both a market and democratic society. Lemo[11] states that corporate governance is a body of the rules of the game by which companies are managed and supervised by the board of directors in order to protect the interest and financial stakes of shareholders that are far removed from the management of the firm. Mensah[12] adds that corporate governance is an institutional arrangement which provides the discipline and check over excesses of controlling managers. For McLaughlin:

> Corporate governance means different things to different people in different contexts. Whenever the term is used, the first question to ask is, in what sense is it being used by the writer? If this is not made clear, it is usually helpful to examine the context in which the term is being used.[13]

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[9]S. Jayashree, ‘Some Views on Corporate Governance’, *Indira Management Review,* Indira School of Management Studies. Pune, (2006).
[10]Oyejideand Soyibo, ‘Corporate Governance in Nigeria’, Paper presented at the Conference on Corporate Governance, Accra, Ghana, 29- 30 January 2001.
[11]T. Lemo, Keynote Address of the 34thConference of ICSAN, Sheraton Hotel and Towers, Banquet Hall,Lagos.22-23 September, 2010.
[12]S.Mensah, ‘Corporate Governance in Africa, The Role of Capital Market Regulation,presented at the 2nd Pan African Consultation Forum on Corporate Governance, Nairobi, Kenya, (2003).
[13] S. McLaughlin, *Unlocking Company Law* (ed), (U.K: Hodder Education, 2009), p. 4-6.

Wilson defines corporate governance as the manner in which corporations are directed, controlled and held to account with special concern for effective leadership of the corporations to ensure that they deliver on their promise as the wealth creating organs of the society in sustainable manner.[14] Of course, the essence of it is to ensure effective running of the corporate business. To Ofo, the foregoing concept means a 'system of reconciling the interest of all the stakeholders of the corporate entity, whether shareholders, managers, suppliers, customers, financiers and society at large.[15]Imala supported this view when he added that it provides a framework that specifies the rights, the roles and responsibilities of different groups, management, the board of directors and shareholders with the associates.[16]

It involves a system by which governing corporate institutions and other organizations relate to their communities and stakeholders to improve their quality of life in Nigeria and by extension worldwide. According to Sun:

> Well executed corporate governance is similar to a police department's internal affairs weeding out and eliminating problems with extreme prejudice. Corporate governance can prevent corporate scandals, fraud and the civil and criminal liability of the company and members of the society in extension. It can also enhance a company's image in the public eyes as a self policing company that is responsible and worth of shareholders and debt holder capital.[17]

According to the former governor of Central Bank of Nigeria, Prof. Sanusi Lamido Sanusi, corporate governance is a key element in enhancing investor's confidence, promoting competitiveness and ultimately improving economic growth.[18] This view is unassailable to an

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[14]I. Wilson, 'Regulatory and Institutional Challenges of Corporate Governance in Nigeria, Post-Banking Consolidation', *Nigeria Economic Summit of the Cadbury Committee (1992)* which simply defined corporate governance as the system by which companies are directed and controlled, pp. 1-10.
[15]N. Ofor, 'Corporate Governance in Nigeria: Prospects and Problems', *Apogee Journal of Business, Property and Constitutional Law,*Vol.1, No.4 (2010), pp. 15-23.
[16] I. Mala, Promoting Good Corporate Governance:the Role of Independent Directors,' CBN Billion, vol. 31, N0. 3 (2007).
[17]L. Sun, 'Why is Corporative Government Important, available at www.business.dictionary.com/Article, accessed on 3 January, 2015.
[18]. S.A. Lamidi, CBN Official Magazine, p. 15.

extent, especially as the economy shifts from predominance of state owned enterprise to private sector-driven by means of the federal government policy of privatization, deregulation and commercialisation. Corporate governance can also be viewed as simply a shared philosophy, practices and culture of an organization and its employees. A corporate institution without a system of corporate governance is regarded as nothing but a body without soul or conscience. If shared philosophy breaks down, then corners will be cut, product will be defective and management still grows complacent.

The Organization of Economic Corporation and Development (OECD) defined corporate governance as a set of relationships between a business management and its board of directors, its shareholders and lenders, and other stakeholders such as employees, customers, suppliers and the community of which it is part of.[19] It involves a system by which governing institutions and other organizations relate to their communities and stakeholders to improve their quality of life.[20] It also involves corporate restructuring such as merger and acquisition in repositioning the business structure of the company. In Nigeria however, companies governed mainly in the interest of shareholders and creditors. Accordingly, the management of the company shall confine itself to the businesses or objects contemplated by the memorandum of association of the company.[21] Corporate governance is therefore about providing effective and accountable leadership in such a manner as will enable the realization of the organization's overall mission. It is characterized by transparency, accountability, probity and protection of shareholders' rights in respect to corporate bodies. Thus, corporate governance is a key element in enhancing investor confidence, promoting competitiveness and ultimately improving economic growth.

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[19]The Organization of Economic Corporation and Development, Principles of Corporate Governance, (Paris, 2009).

[20]J. Mohammed 'Impact of Corporate Governance on Banking Sector Performance in Nigeria ', *International Journal of Economics, Development, Research and investment*, Vol. 2, No. 2 (2011).

[21] Companies and Allied Matters Act, Cap. C20, LFN 2010, ss. 38 and 39.

It should be noted that a critical appreciation of the concept of corporate governance, as highlighted by the different authors will vividly demonstrate the fact that the above definition of corporate governance is shallow and not encompassing. In essence, corporate governance can be seen as a system or procedures adopted by business institutions, companies and other profit and non-profit making organizations in order to ensure efficiency, transparency, sustainability and securing the welfare of all stakeholders and the society at large.

Therefore, the heightened awareness of the need for effective corporate governance is not without justification. Ofo notes that a well implemented corporate governance regime has tremendous benefit. These benefits are the enduring attributes of corporate governance. In the first place, effective corporate governance eliminates financial scandals and curbs corporate failures.[22]

Undoubtedly, corporate governance was merely viewed in the narrow perspective. Even the board perspective elucidated by Oyejide and Soyibo as the heart of both a market and democratic society was not all inclusive of the stakeholders.[23]It is our submission that corporate governance is quite inclusive in terms of its stakeholders. Virtually every person is affected by the activities of a company, and therefore, is a stakeholder.

There has been a renewed concern the world over in the substance of legislation regulating corporate governance systems. These pieces of legislation affect directors, financial statements, auditors, shareholders and other stakeholders' right as well as how they are well integrated in corporate decision-making process.

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[22]N. Ofo, 'Corporate Governance in Nigeria: Problems and Problems', A*pogee Journal of Business and Constitutional Law*, Vol 1. No. 4, 201, 0. p. 17.
[23]O.A. Momoh and M.S. Ukpong, 'Corporate Governance and its Effects on the Nigerian Insurance Industry',*European Journal of Globalization and Development Research*, Vol. 8, No. 1, 2013, p. 481. I, Wilson, 'Regulatory and Institutional Challenges of Corporate Governance in Nigeria Post Banking Consolidation', *Nigerian Economic Summit Group (NESG) Economic Indicators*, April-June 2006, Vol. 12 No. 2, p.1.

In Nigeria, the major legislation governing company affairs is the Companies and Allied Matters Act.[24] It provides how a company is to be incorporated as well as how it is to be run. It contains provisions for how a person can become a member of a company. Furthermore, it provides for the management and directional responsibilities of directors and managers in a company. It also provides a mandatory compliance with the financial statement - how it is to be arranged and laid. In the same vein, it provides for auditing of the firm's financial statement and reports, so as to ensure that accurate information is reported therein.

Hill however notes that the lesson to be learnt from HIH and One-Tel as in Enron as well as Cadbury in Nigeria is that the existence of corporate governance procedures like investment guidelines, an investment committee and codes of conduct are of little use when they are passed without enforcement mechanism.[25] The role of auditors in enhancing corporate governance is indispensable. They aid in checking any shady transaction by the directors or shareholders. Consequently, section 357 of the CAMA provides for the appointment of auditors to audit the financial statements of a company till the next annual general meeting. Section 342 CAMA provides for the tendering of a yearly report by the director which shall contain the names of the directors and the financial activities of the company and its subsidiary over the year. All these are legal sentinels to curb any incidence of financial mismanagement and fraud in the company and to ensure accountability to the shareholders.

On the concept of financial reporting, Okpeahior posits that it is a practice of corporate governance aimed at ensuring or reinforcing the accountability of directors to shareholders. [26] Okeahalam and Akinbode concurred with the view that the financial reports constitute the instrument that shows the impact of the decision of the management with respect to the

[24]Cap.C20, Laws of the Federation of Nigeria, 2010.
[25]J.G. Hill, 'Regulatory Responses to Global Corporate Scandals', *Wisconsin International Law Journal*, vol. 23, No. 3.
[26]R.Opeahior and H.P. Faga, *op.cit*, p.218.

growth of shareholder's wealth. Therefore such reports need not be dearth of credibility and must be verified by an independent expert or auditor since the board of directors is in fiduciary relationship with the company, as enshrined in section 279 of the Companies and Allied Matters Act.[27]

On the conceptual analysis of auditing, Okeahalam opined that the main objective is to detect error or fraud.[28] The internal auditor reports to the Chief Execution Officer and all the same assists the executive manager and board of directors in discharging their duty particularly as concerns safeguarding asset, risk management, operation of adequate controls and transparency of financial statements and stewardship report. Okpeahior observed with precision that internal auditing is not always enough to guarantee error-free financial system.[29] The realization of possible confusion between the executive management and the internal auditor made provision for external auditor an essential factor for more transparency in the accounting system of a company. Chartered accountants, as external auditors, are professional experts empowered to examine these financial statements not only to determine whether they represent true, fair and ideal statement of affairs of the corporate entity and are free from any material misstatement, but also to ascertain if they conform to the universal accepted accounting principles and other relevant pieces of legislation and standards.[30] The main objective of the external auditor is to give a report on the view presented by the financial statement or reports prepared by the managers. Similarly, Okeahalam opined that the detection of fraud and errors are incidental to this main objective.[31] It is observed that the external auditors are usually appointed by shareholder and are required to submit their report to shareholders during annual general meeting. Unlike internal auditors who are accountable

[27]C.C Okeahalam and O.A. Akinbode, 'A Review of Corporate Governance in Africa: Literature, Issues and Challenges', a paper presented at Global Corporate Governance Forum,15th June,2003, p.15.
[28]*Ibid*, p. 17.
[29]*Ibid*,p.218.
[30]Companies and Allied Matters Act (CAMA), Cap. C20 LFN, ss. 358 & 359.
[31]*Ibid.*

to the chief executive, the external auditor is accountable to the body of shareholders.[32] From the understanding so far on the appointment of external auditors, it is discovered that the appointment of external auditors of the banks in Nigeria are done by shareholders of the banks and are expected to receive the approval of the Central Bank of Nigeria in accordance with section 29 of Banks and Other Financial Institutions Act (BOFIA). In furtherance to this end, Okpeahior observed that the report of such external auditors are expected to be read together with the report of board of directors at the annual general meeting while two copies of each report together with the auditors' analysis of bad and doubtful advance, in a form specified by the Central Bank of Nigeria shall be sent to the apex bank, for its information and consideration. In the same view the external auditors are expected to submit two copies of the management or domestic report to the apex bank within 3 months of the end of the financial year.[33]

Okpeahior further observed that audit committee of the corporate institution is traceable to the celebrated fraud case of *McKesson* and *Robin* in the United State of America 1939.[34] More so, audit committee has been mostly described by various learned auditors as the most important development in corporate structure and control in decades. It is conceived as an investors' protection mechanism.' On his part, Otuwanug noted that the recommendation made by the United States Security and Exchange Commission in 1940 over the 'fraud case' was adopted in the Companies and Allied Matters Act of 1990[35] and presently, the audit committee has been mandatorily compelled to be responsible for the reviewing of the

[32]Subject to Section 357(5)(a)and(b) of CAMA, the first auditors of a company may be appointed by the directors at any time before the company is entitled to commence business and auditor so appointed shall hold office until the conclusion of the next annual general meeting. Subsection 3 of the foregoing section provides that where at annual general meeting, no auditors are appointed or re-appointed, the directors may appoint a person to fill the vacancy.
[33]*Ibid*, p.218.
[34]*Ibid.*
[35]Now, Cap C20 Laws of the Federation of Nigeria (LFN),2010.

integrity of the bank's financial reporting and oversee the independence and objectivity of the external auditors.[36]

Okeahalam stated that the audit committee plays an important role in financial and operational control in the whole system of corporate governance by making recommendations to the board concerning the appointment and remuneration of external auditors, reviewing auditors' evaluation of the system of internal control and accounting and making of recommendations on the conduct of any aspect of company which should be brought to the notice of the board of directors among others.[37]

Adeyemi expresses with a firm view that the search for mechanism to ensure reliable and high quality financial reporting has largely focused on the structure of the audit quality. [38]

Wilson remarks that despite the power given to the shareholder to consider and approve the appointment and remuneration of auditors *vis-a-vis* the financial statement in a general meeting so as to ensure that board of directors observe financial discipline in the management of the company, the shareholders have not effectively and efficiently utilized the power.[39] He further affirms that all systems of internal control are subject to limitations and weakness and no matter how good the planning of the system, no matter how strict and consistent its application, it can never give perfect protection and safety to human factors.

Discerning from the foregoing, it is discovered that in practice, shareholders often rubber-stamp the financial statements presented to them sometimes assuming that the financial statement presented, having gone through internal audit controls, ought to be correct and

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[36]S.E. Otuwanuga,'Shareholders' Activism.Role in Corporate Governance and Investor Protection', *Law and Investment Journal,* Vol 1 No 2 (2007) p.25.
[37]*Ibid,*p. 15.
[38]S.B Adeyemi & T.O Fagbemi, 'Audit Quality, Corporate Governance and Firm Characteristic in Nigeria', *International Journal of Business and Management,* vol.5 No.5 (2010) p. 169.
[39]Wilson,*op.cit*, p.3.

accurate. The onus therefore is upon the regulatory bodies[40] to properly scrutinize the financial statement of the company[41] to ensure transparency and defined accountability and auditing.

Orojo observes that directors are required to prepare in respect of each financial year a director's report which will be attached to the balance sheet of the company.[42] The opinion of Bourne is germane and at consensus with that of Orojo. According to the learned author, every company must attach to the balance sheet and profit and loss account a director's reports[43]

It is germane to stress at this point, as a matter of observation that the scope of directors' report as provided in section 342 CAMA, must contain a fair view of the development of the business of the company and its subsidiaries during the year and their position at the end of it. What more, the directors' report shall state the amount (if any) which they shall recommend should be paid as dividend and the amount (if any) which they propose to carry to the reserves. Failure to comply with the requirement and particulars to be given in the director's report is not without legal punishment unless persons involved can prove that they took all reasonable steps in securing compliance to the said requirement. The law provides a punishment for such failure in that every person who was a director of the company immediately before the end of the period prescribed for laying and delivery of financial statement shall be liable to the term of imprisonment for more than 6 months or to a fine of ₦500 only.

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[40]Regulatory bodies such as Central Bank of Nigeria(CBN), Corporate Affairs Commission (CAC), Securities and Exchange Commission(SEC) and host of others.

[41]Since adequate accountability may not be achieved through financial reporting and auditing.

[42]J.O.Orojo, *Company Law and Practice in Nigeria,* 5th edition(London: Lexis Nexis,2008) p.303.

[43]N. Bourne, Principles of Company Law, 3rd edition(London: Cavendish Publishing Limited,1998) p.203.

It has been concurrently agreed among the learned authors that as part of the duty a company has for the privileges of incorporation and limited liability accorded thereto by law, is the degree of openness, and publicity about its affairs. Sealy expresses that the Companies Act has been largely based on this philosophy.[44] Bauley completely expressed similar view with Sealy.[45] The views of these learned authors can be adjudged right in the light of the provisions of the Companies and Allied Matters Act,[46]particularly on the provisions for disclosure with respect to individual interest of members in the share capital of a public company.

However, beyond this, the Cadbury Report of 1992 reported that a major barrier to the flow of relevant information is the risk of opportunism inherent to the manager's influence in the firm which is referred to as an inchoate or distorted disclosure of information and calculated efforts to mislead, distort, obfuscate or otherwise confuse the general public and shareholders.[47]

Seberu and Aremu stated that in Nigeria, society has been a place of increase demands on big business organizations for great social responsibilities in the next decade. This has been a pressure on business to be involved in solving social and economic problems. The concern includes employee's welfare, working conditions, prevention or evacuation of pollution,

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[44]L.S.Sealy. 'Cases and Materials in Company Law',6th edition(London:Butterworth,1996) p.585.
[45]J.Bauley and Laid McCallum, *Company Law*, (London: Heine Mann, 1990), p.8.
[46]Companies and Allied Matters Act (CAMA), *op. cit*, ss. 94-98,273 and 277,340 and 341.
[47] The Cadbury Report, titled *Financial Aspects of Corporate Governance*, is a report issued by 'The Committee on the Financial Aspects of Corporate Governance' in UK, chaired by Adrian Cadbury that sets out recommendations on the arrangement of company boards and accounting systems to mitigate corporate governance risks and failures. The report was published in draft version in May 1992. Its revised and final version was issued in December of the same year.

product-safety, marketing practices, employment and community development[48] among others.[49]

Essentially, corporate governance and risk management are interrelated and interdependent concepts. Knight rightly stated that the sustainability of company's performance is highly dependent on the effective role of both concepts. The element of control is one of the corporate governance roles, while a controlled environment is developed from the risk management process.[50]

According to Essinger and Rosen, risk management is an effective technique for minimizing undesirable effects of risks and optimizing the benefits of risky situations.[51] Chapman and Ward describe the aim of risk management as process enhancement that is established through systematic identification, evaluation and mitigation of project risks.[52] The function and objective of both corporate governance and risk management is to maximize shareholder value. They are connected to assist organizations to better understand risks, to improve and deliver its objectives and to mitigate, assess, and manage risk in an appropriate manner. Recent accounts on company failures, corporate scandals, and frauds are among the reasons for companies to effectively implement risk management programmes. Mitton is of the view that companies' failures should be blamed on poor risk management and corporate

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[48]O.J.Suberu and O.S.Aremu, 'Corporate Governance and Merger Activity in the Nigerian Banking Industry', Department of Banking and Finance, The Polytechnics, Ibadan, Nigeria, *J Economics*, 1 (2), pp. 91-97.

[49]Companies or Corporate Institutions embark on these provisions purely on moral and ethical grounds and never as a legal obligation. Since the investigator's money is involved in such developmental expenditures, the directors, as part of Annual accountability are required to report on the Corporate Institution's social outreach for the year. A new plan may be presented through the reporting for consideration by the shareholders at the General Meeting.

[50] K.W. Knight, 'Risk Management: a Journey Not a Destination', Paper presented at the Executive Meeting 2006, Hotel Do Frade & Golf Resort, Angra Dos Reis, Brazil 20th May 2006.

[51] J. Essinger, & J. Rosen, Using Technology for Risk Management, in M. Jafari, *et al* (2011), 'Effective Risk Management and Company's Performance: Investment in Innovations and Intellectual Capital Using Behavioural and Practical Approach', *Journal of Economics and International Finance*, 3(15), 780-786.

[52] C. Chapman & S. Ward, 'Project Risk Management-Processes, Techniques and Insights in M. Jafari, *et al* (2011), Effective Risk Management and Company's Performance: Investment in Innovations and Intellectual Capital using Behavioural and Practical Approach', *Journal of Economics and International Finance.* 3(15), 780–786.

governance. For example, in the East Asian financial crisis in 1997, weak corporate governance and poor risk management have been found as the main factors of companies' failure.[53]

On the impact of corporate governance on the Nigerian community, Oluyemi considers corporate governance to be of special importance in ensuring the stability of the economy and successful achievement of banking strategy. This is an important framework for development, entrepreneurship and economic growth.[54] Effective corporate governance improves economic efficiency, access to domestic and foreign capital, human resource productivity and development of market economy.[55]

Yahaya, commenting on the impact of corporate governance on the economy of Nigerian community, says it would undeniably have enormous impacts if the principles, structures and mechanisms of corporate governance are applied widely in Nigeria; not only to public listed corporate institutions, but also to the state enterprises, cooperatives and the banking sector, as well as NGOs and to public services management, such as health, and education boards. This will checkmate the rate of corruption in Nigerian economy.[56] Yahaya is strongly optimistic that given the advantages and impact of corporate governance, it would no doubt have an overwhelming impact if the principles, structures and mechanisms of corporate governance be applied widely in Nigeria, and not just to public listed companies. It should extend to state enterprises or corporations, the banking sector, NGOs and to public services management,

[53] T.A. Mitton, 'Cross-Firm Analysis of the Impact of Corporate Governance on the East Asian Financial Crisis', *Journal of Financial Economics*, (2002) p. 64, 215-241.
[54]S.A. Oluyemi, Banking Sector Reforms on Imperative of Good Governance in the Nigerian Banking System, pp.1-33.
[55]Agusto,'Sustaining Effective Corporate Governance in a Corrupt Environment –A paper presented at the Executive Mandatory Continuing Professional Education (EMCPE) of the Chartered Accountants of Nigeria.
[56]A.O.Yahaya, 'Corporate Government in Nigeria: A Focus in the Public Sector, in Olademiji Alo(ed),Issues in Corporate Governance (2003),p.15.

such as health, and education boards. If this is done, it will ameliorate the rate of corruption and the attendant damage it has caused to the Nigerian economy.[57]

The concept of corporate collapse or failure has so much implication both in larger and expansive corporations and smaller corporations. For instance, the recent saga of Enron and WorldCom in the United States in the early 2000 and the lesser corporate scandals as Adelphi's Communications, AOL, Arthur Anderson Global Crossing, Tyco occurring in United States were globally recognized as devastating and highly destructive. There have also been recent scandals in Europe that is Vivendi and Parmalat scandals. These are the most recent such disturbing issues of corporate collapse and business failure across the world.

Unarguably, Nigeria has also had its bite of inelegant business practices that have resulted in failure of some corporate giants without any overt sign of trouble for example, Telkom. It is observed that no company whatsoever can be too big to fail if the practice of good corporate governance is jettisoned.

In the event of collapse of these corporations, apart from business community, community at large, the society, suffers in no small measure. This is because such collapse affects the proper management and organization of the company. In such a case, the society loses as the goods or/and services rendered by the company would cease or come to a sudden halt. Arguden argues that no investor would risk his investment in a corporation riddled with controversies, fraud, financial scandals, maltreatment of stakeholders or one administered as a one-man entity.[58]

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[57]A.O. Yahaya, 'Corporate Governance in Nigeria: A Focus in the Public Sector, in O. Alo (ed), Issues in Corporate Governance (2003), p. 15.

[58]Y.Arguden, 'Measuring the Effectiveness of Corporate Governance', available at: www.knowledge.Insted.Edu>Home?CRS>CorporateGovernance, accessed on 15/05/2014.

According to Lamido, there is no argument to the fact that corporate governance is a key element in enhancing investors' confidence, promoting competitive and ultimately improving economic growth.[59] Even as the economy moves from the predominance of state owned enterprise to a private sector-led one through the ongoing privatization exercise as can be seen recently in the power sector, one of the assurances that investors will realize the dividends of such exercise is the implementation of corporate governance principles and codes by such privatized companies. Ai-faki posits that even from the examples of other jurisdictions like the United Kingdom and the United States, it has been established that there is a direct correlation between a country's gross domestic product (its socio-economic life) and its corporate governance practice.[60]

There has been a few governance principles developed as part of our company laws in Nigeria contrary to the assertion of many authors in Nigeria.[61]According to Okpara, Nigeria have ample laws for the development and implementation of effective corporate governance in the country but noted lack of enforcement as the problem. [62] Oyebode pointed out that while the Companies and Allied Matters Act envisages good governance, the reality of our situation is that all this has largely become academic on account of impotent and moribund regulatory agencies.[63]

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[59]S.A, Lamido, The Central Bank of Nigeria (Official Magazine) p. 15.
[60]M. Ai-faki, 'Effective Enforcement of Disclosure Requirements by Regulatory Agencies: the SEC View Point', *Law and Investment Journal*, Vol. 1, No. 7 [007] pp. 33-39.
[61]Oserogho & Associates, Corporate Governance in Nigeria: Are There Laws and Principles? Available at: {www.documents}, URC http:// oseroghoassociates.com/news-2003-.5html, accessed on 9/1/2015.
[62]J.O Okpara, Perspectives on Corporate Governance Challenges in a Sub-saharan African Economic, available at:[www.Document},URL, http:www.ubicon.pro.com/iijohn.pdf.college.of.business.bioomsburg,university.of.pennysylvania, accessed on 9/1/2015.
[63]O. Akin, The Imperative of Corporate Governance in Nigeria, available at: [www.document} 4RL, http:// www.nigeria.villagesquare.com/articles/alkinoyebose/the-imperative-of-corporate-goverance-Nigeria, accessed on 9/1/2015.

A great deal of work has been done in the area of corporate governance by different authors, especially those whose contributions have been meticulously ingrained into this work. The uniqueness of this analysis however lies in its attempt to juxtapose corporate governance in two leading economies, namely the United Kingdom and the United States to show how their practices have influenced corporate governance in some developing economies, particularly Nigeria and India, and how corporate governance in Nigeria compares to corporate governance in India as a country which shares jurisprudential and economic similarities with Nigeria. The goal is therefore, to see the extent to which Nigeria can learn from these other jurisdictions and incorporate some of their corporate governance practices into Nigerian corporate governance policy for the benefit of the Nigerian community and her economy.

CHAPTER TWO

THE CONCEPT AND DIMENSIONS OF CORPORATE GOVERNANCE

2.1 Introduction

Corporate governance may be viewed from varying models of governance. In general terms, corporate governance refers to both descriptions and prescriptions by the directors and members, especially in large publicly listed companies, who control the company, and in whose interest the powers of a company are exercised.[64] From a regulatory perspective, this would include not merely the legal rights of shareholders, but the contractual covenants of debtors, the commitments entered into with employees, suppliers and customers, the regulations imposed by various government agencies, and the regulatory structuring of the various markets in which the company operates. This perspective is consistent with a 'stakeholder theory' of corporate governance, in which the interests and welfare of employees, creditors, suppliers, customers and the local community are all seen as restricting the freedom of management to maximize wealth for shareholders. This view is obviously based on economic efficiency and/or social justice.[65] It is therefore pertinent to consider the different models of corporate governance.

2.2 Meaning of Corporate Governance

Corporate governance means different things to different people and in varying contexts.Various authors, writers, journalists, researchers, academics and the like have different conceptions of corporate governance. The concept of corporate governance

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[64]H. Gospel and A. Pendleton, 'Finance, Corporate Governance and the Management of Labour: A Conceptual and Comparative Analysis', *British Journal of Industrial Relations*, vol. 41 (2003) 557. Also, Steve Letza*et al*, 'Shareholding Versus Stockholding: A Critical Review of Corporate Governance', (2004) 12 *Corporate Governance: An International Review* 242.

[65] R. Mitchell *et al*, 'Shareholder Value and Employee Interest: Intersections between Corporate Governance, Corporate Law and Labour Law" being a Revised Version of a Paper Presented at the Economic Globalization and Corporate Governance Conference, University of Wisconsin Law School from 11-12 March, 2005 and the 4th Asian Corporate Conference, Korea University, Seoul, 19-20 May, 2005, (Melbourne: Centre for Corporate Law and Securities Regulation and Centre for Employment and Labour Relations Law, 2005) pp. 1-39.

originates from a Greek word*Kyberman* which means to steer, guide and govern. It revolved to Latin where it was known as *gubernare,* and to French where it was referred to as *governer*. Corporate governance is simply the process of decision making and its implementation.[66]This concept can be viewed from two perspectives, to wit: the narrow perspective and the broad perspective.[67]The first perspective or view posits that corporate governance is concerned with the structures within a corporate entity or how the enterprise receivesitsbasicorientation and direction. The second viewregards corporate governance as being the heart of both a marketeconomy and democratic society. Oyejide and Soyibo define corporate governance as the relationship of the enterprise to shareholders or in the wider sense as the relationship of the enterprise to society as a whole. Mayer, on his part defines corporate governance as the sum of the processes, structures and information used for directing and overseeing the management of an organization.[68]Corporate governance refers to the system by which companies are directed and controlled.[69]

Essentially, corporate governance is about how the affairs of companies and other corporate institutions are conducted by those charged with the responsibility of overall management and control.[70]According to Colin Tricker, if management is about running business,then governance is about seeing that it is run properly.[71]In his view, Nat Ofo points out that corporate governance is a system of reconciling the interests of all the stakeholders of a corporate entity, whether as shareholders, management, suppliers, customers, financiers

[66] M.A. Abu-Taparijeh, 'Corporate Governance from Islamic Perspective: A Comparative Analysis with OECD Principles;
[67]T.A. Oyejide and A. Soyibo, 'The Practice and Standard of Corporate Governance in Nigeria,' *DPD Research Report*, Vol. 26, No. 33.
[68] F. Mayer, *Corporate Governance and Performance in Enterprise and community: New Directors in Corporate Governance* (Oxford UK: Blackwell Publisher, 1999).
[69] S.A. Cadbuny, *Report on the Committee on the Financial Aspects of Corporate Governance*, Gee limited (London: Professional Publishing Limited, 1992).
[70]R. Okpeahior& H. Faga, 'Reflection on sound Corporate Governance for a Thriving National Economic Environment,' *Ebonyi State University Law Journal*, Vol.2, No.1, 2007.
[71]O. Tennyson and O.E. Mercy, 'Corporate Governance and Organizational Performance in Nigerian Banks',*European Journal of Business and Management,* Vol.6, No.16 (2014), p.12.

andthesociety at large.[72]He further states that in getting a clear understanding of what the concept is all about effective components of corporate governance should be borne in mind. The common components of effective corporate governance are fairness, transparency, accountability and responsibility.EmekaAnyaoku adopting a wider definition of corporate governance as advanced by the Common Wealth Association for Corporate Governance maintains that corporate governance is basically about leadership for efficiency, forprobity, with responsibility and leadership, which is transparent and accountable.[73]

As a concept, it is concerned with the process by which corporate entities particularly limited liability companies are governed. It is the exercise of power in directing, supervising, managing and controlling the actions of a company with the concern for the effect of the activities of the companyon other parties particularly the stakeholders, and the accountability of corporate administrators.[74] It also improves the structuresand processes of governance which help to ensure quality decision-making, encourage effective succession planning for senior management and enhance the long-term prosperity of companies, independent of the type of company and its sources of finance as it reduces risk of investments.[75]The concept has become necessary for all jurisdictions, including those with already developed andsophisticated economic systems, as well as those with developing economythat areanxious to attract international portfolio investments. This presupposes that corporate governance is imperative in all economies of the world. Therefore, the remark made by the

[72] N. Ofo, 'Corporate Governance in Nigeria: Prospects and Problems, *Apogee Journal of Business, Property and Constitutional Law*, No. 4, 2010, p.20.
[73] E. Anyaoku, 'Corporate Governance and the Enterprise Culture,' *Journal of Commercial Law and Practice,* pp 41-45.
[74] M.I. Yahaya, 'Corporate Governance in the Perspective of Private Sectors, in the Publication of the 28th Annual Accountants' Conference with the theme, - Corporate Governance, September 8-12, 1998, p.130.
[75] M. Alfaki, 'Capital Market Regulation and Corporate Governance Reforms in Nigeria,' being a Paper Presented at the 32rd Annual Conference of the Institute of Chartered Secretaries and Administrators of Nigeria on Thursday, 6th November, 2008.

president of the World Bank is apposite; hence 'the proper governance of companies will become as crucial to the world economy as the proper governance of countries.'[76]

Prescriptively, corporate governance refers to the processes of supervisions and control intended to ensure that the company's management acts in accordance with the interests of the shareholders.[77]It is essential to distinguish governance from executive decision making, the former being the process by which managers, are held accountable for the performance of their functions. The governance structure is the set of rules and institutions of statutory, common law, or anyidentifiable origin, by which the processes of supervision and control are established.Notably, the need for corporate governance arisesessentially to deal with the imbalance associated with the principal/agency relationship which predicates the separation of management and ownership in the modern corporation. In practice, the interests of those who have effective control over the firm differ from the interests of those who supply the firm with external finance. More often than not, this culminates to the agency problem in corporate governance which isdemonstrated in management pursuing activities which may be detrimental to the interest of the shareholders of the firm. However, this agency problem is usually mitigated through the protection derived from good corporate governance.[78]

Furthermore, corporate governance is concerned with creating a balance between economic and social goals and between individual and communal goals while encouraging efficient use of resource, accountability in the use of power and stewardship, and aligning the interests of individuals, corporations and society.[79] It also encompasses the establishment of an appropriate legal, economic and institutional environment that allows companies to thrive as

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[76] World Bank, 'The East Asian Miracle: Economic Growth and Public Policy, 1995, pp. 5-7.
[77] J.E. Parkinson, 'Corporate Power and Responsibility: Issues in the Theory of Company Law; (United Kingdom: Oxford Clarendon Press, 1993) p. 159.
[78] C.C. Okeahalam and O.A. Ajinboade, 'A Review of Corporate Governance in Africa; Literature,Issues and Challenges, a Paper Prepared for the Global Corporate Governance Forum, 15 June, 2003.
[79]*Ibid*.

institutions for advancing long term shareholder value and maximumhuman-central development while remaining conscious of their other responsibilities to stakeholders, the environment and the society in general.[80]As Conhran and Waruick put it, corporate governance is an umbrella term that includes specific issues arising from interactions among senior management, shareholders, boards of directors and other corporate stakeholders.[81]From a public policy perspective, corporate governance is about managing an enterprise while ensuring accountability in the exercise of power and patronage by firms.[82]From a banking industry perspective, good corporate governance demands that banks will operate in a safe and sound manner, comply with applicable laws, rules and regulations, and will also protect the interests of depositors as well as other stakeholders. Interestingly, not many Nigerian banks are noted for their strict observance of corporate governance best practices and high official standards in their operations.[83]Corporate governance describes an apparent attempt by the company to ensure decency in its operations in keeping with the applicable rules.[84] In other words, corporate governance discussions embody the fusels between managers of public companies and their owners over the productive level of shareholder involvement in corporate policy and administration.[85]Some of these trustees are sometimes expressed through shareholder activism, which thus becomes a corporate governance and managerial or board accountability mechanism.[86]Suffice it to state that

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[80]*Ibid*.

[81] P. Cochtan and S. Waruack, 'Corporate Governance: A Review of the Literature,' Financial Executives Research Foundation, Morristown, New Jersey.

[82] Good corporate governance seeks to promote socio-economic objectives to wit: efficient, effective and sustainable corporations that contribute to the welfare of society by creating wealth, employment and solutions to emerging challenges; responsive, accountable and legitimate corporations that are managed with integrity, probity & transparency; and recognition and protection of stakeholder rights, which is an inclusive approach based on democratic ideals, legitimate representation & participation.

[83] U. Aniemena, 'Good Corporate Governance in the Banking System,' being a Paper Delivered at the 3rd Pan Africa Forum on Corporate Governance, 8-10 November, 2005 at Dakar, Senegal.

[84] N. Jackson and P. Carter, 'Organizational Chiarosonro: Throwing Light on the Concept of Corporate Governance,' *Human Relations*, Vol. 48, 1998, pp. 875-889.

[85] K.N. Schacht, 'Institutional Investor and Shareholder Activism: Dealing with Demanding Shareholders, *Directorship*, Vol. 12, No. 5, 1995, p. 8-12.

[86] E. Adegbite, *et al*, 'Political Analysis of Shareholder Activism in Emerging Democracies; A Case Study of Nigeria, CSGR Working Paper 265/10.

shareholder activism is described as the activism undertaken by shareholders in connection with contestation between managers of public companies and their owners.[87]

Indeed, corporate governance as a concept is wide in its significations. However, it is safe to say that it is all about the manner in which corporations are directed, controlled and held to account for their activities. It is concerned with effective leadership of corporations to ensure that they deliver on their promise as the wealth-creating organ of society and that they do soin a sustainable manner.[88]

It is pertinent tonote that as interests abound, corporate governance has played a significant role in engendering progressive renewal of companies, especially at the wake of the high profile collapses and failures of a number of large corporations most of which involve accounting fraud. In Nigeria for instance, corporate scandals in various forms have informed public and political interest in the regulation of corporate governance. These scandals include those of the Cadbury Ltd, the Securities and Exchange Commission and the Central Bank of Nigeria, which necessitated the need to provide Codes of Corporate Governance for public listed companies and the banking sector respectively. The Code of Corporate Governance for Banks and other Financial Institutions which was drafted by the Banker's Committee in 2003 was the first corporate governance code in Nigeria. This was followed by It was followed by the Code of Best Practices on Corporate Governance in Nigeria, 2003, by the Securities and Exchange Commission. This was amended and reissued in 2011. Others include the Code of Corporate Governance of Banks in Nigeria Post-Consolidation, 2006; Code of Corporate Governance for Licensed Pension Operators, 2008, and the Code of Good Corporate Governance for the Insurance Industry, 2009.These actions were taken to restore public confidence in corporate governance. Note that the basis of effective governance is public

[87] K.N. Schacht, *op.cit*, p.875-889.
[88] W. Inam, 'Regulatory and Institutional Challenges of Corporate Governance in Nigeria Post-Banking Consolidation,' *Nigerian Economic Summit Group (NESG) Economic Indicators*, Vol. 12, 2006.

confidence and that confidence is endangered when ethical standard falter or appear to falter.[89]Comparablefailures in the U.S (EnronCorporation andMClInc.), and in Australia (HIH and One Tel) are associated with the eventual passage of the Sarbanes-Oxley Act in 2002 and the CLERP 9 Reforms respectively.

The basic purpose of corporate governance, from the foregoing is to monitor those parties within a company which control the resources owned by investors and the primary purpose of sound corporate governance is to contribute to improved corporate performance and accountability in creating long term shareholder value.However, the foundations to this governance is the action of the individuals more so, their official inclinations and attitudes. In otherwords, these actions are guided by a person's moral stance. Some of the characteristics which are important in the development of an appropriate moral stance include fairness, openness/transparency, independence, probity/honesty, responsibility, accountability, reputation, judgment and integrity.

2.3Principles of Corporate Governance

Nowadays, discussions of corporate governance issues tend to refer to principles raised in three documents released since 1990. The documents include:

a. The Cadbury Report (UK, 1992).
b. The Principles of Corporate Governance (OECD, 1998 and 2004).
c. The Sarbanes-Oxley Act of 2002 (US 2002).

The Cadbury and OECD reports present general principles around which companies are expected to operate in order toensure proper governance. On the other hand, the Sarbanes-Oxley Act informally referred to as Sarbox or Sox, is an attempt by the United States federal

[89]GoodluckEbele Jonathan quoted former president of the U.S, John F. Kennedy in a speech delivered at a one day workshop on corporate governance held at the Civil Reception Centre, Victoria Island, Lagos, on 3 December, 2008.

government to legislate several of the principles recommended in the Cadbury and OECD reports.The principles include:

a. Rights and Equitable Treatment of Shareholder

Companies, by this principle, are expected to respect the rights of shareholders as well as help them exercise those rights. They can help shareholders exercise their rights by openly and effectively communicating information and by encouraging shareholders to participate in general meetings. Information provided should be given at a reasonable time before the meeting. Also, the place of meeting should be adequately considered as well as cost and travelling expenses.[90]

b. Interests of other Stakeholder

Organizations should recognize that they have legal, contractual, social and market driven obligations to non-shareholder stakeholder, including employees, investors, creditors, suppliers, local communities, customers and policy makers. By so doing, theybecome socially responsible to these groups of individuals rather than seeking profit-maximization in their enterprise.[91]

c. Role and Responsibilities of the Board

Given that the board of directors is an important organ in an organization (company), it needs sufficient relevant skills and understanding to review and challenge management performance. It also needs adequate size and appropriate levels of independence and commitment.[92]

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[90] OECD Principles of Corporate Governance, 2004, Articles II and III Retrieved on 24-07-2011; A. Cadbury, 'Report of the Committee on the Financial Aspects of Corporate Governance,' Gee, London, December 1992, sections 3.2, 3.3, 4.33, 4.51 and 7.4.
[91] OECD Principles of Corporate Governance, 2004, Preamble and Article iv.
[92] OECD Principles of Corporate Governance, 2004, Article iv.

d. Integrity and Ethical Behaviour

Integrity should be a fundamental requirement in choosing corporateofficers and board members. Thus, organization should develop a code of conduct for their directors and executives that promotes ethical and responsible decision making.[93]

e. Disclosure and Transparency

Here, Organizations should clarify and make publicly known, the roles and responsibilities of board of directors, and the managementis to provide stakeholders with a level of accountability. They should also implement procedures to independently verify and safeguard the integrity of the company's financial reporting. Disclosure of material matters concerning the organization should be timely and balanced to ensure that all investors have access to clear and factual information.[94]

2.4 The Importance of Corporate Governance

The heightened awareness of the need for effective corporate governance is not without justification. A well implemented corporate governance regime has tremendous benefits. These benefits are the endearing attributes of corporate governance. In the first place, effective corporate governance, backed up with adequate monitoring and enforcement, would build investors' confidence, eliminate financial scandals, and curb corporate failure. It was in view of the above that the Federal Government recently inaugurated Steering Committee that will develop the country's code of corporate governance.[95]

Management of the affairs of the company is vested on the organs of the company - the board of directors and the members in the general meeting. While the general meeting is the supreme legislative authority of the company, the directors are, subject to the articles, vested

[93]Report of the Committee, led by A. Cadbury, on the Financial Aspects of Corporate Governance, published in Gee, London, 1992, sections 3.2,3.3,4.33,4.51 and 7.4.
[94] OECD Principles of Corporate Governance, 2004, Articles I and v.
[95]N.O. Ofor, *op.cit*, p.17.

with the power of managing the company on behalf of the shareholders. Gower[96] noted that both the General Meeting and the Board are organs rather than agents of the company, and both the General Meeting and the Board may be the company: the former when acting under the reserved powers, and the latter when acting under an express power and general delegation.[97]

The concept of corporate governance therefore is basically about how the affairs of companies and other corporate institutions are conducted by those charged with the responsibility of overall management and control.[98] According to the UK Cadbury Report,corporate governance is how a company is directed and controlled. It seeks to maintain the beneficial relationship between the company and the shareholders, other stakeholders and the society at large. Thus, it aligns the interests of the members of the corporation. It seeks to promote the fairness and transparency in disclosing financial detail status of a company, employ appropriate risk management measures, and promote information flow and the responsibility of senior management and the board of directors.

Notably, it is the socio-economic nexus between managed behavior and company administration (or maladministration) that has brought out the subject - corporate governance. Thus, corporate governance comes with lots of benefits to companies. Other benefits include:

i. Good governance helps firms to have favourable access to capital markets[99] (which is a mediator of funds, from surplus to deficit sectors of the economy) so as to enable it

[96]P. Davis and S. Washington, Gower and Davies: *Principles ofModern Company Law*, (London: Sweet and Maxwell Publishers), p. 132.
[97] CAMA, Cap. C20, LFN, 2004, section 63(5).
[98] R. Okpeahior and H.P. Faga, *op.cit*.
[99] I.D. Nworji, *et al*, 'Corporate Governance and Bank Failure in Nigeria: Issues, Challenges and Opportunities', *Research Journal of Finance and Accounting*, Vol. 2, No. 2, 2011.

pool monies from a large number of people and institutions especially in meeting their funding requirements, which is usually colossal.[100]

ii. Better governance restricts controlling shareholders'expropriation of minority shareholders. Thus, where there is no protection of minority shareholders, some investments would be lost and lack of governance would lead to more marginalization of these group of shareholders. This loss of private benefits is more in countries with low investor protection.

iii. Corporate governance is an important concept that relates to the way and manner in which financial resources available to an organization are judiciously used to achieve the overall corporate objective of an organization. It keeps the organization in business and creates a greater prospect for future opportunities.

iv. Corporate failures have come about as a result of bad corporate decisions made by its leaders in attempts to expropriate rents. Thus, the enactment of good corporate governance policies across the globe justifies the importance of this subject matter.

v. Also, effective corporate governance reduces 'control rights' shareholder and creditors confer on managers, thus increasing the probability that managers invest in positive and not just mere present value projects.[101]

vi. Corporate governance in companies helps to reduce the apparent issues arising from the principal-agent relationship.[102]Here, when the agent imbibes the corporate governance principle of integrity and accountability, he would act in a more responsible manner towards the principal.

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[100] S.O.E. Ewah, 'Appraisal of Capital Market Efficiency on Economic Growth in Nigeria', *International Journal of Business Management*, Vol. 4, No. 12, 2009, pp. 219-228.
[101] A. Shleifer and R. Vishny ,'Large Shareholder and Corporate Control', *Journal of Financial Economics*, Vol. 58 (1-2), pp. 3-27, 1996.
[102] L. Bebehuck and Jesse Fried, *Pay Without Performance: the Unfulfilled Promise of Executive Compensation*. (New York: Harvard University Press, 2004), pp. 15-17.

Therefore, the benefits of corporate governance on the economic and financial fronts are overwhelming. There is thus the need to adopt the basic principles of corporate governance to ensure a smooth course in the growth of our economy and the development of our society in general.

2.5 Parties to Corporate Governance

Many companies are managed by directors who have no shares in the company. Many problems have arisen due to the fact that shareholders are separatedfrom management. Due to the many problems which have arisen, one of which is the agency problem, corporate governance has been developed. The company is a separate legal person distinct from the shareholders who constitute the membership of the company.[103]the company delegate control to professional managers i.e. the Board of Directors, to run the company on their behalf. Shareholders normally play a passive role in the day-to-day management of the company.

Companies are basically directed and controlled by the board of directors and the members in general meeting as its organs. However, the affairs of the company are influenced by both internal and external considerations. Good governance requires the following to be considered.

Internal Factors

i. The nature and structure of those who set direction i.e. the board of directors.
ii. The need to monitor major forces through risk analysis
iii. The need to control operations: internal control

[103]CAMA, Cap. C20, LFN, 2004, section 37; *Salomon v Salomon and Co* (1877) AC 22.

External Factors

i. The need to be knowledgeable about the regulatory framework that defines codes of best practice, compliance and legal statute.

ii. The wider view of corporate position in the world through social responsibility and ethical decision.

There are basically two parties to corporate governance:

a. Internal corporate governance stakeholders

b. External corporate governance stakeholders.

Internal corporate governance stakeholders are internal parties involved in corporate governance. Suffice it to state that internal stakeholder is any person or group of persons that can affect or be affected directly by the policies or activities of an organization and its achievement thereto.[104]

Such stakeholders include board of directors, management and shareholders. Each internal stakeholder has:

a. An operational role within the company

b. A role in the corporate governance of the company

c. A number of interests or claims in the company

External corporate governance

On the other hand external corporate governance stakeholders are external parties involved in corporate governance. External stakeholder is therefore any person or group of persons that are indirectly affected by the policies and activities of a company. They include, customers, the government, and the community where the company operate.

[104] R.E. Freeman, 'Strategic Management: A Stakeholder Approach (Boston M.A.: Pitman, 1984).

2.6 Control Mechanisms

Corporate governance mechanisms and controls are designed to reduce the inefficiencies that arise from moral hazard[105]and adverse selection.[106] There are both internal monitoring systems and external monitoring systems. Internal monitoring can be done, for example, by one (or a few) large shareholder (s) in the case of privatelyheld companies or a firm belonging to a business group. The various broad mechanisms provide for internal monitoring. External monitoring of managers'behavior occurs when an independent third party (e.g. the external auditor) attests the accuracy of information provided by management to investors. Stock analysts and debt holders may also conduct such external monitoring. An ideal monitoring and control system should regulate both motivation and ability, while providing incentive alignment toward corporate goals and objectives. Care should be taken that incentives are not so strong that some individuals are tempted to cross lines of ethical behaviour, for example by manipulating revenue and profit figures to drive the share price of the company up.[107]

2.6.1Internal Corporate Governance Controls

Internal controls in accounting and auditing is defined as a process affected by an organization's structure, work and authority flows, people and management information systems, designed to help the organization accomplish specific goals or objectives.[108]It is a means by which organization resources are directed, monitored and measured. It plays an important role in defecting and preventing fraud, and protecting the organization's resources,

[105] A moral hazard is a tendency to be more willing to take a risk, knowing that the potential costs or burdens of taking such risk will be borne, in whole or in part by others.
[106] Adverse selection refers to a market process in which undesired results occur when buyers and sellers have symmetric information (access to different information): the bad products or services are more likely to be selected.
[107] D: Sytle& S. Hein, 'Economic Approaches to Organizations,' 5th edition, Chapter 15, London, 2013, Pearson (3).
[108] D. Sytle& Hein, 'Economic Approaches to Organizations, 5th edition, London, Pearson (1).

both physical (e.g. machinery and property) and intangible resources (e.g. reputation or intellectual property such as trademarks).

At the organizational level, internal control objectives relate to the reliability of financial reporting, timely feedback on the achievement of operational or strategic goals, and compliance with laws and regulations. At the specific transaction level, internal control refers tothe actions taken to achieve a specific objective (e.g. how to ensure that the organization'spayments to third parties are for valid services rendered. Internal controlprocedures reduce process variation, leading to more predictable outcomes.[109]

Internal corporate governance controls monitor activities and take corrective action to accomplish organizational goals. Examples include:

i. **Monitoring by the Board of Directors:**The board of directors, withits legal authority to hire, fire and compensate top management, safeguards invested capital. Regular board meetings allow potential problems to be identified, discussed and avoided. Bhagad and Black argue that non-executive directors are expected to be more independent than executive directors. This alone does not always result in more effective corporate governance and neither does thatenhance corporate performance.[110] The Different board structures are optimal for different firms. Moreover, the ability of the board to monitor the firm's executives is a function of its access to information. Executive directors possess superior knowledge of the decision-making process and therefore evaluate top management on the basis of the quality of its decisions that lead to financial performance outcomes, *ex ante*. It could be argued therefore, that executive directors look beyond the financial criteria.

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[109] The Committee of Sponsoring Organization of the Tresdway Commission (COSO) definition of internal control.

[110]Bhagat& Black, 'The Uncertain Relationship between Board Composition and Firm Performance', *Business Lawyer*, 54.

ii. **Internal Control Procedures and Internal Auditors:**Internal control procedures are policies implemented by an entity'sboard of directors, audit committee, management and other personnel to provide reasonable assurance of the entity achieving its objectives related to reliable financial reporting, operating efficiency, and compliance with laws and regulations. Internal auditors are personnel within an organization who test the design and implementation of the entity's internal control procedures and the reliability of its financial reporting.

iii. **Balance of Power:** The simplest balance of power is very common; it requires that the president be a different person from the treasurer. This is about separation of power which is developed in companies where separate divisions check and balance each other's actions. Thus, one group may propose company-wise administrative changes; another may review and can veto the changes, and a third group check that the interests of people such as the customers, shareholder, employees, etc outside the three groups are being met.

iv. **Remuneration:**Performance-based remuneration is designed to relate some proportion of salary to individual performance. It may be in the form of cash or non-cash payment such as shares and share options, superannuation or other benefits. Such incentive schemes, however, are reliable in the sense that they provide no one mechanism for preventing mistakes or opportunistic behavior, and can elicit myopic behavior.

v. **Monitoring by Large Shareholders and/or Monitoring by Banks and Other Large Creditors:** Given their large investment in the firm, these stakeholders have the

incentive, combined with the right degree of control and power, to monitor the management.[111]

2.6.2. External Corporate Governance Controls

External stakeholders play an important role in ensuring proper corporate governance processes in a business organization. Some of the key external corporate governance controls include:

i. **Government Regulations:** Government regulations are the most effective external controls on the governance of a company. Companies are required to comply with these or face penalties for violations. More so, most corporate governance regulatory requirements are based on the OECD principles of Corporate Governance.

ii. **Media Pressure/Exposure:** Media scrutiny of the workings and processes of a company ensures, to a certain degree the proper governance in an organization. Here, whistleblowers often expose wrong doing within a company to the government and media organizations.

iii. **Market Competition:** Companies withthe best corporate governance practices have the best standing in the market. Reputation, credibility and positive public perception all play a vital role in boosting a company's image and thus help it trump its competition and best among its peers.

iv. **Takeover Activities:** Takeover activities lay a company's internal processes and working open to public scrutiny. Both government regulators and the media will focus on the internal policies and governance structures, thus acting as an effective external control.

[111]M. Goergen, *International Corporate Governance*, First Edition, (Prentice Hall,Harlow, U.K.: Pearson, 2012), pp.104-105.

v. **Public Release and Assessment of Financial Statements:**The public release of financial statements by listed companies exposes them open to assessment or scrutiny by regulators, investors, members of the public and so on. This acts as an external control as companies have to be scrupulous and careful about the details included in these statements and in ensuring that they are properly prepared and audited.

2.7Systemic Problems of Corporate Governance

The dearth of enforcement ofa set of regulatory, market, stakeholder and internal governancehas largely contributed to the on-going financial crisis. Some of the problems of corporate governance include:

i. **Demand for Information:**In order to influence the directors, the shareholders must combine with others to form a voting group which can pose a real threat of carrying out resolutions or appointing directors at a general meeting.[112]

ii. **Monitoring Costs:**A banner to shareholders using good information is the cost of processing it, especially to a small shareholder. The traditional answer to this problem is the efficient market hypothesis in finance.The efficient market hypothesis (EMH) asserts that financial markets are efficient, which suggests that the small shareholder will free ride on the judgments of largerprofessional investors.[113]

iii. **Supply of Accounting Information:**Financial accounts form a crucial link in enabling providers of finance to monitor directors. Imperfections in the financial reporting process will cause imperfections in the effectiveness of corporate governance. This should ideally be corrected by the working of the external auditing process and by means of standard accounting measures and best practices.[114]

2.8 Corporate Governance Models around the World

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[112]Current Trends in Management, 6.9.
[113]*Ibid.*
[114]*Ibid.*

The Cadbury Report which was published in May 1992 has defined 'Corporate governance' as the system by which companies are directed and controlled. It is concerned with the way corporate entities are governed, as distinct from the way business with those companies are managed.[115]

Corporate governance varies according to the particular situation of the company. Different models of corporate governance have grown around the world, for instance, Anglo-Saxon markets model represented by the United States (US), United Kingdom (UK) and Australia. This model also called 'Anglo-American Model or 'the UK-US Model or 'the Outsider Based Model" or 'Ownership Model' tends to emphasize the interest of shareholders. Secondly, there is 'coordinated or multi-stakeholders model' associated with Continental Europe and Japan. Some authors[116] refer to it as 'Contracts Model'. This model recognizes the interest of workers, managers, suppliers, customers and the community.[117]

There are other classifications according to the variety of capitalism in which they are embedded, thus, 'Emerging Markets Models represented by India, Malaysia and Thailand. 'Intermediate markets' (somewhere in between Emerging market and the Anglo Saxon model represented by South Africa, Mexico and Hong Kong.[118]

The approach to the following issues determines the model under which a country is classified:

i. How is the shareholders empowered to ensure accountability, transparency, probity and control of the management? Does the company structure and laws favour the shareholders as the owners of the company with their interests being the ultimate, or

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[115]A. Blake & H.J. Bond, *Company Law*, 5th ed., (London: Blackstone Press Limited, 1996) p. 258.
[116]J.E. Parkinson, *Corporate Power And Responsibility: Issues in the Company Law*, (New York: Oxford University Press Inc. 1993) p. 177
[117]Corporate Governance-Wikipedia available at en.wikipedia available aten.wikipedia.org/wiki/corporate.goo. (Accessed on 10/112013)
[118] F. Ajaogwu, *Corporate Governance in Nigeria: Law and Practice* (Lagos: Centre for Commercial Law Development (CCLD) (2007) pp. 27-29

does the company's structure and laws within a jurisdictions see shareholders as just parties to a corporate contract, and whose interests are not better than that of employees, creditors and the community; with the management regarded as being in better position to determine the ultimate goal(s) of the company?

In line with the above, the questions are:

ii. What should be the actual size of the board of publicly quoted company and the role and responsibilities of the Executive and the Non-Executive Directors? Should the board be two-tier or single tier and should the board be over populated by the management or the non executives?

iii. Should the same person chair the Board and at the same time act as its Chief Executive Officer or should the two posts be a director?

iv. What is the nature of the power of shareholders to appoint or replace a director?

v. How or the extent of the power of shareholders, including the institutional investors in taking major decisions in the company?

vi. How is the minority shareholders class protected?

The approval or method adopted by any given jurisdiction in answering the above questions or issues determines its model.

It is essential to note that some decade ago; it was widely thought that corporate governance practices around the world would gradually converge on the United States model. After the US Securities and Exchange Commission had existed since 1934, sound corporate regulation and reporting system had evolved, and American governance practices were being propagated globally by institutional investors. But that was before the collapse of Enron, Author Anderson, the Sub-Prime Financial Catastrophe and ongoing global economic crises. Also it was believed that the world converge with US practices because the world needed

access to American capital. This is no longer the case. The legal differences in company law, contract law and bankruptcy law between jurisdictions affect corporate governance practices and hence different models. Also, differences between the case law traditions of US, UK commonwealth countries and the codified law of continental Europe, Japan, Latin America and China distinguish corporate governance outcomes.[119]

It suffices to say at this juncture that none of the models developed so far command or tend to assume a universal norm for other jurisdictions. Around the world, despite its increasing popularity, Anglo-Saxon model is far from the norm. A truly global model of corporate governance would need to recognize the following alternatives:[120]

i. The network of influence in the Japanese Keiretsu.
ii. The governance of state-owned enterprise in China, where the China Securities and Regulatory Commission (CSRC) and the State-owned Assets Supervision and Administration Commission (SASAC) can override economic objectives acting in the interests of the people, the party and the state to influence strategies, determine prices and appoint chief executives.
iii. The partnership between labour and capital in company's co-determination rules.
iv. The financially leveraged chains of corporate ownership in Italy, Hong Kong and elsewhere.
v. The domination of spheres of listed companies in Sweden, through successive generations of a family, preserved in power by dual-class shares.
vi. The paternalistic familiar leadership in companies created throughout South-East Asia by successive Diaspora from main land China.
vii. The governance power of dominant families in the South Korean Cha-ebol, and

[119] *Ibid.*
[120] Seegenerally:GovernanceModel/CorporateGovernance,available at www.corporategovernanceoup.word.press.com, accessed on 10/11/2013.

viii. The need to overcome the paralysis of corruption from shop floor, through board room, to government officials.

Notwithstanding the variations, two models have stood out. They are Anglo-Saxon Model (Shareholder Based, Outside Based or Ownership Model) and insider model (or contracts model).

2.8.1 Shareholder Based Model

Two core features of the corporate form underlie this model of corporate governance. The first is investor ownership which implies that shareholders, as residual claimants, have significant rights of control over their companies. These rights include, the right to alter the memorandum and articles of associations of their companies, the right to authorize an increase or reduction in its capital and the purchase or redemption of the company's shares, the right to call for the winding up of company and the right to sanction the payment of dividends (depending on the article of association).[121]

The second is delegated management, which implies that shareholders generally exercise this control indirectly, by participating in the selection or removal of directors or their closest equivalents in closed corporations.[122] Shareholders also have a role in confirming transactions in which the directors have a conflicting interest.[123] In all, the major characteristics of outside based model include dispersed shareholder ownership and liquid capital market where ownership and control are traded frequently.

Thus, this shareholder based model depicts that the business of the company is conducted by the directors to maximize profit for shareholders, and that this principle is central to the

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[121]J.E. Pakinson, *op. cit*, p. 163.
[122]R.R. Kraakman*et., al*; *The Anatomy of Corporate Law: A Comparative and Functional Approach*, (Oxford: Oxford University Press, 2004) p. 33.
[123] J.E. Pakinson, *op. cit*., p. 163; Companies and Allied Matters Act, Cap. C20, LFN, 2004, s. 280.

viability of the corporate firm. The shareholders are however, only beneficiaries of the profit made by the company but the actual control of the company lies with the board of directors.[124]The idea of fraud and mismanagement is premised on the failure of the shareholders to perform this control function.[125]

Supporters of this Outsider Based model argue that corporate performance could be improved by expanding the range of issues for which shareholders consent is required, thereby limiting the ability of management to pursue non-profiting maximizing goals or self seeking transactions. They maintain that a procedural approach of this kind would certainly have greater potential than control by judicial review.[126] Here, shareholders appoint a board of directors who then appoint and monitor managers, and at the same time, managers operate the care function of the corporation and report back to the board of directors, who represent the shareholders.[127]

Arising from the above is the fact that the Anglo-Saxon model operates under one tier board. The one tier board is often composed of executive directors and non-executive directors with the number of the board members varying according to the regulation of the countries.[128]

Moreover, in this model, apart from the control of shareholders through appointment and decision making rights, external market forces such as comparative factors in product market, capital market, and corporate control market act as further monitoring mechanisms for management. Competitive factors in the product market play an important monitoring role as the company's performance vis-à-vis its competitors illustrate whether managers are component and hardworking in their jobs.

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[124]CAMA, Cap. C20, LFN, 2004, sections 63.
[125] J.E. Parkinson, *op. cit,* p. 177.
[126]*Ibid,* p. 163.
[127]CAMA, Cap. C20, LFN, 2004, sections 37 and 64.
[128] Review of Corporate Governance Models and its Implication on China available at: www.business.otago.ac.nc.nz/mgmt/, accessed on 10/11/2013.

In a narrower sense, traditional legal understanding of corporate governance considered the company as a legal instrument whereby shareholders are able to maximize their wealth. This is what is called shareholders focused model of corporate governance or better still 'shareholders value' model of corporate governance. Shareholder value is thus measured according to increasing returns on capital employed and rising share prices, adopted as an index of management success. According to Froud, this entails the financialisation of management goals and the logic of public market valuation of management performance.[129] In the words of H Gospel and A Pendleton:

> The focus on shareholder value reinforces the controlling rights of shareholders in the corporation and the focus of regulatory invention is on the three-tiered hierarchical relationship between shareholders, the board of directors and seniors managers.[130]

Advocates of shareholders primacy introduce corporate governance as the delegation of corporate control to directors and managers to run a company on behalf of all shareholders. This raises a key issue that a set of regulatory or institutional arrangements can ensure that shareholders' interest are adequately protected and managers are rendered accountable; regard being had to the fact that shareholders focused model of governance permits management to become a self-selecting oligarchy in effective control of most corporations, thus giving them ample scope for opportunism, shirking or self dealing.[131]

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[129]J. Froud, 'Shareholders Value and Financialisation: Consultancy Promises, Management Moves Economy and Society', 2000, p 29.

[130] Richard M. *et al*, 'Shareholder Value and Employee Interest: Intersections between Corporate Governance, Corporate Law and Labour Law', *op cit,* p.8.

[131] A. Berle and G. Means, 'The Modern Corporation and Private Property', (New York: Macmillan, 1932).

Manne[132] was one of the earliest respondents to this growing concern. According to him, the shareholders focused model of corporate governance calls for no concern at all; in that shareholders readiness to exit corporation underpinned the liquidity necessary for a functioning market in corporate control. In other words, the dispersed, uncommitted nature of shareholders was a virtue rather than a vice. After all, managers were not as unaccountable as they seemed, but were in fact subject to quite strong market disciplines – or, ideally were subject to such disciplines provided managerialists did not have their way in promoting a radically altered form of economy in which the ideal of the market as a resource allocator was abandoned.

The shareholders model reinstates the maximization of shareholder value as the appropriate goal of management, and this is prompted by demands of efficiency in the running of the enterprise. Managers should thus be running the company to maximize shareholder wealth. Since the shareholders' focused model of governance (focusing on profit and wealth maximization for shareholders) is consistent with the key features of the American practice, we shall use the U.S. model to further illustrate our position here. In line with this, we submit that what drives the U.S. corporate governance 'model' sometimes referred to as Aglo-American' governance model, since many elements are similar in U.K. and U.S., are as follows:[133]

i. The separation of ownership from business control; the rise of equity financing via New York and London Stock Exchanges in 20th century (and the attendant global importance of these markets) led to development of corporate governance principles focused on shareholders' rights. Exchange related regulation brought greater transparency and disclosure obligations for corporate issuers.

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[132] H. Manne, "The 'Higher' Criticism of the Modern Corporation", *Columbia Law Review*, Vol. 62 (1962) p. 399.
[133] L. A. Burnhill, 'Overview: The U.S. Governance Model', being CFI Governance Working Group Presentation, January 30, 2013 pp. 1-13.

ii. At inception, corporate governance principles and market requirements focused on individual investors. In recent decades, institutional investors have become more prevalent, which has influenced the evolution of governance practices. In UK, 62% of shares were owned by institutions in 1981, rising to 86% in 2004. Also in US, institutions owned 34% of shares in 1980, rising to 77% in 2006.

However, the shareholder focused model of governance in contrast to stakeholders' governance model spares little thought for the role of the company in modern society and thereby placed little emphasis on the social or environmental impact of corporate decisions.

As we have noted, in the U.S., U.K., shareholders model of governance is concerned with ensuring that the firm is run in the interests of shareholders and its objective is to create wealth for them. Underlining this view is Adam Smith's notion of the invisible hand of the market as laid out in his seminal book[134] and which proclaims that if firms maximize the wealth of their shareholders and individuals pursue their own interests, then the allocation of resources is efficient in the sense that nobody can be better off without making somebody else worse off. In Nigeria, firms are run to promote the business or object for which the company is formed. This presupposes that managers have a fiduciary duty to act in the interests of the company.[135] This system can lead to an efficient allocation of resources provided, among other things, that market and institutions are well developed and competitive.[136] This underscores the fact that provided stock prices contain enough information about the anticipated future profitability of the firm; fairly, effective, automatic and incentive systems to ensure managers maximize shareholders wealth can in theory be designed. More broadly, some industrial relations scholars have observed a coincidence

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[134] A. Smith, *An Inquiry into the Nature and Causes of Wealth of Nations*, (Dublin: Whiteston, 1776).
[135]CAMA, Cap. C20, LFN, 2004, section 279, .
[136] A. Franklin and Z. Mengxin, *The Corporate Governance of Japan: Shareholders are not Rulers*, (University of Pennsylvania and Bentley College, 2007) p. 12.

between the growing dominance of the corporate law system intent on delivering 'share value' and more fragmented labour market, especially as regards job security, work intensification and investment in training and skills.[137]

Much as the shareholder focused model of governance appears very enticing, it is not devoid of weaknesses. On the other hand, we argue that couplet problem generated by the shareholder model, particularly in its modern variant known as 'agency theory' means that directors in the joint stock company could not be expected to be as vigilant and careful with other people's money as with their own.[138] There is therefore the risk that managers and directors will look after their own interests at the expense of shareholders.[139] On the other hand, we also argue that the shareholders focused model confers enormous powers on the CEOs (equivalent to managing directors in Nigeria). By this, it is meant that where the company's CEO serves as Board Chairman, a great deal of power is vested in that individual. The excessive levels and growth rates of CEO pay are viewed as highly correlated to this phenomenon. Similarly, there is also the risk of sudden loss of independence. By this, it is meant that although notionally, the presence of independent (non-executive) directors serves as a control on management ambition, in practice, they are subject to the influence of the CEO/Chairman and the knowledge that their actions are transparent vis-à-vis executive directors. It is seemingly very hard a decision to vote against an increase in executive compensation when the potential beneficiaries of that vote will continue to sit next to you at Board meeting.[140]

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[137] H. Benneth and B. Barry *The Great U-Turn: Corporate Restructuring and the Polarizing of America*, (New York: Basic Books Books, 1990).

[138] A. Smith, 'The Wealth of Nations, Book V, Chapter 1, Part 3, 1776.

[139] Advocates of shareholder value may debate the exact metric to use in evaluating performance, and various consultancy firms and their principals have developed proprietary concepts to measure management performance, such as 'Economic Value Added' and 'Market Value Added', (Stern Stewart); 'Shareholder Value Added' (LEK/Alcar Consulting group); 'Total Shareholder Return' (Boston Consulting group); 'Economic Profit' (Mckinsey) and so on.

[140] Advocates of the shareholder focused model may again debate that Board functions permit the separation of decision management from decision control. In other words, management frames the strategy debate, but

Thus, the new realities of corporate governance show that no entity or agents is immune from fraudulent practices[141] and have altered the way companies operate; they have re-defined the baseline for what is considered prudent conduct for business and executives.[142] In the face of corporate scandals arising from fraudulent accounting and other illegal practices such as companies exhibition of corporate governance risks predicated on conflicts of interest, inexperienced directors, overly lucrative compensation and unequal share voting rights, there has been a renewed emphasis on corporate governance.

In essence, corporate governance covers a large number of distinct concepts and phenomenon. This can be from the definition given by Organization for Economic Cooperation and Development (OECD) thus:

> Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, manager, shareholders and other stakeholders and spells out the rules and procedures for making decisions in corporate affairs. By doing this, it also provides the structure through which the company objectives are set and the means of attaining those objectives and monitoring performance[143]

The above expatiation of the nuances of corporate governance presupposed that corporate governance includes the relationship of a company to its shareholders and to society; the

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Board's approval is needed to finalize strategic decisions. Again, both executive and non-executive directors participate in setting strategy and managing risk, theoretically ensuring a balance between knowledge of the company's strengths, weaknesses and competitors with broader insight on the economy and operating environment overall. Further still, significant disclosure requirements provide transparency with regard to corporate operations and performance.

