CORPORATE GOVERNANCE CHARACTERISTICS, COMPANY PERFORMANCE AND EXECUTIVE COMPENSATION: THE CASE OF NIGERIA

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ABSTRACT

Executive compensation has attracted much attention as it is exacerbating the agency conflicts. This study extends prior research by examining the influence of corporate governance practice on executive compensation by listed companies in Nigeria, a country that is characterized by low investor protection rights, weak enforcement and compliance mechanism that is very much different from the developed markets. Specific attention is paid to the role of multinational companies' ownership. The data was from 215 company-year observations for the period 2009 to 2013. The time period coincides to the two years before and two years after the publication of the Code of Corporate Governance for Public Companies in Nigeria 2011 (CG Code 2011). The fixed-effects regression was used for testing the study's hypotheses. The result shows there is no significant difference between the executive compensation of the multinational companies and those of the domestic companies. However, the executive compensation after the publication of CG Code 2011 was higher than that before its publication. Further, the findings indicate that board attributes (board size, board composition, Chief Executive Officer (CEO) duality, gender diversity, compensation committee, and compensation committee independence) do not constrain CEO from extracting higher compensation in Nigerian Listed Companies (NLCs). The independence of compensation committee shows significant positive association with executive compensation. The ownership structure (CEO ownership, directors' ownership, and blockholders ownership) do not substitute for effective monitoring of the executives. However, the study shows multinational companies' ownership to be negatively related to executive compensation. Finally, the study results indicate that there are latent weaknesses in the internal corporate governance mechanism operational in NLCs. This result has implication for regulators of Nigeria's capital market, investors, board of directors, company management, researchers and other company stakeholders.

Keywords: executive compensation, corporate governance, multinational companies, ownership structure.

ABSTRAK

Pampasan eksekutif telah menarik banyak perhatian kerana ia memburukkan lagi konflik agensi. Kajian ini merupakan lanjutan daripada penyelidikan lalu dengan mengkaji pengaruh amalan tadbir urus korporat ke atas pampasan eksekutif yang dilakukan oleh syarikat-syarikat yang disenaraikan di Nigeria, iaitu sebuah negara yang mempunyai ciri-ciri perlindungan hak-hak pelabur yang rendah, penguatkuasaan dan mekanisme pematuhan yang lemah yang sangat berbeza daripada pasaran negara maju. Perhatian khusus diberikan kepada peranan pemilikan syarikat-syarikat multinasional. Data yang digunakan untuk penyelidikan ini adalah daripada 215 syarikat bagi tempoh 2009 hingga 2013. Tempoh masa tersebut adalah bertepatan dengan dua tahun sebelum dan dua tahun selepas penggunaan Kod Tadbir Urus Korporat bagi Syarikat Awam di Nigeria 2011 (CG Kod 2011). Kesan tetap regresi digunakan untuk menguji hipotesis kajian. Hasil dapatan menunjukkan tidak terdapat perbezaan yang signifikan di antara pampasan eksekutif syarikat-syarikat multinasional dan syarikat-syarikat tempatan. Walau bagaimanapun, pampasan eksekutif selepas penggunaan Kod CG 2011 adalah lebih tinggi berbanding sebelum penggunaannya. Di samping itu, penemuan menunjukkan bahawa ciri-ciri lembaga pengarah (saiz lembaga pengarah, komposisi lembaga pengarah, dualiti Ketua Pegawai Eksekutif (CEO), kepelbagaian gender, jawatankuasa pampasan, dan kebebasan jawatankuasa pampasan) tidak mengekang CEO daripada mengaut hasil pampasan yang lebih tinggi dalam Syarikat Tersenarai Nigeria (NLCS). Kebebasan jawatankuasa pampasan menunjukkan hubungan positif yang signifikan dengan pampasan eksekutif. Struktur pemilikan (pemilikan CEO, pemilikan pengarah, dan pemilikan pemegang taruh) tidak menggantikan pemantauan yang berkesan ke atas pengarah eksekutif. Walau bagaimanapun, kajian menunjukkan bahawa pemilikan syarikat-syarikat multinasional mempunyai hubungan yang negatif dengan pampasan eksekutif. Akhir sekali, hasil kajian menunjukkan bahawa terdapat kelemahan yang tersembunyi dalam mekanisme tadbir urus korporat dalaman yang beroperasi di NLCS. Keputusan ini memberikan implikasi kepada pengawal selia pasaran modal Nigeria, pelabur, lembaga pengarah, pengurusan syarikat, penyelidik dan pemegang taruh syarikat lain.

Kata kunci: pampasan eksekutif, tadbir urus korporat, syarikat-syarikat multinasional, struktur pemilikan.

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LIST OF ABBREVIATIONS

ABBREVIATION	FULL LIST
ASX	Australian Stock Exchange
CAMA	Companies and Allied Matters Act
CEO	Chief Executive Officer
CG Code	Code of Corporate Governance for Public Companies in Nigeria
DCOMs	Domestic Companies
CAC	Corporate Affairs Commission
FDI	Foreign Direct Investment
ISA	Investment and Securities Act
MNCs	Multinational Companies
NLCs	Nigerian Listed Companies
NSE	Nigerian Stock Exchange
PWC	PriceWaterhouseCoopers
ROSC	Report on the Observance of Standards and Codes
SEC	US Securities and Exchange Commission
SECN	Securities and Exchange Commission Nigeria
UK	United Kingdom
US	United States
USD	United States Dollars

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The diffused nature of shareholders in large complex organizations and the requirement for managerial skills to enable the firm to perform optimally and efficiently have made the professional managers to take full control of the day-to-day management of the company (Fama & Jensen, 1983b; Ghosh, 2006). As a result of the separation of ownership and control, the managers (agents) will not always make decisions that will be advantageous to the shareholders (principals) because of their conflicting risk preferences (Jensen & Meckling, 1976). It is this conflicting interest that is addressed as the agency problem. It is how to maintain a symbiotic and efficient principal-agent relationship so as to minimize the agency conflicts and reduce the agency costs that executive compensation was devised.

Executive compensation has been conjectured to mitigate the principal-agent problem as Jensen and Murphy (1990b) maintain that this problem could be resolved through proper executive compensation policy of the firm. Agency theory posits that once it is optimally contracted it will align the interest of the managers with those of the shareholders thus mitigating the agency conflict and reducing the agency loss (cost) (Elsaid & Davidson, 2009; Fama & Jensen, 1983b; Jensen & Meckling, 1976; Jensen & Murphy, 1990b). After several decades of study by scholars (Barkema & Gomez-Mejia, 1998; Gomez-Mejia & Wiseman, 1997) from different academic disciplines such as accounting (Core, Holthausen, & Larcker, 1999), economics and finance (Jensen & Murphy, 1990b), management (Gomez-Mejia & Wiseman, 1997), and law

(Bebchuk & Fried, 2004) on corporate governance, company performance, and executive compensation, the inconsistent and equivocal results are making the issue more complex and opening wider avenues for further research.

It was Jensen and Murphy (1990b) that stirred the argument that Chief Executive Officers (CEOs) need more pay incentives to motivate them to work for the interest of the shareholders. In their seminal paper, they report that for every 1000USD change in shareholders wealth, the CEO receives a paltry 3.25USD and suggest that executive compensation should be based on shareholders wealth. Their finding suggests that the low pay-performance sensitivity could be a disincentive to the manager. Consistent with Jensen and Murphy (1990b), Barkema and Gomez-Mejia (1998) argue that appropriate compensation will make the executive work for the interest of the shareholders. Since then there have been the rising trend in executive compensation that it has become a concern for both academic researchers and regulators.

In contrast, other scholars have come to the conclusion that company performance does not justify such pay increases (Conyon & Leech, 1994; Harris, 2009; Hubbard & Palia, 1995). Various countries now require companies to make detailed executive compensation disclosure in the annual reports as part of good corporate governance practice (Odewale & Kamardin, 2015a). With numerous other variables being factored into the executive compensation equation, Bebchuk and Fried (2003) argue that managers now exert their influence to de-couple their compensation from company performance. In support of Bebchuk and Fried (2003), Tosi, Werner, Katz, and Gomez-Mejia (2000) find that performance accounts for less than 5% of the variation in executive compensation.

The Securities and Exchange Commission Nigeria (SECN) (2011) in the Code of Corporate Governance for Public Companies in Nigeria (CG Code) (2011) points that "levels of remuneration should be sufficient to attract, motivate and retain skilled and qualified persons to run the company successfully" (p.24). The implication is that executive compensation plays an important role in a firm's human capital build up. Therefore it has to be designed in such a way as to attract and retain qualified executives from the managerial labour market. It is put in place to enhance the welfare of the managers as rewards for their managerial efforts at enhancing shareholders wealth. However, the astronomical rise in executive compensation over the past years has attracted much interests on how it is determined (Bebchuk & Fried, 2003; Conyon & Murphy, 2000; Gabaix & Landier, 2008; Jensen & Murphy, 1990b). Researchers' interest on executive compensation is on the increase considering the attention it has attracted. After the collapse of Enron, Tyco, World Com and Conceco which were blamed on poor corporate governance, there was great rage from the stakeholders on the excessive compensation paid to company executives, especially the CEOs (Brick, Palmon, & Wald, 2006; Correa & Lel, 2014; Kaplan, 2012; Tosi, Shen, & Gentry, 2003) .

Early studies focused on determinants of executive compensation (Ciscel & Carroll, 1980; Deckop, 1988), but another strand of research centres on the explanations for excessive executive compensation (Bebchuk & Fried, 2004; Cremers & Grinstein, 2014; Gabaix & Landier, 2008; Pan, 2010). The reason for the focus on executive compensation is because the CEO provides leadership for the firm (Ghosh, 2006). Therefore he needs enough motivation to align his interest with those of the shareholders in order to prevent him from exhibiting opportunistic behaviour to the

detriment of the shareholders. This is why some countries are putting cap on managerial pay while at the same time requiring that there be detailed disclosure of executive compensation in the annual reports so as to curb perceived excesses.

The bulk of these studies are US domiciled with a few from Europe and recently Asia (Conyon & He, 2011; Kato, 1997; Lin & Lu, 2009; Ozkan, 2007). The situation from Nigeria remains largely unexamined due to unavailability of data and lack of transparency in disclosure of executive compensation in the annual reports by Nigerian Listed Companies (NLCs) (Odewale & Kamardin, 2015a). Prior to the publication of the CG Code 2003, there was no regulation requiring NLCs to make disclosure of executive compensation in the annual report.

The results from previous empirical studies provide mixed findings. For example, in spite of the higher pay received by CEOs, Brick *et al.* (2006) report that executive compensation has association with firm's poor performance. Andjelkovic, Boyle, and McNoe (2002) could not find any positive relationship between executive compensation and firm performance. This finding suggests that executives are self-serving as they mind their own interest instead of those of the shareholders. Interestingly, some other scholars document a positive relationship between executive compensation and firm performance (Buck, Liu, & Skovoroda, 2008; Chalmers, Koh, & Stapledon, 2006; Firth, Fung, & Rui, 2006; Kato, Kim, & Lee, 2007; Zhou, 2000).

It is the tendency in the agent to exhibit opportunistic behaviour if not monitored that makes the principal to assign the monitoring of the agent to the board of directors (Jensen & Meckling, 1976). Agency theory postulates that the board uses the

corporate governance mechanism of monitoring and financial incentives (executive compensation) to align the interest of the agent with those of the principal (Jensen & Meckling, 1976). This is because of the moral hazard problem where the agent's behaviour is unobservable to the principal. The board is a part of the internal corporate governance mechanism of the firm that enables the dispersed shareholders to monitor the executives and ensure the security of their investments (Connelly, Hoskisson, Tihanyi, & Certo, 2010). Munisi and Mersland (2013) argue that board governance serves as a good corporate governance mechanism. There is an increasing global push for board of directors to be comprised of more outside directors in order to perform their monitoring role effectively (Denis & McConnell, 2003; Van Ees, Van der Laan, & Postma, 2008). It is expected that outside director dominated board will not owe their allegiance to the CEO, will mind their reputation and do proper monitoring of managerial activities.

1.2 Problem Statement

The rise in executive compensation has attracted much attention in recent times. (Bebchuk & Fried, 2003, 2004; Cremers & Grinstein, 2014; Muslu, 2010; Tien, Chen, & Chuang, 2013; Tosi *et al.*, 2000; Van Essen, Otten, & Carberry, 2015). Academic researchers, press, public and policy makers are showing much interest in it (Boivie, Bednar, & Barker, 2012; Brunello, Graziano, & Parigi, 2001; Correa & Lel, 2014; Duffhues & Kabir, 2008; Kaplan, 2012; Murphy, 1999; Tien *et al.*, 2013; Tosi *et al.*, 2000; Van Essen *et al.*, 2015), more especially after the corporate failures that characterised corporate giants like Enron, Tyco, and WorldCom in the US. The increased interest results from the perception that executive compensation is not

related to company performance and that the board of directors is not effective in monitoring the executives (Kaplan, 2012).

In Nigeria, before the publication of the CG Code 2003, executive compensation matters were considered as company's confidential information by NLCs (Ehikioya, 2009) and as such are not disclosed in the annual reports (Odewale & Kamardin, 2015a). Odewale and Kamardin (2015a) examine directors' remuneration disclosure transparency in Nigeria and document that none of the companies examined in their study made any disclosures on compensation policy, long-term incentive plans, share options, and individual directors' remuneration. In fact the unwillingness of executives to make voluntary disclosure of their compensation in Nigeria is aptly captured in the statement credited to the Chairman, Nigerian Electricity Regulatory Commission that "it would be irresponsible for a chief executive officer of an organization to disclose his emolument" (Odunsi, 2015). Therefore, not much is known about executive compensation other than the anecdotal evidence that the CEOs are overpaid as reported by the press (Nigerian Bulletin, 2013) and shareholders denunciation of excessive compensation paid to company executives (Ayininuola, 2007). It is also argued that executive compensation among NLCs is excessive and not related to company performance (Ayininuola, 2007). For example, the CEO of Stanbic IBTC Bank Plc has an annual pay of ₦177Million (USD885,000) in 2010 while her counterpart in Mobil Oil Nigeria Ltd earned ₦85Million (USD425,000) (Nigerian Bulletin, 2013). These amounts are considered high in Nigeria.

To ensure transparency in executive compensation matters in the banking sector the Central Bank of Nigeria (CBN) through a Prudential Guidelines for Deposit Money

Banks in Nigeria effective May 1, 2010 required banks to make full detailed disclosure of executive compensation in the annual reports as contained in Section 4.3. In the banks' bid to make executive compensation disclosure remain at the minimal level and make it remain "confidential information" they engaged the CBN in an intense lobby and after much pressure the CBN withdrew the requirement through a revised guideline effective July 1, 2010. For his explanation on this reversal of the Prudential Guidelines, the CBN governor has this to say:

> "On incentives and bonuses, the question was: should they be published on the annual reports and accounts or are there other ways of disclosing them? In other dispensations, you come to an AGM and give the total package of how much you pay the management and how much you pay directors and the AGM has to approve it. We have to decide how to bring transparency, and we are dealing with something that has to do with security, and someone says you come out to disclose your salary, the next day, somebody shoots you. So you have to look at that" (Komolafe, 2010).

This action provides an insight into why there has not been any serious executive compensation regulatory reform in NLCs unlike what obtains in the US, UK, Australia, China, and Malaysia. Non-disclosure of executive compensation in the annual reports has the tendency to aggravate the agency conflicts between shareholders and managers, as Muslu (2010) suggests voluntary disclosure of executive compensation as a means of mitigating the agency conflict. The concern of the regulatory authorities to reduce the agency conflicts between the shareholders and managers as a result of the perceived high executive compensation led to the recommendation of the CG Code 2003 that the emoluments of the directors, chairman and highest paid director should be disclosed in the annual reports by companies (Odewale & Kamardin, 2015a). However, Odewale and Kamardin (2015a) report a low directors' remuneration transparency score of 37.29%. As an improvement over the CG Code 2003, the CG Code 2011 extends the recommendation of the CG Code 2003 on executive compensation by recommending that the remuneration of CEOs

and executive directors as contained in Sections 5.2(g) and 5.3(d) respectively should include performance related items as bonuses, stock options, and other long-term related components that should be disclosed in the annual reports.

Agency theory is used as the underpinning theory for examining the relationship between corporate governance characteristics and executive compensation in this study. The inability of the diffused shareholders in large companies to jointly manage the companies leads to the contracting of the professional managers to manage such companies in anticipation of increase in shareholders wealth. This contract in turn leads to the separation of ownership and control, and makes it impossible for the shareholders to be involved in decision making that includes executive compensation policy decisions in companies. Since the interest of the manager is different from those of the shareholders, the postulation of the agency theory is that the manager who is self-serving will exhibit opportunistic behaviour (such as extracting excessive compensation) in the absence of any constraint (Jensen & Meckling, 1976). This divergence of interests that exists between shareholders and professional managers in companies results into agency conflicts that require a mechanism to mitigate it (Gillan, 2006; Simanjuntak, 2001).

