**CORPORATE GOVERNANCE AND FINANCIAL REPORTING IN NIGERIA BANKING INDUSTRY**

**CHAPTER ONE**

**INTRODUCTION**

* 1. **Background of the study**

The The concept of corporate governance has attracted a good deal of public interest in recent years, because of its apparent importance on the economic health of corporations and society in general. Basically, corporate governance in the banking sector requires judicious and prudent management of resources and the preservation of resources (assets) of the corporate firm; ensuring ethical and professional standards and the pursuit of corporate objectives, it seeks to ensure customer satisfaction, high employee morale and the maintenance of market discipline, which strengthens and stabilizes the bank Recently, the banking industry in Nigeria has been undergoing serious reforms over the past couple of years arising from the central bank of Nigeria's requirement for banks to increase their capital base (share) to a minimum level of twenty five billion naira (N25B), (Ogbeche, 2006:1). This triggered off several mergers and acquisitions that have reduced the number of players from eighty nine (89) to twenty five (25) banks as at the beginning of 2006 (Kama, 2006; 66). It is imperative to note that at the end of the consolidation exercise, the total capitalization (the value of all equities of the banks came to N775.0 billion compared to the figure of N327 billion before the commencement of this program in July 2004. (Adedipe, 2004: 52). The issue of corporate governance has recently been given a great deal of attention in various national and International forays. This is in recognition of the critical role of corporate governance in the success or failure of companies. Corporate governance refers to the processes and structures by which the business 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 other stakeholders. Corporate governance is therefore about building credibility, ensuring transparency and accountability as well as maintaining an effective channel of information disclosure that would Foster good corporate performance.

The strategy for addressing the challenges of corporate governance has taken various forms at both the national and International levels and have culminated in initiatives such as: the OECD Code; the Cadbury Report; the Basel Committee Guidelines on Corporate Governance; the King‟s Report of South Africa etc. It is therefore necessary to point out that the concept of corporate governance of banks and very large firms have been a priority on the policy agenda in developed market economies for over a decade. Further to that, the concept is gradually warming itself as a priority in the African continent. Indeed, it is believed that the Asian crisis and the relative poor performance of the corporate sector in Africa have made the issue of corporate governance a catchphrase in the development debate (Berglof and Von -Thadden, 1999).

Performance may be defined as the reflection of the way in which the resources of a company (bank) are used in the form which enables it to achieve its objectives. According to Heremans, (2007), financial performance is the employment of financial indicators to measure the extent of objective achievement, contribution to making available financial resources and support of the bank with investment opportunities.

These are factors which play a role in shaping the financial status of a company. Most studies divide the determinants of commercial banks’ financial performance into two categories, namely internal and external factors. Internal determinants of profitability, which are within the control of bank management, can be broadly classified into two categories, i.e. financial statement variables and nonfinancial statement variables, (Linyiru, 2006). While financial statement variables relate to the decisions which directly involve items in the balance sheet and income statement; non-financial statement variables involve factors that have no direct relation to the financial statements. The examples of non-financial variables within the this category are number of branches, status of the branch (e.g. limited or full-service branch, unit branch or multiple branches), location and size of the bank, Sudin (2004).

Several events are therefore responsible for the heightened interest in corporate governance especially in both developed and developing countries. The subject of corporate governance leapt to global business limelight from relative obscurity after a string of collapses of high profile companies. Enron, the Houston, Texas based energy giant and WorldCom the telecom behemoth, shocked the business world with both the scale and age of their unethical and illegal operations. In developing economies, the banking sector among other sectors has also witnessed several cases of collapses, some of which include the Alpha Merchant Bank Ltd, Savannah Bank Plc, Societe Generale Bank Ltd (all in Nigeria), The Continental Bank of Kenya Ltd, Capital Finance Ltd, Consolidated Bank of Kenya Ltd and Trust Bank of Kenya among others (Akpan, 2007). In Nigeria, the issue of corporate governance has been given the front burner status by all sectors of the economy. For instance, the Securities and Exchange Commission (SEC) set up the Peterside Committee on corporate governance in public companies. The Bankers‟ Committee also set up a sub-committee on corporate governance for banks and other financial institutions in Nigeria. This is in recognition of the critical role of corporate governance in the success or failure of companies (Ogbechie, 2006:6). Corporate governance therefore refers to the processes and structures by which the business and affairs of institutions are directed and managed, in order to improve long term share holders‟ value by enhancing corporate performance and accountability, while taking into account the interest of other stakeholders (Jenkinson and Mayer, 1992).

* 1. **STATEMENT OF THE PROBLEM**

With the increasing dynamism and complexity of modern business operations, coupled with the ever-present accounting scandals of high profits companies such as Cadbury plc and Enronlinc have questioned the effectiveness of corporate governance mechanism and the quality of financial reports and the credibility of audit functions.  
Since ownership is separated from in their own interest, rather than the interest of shareholders whom they represent. They could manipulate financial statements, giving investors misleading impression about the financial position of the corporation. As a result, financial reports in most cases, do not reflect the true and fair position of the corporation.  
Therefore. The need for accurate, reliable, timely and accessible financial reports is imperative in order to maintain corporate accountability so as to achieve organizational goals and quick decision making.