[141] For example Marshall Cogan (The founder, controlling shareholder, CEO and chairman of the board of directors of Trace Holdings International) over a period of 15 years, took 40 million U.S dollars from the company through a number of self dealing transactions while the officers and directors stood by idly. In an action brought against Cogan and the Trace officers and directors by the trustee, the court held for the trustee, citing the directors utter failure to exercise their legal duties to act on behalf of Trace's shareholders and creditors, and went so far as to impose liability on Trace officers who were part of the board, but who had the authority to preempt Cogan's misappropriations. This was cited in P. Dandino, 'Corporate Governance: Something for Everyone', *Franchising World*, 36 (1), 2004 p. 41.

[142] P. Dandino, 'Corporate Governance: Something for Everyone, *op cit*.

[143] OECD April, 1999 Available at http://www.encycogov.com what is CorpGov.asp visited August 18, 2013 at about 8: 44pm

promotion of fairness, transparency and accountability, reference to mechanisms that are used to govern manager and to ensure that the actions taken are consistent with the interests of key shareholders. The mechanisms referred to above as has been noted already, is twofold to wit: legal compliance mechanism and ethical compliance mechanism. The duo is hereunder discussed:

2.8.2 Insider Based Model (Contracts Model)

This model redefines the company as 'the nexus of set of contracting relationships among individuals. According to Dallas,[144]company is 'a market place where various constituencies contract for their own protection.' Therefore, the company, as an entity capable of being owned, thus disappeared from the picture as it is merely a device to facilitate contract between individuals.[145]

In this line of thought, the shareholders rather than being the company's owners are classified as one of the parties[146] who entered into contracts through the medium of the company in order to coordinate and enhance production for their mutual benefit.

Fama,[147] put it this way:

> We are cautioned that ownership of capital should not be confused with the ownership of the firm. Each factor [of production] in the firm is owned by somebody. The firm is just the set of contracts covering the way inputs are joined to create outputs and the way receipts from outputs are shared among inputs.

The traditional view that a firm is owned by its shareholders having been dispelled, it becomes clear that there is no strong reason why the shareholder should exercise control over company decision making. The shareholders to that extent are 'rationally ignorant' of

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[144] L.L. Dallas, 'Two Models of Corporate Governance: Beyond Berle and Means', cited in J.E. Pakinson*op. cit*, p.178.
[145] J.E. Pakinson, *op. cit* p. 178.
[146] Others include management, employees, suppliers and customers.
[147]E.F. Fana, 'Agency Problems and the Theory of the Firm', cited in D.E. Parkinson, *op. cit*, p. 178.

managerial practices and as such, control and major policy decisions should be left to the management to decide.

According to Anglo-Saxon or ownership model, weak ownership control leaves managers with discretion to pursue non profit goals and otherwise to act in ways that are at variance with the shareholders interests. So, the theory of management power assumes a breakdown of ownership model.[148]

However, supporters of contract model reject the above analytical framework and its accompanying policy agenda. They argue that overbearing of shareholders in major business decisions can be counterproductive, maintaining that corporate efficiency could be increased by expanding the range of issues over which the management has final say. This is the philosophy that informed Insider Based Model. Insider Based Model is effectively practised in Germany and Japan. It makes use of two tier board with employees represented on the board.[149] The two tier board is composed of the management board and the supervisory board. In this system, the management board is appointed by the supervisory board rather than by shareholders as in the case of UK and the US.[150]

Additionally, the management board runs the company and its powers and duties are derived in the main from the statute.[151] The supervisory board as the main monitoring body has a more complex composition. The supervisory directors are usually appointed by the company.[152]

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[148] J.E. Parkison, *op. cit*, p. 177.
[149] Review of Corporate Governance Model and its Implication on China, available at: www.business.otago.ac.nc.nz/mgmt/ANZAM, accessed on 24/05/2014.
[150]*Ibid*., See also J.E Parkison, *op. cit*, p. 192, where it was noted that under the two tier system, the executive directors are appointed by the supervisory directors, or where the company's constitution permits by the members directly.
[151] This is unlike where the company has a single tier board in which the precise division of responsibilities between the two types of directors is a matter to be determined by the board itself.
[152] See Review of Corporate Governance Models and its implication on China, *op. cit*.

Kraakman[153]notedthat major jurisdictions permit a two tier board structure for open companies (public companies) and the two boards are organized vertically rather than horizontally, with an elected supervisory board that, in turn, appoint a managing board whose members are the principal managers of the firm. Thus the two boards are in a semi-hierarchical relationship. But this does not mean that the management board is powerless in two board jurisdictions.

Accordingly, this two tier board structure is entirely consistent with allegiance to shareholder interests. Indeed, it might seem that a two tier board, should be more responsive to shareholder interests than a single tier board, (practised in Anglo-Saxon jurisdiction), since the shareholder directors of the supervisory board are required to be independent, non-executive directors in most two tier jurisdictions.[154]

Those jurisdictions such as Germany and Netherlands, that require a two tier board also bar managers and other corporate employees from serving on the upper board. In France, where the two tier board is optional, up to one third of the members of the supervisory board may be employees and hence executive but not managing directors. The value of this independence is suggested by the trend in single-tier jurisdictions, including the US, towards assigning non-executive directors to decide issues that might implicate executive directors in a conflict of interest.[155]

2.9 Comparing Legal Compliance Mechanism with Ethical Compliance Mechanism

Despite certain congruities and convergences, there are some very important differences in the character and content of ethical and legal requirements which can help us understand why ethics is accorded a normative primacy in practical affairs and legality is to be judged by

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[153] R.R. Kraakman, *op. cit*, p.35.
[154]*Ibid.*
[155]*Ibid.*

reference to ethics (not vice versa).[156]In specific terms, law is concerned primarily with conduct and ethical requirements are centrally concerned with reasons, motives and intentions, and more generally with the character that expresses itself in conduct.[157] Also, law is jurisdictionally limited since what is legitimately required in one state or country may differ from another, whereas ethical values are inclined to be more universal. This agrees with Kidder's definition of ethics as 'obedience to the unenforceable'.[158]

Longstaff has argued that an overemphasis on legal compliance mechanism could be at the expense of ethical reflection since people may have less reason to form their own opinions and take personal responsibility for the decisions they make.[159] This could result in a suitable substitution of 'accountability' for 'responsibility'.[160]

Perhaps, the current business environment provides an excellent opportunity to establish an organizational culture that goes beyond mere legal compliance.[161]Harshbarger and Holden[162] believe that as the new realities of corporate governance sets in, the substance of the new laws and rules must be lost in the race to comply with their form. They stressed that organizations must make a good faith effort to comply not just with the letter of the law, but with the spirit of the new reform that recognized at least three primary benefits: (i) provides

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[156] J. Kleining, *The Ethics of Policing*, (United Kingdom: Cambridge University Press, 1999).
[157] S. Arjoon, *op cit*, p. 11.
[158] R. Kidder, *How Good People Make Tough Choices: Resolving the Dilemmas of Ethical Living* (New York: Fireside, 1995).
[159] S. Longstaff, 'The Ethical Dimension of Corporate Governance' (1986), available at: http://www.ethics.org, visited on 18/08/ 2013.
[160] S. Longstaff, A Recent Study by a World Bank Team in The Economist, 2004, p. 16 revealed that the poorest countries have the most rules which make returns from entrepreneurial risk taking unattractive and provides an avenue for corruption.
[161] A speech given by Commissioner Cynthia Glassman on Sarbanes-Oxley's lesson for Broke Dealers, October 17, 2003, captures this aspect - 'As we move past Sarbanes-Oxley and the requirements, rules and regulations that have come in its wake, it's essential that corporate boards look beyond the letter of the law and be ever mindful of the spirit of the reforms. By determining what makes up the moral DNA of the company and establishing a culture that puts ethics and accountability first, a company and its Board are less likely to fall into the common trap of mere compliance – where simply identifying a new line of legally acceptable behavior and how to maneuver the loopholes that accompany it passes for a commitment to reform', cited from S. Arjoon, *op. cit*., Footnote 7.
[162] S. Harshbarger and T. Holden, 'The New Realities of Corporate, Governance', *Ethics Matters*, (Bentley College, MA: *Centre for Business Ethics*, February, 2004).

organizations with a stronger measure of inexpensive insurance mechanism and is a strong mitigating factor in any action imposed, (ii) more accurate information flows to the top enabling more efficient and effective business decisions, and (iii) the imprecise reforms offer business leaders the opportunity to emerge with more well defined standards (leaders should be embracing this period of reform as an opportunity to institutionalize their system). This represents the new emerging practice in the U.S.A. In essence, legal compliance mechanism tends to promote a 'freedom of indifference' which corresponds to the letter of the law which may not necessarily inspire, or instill excellence, whereas, ethical compliance mechanisms promote a 'freedom for excellence' which corresponds to the spirit of the law. It is therefore submitted that though legal compliance mechanism and ethical compliance mechanism are mutually complementary in exerting good corporate governance regime, the latter is more rewarding. This is why companies can maintain and deliver financial statements which meet the standard and requirements of the law, yet, leaving out falsehood in the accounts of the company at the instance and smart deals of the directors. In a short moment, this scenario presents the company as a viable and stable going concern only to have the company collapse upon careful auditing. With legal compliance, a company can remain afloat though rotten or bankrupt. But with ethical compliance, a company truly has its documents reflect the real state of affairs, and the directors and managers are genuinely committed to business. This concept of freedom explain why legal compliance mechanisms are insufficient and may not be addressing the real and fundamental issues that inspire ethical behaviour.

In a related development, Paine[163] identified an organizational integrity-based stratagem that is more comprehensive and broader than the legal compliance strategy to encourage and support an ethical corporate culture. Four challenges which must be met before an organizational integrity approach can work have at least been identified and include:

i. Developing an ethical framework
ii. Aligning practice with principles
iii. Overcoming cynicism and
iv. Resolving ethical conflicts

Paine[164] also suggested that a useful starting point is to begin by answering some questions to the four fundamental sources of responsibility to wit:

i. What is the organization's fundamental reason for being its ultimate aim (purpose)
ii. Who are the constituencies to whom the company is accountable and on whom it depends for success? What are their legitimate claims and interests (people)
iii. What is the organization's authority and ability to act (power)?, and
iv. What are the organization's obligations or duties, as well as its guiding aspirations and ideals (principle)?

In essence, it is posited that effective corporate governance can be achieved by adopting a set of principles and best practices. A great deal depends upon fairness, honesty, integrity and the manner in which companies conduct their affairs. Whilst companies must strive to make profit in order to grow and survive, however, the pursuit of profits must not go beyond ethical bounds. Ethical compliance mechanisms contribute to stability and growth since it instills confidence; management, leadership, and administration are essentially ethical tasks.

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[163] L. Paine, 'Venturing Beyond Compliance', *The Evolving Role of Ethics in Business*, Report no. 1141 – 96 (New York: The Conference Board Inc. 1996).
[164] Paine L. "Managing for organizational Integrity", Harvard Business Review, 72 (2), March/April, 1994

Ethics is undoubtedly a fundamental ingredient for business success in the 21st century. With the recent financial scandals in Nigeria's banking industry, the question may be asked, were those scandals a direct result of corporate greed and collusion, or were companies driven by market forces which they were unable or unwilling to resist? If the answer to this is in the affirmative, do we need a radical overhaul of corporate governance and codes or can companies be relied upon to regulate themselves? If the answer to this latter question is good enough to diffuse passion, prejudice, pride and self interest of corporate leaders, then effective corporate governance is a civilizing force in bringing about justice and best ethical practices in the business world. Thus, we may conclude this section of the work in the words of Nancy .C. Agha

> Corporate governance is much more than the accuracy of the balance sheets. Indeed, except in cases of rudimentary fraud, the balance sheet is just an output of manifold structural and strategic decision across the entire company, from stock options to risk management structures, from the composition of board of directors to the decentralization of decision making powers. It is concerned with holding the balance between economic and social goals, so as to align as nearly as possible the interest of individual, corporations and society at large. It also requires judicious and prudent management of resources, the preservation of the assets of the corporation firm, maintenance of official and potential standards and pursuit of corporate objectives in an efficient manner[165]

2.10 Global and Community Perspective of Corporate Governance

Corporate governance can be considered as an environment of trust, ethics, moral values and confidence - as a synergic effort of all the constituents of society, which is the stakeholders, including government, the general public; professional/service providers and the corporate sector. It is therefore probably true to say that there is a considerable degree of convergence on a global scale as far as systems of governance are concerned, and this convergence is

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[165] N.C. Agha, 'Effective Corporate Governance and Business Performance in Nigeria', *Journal of Banking, Finance and Development (JBFD)*, Volume 2, Nos. 1 and 2, January/July, 2008, p. 124.

predicated in the dominance of the Anglo-Saxon model of the state, the market and of civil society.[166] Thus, from cultural perspective, business dealings rather than conducted on the basis of purely rational-legal financial considerations, 'transactions are conducted on the basis of mutual trust and confidence sustained by stable, preferential, particularistic, mutual obligated, and legally non-enforceable relationship.'[167]

They may be kept together either by value consensus or resource dependency, that is through 'culture and community' or through dominant units imposing dependence on others.[168] Often, company's main target is to become global while at the same time remaining sustainable as a means to get competitive power. Good governance is therefore extended in meaning and this work is concerned with the extension of that meaning and implications for the operating of a company in an increasing global environment. It demands an understanding of the cultural and community context in which a firm is operating and there are considerable regional differences which is important to understand.[169] It need be re-emphasized here that good corporate governance in the sense of global and community perspective, as depicted through the concept of stewardship, has been extended in meaning; and that corporate firms must also consider, alongside the stewardship of its own resources, the stewardship of both societal resources and of environmental resources located external to the organization. This of course implies changes to operational practice as well as changes to governance requirement across different countries, continental and regional jurisdictions of the globe.

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[166] G. Aras and D. Crowther, *Global Perspectives on Corporate Governance and Corporate Social Responsibility*, cited in C. Mallin, *Corporate Governance*, (Oxford: Oxford University Press, 2004).
[167] T. Clarke and M.D. Rama, *Fundamentals of Corporate Governance*, (London: SAGE Publication, 2008) p. 6.
[168] J.R. Hollingsworth *et al,Capitalism Sectors Institutions and Performance*, in J.R. Hollingsworth *et el* (eds), *Governing Capitalist Economics*, (New York: Oxford University Press, 1994) pp 3-16, at 6.
[169] G. Aras and D. Crowther, *Global Perspectives on Corporate Governance and Corporate Social Responsibility*, op. cit.

However, for ease of discussion, this work would pay greater attention to the United State, United Kingdom (U.K.) and Japan practice with partial reference to other countries like China, Germany and France. In view of the above, in the U.S. and U.K. corporate governance is concerned with the narrow goal of ensuring that firms maximize the wealth of shareholders. In Japan and some other countries, firms are concerned with a broader group of stakeholders, including employees, suppliers, customers and others as well as shareholders.[170] Therefore, if markets and institutions are well developed and competitive, Anglo-American corporate governance ensures an efficient allocation of resources. In other circumstances, focusing on a wider range of stakeholders as the Japanese do can be more efficient.

In the U.S. and U.K., corporate governance is concerned with ensuring that the firm is run in the interest of shareholders with a highly demanding objective of creating wealth for them.[171] This fundamental idea is embodied in the legal framework in the U.K. In these countries, managers have a fiduciary (ie very strong) duty to act in the interests of shareholders. This of course demands that markets must be perfectly competitive in order to understand when the invisible hand of the market works and when it does not. Ironically, in the U.S. and U.K., it is widely agreed that this is not the case and it is accepted that firms' sole and only paramount objective should be to create wealth for shareholders.

In many other countries there is no such consensus. Japan is perhaps the most extreme example. Instead of focusing on the narrow view that firms should concentrate on creating wealth for their owners, corporate governance has traditionally been concerned with a broader view to the effect that corporate governance is concerned with ensuring that firms are run in such a manner that society's resources are used efficiently by taking into account a wider range of stakeholders such as employees, suppliers, and customers, in addition to

[170] F. Allen and M. Zhao, T*he Corporate Governance Model of Japan: Shareholders Are Not Rulers*, (U.S.A: Pennsylvania University and Bentley College, 2007), p. 22.
[171] A. Smith, *An Inquiry into the Nature and Causes of Wealth of Nations*, (Dublin: Whitestone, 1776), p.12.

shareholders. With imperfects, this broad objective can potentially make everybody better off compared to just focusing on the shareholders' interest.[172]

For example, according to Allen[173] if there are externalities such as pollution, then maximizing the value of the firm is well known to cause a misallocation of resources. He posited that if firms were instead to use the broad view above, they would change their behaviour and produce the socially optimal level of pollution. In general, although it may not be possible to obtain efficiency, it may be possible to achieve a better allocation of resources with the broad view than with the narrow view - underlining corporate responsiveness on the one hand and corporate social responsibility on the other hand.

In other countries like Germany and France, it is this broad view that is often stressed. In fact, in Germany, the legal system is quite explicit that firms do not have a sole duty to pursue the interest of shareholders. This is the system of codetermination.[174] In Japan, large corporations' employees have an equal number of seats on the supervisory board of the company which is ultimately responsible for the strategic decisions of the company.[175]

Allen and Zhao[176] had submitted forcefully that the evidence on managers' views of the role of the firm is upheld by the way that wages are structured in the different countries. In the U.S. and U.K. wages are based on the nature of the job done. Employees' personal circumstances generally have no effect on their compensation. In Japan and Germany, it is common for people to be granted family allowances and special allowances for small children. In France vacation allowances based on family are common. These differences

[172] F. Allen, and D. Gale, *Comparing Financial Systems*, (Cambridge, MA: MIT Press, 2000), p.11.
[173] F. Allen and D. Gale, 'Corporate Governance in Emerging Markets', *Oxford Review of Economic Policy*, 21 pp. 164-177.
[174] F. Allen and D. Gale, 'Comparing Financial Systems, *op, cit.,* p.11
[175] K. Scott, 'The Role of Corporate Governance in South Korean Economic Reform', Journal of Applied Corporate Finance, 10, pp. 8-15.
[176] F. Allen and M. Zhao, *The Corporate Governance Model of Japan: Shareholders Are Not Rulers*, *op. cit*, p.15.

underline the fact that in the U.S. and U.K., companies are designed to create wealth for shareholders whereas in Germany and France, the company or firm is a group of people working together for their common benefit.

In this circumstance, we may safely submit that the United Kingdom and United States of America practice seems to be the practice obtainable under the Nigerian corporate jurisprudence considering the enormous rights granted to shareholders by the Companies and Allied Matters Act.[177]

2.11 The Social Implications of Corporate Governance

While shareholder value maximization is still a major goal for corporations worldwide, the rise in social activism and the emergence of new expectations have indeed caused other aspect of corporate performance to be examined alongside social impacts of corporate governance on society. As firms grow in size and influence, they are no longer expected to be mere contributors to the global economy, but rather to reconcile and effectively balance multiple stakeholders.[178] Nowadays, organizations are generally more inclined to broaden the basis of their performance evaluation from a short-term financial focus to include long-term social, environmental, and economic impacts and value added.[179]

In fact, corporate social responsibility which is a core aspect of corporate governance is now conceptualized into four types with each having serious implications/impacts on the entire social strata of the society. These are:

(i) Economic (jobs, wages, services);

(ii) Legal (legal compliance and playing by the rules of the game);

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[177] Companies and Allied Matters Act (CAMA), Cap. C20, Laws of the Federation of Nigeria, 2004, ss. 42, 81, 83, 115, 219, 230, 242, 302 and 408(d).
[178] D. Jamali, 'Insights into Triple Bottom Line Integration from a Learning Organization Perspective', *Business Process Management Journal*, Vol. 12, (2006), pp. 809-821.
[179] T.W. Hardjono and M. Van Marrewijk, 'The Social Dimensions of Business Excellence', *Corporate Environmental Strategy*, Vol. 8, (2001), pp. 223-233.

(iii) Ethical (being moral and doing what is just, right and fair); and

(iv) Discretionary (optional philanthropic contribution)[180]

Corporate social responsibility should be altruistic, humanitarian and philanthropic which means that a company should respond to the needs of the community of its operation irrespective of whether or not the firm will reap financial benefits from such gesture. Examples include efforts to alleviate public concerns (e.g., poverty, illiteracy) in an attempt to enhance society's welfare and improve the quality of life.[181] Considering the diverse impacts of corporate governance on society, priority now shift to need for corporations to assume their duties as citizens, and accord due diligence to their external economic and social-stakeholders and the natural environment.[182] Thus, the environmental issues of corporate governance examines primarily the impacts of processes, products, and service on the environment, biodiversity, and human health, while the social bottom line incorporates such things as community issues, social justice, public problems and public controversies.

At internal level, the social implications of corporate governance mean that companies revise their in-house priorities and accord due diligence to their responsibility to internal stakeholders, adequately addressing issues relating to skills and education, workplace safety, working conditions, human rights, equity considerations, equal opportunity, health and safety, and labour rights.[183]

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[180] A. Carrol, 'A Three-Dimensional Conceptual Model of Corporate Performance', *Academy of Management Review*, Vol. 4 (1979) pp. 497-505; G. Lantos, 'The Boundaries of Strategic Corporate Social Responsibility', *Journal of Consumer Marketing*, Vol. 18 (2001) pp. 595-630.

[181] G. Lantos, *Ibid*.

[182] L.S. Munilla, and M.P. Miles, 'The Corporate Social Responsibility Continuum as a Component of Stakeholder Theory', Business and Society Review, Vol. 110 (2005), pp. 371-387.

[183] P. Jones, *et al*., 'Corporate Social Responsibility and the UK's Top Ten Retailers', *International Journal of Retail and Distribution Management*, Vol. 33 (2005) pp. 882-892.

To be noted of course is the fact that markets sometimes fail and require public policy interventions to prevent failure and/or to recuperate. These interventions might include corporate governance with the synergic principle of corporate social responsibility (CSR) in the form of self-regulation. For example the scale of the 2010 BP oil spillage disaster in the Gulf of Mexico, coming on the heels of the near collapse of the global financial system in 2007/8, highlight the profound and far reaching impact of corporate activities on society. In some circumstances, the social implications may be so negative; in that the spill-over effects is mainly borne by people who did not cause the problem in the instance.

Meanwhile, the governance of corporate negative externalities such as child labour, environmental pollution, employee welfare, consumer protection and labour conditions are already hardwired in the institutional governance of most advanced capitalist economies, while these are still issues in most developing (or weak) capitalist economies.[184]

Also articulating CSR (a core aspect of corporate governance) as a market governance mechanism will ultimately have implications for both theory building and practice in the world economy. There is of course no gainsaying the fact that the capitalist political economy model has leveraged globalization to become the dominant, as well as the idealized, global mode of the economic coordination especially with the decline of the competing socialist political economy model since the late 1980s, as a viable alternative.[185] As such, the capitalist political economy has, to a large extent, become the global yardstick for assessing responsible and irresponsible business behaviours in the management literature, despite the differences in national socio-economic cultures and institutions.

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[184] K. Amaeshi, *et al*, 'Corporate Social Responsibility as a Market Governance Mechanism: Any Implications for Corporate Governance in Emerging Economies?', University of Edinburgh U.K. p. 27.
[185] N. Kang, ''A Critique of the 'Varieties of Capitalism' Approach", *ICCSR Working Paper Series*, Number 46, Nottingham University Business School. Available at http://www.nottingham.ac.uk/business/ICCSR/pdf/researchpdefs/45-2006.pdf

Howsoever the social implications of corporate governance is agreed, the fact remains that corporate governance practices should involve corporate social responsibility as a palliative measure to cushion the hazards orchestrated by the activities of companies. For instance, the activities of multinational enterprises (MNEs) in Nigeria are suffering debilitating impediments owing to the heavy suspicion between host communities (particularly in Niger Delta) and MNES. The people of the region believe that these MNEs are not socially responsible to them but only interested in protecting its foreign interest to the detriment of the people. Being socially responsible for local communities hosting most multinational companies (oil companies for example) is a fundamental content of good corporate governance. As a result, global firms appear to be directly or indirectly compelled, by some external actors (e.g. NGOs, international organizations, and pressure groups), to fill in the transnational governance gap for nation-states, especially in developing economies with weak and fragile institutions that are incapable of governing the activities of MNEs.

The MNEs are therefore, encouraged to be more socially responsible and transparent in their practices. This subtle compulsion often reveals itself in the growing trend of CSR as self-regulation[186] and the private governance of corporate externalities which needs to be further integrated into mainstream management scholarship.[187] By ways of conclusion, we also add that companies are increasingly using social media to communicate with and learn from stakeholders. This is particularly true in emerging markets, where companies are likely to use social media than in many developed countries.

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[186] N. Woods and D. Brown, *Making Global Self-regulation Effective in Developing Countries*, (Oxford: Oxford University Press, 2007).

[187] C. Crouch, 'Modeling the Firm in its Market and Organizational Environment: Methodologies for Studying Corporate Social Responsibility', *Organization Studies*, (2006), Vol. 27 pp. 1533-1551.

2.11.1 The Dynamism of Corporate Social Responsibility (CSR) in Terms of Sustainable Development

Since the origins of industrial capitalism, corporations have wrestled with the dilemma of whether their sole purpose is to generate wealth (narrowly defined as financial profit) or whether corporations have broader obligations to the communities in which they are situated, and from which they derive not only their fundamental resources, but their license to operate.[188] It is claimed that bridging the divide between corporate governance and corporate social responsibilities has posed a great challenge to managers for generations.[189] This presupposes that they are different approaches to corporate social responsibility.

Garriga and Mele[190] attempt a classification of the main theories and related approaches into four groups: instrumental theories, in which the corporations are seen as simply an instrument for wealth creation, and its social activities are only a means to achieve economic result; political theories, concerned with the power of corporations in society and responsible use of this power in the political arena; integrative theories, concerned with the corporation's responsibility to meet social demands; and ethical theories, based on ethical responsibilities of corporations to society. These theories represent four dimensions of corporate activity related to profits, political performance, social demands and ethical values. How to integrate these four dimensions remains a core task in resolving and appreciating to a large extent the dynamics of the relationship of business and society.

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[188] T. Clarke and M. dela Rama, Fundamentals of Corporate Governance, *op cit*, (London: SAGE Publications, 2008) p. 37.
[189] S. Benn and D. Dunphy, *Corporate Governance and Sustainability*, (London and New York: Routledge, 2007), p. 21.
[190] E. Garriga and D. Mele, 'Corporate Social Responsibility Theories: Mapping the Territory' in T. Clarke and M. dela Rama, (eds), *The Fundamentals of Corporate Governance, Volume 4: Stakeholders and Sustainability*, (London: SAGE Publications, 2008) pp. 269-293.

However, issues of socially responsible behaviour are not of course new and examples can be found from throughout the world and at least from the early days of the industrial revolution and the concomitant founding of large business entities[191] and the divorce between ownership and management or the divorcing of risks from reward.[192] Thus, in the past transcending the present, big business was and is recognizing the need to adapt to a new social climate of community accountability but that the orientation of business to financial results was inhibiting social responsiveness.

Definition of CSR abounds but all can be seen as an attempt to explain and define the relationship between a corporation and its stakeholders, including its relationship with society as a whole. Because of the uncertainty surrounding the nature of CSR activity, it is difficult to evaluate any such activity in terms of sustainable development. Aras and Crowther[193] had offered an escape route when they derived three basic principles which together comprise all CSR activity. These are:

i. Sustainability
ii. Accountability
iii. Transparency

However, we will pay greater attention to the wider principle of sustainability since the narrower principles of accountability and transparency have been discussed under the caption 'Ethical Dimensions of Corporate Governance.' We may now safely posit that modern business language has mutated again and the concept of CSR is being replaced by the language of sustainability. Sustainability primary refers to the effective use of our

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[191] D. Crowther, *A Social Critique of Corporate Reporting*, (Aldershot: Ashgate, 2002), p. 10.
[192] D. Crowther, 'Limited Liability or Limited Responsibility' in D. Crowther and L. Rayman-Bacchus (eds), Perspectives on Corporate Social Responsibility, (Aldershot: Ashgate, 2004) pp. 42-58.
[193] G. Aras and D. Crowther, 'Sustainable Corporate Social Responsibility and Value Chain', in M.M. Zain and D. Crowther (eds), *New Perspectives on Corporate Social Responsibility*, (kulala Lumpur: MARA University Press, 2007) pp. 119-140.

environmental resources in such a way that its development meets the needs of the present without compromising the chances of the future generation from meeting their own needs. In corporate practice, sustainability embodies organizational behaviour which translates into the much broader concept of corporate culture. There are therefore, four aspects of sustainability which need be recognized and analysed, namely.[194]

i. Societal influence, which we define as a measure of the impact that society makes on the corporation in terms of the social contract and stakeholder influence.
ii. Environmental Impact, which we define as the effect of the actions of corporation upon its geophysical environment.
iii. Organizational Culture, which we define as the relationship between the corporation and its internal stakeholders, particularly employees, and all aspects of that relationship.
iv. Finance, which we define in terms of an adequate return for the level of risk undertaken (Financial performance)

The cumulative effects of all the four aspects of sustainability outlined and enunciated above produces sustainable development, both for operational companies, and the entire strata of the society. For example, Stern[195] considered the challenges of building and sustaining frameworks for international collective action on climate change with important initiatives coming from both national government and corporations. He considered the various dimensions of action required to reduce the risks of climate change, both for mitigation (including through carbon prices and markets, intervention to support low-carbon investment and technology diffusion, cooperation on technology development and deployment, and action to reverse deforestation), and for adaptation. These dimensions of remedial action are

[194] A. Guler and D. Crowther 'Global Perspective on Corporate Governance and CSR, *op. cit*, p. 25.
[195] N. Stern, 'Framework for Understanding International Collective Action for Climate Change' in T. Clarke and M. dele Rama, (eds), *The Fundamentals of Corporate Governance, Volume 4: Stakeholders and Sustainability*, (London: SAGE Publications, 2008) pp. 340-358.

interdependent: a carbon price is essential to provide incentives for investment in low-carbon technology around the world, and can be strongly complemented by international co-operation to bring down the cost of new carbon technologies. Thus, an overview of existing international cooperation on climate change indicates the immense scale of the problem and negative effects of climate change on the environment. Responsible corporate governance and corporate social responsibility will be essential to securing a sustainable balance between business, society and the environment. Corporate social responsibility in terms of sustainable development should in our present circumstance be measured in terms of board oversight, management execution, public disclosure, emission accounting and strategic planning for emission reduction.

2.11.2 The Relationship between Corporate Social Responsibility and Corporate Governance

There has been considerable debate about the relationship between corporate social responsibility (CRS) and corporate governance, but in recent years the term corporate social responsibility has gained more prominence, both in business and in the press to such an extent that it seems to have become ubiquitous. Guler and Crowther had earlier unraveled the rationale behind relating corporate social responsibility with corporate governance in the following words:

> It is of course no longer questioned that the activities of corporation impact upon the external environment and that such an organization should be accountable to a wider audience than simply its shareholders. This is a central tenet of both the concept of corporate governance and the concept of corporate social responsibility. Implicit in this is a concern with the effects of the actions of an organization on its external environment, and there is recognition that it is not just the owners of the organization who have a concern with the activities of that organization. Additionally there are a wide variety of other stakeholders who justifiably have a concern with those activities, and are affected by those

> activities. Those other stakeholders have not just an interest in the activities of the firm but also a degree of influence over shaping of these activities. This influence is so significant that it can be argued that the power and influence of these stakeholders is such that it amounts to quasi-ownership of the organization.[196]

Thus enlightened companies recognize that there is a clear link between governance and corporate social responsibility; and often, this is no more than making a claim that good governance is a part of their CSR policy as well as a part of their relationship with shareholders.

But we may venture to say here that the relationship between corporate governance and corporate social responsibility cannot be understood without taking geographical, cultural and historical factors into account in order to understand the similarities, difference and concerns to people of different parts of the world.[197] These factors have earlier on been taken care of in this work under the caption, 'Global and Community Perspective of Corporate Governance'.

In fact, there is a clear overlap between this conception of corporate governance and stakeholder conception of corporate social responsibility that considers business as responsible vis-à-vis a complex web of interrelated stakeholders that sustain and add value to the firm.[198]

Corporate governance and corporate social responsibility call on companies to assume their fiduciary and moral responsibilities toward stakeholders. This act of accountability and responsiveness of companies is very core for a business to gain and by necessary extension,

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[196] A. Guler and D. Crowther, 'Global Perspective on Corporate Governance and CSR', *op cit*, pp. 34-35.
[197] G. Aras and D. Crowther, 'Is the Global Economy Sustainable? in S. Barber (ed), *The Geopolitics of the City*, (London: Forum Press, 2007), pp. 165-194;G. Aras and D. Crowther, 'Sustainable Corporate Social Responsibility and the Value Chain, in M.M. Zain and D. Crowther (eds), *New Perspectives on Corporate Social Responsibility*, (Kulala Lumpur: MARA University Press, 2007) pp. 119-140.
[198] E. Freeman, 'Strategic Management: A Stakeholder Approach', (Boston: 1984);E. Post, *et al*, 'Managing the Extended Enterprise: The New Stakeholder View', *California Management Review,* Vol. 45, pp. 33-47.

retain the trust of its financial investors and other stakeholders.[199] Both concepts thus, draw vigor from the sources, namely transparency, accountability, fairness, responsiveness and integrity.[200] Both disciplines are also perceived to confer important long-lasting benefits to ensure the endurance of the business. With respect to corporate governance in particular, it is observed that good governance mechanisms reconcile the interest of owners, managers, and all those dependent on the corporation, allowing corporations to secure long-term capital, retain the confidence of financiers, and to use the obtained capital proficiently.[201]

Windsor and Preston[202]argue that, within the framework of Legitimacy theory, corporate governance and corporate social responsibility are intricately related notions defining the interaction between an organization and its internal and external sociopolitical environment, with both increasingly considered as complementary fundamental prerequisites for sustainable growth within a globalizing business environment.

Marsiglia and Falautano[203] similarly suggested that good corporate governance and corporate social responsibility initiatives are gradually advancing from a philanthropic variant of corporate capitalism to authentic strategies intended to regain the trust of clients and society at large. In other words, while corporate governance implies 'being held accountable for', corporate social responsibility means 'taking account of' and both mechanisms are increasingly used by firms to regulate operations.[204] There is also some evidence suggesting

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[199] J.P. Page, *California Governance and Value Creation*, (University of Sherbrook: Research Foundation of CFA Institute, 2005), p.11.
[200] D.B. Van and C. Louche, 'The Link between Corporate Governance and Corporate Social Responsibility in Insurance',*The Geneva Papers*, vol. 30 pp. 425-4423.
[201] D. Jamali*et al*, *Corporate Governance and Corporate Social Responsibility Synergies and Interrelationships* (University of Southampton: Blackwell Publishing Limited, 2008) p. 446.
[202] S. Windor and L. Perston, 'Corporate Governance, Social Policy, and Social Performance in the Multinational Corporation', Research in Corporate Social Performance and Policy (1988), Vol.10, pp.45-58.
[203]E. Marsiglia and I. Falantano, Corporate Social Responsibility and Sustainability Challenges for a Banc assurance Company', *The Geneva Papers,* (2005) Vol. 30, pp. 485-497.
[204] A. Beltratti, 'The Complementarity between Corporate Governance and Corporate Social Responsibility', Geneva Papers on Risk and Insurance (2005) 30, pp. 373-386.

that corporate governance is significantly correlated with both stock returns and firm value.[205] To be noted is the fact that good corporate governance generally enhances firm competitiveness and results in superior financial performance in the same way that corporate social responsibility increases the trustworthiness of a firm and strengthens relationships with core stakeholders[206]which may lead to deceased transaction costs and increased attractiveness in the eyes of investors.

Admittedly however, short-term cost may be incurred when designing good corporate governance and CSR initiatives, but there are also several indicators pointing to positive win-win outcomes for business that are seriously committed to both.[207] Although we have in recent times witnessed significant advances in research and theory regarding to each of corporate governance and CSR in their respective paradigms, and few recent formulations hinting to their cross-connection, some lingering questions still persist, pertaining to their interrelationships, namely

i. Are corporate governance and CSR independent or interdependent functions?
ii. Are they mutually exclusive or mutually co-existent and increasingly convergent?

A potential convergence is alluded to in a recent paper by Elkington[208] where he stated that 'it is timely to review the increasingly complex cross-connects between the rapidly mutating governance agenda and the burgeoning world of CSR, social entrepreneurship and

[205] P. Gompers, *et al*, 'Corporate Governance and Equity Prices', *Quarterly Journal of Economics*, (2003) 118, pp. 107-155.
[206] R. Aguilera, *et al*., 'Putting the S Back in Corporate Social Responsibility: A Multilevel Theory of Social Change in Organizations', *Academy of Management Review*, (2007) Vol. 32, pp. 836-863.
[207] E. Marsigliaand I. Falantano, 'Corporate Social Responsibility and Sustainability Challenges in a Banc assurance Company', *The Geneva Papers*, (2005) Vol. 30, pp. 485-497.
[208] J. Elkington, 'Governance for Sustainability, Corporate Governance', *An International Review*, (2006) Vol.14, pp. 522-529.

sustainable development'. In heeding this call, Jamali[209] presented a review of several models which have posited a relationship between corporate governance and CSR, namely

i. Corporate governance as a pillar for CSR
ii. CSR as an attribute of corporate governance; and
iii. Corporate governance and CSR as coexisting components of the same continuum.

Finally, we will conclude this segment of the research in the wordings of the U.N. Global Compact Report, 2004 thus:

> In a more globalized, interconnected and competitive world, the way that environmental, social and corporate governance issues are managed is part of companies' overall management quality needed to compete successfully. Companies that perform better with regard to these issues can increase shareholder value by, for example, properly managing risks, anticipating regulatory action or accessing new markets while at the same time contributing to the sustainable development of the societies in which they operate. Moreover, these issues can have a strong impact on reputation and brands, an increasingly important part of company value.[210]

We submit conclusively here that with increasing awareness, CSR aspects of corporate governance are expected to grow in future because non-financial issues are increasingly relevant to a number of industries especially in developing countries with governance gaps such as the situationin Nigeria.

[209] J. Dima, *et al*, 'Corporate Governance and Corporate Social Responsibility Synergies and Interrelationships', Corporate Governance: An International Review (2008), Vol.16, Issue 5, p. 44.
[210] See UN. Global Compact Report, 2004, Who Cares Wins: Connecting Financial Markets to a Changing World, p. 1; See generally ' The Convergence of Corporate Governance and Corporate Social Responsibility', being a Thought-Leaders Study by Caro Strandberg – (Steandberg Consulting: Sperling Avenue, Burnaby, March, 2005) pp. 1-17.

CHAPTER THREE

HISTORICAL DEVELOPMENT OF CORPORATE GOVERNANCE

3.1 Introduction

The concept of corporate governance had existed from antiquity. Historical records show that corporate governance has a long history which date back to the ancient times where existed what is called tribal communes which supervised the activities of the tribe as well as individual members of the tribe to ensure conformity with tribal norms. As time went by, the tribal norms later matured to the level of agrarian communities whereby the concept of family came to the fore with the activities of family members being monitored by the family councils. Also, in his study on corporate governance, Kurkure,[211] submits on its historical development thus:

> In Roman Empire, specific corporate bodies such as municipal bodies were developed to manage public affairs with transparency for common good. In the Middle East, the nomadic tribes had their councils to ensure fair play and justice. The evolution of Christianity and Islam in the Middle East placed the responsibility of governance on religion.

In the post Christ period, with improved navigation of vessels, the traders from Europe especially the Portuguese and the Dutch explored the known expanse of the earth and gave rise to global trading entities. Those entities reported to the king. This was the beginning of corporate governance.[212] As the 16th century was ushered in, the most powerful trading nation, England, formed a variety of regulation and regulatory authorities such as Joint Stock Companies and Bank of England to govern all trading activities on the platform of accountability, efficiency/ effectiveness and stakeholders' satisfaction.

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[211] A.P. Kurkure, 'Elements of Excellence in Corporate Governance - System and Structures: Lesson Learned Paper Presented at the 2006 UICC World Cancer Congress in Washington DC.

[212] L. Oso and B. Semin, 'The Concept and Practice of Corporate Governance in Nigeria: the Need for Public Relations and Effective Corporate Communication, p. 4 of the paper.

The concept of corporate governance was the basic platform for these regulations and regulatory authorities and over a period of time, the concept and its practice took a firm root for all activities.[213] Similarly, Crawford[214] notes that since the late 1970s, corporate governance has been the subject of significant debate in the United States and around the globe. According to the scholar, bold and broad efforts to reform corporate governance have been driven, in past, by the needs and desires of share owners to exercise their rights of corporate ownership and to increase the value of their shares and therefore, wealth. Over the past three decades, corporate directors' duties have expanded greatly beyond their traditional legal responsibility of duty of loyalty to the corporation and its shareowners. By the first half of the 1990s, the concept and practice of corporate governance had become a public debate due to the wave of dismissals of Chief Executive Officers (CEOS) of corporations like IBN, Kodak and Honeywell by their Board of Directors. More interestingly, there was a wave of institutional shareholder' activism under the auspices of the Californian Public Employers' Retirement System (CALPERS) in order to ensure corporate governance value despite the new traditionally cozy relationships between the CEO and the Board of Directors.[215]

In the early 2000s, the massive bank malpractices and criminal malfeasance of Enron and WorldCom as well as lesser corporate debates such as Adelphia Communication, AOL, Arthur Andersen, Global Crossing, Tyco, etc. led to increased shareholder and governance interest in corporate governance. This is reflected in the passage of the US Sarbanes-Oxley Act of 2002. All these put together gave rise to the widespread practice of corporate governance across the globe for it is settled fact that the positive effect of corporate

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[213] *Ibid*, p.5.
[214] C.J. Crawford, Compliance and Conviction: the Evolution: of Enlightened Governance, (California: Santa Clara, 2007).
[215] L. Oso and B. Semin *op. cit.,* p.5.

governance on different stakeholders ultimately, is a strengthened economy. Hence, good corporate governance is a tool for socio-economic development all over the world.[216]

Corporate governance is a nebulous concept that eludes a precise definition. Thus, different scholars have defined the concept in different ways. Wilsosn[217] defines corporate governance as the manner in which corporations are directed, controlled and held to account with special concern for effective leadership of the corporations to ensure that they deliver on their promise as the wealth creating organ of the society in a sustainable manner. In his own view, Jayashree[218] defines it thus:

> Corporate governance when used in the context of business organization is a system of making directors accountable to shareholders for effective management of the companies in the best interest of the company and the shareholders along with concern for ethics and values. It is a management of companies through the board of directors that hinges on complete transparency, integrity and accountability of management.

Another definition also holds that corporate governance is a system of structuring, operating and controlling a company with a view to achieving long term strategic goals to satisfy the shareholders, creditors, employees, customers and suppliers complying with the legal and regulatory requirements apart from meeting environmental and local community needs. Moreover, corporate governance is described as the set of processes, customs, policies, laws and institutions affecting the way a corporation or company is directed, administered or controlled. It also includes the relationship among the many stakeholders involved, the board of directors, employees, customers, creditors, suppliers and the community at large.

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[216] In 1997, the Eastern Asian Financial crisis saw the economies of Thailand, Indonesia, South Korea, Malaysia and the Philippines severely affected by the exit of foreign capital after the collapse of huge assets. The lack of corporate governance mechanisms in these countries highlighted the weakness of the institutions in their economies.

[217] See Wilson I. 'Regulatory and Institutional Challenges of Corporate Governance in Nigeria Post Banking Consolidation: Nigerian Economic summit Group Economic Indicators, 2006. P.10

[218] S. Jayashree, 'Some Views on Corporate Governance', *India Management Review*, India School of Management Studies, Puna: Tathawade.

Still, corporate governance is simply put by the famous Report of Cadbury Committee as the system by which companies are directed and controlled. While the Organization for Economic Cooperation and Development (OECD) also holds that corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. From this array of definitions, it is clear that corporate governance has come to stay. It stands as inevitable for the survival of business or corporation in the world over. It is the cornerstone upon which the corporate goal and sustainability can be achieved and any company that acts otherwise does so at its own peril. More importantly, the essential ingredients of corporate governance such as honesty, trust and integrity, complete transparency, accountability and responsibility, protection of stakeholders interests and satisfaction, participation, business ethics and values, and performance orientation to organization are quite convincing that sincere compliance or adherence to them would pave way for the sustenance of business organization or corporation, realization of corporate goals, good and appreciable turn out and a veritable global market place. These ingredients after critical study were summarized into two broad elements. These are the long term relationship which has to deal with checks and balances, incentives for manager and communication between management and investors and, the transactional relationship which involves dealing with disclosure and authority.[219]

3.2 History of Corporate Governance in the United Kingdom

Initial corporate governance development in the UK began in the late 1980s and early 1990s in the wake of corporate scandals such as Polly Peck and Maxwell.[220] Financial reporting irregularities led to the establishment of the 'Financial Aspects of Corporate Governance Committee' led by Sir Adrian Cadbury. The resulting Cadbury Report published in 1992

[219] L. Oso and B. Semin *op. cit*, p.4
[220] See Kingston City Group: Corporate Governance Development in the U.K., p.I. See also Financial Reporting Council: The UK Approach to Corporate Governance, 2010, p.6.

outlined a number of recommendations around the separation of the role of an organization's chief executive and chairman, balanced composition of the board, selection processes for non-executive directors, transparency of financial reporting and the need for good internal controls. The Cadbury reporting included a Code of Best Practice and its recommendations were incorporated into the Listing Rules of the London Stock Exchange. Following Cadbury, a 'Working Group on Internal Control' was established to provide guidance to companies on how to comply with principle 4.5 of the Cadbury Code reporting on the effectiveness of the company's system of internal control. This led to the publication of the Rutteman Reporting'.

In 1995, following concerns about directors' pay and share options, the Green-bury Report recommended extensive disclosure in annual reports on remuneration and recommended the establishment of a remuneration committee comprised of non-executive directors. Again, the majority of the recommendations were endorsed by the Listing Rules. In January 1996, the Hampel Committee was established to review the extent to which the Cadbury and Green bury Reports had been implemented and whether the objectives had been met. The Hampel Report led to the publication of the Combined Code of Corporate Governance (1998), covering areas relating to structure and operation of the board, directors' remuneration, accountability and audit, relations with institutional shareholders, and the responsibilities of institutional shareholders.[221]

Part of the 1998 and 2003 Combined Code required companies to provide a statement in their annual report on how they have applied the Code principles and Code provisions relating to internal control. Guidance for companies on how this should be approached was needed. This led to the establishment of the Tumbull Committee in 1998 by the Institute of Chartered

[221] The 1998, Combined Code applied to all listed companies from 31 December 1998 until reporting years commencing on or after 1st November 2003. It was appended to Listing Rule. It was appended to Listing Rule 12.43A requiring companies to provide in their annual reports a narrative statement of how they have applied the Code principles and state that they have complied with the Code provisions or, if not, why not and for what period. See generally Kingston City Group, Corporate Governance Development in the United Kingdom, p.1.

Accountants in England and Whale (ICAEW) which then resulted in the Tumbull Guidance, 'Internal Control: Guidance for Directors on the Combined Code published in September 1999.' The Guidance is a Securities and Exchange Commission (SEC) approved framework for management to show that they have adequate reporting procedures in place in order to comply with section 202 of the Sarbanes-Oxley Act.

In 2001, the relationship between institutional investors and companies was addressed with the government Commissioned Miners Review, 'Institutional Investment in the UK'. The objective of the review was to consider whether there were factors distorting the investment decision-making of institutions. It included suggestions for the improvement of communication between investors to companies and their responsibilities.

In 2002, the Directors' Remuneration Report Regulations were introduced to further strengthen the powers of shareholders in relation to directors' pay. The regulations increased the amount of information shareholders are given on director's remuneration, certain disclosures, as well as performance graphs. Shareholder may vote in an advisory capacity to approve the director's remuneration report. In July 2002, the Department of Trade and Industry (DTI) and the Treasury instigated a review of the Combined Code following a review of company law. It initiated the Higgs Report on 'The Role and Effectiveness of Non-Executive Directors" which was published in January 2003.[222] Around the same time, the Financial Reporting Council published the Smith Report, 'Guidance on Audit Committees'. Both the Higgs and Smith Reports were published in January 2003 followed by the Tyson Report on the recruitment and development of non-executive directors commissioned by the DTI. The recommendations from the Higgs and Smiths Report led to changes in the

[222] Recommendations from Higgs include a definition of 'independence'; the proportion of independent non-executive directors on the board and its committees; an expansion on the role of the senior independent director to provide an alternative channel to shareholders and lead evaluations on the chairman's performance; added emphasis on the process of nominations to the board through a transparent and rigorous process and evaluation of the performance of the board, its committees and individual directors.

combined Code of Corporate Governance published in July 2003. It applied to all companies listed on the primary market of the London Stock Exchange for reporting years commencing on or after 1st Nov. 2003.

In 2004, the Financial Reporting Council established the Tumbull Review Group to consider the impact of 'Internal Control: Guidance for Directors on the Combined Code, and to determine whether the guidance needed to be updated. Accordingly, 'Internal control: Revised Guidance for Directors on the Combined Code' was published by the Financial Reporting Council in October 2005.

Recall that in 1998, the UK Government instigated a Company Law Review and produced a white paper in 2002. A number of proposals in the white paper related to company reporting and a significant development was the requirement for companies to provide a Mandatory Operating and Financial Review to provide information on the company's current and prospective performance and strategy. This came into effect from financial year beginning on or after 1st April 2005.

The European Union also significantly influenced corporate governance in the UK. The European Commission's 'Corporate Governance and Company Law Action Plan' (May 2003) proposed a mix of legislative and regulatory measures which would affect all member state relating to disclosure requirements; exercise of voting rights; cross border voting; disclosure by institutional investors, and responsibilities of board members.

The economic crisis has prompted government across the world to re-evaluate their financial regulatory framework, to try tackling the causes of, and fallout from, the global downturn. The UK Government has taken unprecedented action to prevent and curtail future crisis in the

financial markets, and support the broader economy focusing on stabilizing the banking system to protect people's savings and the economy.

The global financial crisis has revealed widespread and massive failures in risk management practices. Many economists, organizations and governments have suggested a link between weaknesses in corporate governance arrangements which did not serve their purpose to safeguard against excessive risk taking in a number of financial service companies. The UK government commissioned Lord Turner in October 2008, to review the causes of the global financial crisis. The Turner Review, issued in March 2009, was a UK regulatory response to the global banking crisis.[223] The Turner Review outlined recommendations on the redesign of regulation and supervisory banking system for the future. The Review also focuses on the improvements in the effectiveness of internal risk management and corporate governance.

In February 2009, Sir David Walker, ex-City regulator had been asked by the Prime Ministry to review corporate governance in UK banks in the light of experience of critical loss and failure throughout the banking system. The Walker Review published in Nov. 2009 recommends more transparent pay and bonus structure for all high earners following a serious and ongoing corporate governance failings in the financial sector. The review examines corporate governance in the UK banking industry and makes recommendations on:

i. the effectiveness of risk management at board level, including the incentives in remuneration policy to manage risk effectively;
ii. the balance of skills, experience and independence required on the boards of UK banking institutions;
iii. the effectiveness of board practices and the performance of audit risk, remuneration, and nomination committees;

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[223] *Ibid*, p.3.

iv. the role of institutional shareholders in engaging effectively with companies and monitoring boards, and

v. whether the UK approach is consistent with international practice and how national and international best practice can be promoted.

As a result of Walker's recommendations, the role of the Chief Risk Officer (CRO) may fundamentally change. Walker suggests that the C.R.O's mandate should encompass all material risks and become at least in part, the 'eyes and ears' of the Board Risk Committee.

3.2.1 The Combined Code and Associated Guidelines

The Combined Code on Corporate Governance sets out standards of good practice in relation to issues such as Board composition and development, remuneration, accountability and audit and relations with shareholders. All companies incorporated in the UK and listed on the main market of the London Stock Exchange are required under the Listing Rules to report on how they have applied the Combined Code in their annual report and accounts. The Combined Code contains board principles and more specific provisions. Listed Companies are required to report on how they have applied the main principles of the code, and either to confirm that they have complied with the code provisions or where they have not, to provide an explanation.

In March 2009, the Financial Reporting Council (FRC) announced a review of the Combined Code, as a result of which it proposes to make a number of revisions to the code consultation and these proposals ends on 5th March 2010. Thus, the FRC has updated the code (known initially as the Combined Code and now as the UK Corporate Governance Code) at regular

intervals, most recently and most substantially in 2010 to reflect lessons learnt from the problems in the UK's financial service sector.[224]

Throughout all of these changes the 'comply or explain' approach first set out in the Cadbury report has been retained. In 2010 it was reinforced by the UK Stewardship Code under which, institutional investors report on their policies for monitoring and engaging with the companies in which they invest.[225]

3.2.2 The Rationale behind the UK Approach

In the UK, the Companies Act 2006 requires directors to focus on enlightened shareholder value. This means that boards must ensure that the business is sustainable and take account of long term consequences in setting its business model and strategies. Good governance can improve the board's ability to manage the company effectively to deliver long term success as well as provide accountability to shareholders. This is in accord with the Cadbury Report which partly provides thus:

> The effectiveness with which boards discharge their responsibilities determines Britain's competitive position. They must be free to drive their companies forward, but exercise that freedom within a framework of effective accountability. This is the essence of any system of good corporate governance.

A regulatory framework that aims to improve standards of corporate governance is more likely to succeed if it recognizes that governance should support, not constrain, the entrepreneurial leadership of the company, while ensuring risk is properly managed. This requires a degree of flexibility in the way companies adopt and adapt governance practices. Boards must see good governance as a means to improve their performance, not just a compliance exercise. In order to be effective, it needs to be implemented in a way that fits the

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[224] *Ibid*, p.4.
[225] See Financial Reporting Council: The UK Approach to Corporate Governance 2010 October, p.7.

culture and organization of the individual company. This can vary enormously from company to company depending on factors such as size, ownership, structure and the complexity of its activity.[226]

3.3 History of Corporate Governance in the U.S.A.

Companies have existed in different forms going back to 3000 B.C..[227] When H.G. Wells wrote 'Outline of History', a comprehensive history of the world published in 1920, he never thought to mention the company. But in the years that followed, public companies would come to occupy a central place in the U.S economy. In 1901, for example, American telegraph had just 10,000 shareholders, and by 1931 it had more than 642,000. This was part of a broader trend, which accelerated during the 1920s, when the number of Americans holding equities rose from 500,000 to 15 million, and these shareholders realized extremely high returns. From March 1928 to September 1929, the value of publicly held shares in U.S. listed companies doubled. Coupled with an average annual growth rate of nearly 5 percent, optimism about the future ruled the day.[228] But some market-watchers thought there was too much optimism. Joe Kennedy, the wealthy and well-connected father of future president John F. Kennedy (as well as the first chairman of the Securities and Exchange Commission), famously sold all of his investments when his shoeshine boy began touting the latest hot stocks, and his pessimism proved prescient. Between October 23 and November 13 of 1929, the now Jones Industrial Average fell by 39 percent. The downward slide would continue until July 1932, at which point the value of all stocks listed on the New York Stock Exchange had declined 83 percent since September 1929. There were many reasons for the massive decline: the role of corporate governance has received little scrutiny, but it is fair to say it did not help. At the time, companies disclosed little about their operations. Most state laws

[226] *Ibid* p.8
[227] See John M. and Adrian W. 'The Company: A short History of a Revolutionary Idea (modern Library, 2003 p. 3)
[228] See the Sovereign Global, A History of US Corporate Governance. 2006. p.2.

governing securities were widely ignored, and there were no generally accepted accounting standards.[229] Of the companies listed on the New York Stock Exchange in 1923, only about one quarter issued annual and quarterly financially reports.[230] An association of financial analysts has described the period by saying, 'many corporate executives and investment bankers elevated capacity to a hallowed business principle.'[231]

Some individuals had already recognized the need for better corporate structures. The American Management Association (AMA) was formed in 1923 and Mc Kinsey, the consulting firm, followed three years later. But the prevailing state of affairs in corporate governance remained somewhat breezy, and with the growth in the number of publicly owned companies, this assumed new significance. Large number of shareholders were being impacted, and yet their influence on corporate operations was eroding. The first book to capture the implications of this growing gulf between ownership and control was the *Modern Corporation and Private Property*, written by Columbia University's Adolf Berle and Gardiner Meoms. The book, published in 1932, highlighted how the growth in the number of company owners/shareholders reduced their incentive to try to exercise any real influence over the corporations in which they had invested.[232]

Those who control the destinies of the typical modern corporations own so insignificant a fraction of the company's stock that the returns from running the corporation profitably accrue to them in only a very minor degree. The shareholder, on the other hand, to whom the profits of the corporation go, cannot be motivated by those profits to more efficient use of the property, since they have surrendered all disposition of it to those in control of the

[229] *Ibid*, p.2.
[230] S. Joel, 'The Transformation of Wall Street: A History of the Securities and Exchange Commission and Modern Corporate Finance (Aspen, 2003).
[231] Quoted in Alex Berenson, 'The Number: How the Drive for Quarterly Earnings Corrupted Wall Street and Corporate America (Random House, 2003), p.9.
[232] See Sovereign Global, *op.cit*, p.3.

enterprise.[233] The net effect was to reduce the influence of shareholders and vest great power in the corporate management, and in particular the chief executive officer. Thus, the decades old joke, from General Electric, that the CEO needed to be careful when asking a colleague for a cup of coffee, the request might be interpreted as guidance to buy Brazil. The growth in public ownership of companies, coupled with the stock market collapse, were catalysts for the passage of a number of laws, one of which created the Securities and Exchange Commission in 1934. The Laws were less geared toward mandating how companies should be governed and more toward what information they would be required to disclose to the public. 'Publicity is justly commended as a remedy for social and industrial diseases', wrote Supreme Court Justice Louis Brandeis, in a passage often cited by President Roosevelt, 'and sunlight is said to be the best of disinfectants.'[234] Henceforth, companies would be required to file publicly available reports attesting to their financial condition (including audited financial statements each year).

The legislation creating the SEC also sought to accord greater rights to shareholders, empowering the agency to write rules 'under which proxies may be solicited with a view to preventing the recurrence of abuses which have frustrated the free exercise of the voting rights of stockholders.'[235] In the decades that followed, there was a steady push and pull between corporate managers and corporate shareowners. However, with the U.S. economy expanding steadily, and the SEC working to enforce the laws that applied to public companies, corporate governance issues were far from a major concern of investors, regulators, or managers.[236] Writing in 1977, Columbia University Law Professor, John Coffee said that corporate boards at the time were akin to 'a 17th century monarch holding absolute power in theory, but cut off from access to information and thereby manipulated by

[233] Adolt B. Gardiner M. 'The Modern Corporation and private property (Macmillan, 1932), pp. 8-9.
[234] Quoted in Seligman, 'The transformation of Wall Street, p. 42.
[235] See Section 14 (a) of the Securities Exchange Act of 1934.
[236] See David Skeel, Learus in the Boardroom (Oxford University Press, 2005), p. 108.

the ministers who are its nominal servants.'[237] The modest corporate governance milestones that were realized during this period included the following:

i. In 1955, the SEC began to require public companies to issue semi-annual earnings reports.

ii. In 1965, a professor of law, Henry Manne, published an academic article arguing that corporate takeover, or the mere threat of them, was likely to yield improvements in corporate governance and corporate performance.

iii. In 1977, the New York Stock Exchange required each listed company to establish an audit committee composed of outside directors, which was a catalyst for the vast majority of public companies to create boards where more than half of the directors were independent.

iv. In 1992, the SEC reformed its proxy rules, giving shareholders new opportunities to communicate with each other (previously, any meeting of 10 or more shareholders was technically prohibited unless the group had field a proxy statement with the SEC. The rule change made it easier for shareholders to create organized opposition to flagging corporate management.[238]

The balance of power between management and shareholders continued to filtrate through the years, although management picked up a significant victory in 1985 when the Delaware Supreme Court ruled that companies were permitted to issue new shares- a 'poison pill'-in the event they were threatened with a hostile takeover. Diluting the potential suitors' shareholdings rendered takeovers much less appealing, and thus helped to insulate corporate managements from shareholder activists. Nonetheless, in January 1993, following the resignation of multiple high-profile corporate chiefs in the previous months, Fortune

[237] Quoted in S. Joel, 'The Transformation of Wall Street p. 539.
[238] See Sovereign Global, *op.cit*, p. 4.

Magazine triumphantly declared the end of the Imperial CEO, proclaiming that the struggle between management and shareholders was over- shareholders have won.[239]

The only sense, in which shareholders had 'won', however, was that they experienced an increase in stock prices in the years that followed. The NASDAQ tripled in value between October 1997 and March 2000, while the Dow's averages annual return from 1995-1999 was nearly 25 percent. But the euphoria could not be sustained, and in 2000 the Dow declined 6 percent, beginning a pattern that would repeat itself in 2001 and 2002. Similarly, when the NASDAQ loomed out in October 2002 it was 78 percent off its peak.

The total value of U.S. stocks fell during this period from $ 17 trillion to $ 9 trillion. A significant factor in these declines was the corporate failures that began in late 2001 with Enron. These failures were largely, though not exclusively, a function of poor corporate governance, thus serving as a powerful reminder of Peter Drucker's warning that 'power without accountability always become flabby or tyrannical, and usually both.' Indeed, there was no shortage of flabbiness and tyranny. Directors were at sleep at the wheel. Auditors fell down on the job, owing in no small measure, to the decline in the share of revenue they realized from auditing (just 38 percent in 1998; down from more than 70 percent in 1976) and the growth of more lucrative consulting arrangements. Sell-side research analysis became handmaidens of their investments banking colleagues, and issued highly compromised reports on individual companies ('what used to be a conflict is now a synergy', in the now-in famous words of one analyst). Lawyers crafted novel arguments to justify sham transactions, and banks didn't think triple about funding these transactions. The business media often celebrated the hysteria, without looking under the hood (most infamously, CFO magazine bestowed "Excellence" awards on Scott Sullivan of WorldCom in 1998, Andrew Fastow of

[239] The King is Dead, 'Fortune, January', 1993.

Enron in 1999, and Mark Swartz of Tyco in 2000-all of whom were later indicted). Perhaps most significant of all, investors became too consummated with achieving out-sized returns that they never thought to ask about a matter as mundane as how a company was governed.[240]

These conditions were encouraged by a financial instrument- the stock option-that had been designed years earlier in an attempt to fully align the interest of management with shareholders, and thus resolve the dilemma described by Berle and Means in 1932. Instead, stock options emerged as the equivalent of a lit match in the hands of a pyromaniac. Alan Greenspan, speaking in 2002, diagnosed the problem thus:

> The highly desirable spread of shareholding and options among business managers perversely created incentives to artificially inflate reported earnings in order to keep stock prices high and rising. This outcome suggests that the options were poorly structured, and, consequently, they failed to properly align the long-term interests of shareholders and managers, the paradigm so essential for effective corporate governance. The incentives they created overcame the good judgment of too many corporate managers. It is not that humans have become any greedier than in generation past. It is that the avenues to express greed had grown so enormously."[241]

Indeed, a 2005 Boston Consulting Group study of public companies found guilty of fraud in the previous five years found that the value of the stock options granted to the CEOs of those firms in the years before the frauds became public was eight times greater than those granted to the CEOs of comparable firms not found guilty of any wrongdoing.[242] According to the economist,' nothing correlated so strongly with corporate fraud as the value of stock options not the standard of the firms governance, or analysts' inflated expectations about their earnings, nor ego-boosting stories about their CEOs in the press."[243]

[240] See Sovereign Global op.cit p. 5.
[241] Available at: http://www.federalreserve.gov./boarddocs/hh/2002/July/testimony.htm, accessed on 10/04/2014.
[242] Available at: http.//www.beg.com/publications/view.jsp? pubint 1300&language. English.
[243] 'Fat Cats Turn to Low Fat,' The Economist, March 3, 2005.

Also contributing to this sorry state of affairs was the shift in the ownership structure of U.S. equities. Institutional investors (pension funds, insurance companies, and mutual funds) began to loom larger on the investing landscape holding 6 percent of company shares in 1950, 19 percent in 1970, 50 percent in 1992, and 66 percent today.

As individual ownership has steadily declined and institutional ownership increased, individual shareholders have tended to fulfill the scenario spelled out by Berle and Means in 1932, abdicating their vital oversight role in holding boards of directors accountable for their financial and ethical actions. This lack of oversight is all too evident when this state of affairs is coupled with a collapse by the traditional gatekeepers (directors in particular), and regulations that gave shareholders little if any, voice it left many companies operating on the equivalent of highways with no speed limits and no guardrails.[244]

Some public pensions funds have chosen to exercise their leverage, but many institutional investors have stayed on the sidelines.[245] There are many explanations, but a fundamental one, particularly for mutual funds, is the short holding periods. With average annual turnover at mutual funds now 100 percent, there is little incentive to invest time or energy on corporate governance at their portfolio companies. But by failing to act, says John Bogle, the former CEO of Vanguard, the mutual fund giant, these institutional investors are 'neglecting the legitimate interests of the ultimate stock owners, the beneficiaries whom they are duty-bound to represent.'[246] Yet institutional investors, given their size, pose considerable leverage to seek corporate-governance improvements in the companies in which they have invested. And they can be a crucial factor, perhaps just as crucial as strong regulation to be encouragement of good governance and strong firm performance. A recent study by Martin Cremers and

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[244] Sovereign Global *op.cit* p. 6.
[245] For explanation, see this 2004 speech by a member of the Federal Reserve; available at http://www. federal reserve.gov/boarddocs/speeches/20040219/default.htm.
[246] Boyle, *The Battle for the Soul of Capitalism*, P. xxi.

Vinary Nair finds that equity prices of firms that have good governance outperform their peers by 10-15 percent per annum, but only if these firms also have large block holdings by institutional investors.[247]

The corporate failures, starting with Enron in December 2001, and culminating with WorldCom six months later, sparked the federal government to act. On July 30, 2002, President Bush held a major ceremony at the White House to sign the Sarbanes-Oxley bill into law. The era of low standards and the phenomena of excessive executive compensation, poison pills are related party transactions. Managers who are not watched over by shareholders will often institute antitakeover provisions to insulate themselves from oversight by markets as well. And false profits are over," he said, adding that 'no boardroom in America is above or beyond the law.'

To that end, the law created a new entity to oversee the accounting profession (the Public Company Accounting Oversight Board); restricted the consulting work of accounting firms; required the creation of independent audit committees; mandated that chief executives sign off on company financial statements, and called on auditors to attest to how effectively companies managed their internal controls.

There are legitimate concerns about the high cost of complying with Sarbanes-Oxley, as well as the Law's collateral effects to wit: public companies going private; private companies staying private; and opportunities never pursued out of fear of being ensnared by regulators. And in their desire to prevent future Enron - style implosions, regulators must be careful not to stifle the 'boldness of enterprise', and that, Alexis de Tocqueville cited in 1835 as the 'foremost cause of (America's) rapid progress, its strength, and its greatness.' Similarly,

[247] Sovereign Global, *op.cit*, p.7.

minor infractions (foot faults) should be recognized as such, and not treated as calamitous events that warrant high fines and/or the sacking of senior management.[248]

Perhaps not enough attention has been given to the less-easily-quantified benefits that were derived from the law's enactment at a time when America's corporate landscape was littered with wrongdoing (and was still recovering from terrorist attacks less than a year earlier). As one of the law's sponsors has said, 'How can you measure the value of knowing that company books are sounder than they were before?' signaling to investors in the U.S. and abroad that America was determined to improve corporate governance helped to restore investor confidence and pave the way for the country's economic revival.[249]

As important as it is to achieve sound corporate governance, it is still no guarantee that a business will be operated honestly, or ethically. Independent directors, for example, are often seen as a touchstone of good corporate governance. The New York Stock Exchange requires that a majority of the directors for each public company be independent. Yet, all but two of the directors at Enron were independent, and the company was frequently hailed for its progressive corporate governance. An article in Chief Executive Magazine one year before Enron's bankruptcy said the company had a board that works hard to keep up with things.[250]

The most important point of all is to remember that regulations in and of themselves cannot deliver good corporate governance. Regulations can only define a minimum standard of behavior and cannot of themselves engender a moral sense. Thus, the most effective forms of corporate governance will be driven not by government dictates/or even investors, but rather an ethical compass that clearly delineates between right and wrong. Corporate leaders must remain firmly rooted on the right side, and they have an obligation to create an ethical, moral

[248] *Ibid*, p.7.
[249] *Ibid,* p.7.
[250] 'Boards on Trial,' Chief Executive, October 2000.

culture in their workplaces that is understood by everyone from employee to director, and to auditor.