Strong and effective corporate governance mechanism and executive compensation are considered crucial as they have been identified as means of mitigating the agency conflicts (Connelly *et al.*, 2010; Core *et al.*, 1999; Duffhues & Kabir, 2008; Jensen & Meckling, 1976; Munisi & Mersland, 2013; Ozdemir & Upneja, 2012). Unfortunately, from the international perspective, executive compensation has been reported to be excessive and exacerbating the agency conflicts (Bebchuk & Fried,

2003; Brick *et al.*, 2006; Harris, 2009; Murphy & Sandino, 2010; Tien *et al.*, 2013). The agency theorists' position that executive compensation optimally contracted will align the interest of the managers with those of the shareholders (Barkema & Gomez-Mejia, 1998; Fama & Jensen, 1983b) is under serious contention as practical and empirical evidences do not support the conjecture. The contention is that if the executives get rewarded for good performance (above the line earnings), they should equally be penalized for poor performance (above the line losses) (Gaver & Gaver, 1998). Agency theory suggests that corporate governance mechanisms that can be used to constrain the CEO from extracting higher compensation and align his interest with those of the shareholders are the board of directors and ownership structure in companies (Jensen & Meckling, 1976). The extant literature argues that the board of directors and ownership structure could either complement or substitute for each other (Core *et al.*, 1999; Fahlenbrach, 2009).

An examination of the literature on the relationship between corporate governance and executive compensation indicates that several studies have investigated the relationship between board attributes (board size, board composition, CEO duality, gender diversity, compensation committee) and executive compensation even though with conflicting results (Anderson & Bizjak, 2003; Boivie *et al.*, 2012; Chhaochharia & Grinstein, 2009; Conyon & He, 2011; Core *et al.*, 1999; Fernandes, 2008; Lam, McGuinness, & Vieito, 2013; Ozkan, 2007; Tien *et al.*, 2013; Van Essen *et al.*, 2015; Yermack 1996). The board is responsible for hiring, disciplining, firing, and designing the CEO compensation package (Boyd, 1994; Brick *et al.*, 2006; Jensen, 1993; Jensen, Murphy, & Wruck, 2004; Linck, Netter & Yang, 2008; Zahra & Pearce, 1989). The unresolved issue is the extent of influence the board has in determining

executive compensation. This is because of the disappointing result from past studies (Core *et al.*, 1999; Tosi *et al.*, 2003). According to Jensen *et al.* (2004), "however well intentioned, boards and remuneration committees are not spending their own money, so there is an agency problem between boards and the company that they are there to represent" (p. 50). It is this dilemma of the board that prop up the influence that ownership structure of companies can have in constraining the CEO from extracting excessive compensation.

Connelly *et al.* (2010) identify ownership structure as both internal and external control mechanisms in companies. It is regarded as internal when managers own substantial shares and external when outsiders own large shareholdings in companies. It is reported that most companies in Nigeria have controlling shareholders (Report on the Observance of Standards and Codes (ROSC), 2008), and share ownership is concentrated in a few hands (Odewale & Kamardin, 2015b; Sanda, Garba, & Mikailu, 2011). This could have implication for executive compensation as controlling shareholders could either use their influence to protect the minority shareholders or extract private benefits of control. The ownership structure (CEO ownership, directors ownership, blockholders ownership, foreign ownership in companies is also argued to influence the executive compensation policy developed by companies (Ben Hassen, El Ouakdi, & Omri, 2015; Cheng & Firth, 2005; Core *et al.*, 1999; Khan, Dharwadkar, & Brandes, 2005; Le, Brewster, Demirbag, & Wood, 2013; Munisi & Mersland, 2013; Shin & Seo, 2011). Most of these studies focus on the developed economies and few emerging economies from Asia and were also oblivious of the influence that multinational companies (MNCs) ownership could have on the level of executive compensation. The study by Boyd, Franco Santos, and Shen (2012) stated

that several emerging economies have been completely neglected with respect to governance and compensation studies. This therefore underscores the need for this study.

Table 1.1
Top 20 Equities by Market Capitalization in January 2013

S/N	Equity	Market Cap. (Naira)	% of Equities Mkt. Cap
1	Dangote Cement Plc	2,383,966,985,959.50	23.38
2	Nigerian Breweries Plc	1,216,082,872,665.60	11.93
3	Guaranty Trust Bank Plc	723,124,073,533.68	7.09
4	Nestle Nigeria Plc	665,831,251,680.00	6.53
5	Zenith Bank Plc	643,628,122,613.00	6.31
6	FBN Holdings Plc	592,598,651,904.96	5.81
7	Guinness Nigeria Plc	432,153,177,067.00	4.24
8	Access Bank Plc	254,059,591,405.80	2.49
9	United Bank for Africa Plc	226,582,132,578.42	2.22
10	Flour Mills Nigeria Plc	209,896,442,321.10	2.06
11	Lafarge WAPCO Plc	196,604,800,262.00	1.93
12	Ecobank Transnational Incorporated Plc	172,099,357,157.00	1.69
13	Unilever Nigeria Plc	169,870,001,625.00	1.67
14	Union Bank Nigeria Plc	142,260,774,356.40	1.40
15	P Z Cussons Nigeria Plc	134,996,219,530.00	1.32
16	Stanbic IBTC Holdings Plc	131,100,000,000.00	1.29
17	Cadbury Nigeria Plc	100,134,021,120.00	0.98
18	Diamond Bank Plc	99,010,662,838.20	0.97
19	First City Monument Bank Plc	91,688,168,056.80	0.90
20	Fidelity Bank Plc	91,560,358,592.68	0.90
	Top 20 total	**8,677,247,665,267.14**	**85.11**

Source: SECN (2013b).

Further, few studies have examined how the presence of MNCs influence the executive compensation of their foreign subsidiaries (Brunello *et al.*, 2001; Le *et al.*, 2013) but have not considered the influence that the proportion of their shareholdings could have. There is therefore a dearth of research, if any that has examined the effect

of MNCs ownership on executive compensation on their foreign subsidiaries, especially from Sub-Saharan Africa. In fact, Munisi and Mersland (2013) in their study confirm the paucity of executive compensation studies from Sub-Saharan Africa. Therefore, a new variable identified as MNCs share ownership is included in this study to consider its influence in determining executive compensation in Nigeria. MNCs have been specifically chosen for inclusion in this study for some reasons. First, the subsidiaries of foreign MNCs are identified as one of the four types of companies in Nigeria (ROSC, 2008). They play important roles in the economy as ten (10) MNCs are reported to be among the top twenty (20) most capitalized companies in Nigeria (SECN, 2013b). This is shown in Table1.1. Second, they are also reported to make high positive contribution to Nigeria's Gross Domestic Product (Bakare, 2010). Third, these MNCs along with other foreign investors are reported to control 81% of the shares on the Nigerian Stock Exchange (NSE) as at 2011 (Anuforo, 2014). Fourth, they are involved in the design of the subsidiaries CEO compensation. For instance, it has been argued that there is agency relationship between the MNC's headquarters and their foreign subsidiaries and that one of the ways to align the interest of the headquarters with those of their foreign subsidiaries is to design the subsidiary's CEO compensation (Roth & O'Donnell, 1996). An understanding on how MNCs influence the executive compensation of their foreign subsidiaries may likely shed light on the determinants of executive compensation in NLCs. This is because it is argued that MNCs have the incentive to control their foreign subsidiaries (Gatignon & Anderson, 1988).

1.3 Research Questions

This study endeavours to find answers empirically to the following three major research questions.

1. What is the extent of executive compensation practice in NLCs?
2. What is the relationship between board attributes (board size, board composition, CEO duality, gender diversity, compensation committee, and independent compensation committee) and executive compensation?
3. What is the relationship between ownership structure (CEO ownership, directors' ownership, blockholders ownership, and MNCs ownership) and executive compensation?

1.4 Research Objectives

This study examines how corporate governance characteristics explain variations in executive compensation in NLCs. Further, effort is made to explain the influence of MNCs ownership on executive compensation in NLCs. There are three set out objectives for this study which are as follows:

1. To examine the extent of executive compensation practice in NLCs.
2. To determine the relationship between board attributes (board size, board composition, CEO duality, gender diversity, compensation committee, and independent compensation committee) and executive compensation.
3. To determine the relationship between ownership structure (CEO ownership, directors' ownership, blockholders ownership, and MNCs ownership) and executive compensation.

1.5 Motivation for the Study

The motivation for this study is the secrecy surrounding executive compensation design in NLCs due to the inadequate information disclosure on it (Odewale & Kamardin, 2015a), and Nigeria's weak corporate governance system (Okike, 2007) that has eroded the effectiveness of the board (Pierce, 2011). Mitigating the agency conflicts will make the managers work for the enhancement of shareholders wealth. In the corporate governance literature, executive compensation has been identified as an important variable for mitigating the conflicts although some studies have argued that it is contributing to the agency conflicts.

A search of the executive compensation literature reveals that no empirical study has been conducted on Nigeria. There is therefore the urge to do empirical examination of factors that determine executive compensation in Nigeria, a country whose investor protection rights, and compliance and enforcement mechanism is very much different from those of the US and UK. Munisi and Mersland (2013) showed that there is paucity of empirical research on executive compensation from Sub-Saharan Africa. This study responds as a contribution to the debate from a developing economy.

Several developed and developing economies have strengthened their legal and regulatory requirements as regards executive compensation matters in order to ensure transparent disclosures in the annual reports. These steps were taken to ensure that managers earn their pay and not as a result of rent extraction. Since the global corporate crisis of 2000/2002 was attributed to poor corporate governance, it becomes imperative to examine the effectiveness of the Anglo-American corporate governance

model in shaping executive compensation policy in NLCs in the light of the provisions of CG Codes 2003 and 2011.

In comparison to other emerging markets in the Sub-Saharan Africa, Nigeria's equity market is rated as the second largest with a market capitalization of ₦9.8 Trillion (USD49 Billion) in September 2008 (ROSC, 2008) that steadily rose to ₦13.23 Trillion (USD66.15 Billion) by the end of 2013 (SECN, 2013a). In order to improve and strengthen the equity market in the country, there is the need to strengthen the corporate governance system to reduce agency conflicts as this may likely encourage more foreign investors into the country. This study lays emphasis on how MNCs influence the executive compensation of their foreign subsidiaries. Further, it pays attention to the effect of the CG Code 2011 on executive compensation.

So far, the results of empirical examination on the relationship between corporate governance characteristics and executive compensation from both developed and emerging economies remain equivocal. There is therefore the need to undertake this study to examine the factors that influence executive compensation in listed companies from Nigeria.

1.6 Scope of the Study

The effect of corporate governance mechanisms (board attributes and ownership structure) on executive compensation in NLCs remains the thrust of this study. This is because it has been less examined in emerging economies especially from Sub-Saharan Africa (Boyd *et al.*, 2012; Munisi & Mersland, 2013).

The sample for the study is limited to companies listed on the NSE because of the diffused share ownership, and separation of ownership and control that breeds agency conflicts. Panel data from 2009 to 2013 is used for the study. This period is chosen as it includes two years before and two years after the publication of the CG Code 2011. The agency theory serves as the underpinning theory for explaining the relationships between executive compensation and the predictor variables. Executive compensation is restricted to cash compensation, as the highest paid director, proxy for the CEO pay is what is disclosed in companies' annual reports. This has also been used in past studies (Conyon & He, 2011; Conyon & Leech, 1994; Munisi & Mersland, 2013).

1.7 Significance of the Study

Researchers have conducted numerous studies on executive compensation in an effort to find explanations for its variations. The preponderance of these studies focus on the US, UK, and some other developed countries. Recently, studies from Asia have begun to emerge due to availability of data from those Asian countries. However, there are few studies on executive compensation from Sub-Saharan Africa, but this researcher has not been able to find evidence of empirical study on executive compensation from Nigeria. The reason for this could be attributed to non availability of data on executive compensation prior to the publication of Corporate Governance Code for Public Companies in Nigeria by SEC Nigeria. Executive compensation study from Nigeria could be important considering its economic strength on the African continent and her socio-cultural, economic, and political characteristics that are very much different from those of the developed economies.

A good number of existing studies from Africa focus on South Africa whose corporate governance code is far superior to that of Nigeria in terms of contents and requirements regarding executive compensation matters. There is therefore the need to investigate executive compensation from Nigeria whose legal and economic setting is very much different from that of South Africa and the developed economies.

The CG Code was first published in Nigeria in 2003 aftermath of the global corporate scandals that was attributed to poor corporate governance in companies. The CG Code was revised in 2011. Since then, the influence of the requirements of the codes on executive compensation is yet to be empirically examined to ascertain its effectiveness or otherwise.

1.7.1 Theoretical Significance

There is not yet any known empirical evidence from Sub-Saharan Africa to the best of the researcher's knowledge distinguishing between executive compensation in MNCs foreign subsidiaries and their domestic counterparts in their host countries, this study contributes to the body of literature in this area. It is also the first study to investigate the influence of MNCs ownership on executive compensation in NLCs. Also, this thesis extends the present literature on board attributes, ownership structure, and executive compensation from an emerging economy with low investor protection rights and weak compliance and enforcement mechanism. It also extends the earlier works of Anderson and Bizjak (2003), Chhaochharia and Grinstein (2009) and Colpan and Yoshikawa (2012) by considering the effect of the new requirements in the CG Code 2011 and MNCs on executive compensation.

Rwegasira (2000) suggested a combination of corporate governance models that suit country specifics for African countries. To the researcher's best knowledge, this is the first study to be conducted on the suitability of the Anglo-American corporate governance model for constraining higher executive compensation from Nigeria.

By investigating both MNCs and Domestic companies (DCOMs), this study examines whether the MNCs behave differently from their domestic counterparts when it comes to designing their executive compensation policies. This will add to the literature on executive compensation and open new research frontiers on examining executive compensation of foreign subsidiaries of MNCs.

1.7.2 Practical Significance

This study responds to the suggestion by Rwegasira (2000) that African countries should evolve a combined model of corporate governance that suits country specific needs in order for it to compete effectively in the emerging global corporate environment.

The regulators, remuneration consultants and investors have much to benefit from this study. An examination of the findings will allow the regulators such as SECN, NSE and the National Assembly to develop a comprehensive corporate governance architecture that will include detailed executive compensation disclosures by companies in the annual report. Making the requirements of the CG Code to be mandatory will in no small way lead to transparency in executive compensation in Nigeria. The ineffectiveness of the board should make the investors to have a say on executive compensation issues at the Annual General Meetings (AGMs).

This thesis is aimed at finding explanations for the variations in executive compensation in NLCs, a country characterized by high concentrated ownership structure, low investor protection rights and weak compliance and enforcement mechanism. There is evidence of poor corporate governance system in Nigeria as the country is ranked 134th and 137th for 2010 and 2011 respectively in Corporate Governance index by the World Bank (Pierce, 2011). Therefore, an improvement in corporate governance structure through increased transparency in executive compensation may likely endear the economy to foreign investors as there will be reduced agency conflicts (Basu, Hwang, Mitsudome, & Weintrop, 2007; Eisenhardt, 1989; Fama, 1980; Gibson, 2003; Murphy & Zabojnik, 2004). This will mean having several billions of US dollars inflow into the country through Foreign Direct Investment (FDI) annually. The implication translates to reducing the unemployment problem in the country as investors' confidence in the economy will swell, resulting in the growth of the industrial sector.

There is empirical research debate as to what should be the structure of the board since this will have implications for firm's value and executive compensation. There is also the question of whether there should be a global standard for corporate governance considering countries' social, political and cultural peculiarities that are addressed as country specifics (Stanwick, 2008). This study provides regulators with important and new suggestions specific to Nigeria to be considered in subsequent corporate governance reforms.

Finally, it is expected that the findings will make the board to be focused on firm's corporate mission as excessive executive compensation will certainly bring the board under scrutiny. This will in turn affect investors' perception about firms, capable of

threatening corporate collapse in certain situations where there are financial statement restatements and claw-backs.

1.8 Outline of the Thesis

The remainder of the thesis is divided into five chapters and organized as follows. Chapter two presents the background of corporate governance and executive compensation in Nigeria. Chapter three discusses literature review on the theoretical framework of corporate governance and executive compensation building on agency theory as the underpinning theory for the study. Considering the complexity surrounding corporate governance and executive compensation, discussion on supporting theories follows. The study provides definition for the corporate governance elements of the study. There is also a review on ownership structure.

Chapter four centres on the theoretical framework and research methodology adopted for the study. Here, the research framework and formulation of research hypotheses are presented. There is also discussion on research methods used for hypotheses testing. Next are the definitions of the dependent variable, independent variables, and control variables of executive compensation as used in the thesis. Sources of data are explained and the research design and determination of sample companies discussed. It also contains the techniques for data analyses. The results and discussions are presented in chapter five. Descriptive statistics and interpretation of the results of the regression models of the statistical analyses are contained in this chapter. Finally, chapter six contains the summary and conclusion of the thesis. The summary and key research findings of the thesis are discussed. Limitations of the thesis are provided and there are suggestions for further study in this area before drawing the conclusion.

