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Corporate Board Attributes And Financial Distress Among Insurance Companies Listed On The Nigerian Stock Exchange

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ABSTRACT

Insurance companies are perceived to be one of the key drivers of the economy as it influences the financial market. The main objective of the study is to examine the effect of board attributes on financial distress among Insurance companies listed on the Nigerian Exchange Group. The study employed Ex-post facto research design to establish the relationship between board independence, board size, frequency of board meeting and financial distress. Secondary data were extracted from audited annual reports of twenty listed insurance companies, covering 2013 to 2021 financial years using SPSS version 26 for analysis of data. Linear regression model was employed in testing the hypotheses. The findings of the study revealed that board independence has an insignificant effect on financial distress of listed insurance companies in the Nigerian Stock Exchange. This is to say that the number of non-executive directors in the board does not really affect a firm's financial status. Also it found out that board size and board frequency of meeting both have significant effect on financial distress of Insurance companies listed in the Nigerian Stock Exchange. The study therefore recommends that Insurance companies listed in Nigeria should follow the code of corporate governance on the minimum size of the board and number of non-executive directors that should be on the board.

Keywords: Board attribute, Board frequency of meeting, Board independence, Board size, Corporate governance, Financial distress.

1. INTRODUCTION

Board attributes such as board independence, board size, CEO duality, frequency of meeting have been studied by many scholars, its influence measured on firm performance. These studies have revealed that the organizations that perform better are those that are well-governed. This means that investors prefer well-governed companies to invest their money in. This has increased the interest of investors and other stakeholders on the corporate governance mechanisms established in the company especially where it concerns the Board. However, the recurrent corporate crises and failures all over the world gave rise to the review of corporate governance practices and the way they are implemented. One of the widely recognized outcome of these reviews was the establishment of the United States Sarbanes-Oxley Act, 2002 known colloquially as SOX. According to Olutuyi, 2017, SOX was built on the idea that corporate governance should not be left to the discretion of the directors and chief executives of the company.

In Nigeria there has been a multiplicity of codes of Corporate Governance issued in Nigeria such as the Code of Corporate Governance for Banks and other Financial Institutions issued in August 2003 by the Bankers' Committee in response to the alarming rate of financial crisis in the 1990s. Recently, the Corporate Governance Guidelines for Nigerian Insurance Companies (2021) was established and its

principal objective is to ensure effective administration, supervision, regulation and control of the Insurance business in Nigeria. The structure and composition of the Board should be such that the confidence of the shareholders or investors and management is maintained (Code of Good Corporate Governance for the Insurance Industry, 2021). The Guidelines however, requires that the board composition of firms should be not less than seven (7) members.

The Board of directors are the agents of the company whose responsibility is to monitor and advise the top management in the discharge of their duties to the owners of the company (Hermalin & Weisbach, 2003).

The incessant failure and scandals of notable organizations and the inability of Insurance companies to oblige in payment of claims as at when due has been a major concern all over the world especially in the Nigerian financial markets. It affected companies such as Diamond Bank, Savannah Bank, Niger Insurance, Standard Trust Insurance, National Insurance Co-operation of Nigeria (NICON), Intercontinental bank, Oceanic bank, Cadbury and the list goes on, thereby contributing to the downturn of the economy. This has increased the attention paid to the role of the Board of directors towards the transparency and financial reporting disclosures. Also it has increased the need for rebuilding public trust and investors' confidence to business reported information. With all of these, companies' sustainability has become an issue in determining the survival and continued growth of a country (Apodore & Zainol, 2014). Investors have asked what must be done to get corporations to maximize shareholders value and improve its performance.

The unique attributes of a company's board of directors is a function of the company's ability to perform well no matter the economic challenges. The absence of corporate governance practices and the inefficiency of the Board of directors in carrying out their responsibilities has led to the failure of Insurance companies to fulfill their obligation of paying the claims of their clients as at when due. This is explained by the role of the Board which is active monitoring of the managerial behavior and the alignment of the interest of both the minority and majority stakeholders (Manzaneque, Priego, & Merino, 2016)

Previous studies have examined the relationship between board attributes and firm performance mainly in other financial institutions and privately-owned companies (Hassan, Karbhari, Isa & Razak, 2017; Oziegbe & Okenwa, 2021; Araoye & Olatunji, 2019; Ghazali, 2014; Shukeri, Shin & Shaari, 2012) and very scanty studies in the Insurance industry. To the best of our knowledge, none has examined the relationship between board attributes and financial distress in the Nigerian Insurance Industry hence the need for this study. The results of this study contributes to the existing literature on corporate governance mechanisms, specifically board attributes and the likelihood of financial distress.