The commitment to ethics and morality will be the ultimate arbiter of every economy's prosperity and sustainability. Capital providers, be they small individual investors or large institutional investors, must have confidence that the entities to which they are directing their capital will, at the very least, use it honestly, and ideally use it productively. A market defined by a low level of trust will discourage investment, drive away reputable companies, and paralyze economic growth. As 19th century American writer Ralph Waldo Emerson concisely put it, thus: 'distrust is very expensive.' Conversely, a market place defined by a high level of trust will be one where capital can flow freely and efficiently to those who use it wisely and productively. And that trust will, in the long run, deliver the greater economic dividend to all.[251]

3.4 History of Corporate Governance in Nigeria

The history of corporate governance in Nigeria can be said to be somewhat distorted and confusing. Nonetheless, corporate governance cannot be divorced from Company Law in general. Prior to the time the expression 'corporate governance' became popular, Company Law recognized and still recognized two organs of a company, the board of directors and the company in general meeting. Corporate governance as a concept merely stressed the greater focus that should be paid on how a company should be run by those put in charge of the company's affairs. Unsurprisingly therefore, the centrality of the board of directors in the institutionalization of the tents of sound corporate governance in every company cannot be denied. The prominence is evident in model definitions of corporate governance which in a nutshell regards corporate governance as the processes and structures by which the business

[251] *Ibid*, p.8.

and affairs of an institution are directed and managed in order to improve long-term shareholder value by enhancing corporate performance and accountability, while taking into account the interest of stakeholders. As convoluted as the historical development of corporate governance is in Nigeria, an attempt has been made here to capture this in proper perspective.[252] It is therefore necessary to discuss the historical development of corporate governance in Nigeria in periodic context. For this purpose, four periods are readily identifiable.

(A) **Pre-1990 Era**: Before 1990, the principal Company Law statute in Nigeria was the Companies Act 1968. This enactment was a comprehensive legislation modeled after the Companies Act 1948 of the United Kingdom. It contained elaborate provisions regarding the running of companies in relation to the roles of the board of directors and the members in general meeting. However, this statute was not without its legions of limitations. As a result of numerous criticisms from stakeholders, the Companies Act 1968 was repealed and replaced in 1990 by the then Companies and Allied Matters Decree No, 1 of 1990.[253]

(B) **1990 to 2003 Era**: The CAMA was the product of a rigorous process championed by the Nigerian Law Reform Commission. It contained a lot of innovative provisions such as provisions on greater and more effective participation in, and control of the affairs of a company through improved provisions in respect of accountability by directors. At the time the initiative to make the statute commenced, corporate governance had not emerged as a distinct concept. Thus, the statute made general provisions on the administration of companies registered in Nigeria.

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[252] N. Ofo. 'Historical Development of Corporate Governance in Nigeria: Available at http.www.thecorporateprof.com. posted on 7 January,

[253] With some minor modifications over the years, this Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria 2004 (henceforth referred to as CAMA is the principal statute regulating companies in Nigeria.

However, after the coming into force of the statute, some corporate challenges around the world brought the issue of corporate governance to the fore. Consequently, some countries started to review their corporate governance practices. This resulted in some countries issuing corporate governance codes to address issues neither specifically nor sufficiently addressed by their respective company legislation. The collapse of Enron, WorldCom and other major corporations in the early 2000s brought corporate governance consideration to the front burner all over the world.[254]

In the case of Nigeria, its foremost formal corporate governance Code would be traced to the Code of Corporate Governance for Banks and other Financial Institutions in Nigeria.[255] This Code was the outcome of the work of the Banker's Committee's sub-Committee on Corporate Governance. It was initiated in response to the financial crisis in Nigeria in the early 1990s and in the realization that poor corporate governance was one of the major factors in virtually all known instances of financial sector distress. As is evident from its nomenclature, the Code was applicable to all banks and other financial institutions operating in Nigeria at the time it was issued. Its major weakness was that it was not issued by a regulator having been issued by a voluntary association of the chief executives of the banks in Nigeria, otherwise known as Banker's Committee. Thus, not much is known about the Code.

The Code was predicated on 11 Principles. These are:

1. Responsibilities of the Board of Directors: The Board should exercise responsibility, leadership, enterprise, integrity and judgment in directing the institution so as to achieve continuing prosperity for the institution and act its best interest, in a manner

[254] N. Ofo, *op.cit,* p. 2.
[255] The Code was issued by the Banker's Committee in August 2003.

based on transparency, accountability and equity. Every institution should be headed by an effective Board that can lead and control the institution.

2. Structure of the Board of Directors: The Board should include a balance of executive and non-executive directors (including independent non-executives) such that no individual or group of individuals can dominate the Board's decision-making process.
3. The Chairman and the Chief Executive Officer: There should be a clear division of responsibilities at the head of the institution - the running of the Board and the management of the institution's business, which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision making.
4. Appointments to the Board: There should be a formal and transparent procedure for the appointment of new directors to the Board.
5. Proceedings of the Board of Directors: The Board should meet regularly and Board members should attend meetings regularly.
6. Directors' Remuneration: Institutions should establish a formal and transparent procedure for developing policies of executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in approving his or her own remuneration. Also, levels of remuneration should be sufficient to attract and retain the directors needed to run the company successfully, but institutions should avoid paying more than is necessary for this purpose. A proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance.
7. Board Performance Assessment: There should be a formal assessment of the effectiveness of the Board as a whole and the contribution by such individual director (including the chairman) to the effectiveness of the Board.

8. Risk management: The Board must identify key risk areas and key performance indicators of the business enterprises and monitor these factors.
9. Financial Disclosure: There should be degree of accountability of directors to shareholders and other stakeholders of the institution and of management to the directors.
10. Relations with shareholders: The Board should serve the genuine interests of the shareholders of the institution and account to them fully.
11. Audit Committee: The Board should establish formal and transparent arrangements for considering how they should apply the financial reporting and internal control principles and for maintaining an appropriate relationship with institution's auditors.

In spite of the comprehensive provisions of the Code, it did not make much impact. A major factor that could have occasioned this was the issuance of the Code of Best Practices on Corporate Governance in Nigeria by the Securities and Exchange Commission in October 2003, about two months after the issuance of the Code.[256]

(C) **2003 to 2011**: The Code of Best Practices on Corporate Governance in Nigeria (2003 SEC Code) issued by the Securities and Exchange Commission in 2003 greatly impacted the corporate governance scene in Nigeria. In the first place, it was the first corporate governance Code to be issued by any regulator in Nigeria. Secondly, it was applicable to all public companies registered in Nigeria.

The 2003 SEC Code was the outcome of the work of a 17 member committee (headed by Mr. Atedo Peterside) set up by the Securities and Exchange Commission in Collaboration with the Corporate Affairs Commission on 15th June 2000. Membership of the Committee was carefully selected to cut across all sectors of the economy including members of professional

[256] N. Ofo, *op.cit*, p.3.

organizations, organized private sector and regulatory agencies. The mandate of the committee was clear: to identify weakness in the current corporate governance practice, and fashion out necessary changes that will improve the corporate governance practice in Nigeria. After the coming into force of the 2003 SEC Code, there were numerous changes in the corporate world. Quite rapidly, the provisions of the 2003 SEC Code became inadequate to address the new developments in the corporate scene; yet no amendment to it was forthcoming from the Securities and Exchange Commission. The oversight in amending the 2003 SEC Code to bring its provisions up to some regulations of specific sectors issuing industry-specific corporate governance codes which not only took into account the current situations when codes were made, but they also contained provisions on some matters peculiar to their respective sectors.[257]

In 2006, the Central Bank of Nigeria issued its Code of Corporate Governance of Banks in Nigeria Post-Consolidation (2006 CBN Code). Compliance with the provisions of this Code is mandatory for all banks operating in Nigeria. Essentially, the Code which was issued following the consolidation of Nigeria Banks in 2005 was meant to address the identified weakness in corporate governance of banks in Nigeria, and to resolve the challenges of corporate governance which are bound to occur post-consolidation. Some of the corporate governance challenges addressed in the 2006 CBN Code were way outside the purview of the 2003 SEC Code. This situation decries the absence of regular amendment to the 2003 SEC Code and justifies the issuance of the 2006 CBN Code. However, it does seem that the lack of regular amendment that bedeviled the 2003 SEC Code has afflicted the 2006 CBN Code. No doubt, the 2006 CBN Code is overdue for revision. It is noted though that the CBN issued an Exposure Draft of a Revised Code of Corporate Governance for Banks in Nigeria in the second half of 2012. This is yet to be finalized.

[257] N. Ofo, *ibid*, p. 3.

In 2008 following the reforms in the pension sector which gave rise to greater private sector involvement in pension fund management, the National Pension Commission (PENCOM) issued the Code of Corporate Governance for Licensed Pension Operators (2008 PENCOM Code). The 2008 PENCOM Code sets out rules to guide pension fund administrators (including closed pension fund administrators) and pension fund custodians on the structures and processes to be used toward achieving optimal governance process. The Code outlines minimum corporate governance requirements, meant to ensure that governance policies are entrenched in the companies. It was developed with a view to establishing overall economic performance and market integrity by creating incentives for pension schemes to impact positively on stakeholders with a view to gaining the confidence of these stakeholders. There are numerous developments in the corporate governance scene which the 2008 PENCOM Code did not contemplate. Thus, it would not be out of place for the PENCOM to commence the process of amending this Code for continued relevance.

The third regulator to issue an industry-specific corporate governance Code is the National Insurance Commission (NAICOM). In 2009, it issued the Code of Good Corporate Governance for the Insurance Industry in Nigeria (2009 NAICOM Code). The 2009 NAICOM Code which was effective on 1st march 2009 is mandatory for all insurance and re-insurance companies under the regulatory supervision of the NAICOM. The expectation of the NAICOM in issuing the 2009 NAICOM Code is to unleash the hidden potential of the insurance sector for maximum impact with a view to inducing strong economic growth in Nigeria. It is believed that sound corporate governance practice in the insurance industry would ensure transparency, accountability and enhanced shareholders value. The 2009 NAICOM Code recognized the following as basic principles of good corporate governance: a proactive, responsible, responsive, accountable and committed Board/Management; definite management succession plan; culture of compliance with rules and regulations; good

knowledge about business and insurance matters with requisite experience; disclosure and transparency; and effective exercise of shareholders' rights.

The three industry-specific corporate governance codes discussed above addressed corporate governance issues peculiar to the respective sectors at the time of their issuance which the 2003 SEC did not address. Furthermore, the 2003 SEC code lacked adequate provisions on other contemporary corporate governance issues. These include independent directors; critical board committees in relation to corporate governance; directors' appointment, tenure, remuneration and evaluation; ensuring the independence of the external auditors; whistle blowing procedures; sustainability issues;' and general disclosure and transparency issues. It was therefore quite obvious that there was a need to update the 2003 SEC Code. Thus on 1st April 2011, the Securities and Exchange Commission issued the Code of Corporate Governance in Nigeria which replaced the 2003 SEC Code.[258]

(D) **2011 to Date**: As already noted, as at 2011 there were four regulators who were active in the corporate governance scene. These are the Central Bank of Nigeria, the National Pension Commission, the National Insurance Commission and the Securities and Exchange Commission. Each of these issued a corporate governance code. Thus, since 2009 to this period, there are four corporate governance codes in force in the country. Of these four corporate governance codes, three of them (those issued by the Central Bank of Nigeria, the National Pension Commission and the National Insurance Commission) are industry-specific. They are applicable to the sector that the Commission concerned has authority. The corporate governance code issued by the Securities and Exchange Commission was applicable to all public companies registered in Nigeria irrespective of the sector in which such companies operated. Also, public companies were bound by the 2003 SEC Code whether they were listed on the stock exchange or not.

[258] *Ibid*

The SEC Code in force in Nigeria until 1st April 2011 was the 2003 SEC Code. However, on 1st April 2011, the Securities and Exchange Commission issued the Code of Corporate Governance in Nigeria 2011 (2011 SEC Code) which replaced the 2003 SEC Code. The making of the 2011 SEC Code commenced in September 2008 when the SEC constituted a National Committee, headed by Mr. M.B. Mahmoud, for the review of the 2003 SEC Code to address its weaknesses and to improve the mechanism for its enforceability. In addition, the Mahmoud Committee was mandated to 'indentify weaknesses in and constraints to good corporate governance, and to examine and recommend means of effecting greater compliance and to advise on other issues that are relevant to promoting good corporate governance practices by public companies in Nigeria, and for aligning the code with international best practices'. In 2009, the committee, after a thorough job, submitted its report together with a draft Revised Code of Corporate Governance to the SEC. After consultations with other regulatory bodies, the SEC at its 43rd meeting reviewed the draft code submitted by the Mahmoud Committee and introduced some amendments to it. In the same year, the SEC exposed a draft Revised Code of Corporate Governance to the public through the print media, and its 2011 SEC Code was released by the SEC with a commencement date of 1st April 2011.

The 2011 SEC Code is expected to be the minimum standards expected of public companies in Nigeria. The 2011 SEC Code has been adjudged to be quite comprehensive. Nevertheless, it is not a perfect document; it still contains some flaws. Interestingly, a few months after the 2011 SEC Code became operational, the Financial Reporting Council of Nigeria Act 2011 was enacted by the Federal Government. This statute has far-reaching provisions regarding the operation of companies in Nigeria. One of the areas the Financial Reporting Council of Nigeria was given express jurisdiction over is corporate governance. Accordingly, sections

23 (g) and 45 provide for the establishment of a Directorate of Corporate Governance for the Financial Reporting Council of Nigeria.

Sections 50 and 51 stipulate the objectives and functions of the Directorate of Corporate Governance of the Financial Reporting Council of Nigeria to be the following: developing principles and practices of corporate governance; promoting the highest standards of corporate governance; promoting public awareness about corporate governance principles and practices; act as the national coordinating body responsible for all matters pertaining to corporate governance; promote sound financial reporting and accountability based on true and fair financial statements duly audited by competent independent auditors; encourage sound systems of internal control to safeguard stakeholders' investments and assets of public interest entities; and ensure that audit committees of public interest entities keep under review the scope of the audit and its cost effectiveness, the independence and objectivity of the auditors. The Directorate of Corporate Governance of the Financial Reporting Council of Nigeria is further empowered to organize and promote workshops, seminars and training in corporate governance issues; issue the code of corporate governance and guidelines, and develop a mechanism for periodic assessment of the code and guidelines; provide assistance in respect of the adoption or institution of the code in order to fulfill its objective; and establish links with regional and international institutions engaged in promoting corporate governance.

It remains to be seen the impact the Financial Reporting Council of Nigeria Act would have on principles and practice of corporate governance in Nigeria. It is appropriate to expect so much from the Financial Reporting Council of Nigeria in view of the enormous powers vested on it by the Financial Reporting Council of Nigeria Act 2011.[259]

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[259] *Ibid*. p. 8.

CHAPTER FOUR

CORPORATE GOVERNANCE AND ADMINISTRATION: ACCOUNTABILITY TO STAKEHOLDERS

4.1 Introduction

The ultimate purpose of corporate governance is the provision of effective and accountable leadership with a view to enhance the realization of the organisation's overall mission. Corporate governance is characterized by transparency, accountability, probity and protection of shareholders' rights in respect to corporate bodies.[260] Thus, corporate governance is fundamental in enhancing investor confidence, promoting competitiveness and ultimately improving economic growth. The current interest[261] in corporate governance has arisen from three major developments including high profile scandals, globalization especially the increasing participation of institutional investors across national frontiers and increased shareholders activism.[262]

Corporate administration and financial audit remain the most important aspects of corporate governance that makes management accountable to stakeholders for its stewardship to a company. It is difficult to separate corporate financial reporting from corporate governance. There may be two reasons for this. First, shareholders have the right to receive information timely on the economic consequences of transactions entered into by the company and other events on the financial position and performance of the company. Therefore, timely

[260] R. Okpeahior and H.P. Faga, 'Reflection on Sound Corporate Governance for a Thriving National Economic Environment', *Ebonyi State University Law Journal,* Vol.2, No 1, (2007) p. 211.

[261] Although companies have been in existence for hundreds of years, the concept of Corporate Governance only emerged as a fully developed concept in the last 25 years. The unexpected collapse of notable UK companies like Ploy Peek International, Bank of Credit and Commerce, the Mirror Group News, Barring Bank, etc and the fall of energy giant Enron in US brought fully to the limelight the issues of Corporate Governance.

[262] Like the Arthur Anderson (Accounting firm) caught up in the Enron Scandal promoted recommendation for change by the New York Stock Exchange.

presentation of financial information, which reflects the economic consequences of transactions and events, is a part of good corporate governance. Secondly, high quality financial information helps the market to value the shares and other securities appropriately and thus strengthen the passive monitoring of the executive management by those who do not have control rights. As a result of the above, there has been an improvement in corporate governance due to right quality financial reporting. The place of financial reporting and auditing in the enhancement of good corporate governance cannot therefore be over-emphasized.

There are fundamental corporate principles that organizations like companies are expected to adhere to such as responsibility, accountability, transparency and fairness. The various codes of corporate governance such as the OECD Principles of Corporate Governance Code and the SEC Code of Corporate Governance in Nigeria emphasize the responsibility of directors who set the strategic direction of the organization within the framework of prudent controls and who employ, monitor and reward management.[263] Similarly, the board must be accountable to shareholders on the financial stewardship of the investment. Finally, with regards to transparency, companies are required to disclose accurate, adequate and timely information so as to allow investors to make informed decisions about the acquisition, ownership, obligations and rights as well as the sales of shares.[264]

The requirement for transparency is reflected in the obligations of financial reporting and auditing, narrative reporting and business review placed on the board of directors. At any rate, corporate responsibility is meant to be captured under Social and Environmental

[263] Shareholder activism is the use of voting right or the threat of the use of the voting right against board of directors to influence the decisions by the board at the general meeting.
[264] The New Central Bank of Nigeria, available at www.cenbank.org., visited on 3/04/2014.

Reporting and Sustainability/Development Reporting to be prepared and presented by board of directors during general meetings. [265] These obligations are however different from the fiduciary duties of directors.[266]

4.2 Administration of Companies in Nigeria

The operations and administration of companies in Nigeria is regulated by, among others, two major legal instruments, to wit: the Companies and Allied Matters Act (CAMA)[267] and the Investment and Securities Act (ISA).[268] We shall in due course discuss the relevant provisions of these instruments. Corporate governance structure is built upon the principal-agent relationship between shareholders and directors and or the management. Thus, the shareholders appoint the board of directors which set the business objectives and directions while the day-to-day running of the affairs of the company is conducted by the management led by the managing director. The board of directors thereafter becomes accountable to the shareholders otherwise referred to as the members in general meeting.[269] Under the Nigerian company law practice, the principal organs of a company are:

i. The board of directors, (including the officers / management)

ii. The shareholders / Members in General Meeting.

The Companies and Allied Matters Act is the major law regulating corporate governance in Nigeria. It provides pertinent mechanisms for corporate governance. These mechanisms include the appointment of directors by the company (members), removal of directors by means of ordinary resolution, duties and liabilities of directors, provisions for auditors and

[265] CAMA, Cap. C20 LFN 2010, ss.331, 342 and 357.
[266] CAMA, Cap. C20 LFN 2010, ss.279, 280 and 282.
[267] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010.
[268] Investment and Securities Act, Cap. I24, Laws of the Federation of Nigeria, 2010.
[269] N.C.S. Ogbuanya, *Essentials of Corporate Law Practice in Nigeria*, (Lagos: Novena Publishers Ltd., 2010), p.321.

audit committee, minority protection, investigation of companies and mandatory involvement of shareholders in critical corporate decisions such as taking resolutions to increase or reduce authorized share capital[270], to restructure the company[271] and even for the conversion or re-registration of the company[272].

Besides the Companies & Allied Matters Act and the Investment and Securities Act, the Code of Corporate Governance in Nigeria which was published by SEC in 2011 came into operation to regulate the activities of companies. The provisions of this code are designed to bring to the fore the principles of transparency, accountability and fairness in the running of the affairs of a company. Given its voluntary character, the SEC Code however, plays only a complementary role to the provisions of the Investments and Securities Act[273] and the Companies & Matters Act[274], which Acts largely contain the provisions of the SEC Code of 2011.

The board of directors and members in general meeting play significant roles in the governance of companies in Nigeria. The board of directors exercises management power in the company while some corporate decisions such as the alteration of the memorandum and articles of association as well as appointment of new directors cannot be taken without the resolution of members in General Meeting.[275]

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[270] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, ss. 102 and 105.
[271] Investment and Securities Act, Cap. I24, Laws of the Federation of Nigeria, 2010, Part XII.
[272] CAMA, Cap. I24, Laws of the Federation of Nigeria, 2010. ss. 50-53.
[273] Cap. I24, Laws of the Federation of Nigeria, 2010.
[274] Cap. C20, Laws of the Federation of Nigeria, 2010.
[275] Y.H. Bhadmus, *Bhadmus on Corporate Law Practice*, (Enugu: Chenglo Limited, 2009), p.158; Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria (LFN), 2010, ss. 63(3), 44-46 and 248.

4.2.1 The Directors of a Company

The directors are persons duly appointed by the company to direct and manage the business of the company.[276] The definition of a director is enlarged to include a shadow director, i.e. a person on whose instruction and directions the directors are accustomed to act.[277] While directors of a company are not servants of the company, the managing director and executive directors are servants of the company.[278] There is a rebuttable presumption in favour of any person dealing with the company that all persons who are described by the company as directors have been duly appointed.[279]When there are persons who are conducting the affairs of the company in a manner which appears to be perfectly consonant with the articles of association, those so dealing with them externally are not to be affected by any irregularities which may take place in the internal management of the company.[280] Thus, any person dealing with a company represented by this category of officials can rightly assume that all the conditions in the memorandum and articles of association of the company have been fulfilled by this category of top officials.[281]

Where a person not duly appointed as director acts as such on behalf of the company, his acts shall not bind the company and he shall be personally liable for such act unless the company

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[276] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s.244(1). *Baffa v Odili* (2001)15 NWLR (pt. 737) 709 at 737; *Olufosoye v Takorede* (1993)1 NMLR (pt. 272) p. 747; *Longe v F.B.N. Plc* (2010)6 NWLR (pt. 1189) p. 1.

[277] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 245(1).

[278] *Yalaju Amaye v. Associated Real Estate & Investment Co. Ltd* (1990) 4 NWLR (pt. 145) 422.

[279] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 244(2), See also ss. 68 and 69 CAMA on abolition of the rule of constructive notice and the enactment of the rule of presumption of regularity.

[280] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s.69; *Royal British Bank v Tarquand* (1856) 6 E&B 327.

[281] MTN (Nig.) *Communication Ltd. v Corporate Communication Investment Ltd*. (2015) 7 N.W.L.R. (Pt.1459) p.437 at 446.

is shown to have held him out.[282] In order to defeat the effect of s. 244(2), a member can seek the order of the court to restrain both the company and such a person from being paraded as a director.[283] The state of mind of the directors is the state of mind of the company and is treated by the law as such.[284] Note that where a person gives advice in his professional capacity which a director acts it does not make him a shadow director.[285]

4.2.1.1 Appointment of Directors

The Companies and Allied Matters Act specifies the categories of persons that should not be allowed to occupy the position of a director, being a sensitive office that requires dedication to duty and integrity. Therefore, the following persons are disqualified from being appointed company directors in Nigeria:

a. an infant, that is, a person under the age of 18 years;
b. a lunatic or person of unsound mind;
c. a person disqualified under ss. 253, 254 and 258 of CAMA; or
d. a corporation other than its representative appointed to the board for a given term.[286]

[282] *Ibid*, s. 244(3). *Longe v. F.B.N Plc* (2010)6 NWLR (pt. 1189) p. 1.
[283] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s.250.
[284] *Bolton (Engineering) Co. Ltd v Graham and Sons* (1957) I QB 159; *Delta Steel (Nig) Ltd v. A.C.T Incorporation* (1999)4 NWLR (pt. 597)53 at 163.
[285] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s.245(1) & (2); *Re Forest of Dean Coal Mining Co.* (1878)10 Ch.D 450.

[286] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 257 CAMA. Note: s. 253 talks about insolvent person. S.254 is about fraudulent person. S. 258 stipulate grounds of vacation of office by director.

Note further that a regulatory agency is permitted by law to set out other qualifications of a person who can be appointed a member of the board of directors in certain companies.[287]

4.2.1.2 Removal of a Director from Office

The articles or the service contract appointing a director usually provide for his removal from office. A company may however by ordinary resolution of which special notice must have been given remove a director before the expiration of his period of office, notwithstanding anything in its articles or any agreement between it and him.[288] A life director can still be removed under this section.[289] A life director is only protected from the application of retirement and rotation rules.[290] At the end of every year, during annual general meeting, one third of the number of directors who are the longest serving directors will retire and new directors will be appointed. This is the principle of rotation of directors. The life director is exempted from the application of this principle. A shadow director need not be removed formally since he was not formally appointed. Once the directors are no longer accustomed to act on his instructions, he is deemed to have been removed. A person ceases to occupy any executive positive such as managing director, executive director, etc the moment he is removed as a director. However, if a person is merely removed from any executive capacity as managing director, it does not affect his membership in the board of directors.[291] Any protective clause capable of restricting the powers of the members to remove a director is void and unenforceable. The issue of removal of a director is a special business that can be transacted at extra-ordinary general meeting, which can even be requisitioned by the members of the company. Any director so removed is entitled to compensation or damages

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[287] *Ibid*., s.251(2) and (3).
[288] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s.262.
[289] *Ibid*., ss.255 and 262.
[290] *Ibid*., S. 259(10 & (2) CAMA.
[291] *Yalaju Amaye v AREC, supra*.

for the termination of his appointment as a director or any other appointment terminating with that of a director e.g. managing director, or as derogating him from any power to remove a director which may exist apart from the foregoing.[292] Life Director obtains prevailingly in private companies as a means of retaining control by being a member of the board of directors for a long time. Note that a life director is also subject to vacation of office if any of the conditions occur;

(a) If he ceases to be a director by virtue of s. 251 share qualification of this Act; or

(b) If he becomes bankrupt or makes any arrangement or composition with his creditors generally; or

(c) If he becomes prohibited from being a director by reason of any order made under s. 254 of this Act; or

(d) If he becomes of unsound mind; or

(e) If he resigns his office by notice in writing to the company.[293]

A vacancy created by the removal of a director can either be filled at the meeting at which he is removed or may be filled as a casual vacancy.[294] The person appointed in place of a director removed can only serve for the remaining period of the tenure of the director he replaced. In other words, he retires at the time the director removed would have retired but for the removal.[295]

4.2.1.3 Duties of a Director

[292] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s.262(6).
[293] *Ibid*., s. 258(1)
[294] *Ibid*., s.262(4).
[295] *Ibid*., s.262(5).

Directors are the most important officers of the company, and they constitute an organ of the company invested with the power of administration of the company. The duties are the obligations the directors owe the company, and they arise from the nature of the relationship between the directors and the company. Directors are trustees of the company's moneys, properties and their powers. Therefore, they are expected to account for all the monies over which they exercise control and shall refund any moneys improperly paid away. The director are obliged to exercise their power honestly in the interest of the company and all the shareholders, and not in their own or sectional interests.[296] The director owes fiduciary duties to the following persons:

i. The company (the directors must observe utmost good faith in any transaction or dealings with or on its behalf).
ii. Shareholders (when directors are acting) as agents to shareholders.
iii. Shareholders (in any transactions affecting his interest).
iv. Any person dealing with the company's securities.[297]

The duties of directors are imposed on them as individual directors or as a board and the duties include the following:

a. Duty to act bona fide for the best interest of his company.
b. Duty to exercise power for proper purpose.
c. Duty not to fetter discretion to vote in a particular way.
d. Duty not to make secret profits by appropriating corporate assets or opportunities.
e. Duty not to allow personal interest with duty.
f. Duty to observe utmost good faith.

[296] *Ibid.*, s.283(1).
[297] *Ibid.*, s.279(2).

The duties are enunciated as follows:

(a) Duty to Act *Bona Fide* for the Best Interest of his Company

A director shall act at all times in what he believes to be the best interest of the company as a whole so as to preserve its assets, further its business, and promote the purposes for which it was formed. The director is also expected to perform his duties in such a manner as a faithful, diligent, careful and ordinarily skilful director would act in the circumstances. In the instance case, the Supreme Court held that the directors of a company must in the exercise of the management power and duties conferred upon them by s. 63(3) CAMA, adhere strictly to the statutory provisions which enjoins them to consider the interest of the company as paramount. It appears there can be no breach of duty if the director honestly believes they are acting in the interest of the company. However, where it is clear that the act or omission of a director resulted in a substantial detriment to the company, the court will most likely hold the director culpable for breach of duty.[298]

(b) Duty to Exercise Power for Proper Purpose

Directors are enjoined to exercise their powers for the purpose for which it is specified and shall not do so for a collateral purpose. Once the power is exercised for the right purposes, it does not constitute a breach of duty even if it incidentally affects a member adversely.

[298] CAMA, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 279(3); *Artra Industries Nigeria Ltd v. Nigerian Bank for Commerce and Industry* (1998) 4 NWLR (Pt. 546) p. 375.

Accordingly, directors are not entitled to use their power of issuing shares merely for the purpose of maintaining their control over the affairs of the company.[299]

(c) Duty Not to Fetter Discretion to Vote in a Particular Way

Directors should not fetter his discretion to vote in a particular manner without the consent of the company. This is because the director is in the circumstance a trustee where as the company is the beneficiary. Therefore, if a director makes an agreement among other directors with shareholders or outsiders to vote in a particular way at the Board meetings, that agreement shall be invalid even if it was made in good faith.[300]

(d) Duty Not to Make Secret Profits by Appropriating Corporate Assets or Opportunities

A director must not make any secret profit or achieve other unnecessary benefits. A director is not supposed to use his position as director to engage in other businesses where he has personal interest. Note that the omission of duties or responsibilities under company's articles or memorandum shall not present a defence to any breach of duty. A director must avoid conflict of interest and making of secret profits. A company can, by its articles, permit a director to contract with its company. However, the director must comply with the provisions of s. 277 CAMA in respect of disclosure of interests in the contract. The director's personal interest must not conflict with any of his duties, and he must not make any secret profit or

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[299] CAMA, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 279(5); *Piercy v. S. Mills & Co. Ltd* (1920) 1 Ch. 77 84; *Punt v. Symons & Co.* (1903) 2 Ch. 506.
[300] CAMA, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 279(6).

achieve other unnecessary benefits in the course of management of the affairs of a company or in the utilization of the company's property. [301]

(e) Duty Not to Conflict Duty and Interest

The personal interest of a director shall not conflict with any of his duties as a director. Thus, directors are not supposed to use their position as director to involve themselves in activities including businesses where they have interest. However, the inability or unwillingness of the company to perform any functions or duties under its articles and memorandum shall not constitute a defence to any breach of duty of a director.[302]

(f) Duty to Observe Utmost Good Faith

The law requires every director of a company to exercise the powers and discharge the duties of his office honestly, in good faith and in the best interest of the company, and shall exercise that degree of care, diligence and skill which a responsible, prudent director would exercise in comparable circumstances. This is an improvement over the common law position that a director need not exhibit the performance of his duties with a greater degree of skill than many reasonably are expected from a person of his knowledge and experience. This is a subjective standard envisaged under the common law. The position under CAMA imposed

[301] CAMA, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 280(1) and (4); *Boston Deep Sea Fishing Co. v. Ansell* (1888) 39 Ch. D 339. Here, a director of a company who contracted, on behalf of the company, for the building of fishing smacks received a commission on the contract from the ship builders without disclosing to the company. The director was also a shareholder in an ice company which aside from paying dividends paid to shareholders who were owners of fishing smacks and who employed the ice company in supplying ice to the fishing smacks. The director employed the ice company in respect of his company's fishing smacks and also received the bonus. The directors were liable to account to the company for the commission and the bonus notwithstanding the fact that the bonus could never have been received by the company because it was not a shareholder in the ice company. See also *Regal (Hastings) Ltd v. Gulliver* (1967) 2 A.C. 134.
[302] CAMA, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 280(4)

the objective professional standard which is commensurate with the enormity of power of directors embodied in s. 63(3) CAMA.[303]

4.2.2 The Shareholders: Rights and Obligations

Shareholders are proportionate owners of interest in a company. Their proprietary interest is determined by the number of shares they respectively have in a company. Accordingly, the members of a company are the subscribers to the memorandum and persons who, from time to time, agree to become members of a company, and whose names have been entered in the company register of members.[304] As a condition precedent, a shareholder must have at least one share. The subscribers are also required to take up at least 25% of the authorized share capital of a company.[305] Suffice it to say that a share is a unit of the rights and obligations in a company. On the rights of shareholders, section 114 of CAMA provides that subject to the provisions of CAMA, the rights and liabilities attaching to the shares of a company shall:

a. be dependent on the terms of issue and of the company's articles, and that
b. notwithstanding anything to the contrary in the terms of issue or the articles include the right to attend any general meeting of the company and vote at such a meeting.

By this provision, two rights enjoyed by shareholders viz right to vote and right to attend meeting are identified.[306] It made right to attend meeting an absolute right as nothing in the articles of association or terms of issue can prejudice this right of a shareholder to attend

[303] CAMA, Cap. C20, Laws of the Federation of Nigeria, 2010, s. 280(1); *Re City Equitable Fire Insurance Company* (1925) Ch. 40.
[304] Companies and Allied Matters Act, *op. cit.* s.79.
[305] Companies and Allied Matters Act, *op. cit.* s.27(2)(b).
[306] *Pender v Lushington* (1877) 6 Ch.D 70.

general meeting. According to Orojo,[307] other rights usually ascribed to shareholders include: the right to dividends if any, right to participate in distribution of assets in the event of winding up of the company, right to receive notice of general meetings, right to receive a copy of the memorandum and articles and every balance sheet to be laid before the general meeting, right to inspect and obtain copies of minutes of general meetings, and right to petition for a remedy under Part X of CAMA which provides generally for the protection of minority against illegal and oppressive conduct. For the purpose of this study, right to vote, right to attend meetings, right of action and special right of minority shareholders shall be given a detailed attention.

4.2.2.1 Right to Attend General Meeting

The right of shareholder to attend general meeting is one that is without any qualification. Of course, the right necessarily includes the right to get notice for the meeting. By virtue of section 277 (1) of CAMA, 'any member of a company (shareholder) entitled to attend and vote at a meeting of the company shall be entitled to appoint another person (whether a member or not) as his proxy to attend and vote instead of him, and a proxy appointed to attend and vote instead of a member shall also have the same right as the member to speak at the meeting. Nevertheless, unless the article of association otherwise provide, a member entitled to attend and vote at a meeting of the company may do so by proxy shall not apply in the case of a company not having a share capital.[308] Also, in every notice[309] calling a meeting of a company having a share capital, there shall appear with reasonable prominence a

[307] J.O. Orojo, *op. cit*., p. 125.
[308] Companies and Allied Matters Act, *op. cit*., the proviso to section 230(1).
[309] The notice required for all types of general meetings from the commencement of CAMA shall be 21 days from the date on which the notice was sent out in accordance with section 217 of the Act. Also, a notice may be given by the company to member either personally or by sending it by post to him or his registered address. This is provided by section 220 of CAMA. And a failure to give notice to a person entitled to receive shall invalidate the meeting unless such failure is an accidental omission on the part of the person or persons giving the notice as provided in section 221 of CAMA.

statement that a member entitled to attend and vote is entitled to appoint a proxy or where that is allowed, two or more proxies, to attend and vote instead of him, and that a proxy need not be a member.[310]

4.2.2.2 Right to Vote

The voting right attached to every ordinary shareholder is of more importance to corporate governance. It is trite fact that in every company which has a conventional capital structure, every shareholder has a right to have a say in the corporate decision making process by virtue of his shareholding. An ordinary share usually confers on its holder the right to cast one vote[311] on all matters put to vote at shareholders meetings.[312] In the case of *North West Transportation Company Ltd v Beathy*,[313] it was held that subject to contrary provision in the article of association, every shareholder has a right to vote on any matter or question irrespective of whatever personal interest he might have in the subject matter and that the shareholder could cast votes as he thought fit. It is essential to note that today's corporate governance environment calls for more shareholders participation and exercise of their voting right often referred to as the voice, a vital tool in exercising control over persons who are managing their money.[314]

4.2.2.3 Right of Action

Companies and Allied Matters Act avails the shareholders the right to the following judicial remedies for breaches of directors' duties: Where however, a member institutes a personal

[310] Companies and Allied Matters Act, *op. cit*.,S. 230 (2).
[311]CAMA has prohibited both non-voting and weighted shares except as provided in the Act. According to section 116 (1) (a) of CAMA, 'any shares by a company after the commencement of the Act shall carry the right on a poll at a general meeting of the company to one vote respect each share.
[312] O. Ojo, *et al* (eds), *Cross-cutting Issues in Nigeria Law: Essay in Honour of Prof. Funso Adaramole* (Lagos: Showers IMC Press, 2007) p. 177.
[313] (1887) 12 AC 589, cited with approval in *Burland v Earle* [1902] AC 83 PC.
[314] Companies and Allied Matters Act, *op. cit*., ss. 81.

action to enforce a right due to him personally, he shall not be entitled to any damages but to declaration or injunction to restrain the company and/or the directors from doing a particular act.[315]

a. Actions in restitution to recover secrete profit.[316]
b. Action in damages and compensation, e.g. in the case of *Georgewill v Ekinne*,[317] a director was held liable in damages for diverting and misappropriating company funds for her personal benefit.
c. Action in the name and on behalf of the company if the board of directors refuses or neglect to do so.[318] The case of *Ladejobi v Odutola Holdings Ltd*[319] is relevant here. In this case, the respondents sought among other things, a declaration against the convening of the meeting by the directors of the respondent company which adversely affected their respective rights in the company. The action succeeded.
d. Restoration of company's property: Section 284 of CAMA prohibit substantial property transaction involving directors or person connected to him and such transaction entered into shall be regarded as voidable at the instance of the company.[320]
e. Winding up proceedings on just and equitable ground[321] A shareholder may, pursuant to section 507 of CAMA, institute misfeasance proceedings in a winding up proceeding against directors who have misapplied company funds or in breach of duty in relation to the company. For a winding up petition to be based on just and equitable ground or clause in section 408(e) of the Companies and Allied Matters Act, Cap.

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[315] *Ibid*., s.301.
[316] *Ibid*., ss. 300 (f) and 280(3).
[317] [1998] 9 NWLR (pt 562) p. 454 cited by O. Olo, *et al*, *op. cit*, p. 177.
[318] Companies and Allied Matters Act, *op. cit*., s. 300 (d).
[319] [2003]. 3 NWLR (Pt.753) p. 121.
[320] See section 285 for exceptions to section 284 of the Companies and Allied Matters Act.
[321] Companies and Allied Matters Act, s. 408 (e).

C20, LFN 2010, the petitioner is required to proffer unchallenged or uncontroverted credible evidence. The issue of alternative remedy is of keystone importance to winding up actions on this ground. The court invited to wind up a company under the just and equitable clause in section 408 (e) of the Companies and Allied Matters Act read with section 312 thereof must be satisfied by the petitioner as a matter of utmost necessity, that there is no other legal remedy to save the life of the company before proceeding to entertain and grant the petition putting to death the company in question.[322]

f. Relief on the ground that the affairs of the company are being conducted in an illegal or oppressive manner.[323]

g. A shareholder has a right to apply to Corporate Affairs Commission to investigate the company's affairs.[324]

4.2.2.4 Protection of Minority Shareholders

The rights of shareholders discussed above are generally described as individual rights of membership. They are attached personally to the status of membership. They are protected by law and the company cannot lawfully deprive the shareholder of their enjoyment.

However, in addition to purely individual membership rights, there are qualified minority rights, that are rights that can be exercised not by a single individual but by a number of

[322] *First Equity Securities Ltd v. Anozie* (2015) 12 N.W.L.R. (Pt. 1473) p. 337 at 342

[323] This relief is provided in section 311 of CAMA.

[324] Companies and Allied Matters Act, *op. cit*, ss. 314 and 315. Note that the Corporate Affair Commission is empowered to appoint investigator to investigate the affairs of a company. If an application supported by evidence showing good reasons is made by the company or members holding not less than one third ($^1/_3$) of the shares issued.

individual members acting in co-operation, for example, by a resolution.[325] These rights are referred to as corporate membership rights. The rights of minority shareholders are statutorily protected to protect them from arbitrary resolutions by majority shareholders.

It is trite and thus a settled law that once a decision has been taken at a general meeting with full compliance to procedures like quorum and notices, no member can challenge such decision in the court of law.[326] Decision whether affecting the company, the members or outsiders are generally taken by the majority vote of members. Thus, where a wrong is done, even to the corporate right of a member, it is the majority of members that will decide whether it should be treated as a wrong which should be redressed or whether it will be overlooked and the majority can validly decide not to redress such wrong. This is the principle laid down in the case of *Foss v Harbottle*.[327] This common law rule has been incorporated in section 299 of CAMA. In spite of the above rule, section 300 of CAMA provides exceptions to the rule in the interest of justice. So, minority shareholders still have the right to challenge the decision of majority shareholders in the following grounds:

i) Where the company enters into any transaction which is illegal or *ultra vires;*
ii) Where the company purports to do by ordinary resolution any act which by its constitution or the act required to be done by special resolution;
iii) Where the company commits any act or omission affecting the applicant's individual right as a member;
iv) Where fraud is being committed on either the company or the shareholders themselves and the directors failed to take appropriate action to redress the wrong.

[325] J.O. Orojo, *op. cit*, p. 205.
[326] *Foss v Harbottle* [1843] 2 KB 46.
[327] *Supra;* J.O. Orojo, *op. cit*. pp. 208-209.

v) Where a company meeting cannot be called in time to be of practical use in redressing a wrong done to the company or minority shareholders among others.

vi) Where the directors are likely to derive a profit or benefit, or have profited or benefited from their negligence or from their breach of duty.[328]

The decision of Megarry VC in the case of *Estmanco (Kilner House) Ltd v Greater London Council*[329] is very instructive on the protection of minority shareholders' rights. In that case, the majority shareholders wished to deprive the company of a right of action under a contract, and proposed and carried a resolution to that effect. A minority shareholder brought an action on behalf of the company to prevent this. In his judgment, Megarry stated thus:

> Plainly that there must be some limit to the power of the majority to pass resolutions which they believe to be in the interest of the company and yet remain immune from interference by the courts. It may be in the best interest of the company to deprive the minority of some of their rights or some of their property, yet I do not think that this gives the majority an unrestricted right to do this, however unjust it may be or however much it may harm shareholders whose rights as a class differ from those of the majority.

It is regrettable to note that the protection of shareholders rights, including minority shareholders, has been a serious challenge for developing, maintaining and implementing effective and efficient corporate governance system in many third world countries. In Nigeria, for instance, it is revealing that series of laws that exist to protect minority shareholders' rights are not being strictly enforced due to the adverse interests and influence of overwhelming shareholders who often constitute the board of directors.

[328] Companies and Allied Matters Act, *op.cit*., s. 300.
[329] [1982] IALL ER 437

4.2.2.5 Obligations of Shareholders

Where there is a right, there is a corresponding obligation. The obligation of a shareholder comprises primarily the payment of their shares whenever a call is made and to contribute to the assets of the company in the event of the company being wound up. The obligation to contribute to the assets of a company however, depends on the extent of the liability of members in a company as stipulated in the memorandum of association of a company, i.e. either limited by shares, limited by guaranty or unlimited.

4.2.3 The Organic Theory in Company Management

The organic theory recognizes the separate legal personality of a company with particular attention on its artificial nature. The company, being an artificial legal person therefore, carries out its business activities through human elements institutionalized as the organs of the company. A company is designed by law to act through its members in general meeting or its board of directors or through officers or agents, appointed by, or under authority derived from the members in general meeting or the board of directors.[330]

It is pertinent to identify a member of a company and a director of a company. The subscribers of the memorandum of a company shall be deemed to have agreed to become members of the company and on incorporation of the company will have their names entered as members in the register of members.[331] Every other person who agrees in writing to become a member of a company, and whose name is entered in its register of members, shall be a member of the company.[332] In the case of a company having a share capital, each

[330] Companies and Allied Matters Act, *op.cit.*, s.63(1).
[331] *Ibid.*, s. 79(1).
[332] *Ibid.*, s. 79(2); *Alalade v. Northline Ind. & Agric Serv. Ltd*. [2003] 14 NWLR P.172 AT 175.

member shall be a shareholder of the company and shall hold at least one share.[333] Membership may also include any person financially interested in the company.[334] It also includes the heir, executor, administrator or other personal representative, as the case may be, of the member.[335] However, a person of unsound mind as declared by the court, an undischarged bankrupt and a corporate body in liquidation shall not be capable of becoming a member of a company. Besides, a person under the age of 18 years shall not be counted for the purpose of determining the legal minimum number of members of a company.[336]

The directors, on the other hand, are persons duly appointed by the company to direct and manage the business of the company.[337] The first directors are usually appointed by the subscribers to the memorandum. Subsequent directors are duly appointed by the members in a general meeting who stand to increase or decrease the number of directors.[338]

4.2.3.1 Exercise of Authority by Directors Vis-a-vis the General Meeting

The traditional corporate jurist held the view that ultimate control of the affairs of a company rest on the members in a general meeting. This view dwarfed the position of directors as mere agents of the company prone to be removed at any time. This view was overtime held up to derision as it was capable of being exploited by unbridled members to bleed the company to death.[339] Any act of the members in general meeting, the board of directors or of a managing director while carrying on in the usual way the business of the company shall be reputed as

[333] Companies and Allied Matters Act, *op.cit.*, s.79(3).
[334] *Ibid.*, s. 46(11).
[335] *Ibid.*, s. 567.
[336] *Ibid.*, s.80.
[337] *Ibid.*, s.244.
[338] *Ibid.*, ss.247-249.
[339] *See Isle of Wright Railway Co. v. Tahourdin* (1883) 25 Ch. D 320.

the act of the company itself. Accordingly, the company shall be criminally and civilly liable thereof to the same extent as if it were a natural person.[340]

The new trend tilts in favour of the board of directors wielding much more authority in terms of controlling the affairs of the company. Undoubtedly, the respective powers of the members in general meeting and the board of directors shall be determined by the company's articles.[341] The power of managing the company is also vested on the board of directors.[342] The provisions of s. 63 CAMA seem to pontificate that if the articles of association give directors the power to manage the company and do all such things as are not by the Act or the articles required to be exercised by the members in general meeting, then the members are forbidden from interfering in the exercise of such powers.[343] Obviously, the members in general meeting cannot give directives on how the affairs of the company are to be conducted. Accordingly, unless the articles shall otherwise provide, the board of directors when acting within the powers conferred upon them by CAMA or the articles of association, shall not be bound to obey the directions or instructions of the members in general meeting.[344] Therefore, the d acts of the directors in conducting the business of the company cannot lightly be overruled by the members in general meeting. However, the members in

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[340] Companies and Allied Matters Act, *op.cit*., s. 65; *C. B. Ltd. v Intercity Bank Plc* (2009) 15 NWLR (pt. 1165) p. 445 at 450.
[341] Companies and Allied Matters Act, *op.cit*., s. 63(2).
[342] Companies and Allied Matters Act, *op.cit*., s63(3).
[343] *Ibid*., s. 63(4); In the case of *Shaw & Sons Salford Ltd. v. Shaw* (1935) 2 KB 113, members in general meeting resolved that proceedings which has been instituted by the directors in the company's name be discontinued. The articles had clearly delegated management of the affairs of the company to the directors. The court therefore held the resolution of the general meeting invalid. The same position was earlier assumed by the court in *Automatic self-Cleaning syndicate Co. Ltd. v. Cunninghan* (1906) 2 Ch. 34. Here, the company's articles of association vested the management of the business and the control of the company in the directors. The articles of association of the company also specifically empowered the directors to sell any property of the company on their own determined terms and conditions. The members in general meeting subsequently passed a resolution directing the board of directors to sell the company's undertaking to a new company specifically formed for that purpose. The directors however disapproved this resolution in pursuance of the provision of the articles of association of the company adumbrated earlier. The court held that the member in general meeting could not compel the board of directors to act contrary to the stipulations of the articles. The modern rule therefore appears to give strength to the terms of Table A of the Companies &Allied maters Act which sets out a typical example of the articles of association.
[344] Companies and Allied Matters Act, *op.cit*., s.63(4).

general meeting still have reserved power to exercise control over the directors where they appear to manage the affairs of the company in a manner oppressive to the members of the company. The reserved powers are to the effect that the members in general meeting may:

(a) Act in any matter if the members of the board of directors are disqualified or are unable to act because of a deadlock on the board or otherwise;
(b) Institute legal proceedings in the name and on behalf of the company if the board of directors refuse or neglect to do so;
(c) Ratify or condemn any action taken by the board of directions; or
(d) Make recommendations to the board of directors regarding action to be taken by the board.[345]

Apart from the foregoing, the members in general meeting can in myriad of other ways exercise control on the directors even if the exercise of control is indirect. Thus, it is possible for the members in general meeting to remove a recalcitrant director by ordinary resolution. It is immaterial if the said director was appointed for life.[346] Besides, the members can, through special resolution, amend the articles to curtail the powers of the board of directors. However, no alteration of the articles of association of the company shall invalidate any prior act of the board of directors which would have been valid if that alteration had been made.

It need be stated at this juncture that beyond the roles played by the organs of a company i.e. the board of directors, acting through the managing director and the members in general meeting, the Companies and Allied Matters Act established the Corporate Affairs Commission (CAC) as a regulatory body over the affairs of companies in Nigeria.[347] The CAC is charged, among others with the administration of the Companies and Allied Matters

[345] Companies and Allied Matters Act, *op.cit.*, s.63(5); *Odutola Holdings Ltd. v. Ladejobi* (2006) M. J. S. C. P. 70 at 73.
[346] Companies and Allied Matters Act, *op.cit.,* s.62.
[347] *Ibid.,* s.1.

Act, including the regulation and supervision of the formation, incorporation, registration, management and winding up of companies. It is also mandated to perform other functions specified by any Act or enactment, and to undertake other activities as are necessary or expedient for giving full effect to the provisions of this Act. Of more striking in advancing corporate governance is the role of CAC in investigating into the affairs of companies. Accordingly, the CAC is empowered to arrange or conduct an investigation into the affairs of any company where the interest of the shareholders and the public so demand.[348] In the event of dispute however, the Federal High Court shall have and exercise jurisdiction to the exclusion of any other court in civil causes and matters arising from the operation of the Companies and Allied Matters Act or any other enactment replacing that Act or regulating the operation of companies incorporated under the Companies and Allied Matters Act.[349]

4.2.3.2 Lifting the Veil of Incorporation to Attach Civil and Criminal Liabilities

The trite rule underlying the operations of companies is that a company, upon incorporation, has its own legal identity distinct from that of its shareholders. Thus, if a company gets sued, only the assets of the company can be sequestrated to satisfy the debt of the company pursuant to a judgment. The implication is that if a company is insolvent, its debts may well go unsatisfied. The creditors cannot go beyond the properties of the company to attach the assets of the individual shareholders. This is predicated on the concept of separate legal personality which cloaks corporate veil over the company.[350] Consequently, one is not entitled to go behind this veil. However, since a statute will not be allowed to be used as a vehicle of fraud or to justify illegality thereby occasioning grave injustice on unsuspecting public, the court, in certain exceptional circumstances, would have to lift, pierce or crack the

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[348] Companies and Allied Matters Act, *op.cit*., s.7
[349] Constitution of the Federal Republic of Nigeria, 1999 (as amended) s. 251(1)(e).
[350] Companies and Allied Matters Act, *op.cit*., s.37; *Salomon v Salomon & Co. Ltd* (1877) AC 22; *Habib (Nig) Bank Ltd. v Ochete* (2001) 3 NWLR (pt. 699) 114.

veil of incorporation to look behind the corporate personality and examine the reality of the prevailing situation.

(a) Lifting the Veil under Case Law

The separate personality principle of the company cannot be allowed by the courts as a cloak for fraud or dishonesty. In other words, were it is evidenced that a company was defrauding impressionable persons, the company and the individuals may be treated as both one and the same person.[351] The occasions where the veil of incorporation would be lifted are when the company is liable for perpetration of fraud, carrying out improper conduct/unfair act, carrying out act capable of defeating the aim of law and/or evading legal obligation.

The consequence of recognizing the separate personality of a company is to draw a veil of incorporation over the company. One is therefore generally not entitled to go behind or lift this veil. However, since a statute will not be allowed to be used as an excuse to justify illegality or fraud, it is in the quest to avoid the normal consequence of the statute which may result in grave injustice that the court, as occasion demands, have to look behind or pierce the corporate veil. Accordingly, allegation of fraud lifts the veil of corporate associations and unmasks the face of the suspected criminal to face prosecution. Where the veil is lifted, the law would go behind the corporate entity so as to reach out to individual members of the company whose conduct or act is criminally reprehensible.[352]

(b) Lifting the Veil under the Statute

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[351] *Gilford Motors Co. Ltd. v. Horne* (1933) Ch. 935, In this case, Horne, a former employee of the plaintiff company attempted to avoid a restrictive covenant claiming that as a person he might be bound by the restraint but the company being a separate entity may not be so bound. The court described the company as a device, a stratagem and a mere cloak or sham, and therefore cracked the corporate veil. See also *Adeyemi v. Lan and Baker (Nig.) Ltd & Anor* (2000) 7 NWLR (pt. 663): 33.

[352] *Oyebanji v State* (2015) 14 N.W.L.R. (PT.1479) p.270 at 275; *Alade v Alic (Nig.) Ltd*. (2010) 19 N.W.L.R. (Pt. 1226) 111; Ciminal Code Act, Cap. C38, Laws of the Federation of Nigeria, 2010, s.35.

Circumstances under which corporate personality could be disregarded under the Companies & Allied Matters Act are as examined hereunder:

(i) **Company's Membership Falls below the Prescribed Minimum**: Where a company carries on business without having at least two members and does so far more than 6 months, every director or officer of the company during the time that it so carries on business after those 6 months shall be liable jointly and severally with the company for the debts of the company contracted during that period.[353] At the expiration of the statutory six months period, a company cannot however avoid a lifting of the veil by appointing a director to make up the required minimum number of directors, with the attendant share qualification which invariably adds to the membership.[354]

(ii) **The Number of Directors Gets Less Than Two**: Where the number of directors fall below two, any director or member of a company who knows that a company carries on business after the number of directors has fallen below two for more than 60 days shall be liable for all liabilities and debts incurred by the company during that period when the company so carries on business.[355]

(iii) **Fraudulent Trading**: Where, in the course of winding up (liquidation), it appears that any business of the company has been carried on in a reckless manner or with intents to defraud creditors of the company or creditors of any other person for any fraudulent purpose, the court may declare that any persons who were knowingly

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[353] Companies and Allied Matters Act, *op.cit.*, s.93. It has been held that this provision of the law does not create any offence but merely admits the defaulting persons named therein to personal liability; *Iro v. Park* (1972) 12 SC 93.

[354] *Fadipe v. the Manager, UBA* (1973) F R C R 15.

[355] Companies and Allied Matters Act, *op.cit.*,s. 246(3) CAMA. Note that the liability contemplated under this section is not restricted to debts incurred by the company during the period but all other liabilities.

parties to the carrying on of the business in the said manner shall be personally responsible for any of debts or other liabilities of the company in accordance with the directive of the court. Note that the court can only make such declaration upon an application of the official receiver or the liquidator or any creditor or contributory of the company.[356] This provision does not however, overrun the guilt or otherwise of the criminal offence constituted by the act of the defaulting persons.

(iv) Personal Liability of Directors: There is no law that forbids a company from receiving money by way of loan for specific purpose, or receiving money or other property by way of advance payment for the execution of a contract or project. However, where the company with intent to defraud, fails to apply the money or other property for the purpose for which it was received, every director or other officer of the company who is in default shall be personally liable to the party from whom the money or property was received for a refund of the money or property so received and not applied for the purpose for which it was received. The foregoing nonetheless, does not affect the liability of the company.[357] The foregoing provision is designed to prevent diversion of money borrowed from financial institutions or from individuals by means of debenture from purposes for which they were received. The provision also affords wider remedy to third parties dealing with the company. The condition precedent for invoking the application of this provision is the establishment of fraudulent intent. Therefore, innocent misapplication of fund borrowed in situations honestly believed to be in the best interest of the company would exonerate defaulting directors or officers from personal liability.[358]

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[356] Companies and Allied Matters Act, *op.cit.*,s. 506(1).
[357] Companies and Allied Matters Act, *op.cit.*, s.290.
[358] *Public Finance Securities Ltd. v. Jefia* (1998) 3 NWLR (pt. 543) 602.

(v) **Company Not Mentioned on the Bill of Exchange**: Upon incorporation, a company is required to cause its name and registration number to be painted or affixed outside its office or place of business, and to have its name engraved in its seal. The company is also required to have its name and registration number mentioned in legible character in all business letters, notices, advertisements, bill of exchange, cheques and other official publications of the company.[359] In default of so doing, the company as well as every director and manager of the company who knowingly and willfully authorizes or permits the default shall be liable to the prescribed penalty.[360] Where only an essential part of the company's name is omitted, the foregoing provision still holds sway.[361]

(vi) **Holding and Subsidiary Companies**: The law requires that where a company has subsidiaries, the directors shall, as well as preparing accounts for the individual companies, also prepare group financial statements being accounts or statements which deal with the state of affairs and profit or loss of the company and the subsidiaries.[362] The collective reading of the provisions of ss.336 and 338 CAMA implies the lifting of corporate veil of either of the holding company or its subsidiary. It is a negation of their respective individual corporate personalities.

(vii) **Investigation into Related Companies**: The Corporate Affairs Commission can appoint one or more competent inspectors to investigate the affairs of a company and

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[359] Companies and Allied Matters Act, *op.cit*.,s.631(1).
[360] Companies and Allied Matters Act, *op.cit*.,s.631(2).
[361] In *West Nigerian Finance Corporation v. West Coast Builders Ltd* (1971) U. I. L. R. 316, the court held that the omission of the word limited on a company's contract constitutes a misdescription of the company which rendered the contract a nullity.
[362] Companies and Allied Matters Act, *op.cit*.,s.336(1).

to report on them in such a manner as it may direct. This investigation is upon the application of its members or by the companies own volition. The investigation could also be conducted if the court, by order, declares that the affairs of the company ought to be so investigated.[363] The investigator, if he thinks it necessary for the purpose of his investigation, may investigate also into the affairs of any other related company in so far as he thinks that the results of such investigation are relevant to the main investigation. This constitutes a crack on the separate legal personality of those related companies, hence, lifting the veil of incorporation.

It is further stated that the basis for such investigation is that the companies are beyond the reach of the ordinary individuals who are its members. Accordingly, the statute has intervened to allow the Corporate Affairs Commission to appoint inspector to investigate the affairs of a company. This remains a veritable avenue available to the public, by which the conduct of companies can be investigated.[364]

4.3 Financial Reporting

The pertinent question is how does financial reporting and auditing enhance corporate governance in ensuring accountability by board of directors to shareholders? The board of directors comprises of professional people who are appointed by the company to direct and manage the business and its corporate resources for the benefits of the resource owners. This assertion assumes that directors do not have any equitable interest in the organization. Thus, the separation of ownership from control of business has made the rendering of stewardship a critical key to corporate governance.

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[363] Companies and Allied Matters Act, *op.cit.*,ss.314 & 315.
[364] *Ofong v. Mogal Nigeria Ltd* (1978) F. R. C. R. 80 at 82.

Directors as trustees are obliged by law[365] to present their stewardship report in the form of financial statement (i.e. balance sheet, profit and loss account and statement of changes in financial position) as well as a statement of how the business was managed, to the shareholders at specific times, usually at Annual General Meetings (AGM) for consideration and possible approval. This practice of corporate governance is targeted at ensuring or strengthening the accountability of directors to shareholders.[366]

4.3.1 Financial Reporting as a Corporate Governance Tool

Financial reporting is not an end in themselves but a means to an end. One of the major objectives of financial reports is to supply information on which management decision making is based. This will require complete and accurate disclosure of both quantitative and qualitative data. [367] This is in line with the long standing principle in financial reporting which requires that there must be fair and adequate disclosure in order for a good corporate governance to operate.[368] Section 331 (1) and (2) of the Companies and Allied Matters Act[369] states: 'Every company shall cause accounting records to be kept … the accounting records shall be sufficient to show and explain the transactions of the company and shall be such as to:

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[365] Section 345 of Companies and Allied Matters Act (CAMA), Cap. C20, LFN 2004 provides that directors in respect of each year at a date not later than 18 months after incorporation of a company and subsequently once at least in every year, shall lay before the company in general meeting copies of financial statement of the company made up to the date not exceeding nine months previous to the date of the meeting.
[366] R. Okpeahior and H.P. Faga, *op. cit*, p.215 8.5. 279 of CAMA provide that a director of a company stands in a fiduary relationship to wards the company.
[367] Available at: http://m.business-standurd.com/wapnew/storypage-content.php, accessed on 9/05/2014.
[368] O. Aguolu, *Fundamentals of Auditing*, 3rd edn, (Institute for Development Studies, Nigeria, 2008) p. 570.
[369] Cap. C2O Laws of the Federation of Nigeria, 2004.

i. Disclose with reasonable accuracy at any time, the financial position of the company, and

ii. Enable the directors to ensure that many financial statements prepared under this part comply with the requirements of this act as to the form and content of the company's financial statements.'

An audit is the verification of a company's book and records, performed by an independent expert usually external expert, with a view to ascertaining its compliance with the accounting policy of the company and accounting standard rules. [370]It involves an examination and, therefore, an investigation into the past history, records and data about a company in order to gauge and discover the legality of the business operations, transactions, tax reporting and the overall handling of finance within the business .The essence of auditing is to ascertain that the books of account corresponds with the accounting policies of the company as well as the accounting standards set out by the standard-setting boards. Generally accountants must use Generally Accepted Accounting Principles (GAAPs) and Generally Accepted Auditing Standards (GAASs). More so, the audited account must show the financial status of the company as it constitutes the proof of the financial status of a company, and as the courts have it, it is the best way of showing the financial position of the company at any given time.[371] The various changes in accounting, financial reporting and auditing were all designed to provide protection to investors. This is being achieved by importing a duty of accountability upon the managers of a company. [372]In essence, auditing is used to provide the needed assurance for investors when relying on audited financial statements. More so, the

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[370] F. Ajogwu, corporate governance in Nigeria, law and practice (Lagos center for commercial law Development 2007).

[371] *Livestock Feeds Plc v. Igbino Farms Ltd* (2002) 5 NWLR (Pt.759) CA 118 at 134.

[372] D. Crowther & R. Jatana, 'Agency theory: A case of failure in corporate Governance: in Crowther & R. Jatan (eds) international Dimensions of corporate social Responsibility, 1, 2005, pp. 135-152.

role of auditing is to reduce information asymmetry in accounting to members, and to minimize the residual loss resulting from managers' opportunism in financial reporting. Effective and perceived qualities (usually designated as apparent quality) are necessary for auditing to produce beneficial effects as a monitoring device.[373] Thus, it is as important as the effective audit quality. Audit quality implies that the auditor discovers an anomaly in the financial statements, and reveals it. [374]As an objective approach, auditing is concerned with an expert opinion on the fairness with which financial statement present in all material respects, a company's financial position, results of operations and cash flows in conformity with GAAP. Again, to be able to express such an opinion, the auditor must examine the financial statements and supporting records using sound auditing techniques. [375]Given that corporate governance is concerned with aligning the interests of stakeholders with that of management and that the principles of integrity, transparency and adequate disclosure requirements are essential components of good corporate governance, it follows therefore that auditing is employed in observation of these social responsibility bearing in mind the effect that the reporting of the financial statement will have on the shareholders and the community at large.

The Act requires the accounting records in particular to contain entries from day to day of all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure take place and a record of the assets and liabilities of the company.[376] According to a learned writer,[377] financial statement (through financial

[373] S. B. Adejemi & T.O. Fagbemi, 'Audit Quality, corporate Governance and management, Vol.5, N0-5, 2010 p. 171 169-179.
[374] L.E. De Anglo, 'Auditors size and Audit quality,' journal of Accounting and Economics, 3, 1981, pp 183-199.
[375] Braodlly & D.T. Dohmateu, 'Auditing and its Role in corporate Governance,' Bank for international settlements, FSI seminar on corporate Governance for banks, 20 June, 2006.
[376] Companies and Allied Matters Act (CAMA), Cap. C20, Laws of the Federation of Nigeria, 2004, S. 331 (3).

reporting) show the annual state of affairs of the company and they are vital and indeed, of crucial importance not only to members of the company but also to third parties dealing with it. While the financial statements enable a member to know, for instance, whether his investments are growing or depreciating and whether to sell off or retain his shares in the company, they provide a potential investor with information which would either persuade him to invest or dissuade him from investing in a particular company.

The practice of financial reporting serves as an overview of financial activities of a company. It is a standard practice for companies to prepare and present financial statements in a clear and concise manner for both the company and stakeholders in compliance with the regulations of the locale the company is domiciled, and according to the prescriptions of the board authority to maintain continuity of information and presentation across borders. By virtue of section 331 (1) (2), every company is required to keep accounting records in accordance with this section which shall be sufficient to show and explain the transactions of the company so as to disclose with reasonable accuracy, at any time, the financial position of the company and to enable the directors to ensure that any financial statements prepared under this part comply with the requirements of this Act as to the form and content of the company's financial statements.

Financial reporting has gradually become a slightly complex activity that is of interest to many persons throughout modern and contemporary society. In the past, it was a relatively simple practice primarily of interest to small group of industrialists and financiers. The development of financial reporting within individual countries differs due to the influences of

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[377] O.J. Orojo, Company Law and Practice in Nigeria, 5th edn, (Dayo Orojo of Royet and Day Publications Ltd, 2008) p. 295.

the territory of each country.[378] For instance, the British view has traditionally been that the main purpose of financial reporting is to provide information for investors across the European continent. The European view has been that financial reports can be used for several purposes or more specifically for corporate governance purposes.[379]As it is, financial reporting/ accounting can be defined as the product of corporate accounting and external reporting systems that measure and publicly disclose audited and qualitative data concerning the financial position and performance of firms. Thus, financial accounting or reporting is the fundamental source of independently certified and promoting systems that provide valuable information to corporate control mechanisms that help to alleviate the agency problem which results from the separation of managers and financiers.[380] For investors to make good and crucial investment decisions, it is imperative to understand the theory of principal- agency relationships. Suffice it to say that this theory will be crucial for investors as it will provide them with adequate information as regards financial reporting. Thus, principal agent relationship exists between two contractual parties in business terms. It occurs when a person (an agent) acts on behalf of another (the principal). For the shareholders (i.e. the principal) engage management (agents) to act on their behalf and in full authority as delegated to the management to carry out the intention of the shareholders.[381] Given that most agents are expert at taking important decisions, however, when the decisions are conflicting with the interest of the principal, there is bound to be problem arising in this relationship because the principal is unable to monitor the agent's activities perfectly and get the exact information as the agent without expending any cost hence, the risk of opportunistic behavior on the side of

[378] R. Baker & P. Idallagey. 'The Future of Financial Reporting in Europe: its Role in Corporate Governance,' The International Journal of Accounting, 35:2, 2000, pp. 173-189:

[379] D. Ordelheide, "True and Fair View: A European & a German Perspective," European Accounting Review, 2:1, 1993, pp. l & 90; C. Kuhner, 'Maintaining Economic Stability as a Motored for Statutory Accounting Requirements," the European Accounting Review, 6:44, 1997, pp. 33-754.

[380] R.M. Bushmen and P A.J. Smith, 'Financial Accounting, Information & Corporate Governance', *Journal of Accounting & Economics*, 32:1-3 2001, pp. 237-333.

[381] W.D. Olugbenga, 'Significance of Financial Reporting to Stakeholders in Nigeria - Investors Perspective, Business Economics and Law Journal, 2070.

the management. More often than not, this heads to information asymmetry, a system where one party has more or better information than the other. This creates an imbalance of power in transactions leading to a kind of market failure in the worst case. Examples of this problem are adverse selection,[382] moral hazard [383]and information monopoly. [384] Further, agency costs are incurred by the principal while attempting to avoid a moral hazard on the part of the agent. Although, this cost might be expected but not to a large extent and it could be reduced through strict monitoring measures for effective reduction in agency costs. Therefore, the principal has to enforce their interest through monitoring and controlling the agent. [385]Monitoring simply means the gathering of additional information about the firm's current & future financial and economic possibilities and other information which are considered necessary for shareholders meetings. On the other hand, control signifies restrictions of certain management activities like decisions about the amount of retained earnings. However, it might not be completely possible for the principal to effect this monitoring measure due to high cost involved and shareholders are indeed never able to replace management completely. So, there always remains a certain level of risk of opportunistic behavior from the agents side due to principal financial limitations. Deduced from above is where the need for corporate governance comes from and why it is important in the contemporary world of corporations. Emphatically, the original need for corporate governance stems from the separation of ownership and control in publicly held companies. Investors seek to invest their capital in profit- making firms so that they can enjoy this profit in the future. Many investors lack the time and enterprise necessary to operate a firm and ensure that it provides an investment return. As a result, investors hire individuals with management expertise to run

[382] This refers to a market process in which undesired results occur when buyers and sellers have access to different information; the bad products or services are more likely to be selected,

[383] A moral hazard is a situation where a party will have a tendency to take risks because the costs that could result will not be borne by the party taking the risk.