CHAPTER TWO

CORPORATE GOVERNANCE AND EXECUTIVE COMPENSATION PRACTICE IN NIGERIA

2.0 Introduction

This chapter discusses corporate governance and executive compensation practice in Nigeria. The primary objective is to provide an overview of recent corporate governance reform efforts by SECN and executive compensation as applicable in Nigeria. In section 2.1 the chapter reviews the regulation of Nigeria's capital market. Section 2.2 describes the development of Nigeria's corporate governance system. Section 2.3 provides the executive compensation practice in Nigeria. The summary of the chapter is presented in section 2.4.

2.1 Overview of Regulation in Nigeria's Capital Market

There are statutory bodies responsible for the regulation of Nigeria's corporate governance environment as an emerging market in Sub-Saharan Africa. This study notes that some of these bodies do not put sufficient emphasis on executive compensation matters. For example, there is no demand for information on companies' executive compensation in the Listing Requirements of the NSE. This contrasts with developments in the UK where the directors' remuneration disclosure requirements have been incorporated into the Listing Requirements of the London Stock Exchange and the Companies Act, and the US where the US Securities and Exchange Commission has been providing the lead on executive remuneration disclosure matters since 1938 (Odewale & Kamardin, 2015a). This lack of emphasis provides an insight into why there has not been any serious reform effort with respect

to executive compensation disclosure in the annual reports or through other means that will make relevant stakeholders gain insight into companies' compensation policies.

The Companies and Allied Matters Act (CAMA) 1990 provides the legal framework for the registration and operation of companies in Nigeria. The Corporate Affairs Commission (CAC) is an independent body established under the Act that is empowered to administer the Act under the administration of the Registrar-General. Companies recognised by the Act could be either private or public owned. It is the public owned companies that are listed on the NSE that have attracted much attention concerning corporate governance practice as the recommendations of CG Codes 2003 and 2011 are specifically for this category of companies (SECN, 2011). Sections 267 and 268 of the Act discuss the remuneration of the directors and that of the managing director respectively but do not require their disclosure and that of the company's remuneration policy in the annual report. In section 267 (1), it is required that the remuneration of the directors be determined at the company's general meeting while section 268 (1) assigns the determination of the remuneration of the managing director to the company directors. The implication is that shareholders determine the remuneration of the directors while that of the CEO is determined by the board of directors who are representatives of the shareholders (Munisi & Mersland, 2013).

The World Bank/International Finance Corporation (IFC) Report on the Observance of Standards and Codes (ROSC) (2008) documents that the CAC lacks the capacity to effectively perform the functions assigned to it under CAMA 1990. The ability of the CAC to effectively do adequate supervision of registered companies in Nigeria has

been acknowledged in past studies (Adegbite, 2012; Okike, 2007). Several reasons could be adduced for this inability. For example, Adegbite (2012) points that according to a senior official of the CAC:

> The commission's capacity is constrained by myriad internal and environmental problems. Internal problems include corruption and the lack of human expertise. One of the environmental problems which confront the CAC is the lack of independence from the polity and politicians. (p. 264)

Further, penalty for non-compliance with Section 345 that requires directors to lay and deliver financial statements attracts a fine of ₦500 (USD2.50) daily per director. In Section 348, the fine for presentation of defective financial statements is ₦100 (USD0.50) per director. As indicated above, these penalties are too low and outdated such that defaulting companies may not likely have much difficulty paying such fines once infraction is established. According to the ROSC (2011, p. 13), "the CAMA is outmoded regarding penalties for noncompliance," and suggests that the penalty should be reviewed to make it compliant with present reality. It could therefore be surmised that the low penalty fees required under CAMA 1990 and the weak enforcement of compliance provisions have made the CAC to remain ineffective in the discharge of its statutory functions.

Another independent body responsible for ensuring good corporate governance practice of Nigeria's capital market is the SECN. The SECN is the principal regulator of the securities market that administers the Investment and Securities Act (ISA) 2007. The SECN was established in 1979 to replace the Capital Issues Commission that was established in 1973 as a replacement of the Capital Issues Committee of 1962 (Adegbite, 2012; Okike, 2007). This is the outcome of reform efforts to make the capital market more attractive to investors. As reform continues, the ISA 2007 was

passed to replace the ISA 1999. The promulgation of ISA 2007 gave wider powers to SECN on activities of Nigeria's capital market. The duties of SECN as contained in Section 13 of ISA 2007 include the regulation of the activities of the capital market to protect the interests of investors.

In 2003, the SECN published the first CG Code 2003 to improve the corporate governance practice in the country. This was revised in 2011 to address the observed weaknesses of the CG Code 2003 to align it with global best practices (SECN, 2011). The CG Code 2011 contains significant recommendations over that of 2003 such as disclosure in the annual report of the level of compliance with the CG Code by companies, provision for independent directors, remuneration of the CEO and executive directors to contain performance related components that should be disclosed in the annual reports among others. It is however pertinent to note that under both codes there are no requirements for disclosure of executive compensation on individual basis compared to the practice in the UK and US.

The NSE was established in 1960 as the Lagos Stock Exchange, but started operations in 1961 after the promulgation of the Nigerian Stock Exchange Act of 1961 (Adegbite, 2012; Okike, 2007). It is a self regulatory body that is responsible for the mobilization of capital for listed companies, supervision of the operations of the securities market and regulation of the activities of the second-tier capital market (Okike, 2007; ROSC, 2004). Okike (2007) notes that the NSE had about 20 companies on its trading floor as at 1970 even though there were more than 2000 companies owned by foreigners that were operating in the country at that time. Before 1960, several of the registered companies in Nigeria were controlled by foreigners

and this continued to the early 1970s. The plausible explanations for this could be the Colonialist's drive to deny the people of their colonies economic power, inability of the locals to raise the needed capital, and scarce managerial ability of the few educated Nigerians before independence to manage such companies. To halt this trend and empower Nigerians economically, the Federal Government of Nigeria promulgated the Nigeria Enterprises Promotion Decrees of 1972 and 1977. It was these decrees that put restrictions on the extent that foreigners could do business in Nigeria (Aina, 2013) that opened the way for the increase in number of listed companies on the NSE. With the decrees in place, the foreign companies were required to sell part of their shares to the Nigerian public. Even though the indigenization policy was not well accepted by the foreigners, nevertheless, the shares were oversubscribed by Nigerians (Okike, 2007).

Another landmark was made in 1988 with the promulgation of the Privatization and Commercialization Act No. 25 of 1988 that marked the beginning of government's effort at divesting from some of the public enterprises it had acquired under the indigenization policy of the 1970s. This again made the government to divest its holdings in the government owned companies to the Nigerian public. This further led to the increase in the number of companies listed on the NSE. As at September 30, 2008 there were 218 listed companies on the NSE, however due to delisting of some, the number decreased to 198 by December 31, 2013 (NSE, 2013). ROSC (2008) categorized large companies in Nigeria into four: domestic financial institutions, domestic controlled companies, subsidiaries of MNCs, and state-owned enterprises. The MNCs have strong impact on Nigeria's economy as it is reported that ten of the twenty most capitalized companies on the NSE are MNCs (SECN, 2013b). However,

it is sometimes difficult to identify the real owners of shares in Nigerian companies because of lack of transparency in ownership disclosure (ROSC, 2008).

The NSE has its Listing Requirements for companies applying for listing on the exchange. Again, the Listing Requirement is silent on executive compensation disclosure matters. Adegbite (2012) argued that the problem confronting the NSE is that of weak structure, the consequence of which is its inability to enforce good corporate governance practice among NLCs. ROSC (2004) identified weak enforcement and administrative sanctions as part of the major challenges facing SECN. Further, the only sanction that NSE can apply to any company that does not meet the Listing Requirements is de-listing from the Exchange. Similarly, ROSC (2011) reports that the monitoring and enforcement mechanism of the NSE is weak, thus, it is unable to do adequate monitoring of the disclosures by companies in the annual report to ensure compliance with regulations. According to PriceWaterhouseCoopers (PWC) (2013, p.62), "... the legal system is inefficient, as the judicial system is susceptible to political interference and the rule of law is generally weak throughout the country." This aptly summarizes the reasons for the inefficiencies in the regulations of Nigeria's capital market.

2.2 Development of Corporate Governance in Nigeria

With explosive research efforts across the globe on corporate governance, little is known about it in Nigeria except from some recent studies (Adegbite, 2012; Adekoya, 2011; Ehikioya, 2009; Okike, 2007; Yakasai, 2001). An overview of corporate governance development in Nigeria is presented in this section. Historically, it was the British colonialists that introduced company formation that recognised the

separation of ownership and control into Nigeria and the subsequent promulgation of different companies' legislation prior to Nigeria's independence in 1960 (Okike, 2007). It is specified in these legislations how a company is to be governed responsibly. During this period, majority of the companies were foreign owned. Before 1970, there was little concern for how corporate enterprises were run in Nigeria (Yakasai, 2001). This was because most of those companies were either foreign or government owned.

However, beginning 1980s, with the extensive structural and economic reforms embarked upon by Nigeria during the implementation of the privatization and commercialization of some public enterprises, the new owners started demanding for transparency and accountability from company managers. This was an effort at ensuring that these companies were properly governed because prior to that time the public enterprises were seen as mere financial drain pipes that gulp billions of Naira in annual budget without any tangible output (Etieyibo, 2011; Mohammed, Chapola, & Bello, 2013). These public enterprises performance was abysmally low and does not meet the expectations of the citizens (Emeh, 2012).

The accompanying challenge was how to manage the companies profitably and deliver value to the investors. Some of the privatized enterprises later failed, which raised serious concerns among stakeholders on how to nip such happenings in the bud in the future (Etieyibo, 2011). It was the Institute of Chartered Accountants of Nigeria during its Annual Conference in 1998 that extensively discussed the issue of corporate governance in companies resulting from the allegations levelled against auditors by the public for not doing enough regarding the corporate scandals in

Nigeria (Okike, 2007). These scandals involved Lever Brothers Nigeria Ltd. and some commercial banks (Ahunwan, 2002; Aina, 2013). It was aftermath of this that an exhaustive discussion of corporate governance in the Nigeria banking sector with its accompanying challenges was conducted (Yakasai, 2001), while Ahunwan (2002) and Adegbite (2012) examined corporate governance in Nigeria and corporate governance regulation in Nigeria respectively.

In an attempt to enhance the corporate governance practice in NLCs, Section 359 (4) CAMA 1990 established the Audit Committee (not more than six members) to be comprised of an equal number of shareholders and directors. This committee is required to make its report to the shareholders at the Annual General Meeting. Section 1 of CAMA 1990 established the CAC with accompanying functions contained in Section 7 that empowers the Commission to have oversight functions over registered businesses in Nigeria. CAMA 1990 remains almost the same since its promulgation without any major amendment to take into consideration dynamism in the global business environment. For example, Aina (2013) maintains that CAMA 1990 has remained static and non progressive. In order to make CAMA responsive to recent global developments, ROSC (2008) suggests:

> A new CAMA should be drafted and passed into law. It should draw on experience from the recent updates of the UK and Australian companies acts. It should be fully harmonized with recent developments in the legal framework, improve shareholder rights, and raise the fines for non compliance. (p. 10)

With the global corporate scandals and failures coupled with increasing emphasis on good corporate governance practice by developed and emerging economies, it was not long for Nigeria to decide on a standard corporate governance code for its listed companies if it must remain attractive to foreign and informed investors. The

financial crisis in the banking sector in the 1990s added fervour to this pursuit. It was this line of reasoning that led the SECN on June 15, 2000 to constitute a seventeen member committee that has Atedo Peterside as chairman with four key terms of reference to draft a standard corporate governance code for the listed companies in Nigeria. The terms of reference for the Peterside committee as contained in SCEN (2003) are:

1. To identify weaknesses in the current corporate governance practices in Nigeria with respect to public companies.
2. To examine practices in other jurisdictions with a view to the adoption of international best practices in corporate governance in Nigeria.
3. To make recommendations on necessary changes to current practices.
4. To examine any other issue relating to corporate governance in Nigeria.

(p. 2)

The Peterside committee's recommendations were published as Code of Corporate Governance for Public Companies in Nigeria in October, 2003. The SECN code took after the UK code by adopting the single-tier board that is operational in the market-based system of corporate governance. In spite of the fact that the code took after the UK code it fell short of international benchmark for standard corporate governance practice compared to that of South Africa, Malaysia, India and some other emerging economies. The inadequacy of the code was captured as the only code in Africa that does not adopt the all inclusive model of corporate governance (Rossouw, 2005). It adopted the narrow view classification of Claessens and Yurtoglu (2013).

The weaknesses of the code were not late in manifesting following the Cadbury Nigeria Plc financial fraud in 2006/07 and the banking sector crisis that cost the country about ₦2 Trillion (USD10 Billion) (ROSC, 2008, 2011). The expectation was that the adoption of the code would deepen investors' confidence in the economy, provide protection for minority shareholders, make the capital market more liquid and

encourage foreign investors into the country. This is because foreign investors will prefer making investments in countries with sound corporate governance practices (Stanwick, 2008).

Remuneration disclosure matters received little attention in the code. For example, out of the fifteen sections contained in the code, sections one to six addressed board matters, section seven centres on compensation of board members while section eleven to fifteen focused on the audit committee. The recommended board size ranges from five to fifteen while there is no specific requirement for independent board. It further recommends the separation of chairman from the CEO position to avoid concentration of power in an individual. As a means of improving the CG Code 2003, SEC Nigeria set up another committee in September, 2008 with M. B. Mahmoud as chairman to craft a new corporate governance code for NLCs (SECN, 2011). Mahmoud's committee's final report was published in April, 2011 as Code of Corporate Governance for Public Companies in Nigeria by SEC Nigeria.

Adekoya (2011) discussed the inadequacy of corporate governance mechanisms in Nigeria as there are reported corporate scandals in spite of legal and regulatory framework put in place to ensure good corporate governance practice. Between 2008 and 2010 the country witnessed another series of banking crisis in spite of the code for banks issued by the Central Bank of Nigeria in 2006 after the banking consolidation exercise. This crisis was attributed to poor financial reporting by Nigerian banks (ROSC, 2011). Attention was once again focused on the effectiveness of the board of directors in performing their monitoring duty. Adegbite (2012) argued for a legal corporate governance regulatory framework in Nigeria in the short run

given the corporate corruption that is deep in the country's corporate governance system. In addition, Sanda *et al.* (2011) argued for the need for NLCs to evolve better corporate governance mechanisms that will diminish the CEO's influence over the board and its committees and thus improve company performance. The issue at hand is whether the corporate governance reforms (especially board independence and the compensation committee) have had any effect on executive compensation practice in NLCs.

Previous studies from Nigeria centre on corporate governance and firm performance (Ehikioya, 2009; Sanda, Mikailu, & Garba, 2005); evolution and practice of corporate governance (Okike, 2007; Yakasai, 2001); evaluation of the Nigeria corporate governance regulatory system (Adegbite, 2012); and challenges to corporate governance reforms (Adekoya, 2011). Some of the studies focused on the period before the CG Code 2003 while others used data after the CG Code 2003. None of them however relates corporate governance to executive compensation. For example, Sanda *et al.* (2005) specifically mentioned the exclusion of incentives scheme from their study. Past studies from Nigeria have not examined executive compensation issues due to lack of data prior to the publication of CG Code 2003. Before the code, there was no legislative or regulatory requirement for companies to make public disclosure of executive compensation. Further, Odewale and Kamardin (2015a) find that the level of transparency of executive compensation among NLCs is low because of the unwillingness of the executives to make voluntary disclosure in the annual reports.

2.3 Executive Compensation Disclosure Practice in Nigeria

Executive compensation disclosure is important because investors are interested in how executives are remunerated since executives have the tendency to understate their total compensation (Australian Stock Exchange (ASX), 2014; Yermack, 1998). Voluntary disclosure of executive compensation by companies is suggested to likely reduce agency conflicts between shareholders and managers that results from information asymmetry and also prevents executives from extracting excessive compensation (Healy & Palepu, 2001; Muslu, 2010). Little is known about executive compensation in NLCs due to dearth of data and empirical research unlike what is available from developed economies and some emerging economies from Asia (Abe, Gaston, & Kubo, 2005; Albuquerque, 2009; Barontini & Bozzi 2011; Ben Hassen *et al.*, 2015; Brick *et al.*, 2006; Buck *et al.*, 2008; Carpenter, 2001; Carpenter, 2004; Chalmers *et al.*, 2006; Chhaochharia & Grinstein, 2009; Colpan & Yoshikawa, 2012; Conyon & He, 2011; Conyon & Peck, 1998; Core *et al.*, 1999; Duffhues & Kabir, 2007; Firth *et al.*, 2006; Firth, Fung, & Rui, 2007; Gray, 1997; Grinstein & Hribar, 2004; Harris, 2009; Jensen & Murphy, 1990b; Kato, 1997).

