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Corporate Governance Code: The Application and Effect on Sustainability of Selected Insurance Companies in Nigeria

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Abstract

Corporate governance as a concept operates on expectation placed on organisations to have in place processes which will promote, ensure and encourage accountability. This paper sought as its essence, to examine corporate governance code and its effect on sustainability of selected companies in the Nigerian insurance industry. With the aid of a cross-sectional survey and a structured questionnaire, the study sampled a population of 238 employees with responses was gotten from 165 accounting for about 70% response rate which were utilised. The study employed regression analysis in order to ascertain and establish the relationship existing between both the dependent and the independent variables. Study results revealed that a significant relationship exists between board size of an organisation and sustainability at ($r = 0.417$, $p < 0.05$), and with audit committee and sustainability at ($r = 0.442$, $p < 0.05$), thus accepting the alternate hypothesis. Based on the above, the study recommends that it is quite important for insurance companies to adhere to the code, also ensure that the triple bottom lone rule of sustainability is also made an integral part of the organisation.

Keywords

Corporate governance code, sustainability, audit committee, board of directors, insurance

JEL Codes: M10, M14

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1. Introduction

Insurance is a pooling of unforeseen losses through a risk transfer mechanism to insurers, who undertake to pay the insured a compensation for any loss suffered, provide financial benefits upon the happening of such losses and render relevant services to mitigate issues arising from such risks (Ubom *et al*., 2017). Insurance is recognised across the world as an important mode of protecting the economy as it provides safety net for assets and finances belonging to individuals or organisations and enables them to function effectively. Most regimes across the globe identify this and place great prominence to this sector of the economy (Irukwu, 2009). The insurance industry constitutes a major composite with potential to impact, of the finance sector in most countries across the world, Nigeria inclusive. According to Newman (2014), setting the foundation for an effective and smooth run of business activities starts and lies within insurance services as they serve as the prop of the economy and help to provide loose long-term funding which can be used to facilitate economic development and growth.

Sustainability within the business world, is the ability of an organisation to manage its' financial, social and environmental obligations properly while at the same time, harness the inherent opportunities, thus representing the capacity of an organisation to survive shock and exhibit resilience (Tascioglu, 2015). Sustainability occurs when individuals and organisations can meet their needs and objectives without adverse effect in the long run on the environment or people. In the insurance industry, sustainability can only be realised where buying conditions of insurance products gives the insured the incentive to adhere to physical risk control by either reducing or eliminating possible loss exposures (Adeyele and Maiturare, 2012). As a value, sustainability is shared by both organisations and individuals who in their day to day activities, demonstrate this value. It therefore is imperative, that these regulatory frameworks which have been constituted for supervision of organisations, to safe guard the interest of stakeholders as well as grow the economy, are adequate, efficient and thoroughly adhered to. Corporate governance code states the requirement by which companies are to be run based on certain guidelines and also require that they adhere to the rules as stipulated with respect to their board of directors, board committees, auditors, accounting principles and reporting which all have important roles to play (NAICOM, 2009). However, this study examines only two of the above requirements: directors of the board and audit committee as they have quite an impact with regards to sustainability of the company. The focus is brought on the board of directors because the code saddles them with the responsibility of monitoring the effectiveness of the corporate governance through the various committees, one of which is the audit committee and they are expected to carry out these oversight functions. The fulcrum of corporate governance on which the code exists is accountability and transparency, and the responsibility of this, lies with the directors while the audit committee has the responsibility of ensuring that the sounding panel of honesty and integrity is maintained and the ideals upheld.

1.1. Statement of problem

A common belief is that good governance does not necessarily prevent a fraud. Fresh in people's thought, is the Cadbury Nigeria 2008 issue and the Enron case of 2001 in America which were both in the news. Accountability, ensuring not only superlative run-through but also unambiguousness to all shareholders, and strengthening of checks and balances through proper adherence to corporate governance codes are some of the salient points of corporate governance. Various other research work agree that good organisational governance stretches performance in organisations and that there was a strong relationship between both variables with the attendant effect on sustainability (Garcia-Castro *et al.*, 2013; Gompers *et al.*, 2003; Grove *et al.*, 2011). The recurring issues of exorbitant management expenses in excess of premium income, excess liabilities and inability to meet claims payments amongst others by insurance companies has given rise to doubts within the stakeholders and the insuring public as to the transparency, accountability and honesty of insurance companies with respect to financial propriety.