[384] J.O. Ledyard, 'Market Failure, The New Palgrave Dictionary of Economics, 2nd ed. 200, Abstract.

[385] TJ.D. Olugbenge, "significance of financial Reporting to stake holders in Nigeria- investors' perspective," Business Economics & Tourism, 2070.

the company on a daily basis to see to it that the company's activities enhance its profitability & long term performance. However, these managers and or directors often take actions that affect the value of shareholders investment.[386]Such attitude of management obviously affects the performance and financial viability of the firm and illustrates the need for corporate governance. More so, the principal and concept of corporate governance has arisen due to the high profile collapses that were witnessed across the world of which Nigeria was no exception. The scandals precipitated concerted efforts at evolving codes of best practices for companies. There have been instances of corporate fraud on the international scene, which eventually led to the collapse of notable companies. A very popular example is the *Enron case in the US.*

The collapse of Enron had a negative impact on Arthur Andersen, an auditing firm that helped it to call the shots. Some of the company's principal officers were prosecuted, convicted and sentenced to various terms. Rank Xerox is another popular case. The company had to pay a fine to the tune of 10m dollars following the US SEC investigation of its accounting practices. Other examples are the WorldCom and Parmalat saga in Europe. On the local scene, we also have some notable cases such as the failure of some Nigerian banks in the early 1990's. Another one is the case of Lever Brothers Plc (now Unilever) in 1998 where over-valuation of stocks running into billions of Naira was discovered. Another is the case of the African Petroleum (AP) Plc where the company's Board concealed its indebtedness to the tune of about #22 billion in its offer for sale of shares in 2000. Again, the Cadbury Nigeria Plc's overstatement of its audited financial statements in its Annual Reports and Accounts for 2005 is another case in point. Upon review of Cadbury's annual report, the SEC wrote to Cadbury on a letter dated September 22, 2006 to express concern about issues

[386] J. Triole, "corporate Governance," Economics, 69, No.1 2001, P.2.

arising from the report in the areas affecting profitability, worsening leverage ratio, deteriorating cash flow, inadequate disclosure, non-compliance with corporate governance code, and obtaining loans for the payment of loans and for the payment of dividends to shareholders contrary to SEC regulations. Also, a very recent case concerning the African Petroleum Plc shares has brought to light the issue of corporate governance practices in Nigeria. Following these collapses therefore, organizations have come to the realization that to maximize returns on their investment, accurate information need to be adequately provided for to reassure investors and the public alike, whose investment decisions are influenced by such information provided for, hence, the need for corporate governance. Thus, corporate governance is a system by which companies are directed and controlled.[387] It is concerned with holding the balance between social and economic goals between individual (shareholder) and communal goals. The aim is to align as nearly as possible the interests of individuals, corporations and society. It implies rules and regulations that ensure that a company is governed in a transparent and accountable manner such that the enterprise survives and meets the expectations of its shareholders, creditors and stakeholders of which society forms a large part of. Having noted the concept of corporate governance in passing, it would be difficult trying to separate financial reporting from corporate governance.[388]This is the basis that shareholders have the right to receive information timely on the economic consequence of transactions entered into by the company and other events on the financial position and performance of the company. Therefore, timely presentation of financial information, which reflects the economic consequences of transactions and events, is a part of good corporate governance. More so, high quality financial information helps the market to assess the shares and other securities appropriately and thus strengthens the passive

[387] S.A. Cadbury,' Report on the Committee on the Financial Aspects of Corporate Governance,', (London: Gee Limited / Professional Publishing Limited, 1992).

[388] A.K. Bhattacharyya, 'Transparent Financial Reporting: Essential for Corporate Governance', *Economic Policy*, 2012, 17 September.

monitoring of the executive management by those who do not have control rights (e.g. analyst and credit rating agencies). As a result, high reporting improves corporate governance. Therefore, it is not surprising that with increased focus on corporate governance, the focus on corporate financial reporting has also increased. Almost every country has initiated action to improve the quality of financial reporting in order to enhance the value relevance of the financial information provided in financial statements. Prudence, reliability and relevance are the cornerstones of financial reporting.[389] Application of the principles of prudence requires a company to recognize a loss or a liability immediately it is identified, while it prohibits a company to recognize an income unless it is earned and its collectability is reasonably certain. Thus, the principle of prudence is a check against the opportunistic behavior of the management that has the incentive to defer recognition of a loss or liability and to advance the recognition of income. Although accounting is moving away from the historical cost basis of accounting, standard-setters have not yet given up this concept of prudence.[390] Notably, the use of accounting information in corporate governance mechanisms can be explicit (direct) or implicit (indirect). Financial report is explicitly used in managerial incentive contracts or debt contracts (direct use), but also contributes to the information contained in stock prices (indirect use) Furthermore, financial accounting information is both an output of the governance process, since it is produced by managers, and also an input since it is used in corporate control mechanisms.[391] As a result, additional governance mechanisms are required in order to ensure the quality, integrity, transparency and reliability of the

[389] *Ibid*.
[390] *Ibid*.
[391] R.G Sloan, financial Accounting and corporate Governance: Discussion: Journal of Accounting and Economics, 32:1-3, 2001, pp. 337-347.

accounting information supplied by managers, such as adequate internal control systems, independent board members, vigilant audit committees and independent external auditors.[392]

Financial accounting information is an input of the governance process.[393] Fundamentally, corporate disclosure and transparency are vital for a strong corporate governance framework. Transparency, which is a desirable characteristic of financial reporting, can be defined as 'the extent to which financial reports reveal an entity's underlying economic reports."[394] The need for accurate, reliable, timely and accessible financial and non-financial business information is imperative in order to maintain corporate accountability. As earlier mentioned, the effusion of corporate frauds and failures obviously bring company directors, accounting regulations, auditors and in general the accounting profession into sharp focuses.[395] This brings up the need to examine the role of financial reporting in corporate governance and also the extent to which financial reporting serves the needs of corporate governance for the benefit of a wide range of stakeholders and for the befit of society in general. There are arguments that an 'effective system of corporate governance requires an effective financial reporting system, and that an effective financial reporting system requires a well-ordered system of financial accounting.[396] Thus, it follows that where there is accurate, timely and transparent disclosure, certain fraudulent acts and failures would be prevented. One of such situations that transparent corporate financial reporting helps to combat is the financial statement fraud.

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[392] Z. Rezaee, causes, consequences and Deterrence of financial statement fraud,' critical perspectives on Accounting, 16:3, 2005, pp. 277-298.

[393] V. Arvanitidou etal, 'the Role of Financial Accounting information in strengthening corporate control mechanisms to Allenate corporate corruption; University of Macedonia, Greece

[394] M.E Barth & K. Sdipper, Financial Reporting Transparency," Journal of Accounting, Auditing & Finance, 23:2, 2008, pp 173—190.

[395] L. D Parker, 'Financial and External Reporting Research; the Broadening corporate Governance challenge," Accounting and Business Research, 37:1, 2007, pp 39-54.

[396] R. Baker & P. Idallagey, 'the future of financial Reporting in Europe: its Role in corporate Governance, the international journal of Accounting, 35:2, 2000, pp. 173-187

Financial statement fraud[397]is a deliberate attempt by corporations to deceive or mislead especially investors and creditors, by preparing and disseminating materially misstated financial statements. Misstated financial statement may involve liabilities, or failure to disclose transactions or other information material to a fair presentation of the reported result of operations, and for materially misleading disclosures.[398]Among the most common motivations for companies to commit financial statement fraud are the constant pressure to meet earning projections competition for capital and the perverse compensation arrangements.[399] Imhoff[400] argues that within the U.S. financial reporting environment, managers have increasingly been offered mainly through cash bonus and stock option plans based on accounting results, incentives to manage earnings and to delay or conceal bad news. Therefore, while the financial reporting process produces investors and creditors with information about the entity's performance, it also impacts the current and future wealth position of its managers. For this reason, the use of accounting performance measures in management compensation contracts has been the most thoroughly researched corporate governance issue.[401]However, the external financial reporting-corporate governance relationship is not limited to financial compensation and results alone, since governance accountabilities are also affected by corporate social and environmental impacts.[402] The reporting environment of a publicly held firm includes a monitoring network comprised of those who follow the firm in the role of owner /investor, an intermediary such as an analyst or an investment banker, and who have actual overnight responsibility such as the external

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[397] Z. Rezaee, 'courses, consequences, and Difference of financial statement fraud,' critical perspectives on Accounting, 16:3, 2005, pp. 277-298.

[398] D.V. Dooly, Financial Fraud: Accounting Theory and Practice', *Fordham Journal of Corporate & Financial Law*, September, 8 2002, pp. 53-88.

[399] R.T. Fahnestock & G.C. Yost, 'The Rationale for and Implications of Recent Business Failures on the Accounting Professions,' *Journal of Accounting and Fiancé Research*, 12:5, 2004, pp. 18-131.

[400] E.A. Imphoff, 'Accounting Quality, Auditing and Corporate Governance,' *Accounting Horizons*, September 17, 2007, pp. 117-128.

[401] L.D. Parker, Financial and Extant Reporting Research: the Brooding corporate Governance Challenge," *Accounting and Business Research*, 37: 2007, pp. 39-34.

[402] *Ibid*.

auditor.[403] Ironically, the role of external auditors has been perceived as the most important factor in defecting and preventing financial statement fraud. In recent years however, the entire corporate governance system (board external auditor, committee, top management team, internal auditors, external auditors, and governing bodies) is responsible for ensuring the integrity, transparency and quality of financial statements. In conclusion, timely, accurate and transparent disclosure of the financial statement of the company is a *sine qua non* for the observance of good corporate governance, hence, the essence of financial reporting in helping investors to make good investment decisions.

Financial reporting as a corporate governance tool connects the people that are involved in corporate governance such as the management including the board of directors, auditors, information distributors, analyst and shareholders. It is the bridge that connects the company with the external parties and will be the measurement to determine the performance or outcome of the company. The financial information is the first source of independent and true communication about the performance of company managers. This relevance makes the financial reporting as the main attraction to management influence. The integrity of financial reporting is highly dependent on the performance and conduct of those involved in the financial reporting ecosystems, particularly directors, management and auditors.[404] In other words, the integrity of financial reporting relies on corporate governance. The board of directors has a primary responsibility of overseeing the firm's financial reporting process. This board of directors together with management will try to produce a financial statement that shows that the company achieved a recommendable profit. The independent person that

[403] C.K. Latham & F.A. Jacobs, 'Monitoring and Incentive Factors Influencing Misleading Disclosures,' *Journal of Managerial Issues,* 12:2, 2000, pp. 169-187.
[404] N.M. Norwani, *et al*, 'Corporate Governance Failure and its Impact on Financial Reporting Within Selected Companies', *International Journal of Business and Social Science*, vol. 2 No 1 (November, 2011), p. 207.

reviews the corporate reporting is the auditor. They need to follow the auditing standard with competence, diligence and integrity. They suppose to give their opinion on the reported information.[405]

It is the duty of the directors to prepare financial statements. The Companies and Allied Matters Act[406] provides in section 334 (1) that the directors must, in respect of each financial year of a company, prepare financial statement for the year which will include the following:

a. A statement of the accounting policies;
b. The balance sheet as at the last day of the financial year;
c. A profit and loss account or, in the case of a company not trading for profit an income and expenditure account for the financial year;
d. Notes on the accounts;
e. The auditor's report;
f. The director's report;
g. A statement of the source and application of fund;
h. A value added statement for the financial year;
i. A five year financial summary, and
j. In the case of a holding company, the group financial statements.[407]

[405] *Ibid.*
[406] *Ibid.*
[407] Companies and Allied Matters Act (CAMA), Cap. C20, Laws of the Federation of Nigeria, 2004, S. 334(2).

The financial statements of a private company however, need not include the matters stated in paragraphs (a), (g), (h) and (i) above.[408]

The shareholders usually understand the limitations of the corporate structure from its inception, and often appoint representatives to serve their interests. So the directors and management have duties and must exercise these duties to the shareholders with diligence and with care. They should never be negligent in performing their duties, especially when preparing the financial statement in every occasion.

In a viable financial reporting as a very important tool in corporate governance, there are certain basic features that must be present. These characteristics are as follows: prudence, reliability, relevance and understandability.

Information is reliable if it is free from bias and error and can as supposed be depended on by the public who are in one way or the other affected by the result, as represent events and transactions faithfully. Difficulties of measurement can at times affect the reliability of information as financially reported. In addition, information of the financial statement must not be designed to influence anybody or body of persons, because it can affect its reliability negatively. The financial statement if reliable has the following attribute associated with it,[409] namely: representational faithfulness, meaning that for the information or statement to be reliable, it must represent accurately the transactions and other circumstances of the entity. One particular piece of information may be relevant to the extent that it represents the true transactions of the entity but the circumstances on which the entity operates may render the

[408] *Ibid*, S. 334(3).
[409] O. Aguolu, *op. cit*, pp. 578-581.

information unreliable. Others include substance over form, that is to say that for the financial statement to be reliable, it should reflect the substance of the transaction and not necessarily the legal form. Another one is neutrality. It means that such financial statement should be designed in such a way that it should not intentionally or by default, mislead the user to make a particular decision which the preparer desires. Also, the financial statement must be complete, and balance between costs and benefits.

Another characteristic of financial statement is that the information must be relevant. Information in a financial statement is relevant if it helps to influence the economic decisions of users. It will thus help them to evaluate present events and forms the basis for predicting future events as they relate to the entity. It is also to be relevant if it helps to correct previous faulty evaluation that was made in relation to the entity. In addition, the financial statement must be presented in such a way that it is readily understandable by the people concerned who have reasonable knowledge of business, economic activities and accounting and who are willing to study this information diligently.

In all of the above, there must be the existence of true and fair report. This means that the financial statement must represent and have the attribute of being true and fair to the best of their knowledge that is the directors that are mandated to prepare the financial statements. These will all ensure that good and effective financial reporting as a tool in corporate

governance will be actualized if the directors and the auditors, etc are diligent enough and not negligent in their respective duties. [410]

4.3.2 Financial Reporting Failure Leads to Corporate Governance Failure and Vice-versa

Corporate governance which is characterized by transparency, accountability, probity, and the protection of shareholders rights, cannot be said or proved to exist if there is poor financial reporting. In fact, poor financial reporting can lead to corporate governance failure, and the concerned and affected company can go into bankruptcy. That is why it is usually emphasized that financial reporting is a very vital tool in effective corporate governance. In order to buttress the above statement, there have been occasions of corporate accounting scandals. Corporate scandals that happen today are not unique. It is continuous from previous episode that posed threats to the nation's economy. At the end, either the auditor(s) or the management is to be blamed. So, a good, true and fair financial reporting, as we are going to see shortly, will ensure that the company functions and lives, but in the other way round, the reverse will be the case.

One of such corporate accounting scandal resulting from poor financial reporting is the case of Enron.[411] Enron accounting scandal was a popular one. Enron was established in 1985 as US based energy company and it was prosperous in its early life that its stock rose to by 311% in 1990s. Though the sign of distress in the company started emerging in 1997 when it wrote off $537 million to settle a contract dispute with another company. It became obvious that Enron was in serious problem when in November, 2001 it restated its account of 1997-

[410] V. Asvanitidou etal, 'the Role of financial Accounting information in strengthening corporate control mechanisms to alleviate corporate corruption, University of Macedonia, Greece.
[411] J.O. Alabede, 'The Role, Compromise and Problems of the External Auditor in Corporate Governance', *Research Journal of Finance and Accounting*, Vol. 3 No 9 (2012), available at URL www.iiste.org, accessed on 21/09/ 2013. p. 119

2000 to correct accounting abnormality. The restatement brought down its reported earnings for this period by $591 million and increased the debt by $658 million. Consequently, the credit rating agents downgraded the company and it filed for bankruptcy in December 2001. Arthur Andersen that was the auditor of Enron was accused of negligence in its duty and was criticized of compromising its professional position for financial gain and this led to the winding up of the firm.

Other corporate accounting scandals are the case of Parmalat, an Italian company, Worldcom,[412]a US-based telecommunication company, among others. To be considered also in respect of corporate accounting scandal is Perwaja Steel Sdn. Bhd,[413] a Malaysia based company. One of the well known corporate governance failures in Malaysia is the scandal of Perwaja Steel Sdn. Bhd. Perwaja was established in 1982 by HICOM BhD, a company owned by the government in collaboration with Japanese Company, Nippon Steel Corporation to fulfill the government's mission in implementing the heavy industrial policy. The corporate governance of Perwaja was collapsed due to misconduct in the directorship. The director has paid RM 74.6 million to Japan's NKK Corporation without getting approval from board of directors or tender committees. Later it was revealed that the payment was made via Hong Kong based firm. No qualification of accounts was made by the external auditors during the period 1992 to 1995 with respect to Perwaja's accumulated losses. Investigation revealed that there was an alarming lack of an internal control system within Perwaja. There are inaccurate records, and this demonstrated a failure of corporate governance in which internal control mechanisms were short-circuited by conflicts of interest that enriched certain directors and has an impact on the reporting failure.

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[412] *Ibid,*

[413] N. M. Nowani, *et al*, *op cit*, p. 208.

In all these cases of corporate scandals, it truly showed that the importance of financial reporting is very crucial in corporate governance. And that if there is true and fair financial reporting, it will be very difficult for a company to go bankrupt but instead it will immediately redress the wrong as stated and discovered in the financial statements.

4.4 Narrative Reporting

Narrative Reporting describes the non- financial information included in annual reports to provide a broad and meaningful picture of the company's business, its markets position, strategy, and performance and future prospects. This includes the director's report, the chairman's statement, the directors' remunerations report and corporate governance disclosure.[414] These make-ups of narrative reporting shall be explained seriatim:

4.4.1 The Directors Report

Directors are required to prepare in respect of each financial year, a director's report which will be attached to the balance sheet.[415] Therefore, every company must attach to the balance sheet and profit and loss account a director's reports.[416] According to section 342 of CAMA, there shall be prepared in respect of each year a report by the director which shall contain the following:

i. The names of persons who, at any time during the year, were directors of the company.[417]
ii. The financial activities of the company and its subsidiary in the course of the years.[418]

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[414] www.nortonrosefulbright.com/knowledge(accessed26/08/13).
[415] J.O. Orojo, *Company Law and Practice in Nigeria,* 5th edition (London: Lexis Nexis, 2008) p.303.
[416] N. Bourne, Principles of Company Law, 3rd edition, (London: Cavendish Publishing Ltd, 1998) p.203.
[417] Companies and Allied Matters Act, *op. cit*, Section 342(2).
[418] *Ibid*, S.342.

iii. And any significant change in the financial activities of the company and its subsidiaries.[419]

iv. The report shall also state the matter, and give the particulars required by Part I of Schedule 5 to the CAMA.[420]

On the scope of coverage of director's report, section 342(1) of CAMA provides that the report shall contain a fair view of the development of the business of the company and its subsidiaries during the year and their position at end of it.[421] Secondly, the director's reports shall state the amount (if any) which they recommend should be paid as divided and the amount (if any) which they propose to carry to reserves.[422]

The law provides for punishment for failure to comply with the requirement. Accordingly, any failure to comply with the requirement of CAMA as to the matters to be stated and the particulars to be given in the director's report, every person who was a director of the company immediately before the end of the period prescribed for laying and delivery of financial statements, shall be guilty of an offence and liable on conviction to a term of imprisonment for more than 6 months or to a fine of ₦500.[423] The above provision for punishment notwithstanding, it shall be a defence for the director to prove that he/she took all reasonable steps for securing compliance with the requirements in question.[424]

4.4.2 Chairman's Statement

As already noted, the annual report of a company is a key information source for shareholders of such company to find out its performance in the previous financial year. Its content can be divided into two main categories: quantitative and qualitative. The section under quantitative

[419] *Ibid*, S.342.
[420] *Ibid*, Section 342 (3).
[421] *Ibid*, S.342(1)(a).
[422] *Ibid*, S.342(1)(b)
[423] *Ibid*, S. 342 (6).
[424] *Ibid*, S. 342(7).

category is basically the financial statement of the company. On the other hand, qualitative category consists mainly of the chairman's statement and management discussion. This chairman's statement is getting more attention as investors realize that by going through these contents they can gain insight into the overall company performance, business activities, and development and future directions.

In an annual report, the chairman's statement is always located at the start of the report. Since it is a voluntary disclosure,[425] the statement usually comprises what the senior management of the company wants to disclose to the public. Often the Statement exaggerates positive news during the good years and places less focus in bad news in lack luster years.[426] When a company reports good performance and prospect, the words used in the chairman's statement tend to be more optimistic and compelling. The discussion of its performance is more elaborate, most of the time with reference and supporting financial materials. Success will also be attributed to company's management. On the other hand, if the company is reporting poor performance, lengthy explanations about business activities or financial performance are withheld especially to those involving issues. Even when negative issues are brought up, the explanation given tends to be ambiguous and will most likely focus on external factors beyond the management's control. In some cases, when the chairman is trying to hide bad news from the public or facing crisis that has not yet been made known to the public more often than not the statement will avoid words that indicate certainty or commit the company to a particular position.

[425] Meaning there is no regulatory requirement or accounting guide-lines that applies to it.

[426] As a result of the exaggeration of good news of profits or economic presentation of facts of loss, the unsophisticated investors may be misled by optimistic message presented by the chairman.

Finally, the chairman's statement uses graphs and pictures for support.[427] Also chairman statement is a great place to find apologies for problems that occurred during the year which may or may not have been solved.[428]

4.4.3 The Directors Remuneration Report

By virtue of section 268 of CAMA, a managing director shall receive such remuneration (whether by ways of salary, commission or participation in profits, or partly in one way and partly in another) as directors may determine. According to Orojo,[429] the remuneration of directors is , as a rule, regulated by the Act and articles, but unless so provided, or there is an agreement to that effect, they are not entitled to remuneration for services since they are not servants of the company, but are in the position of managers. Section 267(1) of CAMA provides that the remuneration of the directors shall from time to time be determined by the

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[427] 'Securities Industries Development Corporation', available at: www.min.com.my/articles/ investment, accessed on 5/04/2014.

[428] This is an extract of chairman's statement of Standard Chartered Company as presented in the year 2010:2010 was another year of great performance. We have demonstrated that we have the right strategy, the right culture and the right geographical footprint to deliver consistent and sustained value for our shareholders. I am delighted to report that 2010 was eight consecutive year of record income and profit. Against an uncertain global recovery and despite the return of competition in many markets, Standard Chartered continued to perform strongly. Our performance in 2010 once again demonstrates our ability to deliver substantial, sustained value for our shareholders. Income increased by 6 percent to $16.1 billion profit before taxation rose by 19 percent to 6.12 billion. Normalized earnings per share went up by 14 percent to 197.0 cents. The board is recommending a final dividend of 46.65 cents per share, making a total annual dividend, on a post rights issues basis, of 69.15 cents per share, up 9 percent. For the many shareholders who participated in our rights issue last October, the total dividend received is up 15 percent on 2009 dividend payment. We are proud of our long track record in creating shareholder value. Over recent years, we have simultaneously increased our income, earnings per share, capital ratio and total dividends paid out….[428]'Reading Annual Report', available at www.dummies.com/how-to/content/read (accessed on 2/09/2013).

[429] J.O. Orojo, op. cit, pp. 278-279.

company in a general meeting and such remuneration shall be deemed to accrue from day to day. Also that the directors may be paid all traveling, hotel and other expenses properly incurred by them in attending and returning from meeting of the directors or any committee of the directors or general meetings of the company or in connection with the business of the company.[430]

What is clear from both section 267 and 268 of CAMA is that the remuneration of managing director is a mandatory obligation imposed on the company by CAMA to be determined, however, by directors, but on the part of the directors, the company shall not be bound to pay them, unless where the company agrees to pay or same is fixed by the article of association. Such agreement to pay is usually at the general meeting. And where remuneration of director has been fixed by articles, it shall be alterable only by a special resolution.[431] Consequently, the remuneration of directors is no longer required to be stated in the prospectus, but the aggregate amount of directors emoluments must be shown in the notes to the narrative reporting.[432] This report will enable the shareholders to review the agreement to pay directors or alter the article to make changes to the fixed remuneration of the directors where necessary.

4.4.4 Corporate Governance Disclosure

From very earlier days, it has been recognized that the 'prize' which companies should pay for the privileges of incorporation and limited liability should be a fair degree of openness and publicity about their affairs. The Companies Acts have been largely based on this philosophy.[433] In response to recent corporate governance scandals, governments have adopted a number of regulatory changes. One component of these changes has been increased

[430] Companies and Allied Matters Act, op. cit, S. 267(2) of CAMA.
[431] *Ibid*
[432] J.O. Orojo, *op. cit*., pp. 279-280.
[433] L.S. Sealy, Cases and Materials in Company Law, Sixth edition, (London: Butterwork, 1996) p.585; J. Bauley and lain MC Callum, Company Law, (London: Heine Mann, 1990), p.8.

disclosure requirements. It has been reported[434] that a major barrier to the flow of relevant information is the risk of opportunism inherent to the manager's influence in the firm, which is referred to as an incomplete or distorted disclosure of information and calculated efforts to mislead, distort, obfuscate or otherwise confuse the public and shareholders.

Companies and Allied Matters Act makes provisions for disclosures with respect to the individual interest of members in the share capital of a public company.[435] The aims for this requirement of disclosure by CAMA are as follows:

i. To reveal the identities of persons who may be acquiring shares in the company with a view to controlling it.
ii. To enable the company make its own investigations in this respect without resort to an investigation ordered or supervised by the Corporate Affairs Commission.
iii. To help check abuse and corruption. The disclosure obligations are directed towards two areas namely shares held in trust and substantial shareholding.[436]

Equally, there is a requirement of disclosure in respect of loans and other transactions favouring directors and officers.[437] More generally, the principle of cooperate governance disclosure demands for publicity of every decision of general meeting and that of the directors which affects business activities or interests of the members of the company and/or the general public. This corporate governance disclosure is usually made as part of the annual report as stipulated by the CAMA. According to Ofo,[438] beyond the disclosure made in the annual reports of companies as stipulated by the CAMA, there is real need to take further

[434] Cadbury Report (1992).
[435] Companies and Allied Matters Act (CAMA), *op. cit*, SS. 94-98.
[436] J.O. Orojo, op cit., p.202.
[437] This is by virtue of sections 340 and 341 of CAMA; see also sections 273 and 277 of CAMA.
[438] N. Ofo, Corporate Governance in Nigeria: Prospects and Problems', *Apogee Journal of Business Property and Constitutional Law*, Vol. 1 No.4, (2010), p.20.

steps to ensure that shareholders actually get corporate information. The information could be provided in a dedicated corporate governance section in a company's website. The corporate governance section or report of the annual financial statement should contain appropriate websites references and links to enable shareholders to access the information.

4.5 Business Review

Generally, the functions of the board of directors include inter alia:

i. Defining the business or businesses in which the company shall engage and
ii. Setting the company's long term objectives and strategic plans and ensuring that there is adequate machinery for planning.[439]

In case of every company, there shall be prepared in respect of each year a report by the directors containing a fair view of the development of the business of the company and its subsidiaries during the year and of their position at the end of it.[440] In making the business review, the directors' report should give details of the general nature of the business, changes in its asset value, director's shareholdings, training matters, acquisition of its own shares, policy to be disabled, health and safety matters and employee participation policy.[441]

Business review is properly reflected in the financial statement prepared by director. According to section 334(2) of CAMA financial statements of a company shall consist of the following items:

[439] A. Badaiki 'Exercise of Company's Powers and Shareholders' Control of Corporate Management', *LASU Law Journal*. Vol. IV, Issue 1 (2001) p.79.
[440] Companies and Allied Matters Act, *op. cit*, S.342.
[441] N. Bourne, 0p. cit., p.203.

a. Statement of the accounting policies
b. The balance sheet as at the last day of the year
c. A profit and loss account or in the case of a company not trading for profit, an income and expenditure account for the year.
d. Notes on the accounts;
e. The auditors' reports;
f. The directors' report;
g. A statement of the source and application of fund;
h. A value added statement for the year
i. A five-year financial summary
j. In case of a holding company, the group financial statements.

When these items are presented appropriately, they stand as a general review of business of a given company.

4.6 Social and Environment Reporting

Social and environmental reporting is usually captured in the chairman's statement. People generally feel that business and other organizations have social obligations and responsibilities. Social responsibility includes obligations that an organization including company owes the general public and to specific interest groups and they arise from organizational activities that affect society to a greater degree.

In respect to companies, a social responsibility is embodied under the concept of corporate social responsibility.[442] In Nigeria society has been placing increased demands on big business organizations for greater social responsibilities in the next decade. There has been pressure on business to be involved in solving social and economic problems. The concern includes employee welfare, working conditions, pollution, product safety, marketing practices, employment and community development among others.[443]

Companies embark on these provisions purely on moral and ethical grounds and never as a legal obligation. Since the investors money is involved in such developmental expenditures, the director, as part of the annual accountability, are required to report on the company's social outreach for the year. A new plan may be presented through the reporting for consideration by the shareholders at the general meeting.

On the other part, environmental reporting is a national policy as required by Environmental Impact Assessment Act (EIAA).[444] One of the objectives of environmental impact assessment[445] is to establish, before a decision is taken by any person, authority, corporate body or unincorporated body, including the Government of the Federation, State or Local Government intending to undertake or authorize the undertaking of any activities, those matters that may likely or to a significant extent affect the environment or have an

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[442] The Concept of Corporate Social Responsibility may be seen as the moral and ethical content of managerial and corporate decisions over and above the programmatic requirement imposed by legal principle and market economy

[443] See generally O.J. Seberu and O.S. Aremu, *Department of Banking and Finance: The Polytechnic*, (Ibadan Nigeria, 2010) p.96.

[444] Cap. E12, Laws of the Federation of Nigeria, 2010.

[445] Article 1 (VI) of Expoo Convention defined Environmental Impact Assessment as 'a national procedure for evaluating the likely impact of a proposed activity on the environment.

environmental effect on those activities, and same shall be taken into account.[446] Secondly, the Act[447] has also the goal of encouraging the development of procedures for information exchange, notification and consultation between organs and persons when proposed activities are likely to have a significant effect on boundary or trans-state or on the environment of bordering towns and villages.[448]

Experiences all over the world have revealed that failure to incorporate and institutionalise EIA into a project and the production process at the outset generally results in higher costs later for curative health and environmental programmes to control pollution and manage industrial wastes.[449]

Environmental responsibility of companies, especially those that their activities affect environment, forms part of the concept of corporate social responsibility. Under the Nigerian law, a registered company can only engage in and apply its funds for businesses which are authorized by its object clause in the memorandum of association.[450] It will therefore be *ultra vires* for a company acting through the directors to expend its resources for social, political, environmental or charitable purpose except such is justified as being in the interest of the company and to promote its prosperity. The possible exceptions to this rule are where the company's object expressly permits the use of the company's money for a specified purpose without any reference to the relevance or utility of the expenditure to the company's

[446] Environmental Impact Assessment Act (EIAA), Section 1(a).
[447] Environmental Impact Assessment Act, op. cit., S.62.
[448] *Ibid*, S.1c.
[449] C.A. Omaka, 'The Concept of Environmental Impact Assessment in Nigeria', Ebonyi, State University Law Journal, Vol. 2 No 1 (2007) p. 67
[450] Companies and Allied Matters Act, *op. cit*, S.27(1)(c).

prosperity and where the company, being a charitable organization, applies its funds for a charitable purpose.[451]

As noted above, as far as Nigerian company law is concerned, there is no obligation on a company to act as a good corporate citizen or with altruistic sense of responsibility towards the environment. This has however, been made possible because the objects clause of companies these days is framed so widely as to permit necessary discretion or to engage in any business or activity which will promote the interest of the company.[452] Also, National Policy on Environment imposes an obligation on corporate bodies to take responsibility toward the environment. Thus, if a company expands its funds voluntarily for the purpose of improving the environment, such expenditure need to be reported to the shareholders at the general meeting. Also future plan for the environment must also be presented before the shareholders for approval or rejection or even amendment. This duty of environmental reporting becomes very necessary considering the fact that the object/business clause may not have specifically authorized environmental expenditure.

Presumably, acting under the above requirement and exceptions, Nigerian companies indeed have been engaged in one charitable giving or other activities for the improvement of the environmental. Some of the examples of these social and environmental responsibilities include the building by Guinness Nigeria Limited of an Eye Hospital in Onitcha, bursaries and scholarships have been provided for secondary and universities education by companies like UAC Nigeria Limited, P.Z Nigeria Limited and Gulf Oil Company (Nigeria) Limited. Equally, research grants and professional chairs in universities have been endowed by First City Merchant Bank Limited, Unity Bank of Africa Limited and International Merchant Bank

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[451] *Re Horsley and Wright Limited* (1982) ch. 442 cited in J.A. Omotola, *Environmental Laws Including Compensation* (Lagos: UNILAG, 1990) p. 82.

[452] J.A. Omotola, op. cit., pp. 82-83.

Limited.[453] With particular reference to environmental improvement, Mobil Producing Nigeria Limited as well as other major oil producing companies have constructed several kilometers of roads in rural areas; provided water, electricity and built schools for rural communities where they operate.[454] All these constructions, buildings, grants and charitable donations are presented in the annual general meeting of a company as 'Social and Environmental Reporting'.

4.7 Sustainability / Development Reporting

According to Black's Law Dictionary,[455] sustain means 'to support or maintain especially over long period'. Also, development means 'a human created change to improve….' When combined, sustainable development means development that meets the needs of the present without compromising the ability of future generations to meet their own needs…. It is a process of change in which exploitation of resources, the direction of investments, the orientation of technology development, and institutional change are all in harmony and enhance both current and future potential to meet human needs and aspirations.[456]

Company business or corporate activities should be carried out in such a way as not to obstruct or endanger human and environment development. The social environment in which corporate bodies operate should be preserved for future generation to utilize for continuity of life and its environment.

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[453] J. A. Omotola, op. cit, p. 84.
[454] *Ibid.*
[455] Black's Law Dictionary, 8th Editions.
[456] World Commission on Environment and Development (1987) Report, also known as Brundt Land report.

The duty of sustainability forms part and parcel of corporate social responsibility. With regard to company, its implication is that a company should not cut the bridge after crossing all in effort to make profit or achieve success. The motive for profit or success must be balanced with the need to sustain or develop the sources available for present and future utilization. When a company spends its resources to develop the environment, it should be accounted for. This is the basis for sustainability/development reporting. This report is usually contained in the chairman's statement. See, for instance, an extract of chairman's statement /annual report of 2011-2012 containing sustainability/development reporting in Hindustan Unilever Limited (HUL).[457]

4.8 Auditing

[457] Dear Shareholders, in 2011, we have delivered a robust business performance, which has been consistent and competitive through the year and at the same time made good progress on our sustainability agenda…. We made good progress against targets in the first year of our Unilever Sustainable Living Plan. In 2011, we reduced Co_2 emission per ton of production by 14.7% and water usage in our manufacturing operations by 10.1% compared to our 2008 baseline. HUL has been working for more than a decade in the area of water conservation in locations which face acute water shortage. Through the Hindustan Unilever Vitality Foundation, we are, with NGOs, engaged in community projects to conserve water. By 2015, we expect hundred billion liters of water to be harvested through the project we have undertaken. One million people in 180 villages across India will benefit in most projects, a 50% rise in crop production is expected. In another initiative, HUL has entered into partnership with UNICEF and Department of Rural Development, Government of Madhya Pradesh, to implement hygiene awareness programme in over 5000 schools in 2012. This will further strengthen the life buoy hand wash programme in India, which is now reaching 30 million people across the country. We firmly believe that sustainability has to be at the heart of our business model and will help us drive faster growth and reduce costs. We see this as a source of competitive advantage for the business now and in the year ahead.[457]

There is always an independent body of persons who are to verify the records of stewardship prepared and recorded by those in fiduciary capacities to resources owners.[458] Such reports which show the impact of management's decision on the growth of shareholders wealth will lack credibility if not verified by an independent expert. These independent bodies are: the internal auditors, external auditors and audit committee. Accordingly, our company legislation provides thus:

> Every company shall at each annual general meeting appoint an auditor or auditors to audit the financial statements of the company and to hold office from the conclusion of that, until the conclusion of the next annual general meeting.[459]

It shall be the auditors' duty to consider whether the information given in the directors' report for the year for which the accounts are prepared is consistent with those accounts and if they are of the opinion that it is not, they shall state that fact in their report.[460]

Internal Auditing

The internal audit system has, as its main objective the facilitation of early detection of errors or fraud. The internal audit is an integral element of corporate governance and is carried out by an internal auditor who reports to the chief executive officer who is referred to as the managing director in Nigeria, and is supposed to assist the executive management and the board in the discharge of their obligations relating to safeguarding asset, risk management,

[458] Section 279 of CAMA provides that a director of a company stands in a fiduciary relationship towards the company.
[459] Companies and Allied Matters Act (CAMA), Cap. C20, Laws of the Federation of Nigeria 2004, S.357.
[460] Companies and Allied Matters Act, *op. cit*, S.360 (5).

operation of adequate controls and reliability of financial statements and stewardship reporting.[461]

4.8.2 External Auditing

Internal auditing is not always enough to guarantee error free financial statement, and the realization of possible collusion between the executive management and the internal auditor made the provision for external auditor an essential factor for more transparency in the accounting system of company. According to section 358 and 359 of CAMA, chartered accountants, as external auditors are the professional experts empowered to examine these financial statements not only to determine whether they represent a true and fair view of the state of affair of the entity and are free from any material misstatement but also to ascertain whether they conform to the generally accepted accounting principles and other relevant legislations and standards - whether there are errors, misstatement or fraud in the account.[462]

The main objective of external audit is to give a report on the view presented by the financial statements prepared by the managers. The detection of fraud and errors are incidental to this main objective.[463] External auditors are usually appointed by shareholders and are required to submit their report to shareholders during annual general meeting. This means that external auditors are accountable to the body of shareholders. Nevertheless, subject to section 357(5)(a)&(b) of CAMA, the first auditors of a company may be appointed by the directors at any time before the company is entitled to commence business and auditor so appointed shall

[461] C.C. Okeahalam and O.A. Akinbode, 'A Review of Corporate, Governance in Africa: Literature, Issues and Challenges', a Paper Prepared for the Global Corporate Governance Forum, 15 June, 2003.
[462] R. Okpeahior and H.P. Faga, *op. cit*, p.218.
[463] C.C. Okeahalam and O.A. Akinbode, *op. cit*, p.15.

hold office until the conclusion of the next annual general meeting.[464] With respect to banks in Nigeria, the appointment of external auditors by the shareholders of a bank is expected to receive the approval of Central Bank of Nigeria (CBN) in line with section 29 of Banks and Other Financial Institutions Act (BOFIA). The report of such external auditors are expected to be read together with the report of the board of directors at the Annual General Meeting while two copies of each report together with the auditor's analysis of bad and doubtful advance in a form specified by the Central Bank of Nigeria shall be sent to the apex bank for its information and consideration. The external auditor is also expected to submit two copies of the management or domestic report to the CBN within 3 months of the end of the financial year of the bank.[465]

The external auditor is an audit professional who performs an audit in accordance with specific laws or rules on the financial statements of a company, government entity, other legal entities or organizations, and who is independent of the entity being audited. Users of these entities financial information such as investors, government agencies, and the general public, rely on the external auditor to present an unbiased and independent audit report. The responsibility of an external auditor is to make sure that there is nothing bad or wrong going on within a company financially. More so, he is engaged to consider an opinion on whether a company's financial statements are presented fairly in all material respects, in accordance with financial reporting framework. An audit conducted in accordance with GAAS and relevant ethical requirements enables the auditor to form the opinion, thus, the auditor gathers appropriate and sufficient evidence and observations that compares and confirms the opinion with reasonable assurance. The auditor then forms an opinion of whether the financial

[464] See generally S. 357 of CAMA particularly, subsection 3 of same section which provides that where at an annual general meeting, no auditors are appointed or re-appointed, the directors may appoint a person to fill the vacancy.
[465] R. Opeahior and H.P. Faga, *op. cit*, p.218.

statements are free of material misstatement, either due to fraud or error. The emphasis is on 'independence'. First and foremost, auditor does not take responsibility for the financial statements on which they form an opinion. The responsibility for financial statement presentation lies squarely in the hands of the company being audited. Thus, auditors are not a part of management which means that the auditor will not:

a. Authorize, execute or consummate information on behalf of a client
b. Prepare or make changes to source documents.
c. Assume custody of client assets, including maintenance of bank accounts.
d. Establish or maintain internal controls, including the performance of ongoing monitoring activities for a client
e. Supervise client employees performing normal recurring activities
f. Report to the board of directors on behalf of management
g. Serves as a clients stock or escrow agent [466]or general counsel
h. Sign payroll tax returns on behalf of a client
i. Approve vender invoices for payment
j. Design a clients financial management system or make modification to source code underlying that system
k. Fires or terminate employees

On the while, the external auditor evaluates whether audit evidence raises doubt about the ability of the client to continue as a going concern in the passable future. He expresses his assurance on the financial statements in an auditor's report. Further, he has the responsibility to express an opinion on whether management has fairly presented the information in the financial statements.

[466] Escfow a bond, deed, or other document kept in the custody of a third party and taking effect only when a specified condition has been fulfilled.

Corporate governance can as well work through external auditors which are another mechanism that corporate governance can operate effectively and efficiently. There is often the need to have an independent body of persons who are to verify the records of stewardship prepared and recorded by those in fiduciary capacity to resource owners. Such reports which show the impact of management's decision on the worth of shareholder's wealth will lack creditability if not verified by an independent expert. Accordingly by sections 358 and 359 of the Companies and Allied Matters Act,[467] chartered accountants, as external auditors, are the professional experts empowered to examine these financial statements not only to determine whether they in any way represent a true and fair view of the state of things or business of the company and are also free of any material misstatement but also to ascertain whether they conform to the generally accepted accounting principles and other relevant laws and standards -whether there are errors, misstatements or fraud in the accounts.[468]

External auditors are most at times appointed by and are required to submit their reports to shareholders during Annual General Meetings.[469] By necessary implications, these external auditors are accountable to the body of shareholders but the reverse was the case in the Enron's crisis which showed evidence of misleading accounts, shoddy auditing, and bad management and quite probably an outright fraud. Although Enron is not a financial institution, it was a Houston-based energy firm, founded by Kenneth Life Span from an obscure gas pipeline concern to the World's largest energy trading company. Encouraged by deregulation, the company turned to electricity to supply its natural gas business. Its

[467] Cap. C20 LFN, 2004.
[468] A.A. Asein, 'Managing Audit Risks', *The Nigerian Accountant*, Vol. 32 No 1 (January and March, 1999) (Cited in R. Okpeahior & H.P. Faga, *op. cit*, p. 1.
[469] Companies and Allied Matters Act, *op. cit*, S. 357.

attempted entry into California's retail electricity market in 2001 was unsuccessful. In the same year, the company's decade-long involvement in DAHOL and India power plant project also ran into deep waters. Lack of transparency undermined Enron's credibility and in October 2001, its shares and credit rating plummeted considerably. In November 2001, a rival firm, backed out of a proposed life line merger after Enron's debt was downgraded to junk status filed for bankruptcy in December 2001. The involvement of a reputable accounting firm like Anderson in shredding of incriminating document just ahead of investigation was very unprofessional.[470]

In certain exceptional `cases, however, the board of directors can appoint external auditors, if the shareholders failed to do so at the Annual General Meeting and such appointment must be communicated to the Corporate Affairs Commission within one week of exercising that power under section 357 (3) of Companies and Allied Matters Acts.[471] In the case of banks, the appointment of external auditors by shareholders of bank is, however expected to receive the approval of the Central Bank of Nigeria (CBN) in line with section 29 of Banks and other Financial Institutions Act.[472] The reports of such external auditors are expected to be read together with the report of the board of directors at the Annual General Meeting –while two copies of each report together with the auditor's analysis of bad and doubtful advances in a form as stipulated by the CBN shall be forwarded to the apex bank for its information and consideration. The external auditor is also expected to submit two copies of the management or domestic report to CBN within 3 months of the end of financial year of the bank.[473] The external auditor is an independent person or firm of auditors appointed by the shareholders to

[470] E.A. Onwuoduoki, 'Current World Financial Crisis: Lessons to be Learnt, in O. Alo (ed), Issues in Corporate Governance, (2003) p. 51, cited in R. Okpeahior & H.P. Faga, *op. cit*, pp. 217-218.
[471] *Ibid*.
[472] Cap. B3, LFN, 2004.
[473] Banks and Other Financial Institutions Act, Cap. B3, LFN, 2004, S. 29.

investigate the financial statements prepared by the management and report its findings to the shareholders. The internal auditors are the employees of a company who are appointed by the management to carry out audit of the day-to-day affairs of the company as part of the internal control system.[474] But, unlike the internal auditor, the external auditor also is an independent person or firm of auditors appointed according to statutory requirement(s) to investigate the financial statements of an entity and express his opinion in form of report on the true and fair view of such financial statements.[475]

Accordingly, in relation to the external auditors' roles and duties, section 360 (1) - (5) of the Companies and Allied Matters Act[476] provides that it shall be the duty of the company's auditors, in preparing their report, to carry out such investigations as may enable them to form an opinion as to the following matters whether –

a. Proper accounting records have been kept by the company and proper returns adequate for their audit have been received from branches not visited by them;
b. The company's balance sheet and (if not consolidated) its profit and loss account are in agreement with the accounting records and returns.

Subsection (2) of same section provide that if the auditors are of opinion that proper accounting records have not been received from branches not visited by them, or if the balance sheet and (if not consolidated) the profit and loss account are not in agreement with the accounting records and returns, the auditors shall state that fact in their report. Also

[474] K.O. Alabede, 'The Role, Compromise and Problems of the External Auditor in Corporate Governance', *Research Journal of Finance and Accounting*, Vol. 3 No 9 (2012) p. 115,available at: URL www.iiste.org, accessed on 21/09/13; O. Aguolu, *op. cit*., at p. 7.
[475] *Ibid*.
[476] Cap. C20 LFN, 2004; See also the equivalent provisions in the United Kingdom Companies Act 2006, particularly sections 495-498.

subsection (3) provides that every auditor of a company shall have a right to access at all times the company's books, accounts and vouchers, and entitled to require from the company's office such information and explanations as he thinks necessary for the performance of the auditor's duties.

Also, if the requirements of Part V and VI of Schedule 3 and Part I-III of Schedule 4 to this Act are not complied with in the accounts, it shall be the auditors' duty to include in their report, so far as they are reasonably able to do so, a statement giving the auditors' duty to consider whether the information given in the director's report for the year for which the accounts are prepared is consistent with those accounts; and if they are of opinion that it is not, they shall state that fact in their report. In the case of *Leads Estate Building and Investment Co. v Shepherd*,[477] the court stated that it is the duty of the auditor not to confine himself merely to mechanical audit. Although they had not checked the articles of association, they must have known of their existence because every company was required to have articles. In *Henry Squire v Ball Baker*,[478] the auditors are expected to go beyond the books and records of the client for evidence to support their opinion about the truth and fairness of the financial statement.

Following the case of *AWA v Daniels (Trading as Deloitte Haskins & Sells) & others,*[479] the court stated that Deloitte failed to perform their contractual duties in three ways:

i. It was clear that the books and records relevant to AWA's foreign exchange transactions were inaccurate and inadequate and the auditors should have formed the opinion that accounting records had not been kept.

[477] (1887) 36 Ch. D 787.
[478] (1911) 44 Acct LR 25, See also *Re City Equitable Fire Insurance Co. Ltd* (1924) 71 Acct LR 81.
[479] (1992) 10 ACLC 933.

ii. The auditors had doubts about the extent of the foreign exchange manager's authority to enter into foreign exchange transactions on behalf of AWA. The auditor had a duty to make enquiries from an appropriate level of management.

iii. The auditors had discussed the inadequate system of recording foreign exchange transactions with the recording manager of AWA, but they did nothing to ensure that the matter was dealt with urgently and effectively, neither did they ensure that it was referred to AWA's board of directors.

The auditors had been negligent in the performance of their duties and their negligence had contributed to the loss suffered by AWA. AWA's senior management was also found to have contributed to the company's loss by virtue of deficiencies in its system of internal controls and record keeping.

The role of the external auditor is also extended to ascertain and to test the company's financial statement of accounts. An external auditor tests a financial statement item to verify that an account balance is correct and agrees with ledger amounts. A ledger is an accounting record.[480] For instance, an auditor might review a company's customer accounts to ensure that individual customer balances agree with total accounts receivable. In addition, an external auditor checks the company's accounts and reports to the company based on its findings on such accounts. Thus, in *Re London & General Bank*,[481] the court stated that the auditor's business is to ascertain and state the true financial position of the company during audit. The auditor should examine the books of the company and enquire and take a reasonable care to ascertain that the books of the company show its true position.

[480] http://www.eh ow.com/list - 6582612 - external – auditor – s – duries – html.
[481] (1895) 2 Ch. 673

The external auditor must ensure that the board of directors and the management are acting responsibly towards the shareholder's investment interest. By keeping objectivity, the external auditors can add value to shareholders by ensuring that the company's internal controls are strong and effective. And by working with the audit committee and liaising with internal auditors, external auditors can help to facilitate a more effective oversight of the financial reporting process by the board of directors. The external auditor also observes the system and management in the company, especially as it relates to its financial statement in the company and if it discovers that the system is weak, that suggests that it is less reliable. In this case, the auditor may have to do more substantive tests in his work and role. Auditor is expected to inform the management about any weakness he observes in the system of its financial statement. It should be noted that weakness in the internal control system in the company makes the work of auditor more difficulty. Empirically, Krishaman and Visvanathan[482] show that companies with weak internal control system witnessed more auditor changes. The consequence of weak internal control was manifested in the case of *Baring Bank* in which the General Manager (Leason) to Singapore Office engaged in an authorized speculative trading on the Nikkei, which resulted to loss of E827 million which was without head knowledge of the management at head office in London.[483]

The existence and establishment of an external auditor will ensure that the inaccuracies and deficiencies associated or perpetrated in the internal control system of the company is under control, and that these external auditors role will go a very long way to curtail these problems. This is in order to restore trust and public confidence in the company and as well

[482] G.V. Krishaman and G. Visvanathan, 'Reporting Internal Control Deficiencies in the Post Sarbanes Oxley Era: the Role of Auditors and Corporate Governance', International Journal of Auditing 11, pp. 73-90, cited in J.O. Alabede, *op cit*, p. 118.
[483] *Ibid*.

remove the probability of the company going bankrupt. And through the role performed by the external auditors, the shareholders monitor and control the management, and this in return will help to enhance transparency and accountability in the company.

An external auditor reviewing a business entity's processes and final statements learns about the entity's operating environment prior to starting an audit. This involves external and internal factors affecting how the company operates. In other words, this role is referred to as a good understanding of the entity's environment. External factors could include industry practices, regulatory guidelines and business trends. Internal factors might be top management's ethical rules and leadership style, corporate policies and departmental rules. An external auditor analyses financial reporting risks and discusses risks with management. An external auditor reviews internal controls and processes around financial reporting mechanisms to ensure that such mechanism report complete and accurate financial statements. An audit specialist also verifies that a company's records agree with generally accepted accounting principles. And completeness in reporting includes certain types of data sets such as balance sheet, a statement of profit and loss, a statement of cash flows and a statement of shareholders' equity.

Basically, another role carried out by the external auditors is stated in section 359 (1) of Companies and Allied Matters Act,[484] which provides that the auditors of a company shall make a report to its members on the accounts examined by them, and on every balance sheet and profit and loss account, and all group financial statements copies of which are to be laid before the company in general meeting during the auditors' tenure of office. In the case of

[484] Ibid.

Sasea Finance Ltd. v KPMG,[485] the court stated that the primary obligation for the auditor is, within a reasonable time, to exercise an appropriate level of skill and care in reporting to the company's members on the accounts of the company stating, in their opinion, whether the accounts of the company give a true and fair view of the company's financial affairs. KPMG has a duty to warn the company's directors as soon as the fraud or irregularities had been detected.

However, it should be clearly pointed out that it has been held in auditor's favour that it was not part of their duties to tell directors how to run the business and they had no power to insist that their recommended changes were put into operation.[486]A learned author[487] also added that the two main duties of an auditor includes to audit the accounts of the company and secondly to report to the members of the company on the account i.e. on every balance sheet and profit and loss account and all group account if any, laid before the company in general meeting during his tenure of office. The auditors' report must be open to inspection by any member.[488]

An external auditor must act honestly, and with reasonable care and skill. He is liable to the company for loss resulting from his breach of duty. He may be liable in tort for negligent misstatements to the shareholder, debenture holder or investor if he knows that they intend to act on his statements.[489]

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[485] (2000) 1 All ER 676.
[486] Re SP Catterson & Sons (1937) 81 Acct LR.
[487] D. Keenan, Smith & Keenan's Company Law for Students, 10th edn, (Great Britani: Financial Times Pitman Publishing, 1996).
[488] *Ibid*, pp. 414-415.
[489] *Hedley Byrne v Heller* (1964) A.C. 465.

His duty is not confined to the machines of checking vouchers and making arithmetical computations. He should approach his job with an alert mind and if there is anything suspicious, he should probe it exhaustively. Thus, in *Re Thomas Gerrard and Son Ltd*,[490] the company's managing director falsified the company's books and invoices in a manner which would immediately raise suspicion. Believing him to be of the highest integrity, the auditors accepted his explanations of the alterations and certified the accounts. As a result the company paid tax and dividends on inflated profits. The auditors were held liable. But in the absence of suspicious circumstances, an auditor is entitled to assume that the company's officers are honest and responsible and he may rely on their representations provided he is careful.[491]

In *Re London and General Bank (No.2)*[492] the accounts contained in the face value of certain loans which the auditors knew were not realizable. He had pointed this out to the directors showing the gravity of the company's position, but his report to the shareholders merely stated that the value of the assets as shown on the balance sheet is dependent upon realization. As a result, dividends were paid out of capital. He was held liable for the amount of the dividends paid. In *Re Thomas Gerrard and Sons Ltd*,[493] the court stated:

> The auditors of a company owe a statutory duty to make to the members a report containing certain statements. If the directors do not allow auditors time to conduct such investigations as are necessary in order to make these statements, the auditors must, it seems to me, either refuse to make a report at all or make an appropriately qualified

[490] (1968) Ch. 455, *Re City Equitable Fire Insurance Co. Ltd.* (1925) Ch. 407.
[491] *Re Kingston Cotton Mill Co.* (No. 2) (1896) 2 Ch. 279.
[492] *Supra*.
[493] *Supra*.

> report. They cannot be justified in making a report containing a statement the truth of which they have not had an opportunity of ascertaining.[494]

It was also stated in this case that the standards of reasonable care and skill are more exacting today than those which prevailed in 1896 when *Re Kingston Cotton Mill Co. (No. 2)*[495] was decided.

4.8.3 Audit Committee

The financial statement prepared by the board of directors shall also pass through the Audit Committee.[496] The Audit committee plays a vital role in financial and operational control in the whole system of corporate governance by making recommendations to the board concerning the appointment and remuneration of external auditors, reviewing auditors evaluation of the system of internal control and accounting and consideration and making of recommendations on the conduct of any aspect of the company which should be brought to the notice of the board of directors among others.[497]

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[494] *Ibid*, at p. 477, per Penny Cuick, J.

[495] *Supra;* See also Gaius Ezejiofor, *et al., Nigerian Business Law*, (London: Sweet & Maxwell Limited, 1982) p. 317.

[496] This is after external auditor had audited the financial statement, the auditor is required to make report to audit committee in case of public company - see section 359(1)(3) of CAMA.

[497] C.C. Okeahalam and O.A. Akinbode, *op. cit*., p.15.

According to section 359(4) of CAMA,[498]'the Audit Committee shall examine the auditor's report and make recommendations thereon to the annual general meeting as it may think fit.' And subject to such other additional functions and powers that the company's article of association may stipulate, the objectives and functions of audit committee shall be to:

a. ascertain whether the accounting and reporting policies of the company are in accordance with legal requirements and agreed ethical practices;
b. review the scope and planning of audit requirements;
c. review the findings on management matters in conjunction with the external auditor and departmental responses thereon;
d. keep under review the effectiveness of the company's system of accounting and internal control.
e. make recommendations to the board in regard to the appointment, removal and remuneration of the external auditors of the company; and
f. authorize the internal auditors to carry out investigations into any activities of the company which may be of interest or concern to the committee.[499]

The Audit Committee has been described as the most important development in corporate structure and control in decades. It is conceived as an investor's protection device. The origin of corporate audit committee is traceable to the celebrated fraud case involving Mc Kesson and Robin in the United State of America 1939. An enduring legacy of the case was the recommendation by the United State Securities and Exchange Commission in 1940 that every

[498] In Nigeria, the Corporate Audit Committee made its first appearance in the Companies and Allied Matters Act of 1990. It is to be composed of an equal number of the company's directors and representatives of the shareholders, subject to maximum number of six members. See section 359(3) of CAMA.
[499] Companies and Allied Matters Act, *op. cit*., Section 359 (6)(a)-(f).

public company should establish an Audit Committee to strengthen its structure of corporate governance and accountability.[500]

This recommendation was adopted by the 1990 Companies and Allied Matters Act in Nigeria and presently, the Audit Committee has been mandatorily compelled to be responsible for the review of the integrity of the bank's financial reporting and oversee the independence and objectivity of the external auditors.[501]

In all, good corporate governance by board of directors is recognised to influence the quality of financial reporting which in turn has an important impact on investor confidence. The search for mechanisms to ensure reliable, high quality financial reporting has largely focused on the structure of audit quality.[502] Therefore, financial reporting and auditing were all designed to provide protection to investors. This is being achieved by imposing a duty of accountability upon the managers of a company. In essence, auditing is used to provide the needed assurance for investors when relying on audited financial statements.[503] It has been observed by Wilson[504] that despite the power given to the shareholder to consider and approve the appointment and remuneration of auditor(s) as well as the financial statement in a general meeting so as to ensure that the board of directors observes financial discipline in the management of the company, the shareholders have not efficiently utilized the power. In practice, the shareholders usually rubber stamp the financial statements presented to them

[500] R. Okpeahior and H.P. Faga, *op. cit*., p.218.
[501] S.E. Otuwanuga, 'Shareholders' Activision - Role in Corporate Governance and Investor Protection', *Law and Investment Journal,* Vol. 1 No 2 (2007), p. 25.
[502] S.B. Adeyemi & T.O. Fagbemi, 'Audit Quality, Corporate Governance and Firm Characteristics in Nigeria', *International Journal of Business and Management*, Vol.5 No.5 (2010), p.169.
[503] *Ibid*, p.177.
[504] I. Wilson, 'Regulatory and Institutional Challenges of Corporate Governance in Nigeria - Post Banking Consolidation', *Nigerian Economic Summit Group (NESG) Economic Indicators*, April-June 2006, Vol.12 No.2, p.3.

sometimes assuming that the financial statements presented, having gone through internal audit controls, ought to be in order. Wilson[505] further stated that all systems of internal control are subject to limitations and weakness and no matter how good the planning of the system, no matter how strict and consistent its application, it can never give perfect protection and safety to human factors, e.g. proneness to errors and deceit as well as collusion between members of staff.

Therefore, the burden then falls on regulatory organs such as the Central Bank of Nigeria (CBN), Corporate Affairs Commission (CAC), Securities and Exchange Commission (SEC), etc to properly scrutinize the financial statement of the company since adequate accountability may not be achieved through financial reporting and auditing.

Corporate governance does not just work in isolation, it works through some mechanisms. The direction and control of corporate entities are statutorily regulated in Nigeria as in many other countries of the world through the following mechanisms: The board of directors, audit committees, Members at Annual General Meeting (AGM) and external auditors.[506] However, only one of the mechanisms will be discussed in detail and that is audit committee. The Audit Committee has been described as the most important development in corporate structure and control in decades.[507] It is however seen as an investor's protection device. Audit Committee

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[505] *Ibid*.

[506] R. Okpeahior & H.P. Faga, 'Reflection of Sound Corporate Governance for a Thriving National Economic Environment, *Ebonyi State University Law Journal*, Vol. 2 No. 1, (2007) p. 210-222, p. 215.

[507] A.A. Berle and G.C. Means, The Modern Corporation and Private Property (New York: Macmillan, Nineteenth Printing, 1962) p. 13, cited in R. Okpeahior and H.P. Faga, *op. cit*, at p. 218).

is also an essential organ of corporate governance, particularly in public companies. Every public company should as a matter of necessity have Audit Committee.[508]

The audit committee is therefore a key governance structure charged with oversight over financial reporting and disclosure. Apart from the statutory Audit committee, as required (of public companies by the Companies and Allied Matters Act [509]which is made up of an equal number of directors and shareholder representations, a company may also have a Board Audit committee. Indeed, the CBN code of corporate governance provides for the establishment of a Board Audit Committee made up of non-executive directors and chaired by an independent director. The statutory duties and role of the audit committee are clearly encapsulated in section 359 (3) and (4).[510] In addition, the various codes of corporate governance - the CBN, SEC and NAICOM codes set out the corporate governance role & responsibilities of the audit committee to include the following:

i. Ascertain whether the accounting and reporting policies of the company are in accordance with legal requirements and agreed ethical practices,
ii. Review the scope and planning of audit requirements.
iii. Review the findings on management matters in conjunction with the external auditor and departmental responses thereon (management letter);
iv. Keep under review the effectiveness of the company's system of accounting and internal control;
v. Make recommendations to the Board in regard to the appointment, removal and remuneration of the external auditors of the company, ensure the independence and

[508] N.C.S. Ogbuanya, Essentials of Corporate Law Practice in Nigeria, (Nigeria: Novena Publishers Ltd, 2010) p. 453.
[509]CAMA, Cap.C20, LFN, 2004.
[510] *Ibid*.

objectivity of the external auditors and that there is no conflict of interest which could impair the independent judgment of the external auditors; and

vi. Authorize the internal auditor to carry out investigation into any activity of the company which may be of interest or concern to the committee.

vii. Assist the oversight of the integrity of the company financial statements and establish and develop the internal audit function.

The Audit committee has a responsibility to ensure that the company's financials are void of any misrepresentation or misleading information. The committee may also play a significant role in the oversight of a company's risk management policies and programmers where there is no Board Risk Management Committee charged with this function. The role of the audit committee in corporate governance has evolved in the wake of the corporate governance failures around the world. Thus, the audit committee has become increasingly relevant in enhancing confidence in the integrity of an organizations processes and procedures relating to internal control and corporate and financial reporting. The Audit committee has become one of the main pillars of corporate governance in checkmating and forestalling corporate misconduct. The effectiveness of the audit committee determines to a large extent the integrity of a company's financials. To be effective therefore, the audit committee should have a charter that should clearly define its responsibilities and modus operandi, and establish the right tone at the top. Members of the committee should possess basic financial literacy. Indeed it is not out of place to designate a member as the financial expert; be able to commit time and effort to the task; ask the right questions of management, seek professional advice where necessary, recognise that the role is not merely ceremonial and above all, be men and women of integrity. [511]

[511] B.Adeifemi, Role of Audit committee as corporate governance Business intelligence, September 23, 2013.

Subject to the additional powers that may be stipulated and provided in the company's articles of association, the audit committee is to examine the auditor's report and make recommendations thereon to the Annual General Meeting as it may think fit.[512] Most importantly, Section 359 (6)[513]generally sets out more particularly the objectives and functions of the committees. The objectives and functions of the audit committee shall be to-

i. ascertain whether the accounting and reporting policies of the company are in accordance with legal requirements and agreed ethical practices;
ii. review the scope and planning of audit requirements;
iii. review the findings on management matters in conjunction with the external auditor and departmental responses thereon;
iv. keep under review the effectiveness of the company's system of accounting and internal controls;
v. make recommendations to the board in regard to the appointment, removal and remuneration of the external auditors of the company; and
vi. authorize the internal auditor to carry out investigations into any activities of the company which may be of interest or concern to the committee.

It is pertinent to note that in the United Kingdom, for example, no statutory functions are imposed on the audit committees.[514] However, as postulated by a learned author[515] on the duty of the audit committee, made up of non-executives, their function is to review the effectiveness of the company's auditing procedures and to liaise with the auditors. The

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[512] Companies and Allied Matters Act, *op. cit*, S.359.
[513] *Ibid*.
[514] O.J. Orojo, *op. cit*., p. 311.
[515] J.E. Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law* (New York: Oxford University Press Inc., 1993) p. 58.

Nigerian provisions set out the functions of the committee in details designed perhaps to solve the peculiar problems of the Nigerian corporate management.

The audit committee as already noted consists not of 'insiders' only but also 'outsiders' who can bring their respective ideas and independent minds to bear on the issues at hand. However, due care and diligence must be exercised and taken in other to ensure that the committee does not become forum for confrontation in the affairs of the company especially between the directors on the one hand and shareholders on the other. Rather, their effort should be geared towards ensuring that they work harmoniously to correct errors, and implement and observe its functions duly accorded it.

4.8.4 Impact of Auditing under the Rules of Corporate Governance

Audit deals with the examination of the books of accounts of a company by external experts with a view to ascertaining its compliance with the accounting policy of the company and accounting standard rules. The audited account also shows the financial state of the company. Thus, audited account of a company constitutes the proof of the company's financial status.[516] In the case of *Livestock Feeds Plc v Igbino Farms Ltd,*[517] the court held that the audited statement of account of a company is the best way of showing the financial position of the company at any given time.

Auditing has been defined as the independent examination of the financial statements (together with the underlying books and records) of an organization, the purpose being to

[516] N.C.S. Ogbuanya, Essentials of Corporate Law Practice in Nigeria, (Novena Publishers Ltd, (Best Practice Books Series) Nigeria 2010) p. 444.
[517] (2002) 5 NWLR (Pt.759) 118-134.

enable the auditor form an opinion on the basis of which to make a report that the financial statements, the subject of his examination, show a true and fair view.[518]

One of the mechanisms for providing assurance to the investors and other stakeholders is corporate auditing. The principal characteristics of ensuring effective corporate governance such as transparency, accountability and integrity are enhanced with conduct of audit into the affairs of a company. Generally, internal and external auditors may conduct audit into the operation of a company. The internal auditors are the employees of a company who are appointed by the management to carry out audit of the day-to-day affairs of the company as part of the internal control system. The external auditor on the other hand, is highly regarded in the corporate governance framework because unlike the internal auditor, he is appointed by the shareholders. The external auditor is an independent person or firm of auditors appointed according to statutory requirement to investigate the financial statements of an entity and express his opinion in form of report on the true and fair view of such financial statement.[519]

Auditing standards ensures that the basic rules of corporate governance such as objectivity, integrity, accountability, etc which are essentially in the auditors' performance of his responsibilities are highly actualized. These basic rules of governance, when it is fully observed with implementation, make good corporate governance to thrive. It is, however, auditing process that can impact positively in the concerned company in achieving these goals. So a good auditing is very crucial in the rules of corporate governance.

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[518] O. Aguolu, Fundamentals of Auditing, 3rd edn., (Institute for Development Studies, Nigeria, 2008) p. 560.

[519] J.O. Alabede, 'The Role, Compromise and Problems of the External Auditor in Corporate Governance', *Research Journal of Finance and Accounting*, vol. 3 No 9 (2012), p.155 available at URL www.iiste.org, accessed on 21/09/ 2013).

Auditing can impact the risk taking incentives of management through an appropriate application of accounting policies. However, it is also important to ensure that rules (in the event of a breach of accounting policies) are correspondingly enforced. Another effect auditing has impacted positively in a company is corporate accounting scandal. Under this case, there must be a fair and true auditing, if not, corporate accounting scandal can surface and at the end leaves the company no choice than going bankrupt.

The frequency of corporate scandal in the past decades is alarming and has caused the public to question what the role and impacts that auditors have in corporate governance. The numerous cases of corporate accounting scandal have created crisis of confidence in the accountancy profession though not every case of corporate scandal and failure can be attributed to auditing failure or auditor's negligence. Some of the high profile cases of such corporate scandals are *Enron, WorldCom, Parmalat*, etc.[520]

Auditing has established an enhanced corporate accountability by working with the board of directors and management to improve control and strengthen the financial reporting practices of a company. The goal has been to promote proper conduct of the affairs of the corporation in line with generally accepted accounting, ethical and legal standards. That being the case, the achievement of these objectives provides protection for the shareholders especially their respective interest.

