Board of directors and corporate governance in Nigeria

Kunle Aina

Department of Private and Business Law, Faculty of Law, University of Ibadan, Ibadan, Nigeria. E-mail: kunleaina@hotmail.com.

ABSTRACT

The board of directors of a company is a very important organ not only responsible for management but also for adopting good corporate governance and practice in the company. This paper discussed and analyzed with the aid of comparative law, the Code of Corporate Governance in Nigeria and its effect on the board structure, the role, effectiveness and duties of the non-executive directors (NEDs) and how their independence can be assured, guaranteed and monitored to enhance the board’s effectiveness, ensure full compliance with the codes of corporate governance. The regime of compliance and regulation is extremely weak and a case is made for a specialized regulator agency to monitor compliance with the codes, upgrade standard and harmonize the different codes.

INTRODUCTION

An efficient, effective and accountable Board of Directors is not only essential to every company but is now demanded by the Code of Corporate Governance in almost all civilized jurisdictions of the world. The Board of Directors in fact is the most important organ of the company solely responsible for the management of the company. 1 The principal objective of the board is to ensure that the company is properly managed.2 The board must act responsibly in ensuring an effective performance of the management in order to protect and enhance shareholder value and to meet the company’s obligations and other stakeholders3. The Cadbury Report4 defined corporate governance as “the system by which companies are directed and controlled”. Whilst management processes have been widely studied relatively little attention has been paid to the processes by which companies are governed. It is clear that good corporate governance practice adopted by a board of directors is reflected in the value it adds to its operations and insulates generally the company from corporate failures. The failure of big corporate organizations all over the world without any prior sign or indications ultimately points to loose and fraudulent practices which ordinarily would have been detected by the regulators where a good corporate governance practice had been in force.5

Nigeria like most other jurisdictions has also developed its peculiar Code of Corporate Governance, which unfortunately, is yet to be combined6. Therefore, different codes are applicable to different sectors of the economy. This paper looked at the board of directors as currently structured under CAMA 2004 and the impact of the different Codes on Corporate Governance. Also, the author considered the one-tier board structure and their effectiveness, the role of non-executive director (NED) on the board and conclude with recommendations for

---

1Section 63 (1) and (3) Companies and Allied Matters Act 1990. Cap C20, Laws of the Federation 2004 (hereinafter called CAMA).
2Code of Corporate Governance for Public Companies in Nigeria issued by the Securities and Exchange Commission (hereinafter called SEC Code)
3SEC Code
4The Report of the Committee on the Financial Aspects of Corporate Governance otherwise known as the Cadbury Report published in 1992 and was later described as a “landmark in thinking on Corporate Governance”. The report included a Code of Best Practice (The Cadbury Code).
5Sir Adrian Cadbury’s speech on the 20th Anniversary of the Corporate Governance Code Event – October 2012.
6Unlike the English Combined Code or the South African King’s Code IV.
WHY IS CORPORATE GOVERNANCE IMPORTANT?

A Company should have objectives. Generally, the most important objectives are required to be written out in the companies memorandum and articles of association. Historically, this is so mandatory and serious that where the company goes beyond its stated objects such act is beyond its powers and illegal and must be rendered null and void. The important objectives and essentially, the way and manner of achieving these objectives are never stated in the registered documents and may only be ascertained in the internal documents of the Company.

Corporate governance is therefore not about the day to day operational management of the company by the managers and executives, but is concerned with the overall strategic plan to move the company forward. Good corporate governance enhances the value of the company and attracts investment to the company. It enables the company to meet its objectives and contributes to its growth and profits. On a national scale, countries that adopt good corporate governance models attract more direct foreign investments than those that ignore its principles. The root cause of most corporate failures can be attributed to failure of corporate governance. Due to the importance of some of these big companies to the economy of the nation and stability of the economy, the governments of developing countries like Nigeria have now taken the issue of corporate governance more seriously.

DEVELOPMENT OF CORPORATE GOVERNANCE IN UK

In the United Kingdom, following the scandals that brought down big companies like Maxwell, Polly Peek, Barrings, which affected the City of London and the financial markets during the late 1980s. The Sir Adrian Cadbury Committee was set up to look into the financial aspects of corporate governance by the Financial Reporting Council, the London Stock Exchange and the Accounting profession. The Committee reported in 1992 and concluded that the issue of corporate governance is not a matter for legislation. The Cadbury Report also produced a code of best practice divided into 19 provisions and 14 notes dealing with board of directors, and setting up of board committees structure, remuneration, financial reporting and the relationship between the board and auditors. The Securities and Exchange Commission (SEC) Listing Rules in London was modified in compliance with the Cadbury Report and part of the Listing Rules was that companies are to state in their Annual Returns whether they have complied with the Cadbury Code or to explain why the non-compliance.

In 1995, following the alarming and unregulated remunerations being paid to the directors and senior executives of newly privatised utility monopolies by the so called ‘Independent Remuneration’ Committees, the Greenbury Committee on Directors’ Remuneration was convened in January 1995 and submitted its report in July 1995. The Greenbury Report also issued a Code of Best Practice on establishing remuneration committees for disclosure of much more important disclosures on the remuneration of directors. The Code was also adopted into the Listing Rules on comply or explain basis.

The same year, a working group was set up to look into the relationship of companies and institutional investors. The group was chaired by Paul Myners and produced the Myners Report. The report included suggestions on the operational behaviour of institutional investors, their role as shareholders and as responsible investors; they ought not to sell their shares when a company is not doing well, but to contribute their quota by assisting the company. A review was carried out by Government in 2004. A Committee on Corporate Governance was set up to review the recommendation of the Cadbury and Greenbury Reports. The Committee was chaired by Sir Ronald Hampel. The Committee was referred to as the Hampel Committee and its report was published in 1998. The important addition to the development of corporate governance by the Hampel committee stems from the criticism leveled against the earlier committees that the companies only “box tick” and do not in fact comply with the principles and rationale that underpin these set of principles. Listed companies must therefore “comply with not only the principles but also the provisions that forms the basis of these principles”. Where they are unable to do this, they must explain such non-compliance. This suggestion was adopted in Section 27 CAMA 2004.