This has made it imperative that the corporate governance code be applied in totality especially with respect to the board and the audit function so as to ensure that organisations and their finances are managed properly and duly accounted for as well as the survival and sustainability of these companies are guaranteed. However, to the knowledge of the researchers, there seems to be little work done on the corporate governance code with respect to reviewing the board of directors along with the audit committee and the subsequent influence on sustainability of insurance companies in Nigeria. This is a gap that has been observed and which needs to be researched as the insurance industry is a risk bearing entity, saddled with the responsibility of ensuring that insured clients are adequately provided for when they suffer a loss, as such, sustainability is a key ingredient and the proper corporate governance code will impact the firm holistically in terms of employees, profitability, performance, shareholders and sustainability. The study examines the affiliation existing amid the corporate governance code with specific emphasis on board of directors (BOD) and audit committee (AUDCOM) and the sustainability of insurance companies in Nigeria.

Research questions were raised thus:

(i) To what extent is sustainability of Nigerian insurance companies influenced by its board of directors?

(ii) To what degree does relationship exist between the audit committee of Nigerian insurance companies and their sustainability?

2. Literature review

The financial benefits were predominantly emphasised by early theoretical corporate governance developments. With time however, theories in governance like the stakeholder and ethical theories changed focus and started looking to safeguard the interest of other stakeholders and intensification of affluence as corporations' objective.

2.1. Stakeholder theory

The stakeholder theory premises on the view that organisations as corporate entities, serve a public purpose that is broad and they exist in the society to create absolute value (Parmar *et al.*, 2010). The theory advocates that organisation's managers, have a wide network of relationships ranging from the employee, the shareholders, business partners, suppliers and contractors (El-Kassar *et al.*, 2018). A stakeholder according to Lawrence and Weber (2014) can be said to be, everyone who has a possible effect, or is likely to be impacted by organisations activities, through having a non-market association or otherwise which could be internal or external. The stakeholder theory in the interest of all, proposes a representation on an organisation's board, all stakeholder groups for consensus building, conflict avoidance and harmonization of organisational efforts in achieving objectives (Donaldson and Preston, 1995).

2.2. Ethics theory

Discussing corporate governance and the corporate governance code without discussing ethics may seem empty as ethical theories focus on issues with regards to right and wrong, principles and rules through studying morality and application of reason. Whilst there are quite a few ethics theories, this study looks at the virtue and the business ethics theory (Abdullah and Valentine, 2009) mainly because, virtue is seen as a power that impacts within prearranged circumstances, action. Virtue ethics theory emphasises character that is virtuous, focuses on good character and moral excellence and also leads to developing a morally positive behaviour (Crane *et al.,* 2008). Business ethics theory on the other hand, addresses the rights and the wrongs of the decision making business situations, giving a new dimensional view of both traditional and modern ethics. In applying the corporate governance code within organisations, the essence of virtue ethics which influences action and business ethics which reflects issues of rights and wrongs becomes imperative as they form part of the building blocks upon which a successful corporate governance code is reliant upon for implementation.

2.3. The insurance industry

Insurance is one of the forms of risk management used by an individual or organisation to protect themselves against losses through an equitable transfer of risks from one (insurer) to the other (insured), over a stipulated time period in exchange for an agreed amount (Adeyele and Maiturare, 2012). According to Adeyele (2011), insurance in Nigeria, is very important to its economic sustainability.

2.4. Sustainability

According to Capron and Mitchell (2012), sustainable advantage is the underlying capabilities possessed by an organisation, not necessarily achieved through a set of products or market power, which it uses to create innovations and new products. In ensuring that these assets together with the competencies stay centre of scrutiny, organisations are able to recognise fundamental crack, choose the progression path which is appropriate and required in line with the gap. Within the business circle, defining sustainability can be varied as it is most often dependent on the type of business. Acknowledged widely as the definition for sustainability, the triple bottom line approach of economy, society and environment viability has emerged with the belief that to transpose it to the corporate level, it must be able to attend to the needs of the current stakeholders while still not compromising the needs of the future stakeholders (Swarnapali, 2017).