[520] *Ibid*, et el, p. 119.

Auditing ensures checks and balances on the board of directors and management. It is very important to bear on companies the political doctrine of separation of power. That power corrupts and absolute power corrupts absolutely, is a well known adage. To saddle the chairman of a company with the additional duty of chief executive is to make him accountable to himself as he presides over both the board and management and without much power on any other person to question his action or inaction. Same thing applies to the directors that prepare the financial statement of a company.

It is however, auditing that would act as cheek on them and as well the auditors will in turn be accountable and answerable, to the members in general meeting. When this auditing process is there, the directors and the management will be moved to be diligent and careful in performing and carrying out their respective duties without any symptom of negligence on their part.

Another impact of auditing under the rules of corporate governance is publication of credible and reliable information about the subject matter concerned especially to the members. The auditor has done or contributed much in the nation. The credible and reliable information, especially financial statements published, avails the members wherever they are to reasonably determine whether the company they are investing in is worth it. This is because even the company's profit and loss account is also contained in the report. It then leaves the member the choice to decide whether to continue investing in such a company or to decline. The auditing process also is a cheek whether the financial information given to investors is reliable or not. Auditing process has gone very far in establishing confidence and trust on the company which in turn has reduced uncertainty and risk thereby adding value. If there is

confidence and trust among the members in a company it will be a motivating factor that increases their investment in the company thereby enhancing profits.

The efficacy of the accounting system in reducing agency conflicts depends, at least in part, on whether accounting principles are applied in a manner consistent with Generally Accepted Accounting Principles (GAAP), or other standards outlined in the contracting setting. The auditor has served as a central effort beyond it. That is, in order for accounting reports to be effective in reducing agency costs, contracting parties must be provided with some assurance that the financial reports have been prepared in accordance with the provisions of the contract. This gives rise to a demand for auditing, as an audit certification provides some assurance that the financial statements have been prepared in accordance with a set of recognized principles. This assurance can come from either the insurance role of the audit (i.e, the auditor can be sued if there is an error or irregularity), or from the auditors reputation. When financial accounting numbers play a more prominent role in the contract, the demand for auditing is expected to be greater.

It is widely acknowledged that the impact of auditing is very alarming. There is no doubt that auditing has brought about improvement in accountability and transparency in corporate governance thereby reducing the company's death or bankruptcy.

4.8.5 Independence of Auditors

Independence of the auditor is a very vital underlying tool for every audit engagement for good and effective corporate governance. The auditor must be independent of his mind

devoid of any kind of inhibitions especially from the board or management in performing his duties and functions. He should be free to reason the way that he thinks to be the best practice and as well free to evaluate the financial statements the way he chooses to be professional. In this case, accounting scandal and collapse of company can be highly avoided, and on the contrary will lead to winding up of the company. Accordingly, a learned author,[521] in his book stated:

> Both in statutory audit and private audit engagements, the auditor is expected to exercise independence in the performance of his job. This is necessary for him to give an objective and unbiased report. For all statutory audits, the auditor is considered to be independent. Practically however, it is impossible for the auditor to be absolutely independent as envisaged in the act, since he needs to maintain a constructive and proactive working relationship with the directors who actually pay his fee. Nonetheless, the independence of the auditor is very important for any successful audit. The independence of the auditor is not just a matter of fact. It is also a matter of the attitude of his mind. By his conduct, he must be truly independent. To ensure the independence of the auditor, the law grants him substantial rights and protection.[522]

The faith of the stakeholders in the auditor's report is rooted in the fact that auditor is free from the influence of management, that is independent of management. Independence of the auditor is central to audit. The report of auditor who is not seen to be independent may be regarded as unreliable and lacking credibility. Auditors are expected to be independent of the company and report on the company objectively. Actually, auditors can only play their role effectively if they are independent. This is based on the fact that they have to conduct their tasks in the most independent and reliable manner to provide investing public with the level of much assurance to make their decisions base on financial statements.

[521] O. Aguolu, Fundamentals of Auditing, op. cit, p.10.
[522] *Ibid*, p.12.

Auditor independence therefore refers to the independence of the internal auditor or of the external auditor from parties that may have a financial interest in the business audited.[523] Independence requires integrity and an objective approach to the audit process. The concept requires the auditor to carry out his or her work freely and in an objective manner. In addition to a clear understanding of the independence of auditors, independence of internal auditors means independence from parties whose interests might be harmed by the results of an audit. Specific internal management issues are inadequate risk management, inadequate internal controls, and poor governance.[524] Independence of the external auditor, on the other hand, means independence from parties that have an interest in the results published in financial statement of an entity. Auditor independence is commonly referred to as the cornerstone of the auditing profession since it is the foundation of the public's trust in the accounting profession.[525]

On the other hand, Black's Law Dictionary,[526] defined independent audit as an audit conducted by an outside person or firm not connected with the person or organization being audited. It also defined internal audit to mean an audit performed by an organization's personnel to ensure that internal procedures, operations, and accounting practices are in proper order.

Auditors' independence may be threatened by factors such as deriving significant financial interest from a client, provision of non-audit services to a client, having close relationship

[523] Available at: http://on.m.wikipedia.org/wiki/wuditor-indepndence, accessed on 11/05/14.
[524] *Ibid*.
[525] *Ibid*.
[526] B.A. Garner, Black's Law Dictionary, 7th edn, (West Group, St. Paul, Minn., 1999) p. 126.

with a client and intimidation.[527] In recent times, it was reported that the greatest threat to the auditor's independence is the provision of non-audit services to clients.[528] Auditors may compromise their independence because they derived substantially part of their income from non-audit services. Evidence has shown that the large firms derive great part of their income from non-audit services. The problem with provision of non-audit services is that it divides the focus of the auditor and creates unnecessary compromise.[529]

Another area of independence, which not much is talked about, is appointment of external auditors, which in theory is done by the shareholders[530] from recommendations of the directors. In reality, the management does the appointment and auditor may do anything to favour his employer.[531]Safeguards which exist to ensure that threats to auditor's independence are mitigated include: prohibitions, restrictions, policies, procedures and the requirement for disclosures. Notwithstanding the above mitigating factors, the Cadbury's Report532 stated that the auditor's independence could be affected due to the close relationship between auditors and company managers and due to the auditor's intention to develop a constructive relationship with their clients. There are a number of threats to providing non-audit services since non-audit services are lucrative. Auditors can obtain the contracts for non-audit services only if they maintain a good relationship with the management.

[527] J.O. Alabede, 'The Role, Compromise and Problems of the External Auditor in Corporate Governance', *op.cit*, p. 120.
[528] *Ibid*.
[529] *Ibid*.
[530] Companies and Allied Matters Act, Cap. C20, LFN, 2004, S.357(1).
[531] *Ibid*
[532] Report of the Committee on the Financial Aspect of Corporate Governance (1992).

Lack of auditor independence has resulted to corporate accounting scandal and collapse of companies.[533] When there is auditor's independence, it will be difficult to raise the defence that it is clients' responsibility to detect and prevent fraud, error and other irregularities in their company. This is due to the fact that the auditors are still seen as the watchdog that detects when and when not the company is suffering from any ill health or embarking on any unprofitable transaction.

However, on the account of auditor's relationship with their client, in May 2002 the Commission[534] issued a recommendation on the independence of statutory auditors. A recommendation is not legally binding on member states but it is a statement of good practice

[533] J.O. Alabede, *op cit*., p. 119. Note for instance, Enron accounting scandal was a popular one. Enron was established in 1985 as US based energy company and it was prosperous in its early life that its stock increased by about 311% in the 1990s. Though the sign of distress in the company started emerging in 1997 when it wrote off $537 million to settle a contract dispute with another company, it became obvious that Enron was in serious problem when in November, 2001 it restated its account of 1997-2000 to correct accounting abnormality. The restatement brought down its reported earnings for this period by $591 million. Consequently, the credit rating agents downgraded the company and it filed for bankruptcy in December 2001. Arthur Andersen who was the auditor of Enron was accused of negligence in its duty and was criticized of compromising its professional position for financial gain and this led to the winding up of the firm.[533] Another incidence of accounting scandal is the case of WorldCom which is also another high profile accounting scandal resulting from audit failure. WorldCom was US based telecommunication company, which grew rapidly through aggressive acquisition. In 2002, the internal auditors of the company uncovered $3.8 billion fraud perpetrated by inflating the revenue and treating revenue expenses as capital expense. This resulted into $3.3 billion not properly accounted for between 1999 and first quarter of 2002. Arthur Anderson who was the auditor of the company issued a clean health report on the company during the period and did not uncover the fraud.

[534] European Commission Recommendation of 16 May 2002 – Statutory Auditors' Independence in the European Union: A Set of Fundamental Principles', *OJL* 191, 19. 07. 2002, p. 22, cited in B. Hannigan, *Company Law*, (Lexis Nexis, Butterworths, UK, 2013) p. 51.

which the member states are expected to take into account. The key element of the Recommendation is that auditors should be prohibited by law from carrying out a statutory audit if they have any relationship with their client (meaning any financial, business, employment or other link including the provision of non-audit services) that might jeopardize their independence.

As earlier noted, auditor's independence refers to the independence of the internal auditor or of the external auditor from parties that may have a financial interest in the business being audited. Independence requires integrity and an objective approach to the audit process. The concept requires the auditor to carry out his or her work freely and in an objective manner. An independent auditor is a certified public accountant who examines the financial records and business transaction of a company that he/she is not affected with. As it is, an independent auditor is typically used to avoid conflicts of interest and to ensure the integrity of the auditing process. In other words, independent auditors are often used-or even mandated to protect shareholders and potential investors from the occasional fraudulent or unrepresentative financial claims made by public companies.

Auditor's independence is commonly referred to as the cornerstone of the auditing profession since it is the foundation of the public's trust in the accounting profession.[535] Since 2000, a wave of high profile accounting scandals has cast the profession into the limelight, negatively affecting the public perception of auditor independence. The charter of audit and the reporting to an audit committee of the company (and of the internal audit profession) helps to give guidance and independence from suppliers, clients, third parties etc. The support from

[535] D.L. Lindbery & F.D. Beck, 'Before and After Enron: CPAs View on Auditor Independence, 'The CPA journal online, 2004

and in relation to the Audit committee of the client company, the contract and the contractual reference to public accounting standards/ codes generally provides independence from management.

4.8.5.1 The Need for Auditor Independence

The auditor should be independent from the client company. The auditors are expected to give an unbiased and honest professional opinion on the financial statements to the shareholders. Doubts are sometimes expressed regarding the independence of external auditors. It can be argued that unless suitable corporate governance measures are in place, a firm of auditors may reach audit opinions and judgments that are heavily influenced by the wish to maintain good relations with the client company. If this happens, the auditors can no longer be said to be independent and the shareholders cannot rely on their opinion. Further, accounting firms sometimes engage and set auditor fees at less than the market rate and make up for the deficit by providing non-audit services such as management consultancy and tax advice. As a result, some audit firms have commercial interest to protect too. This raises concerns that the auditor's interests to protect shareholders of a company and his commercial interests may conflict with each other.[536] It could be rightly said that auditor independence is important given the numerous advantages enjoyed in such practice. Its importance includes:

a. Provision of Reliable Financial Information: Shareholders and other stakeholders need a trustworthy record of director's stewardship to be able to take decision about

[536] A trite profile example would be the relationship between Enorn and their auditor, Arthur Andddersen. In 2000, Andersen received & s17m for non-audit services, compared with & 25m for anti services. Meaning Enorn accounted for over 25% of the fees general by the firms Houston office. In the after math of Enorn's demise, the accounting firms was accused of not acting independently and suggestions were made that they had gone along with the accounting practices in Enron in order to retain their work.

company. More so, assurance provided by auditors is a key quality control on the reliability of information.

b. The provision of credible financial information: Unqualified report by independent external auditors on the account should give credibility and enhance the appeal of the company to investors. This unqualified report should represent the views of independent expert who are not motivated by personal interests to give a favourable opinion.
c. Value for Money of Auditor Work: A lack of independence seems to mean that important auditor's work may not be done, and thus, shareholders are not receiving value for the audit fees.
d. Threats to Professional Standards: A lack of independence may lead to a failure to form the basis of an audit opinion, in this case, to obtain details of a questionable material item, and failure by auditors to do this undermines the credibility of the accountancy profession and the standards it enforces.

4.8.5.2 Threats to Auditor Independence

The audit profession has recognized the following threats to auditor independence, many of which are linked to the provision of non-audit services:

i. Self interest threats: This involves where an auditor is financially dependent on the audit client or where an auditor or someone closely associated with him has a financial or other interest in the audit client; and the auditor also depends on the management of the company to secure its reappointment as auditor.

ii. Familiarity threats: The relationship between the auditor and client could be long-standing or otherwise is so familiar that the auditor becomes involved in advising the client or acting in a management role.

iii. Self Review Threats: A judgment is required of the auditor which demands that previous work of the firm (whether audit or non-audit) be challenged or re-evaluated.

iv. The Trust Threats: The auditor becomes too trusting of directors and management, thereby preventing a proper testing of management information and representations.

v. The Intimidation Threats: The auditor is intimidated by actual or potential pressures from the client or other party.

vi. The Advocacy Threats: The auditor becomes involved in actively promoting or defending the client's interests.

The need for independence arises because in many cases users of financial statement and other third parties do not have sufficient information or knowledge to understand what is contained in a company's annual accounts. Thus, they rely on the auditor's independent assessment. Public confidence in financial markets and the conduct of public interest entities rely partly on the credibility of the opinions and reports given by auditors in relation with financial audits.

4.9 Impact of the Investment and Securities Tribunal (IST) on Corporate Governance

The tribunal was established under the Investment & Securities Act (ISA).[537] The tribunal is deemed to be a civil Court. It is required to conclude any case before it within 90 days of the commencement of the action. The objective of the court is efficient and timely resolution of investment and capital market disputes with flexibility, transparency and fairness. The tribunal operates both litigation and ADR Centre. The decision of the tribunal is enforced as a

[537] Investment and Securities Act, Cap. I24, Laws of the Federation of Nigeria, 2010, s.274.

judgment of the Federal High Court, and any appeal against its judgment lies directly to the court of Appeal only on points of law, because it is assumed that the capital market assessors who have cognate experience in capital market operations would have resolved all facts relating to the capital market issues at the trial stage at the Investment and Securities Tribunal. The Tribunal is therefore, final court on issues of facts on capital market adjudication.

The Investment and Securities Tribunal is also empowered to adjudicate on pensions disputes in Nigeria.[538] Note that there is likelihood of fusion of pension disputes with capital market disputes given the usual investment of pension funds or assets in the capital market by the Pension Fund Administrators (PFA). Therefore, if any party is dissatisfied with any decision of the National Pension Commission, he may refer the matter to investment and Securities Tribunal.

The exclusive jurisdiction over capital markets and pension disputes poses another jurisdictional challenge to the Federal High Court. Accordingly, Investment and Securities Tribunal shall, to the exclusive of any other court of law or body in Nigeria, exercise jurisdiction to hear and determine any question of law or dispute involving:

(a) a decision or determination of the Commission in the operation and application of this Act, and in particular, relating to any dispute:

    i) between capital market operators
    ii) between capital market operators and their clients
    iii) between an investor and a securities exchange or capital trade point or clearing and settlement agency

[538] Pension Reform Act, Cap. P4, Laws of the Federation of Nigeria, 2010, s.93.

iv) between capital market operators and self regulatory organization

(b) the Commission and self regulatory organization

(c) a capital market operator and the Commission

(d) an investor and the Commission

(e) an issuer of securities and the Commission, and

(f) Dispute arising from the administration, management and operator of collective investment schemes.[539]

The Tribunal shall also exercise jurisdiction in any other matter as may be prescribed by an Act of the National Assembly.[540] In the exercise of its jurisdiction, the Tribunal shall have power to interpret any law, rules and regulations as may be applicable.[541]

4.9.1 The Investment and Securities Tribunal ADR Centre

The IST ADR Centre is designed to provide sessions for various alternative dispute resolution options such as mediation, conciliation or early neutral evaluation. The ADR processes include negotiation, mediation and arbitration. The ADR centre was established essentially to enable quick access to justice.[542] The IST is empowered to promote reconciliation among parties to an action and encourage and facilitate amicable settlement of disputes which the Tribunal does through the application of ADR principles.[543] The objective is to assist disputing parties using a structured process to create a voluntary and functional agreement suiting to the needs of the parties.

4.9.2 The Jurisdiction Conflict between the Federal High Court and the Investment and Securities Tribunal (IST)

[539] N.C.S. Ogbuanya, *Essentials of Corporate Law Practice*, (Lagos: Novena Publishers Ltd), p. 636.
[540] Investment and Securities Act, Cap. I24, Laws of the Federation of Nigeria, 2010, s.284(2).
[541] *Ibid*., s.284(3).
[542] Investment and Securities Tribunal (Procedure) Rules 2003, Rules 3(2), 4 and 34(1).
[543] *Ibid*., Rule 4.

In view of the corporate matters covered by s. 284 of ISA, and the exclusive jurisdiction granted to the Tribunal by virtue of s. 294 ISA, a jurisdictional conflict is raised between the Tribunal and the Federal High Court which has exclusive jurisdiction over matters arising from the operation of the Companies and Allied Matters Act or any other enactment regulating the operations of companies incorporated under the Act.[544] The Investment & Securities Tribunal has held that it has competence to deal with matters contained in the Companies and Allied Matters Act (CAMA). It is however submitted on the contrary that disputes involving Securities & Exchange Commission (SEC), being an apex regulator of the capital market should be removed from the jurisdiction of the Investments and Securities Tribunal and be left for the Federal High Court since they constitute matters involving disputes over decisions of a Federal Government agency.[545] It is argued that the Federal High Court is better disposed and equipped for any such litigation which falls within its jurisdiction scope under s. 251(1) of the 1999 constitution, because of its structural guides for fair hearing.

The adjudicatory powers of the IST appear to have dwindled given that SEC has been made a trial adjudicator on major capital market disputes. The IST is thereby made to assume jurisdiction only after SEC has heard a matter and a party has cause to complain against its decision.[546]

4.9.3 The Role of Securities and Exchange Commission (SEC)

In a bid to maintain effective regulation of the capital market, the SEC plays the following roles:

[544] Constitution of the Federal Republic of Nigeria, 1999 (as amended), s.251(1)(e); Federal High Court Act, Cap. F12, LFN, 2010, s.7(1)(c)(i).
[545] *FIS Securities Ltd v SEC,* NISLR 165.
[546] N.C.S. Ogbuanya, *op. cit.,* p.638.

(i) Ensures good corporate governance by providing a code of best practices to be complied by all listed public companies so as to prevent corporate failures.

(ii) Educates investors through workshops, advertisements, etc.

(iii) Bringing all capital market operators under control and supervision through licensing.

(iv) Ensures public companies observe effective control of financial reporting and disclosure of quarterly returns.

(v) Formulate accounting standards for public companies, and ensures that they make annual and periodic reports to the Commission.

(vi) Ensures that auditors of public companies are registered with the Commission.

(vii) Ensures compliance with disclosure requirements by companies under the ISA, by scrutinizing every prospective before registration.

(viii) Stands as quasi-judicial body by being given opportunity to attend to cases and complaints by capital market operator, investors and relevant institutions.

(ix) Sanctions capital market operators, companies and officers who fail to comply with the standard prescribed by the Commission.[547]

4.10 Corporate Restructuring as a Corporate Governance Tool

The incorporation of a company ushers in a company, and the company is expected to commence active life as a going concern. In the course of time, the company is prompted by changes in its business fortune, economic realities as well as changes in corporate legal framework, to restructure itself. The increasing buoyancy or even downward turn in the progress of the company business could necessitate the restructuring of the company. The restructuring can be in the form of arrangement and compromise, arrangement on sale, merger and acquisition, take-over, etc. It is left for the company to choose any of the

[547] Y.H. Bhadmus, *op. cit.,* p.384; *First Bank of Nigeria Plc v Banjo* (2015) 5 N.W.L.R. (Pt. 1452) p.253 at 259; *Oni v Administrative Proceedings Comm., SEC* (2014) 13 N.W.L.R. p.334 at 337.

foregoing options depending on the business strategies the company wants to adopt and depending also on the state of affairs of the business of the company.

4.10.1 Arrangement and Compromise

The two terms are practically used interchangeably. Arrangement is therefore any change in the rights and liabilities of members, debenture holders or creditors of a company or any class of them or in the regulation of a company other than a charge effected under any other provision of the Act or by the unanimous agreement of all parties affected thereby.[548] This involves a negotiation whereby the company seeks a variation or relinquishment of its obligations to its shareholders or debenture holders. In this ways, the rights of the members or creditors are altered and the process sanctioned by the court. The act of compromise and arrangement facilitates, for instance, the modification of class rights once the majority of them assent to the arrangement. However, the court shall ensure that the terms of arrangement are fair and equitable in the circumstance and proceed to sanction it. Once the scheme is sanctioned by the court, it becomes binding on the company and the affected members or creditors.

Where a compromise or arrangement is proposed between a company and its creditors or any class of them or between the company and its members or any class of them, the court may, on the application in a summary way, of the company or any of its creditors or members or, in the case of a company being wound up, of the liquidator, order a meeting of the creditors or class of creditors , or of the members of the company, or class of members, as the case may be, to be summoned in such a manner as the court directs.[549]The court has held that

[548] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria, 2010, s.537.
[549] *Ibid.,* s.539.

compromise involve some dispute, arguing that there can be no compromise unless there is some dispute.[550]

4.10.2 Arrangement on Sale

A company, in a bid to effect any arrangement, may by special resolution resolve that the company be put into members' voluntary winding up, and that the liquidator be authorized to sell the whole or part of its undertaking or assets to another body corporate in consideration or part consideration of fully paid shares, and distribute the same in specie among the members of the company in accordance with their rights in the liquidation.[551] The money realized can be used in the flotation of a new company or as equity contribution to any scheme of arrangement for restructuring, such as merger. The winding up embarked on during restructuring results in the resurrection of the company in another form, either as a new company or the company in another form; whereas the winding up for liquidation of the company brings the company to a permanent end since the assets are distributed to those entitled according to the rules of distribution of assets of dissolved company.

Note that the liquidator must be authorized to carry out the sale and the authority must be given to the liquidator by a special resolution.[552]

4.10.3 Merger and Acquisition

Merger and acquisition is one of the most expedient restructuring options which has an enduring effect of addressing business problems as well as enhancing business efficiency and profitability. Although mergers and acquisitions are often used synonymously, there exist clear distinctions. Merger is a business combination which involves the fusion of two or more corporate entities into one largely of equal terms. The evolving corporate entity may

[550] *Sneath v. Valley Gold Ltd*. (1983) 1 Ch. 477.
[551] Companies and Allied Matters Act, *op. cit.* s.538.
[552] *Etheridge v Central Uruguayan Northern Extension Railway* (1913) 1Ch. 425.

retain the name or identity of one of the merging companies or assume a completely different name. Acquisition, on the other hand is the purchase of all or substantial interest of one company by another.[553] Hence, the acquired company becomes a subsidiary or division of the acquiring company. There are plethora of reasons for a company to embrace merger and acquisition:

i. It is easier and cost effective for a company to diversify its operations or business, thereby reducing business risk, by means of merger and acquisition.
ii. The amalgamation of entities leads to expanded growth of business and enhanced productive capacity of the evolving corporate entity.
iii. It enhances a company's chance of meeting the requirements for listing at the Stock Exchange.
iv. It brings about corporate leverage by helping a company to improve its debt/equity ratio.
v. It helps a company to embrace technological drive by merging with another which has technological advantage over it.
vi. It enhances management expertise via capacity building, technical and managerial skills necessary to achieve its corporate objective of quality and increased production.
vii. It gives opportunity to harness the facilities of the other company to achieve the desired growth
viii. It helps companies to survive regulatory requirements for consolidation.

Companies proposing a merger, acquisition or other forms of business combination shall:

i. File with the SEC, a pre-merger notice for evaluation;
ii. Upon notification of approval in principle, of (i) above, file a draft scheme of arrangement for clearance;

[553] Afolabi v Western Steel Works Ltd. (2012) 17 N.W.L.R. p.287 at 290.

iii. File an application in the Federal High Court seeking an order to convene a court ordered meeting;

iv. Following the resolution of the shareholders at the court ordered meeting, the applicants shall file with the SEC, a formal application for approval of the merger.

Note that pre-merger notice shall be filed by submitting to the Commission a report which shall contain material particulars of the merging companies.

The Securities and Exchange Commission is however empowered to revoke the decision on approved or conditionally approved merger scheme under any of the categories, based on the following:

(a) Incorrect information for which a party to the merger is responsible; or

(b) An approval obtained by deceit; or

(c) Breach of an obligation attached to the merger by any of the merging parties.

Note that the power of revocation is unreserved and is not barred by any time limit stipulated under the Act.

The SEC also has powers to break up companies to forestall unnecessary monopoly. The major regulatory strategy to checkmate monopoly of dominant companies is the anti-trust provisions in the ISA, empowering SEC to order break up of company creating a monopoly and engages in anti-competition conducts. The SEC consequently refers such directive to break up to the Federal High Court for sanctioning. Upon the sanctioning by the court, the affected companies must be bound by it.

4.10.4 Take-Over

This is a restructuring process which results in the acquisition of a substantial interest (shares) either by an individual or company in another company sufficient enough to give the

acquiring company substantial control over the management of the target company.[554] When an individual or group of individual investors acquires the requisite sufficient and controlling shares in the target company, he/they would be referred to as the core investor(s) of the target company. If it is a corporate investor, the acquiring company and the target company would form a single group. The bigger and stronger company (acquirer) is the holding company and the smaller or weaker (target) company becomes the subsidiary. Under this arrangement, both companies exist without losing their individual identities.

Upon the acquisition of the requisite 30-50% of the called up shares of the target company, the acquirer can proceed with takeover bid in accordance with Rules 235 SEC Rules 2007 as amended 2010.[555] Some shareholders who do not accept the acquisition scheme of the company may decline to accept the offer to surrender their shares for purchase by the acquiring company. If the dissenting shareholders and the quantity of shares they possess are so much as to prevent the acquiring company from possessing the number of shares required to achieve a successful bid, then the bid is bound to fail. On the contrary, the dissenting shareholders of the target company cannot prevent the takeover bid.[556]

4.11 The Impact of Central Bank of Nigeria (CBN) on Corporate Governance in the Nigerian Banking Industry

The CBN identified some problems and weaknesses in corporate governance in banks in Nigeria. There are namely:

i. Disagreement between Board and Management giving rise to Board squabbles.

ii. Ineffective Board oversight functions

[554] Afolabi v Western Steel Works Ltd., *supra.*
[555] Investment and Securities Act, *op. cit.,* s.131(1).
[556] *Ibid.,* ss.146-147.

iii. Fraudulent and self-serving practices among members of the Board, Management and Staff.
iv. Overbearing influence of Chairman or MD/CEO especially in family-controlled banks.
v. Weak internal controls.
vi. Ignorance of and non-compliance with rules, laws and regulations guiding banking business.
vii. Non-compliance with laid down internal controls and operations procedures
viii. Passive shareholders
ix. Poor risk management practices resulting in large quantum of non-performing credits including insider-related credits.
x. Sit-tight directors even where such directors fail to make meaningful contributions to the growth and development of the bank.
xi. Succumbing of pressure from other stakeholders' appetite for high dividend and depositors' quest for high interest on deposits.
xii. Technical incompetence, poor leadership and administrative inability.
xiii. Inability to plan and respond to changing business circumstances.
xiv. Ineffective management information system. [557]

Banks occupy a unique position in an economy. They are critical to the efficient functioning of the economy. This is by virtue of their role as financial intermediaries. In that capacity, they mobilise savings and use such funds to support productive activities. Given the pivotal nature of this role from the viewpoint of economic advancement of any country, it is crucial for the banking industry to be virile, safe and sound. It is equally important for the health of

[557] CBN, 'Code of Corporate Governance for Banks in Nigeria Post Consolidation' (2006), available at: http:// www.cenbank.org., accessed on 17/05/2014.

each institution to be guaranteed. This explains why the issue of sound corporate governance in the industry cannot be taken lightly.

In view of the foregoing, it was not surprising that analysts and stakeholders were concerned about the quality of corporate governance in the Nigerian banking industry prior to the consolidation programme. It would be recalled that poor corporate governance practices were one of the justifications why the CBN, under the leadership of the past governor, Professor Charles Soludo, introduced the banking sector reform programme.[558]

4.12 Winding-Up of Companies As a Corporate Governance Measure

Winding up of an incorporated company is part of the corporate governance process, which seek to protect the interest of its members and creditors in the event that the company can no longer remain a going concern. Rather than allowing the company to collapse and its assets dissipated, it becomes imperative for the said company to be subjected to a formal process of liquidation called winding up. The incorporation of a company brings its life span to perpetuity. Once a company is incorporated, it acquires perpetuity of life span except it is subjected to winding up. The process of bringing a company into extinction therefore is by winding up. Winding up is the process whereby the company is liquidated and its assets administered for the benefit of creditors, members and employees. There are two basic ways the life of a company can be brought to an end, to wit:

(i) By the process of winding up as provided in the Act

(ii) By striking off the name of the company from register of companies for being defunct by the Corporate Affairs Commission (CAC).[559]

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[558] In his address at the special meeting of the Bankers Committee held on the 6th July, 2004, the then CBN Governor stated inter alia, that there were several instances where board members and management staff failed to uphold and promote the basic pillars of sound corporate governance because they were pre-occupied with the attainment of narrowly defined interests.

[559] Companies and Allied Matters Act, *op. cit.* s.525.

Unlike other business and non business organizations, only companies undergo both winding up and dissolution processes, and there are three modes of winding-up:

(i) Winding up by the court (Compulsory winding up)

(ii) Voluntary winding up (members voluntary winding up and creditors voluntary winding up)

(iii) Winding up subject to the supervision of the court.[560]

A. Winding Up by the Court / Compulsory Winding Up

The following are the grounds upon which a company shall be wound up: [561]

(a) The company has by special resolution resolved that the company be wound up by the court

(b) Default is made in delivering the statutory report to the Corporate Affairs Commission or in holding the statutory meeting

(c) The number of members is reduced below two

(d) The company is unable to pay its debts[562]

(e) The court is of opinion that it is just and equitable that the company should be wound up.[563]

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[560] In Re: Amolegbe (2014) 8N.W.L.R. p.76 at 84

[561] *Ibid.,* s. 408; *G. E. B. Plc v. Odukwu* (2009) 14 N.W.L.R. (pt. 1160)p. 43.

[562] *Ibid.,* s. 408; Note that a company is deemed unable to pay its debt under the following circumstances:

(a) A creditor, by assignment or otherwise, to whom the company is indebted in a sum exceeding ₦2, 000 then due has served on the company, by leaving it at its registered office or head office, a demand under his hand requiring the company to pay the sum so due, and the company has for three weeks thereafter neglected to pay the sum or to secure or compound for it to the reasonable satisfaction of the creditor; or

(b) Execution or other processes issued on a judgment, decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or

(c) The court, taking into account any contingent or prospective liability of the company is satisfied that the company is unable to pay its debts; *Tate Industries PLC v. Devcom M. B. Ltd* (2004) 17 N.W.L.R. (Pt. 901) 182; *Ado Ibrahim & Co. Ltd. v B.C.C. Ltd.* (2007) 15 N.W.L.R. (Pt.1058) p.538; *Pharma-Deko Plc v Financial Derivates Co. Ltd* (2015) 10 N.W.L.R. (Pt.1467), p.225 at 233.

[563] *First Equity Securities Ltd. v Mr. Victor Anozie* (2015) 12 N.W.L.R. (Pt.1473) p.337 at 344.

Winding up of a company or the appointment of liquidator does not by itself lead to the death of the company. Under winding up, a company is still alive. It can only die at the point of its dissolution. However, if a winding up order is made or a provisional liquidator is appointed, no action or proceeding shall be proceeded with or commenced against the company except by leave of the court.[564]

B. Voluntary Winding Up

Voluntary winding up shall be either by members or by the creditors. In members' voluntary winding up, the company makes declaration of solvency and delivers the same to CAC for registration, the company calls a general meeting and appoints one or more liquidators to wind up the affairs of the company. Consequently, all the powers of the directors cease. Upon the winding up of the affairs of the company, the auditor will prepare and send to every member of the company financial accounts of the winding up showing how the winding up has been conducted, and the result of the trading during such time as the business of the company had been disposed of. The liquidator shall thereafter convene a general meeting of the company for the purpose of laying the accounts before it. The liquidator sends copies of the accounts and a statement of the holding of the meeting and its date to CAC within 28 days after the said meeting.[565]

In creditors' voluntary winding up, no declaration of solvency is made. In this case, separate meetings of the members and creditors must first hold. The company will summon a meeting of the creditors of the company for the day, or the day next following the day on which the company is to hold the meeting at which it is to propose the resolution for voluntary winding up.

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[564] *Onwuchekwa v. N. D. I. C.* (2002) 5 N.W.L.R. (Pt.760) 371 at 393.
[565] Companies and Allied Matters Act, *op. cit.* ss.463-470.

The meeting of the creditors will be presided over by the directors of the company. The director shall cause a full statement of the position of the company's affairs together with a list of the creditors of the company and the estimated amount of their claims to be laid before the meeting.

At their respective meetings, the creditors and the company may nominate a person to be the liquidator. If different persons are nominate as liquidators at the separate meetings of creditors and of the company, then the person nominated by the creditors shall be the liquidator. If no person is nominated by the creditors, then the person nominated by the members shall be the liquidator.[566] Alternatively, a director, member or creditor may apply to court to order otherwise. All powers of the director must cease on the appointment of the liquidator unless otherwise permitted by the committee of inspection (if any) or the creditors. Note that any vacancy arising in the position of a liquidator (other than one appointed by court) may be filled by the creditors.[567]

In the event of the winding up continuing for more than one year, the liquidator must call a meeting of the company and a meeting of the creditors at the end of the first year of the commencement of the winding up, and in every subsequent year and lay before the meetings and account of his acts and dealings and of the conduct of the winding up during the preceding year.[568]

As soon as the affairs of the company have been fully wound up, the liquidator must prepare an account of the winding up showing how the winding up has been disposed of. He will then call a general meeting of the company and a meeting of the creditors and lay the account

[566] *Ibid.,* s.473.
[567] *Ibid.,* s.476.
[568] *Ibid.,* s.477.

before them, with explanations thereof.[569] The meeting must be called by notice published in the Gazette and in some newspapers printed in Nigeria and circulating in the locality where the meeting is being called at least one month before the meeting.[570]The liquidator must send a copy of the account to the CAC and make a return on the holding of the meeting within 7 days after the said meeting.[571]

On the receipt of the account and the returns, the CAC must register them, and on the expiration of three months from the date of registration of same, the company will be deemed to be dissolved unless the date of dissolution of the company is deferred by the order of the court.[572]

C. Winding Up Subject to Supervision of Court

Where a company passes a resolution for voluntary winding up, the court may, on petition, order that the voluntary winding up shall continue subject to the supervision of the court and on such terms and conditions as the court may think fit.[573] A petition for winding up subject to the supervision of the court operates for most purpose as a petition for winding up by the court.[574] The court in making the supervision may appoint additional liquidator to act with the existing liquidator.[575] Note that order of supervision does not change the date of commencement of the winding up which remains the day the resolution for voluntary winding up was passed by the company in general meeting.

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569 *Ibid.,* s.478(1).
570 *Ibid.,* s.478(2).
571 *Ibid.,* s.478(3).
572 *Ibid.,* s.478(4).
573 *Ibid.,* s.486.
574 *Ibid.,* ss.487 and 490..
575 *Ibid.,* s.489(1).

CHAPTER FIVE

CORPORATE GOVERNANCE: CORPORATE RISK MANAGEMENT

5.1 Introduction

The role of auditors in enterprise risk management has become increasingly challenging as expectations for board engagement are at all time high. This presupposes that while business leaders know organizations must regularly take risks to enhance stakeholder value, effective organizations recognize strategic advantages in managing risks. To actualize these anticipated advantages in managing risks, auditors play the all important role of internal auditing. Internal auditing is an independent, objective assurance and consulting activity. Its core role with regard to enterprise risk management is to provide objective assurance to the board on the effectiveness of risk management, and this will form the basis of discourse in this chapter.

5.2 The Role of Auditors in Risk Management

Indeed, research has shown that internal auditors agree that the two most important ways that internal auditing provide value to the organization are in providing objective assurance that the major business risks are being managed appropriately and providing assurance that the risk management and internal control framework is operating effectively.[576] Internal auditors will normally provide assurances on three key areas:

i. Risk management process, both their design and how well they are working;
ii. Management of those risks classified as key, including the effectiveness of the controls and other responses to them; and
iii. Reliable and appropriate assessment of risks and reporting of risk and control status.

[576] The Value Agenda, Institute of Internal Auditors – Uk and Ireland and Deloitte and Touche 2003. See also the Institute of Internal Auditors (11A) Position Paper: The Role of Internal Auditing in Enterprise-Wide Risk Management (Issued January, 2009 Revised) p. 3.

Although everyone in the organization plays a role in ensuring successful enterprise- wide risk management, the primary responsibility for indentifying risk and managing them however lies with management comprising of auditors and board of directors. The main factors that chief audit executives (CAES) should or normally take into account when determining internal auditor's role are whether the activity raises any threats to the internal auditors' independence and objectivity, and whether it is likely to improve the organization's risk management, control and governance processes. The Institute of Internal Auditors' (IIA's) position paper indicates which roles internal auditing should and should not play throughout the enterprise risk management (ERM) process. Below are some of the core internal auditing roles in regard to ERM process.

i. Giving assurance on risk management processes. This of course includes an objective examination of evidence for the purpose of providing an independent assessment on risk management, control, or governance processes for the organization. Example may include financial, performance, compliance, system security, and due diligence engagements.
ii. Giving assurance that risks are correctly evaluated
iii. Evaluating risk management processes
iv. Evaluating risk reporting of key risks
v. Reviewing the management of key risk

Legitimate Internal Auditing Roles with Safeguards

i. Facilitating identification and evaluation of risks
ii. Coaching management in responding to risks
iii. Coordinating Enterprise risk management activities
iv. Consolidating the reporting on risks
v. Maintaining and developing the Enterprise Risk Management (ERM) framework

vi. Championing establishment of ERM.

vii. Developing risk management strategy for board approval.[577]

Roles that Internal Auditing Should Not Undertake

i. Setting the risk appetite: Risk appetite in this context means the level of risk that is acceptable to the board or management. This may be set in relation to the organization as a whole, for different groups of risks or at an individual risk level.

ii. Imposing risk management processes: Risk management processes include processes to identify, assess, manage, and control potential events or situations, to provide reasonable assurance regarding the achievement of the organization's objectives.

iii. Management assurance on risks

iv. Taking decisions on risk responses: Risk response here means the means by which an organization elects to manage individual risks. The main categories are to tolerate the risk; to treat it by reducing its impact or likelihood, to transfer it to another organization or to terminate the activity creating it. Internal controls are one way of treating risk

v. Implementing risk responses on management's behalf

vi. Accountability for risk management

vii. Internal audit cannot also give objective assurance on any part of the ERM framework for which it is responsible. Such assurance should be provided by other suitably qualified parties.[578]

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[577] See the Institute of Internal Auditors-The Role of Internal Auditing in Enterprise-Wide Risk management, September, 29, 2004, pp. 1-2.

[578] The IIA-UK and Ireland Position Statement on Risk Based Internal Auditing, 2003. Also Attributable Standard 1130 cited in the Institute of Internal Auditors-The Role of Internal Audit in Enterprise-Wide Risk Management, 2004 Edition, p. 5.

Internal auditors thus should provide advice, and challenge or support management's decisions on risk, as opposed to making risk management decisions. In other words, the nature of internal auditing responsibilities should be documented in the audit charter and approved by the audit committee. Internal audit may provide consulting services that improve an organization's governance, risk management, and control processes. The extent of internal audit's consulting role in enterprise risk management will depend on the other resources, internal and external, available to the board and on the risk maturity[579] of the organization and it is likely to vary overtime. Perhaps, internal audit's expertise in considering risk, in understanding the connections between risk and governance and in facilitation means that it is well qualified to act as champion and even project manager for Enterprise Risk Management (ERM), especially in the early stages of its introduction. In most cases however, as the organization's risk maturity increases and risk management becomes more embedded in the operations of the business, internal auditor's role in championing ERM may reduce on the one hand. On the other hand, if an organization employs the services of a risk management specialist or functions, internal audit is more likely to give value by concentrating on its assurance role, than by undertaking the more consulting activities. It is however warned, that if internal audit has not yet adopted the risk-based approach, it is unlikely to be equipped to undertake the consulting role activities in the centre.

5.3 Consulting Roles of Auditors in Risk Management

Some of the consulting roles that internal audit/auditors may undertake according to IIA-statement are:

i. Making available to management tools and techniques used by internal audit to analyze risks and controls;

[579] The Institute of Internal Auditors (IIA) –Uk and Ireland Position Statement on Risk Based Internal Auditing, 2003.

ii. Being a champion for introducing ERM into the organization, leveraging its expertise in risk management and control and its overall knowledge of the organization;
iii. Providing advice, facilitating workshops, coaching the organization on risk and control and promoting the development of a common language, framework and understanding;
iv. Acting as the central point for coordinating, monitoring and reporting on risks; and
v. Supporting managers as they work to identify the best way to mitigate risk.

Of course, the key factor in deciding whether consulting service are compatible with assurance role is to determine whether the internal auditor is assuming any management responsibility. In the case of ERM, internal audit can provide consulting services so long as it has no role in actually managing risk, i.e. management's responsibility, and so long as senior management actively endorse and support enterprise risk management. It is our proposition here that whenever internal audit acts to help the management team to set up or to improve risk management processes, its plan of work should in the main include a clear and identifiable strategy and timeline for migrating the responsibility for these activities to members of the management team. Internal audit may extent its involvement in ERM or corporate risk management, provided that certain conditions apply. It is these conditions that Institute of Internal Auditors (IIA) technically called 'safeguards and they are:

i. It should be clear that management remains responsible for risk management.
ii. The nature of internal audit's responsibilities should be documented in the audit charter and approved by the Audit Committee[580]
iii. Internal audit should provide advice, challenge and support to management's decision making, as opposed to taking risk management decisions themselves.

[580] Attribute Standard 1000. C1 (Quoted in the IIA-CK and Ireland Position Statement on Risk Based Internal Auditing, 2004).

iv. Internal audit cannot also as noted earlier in this work give objective assurance on any part of the ERM framework for which it is responsible. Such assurance should be provided by other suitably qualified parties.[581]

v. Any work beyond the assurance activities should be recognized as a consulting engagement and the implementation standards related to such engagements should be followed.[582]

Worthy of note is the fact that internal auditors and risk managers share some knowledge, skills and values. Both, for example, understand corporate governance requirements; have project management, analytical and facilitation skills and values having a healthy balance of risk rather than extreme risk taking or avoidance behaviours. This is more so, as risk management is a fundamental element/component of corporate governance.

Sobel[583] opined that auditors' roles in corporate risks management should extend further to:

(i) Evaluation of strategic risks; i.e. Whether management has:

a. comprehensively identified key strategic risks,
b. developed prudent risk management techniques to address those risks, and
c. established sufficient monitoring of strategic risk 'signposts' to identify risk occurrence in time to take appropriate actions.

(ii) Devote the time, resources, and leadership to developing internal audit teams so that they have the right level of skills and experience related to risk management.

[581] Attribute Standard 1130 (Quoted in the IIA-UK and Ireland Position Statement on Risk-Based Internal Auditing, 2004)

[582] Performance Standards 2010, C1, 2110. C1 and C2, 2120 C1 & C2, 2130. C1, 2201. C1, 2210. C1, 2220. C1, 2240. C1, 2330. C1, 2410. C1, 2440. C1 & C2 and 2500. (Quoted in IIA).

[583] P.J. Sobel, 'Internal Auditing's Role in Risk Management', *The Institute of Internal Auditors Research Foundation*, March, 2011 p. 4.

(iii) Use third-party and other internal resources to supplement the risk management skills of the internal audit activity. This of course may be very challenging for many chief audit executives (CAES), but those with the right level of skills, experience, and confidence and a sufficiently high position in the organization, will be able to carry out their roles and truly add value to their organizations.

In fact, since the 2008 financial crisis that shocked the business world, regulatory and economic pressures are forcing auditors of corporate organizations to a more thorough job when conducting enterprise wide risk assessments, pursue strategic opportunities in a risk effective manner, increase the effectiveness of risk mitigation efforts, and focus on a more holistic approach to risk management.

According to a 2010 Institute of Internal Auditor (IIA), Global Internal Audit Survey [a component of the Common Body of Knowledge (CBOK) studies], about 57 percent of internal audit activities around the world perform audits of enterprise risk management processes. Furthermore, about 20 percent of respondents indicate that they believed that performing current roles for internal auditing would become more prominent over the next five years.[584] However, it is important to note that the study also concluded that to play a more effective role in risk management and governance, more resources are needed. This means hiring people with the right qualifications and/of buying the necessary tools to optimize the efficiency of the audit work.[585]

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[584] 2010 IIA Global Internal Audit Survey: A Component of the CBOK Study, Report I, Characteristic of an Internal Audit Activity (Altamonte Springs, FL: the Institute of Internal Auditors Research Foundation, 2010).
[585] 2010 IIA Global Internal Audit Survey: A Component of the CBOK Study, Report IV, What's Next for Internal Auditing? (Altamonte Springs, FL: The Institute of Internal Auditors Research Foundation, 2011).

Similarly, another study revealed and rated ‘enterprise risk management’ the fifth most important knowledge area for internal auditors (58 percent).[586] The survey included more than 13,500 useable responses from respondents in more than 107 countries; so it clearly represents a global view or perspective of the most important skills for internal auditors.

As to what skills internal auditors should be focusing on to ensure they can effectively play their auditing roles, the Global Internal Audit Survey (GIAS) flash survey asked that very question; specifically: ‘To effectively assess risk management in an organization, what are the skill sets and expertise required.’ The most frequent responses were:

i. Business and industry understanding/knowledge
ii. Risk management expertise/knowledge
iii. Good Communication skills - facilitation, negotiation, and interviewing
iv. Analytical skills
v. Comprehensive internal audit knowledge and experience
vi. Expertise in specialized areas, other than finance, and their related controls
vii. Knowledge of finance process, controls, and risk.[587] In a similar vein, Chief Audit Executives (CAES) participating in a March 2009 roundtable discussion on several ways of enhancing internal audit efforts recommended actions that internal auditors can take to help their organization adopt a more strategic risk management focus.

    They include:

a. Ensuring that risk assessment identifies those risks presenting the most significant risks to shareholder value
b. Facilitating risk management discussions across the organization.

[586] 2010 IIA Global Internal Audit Survey: A Component of the CBOK Study, Report II, Core Competencies for Today’s Internal Auditor (Altamonte Springs, FL: The Institute of Internal Auditors Research Foundation, 2010).

[587] IIA GAIN Flash Survey, Internal Auditing’s Role in Risk Management, August, 2009.

c. Viewing risk management as a core competency and ensuring that auditors receive appropriate training on risk and management practices.
d. Reviewing business plans to determine whether they assess the risk embedded in their strategies and have risk monitoring and trigger points.
e. Reviewing the annual report to determine whether risks are addressed appropriately.
f. Continuously monitoring and assessing stakeholder expectations relative to risk and risk management, as well as assisting in the education of these stakeholders.
g. Building a stronger relationship with other risk and control business functions to drive an enhanced process to identify emerging risks.
h. Identifying and sharing best practices in risk management.[588]

Thus, the role of corporate auditors in risk management is very central and core to the survival of any corporate institution regard being had to the enormous roles, duties and responsibilities discharged by internal corporate auditors in running the day to day activities of the company.

5.4 The Role of Directors in Risk Management

The company's directors in a narrower sense and board of directors in a wider sense play a critical role in overseeing an enterprise - wide approach to risk management. Because management is accountable to the board of directors, the board's focus on effective risk oversight role is critical to setting the tone and culture towards effective risk management through strategy setting, formulating high level objectives, and approving broad-based resource allocations. This of course is the more reason why Enterprise Risk Management has been described as a process, effected by the entity's board of directors, management, and other personnel; applied in strategy setting and across the enterprise; designed to identify

[588] IIA Knowledge Report, Internal Auditing and Risk Management, October, 2009, cited in P.J. Sobel, Internal Auditing's Role in Risk Management – The Institute of Internal Auditors Research Foundation, March, 2011, *op. cit*, p. 18.

potential events that may affect the company, and manage risk to be within the risk appetite; and to provide reasonable assurance regarding the achievement of objectives.[589] Corporate directors are embracing the concept of enterprise risk management to better connect their risk oversight with the creation and protection of stakeholder value. Corporate directors thus adopt a robust and holistic top-down view of key risk facing an organization. While Enterprise Risk Management (ERM) is not a total panacea for all the turmoil experienced in the markets in recent years, robust engagement by the directors in enterprise risk oversight strengthens an organization's resilience to significant risk exposures. Following the fallout of the 2008 financial crisis, directors or the board of directors are being asked, and many are asking themselves: Could they have done a better job in overseeing the management of their organization's risk exposures and could improved board oversight have prevented or minimized the impact of the financial crisis on their organization?[590] In the United States, for example, the country's Securities and Exchange Commission (SEC) has recently considered whether greater disclosure is needed about how a company and the company's board in particular manage risk, both generally and in the context of setting compensation.[591] This is quite suggestive of the fact that corporate directors role nowadays is predominantly geared towards effectively overseeing the company's or organization's enterprise - wide risk management, in a way that balances managing risk while adding value to the organization. The question may be asked 'How do the corporate directors or board of directors carry out their most significant oversight roles in risk management within the company or the organization? It does seem that directors or board of directors across the world (though more

[589] Committee of Sponsoring Organisations of the Trade way Commission (COSO's), Enterprise Risk Management - Integrated Framework September, 2004, available at: www.coso.org, accessed on 11/08/2013, New York, NY.
[590] COSO-Effective Enterprise Risk Oversight: The Role of the Board of Directors, 2009, available at: www.COSO.org, accessed on 11/08/2013 New York, NY.
[591] U.S. Securities and Exchange Commission, speech by SC Chairman, Mary Schapiro: Address to the Council of Institutional Investors, April, 2009, available at: www.Sec.gov/new/speech/2009/specho40609. accessed on 11/08/2013.

prevalent in the United States) use board committees in carrying out certain of their oversight duties. The use and focus of committees vary from one company to another, although common committees are the audit committee, nominating/governance committees, compensation committees, with each focusing attention on element of enterprise risk management. While risk oversight, like strategy, is a full board responsibility, some companies may choose to start the process by asking the relevant committees to address risk oversight in their areas while focusing on strategic risk issues in the full board discussion.

In so doing, board of directors use the mechanism of Enterprise Risk Management to provide a path of greater awareness of the risks the organization faces and their inter-related risks, and more transparent decision making around risk/reward trade-offs, which can contribute toward greater likelihood of the achievement of objectives.

Specifically, for the banking industry, key risk management steps that directors should take in discharging their corporate risk oversight roles have been suggested.[592] These steps may be categorized into five – identify, assess, control, report, manage and challenge.

A. **Identify:** Under this heading, the following steps are suggested:
   i. Identify the risk inherent in achieving the Bank's goals and objectives.
   ii. Establish risk appetite across the entire risk spectrum.
   iii. Establish and communicate risk management frameworks.

B. **Assess:** Under this heading, the following steps are proposed:
   i. Build accurate and consistence risk assessment.
   ii. Establish and implement measurement reporting standards/methodologies.
   iii. Build a risk profile for the Bank.

[592] T. Oshikoya, 'Corporate Governance and Risk Management,' *GARP*, July, 2012, p. 58.

C. **Control:** Additional steps proposed here are:

i. Establish key control processes, practices, and reporting requirements.

ii. Monitor the effectiveness of control.

iii. Ensure all the Bank's exposures are adequately identified, measured and managed in accordance with Board approved framework.

iv. Provide early warning signals. Ensure risk management practices are adequate and appropriate for managing the Bank's risks.

D. **Report:** The following are suggested:

i. Report areas of stress where crystallization of risk is imminent.

ii. Present remedial actions to reduce and/or mitigate such risks.

iii. Report on sensitive and key risk indicators.

iv. Communicate with relevant parties.

E. **Manage and Challenge:** The following is further suggested:

i. Review and challenge all aspects of the Bank's risk profile

ii. Advise on optimizing and improving the Bank's risk profile.

iii. Review and challenge risk management practices

Aside the above, COSO[593] had earlier in 2004 presented a company director's current version of risk management made up of eight framework components to wit:

i. Internal Environment – Risk management philosophy and risk appetite, ethical values, etc.

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[593] COSO-Effective Enterprise Risk Oversight – Integrated Framework, 2004, *op. cit.* Note I above. Note also that 'COSO' is s voluntary private sector organization comprised of American Accounting Association, American Institute of Certified Public Accountants, Financial Executives International, and Institute of Management Accountants and the Institute of Internal Auditors. The organization is dedicated guiding executive management and governance participants towards the establishment of more effective, efficient and ethical business operations on a global basis. It sponsors and disseminates frameworks and guidance based on in-depth research, analysis and best practices.

ii. Objective Setting – Management must have process to set objectives and ensure it aligns with company's mission and are consistent with risk appetite.
iii. Event Identification – Internal and external events affecting achievement of objectives must be identified, distilling between risk and opportunity.
iv. Risk Assessment – Risk are identified and analyzed considering likelihood and impact, as a basis for determining how they are managed.
v. Risk Response – Develop set of actions in line with risk appetite - avoid, accept, reduce or share risks.
vi. Control Activities – Policies and procedures to ensure risk response is effectively implemented.
vii. Information and Communication – Relevant information is identified and communicated in the firm and time table for people to execute functions.
viii. Monitoring – Entirety of enterprise risk management is monitored and modifications made as appropriate.

Thus, the above eight framework components are designed to achieve, through the oversight risk management role of directors, the following four categories of business objectives:

i. Strategy – High level goals, aligned with company's mission
ii. Operations – Effective and efficient use of resources
iii. Reporting – Reliability of reporting
iv. Compliance – Compliance with applicable laws and regulations.

In addition to the above, the COSO 2009 release[594] recommends concrete steps for boards such as understanding a company's risk philosophy and concurring with its risk appetite, reviewing a company's risk portfolio against that appetite, and knowing the extent to which

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[594] See COSO – Effective Enterprise Risk Oversight: The Role of the Board of Directors, 2009 WWW. COSO. Org, New York, NY op. cit note 2

management has established effective enterprise risk management and is appropriately responding in the face of risk.

Thus, the role of directors in risk management involves taking some specific types of actions that the appropriate committees may consider as part of their risk management oversight and include the following:[595]

i. Review with management the categories of risk the company faces, including any risk concentrations and risk interrelationships, as well as the likelihood of occurrence, the potential impact of those risks and mitigating measures;
ii. Review, with management, the company's risk appetite and risk tolerance; the ways in which risk is measured on an aggregate, the company-wide basis, the setting of aggregate and individual risk limits (quantitative and qualitative, as appropriate), and the actions taken if those limits are exceeded;
iii. Review with committees and management the board's expectations as to each groups respective responsibilities and roles;
iv. Review the risk policies and procedure adopted by management, including procedure for reporting matters to the board and appropriate committees and providing updates in order to assess whether they are appropriate and comprehensive;
v. Review management implementation of its risk policies and procedures, and to assess whether they are being followed and are effective;
vi. Review with management the quality, type and format of risk –related information provided to directors;

[595] See Martin Liptop, et al, Risk management and the Board of directors, Bank and Corporate Governance Law Reporter, volume 45, Number 6, February, 2011.

vii. Review the steps taken by management to ensure adequate independence of the risk management function and the process for resolution and escalation of differences that might arise between risk management and business functions;

viii. Review with management the design of the company's risk management functions, as well as the qualifications and background of senior risk officers and the personnel policies applicable to risk management, to assess whether they are appropriate given the company's size and scope of operation;

ix. Review with management the means by which the company's risk management strategy is communicated to all appropriate groups within the company so that it is properly integrated into the company's enterprise – wide business strategy;

x. Review internal systems of formal and informal communication across divisions and control functions to encourage the prompt and coherent flow of risk-related information within and across business units and, as needed, the prompt escalation of information to management and to the board or board committees as appropriate; and

xi. Review reports from management, independent auditors, internal auditors, legal course, regulators, stock analysts, and outside experts as considered appropriate regarding risks that the company faces and the company's risk management function.

In the United States, the risk oversight function of the directors or board of directors derive primarily from state law fiduciary duties, federal laws and regulations, stock exchange listing requirements, and certain established (and evolving) best practices. This development of course raises a striking question for determination – Does the fiduciary duties of directors of a company to shareholders and stakeholders alike extends to corporate risk management? Learned authors think so.[596]The learned authors state that the Delaware Courts have

[596] M. Lipton, *et al*, Risk Management and the Board of Directors, Bank and Corporate Governance Law Reporter, volume 45, Number 6, February, 2011. p. 7.

developed a framework for assessing whether board oversight of risk management, in any given case, satisfies the directors' fiduciary duties. In *Re Caremark International Inc Derivative Litigation*,[597] the rule was established that directors can only be liable for a failure of board oversight where there is 'sustained or systemic failure of the board to exercise oversight – such as an utter failure to attempt to assure a reasonable information and reporting system exist', noting that this is a demanding test. The Delaware Courts have made clear that they will not impose liability under a 'Caremark' theory unless the directors intentionally failed to implement any reporting or information system, or controls or, having implemented such a system, intentionally refused to monitor the system or act on warnings it provided.

Two 2009 Delaware Court of Chancery decisions have expanded upon 'care mark', while reaffirming that the Caremark standard remains the fundamental standard. In *Re Citigroup Inc. Shareholder Derivative Litigation*, the plaintiffs alleged that the defendants, current and former directors of Citigroup, had breached their fiduciary duties by not properly monitoring and managing the business risks that Citigroup faced from subprime mortgages and securities, and by ignoring alleged 'red flags' that considered primarily of press reports and events indicating worsening conditions in the subprime mortgages and credit markets. The court dismissed these claims, reaffirming the 'extremely high burden' plaintiff face in bringing a claim for personal director liability for a failure to monitor business risk and that a 'sustained or systemic failure' to exercise oversight is needed to establish the lack of good faith that is a necessary condition to liability.

The Citigroup Court observed that its decision to block further litigation against the Citigroup directors could be thought to be at variance with the result in American International Group,

[597] 698 A. 2d 959, 971 (Del. Ch. 1996).

Inc. Consolidated Derivative Litigation, a Delaware case decided shortly before Citigroup involving shareholder claims arising out of conduct by American International Group, Inc (AIG). In the AIG case, the Court of chancery allowed claims based on alleged fraud and illegalities at AIG to survive a motion to dismiss, relying in part on a theory that the defendants had 'consciously failed to monitor or oversee the company's internal controls. However, the individual defendants in the AIG case were executives and inside directors who were allegedly 'directly knowledgeable of and involved in much of the wrongdoings,' rather than independent, non-executive directors. The Citigroup Court did rely on the distinction between business decisions and matters of corporate fraud and violations of law. Over all, the case that it is difficult to show a breach of fiduciary duty for failure to exercise oversight and that the board is not required to undertake extraordinary efforts to uncover non-compliance within the company provided a monitoring system in place.

In 2010, the European Commission, in a consultation paper seeking comments on options to impose corporate governance in financial institutions, suggested strengthening 'legal liability of directors by an expanded duty of care.' The possibility is increasingly imminent that higher standards of care could eventually be imposed not only on directors of financial institutions, but on director of all corporations. Therefore, directors should through their oversight role, satisfy themselves that the risk management policies and procedures designed and implemented by the company's senior executives and risk managers are consistent with the company's corporate strategy and risk appetite, and that these policies and procedures are properly functioning and working as it should.

5.5 Situating the Risk Oversight Function of Directors

In the U.S, most board delegate oversight of risk management to the audit committee, which is quite consistent with the New York Security Exchange (NYSE) rule that requires the audit

committee to discuss policies with respect to risk assessment and risk management. Financial companies covered by the Dodd-Frank Act[598] must have dedicated risk management committees. The appropriateness of a dedicated risk committee at other companies will depend on the industry and specific circumstances of the company. Directors should on this score bear in mind that different kinds of risk may be best suited to the expertise of different committees – an advantage that may in the long run outweigh any benefit from having a single committee specialized in risk management. Regardless of the delegation of risk oversight to committees, however, the full board of Directors collectively and directors individually should satisfy itself and themselves that the activities of the various committees are coordinated and that the company has adequate risk management processes in place. To this end, risk oversight is a focus of committees; those committees should report key findings periodically to the full board of directors and also confer amongst themselves.

If the company keeps the primary risk oversight function in the audit committee and does not establish a separate risk or subcommittee, the audit committee should schedule time for periodic review of risk management outside the context of its role in reviewing financial statements on the one hand and accounting compliance on the other hand. The goal should be to achieve serious and thoughtful board level attention to the company’s risk management process and system, the nature of the material risk the company faces, and the adequacy of the company’s policies and procedures designed to respond to and mitigate these risks.

To be noted however, is the interesting fact that Risk management issues involving corporate directors may arise in the context of the work of other committees, and the decision-making

[598] Dodd-Frank Act is a U.S legislation passed into law on July, 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (hereinafter referred to as the ‘Dodd-Frank Act’). The Act has created new federally mandated risk management procedures principally for financial institutions. The Dodd-Frank Act requires bank holding companies with total assets of $10 billion or more, and certain other nonbank financial companies as well, to have a separate risk committee which includes at least one risk management expert with experience in managing risk of large companies. This requirement may be extended to bank holding companies with less than $10 billion in assets by the Federal Reserve Board of the U.S.

in those committees, should take into account or cognizance the company's overall risk management system. Thus, specialized committees may be tasked with specific areas of risk exposure. Financial institutions in Nigeria, for instance, often maintain credit finance committees, while energy companies may have public policy committees largely devoted to environmental and safety issues. Where however, different board committees are responsible for overseeing and managing specific risk (for instance credit and reputational risks), the work of these committees should be coordinated in a coherent manner both horizontally and vertically so that the entire board of directors can be satisfied as to adequacy of the risk oversight function and the company's overall risk exposures are understood, including risk interrelationships.

The board of directors as a matter of course should undertake an annual review of board and committee-level risk oversight policies and procedures, a presentation of 'best practices' to the extent relevant, and tailored to focus the industry or regulatory arena in which the company operates and a periodic review of other relevant issues such as when and where a major risk comes to fruition.

5.6 Information Technology and Risk Management

Technology can be a key enabler for any risk management programme. Most organizations will find that they need a technology solution to manage all of the data gathered, and such solutions may also address monitoring, follow-up, and communication challenges. However, it is important to establish the risk management approach before selecting a technology solution. Otherwise, the organization may be forced to adopt the vendor's approach instead of one that better fits the organization's needs and culture[599]

[599] Real World Perspective, Quoted in P.J. Sobel, 'Internal Auditing's Role in Risk Management', The Institute of Internal Auditors Research Foundation, March, 2011, *op. cit*, p. 15.

Over the past two decades, enterprise resources planning (ERP) systems have allowed corporate managers to utilize software to integrate information about projects across the enterprise. These systems are designed to integrate internal and external information, enhance the flow of communication and decision making across an enterprise, and focus on business processes and functions. However, integrating information about operations all across an enterprise to make information more accessible and flow via an enterprise resource planning (ERP) system presents a number of significant risks.

The World Economic Forum[600] divided the risks into five categories namely economic, environmental, societal, geopolitical and technological risks. In the United States, for example, cyber crime is becoming an increasing problem for companies resulting in million dollar damages and creating major reputation risks for companies affected. While attacks are often frustrating, some thinking about cyber related risks can lead to preparation that may lessen the impact of these events. A cyber crisis plan can for example be derived and implemented through an ERP process, which with the main strengthen an organization's ability to manage through a cyber threat by having a plan that identifies who needs to do what and when they need to do it.

This kind of preparation can help companies avoid major losses, reputation hits, and congressional scrutiny. To be noted is the fact that managing social media risks is also very important in this regard. This is because as organizations or companies realize the potential of social media to positively benefit their marketing and advertising strategies, they are also aware of potential risks. Given the highly interconnected world that information technology now accommodates, organizations are also able to expand their operations and systems all around the globe. While those information technology systems create significant business

[600] World Economic Forum, Global Risk Report, Seventh Edition, January 1, 2012.

opportunities, those same tools may be opening organizations up to significant vulnerabilities that can be activated from most of the technology connection point around the world. This risk, often referred to as cyber security risk is being realized more and more by all types of organizations. Sometimes those risks also arise from internal sources who leak sensitive information to the outside world, similar to wikeleaks situations.[601]

The question now is 'What should corporate board of directors know about social media as it relates to a company's ability to do business and safeguard its image? And what is the board's role in helping a company make the best use of social media, and depending against its misuse? It does seem that the first step to be taken in attempting to address these questions is for directors and managers to understand social media technologies, the ethos of social media users, the dynamics of how 'conversations' occur and people engage with one another and the tools used to monitor and analyze social media activities. In fact Board oversight of social networking requires more than an understanding of the underlying technology. It also calls for an understanding of the sociology and the implications of the phenomenon.[602] Yet few board directors have experience as a chief technology officer or expertise in information technologies.[603] Very few too, have led communications, public relations and marketing initiatives. However, the truth is that social media makes it more difficult for organizations and companies to control information. Information that might once have been safely proprietary can now escape the confines of a corporation and gain viral public exposure.

[601] It will be recalled that publication of secret diplomatic cables through wikileaks shocked governments and provided a sudden wake-up call to all who seemingly were safe from the new power of social media. Consequences went well beyond mere embarrassment; they helped spark the first 'Arab spring' upspring in Tunisia, and other forms of social media helped sustain popular dissent elsewhere in the Middle East and North Africa region. What quickly became obvious is that communications online had demonstrated a new capacity to upend political agendas everywhere.
[602] See Paul Cantor, Board Governance of social Networking, //WWW.bennettjones. com/uploaded files/publications/Articles/Paul Cantor Director Journal. PDF (visited 9/8/2013 at about 8: 12pm)
[603] Deloitte, 2011 Board practices Report: Design, Composition and Function, society of corporate secretaries and Governance professionals (2011). WWW. Corgov. Deloitte.com/binary/com. epicentric. content management. Servlet. Content delivery servlet/Us Eng/Documents /Board % 20 Governance/2012. Pdf (visited 9/8/2013 a t 8: 19pm).

Corporate missteps that might once have been easily and quietly managed can get magnified into crises. Shareholders with the most insignificant stakes can now stir wide rebellion at negligible cost. Moreover, given the global nature of access to media, implications affect companies no matter where they call home, and whether they are controlled by families or are widely held. This is however, without prejudice to the fact that widespread use of social media has equal potential to transform corporate agendas. By the same token, though, corporations can use social media channels creatively to improve stakeholder loyalty, and improve performance. Companies can develop new means of constructive dialogue with different constituencies. Benefits might include early warning of threats, identification of new ideas, and amplified means of responding. New Communication channels can be a force multiplier and a risk management tool to advance the interest of the business.[604] Perhaps, the 2008 financial meltdown that nearly crippled the entire global business world mean that economic crisis is changing risk management landscape in various ways. The government bailouts adopted in response to the economic crisis had many effects, with the greatest potential effect on risk appetites of organizations. The magnitude and frequency of bailouts could encourage increased risk appetites or there could be increased risk aversion in response to what is currently perceived as a high-risk environment. This enhanced perspective can then be used to address concerns such as insider threats, information risk, and product protection.[605] Of course Information Technology (IT) risk, it should be understood, is a business risk associated with the use, ownership, operation, involvement, influence and adoption of Information Technology (IT) within an enterprise.

[604] Santiago chaher and James David Spellman, corporate Governance and social media: A brave New World for Board Directors, A Global Corporate Governance Forum publication P.2 – Foreword by Stephen Davis (Non resident senior fellow in governance studies at the Brookings institution, Senior fellow at the Harvard law school program on corporate governance, and former Executive Director of Yale University school of management's Millstein centre for corporate Governance and performance).

[605] Enhancing information Technology (IT) Risk Management: An Exposure Draft February 1, 2009 available at http.//WWW.mozilla.com/en-us/firefox/central/pdf (visited 11/30/2013 at 9:33 AM).