**1.3     OBJECTIVE OF THE STUDY**

The followings are the purpose of the study:

1. To establish the relationship that exist between corporate governance and financial reporting
2. To establish the relationship between management and shareholders’ interests.
3. To ensure that the financial reports in most cases reflect the true and fair position of the corporate.
4. To enhance the need for accurate, reliable, timely and accessible financial reports necessary for corporate accountability so as to achieve organizational goals and quick decision making.
   1. **RESEARCH HYPOTHESES**

For the successful completion of the study, the following research hypotheses were formulated:

**H0:** corporate governance has no effect on the financial reporting of the banks

**H1:** corporate governance has effect on the financial reporting of the banks

**H0:**  Corporate governance does not enhance management and shareholders relationship through transparency and accountability.

**H2:** Corporate governance does enhance management and shareholders relationship through transparency and accountability

* 1. **SIGNIFICANCE OF THE STUDY**

It is believed that at the completion of the study, the findings will be of great importance to the central bank of Nigeria who are charged with the responsibility of regulating the activities of the commercial banks to ensure strict compliance with the corporate governance guideline. The study will also be of great importance to the managers of commercial banks as the findings will remind them of the tremendous benefit of corporate governance practice.

The study will also be of great benefit to researchers who wishes to embark on a study in similar topic as the study will serve as a guide to them. Finally the research will be of great importance to student, teachers, lecturers, academia’s and the general public.

**1.6 SCOPE AND LIMITATION OF THE STUDY**

The scope of the study covers the effect of corporate governance on the performance of commercial banks in terms of profitability. In the course of the study, the researcher encounters some constrain which limited the scope of the study. Some of these constrain are stated below:

1. **Availability of research material:** The research material available to the researcher is insufficient, thereby limiting the study.
2. **Time**: The time frame allocated to the study does not enhance wider coverage as the researcher has to combine other academic activities and examinations with the study.
3. **Finance:** The finance available for the research work does not allow for wider coverage as resources are very limited as the researcher has other academic bills to cover.
   1. **DEFINITION OF TERMS**

**Management**

Management (or managing) is the administration of an [organization](https://en.wikipedia.org/wiki/Organization), whether it is a [business](https://en.wikipedia.org/wiki/Business), a not-for-profit organization, or government body.

**Banks**

A bank is a [financial institution](https://en.wikipedia.org/wiki/Financial_institution) that accepts [deposits](https://en.wikipedia.org/wiki/Deposit_account) from the public and creates [credit](https://en.wikipedia.org/wiki/Demand_deposit). Lending activities can be performed either directly or indirectly through [capital markets](https://en.wikipedia.org/wiki/Capital_market).

**Corporate Governance**

The methods by which suppliers of finance control managers in order to ensure that their capital cannot be expropriated and that they earn a return on their investment.

**Commercial banks**

Bank that dealing with businesses: a bank whose primary business is providing financial services to companies

* 1. **Organization of the study**

This research work is organized in five chapters for easy understanding as follows Chapter one is concern with the introduction which consist of the (overview, of the study), statement of problem, objectives of the study, research question, significance or the study, research methodology, definition of terms and historical background of the study. Chapter two highlights the theoretical framework on which the study it’s based thus the review of related literature. Chapter three deals on the research design and methodology adopted in the study. Chapter four concentrate on the data collection and analysis and presentation of finding. Chapter five gives summary, conclusion and recommendations made of the study.

**CHAPTER TWO**

**REVIEW OF RELATED LITERATURE**

**2.1 Introduction**

The importance of a vibrant, transparent and healthy banking system in the mobilization and intermediation of fund, for the growth and development of the economy need not be over-emphasized. Worthy of is the fact that the level of functioning of the financial sector depend on the perception and patronage of the citizens towards its services (Al- Faki, 2006). The situation where the public losses confidence in the financial institutions, can result in panic and consequential financial and economic woes. The absence of confidence in any organization is attributable to opaque management practices with deleterious effect on its performance. The measure of performance in this case is not limited to the financials (turnover and profit) but also customer satisfaction, employee welfare, social corporate responsibility, indeed, the whole gamut of balanced score card. There are many ways of defining corporate governance, ranging from narrow definitions that focus on companies and their shareholders, to broader definitions that incorporate the accountability of companies to many other groups of people, or ‘stakeholders’. The Cadbury Report (1992) was set up by the Committee on the Financial Aspects of Corporate Governance, known as the Cadbury Committee in May 1991 by the Financial Reporting Council, the London Stock Exchange, and the accountancy profession. The report made far reaching recommendations on corporate governance concerning the way in which companies are directed and controlled. The central components of the voluntary code of corporate practice are: that there be a clear division of responsibilities at the top, primarily that the position of Chairman of the Board be separated from that of Chief Executive, or that there be a strong independent element on the board; that the majority of the Board be comprised of outside directors; that remuneration committees for Board members be made up in the majority of non-executive directors; and that the Board should appoint an Audit Committee including at least three non-executive directors. Corporate performance is an important concept that relates to the way and manner in which financial, material and human 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. The overall effect of good corporate governance should be the strengthening of investor’s confidence in the economy of our country. Corporate governance is therefore about building credibility, ensuring transparency and accountability as well maintaining an effective channel of information disclosure that would foster good corporate performance. It is therefore crucial that banking sector observe a strong corporate governance ethos. Massive corporate collapses resulting from weak systems of corporate governance have highlighted the need to improve and reform corporate governance at an international level. The Enron in the USA, Cadbury in Nigeria and other similar cases around the world have led to enactment of the Sarbanes–Oxley Act in July 2002 in the USA, the Higgs Report and the Smith Reports in 2003 in the UK and the st-code for corporate governance for banks in Nigeria which became operational in 2006 amongst others. Corporate governance is the system of checks and balances, both internal and external to companies, which ensures that companies discharge their accountability to all their stakeholders and act in a socially responsible way in all areas of their business activity (Solomon and Solomon, 2004).