It is therefore appropriate to understand the executive compensation disclosure practice in NLCs under the market-based corporate governance system practice in the country. Legal and regulatory framework on executive compensation in Nigeria is different compared to the UK. It remains to be ascertained if the factors that influence executive compensation in the UK will also have equal effect in Nigeria considering country specifics. Nigeria is a part of the global economic community and as such is not immune from the happenings in other countries of the world in this era of globalization. Before 2003, there was no regulation requiring listed companies in

Nigeria to provide information on executive compensation in the annual reports and there is no evidence that any of the companies made voluntary disclosure of executive compensation to the public.

In Nigeria's quest to make its companies conform to corporate governance best practice that is in line with international standards; the CG Code 2003 was published by the SECN with a revised version in 2011. The CG Codes require the disclosure of executive compensation in the annual report. Items for disclosure include the emolument of the directors, chairman and highest paid director. It further recommends the emoluments of the CEO and executive directors should include performance related elements like bonuses, stock options, and long term related components like pensions. There is however no recommendation for the disclosure of executive compensation in the annual report on individual basis.

In Nigeria, the CAMA 1990 remains the only legislative guide on executive compensation. However, the Act does not require companies to make disclosure of details of executive compensation in the annual reports. For the CG Code 2011, it provides that company's remuneration policy and all material benefits and compensation paid to directors (including executive directors' remuneration and share options) should be disclosed in the company's annual report. However, there is no provision for full disclosure of the remuneration (with its breakdown) of each individual director and key management personnel. As further evidence that regulatory authorities in Nigeria do not pay the required attention on executive compensation matters, the Listing Requirements of the NSE does not make any demand on executive compensation disclosure by listed firms.

The report by the World Bank/IFC on corporate governance assessment on Nigeria, ROSC (2008) documents that none of the companies surveyed on the exchange disclosed individual compensation of its directors while only 71% and 50% disclosed the emolument of the chairman and the highest paid director respectively. The non disclosure of the compensation on individual basis could be attributed to the CG Codes that do not recommend such disclosure. In addition, the companies are not willing to make voluntary disclosures since executive compensation matters suffer from lack of transparency in NLCs (Odewale & Kamardin, 2015a). The report further reveals that only 51% of the survey sample of NLCs disclosed aggregate compensation paid to executives. In all these there is no mention of sanction on the non-compliant companies. This provides support for the finding of ROSC (2008) that enforcement and compliance mechanism is weak in Nigeria.

This practice however contrasts that of developed economies that are accepted as constituting good practice. For example, the US Securities and Exchange Commission (SEC) have been at the forefront of enacting rules that require companies listed in the US to make mandatory disclosure of compensation paid to executives in their proxy statements since 1938 (SEC, 2006). The components of the total compensation to be disclosed include name and principal position, year, salary, bonus, stock awards, option awards, non-equity incentive plan compensation, change in pension value and nonqualified deferred compensation earnings, and all other compensation that must be provided in tabular form (SEC, 2006). In Nigeria, there is no provision for the disclosure of executive compensation by companies in the Listing Requirements of the NSE. The case of Nigeria is different from that of the US as the Listing Requirements of the NSE do not include executive compensation matters. In spite of the low transparent disclosure of executive compensation in NLCs, there is no

evidence of any regulatory reforms on executive compensation in Nigeria (Odewale & Kamardin, 2015a).

As the reform progresses in the advanced economies, in addition to the executive compensation disclosure requirements, shareholders are demanding to have a say in executive compensation as it is already established in several countries (Correa & Lel, 2014). This is because appropriate disclosure of executive compensation may likely assist in mitigating the agency conflict as it serves as a restraining force on the executives and it is likely to prevent them from rent extraction tendencies (Muslu, 2010).

2.4 Summary of the Chapter

In this chapter, the background of Nigeria's corporate environment has been discussed with emphasis on the regulators of the country's capital market highlighting the inherent weaknesses associated with inability to perform their assigned duties. The corporate governance landscape was also presented arguing for a mandatory disclosure regime that is backed up by relevant legislation. Further, the executive compensation disclosure is shown to be low because of lack of mandatory disclosure requirement for executive compensation for the public listed companies. The review of relevant literature as pertains to this study is presented in the next chapter. This includes different theories on corporate governance and executive compensation. The international perspectives on corporate governance and past empirical research on the relationship between executive compensation and this study's explanatory variables are also presented.

CHAPTER THREE

LITERATURE REVIEW OF EMPIRICAL STUDIES ON CORPORATE GOVERNANCE AND EXECUTIVE COMPENSATION

3.0 Introduction

This chapter's discussions centre on both theoretical and empirical literature on executive compensation to provide the basic background for the study. The rest of the chapter is structured as follows. Section 3.1 discusses executive compensation while theoretical review is presented in section 3.2. Section 3.3 presents definitions of corporate governance. In section 3.4, discussion centres on the board of directors while section 3.5 focuses on ownership structure. Section 3.6 discusses the control variables for executive compensation used for the study. Prior studies on executive compensation are discussed in section 3.7 and section 3.8 summarises the chapter.

3.1 Executive Compensation

Executive compensation is the pay incentive reward to the CEO for his past managerial efforts at enhancing the wealth of the shareholders by increasing the value of the company (Fama, 1980; Tosi *et al.*, 2000). The reward structure is designed to attract and retain high calibre executives from the managerial labour market and as much as possible reduces executive turnover so as to remain competitive in the industry (Bohlander & Snell, 2010). Components of executive compensation vary in the literature subject to the intent of study and available data, ranging from cash compensation (salary and bonus) to total compensation (cash compensation, restricted stock granted, long-term incentive plans, stock options, pension plans) (Bebchuk &

Grinstein, 2005; Brick *et al.*, 2006; Buck *et al.*, 2008; Conyon & Leech, 1994; Hubbard & Palia, 1995).

In their seminal works Fama and Jensen (1983b) and Jensen and Meckling (1976) point to the conflict situation between managers and shareholders in the course of managing the firm. This is as a result of conflict of interests between the two parties addressed as the agents (managers) and the principals (shareholders) (Eisenhardt, 1989) as each party wants to maximize his individual utility. This conflict of interest is addressed as the agency problem. Since then many researchers have been making efforts at proffering empirical ways of mitigating this agency conflict. This is because there is no way the agency conflict can be totally eliminated (Jensen *et al.,* 2004). Jensen and Murphy (1990b) report that this conflict could be mitigated through proper executive compensation policy of the firm. The determinants of executive compensation remain another complex issue that has remained unresolved in literature.

Different academic researchers have found different parameters for determining executive compensation (Balsam, Fernando, & Tripathy, 2011). The focus of corporate governance reforms has shifted to executive compensation disclosure and board independence as some developed countries are carrying out legislative and regulatory reforms as it affects executive compensation and board structure (Dalziel, Gentry, & Bowerman, 2011; Denis & McConnell, 2003; Odewale & Kamardin, 2015a). Several countries have now incorporated the Say on Pay (SOP) into their laws allowing shareholders to have their say on executive compensation. To show the extent of how countries are enacting such laws, Correa and Lel (2014) in their study

examined the effect of the SOP law on executive compensation in 39 countries. They conclude that the enactment of the SOP laws shows association with lower CEO pay. The study also documents a strong association between pay and performance.

Therefore, executive compensation is the outcome of the means of resolving the agency conflicts that result from the separation of ownership and control that characterise large corporations. Agency theory predicts that once executive compensation is optimally contracted it will align the interest of the managers with those of the shareholders thus mitigating the agency conflict and reducing the agency loss (Elsaid & Davidson, 2009).

3.2 Theoretical Review

This section presents a review of different theories associated with corporate governance and executive compensation.

3.2.1 Theories on Executive Compensation

This sub-section presents different theoretical perspectives that have been advanced by past research in proffering explanation for executive compensation, that include agency theory, managerial power theory, and managerial talent theory.

3.2.1.1 Agency Theory on Executive Compensation

The separation of ownership and control gives rise to the agency conflict (Jensen & Meckling 1976). The problems inherent in the agency relationship are the conflict of interests related to the inability of the principal to monitor the agent because of the

principal's diffused nature, the associated costs of such monitoring, and the different preferences for risk (Eisenhardt, 1989). The inability of the shareholders to know what actions the CEO would take, and what investment opportunities are available to the company due to the information asymmetry results in the agency conflicts. Executive compensation as a mechanism is expected to mitigate the agency loss (Eisenhardt, 1989).

Elsaid, Davidson, and Benson (2009) argue that failure of managers to run the companies and to enhance the shareholders wealth results in the costly agency problems. They identified executive compensation which is based on company performance as a part of the internal solution to the agency problems. Consistently, Fama (1980) suggests that managerial incentives in the form of executive compensation can be used to resolve the agency problem that exists in companies. Through the wage revision process the managerial labour market is able to set up the managerial incentives at the beginning of the period based on the manager's past performance.

Jensen and Murphy (1990b) argue that the compensation policy that makes the executive compensation to be dependent on shareholders wealth will incentivize the CEO to take actions that will enhance the wealth of the shareholders. This theory is anchored on the conjecture that managerial behaviour will be markedly different from maximizing the wealth of the shareholders because the manager has his own self interest to pursue. Agency theory posits that once executive compensation is designed optimally it will motivate the managers to work towards maximizing shareholders wealth. The compensation package should include incentives that will

align managerial interests with those of the shareholders (Jensen & Meckling, 1976). This includes share plans for the executives and making compensation to be sensitive to company performance. The optimal contract provides that the board of directors will negotiate compensation with the manager at arm's length that will maximize value to the shareholders and help mitigate the agency conflicts. Eisenhardt (1989) extolled the agency theory and suggested its use by academics investigating principal-agent conflicts in organizations.

In recent times this theory has come under intense criticism by identifying its shortcomings (Bruce, Buck, & Main, 2005; Heracleous & Lan, 2012; Lubatkin, Lane, Collin, & Very, 2005; Lubatkin, Lane, Collin, & Very, 2007). Bruce *et al.* (2005) argue that the agency theory approach to examining executive compensation does not extend outside a narrow focus and that institutional environment (national culture) has a powerful effect on corporate governance and executive compensation. They conclude that agency theory alone cannot fully explain corporate governance and executive compensation and as such requires that other theories be embraced. Heracleous and Lan (2012) argue that it is time to do a critical review of the base of the agency theory because of its perceived shortcomings. Lubatkin *et al.* (2005) argue that agency theory is suitably conjectured for the US institutional setting thereby neglecting other institutional contexts such as economic, political, and cultural settings obtainable in other countries. The agent's behaviour to either align with the interest of the shareholders or to exhibit opportunistic behaviour is said to be dependent on the company's social context (Lubatkin *et al.*, 2007).

Wiseman, Cuevas-Rodríguez, and Gomez-Mejia (2012) stoutly rose in defence of the agency theory by arguing that it can be made to become instituionally sensitive through deductive approach (the use of existing theories for model building). Heracleous and Lan (2012) countered this approach as they informed that several studies have taken this context into consideration but clarification still needs to be made as to the responsibility of the board of directors in the agency setting. They therefore offered an inductive approach (observing actual board decision processes for theory building) to the perceived problems with agency theory rather than the deductive approach as suggested by Wiseman *et al.* (2012). The challenge is understandable because the board is also an agent of the shareholders who could also have the propensity to put up self-serving behaviour to the detriment of the shareholders. To buttress this position, Jensen *et al.* (2004) admitted the existence of agency problem between the board of directors and shareholders because they earn their pay from the company.

In spite of the criticisms against agency theory, several economics and finance literature still use it to anchor their studies, as such this study also adopts it as the underpinning theory. The next sub-section discusses the managerial power theory.

3.2.1.2 Managerial Power Theory on Executive Compensation

The large volume of empirical literature that found insignificant or weak positive relationship between pay and performance has further emboldened the critics of agency theory. Another stream of literature on executive compensation challenges the optimal contract of the agency theory by focusing on the inability of the board of directors to enter into arm's length contract with the manager for his compensation

contract. The managerial power theory otherwise called managerial entrenchment theory posits that CEOs that have strong influence over their boards will extract private benefits in form of higher compensation that is less related to performance as predicted by the agency theory (Bebchuk & Fried, 2003; Fahlenbrach, 2009). Managerial power theory challenges the position of the agency theory that the board of directors would be good monitors of managerial actions. Bebchuk and Fried (2003, 2004) a strong critic of the optimal contract (agency) theory and an ardent advocate of managerial power theory, argue that outside directors will not automatically work for the interests of the shareholders and that they are inclined to align their interests with that of the manager where the board is a captive of the CEO. The inability of the board to negotiate CEO pay at arm's-length could be as a result of board culture that does not give place for contrary opinion that may be seen as antagonistic (Jensen, 1993).

The proposition of the managerial power theory is that executive compensation levels and structures should be considered under the circumstance that surrounds the actual pay setting process. Under this theory, executive compensation is seen as exacerbating the agency conflict rather than mitigate it as envisaged by the agency theorists (Van Essen *et al.*, 2015). Bebchuk and Fried (2003, 2004) also assert that optimal contracting has failed to promote the shareholders interest as the excessive executive compensation does not lead to enhancement of shareholders value. It is argued that the CEO is able to influence his compensation contract when he is able to influence the choice of who is nominated to the board, CEO duality, other CEOs sit on his compensation committee, and weak ownership structure (Renneboog & Zhao, 2011). Brown and Lee (2010) examine the influence of corporate governance on the

pre-Enron and post-Enron periods using 8048 firm-year observations from 1998 to 2006. Consistent with the managerial power theory they provide evidence that CEOs receive higher equity grants when the corporate governance mechanism is weak. They were however oblivious of the influence that MNCs ownership could have in substituting for good corporate governance practice. Correa and Lel (2014) document that excessive executive compensation is attributed to CEO power as they find that SOP laws in 39 countries is associated with lower executive compensation. In addition they also find that pay performance sensitivity increased post-SOP period.

Faulkender and Yang (2010) examine the influence of peer groups in the CEO pay setting process. They find that CEOs with immense power are able to receive higher compensation by having the company benchmark their pay against their highly paid colleagues. They interpret the immense CEO power as evidence of weak corporate governance. In a study using 1,555 CEOs from the US, Shin (2013) shows that powerful CEOs are able to get upward review of their compensation if they are underpaid, compared to their peer group. Such CEOs are also able to avoid benchmarking when they are overpaid. Consistent with Shin (2013), Skantz (2012) argues that entrenched CEOs can successfully influence their compensation committee to their advantage. In the same vein, the possibility of forfeiting any excessive compensation is minimal just as it is difficult to disengage them from office.

A weak corporate governance system will enable the manager to have power to influence his compensation contract to the disadvantage of the shareholders (Fahlenbrach, 2009) as he or she will be inclined to decouple his or her pay from

performance (Tosi & Gomez-Mejia, 1989). This is in support of the finding of Core *et al.* (1999) that executive compensation is higher in companies with ineffective corporate governance system that enables the manager have overbearing power over the board. This is also consistent with the view that powerful CEO will be able to increase his or her compensation in an environment where weak corporate governance subsists (Fahlenbrach, 2009).

3.2.1.3 Managerial Talent Theory on Executive Compensation

In the course of finding explanations for the variation in executive compensation, managerial talent theory has come to find a place. Several academic scholars have argued against the managerial power theory insisting that the CEOs do not engage in rent extraction in form of excessive compensation, but rather receive higher pay as rewards for their unobserved skills and talents (Albuquerque, De Franco, & Verdi, 2013; Bizjak, Lemmon, & Naveen, 2008; Cremers & Grinstein, 2014; Falato, Li, & Milbourn, 2015; Gabaix & Landier, 2008; Hubbard, 2005; Terviö, 2008). In designing CEO compensation contract, the CEO's ability is a key factor that is taken into consideration (Gabaix & Landier, 2008; Pan, 2010). Talented managers will be needed to manage complex companies. According to Eriksson (2003) more talent is associated with more power and higher executive compensation. Hermalin and Weisbach (1998) in their model show that executive compensation is the outcome of negotiation between the CEO and the board. It is the CEO's ability that confers on him the power to negotiate his compensation with the board. As much as possible companies design their compensation structures so as to recruit and retain talented managers in the company. Large complex organizations will require the services of talented managers to drive the company in the course of pursuing organizational goals

(Gabaix & Landier, 2008). CEOs that manage complex organizations because of their skills and talent will therefore need to be necessarily compensated.

Hubbard (2005) in his critique of 'Pay without Performance' by Bebchuk and Fried (2004) argues that CEO compensation is driven by the managerial labour market for talent and not necessarily by the generally held view of skimming. Falato *et al.* (2015) examine which CEO skills matter in the managerial labour market for CEOs. They used CEO credentials which include his or her reputation, career, and education as proxies for talent. They provide evidence of a positive relationship between CEO credentials and company performance. They conclude that CEOs with better credentials manage larger companies which in turn translate to higher pay. Bizjak *et al.* (2008) in their study of the use of peer groups in executive compensation design, report that firms engage in benchmarking executive compensation not necessarily for the purpose of performance but to retain high quality executives for the firm because of the scarcity of managerial labour talent.