5.7 The Control Measures in Risk Management

It has become very imperative to devise control measures for managing risks in organizations because of the imminent threat to business interest of corporate bodies. Directors and auditors of corporate organizations and their functions/role thereof is very central in taking decisions as to the type of measure that should be taken to manage or mitigate the impact of risks in companies. In Japan, a measure called internal control compliance mechanism have been adopted by companies in a bid to circumvent the negative impact of risk that business organizations resident in that jurisdiction are bound to suffer. NEC, an organizational governance outfit in that country has established the basic policy on internal control systems as a guideline for developing systems for ensuring that the performance of directors' duties complies with laws and regulations and NEC's articles of incorporation, and system for ensuring the appropriateness of other operations.[606]

Further, NEC conducts annual evaluations of the establishment and operation of the internal control systems under this policy, as well as implementing the measures necessary for its improvement. In this way, internal control systems have been established and are operating effectively. Two key themes with respect to internal control systems are compliance and risk management. Guided by the key concepts of 'awareness and 'information sharing', the Japanese practice and approach to implementing compliance is to foster an awareness among every officer and employee so that irregularities are recognized as 'abnormal and to encourage officers and employees to consult with supervisors, related departments and the compliance hot line without brushing under the carpet any issue they may have noticed, with the view to resolving and improving those issues collectively as an organization.

[606] See Generally Article 362, paragraph 4, item 6 of the company law of Japan.

To enforce compliance and implement effective risk management, NEC Corporation in particular and other Japan Corporations in general conduct activities led by the Risk Control and Compliance Committee, the Internal Control Division and the Risk Control and Compliance Promoters:

i. The Risk Control and Compliance Committee, whose members are officers, investigates the underlying causes of serious compliance breaches, studies related preventive measures, and discusses policies for risk management activities and measures to select and address priority risks.

ii. The Internal Control Division exchanges opinions on various occasions with designated employees in corporate staff and other divisions specializing in matters described in the NEC Group Code of Conduct. In addition, the internal control division provides necessary support and coordination, as well as guidance to ensure that risk management at business divisions and corporate staff divisions is implemented systematically and effectively.

iii. The Risk Control and Compliance Promoter system is a company-wide framework designed to rigorously enforce compliance and risk management among group employees.[607] Under this arrangement, given its oversight role with respect to business execution, the Board of directors receives reports related to material misconduct along with reports on priority risks. In the same vein, the Corporate Auditing Bureau and Corporate Auditors perform internal audits according to each of their roles to check whether there are any problems in the execution of business operations by companies from the viewpoints of accounting and legal compliance of NEC group of companies.

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[607] Risk control and compliance promoters assigned to business divisions (415 people) and NEC Group subsidiaries in Japan (139 people) serve as points of contact for the internal control Division (As of march 31, 2012).

Notably, from among group-wide important risks, the NEC corporation selects priority risks following deliberations by the Risk Control and Compliance Committee and the Executive Committee on risks deemed to require new countermeasures, including improvement of existing countermeasures, and on risks that may significantly impact the corporation's group continuity. The division nominated by the Risk Control and Compliance Committee then takes the lead in devising countermeasures.

In this manner, NEC Corporation aims to bolster the entire groups risk management capabilities.[608]

Also, in Australia, the responsibility for the oversight risk management and fraud control measures have moved the governance, planning and assurance branch to fraud investigations and prosecutions branch within the newly created Risk, Fraud and Integrity Division (RFID). This is aimed at centralizing, enhancing and streamlining risk and integrity related functions.[609] This measure of Risk management may be termed 'Technological Measures'. This is because RFID employs a range of new and innovative tools and capabilities to analyze risk and to identify mitigation measures/strategies. A key tool employed by RFID is the application of enhanced analysis to facilitate identification. These enhanced analysis are used to inform a variety of innovative products and outputs, including fraud, risk and

[608] NEC also participates in activities of external organizations. For example, NEC Corporation has been a member of "Business Ethics Research Center' since the center was establishment in 1997. NEC Corporations is also a member of 'Caux Round Table Japan Committee' since it was established in 2000. At the Round table, NEC exchanges information and collaborates in promoting the spread of CRS in Japan. In addition, these meetings help in proposing measures to promote CRS activities in NEC. In the same vein, NEC Corporations participates in a variety of study groups and committees, where it strives to absorb knowledge of examples of the ethics activities of various companies, while introducing examples of NEC's ethics activities.

[609] Risk Management and Fraud Control Measures – Management and Accountability – annual Report 2010 -11, Australian Government – Department of Immigration and Citizenship, available at: http://WWW.immi.gov.au/index.htm., visited on 11/29/2013.

integrity scans, flashpoint bulletin and risk management processes. The system works in partnership, across the department and globally, to deliver professional risk, fraud, intelligence, investigations and identity services to lead a risk-tiered approach to support the integrity of corporate risks and by necessary extension boarder risk, migration and related programmes. The advanced analytics technology uses or applies mathematical, statistical and machine-intelligence technique to extract knowledge from data to assist in decision making. The processes produce evidence-based data than can inform policy, operational and service delivery. The advanced analytics also uses enhanced alerts with business intelligence processes which allow it to accurately forecast future trends and generate alerts when normal parameters are breached.

5.8 Nature of Risk in Company Management

Risk by its very nature in company management is multi-faceted concept which extends to such topical factors like hazard risks, financial risks, personal injury and death, business interruption/loss of services, damage to a corporation's reputation, errors and omissions and lawsuits.

These risks predominantly take the form of a possible lurking danger around the corner of corporate financial management which does constitute an actual threat to financial and organizational stability of corporate bodies ranging from those of banking to insurance companies and of course the world of commerce. The 2008 financial crisis that rocked the world manifested itself very much in this regard. Risk is a pervasive part of everyday business and organizational strategy.

However, the complexity of business transactions, technology advances, globalization, speed of product cycles, and the overall pace of change have increased the volume and the complexities of risks facing organizations over the last decade in Nigeria. The management

of these risks involves the proper identification, assessment, and prioritization of the said risks. It extends to the effect of uncertainty and objectives (whether positive or negative) followed by coordinated and economical application of resources to minimize, monitor, and control the probability and/or impact of unfortunate events or to maximize the realization of opportunities.

According to Bianca[610] corporate risk management refers to all of the methods that a company uses to minimize financial losses. Risk managers, executives, line managers and middle managers, as well as all employees are all involved in this process and thus perform practices to prevent loss exposure through internal control of people and technologies as the case may be. It basically relates to external threats to a corporation, such as the fluctuations in the financial market that affects its financial assets.

Perhaps, risks in company management cover a wide range of credit risk which is most simply defined as the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms. It further extends to market risk, which refers to the risk of loss to an institution resulting from movements in market prices, in particular, changes in interest rates, foreign exchange rates, and equity and commodity prices and of course operational risk which is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Thus, issues so grave as probability (likelihood) of event occurring and severity (impact) of the event on set objectives is brought to the limelight in this regard. Thus, standardized capital requirement for market, credit and operational risk elements carry with it other contingent risk which include but not limited to liquidity risk, residual risk, securitization risk and concentration risk. Others include interest rate risk, reputation risk (as noted earlier), and business risk among others. These contingent risks as noted above is usually measured through internal economic capital framework. This

[610] A. Biabca, "What is Corporate Risk Management? available at: http://www , Ehow.com/print/info-7804647 – corporate risk management. Html., visited 11/29/2013.

measurement of course reveals that the consequences of risk in company management are very enormous and could lead to job losses and in extreme cases outright company collapse. Hence, risk by its very nature in company management manifests itself as a multi-disciplinary concept which wear different shapes in business organizations depending on the types of business risk involved, the effects of such risk on shareholder and stakeholders' interest and possible control measures.

CHAPTER SIX

COMPARATIVE ANALYSIS OF CORPORATE GOVERNANCE IN VARIOUS JURISDICTIONS

6.1. Introduction

Corporate governance refers to that blend of laws, regulations, which attract financial and human capital, perform efficiently, and thereby perpetuate itself by generating long-term economic value for its shareholders.[611] The principal characteristics of effective corporate governance are: transparency (disclosure of relevant financial and operational information and internal processes of management oversight and control); protection and enforceability of the prerogative of all shareholders and directors capable of independently approving the corporation's strategy and major business plans and decisions, and of independent management, monitoring management performance and integrity, and replacing management when necessary.

Furthermore, corporate governance has been defined as the framework within which companies are directed, controlled and held to account.[612] This is distinct from the management of enterprises on day-to-day basis, which is a task delegated by boards to executive directors/management. Corporate governance has more strategic and overreaching function. It is concerned with steering a company in a direction that is consistent with its long-term value and objective[613].

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[611] H.I. Gregory, 'International Comparison of Selected Corporate Governance and Code of Best Practice', (Sept. 2008), available at www.charobles.com/secmemorandumgreculam0022002html, accessed on 21 November, 2014.
[612] R. Barker, 'The UK Model of Corporate Governance: An Assessment from the Midst of a Financial Crisis. (Oct 3, 2008), available at: www.iod.com/policy, accessed on 22 November, 2013.
[613] *Ibid*

Corporate governance practices in the globe are surprisingly diverse. Differences partly reflect the varying sizes, sectors of activity, and live cycle stages of enterprises. However, the nation state is still the main driver of the economy. Variations, for e.g., prominent multinational corporations like Toyota, Volkswagen and General Motors are engaged in broad similar economic tasks like manufacturing and distribution of automobiles. However, their activities are subject to entirely differing frameworks of monitoring, oversight and control due to the distinctive governance environment of their respective countries of incorporation. However, global market forces do have impact on governance practices. Large public quoted firms in different jurisdictions increasingly conform to international standard of corporate governance 'best practiced' as defined by organizations such as the Organisation for Economic Cooperation and Development (OECD), the European Union (EU), and the International Accounting Standards Board. Such behaviour helps them to the favour of capital market investors and thereby gains access to external finance at the lowest possible cost.[614] For an individual company, an appropriate framework of corporate governance coordinated by a proper function of board of directors seems to increase confidence in the firm's long term viability. This builds trust and credibility with investors, creditors, employees and other stakeholders. At national level, corporate governance is a determinant of national competitiveness, and helps to establish the legitimacy of corporate activities vis-a-vis the rest of society.

There has been a long standing debate that has raged around as to which national model of corporate governance is most desirable. Conventional wisdom on this issue exhibits a strong correlation with the performance of the underlying economy with which a national model is associated. For example, at the beginning of the 1990's, Professor Michael Porter of Harvard Business School along with many other leading management thinkers, praised the strength of

[614] *Op cit*, footnote 2.

the German and Japanese models as enterprises in these countries enjoyed a stable ownership structure, and worked in close collaboration with banks and controlling shareholder. According to Porter**,** this gave rise to much effective corporate decision making than observed in the short-term Anglo-Saxon business world, particularly in the manufacturing sector.[615]

However, by the mid-1990 the U.S model, with its emphasis on arms length powerful management, and capital market financing had staged a comeback. The US business environment was seen as offering better opportunities for new company format, and the application of new technology, particularly in emerging sectors of the 'new economy such as, telecom and life science. High level of productivity and employment growth in the U.S during the 1990,s appear to substantiate this claim. In contrast, by the 1990s, the German and Japanese models were no longer delivering much economic growth, and appeared resistant to change and innovation.[616] Unfortunately, the busting of the Dot-com bubble in 2001, and series of high profile scandals at major corporations affected U.S business framework. It also catalyzed a punitive regulatory response from US legislators that imposed significant cost on the US economy.[617] Although US corporations continued to dominate many important sectors of the world economy, the US corporate governance framework is no longer viewed as the 'gold standard' that should be emulated around the world.[618]

We shall under this sub-heading discuss the United Kingdom model of corporation in brief as we are going to have a full discussion on the corporate governance of different jurisdictions such as India, United State of America and U.K inclusive.

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[615] *Ibid*., p. 2.
[616] *Ibid*., p. 3.
[617] The Sarbanes Oxley Act of 2002.
[618] *Ibid*.

The correct UK corporate governance system has its origin in a series of corporate scandals in the late 1980s and early 1990s, including the collapse of Polly Peck, the Rober Maxwell Pension Fund and the BCCI Bank. The UK community recognized a clear need to improve the robustness of its governance. This led to the establishment of the committee on the financial aspect of corporate governance in 1991, led by Sir Adrian Cadbury, which issued a series of recommendations, known as Cadbury Report in 1992.

The Cadbury Report addressed a number of issues of corporate governance that were not dealt with in the existing Company Law such as the relationship between the chairman and chief executive, the roles of the non-executive directors, and the reporting internal controls, and defines best practice in these areas. The key policy following these reports was to introduce a requirement within the listing rules of London Stock Exchange that companies should report whether they had followed Cadbury's recommendations, or explain why they had not done so (the so called comply or explain principle).[619]

The recommendations in the Cadbury Report have been reviewed and redefined at regular intervals since 1992. In 1995 the Greenbury Report set out recommendations on the remuneration of directors. In 1998 the Cadbury and Greenbury reports were brought together and updated in the form of Combined Code. In 1999 the Trumbull guidance was issued to improve directors with guidance on how to develop an effective system of internal control. Following the Enron and WorldCom scandals in US, the Combined Code was updated in 2003 to incorporate recommendations from reports on the roles of non-executive directors (the Higgs Report) and the role of the audit committee (The Smith Report). In the same year,

[619] R. Banker, *op. cit,* p. 4.

they assume responsibility for publishing and maintaining the code. The (FRC) made further limited changes to the code in 2006 and 2008.[620]

Contemporary discussion of corporate governance tends to refer to principle raised in three documents: The Cadbury Report (UK 1992), the principles of corporate governance of OECD (OECD, 1998 and 2004), the Sarbanes-Oxley Act of 2002 (USA, 2002). The Sarbanes-Oxley Act, informally referred to as 'Sax box or Sox, is an attempt by the Federal Government of United State to legislate several of the principles recommended in the Cadbury and OECD reports. The latTer however presents general principles around which businesses are expected to operate to assume proper governance.[621]

Over the years, inhibiting corporate collapse and failures of corporate bodies has been on the agenda of governments and management authorities. This motivation flow from the effect of collapses and accounting scandals witnessed in high profile enterprise that shook the corporation and the entirety of the nation.[622] More often than not, these failures and collapses are associated with impropriety in reports made in the financial statements of the company. In other words, transparent disclosure, accountability and protection of shareholders and other stakeholder interest, as principles of corporate governance are not observed. These accounting scandals are often political or more ironical in that it arises with the disclosure of financial misdeeds by trusted executives of corporations. Such misdeeds typically involve complex method of misusing or misdirecting funds, overstating revenues, understating expenses, overstating the value of corporate assets or underreporting the existence of liabilities. Corporate failure rarely happens by accident. Companies drift rafter than fall into

[620] *Ibid*
[621] P.R. Kousalya, *et al*, 'Research Paper Management: Corporate Governance Models around the World, available at: www.theglobalformals.com, accessed on 23 Nov. 2013.
[622] Examples of such collapse include Enron and WorldCom in the U.S, Parmalat in Italy, HIH and One. Tel in Australia, Cadbury Plc and Lever Bros in Nigeria, to mention but a few.

collapse.[623] This is basically due to bad management and nonchalance of the players in a corporate entity. The effect of such collapse is detrimental to investors' confidence, the economic growth of the country and that of the public at large.

These corporate collapses, oftentimes, are associated with principal-agent issues.[624] In the agency relationship, the agents who constitute the upper management may have very different interests and information than the principals who constitute the shareholders. This form of issue between the principal and the agent is referred to as information asymmetry.[625] In this situation of agency problem, the agent has more information than the principal whom they represent. Consequently, this creates an imbalance of power in transactions which can cause the transaction to go away sometimes, or a kind of market failure in the worst case. Thus, this problem of information asymmetry could lead to adverse selection,[626] moral hazard[627] and information monopoly. Due to information asymmetry, the executives can accelerate accountings of expected expenses, delay accountings of expected revenues, engage in off balance sheet transactions to make the company's profitability appear temporarily poorer or simply to promote and report severely conservative estimates of future earnings.

Notably, research in strategic management was quick to realize that people who were affected by organizational behaviour might have an impact on the achievement of organizational goals irrespective of sparing necessary information from them. Therefore, a stakeholder in an organization is any group or individual who can affect or is affected by the achievement of

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[623] A collapse involves a major insolvency or bankruptcy of an enterprise. It could stem from a scandal involving allegations of unethical behavior by people acting within or on behalf of a corporation.

[624] D.A Awotunchin, *et al*., 'Corporate Governance and Stakeholder Interest: A Case of Nigerian Banks', *International Journal of Business and Management*, Vol. 6, No.10, 2011, p.104.

[625] Information asymmetry is a concept in economics and contract theory that deals with the study of decision in transactions where one party has more or better information than the other.

[626] Adverse selection is a term used in economics, insurance, risk management and statistics. It refers to a market process in which undesired results occur when buyers and sellers have asymmetric information, and here, bad products or services are more likely to be selected.

[627] Moral hazard is a situation where a party will have a tendency to take risks because the costs that could be incurred will not be felt by the party taking the risk. In other words, it is a tendency to be more willing to take a risk knowing that the potential costs or burdens of taking such risk will be borne, in whole or part by others.

the organizations objectives.[628] Further, the stakeholder theory[629] argues that the corporation is a social entity that affects the welfare of many people. Research suggests that the participation of stakeholders in corporate decision making can enhance efficiency[630] and reduce conflicts.[631] However, the central question of concern is how do corporations integrate stakeholder concerns into their decision making structures and conduct business responsibly towards them?[632] Basically, a reactive or proactive attitude has been distinguished in this regard by Kaptein and Van Tulder[633] who analyzed various firms on their approach to stakeholder management.

Thus, companies approaching stakeholder in a reactive fashion will not integrate their concerns into corporate decision making and take responsibility for their claims. The inherent risk of this approach is that organizational goals and stakeholder demands become misaligned, thereby causing conflict or corporate irresponsibility to sprout.[634] Scandals such as that of Enron have been attributed to a lack of consideration of stakeholder concerns.[635] In short, the reactive attitude toward stakeholder concerns contains significant risks and is likely to lead to an antagonistic business in society relationship.[636]

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[628] R.E. Freeman, 'Strategic Management: A stakeholder Approach', (Boston MA: Pitman, 1984).

[629] T. Donaldson & L.E. Preston, 'The Stakeholder Theory of the Corporation: Concepts, Evidence and Implications', *Academy of Management Review*, Vol. 20, No. 1, 1995, pp. 65-91.

[630] S. Turnbull, 'Stakeholder Democracy: Redirecting the Governance of Firms and Bureaucracies', *Journal of Socio-economics*, Vol. 23, No. 3, 1994, pp 321-361.

[631] J. Rothman & V.J. Friedman, 'Identity, Conflict and Organizational Learning', in M.Dierkis *et al* (eds.), *Handbook of Organizational Learning and Knowledge*, (New York: Oxford University Press, 2001), pp. 582-597.

[632] B. Marille & J. Ober, 'Beyond Empowerment: Building a Company of Citizens', *Harvard Business Review*, Vol. 81, No. 1, 2003 pp. 40-53.

[633] M. Kaptein & R. Van Tulder, 'Toward Effective Stakeholder Dialogue', *Business and Society Review*, Vol. 108, No. 2, 2003, pp 203-224.

[634] C. Mackenzie, Boards, Incentives and Corporate Social Responsibility: The Case for a Change of Emphasis on Corporate Governance, *An International Review*, Vol. 15, No. 5, 2007, pp. 935-943.

[635] S. Watkins, 'Former Enron Vice President Sharron Watkins on the Enron Collapse' *Academy of Management Executive*, Vol. 17, No. 4, 2003, pp 119-125.

[636] S. Beloe *et al*, 'From Corporate Responsibility to Good Governance and Scalable Solutions, Sustainability and the Global Compact, London.

On the other hand, more proactive companies seem to integrate stakeholder concerns into their decision making processes and establish necessary governance structures.[637] This proactive attitude of companies to stakeholders is more of a corporate social responsibility. Accordingly the Business for Social Responsibility defines corporate responsibility as a set of policies, practices and programs that are integrated throughout business operations and decision making processes, and intended to ensure that the company maximizes the positive impacts of its operations on society.[638] It could be adduced from the stakeholder theory that if stakeholder interest were aligned with the corporation management, collapse or failure would be avoided.

As a corollary to the stakeholder theory, the concept of Corporate Social Responsibility or Corporate Responsibility[639] has arisen in curbing systemic failures and collapses that have prevailed over the years. Oftentimes, the corporate social responsibility is argued to be a prerequisite in entrenching good corporate governance practices as opposed to the traditional method of legislation. The story of corporate social responsibility (CSR) in the 21st century is a story of progressive business sensitization to systems and dynamics of governance beyond government; regulation beyond law, and responsiveness beyond responsibility.[640] CSR is about a rapidly growing alignment across many individual businesses, industry sectors and geographical regions between those systems and dynamics of governance, regulation and responsibility on one part, and a company's business model, strategy and impact on the other part.[641] Corporate social responsibility, as a commitment to improve community well being

[637] De Wit, *et al*, 'Harduring and Softuring Corporate Responsibility: A Vital Combination', *Corporate Governance*, vol. 6, No. 4, 2006, 491-505.
[638] H. Spitzeck, 'Organizational Structure and Processes: The Development of Governance Structure for Corporate Responsibility', *Corporate Governance*, Vol. 9, No. 4, 2009, pp 493-505.
[639] S. Kladdock, 'Building the Institutional Infrastructure for Corporate Social Responsibility, (Working Paper, No. 23, John F. Kennedy School of Government, 2006), 5.
[640] B. Horrigan, '21st Century Corporate Social Responsibility Trends: An Emerging Comparative Body of Law and Regulation on Corporate Responsibility, Governance and Sustainability, *MqJBL*, Vol. 4, 2007, pp. 85-122.
[641] *Ibid.*

through discretionary business practices and contributions of corporate resources[642]is now an important component of the dialogue between companies and their stakeholders.[643]

Nowadays, companies engage in CSR in large part because executives believe that such activity will elicit company favouring responses from stakeholders.[644] It is a truism that a company's investment in corporate social responsibility initiatives provides reform to the company. This is supported in the scholarly literature by a large and growing body of evidence showing that individuals across numerous stakeholder realm reward companies that engage in CSR activity. In the consumer realm, for instance, the CSR record of a company has a positive effect on consumers' evaluations of the company and their intent to purchase the company's products.[645] Likewise, in the employment realm, CSR activity has been shown to have a positive effect on job seeking intent[646] as well as behaviours on the job like interpersonal corporation and job-related effort.[647] In the same vein, some evidence show that investors both attend to and make investment decisions based upon the corporate social responsibility of public companies.[648] Due to the inherent benefits of inculcating the attitude of being corporately-socially responsible, developed and developing worlds are rapidly reaching the point where they must decide if today's global corporate social responsibility is a passing social fad, a threat to economically efficient corporate capitalism, an intrinsic element of corporate responsibility, or even a key to humanity's long term survival.[649]

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[642] P. Koffer & N. Lee, 'Corporate Social Responsibility: Doing the Most Good for your Company and your Cause, Hoboken, NJ: Wiley and Sons, Inc, 2004, p. 3

[643] I.E Berger *et al*, 'Mainstreaming Corporate Social Responsibility: Developing Markets for Virtue', *California Management Review*, 49(4), 2007, pp. 132-157.

[644] Mckinsey & Company, 'Global Survey of Business Executives', in the *Macinsey Quartery*, 2006.

[645] S. Sen & C.B. Bhattachaya, 'Does Doing Good Always Lead to Doing Better?: Consumer Reactions to Corporate Social Responsibility', *Journal of Marketing Research (JMR)*, Vol. 38, No. 2, 2001, pp. 225-243.

[646] D.W. Greening & D.B. Turban, 'Corporate Social Performance as a Competitive Advantage in Attaching a Quality Workforce, *Business and Society*, Vol. 39, No. 3, 2000, p. 254.

[647] C.A Bartel, 'Social Comparisons in Boundary Spanning Work: Effects of Community Outreach on Member Organizational Identity and Identification, *Administrative Science Quarterly*, Vol. 46, No. 3, 2007, p. 379-414.

[648] A. Domini, What is Social Investing? Who are Social Investors in the Social Investment Almanac, Lydenberg and Domini kinder, (Ed), (New York: Henry Host and Company, 1992).

[649] B. Hogan, *op cit*.

Notably, the entrance of this body of corporate social responsibility is timely and important for a number of reasons. Policy makers, legislative official inquiries and law reforms charged with reviewing corporate responsibility and governance are increasingly looking towards international and comparative models and other sources of guidance as evidenced by the two major Australian CSR inquiries that reported in 2006 as well as the revised Australian Stock Exchange (ASX) Corporate Governance Council, Corporate Governance Principles and Recommendation (ASXCGC Principles).[650] In some contexts, 'corporate social responsibility' is sometimes used interchangeably with terms like, 'corporate citizenship', 'responsible business', 'corporate sustainability', and 'triple bottom line responsibility'.[651] However, some commentators challenge the suitability of each element of the compound phrase 'corporate social responsibility'. They often ask such questions as – why should this form of responsibility be limited to corporate entities and not other public and private entities; why should it be limited to social responsibilities and not other responsibilities, and why should it be confined to legal and even ethical responsibility instead of under notions of corporate citizenship and responsiveness to societal conditions? In an attempt to reorient traditional thinking about the financial bottom-line of business sustainability, John Elkington[652] famously described 'a triple bottom-line for business in which considerations of 'economic prosperity', 'environmental quality, 'social justice combined and filtered their way into the overall calculus for business.

As a matter of fact, the CSR activities are about ethics and virtues. This is consequent upon the fact that corporate governance is concerned with how companies are managed and controlled, aligning the interests of stakeholders with that of management. The basic

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[650] For example, the term of reference for the Parliamentary Joint Committee on Corporations and Financial Services (PJCCFS) inquiry into CSR included reference to 'whether regulation, legislation, etc of other countries could be adopted or adapted for Australia.

[651] B. Honigan, *op cit*.

[652] J. Elkington, 'Cannibals with Forks: The Triple Bottom Line for 21st Century Business (reposted ed. 2002) 1999, 2.

principles of corporate governance as in transparent disclosure, accountability, fairness, appropriate risk management measures, information flow and the responsibility of senior management and the board of directors are all in tandem with the concept of corporate social responsibility. It could be concluded that from the above, the incision of CSR activities in corporate governance structures would not only harmonize existing interests in the company's sphere of business operation and guarantee sustainable development,[653] but it will go further to ameliorate the systemic failures, and help directors in their behavioural governance[654] such that the various interests in the corporation will be effectively aligned and maximization of interests achieved.

Having considered the benefit and how important it is to inculcate the stakeholder theory and the CSR in management of corporations, suffice it to say that a glimpse of the traditional way of managing corporations – legislative provisions, and a comparison of which of the two methods will go a long way in boosting the performance of corporations, will be made. This is clearly to show the importance of complying with legal or ethical mechanisms or otherwise.

There has been a renewed concern the world over in the substance of legislation regulating corporate governance systems. As already stated, the pervasive influence of business malfeasance, failures and collapse on investors' confidence, is nothing but a sorry story. Majorly, these pieces of legislation affect directors, financial statements, auditors, shareholders and other stakeholders' rights, as well as how they are well integrated in corporate decision making process. A cursory look at three jurisdictions to wit: U.K, U.S, India and Nigeria will be made in this regard.

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[653] I.O. Smith, 'Corporate Social Responsibility: Towards a Healthy Environment', *MPJFR*, Vol. 1, No. 1, 2000, p. 41.

[654] P.C. Iwu-Egwuonwu, 'Behavioural Governance, Accounting and Corporate Governance', *Quarterly Journal of Economics and International Finance,* Vol. 3, No. 1, 2011, p.1-12.

6.2 Corporate Governance in the United Kingdom

The United Kingdom operates Anglo-Saxon model of corporate governance which emphasizes the shareholder's interest. It relied on a single Board of Directors that is normally dominated by non-executives elected by shareholders.

Within this system, many boards include some executives from the company (who are ex-official members of the board). Non executive directors are expected to outnumber executive directors and hold key posts including audit and compensation committees.

In United Kingdom unlike the US, the Chief Executive Officer (CEO) generally does not serve as chairman of the Board. The core feature of corporate governance in United Kingdom, as well as in other Anglo-Saxon jurisdictions, is the shareholders control system. It involves corporate performance through strategy formulation and policy making, corporate conformance through management supervision and accountability to the shareholders.
According to Parkinsons,[655]

> The central feature of the current corporate governance is the vesting of executive powers in the board; and of control rights, most importantly, the power to remove the directors and also the right to decide certain other issues by the general body of shareholders. It is made up also of crucial ancillary rules relating to such matters as disclosure of financial information and audit, and the holding and conducting of shareholder meeting, liability rules, restricting managerial discretion and imposing standards of fair dealing and competence, and the rules determining who has standing to enforce those rules are also part of the overall structural control.[656]

[655] J.E. Parkinson, *op.cit*, p.159.
[656] Apparently referring to Anglo-Saxon model as practised by the United States, etc.

These control mechanisms put in place to achieve corporate governance in United Kingdom shall be discussed in the following headings.

i. Decision-making structure of the board
ii. Reward system
iii. Trusteeship strategy
iv. Right of appointment of directors by shareholders
v. Power to replace board members by shareholders
vi. Power of decision making of the shareholders
vii. Facilitation of collective action.
viii. The constraints rules
ix. Affiliation rights
x. Minority protection

The Decision-Making Structure of the Board

In contrast to the law of many jurisdictions, UK board permits the full delegation of board powers to committees of the board. This they do if, as is usual, the company's articles permit them to do so.

The boards of British firms tend to be small, like their US counterparts, and their articles now frequently require Audit and Compensation committees staffed by non-executive directors in keeping with emergent norms of good governance. But, it is noted that British firm typically have fewer non-executive directors when compared with the American companies; this is

notwithstanding the recommendation of the influential Cadbury Report of 1992[657] to have the non-executive directors in majority.[658]

The Reward System

It is noteworthy that the principal rewards to management for pursuing shareholders interest are created by contract rather than by law, notably through the vehicle of compensation contracts. Top managers tend to be monitored by means of market-based rewards and penalties.

The more important reward strategy is 'pay for performance'. This is used to provide managers with high-powered incentives based on their performances in order to encourage hardworking and honesty which in turn create shareholder value.

The Trusteeship Strategy

Trusteeship strategy places authority over the interest of a vulnerable constituency in the hands of decision makers who lack strong conflicting interest. In the case of shareholders, trusteeship protection implies a decision making authority within the firm that does not share the financial interests of hired managers.[659] What this implies is that in a company, a group of managers designated as directors are given powers and liabilities not shared by other managers and this arrangement invariably create a measure of trusteeship in so far as the manager-directors take more of the credit when the company does well and faces more of the blame when it does badly.

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657 Cadbury Committee published a report at the end of 1992 titled 'The Financial Aspects of Corporate Governance', which contains a code of best practices endorsed by the London Stock Exchange (LSE). The Report deals with four matters: The Board of Directors, Non-Executive Directors, Executive Directors and Reporting and Control. See Charles worth and G. Morese, *Company Law*, (London: Sweet & Maxwell 1996) p. 557.

658 R.R. Kraakman *et al., op. cit*, p.39; Non Executive directors are in general not involved in the actual running of the business, and so an obvious advantage in their ability to assess the company's performance, and that of management, from a more neutral stand point. They are now common in large companies and their appointment has been encouraged by the Bank of England, the Confederation of British Industry. The Cadbury committee proposes that all listed companies should appoint audit committees consisting exclusively of non-executive directors, and remuneration committees with membership mainly or wholly of non-executive directors; See J.E. Parkinson, *op. cit*, pp. 192-193.

659 R.R. Kraakman, *et al., op. cit*, p. 49.

Kraakman[660] observed that the law can reinforce trusteeship roles by removing opportunities for conflict with shareholders interest. This, according to him, can be done, not just by imposing restrictions on the ability of directors to enter into self-dealing transactions (restrictions that are similar in character to, though perhaps different in details from, those imposed on managers in general), but also by completely separating directors and managers: that is by mandating that some directors cannot be salaried employers.

The United Kingdom has been moving in above direction, but this does not show up so much in the statutory or decisional law in the listing rules. Consequently, a gap in governance opened up between listed and non listed public companies which currently the UK Company Law Review has moved to close.[661] However, the UK leads the US in dividing the role of the CEO and chairman of the board of directors by assigning the powerful chairman's position to a non-employee director. This has improved and strengthened the fiduciary relationship between the directors and the shareholders.

Right of Appointment of Directors by Shareholders

In Anglo-Saxon model of corporate governance, all the directors are appointed or elected by means of voting by the shareholders at the general meeting. The United Kingdom being a major jurisdiction that operates Outsider Based Model encourages the shareholders to use their voting rights to appoint people of proven integrity to serve as board members. This appointment right form one of the major powers given to shareholders for effective control of their company.

[660] *Ibid*, p. 50.
[661] *Ibid*

The Power to Replace Board Members by Shareholders

There are two aspects of the power of shareholders to remove or replace the directors: one of the aspects is the ability to remove a director at the end of his/her term in office. Statutory limitations on directorial terms range from as low as two years and above. In United Kingdom, the term in office of directors is from two years to no statutory term limits at all in the case of private companies which occasionally appoint director for life.[662]

The second aspect of removal power of the shareholder is the ability to replace a director midterm. British laws give the shareholders majority a strong non variable right to remove director without cause.[663] Unlike US, Britain permit length or even life time terms of office for directors but however offset its possible abuse by providing a strong removal power that is easily invoked and cannot be waived.[664]

The Power of Decision Making of the Shareholders

It is instructive to note that it is not all issues of corporate interest that shareholders are invited to participate in taking decision at the general meeting. Direct voting in any company with numerous shareholders involves high process costs and may often result in poor decision since small shareholders have little incentive to inform themselves.

Consequently, corporate law sharply limits the kinds of decisions for which shareholders are required or encouraged to make. The law ordinarily encourages shareholders to participate directly in substantive decision making only when full delegation of the power to decide to the management is clearly inappropriate or unsafe, as when directors are personally interested in the matter or when a corporate decision will fundamentally alter the corporation.[665]

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[662] *Ibid*, p. 37.
[663] UK Company Act, s. 303 (Removal within term) and S. 368 (Setting 5% threshold to call special meeting) UK, cited in R.R. Kraakman, *et al., op. cit*, p. 37.
[664] R.R. Kraakman, *op. cit*, p. 38.
[665] *Ibid*, pp. 40-47.

United Kingdom requires the general shareholders meeting not only to approve the appointment of the company's auditors but also to approve the distribution or re-investment of the company's earnings. The case of UK unlike that of US, where power of shareholders in general meeting is to a greater extent limited by statute suggest that the managerial list restrictions on shareholder powers are not the inevitable consequence of diffuse ownership, at least not where institutional shareholders retain a major role in corporate governance.[666]

Facilitation of Collective Action

Shareholders activism has attracted publicity for its political strength to bring pressure on the board of directors in the United Kingdom. In a bid to encourage shareholders activism, the Institutional Shareholders Committee (ISC), a joint body representing the largest institutional investor association in 2002 issued a statement of principle on shareholders action to adopt.

Institutional Shareholder Committee set out a statement of best practices concerning the responsibilities of institutional shareholders with regard to the companies in which they invest with the aim of securing for the ultimate beneficiaries through constant monitoring of the companies in which they invest. The institutional investors are encouraged to vote against the board of director at general meeting when they fail or refuse to accept criticism.[667]

Equally in UK, proxies are solicited by corporate partisans themselves, by management alone in the case of uncontested vote, and by management and its opponents in the case of contested votes. So, a proxy solicitation is relatively unregulated in UK jurisdiction thus encouraging shareholders action.[668]

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[666] *Ibid*, p. 49.
[667] O. Oke, *et al.,* Cross-cutting Issues in Nigeria Law - Essays in Honour of Prof. Funso Adaramola, (Lagos: Showers IMC Press, 2007) pp. 178-179.
[668] R.R. Kraakman, *et al., op.cit*, p. 42.

The Constraints Rules

Many rules have developed in UK companies law aimed at encouraging corporate governance by way of defining the business relationship between the directors and the shareholders. One of the rules of standard that qualifies as a general instrument of corporate governance is the duty of care. This duty constrains the directors as it defines actions that are 'negligent' or 'gross negligence'.

The Affiliation System

The regulation of terms of entry and exit perform a corporate governance function in major jurisdictions, including United Kingdom. Shares in large and liquid markets continuously aggregate and assess information about firm performance, and instantly exposes the key managers who appear to act contrary to shareholders interest. Securities law, listing rules and mandatory disclosure regime for public companies contribute to the quality and speed with which information about performance is reflected in share prices.[669] So with these interconnections and disseminations of information, shareholders become fully aware about business prospects and transactions which generate their actions and reactions at the general meeting and at the same time, the directors realize that their actions and inactions will always be known and assessed. Secondly, corporate law influences governance through entry and exit. Shareholders who lost confidence in a particular company are permitted by law to transfer their interests to another company without managerial bottle neck.

UK's city code mandates managerial passivity in the face of hostile offer. In effect, UK exhibits the most take-over friendly legal regime. The law allows hostile takeover in that jurisdiction to have real bit as a governance mechanism. Kraakman submitted thus:

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[669] *Ibid*; p. 52.

> More than elsewhere in corporate law, we suspect that the decisive fact here is the greater political influence of institutional investors in the UK (as augmented by centralized and self regulatory law making) as compared to the greater political power of managers in the US (as augmented by decentralized law making by state courts and legislature).[670]

Minority Protection

Although the corporate Governance system is principally designed to promote the interests of shareholders as a whole, however, agency problems of the corporate firm are normally expected to be addressed to give full effect to a good governance system. The agency problems are the usual conflict between majority and minority shareholders and that between shareholders and non shareholders constituencies.

To the extent that the law adopts the instrument of corporate governance to mitigate either of the agency problems, it inevitably modifies the governance in ways that reduced the power of the shareholders majority for the benefit of minority shareholders and non shareholder constituencies.

United Kingdom is one of the jurisdictions that have effectively used reward strategy to breach the gap between shareholders or majority and minority shareholders. This is achieved by providing that dividends must be paid to shareholders on pro rata basis within a given class of shares. It follows that corporate distribution that benefit controlling shareholders must benefit minority shareholders too.

Other rules that aim at pro rata distributions are to the same effect, for example, rules prohibiting the firm from repurchasing shares from selected shareholders to the exclusion of

[670] *Ibid*, p. 53.

others, or curtail rules that give minority shareholders an option to piggy back on the sale of control blocks of shares.[671]

Further, there is a significant protection of minority shareholders through direct voting, litigation to enforce judiciary duties and through mandatory disclosure rules, securities laws and listing requirement. UK and US scope for mandatory disclosure remains most extensive in all jurisdictions.[672]

Conclusively, United Kingdom is said to be at forefront in corporate governance when compared to other jurisdictions or countries like United State of America.[673]

6.3 Corporate Governance in United States

United States is a country rooted in Anglo-Saxon model of corporate governance. Here, corporate governance typically focuses on companies outside investors mainly shareholders.

In United States, corporations are directly governed by state laws, while the exchange (offering and trading) of securities is governed by Federal legislation. Many US States have adopted the model Business Corporation Act but the dominant State law for publicly traded corporations is Delaware, which continue to be the place of incorporation for the majority of publicly traded corporations. Individual rules for corporations are based upon the corporate charter and less authoritatively the corporate by-laws. I will now proceed to show how these laws and other corporate practices in US have influenced or encouraged the establishment of corporate governance in that jurisdiction. The format used in discussing UKs jurisdiction shall be equally followed here.

The Decision-making Structure of the Company's Board

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[671] *Ibid*, pp. 59-60.
[672] *Ibid*
[673] O. Oke, *et al., op. cit*, p. 89.

There is a growing consensus among corporate analysts that good corporate governance depends on numerous 'best practices', chief among these are the size of the board (small board better), the committee structure of the board (independent audit, compensation and nominating committees are good), the frequency of board meetings (more meeting are better) and the ratio of insiders to independent directors (a majority of independent directors is good).[674]

The US being the birth place of corporate governance reform has introduced laudable standards so far. It is therefore not surprising that the model US public company now follows many of these governance standards. For instance US board tends to be small by international standards (although this is not legally mandated). They also tend to have well developed committee structure.[675]

In contrast to the law of many jurisdictions, United States permits full delegation of board powers to committees of the board.[676] In 1970, the New York Stock Exchange (NYSE) first required listed companies to appoint audit committee staffed by independent directors. In the wake of Enron cohort of financial scandal, the major US Exchange have proposal requiring an absolute majority of independent directors on the boards of listed companies as well as nomination committees composed entirely by New York Stock Exchange (NYSE).

Moreover, in reaction to the same wave of scandals, the Securities and Exchange Commission (SEC) has promulgated rules requiring all public companies to disclose whether they have a 'financial' expert who is independent from management service on their audit committee (and if not; to explain why not).[677]Nevertheless, in America where non executives are often in the majority, one commentator has observed that 'boards of directors of most

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[674] R.R. Kraakman, *et al., op. cit*, p. 38.
[675] *Ibid*, p. 38.
[676] *Ibid.*
[677] *Ibid*, p. 39.

companies do not do an effective job in evaluating, appraising, and measuring the company precedent until the financial and other results are so dismal that some remedial action is forced upon the board.[678]

The Reward System

As noted before, the more important reward strategy is ‘pay for performance’ which is widely used in US. United States corporate law, in particular, goes far toward facilitating performance-based compensation by authorizing the issuance of stock options, shadow stock, and other forms of incentive compensation.

In addition to the above, United States disclosure rules and tax regulation also favour performance-based compensation.[679] All these spur the management to be at their best as they will be rewarded according to the honest contribution and output generation.

The Trusteeship Strategy

United States law, although not so categorical, strongly encourages non-employees (and other independent) directors on board of public companies. Also, US exchange rule now require a majority of independent directors on the boards of listed companies.[680] These arrangements create the sense of trusteeship on the management and thus discourage self enrichment and betrayal of the interests of the shareholders.

Right of Appointment of Directors by Shareholders

US jurisdiction is reputed in its rules on the ‘independent directors’ and committees. The non executive board from which independent directors emerge are all regularly appointed or elected by the shareholders at the general meeting. The value of this independence is assured

[678] M.L. Mace, ‘Directors: Myth and Reality-Ten Years Later’, (1979) 32 *Rutgers Law Rev*. 293, cited in J.E. Parkinson, op. cit, p. 195.
[679] R.R. Kraaakman, *et al., op. cit*, p. 57.
[680] *Ibid*; p. 50.

in United States in its trend towards assigning non executive directors to decide issues that might implicate executive directors in a conflict of interest. In effect, these developments imitate decision making in a two-tier board by using a committee of independent directors on single tier board as quasi supervisory board.[681]

The Power to Replace Board Members by Shareholders

United States law provides a weak removal power to the shareholders. However, some important US jurisdictions make shareholders power to removal without cause a default provision as provided in Revised Model Business Corporation Law.[682] Other jurisdictions grant the power as a mandatory right (unless the board is classified) but limits its scope by denying shareholders the authority to call a special shareholders meeting unless the charter expressly permit it.[683]

On the period in which a director can hold office, US corporate law falls at the short end of the spectrum, with a one-year term as the default rule and ordinarily a maximum term of three years for staggered boards.[684] Interestingly, although US law establishes a relatively weak removal right (especially in the critical state of Delaware, it also fixes shorter term of office than do many other jurisdictions).[685]

The Power of Decision Making of the Shareholders

United States shareholders can ratify fundamental corporate decisions such as mergers and charter amendment but are powerless to initiate them.[686] In US jurisdiction, the power of the shareholders at the general meeting is substantially curtailed. The reason for this is less

[681] *Ibid*, p. 35.
[682] Revised Model Business Corporation, s. 8.08(a).
[683] Dalaware General Corporation Law, s. 141(K).
[684] R.R. Kraakman, *et al, op. cit*, p. 37.
[685] *Ibid*, p. 38.
[686] *Ibid*, p. 47.

straight forward, since one might suppose that direct shareholder decision rights would actually improve the governance of public companies.

Gilson and Kraakman[687] point out that the reason why these rights are not available to US shareholders is the considerable political power of corporate managers. In particular, if US shareholders were able to shape corporate policy by, for example, amending the corporate bylaws, they could also dismantle the defensive tactics that management erect toward hostile acquirer.

Facilitations of Collective Action

In US just like in United Kingdom, proxies are solicited by corporate partisans themselves, by management alone in the case of opponents in the case of a contested vote. In United States however, heavy regulation of proxy solicitation has been a major obstacle to shareholder action.[688]

US securities law on the other hand favours shareholder insurgency. For example, the SEC proxy rules can force insurgent managers to make sweeping and often embarrassing disclosures, guarantee that insurgent solicitation materials will reach the company shareholders, and in some cases permit shareholders to piggy back proposals opposed by management at negligible cost on management's own proxy solicitation. It is essential to note that United States may be the only jurisdiction to permit corporations to compensate successful insurgent *ex post* their campaign cost.[689]

The Constraint Rules

[687] R.R. Kraakman, *op. cit*, p. 49.

[688] In 1992, there was a reform to the proxy system in US through Regulation of Communication Among Shareholders, SEC Release N0 34-31326 (1992). This reform relaxed many of the regulatory barriers to shareholder communication, such as filling and disclosure requirements. But, significant barriers remained; *Ibid*, p. 42.

[689] *Ibid*, pp. 42-43.

US jurisdiction, through provisions for committees like audit committee, nominating committee etc, has been able to check the activities of the board of directors and consequently solidified a vibrant corporate governance in both public and private companies or corporations in United States and beyond.

The Affiliation System

As noted above in UK jurisdiction, corporate law influences corporate governance through the entry and exit strategies by intervening in the market to make hostile takeovers more or less difficult. US (and Netherland) are the only countries that specifically empower boards to block hostile bids. Indeed, US courts, in particular, have endorsed the so called 'poison pill', which precludes a hostile bid entirely over the objection of a defending board of director. Perhaps, the factor responsible for anti-takeover defensive tactics in US is the greater political power of managers as augmented by decentralized law making by state courts and legislature.[690]

Minority Protection

Under United States law, the authority to initiate proposals to merge or dissolve a company is vested exclusively on the board of directors.[691]This measure has been observed to be in protection of minority shareholders whose interest or merger or winding up of their company can be displaced by the interests of the majority shareholders who may not be in majority in terms of number but by the volume or class of shares in their control.

Secondly, United States provides significant protection of minority shareholders through mandatory disclosure rules, securities laws and listing requirement.[692] Furthermore, US corporate law provide for exit right, though, only upon egregious abuse of power by a

[690] *Ibid*, p. 53.
[691] *Ibid*, p. 58.
[692] *Ibid*, pp. 59-60.

controlling shareholder or upon the occurrence of major transaction that threaten to transform the enterprise, for example, the possibility of appraisal rights (a mandatory buyout option) upon occurrence of fundamental transaction.[693]

6.4 Corporate Governance in India

Under the Securities and Exchange Board of India (SEBI),[694]the Committee on Corporate Governance defines Corporate Governance as 'acceptance by management of the inalienable rights of shareholders as the true owners of corporation and of their own role as trustees on behalf of the shareholders. It is about making a distinction between personal and corporate fund in the management of a company'. It has been suggested that Indian approach is drawn from Gandhian principle of trusteeship and the Directive Principles of Indian Constitution.[695]

Although India has been rather slow in establishing corporate governance principles over the last decades, 2012 was a positive year for progression in India corporate governance arena. The Companies Bill 2012, passed by Lok Sabha (the lower house) on 18 December 2012, includes a number of new provisions aimed at improving the governance of public companies.

Interestingly, despite the facts classifying India under emerging market and the structure of Indian businesses differing significantly from those in the UK, the foundations of the new Indian corporate governance model are drawn from Anglo-Saxon governance model.

The investor based in the Indian corporate market for instance, largely consists of company founders, the respective family members and the government.[696] Thus, though India tends toward British model of corporate governance, in contrast, shareholders in UK companies are

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[693] *Ibid.*
[694] SEBI-Securities and Exchange Board of India.
[695] Corporate Governance in India-Corporate/Commercial Law, available at: www.mondaq.com/india/x/246876/corp. (accessed on 10/11/2013).
[696] *Ibid.*

less concentrated towards a certain group of people, are geographically dispersed and largely held by professional investors. However, notwithstanding the significant differences in corporate structure in the two markets, the corporate governance proposals[697] published in India are similar to those adopted in the UK.

It is important to note that though it is clear that the proposal stem from the Anglo-Saxon corporate model, in some instances they go further to introduce new initiatives which recognize the need for certain obligatory requirements and the need for training in a market that has for centuries been based on closed board structure and investor base.

Also, there has been a clear move in India to develop corporate market to attract foreign investment. Foreign investments are slowly increasing shareholder diversity in some companies. This in turn pushes the agenda for the introduction of a regulated and universal governance model.[698] The criteria used in assessment of corporate governance in UK and US shall be replicated, though limited to structure of the board, disclosure mechanisms and decision (voting) rights of the shareholders.

The Decision-Making Structure of the Board

In India, the number of directors of a company is set in the Articles of Association as being no less than five (5) directors and no single person is expected to hold directorship in more than 10 listed companies.[699] Also there is requirement that where the roles of chairman and CEO are combined, there should be a strong independent element on the board and the

[697] The Indian market, the Securities and Exchange Board of India (SEBI), recently issued a consultative paper on the 'Review of Corporate Governance' encouraging a wider debate on governance. The paper calls for, *inter alia*, the splitting of the role of Chairman and Chief Executive, disclosure of the reason for independent director's resignation from office, a limit on the term of appointment of independent directors and greater involvement of institutional investor, the appointment of independent director by minority shareholders, independent directors to receive compulsory training and pass examinations and the adoption of a principle based approach for certain issues. See Corporate Governance India.
[698] *Ibid.*
[699] F. Ajaogwu, *op. cit*, pp. 394-395.

decision to combine the roles of Chairman and Chief Executive should be publicly explained. The chairman should in principle be separate from the Chief Executive.[700]

Directors are to be elected at a shareholders meeting in accordance with the Article of Association. Independent directors must be independent of any major shareholder and not involved in the day to day operations of the listed company. In line with the above, it is required that director must:

i. Be independent from the major shareholders of the company or any shareholder in the group.
ii. Not be an employee, staff member or other regular benefit from the company or its affiliated company, associated company or related company.
iii. Having no share in their own name, or in a related person's name, representing more than 0.5% of the respective paid up capital of the company, an affiliated company, associated company or related.
iv. Protect the interests of all shareholders of the company equally.
v. Prevent conflict of interest between the company and its management or major shareholders or other companies which have the same management group or major shareholders, as the company.
vi. Attend board meetings to make decisions on significant company activities.

Moreover, each board is required to establish an Audit Committee, Nominating Committee and Remuneration Committee in the listed company and an executive committee to which the board will delegate some of its duties is recognized unless expressly provided otherwise in the Articles of Association and sanctioned by the Act.[701]

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[700] *Ibid*, p. 397.
[701] *Ibid*, pp. 400-401.

Disclosure and Reward System

The following disclosures are required for companies in India in promotion of corporate governance:

i. Comprehensive report on the relatives of directors;

ii. Disclosure of interests of directors;

iii. The directors' shareholding register should be stated in the notice of AGM of companies; and

iv. Details of loans to directors.[702]

The board should show in its annual reports:

i. Whether one-third of the board is independent and where the company has a significant shareholder, whether the board representation shows the investment of the minority shareholders in a company.

ii. An analysis of the application of the best practices to the circumstances of the board.

iii. The nominating committee should annually review the mix of skills and experience and core competence, which non-executive directors should have.

iv. The number of board meetings held per year and the attendance of each director at the meeting held. This will assist the company to reward the director, according to contribution and performance, thus, remuneration of directors approved by an AGM should be disclosed in the Annual Report.

v. The number of audit committee meetings held each year, and the details of attendance of each individual director, the obligation to disclose the activities of the audit committee lies with the board and not the audit committee.[703]

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[702] *Ibid*, p. 405.
[703] *Ibid.*

The Power of Decision Making of the Shareholders

Shareholder approval is required for amendments to the company's memorandum and article of associations, sale of major assets, increase or decrease of capital, appointment of directors, transfer or acquisition of business, amending or ceasing a major leasing agreement, authorizing other people to manage the company's business, amalgamations with other company's business, issuance of debentures, merger and company's dissolution (winding up).[704]

6.5 Corporate Governance in Nigeria

Corporate Governance has received attention in Nigeria. It came as a reaction to allegation of financial misrepresentations or misstatements by some companies such as Lever Brothers Ltd, Cadbury Plc and Telkom Ltd. This prompted the Securities and Exchange Commission to set up a committee on corporate governance, which produced its report leading to the drafting of the Code of Best Practices on Corporate Governance in Nigeria (2003 SEC Code) which was later revised in 2011 and became known as Code of Corporate Governance in Nigeria (2011 SEC Code).

Similar reaction has trailed the allegation of misstatements against Cadbury Plc of Nigeria prompting the Security and Exchange Commission to conduct investigation and hearing on the allegations.[705] It is instructive to note that this power of investigation has been vested on Corporate Affairs Commission by Companies and Allied Matters Act. [706]

With the coming into force of the Companies and Allied Matters Act 1990 (now Cap. C20 LFN 2010) and several codes of corporate governance in Nigeria, issues of corporate governance have been enhanced and promoted like in other major jurisdictions of the world.

[704] *Ibid*, p. 408.
[705] *Ibid*, p. 6.
[706] Section 7 (1) (c).

The mechanism and practices of corporate governance in Nigeria shall be discussed following the above criteria used in UK and US.

The Decision Making Structure of the Board

It is instructive to note firstly, that the Companies and Allied Matters Act (CAMA) which is the major legislation regulating company in Nigeria did not provide for a structure of the board to reflect modern realities in corporate governance, thus, making the issue of governance a matter of individual corporate practices defined and promoted by different codes of corporate governance. Though, Nigeria could be said to be moving toward Anglo-Saxon model of corporate governance, its core principles or features have not been properly enthroned in Nigerian jurisdiction.

To start with, section 244 of CAMA provides that directors are persons duly appointed by the company to direct and manage the business of the company. Now the practical problem in Nigerian companies is the confusion as to where the duties of the management end and where those of the directors begin.[707]

Regarding the number of non-executive directors, it is interesting to note that the Act does not make any provision with respect to the need for non executive directors. However in practice, some companies still designate a portion of its director as non executive. Also the issue of whether the Board composition should not have more of the executive or more of non executive has been a burning issue in Nigeria. Onosode,[708] while acknowledging the importance of the issue warned:

[707] Section 63 of CAMA also provides that 'except as otherwise provided in the company's articles, the business of the company shall be managed by the board of director or…'
[708] G. Onosode, 'I Don't Believe that You Get Good Governance by Merely Transiting from Public to Private', *Privatization Digest Journal of Bureau of Public Enterprises*, January March 2010.

> I need to sound this note of caution, it is not the mathematical distinction between executive and non executive that guarantees the quality of decision in the board room…the quality of the individual is what ultimately determine the capacity of our corporate governance processes and procedures.

Another issue is the independence of directors. CAMA does not have specific provisions with respect to independence of directors although by virtue of section 279 (6), there is an allusion to that. According to the subsection 6, 'a director shall not fetter his discretion' to vote in a particular way.

Moreover, the Companies and Allied Matters Act does not place any limitation[709] on the number of directorship that may be held by any one person. In fact, it indirectly endorsed multiple directorships when it provided in section 281 that:

> The fact that a person holds more than one directorship shall not derogate from his fiduciary duties to each company including a duty not to use the property, opportunity or information obtained in the course of the management of one company for the benefit of the other company; or to his own or other person's advantage.

This multiple directorship is one of the problems facing Nigerian companies as it reduces the possibility of having truly independent directors in the board whose decision will be devoid of sentiments and personal business attachments.

Finally, section 263 (4) of CAMA provides that directors may elect a chairman of their meeting and determined the period for which he is to hold office. But the Act is silent on whether or not the chairman is to have day to day management powers.

[709] The Act however provide for the minimum and maximum number that will make up a board. Section 246 of CAMA provides that every company registered on or after the commencement of this Act shall have at least two directors. The maximum shall be determined by the Article of Association. See section 249 (3) of CAMA).

However, by the Code of Corporate Governance in Nigeria, the position of the chairman and chief executive should be clearly separated and held by different persons. A combination of the two posts in an individual represents an undue concentration of power. In exceptional circumstance where the two positions are held by the same person, there shall be strong non-executive independent directors as vice-chairman of the board.[710]

Reward System

The remuneration of directors is, as a rule regulated by the Act and the articles, but unless so provided, or there is an agreement to that effect, they are not entitled to remuneration for service since they are not servants of the company, but are in the position of managers. According to Orojo,[711] a director may of course, hold some other position as servant of the company; for example secretary or managing or executive director in which case he is entitled to a salary for these services.

Nevertheless, the shareholders play a major role in determining the remuneration when provided in the article. Companies and Allied Matters Act[712] provide that the remuneration of directors shall from time to time be determined by the company in general meeting. With this arrangement, the shareholders reward the directors handsomely whose performance is high. But, if the directors performed abysmally, they (shareholders) will reproach the directors through proportionate review of their remuneration. These promoters encourage hard work and honesty among the directors.

[710] J. O. Orojo, Company Law and Practice in Nigeria, 5th ed. (Cape town: LexisNexis, 2008) p. 283.
[711] *Ibid*, p. 279.
[712] See section 267 (1). Apart from salaries, the director may also be paid all travelling, hotel and other expenses properly incurred by them in attending and returning from meetings of the directors or any committee of the directors or general meeting of the company or in connection with the business of the company. See s. 267 (2), CAMA.

Trusteeship Strategy

Directors must observe good faith toward the shareholders and non shareholders constituency. This duty is imposed by law.[713] A director shall act at all times in ways which he believes to be the best interest of the company as a whole as to preserve its assets, further its business and promote the purpose for which it was formed.[714]

Therefore, director(s) who so used their power as to obtain benefit for themselves at the expense of the shareholders, without informing them of the fact, cannot retain those benefits and must account for them to the company.[715] It is important to know that directors' duty of trusteeship is for the whole company and not individual or collective shareholders alone. This trusteeship strategy has been put in place by the law to ensure trust, accountability and effective management and these ensure good corporate governance.

Right of Appointment of Directors by Shareholders

The appointment of directors is governed by the Act and the articles. Accordingly, section 247 provides for the appointment of the first directors whose appointment shall be by the subscribers of the memorandum of association. But subsequently, the members at the general meeting shall have power to re-elect or reject directors and appoint new ones.[716] With this power of reelecting or rejection having been given to shareholders at the general meeting, any non-performing director can be dropped. The realization of this power by the directors keeps them in check in pursuing personal gains detrimental to the interests of the shareholders.

[713] See section 279 of CAMA which provides that a director of a company stands in a fiduciary relationship towards the company and shall observe the utmost good faith towards the company in any transaction with it or on its behalf.
[714] Companies and Allied Matters Act (CAMA), s. 279 (3).
[715] J.O. Orojo, o*p. cit,* p. 265
[716] CAMA, s. 248.

The Power to Replace Board Members by Shareholders

This right of shareholder to replace or remove a director is different from the one discussed above. Right of appointment or rejection accrues at the end of the tenure of the director. However, a company may by ordinary resolution remove a director before the expiration of his period of office, notwithstanding anything in the articles or in the agreement between the company and the director.[717] The effect of the [provision] is that even a person appointed a director for life or as a permanent director by the articles or by agreement may nevertheless be removed by the general meeting, subject of course, to his right to compensation, if any. The foregoing position is key to corporate governance as it is designed to have effect of checking the excesses of the directors, by allowing the shareholders to assert themselves against the director, if need be and make it clear that the ultimate control of the company is in the hands of the shareholders considered as the owners of the company, and not the directors.

The Power of Decision Making of the Shareholders

CAMA[718]gives the shareholders in Nigeria wide powers to participate in taking decisions that affect the business of the company to which they are members. Two most important of these rights/powers of decision making of the shareholders in Nigeria are the right to attend meeting, where major issues of company's affairs are taken in Nigeria and the right to vote.[719]

Facilitation of Collective Action

Collective action is usually expressed by way of activism by the shareholders especially the institutional investors. While shareholders activism has reached its credendum in UK, in

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[717] *Ibid*, s. 262.
[718] Companies and Allied Matters Act
[719] Section 114 of CAMA provides for this, and clearly assert that these rights cannot be derogated from through article of association of the company.

Nigeria it is still a mirage. The increasing listing on the Stock Exchange by companies, financial institutions like banks, insurance companies, Pension fund, etc suggest that more of investors or shareholder's fund would be left in the hand of management.[720]

The Constraints Rules

Companies and Allied Matters Act contains a lot of rules of restriction on the director to prevent fraud and secret transactions and gains. For instance section 280 of CAMA prohibit secret profit or other unnecessary benefits. Others include prohibition of payment of discount and commission out of shares and capital.[721] This is subject to some exceptions. Also, a person convicted of fraud by a High Court of any offence in connection with the promotion, formation or management of a company or winding up of a company shall be barred from becoming or retaining the post of director for a period not exceeding 10 years, to be ordered by the court.[722] These rules help in maintaining and promoting corporate governance.

Minority Protection

Minority protection is a matter of law in Nigerian corporate affairs. Copious provisions have been enacted into the Companies and Allied Matters Act aimed at protecting the interests of minority shareholders in Nigeria. This has encouraged good corporate governance as there is little or no room for majority's oppression and manipulations.[723] On incorporation, the company acquires a separate legal personality distinct from its members. This presupposes, among others, that only the company may sue for wrong done to it or ratify irregular conduct. Accordingly, where irregularity has been committed in the course of a company's affairs or any wrong has been done to the company, only the company can sue to remedy that wrong

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[720] It is however important to note that CAMA made provision that can facilitate collective action by allowing proxy voting, (section …), written resolution for private companies (section 234), right of attendance at general meeting (section 227).

[721] CAMA, s. 130.

[722] *Ibid*, s. 254.

[723] See generally sections 299-301.

and only the company can ratify the irregular conduct.[724] This principle is however not absolute as it would operate in complete disregard of the interest of minority shareholders. Therefore, a measure of protection is afforded the minority against illegal and oppressive conduct by the majority whose view prevails in the company.[725] Where however, a member institutes a personal action to enforce a right due to him personally, he shall not be entitled to any damages but to declaration or injunction to restrain the company and/or the directors from doing a particular act.[726]

As has been mentioned earlier corporate governance around the world differs according to the variety of capitalism in which they are embedded. The Anglo-American 'Model' tend to emphasize the interest of shareholders, the quasi shareholder or coordinated model associate with continental Europe and Japan also recognizes the interest of workers, managers, suppliers, consumers and the community. A related distinction is between market orientated and network orientated models of corporate governance.[727]

We shall now discuss the models of corporate governance in the different countries, to wit: United Kingdom, United States, India and Nigeria. In this discussion, we shall comparatively compare the model of corporate governance of each of the country, placing side by side the corporate governance guidelines and code of best practice of each of the country. In our discussion, we shall take cognizance of the following components of corporate governance as it functions in each of the jurisdiction in discourse:

i. An overview of the corporate governance of each of the country
ii. Definition of corporate governance by each country's corporate governance
iii. The corporate objective and mission of the board of directors

[724] CAMA, Cap. C20 LFN 2010, s. 299.
[725] CAMA, Cap. C20 LFN 2010, s. 300.
[726] *Ibid*., s. 301.
[727] Ibid, see also Williansom Oliver E (1988) "corporate finance and corporate governance, "Journal of finance. 43(3) , PP 567-591.

iv. Board membership criteria/Director qualification standards

v. Separation of chairman & CEO

vi. Mix of executives, non-executives and independent directors

vii. Definition of independence.

viii. Conflicts of interest & ethics

ix. Election terms, term limits & mandatory retirements

x. Director compensation and stock ownership.

xi. Evaluating board performance.

xii. Board interaction/Communication with shareholders, press, customers etc.

xiii. Board meetings and agenda

xiv. Number, structure and independence of committee

xv. Formal evaluation of the CEO

xvi. Executive compensation and stock ownership

xvii. Corporate governance guidelines

xviii. Internal control system

xix. Shareholder voting powers

xx. Shareholder meeting and proxy proposals

xxi. Anti-takeover devices

6.6 Analytical Comparison of Corporate Governance in UK, USA, India and Nigeria

A comparative analysis of the above listed components as it pertains to each country is discussed in details below:

Overview of the Corporate Governance of Each of the Countries Named Above

In our discussion here, particular emphasis is placed on the legal document or instrument providing for corporate governance, the issuing body, the legal basis of compliance, objective, scope and predominant board structure.

Starting with the United kingdom, the applicable Code is the Report of the Committee on Financial Aspect of Corporate Governance (Cadbury Report) issued in Dec 1992 by the Financial Reporting Council and the London Stock Exchange and reissued in 1996 and the Combined Code on Corporate Governance issued in July 1998 by the Financial Reporting Council (FRC) a UK association that include representatives of business accountancy, law, government, and public sector, revised in July 2003, June 2006, June 2008.

Both codes are the legal instruments providing for corporate governance in the U.K. Within the jurisdiction of the United States of America, however, the Report of the NACD Blue Ribbow Commission Director, Professor Alesm issued in Nov, 1996 by National Association of Corporate Directors (NACD) and reviewed 2002, 2005 as well as the BRT Principle of Corporate Governance issued in May 2002 by the Business Roundtable (BRT) a committee related to business industry/academic association and revised Nov, 2005).

In India, the applicable code is the Report of the Committee appointed by SEBI on corporate governance, which was issued in February, 2000 by the Security and Exchange Board of India SEBI. Turning over to Nigeria, the Securities and Exchange Commission (SEC) came up with 'the SEC Code of Best Practices on Corporate Governance 2003' (for public quoted companies). The CBN came up with two codes in 2006 namely: 'the Codes of Conduct for Directors of Licensed Banks and Other Financial Institutions, and the Code of Corporate Governance for Banks in Nigeria Post Consolidation. Issues of corporate governance could

be read into the provisions of the Companies and Allied Matters Act (CAMA)[728]which is obviously an enactment of the National Assembly.

As to the nature of compliance required under the various codes applicable in the various jurisdictions; the Cadbury Report applicable in the U.K requires that companies should either comply with the provisions of the code or explain the reason for non compliance i.e. disclosure (comply or explain). The Combined code on the other hand includes principles which are mandatory as well as provisions which are to be observed on a comply or explain basis. The code has been appended to the listing rules of both the London Stock Exchange (LSE) and the Irish Stock Exchange (ISE).

In the United States of America under both codes applicable in that jurisdiction, compliance with the provisions of the codes is voluntary. The Report of the Committee appointed by SEBI on corporate governance applicable in India is voluntary. The provisions as contained in the Code of Best Practices on Corporate Governance in Nigeria, 2003,[729] which was issued by the Securities and Exchange Commission; the Code of Corporate Governance for Bank in Nigeria Post Consolidation, 2006[730] which was issued by the Central Bank of Nigeria (CBN), and the Code of Corporate Governance for Licensed Pensions Operators, 2008[731] which was issued by the Pension Commission, are all voluntary. However, the provisions of CAMA regarding corporate governance are mandatory on all companies in Nigeria, especially because they are statutory enactment and not just provisions of a code.

[728] Cap C20 LFN 2004
[729] I.e. 'the 2003 SEC Code.'
[730] Referred to as the CBN 2006 Code
[731]Referred to as the 2008 PENCIM Code

The objectives of corporate governance under these countries under review to a large extent appear to be similar, to wit:

i. to improve the quality of (supervisory) governance
ii. to improve governance related information available to equity markets.

In India however, the major objective is to improve companies' performance, competiveness and for access to capital.

The scope of the various codes applicable in the various jurisdictions under consideration relates only to listed companies although it is an accepted view that all other companies are encouraged to observe the provisions of these codes. The predominant board structure in all named jurisdiction above is unitary.

Corporate Objective and Mission of the Board of Directors

In the U.K and as contained in the Cadbury Report, the board should retain full and effective control over the company and monitor the executive management.[732] Boards must be free to drive their companies forward, but should exercise that freedom within a framework of effective accountability. Thus, every company should be headed by an effective Board, which is collectively responsible for the success of the company.[733]

The board's role is to provide entrepreneurial leadership of the company with a framework of prudent and effective control which enables risk to be assessed and managed. The board should set the company's strategic aims, ensure that the necessary financial and human resources are in place for the company to meet its objectives and review management

[732] UK Combined Code, s. 1.1.
[733] Cadbury Report, s. 1.1; Main Principle A1.

performance. It should set the company's values and standard and ensure that its obligation to shareholders and others are understood and met.[734]

On the other, hand in the United States, and under the NACD Report, the objective of the corporation (and therefore of its management and board of directors) is to conduct its business activities so as to enhance corporate profit and shareholder gain. In pursuing this corporate objective, the board's role is to assume accountability for the success of the enterprise by taking responsibility for management, in both failure and success. This means selecting a successful corporate management team, overseeing corporate strategy and performance, and acting as a resource for management in matters of planning and policy. Among the most important missions of the board is ensuring that shareholder value is both enhanced through corporate performance and protected through adequate internal financial control.[735] According to other applicable codes in the US especially the BRT Principles, the business of a corporation is managed under the direction of the corporation's board. The board delegates to the CEO and through the CEO to the senior management, the authority and responsibility for managing the everyday affairs of the corporation. Directors monitor management on behalf of the corporation's shareholder.