The Nigerian banking system has undergone remarkable changes over the years in terms of the number of institution, ownership structure and the depth and breadth of the operations. These changes have been influenced largely by the opportunities presented by the deregulation of the financial sector, globalization of operations, technological advancements, impact of global economic downturn and the adoption of regulatory guidelines that conform to international standards. The developments in the Nigerian banking industry show that absence of good corporate governance was mainly responsible for the dismal performance of the industry as a catalyst for economic growth. In 1992, Bank of Credit and Commerce International (including its Nigerian affiliate) went bust and lost billions of dollars for its depositors, shareholders and employees. Another company, Polly Peck, reported healthy profits in 1992 while declaring bankruptcy the next year. Given the nature of banking business and the antecedents of the operators such as unrecoverable loans, unethical bank practices, illiquidity, etc of Nigeria banks, corporate governance is fundamental to the nation’s financial stability Afrinvest, (2010). Shleifer and Vishny (1997) opined that effective corporate governance reduces control rights, shareholders and creditors confer on managers, increasing the probability that managers invest in positive net present value projects. Thus, the relationship of the board and management, according to Al-faki (2006), should be characterized by transparency to shareholders, and fairness to other stakeholders. This study will add to the general body of knowledge, on the impact of corporate governance and performance of banks in Nigeria; which is a very sensitive and vital sector. It also expands the body of literature in terms of its scope in integrating both bank internal factor, regulatory factor and the economic factor that may mitigate bank performance. Narrowing to sectorial macro analysis, picking Six Banks; 2 first generation, 2 new generation and 2 middle generation banks; In order to make a generalization on corporate governance level in the banking industry of Nigeria, as such seem limited in corporate governance literature in Nigeria. Considering the sensitivity of the subject area of corporate governance, and the limitation of gaining access to relevant materials, this study will cover and review corporate governance and performance of six major banks in Nigeria {First Bank of Nigeria Plc, United Bank of Africa (UBA), EcoBank, Fidelity Bank, First City Monument Bank (FCMB), and Guarantee Trust Bank (GTB)} in the post consolidation era- 2005 to 2009 and Bank PHB.

**2.2 CONCEPTUAL REVIEW ON CORPORATE GOVERNANCE**

Corporate governance is a uniquely complex and multi-faceted subject. Devoid of a unified or systematic theory, its paradigm, diagnosis and solutions lie in multidisciplinary fields i.e. economics, accountancy, finance among others (Cadbury, 2002). As such it is essential that a comprehensive framework be codified in the accounting framework of any organization. In any organization, corporate governance is one of the key factors that determine the health of the system and its ability to survive economic shocks. The health of the organization depends on the underlying soundness of its individual components and the connections between them. According to Morck, Shleifer and Vishny (1989), among the main factors that support the stability of any country‟s financial system include: good corporate governance; effective marketing discipline; strong prudential regulation and supervision; accurate and reliable accounting financial reporting systems; a sound disclosure regimes and an appropriate savings deposit protection system. Corporate governance has been part of research into the business profession since Adam Smith‟s (1776) seminal publication of An inquiry into the nature and causes of the wealth of nations and undoubtedly given impetus through Berle and Mean‟s (1932) classic publication of the separation of corporate ownership from control. Corporate governance is aimed at reducing conflicts of interest, short-sightedness of writing costless perfect contracts and monitoring of controlling interest of the firm, the absence of which firm value is decreased (Denis and McConnell, 2003). Good corporate governance can also be considered as the diligent way in which providers of corporate financial capital guarantee appropriate rewards in a legal and ethically moral way. There are both internal and external ways of achieving this (Jensen, 1993). The first is through the structure of ownership (shareholding concentration and voting rights), and board of directors or supervisory board in some regulatory regimes (who monitor firms and are supposed to work in the interest of shareholders). The second is through the market for corporate control (takeover threats), regulatory intervention, and product and factor markets. Corporate governance codes that serve as templates of achieving value to shareholders (and stakeholders) have been written in several countries. Corporate governance, as a concept, can be viewed from at least two perspectives. The narrow view is concerned with the structures within a corporate entity or enterprise receives its basic orientation and direction. The broad perspective is regarded as being the heart of both a market economy and a democratic society (Oyejide and Soyibo, 2001) the narrow view perceives corporate governance in terms of issues relating to shareholder protection, management control and the popular principal-agency problems of economic theory. Corporate governance has been looked at and defined variedly by different scholars and practitioners. However they all have pointed to the same end, hence giving more of a consensus in the definition. Coleman and Nicholas-Biekpe (2006) defined 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. However, Mayer (1999) offers a definition with a wider outlook and contends that it means the sum of the processes, structures and information used for directing and overseeing the management of an organization. The Organization for Economic Corporation and Development (1999) has also defined corporate governance as a system on the basis of which companies are directed and managed. It is upon this system that specifications are given for the division of competencies and responsibilities between the parties included (board of directors, the supervisory board, the management and shareholders) and formulate rules and procedures for adopting decisions on corporate matters. In another perspective, Arun and Turner (2002b) contend that there exists a narrow approach to corporate governance, which views the subject as the mechanism through which shareholders are assured that managers will act in their interests. However, Shleifer and Vishny (1997), Vives (2000) and Oman (2001) observed that there is a broader approach which views the subject as the methods by which suppliers of finance control managers in order to ensure that their capital cannot be expropriated and that they can earn a return on their investment. There is a consensus, however that the broader view of corporate governance should be adopted in the case of banking institutions because of the peculiar contractual form of banking which demands that corporate governance mechanisms for banks should encapsulate depositors as well as shareholders (Macey and O‟Hara (2001). Arun and Turner (2002b) supported the consensus by arguing that the special nature of banking requires not only a broader view of corporate governance, but also government intervention in order to restrain the behaviour of bank management. They further argued that, the unique nature of the banking firm, whether in the developed or developing world, requires that a broad view of corporate governance, which encapsulates both shareholders and depositors, be adopted for banks. They posit that, in particular, the nature of the banking firm is such that regulation is necessary to protect depositors as well as the overall financial system. This study therefore adopts the broader view and defines corporate governance in the context of banking as the manner in which systems, procedures, processes and practices of a bank are managed so as to allow positive relationships and the exercise of power in the management of assets and resources with the aim of advancing shareholders‟ value and shareholders‟ satisfaction together with improved accountability, resource use and transparent administration.