The first version of the UK Code on Corporate Governance was produced in 1992 by the Cadbury Committee. In paragraph 2.2, thereof, the codes states as follows ‘Corporate Governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The responsibilities of the Board include setting the Company’s strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board’s actions are subject to laws, regulations and the shareholders in general meeting.

12Myners Reports
14The Companies are to “apply” with the 18 principles drafted by the Hampel Committee and to state whether they “complied” with the 42 provisions which forms the basis of the SEC Rules.
“The Combined Code”

In September 1999, the Institute of Chartered Accountants of England and Wales published a report on internal control pursuant to the provisions of the Combined Code. The Combined Code provided that companies should “maintain a sound system of internal control” and should conduct an annual review of “the effectiveness of the system of internal control” which should be reported to shareholders. The Turnbull Committee produced a short booklet known as “Turnbull Guidance on Internal Control” and made a number of important guidelines which companies can introduce to assist in their internal control mechanism and avoidance of risk.

By the year 2003, two important committee works were added to the growing literature and development of corporate governance in UK. These are the Higgs Report commissioned by the government which considered the role and effectiveness of the NEDs. The second report was the Smith Report which was commissioned by the Financial Reporting Council (FRC); the Smith Committee Report provided the much needed guidance for audit committees. The responsibility for the combined code was transferred to the FRC, and in 2003, a revised combined code was published incorporating the Higgs and Smith recommendation. In 2010, the FRC which had been responsible for the combined code and the guidelines reviewed the combined code and published the UK Corporate Governance Code. The FRC also incorporated in the UK Corporate Governance Code the Walker report of 2009, which dwelt on the corporate governance in the Banking Industry in UK. The current Code of Corporate Governance was issued in 2012.

The European Union (EU) and the EU Directives have also imposed stricter rules on disclosure of directors’ remuneration which are now part of the UK Listing Rules. The Companies Act 2006 statutory duties on directors that had been basically Common Law duties.

The FRC also issued the UK Stewardship Code which can be traced to ‘The Responsibilities of Institutional Shareholders and Agents: Statement of Principles’ which was first published in 2002 by Institutional Shareholders Committee (ISC) and later converted to a Code in 2009.

CORPORATE GOVERNANCE CODES IN NIGERIA

Development of company in Nigeria

Evolution and development of company in Nigeria coincided with the discovery of the wider world such as Columbia, West Indies etc. The aim of the adventurers was trading; this period also opened the way for companies like Royal Niger Company to come to sub-Saharan Africa and had been involved in trading activities in the Niger-Delta zone of the territory later known as Nigeria. The first legislation on companies was enacted in 1921 known as Company Ordinance 1912 which for the first time made provisions for incorporation of companies in Nigeria. This Act was based on the 1908 Consolidation Act of Great Britain. After the amalgamation of the country in 1914, the Companies Amendment and Extension Ordinance extended the provisions of the Act to cover the entire country. In 1922 the earlier ordinance was repealed and replaced with the Companies Ordinance of 1922. This ordinance was later changed to Companies Act and appeared as Chapter 37 of the 1958 Laws of the Federation. This was the Law in force in Nigeria until the Companies Act of 1968. The 1968 Act was based on the English Companies Act of 1948 and the only deviation was the provisions on mandatory registration by foreign companies in Nigeria. The 1968 Act was in force in Nigeria for about Twenty-two years until the enactment of the Companies and Allied Matters Act 1990. The CAMA 1990 is currently the law in force in Nigeria. It is quite interesting that while major jurisdictions and especially UK had continued to review their laws, the Nigerian law had remained stagnant and unprogressive.

The road to the codes

Following the independence of Nigeria in 1960, the Government due to the exigencies of the period and the government’s anxiety to cause rapid development, the country kick start the industrial growth and economic self-
dependence of the post-colonial Nigeria. The state not only did not permit individual control of public utilities such as electricity, water, telecommunications, postal services, air travel etc. The virtual monopoly of government in the provision of infrastructure and development in many ways contributed to the underdevelopment of the country. The government enacted two important pieces of legislations, these are the Foreign Exchange Control Act 1962 and the Nigerian Enterprises Promotion Decree (now Act) No 4, of 1972 and 1980. The Foreign Exchange Control Act 1962 prohibited the transfer of any security or interest in a security in favour of a person resident outside Nigeria except with the permission of the Minister; in fact it is a criminal offence to do so. The effect is to discourage foreigners from investing in Nigeria generally. Whilst the Indigenisation Decree even with the several amendments, was calculated to encourage Nigerians to own certain enterprises in Nigeria and also restrict foreign investment in manufacturing sectors of the economy.

The plan of government in enacting these laws was to transfer the control of the economic activities from the foreign control to indigenous control by local businessmen. Unfortunately, the laws failed to achieve these lofty ideals and have no significant impact on the corporate governance and development in the country. Unfortunately, until the two enactments were repealed there was no significant impact on the economy. The laws do not mention anything on corporate governance. The government also enacted the Nigerian Enterprises Promotion Act of 1995 (NEPC) to encourage and promote investment in the Nigerian economy, also with no reference to corporate governance of companies.

Intervention of government in corporate governance

Not until the enactment of the CAMA 1990 can we say that the government was really interested in corporate governance in Nigeria. However, there was no conscious effort made in this direction until the SEC set up a committee to look into the issue of corporate governance under the chairmanship of Atedo Peterside known as Peterside Committee on Corporate Governance in Public Companies. The committee submitted its report in October 2003. This led to the issue of the code of corporate governance for public companies. The same year saw the Central Bank also issuing a code of corporate governance for banks and other financial institutions in Nigeria. This code came about as a result of the work done by the Bankers’ Committee of the bank, chaired by the United Bank for Africa. However, in spite of the codes in 2003, the banking subsector in Nigeria was characterized by weak and fragile banks, as far back as 1989-1991 there has been noticeable financial crisis as some seven distressed banks failed and caused huge disruptions in the economic stability of the country. The interbank market also collapsed in 1993 and which spread to all segments of the financial system in 1995. The Banking system was characterized with poor corporate governance, poor monitoring and reporting mechanism, very low minimum capital requirements. There were eighty-nine small banks most at the brink of failure. This was the position before consolidation of Banks in Nigeria. The Central Bank of Nigeria (CBN) thereafter, realizing that the “ongoing industry consolidation is likely to pose additional corporate governance challenges arising from integration processes, IT and culture. Research had shown that two-thirds of mergers, worldwide, fail due to inability to integrate personnel and systems as well as due to irreconcilable differences in corporate culture and management, resulting in board and management squabbles. In addition, the emergence of mega banks in the post-consolidation era is bound to task the skills and competencies of boards and management in improving shareholder values and balance same against other stakeholder interests in a competitive environment. A well-defined code of corporate governance practices should help organizations overcome such difficulties.”