Under the Indian corporate law jurisprudence, the pivotal role in any system of corporate governance is performed by the board of directors. It is accountable to the stakeholder, including shareholder, and directs and controls the management, stewards the company; sets its strategic aim and financial goals and oversees the implementation; puts in place adequate internal controls, and periodically reports the activities and progress of the company in a transparent manner to the stakeholders. The board of a company provides leadership and strategic guidance, objective judgment independent of management to the company and

[734] (Supports Principle A.I)
[735] See Report of the NACD Blue Ribbon Commission on Board Leadership (2004).

exercise control over the company, while remaining at all times accountable to shareholders.[736] The shareholders are the owners of the company, and as such they have certain rights and responsibilities. As owners of the business, the shareholders delegate many of their powers to the directors.[737]

In Nigeria, the corporate objective and mission of the board of directors can be summarized to be the management and organization of the business of the company in the interest of the members who are the shareholders and that of the creditors of the company. This objective can be implied in the relevant provisions of CAMA.[738]

Board Membership Criteria/Director Qualification Standards

The issue of board membership criteria is not expressly mentioned in the Cadbury Report. It is however noted that given the importance of their distinctive contribution, non-executive directors should be selected with the same impartiality and care as senior executives.[739] Accordingly, it is recommended that their mode of appointment should be a formal selection process, which will reinforce the independence of non-executive directors and make it evident that they have been appointed on merit and not through any form of patronage.

In the same vein, under the Combined Codes still within the UK jurisdiction, appointments to the board should be made on merit and against objective criteria.[740] The board should satisfy itself that plans are in place for orderly succession for appointment to the board so as to maintain an appropriate balance of skill and experience. The board should set out to

[736] *Ibid*, s. 6(1).
[737] *Ibid*, s. 14(1).
[738] Companies and Allied Matters Act, s. 244.
[739] NACD Report, s. 4(15).
[740] Principle A.4.

shareholders in the paper accompanying resolution to elect a non-executive director why they believe an individual should be elected.[741]

Similar criteria is applicable within the jurisdiction of the US where, as provided for by the NACD Report, to be considered for board membership, a prospective director should possess all of the following personal characteristics: integrity and accountability, informed judgment, financial literacy, mature confidence, and high performance standard. The Commission[742] recommends that the board as a whole should possess all of the following core competencies with each candidate contributing knowledge, experience, and skills in at least the domain of accounting and finance, business judgment, management crisis response, industry knowledge, international markets, leadership and strategy. Boards should consider the distinctive skills, perspectives and experiences, which candidates, diverse in gender, ethnic background, geographic origin and professional experience, can bring to the boardroom. To have greater congruence with shareholders' interests, candidates should be prepared to own a significant equity position in the company.[743]

Borrowing a leaf from the above code, the Business Round Table (BRT Principles) believes that having directors with relevant business and industrial experience is beneficial to the board as a whole. Directors with this experience can provide a useful perspective on significant risks and competitive advantages and an understanding of the challenges facing the business. A diversity of background and experience, consistent with the corporation's need for particular backgrounds and experience may change overtime. The board should monitor the mix of skills and experience that directors bring to the board against established board membership criteria to assess, at each stage in life of the corporation, whether the

[741] *Ibid*., A. 7.2.
[742] The Blue Ribbons Commission set up by NACD.
[743] J.H. Gregory, *op. cit*, pp. 9-11,15 and 14 respectively.

board has necessary tools to perform its oversight function effectively.[744]Planning for the departure of directors and the designation of new board members is essential. The board should plan ahead for changes in membership, and it should have written criteria for director candidates that should be relevant and re-evaluated periodically.

No formal departure is made in India where good corporate governance is seen to dictate that the board be comprised of individuals with certain personal characteristics and core competencies such as recognition of the importance of the board's tasks, integrity, a sense of accountability, track record of achievements, and the ability to ask tough questions. Beside, having financial literacy, experience, leadership qualities and the ability to think strategically, the directors must show significant degree of commitment to the company and devote adequate time for meeting, preparation and attendance.[745] The committee is of the view that the nonexecutive directors, that is, those who are independent and those who are not, help bring an independent judgment to bear on board's deliberations especially on issues of strategy, performance, management of conflicts and standards of conduct. The committee[746] therefore lays emphasis on the caliber of the nonexecutive directors, especially of the independent directors.[747]

Under the Nigerian regime, although the Companies and Allied Matters Act (CAMA) does not expressly outline the criteria for board membership, section 257 contains attributes capable of disqualifying a person to be appointed director. The converse therefore will constitute traits to be expected of a director. They include: that he should be mature both in age and mind and must not be less than 18 years of age; he should be of sound mind so as to adequately manage or contribute to the management of the affairs of the company; he should

[744] H.J. Gregory, *op. cit*, p.13.
[745] Securities and Exchange Board of India (SEBI), s. 7.
[746] The committee appointed by SEBI.
[747] *Ibid*., s. 6(6).

have integrity and must not be a fraudulent person[748]; he must not be insolvent[749] so that he may not be tempted to misappropriate the funds of the company for his personal interest; and he must also have the requisite experience and capable of exercising the skill that his position demands.[750]

Separation of Chairman and CEO

In UK, given the importance and particular nature of the chairman's role, the office of the chairman of a company should in principle be separated from that of the chief executive officer.[751]There should be a clearly accepted division of responsibilities at the head of a company which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision.[752]

The same position is obtainable under the combined code wherein it is stated that there should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered power of decision.[753]The role of chairman and chief executive should not be exercised by the same individual. The division of responsibilities between the chairman and CEO should be clearly established, set out in written and agreed by the board.[754]

[748] Section 254 CAMA
[749] Section 253
[750] Section 282
[751] Cadbury Report, s. 4.9.
[752] *Ibid*, s. 1.2.
[753] Combined Code, Main Principle A.2.
[754] Combined Code, Provision A.2.1.

However under the combined code, in exceptional cases where a board decides that a CEO should become chairman, the board should consult major shareholders in advance and should set out to the shareholders its reason at the time of the appointment and in the next annual report.[755]

In the USA, the roles of nonexecutive chairman or board leader have been under consideration for some years under the NACD Report. The purpose of creating these positions is not to add another layer of power but instead to ensure organization of, and accountability for, the way and means the director functions. The board should ensure that someone is charged with: organizing the board's evaluation of the CEO, and providing continuous ongoing feedback; charging executive sessions of the board; setting the agenda with the CEO and leading the board in anticipating and responding to crises. Boards should consider formally designating a nonexecutive chairman or other independent board leader if they should designate, regardless of title, independent members to lead the board in its most critical function. The BRT Report appears more or less to be indifferent as to whether there should be the separation of the chairman and CEO. The report posits that most American corporations have been well served by a structure in which the CEO also serves as chairman of the board. The Chief Executive Officer (CEO) serves as a bridge between management and the board, ensuring that both act with a common purpose. The decision whether the CEO also should serve as chairman of the board often is part of the succession planning processes, and the board should make that decision in the light of the corporation's fact and circumstances. Although no one structure is right for every corporation, it is critical that the board has independent leadership. Some corporations have found it useful to separate the roles of CEO and chairman of the board.

[755] *Ibid*., Provision A 2.2.

Unlike in the United States where the applicable codes are indifferent as to whether there should be the separation of the position of chairman and that of CEO, in India, the Committee is of the view that the chairman's role should in principle be different from that of the chief executive officer, though the same individual may perform both roles.[756]

In Nigeria, the position appears to be what is applicable in India. There is separation of the role and powers of the CEO[757] from that of the Chairman. For instance, the managing director pursuant to Section 64, CAMA may exercise any or all the powers of the Board but the chairman cannot do so. The chairman's role is most evident during the proceeding of the directors. The same person however can occupy both positions.[758]

Mix of Executive, non-Executive and Independent Directors

It is strongly advocated in the UK that the board should include non-executive directors of sufficient caliber and number for their views to carry significant weight in the board's decisions.[759]Non-executive directors should bring an independent judgment to bear on issues of strategy, performance, resources, including key appointments and standards of conduct.[760] Every public company should be headed by an effective board which can both lead and control the business. This means a board made up of a combination of executive directors, with their intimate knowledge of the business, and of outside, non-executive directors, who can bring a broader view to the company's activities, under a chairman who accepts the duties and responsibilities which the post entails.[761]Still under the Combined Code, the board should include a balance of executive and non-executive directors (and in particular independent non-executive directors) such that no individual or small group of individuals

[756] Securities and Exchange Board of India (SEBI), s. 8.1.
[757] In Nigeria, the terminology Managing Director is used to refer to the CEO
[758] Companies and Allied Matters Act, s. 64.
[759] The Combined Code, S. 1(3) (Cadbury Report).
[760] The Combined Code, s. 2.1
[761] Cadbury Report, s. 4.1.

can dominate the board's decision taking.[762] To ensure that power and information are not concentrated in one or two individuals, there should be a strong presence on the board of both executive and non-executive directors.[763]Except for smaller companies, at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent. A smaller company should have at least two independent non-executive directors.[764]

In the US, on the other hand, under the NACD Report, it is provided that the Boards should require that independent directors fill the substantial majority of board seats. Boards should ensure that any director candidate under consideration, with the exception of their own CEO or senior managers is independent.[765] The BRT Principle is more particular in its provision to the effect that a substantial majority of directors of the board of a publicly owned corporation should be independent, both in fact and appearance, as determined by the board. In accordance with the listing standards of the major securities markets, the board should make an affirmative determination as to the independence of each director annually and should have a process in place for making these determinations.[766] The board of a publicly owned corporation should have a substantial degree of independence from management. Board independence depends not only on directors' individual relationships but also on the board's overall attitude toward management. Providing objective independent judgment is at the core of the board's oversight function, and the board's composition should reflect this principle.

The position in India as regards the mix of executive and non executive director is that the committee posits that the board of a company has an optimum combination of executive and non-executive directors with not less than fifty percent of the board comprising the non-

[762] The Combined Code, Main Principle A.3.
[763] The Combined Code, Supporting Principle A. 3.
[764] The Combined Code, Provision A. 3.2.
[765] NACD Report 11.
[766] BRT Principle 14.

executive directors. The number of independent directors would depend on the nature of the chairman of the board. In case a company has a non-executive chairman, at least one-third of board should comprise of independent directors and in case a company has an executive chairman, at least half of board should be independent.[767]

There is not in CAMA any express provision as to the proposition of the mix of executive and non executive director. That notwithstanding, there must be at all times at least two directors.[768] Mostly in practice, the two directors are usually non-executive directors.

Definition of Independence

In the UK, it is agreed that the majority of non-executive directors should be independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgment, apart from their fees and shareholding. Their fees should reflect the time which they commit to the company.[769] This means that apart from their fees and shareholdings, the directors should be independent of management and free from any business or other relationship which could materially interfere with exercise of their independent judgment. It is for the board to decide in particular case whether this definition is met. Information about the relevant interests of directors should be disclosed in the directors' report.[770]

The Combined Code defined the relationships or circumstances relevant to a board's determination of director independence which include whether the director:

i. has been an employee of the company or group within the last five years;

[767] Report of the Committee appointed by SEBI, s. 6.9.
[768] Section 246 CAMA
[769] The Combined Code, s. 2.2.
[770] Cadbury Report, s. 4.12.

ii. has, or had within the last three years, a material business relationship with the company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company;

iii. has received or receives additional remuneration from the company apart from a director's fee, participates in the company's related pay scheme, or is a member of the company's pension scheme;

iv. has close family ties with any of the company's advisers, directors or senior employees;

v. holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;

vi. represent a significant shareholder, or

vii. has served on the board for more than nine years from the date of their first election.[771]

Notably, serving more than nine years could be relevant to the determination of a non-executive director's independence.[772] Also, holding of share options could be relevant to the determination of a non-executive director's independence.[773]

In the US and under the NACD Report, the **r**elationships that may compromise a director's independence include but are not limited to: reciprocal directorships or 'director interlock'; an existing significant consulting or employment relationship; an existing substantial commercial relationship between the director's organization and the board's company: or new business relationships that develop through board membership.[774] In order to ensure board independence, the Committee recommends as follows:

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[771] Combined Code, Provision A. 3.1.
[772] *Ibid*, Provision A. 7.2.
[773] *Ibid*., Provision B. 1.3.
[774] NACD Report, Provision 11.

i. Boards should disclose to shareholders a definition of 'independent director'.

ii. Boards should require that director candidate disclose all existing business relationship between them or their employer and the board's company the extent to which, if any, a candidate's other activities may impinge on his or her independence as a board member and determine when relationships are such that a candidate can no longer be considered independent.[775]

In addition and similar to what is obtainable under the NACD Report, the BRT Report advances the view that an independent director should not have any relationships with the corporation or its management – whether business, employment, charitable or personal, that may impair the ability to exercise independent judgment. The listing standards of the major securities market define 'independence' and enumerate specific relationships such as employment with the corporation or its outside auditor that precludes a director from being considered independent. When considering whether a director is independent, the board should consider not only whether the director has any of the relationships covered by the board's independent standards, but also whether the director has any other relationships with the corporation, senior management or other board members that could affect the director's actual or perceived independence. [776]The board's director independence standards should include standards for assessing directors' relationships with not-for-profit organizations that receive support from the corporation. Independence issues are most likely to arise when a director is an employee of the not-for-profit organization and when substantial portion of the organization's funding comes from the corporation.[777]

[775] *Ibid*., Provision 12.
[776] *Ibid*., Provision 4.
[777] *Ibid*., Provision 15.

The definition of independence of directors in Nigeria corporate law jurisprudence can be read into the duties of a director not to fetter his discretion especially while voting or making a decision for the company.[778] This is similar in some respect to the definition in the US and in Indian company law jurisprudence. The director is not expected to engage in any personal business with the members that are of such a nature as to affect the independence of his judgment when such is required.

Conflicts of Interest and Ethics

This is not expressly covered under the UK Cadbury Report, but it is provided that the majority of non-executive directors should be independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgment, apart from their fees and shareholding.[779] In order to safeguard non-executive directors' independent position, we regard it as good practice for non-executive directors not to participate in share option schemes and for their service as non-executive director not to be pensionable by the company.[780] Audit firms are in competition with each other for business to the extent however that audit firms compete on price and on meeting the needs of their clients, and this may be at the expense of meeting the needs of shareholders.[781] Under the UK Combined Code, the board should set the company's values and standards.[782] Where executive directors or senior management are involved in advising or supporting the remuneration committee, care should be taken to recognize and avoid conflicts.[783] The audit committee should review arrangements by which staff of the company may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters. The audit committee's objective should be to ensure that arrangements are in place for the

[778] Companies and Allied Matters Act, Cap. C20, L.F.N., s. 279(6).
[779] Combined Code, s. 2.2.
[780] Cadbury Report, s. 4.13.
[781] *Ibid*., s. J.3c
[782] UK Combined Code, Supporting Principle A.1.
[783] *Ibid*., Supporting Principle B.2.

proportionate and independent investigation of such matters and for appropriate follow-up action.[784]

In the USA, the NACD Report does not expressly provide for conflict of interest and ethics. It provides that the Board should require that director candidates disclose all existing interests or their employer and the board's company. Boards should then evaluate the extent to which, if any, a candidate's other activities may impinge on his or her independence as a board member, and determine when relationships are such that a candidate can no longer be considered independent.[785]The board should seek disclosure of any relationships that would appear to compromise director's independence.[786] The BRT Principle provides that management and directors should never put personal interest ahead of or in conflict with the interest of the corporation.[787] It is the responsibility of the CEO and senior management, under the CEO's direction, to operate the corporation in an effective and ethical manner.[788] Business roundtable believes that corporation should have a CEO of integrity who takes responsibility for the corporation, adhering to the highest ethical standards. A strong, ethical 'tone at the top' set by the CEO and senior management that establishes a culture of legal compliance and integrity communicated to personnel at all level of the corporation require an effective compliance program. Senior management should take responsibility for implementing and managing an effective compliance program relating to legal and ethical conduct. As part of its compliance program, a corporation should have a code of conduct with effective reporting and enforcement mechanisms. Employees should have a means of seeking guidance and alerting management and the board about potential or actual misconduct

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[784] *Ibid*., Provision C.3.4.
[785] NACD Report, Provision 12.
[786] *Ibid*., Provision 22. See also NACD, Corporate Director's Ethics and Compliance Handbook (2003).
[787] BRT Principle 2.
[788] *Ibid*., Principle 10.

without fear of retribution, and violation of the code should be addressed promptly and effectively.[789]

In India, non-executive directors help to bring an independent judgment to bear on management of conflicts.[790] There is another set of directors in Indian companies who are the nominees of the financial or investment institution to safeguard their interest i.e. the interest of nominee directors. Those who oppose this practice argue that there is an inherent conflict. The committee would therefore recommend that institution should appoint nominees on the board of companies only on a selective basis.[791] The policy on director remuneration should avoid potential conflicts of interest between the shareholders, and the management.[792]The committee recommends that to avoid conflict of interest, the remuneration committee should comprise at least three directors, all of whom should be non-executive directors, the chairman of committee being an independent director.[793] The committee recommends that disclosures must be made by the management to the board relating to all material financial and commercial transactions, where they have personal interest, that may have a potential conflict with the interests of the company at large (e.g., dealing in company shares, commercial dealings with bodies which have shareholdings of management and their relatives, etc).[794]

In Nigeria, there is the duty on the part of the directors not to engage in any activity that may engender any conflict between his duties and his personal interest. The Companies and Allied Matters Act (CAMA) is explicit as regards this duty. The acts that constitute conflict of

[789] *Ibid*., Principle 12.
[790] Securities and Exchange Board of India (SEBI), s. 6.6.
[791] *Ibid*., ss. 7.1-7.3.
[792] *Ibid*., s. 10.1.
[793] *Ibid*., s. 10.4.
[794] *Ibid*., s. 13.5.

interest are contained in the same section although arguably the section cannot be said to be exhaustive of such acts.[795]

Election Terms, Term Limits and Mandatory Retirements

In UK, the Cadbury Report provides that non-executive directors should be appointed for specified terms and reappointment should not be automatic.[796] Executive directors' service contracts should not exceed three years without shareholders' approval.[797]Companies have to be able to bring about changes in the composition of their boards to maintain their vitality. Nonexecutive directors may lose something of their independent edge if they remain on a board too long. Furthermore, the make-up of a board needs to change in line with new challenges. We recommend, therefore, that nonexecutive directors should set out their duties, and terms. Their letter of appointment should set out their duties, term of office, remuneration and its review. Reappointment should not be automatic, but by a conscious decision by board and the director concerned.[798] Still in the UK but under the Combined Code, all directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance. The board should ensure planned and progressive refreshing of the board.[799]All directors should be subject to election by shareholders at the first annual general meeting after their appointment, and to re-election thereafter at interval of not more than three years.[800]Nonexecutive directors should be appointed for specified terms subject to re-election and to the provisions of the Companies Acts relating to the removal of a director. Any term beyond six years (e.g., two three year terms) for a nonexecutive director should be subject to particularly rigorous review, and should take into account the need for progressive directors to serve longer than nine years (e.g., three three-year terms), subject to annual re-election.

[795] Companies and Allied Matters Act, Cap. C20 LFN 2010, ss. 280 and 287.
[796] Cadbury Report, s. 2.3.
[797] Cadbury Report, s. 3.1.
[798] Cadbury Report, s. 4.16.
[799] Combined Code, Main Principle A.7.
[800] Combined Code, Provision A.7.1)

Serving more than nine years could be relevant to the determination of a nonexecutive director's independence. [801]The provision of B.1.6 is to the effect that the notice or contract periods should be set at one year or less.[802] If it is necessary to offer longer notice or contract periods to new directors recruited from outside, such periods should be reduced to one year or less after the initial period.

As advocated under the NACD Report in the US, until processes are established for a strong individual director evaluation process, boards should recognize when certain predetermined criteria are met for example 10 to 15 years of service or a specified retirement age. It may be desirable to promote director turnover to obtain the fresh ideas and critical thinking that a new director can bring to the board. However, for the sake of continuity some directors' tenures should survive that of the CEO. Unless boards have a process to evaluate the performance of individual directors, they should establish tenure conditions under which, as a matter of course, directors should submit a resignation for consideration or offer to withdraw from consideration for re-nomination.

According to the BRT Principle, the board should establish procedure for the retirement and replacement of board members. These procedures may, for example, include a mandatory retirement age, a term limit and/or a requirement that directors who change their primary employment tender a board resignation, providing an opportunity for the governance committee to consider the desirability of their continued service on the board. Planning for the departure of directors and the designation of new board members is essential. The board should plan ahead for changes in membership, and it should have written criteria for director candidates that should be re-evaluated periodically. [803]

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[801] Combined Code, Provision A.7.2.
[802] *Ibid*., B. 1,6.
[803] BRT Principle 29.

In India, the tenure of office of the directors will be as prescribed in the Indian Companies Act.[804]

Similar position holds sway in Nigeria where the Companies and Allied Matters Act provides conclusively for the appointment, term of office, remuneration and retirement of directors.[805]

Director Compensation and Stock Ownership

Although not covered directly by Cadbury Report, however, the code $ 3.2 provides that there should be full and clear disclosure of directors' total emoluments and those of the chairman and highest-paid UK director, including pension contributions and stock options. Separate figures should be given for salary and performance related elements, and the basis on which performance is measured should be explained.[806] The Combined Code prescribes that levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose.[807] Essentially, no director should be involved in deciding his or her own remuneration.[808]

Level of remuneration for non-executive directors should reflect the time commitment and responsibilities or the role. Remuneration for non-executive directors should not include share options. If share options are granted, shareholders' approval should be sought, and any share acquired by exercise of the options should be held until at least one year after the non-executive director leaves the board.[809] The board itself or, where acquiesced by the articles of association, the shareholders should determine the remuneration of the non-executive directors. Where permitted, the board may delegate this responsibility to committee, which

[804] Indian Companies Act, s. 6(10).
[805] Companies and Allied Matters Act (CAMA), Cap. C20, LFN 2010, ss. 247,248 and 259.
[806] Combined Code, s. 3.2.
[807] Combined Code, Main Principle B.1.
[808] *Ibid*., Main Principle B.2.
[809] Combined Code, Provision B. 1.3.

might include the Chief Executive.[810] Shareholders should be invited specifically to approve all new long-term incentive schemes as defined in the listing rules and significant changes to existing schemes, save in the circumstances permitted by the listing rule.[811] The design of performance related remuneration is provided in schedule A.[812]

There is consensus of opinion that a significant ownership stake leads to a stronger alignment of interest between directors and shareholders increasingly, and compensation programs for directors and senior management are emphasizing stock over benefits

The report of the NACD Blue Ribbon Commission on Director Compensation, issued in 1995, recommended the following best practices with respect to director compensation:

i. Boards should establish a process by which directors can determine the compensation program in a deliberative and objective way.
ii. Boards should set a substantial target for stock ownership by each director and a time period during which this target is to be met.
iii. Boards should define the desirable total value for all forms of director compensation.
iv. Boards should pay directors solely in the form of equity and cash with equity representing a substantial part of the total up to 100 percent; boards should dismantle exit profit programs and avoid creating new ones.
v. Boards should disclose fully in the proxy statement the philosophy and process used to determine director compensation and the value of all element of compensation.[813]

Just as the position held under the NACD report, the BRT principles assert that**,** directors should receive incentive to focus on long-term stockholder value. Including equity as part of directors' compensation helps to align the interests of directors with those of the

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[810] *Ibid*, Provision B. 2.3.
[811] *Ibid*, Provision B. 2.4.
[812] *Ibid*., Combined Code, Provision 23.
[813] *Ibid*., Provision 7.

corporation's shareholders. Accordingly, a meaningful portion of a director's compensation should be in the form of long-term equity. In this regard, corporations increasingly are providing the long-term equity component of directors' compensation in the form of restricted stock rather than stock options, to better align directors' interests with those of shareholders. Corporations should establish a requirement that directors acquire a meaningful amount of the corporation's stock.[814]

The Indian position as to Directors' compensation and stock ownership tally with those of the jurisdictions above mentioned to the effect that it is recognized that it is important that adequate compensation package be given to the non-executive independent directors so that these positions become sufficiently financially attractive to attract talent and that the non-executive directors are sufficiently compensated for undertaking this work.[815]

The committee recommends that the board of directors should decide the remuneration of non-executive directors.[816]

In Nigeria on the other hand, there is no provision in CAMA directing that directors should be remunerated although this can be agreed by the company. Where such remuneration has been fixed, it accrue from day to day and not necessarily proportionate to the work done by them. Expenses incurred by the directors in pursuance of the activities of the company are borne by the company.[817]

Evaluating Board performance

Cadbury Report is silent on the issue of evaluating board performance. However under the Combined Code, the board should undertake a formal and rigorous annual evaluation of its

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[814] *Ibid*., Provision 25.
[815] Securities and Exchange Board of India (SEBI) Report, s. 6.7.
[816] *Ibid*., s. 10.7.
[817] Companies and Allied Matters Act (CAMA), s. 267.

own performance and that of its committees and individual directors.[818] Individual evaluation should aim at showing whether each director continues to contribute effectively and to demonstrate commitment to the role. The chairman should act on the result of the performance evaluation by recognizing the strength and addressing the weaknesses of the board and, where appropriate, proposing new members to be appointed to the board or seeking the resignation of directors.[819] The board should state in the annual report how performance evaluation of the board, its committee and its individual directors has been conducted. The non-executive directors, led by the senior prudent director, should be responsible for performance evaluation of the chairman, taking into account the views of executive directors.[820]

The chairman should confirm to shareholders when proposing re-election that following formal performance evaluation, the individual's performance continues to be effective and to demonstrate commitment to the role.[821]

The non-executive directors, led by the senior independent director, should meet without the chairman present at least annually to appraise the chairman's performance.[822] In the USA, the NACD Report contemplates three separate aspects to effective evaluation at the board level each of which constitutes a critical component of board professionalism and effectiveness. CEO evaluation, board evaluation, and individual director evaluation, all three of these evaluations should be addressed vis-à-vis pre-establishment. Accordingly, the NACD posits as follows:

[818] Combined Code, Main Principle A.6.
[819] Combined Code, Supporting Principle A. 6.
[820] *Ibid*., Provision A.6.1.
[821] *Ibid*., Provision A.7.2.
[822] *Ibid*., A.1.3.

i. The performance of the full criteria to provide the CEO, the board as a whole, and each director with critical information pertaining to their collective and individual performance and area that can be improved.

ii. Boards should ensure that independent directors create and control the methods and criteria for evaluating the CEO, the board, and individual directors. Such an evaluation practice will enable boards to identify and address problems before they reach crisis proportions.[823] Creating a board of self-assessment methodology constitutes board evaluation practicalities.[824]

The BRT principles corroborated the above position by positing that the board should have an effective mechanism of evaluating performance on a continuing basis. Meaningful board evaluation requires an assessment of the effectiveness of the full board, the operation of board committees and the contribution of individual directors. Board should be evaluated annually, as should the performance of its committees. The board should use the annual self-evaluation to assess whether it is following the procedures necessary to function effectively. Each board committee should conduct an annual self evaluation to access its effectiveness, and the results of this evaluation should be reported to the full board. Essentially, the board should have a process of evaluating whether the individuals sitting on the board bring the skills and expertise appropriate for the corporation and how they work as a group. Positions should not be regarded as permanent. Directors should serve only as long as they add value to the board, and a director’s ability to continue to contribute to the board should be examined by the corporate governance committee each time the director is considered for re-nomination.

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[823] *Ibid*., Provision 7.

[824] *Ibid*., Appendices Di and D2; Report of the NACD Blue Ribbon Commission on Performance Evaluation of Chief Executive Officers, Boards, and Directors (1994).

In India, there is no express provision requiring the evaluation of the board, and to that effect, the committee is however of the view that the institutional shareholders should:

i. Take active interest in the composition of the Board of Directors
ii. Be vigilant.
iii. Maintain regular and systematic contact at senior level for exchange of views on management strategy, performance and the quality of management.
iv. Ensure that voting intentions are translated into practice.
v. Evaluate the corporate governance performance of the company.[825]

There is also no express provision for director evaluation under the Nigeria corporate law jurisprudence. It is therefore recommended that the UK approach be adopted.

Board Interaction / Communication with Shareholders, Press and Customers

The issue of board interaction with the shareholders is not covered directly under the Cadbury Report. However, it is provided that the institutional investors should encourage regular systematic contact at senior executive level to exchange views and information on strategy, performance, board membership and quality of management.[826]The Combined Code states expressly that there should be a dialogue with shareholders based on the mutual understanding of objectives. The board as whole has responsibility for ensuring that a satisfactory dialogue with shareholders takes place.[827]

Whilst recognizing that most shareholders contact is with the chief executive and finance director, the chairman, the senior independent director and other directors as appropriate, should maintain sufficient contact with major shareholders to understand their issues and

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[825] BRT, Principles 14(16).
[826] Cadbury Report, ss. $ 6.1-6.16.
[827] Combined Code, Main Principle D.I.

concerns.[828] The chairman should ensure that the views of shareholders are communicated to the board as a whole. Non-executive directors should be offered the opportunity to attend meetings with major shareholders.[829]Institutional shareholders should enter into a dialogue with companies based on the mutual understanding of objectives.[830] Also, when evaluating companies' governance arrangements, particularly those relating to board structure and composition, institutional shareholders should give due weight to all relevant factors drawn to their attention.[831]

In the USA, the NACD Report is totally silent on the issue of board interaction with the shareholders. The BRT principle is express when it provided that it is the responsibility of the board to respond appropriately to shareholders' concerns. Additionally, corporations have a responsibility to communicate effectively and candidly with shareholder. The goal of shareholder communications should be to help shareholders undertake the business, risk profile, financial condition and operating performance of the corporation and the board's corporate governance practices. Companies should have effective procedures for shareholders to communicate with the board and for directors to respond to shareholders' concern. The board, or an independent committee e.g. corporate governance committee, should establish a regular procedure; oversee or review and update these procedures as appropriate. All of these communications should provide consistency, clarity and candor.[832]

Under the Indian company law jurisprudence, the issue of board interaction/communication with shareholders, press, customers, etc. is not covered directly in the SEBI report. The report however, states that the committee is of the view that the institutional shareholders should:

i. Take active interest in the composition of the board of directors.

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[828] Combined Code, Supporting Principle D.1
[829] *Ibid*., Provision D.1.1.
[830] Ibid., Main Principle E.1.
[831] Ibid., Main Principle E.2.
[832] See the business roundtable (BRT), Guidelines for Shareholder Director Communications (May 2005).

ii. Be Vigilant.
iii. Maintain regular and systematic contact at senior level for exchange of views on management strategy, performance and the quality of management.
iv. Ensure that voting intentions are translated into practice.
v. Evaluate the corporate governance performance of the company.[833]

In Nigeria, there is no clear-cut procedure on the evaluation of board interaction with shareholders. It is therefore recommended that the procedure in UK, USA and India should be adopted.

Board Meetings and Agenda

It is provided under the Cadbury Report that the board should meet regularly.[834] The board should have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the company is firmly in its hands.[835] The Combined Code restates the above position when it stated that there should be a meeting of the board regularly to discharge its duties effectively. There should also be a schedule of matters specifically reserved for its decision. The annual report should include a statement of how the board operates, including high level statement of which types of decisions are to be taken by the board and which are to be delegated to management.[836]The chairman is responsible for leadership of the board, ensuring its effectiveness on all aspects of its role and setting its agenda. The chairman should also facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.[837]

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[833] SEBI Report, s. 14(16).
[834] Cadbury Report, Code s.1.1.
[835] *Ibid*., s. 1.4.
[836] Combined Code, Provision A.1.1.
[837] *Ibid*., Supporting Principle A.2.

The US NACD Report considers the Board and committee meetings as the settings in which most of the directors' decisions are made. Therefore, developing the agenda for such meetings is a critical element in determining and reinforcing board independence and effectiveness. Accordingly, the Report posits as follows:

i. Boards should ensure that members are actively involved with their CEO in setting the agendas for full board meetings. A designated director or directors should work with the CEO to create board agenda.

ii. For committee meetings, committee chairs should work with the CEO and committee members to create agendas, and incorporate other members' input as provided.

The BRT Principles provides further that when arranging a meeting schedule for the board, each company should consider the nature and complexity of its operations and transactions, as well as its business and regulatory environment. The board's agenda must be carefully planned, yet flexible enough to accommodate emergencies and unexpected developments. The chairman of the board should work with the lead director (if any) in setting the agenda and should be responsive to individual directors' requests to add items to the agenda and open to suggestions for improving the agenda. The agenda and meeting schedule should permit time for discussion and striking compromise between the board members and management. The CEO and senior management generally take the lead in strategic planning. With the overall strategic plans in mind, senior management develops annual operating plans and annual budgets for the corporation and present some to the board for review and approval, and once approved, the management team implements them.

In India, the committee recommends that board meetings should be held at least four times in a year, with a maximum time gap of four months between any two meetings.[838]

In Nigeria, there is no number of times that directors are required to meet in any financial year although they are required to meet not later than six months after the incorporation of the company. A meeting of the board may be summoned at any time by a director or the secretary on the requisition of a director.[839]

Number, Structure and Independence of Committee

In the UK, the Cadbury Report provides that the board should establish an audit committee of at least three (3) non-executive directors with written terms of reference which deal clearly with its authority and duties. A nomination of committee should have a majority of non-executive directors on it and be chaired by either chairman or a non-executive director.[840]Membership of the audit committee should be confined on the non-executive directors of the company, and a majority of the non-executives serving on the committee should be independent.[841]Board should appoint remuneration committees consisting wholly or mainly non-executive directors, to recommend to the board the remuneration of the executive directors in all its forms as necessary.[842]

Under the Combined code, there should be a nomination committee which should lead the process for board appointments and make recommendation to the board. A majority of members of the nomination committee should be independent non-executive directors. The chairman or an independent non-executive director should chair the committee, but the chairman should not chair the nomination committee when it is dealing with the appointment

[838] SEBI Report, s. 11.2.
[839] Companies and Allied Matters Act, *op. cit*., s. 263.
[840] Cadbury Report, Code s. 4.30.
[841] *Ibid*., Code s. 4.35 (b).
[842] *Ibid*., Code s. 4.42.

of a successor to the chairmanship position.[843] The board should establish a remuneration committee of at least three (3), or in the case of smaller companies two (2), members, who should all be independent non-executive directors. In addition, the company chairman may also be a member of, but not chair, the committee if he or she was considered independent on appointment as chairman.[844] The board should establish an audit committee of at least three (3), or in the case of smaller companies two (2), independent non-executive directors. In smaller companies the company chairman may be a member of, but not chair, the committee in addition to the independent non-executive directors, provided he or she was considered independent on appointment as chairman. The board should satisfy itself that at least one (1) member of the audit committee has recent and relevant financial experience.[845] No one other than the committee chairman and members is entitled to be present at a meeting of the nomination, audit or remuneration committee, but others may attend at the invitation of the committee.

In the USA, the position under the NACD Report is not totally different from that in the UK. The report provides that the boards should require that key committee – compensation, audit, and nominating or governance – should include only independent directors. Boards should establish guidelines for, and discuss with some predefined frequency, the number of committee as well as the size and structure of committees.

The BRT Principle specifically provides that every publicly-owned corporation should have an audit committee of at least three members who should all be independent directors. Every publicly-owned corporation should have a committee composed solely of independent directors that addresses director nominations and corporate governance matters. It should have at least three (3) members. Every publicly-owned corporation should have a committee

[843] Combined Code, Provision A.4.1.
[844] *Ibid*., Provision B.2.1.
[845] *Ibid*., Provision 3.1. and Supporting Principle A.3.

composed solely of independent directors that addresses compensation issues. Additional committees, such as finance or risk management committees, also may be used. Some corporations find it useful to establish committees in greater depth than would otherwise be feasible. It is the responsibility of the board, through its corporate governance committee to oversee the structure of the board and its committees. Business Roundtable believes that the functions generally performed by the audit, compensation and corporate governance committees are central to effective corporate governance but does not believe that a particular committee structure is essential for all corporations. What is important is that key issues are addressed effectively by the independent members of the board. Virtually all boards of directors of large, publicly-owned corporations operate using committees to assist them. A committee structure permits the board to address key areas in more depth than may be possible in a full board meeting.

In India, on the number, structure and independence of committees, the committee recommends that a qualified and independent audit committee should be set up by the board of a company.[846] The composition of the audit committee is based on the fundamental premise of independence and expertise. The committee therefore recommends that the audit committee should have a minimum of three (3) members, all being non-executive directors, with the majority being independent, and with at least one director having financial and accounting knowledge; and the chairman of the committee should be an independent director.[847]The committee recommends that the board should set up a remuneration committee.[848]The remuneration committee should comprise at least three (3) directors, all of whom should be non-executive directors, the chairman of the committee being an

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[846] Securities and Exchange Board of India (SEBI) Report, s. 9.4.
[847] *Ibid*., s. 9.6.
[848] *Ibid*., s. 10.2.

independent director.[849]The committee recommends that a board committee under the chairmanship of a non-executive director should be formed to specifically look into the redressing of shareholder complaints like transfer of shares, non receipt of balance sheet, non receipt of declared dividends, etc.[850] The board should delegate the power of share transfer to an officer, or a committee or to the registrar and share transfer agent.[851]

Formal Evaluation of the Chief Executive Officer (CEO)

The issue of formal evaluation of the CEO is not covered directly. However, non-executive directors make important contributions in reviewing the performance of the board and of the CEO.[852] As is more expressly provided for in the Combined Code, the board should review management performance. Non-executive directors should scrutinize the performance of management in meeting agreed goal and objectives and monitor the reporting of performance. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They are responsible for determining appropriate levels of remuneration of executive directors and have prime role in appointing, and where necessary removing, executive directors.[853]

In the USA on the other hand, as contained in the NACD Report, it is accepted that there are three (3) separate aspects for effective evaluation at the board level, each of which constitutes a critical component of board professionalism and effectiveness: CEO evaluation, board evaluation, and individual director evaluation. All three of these evaluations should be assessed *vis-a-vis* pre-established criteria to provide the CEO, the board as a whole, and each director with critical information pertaining to their collective and individual performance and areas that can be improved. The NACD Report specifically posits as follows:

[849] *Ibid*., s. 10.4.
[850] *Ibid*., s. 14.13.
[851] *Ibid*.
[852] Cadbury Report, ss. 4.4-4.5.
[853] Combined Code, Supporting Principle A.1.

i. Boards should regularly and formally evaluate the CEO, the board as a whole, and individual directors;

ii. Boards should ensure that independent directors create and control the method and criteria for evaluating the CEO, the board, and individual directors. [854]

Under the BRT Principle, Making decisions regarding the selection, compensation and evaluation of a well-qualified and ethical CEO is the single most important function of the board. Under the oversight of an independent committee or the lead director, the board should annually review the performance of the CEO, and participate with the CEO in the evaluation of members of senior management. All non management members of the board should participate with the CEO in senior management evaluations. The results of the CEO's evaluation should be promptly communicated to the CEO in executive session by representatives of the independent directors and used by the compensation committee or board in determining the CEO's compensation.

In India, requirement for the formal evaluation of CEO is not covered directly, but the SEBI Report provides that the committee believes that the management should carry out the following functions:

i. Assisting the board in its decision-making process in respect of the company's strategy, policies, code of conduct and performance targets, by providing necessary inputs, and implementing the policies and code of conduct of the board.

ii. Managing the day-to-day affairs of the company to best achieve the targets and goals set by the board, to maximize the shareholder value.

iii. Providing timely, accurate, substantive and material information, including financial matters and exceptions, on the board, board committees and the shareholder.

[854] see also the report of the NACD Blue Ribbon Commission on performance evaluation of chief executive officers, boards and directors (1994).

iv. Ensuring compliance of all regulations and laws.

v. Ensuring timely and efficient service to the shareholders and to protect shareholder's right and interest.

vi. Setting up and implementing an effective internal control system commensurate with the business requirements.

vii. Implementing and complying with the code of conduct as laid down by the board, and cooperating and facilitating efficient working of board committees.[855]

The committee is of the view that the institutional shareholders maintain regular and systematic contact at senior level for exchange of view on management strategy, performance and the quality of management.[856]

In Nigeria, there is no formal examination of the managing director, which is akin to the position of a Chief Executive Officer (CEO). Therefore, the position in UK, USA and India is recommended to ensure effective corporate governance.

Executive Compensation and Stock Ownership

The UK Cadbury Report on compensation and stock ownership of executive provide that executive directors' service contracts should not exceed three (3) years without shareholder's approval, and their pay should be subject to the recommendations of a remuneration committee made up wholly or mainly of non-executive directors[857] It is also recommended that boards should appoint remuneration committees consisting wholly or mainly of non-executive directors, to recommend to the board the remuneration of the executive directors in all its forms, drawing on outside advice as necessary.[858] Under the Combined Code, levels of remuneration should be sufficient to attract, retain and motivate directors of the quality

[855] SEBI Report, s. 13.3.
[856] *Ibid*., s. 14.16.
[857] Cadbury Report, ss. 3.1-3.3.
[858] *Ibid*., s. 4.42.

required to run the company successfully, but a company should avoid paying more than is necessary for this purpose. A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance.[859]There should be a formal and transparent procedure for developing policy on executive remuneration.[860]The performance-related elements of remuneration should form a significant proportion of the total remuneration package of executive directors and should be designed to align their interests with those of shareholders and to give these directors keen incentives to perform at the highest levels. In designing schemes of performance-related remuneration, the remuneration schedule A to this code should be adopted *mutatis mutandi*.[861] Executive share options should not be offered at discount save as permitted by the relevant provisions of the listing rule.[862]Shareholders should be invited specifically to approve all new long-term incentive schemes as defined in the listing rules and significant changes to existing schemes save in the circumstances permitted by the listing rules.[863]

In the USA, it is considered under the NACD Report that creating an independent and inclusive process for remunerating the CEO will ensure board accountability to shareholders and reinforce perceptions of fairness and trust between and among management and board members. Boards should involve all directors in all stages of the CEO selection and compensation process. A significant ownership stake leads to a stronger alignment of interests between directors and shareholders. Increasingly, compensation programs for directors and senior management are emphasizing stock over benefits.[864]Still in the USA under the BRT principle, it is the responsibility of the board, through its compensation

[859] Combined Code, Main Principle B.1.
[860] *Ibid*., Main Principle B.2.
[861] *Ibid*., Provision B.1.
[862] *Ibid*., Provision B.12.
[863] *Ibid*., Provision 2.4.; See also schedule A on the design of performance related remuneration.
[864] See the Report of the NACD Blue Ribbon Commission on Executive Compensation and the Role of the Compensation Committee (2003).

committee, to adopt and oversee the implementation of compensation policies, establish goals for performance – based compensation, and determine the compensation of the CEO senior management. The compensation committee should require senior management to build and maintain significant continuing equity investment in the corporation. The committee also should consider whether to require senior management to hold for a period of time a specified amount of stock earned. Through incentive-based awards, the compensation committee establishes appropriate incentives for management. Executive compensation should directly link the interests of senior management to the long-term interest of shareholders. It should include significant performance-based criteria related to long-term shareholder value and should reflect upside potential and downside risk. The compensation committee should consider whether the benefits and perquisites provided to senior management are proportional to the contributions made by management.[865]

In India, on executive compensation and stock ownership, the committee recognized that the remuneration package should be good enough to attract and motivate the non-executive directors of the quality required, but not more than necessary for the purpose. The remuneration committee should be in a position to bring about objectivity in determining the remuneration package while striking a balance between the interest of the company and the shareholders.[866]

In Nigeria, the chief executive officer i.e. the managing director is entitled to remuneration to be fixed by the directors.[867]On the issue of share qualification, no share qualification is required of the directors unless same is fixed by the articles of association. When fixed, the directors must comply strictly thereto.[868]It is apposite to submit that share qualification

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[865] The Business Roundtable, Executive Compensation: Principles and Commentary (November 2003).
[866] Securities and Exchange Board of India (SEBI) Report, s. 10.3.
[867] Companies and Allied Matters Act (CAMA), Cap. C20, LFN 2010, s. 268.
[868] *Ibid*., s. 251.

should not be optional and the articles of association should so provide. Share qualification should be mandatory to align the director's interests with those of the shareholders.

Corporate Governance Guidelines

The UK Cadbury Report recommend that listed companies should state in the report and accounts whether they comply with the code, identifying and giving reasons for any areas of non compliance.[869]It is envisaged, however, that many companies will wish to go beyond the strict terms of the London Stock Exchange rule and make a general statement about the corporate governance of their enterprises, as some leading companies have already done. The committee welcomes such statements and leaves it to boards to decide the terms in which they make their statements of compliance.[870]Companies must state whether or not they comply with the remuneration committees and policy sections of the Cadbury report.[871]

Under the Combined Code however, the annual report should identify the chairman, the deputy chairman (where there is one), the chief executive, the senior independent director and the chairman and members of the nomination, audit and remuneration committee. It should also set out the number of meetings of the board and those committees and individual attendance by directors.[872] The board should identify in the annual report each non-executive director it considers to be independent.[873] A nomination committee should make available its terms of reference, explaining its role and authority.[874] Terms and conditions of appointment of non-executive directors should be made available.[875]A separate section of the annual report should describe the work of the nomination committee, including the process it has used in

[869] Cadbury Report, s. 3.7.
[870] *Ibid*., s. 3.8.
[871] London Stock Exchange Listing Rule 12.43 (w) and (x).
[872] Combined Code, Provision A.1.2.
[873] *Ibid*., Provision A.3.1.
[874] *Ibid*., Provision A.4.1.
[875] *Ibid*., Provision A.4.4.

relation to board appointments.[876]The board should state in the annual report how performance evaluation of the board, its committees and its individual directors, has been conducted.[877] A remuneration committee should make available its terms of reference, explaining its role and authority.[878] Terms of reference of the audit committee, including its role and authority should be made available. A separate section of the annual report should describe the work of the committee.[879]There is also disclosure of corporate governance arrangement.[880]

In the USA NACD Report, boards should establish guidelines for committees to ensure board independence. Boards should define and disclose to shareholders a definition of 'independent director'. Shareholders' understanding of board and director assessment processes and criteria is indispensable to both board credibility and shareholders' ability to appraise the board's recommended resolutions and proposed state of directors. Boards should disclose evaluation procedures to shareholder in the proxy statement or other shareholder communication. Board disclosure of procedures is distinct from sharing the substance of such deliberations which should be confidential. The board should seek disclosure of any relationships that would appear to compromise director independence.

The BRT principle recommends that the corporate governance committee should develop and recommend to the board a set of corporate governance principles, review them annually, and recommend changes to the board as appropriate. The corporation's corporate governance principles should be publicly available and should address at a minimum, board leadership, qualification for directors, including independence standards, director responsibilities, and the structure and functioning of board committee, board access to management and advisers,

[876] *Ibid*., Provision A.4.6.
[877] *Ibid*., Provision A.6.1.
[878] *Ibid*., Provision B.2.1.
[879] *Ibid*., Provision C.3.3.
[880] See Schedule C of the Combined Code.

director compensation, director orientation and continuing education, board evaluations and management succession.

A corporation's procedures for shareholder communications and its governance practices should be readily available to shareholders. Information about the board, structure and operations, committee composition and responsibilities, corporate governance principles and codes of ethics should be widely disseminated to shareholders. Effective corporate governance requires a proactive, focused state of mind on the part of directors, the CEO and senior management, all of whom must be committed to business success through the maintenance of the highest standards of responsibility and ethics. Even the most thoughtful and well drafted policies and procedures are destined to fail if directors and management are not committed to enforcing them in practice.

On the Indian corporate governance guideline, the committee recommends that there should be a separate section on corporate governance in the annual report of companies, with a detailed compliance report on corporate governance. Non compliance of any mandatory recommendation with reasons thereof and the extent to which the non mandatory recommendations have been adopted should be specifically highlighted. This will enable the shareholders and the securities market to assess for themselves the standards of corporate governance followed by a company.[881] The committee also recommends that the company should arrange to obtain a certificate from the auditors of the company regarding compliance of mandatory recommendations and annex the certificate with the directors' report, which is sent annually to all the shareholders of the company. The same certificate should also be sent to the stock exchanges along with the annual returns filed by the company.[882]In Nigeria, the

[881] Securities and Exchange Board of India (SEBI) Report, s. 15.6. Note that a suggested list of items to be included in the compliance report is enclosed in Annexure 4.
[882] $15.7

board of directors are required to submit annual reports, but not specifically required to include compliance report on the company guidelines.

Internal Control System

In the UK and under the Cadbury Report, directors are responsible for maintaining adequate accounting records.[883] To meet these responsibilities, directors need a system of internal control over the financial management of the company, including procedures designed to minimize the risk of fraud. There is, therefore, already an implicit requirement on directors to ensure that a proper system of internal control is in place.[884]Directors should make a statement in the report and accounts on the effectiveness of their system of internal control and that the auditors should report thereon.[885] Where an internal audit function exists, the audit committee should ensure that it is adequately resourced and has appropriate standing within company.[886] An effective internal control system is an essential part of the efficient management of a company. A great deal of detailed work is now necessary to develop those proposals, and we recommend that the accounting profession take the lead.[887]Under the Combined Code, the board should maintain a sound system of internal control to safeguard shareholders' investment and the company's assets.[888]The board should establish formal and transparent arrangements for considering how they should apply the financial reporting and internal control principles and for maintaining an appropriate relationship with the company's auditors. The board should, at least annually, conduct a review of the effectiveness of the group's system of internal controls and should report to shareholders that they have done so. The review should cover all material controls, including financial, operational and

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[883] UK Companies Act 1985, s. 221.
[884] Cadbury Report, s. 4.3.1.
[885] *Ibid*., s. 4.32.
[886] *Ibid*., s. 4.35(f).
[887] Ibid., s. 5.16.
[888] Combined Code, Main Principle C.3.5.

compliance controls and risk management systems.[889] The audit committee should monitor and review the effectiveness of the internal audit function, the audit committee should consider annually whether there is a need for an internal audit function and make a recommendation to the board and the reasons for the absence of such function should be explained in the relevant section of the annual report.[890]

In the USA NACD Report, among the most important mission of the board is ensuring that shareholders value is both enhanced through corporate performance and protected through adequate internal financial controls. Board should seek candidates with expertise in financial accounting and corporate finance.[891]Still within the USA under the BRT Principles, it is thought that to achieve accuracy and clarity in the corporation's financial statements and other disclosures prepared by management, the board, through its audit committee, should have an understanding of the corporation's financial statements, including why the accounting principles critical to the corporation's business were chosen, what key judgments and estimates were made by management, and how the choice of judgments and estimates affect the reported financial results of the corporation. Senior management is responsible for the integrity of the corporation's financial reporting system and the accurate and timely preparation of the corporation's financial statements and related disclosures in accordance with generally accepted accounting principles and in compliance with applicable laws and regulations. It is senior management's responsibility, under the direction of the CEO and the corporation's principal financial officer, to establish, maintain and periodically evaluate the corporation's controls over financial reporting and the corporation's disclosure controls and procedures. The CEO and principal financial officer also are responsible for certifying the

[889] Combined Code, Provision C.2.1.
[890] *Ibid*., Provision C.3.5.
[891] See Report of the NACD Blue Ribon Commission on Risk Oversight (2002).

accuracy and completeness of the corporation's financial statements and the effectiveness of the corporation's internal and disclosure controls. Employees should have a means of seeking guidance and alerting management and the board about potential or actual misconduct without fear of retribution, and violations of the code of conduct should be addressed promptly and effectively.

In the Indian internal control system, the responsibility of the management is to put in place adequate control systems and to ensure their operation. The responsibility of the audit committee's should include:

i. Oversight of the company's financial reporting process and the disclosure of its financial information.
ii. Reviewing with management the annual financial statements before submission to the board
iii. Reviewing with the management, external and internal auditors, and the adequacy of internal control systems.
iv. Reviewing the adequacy of internal audit function.
v. Discussion with internal auditors of any significant findings.
vi. Reviewing the findings of any investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems and reporting the matter to the board.
vii. Discussion with external auditors before the audit commences, of the nature and scope of audit. Also post-audit discussion to ascertain any area of concern.
viii. Reviewing the company's financial and risk management policies.
ix. Looking into the reasons for substantial defaults.[892]

[892] Securities and Exchange Board of India (SEBI) Report, ss. 2.3 and 9.10. See also s. 2.9 (Regulations regarding insider information and insider trading); s. 9.9 (the powers of the Audit committee should include

The UK position is very much similar with the position in Nigeria where the company appoints internal auditor, external auditor and even auditors committee, and to deliver auditor report annually.

Shareholder Voting Powers

On the issue of shareholders' voting powers, the Cadbury Report has no express provision but however, states that shareholders have delegated many of their responsibilities as owners to the directors, who act as their standards.[893] It is for the shareholders to bring the directors to book if they appear to be failing in their stewardship, and they should use this power. While they cannot be involved in the direction and management of their company, they can insist on a high standard of corporate governance, and good governance is an essential test of the stewardship. The accountability of boards to shareholders will therefore, be strengthened if shareholders require their companies to comply with the code. The issue is also not covered directly under the Combined Code. It is provided however that at any general meeting, the company should propose a separate resolution on each substantially separate issue, and should in particular propose a resolution at the AGM relating to the report and accounts. For each resolution, proxy appointment forms should provide shareholders with the option to direct their proxy to vote either for or against the resolution or to withhold their vote. The proxy form and any announcement of the results of a vote should make it clear that a 'vote withheld' is not a vote in law and will not be counted in the calculation of the proportion of the votes for and against the resolution.[894]

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powers to seek information from any employee); s. 12.1, (Accounting Standards and Financial Reporting), and s. 13.3, (functions of management).

[893] Cadbury Report, s. 6.6.

[894] Combined Code, Provision D.2.1.

In the USA, the NACD Report contains no provision express or otherwise on the issue. Under the BRT Principle however, it widely accepted that shareholders are not involved in the day-to-day management of corporate operations but have the right to elect representatives (directors) to look out for their interests and to receive the information they need to make investment and voting decisions. The board should be responsive to communications from shareholders and should address issues of concern to shareholders.

The board should respond appropriately when a director nominee receives a significant 'withhold' or 'against' vote with respect to his or her election to the board. The corporate governance committee should assess the reasons for the vote and recommend to the board the action to be taken with respect to the vote, which should be communicated to the corporation's shareholders.

In India, on shareholders' voting powers, the basic rights of the shareholders include right to transfer registration of shares and participating and voting in shareholders meeting[895]A company must have appropriate systems in place which will enable the shareholders to participate effectively and vote in the shareholders' meetings. The company should also keep the shareholders informed of the rules and voting procedures which govern the general shareholder meeting.[896] The company must also ensure that it is not inconvenient or expensive for shareholders to cast their vote.[897] For shareholders who are unable to attend the meetings, there should be a requirement which will enable them to vote by postal ballot for key decisions.[898] The committee recommends that a board committee under the chairmanship of a non-executive director should be formed to specifically look into the redressing of shareholder complaints like transfer of shares, non-receipt of balance sheet, non-receipt of

[895] Securities and Exchange Board of India (SEBI) Report, s. 14.5.
[896] *Ibid*., s. 14.9.
[897] *Ibid*., s. 14.10.
[898] *Ibid*., s. 14.11. See also Annexure 3 for a detailed list of the matters which should require postal ballot.

declared dividends, etc. The committee believes that the formation of such a committee will help focus the attention of the company on shareholders' grievance and sensitize the management to redressing of their grievance.[899]

Shareholders Meeting and Proxy Proposals

In the UK, the position under the Cadbury Report is that the chairman of the remuneration committee should be available to any concerns of shareholders at the Annual General Meeting.[900]The Annual General meeting provides the opportunity for shareholders to make their views on such matters as directors' benefits known to their boards. Shareholders can play a more practical governance role by aiming to influence board policies in this way than by seeking to make the details of board decisions subject to their vote.[901] Shareholders can make their views known to the boards of the companies in which they have invested by communicating with them directly and through their attendance at general meeting.[902] Reports and accounts are presented to shareholder at the Annual General meeting. In particular, the Annual General Meeting gives all shareholders direct and public access to their boards.[903] The chairman of the Audit Committee should be available at the AGM[904]

Under the Combined Code, the company should propose a separate resolution on each substantially separate issue, and should in particular propose a resolution at the AGM relating to the report and account. For each resolution, proxy appointment forms should provide shareholders with the option to direct their proxy to vote either for or against or to withhold their vote. The proxy form and any announcement of the results of a vote should make it clear that a 'vote withheld' is not a vote in law and will not be counted in the calculation of the

[899] Securities and Exchange Board of India (SEBI) Report, s. 14.12.
[900] Cadbury Report, s. 4.44.
[901] *Ibid*., s. 4.45.
[902] *Ibid*., s. 6.5.
[903] *Ibid*., s. 6.7.
[904] *Ibid*., Appendix 4, 6(f).

proportion of the vote for and against the resolution.[905] Shareholders should be invited to approve all new long-term incentive schemes and significant changes to existing schemes.[906] The company should ensure that all valid proxy appointments are properly recorded and counted and that the number of shares in respect of which proxy appointments has been validly made; the number of votes against the resolution; and the number of shares in respect of which the vote was directed to be withheld, are made available.[907] The chairman should arrange for the chairman of the audit, remuneration and nomination committees to answer questions for all directors that attend.[908]The company should arrange for the notice of the AGM and related papers to be sent to shareholders at least 20 working days before the meeting.[909]

In the USA, the NACD Report does not cover the subject matter. Under the BRT Principle, it is however provided that directors should attend the corporation annual meeting of shareholders, and the corporation should have a policy of requiring attendance register in unusual circumstances. Time at the annual meeting should be set aside for shareholders to submit question and for management or directors to respond to those questions. The board should seriously consider issues raised by shareholder proposals that receive substantial support and should communicate its response to proposals to the shareholder proponents and to all shareholders. It is the responsibility of the board to respond appropriately to shareholders' concerns. The board should be notified of shareholder proposals, and the board and its corporate governance committee should oversee the corporation's response to these proposals.

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[905] Combined Code, Provision D.2.1.
[906] *Ibid*., Provision B.2.4.
[907] *Ibid*., D.2.2.
[908] *Ibid*., D.2.3.
[909] *Ibid*., D.2.4.

In India, the committee believes that the general body meeting provides an opportunity to the shareholders to address their concerns to the board of directors and comment on and demand any explanation on the annual report or on the overall functioning of the company. It is important that the shareholders use the forum of general body meetings for ensuring that the company is being properly stewarded for maximizing the interests of the shareholders.[910] The annual general meetings of the company should not be deliberately held at venues or the timing should not be such which makes it difficult for most of the shareholders to attend.[911] Currently, although the formality of holding the general meeting is gone through, in actual practice only a small fraction of the shareholders of that company do or can really participate therein. This virtually makes the concept of corporate democracy illusory. It is imperative that this situation which has lasted too long needs an early correction.[912] The committee recommends that the audit committee chairman should be present at Annual General Meeting to answer shareholders' queries.[913]The committee also recommends that the chairman of the remuneration committee should be present at the Annual General Meeting, to answer the shareholders' queries. However, it would be up to the chairman to decide who should answer the queries.[914]

Anti Takeover Devices

No express provision on the subject matter is contained in the Cadbury Report, but the provisions of the Report can help to resolve problem situations.[915] Similarly, the Combined Code made no express provision on the subject matter. However, it is provided that there should be a dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders

[910] Securities and Exchange Board of India (SEBI) Report, s. 14.2.
[911] *Ibid*., s. 14.10.
[912] *Ibid*., s. 14.11.
[913] *Ibid*., 9.6.
[914] *Ibid*., s. 10.6.
[915] Cadbury Report, s. 4.6.

takes place.[916]The chairman should ensure that the views of shareholders are communicated to the board as a whole. The chairman should discuss governance and strategy with major shareholders. Non-executive directors should be offered the opportunity to attend meetings with major shareholders and should expect to attend them if requested by major shareholders. The senior independent director should also be offered the opportunity to attend meetings with major shareholders and should expect to attend them if requested by major shareholders. The senior independent director should attend sufficient meetings with a range of major shareholders to listen to their views in order to help develop a balanced understanding of the issues and concerns of major shareholders.[917]

In the US, neither the NACD Report nor the BRT Principle contains any provision on the subject.

In India however, the committee recommends that as shareholders have a right to participate in, and be sufficiently informed on decisions concerning fundamental corporate changes, they should not only be provided information as under the Companies Act, but also in respect of other decisions relating to material changes such as takeovers, sale of assets or divisions of the company and changes in capital structure which will lead to change in control or may result in certain shareholders obtaining control disproportionate to the equity ownership.[918]

In Nigeria, the Companies and Allied Matters Act makes provision for certain level of participation of shareholders in takeover bids, including the protection afforded to dissenting shareholders.

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[916] Combined Code, Main Principle D.1.
[917] Combined Code, Provision D.1.1.
[918] Securities and Exchange Board of India (SEBI) Report, s. 14.7.

CHAPTER SEVEN

THE IMPACT OF CORPORATE GOVERNANCE ON THE NIGERIAN COMMUNITY

7.1 Introduction

There has, since the last decade of the 20th century, been increased global attention on corporate governance in terms of structures, processes, system, and practices which drive the conduct of business. This is in recognition of the critical role of corporate governance in the success or failure of companies and indeed of national economies in the increasingly globalized world economy.[919]

It goes without saying that corporate governance has wide reaching importance. The importance of corporate governance is further highlighted by the adoption of corporate governance codes by nearly every country. In Nigeria, apart from the main statute regulating corporate organizations in the country, that is, the Companies and Allied Matters Act[920] (CAMA), there are several corporate governance codes in force. The corporate governance codes applicable in the country includes, the Code of Best Practices on Corporate Governance in Nigeria, 2003,[921] which was issued by the Securities and Exchange Commission; the Code of Corporate Governance for Bank in Nigeria Post Consolidation, 2006[922] which was issued by the Central Bank of Nigeria (CBN); the Code of Corporate

[919]R. Ikpeahior& H.P. Faga 'Reflection on Sound Corporate Governance for a Thriving National Economic Development', *Ebonyi State University Law Journal*, Vol. 2, No. 1, 2007, pp. 210-222.
[920]Cap. 120, Laws of the Federation of Nigeria, 2004.
[921]I.e. 'the 2003 SEC Code.'
[922] Referred to as the CBN 2006 Code

Governance for Licensed Pensions Operators, 2008[923] which was issued by the Pension Commission, etc.

Hence, the heightened awareness of the need for effective corporate governance is not without justification. A well implemented corporate governance regime has tremendous benefit. These benefits are the enduring attributes of corporate governance. In the first place, effective corporate governance, backed up with adequate monitoring and enforcement, would build investors confidence, eliminate financial scandals and curb corporate failures.[924] It was in view of the above that the Federal Government, recently, inaugurated steering committee that will develop the country's code of corporate governance.

The inauguration of the committee was in accordance with section 119(1) of the Financial Reporting Council of Nigeria Act[925] which empowers the council as the only statutory body responsible for the development of code of corporate governance practices in both public and private sectors of the economy.[926]Generally, good corporate governance would help prevent corporate scandals, fraud and potential civil and criminal liability of the organization. It is also seen as good businesses as it enhances the reputation of the corporate entity and makes it more attractive to customers, investors, suppliers and contributors in the case of non-profit organizations.In addition, good corporate governance ensures corporate success and economic growth while it maintains investors' confidence, as a result of which, a company

[923]Referred to as the 2008 PENCIM Code
[924] N. Ofo, *op cit*, p. 17.
[925]No. 6 of 2011.
[926] O. Gabriel, 'FG Inaugurates Committee on Code of Corporate Governance: The Vanguard, Friday, January 18, 2013. According to the Minister of Trade and Investment, Mr. OlusegunAganga, the committee would develop unified code of corporate governance for all matters pertaining to corporate governance in both private and public sectors of the Nigerian economy, promote the highest standards of corporate governance principles and practices and encourage sound systems of internal control and information systems control to safeguard stakeholders' investment and assets of public interest entities among other things.

can raise capital efficiently and effectively. It also provides proper inducement to the owners as well as managers to achieve objectives that are in the interests of the shareholders and the organization even as it minimizes wastages, corruption, risk and mismanagement and above all, it ensures that the corporate body is managed in a manner that fits the best interest of all.

Traditionally, the focus of company jurisprudence is solely on the rules and principles that safeguard the interest of the company's members and sometimes creditors only. This is no longer the case, as many jurisdictions, Nigeria inclusive is now taking a different approach by noticing that the way companies are run affects not only their members and creditors, but also their customers, suppliers employees, and neighbours, and also the society in a more general sense.[927] Thus, how a company is governed, and decisions made in companies are a major determinant of employment levels, regional development, the pale and contours of technological change, and the condition of our physical, and even cultural, environment. The point is not just the obvious one that companies 'affect' community, but that their decisions constitute exercise of significant social power.[928] This gives credence to the popular saying by the Confederation of British Industry, 1973[929] "our style of life is largely determined by the activities and style of business; and the style of business is largely determined by the activities and style of our companies.

7.2 The Effect of Corporate Insolvency on Long Time Economic Growth in Nigeria

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[927]J.E Parkinson, *Corporate Power and Responsibility, Issues in the Theory of Company Law*, (U.S.A.: Oxford University Press, 1993) p.I.
[928]*Ibid*.
[929]Confederation of British Industry, the Responsibilities of the British Public Company (1973) 9+8.

A company is considered insolvent when it is unable to pay its debts as and when they fall due.[930] Insolvency is a condition of being unable to pay debt as they fall due or in the usual course of business. It is the inability to pay debt as they mature.[931]

For a developing country such as Nigeria, corporate governance is of critical importance. In recent history, corporate insolvency has led to serious economic upheavals. For example in the late 1980 and early 1990s, the country witnessed a near collapse of the financial sector through the phenomenon of failed bank and other financial institutions. In consequence, the Failed Banks (Recovery of Debt) and Financial Malpractice in Banks Act was enacted to facilitate the prosecution of those who contributed to the failure of the banks and to recover the debts owed to the failed banks. Secondly, the privatization and commercialization programme of the Nigerian Government was a reaction to insolvency recorded in many state owned enterprises (SOE)[932] According to El-Rufal, data obtained from various government department estimates reveal that in 1998, Nigeria Public Enterprises (NPE) were given about ₦265 billion in transfer, subsidies and waivers, which could have been better invested in our education, health and other social sectors.[933]

When a corporation runs insolvent and so continues, its effect are enormous, such prolonged insolvency usually leads to reconstruction, re-engineering, rightsizing, involuntary take-over, bankruptcy, liquidation and winding up if the insolvency becomes intractable.[934] This leads to

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[930] A.O. Unaegbu, L.A. Onoyah, Efficacy Assessment of Z-Score in Selected Sectors of Emerging Economy; *Greener Journal of Economic and Accountancy* p. 101.2, No1, pp 17-29, p. 17.

[931] B.A. Garner, (ed), Black's Law Dictionary (St Paul, Minn: West Group, 1999) p. 811. See also section 56 (AMA for the definition of an insolvent person .

[932] D.I. Nwogi, *et al*, Corporate Governance and Bank Failure in Nigeria: Issues, Challenges and Opportunities, *Research Journal of Finance and Accounting*, Vol. 21, No 2 (2011) pp 1-18, p. 5

[933] *Ibid*.

[934] O. Unaegtu, *op cit*, p. 20.

the appointment of a receiver and manager to salvage the interest of creditor primarily as a corporate governance measure.