Businesses are required to adhere for sustainability purpose, to sustainable development principles which is defined as development with the strength to meet the needs now of generation present whilst endeavouring to ensure that future generations' ability to meet their own needs is not unfairly compromised (WCED, 1987). According to Porter and Kramer (2006) sustainability is an organisation securing its economic performance in the long term by avoiding environmentally wasteful behaviour that are detrimental in the short term. It is an intersection of environmental, economic and social superiority (Paulraj, 2011). In the management of sustainability tensions, ad hoc governance structures play a key role (Giovannoni and Fabietti, 2014).

2.5. Corporate governance

Described as a system, corporate governance is a means by which an organisation is properly managed, its risks monitored and assessed, its objectives set and achieved and its performance optimized (Grace *et al*., 2018). It is sometimes defined, as the mode and manner an organisation is being directed and controlled, how the board is run and constituted, and how authority is delegated (Nainawat and Meena, 2013). It is concerned with putting in place structures that will facilitate the management of an organisation to promote through accountability, long-term shareholder value and enhance organisational effectiveness and performance. It represents the framework organisations place judgements (Lakshmi and Niveda, 2016). The guidelines frame from whence an organisation is managed and board controlled so as to protect stakeholder interest (Ofuani *et al*., 2018).

2.6. The code

The corporate governance codes are a set of recommendations issued in accordance with best practice to redress observed deficiencies and improve transparency and accountability within an organisation (Gadi *et al*., 2015). Constructing corporate governance is based upon legal processes in order to ensure compliance, however, there are a few who believe that this places limits on the moral aspect. In reviewing the key elements encapsulated within the corporate governance code, a multiplicity seems to exist. In Nigeria and in the practice of insurance, approvals, requirements and sanctions regarding corporate governance is embodied in the 2009 National Insurance Commission (NAICOM) code drawn up to attend to compliance issues as well as the increasing level of societal awareness. NAICOM is responsible for supervision of the conduct of insurance business in Nigeria (Ubom *et al.,* 2017). In further quest for sanitization, the code outlined certain expectations from organisations such as the existence of board of directors, board committees and to attend to all disclosure and transparency issues as discussed below:

Board of Directors

Organisations are required to implement a corporate governance framework which is anchored on the appointment of an operational responsible board, who is responsible for the deliberate supervision of the company. The company is also expected to have a complaint board structure, requisite quality board members and appropriate number in terms of board composition. The code outlines the board's responsibilities, its conduct and states the expectation that the board effectively monitors the governance practices manage potential conflict and provide direction to management. These oversight functions are exercised through its various committees

Board Committees

The board committees are a standing requirement of the NAICOM corporate governance code. It stipulates that the board should have the following standing committees:

(i) Finance and General Purpose Committee: which has supervisory functions over finance related issues and investments as well as consideration for placements over and above certain approved limits. It also has responsibility for the review of the investment manual and approval on a periodic basis, with specific focus on new and major investment initiatives and strategies and the likely financial implication.

(ii) Enterprise Risk Management Committee: This committee has function over companywide risk management. It oversees the risk profile portfolio, underwriting functions and strategy regarding risk reward of the company as agreed by the board of directors. They it is, who are responsible for overseeing the process of identifying major risks across the company on behalf of the management, the adequacy of detection, prevention and reporting mechanism put in place as well as review large risks and confirm that reinsurance protection is adequate.

(iii) Audit and Compliance Committee: The code requires that the audit committee be headed and chaired by an independent director who will have the responsibility for reviewing data integrity and also the information which is provided in the financials. They are also required to provide oversight functions as regards the financial statement of the company, control function internally and risk management. To appreciate the importance of this committee, they are also mandated to oversee the legal compliance of the company, assess the qualification and the independence of auditors externally appointed, and other regulatory requirements.

Romano, Ferretti and Rigolini (2012), impressed the importance of board committees noting that they are very instrumental in successful application through monitoring of the corporate activities which help guard investor worth.

Disclosure and Transparency Issues

The 2009 code requires disclosure and reporting to be in accordance with the policy guidelines within the industry. This requirement of the code stipulates that annual account of company's shall disclose each shareholder information, indicate the manner of compliance by companies or deviation from the code and any contravention within the reporting period on which penalties have been paid or imposed.