The above was one of the avowed rationales for the review of the Bankers Committee Code of Corporate Governance for the Banking industry. The CBN issued the current Code of Corporate Governance with effective date fixed for the April 3, 2006. Compliance with the provisions of the Code is mandatory.

In 2008, the SEC inaugurated a national committee chaired by M.M.B. Mohammed for the “review of the 2003 Code of Corporate Governance for Public Companies in...”
Nigeria to address its weaknesses and to improve the mechanism for its enforceability. The Committee was to identify the weaknesses in and constraints to good corporate governance and to recommend ways of effecting greater compliance. The SEC issued the new code in April, 2011.

National Insurance Commission also issued a separate Code of Corporate Governance for Insurance Industry in February, 2009 (hereinafter called NAICOM Code) which was sector specific though stated to be in consonance with the 2003 version of Code of Corporate Governance issued by the SEC. The NAICOM Code considered the following as the basis for the sectorial mode:

1. Compliance with rules, laws, regulations and principles guiding insurance business;
2. Differences between Board and Management giving rise to board squabbles;
3. Ineffective board oversight functions;
4. Fraudulent and self-serving practices among members of the board, management and staff;
5. Overbearing influence of chairman or MD/CEO, especially in family controlled business;
6. Weak internal controls;
7. Passive shareholders;
8. Power of controlling shareholders over minority shareholders;
9. Ineffective management information system;
10. Increasing level of societal awareness about the sector;
11. Conflict of interest.

The NAICOM Code made some important contributions to development of corporate governance in Nigeria far beyond the SEC Code. A year earlier, the National Pension Commission (PENCOM) a body established under the Pension Reform Act 2004 with the principal object of regulating, supervising and ensuring the effective administration of pension matters in Nigeria. The PENCOM also issued a Code of Corporate Governance to guide and regulate the registered Pension Fund Administrators (PFA) and Pension Fund Custodians (PFC). The provisions of the PENCOM Code was based on the principle of comply or explain basis. The Pension Code (PenCode) is another important sectorial code existing side by side with the SEC Code. It is not clear in cases of conflict, whether the SEC Code will prevail over the PenCode and which code ought to be observed by the PFA or PFC that is also listed with the Stock Exchange.

THE BOARD OF DIRECTORS

Meaning of directors

The Companies Act do not define the term ‘director’ but seemed to describe or ascribe a meaning to it. Section 244(i) of CAMA 1990 merely stated that “directors of a company under this Act are persons duly appointed by the company to direct and manage the business of the company.

Section 650 also defines the director as including ‘any person occupying the position of directors by whatever name called’. It may be easier to understand the position of the director by simply understanding their role and duties in the Company. The law is that the board of directors is the sole organ of the company responsible for the management of the company. In Nigeria, every company must have a minimum of two directors, while in UK a private company must have at least one director and a public company must have two directors. The Act is silent on the day to day role and power of the directors and has been left to the company articles. There is also no mention of the way and manner the board ought to be organized and it follows that each company apart from appointing members of the board must also specify the structure, role and powers of its directors in the articles of association. The first directors are appointed by the subscribers to the memorandum and articles of association while subsequent appointments are made by the general meetings. The Act does not also give any indication as to the type of person that may be appointed and the quality or qualification they possess. This is also left to the discretion of the members. However, the law listed certain categories of persons that are disqualified from being appointed as directors in Nigeria. Section 257 listed the following:

1. An infant, that is, a person under the age of 18;
2. A lunatic or person of unsound mind;
3. A person disqualified under Sections 253, 254, and 258 of the Act;

---

4Section 63(3) CAMA 1990.
4Section 246(1) CAM 1990.
4Section154 UK Companies Act 2006 (UK Act).
4Section 247 CAMA 1990, The names may also be listed in the articles of association.
4Section 248; ‘The members in general meeting shall have the power to re-elect or reject directors and appoint new ones’.
4. A corporation other than its representative appointed to the board for a given term.

We must note quickly that the disqualification of these categories of persons is not only uncalled for but may be difficult to enforce. For instance, the disqualification of an infant in this jet age where it is possible for a child under 18 to be enterpriseing enough to establish his own business, though the Act allows an infant if he joins with two other persons not disqualified as subscriber to the memorandum. If the so called infant understands the effect of his action, there ought not to be any restrictions on his right to be appointed a director; in any case, it is the preference of the shareholders of the Company. In Nigeria, there are no proceedings to declare a person a lunatic or person of unsound mind, and only except where the unsoundness is obvious, it will be difficult for this subsection to disqualify anybody. The other provisions on disqualification are obviously unenforceable.

**Types of directors**

There are two main categories of directors, the executive and the NEDs. The executive director is a full time officer of the company, who may generally be appointed under a contract of service with the company. The articles normally provide for the appointment of the executive director and he is normally part of the management team but usually as the head of specific department in the company. They are professionals who are required to be qualified for their office either by educational qualification or cognate experience or both. The executive director has been described as an employee of the company with a proper contract of service with the company.

The NEDs are normally appointed to the board (mainly in public companies) to act as monitors of the executive management. Their appointments are typically on part-time basis and are only expected to attend meetings without having any office in the company. Their position is adversarial mainly and is not expected to participate in the day to day management of the company. A shadow director is simply a person on whose instructions and directions the directors are accustomed to act. In order to avoid the duties imposed on directors by the Act and common law, certain persons may decide to stay underground and ‘pull the strings’ to control the de facto directors, the law will ascribe the role to such a person and he will be held liable for any breach of duty by the de facto directors. But a professional person may not be a shadow director if he only acts in a professional capacity. If however, his conduct amounted to effectively controlling the company’s affairs, he will be held to be a shadow director. Millet J. in the case of Re Hydrodam (Corby) Ltd identified four factors to consider in determining whether or not an individual is shadow director.