Consistent with Bizjak *et al.* (2008), Albuquerque *et al.* (2013) examine the relative extent to which the peer pay effect reflects self-serving behaviour or a reward for CEO talent in US firms for a sample of 3,158 firm-years and 45,281 firm-year-peer observations during the period 2006 to 2008. Their results suggest a significant positive association between talent and CEO compensation. They explain this association to indicate that firms benchmark CEO pay with higher paid CEOs of comparable companies so as to attract and retain high quality executives. In their own contribution to the debate, Cremers and Grinstein (2014) investigate the influence of CEO talent in explaining variations in executive compensation. They show that it is

the external and internal markets for the CEO that strongly determines the level of executive compensation and not company size as espoused in the literature. They also document that the compensation of the CEOs that are hired from outside is benchmarked with those of their peers so as to have high calibre executive for the firm and does not represent self-serving behaviour of the executive. They called this 'pay for luck' thus supporting the managerial talent hypothesis.

In consonance with Cremers and Grinstein (2014), Elsaid and Davidson (2009) provide empirical evidence from their analysis of 508 successions, as they show that those CEOs that are hired from outside earned 69% more than their predecessors in total compensation. In contrast, Faulkender and Yang (2010) submit that such association is an indication that firms select high paying peers to justify their excessive executive compensation. The next discussion focuses on the international perspective of corporate governance as documented in the extant literature.

3.2.2 Theoretical Models of Corporate Governance

Resulting from the heterogeneous definitions of corporate governance presented by various scholars is the evolvement of two main corporate governance models; the agency theory of the firm (shareholder) and the stakeholder theory of the firm models (Charreaux, 2008; Ntim, Opong, & Danbolt, 2012). These are now discussed in turns.

3.2.2.1 The Agency Theory Model of Corporate Governance

Relationships exist between two parties when there are tasks to be performed and risks to be shared. Jensen and Meckling (1976), and Fama and Jensen (1983b) discussed the relationship between managers of firms and the shareholders in widely

held firms as the agency relationship. Fama and Jensen (1983a) in their explanation on the survival of firms where there is separation of ownership and control identified the residual claimants as the owners of the firm that bear the associated risks to the firm. Residual claimants have no role to play in the management of the firm as they have appointed the decision agents (managers) to make decisions concerning the firm on their behalf. They identified four categorical steps in the decision process as initiation, ratification, implementation and monitoring. This leads to two core components: decision management and decision control. Further, to avoid concentration of the two functions in one agent there is the need for a separation. This leads to the creation of another agent called the Board of Directors (representative of the residual claimants). This results from the tendency to exhibit opportunistic behaviour if the functions are concentrated in the decision agent (manager) because he is a utility maximizer.

Due to the diffused nature of the shareholders, the contractual term empowers and authorizes the manager to make decisions for the firm that will enhance the value of the shareholders (Fama & Jensen, 1983b; Jensen & Meckling, 1976). After the emergence of these works researchers from various fields of financial economics, law, sociology, human resources management, and finance to accounting (Rwegasira, 2000) have continued to amplify on this relationship from different lenses. The agency theory has become a key theory in the corporate governance literature as numerous other studies have rested on it incorporating other theories as suggested by Eisenhardt (1989). This relationship creates a division between decision implementation and control functions in large companies. In the normal entrepreneur-owner manager, these functions are fused into one person because of lack of division

of interest (Jensen & Meckling, 1976). This however cannot be said in firms where there are diverse and dispersed owners with their shares freely transferrable. The manager is perceived as a self-serving individual seeking to maximize his own utility at the expense of the shareholders and will only work for the interest of the shareholders if properly monitored and incentivized. In other words it becomes an obvious assertion that there is a divergence of interests between the managers and the shareholders (Eisenhardt, 1989).

3.2.2.2 Stakeholder Theory Model of Corporate Governance

Stanford Research Institute (SRI) defined stakeholders as "those groups without whose support the organization would cease to exist" (SRI, 1963; quoted in Freeman, 1984, p. 31). The underlying assumption of the stakeholder theory is that the firm does not operate in isolation as there are many groups that contribute to the success mission of the firm. Their interests must also be taken into consideration by the company. This theory goes beyond the principal-agent relationship. These stakeholders include but not limited to the host community, government, employees, creditors, suppliers, customers etc. (Ayuso, Rodriguez, Garcia-Castro, & Arino, 2014; Gillan, 2006; John & Senbet, 1998). According to Freeman (1984), anyone that is a necessary contributor to the survival of the firm is deemed a stakeholder as they expect different kinds of return. Countries like Japan and Germany incorporate this theory into their corporate governance codes where the interest of other firm stakeholders is taken into consideration in the composition of the boards as they operate a two-tier board system. This school of thought find support from John and Senbet (1998) who are of the view that managers are not for the interest of the shareholders alone as posited by the agency theory, but also caring for the interest of

other stakeholders. Therefore, the goal of the firm must go beyond financial performance measure as used in the financial and economics literatures and should encompass what Ayuso *et al.* (2014) addressed as the Corporate Social Responsibility (CSR) concept.

Donaldson and Preston (1995) classify the stakeholder theory as consisting of three different categories; descriptive/empirical, instrumental, and normative. The descriptive classification provides insight into the company as a constellation of co-operative and competitive interests possessing intrinsic value, and explains company specific characteristics and the managerial behaviour. This theory underscores the fact that the firm has stakeholders. Instrumental aspect of the stakeholder theory projects that recognition of the stakeholders by the management will drive them towards the organizational goals as it provides the outcome of the company/managerial behaviour. It holds that once other firm stakeholders are considered in decision making by management, it will result in better company performance (financial and otherwise) that will be to the advantage of the shareholders in the long run. In other words the outcome is contingent on the behaviour (Jones & Wicks, 1999). Normative aspect of the stakeholder theory provides insight as to the reason for stakeholders' recognition by the management and is used to interpret the function of the corporation, including the identification of ethical guidelines for the operation and management of companies. The thrust of the normative aspect is that moral obligation is placed on the managers to accommodate the interests of all the divergent stakeholders (Jones & Wicks, 1999).

Jones and Wicks (1999) discussed the combination of normative and instrumental elements of the stakeholder theory into what they termed convergent stakeholder theory. They grouped the stakeholder theory classification of Donaldson and Preston (1995) into two by identifying the descriptive/empirical and instrumental elements as the social science-based theory and the normative element as ethics-based theory.

3.2.3 Resource Dependence Theory of the Board of Directors

In as much as the agency theory satisfies the monitoring role of the board, it does not make up for the advisory and resource provision roles of the board and the ability of the board to do effective monitoring. Hillman and Dalziel (2003) therefore suggest the integration of agency theory and resource dependence theory so as to enhance the effectiveness of the board. Mudambi and Pedersen (2007) in their examination of the complementary role of the two theories described them as pillars upon which decision making in MNCs subsidiaries by managers can be understood. According to Hillman, Cannella, and Paetzold (2000, p. 238), the board of directors in their resource dependence role, "serve to connect the firm with external factors which generate uncertainty and external dependencies." The ability of the board to satisfy these dual roles (Johnson, Daily, & Ellstrand, 1996) depends on its diversity and this is considered under the resource dependence theory (Şener, Varoğlu, & Aren, 2011). The board is seen as a cohesive agent that bonds the interest of the shareholders and other stakeholders to that of the executive management. Şener *et al.* (2011) and Zahra and Pearce (1989) describe them as boundary-spanners who provide timely needed information to the executives. Hillman *et al.* (2000) describe the board as an important link between the firm and her external environment that assists the company in reducing the uncertainty in the external environment.

Hillman and Dalziel (2003) argue that both monitoring and advisory roles of the board are functions of the board capital (experience, reputation, expertise, and network ties) since outside directors are heterogeneous. In integrating the agency and resource dependence perspectives as suggested by Hillman and Dalziel (2003), Dalziel *et al.* (2011) examined the different effects of inside and outside directors' human capital on R&D using a sample of 221 companies in the US. They conclude that director independence has effect on the extent that directors use their human capital to influence R&D spending. Directors that must be admitted to the board must have the above requisite qualifications that will make them add value to the company. Such value adding services include attracting resources to the firm from outside through their network ties, building political linkages for the firm, introducing new customers and suppliers, and through their wealth of experience and knowledge providing sound advisory services to the executives for the enhancement of firm value (Haniffa & Cooke, 2002; Hillman *et al.*, 2000; Linck *et al.*, 2008; Sarkar & Sarkar, 2009).

Hillman *et al.* (2000) report that environmental characteristic is an important influencer of board composition as new environmental factors will dictate the new resources that will be needed by the firm. It is also reported that politically connected boards add value to the company (Goldman, Rocholl, & So, 2009). A firm that is moving from a regulated regime to deregulation era will need to make a change in its board composition to suit the need of the moment. The same effect is seen when there are changes in corporate governance codes of countries making new specific demands on the firm's corporate governance practice such as having more independent board members. This group of outside directors with requisite

knowledge of the business environment will be able to make meaningful input into executive compensation design policy decisions for the firm. Outside directors because of their reputational concerns may likely desire to strengthen the company's credibility and reputation (Daily & Schwenk, 1996).

Boone *et al.* (2007) examine the factors that shape corporate boards for a ten-year period beginning from its IPO date. They document that there is a positive relationship between firm complexity and board structure (board size and independence) in high growth firms. They show further that board structure is a reflection of both firm's competitive environment and managerial characteristics. Boone *et al.* (2007) finding receive empirical support from Linck *et al.* (2008) as they document that firm size is positively related to board size and independence. As board reforms continue in several countries, Boone *et al.* (2007) identify three forces that are determinants of board size and composition as the scope of operation hypothesis, monitoring hypothesis, and negotiation hypothesis.

3.3 Corporate Governance

Effective corporate governance mechanism in any corporate organization cannot be overemphasized as it has been identified as a *sine qua non* by institutional investors that desire to invest in emerging economies (Gibson, 2003). It is argued that adherence to the codes by companies signals their governance quality (Munisi, Hermes, & Randøy, 2014). The extant literature provides empirical support for the influence of corporate governance on executive compensation and company performance (Chen, Cheung, Stouraitis, & Wong, 2005; Core *et al.*, 1999; Reddy, Abidin, & You, 2015). The Asian financial crisis and the collapse of Enron, Tyco,

and WorldCom and other companies around the globe were all blamed on poor corporate governance practice (Brown, 2008; Glick, 2002; Johnson, Boone, Breach, & Friedman, 2000; Walker, 2005). A rational investor will be very much concerned about the corporate governance practice of the firm he wants to add to his investment portfolio. Stanwick (2008) argues that foreign investors will be glad to invest in countries with good corporate governance structure at a premium. This is because such environment guarantees the safety of their investments.

Different international organisations like the Pan African Consultative Forum on Corporate Governance, Organisation of Economic Cooperation and Development (OECD), Global Corporate Governance, and the Commonwealth Association of Corporate Governance are at the forefront of the campaign for good corporate governance practice by companies (Adekoya, 2011). In 2003, Nigeria formally joined the league of countries with corporate governance codes for listed companies in an effort to make listed companies conform to international good corporate governance practice by publishing the Code of Corporate Governance for Public Companies in Nigeria.

It therefore becomes necessary to provide insight into the various definitions of corporate governance so as to understand its context in this research topic. In this section, corporate governance is considered from the international perspective so as to have a broader view of the subject matter since the Nigerian corporate governance system has been discussed in chapter two. The corporate governance landscape is a fairly well-researched topic spanning several countries from the Americas to Europe and Asia (Naciri, 2008). The results from the literature suggest that there cannot be a

uniform corporate governance system because of the differences in legislation, national culture, and level of economic development. For example, Stanwick (2008) examined and compared the corporate governance system in the US and Europe and concludes that while there are certain standards that are universal in nature, some others are country specific. In the normal owner entrepreneur enterprise the issue of executive monitoring does not arise since the manager and the owner is the same individual that does not make for any form of divergence of interest.

However, the separation of ownership and control in large organizations results in agency conflict between managers and shareholders as predicted by the agency theory (Jensen & Meckling, 1976). This agency conflict requires a mechanism that will help mitigate it (Gillan, 2006; Simanjuntak, 2001). Besides, there are other company stakeholders whose interests must be synchronized with that of the overall organizational objectives. According to Freeman and Reed (1983), anyone that is a necessary contributor to the survival of the firm is deemed a stakeholder. This group includes but not limited to the host community, government, employees, creditors, suppliers, and customers who have different interests in the organization resulting in different agency problems (Gillan, 2006; John & Senbet, 1998).

It is as a result of the above needs that corporate governance evolved as a field of research. After several decades of study there is no accepted universal definition of corporate governance because it has its roots in several academic disciplines as finance, economics, accounting, law, management, organizational behaviour etc. (Balc, Ilies, Cioban, & Cuza, 2013; Durisin & Puzone, 2009; Rwegasira, 2000). In fact, Durisin and Puzone (2009) in their study had to investigate whether corporate

governance is a discipline on its own or multi-disciplinary research area. They report that corporate governance has come of age in sophistication, depth and rigour, and consistency in the extent of its intellectual structure. Resulting from its root in different academic disciplines, there is bound to be diverse definitions from different authors depending on their perception on the subject. Claessens and Yurtoglu (2013) agree to the heterogeneous definition of corporate governance as they discussed the narrow and broad definitions of corporate governance. The narrow view definitions focus on the role of board of directors in protecting the interests of the shareholders while the broad view definitions centre on all inclusive corporate governance mechanisms by considering the interests of all the company's relevant stakeholders. The literature points that corporate governance mechanism could either be internal or external to the firm (Baysinger & Hoskisson, 1990; Denis & McConnell, 2003; Gillan, 2006). For example, Denis and McConnell (2003) states that board of directors and ownership structure are internal corporate governance mechanisms while corporate control and legal system are external mechanisms.

In another strand of literature, Rwegasira (2000) and Denis and McConnell (2003) classified corporate governance as either market-based or institutionally-based system. The market-based system takes after the Anglo-American model while the institutionally-based system takes after the Germany-Japan model of corporate governance. Discussed hereunder are the various definitions of corporate governance as contained in the extant literature. For some scholars corporate governance is seen as a part of the solution to the agency problem by devising measures to align the interest of the manager with those of the shareholders. For example Baysinger and Hoskisson (1990, p. 72) define corporate governance "…as the integrated set of

internal and external controls that harmonize manager-shareholder (agency) conflicts of interest resulting from the separation of ownership and control." According to Shleifer and Vishny (1997), and Denis and McConnell (2003), corporate governance is a mechanism through which suppliers of capital are able to induce and monitor the manager so as to guarantee the security of their investment. The above definitions fall under the narrow view of corporate governance as a means of serving the interests of the investors by excluding other firm stakeholders as classified by Claessens and Yurtoglu (2013). These definitions underscore the point that corporate governance practice serves to mitigate the agency conflict between the managers and shareholders of companies.

Other definitions that consider other firm stakeholders whose interests must be catered for by the company's management are discussed next. These definitions come under the broad view categorization of Claessens and Yurtoglu (2013). The Cadbury Committee (1992) defines corporate governance as a system through which the operations of a company are directed and controlled. Filatotchev and Boyd (2009) view corporate governance from a broader perspective as a means that assures a company is effectively and efficiently managed. Taking a structural view, Rwegasira (2000) defines corporate governance as the internal structures put in place to guide the operations of the company. Similar to Rwegasira (2000), Ehikioya (2009) defines corporate governance not only as a structure but also a process that ensures the interests of all relevant stakeholders of the company are adequately catered for.

For Sanda *et al.* (2005), corporate governance is a mechanism adopted by company stakeholders to make the internal managers work for the protection of their interests.

According to John and Senbet (1998, p. 374) "…corporate governance is a means by which various stakeholders exert control over a corporation by exercising certain rights as established in the existing legal and regulatory frameworks as well as corporate bylaws." Another definition provided by the Organization of Economic Co-operation and Development OECD (2004, p. 11) shows that "Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined."

The above definitions show corporate governance as an effort at meeting the needs of all the company stakeholders as OECD definition builds a nexus between the narrow and broad view classifications. Conclusively, it is deemed appropriate at this juncture to align with the broad view of corporate governance and as such for the purpose of this study, corporate governance is defined as a mechanism whether internal to the firm or externally imposed that ensures firms are transparently managed to deliver value to all relevant stakeholders. This suggested definition of corporate governance here implies the ability of the board to enter into transparent optimal contract with the CEO for his or her pay and enhancement of the company's performance whether financial, social, ethical or otherwise.