**2.3 THEORETICAL REVIEW**

**2.3.1 Agency Theory**

It is an acknowledged fact that the principal-agent theory is generally considered the starting point for any debate on the issue of corporate governance emanating from the classical thesis on The Modern Corporation and Private Property by Berle and Means (1932). According to this thesis, the fundamental agency problem in modern firms is primarily due to the separation between finance and management. Modern firms are seen to suffer from separation of ownership and control and therefore are run by professional managers (agents) who cannot be held accountable by dispersed shareholders. Agency theory suggests that there are several mechanisms to reduce the agency problem in the firm. For examples, managerial incentive mechanism compensates managerial efforts to serve the owners’ interests; dividend mechanism reduces managerial intention to make an overinvestment decision which will be financed by internal free cash flow; bonding mechanism reduces managerial moral hazard which potentially occurs when they are not restricted by bond contract and bankruptcy risk. Other owners’ efforts to reduce agency cost of equity, potentially created by moral hazard managers, include the intention of owners to choose reputable board of directors; direct intervention by shareholders, the threat of firing, and the threat of takeover(Sanda et al., 2005).

**2.3.2 Stakeholder Theory**

One argument against the strict agency theory is its narrowness, by identifying shareholders as the only interest group of a corporate entity necessitating further exploration. Stakeholder theory has become more prominent because many researchers have recognized that the activities of a corporate entity impact on the external environment requiring accountability of the organization to a wider audience than simply its shareholders. For instance, McDonald and Puxty (1979) proposed that companies are no longer the instrument of shareholders alone but exist within society and, therefore, has responsibilities to that society. One must however point out that large recognition of this fact has rather been a recent phenomenon. Indeed, it has been realized that economic value is created by people who voluntarily come together and cooperate to improve everyone’s position (Freeman et al., 2004). Jenson (2001) critique the Stakeholders theory for assuming a single-valued objective (gains that accrue to a firm’s constituencies). The argument of Jensen (2001) suggests that the performance of a firm is not and should not be measured only by gains to its stakeholders. Other key issues such as flow of information from senior management to 14 lower ranks, inter-personal relations, working environment, etc are all critical issues that should be considered. Some of these other issues provided a platform for other arguments as discussed later. An extension of the theory called an enlightened stakeholder theory was proposed. However, problems relating to empirical testing of the extension have limited its relevance (Sanda et al., 2005).

**2.4 Corporate governance from Theoretical Perspective**

Board of Directors (BODs) has an important role in the management of organizations. Since, BODs are considered to be one of the important governance mechanisms, these groups are increasingly being hold responsible for the organizational performance. For this reason, many studies from diverse fields, including law, economics, finance, sociology, organizational theory and strategic management, focus on BODs (Kiel and Nicholson, 2003). The performance of the organizations is dependent on the realization of the roles of BODs, (Jacob, 2011). These roles are both important and numerous (Finkelstein and Money, 2003). Johnson, Daily and Ellstrand (1996) suggest that the most emphasized roles of BODs in the literature are control, service and resource dependence roles. The control role entails directors monitoring managers as fiduciaries of stockholders, hiring and firing executives and determining executive compensation. The service role, on the other hand, involves advising executives on administrative and other managerial issues as well as actively initiating and formulating strategy, (Njoka, 2010). Finally, the resource dependence role views the board as facilitating the acquisition of resources critical to firm success.