1. The de jure directors of the company must be identifiable;
2. That the person is question directed those directors on how to act in relation to the company’s affairs or that he was one of the persons who did;
3. That the directors did act in accordance with his instructions;
4. That they were accustomed to so act.

Millet J. went further when he stated that, it must be shown a pattern of behaviour, ‘in which the board did not exercise any discretion or judgment of its own but acted in accordance with the directions of others’.

The shadow director must also be proved to have exercised control over the whole board and not individual director.

**Size and composition of the board**

One of the primary responsibilities of the board is to ensure good corporate governance in the company. The SEC Code states thus, ‘... the board should ensure that the company carries on its business in accordance with its articles and memorandum of association and in conformity with the laws of the country observing the highest ethical standards and on an environmentally sustainable basis’.

The above is unattainable unless the board is properly constituted in terms of size and composition. The SEC Code provides that membership of the board should not be less than five, but on a general note the “Board should be of a sufficient size relative to the scale and complexity of the company’s operations and be composed in such a way as to ensure diversity of experience without compromising independence, compatibility, integrity and availability of members to attend meeting”. While the Act does not specify or make it mandatory that companies should appoint NEDs, the SEC Code makes it mandatory for all companies to appoint executive and

---

53In the U.K the minimum age is 16, but the restriction on age ought to be removed entirely from the Act and leave the discretion to the shareholders. The 2006 Act ade copious provisions on the issue including exceptions from minimum age requirement etc, if the issue of minimum age had been left to the General Meeting, the Company will be in the best position to ascertain the desirability of appointing an infant as director.
54Per Salami JCA in *Longe v. First Bank Plc* (2006)3NWLR (p967) p.228 CA; you may see also the Supreme Court decision that overruled the Court of Appeal decision in SC116/2007 delivered on 5-3-2010.
55Section 254 CAMA 1990.
56Re Tashbin Ltd (No. 3) (1993) BCLC297.
57(1994) BCCL 61.
NEDs and must be mixed in such a way that the majority of the board are NEDs and also at least one of whom should be an independent director.

The board’s effectiveness is dependent on its size and composition. The board must not be too big as to become unwieldy and uncontrollable which will result in time waste before simple decisions would be arrived at, or too small that will exclude the necessary knowledge, skills and experience to make effective decisions. The right mix also of the executive and NEDs is also very important69. Executive directors are in a better position to ascertain the core professional issue and decisions to be taken80 while a proper and proportionate balance61 of the executive and NEDs will bring a proper and genuine growth62 and quality decision backed by experience.63 In an ideal world, all boards of directors would comprise a diverse group of experienced and talented individuals all of whom would expose and practice the characteristics and values of good commercial sense, courage, openness and integrity64. The Higgs Review,65 suggested thus, an effective board should not be so large as to become unwieldy. It should be of sufficient size that the balance of skills and experience is appropriate for the requirement of the business and that changes in the board’s composition can be managed without undue disruption.

In England, Principle A3 of the Combined Code states, the board should include a balance of executive and NEDs (or in particular independent non-executive directors) such that the individual or small group of individuals cannot dominate the Board decision-taking.66

In Nigeria, the SEC Code provides that the majority of the board members should be NEDs and at least one of them should be an independent director.67 The officers of the board will therefore comprise the following:

1. The chairman who should be a NED68;
2. The chief executive officer (CEO) or Managing Director, who is the head of the management team

and is answerable to the Board69;
3. Executive Directors;
4. Non-executive directors (NEDs);
5. Independent Directors.

In the UK, a key principle of good corporate governance is that there should be a balance of independent NEDs on the board to create a balance of power between the executive and NEDs. In South Africa, which adopted the unitary board, the King III Code also recommended that the majority of the directors should be NEDs and majority of them should be independent. In South Africa, the code provides that there should be at least two executive directors on the board, that is, the managing director and director of finance.70 The SEC code failed to make definite provision on the number of each cadre of directors required for the board.

Governance responsibility of the board

The Board is the most important decision making body of the company. A company should have a dedicated and responsible board to ensure that the company continues to achieve its objectives. The SEC Code listed the responsibilities of the board as follows:

1. The board is accountable and responsible for the performance and affairs of the company;
2. The principal objective of the board is to ensure that the company is properly managed;
3. The responsibility of ensuring good corporate governance lies with the board;
4. The board must define the framework for the delegation of its authority or duties to management.71

The UK Code 2012 on the role of the board provides that: “Every company should be headed by an effective board which is collectively responsible for the long-term success of the company”. The supporting principles: “The board’s role is to provide entrepreneurial leadership of the company within a framework of prudent and effective controls which enables risk to be assessed and managed. The board should act as the company’s strategic aims, ensure that the necessary financial and human resources are in place for the company to meet its objectives and review management performance. The board should set the company’s values and standards and ensure that its obligations to its shareholders and

---

67Weldo C.H. 1985, Board of Directors; Their changing roles, structure and information needs. Westport CT.
71Smender R. 2007, A Practical guide to Corporate Governance, London; Sweet and Maxwell, pg 49-50
73Principle A3 Combined Code
74SEC Code para. 4.
75SEC Code para 5.1.
76SEC Code para 5.2.
77Kings Code III.
78SEC Code para 5.
others are understood and met.\textsuperscript{73}

The Kings Code of Corporate Governance Principles (King III) made extensive provisions on the role and duties of the board in corporate governance. The code divided the role into three important aspects\textsuperscript{74}:

i. Responsible Leadership – This listed the leadership responsibilities of the board which includes, the strategy and operations to sustainable business\textsuperscript{75},

ii. impact of the board’s decisions on the society\textsuperscript{76}, economy and environment\textsuperscript{77};

iii. ethical issues\textsuperscript{78}; environmental issues\textsuperscript{79} and impact on the stakeholders\textsuperscript{80}.