Firms are heterogeneous entities that have different governance problems that will require different approaches to tackle those (Adams, Hermalin, & Weisbach, 2010). Therefore applying the same governance standards for all firms may not be suitable as it will sometime be counterproductive. It is also appreciated that different countries

have developed different approaches to corporate governance system that is most suitable to their specific environment (see Naciri, 2008). In fact, Rwegasira (2000) suggests that African countries should adapt the institutionally-based model to suit their country specifics just as Ehikioya (2009) document that there is no one size fits all corporate governance system.

Table 3.1
Summary of Definitions of Corporate Governance

Author and Year	Mechanism	Structure	Narrow view	Broad view
Baysinger and Hoskisson (1990)	√		√	
Denis and McConnell (2003)	√		√	
Shleifer and Vishny (1997)	√		√	
Cadbury Committee (1992)	√			√
Filatochev and Boyd (2009)	√			√
Rwegasira (2000)		√		√
Ehikioya (2009)		√		√
Sanda *et al.* (2005)	√			√
John and Senbet (1998)	√			√
OECD (2004)	√			√

3.3.1 Market-Based Vs. Institutionally-Based Corporate Governance System

Market-based corporate governance system is operational in US, UK because of their strong support for the free market economy. It is described as the Anglo-American system of corporate governance (Rwegasira, 2000). This system is characterized by a single-tier board with large diffused shareholders, market for corporate control, and strong investor protection rights (Rwegasira, 2000). Denis and McConnell (2003) in their study identify board of directors and ownership structure as the internal corporate governance mechanisms of the firm while corporate control and legal system serve as external mechanisms. Gillan (2006) on his part identifies board of

directors, managerial incentives, capital structures, bylaw and charter provisions, and internal control system as internal mechanisms while law/regulation, markets, and media are identified with external corporate governance mechanisms. The board of directors serves as the agent of the diffused shareholders whose duty is to monitor, discipline, hire and fire the manager whenever the need arises (Jensen, 1993). The alienable rights of the shareholders help them to dispose of their shares at will if they are not satisfied with the running of the company. This may in turn have adverse effect on the fortunes of the company and ability of the manager as there could be takeover bids from raiders.

The institutionally-based system of corporate governance is also called the "bank-based" system because of the role of the bank in providing long-term fund for the company. Under this system the dual board structure comprising the management board and the supervisory board is operational (Rwegasira, 2000). This is the Germany-Japan system of corporate governance. Further, Bien, Délga, and Ged (2008) show that a country's legal system has strong influence in determining its corporate governance system. They argued that the Anglo-American corporate governance system is suitable for countries with "common law" origin like US and the UK but not for France with a "civil law" origin. While Rwegasira (2000) offered Africa a choice to adapt the institutionally-based corporate governance system, Denis and McConnell (2003) combine both systems in their definition of corporate governance. Claessens and Yurtoglu (2013) report that voluntary and market corporate governance mechanisms are not suitable for a country with weak corporate governance system. Similarly, Rwegasira (2000) show that the Anglo-American model of corporate governance is suitable for countries with strong investor

protection rights. It can therefore be inferred that the Anglo-American model of corporate governance may not be suitable for a country like Nigeria with weak investor protection rights (Okike, 2007; Yakasai, 2001). However, Nigeria's corporate governance code is patterned after the UK style of corporate governance even though the requisite attributes for its effective operation is absent in the country.

3.4 Board of Directors

In a typical market economy there is the separation of ownership and control in companies where the shareholders have delegated the control of the company to professional managers. If the professional managers are left to themselves they may actually not act in the overall interest of the shareholders as they are likely to exhibit opportunistic behaviour to the detriment of the shareholders. The diffused nature of shareholdings in public companies makes it practically impossible for all of them to be involved in monitoring the activities of the professional managers. Evidence from past studies show that large groups have problem of ease of coordination, consensus in reaching decisions and free riding (Cahan, Chua, & Nyamori, 2005; John & Senbet, 1998; Linck *et al.*, 2008).

This predicament of the shareholders found "relief" in the creation of another agent termed the board of directors to do the monitoring of the executives on behalf of the shareholders. The board therefore has been described as an internal corporate governance mechanism of the company that is put in place to serve as the representatives of the diffused shareholders to monitor the executives and ensure the safety of their investments (Baysinger & Hoskisson, 1990; Boyd, 1994; Brick *et al.*,

2006; Dehaene *et al.*, 2001; Guest, 2008; Hermalin & Weisbach, 2003; Hillman *et al.*, 2000; Jensen, 1993; Lefort & Urzúa, 2008; Ozdemir & Upneja, 2012).

The board is little known once the company is performing well as all accolades go to the management team especially the CEO who then becomes a superstar. This could be attributed to the fact that the board seldom meets as a group coupled with the committee structure of the board that also does not meet regularly. Above all, the board has delegated the day-to-day running of the company to the executive management. However, once there is a bust in the company's operations the board gets easily noticed (Adams *et al.*, 2010). The importance of the existence of the board in corporate organizations is not in doubt. It is widely acclaimed that it has a role to play in mediating between the diffused shareholders and the professional managers who have taken control of the day-to-day running of the company (Fama & Jensen, 1983b; Jensen & Meckling, 1976). In a situation where the takeover market is weak and the internal control mechanism is also weak, it becomes a tedious task replacing a poor performing manager. According to Fama and Jensen (1983b), more outside directors on boards do the monitoring of the management in situations that there is weak takeover market. This aptly fits the Nigerian situation where the takeover market is almost non-existent and as such there is supposed to be strong independent boards to meet the expectation of the agency theory.

The board is one of the firm's key internal corporate governance mechanisms that have been discussed extensively in the corporate governance literature (Fama & Jensen, 1983b; Guest, 2008; Şener *et al.*, 2011). The board performs various functions as policy and strategy formulation, hiring and firing executives,

determination of executive compensation, advising, and monitoring the activities of management (Boyd, 1994; Brick *et al.*, 2006; Jensen, 1993; Linck *et al.*, 2008; Zahra & Pearce, 1989). In a nutshell, it is the responsibility of the board to ensure that the codes of corporate governance are adopted and implemented by the management. If this function is dutifully performed it is expected to produce increased firm performance and constrain the CEO from extracting higher compensation. However, in the case of Nigeria, there is low board transparency and inadequate professionalism by the directors (Pierce, 2011) which may in turn negatively affect their level of effectiveness.

Zahra and Pearce (1989) identified control, service and strategy as the main functions of boards. Their control is exercised over the activities of management by monitoring, hiring, firing, and determining the compensation of the executive (Masulis, Wang, & Xie, 2012; Şener *et al.*, 2011). On the service role of the board, they bring in their expertise to bear on the operations of the company since the outside directors have different backgrounds, by providing useful advice to the executive. Finally, they are responsible for drawing up the strategic plans and make strategic decisions that provide direction to the company. Since the creation of the board, the often asked question has been whether the board has been effective or otherwise in the performance of its monitoring role.

Jensen (1993) asserts that board of directors' remain ineffective to monitor the CEO because of the board culture that does not allow for antagonism. Jensen views this culture as one that needs to be jettisoned if the board must perform its assigned duty effectively. Brick *et al.* (2006) empirically investigated Jensen's view of the board

culture that does not allow for conflict. Using a sample from 1,163 to 1,441 companies in the US, they examined the CEO compensation and the directors' compensation as they relate to company performance. They report that when the directors' compensation is high, the CEO receives higher compensation. They describe their result as evidence of cronyism and that "mutual back scratching" exists between the board members and the CEO. A board that aligns with the management's interest is shirking one of its main responsibilities to the shareholders and the company. Faleye, Hoitash, and Hoitash (2011) examined the cost of intense monitoring on directors' effectiveness in the US. They find that improvement in board's monitoring quality is associated with lower executive compensation. They also acknowledge that a board that does intensive monitoring will limit managerial initiatives, as such firms are found to be less innovative. A manager that is under intense monitoring will become risk averse and as such would not want to take the risk of investing in any project that has long-term value because of the uncertainty in the business environment.

The corporate scandals and failures of the first decade of this century in the US, Europe, Australia and other countries were blamed on poor corporate governance practice. This have made legislative and regulatory authorities from several countries to turn their focus on the board of directors, in an effort to improve their corporate governance practice (Boone *et al.*, 2007; Denis & McConnell, 2003). Hillman *et al.* (2000) asserts that board structure (composition and size) is a function of uncertainty and environmental dependency facing the company. The implication is that there cannot be a uniform board structure for all companies. Consistent with Hillman *et al.* (2000), Coles, Daniel, and Naveen (2008) report that firm's complexity determines

the board structure, as complex firms are found to have large boards and majority outside directors. They associated large boards to the advisory needs of the company resulting from its complexity.

Hermalin and Weisbach (1998) argue that the board is endogenously determined as nomination to the board is through the recommendations from incumbent board members and primarily by the CEO through the nominating committee. It is therefore likely that the new board members will belong to the directors' social network. If this situation holds, then such boards may not be able to perform its monitoring role effectively, as they would like to avoid confrontation as much as possible. The outcome will be the making of a CEO that has strong influence over the board that will eventually lead to his entrenchment. Kirchmaier and Stathopoulos (2008) demonstrate that the CEOs that have access to large social networks will manifest opportunistic behaviour to the detriment of the firm. They find that CEOs social network impact on firm performance is negative, as highly connected CEOs are able to evade proper board monitoring.

3.4.1 Board Attributes

From the foregoing discussions it is evident that the board is an important corporate governance mechanism. In this section, diverse board attributes as contained in the literature from the agency theory and resource dependence theory perspectives that are expected to influence executive compensation are discussed. Since executive compensation is a regular expense that companies incur, it can be used to gauge the effectiveness of the board, since they are responsible for the design of the executive compensation policy of the company (Core *et al.*, 1999). The study limits discussion

on the following board attributes: board size, board composition, CEO duality, gender diversity, and compensation committee.

3.4.1.1 Board Size

A prominent issue in literature is the question of what should constitute the size of the board of directors that will make it effective in the discharge of its roles. Past research suggests that board size has influence as to how the board performs its oversight functions (Bebchuk & Fried, 2004; Jensen, 1993; Van Essen *et al.*, 2015; Yermack, 1996; Zahra & Pearce, 1989). Zahra and Pearce (1989) in their development of integrative model for board of directors argue that firms with large boards will have board members that are experts with experience. It is argued further that these directors will be a vital resource for the company that will enhance its financial performance. Consistent with Zahra and Pearce (1989), Anderson, Mansi, and Reeb (2004) support large boards, as they argue that this will make room for adequate monitoring of the management and thus lead to better firm performance. They argue further that large boards will do proper monitoring of management that will result in lower cost of debt. They empirically examined the relationship between board structure and the cost of debt financing in the US using a sample of 252 companies with 1,052 company-year observations from 1993 to1998. Their result indicates a negative relationship between cost of debt and board size. This suggests the effectiveness of large board size and that debtor companies are sensitive to their board size when entering into debt covenants with the creditors. In contrast, Abor (2007) examines how corporate governance influences debt financing among Ghanaian listed companies and documents that high leveraged companies are associated with larger board size.

In support of large board argument under the resource dependence theory, Coles *et al.* (2008) examined the reasoning and data behind the preference for smaller and more independent boards. They document that large boards are appropriate for complex companies because of their greater advisory needs. Further, Muth and Donaldson (1998) argue that large board will be independent of the CEO as it will be difficult for the CEO to exert dominance over the board as would otherwise be possible for a small size board. With large boards, opportunistic managers will be constrained from extracting rent as there is likely to be proper monitoring of management activities (Boone *et al.*, 2007).

On the contrary, larger boards are argued to be associated with greater agency problems that may lead to excessive executive compensation (Elkinawy & Stater, 2011). Past studies provide empirical evidence of a positive association between board size and executive compensation (Conyon & Peck, 1998; Core *et al.*, 1999; Reddy *et al.*, 2015). Conyon and Peck (1998) use cash received by the highest paid director as measure for executive compensation. On the other hand, Core *et al.* (1999) use the total compensation received by the CEO. The implication is that large boards pay higher compensation to their CEOs while lower compensation is paid to CEOs with smaller boards. Core *et al.* (1999) describe their result as proof of weak corporate governance practice that is associated with greater agency problem. In another study, Yermack (1996) examines the effectiveness of small boards in his study of 452 large industrial companies from US between 1984 and 1991. Using inside stock ownership, availability of growth opportunities, industry, board composition, firm size, diversification, company age as control variables he argues that decision making is not made quickly in large boards and as such concludes that

the size of the board be minimal. He reports that small board size firms report higher firm value. He went further to show that board size and firm performance are negatively related, and that smaller boards are associated with CEO receiving performance incentives compensation as part of his or her total compensation. Boyd (1994) lends support for small boards as this allows for stronger control of the company.

Contrary to Muth and Donaldson (1998), Cheng (2008) argues that CEO becomes powerful and is able to exercise control over the board as the board size increases. Using the heteroskedasticity test to panel data, he documents that decision making in large boards is laden with compromises that tend to lower variability of firm performance measured as annual ROA, monthly stock returns, and Tobin's Q. Cahan *et al.* (2005) examined whether board structure affects board effectiveness in public companies in New Zealand with focus on the relationship between board characteristics and CEO compensation. They argue that cohesion on large boards will be low just as Jensen (1993) in his criticism of large boards suggests a board size of seven or eight will make for board effectiveness. This is because large boards are likely to have coordination problems and hard to reach consensus (Cahan *et al.*, 2005; Cheng, 2008; Yermack, 1996). They conclude that smaller boards constrain the CEO from extracting higher compensation as they find that CEOs receive higher pay in companies with large boards. It is therefore likely that the difficulty of coordination and reaching consensus in decision making associated with large boards, will make the CEO have control over the board and thus appropriate private benefits in form of excessive executive compensation (Jensen, 1993).

Recently, in an assessment of the managerial power theory, Van Essen *et al.* (2015) conducted a meta-analysis of 219 US companies to understand the determinants of executive compensation. Consistent with past studies Bebchuk and Fried (2004), and Zahra and Pearce (1989), they argued that large boards may not likely constrain managerial power because of their coordination problem and inability to reach consensus. They find support for the managerial power theory and conclude that CEOs of companies with large boards receive higher total compensation. Correa and Lel (2014) examined the effect of say-on-pay law from 39 countries and find evidence of a positive association between board size and executive compensation. Recent study in New Zealand also suggests that CEOs receive higher compensation when the number of board members increases (Reddy *et al.*, 2015).

Straddled between the small and large board advocates are other authors whose findings return indifferent results. For example, using industry-adjusted return on assets as a measure of companies profitability, Eisenberg, Sundgren, and Wells (1998) in their study of 900 small companies from Finland report a negative correlation between board size and profitability. They went further to conclude that there is no universal standard size for board of directors as it is largely determined by the size of the firm. Similarly, Linck *et al.* (2008) could not find any evidence to support the argument that small size boards are superior to large boards and vice-versa. They report that 45% of the variation in board structure is as a result of costs and benefits associated with the board's monitoring and advising roles. The equivocal results from the extant literature suggest there is no one size fits all approach as there could be advantages and disadvantages for adopting either the large or small size board. With contradicting result from literature, in Nigeria, the CG Code recommends a minimum

board size of five while there is no stipulated maximum size. The required board size should therefore be in line with company's requirement considering the complexity of its operations.

3.4.1.2 Board Composition

Barkema and Gomez-Mejia (1998) attributed the attention being paid to boards to their link with the excessive CEO compensation, since they are responsible for designing the company's compensation policy. The focus on board composition is the question as to what should be the proportion of the inside and outside directors on the board. There are different arguments as to whether the board should be independent of the management or otherwise. Those that are against board independence argue that the non-executive directors lack the inner working knowledge of the company, that incapacitates them from providing quality leadership and direction for the company (Linck *et al.*, 2008). In addition, as a result of information asymmetry between the outside and inside directors, the outside directors will have to depend on the information provided by the management (Chalmers *et al.*, 2006). It has been shown that board independence does not serve as a check against self-serving behaviour of the CEO. For example, Tosi *et al.* (2003) report that most of the companies that experienced scandals that led to their collapse in the US had independent director controlled boards. It has further been argued that firms facing uncertain conditions have need of inside directors on their boards (Burkart, Gromb, & Panunzi, 1997). Past studies argue that inside directors possess more firm-specific information than their outside counterparts (Byrd & Hickman, 1992; Fama & Jensen, 1983b; Raheja, 2005). Therefore, decreasing their presence on the boards could deny the company their beneficial contributions that will reduce costs to the company.

Those that argue for board independence are of the view that independent boards will be good monitors of management and as such will be able to prevent them from exhibiting any self-serving tendency as posited by the agency theory (Hillman *et al.*, 2000; Ozdemir & Upneja, 2012; Ozerturk, 2005). An insider dominated board they argue will remain a captive of the CEO as the inside directors owe their allegiance to the CEO (Hillman *et al.*, 2000; Hossain, Prevost, & Rao, 2001; Jensen, 1993). Hossain *et al.* (2001) argue that inside directors cannot be effective monitors of management as they may not be objective in their evaluation, since they are part of the top management team. Prior studies have shown evidence of independent boards' representation of shareholders' interest, which aligns with the argument of Fama and Jensen (1983b) that independent boards will curb managerial opportunism as they will become effective monitors of management activities.