Hillman and Dalziel (2003) assert that, monitoring as well as resource providing is considered by BODs to be an integral part of their board activities. Agency theory being the dominant framework (Zahra and Pearce, 1999; Daily, Dalton and Cannella, 2003), researchers employed various theoretical perspectives (i.e. stewardship theory, managerial hegemony theory, stakeholder theory, institutional theory, and resource dependence theory) for the study of BODs. Within the frame of agency theory, it is assumed that BODs control the opportunistic behaviors of the managers; therefore, these groups represent the primary internal control system that fit the interests of shareholders and managers, (Jensen, 1993). According to Choe and Lee (2003), board composition is very important to effectively monitor the managers and reduce the agency cost. Although the executive directors have specialized skills, expertise and valuable knowledge of the firms’ operating policies and day-to-day activities, there is a need for the independent directors to contribute the fresh ideas, independence, objectivity and expertise gained from their own fields (Weir, 1997; Firth et al., 2002). Hence, the agency theory recommends the involvement of independent non-executive directors to monitor any self-interested actions by managers and to minimize agency costs (Le et al. 2006; Williams et al. 2006). Jensen (1993) mention that boards with more than seven or eight members are unlikely to be effective. They further elaborate that large boards result in less effective coordination, communication, and decision making, and are more likely controlled by the CEO. Yoshikawa and Phan (2003) also highlight that larger boards tend to be less cohesive and more difficult to coordinate because there might be a large number of potential interactions and conflicts among the group members. In addition, they further state that large boards are often created by CEOs because the large board makes the board members disperse the power in the boardroom and reduce the potential for coordinated action by directors, leaving the CEO as the predominant figure. The primary focus of re-source dependence theory is the fact that the organizations should interact with its environment as much as it is necessary. Within the frame of resource dependence theory, organizational needs to access environmental resources, emerge as a vital issue for the survival, (Linyiru, 2006). Organizations are considered as an open system that is dependent on other organizations for the provision of important resources (Pfeffer and Salancik, 1998). It is assumed that the success of the organizations is based on their abilities to provide and control the external resources (Aldrich and Pfeffer, 1996). The mechanisms that administer these external dependencies are BODs (Pfeffer and Salancik, 1998).

**2.5 Corporate Governance and Bank Performance**

Tandelilin et al., (2007) asserts that the central focus in most literature around, discussion analysis in research all over the world on matters to do with corporate governance has been the role of ownership structure as a corporate governance mechanism. Whether the kind of ownership structure matters and what are its implications for corporate governance are areas that raise some concern (Tandelilin et al., 2007). Corporate 17 governance can be defined as the relationship among shareholders, board of directors and the top management in determining the direction and performance of the corporation, (Wheelen and Hunger 2006). In Kenya, financial reforms have encouraged foreign banks to enter and expand banking operations in the country. Kamau (2009) affirm that foreign banks are more efficient than local banks. She attributes this to the fact that foreign banks concentrate mainly in major towns and target corporate customers, whereas large local banks spread their activities more widely across the country. Foreign banks therefore refrain from retail banking to specialize in corporate products, while large domestic banks are less discriminatory in their business strategy, (Njoka, 2010). These different operational modalities affect efficiency and profitability she notes. Studies with regard to corporate governance theme have mainly been carried out in developed economies mostly in the United Kingdom and the United States of America with few afore mentioned being done in Africa and specifically Kenya, (Njoka, 2010). However, the concept of governance in Kenya is now increasingly being embraced knowing that it leads to sustainable growth and more so, since Kenya has had a history of poor governance system in the banking industry attributed to weak corporate governance practices, lack of internal controls, weaknesses in regulatory and supervisory systems, insider lending and conflict of interest which led to the collapse of many financial institutions with others going under receivership (Awino, 2011).

**2.6 ELEMENTS OF CORPORATE GOVERNANCE IN BANKS**

Different authors and management specialists have argued that corporate governance requires laid down procedures, processes, systems and codes of regulation and ethics that ensures its implementation in organization (Altunbas, Evans and Molyneux, 2001). Some suggestions that have been underscored in this respect include the need for banks to set strategies which have been commonly referred to as corporate strategies for their operations and establish accountability for executing these strategies. El-Kharouf (2000), while examining strategy, corporate governance and the future of the Arab banking industry, pointed out that corporate strategy is a deliberate search for a plan of action that will develop the corporate competitive advantage and compounds it. In addition to this, the BCBS (1999) contends that transparency of information related to existing conditions, decisions and actions is integrally related to accountability in that it gives market participants sufficient information with which to judge the management of a bank. The Committee advanced further that various corporate governance structures exist in different countries hence, there is no universally correct answer to structural issues and that laws do not need to be consistent from one country to another. Sound governance therefore, can be practiced regardless of the form used by a banking organization. The Committee therefore suggests four important forms of oversight that should be included in the organizational structure of any bank in order to ensure the appropriate checks and balances.