From the above comparative analysis it is obvious that the Nigerian SEC Code falls far short of international standard and best practices. The board having been recognized as the most important decision making organ of the company and corporate governance, standard ought to be as high as possible and to ensure that Nigerian companies are responsible corporate citizens that can stand with their peers all over the world. The issue of ethical conduct, sustainability of the business in the long and short term, responsibility to the stakeholders and their immediate environment are some of the issues that must be included in the next review of the SEC Code.

Effectiveness of the board

Decision making is an important board activity and the quantity and quality of the board’s decision will translate into effectiveness and progress for the company. The CAMA 2004 is silent on the selection of the directors and the choice is left to the discretion of the shareholders, unfortunately, the codes have continued to hammer on the standards and role of the board while leaving the important issue of selection to the discretion of the shareholders. The quality of the directors will reflect most certainly on the effectiveness\textsuperscript{81}. The Higgs Review\textsuperscript{82} on the role and effectiveness of NEDs identified a number of important characteristics of an effective unitary board.\textsuperscript{83}

He identified the role of a chairman, complimentary relationship with the chief executive and the other members of the board and who is able to relate and coordinate all the activities of the executive and non-executive members of the board as the most important factor for an effective board. The review also demonstrates that a culture of openness and constructive dialogue in an environment of trust and mutual respect is also an important underlying factor for an effective board. The chairman has a central role to play in fostering these conditions through their own actions and through engagement with the members of the board\textsuperscript{84}.

Where there are mutual suspicions between the NEDs and the executive on the board, the NEDs may feel they do not have enough information to arrive at a good decision, while the executives believe that the quality of decisions from the board does not enhance productivity\textsuperscript{85}.

The quality and effectiveness of the board could easily be improved by presence of a dominant personality on the board or a dominant group. This must have informed the provisions in the CBN Code which limited government direct and indirect equity holding in any bank to 10% by the end of 2007\textsuperscript{86} and also no individual is permitted to own more than 10% equity in banks without CBN approval\textsuperscript{87}. This provision has been effected and has substantially reduced the dominant effect of owner/ founder status in Nigerian banks. The post of chairman and CEO has also been split so that no one person is allowed to hold the two positions.\textsuperscript{88} Also, no two members of the same extended family are allowed to occupy the position of chairman and that of the CEO or executive director of a bank at the same time.\textsuperscript{89}

The American based National Association of Corporate Directors\textsuperscript{90} also identified a number of important issues for an effective Board:

1. Knows and understands the company’s business and competition;
2. Focuses on strategic issues;
3. Provides intelligent “capital” including performance enhancing ideas, networking and strong support of corporate best practices;
4. Demands high but realistic standards of performance;
5. Enhances decision making with rigorous analyses;
6. Energizes management by empowering management and holding them accountable;

\textsuperscript{73}The King Code of Corporate Governance Principles King III retrieved on 29\textsuperscript{th} November 2012.
\textsuperscript{74}King III para 1.1.1.
\textsuperscript{75}King III, para 1.1.2.
\textsuperscript{76}King III, para 1.1.3.
\textsuperscript{77}King III para 1.1.4.
\textsuperscript{78}King III para 1.1.5.
\textsuperscript{79}King III para 1.2.1.
\textsuperscript{80}King III para 1.2.2.
\textsuperscript{81}Eisenberg M. 1979, A Larger role for a non –executive director in D. Schwartz, Ed. Commentaries on Corporate Governance and Structure, New York.
\textsuperscript{82}Higgs Review on the role and effectiveness of Non-Executive Directors, retrieved on 29\textsuperscript{th} November 2012.
\textsuperscript{83}Higgs Review, para. 6/9.
\textsuperscript{84}See also DTI publication; Building Better Boards: www. Dti.gov.uk/lbf/corp-governance/betterboards/page 17362.htm/
\textsuperscript{86}CBN Code, 2006, para 5.1.
\textsuperscript{87}CBN Code, 2006, para 5.1.2.
\textsuperscript{88}CBN Code, 2006, para5.2.2.
\textsuperscript{89}CBN Code, para 5.3.3.
7. Tracks and retains a top leadership team and has a strategy for the orderly succession and replacement both of the leadership team and of the Board itself;
8. Links executive compensation to shareholder value.

Boards may consider taking extra measures in ensuring that they arrive at a good decision in their deliberations by contacting experts for advice or commissioning an independent report or form a sub-committee on any important matter, or insist on getting better information from the Executive.

In Nigeria, the code ought to include specific provisions on the type of gift and emoluments outside the prescribed allowances that can be received by the members of the board as we shall discuss below. Corruption is another important factor mitigating against the effectiveness of the board.

The role of non-executive directors

Legal status

There is no difference between the legal role and duties of the executive and the NEDs, the CAMA 2004 do not in fact distinguish between the two. The distinction sought to be introduced by the Court of Appeal in Nigeria in the case of Longe v. First Bank of Nigeria Plc91 where Salami JCA attempted to draw a distinction between the executive and NEDs when he stated thus: “The respondent’s board in the instant case, consists of two classes of directors, executive and non-executive. The non-executives are directors appointed directly under Sections 247, 248 and 249 of the Companies and Allied Matters Act, Cap. 59. The second tiers of directors are not employees of the company as they do not have contract of employment and do not draw salaries”.

The learned Justice of the Court of Appeal went on to draw a distinction between the NED and executive directors, and classified the latter as “employees” who owes their tenure of office to their contract of service; that their appointment is not recognized by the CAMA 199092. The Learned Justice was of the view that, “… executive directors are mere senior managers appointed by the board under the Articles of Association for governance and interest of running the company”.

This position is far from the truth. The Supreme Court had the opportunity of correcting the position taken above, on appeal93. Ogundare JSC after explaining the position of the law laid down the correct position by clearly stating that “all directors whether executive or non-executive are the same as long as they are all engaged to direct and manage the business of the company”94.

The NED being a director is also subject to the duties directors owe the company, both the duty of care and skill and fiduciary duties,95 under common law and statute96.