Coles *et al.* (2008) document that complex firms with more advisory needs will derive greater value by having more outside directors on their boards. Similarly, Lefort and Urzúa (2008) with evidence from Chile find that firms derive greater value by increasing the proportion of outside directors on their boards. They also report that in an attempt to improve their corporate governance rating, firms that harbour the agency conflict situation will admit professional directors to their boards. In another study, Bhagat and Bolton (2008) document that board independence is a signal for good corporate governance practice in a company. In addition, they find a positive relationship between management turnover and board independence when a company reports poor performance. In NLCs, the outside directors are required to be in the majority with at least one independent director. This is expected to ensure adequate monitoring of the management, and that compensation contract is entered into at

arm's length. This notion is not shared by a few as the press and shareholder activists are demanding the presence of more outside directors on the boards. They are not alone in this pursuit as regulators from several countries are beginning to demand for outside director majority boards in the corporate governance codes (Denis & McConnell, 2003).

Prior studies have examined the influence of board composition (independent board) on executive compensation practice of companies (Beiner, Schmid, & Wanzenried, 2011; Gregory-Smith, 2012; Mobbs, 2013; Reddy *et al.*, 2015). Different studies have argued from different perspectives from the support for majority non-executive directors dominated boards to executive directors controlled boards (Bebchuk & Fried, 2004; Beiner *et al.*, 2011; Conyon & He, 2011; Kumar & Sivaramakrishnan, 2008; Mobbs, 2013). Bebchuk and Fried (2004) recommend greater independence of the board as panacea for improving corporate governance practice and executive compensation plans in companies, as this is envisaged will more likely diminish the influence of the CEO over the board.

Past studies on the relationship between board independence and executive compensation have produced mixed findings. For example, Basu *et al.* (2007) examine the influence of corporate governance in determining top executive compensation in Japan, a country that has different economic and cultural setting from US to ascertain whether their result will be consistent with that of Core *et al.* (1999) in the US. Their result contrasts that of Core *et al.* (1999) as they find board independence to be associated with lower executive compensation. Likewise, Chhaochharia and Grinstein (2009) using the US stock exchange's new requirements

of independent director majority board, independent nominating committee and independent compensation committee, they examine the role of the board in determining the CEO compensation. They find an association between board independence and decrease in CEO compensation after the introduction of the new requirement for board independence. In contrast, Kumar and Sivaramakrishnan (2008) present a model to the effect of board independence on executive compensation in response to corporate governance reforms that encourage companies to have independent boards. To mitigate the agency conflict they allowed directors to receive equity-based incentives award from the shareholders to encourage them to do adequate monitoring of the CEO. They however find that the more dependent the directors are on the manager the more likely they are to improve shareholder value. They therefore conclude that independent boards may perform worse than dependent boards in the design of executive compensation contracts.

Chalmers *et al.* (2006) in a panel study of Australian firms from 1999 to 2002 using 532 firm-year observations find an insignificant relationship between total compensation and proportion of outside directors. Similarly, Beiner *et al.* (2011) examined a panel of over 600 firm-year observations from 2002 to 2005 of Swiss companies. Their concentration is on the effect of product market competition on executive compensation. They report an insignificant relationship between the proportion of outside directors and the fraction of equity-based to cash compensation. Gregory-Smith (2012) investigated the influence of independent compensation committee on executive compensation in the UK using a panel data of companies from 1996 to 2008. He documents lack of relationship between board independence and executive compensation. In a recent study, consistent with the insignificant

results, Reddy *et al.* (2015) document that independent directors do not have association with executive compensation in New Zealand. In a study of 2,231 companies with 12,166 company-year observation for a ten year period from 1997 to 2005, Mobbs (2013) finds that talented inside directors that are readily available substitutes for the CEO serves to strengthen board monitoring. He further reports that the demand for independent boards may not likely constrain the CEO from extracting higher compensation. These conflicting research findings could be attributed to different methodological approaches, sample population, firm characteristics and institutional contexts.

3.4.1.3 CEO Duality

Jensen (1993) argues that CEO duality leads to CEO entrenchment that enables him to exhibit opportunistic behaviour at the expense of the residual claimants. From the agency theory perspective, the separation of the position of the chairman from the CEO is seen as indicating good corporate governance practice that will ensure proper monitoring of the executives. Bebchuk and Fried (2004) argue that powerful CEOs will make it impossible for the board to negotiate their compensation contract at arm's length and that they are prone to extracting rent in form of excessive compensation. For example, Hermalin and Weisbach (1998) develop a model wherein they show that the admission of new directors to the board and executive compensation is the outcome of the bargaining process between the board and the CEO. A powerful CEO will bargain for more insiders and small size board over which he is likely to maintain control. Consistent with Hermalin and Weisbach (1998), Chen and Al-Najjar (2012) with evidence from China argue that the CEO duality will increase the CEO's bargaining power for more inside directors and small board size. Boone *et al.* (2007,

p. 71) state that "the negotiation hypothesis implies that the proportion of outsiders on the board will be negatively related to the CEO's influence and positively related to constraints on the CEO's influence." One of such constraints on the CEO's influence remains the separation of the chairman's position from the CEO as recommended by the UK Cadbury's report 1992 that has been accepted as a global good corporate governance practice.

Beatty and Zajac (1994) suggest that the separation of the chairman from the CEO can enhance the board's monitoring duty of managerial activities and thus curb managerial opportunism that can manifest in form of excessive compensation. This view is consistent with the finding of Core *et al.* (1999) that report a positive relationship between CEO duality and executive compensation, implying that weak corporate governance system will empower the CEO to earn excessive compensation. Yermack (1996), in contributing to the argument lends support for the separation of the chairman from the CEO as he finds that separating these roles has positive effect on the value of the company. Van Essen *et al.* (2015) argue that CEO duality confers immense power on an individual that is likely to make him or her evade proper board monitoring and exert immense influence over the pay setting process.

Chen, Cheung, Stouraitis, and Wong (2005) examine the impact of corporate governance on company performance in their study of 412 publicly listed companies in Hong Kong from 1995 to 1998. Using multivariate analysis they report a significant negative relationship between CEO duality and company performance measured as market-to-book ratio. Managerial entrenchment that leads to lower company performance is likely to make such managers extract private benefits in

form of excessive compensation, since the board may not able to question their actions. In contributing to the debate, Boyd (1994) argues that CEO duality so much empowers the CEO that he is able to evade board control. Under this circumstance there is the probability that the CEO will be able to influence his compensation contract. In contrast to the above findings, Dehaene *et al.* (2001) examine corporate performance and board structure using a sample of 122 large Belgian companies and report a higher ROA where the chairman is also the CEO. They interpreted their result to indicate that combining both positions in one individual will encourage the CEO to increase the size of the company or enhance his personal status. It is however pertinent to note that either of the options will increase his compensation. Firm size has been found to account for about 40% of the variation in executive compensation (Tosi *et al.*, 2000). In addition, enhancing his status will make him attract rent from the managerial labour market.

Past research documents incongruous relationship between executive compensation and CEO duality (Correa & Lel, 2014; Gregory-Smith, 2012; Tien *et al.*, 2013; Van Essen *et al.*, 2015). Correa and Lel (2014) provide evidence of a negative association between CEO duality and executive compensation with data from 39 countries when they examined the effect of say-on-pay law on executive compensation. Tien *et al.* (2013) also document that CEO duality has a negative effect on both the long-term pay and total pay for a sample of companies from computer related industries in the US. In contrast, Van Essen *et al.* (2015) report a positive relationship between CEO duality and executive compensation in another US study. Brick *et al.* (2006) investigated the relationship between directors and CEO compensation. Using a sample size of between 1,163 to 1,441 firms for their pooled OLS and fixed-effects

regression, they provide empirical support for Van Essen *et al.*'s (2015) finding as they document that companies report higher total compensation for directors where the CEO is also the board chair, suggesting it as evidence of cronyism.

However, with focus on large UK companies, Conyon (1997) examines the impact of corporate governance on top director compensation. Using a sample of 213 companies covering the period between 1988 and 1993, he could not find a significant relationship between CEO duality and director compensation unlike Brick *et al.* (2006) in their US study. Similarly, Gregory-Smith (2012) with evidence from the UK shows that CEO duality does not lead to higher executive compensation. In Nigeria, the CG Code 2011 requires the separation of the position of board chair from the CEO in order to avoid concentration of power in an individual as this could lead to exhibiting opportunistic behaviour in the form of extracting excessive compensation.

3.4.1.4 Gender Diversity

The argument from extant literature is that few women occupy directorship positions in companies (Adams & Ferreira, 2009; Farrell & Hersch, 2005; Singh, Terjesen, & Vinnicombe, 2008) and as such there are calls for increased women representation on corporate boards. Empirical support for the argument demanding more women on boards is provided by Brammer, Millington, and Pavelin (2007) where they examine the ethnic and gender diversity of boards of companies of FTSE All-Share Index in the UK in 2002. Their sample consists of all directors in 543 companies. They find that both ethnic and gender diversity are very limited and that executive positions are occupied by fewer women. Interestingly, there is increasing trend of women occupying top corporate positions in companies not because of gender affirmative

action's but because of their expertise (Lam *et al.*, 2013). Farrell and Hersch (2005) argue that a company that has diversity as an objective is more prone to add a woman to the board if there are few women on board.

What could be the reason for the clamour that more women be included in board positions? The finding of Adams and Ferreira (2009) suggests that boards with higher proportion of women do adequate monitoring of the CEO and tend to align more with the interests of the shareholders. As a proof that women directors could be really resourceful, Norway and Spain have enacted laws that require listed companies in their countries to reserve 40% of board positions for women (Adams & Ferreira, 2009; Gul, Srinidhi, & Ng, 2011). While that of Norway is already operational since 2008 that of Spain takes effect from 2015.

In a recent study Gul *et al.* (2011) investigate the effect of board gender diversity on stock price informativeness and argue that board gender diversity allows for better managerial monitoring by the board and encourages quality disclosure of information by companies. They argue further that the presence of female directors will alter the board dynamics that will make them exhibit more transparent behaviour and openness in their board deliberations. Their result shows a positive relationship between gender diversity and stock price informativeness. The presence of women directors in effect may lead to improvements in board behaviour that is also expected to influence the determination of executive compensation. Adams and Ferreira (2009) investigate whether board gender diversity has influence on firm's corporate governance and financial performance. Their sample consists of 86,714 directorships in 1,939 firms during the period 1996 to 2003. Using OLS and fixed-effects regressions, they report

that board diversity enhances meeting attendance by directors. Board diversity could therefore be a strategy for enhancing firm value. They however report no significant statistical relationship between the proportion of women on board and CEO compensation.

However, in contrast to the above arguments, Campbell and Mínguez-Vera (2008) examine the influence of gender diversity in the boardroom on company performance of Spanish companies. Two Stage Least Squares (2SLS) was used for analysis of the panel data that covered the period January 1995 to December 2000. They report an insignificant effect of the presence of one or more women director on company value measured as Tobin's Q. The ratio of men to women is found to positively influence company value. Using event study methodology, Farrell and Hersch (2005) document that the announcement of a woman as board member does not have any value enhancing effect on the company as the result showed insignificant abnormal returns on the announcement date. Elkinawy and Stater (2011) examine gender differences in executive compensation. They report that there is a positive relationship between an increase in proportion of women directors and compensation received by women. This could be an indication that female board members may be inclined to take interests in executive compensation matters as it affects women CEOs. In Nigeria, women affirmative action is gaining ground in the public sector as women are demanding for more positions in government, but this cannot be said of the private sector. From anecdotal evidence, few women occupy top executive positions in NLCs, and same applies to board directorship positions. There is dearth of research studies on women directors in Nigeria, just as there are few studies that examine women directors and executive compensation in international literature.

3.4.1.5 Compensation Committee

The perceived excessiveness of executive compensation has caused general attention to be focused on the board of directors and its compensation committee. Previous studies show that compensation committee is a committee of the board saddled with the responsibility for designing, advising on executive compensation matters, and making recommendations to the board (Anderson & Bizjak, 2003; Boivie, Bednar, & Barker, 2012; Klein, 1998; Sun & Cahan, 2009, 2012). However, the ability of the compensation committee to rein in excessive executive compensation remains inconclusive.

The demand for independent compensation committee is strong as it is expected to have effect on the executive compensation policy of the company. Countries' corporate governance reforms are requiring for compensation committee comprising of only independent directors in the expectation that it will curb managerial opportunism. A compensation committee with a good number of inside directors is suspect to be a captive of the CEO by the government and regulatory authorities as evidenced in government's corporate governance reforms (Anderson & Bizjak, 2003; Vafeas, 2003). Empirical evidence however remains inconclusive. For the compensation committee to be effective, Sun and Cahan (2012) emphasized the importance of having a high quality compensation committee in a company. In contrast to the preference for high quality compensation committee, O'Reilly and Main (2007) argue that there is no evidence that corporate governance mechanism such as compensation committee, demand for increase of non-executive directors on the compensation committee have provided any explanation for executive

compensation. Further, they show that reciprocity and social influence shape the executive compensation designed by the board (compensation committee).

Consistent with O'Reilly and Main (2007) argument, Klein (1998) describes it as sentiment the notion that outside directors and compensation committee will do better monitoring of management activities. The corporate scandals of 2000/2002 in the US is an affirmation of Klein's position as many of the failed companies had boards comprised mainly of independent directors (Tosi *et al.*, 2003). Further, Anderson and Bizjak (2003) provide empirical support for the argument against independent compensation committee, when they examine whether CEOs influence their compensation when they sit on their company's compensation committee. They sampled one hundred companies split into two equal halves (50/50) where the first fifty are companies with CEO on the compensation committee and the second fifty where the CEO does not sit on the compensation committee. The study period covered 1985 to 1998. Using multivariate analysis, they report that independent compensation committee has little effect on executive compensation, the CEO and inside directors on the compensation committee neither increases nor decreases the executive compensation. Their finding is consistent with that of Newman and Mozes (1999) which report that inside directors on the compensation committee has no relationship with executive compensation.

Daily and Johnson (1998) examine whether the composition of the compensation committee has any influence on executive compensation. Using structural equation modelling for the analysis of their 194 sample firms they find no evidence that pressure sensitive directors pay higher CEO compensation. Similarly, in a recent

study, Gregory-Smith (2012) investigates the influence of independent compensation committee on executive compensation in the UK using a panel data of companies from 1996 to 2008. The study finds a statistically insignificant relationship between executive directors on the compensation committee and executive compensation. From the extant literature, inside directors have been reputed to possess company specific information more than their outside counterparts (Fama & Jensen, 1983b). Therefore, from the information and cost perspective, having insiders on the compensation committee may be to the advantage of the company (Anderson & Bizjak, 2003).

On the contrary, Boivie *et al.* (2012) argue that the appointment of new directors by the CEO and other directors creates what Brick *et al*. (2006) describe as cronyism that may make them support any executive compensation template presented to them, because there is a board culture that does not allow for criticism. This argument lends credence to the conjecture that captive boards cannot work to protect the interest of the shareholders. In another study, Melis, Carta, and Gaia (2012) provide evidence from Italy of a significant positive relationship between independent compensation committee and stock option plans component of executive compensation. Sun and Cahan (2012) study the economic determinants of compensation committee quality in firms that have only independent directors on the committee. They used six compensation committee characteristics developed by Sun and Cahan (2009) for their regression analysis. The result shows the following to be likely contributors to composition of the formation of high quality compensation committees: where the CEO does not have much influence, less institutional investors, less growth opportunities, and small size firms. This is interpreted to mean that CEOs with much

influence will compromise the compensation committee and institutional investors could have overbearing influence over the committee. With established various determinants of compensation committee quality, it becomes evident that there is no universal model that will suit similar firms under different circumstances.

In addition, prior studies provide evidence of inside director dominated compensation committee awarding higher pay to the CEO. For example, Vafeas (2003) examines director tenure and outside director independence as a measure of board quality. Using regression analysis on a sample of 483 companies for 1994, he documents that inside directors on the compensation committee show opportunistic behaviour in the pay setting process prior to the compensation disclosure reform in the US by US Securities and Exchange Commission in 1992. However, listed companies in Nigeria are required to establish a compensation committee comprising only outside directors. This is an effort at ensuring the committee independence from the management so as not to be able to influence their compensation.