1.1 Objectives of the Study

The general objective of this study is to ascertain the effect of corporate board attributes on financial distress among Insurance companies listed on the Nigerian Stock Exchange. The specific objectives are:

1. To determine the effect of board independence on financial distress among Insurance companies listed on the Nigerian Exchange Group.
2. To determine the effect of board size on financial distress among Insurance companies listed on the Nigerian Exchange Group.
3. To determine the effect of board frequency of meeting on financial distress among Insurance companies listed on the Nigerian Exchange Group.

1.2 Hypotheses.

Ho1: Board independence has no significant effect on financial distress among Insurance companies listed on the Nigerian Exchange Group.

Ho2: Board size has no significant effect on financial distress among Insurance companies listed on the Nigerian Exchange Group.

Ho3: Board frequency of meeting has no significant effect on financial distress among Insurance companies listed on the Nigerian Exchange Group.

2. LITERATURE REVIEW

2.1 Conceptual review

2.1.1 Board Attributes:

The attributes of the board of directors identified and studied in relation with the likelihood of financial distress are discussed below:

2.1.1 Board Independence.

The board consists of both independent and dependent directors. An independent director is one who is not currently employed by the company or has no psychological or economic dependence on its managers (Akhmetova & Batomunkueva, 2014). They are also referred to as Non-Executive directors whereas the dependent directors are referred to as the Executive directors (Zulfiqar, Shah, Safdar, Butt, 2011). Board independence is the proportion of non-executive directors to the total number of directors on the board. In Nigeria, The Corporate Governance Guidelines for Insurance companies was issued and it became effective as at June 2021 by NAICOM. It requires that the board composition of the Insurance companies in Nigeria should not be less than seven members, with at least one independent Director who does not represent any particular shareholding interest nor hold any business interest. It also emphasizes that the Board shall consist of Executive and Non-Executive directors out of which not more than 40% of the members shall be in the executive capacity. A director who has ties with the management of the company or represents the organization that has major business deals with the company cannot be considered as independent (Baysinger & Butler (1985) as cited in Akhmetova & Batomunkueva (2012).

2.1.2 Board Size

This represents the number of directors that make up the board. It is an important attribute of the board and it can have influence on the overall board performance in respect to the effective discharge of its duties. The 2021 Code of Good Corporate Governance for Insurance companies proposed a minimum of seven members. The size of the board can be too large to effectively carry out its duties. It has been argued, however that large board size has a lack of coordination, which precludes strategic decision-making (Ud-Din, Khan, Javeed & Pham, 2020). Disagreement among board members slows down decision-making process while a large number of board members is a burden on the corporate resources. This disagreement among the board members has great benefits for the management who may start to secure their self-interest (Ud-Din et al, 2020). In other words, it can be said that a small board plays a more significant role and also has effective control over the management than a large board size. Smaller boards are more effective in monitoring for being more productive, connected and easier to interact and discuss the issues that are brought up (Coles, Naveen & Naveen, 2008). More value is added to the company with smaller boards. Larger boards tend to suffer from free-riding, social loafing and higher coordination costs. Meanwhile, the advantages of having a larger board includes not being totally influenced by the managers because it is made up of different individuals with different characters and from different fields of life (heterogeneous) who have different skills and knowledge and so they cannot easily be influenced. The performance of the managers can be monitored and controlled more effectively in order to achieve goal congruence. Nevertheless, it can be said that it is more advantageous to have a smaller board size than having a large board size.

2.1.3 Board Frequency of Meeting

The board of directors have to be active and committed so as to ensure high quality and transparent reporting in annual reports. In the Code of Corporate Governance Guidelines for Insurance Industry 2021, it states that the Board shall not meet less than four (4) times in a year. Boards that meet frequently are most likely to carry out their duties diligently and effectively (Aronokhale, 2017). Diligent boards are also likely to enhance the level of oversight of the financial reporting process directly and indirectly through the choice of external auditor and the composition of the audit committee (Kent & Clarkson, 2006).

2.1.4 Financial Distress

A firm is financially distressed when it experiences difficulty to meet up with its financial obligations especially to its creditors. The problems of financial distress arise when the companies have difficulties to pay the financial commitment (Khaliq, 2014).