Current status

The law has moved away from the subjective duty of care and skill laid down by Romer J in Re City Equitable Fire Insurance97 to a more objective standard. In the Australian case of Deniole v. Anderson98 the Court of Appeal of NSW, applied the objective test and found out that NEDs were not liable for failure to discover fraud in one of the subsidiaries of the company, while the CEO was held liable.99

The NED must therefore ensure that they monitor the activities of the executive as strictly as possible. The level and extent may not be too clear now. In the Australian case of Awa Ltd v Daniels,100 the Court of Appeal in New South Wales stated; “In our opinion the responsibilities of directors require that they take reasonable steps to place themselves in a position to guide and monitor the management of the Company”.101

The NED must therefore play a more active role in the company. The days of merely attending meetings intermittently102 is over, and the statutory intervention has placed a much strict burden on the NED to ensure that they not only attend meetings but also take interest in the affairs of the company.103 Where they delegate,104 they have the duty to supervise their delegate failure of which they will still be held liable.105 It is no longer an excuse to state that the director was absent while a particular decision was taken that is in breach of duty, unless justified, the director will be held liable.106

It therefore the duty of the NEDs to not only depend on the information supplied by the executives but to go further and source for information upon which to address

94 per Ogundare JSC.
96 See Sections 282 on the Duty of care and skill, and Section 279. On fiduciary duties in England you may see Sections 171 to 179 CA 2006 for the duties.
97 Re City Equitable Fire Insurance Co supra.
101 Sections 174 (duty to exercise reasonable care, skill and diligence) and 172 (duty to promote success of the company) of UK 2006 Act reinforces the position; contrasts with Sections 279 (fiduciary duties of directors) and 280 (conflict of duties and interests) in the CAMA 1990.
102 Romer J. in Re City Equitable Fire Insurance Co. op. cit.
103 Section 279 CAMA 1990.
104 Section 279(7) CAMA 1990.
105 Section 282(3) CAMA 1990.
106 Section 282(3) CAMA 1990.
issues before them.\textsuperscript{107} This seemed to have been given a judicial pronouncement and approval by Morrat C. J. in Re Barings Plc (No. 5) where the Court of Appeal in England approved the summary of the law given by Paulon J. at first instance in these terms:

1. Directors have both collectively and individually a continuing duty to acquire and maintain a sufficient knowledge and understanding of the company’s business to enable them properly discharge their duties as directors;
2. Whilst directors are entitled (subject to the articles of association of the company) to delegate particular functions to those below them in the management chain, and to trust them; their power of delegation does not absolve a director from the duty to supervise the discharge of the delegated functions;
3. No rule of universal application can be formulated as to the duty referred to in (2) above.

The NED must therefore take care not only to diligently attend to the affairs of the company, but cannot say that they relied on the information or judgment of the executive to escape liability. In the case of Equitable Life Assurance Society v Bowley & Others\textsuperscript{108} former non-executive directors with the executive directors of the claimant had been made defendants in proceedings commenced by the society through its current Board in a claim for breach of duty and damages. The NEDs have applied that the case does not disclose any case against them because they were entitled to rely on the executive directors and should be relieved under Section 123 of the Companies Act 1985. The Hon. Justice Langley refused to strike out the claim against them and said; “I do not think this statement (that is, directors are entitled to trust the full time executives for information) does represent the modern law, at least, if (as the applicant were inclined to submit) it means unquestioning reliance upon others to do their job. It is well known that the role of NEDs in corporate governance has been the subject of some debate in recent years. For the present purposes, it suffices to say that the extent to which a NED may reasonably rely on the executive directors and other professionals to perform their duties is one in which the law can fairly be said to be developing, and is plainly ‘fact sensitive’. It is plainly arguable, I think, that a company may reasonably at least look to NEDs for independence of judgment and supervision of the executive management.\textsuperscript{109}

For the NEDs, the position has changed drastically and with the codes, their duty to the company is now further entrenched and escape from liability, for breach of duty may have to be on very genuine reasons and terms.

The role of non-executive directors and their effectiveness

Through the codes

The SEC Code provided for the appointment of NEDs to the board, by providing that, there should be a mix of executive and NEDs so that a majority of the board members should be NEDs and at least one of whom should be an independent director\textsuperscript{110}. The NEDs are expected to be key members of the board. They are to develop independent judgment as well as necessary scrutiny to the proposals and actions of the management and executive directors especially on issues of strategy, performance evaluation and key appointments.\textsuperscript{111} They are expected to be persons of high caliber with broad experience, integrity and credibility.\textsuperscript{112} They are to be provided with conducive environment for the effective discharge of their duties.\textsuperscript{113} The Code added that adequate and comprehensive information on all board matters are to be provided in a timely manner.\textsuperscript{114} The CAMA 2004 made it clear that there is no distinction in relation to the standard of care expected from both executives and NEDs in terms of their duties to the company.\textsuperscript{115} The Cadbury Report 1992 stated that, NEDs should bring “an independent judgment to bear on their work as of strategy, performance, resources including key appointments and standard of conduct”. The Hampel Report also stated that “non-executive directors are appointed for their contribution to the development of the Company’s strategy”. That they are appointed into the board based on their immense technical knowledge, their knowledge of overseas markets or their political contacts.\textsuperscript{116}

Higgs Review (2003) looking into the role and effectiveness of NEDs identified two important roles for the NEDs. These are, monitoring executive activity\textsuperscript{117} and contributing to the development of strategy.\textsuperscript{118} Higgs went on to say that, the key to NED effectiveness lies much in behaviors and relationships as structures and processes.

The UK Corporate Governance Code 2012, supporting principles on the NEDs, provided \textit{inter alia}, that ‘NEDs should scrutinize the performance of management in meeting agreed goals and objectives and monitor the

\textsuperscript{108} (2003) EWHC 2263 (Comm).
\textsuperscript{109}Ibid, see also Re-Barings Plc (No.5) (2000) 1BCLC 523 at 525.
\textsuperscript{110}SEC Code, para. 3.1.
\textsuperscript{111}SEC Code, para 5.4(a)
\textsuperscript{112}SEC Code, para 5.4(b)
\textsuperscript{113}SEC Code, para. 5.4(c)
\textsuperscript{114}SEC Code, para 5.4(c)
\textsuperscript{115}Section 282(4).
\textsuperscript{116}Hampel Report para. 3.8, 3.15
\textsuperscript{117}Higgs Review, para 5.002
\textsuperscript{118}Higgs Review, para 5.004
reporting of performance. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible.\textsuperscript{119}

All the other Codes in Nigeria made provisions for NEDs almost in line with the SEC Code.