2.7. Code of corporate governance and sustainability

The development in the global financial market within the last decade raised some questions corporate regarding the management of financial services industry and the oversight both at the micro and macro levels (International Actuarial Association, 2009). Good corporate governance extends past putting in place directions. It is not a guarantee to corporate success however, where there is an absence of such standards, there may be a prevalence of fraudulent actions and practice, ineptitude in action and corporate failures. Lawrence and Weber (2014) described corporate governance as procedure for controlling or governing a firm through which a firm is controlled or an organisation is governed, noting that, it is an internal governance system that determines the overall strategic direction of a company and balances at other times, divergent interests. Where a good corporate governance code is in existence, it helps improve labour and stakeholder relations and protect the environment (Ene and Bello, 2016).

In allocating power, a company decides how it hopes to be run and by whom. The board has the charge of efficiently running the company and discharging in full; it's financial, legal and regulatory obligations as well as reviews the corporate strategy, performance and objectives of the company. They it is, who is responsible for managing the organisation and are accountable to the shareholders in the creation and delivery of sustainable value through effective management. The constitution usually composes of both executive as well as non-executive directors who are answerable for driving mechanism of corporate governance in the company. The BOD endorsements form the fundamentals of good governance (Gadi *et al*., 2015), this study thus hypothesizes that:

Ho_1: Board of directors do not influence the sustainability of Nigerian insurance companies.

The industry adoption of corporate governance is unavoidable as it plays an important role within the economy. A system with operative governance gives prospective stakeholders confidence which could lead to monetary development (Momoh and Ukpong, 2013). The industry manages the risks of others and is also saddled with market stability responsibilities, investment and economic growth which to be effectively achieved, requires in place, a corporate governance system that is good (Kwon, 2001). Scholars (Demb & Neubauer, 2010; Pugliese *et al*., 2009) recommend creation of board committees (audit, finance, and so on) so as to avoid governance problems and increase performance. Auditing is important as it ensures that accounting norms applicable to insurance business is effectively applied, maintained, internal control processes are monitored and directives complied with. The audit committee is responsible for reviewing data integrity and also the information provided in the financial statements. However, there seems to be little idea within the insurance industry of any likely impact this may have on organisations' sustainability, thus, the study hypothesizes that:

Ho_2: Audit committee does not impact sustainability of Nigerian insurance companies.

2.8. Conceptual model

A system, by which an organisation's risks are managed, monitored and assessed, corporate governance ensure its objectives are set, achieved and its performance optimized (Grace *et al.,* 2018). An attempt is thus made here, to establish a correlation between the corporate governance code laid down rules (board of directors and audit committee) the independent variables, and sustainability of organisation which is used here as the dependent variable. This correlation is indicated in figure 1 below:

Code of Corporate Governance

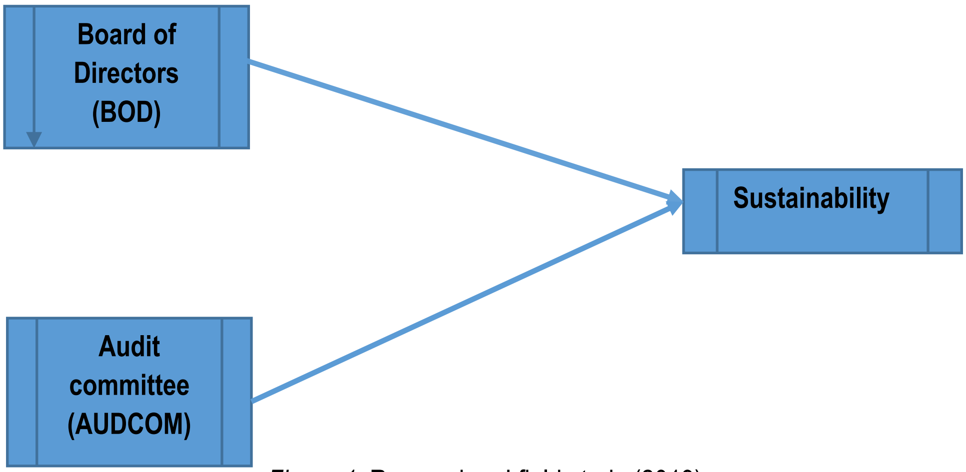

Figure 1. Researchers' field study (2019)

2.9. Empirical review

Corporate governance has as its basic concern, stakeholders' role and the impact being made on the communal well-being of the society. Empirically, the leaning of most corporate governance studies tends to be towards the financial indices. Mbu-Ogar *et al.* (2017) using a survey research design, studied corporate governance and performance and concurred with an increasing consensus that economic growth and good corporate governance are closely linked, while board composition along with the size and audit committee also had substantial effect. Grace *et al.* (2018) looked at corporate governance of financial institutions in Kenya and performance, and found that it had a significant influence on performance with board skills having a positive influence and board committees having a negative influence, thus implying the need to ensure that board members appointments are properly considered.