7.2.1 Appointment and Duties of a Receiver and Manager

The Companies and Allied Matters Act (CAMA) permits companies to borrow money for the purpose of their business, or to fulfill any of their obligations. CAMA also permits companies to secure loans obtained, by their properties. The loan may be secured by a fixed charge or a floating charge. Upon default, the secured creditor may appoint a receiver (and or a manager) to realize unpaid debt.[935]Any person can be appointed a receiver/manager except the following categories of persons to wit: an infant, a person of unsound mind, a body corporate, an undischarged bankrupt, a director or auditor of the company and a person convicted of any offence involving fraud, dishonesty, official corruption and moral turpitude.[936]Once a receiver/manager is appointed over a company, he becomes the alter ego of the company. Where a creditor enforces his security by appointing a receiver/manager, the assets belonging to the debtor company now come under the receiver/manager. Thus, upon his appointment, the receiver/manager is automatically vested with the power to manage the company's business.[937]Usually, a receiver is appointed where the loan agreement is secured by a fixed charge, while a receiver and manager is appointed when the loan agreement is secured by charges including floating charge over a part or the whole of the company's assets.[938] A receiver or manager appointed out of court shall be deemed to be an agent of the person or persons on whose behalf he is appointed.[939]The person(s) appointed as a receiver of any

[935]Companies and Allied Matters Act (CAMA), Cap. C20 LFN 2010, s. 209.
[936] Companies and Allied Matters Act (CAMA), Cap. C20 Laws of the Federation of Nigeria, 2010, s. 387.
[937]*Jukok Int'l Ltd. v Diamond Bank Plc,*(2016) 6 N.W.L.R. (Pt. 1507) p.55 at 68; Intercontractors (Nig) Ltd. V UAC of Nig. Ltd. (1988) 2 N.W.L.R. (Pt. 76) p. 303.
[938] J.O. Orojo, *Company Law and Practice in Nigeria*, (Lagos: Mbeyi& Associates, 1999).
[939] CAMA, Cap. C20 Laws of the Federation of Nigeria, 2010, s. 390.

property of a company shall subject to the rights of prior encumbrances take possession of and protect the property, receive rents and profits and discharge all outgoings in respect thereof and realize the security for the benefits of those on whose behalf he is appointed, but unless appointed manager, he shall not have power to carry any business or undertaking.[940] The receiver or manager appointed out of court has the discretion whether or not to apply to the court for direction with regard to any particular matter arising therefrom and pertaining to the performance of his function.[941]

The purpose of appointing a receiver for a company as can be deduced from the Act and from case law, is to work towards paying outstanding debt or redeeming security or freeing property from some jeopardy for the benefit of creditors or debenture holders on whose behalf the appointment is made.[942]Accordingly, any person appointed a receiver of any property of a company shall subject to the rights of prior incumbrances, take possession of and protect the property, receive the rents and profits and discharge all outgoings in respect thereof and realize the security for the benefit of the creditors. He shall also have the power to carry on any business or undertaking of the company. As a manager, he shall manage the whole or any part of the undertaking of a company with a view to the beneficial realization of the security of those on whose behalf he is appointed.[943]In *Fasakin v. Fasakin,*[944] the court gave the following examples, where, in practice appointment has been made:

i. Where a company about to be wound up is wholly insolvent and other creditors are threatening action against the company for recovery of the debt; or

[940]*Ibid*., 2004, s. 393 (1).
[941]*Jukok Int'l Ltd. v Diamond Bank Plc, supra*, p. 67.
[942]*Anatogu v Anatogu* (1998) 5 NWLR (pt. 548) 42.
[943] CAMA, Cap. C20 Laws of the Federation of Nigeria, 2010, s. 393.
[944](1994) 4NWR (Pt. 340) 597 at 619.

ii. Where a company was insolvent and its works closed; or[945]

iii. Where judgment had been obtained against a company and execution was likely to issue,[946] or

iv. Where a company is proposing to distribute among its shareholders a reserve fund which constitutes practically its only asset, thereby putting the debenture holders' interest at risk, or

v. Where the company's auditors declared at a general meeting and without being challenged by the director that after providing for liabilities, the company's assets would only cover principal loans secured and that the company's credit and funds were exhausted[947]

The larger the business of a company, the larger the impacts its operations will have on a larger number of individuals and, consequently the economy, considering the potential for the environment (i.e. society) to be very significantly affected by a company that owns and is actively expanding its network of oil pipelines. Similarly, a large company may run nuclear power station products, best practice waste-management of which involves the storage into the long term future of active material. A large company is that one that employs a significant proportion of workers in a locality. It may be the largest purchaser of particular product or products in the country so that producers are dependent upon its continuing to buy a large share of their output.[948] When such a giant company suddenly runs insolvent on ground of ineffective governance, its effect is manifold. Such companies outlive their usefulness and

[945] *MacMahon v North Kent Ironworks Co*. (1891) 2ch 148.
[946] *Edwards v Standard Rolling Stock Syndicate* (1893) 1ch 574.
[947] *Fasakinv.Fasakin* (supra)
[948] The telecommunication companies the banking sector and the oil giants clearly exemplify this pant.

become financially non-viable. This is so because, before a company runs insolvent, its ongoing operations are brought to an end, its assets are sold and the proceeds of sale are used to pay those to whom it owes. This process is called 'winding up' or liquidating' the company. And in economic parlance, it is said that its productive potential has ended[949] because it ceases to trade, has no assets, and stops making the required annual returns to the registrar,[950] and the government in form of taxes and the community in the form of social responsibility.

To further buttress the point being made, it may be pertinent to gain an impression on the size of individual enterprises on a global scale.The world's ten largest companies (by number of employees) employ a total of 4.3 million, and it has been estimated that when the dependants of those employees are taken into account the welfare of up to 21 million people, a figure approaching the population of the Scandinavian countries, is directly affected by their decision. In 1989 their assets totaled US $560 billion, equivalents to the GNP of Canada.[951] As regards the UK in 1985, 165 companies in the UK employed over 10,000 people,[952] a composite picture of the position of large companies within the economy is presented in a study of statistics relating to the 'top 100' manufacturing companies published by the department of industry in 1976. It revealed that these companies accounted for about 40 percent of manufacturing industry's net assets, employment, and inward direct-investments from overseas (excluding oil companies investment), 40-50 percent of visible exports, 70 percent of expenditure on industrial scientific research and development, and about 75

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[949] See S. Mclaughlion, *Unlocking Company Law* (ed), (U.K: Hodder Education, 2009) p. 4- 6.
[950]*Op cit*, p. 398.
[951] A. Demb and F.F., Neubauer, The Corporate Board: Confronting the parodoxes (1992) at 3.
[952] Hay and Morris, Industry Economics and organization: Theory and Evidence (1991), at 281 – 285, in J.E. Parkinson, *op cit*, p. 5.

percent of direct investment by UK companies (excluding oil) in manufacturing overseas.[953] In the same vein, the Bullock Committee in 1977 noted that the 'last 20 years have seen the growth of the giant industrial enterprise and the concentration of economic power in the hands of such companies. By 1981, 328 companies accounted for over 50 percent of manufacturing employment, and a mere 66 companies for 30 percent.[954]

When these companies that hitherto contributed immensely to the economic life of a nation cease to exist, it would in the long run exacerbate economic and financial crisis. Because of the far reaching role played by these corporate entities, their 'death' is largely felt by all sectors.

7.3 The Effect of Corporate Collapse on the Community of Operation

It has been observed that contrary to the assertion of many personalities in the business community, a few governance principles have always been a part of our company laws in Nigeria.[955] The problem remains that no director, shareholder, or other stakeholder has made any significant attempt to enforce or redress a breach of any of the rule because of the possible ignorance of those in control of the corporations who see any challenge as hostility from the 'enemy'. According to Okpara,[956] Nigeria has ample laws for the development and implementation of effective corporate governance in the country but noted lack of

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[953]Department of Industry, 'the Importance of Top 100 Manufacturing Companies', *Economic Trends*, No. 274 (1976) at 85.

[954] DTIC, Report on the Census of Production 1981,' Summary Tables, *Business Monitor* PA, 1002 (1984), at 258; see generally J.E. Parkinson Corporate Power and Responsibility, Issues in the Theory of Company Land (U.S.A.: Oxford University Press, 1992).

[955]Oserogho& Associates, 'Corporate Governance in Nigeria: Are There Laws and Principles?, available at: [www.document],URL http://oseroghoassociates.com/news-2003-02.5html, accessed on 15/05/2014.

[956] J.O. Okpara, Perspectives on Corporate Governance Challenges in a Sub-Saharan African Economy, available at: [www.document], URL, http://www.ubiconpro.com/11john.pdf.collegeofbusiness,bioomsburg,unversityof pennysylvania, accessed on 15/05/2014.

enforcement as the problem. Oyebode[957] pointed out that while the Companies and Allied Matters Act envisages good governance, the reality of our situation is that all this has largely become academic on account of impotent and moribund regulatory agencies. According to him:

> The recent collapse of the stock market and uncovering of flagrant abuses of loans and perquisites in the banking sector and the high incidence of corruption in the Nigerian economy generally are enough to pose the question indeed of not corporate governance out actually its absence in this country. The massive fraud and cooking of books in companies, a notable example of which is Cadbury not to mention insider dealings and compromised boards in many companies as well as spineless shareholders' associations, audit committees and rubber stamp annual general meetings suggests the collapse of corporate governance in Nigeria.[958]

Recent occurrences in the international corporate environment have focused the world's attention to concerns for effective domestic corporate governance initiatives that would ensure credibility on how companies conduct business in our post moderngloballised world. The Enron and the WorldCom saga in the United States, the Vivendi and the recent Parmalat scandals in Europe are the most recent of such disturbing issues of corporate collapse and business failure. Nigeria has also had its share of inelegant business practices that have resulted in failed corporate giants that once stood likeIroko tree without any overt sign of trouble for example, Telkon.[959]

Wilson emphasized the fact that no company whatsoever can be too big to fail if the practice of good corporate governance is jettisoned.In his words,

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[957] O. Akin, 'The Imperative of Corporate Governance in Nigeria, available at: (www.document) URL http://www.nigeriavillagesquare.com/articles/alkinoyebode/the-imperative-of-corporate-governance-nigeria, accessed on 15/05/2014.
[958] *Ibid*
[959] A. Nwogiolagunju, *op cit,* p. 3.

> The clear lesson Enron, Parmalat, World-com, and Barings Bank taught the corporate world is that no company or bank can be too big … to fail. A common thread that ran through these monumental corporate failures was the poor corporate governance culture, to wit, poor management, poor regulation and poor supervision.[960]

Hence, the neglect of good corporate governance practices comes with far reaching effects and losses usually incurred by unsuspecting shareholders and the prospective clients.[961] In most corporate entities, the shareholders delegate decision rights to the managers to act in their interests. This separation of ownership from control implies a loss of effective control by shareholder over managerial decisions partly as a result of this separation between the two parties or systems of corporate governance. Corporate governance is needed to assist in aligning the incentive of managers with those of shareholders. Hence in the event of a collapse in the proper governance of a company that is an abstraction and can only act through human elements,[962]it will pave way for fraud and financial difficulties.[963] The point remains that effective and proper governance is fundamental to the whole operation and activities of the company. No problem challenges the survival of a business community more intensely than pooror a collapse in corporate governance.

In the past, experience has shown that lack of proper and effective governance framework in Nigeria has been exploited by senior managements of companies at the expense of other

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[960] I. Willson, 'Regulatory and Institutional Challenges of Corporate Governance in the Nigeria Post Banking Consolidation', *Nigeria Economic Summit Group Economic Indicators* 12 (2), pp.1-10.

[961] G. Jonathan 'The Private Sector Must Do its Part to Earn the Confidence Reposed on it by Government', *Journal of the Buren of Public Enterprises*, (January – March, 2010) pp, 6-7.

[962]*Bolton (Engineering) Co Ltd v Graham and Sons* (1957) IQB 159, per Denning, L.J; see also the position of Viscount Tlaldane, in *Lennard's Carrying Co. Ltd v Asiatic Petroleum Co Ltd* (1915) AC 705, 7134; *Trenco (Nigeria) Ltd v African Real Estate Ltd* (1978) 4 SC9, per Aniagolu, JSC.

[963] See generally, 'Improving Business Behavior: Why We Need Corporate Governance – Speech Following the Adoption of the OECD Principles of Corporate Governance; Companies and Allied Matters Act, *op. cit*, s. 37; *Union Bank (Nigeria) Ltd v Penny Mart* (1992) 5 NWCR (Pt 240) 228 at 237.

shareholders. The recent down turn of the Nigerian stock exchange also brought to fore some of these practices by capital market operators and companies alike.[964] The recent collapse or near collapse of almost eight (8) banks with an estimated total market share of thirty five percent (35%) of the industry's total deposit brought to fore the effect of corporate collapse on the community. The then governor of the Central Bank of Nigeria (CBN) MallamSanusi, Lamido explained that five (5) out of the eight (8) banks became stressed as a result of 'poor corporate governance.[965] One cannot forget in a hurry the extent to which fraud, poor practices and poor management contribute to the failure and collapse of Savannah Bank Plc, which led to the revoke of its licence.[966]

In the corporate world, the need for proper governance and corporate governance principles assumes greater proportion because of the wide reaching effects of the consequences.[967] The availability of accurate or up-to-date information on company performance is of fundamental importance. In the absence of reliable accounting data, effective shareholder supervision of management is impossible. The sudden collapse in recent years of well known companies which, according to their duly audited accounts, were thriving, have repeatedly focused attention on the considerable scope for the distorted presentation of financial information.[968] The Committee on the Financial Aspects of Corporate Governance (the Cadbury committee), a body set up by the Financial Reporting Council, the London Stock Exchange and the Accounting profession notes that a 'basic weakness in the current system of financial reporting is the possibility of different accounting treatments being applied to essentially the

[964] B. Ilori, Corporate Governance in Nigeria, What We Need to Do, *Punch*, Sunday, May, 12, 2013.
[965] L. Sanusi, 'There's Clearly a Failure of Regulation, *Punch News Paper*, Sunday August 16, 2009, pp. 24-25.
[966] And this sector is the nerve centre of any modern economy, being the repository of people, wealth and supplier of credits which lubricates the engine of growth of the entire system.
[967] After the Enron saga, many other big and giant companies faced similar closure.
[968] J.E, Parkinson, *Corporate Power and Responsibility, Issues in the Theory of Company Law*, (New York: Oxford University Press, 1993) p. 160.

same facts.[969] For example, companies have been able to inflate reported profits by reducing the apparent level of debt through techniques such as off-balances, sheet financing, and to improve earnings figures by classifying costs as 'extraordinary items' and thus presenting them 'below the line – such practices may not only conceal questionable solvency but also make it more difficult to assess the quality of the board's stewardship and the company's prospects in general.[970] This would pave way for management self-dealing i.e. transactions involving the company in which a director has a conflicting interest and to the diversion by directors to themselves or affiliates of 'corporate opportunities'.[971] The point is that self-dealing usually occasions when there is corporate collapse or separation of ownership and control. This would encourage managerial slackness, with the possibility of obtaining illicit wealth transfers. This perception of a collapse or unfairness undermines investor confidence, and if widespread would seriously diminish the capacity of the corporate system to raise capital, and ultimately survive.[972] In the case of banks, such failure had resulted in massive withdrawal of funds from the failed ones to the healthy ones, a phenomenon known as 'flight to safety'[973] even though outright dishonesty is presumably rare in the upper echelon of corporate management. Also as company's corporate governance structure collapsed, and in most cases as companies approach insolvency, shareholders incentives to siphon away value or gamble on risky projects grew rapidly.[974]

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[969] *Ibid*.
[970] J.E. Parkinson, *op cit*, p 161.
[971] J.E. Parkinson, *op cit*, p. 1200.
[972] Alfred Marshall believed that companies were only viable because of the growth of commercial morality: if the leading officers of great public companies … showed an eagerness to avail themselves of opportunities for wrong doing … their wrong uses of trusts imposed on them would have been so great a scale as to prevent the development of this democratic form of business; A, Marshall, Principles of Economics (1890), at 253, in J.E. Parkinson, *op cit*, p. 202.
[973] T.A. Olaniyi, 'Predicting Potential of Failure, in Nigerian Banking Sector, A Comparative Analysis of First Bank Plc, and Trade Bank Plc', *Bascock Journal of Management and Social Sciences*, Vol. 6, No 1, pp. 64-73.
[974] R. Kraakman, *et al*, *The Anatomy of Corporate Law. A comparative Approach* (New York: Oxford Press, 2004) p. 73.

The fact is that good corporate governance ensures that the business environment is fair and transparent and that companies can be held accountable for their actions. Conversely, weak corporate governance leads to waste, mismanagement and collapse. Regardless of the type of venture, only good governance can deliver sustainable good business performance.

Apart from the business community, the community at large i.e. the society, suffers a no small effect in the event of corporate collapse.[975] This is so because corporate governance is about performance.[976] Corporations must deliver good results not only to the shareholders, but also to the stakeholders, the business community, the society and the economy as a whole. Hence corporate collapse comes with attendant massive disaster. While not all problems of a corporate entity can be linked to collapse of corporate governance, many of them can. For example the much emphasized Enron saga provides a well-known example of systematic problems within a corporation that could have been addressed by improved corporate governance. The recent (and several) one spice from B.P also represents an example of how corporate governance problems within the company created potential danger. The global financial crisis is yet another example of how failure of boards and executives to understand and manage risk led to governance failures with very serious consequences, not only for financial firms and banks, but for individuals and national economies around the world.[977]

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[975] This is so because such collapse affects the proper management and organization of the company and could lead to its eventual collapse or insolvency. In such case, the society losses as the goods or/and services rendered by the company would cease or come to a sudden halt. Also, other benefits that had beforehand accrued to the society would cease. For a clear understanding on this see our discussion on corporate social responsibility, *infra*.

[976] It is about how companies make seasons, how they organize themselves and communicate with shareholders and the rest of the world.

[977] R. Adamson, 'Corporate Governance, Risk Management and Corporate Social Responsibility in Emerging Markets: A Symbiotic Relationship', available at: beedle.stu.ca/corporate-governance-and-risk-management-corporate-social-responsibility, accessed on 22/03/2014. Robert Adamson is the executive director, Centre for Corporate Governance and Risk Management.

Issues such as Board Composition, their agenda and processes for decision-making and how they learn to continuously improve the governance of corporation, critically influence both the quality of decision and of management. The main responsibility of the board is to provide effective oversight and strategic guidance for the management. The quality of their decisions is critically dependent on the quality of information they have. Establishing a culture that sets the right tone at the top is critical for establishing the 'trust' for the corporation with all its stakeholders.[978]

7.4 The Imperative of Corporate Governance on the Socio-Economic Life of Nigeria

In a country like Nigeria undergoing development process, greater attention and implementation of effective corporate agenda is imperative in earning policy credibility. Corporations intending to enter into strategic alliances with investors must ensure sound corporate governance. No investor would risk his investment in a corporation riddled with controversies, fraud, financial scandals, maltreatment of stakeholders or one administered as a one-man entity.[979]

Thus, the degree to which corporations observe basic principles of good corporate governance is an increasingly important factor for investment decisions. Although companies have been in existence for hundreds of years, the concept of corporate governance in the form

[978] Y. Arguden, Measuring the Effectiveness of Corporate Governance, available at: www.Knowledge.Instead.Edu>Home>CRS>Corporate Governance, accessed on 15/05/2014 (created April 16,2012).

[979] J.U.K .Igwe, 'Investment, Nigeria Capital Market and Corporate Governance, with Comparative Illustration, Laws, Practices and Ethics', vol. 3, *Law Developing Research Publications and Consulting Limited*, 2005, pp. 4-5.

in which we know it today only, emerged in few decades ago.[980] The concept has become necessary for all countries – both those with already sophisticated economic system, and those with developing economic infrastructure which are anxious to attract international portfolio investment.[981] It is against this backdrop that the remark made by the president of the World Bank is apposite. According to him; 'the proper governance of companies will become as crucial to the world economy as the proper governance of countries.[982]

On the imperative of corporate governance on the socio-economic life of any nation, Jayashree stated thus:

i. Adherence to the practice of good corporate governance enhances the efficiency of corporate organisations.
ii. Good corporate governance provides stability and the desirable growth of the company
iii. Effective corporate governance reduces perceived risks, consequently reducing cost of capital.
iv. Good corporate governance system demonstrated by adoption of good corporate practices and ethics builds stakeholders' confidence.
v. Adoption of corporate governance promotes stability and long-term sustenance of stakeholders' relationships.
vi. Potential shareholders aspire to enter into a relationship with enterprises whose corporate governance credentials are exemplary.[983]

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[980] R. Ikpehior& H.P. Faga, *op. cit*, p. 211.
[981] *Ibid*.
[982] W. Bank, The East Asian Miracle: Economics Growth and Public Policy (1993) pp. 5-7. Cited in R. Ikpehior and H.P. Faga, *op. cit*., p.211.
[983] S. Jayashree, 'Some Views on Corporative Governance', *InderaManagement Review*, Indera School of Management Studies (Pune Tathawade, 2006).

Corporate governance is a key element in enhancing investors' confidence, promoting competitiveness and ultimately improving economic growth.[984] Even as the economy moves from the predominance of state-owned enterprise to a private sector-led one through the ongoing privatization exercise, one of the assurances that investors will realize the dividends of such exercise is the implementation of corporate governance principles and codes by such privatized companies. Even from the examples of other jurisdictions like United Kingdom and the United States, it has been established that there is a direct correlation between a country's gross domestic product (its socio-economic life) and its corporate governance practice.[985]

Well executed corporate governance is similar to a police department's internal affairs weeding out and eliminating problems with extreme prejudice.Corporate governance can prevent corporate scandals, fraud and the civil and criminal liability of the company and members of the society in extension. It can also enhance a company's image in the public eyes as a self-policing company that is responsible and worth of shareholders and debtholders' capital.[986] It dictates the shared philosophy practices and culture of an organization and its employees. A corporation without a system of corporate governance is regarded as a body without a soul or consciences.If this shared philosophy breakdown, then corners will be cut, product will be defective and managementwill grow complacent and corniest.[987] The resultant effect would be a defective economic life and wide-scale social

[984] S.A, Lamido, The Central Bank of Nigeria (Official Magazine) p. 15.
[985] M. Ai-faki, Effective Enforcement of disclosure Requirements by Regulatory Agencies: The SEC View Point, *Law and Investment Journal*, Vol 1, No7 {007}pp. 33-39.
[986] Leo-Sun 'Why is Corporative Government Important, available at: www.business dictionary.com/article.
[987] *Ibid*.

deviance.Corporate governance plays a vital role in underpinning the integrity and efficiency of financial markets.

Recent financial crisis and enterprise collapse across the globe[988] reinforce the need and imperative of corporate governance on the socio-economic life of any nation. It is true that a company is an artificial entity, with all the rights and powers of a natural person of full capacity conferred upon it by law, however, it was not the intention of Lord MacNughten (or indeed statutory codification of those principles) in laying out this principle in the locus classicus of company law – the old case of *Salomon v Salomon Co Ltd*[989], that there should be a total extrication of the importance of human behaviour in the management of these entities created by law.[990]

It is the socio-economic nexus between management behaviour and company administration (or maladministration) that has brought out the subject – corporate governance. The 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.[991]

Juan Elegidooutlines the essence of corporate governance and the need for ethical business thus:

i. It enables members to live good lives in the real sense.

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[988]And its aftermath.

[989] {1897}Ac 22; 45 WR 193.

[990] F. Ajogwu, SAN, 'Corporate Governance and Ethical Business Dealings in Nigeria: The Imperatives', *Businessday*, Thursday 21 February 2013, p. 12.

[991]*Ibid*.

ii. It is an easy way of acquiring good business reputation within its business environment.

iii. Helps in winning the trust of stakeholders (shareholders, customers, employees, creditors, tax authorities and society).

iv. It avoids social discord, by fostering among employees an attitude of commitment to firm's interest.[992]

As the nation marches forward in her vision to become one of the top 20 economies by the year 2020 as envisioned in the financial sector strategy (FSS, 2020), one of the issues that remain unavoidable and at the front burner to build investors' confidence in domestic economy is good corporate governance. The parties to corporate governance in Nigeria are all encompassing. It includes the regulatory bodies like the Securities and Exchange Commission, the Corporate Affairs Commission, and the Central Bank of Nigerian (in the case of banking industry), etc. Other stakeholders are the chief executive officers, the board of directors, the management team, the auditors and the shareholders. There are also those who are indirectly interested in corporate governance like the customers, employees and the community at large.

All parties to corporate governance have an interest whether direct or indirect in the effective performance of the company. Directors, workers and management receive salaries, benefits and reputation, while shareholders receive capital return, and the customers receive services. In return, these individuals provide value in the form of natural, human, social and other forms of capital. Hence, the point remains that companies can make choices or decisions

[992] *Ibid*.

with respect to its governance which could have social consequences: they make private decisions which have public results.[993] Such decision could either make or mar the business, and opportunities for investors to ensure the integrity of their investment.

Good corporate governance extends beyond the basic minimum of what companies need to make decisions and create governance structure. Good corporate governance includes a much more sophisticated structure for improving decision making and creating avenues for shareholder engagement. These good corporate governance techniques may include improvements in how boards are chosen and compensated, how much information is available to the investors and the community at large, how companies identify and analyze risks including the disclosure of these risks, providing for shareholder voting on board election and management compensation issues.[994]

While good corporate governance practices vary from company to company, and from place to place, there is growing consensus on what are best practices in good corporate governance. For example, the OECD has provided a model for good corporate governance that companies can adopt. Beyond these guidelines, companies operating around the world provide useful models in good corporate governance and set the standard for other companies in respect of what is possible for corporate governance practices.[995] Good corporate governance is a culture and climate of consistency, responsibility, accountability, fairness, transparency, and

[993] J.K.Galbraith, On the Economic Image of Corporative Enterprise, in R.Nader and M. Green (eds), *Corporative Power* in America (1973) p.6.

[994] R. Adamson, Corporate Governance, Risk Management and Corporate Social Responsibility in Emerging Market: A Symbiotic Relationship, available at: www.bee/dic/sfu/ca/corporate-governance-and-risk-managment-and-corporate-social-responsibility, accessed on 22/03/2014.

[995] *Ibid*.

effectiveness (often represented by the acronym, CRAFTED) that are deployed as principles of good governance throughout the organization.[996]

7.5 The Impact of Good Corporate Governance on the National Economy

Corporate governance is an effective policy instrument in the operation of the national economy. There is an obvious link between corporate governance and the economic health of the nation. Just as good governance is a categorical imperative in the public domain, effective corporate governance is inevitable for healthy growth and development of any economy.

Oluyemi consider corporate governance to be of special importance in ensuring stability of the economy and successful achievement of banks' strategy. Corporate governance is an important framework for development, entrepreneurship and economic growth.[997] Effective corporate governance improves economic efficiency, access to domestic and foreign capital, human resource productivity and development of market economy.[998]

Sound corporate governance contributes to the national economy in the following respects:

i. Increase probity, efficiency and effectiveness of financial markets and contributes to improved risk management and better strategic direction and oversight of operational efficiency,

[996] Y. Arguden, 'Measuring the Effectiveness of Corporate Governance', available at: www.knowledge.instead.edu>Home><SR>corporate(created, April, accessed on 18/05/2014.
[997] S.A. Oluyemi, 'Banking Sector Reforms and the Imperative of Good Corporate Governance in the Nigeria Banking System', available at: www.ndic-ng.com/p of cgovbk.pp, p. 1-33, accessed on 18/05/2014.
[998] Agusto, 'Sustaining Effective Corporate Governance in a Corrupt Environment' - A Paper Presented at the Executive Mandatory Continuing Professional Education (EMCPE) of the Chartered Accountants of Nigeria.

ii. Contributes to the fight against corruption which reduces its enormous damaging effect on the national economy, especially in a corporate, self-regulatory environment like Nigeria.[999]

Given the advantages and impact of corporate governance, it would no doubt have an overwhelming impact if the principles, structures and mechanisms of corporate governance be applied widely in Nigeria, not only to public listed companies. It should extend to state enterprises, corporate and the banking sector, NGOs and to public services management such as health and education boards. If this is done, it will ameliorate the rate of corruption and the attendant damage it has caused to the Nigerian economy.[1000]

The need for corporate governance is most seriously felt in the banking sector which can be described as the life-blood of the Nigerian economy. A healthy banking system is a prerequisite for the much needed economic development in Nigeria. Apart from the fact that the banks themselves are in need of sound internal governance, they can also be pivotal to promoting sound external governance practices in the boardrooms of other companies in Nigeria. This is because in many developing countries including Nigeria, the equity markets are too small to play a strong role in the national capital markets, and therefore companies rely heavily on debt finance from their banks. There is almost no influence by institutional investors on the sound management of companies. The banks can therefore exert strong

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[999] R. Okpeahior& H.P. Faga, *op. cit*, p. 220.

[1000] A.O. Yahaya,' Corporate Governance in Nigeria: A Focus in the Public Sector, in O. Alo (ed), Issues in Corporate Governance (2003), p.15.

influence on their debtor to determine the corporate governance strategy to be adopted by their customers in order to qualify them for loan.[1001]

The far reaching impact which corporate governance plays on the Nigerian economy was clearly stated by the former Governor of Central Bank of Nigeria, Prof. Sanusi in the following words:

> Issues of corporate governance have become so pervasive in recent years and the lessons learnt from experiences of corporate organizations have become major actors in the political economy of many countries, under the current neo-liberal economic philosophy, they are regarded as the engine room of growth and development. Based on this premise the performance of these organizations is of interest to both the government and the citizens. Essentially, various measures, models and concept name have been developed globally and nationally to ensure that these corporate organizations not only survive but operate in the best interest of all stakeholders including the government.Dealing with them is so important that promoting corporate governance with its attendant challenges have become relevant and timely. Moreover, it is important to recognize that economic performance of any country is shaped largely by the quality of the effectiveness of the nation's corporate governance.[1002]

Still on the impact of corporate governance on the economic performance of the country, Sanusi further emphasized that, the impact of good corporate governance on economic performance can be appreciated when it is recognized that growth is positively related not only to the size of investment but also to the efficiency and transparency that directors and

[1001] A.O. Yahaya, *op. cit*.
[1002] L. Sanusi, 'Promoting Good Corporate Governance in Nigeria: Issues and Challenges', A Paper Presented at the 2002 Directors Seminar Organized by Financial Institute Training Centre, Nigeria on 4-6 June, 2002.

managers of enterprises carry out their duties within a framework of accountability and transparency.[1003]

As a body of principles that stipulates how companies should be effectively managed, corporate governance, no doubt, have wide impact to the national economy. It controls and monitors the roles, actions and behaviour of board members. This brings about transparent transaction for national development. Since corporate governance regulates the hiring, sacking and compensation of executives on basis of *quantum meruit*, it naturally leads to maximal selection and utilization of best managers for economic development. The functions and benefits of corporate governance are meant to serve as a strong base for capital development which in turn serves as the fertile ground for economic development. The presence of strong governance standards provides better access to capital and aids economic growth.

Since failures of corporate governance and risk management can have impacts that reach far beyond the company itself and lead to systematic or systemic harm for national economies, or even the global economy, policy makers have taken a strong interest in passing rules and regulations that ensure that companies adopt good corporate governance and risk management practices.[1004]With the recent financial crisis as a new catalyst, policy makers across the globe have been identifying ways in which corporations need to do a better job of

[1003]*Ibid*.

[1004] R. Adamson, Corporate Governance, Risk Management and Corporate Social Responsibility in Emerging Market: A Symbiotic Relationship, available at: www.bee/dic/sfu/ca/corporate-governance-and-risk-managment-and-corporate-social-responsibility, accessed on 22/03/2014. Robert Adamson is the executive secretary, Risk Management and Corporate Social Responsibility in Emerging Markets Centre of Corporate Governance.

corporate governance[1005] as good corporate governance is very important for sustainable development, not only for the individual company but the economy as a whole.[1006]

7.6 Corporate Social Responsibility (CSR) and the Community

Corporate Social Responsibility (CSR), also corporate conscience, corporate citizenship, corporate performance, or sustainable responsible business, is the responsibility shown by a company (or other organization) for matters of general concern to the society in which it operates such as protection of the environment, health and safety and social welfare.[1007]

The World Business Council for Sustainable Development, defined CSR as the continuing commitment by business to behave ethically and contribute to economic development while, improving the quality of life of the work force and their families as well as the local community and society at large.[1008] The principles of CSR demand that a company deriving a utility from a community should respond positively to the problem of that community.[1009]

The Ecumenical Committee for Corporate Responsibility (ECCR) defined CSRs as being concerned with the ecosystem, that is the environment in which the business operate, the national communities in which the business is developed and sustained; local communities which are 'hosts' to companies and industries; the employees who provides the labour; and

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[1005] *Ibid*.

[1006] Y. Arguden, 'Measuring the Effectiveness of Corporate Governance', available at: www.knowledge.instead.edu>Home>CRS>corporate, accessed on 18/05/2014.

[1007] O. Busari, Corporate Social Responsibility, being a paper delivered at the Advanced News Journalism Sub-Editing Media law Course conducted in Dubai by Foreign Corporate Training Limited (FCTL), UK.2012.

[1008] A. Balogun, 'Nigeria: Corporate Social Responsibilities', a paper delivered to the Section in Energy and Natural Resources at the Law of International Bar Association, 2001.

[1009] L. Holme and R.Watts, 'Corporate Social Responsibility: Making Good Business Sense, a paper presented at the World Business Council for Sustainable Development(WBCSD) meeting at Geneva, Switzerland, January 2000. The WBCSD is a major driving force in the concept of CSR, and was established in January 1995. The WBCSD is an association of over 140 international companies drawn from over 30 countries representing more than 20 industrial sectors.

the customers, suppliers and contractors who feel the impact of the company's activities in many differing ways.[1010]

CSR is a form of corporate self-regulation integrated into a business model. CSR policy functions as a built in, self-regulating mechanism whereby a business monitors and ensures its active compliance with the spirit of the law, ethical standards, and international norms. The goal of CSR is to embrace responsibility for the company's actions and encourage a positive impact through its activities on the environment, consumers, employees, communities, stakeholders and other members of the public.[1011]

A fast establishing trend in the business world is the evolution of corporate social responsibility packages by multinationals and other corporate bodies. This is not unconnected with public outcries over the adverse effect of day-to-day business activities, how it affects the environment, the economy and the lives of the host communities.Corporate social responsibility is a set of standards to which a company subscribes in order to make its impact on society. It has a potential to contribute to sustainable development and poverty reduction, and to cater for the vulnerable and senior citizens as well as contributes to national economy and private enterprise. This in recent times is fast becoming an apology medium for vagrant

[1010] The Ecumenical Committee for Corporate Social Responsibility (ECCSR), Principles for Global Corporate Responsibility: Benchmarks for Measuring Business Performance (Fareham Hants, England: Bumhamwood, 1995).The Ecumenical Committee for Corporate Social Responsibility (ECSR) began work in 1993 to create benchmarks for measuring corporate responsibility globally in 1995. ECCR launched a set of agreed principles on corporate social responsibility.

[1011] O. Busari, *op. cit*, p.2.

abuses of social responsibility and protection of the environment in the scramble for maximizing profits.[1012]

Proponents of CSR argue that corporations make more long term profits by operating with a perspective, while critics argue that CSR distracts from the economic role of business. Others argue that CSR is merely window-dressing or an attempt to pre-empt the role of government as a watch dog over powerful multinational corporations.[1013]

Major issues of CSR vary from one company to another according to its particular circumstances, but include:

i. Minimizing damage to the environment and promoting sustainable' business development
ii. Having liberal employment policies
iii. Investing money in local communities
iv. Helping in fighting against crime.[1014]

Currently, CSR could be seen in the light of corporate philanthropy, corporate citizenship, community relations, community advocacy, corporate governance, accountability and transparency, corporate competence, corporate ethics, employee relations, human rights and so on.[1015]

[1012] O. Busari, *op. cit*, p.2; H. Bulkele, 'Governing Climate Change: The Politics and Risk Society', *Transactions of the Institute of British Geographers*, New Series, Vol.26,No.4,pp430 – 447(2001); and K.C.JohnWel, 'Corporate Social Responsibility - a Comparism between Vietnam and china', *International Journal of Governance*, vol.1,no.1, July 2011.
[1013] O. Busari, *op. cit*, p. 3.
[1014] O. Busari, *op. cit*, p. 3.
[1015] K. Jimi, 'The Public Sector Dimension in Corporate Social Responsibility Practice and Management in Nigeria, in L.Y. Ajayi (eds), Corporate Social Responsibility of Business: Principles and Perspectives - Ogun State, Nigeria, Institute of Public Relation Chapter, Nigeria, pp. 88-100.

7.7 Governance and Corporate Social Responsibility in Nigeria

From oil multinationals in the restive Niger Delta region of Nigeria to the telecommunications giants, drug maker, down to the consolidated banking sector, it has become a vogue to engage in highly publicized charitable and philanthropic ventures as act of corporate social responsibility to placate the abused public. Overtime, multinational companies in Nigeria simply sign agreements with indigenous governments without deference to the host communities. This is what informed the variously protracted restiveness in the oil rich Niger-Delta, as the multi- nationals for decades have continued to violate environmental rules to the detriment of host communities like Ogoniland as well as being accomplices to the brutal violation of human rights in these communities by successive civilian and military governments[1016]

When Gen-SaniAbacha hanged the frontline author and activist, Ken Sarowiwa and eight[1017] members of the Movement for the Survival of the OgoniPeople (MOSOP) against local and international outcry in 1995, oil multinationals like Shell could not exonerate itself from the complicity in the killings. This is because they failed to meet the legitimate claims of the host communities. Shell would have been deemed socially responsible if it had meaningfully provided employment and payment of royalties and compensation.[1018]

The sheer neglect of social responsibilities by most companies made Etekpe to have said that 'the multinational oil companies (MNOCs) constitute more of curses than blessings to

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[1016] P.J. Aderemi, 'Governance and Corporate Social Responsibility in Nigeria, available at: www.Nigeria.observers.news.com; Also cited in O. Busari, 'Corporate Social Responsibility, being a paper delivered at the Advanced News Journalism Sub-editing & Media Law Course, 2012 .

[1017] F. Nuante, DrBarinemKiobel (former Commissioner), NorduEawo, John Kpuinem (former Vice President NYCUP), Paul Levura, Baribo Bern, Saturday Dobe and David Kpokoo.

[1018] O. Busari, *op cit*, pp. 8-9.

the oil producing communities.'[1019]Since the Willinks Committee in 1957, several committees or panels have been set up by the federal government, the United Nations, and the United Nations Development Programmes to look into the activities of oil and gas companies in the area(s) of operation. These committees are: the Belgore Judicial Committee, 1992, Don Etiebet Inter-ministerial Fact Finding Team 1994, Vision 2010 Committee 1996, Papoola Committee 1998, OgomudiaSpecial Security Committee on Oil Producing Areas, 2001, Presidential Panel on National Security 2003, Niki Tobi National Political Reform Conference 2005, Presidential Council on the Social and Economic Development of the Coastal States 2006, UN Special Rapporteuron Human Rights Situation in Nigeria 2007, among others.[1020] Virtually all these committees recommended to the federal government, in their respective reports, that one of the ways of addressing the problems of underdevelopment, unrest and insecurity in the community of operations is taking steps with a view to creating and enforcing social responsibility.

Particularly, the Vision 2010 Report on the Up-stream sector sets out seven (7) objectives of the industry, the third objective being, to 'make community stakeholder in the successful operations of the industry.' One of the strategies adopted by the report to achieve this vision for the communities is to 'continue industry funded community development programmes.'[1021]Now, corporate social responsibility activities are gaining momentum following the promulgation of the Fiscal Responsibility Act.

[1019] A. Etekpe, 'The Politics and Conflict over Oil and Gas in the Niger-Delta Region: The Bayelsa State Experience (Porthacourt: Tower-Gate Resources, 2007), p.11.

[1020] P. Ahiarammunnah, 'Oil Companies: Legislation on Corporate Social Responsibility and Peace in the Niger-Delta, *Ebonyi State University Law Journal,* Vol.2, No 1, 2007, pp. 188-209, p.192; Section 17(2) of 1999 Constitution of the Federal Republic of Nigeria abhors the exploration of human and natural resources other than for the good of the community.

[1021] The Vision 2010 Report cited in A. Balogun, *op cit.*

Be that as it may, the corporate social world should adhere strictly to the principles of CSR.[1022] Also, it is apposite that the Nigerian government should enact laws specifically on corporate social responsibility similar to the Denmark law on corporate social responsibility which makes it mandatory for the companies, investors and state owned companies to include information on CSR in their annual financial reports.[1023]

This is necessary because the idea of CSR is new to our company law jurisprudence and its true basis is not entirely without question. It can be rightly argued that under the Nigerian company law (and as in some jurisdictions), a registered company can only engage in and apply its funds for businesses that are authorized by its objects clause in the memorandum of association. It was therefore seen to be ultra-vires a company to apply its fund[1024] or resources for social, political[1025]or charitable purpose except such be justified as being in the interest of the company and to promote its prosperity.[1026]

The possible exceptions to this rule are where the company's objects expressly permits the use of the company's resources for a specified purpose without any reference to the relevance or utility of the expenditure to the company's prosperity[1027] and where the company, being a charitable organization applies its fund for charitable purpose. Short of these, charity has no place in the normal running of a company's affairs qua charity,[1028]and

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[1022]As part of international practices.

[1023] Danish Centre for Corporate Social Responsibilities, official website-CSR.gov.DK. The Denmark law was passed into law in December 2008 and became effective on 1st January 2009 .the requires companies, both public and state owned companies to provide information on CSR in their annual reports.

[1024]*Asbury Railway Carriage and Iron Company Ltd v Riche* (1875) 7 H.L., 613; Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria (LFN) 2004, s. 27(1)(c).

[1025] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria (LFN) 2004, s. 38(2).

[1026]*Hutton v West Cork Railway Company* (1883) 23 Ch.D, 654.

[1027]*Charter bridge Corporation Limited v Lloyds Bank Limited* (1971), Ch 62, *Re Holsley and Weight Limited* (1982) Ch. 442.

[1028]Per Bowen L.J. in *Hutton West Cork Rly Coy*, *supra*.

as such, the view which has been expressed by a commentator[1029] that the Nigeria Companies Act requires that companies must cater for interests other than those of their shareholders is clearly erroneous. There is no obligation on a company to act as a good citizen or with an altruistic sense of responsibility toward the community. This has however, been made possible because the objects clause of companies these days is framed so widely as to permit the directors to engage in any business or activity which will promote the interest of the company. If a company should thus expend its fund or resources voluntarily for the purpose of improving its area of operation or the community of business, there will be no difficulty in holding the expenditure *intravires*.[1030] This also agrees with Dahl's claim that every large corporation should be thought of as a social enterprise, that is, as an entity whose existence and decisions can be justified only insofar as they serve public or social purposes.[1031] Social responsibility in this sense reflects an increased sensitivity to the impacts of the company's activities to third parties, or a corporate concern with social issues more generally without any necessary implication that a divergence from the profit goal is involved. Social responsibility in this sense may have a neutral effect on profits, or may even lead to an increase in profitability in the long run. It may, for example, have a beneficial effect on the company's reputation with customers and potential employees.[1032] In the English case of*Evan vBrunnes, Mond and Co Ltd,*[1033] the shareholders passed a resolution authorizing the directors to make donations up to a total sum of £100,000 'to such universities, or other scientific institutions in the United Kingdom as they may select for the

[1029]J.A M. Agbonika, 'Social Responsibility of Companies in Nigeria', Ahmadi Bello University Law Journal, vol. 1 (1983).

[1030] A.O, Osunbor, 'Corporate Social Responsibility Towards the Environment', in J.A. Omotala, (ed) Environmental Land in Nigeria I including Compensation, (Lagos: Unilag Faculty of Law, 1990) p .82.

[1031]R.A Dahl, 'A Prelude to Corporate Reform', *Business and Social Reviews*, (1972).

C. Njason (ed), The Corporation of Modern Society (1959) 25, in J.E Parkinson, Corporate Power and Responsibility, Issues in the Theory of Company Law (New York: Oxford University Press, 1993) p. 23.

[1032] J.E. Parkinson, *op. cit*, p. 261.

[1033](1921) 1 ch. 359.

furtherance of scientific education and research.’ The company was involved in the manufacture of chemicals, and the directors hoped that, by making appropriate donations, the company might in due course benefit from an enlarged pool of trained personnel from which to draw staff. The resolution was challenged by a shareholder who contended that it was the community at large that would be the true beneficiary, and that the company, as part of the community, may derive some remote and more or less insignificant benefit but a benefit out of all proportion to the cost. He contended that the transaction cum resolution be rendered *ultra vires*. This contention was rejected and the court held that the resolution was valid. It accepted the view of the directors, there being no evidence to the contrary, that the advantages to the company were likely to be substantial, and not ‘too speculative or too remote.’ The resolution was accordingly *intra-vires*.

However, corporate donations to political parties and other related bodies would be better described as ‘political activism’ than ‘social activism’. In the case of political donations, identifying a (legally acceptable) benefit to the company may be difficult than where the involvement is with some social clause. The public relations argument is problematic, since the advantages of being associated, in the public mind, with a political party are dubious. If the party is elected and implements polices favourable to the company, the company will clearly be benefited, but any connection between the benefit and the donation would surely be extremely speculative and remote. Possible benefit to the company by way of quid pro quo would be tainted with corruption and so could not be relied upon in support of a gift.[1034]

[1034] J.E. Parkinson, *op cit*, p. 275.

In the English case of *Simmonds vHeffer,*[1035] the company, the League Against Cruel Sports Ltd, an organization formed to oppose crudity to animals, had made two donations to the LabourParty. One was to the party's election campaign fund generally, the other to help finance publicly for the party's manifesto commitment to make certain sports illegal. The latter was held to be valid as furthering the league's object of opposing cruelty. The gift to the LabourParty generally, however, was held to be *ultra vires* on ground that it contravened an implicit prohibition (inferred from the objects clause) on spending money for purposes 'alien' to the company's stated objects.

In our jurisprudence, the position is clear on this. Accordingly, the Act provides as follows:

> A company shall not have or exercise power either directly or indirectly to make a donation or gift of any of its property or funds to a political party or political association, andin breach of the subsection makes any donation or gift of its property to a political party or political association, or for any political purposes, the officers in default and any member who voted for the breach shall be jointly and severally liable to refund to the company the sum or value of donation or gift and in addition, the company and every officer or member shall be guilty of an offence and liable to afine equal to the amount or value of the donation or gift.[1036]

7.8 Modern Dimensions of Corporate Social Responsibility (CSR)

In recent years, company law scholars and business managers have advocated different approaches to CSR, thus:

[1035](1983) BCLC, 298.

[1036] Companies and Allied Matters Act, Cap. C20, Laws of the Federation of Nigeria (LFN) 2004, s. 38(2). The above section is applauded because outside political donations, the recipients of corporate support are diverse and not lacking, with education, medical and health community projects, etc at the forefront. Hence, donations to political parties are needless.

i. Duty to shareholders
ii. Duty to employees
iii. Duty to consumers
iv. Duty to stakeholders and
v. Duty to society as part of CSR[1037]

Duty to Shareholders

Since the owners of any corporate business firm are the shareholders, corporate directors and officers have a duty to act in the shareholders interest. Corporate directors and decision makers are regarded as trustees of the shareholders' funds. Because of the nature of the relationship between corporate directors and the shareholder/owners, the law holds directors and officers to a high standard of care in business decision making.

Traditionally, it was perceived that this duty to shareholders took precedence over all other corporate duties and that the primary goal of corporations should be profit maximization. Still today, some observers claim that profit maximization is a corporate primary duty. MlltonFriedman, the Nobel Prize winning economist, effectively phrased this view thus:

> In a free enterpriseprivate property system, a corporate executive is an employee of the owners of the business (shareholders). He (or she) has direct responsibility to his (or her) employers. That responsibility is to conduct the business in accordance with their desires, which generally is to make as much money as possible while conforming to the basic rules of society both those embodied in law and those embodied in ethical custom.[1038]

Duty to Employees

[1037]R.L. Muller and G.A. Jents, *Fundamentals of Business Law*, third edition, (St. Paul. minneapouls, West Publishing Co.) p.41.
[1038] M. Friedman, Does Business Have Social Responsibility?' *Bank Administration*, April 1971,pp. 13-14, in R.C. Miller and G.A Jents, *op.cit*, p.36.

One of the primary concerns of every employer is the ability to control the workplace environment. After all, it is the employer who is responsible for making the business firm a success, and success requires qualified, competent, loyal employees and efficient operations. But employees also have concerns. They want to earn a fair wage; they want to work in an environment free of health-endangering hazard, they want to be treated fairly and equally by their employers and in recent years, they want employers to respect their personal integrity and privacy rights.[1039]

Duty to Consumers

Many people believe that the corporation has an ethical duty to look beyond profit maximization to the welfare of consumers. To a certain extent, product liability laws, and other laws protecting consumers help to ensure that corporations will indeed market only products that are safe to use or consume. But there is a large 'gray area' in which marketing (in the case of marketing companies) a certain product may be legal but would be considered unethical. For example, suppose a corporation produces a type of babies that babies like and mothers buy but that is not nutritionally satisfactory for babies because of high sugar content etc. It would not be illegal to market the food, even though it might be unethical to do so.[1040]

Duty to Stakeholders

In recent years, some business managers have advocated a stakeholder view of corporate social responsibility. From this perspective, the links established by a business firm to its employees, customers, supplier and local communities may balance or even outweigh the

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[1039]R.L. Miller and G.A Jents, *op.cit*, p.37.

[1040] This is so because it has passed the legal test, unless there is legislation to the contrary. See R. Miller and G.A. Jents,*op.cit,* p.39. See also the English case of Campbell v Bil Corp (1992)586, N.Y.S.2d.871.

firm's duty to its shareholders. For example when bad management or unethical behaviour causes a firm to lose profits and eventually go out of business, the shareholders would of course be affected, but so would the welfare of the other above mentioned groups. Consider another example - a heavily indebted corporation is facing imminent bankruptcy/insolvency. The shareholder/investors have little to lose in this situation because their stock is already next to worthless. The corporation's creditors will be the first in line for any corporate asset remaining. In this situation it is the creditors who have the greatest 'stake' in the corporation, under the stakeholder view.Corporatedirectors and officers should give greater weight to the creditors' interests than to those of the shareholders.

Those who advocate a stakeholder view of corporate responsibility implicitly base their argument on a duty based on ethical standard: corporations have an ethical duty to consider the fate of these other groups, most of which are external to the corporation itself, when making decisions that significantly affect these groups.[1041]

Duty to Society

Most people concede that a corporation should be concerned not only with the welfare of its employees and the consumers of its products, but also with the welfare of the community in which it operates or society in general. But people have different ideas how corporations can best enhance social welfare.[1042]

The world over, progressive opinion now recognizes the need for broader accounting by corporation, encompassing social performance (in addition to its responsibilities towards

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[1041]R.L.Miller and G.A Jents, *op. cit.* p.40.
[1042]*Ibid*.

customers, employees and shareholders). Hence a company[1043] has, as its vision statement, to be successful.We have to provide a balance to the needs of all four of these groups (customers, employees, shareholders and the society). If we maximize the return to any one or two of these stakeholders groups at the expense of the others, we won't survive very long.[1044]

Even if some companies and their management are not convinced on the merits of CSR as a business strategy and an integral practice of good corporate governance, companies should remain open for further considering and evaluating the importance and benefits of CSR.More and more academic studies and company case studies are illustrating that these CSR policies bring significant benefits for the company and assist it in managing reputation risk, improving relationship with stakeholders and improving the company's corporate governance procedures.[1045]

[1043] See the vision statement of Duo company (a foreign company

[1044] P. Ravindran, Importance of Good Corporate Governance, *Hindu Business Line,* Saturday July 01,2000.

[1045] R. Adamson, Corporate Governance, Risk Management and Corporate Social Responsibility in Emerging Market: A Symbiotic Relationship, available at: www.bee/dic/sfu/ca/corporate-governance-and-risk-managment-and-corporate-social-responsibility, accessed on 22/03/2014.

CHAPTER EIGHT

FINDINGS, RECOMMENDATIONS AND CONCLUSIONS

8.1 Introduction

As good governance is categorically imperative in every institution. Effective corporate governance is a desideratum for the healthy growth and development of any economy which is controlled by private individuals as its organ. It has been observed that the development and financial growth of every company is dependent upon the effectiveness of the corporate governance. This is provided with lots of legal frameworks which help to guarantee accountability, integrity, transparency and adequate disclosure of information, where accurate disclosure of financial statement is made to the investors as well as information regarding the structure and mode of operation and financial status of an investment outlet. This is because the investors are always in search of safe haven for their investment. They want to be sure that the information and disclosure in the financial statements is a true reflection of the worth or state of affairs of the corporate institutions in which they invest.

Similarly, it contributes to combat against corruption which has permeated all facets of the economy. As observed earlier in this research, the sanction of some top bank managers on issues of corruption is a clear effort usually anchored in the legal framework to foster the development and enforcement of corporate governance in Nigerian corporate institutions.

Furthermore, the health of the economy as well as effective running of corporate institutions is dependent on the sound legal framework for the corporate governance, by means of supervising and regulating corporate institutions to ensure that the investors vis-à-vis the corporate institutions are protected against available or foreseeable losses. This thereby strengthens the confidence of the investors and financial system of the company, promoting the smooth operation of payments system, and avoiding systematic failure or collapse by the

corporate institutions. Effective corporate governance thus promotes improved shareholder wealth and the wealth of other corporate stakeholders.

Moreover, the objective of the corporate governance regulation and supervision is wholly derived from the Companies and Allied Matters Act and other legal instruments, which promotes monetary stability and financial system of the company. For example in the Banking sector, different bodies and statutes such as CBN, NDIC, BOFIA etc play vital role in the supervision of the banking institution. They try to ensure that monetary and payment system in the financial institution is not impaired. They also promote the monetization of the economy, and protect customer’s interest and depositors. The objective of the bank and other corporate institutions supervision and regulation is to guide against corporate failure and collapse and rip from the bud all that can be a causal effect to corporate instability.

8.2 Observations

It is a worthy observation that there are ample measure of legal frameworks in Nigeria, but the aim is impaired by lack of sufficient enforcement or implementation mechanism to ensure total compliance with the different laws, rules and codes setup to guide the activities of these incorporated companies. This is a bewildering factor that seriously hinders a robust corporate governance. This is discernible from various observations that governance principles have always been a part of our corporate laws in Nigeria, but the problems remain that no significant attempt has been made to enforce or redress a breach of any of the principles probably because of the ignorance of those in the helm of affairs in corporate institutions who view any challenge as a threat and hostility from the ‘enemy’.

It is also a matter of great concern as observed that due to the recent occurrence in the international corporate edifice the world/corporate institutions have focused attention to the concerns for effective domestic corporate governance initiatives that would enhance

credibility on the manner corporate institutions conduct business in the post modern globalised world.

In a related development, it is observed that no corporate institution is beyond collapse or failure; however, failure can be prevented if effective corporate governance is practised. Hence the neglect of good corporate governance practices comes with far reaching effects and losses incurred by the innocent shareholders and the prospective client.

It is my humble observation that in the past, experience has shown that lack of proper and effective governance framework in Nigeria has been exploited by senior managements of the corporate institutions to the detriment of other shareholders. The recent shake in the Nigerian Stock Exchange brought to fore some of these practices by capital market operators and corporate entities alike.

The collapse or near collapse of almost 8 banks with estimated total of 35% of the industry's total deposit brought to fore the effect of corporate collapse in the community. The governor of Central Bank of Nigeria (as he then was), Mallam Sanusi Lamido explained that five out of eight banks got distressed as a result of poor corporate governance. Of course, one cannot forget the extent of sinister effects of fraud and poor practices/management that contributed to the collapse of Savannah Bank Plc which led to the revocation of its licence. Therefore there is a need for proper governance, and corporate governance principles assume greater proportion because of the wide reaching effects of the consequences.

However, apart from the corporate institution, the community and the society at large, all suffers in no small measure in the event of corporate collapse. This is because corporate governance is all about performance strengthened by the appropriate legal framework. Proper

governance of the corporate institution has become crucial to the world economy and has wide reaching benefits.

It is important to add that the availability of legal framework on corporate governance, has recently helped in the proper conduct of affairs of the corporate institution and this has helped to prevent corporate failure and collapse. With this stability in the corporate institution, job opportunities are created.The available jobs so secured impart on the lives of the entire Nigerian communities and beyond, as both nationals and foreign investors will readily be attracted to the corporate institution, and this will generate revenue to the government, infrastructure development, academic development cum scholarships, e.g. P.T.F. contributions to the Higher institutions of learning, as well as employment to the people, making the community a better place.

In contrast to the retrenchment and unemployment generated by the CBN's policy and reform on the banks, logistics have it that in Oceanic BankPlc, about 1,500 workers were retrenched while at Intercontinental Bank Plc, approximately 3,000 workers were retrenched. However, the defect discovered is the problem of enforcement of legal framework on corporate governance to ensure more benefit to the Nigerian communities at large. The burden then, falls on the regulatory organs such as the CBN, CAC, SEC, etc to ensure proper supervision and adequate regulation of the corporate institutions in the perspectives of the law.

It was discovered that there is no universally accepted model for good corporate governance which every company and other corporate institutions must adopt in other to ensure good, proactive and sustained corporate governance. Moreover, it was discovered in the course of the research that there are no effective and proactive enforcement mechanism specifically meant to ensure that companies and other corporate bodies strictly adopt good corporate

governance, as issuing the codes of corporate governance alone is not enough without adequate enforcement.

Again, it was also discovered that the historical development of corporate governance largely involves making or enactment of rules or codes in a bid to regulate corporate bodies in order to ensure good corporate governance within the various jurisdiction studied in this research. More so, in the course of the research, it was discovered that corporate governance is not only felt in companies and other corporate bodies but also in any organization, association or even groups that is not a one man affair wherein rights, duties and obligations are obtainable.

Notably, a critical research on the history of corporate governance in the three countries studied in this research reviewed that their histories have close ties with each other in many ways especially as they all engaged in similar regime in the development of their corporate governance by means of enactment of codes.

Recent financial crises and enterprise collapse across the globe (and their aftermaths) reinforce the need and imperative of corporate governance on the socio-economic life of any nation. Notably, compliance with legal mechanisms is inadequate as it lacks the moral firepower to restore confidence and the ability to build trust. The tendency to over-emphasize legal compliance mechanisms may result in an attempt to substitute accountability for responsibility and may also result in an attempt to legislate morality.

From an ethical dimension, at a fundamental level, the key issue of corporate governance involves questions concerning relationship and building trust both within and outside the organization. While many of the governance issues that organizations face are not new, the environment in which they confront them is more challenging than ever in Nigeria. For instance, one cannot possibly comment on the quality of the governance structures in the

public domain whose government actions affect the entirety of the nation without mentioning the menace of corruption. As such, corporations in such economy cannot but be influenced by the governance outfit of the public sector.

Indeed, no doubt that the heightened awareness of the need for effective corporate governance is not without justification. Well implemented corporate governance and risk management has tremendous benefits. The benefits are the enduring attributes of corporate governance. In the first place, effective corporate governance backed up with adequate monitoring and enforcement, would build investors confidence, eliminate financial scandals and curb corporate failures.

However, notwithstanding these measures and its intending benefits, it has been observed from the study of the concept of corporate governance and risk management that it has been seriously hampered by the dearth of institutional capacity and professional will to ensure enforcement irrespective of a national code of conduct by the incorporated companies. Lack of observance of these codes of conduct by the incorporated companies has increased the unscrupulous activities by some shareholders which hamper the growth and sustenance of corporate governance.

The issue of dearth of effective monitoring and supervision of the activities of the board of directors and other stakeholders especially the shareholder tends to hamper the growth of the business of such a company. This is because where the unscrupulous activities of the board of directors and the management team of the company is not monitored and supervised effectively and efficiently, it will surely lead to corporate collapse.

We also observed that in some of these incorporated companies, they are no well trained and qualified directors and personnels that pilot the affairs of these companies. This is pertinent given that the choice for the appointment of the members of the board of directors and other personnel may be motivated by personal interest and benefits especially by those having or holding the most aggregate number of shares in the companies.

8.3 Recommendations

The survival and stability of any corporate institution depends, to a great extent, on the quality of its governance. Inspite of the available legal frameworks to strengthen the arms of corporate governance, corporate institutions were still susceptible to collapse and failure. The loss inherent in this collapse is enormous on the dignity and growth of corporate institutions and stakeholders. It is therefore recommended as follows:

i. Government should put in place strong corporate governance legal framework that improves and enhances compliance and that will adequately sanction the non compliance to corporate governance codes.

ii. The benefits of corporate governance to the Nigerian companies and the community in general cannot be over emphasised. However, these benefits can only be realized when the basic principles of corporate governance are observed in companies. This is made possible where the interest of the managers and stakeholders are properly aligned. Review of literature showed that both the market and non-market mechanisms could be used to promote the alignment of the interest of managers and stakeholders. What this means is that corporate governance revolves around ownership and control. Given the potential separation of ownership from control, various mechanisms are imperatively needed to align the interest of principal and agent. For instance, the shareholders maximize returns at the reasonable risk, focusing on a high dividend and the rising stock prices. Managers on the other hand, may

possibly prefer growth to profit, may be lazy or fraudulent and may maintain costly labour of product standards above the necessary competitive minimum. This agency costs is because shareholders face problems in monitoring management. They have imperfect information to make decision, contractual limits to management discretion may be difficult to enforce and shareholders confront free-rider problems when portfolios are diversified. There should therefore, be a medium within the corporate institution to make possible and more realistic the interests of the managers and stakeholders of the corporate institution to be in term with proper information disclosure. Therefore, a proper system of accounting and auditing of internationally acceptable standard should be put in place by the government in consultation with the relevant accounting body. This will reduce sinister effect of fraud within the corporate institutions.

iii. Furthermore, there should be avenue to ensure that the legal frameworks on corporate governances is put into practice. This is because investors with their hard earned investment seek to invest their capital in profit making firms so that they can enjoy the profits in the future, although many investors lack the time and expertise necessary to operate a firm and ensure that it provides an investment return. As a result of these, investors hire individuals with the management expertise to efficiently run the company on a daily basis to see to it that the company's activities enhance its profitability and long term performance. It affect the value of the corporate institution and such actions are capable of making the institution susceptible to failure and financial vulnerability. Hence a great need to fight against it.

iv. Within the corporate institution, a manager has the incentive to monitor the behavior of other managers whether subordinates or superiors. We are of the view that since corporate institution is the market for new managers and the reward-system should be

based on the performance; so as to attract good managers or even to retain the already existing ones. Of course, if this is imbibed by the corporate institution, it is fervently hoped that, it will attract public patronage and even prospective investors. It will also enhance the transparency and hard working amongst the directors as one will be diligent in his duty, knowing full well that such a director is under close surveillance and will be rewarded accordingly. The problem should be how can this view be realized? It is humbly recommended that in addition to other rules and subject to the CAMA, the company should, through its articles of association, formulate a strategy to put this into practice. It could be by way of internal review, the ethics of the company notwithstanding.

v. In the same vein, corporate governance mechanisms assure investors in corporate institution that they will receive adequate returns on their investments. This corporate governance mechanism should be properly maintained as it assures the investors or shareholders of the confidence to keep on their investment in the company. Also the views of Shleifer and Emmons are worthy of recommendation. In giving credence to this view, they maintain that if the mechanisms do not exist or fail to function properly, outside investors would lend to the corporate institution or buy their equity securities.

vi. Now that corporate social responsibility activities are gaining momentum following the promulgation of the Fiscal Responsibility Act, the corporate social world should enact laws specifically on corporate social responsibility similar to Denmark law on corporate social responsibility which makes it mandatory for the companies, investors and state owned companies to include information on CSR in their annual financial reports

vii. Considering the overwhelming importance of good corporate governance to the development of the economy of any nation, it is recommended that a well defined and effective enforcement mechanism is adopted to ensure a strict adherence to the established codes of good corporate governance for companies and other corporate bodies both private and public. This may be by way of establishing an agency with the sole responsibility of enforcement and supervision to ensure strict compliance with the code of good corporate governance.

viii. It is also recommended that a uniform code of best corporate governance practice should be adopted. Here, all the relevant stakeholders in the system such as the Central Bank, the Security and Exchange Commission should come together for proper harmonization in order to achieve this fit.

ix. It is my humble recommendation also that public lectures should be organized for universities, organizations, co-operative societies and the public in general by the relevant stakeholders in order to properly educate and acquaint them on the importance, impacts, history and the content of code of best practice of corporate governance. All these should not be documented in big books and journals alone, they should be made known to the people.

x. The government should device workable means in ensuring that companies live up to their corporate social responsibility as part of corporate governance, for example, by making it a mandatory requirement through legislation. Effective mechanism should be developed to ensure total compliance with the necessary laws, rules and codes that regulate the activities of these incorporated companies.

xi. It is recommended that an effective monitoring and supervisory committee should be set-up to oversee and monitor the extent of compliance to these laws, rules and codes. The duty of such a committee should also extend to the point of supervising or

monitoring how they have complied with code for corporate governance and risk management. The mandate of this committee should also extend to the fact collating corporate governance related data and constructing the relevant indices to facilitate corporate governance research in Nigeria.

xii. It is recommended that there should be a report for shareholders by the management of the company, at the annual general meeting, on the general state of corporate governance in the company in question.

xiii. Moreover, it is recommended that public policy responses to corporate governance failure should be strategically formulated to ensure corporate vitality and minimize market failure.

xiv. It is further recommended that there should be an established professional qualification for board members as a means of ensuring high level of professionalism and competence in the control and management of the business of the companies since they are regarded as the key to the survival of the company.

xv. Given that financial reporting and auditing are instrumental to the practice of good corporate governance, it follows that the following needs to be done for a better practice to emerge:

  a. Awareness should be raised for investors, directors, managers and auditors to improve the degree of compliance with financial reporting requirements especially by publicly traded companies

  b. There should be a statutory framework of accounting and auditing to protect the public interest.

  c. Government should establish and strengthen an independent body to monitor and enforce accounting and auditing standard and codes.

  d. Sanctions for violations shall be enforced.

e. Strengthening professional education and training.

f. Strengthening the capacity of the regulatory bodies and review adequacy of statutory enforcement provisions.

8.4 Conclusion

Management of the affairs of the company is vested on the organs of the company, the Board of Directors and the members in general meeting. The members in general meeting is the supreme legislative authority of the company, the directors are, subject to the Articles, vested with the power of managing the company on behalf of the shareholders. The members in general meeting and board of directors are organs rather than agents of the corporate institution. The concept of corporate governance is basically about how the affairs of the corporate institutions are run by the organs to prevent corporate failure or collapse.

However, collapse or failure in the corporate governance poses a gross threat to the success and posterity of every corporate institution and community in general. The legal framework is conceived to forestall the collapse or failure of the corporate institutions, yet they still collapse and fail. This incidence of collapse adversely affects the investors' confidence. As shown earlier in this research work, adherence to the principles of corporate governance, corporate social responsibility, and stakeholder theory are designed to inhibit failure and collapse of corporate institutions in Nigeria. Effective corporate governance based on core values of integrity and trust, will apparently have competitive advantages in retaining 'talent' and thus, generate positive reactions in market place. Similarly, if one has a reputation for ethical behavior in today's market place, it will foster both the customers and the employee's loyalty, including the investors will be attracted.

This effective corporate governance can be achieved by adopting a set of principle and best practices. A great deal depends on the core values of fairness, honesty, integrity and good ethics which the corporate institutions imbibe in their affairs. Certainly, corporate institutions must make profit in order to survive and grow, but that should not defeat the sanctity of the corporate governance. Therefore, the pursuance of profits must be confined within the ethical bounds. Ethics as well as behavioural governance is purely an essential ingredient for business success and of course, this will serve as a cornerstone for the success of corporate institution as mere black letter methods/ models have failed us. It is therefore more important to set strong ethical principles for a sustainable development for more efficiency and consequent positive impact on the Nigerian community.

It is an indisputable fact that good corporate governance is a veritable instrument not only for a sustainable economic development but also for ensuring a better and improved socio-economic life of the people. Corporate governance does not only prevent tyranny, fraud and failure, it promotes accountability, transparency, equality and protects the interest of all stakeholders in any given company or other establishments. As the country moves towards becoming one of the top twenty economies in the world by the year 2020 in the midst of the current world economic crisis, insecurity as a result of the deadly Boko Haram insurgence and the high level of unemployment, Nigeria must adopt and implement policies that will always encourage good and effective corporate governance practices in order to achieve such a laudable big dream.

The significance of corporate governance cannot be over emphasized as it creates the necessary organizational setting for the internal operations of a business enterprise. Today, the society and government are demanding more from business than just declaring profit and paying tax. Today’s business must be socially responsible, morally upright, transparent and

accountable in its behaviour and activities. It was also noted that where there is effective and efficient corporate governance in business institutions, it will help to manage business risk since all the stakeholders are assumed to be up and doing especially as regard the financial auditors and directors in the risk management. When a risk is properly managed, it boosts business and therefore enhances and increases business opportunities for creditors and investors to explore.

Further, for a robust corporate governance to be achieved, there must be corporate communication mechanism which should be able to gather, analyze and disseminate the views and perspectives of all shareholders and a regular reports by the board to the shareholders on the general meeting on the state of corporate governance. While government is urged to put up more effort in terms of enforcement of the laws and codes to ensure total compliance by these companies, it is our hope and expectations that they will meet up with their corporate social responsibilities as expected. It is therefore concluded that failure in corporate governance is a real threat to the future of every corporation and by extension, the economy of the country. With effective corporate governance based on core values of integrity and trust, companies will have competitive advantage in attracting and retaining talents and generating positive reactions in the market place. Effective corporate governance can be achieved by adopting a set of principles and best practices. A great deal depends on integrity, trust, fairness and the manner in which companies conduct their affairs. So much also depends on the sufficient legislative framework as well as the implementation and enforcement mechanism put in place to facilitate and enhance the observance of corporate governance principles. Companies should also adopt policies that can include environmental protection and ethical training of its personnel. This will assist in building corporate image and reputation, gain loyalty and elicit trust from the public. In this way, good corporate governance would have been affirmed to tremendously improve on the performance of

companies as well as other corporate institutions. Invariably, more earnings and returns shall avail the shareholders, and enhanced services and values shall be at the disposal of other stakeholders. The cumulative and incidental impact will be an improved socio-economic well-being of the community of operation in particular, the Nigerian society and the global community in general.

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