**Effectiveness**

The NEDs carry with them substantial responsibilities towards their company.\textsuperscript{120} Their effectiveness and capability to carry out their duties must be examined and constraints removed. Rather than increasing their duties only without correspondingly removing the constraints to their effectiveness, the law is placing upon them an onerous task not easily attained.\textsuperscript{121}

**Independence**

Both the Nigerian Codes and the UK Code do not imply that all NEDs should be independent. The SEC Code made provision for only one independent NEDs, where all the other NEDs are not independent. The obvious conclusion is that they are likely to tow the line of their sponsors and will create problems not only for the board but also the company.\textsuperscript{122} Where they are nominees of a strong and dominant person or a majority shareholder they are likely to voice the opinion and direction of their master. The probability of achieving any serious purpose is jeopardized. The executive directors are not independent as they rely on the company for their remuneration. The problem therefore is that the existence of the company and the effective deliberations of the board is most likely going to be affected where all the board members have different objectives in mind that is not likely to be of a general but selfish end. Where the NEDs appointment was sponsored by the chairman or the CEO, he is not likely to give any independent opinion and not likely oppose the suggestions of these people and is constrained in his inputs to the board.\textsuperscript{123}

The NED who accepts contracts from the company, or serves as its consultant, or accepts any remuneration from the company outside the normal allowance is not likely to be independent and cannot effectively contribute to the deliberations of the board. The solution recommended in the UK Code is that the NEDs should be selected from a formal process. In Nigeria, we suggest that the nomination and appointment be done in an open and fair election after a committee has been set up for this purpose. The committee must have advertised and received applications from interested individuals who must have satisfied the qualifications required by the company. The interview and eventual appointment could also be handled by professionals outside the control of the company.\textsuperscript{124}

The UK Code and the King III Code do not consider a NED that has served for more than nine years to be independent as the longer time he serves on the board is likely to diminish his independence. There have been arguments as to whether in fact a NED that has served for nine years could be considered non-independent. The point is that, the NED would have gained much experience and is capable of contributing much more effectively than those who are just being appointed and who do not know the rudiments of their duties. In view of these arguments, the UK Code is more practical in its approach. Where the company is satisfied that the director is independent, he may still be considered ‘independent’ for the purposes of the corporate governance provisions. In fact, the entire purpose for the corporate governance code will be defeated if the code fails (as in the Nigerian Codes) to make provisions adequately for appointment of substantially independent NEDs.\textsuperscript{125}

**Senior independent director (SID)**

All the Nigerian Codes make provisions for appointment into the board of an independent NED. The CBN Code in fact provided for appointment of two (2) non-executive board members who do not represent any particular interest and hold no special business interest with the bank, appointed by the Bank on merit.

In UK, the UK Governance Code made provisions for the appointment of senior independent director (SID) whom shareholders could approach to discuss problems and issues when the normal communication route through the chairman has broken down. The SID stands in between the shareholders and the board, he creates the enabling environment through which the NEDs, shareholders and the chairman can interact and discuss especially in times of disagreement on the board.

In view of the Nigerian Codes, which is silent on the independence of the chairman,\textsuperscript{126} the chairman is

\textsuperscript{119} UK Corporate Governance Code 2012 para A4.

\textsuperscript{120} Ghosh D.N; 2000, ‘Corporate Governance and Boardroom Politics. Economic and Political Weekly, 35:46. 4010.

\textsuperscript{121}McNulty T, Roberts J and Stiles P; Creating accountability within the board: The work of the effective Non-Executive Director, A report for the review of the role and effectiveness of the Non-Executive Director conducted by Mr. Derek Higgs.


\textsuperscript{123}Baxt B, Corporate Governance – Is this the answer to corporate failures

\textsuperscript{124} Ibid.


\textsuperscript{126} See also UK Code provision A 3.1.
therefore most likely to be biased and close to the management. The position of the SID will become very important, as he will likely provide an independent leading role within the board. Critics may argue that the SID’s position and role is better played by the chairman and the position is superfluous and unnecessary. However, the practical implication of the position of the chairman as a head of the board is that he always have close ties with the executive and never independent. The SID position therefore is important because he provides independent leadership for the board and he will set the agenda for board meetings and acts as the main spokesman for the independent members of the board. The ICGN (International Corporate Governance Network) Global Corporate Governance Principles also advanced reasons why a SID is necessary as an important ‘alternative conduit for communication with the shareholders’. 

Unitary and two-tier boards

Nigeria and most commonwealth countries follow the position in UK on the adoption of the unitary board system. In Germany, Austria and some others adopted a two-tier board system. The executive board is the first tier, while the non-executives sit as the supervisory board. The chairman of the supervisory board coordinates and cooperates with the management board. The strategy for the company is developed by the supervisory board and ensures general supervisions of the management boards. In Germany, the German Corporate Governance Code provides that the supervisory boards appoints, supervise and advises the members of the management board and is directly involved in decisions of fundamental importance to the enterprise. The chairman of the supervisory board coordinates the work of the supervisory board. The members of the supervisory board are elected by the shareholders at the general meeting. In enterprises having more than 500 to 2000 employees in Germany, employees are also represented in the supervisory board. The criticism against the two tiers board had been that the employee representation is a source of unnecessary antagonism against the management. Other criticism, is the large number of board members which may increase the financial burden on the company, the large number may also cause unnecessary delay in decision making. The Walker Report which considered the corporate governance in banks, whether unitary boards may have contributed to the financial problems in 2007-2009 and whether the two-tiers board structure might be more suitable for large banks. It concluded with a critical assessment of the two-tier structure.

In practice, two-tier structures do not appear to assure members of the supervisory board of access to the quality and timelessness of management information flow that would generally be regarded as essential for non-executives on a unitary board.

In spite of the above, we will recommend that the two-tier structure be adopted for Nigeria, as the unitary system has not fostered good corporate governance practice in the country. The unitary structure has been a source of serious corruption and ineptitude. The NEDs even if they seem independent at inception are quickly coerced and manipulated by the executive with loans, contracts and other free gifts like holidays abroad, with these they lose their independence and easily become ‘rubber stamps’ in the hands of the management.