**2.7 RELATIONSHIP BETWEEN CORPORATE GOVERNANCE AND FIRM PERFORMANCE**

Better corporate governance is supposed to lead to better corporate performance by preventing the expropriation of controlling shareholders and ensuring better decision-making. In expectation of such an improvement, the firm‟s value may respond instantaneously to news indicating better corporate governance. However, quantitative evidence supporting the existence of a link between the quality of corporate governance and firm performance is relatively scanty (Imam, 2006). Good governance means little expropriation of corporate resources by managers or controlling shareholders, which contributes to better allocation of resources and better performance. As investors and lenders will be more willing to put their money in firms with good governance, they will face lower costs of capital, which is another source of better firm performance. Other stakeholders, including employees and suppliers, will also want to be associated with and enter into business relationships with such firms, as the relationships are likely to be more prosperous, fairer, and long lasting than those with firms with less effective governance. Implications for the economy as a whole are also obvious. Economic growth will be more sustainable, because the economy is less vulnerable to a systemic risk. With better protection of investors at the firm level, the capital market will also be boosted and become more developed, which is essential for sustained economic growth. At the same time, good corporate governance is critical for building a just and corruption-free society. Poor corporate governance in big businesses is fertile soil for corruption and corruptive symbiosis between business and political circles. Less expropriation of minority shareholders and fewer corruptive links between big businesses and political power may result in a more favorable business environment for smaller enterprises and more equitable income distribution (Iskander and Chamlou, 2000). According to a survey by McKinsey and Company (2002) cited in Adams and Mehran (2003), 78% of professional investors in Malaysia expressed that they were willing to pay a premium for a well-governed company. The average premium these investors were willing to pay generally ranged from 20% to 25%. Many scholars have attempted to investigate the relationship between good governance and firm performance in a more rigorous way.

**2.8 EMPIRICAL REVIEW ON CORPORATE GOVERNANCE ON BANK PERFORMANCE**

Most of the studies on the link between corporate governance and firm performance confirm causality (Abor & Adjasi, 2007). However, the evidence indicates between a strong and very weak relationship. Black (2001), for instance found a strong correlation between corporate governance and firm performance, as represented by stock valuation. Choi and Hasan (2005) examined the effect of ownership and corporate governance on Korean bank’s performance during 1998 – 2002 by using a simple ordinary least squared model reporting that the existence of one foreign director on the board improves bank performance significantly, but multiple foreign directors on the board do not improve bank’s performance. In the same way, the empirical evidence is supportive of the hypothesis that large shareholders are active monitors in companies, and that direct shareholder monitoring helps boost the overall profitability of firms. This result is also borne out by studies of managerial turnover. For example, Franks and Mayer (1994) find a larger turnover of directors when large shareholders are present, again indicating that large shareholders are active monitors. It seems, therefore, that the beneficial effects of direct monitoring, and a better match between cash flow and control rights, more than outweigh the costs of low diversification opportunities or rent extraction by majority owners. In addition, Roe (1994) states that the low ownership concentration in the US compared to other countries may be the result of policies initiated by controlling managers that discourage large holdings e.g. anti-takeover devices. This implies that for the US at least, that managers are strong relative to shareholders and that management entrenchment is a serious problem. Therefore, policy makers in outsider systems like the US and UK should pay particular attention to the negative effects of mechanisms that are often employed by management that inhibit the market for corporate control. In surveys of corporate governance, Shleifer and Vishny (1997) and Gugler (1999) find that the empirical evidence suggests that control is valued, which would not be the case if controlling blockholders or large shareholders received the same benefits as other investors. For example, Barclay and Holderness (1992) find that in the US, large blocks of equity trade at a substantial premium to the post-trade price of minority shares, and that on average these blocks trade at a 20% premium. This supports the hypothesis that purchasers of the block of shares that may have a controlling influence receive private benefits. Other studies, taking a different approach, also support this hypothesis by comparing the price of shares that have identical dividend rights but differential voting rights. For the US, Zingales (1995) find that shares with superior voting rights trade at a premium, but that this premium is small. Therefore, while direct shareholder monitoring is a good substitute for compensation incentives, the evidence suggest that the board and monitoring by institutional investors, on the other hand, are relatively weak monitoring devices and not a good substitute for direct monitoring. Love and Rachinsky (2008) in their paper investigate the connection between ownership, corporate governance and operating performance in the banking sector for the period 2003 – 2006. Their sample consists of 107 Russian banks and 50 Ukrainian banks. Regression results showed some significant but economically unimportant relationship between corporate governance and operating performance. Tandelilin et al. (2007) examined the correlation among corporate governance, risk management and bank performance using a sample of 51 Indonesian banks for the period 1999 – 2004. For the empirical study they used a Triangle Gap Model with primary data analysis and secondary data analysis. This study revealed that bank ownership affects both the relationship of corporate governance and bank performance and corporate governance and risk management. It is worth mentioning that the model used in this study found no linear effect of corporate governance on bank performance. Rose (2007) used a sample of all Danish firms listed at the Copenhagen Stock Exchange for the period 1998 – 2001 excluding banks and insurance companies in order to examine whether ownership affects firm’s performance, measured by Tobin’s q. The cross sectional regression analysis showed that increased ownership by institutional investors did not have an impact firm’s performance. However decomposing the results, it was evident that ownership by banks had a positive significant impact on performance. Barako and Tower (2007) investigated the association between ownership structure and bank performance in Kenya. Their empirical analysis included all financial institutions operating in Kenya and ran a multivariate regression with variables referring to ownership, bank size and ROA. 29 The results provided a strong support that ownership structure influence bank performance. Specifically, board ownership is significantly and negatively associated with performance, institutional shareholders have no significant influence on performance and foreign ownership has a significant positive impact of bank’s performance. Nam et al., (2002) found that corporate governance should lead to better performance since managers are better supervised and agency costs are decreased. Poor corporate governance on the other hand is a fertile ground for corruption and poor financial performance. Brown et al (2003) found that firms with weaker corporate governance perform poorly compared to those with stronger corporate governance in terms of stock returns, profitability, riskiness and dividend payments.