Fadun (2013) looked at inherent challenges in the insurance system and opportunities in Nigeria with the aid of a survey research design; found amongst other things, that where there is an application of the corporate governance code in its entire proper manner, growth increased within the sector. Emphasising the need for involvement in a qualitative study, of professionals in risk models, Adeyele and Maiturare (2012) noted that repositioning adequately, the insurance industry in Nigeria for manageable advancement involved invention and also generating consciousness of the products. They conclude that the ultimate responsibility lies with the governing body, for the industry's excellent performance and they should ensure full compliance. Sulaimon *et al.* (2016) investigated the relationship existing between corporate governance practices and performance and found that both variables had a significant relationship. On the contrary, Letting *et al.* (2012) using survey research design, investigated board diversity and performance and noted that it had no relationship, while Nyamango and Temesgen (2013) using secondary data also found that large board size negatively impacted performance thus affecting sustainability. In a study of corporate governance and the likely influence on earnings management through a survey of quoted Nigerian firms, it was found that size, board independence, audit committee strength and organisations proportions were all practices that had major influence towards earnings management with a recommendation for improvement (Egbunike *et al*., 2015).

3. Methodology of research

This study employed the aid of a cross-sectional research design. With a population comprised of all employees from three (3) insurance companies with two of them selected based on their previous bank affiliations and their adherence to the NAICOM corporate governance code as contained in their financials while the third company selected based on the intervention of NAICOM in the top management to correct perceived mismanagement. All of them fully represent the business of insurance in that, all three are engaged in general business underwriting, are regulated by the same authority, and have consistently, as indicated in their financials, been bound by the corporate governance code.

Employees across all cadres were chosen so as to elicit genuine responses as it is believed that management staff may be circumventing in their responses. The sample consists of 238 employees of the selected companies derived using the Yemane (1967) formula: n= N ÷1 + N (e)2, where n = sample size, N = population, e = precision estimate (0.05) and a response rate of about 70% gotten. The research instrument was a 5–point Likert scale questionnaire divided into sections A and B with responses ranging from strongly agree at 5 and strongly disagree at 1.

The items measuring corporate governance was adapted from El-Kassar, Elgammal and Bayoud (2014), while items measuring sustainability was adapted from Lapinskaitte and Radikaite (2015) Dow Jones sustainability indexes (DJSI) key indicators. A pilot study of 20 respondents without replacement was carried out on the instrument with a Cronbach Alpha observed within the acceptable threshold. The study employed regression analysis to examine the level of influence of corporate governance indices of board of directors and audit committee had on sustainability among the study population.

4. Results and discussion of findings

To effectively measure the relationship between the study variables in response to our hypothesis, a regression analysis was carried out.Table 1 and 2 shows the result for Hypothesis 1: Board of directors do not influence the sustainability of Nigerian insurance companies.

Table 1. Model Summary & Anova (BOD)

Model	R	R^2	Adjusted R^2	Std Error of Est	Durbin Watson	F	Sig
1	0.417	0.174	0.169	8.546	1.689	34.584	.000[b]

a. Predictor: (Constant), BOD = Board of Directors

b. Dependent variable: Sustainability

Table 2. Coefficients[a]

Model	Variation	Unstandardized	Coefficient	Std Coeff Beta	T	Sig	VIF
		B	Std Error				
1	Constant	30.796	4.260		7.229	0.000	
	Board of Directors	1.206	0.205	.417	5.881	0.000	1.000

a. *Dependent variable: Sustainability (SUS).*

Source: *Researchers' (2019)*

Table 1 above shows us how the variance overall is explained where our R2 = 0.174 implying that the predictor variable (BOD) is explained by 17.4% variance, while R =0.417 indicates an existence of correlation between both variables. The average observed sustainability of the selected insurance companies is seen to step outside the expected line of regression as shown in the standard error of estimate by 8.546. There is no multi-collinearity with a variance inflation factor (VIF) of 1. Table 2, in responding to the hypothesis, gives us the contribution of BOD to sustainability, with the β coefficients giving us the standardized value, the result reflects a positive significant relationship between BOD and sustainability ($\beta = 0.417$; $t = 5.881$, $p < 0.05$).