A company facing financial difficulties has a higher probability to end up in bankruptcy and this can bring bad reputation to the company. The users of financial statements such as creditors are observing for the liquidity ratios in their analysis as it can give the information whether the cash flow from operation is able to cover the short-term obligation (, 2009; Fawzi, Kamaluddin & Sanusi, 2015). A company in distress, it is expected, experiences high cost due to one reason or the other. One of the costs may be their employees turning out to be less productive because of their fear of job loss and their deteriorating self-confidence. Also, disaster occurs when the current and prospective investors withdraw their capital or refuse to invest in the company thereby reducing capital. This causes the survival of the company to be at stake. Furthermore, the company will tend to incur more borrowings in order to strive in the market and this leads to the challenging scenario of having to fulfill the current and future commitments when they are in a distressed situation (Khaliq, 2014).

2.2 Theoretical Review

2.2.1 Agency Theory

This study is anchored on the Agency theory. Due to its relevance in resolving conflict that may arise between the principals and the agents, the Agency theory is defined as the relationship between the agents, that is, the company executives and the principals who are the shareholders. Shareholders who are the owners of the business do hire the agents to perform their duties. Principals delegate the running of the business to the managers, who are the agents (Clark, 2004). Again, shareholders are expected to trust the agents who are supposed to carry out their duties and make decisions to the best interest of the shareholders. This means that the CEO presumably is the one who takes the decision on what kind of information is presented to the Board. For a company to survive, there should be a separation of duties between the CEO and the Chairman of the Board. This means that the quantity and quality of information given determines the ability of the Board to monitor and evaluate the firm's performance. When there is inadequate information, it leads to information asymmetry. Agency problems arise when the decision makers are not the major residual claimants, who bear all the risks associated with the decisions taken. Without control, decision makers can neglect the interest of residual claimants (Fama & Jensen (1983) cited in Akhmetova & Batomunkueva (2014). Unfortunately to the detriment of the principal, the agent may have his own interests and may seek to satisfy them. This can create agency problems. Indeed Agency theory can be employed to explore the relationship between the ownership and management structure. Where there is a separation, the agency model can be applied to align the goals of the management with that of the owners -shareholders (Solomon & Obah, 2018).

2.2 Empirical Review

Mohamed S. E. & Maha S. R. (2020) in their study examined the Impact of Financial Distress, Firm Size, and Audit Quality on Earnings' Management Evidence from Companies listed in the Egyptian Stock Exchange. A sample of 42 companies listed in the Egyptian Stock Exchange market were used from the period 2015-2017. Regression analysis was also used to test the variables. The research results showed that financial distress and audit quality have a significant impact on earnings management practices. However, the researcher failed to find a significant effect for firm size on earnings management. They also recommended that this study be extended to include larger sample and a more recent period including the financial distress as a result of COVID 19 pandemic. This means that the financially distressed companies are expected and encouraged to enhance the image of the company in the eyes of their investors and creditors by practicing earnings management.

Ud-Din, Ya Khan, Javeed and Pham (2020) in their study examined the relationship between Board Structure and Likelihood of Financial Distress. A sample of 146 non-financial listed firms listed on the

Pakistan Stock Exchange (PSX) was used for a period of 15 years, from 2005 to 2019. Altman Z-Score was also used as a proxy for firm financial distress. Descriptive statistics and panel logistic regression were used for analysis. The study exhibits a significant negative relationship between board size, board independence and the likelihood of financial distress. This implies that large companies have a low probability of financial difficulty due to their experiences and capability. Also, leverage is found to be positive and significant, which suggests that debt financing can increase the probability of financial distress. Therefore, the study suggests that the role of independent non-executive should be clearly defined in the Code of Corporate Governance.

Bakare (2019) in his work on Board Independence and Audit Quality in Nigeria examined the relationship between board independence and audit quality of firms. He sampled 71 non-financial firms and for the period 2009 to 2016. Data collection data was done with secondary source documents. Analysis was also carried out with the binary logit regression. The findings of the study revealed that board independence is negatively related to audit quality. This is possible because board independence which is one of the corporate governance mechanisms can be used as a monitoring tool and ensures quality financial reporting. The study recommended that the composition of non-executive directors as members of the board should be sustained and improved upon.

Kenge (2018) examined the Effect of Corporate Governance on Financial Performance of Companies listed at the Nairobi Securities Exchange, Kenya. 35 listed companies were used as the sample. Secondary source of data was used and the multivariate regression analysis used to analyze the data. The study revealed that board composition has a negative and significant effect on financial performance while board size and CEO duality have positive effect on financial performance. It also determined that shareholders' ownership has an insignificant effect on financial performance of companies in Kenya. They recommended that a good balance between the non-executive and the executive members of the Board should be in place so as to ensure high level of autonomy.