**CHAPTER THREE**

**RESEARCH METHODOLOGY**

* 1. **INTRODUCTION**

This chapter deals with the method used in collecting data required in carrying out this research work it explains the procedures that were followed and the instrument used in collecting data.

* 1. **SOURCES OF DATA COLLECTION**

Data were collected from two main sources namely

Primary source and

Secondary source

**Primary source:** These are materials of statistical investigation, which were collected by the research for a particular purpose. They can be obtained through a survey, observation questionnaire or as experiment; the researcher has adopted the questionnaire method for this study.

**Secondary data:** These are data from textbook Journal handset etc. they arise as by products of the same other purposes. Example administration, various other unpublished works and write ups were also used.

**3.3 POPULATION AND SAMPLE SIZE**

The population of the study is staff of selected banks in Lagos state. A population of 200 staff of banks in Lagos metropolis was selected as the population of the study. Applying the general formula of determining sample size by Taro Yamani (1964):

* 1. **SAMPLE AND SAMPLING PROCEDURE**

Sample is the set people or items which constitute part of a given population sampling. Due to large size of the target population, the researcher used the Taro Yamani formula to arrived at the sample population of the study.

n= N

1+N(e)2

n= 200

1+200(0.05)2

= 200

1+200(0.0025)

= 200 200

1+0.5 = 1.5 = 133.

**3.5 INSTRUMENT FOR DATA COLLECTION**

The major research instrument used is the questionnaires. This was appropriately moderated. The secretaries were administered with the questionnaires to complete, with or without disclosing their identities. The questionnaire was designed to obtain sufficient and relevant information from the respondents. The primary data contained information extracted from the questionnaires in which the respondents were required to give specific answer to a question by ticking in front of an appropriate answer and administered the same on staff of the two organizations: The questionnaires contained about 20 structured questions which were divided into sections.

* 1. **VALIDATION OF THE RESEARCH INSTRUMENT**

The questionnaire used as the research instrument was subjected to face its validation. This research instrument (questionnaire) adopted was adequately checked and validated by the supervisor, his contributions and corrections were included into the final draft of the research instrument used.

* 1. **RELIABILITY OF THE RESEARCH INSTRUMENT**

Reliability test deals with the generalizing of the study. To ensure proper reliability the questionnaire was administered to some people for them to score. Also a test retest method was adopted by administering the same number of people after two weeks interval at the end the responses were received and the researcher checked the responses to see whether there were variations or consistency, the questionnaire proved very consistent.

**3.8 METHOD OF DATA ANALYSIS**

The data collected was not an end in itself but it served as a means to an end. The end being the use of the required data to understand the various situations it is with a view to making valuable recommendations and contributions. To this end, the data collected has to be analysis for any meaningful interpretation to come out with some results. It is for this reason that the following methods were adopted in the research project for the analysis of the data collected. For a comprehensive analysis of data collected, emphasis was laid on the use of absolute numbers frequencies of responses and percentages. Answers to the research questions were provided through the comparison of the percentage of workers response to each statement in the questionnaire related to any specified question being considered.

Frequency in this study refers to the arrangement of responses in order of magnitude or occurrence while percentage refers to the arrangements of the responses in order of their proportion.

The simple percentage method is believed to be straight forward easy to interpret and understand method. The researcher therefore chooses the simple percentage as the method to use. The formula for percentage is shown as.

% = f/N x 100/1

Where f = frequency of respondents response

N = Total Number of response of the sample

100 = Consistency in the percentage of respondents for each item contained in questions.

**CHAPTER FOUR**

**PRESENTATION ANALYSIS INTERPRETATION OF DATA**

**4.1 Introduction**

Efforts will be made at this stage to present, analyze and interpret the data collected during the field survey. This presentation will be based on the responses from the completed questionnaires. The result of this exercise will be summarized in tabular forms for easy references and analysis. It will also show answers to questions relating to the research questions for this research study. The researcher employed simple percentage in the analysis.

**DATA ANALYSIS**

The data collected from the respondents were analyzed in tabular form with simple percentage for easy understanding.

A total of 133(one hundred and thirty three) questionnaires were distributed and 133 questionnaires were returned.

Question 1

Gender distribution of the respondents.

TABLE I

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Gender distribution of the respondents** | | | | | |
| Response | | Frequency | Percent | Valid Percent | Cumulative Percent |
| Valid | Male | 77 | 57.9 | 57.9 | 57.9 |
| Female | 56 | 42.1 | 42.1 | 100.0 |
| Total | 133 | 100.0 | 100.0 |  |

From the above table it shows that 57.9% of the respondents were male while 42.1% of the respondents were female.