Table 3 and 4 responds to Hypothesis 2: Ho_2: There is no relationship existent between the audit committee and sustainability of Nigerian insurance companies.

Table 3. Model Summary & Anova (AUDCOM)

Model	R	R^2	Adjusted R^2	Std Error of Est	Durbin Watson	F	Sig
1	0.443	0.196	0.192	8.430	1.712	40.102	.000[b]

a. Predictor: (Constant), AUDCOM = Audit Committee

b. Dependent variable: Sustainability

Source: Researchers' (2019)

Table 4. Coefficients[a]

Model	Variation	Unstandardized	Coefficient	Std Coeff Beta	T	Sig	VIF
		B	Std Error				
1	Constant	26.011	4.709		5.523	0.000	
	Audit Committee	1.521	0.240	.443	6.333	0.000	1.000

Dependent variable: Sustainability (SUS)

Source: Researchers' (2019)

Results in table 3 above gives us R2 = 0.196 implying that 19.6% variance in sustainability is as a result of variation in AUDCOM and our R = 0.443 indicating a correlation between the dependent and the independent variables. The standard error of estimate = 8.430 and no multi-collinearity with VIF = 1. Table 4 shows us the contribution of AUDCOM to sustainability ($\beta = 0.443$; $t = 6.333$, $p < 0.05$) thus indicating that there exists a significant relationship between AUDCOM and sustainability. While both results show that the independent variables both contribute to the equation significantly as the values of probability of both are $p< 0.05$, when compared individually, the standardized coefficient values show that AUDCOM acts as a stronger predictor of sustainability ($\beta = 0.443$; $t = 6.333$, $p < 0.05$).

5. Discussion and conclusions

Using selected companies with emphasis on two of the code requirements, namely, board of directors and audit committee, the study examined likely influence of corporate governance code on sustainability of insurance companies in Nigeria. Study results indicate an existence of an affirmative weighty connection between the board of directors and sustainability as well as audit committee and sustainability, however, with the latter being a greater predictor. The results align with Egbunike, Ezelibe and Aroh (2015) who observed amongst other things, that board independence, committee strength and organisations proportions were all practices that had major influence towards earnings management. The study results goes further to also buttress the points made by Fadun (2013) that good corporate governance code when implemented, contributed to growth; and that made by Romano, Ferretti and Rigolini (2012) who noted that board committees were important as they are very instrumental in successfully applying the code. The above results reveal that corporate governance code is a very important governance tool for the insurance industry with specific emphasis on the audit committee being a strong predictor of sustainability. This implies therefore, that there is a strong need for the insurance sector to adhere to the code, implement the requirements, promote accountability with the aim of ensuring organisational sustainability as this is pertinent to the success of meeting their core function which is indemnifying the insured, restoring them back to the position they were in prior to the loss, which aids continuance of their businesses and in turn helps contribute to economic growth of the nation.

Based on the above, the study recommends that organisations within the Nigerian insurance industry ensure strict adherence to the code in every sphere and monitor implementation. This will help improve the performance of organisations and engender trust in stakeholders; feedback across the organisation so as to encourage and maintain open communication (top-bottom; bottom-top) and that the triple bottom line rule of sustainability is also made an integral part of the organisation as an organisation that consciously preserves its environment while pursuing its goals in the present has greater capacity of sustenance in the long term which is the end goal of every organisation. There are however, certain limitations to this study, as the study sample size is limited to three (3) selected insurance companies. The researchers thus suggest that larger sample size as well as other items under the code be undertaken for future studies. Also the study employed a cross sectional survey which does not give room for causal inferences. It will be interesting to know the possible results from a longitudinal study as this may give more light. It is also suggested that a mixed method research be conducted as it is probable that the quantitative approach may limit honest responses from respondents who may be scared to open up for fear of reprisal.

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