Akhmetova and Batomunkueva (2014) in their study, Board Composition and Financial Distress: An Empirical Evidence from Sweden and Denmark was able to reveal that board independence, board ownership, employee representatives and market capitalization (which is the control variable) have significant relationship with likelihood of financial distress. The cross-sectional research design was adopted while multiple and binary regression analyses were used. The study revealed that board size has shown no significant relationship with financial distress. From the above, it was revealed that companies with more independent directors have superior performance with the ability to call to order or to dismiss any under-performing CEO after poor performance thus, bringing benefit to the company.

Miglani, Ahmed and Henry (2014) examined the role of Voluntary Corporate Governance mechanisms in mitigating the financial distress status of firms. A sample of 171 financially distressed and 106 healthy listed firms in Australia was used for a period of 5 years, 1999 to 2003. Secondary source of data collection was used and the Descriptive Statistics and the Univariate t-test used to analyze the data. The findings revealed that there was no significant relationship between board independence, CEO Duality and financial distress of the sampled firms.

3. MATERIALS AND METHOD

In this study, the researcher adopted the Ex-post facto research design. The Ex-post facto is a type of design in which the source data cannot be altered as at when information is being collected. The researcher used the data from the readily available financial statements of the sampled companies through the internet. The period chosen is from 2013 to 2021. The population of the study includes all insurance companies listed on the Nigerian Exchange Group as at December 2021. Purposive sampling method, a non-probabilistic method was used, sampling 20 insurance companies; this is influenced by the availability of the annual reports. The revised Altman Z-score (1993) was used as the accounting-based tool measuring the dependent variable, financial distress. Also, the linear regression model was used to analyse and test the hypotheses using SPSS version 22 at 5% level of significance.

The model used and improved upon was adopted from the work of Onyema and Ezeagba (2022). It is represented as follows:

$FD_{it} = \beta_0 + \beta_1 BS_{it} + \beta_2 BI_{it} + \beta_3 BF_{it} + \beta_4 FSZE_{it} + e_{it}$

Where:
FD = Financial distress measured using the revised Altman Z-score model (1993)
BS = Board size measured as the total number of directors on the Board
BI = Board independence measured as the percentage of non-executive directors to total directors
BF = Board frequency of meeting measured as the number of meetings held by the Board within a year
FSZE = Firm size measured as the natural logarithm of total assets
β_0 = Intercept; β_{1-8} = Unknown Coefficients; $_{it}$ = company i in year t; e_{it} = error term of firm i at time t.

4. RESULTS AND DISCUSSIONS

4.1 Descriptive analysis

Table 4.1 Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
FINDISTRESS	20	-3.81	3.59	1.3665	1.73793
BOARDINDP	20	14.29	70.00	56.8137	12.54798
BOARDSIZE	20	7.00	13.00	10.2000	2.48363
BOARDFREQ	20	16.00	50.00	38.4000	8.68998
FIRMSIZE	20	9.98	10.58	10.2762	.15982
Valid N (listwise)	20				

Source: Extract from SPSS 26.0 Printout result

In the table 4.1 above, the characteristics of the variables from the twenty sampled Insurance companies are shown. It shows the mean value of financial distress to be approximately 1.3665. This means that on average, the Z-scores of Nigerian Insurance firms listed in the Nigerian Exchange Group is 1.37 in the last nine years. This is to say that the Insurance firms listed in the Nigerian Exchange Group are safe and non-distressed because according to Altman (2002), Z-score values between 1.1 and 2.6 are considered the "grey zone" or zone of ignorance. 57% of the directors in the Board of Insurance companies listed in the Nigerian Exchange Group are mostly non-executives. This shows a high level of independence of the non-executives to the executive members. It also shows the mean value of board size to be 10, this means that on the average the board size of most of the Insurance companies listed in the Nigerian Exchange Group is not less than 10. The mean number of times board meetings are held is approximately 38 for the year.

4.2 Hypothesis Testing

4.2.1 Hypothesis One

Ho1: Board independence has no significant effect on financial distress among Insurance companies listed on the Nigerian Exchange Group.

The statistical procedure used by researchers to explore the relationship that may arise between a particular dependent variable and two or more independent variables is the linear regression analysis. In this study, the linear regression is used to test the variables.

Table 2: Analysis output for linear regression model 1

Variables	Coefficient	t-values	P-values	Tolerance/VIF
Constant	13.04	.439	.666	
BOARDINDP	.196	.759	.458	.819/1.220
FIRMSIZE	-.117	-.453	.658	.819/1.220
R	.267[a]			
R^2	.072			
Adj R^2	-.038			
Durbin- Watson	.811			

a. Dependent Variable: FINDISTRESS
Source: SPSS Version 26. Analysis Results 2023

4.2.1.1 Discussion of Result

In Table 2 above, it shows an R^2 of 0.072 which indicates that 7.2 percent of the variation in financial distress can be explained by variability in board independence. This means that financial distress changes by 7.2% when the independent variable changes. The result for the test of hypothesis 1 showed that BOARDINDP show a positive (β = .196) but statistically insignificant (p = .458) effect on financial distress.