In January 2010, the Economic and Financial Crimes Commission (EFCC) filed fraud related charges against seven NEDs of Intercontinental Bank for granting over N60 billion naira loans to companies in which they allegedly have interests. The constant interaction between the management and the NEDs in Nigeria instead of assisting in the progress of the company and good corporate governance but only helps to destroy it. The two-tier structure will ensure a total separation of the management from the supervisory arm of the board and ensures discipline and real supervision of the management.

Relationship with shareholders

The UK code main Principle D.1 states: There should be dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that there is a satisfactory dialogue with shareholders.

Until the Higgs Review, it was generally assumed that NEDs should not have direct interaction with shareholders that was reserved for the chief executive or chairman. Higgs rejected the argument that the annual general meeting should be the main or only mechanism through which major shareholders and NEDs have contact. The Nigerian SEC Code only provided for the general meeting as the primary avenue for meeting and interaction between the shareholders, management and

---

127Except stating in para 4.5 that the board should be independent of management to carry out its oversight functions in an objective and efficient manner.
128ICGN.
129German Corporate Governance Code (as amended on May 15, 2012) www.ecgi.org/codes/documents/cg_code_germany/15may2012_empdf
129Ibid.
board.

For a good corporate governance practice, the shareholders ought to have more direct participation in the affairs of their company. They need not wait until the next general meeting; they should have the opportunity to express their views, suggestions and questions. The annual general meeting may be a venue where they can ask a few questions, but detailed enquiries of serious concern or follow up to resolutions and decisions of importance cannot be done at the same venue until a year later. There must be an avenue created to treat issues arising before the next meeting. The best option is to encourage a meeting with the NEDs, who should be in a better position to communicate with the board. Institutional investors must be encouraged to hold regular meetings with NEDs, and the NEDs will in turn ensure that the views of the shareholders are adequately represented at board meetings.

Higgs who conducted an extensive research on the subject clearly stated the best approach which is: “... one approach to strengthening relationships which has been noted is for NEDs to meet with some of the company’s major shareholders, individually or collectively, on a regular formalized basis without executive management present. The purpose of the meeting would be for NEDs to communicate the company’s strategy or to account for its performance. NEDs would attend such meetings to listen to investors’ views and to answer questions about governance.”

The SEC Code must be reviewed urgently to accommodate the modern trends in the corporate governance. Shareholder participation in governance and the role of institutional investors must be recognized. The NEDs relationship with shareholders as a potent source of communication must also be recognized.

Other issues affecting NED’s effectiveness

The SEC Code must address in a more serious manner the following issues that not only affect the performance of the board but may be an impediment to good corporate governance practice in Nigeria. These are:

1. There is currently no limit to the number of NED positions an individual may hold in companies. The only exception is that two members of the same family should not sit on the board of a public company at the same time. Also, memberships on the boards of two or more companies are only to be discouraged not prohibited. The NEDs may therefore hold as many NED position as possible; this of course will reduce effectiveness, loyalty and competence. The NED position is no longer of an intermittent nature, but must be taken serious for effective corporate governance.

2. Many NEDs bring inefficient knowledge about the affairs of the company into office, due to the short tenure they enjoy in the office, provision for continuous education may be wasteful and unfruitful. Many of them are only beginning to understand the office and its demands and were quickly removed. It is of importance to understand that the more years spent in the office will enhance productivity and experience and a sense of belonging and loyalty. The continuous education should be made compulsory and not optional, and the term of a director should be made not less than ten years, subject to section 262 of CAMA 1990.

Conclusion

Every company should be managed by an effective board, which is responsible for the long term success of the company. The Corporate Governance Codes not only acknowledge this fact but also principally address the conduct and responsibilities of the board. The SEC Code applies to all public companies in Nigeria, especially those whose securities are listed on a recognized securities exchange. The compliance seems to be mandatory because the Code used the word ‘shall’ comply with the principles and provisions of the Code and it is supposed to be the minimum standard expected from any public company in Nigeria. There is in fact no modality for enforcement, there is no facility for monitoring compliance and there is no penalty whatsoever for non observance of the Code. The Code standard of corporate governance is extremely lower than expected from a country looking for foreign direct investment and the provisions are of a general nature that it cannot be easily enforced.

Due to the very deep propensity of Nigerian directors to benefit themselves from their position, it is good not only to raise the corporate governance standards, but to adopt the two-tier board structure as is practiced in Germany. This will reduce the influence now daily exercised on NEDs by the management. It will also assure of wider involvement by all other stakeholders like the shareholders, employees and the immediate community.

There is currently no specialised agency or department monitoring and enforcing the Corporate Governance Code. There should be established a body independent of SEC to monitor the public companies, because it is a specialized organ, it is in a better position to identify lapses quickly and correct or punish the erring Company as at when due. It will also be able to monitor directors, and keep a register of all directors of public companies in

---

134 Dialogue with institutional shareholders.
135 Higgs Review, para. 15.12.
136 SEC Code, para 7.1.
Nigeria. The Section 254 of the CAMA 1990 which states that any person who has been found guilty of fraud related offence in the management of a company is disqualified from being appointed a director for a period not exceeding 10 years is unenforceable unless there is a body that will be empowered to keep the record, and insist that there shall be compliance with this provision.

Lastly, we recommend that all the existing Codes be harmonized and merged. This will assist the companies to determine which code to apply and comply with. Currently, the SEC Code that is more of a general applicability should be urgently reviewed, upgraded and standardized to meet with current global standard.

REFERENCES


Code of Corporate Governance for Licenced Pension Operators.

Code of Corporate Governance for Public Companies in Nigeria issued by the Securities and Exchange Commission.

Code of Corporate Governance for the Banking Industry in Nigeria (post consolidation).

Code of Corporate Governance for the Insurance Industry.


Hampel Report on Corporate Governance.


This Day Newspaper (2010). This Day Newspaper report of 21st January 2010.

UK Stewardship Code (2012). The King Code of Corporate Governance Principles King III.


Weldo C. H. (1985). Board of directors; Their changing roles, structure and information needs. Westport CT.