Question 2

Location of respondents

TABLE II

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Location of respondents** | | | | | |
| Response | | Frequency | Percent | Valid Percent | Cumulative Percent |
| **Valid** | Accountants | 37 | 27.8 | 27.8 | 27.8 |
| Branch managers | 50 | 37.6 | 37.6 | 65.4 |
| Customer care | 23 | 17.3 | 17.3 | 82.7 |
| Marketers | 23 | 17.3 | 17.3 | 100.0 |
| Total | 133 | 100.0 | 100.0 |  |

The above tables shown that 37 respondents which represents 27.8% of the respondents are accountants, 50 respondents which represents 37.6 % are branch managers, 23 respondents which represents 17. 3% of the respondents are customer care representative, while 23 respondents which represent 17.3% of the respondents are marketers.

**TEST OF HYPOTHESES**

Corporate governance has no effect on the financial reporting of the banks **Table III**

|  |  |  |  |
| --- | --- | --- | --- |
| **corporate governance has no effect on the financial reporting of the banks** | | | |
| Response | Observed N | Expected N | Residual |
| Agreed | 40 | 33.3 | 6.8 |
| strongly agreed | 50 | 33.3 | 16.8 |
| Disagreed | 26 | 33.3 | -7.3 |
| strongly disagreed | 17 | 33.3 | -16.3 |
| Total | 133 |  |  |

|  |  |
| --- | --- |
| **Test Statistics** | |
|  | corporate governance has no effect on the financial reporting of the banks |
| Chi-Square | 19.331a |
| Df | 3 |
| Asymp. Sig. | .000 |
| a. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 33.3. | |

Decision rule:

There researcher therefore reject the null hypothesis that state that corporate governance has no effect on the financial reporting of the banks as the calculated value of 19.331 is greater than the critical value of 7.82

Therefore the alternate hypothesis is accepted that state that corporate governance has effect on the financial reporting of the banks.

**TEST OF HYPOTHESIS TWO**

Corporate governance does not enhance management and shareholders relationship through transparency and accountability .

Table V

|  |  |  |  |
| --- | --- | --- | --- |
| **Corporate governance does not enhance management and shareholders relationship through transparency and accountability** | | | |
|  | Observed N | Expected N | Residual |
| Yes | 73 | 44.3 | 28.7 |
| No | 33 | 44.3 | -11.3 |
| Undecided | 27 | 44.3 | -17.3 |
| Total | 133 |  |  |

|  |  |
| --- | --- |
| **Test Statistics** | |
|  | Corporate governance does not enhance management and shareholders relationship through transparency and accountability |
| Chi-Square | 28.211a |
| Df | 2 |
| Asymp. Sig. | .000 |
| a. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 44.3. | |

Decision rule:

There researcher therefore reject the null hypothesis that state thatCorporate governance does not enhance management and shareholders relationship through transparency and accountability as the calculated value of 28.211 is greater than the critical value of 5.99

Therefore the alternate hypothesis is accepted that state that Corporate governance does enhance management and shareholders relationship through transparency and accountability.

**CHAPTER FIVE**

**SUMMARY CONCLUSION AND RECOMMENDATION**

**5.1 Introduction**

It is important to ascertain that the objective of this study was to ascertain the effect of corporate governance and financial reporting in Nigeria banking industry.

In the preceding chapter, the relevant data collected for this study were presented, critically analyzed and appropriate interpretation given. In this chapter, certain recommendations made which in the opinion of the researcher will be of benefits in addressing the effect of corporate governance and financial reporting in banks.

**5.2 Summary**

For so many years banks in Nigeria operated ignoring the basic duties of banking which are high degree of professionalism, transparency, and accountability. These duties or roles of the banking sector are very essential for building strong public confidence in the banking industry. It has been shown that behaving ethically is in the best interest of businesses as well as in the interest of other stakeholders in the system. To behave unethically has dire consequences for all stakeholders and for the system. Given the above it thus becomes necessary to establish frameworks with which such behaviours are measured and guided. Regulators, both professional such as the CIBN and institutional such as the CBN and NDIC, should therefore take the subject of ethics in banks governance beyond the development of codes and submission of reports. The question should not therefore be whether regulatory codes exist, as there are already too many in circulation, but that they should be enforced to a point where it would yield a remarkable change in the system, saving it of possible future downturn similar to what it was in the past

**5.3 Conclusion**

The four pillars of corporate governance which are accountability, independence, fairness and transparency cannot be deleted from financial reports of business organizations. The financial reports when they contain reliable facts and faithfulness in contents, it proves that the business organization is presenting a sustainable performance that will attract investors and relevant stakeholders. Trust and confidence have been identified over time as the key blocks for laying the foundation of survival and profitability in the banking industry.

**5.4 Recommendations**

Based on the analysis carried out and the findings deduced in addition to the review of relevant literature and open ended responses of respondents, the following recommendations are deemed necessary to ensure high ethical banking governance and operations which would invariably lead to a sound and ethical system of reporting Risk management should be transparent and ethical in order to promote the image of the banking sector. Non-compliance with the standard of reporting and disclosure requirement should be sanctioned. Executive compensation should be regularly reviewed to discourage misappropriation of firms' resources. The level of the remuneration should be sufficient and reasonable to motivate employees for higher performance.

Efforts to improve corporate governance should focus on the value of the stock ownership of board members, since it is positively related to both future operating performance and to the probability of disciplinary management turnover in poorly performing banks.

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