4.2.1.2 Decision: The p-value is significant if it is less than 5% significance level. The calculated p-value of board independence is 0.458 which is greater than 5 percent making it is insignificant at 5 percent. This implies therefore, that board independence has no significant effect on financial distress among Insurance companies in Nigeria. This means that a unit increase in the number of non-executive members in the board leads to an insignificant decrease on the likelihood of financial distress. The Durbin-Watson test checks the auto-correlation among the variables studied. Its value of 0.799 which is less than 2 means there is no auto-correlation among the variables.

4.2.2 Hypothesis Two

Ho2: Board size has no significant effect on financial distress among Insurance companies listed on the Nigerian Exchange Group.

Table 3: Analysis output for linear regression model 2

Variables	Coefficient	t-values	P-values	Tolerance/VIF
Constant	51.51	2.958	.009	
BOARDSIZE	.825	5.167	.000	.862/1.160
FIRMSIZE	-.507	-3.175	.006	.862/1.160
R	.792[a]			
R^2	.627			
Adj R^2	.583			
Durbin- Watson	1.013			

a. Dependent Variable: FINDISTRESS
Source: SPSS Version 26. Analysis Results 2023

4.2.2.1 DISCUSSION OF RESULT

In Table 3 above, it shows an R^2 of 0.792 which indicates that 7.9 percent of the variation in financial distress can be explained by variability in board independence. This means that financial distress changes by 7.9% when the independent variable changes. The result for the test of hypothesis II showed that BOARDSIZE show a positive (β = 0.825) value but statistically significant (p = .000) effect on financial distress.

4.2.2.2 Decision: The p-value is significant if it is less than 5% significance level. The calculated p-value of board size is 0.000 which is less than 5 percent making it is significant at 5 percent. This implies

therefore, that board size has a significant effect on financial distress among Insurance companies in Nigeria. This means that a unit increase in the number of members in the board leads to a significant decrease on the likelihood of financial distress. The Durbin-Watson test checks the auto-correlation among the variables studied. Its value of 1.013 which is less than 2 means there is no auto-correlation among the variables.

4.2.3 Hypothesis Three

Ho3: Board frequency of meeting has no significant effect on financial distress among Insurance companies listed on the Nigerian Exchange Group.

Table 4: Analysis output for linear regression model 3

Variables	Coefficient	t-values	P-values	Tolerance/VIF
Constant	24.41	1.220	.239	
BOARDFREQ	.646	3.600	.002	.994/1.006
FIRMSIZE	-.251	-1.396	.181	.994/1.006
R	.675[a]			
R^2	.455			
Adj R^2	.391			
Durbin- Watson	1.312			

a. Dependent Variable: FINDISTRESS
Source: SPSS Version 26. Analysis Results 2023

4.2.3.1 DISCUSSION OF RESULT

In Table 3 above, it shows an R^2 of 0.455 which indicates that 4.6 percent of the variation in financial distress can be explained by variability in board independence. This means that financial distress changes by 4.6% when the independent variable changes. The result for the test of hypothesis III showed that BOARDFREQ show a positive ($\beta = 0.646$) value but statistically significant ($p = .002$) effect on financial distress.

4.2.3.2 Decision: The p-value is significant if it is less than 5% significance level. The calculated p-value of board frequency of meeting is 0.002 which is less than 5 percent making it is significant at 5 percent. This implies therefore, that board frequency of meeting has a significant effect on financial distress among Insurance companies in Nigeria. This means that a unit increase in the number of meeting held by the board members lead to a significant decrease on the likelihood of financial distress. The Durbin-Watson test checks the auto-correlation among the variables studied. Its value of 1.312 which is less than 2 means there is no auto-correlation among the variables.

5. CONCLUSION AND RECOMMENDATIONS

The study specifically concludes that board size and board frequency of meeting do have a significant effect on financial distress while board independence have insignificant effect on financial distress. This means that a unit increase in the number of board directors and the number of times the board meets leads to a significant decrease in the probability of the company being financially distressed while a unit increase in the number of non-executive directors does not decrease significantly the possibility of the firm being financially distressed. The study therefore recommends that Insurance companies listed in Nigeria should follow the code of corporate governance on the minimum size of the board and number of non-executive directors that should be on the board. The number of times the board should meet should be improved upon so as to enhance the supervisory role of the board on the management.

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