3.5 Ownership Structure

3.5.1 CEO Ownership

Agency theory recognizes that substantial shareholding by CEOs can help align their interests with those of the shareholders thus mitigating the agency conflicts (Fama & Jensen, 1983b). Jensen and Meckling (1976) argue under the convergence of interest hypothesis that higher equity holdings by the CEOs will align their interest with those of the shareholders. It is therefore likely that higher CEO shareholding would inhibit excessive executive compensation and also reduce monitoring costs. When CEOs own shares in their companies they have the incentive to improve company

performance and earn additional dividend income as poor performance will often lead to CEO turnover (Hermalin & Weisbach, 2003). In support of this argument, Renneboog and Zhao (2011) suggest that CEO ownership may prevent excessive executive compensation. Hubbard and Palia (1995) assert that CEO equity holdings align their interest with those of the shareholders. This preposition holds under the convergence of interest hypothesis. On the other hand is the entrenchment hypothesis which posits that as the CEO's shareholding increases, he acquires more power that enables him exercise control in the company and earn higher compensation (Fahlenbrach, 2009). This power may likely make him behave in a way that hurts other shareholders in as much as his interest is secured.

Shin and Seo (2011) examine how institutional investor heterogeneity influences CEO pay after distinguishing pension funds from mutual funds. After controlling for CEO ownership, they find a significant negative relationship between CEO ownership and CEO pay (total pay and cash pay). In another study, Conyon and He (2011) document that CEOs equity holdings will align their interest with those of the shareholders. The finding of Lin, Kuo, and Wang (2013) is similar to that of Conyon and He (2011). In a recent study that contrasts the above findings, Ben Hassen *et al.* (2015) examine the relationship between executive compensation and ownership structure in France. They argue that share ownership by CEOs will make them receive higher compensation. They find support for their argument as they document a positive relationship between CEO ownership and executive compensation. The implication is that CEOs use their shareholding to extract private benefits of higher compensation thus expropriating the minority shareholders. From the UK, Gregory-Smith (2012) provides evidence of no significant relationship between CEO

shareholding and executive compensation. The above findings provide evidence of mixed results on the relationship between CEO ownership and executive compensation from previous studies.

3.5.2 Directors Ownership

The primary duty of the directors is the monitoring of managerial actions to protect the interest of the shareholders. It has however been noted that directors may not be fully committed to serving the shareholders interest without any personal stake. It is on this premise that the agency theory proposes that directors should have equity holdings in companies where they sit as directors so as to make them align their interest with those of the shareholders. Share ownership by directors has been suggested as a way of mitigating the principal-agent conflicts as this will help align the interest of the directors with those of the shareholders, thereby making them to take delight in doing adequate monitoring of managerial activities (Cheng & Firth, 2005; Jensen & Meckling, 1976; Jensen, 1993). It is argued that substantial shareholdings by directors will make them align their interest with those of the shareholders as poor company performance will hurt them personally (Yakasai, 2001). There is however contradictions from theory as the convergence of interest differs from the entrenchment hypothesis. Empirical studies also provide equivocal results. Under the convergence of interest hypothesis, it holds that the more shareholding by the directors the more they endeavour to align with the interest of the shareholders. Under the entrenchment hypothesis, increased shareholding may diverge their interest from those of the shareholders, as they become self-serving in contrast to the agency theory conjecture (Jensen, 1993; McConnell & Servaes, 1995).

Bhagat and Bolton (2008) recognized the possibility of directors with appropriate stock ownership to be motivated to do effective monitoring of the executive. In their study of 847 companies covering the period between 1998 and 2002, they examine the relationship between management turnover and director stock ownership. They report a positive relationship between management turnover and director stock ownership when a company reports poor performance. In another study, Ozkan (2007) report a negative relationship between directors' ownership and executive compensation in UK indicating that managerial ownership aligns managers' interests with those of the shareholders. Shareholders (directors) however become weak once they enter into business relationship with the company that makes them become pressure sensitive. Consistent with this view, David, Kochhar, and Levitas (1998) aver that CEOs are likely to become self-serving in the presence of weak owners as this may likely make them powerful and have overbearing influence in determining their own compensation. They examined the influence of institutional investors on CEO compensation policy in their sample of 125 firms from 1990 to 1994. Using Generalized Least Squares (GLS) method for analysis, they find a negative relationship between institutional investors that are pressure resistant and executive compensation. This suggests that investors without any business relationship with the company may be inclined to do proper monitoring of executive compensation to ensure pay-for-performance and not pay-for-luck.

With evidence from Hong Kong, Firth, Tam, and Tang (1999) examine the determinants of top management compensation from a sample of 125 companies covering the period 1990 to 1994. Using GLS they report that directors' ownership has moderating effect on the pay-performance relationship. In contrast to this finding,

Core *et al.*(1999) document that outside directors shareholdings have no relationship with executive compensation. Similarly, Reddy *et al.* (2015) find no significant relationship between directors' ownership and executive compensation.

3.5.3 Blockholders Ownership

The role of the blockholders ownership in influencing company management remains mixed in the extant literature. While it is argued that their presence protects the interests of the minority shareholders by some scholars, others have argued from the expropriation point of view (Chhaochharia, Kumar, & Niessen-Ruenzi, 2012; Derrien, Kecskés, & Thesmar, 2013; Firth *et al.*, 2007; Khan *et al.*, 2005; La Porta, López de Silanes, Shleifer, & Vishny, 1998; La Porta, Lopez-de-Silanes, & Shleifer, 1999; Lemmon & Lins, 2003; Ozkan, 2007). For example, La Porta *et al.* (1998) argue that companies in countries with weak market for corporate control and weak investors' protection rights will experience increased agency problems between controlling shareholders and the minority shareholders. Similarly, La Porta *et al.* (1999) recognised blockholders ownership as a source of agency problem in companies because of the propensity in them to extract private benefits of control to the detriment of the minority shareholders. There are studies that have examined how blockholders ownership influence company performance, but does not show how it influences executive compensation (Boubakri, Cosset, & Guedhami, 2005; Cronqvist & Fahlenbrach, 2009). There is however another strand of literature that discusses the relationship between blockholders ownership and executive compensation (Cheng & Firth, 2005; Firth *et al.*, 2007; Khan *et al.*, 2005).

Previous studies that examine the relationship between blockholder ownership and executive compensation document that the proportion of shares held by block shareholders is associated with lower executive compensation (Cheng & Firth, 2005; Firth *et al.*, 2007; Khan *et al.*, 2005; Ozkan, 2007). Firth *et al.* (2007) argue that block outside shareholders will use their influence to constrain the CEO from extracting excessive compensation. Their result documents a statistically significant negative relationship between large outside shareholders and executive compensation. They were however unmindful of the tendency those heterogeneous block shareholders will have different investment objectives. For example, Shin and Seo (2011) report that mutual fund ownership and public pension fund ownership exert opposite influence on executive compensation.

Cheng and Firth (2005) examine how ownership structure and governance characteristics affect top executives pay in Hong Kong during the period 1994 to 1999 using a sample of 2,016 firm-year observations. Using highest paid director as proxy for CEO compensation, they find a significant negative relationship between institutional share ownership and executive compensation. This finding supports their argument that institutional investors will constrain the CEO from extracting higher compensation as a result of their monitoring and oversight activities. Ozkan (2007) investigates the influence of ownership and board structure of companies on the level of CEO compensation. Using data for 2003/2004 fiscal year for a sample of 414 large UK companies after controlling for other company characteristics, they find that block shareholders are associated with decrease in CEO compensation. This is in congruence with the argument that block shareholders do active monitoring in companies to protect their investments.

In Australia, Chalmers *et al.* (2006) examine the determinants of executive compensation in a sample of 532 firm-year observations from 1999 to 2002. Using pooled time-series cross-sectional multiple regression analysis, they report regression results for total compensation, salary and allowances, bonus, options granted, and shares granted. They find that block (substantial) shareholders are not determinants of executive compensation as the result indicates no significant relationship. This finding contrasts the result of Ozkan (2007). In a related study, Lee (2009) investigates CEO performance-based compensation in Australian and Singaporean companies. The sample consists of 150 companies comprising both performance-increasing and performance-declining companies during the period 2003. The result indicates that ownership concentration is not a strong determinant of performance-pay component of executive compensation in both countries.

Blockholders ownership is expected to have an influence on executive compensation. For instance, Conyon and He (2004) examine the relationship between compensation committee and CEO compensation in US entrepreneurial companies. They document that large shareholders' presence on the compensation committee is negatively related to CEO compensation. Shleifer and Vishny (1997) suggest that block shareholders can be effective monitor of management thus assisting in mitigating the agency conflict. O'Sullivan (2000) argues that the size of their holdings incentivizes the block shareholders to engage in adequate monitoring of managerial behaviour. They are thus expected to take keen interest in executive compensation matters as this will cause the manager to align his interest with theirs. Firth *et al.* (2007) argue that the presence of outside block holders will prevent executive recklessness that leads to excessive compensation in companies. In Nigeria, there is high concentration of

ownership in a few hands whether they are institutional investors, MNCs or individual investors (Odewale & Kamardin, 2015b; ROSC, 2008; Sanda *et al.*, 2011). Their presence therefore is expected to influence the design of executive compensation. Their influence will depend on whether they align with the interest of shareholders (convergence or alignment hypothesis) or that of the manager (expropriation hypothesis).

3.5.4 Multinational Companies (MNCs) Ownership

Hannon, Huang, and Jaw (1995, p. 532) offered a definition of multinational corporation as "...a group of geographically disperse and goal-disparate organizations (including a headquarters, domestic operations and foreign ventures)." Rosenzweig and Singh (1991) define an MNC as an organization with foreign subsidiaries operating in a global environment with the challenge on how the subsidiaries will build a nexus between the local environment and overall organizational goals. The task of the MNC's subsidiary CEO is enormous as he is not only concerned with firm performance in the local market but also with the subsidiary's contribution to the MNC's global performance. Roth and O'Donnell (1996) argue that the agency problem between the MNC and its foreign subsidiaries is a vital stimulus in determining the foreign subsidiary's compensation strategy by the MNC's headquarters. It is on this premise that they suggest an MNC should have appropriate reward system for its foreign subsidiaries because of the complexity of globalization.

The MNC will be inclined to control the activities of its foreign subsidiaries so as to safeguard against hazards and achieve overall corporate objectives (Gatignon & Anderson, 1988). Gatignon and Anderson (1988) identified political and cultural

issues as reasons why it is inappropriate for MNCs to have wholly owned subsidiaries in foreign countries and suggest joint ventures with local investors. The way and manner an MNC enters a foreign market depends on its investment goal which is addressed as choice of entry mode (Musteen, Datta, & Herrmann, 2009). It could be as a wholly owned subsidiary or in joint venture with local investors. It is this joint venture that MNCs operate in foreign countries that avail local investors to own shares in MNC's subsidiaries. According to Colpan and Yoshikawa (2012), heterogeneous investors have different investment objectives and as such will favour different performance measures. In their study of large Japanese manufacturing companies, they document that the relationship between firm profitability and bonus pay is positively moderated by the presence of foreign shareholders. They further document that domestic institutional investors accept firm growth as a measure of firm performance while foreign investors use firm profitability.

As a result of diverse investment interests in foreign countries, MNCs are well equipped to transfer knowledge and intellectual capital across country borders and leverage her organizational capabilities globally (Fey & Furu, 2008; Kostova & Roth, 2002). As this is done, it may impact on the executive compensation practice of the foreign subsidiaries. From the extant literature, it is evident that the MNCs headquarters are involved in the design of the executive compensation of their foreign subsidiaries (Fey & Furu, 2008; Roth & O'Donnell, 1996) as part of their control efforts (Gatignon & Anderson, 1988). It is also possible for MNCs to appoint CEOs for their foreign subsidiaries, since these subsidiaries rely on the headquarters for resources and administrative guide (Rosenzweig & Singh, 1991) and knowledge sharing (Fey & Furu, 2008).

Fey and Furu (2008) examine how compensation systems affect knowledge sharing in MNCs and suggest that MNCs headquarters should design the top management team compensation of their subsidiaries. This is expected to align their interests with those of the MNCs CEOs at the headquarters in order to create appropriate knowledge sharing among the subsidiaries. This in turn translates to overall growth of the parent company. Realising the imperative, most recently, researchers have moved from institutional investors building a link between pay and performance to distinguishing between their different measures of performance (Colpan & Yoshikawa, 2012; Yoshikawa, Rasheed, & Del Brio, 2010). This is because institutional investors go for decisions that will suit their investment objectives due to their heterogeneity. Colpan and Yoshikawa (2012) find that the presence of foreign shareholders has a positive moderating influence on the relationship between firm profitability and bonus pay. Further, domestic institutional investors are reported to accept firm growth as a measure of firm performance, foreign investors use firm profitability, while bank investors favour the two measures of performance (Colpan & Yoshikawa, 2012). This confirms their conjecture that heterogeneous investors have different investment objectives and as such will favour different performance measures. There are studies on the human resource management of MNCs and their subsidiaries (Beechler & Yang, 1994; Hannon *et al.*, 1995), but research effort on the compensation policy of their subsidiaries is sparse (Roth & O'Donnell, 1996).

Jensen (2003) argues that a country's need to attract MNCs through foreign direct investment could make her to become pressure sensitive that could in turn make the country alter her domestic economic policy. On the contrary, Kostova and Roth (2002) state that MNCs are prone to pressure to conform to local practices and

become isomorphic with the local institutional context so as to derive and maintain its legitimacy in the foreign country. On a broader view, MNCs can exert some sort of influence on the domestic environment that will include executive compensation practice. For example, Brunello *et al.* (2001) document that listed companies that are affiliated to the MNCs report higher pay-performance sensitivity in Italy. Le *et al.* (2013) examine management compensation practice between MNCs and DCOMs in a cross country study. They argue that MNCs will use share-based incentives for their management more than the DCOMs. Consistent with their argument, they find that MNCs are more inclined to use share-based incentives for their management compensation more than the DCOMs. This finding suggests that MNCs influence the design of the executive compensation of their foreign subsidiaries. These authors only considered the presence of MNCs and failed to recognise that their share ownership could have impact on the level of executive compensation.

Colpan and Yoshikawa (2012) examine 153 large manufacturing companies that are publicly traded in Japan from 1997 - 2007 to ascertain the impact of diverse ownership structure on the firm performance–executive compensation relationship. They introduced domestic corporate-appointed directors, bank-appointed directors, and foreign ownership as moderating variables while size, leverage, executive tenure, CEO age, succession, and independent directors were used as control variables. They argue that different institutional investors have different investment (objectives) goals that will invariably affect their perceived measure of firm performance. Specifically they conjecture that foreign investors could use their influence to impact on executive compensation design of the company. In agreement with their predictions, they report that the relationship between company growth and bonus pay is positively moderated

by the domestic corporate-appointed directors, while the relationship between firm profitability and bonus pay is positively moderated by foreign ownership. As for bank appointed directors, they link firm profitability and bonus pay, at the same time show positive influence on the firm growth and bonus pay relationship. In Japan, the foreign investors may not have representations on the board but their influence is always felt as their opinions are recognised by the executive management (Colpan & Yoshikawa, 2012). In spite of the evidence that MNCs are involved in the design of executive compensation for their foreign subsidiaries, not much effort has been made to examine the extent of their influence in this regard. In Nigeria, the MNCs are among the highly capitalized companies on the NSE whose influence on executive compensation matters cannot be ignored.

It is however pertinent to emphasize that there is a wide gap between corporate governance practice in US and UK compared to Nigeria. The Anglo-American corporate governance system is reported to be suitable for countries with strong investor protection rights (Rwegasira, 2000) where the ownership is largely diffused. In the case of Nigeria, there is weak investor protection rights (Okike, 2007; Yakasai, 2001) and high concentration of ownership (Sanda *et al.*, 2011). The blue chip (large) companies like Nestle Nig. Plc, Unilever Nig. Plc, Cadbury Nig. Plc, Mobil Nig. Plc, Total Nig. Plc, PZ Cussons Nig. Plc, Guinness Nig. Plc, and Julius Berger Nig. Plc are MNCs with headquarters in foreign countries. The headquarters of these MNCs own substantial shares in their Nigerian subsidiaries which confers controlling rights on them.

The role of MNCs in developing Nigeria's economy is very important because of their level of investments in the country. Bakare (2010) report a positive relationship between MNCs and growth in Nigeria as he finds that 80% growth in the country's Gross Domestic Product (GDP) was as a result of 1% increase in MNCs direct investments. Under this circumstance it becomes imperative to understand the extent of influence exerted by MNCs on executive compensation matters in their foreign subsidiaries in Nigeria. MNCs own different percentage of shares in their foreign subsidiaries and this is likely to determine their behaviour towards the minority shareholders. Morck *et al.* (1988) in their study document that different level of shareholdings by large shareholders influences their behaviour. The extant literature distinguishes between various kinds of block shareholders to include family, directors, institutions, state and business groups (Chang, 2003; Cheng & Firth, 2005; Kato *et al.*, 2007; La Porta *et al.*, 1999). However, none has identified the influence of MNCs shareholding in their foreign subsidiaries on executive compensation in a developing economy like Nigeria.

3.6 Control Variables of Executive Compensation

Omission of important variables could result in wrong statistical decisions when evaluating relationships between dependent and independent variables. Control variables are variables that have been shown from previous studies to have effect on the dependent variable even though they are not part of independent variables of the present study. Therefore omitting certain variables that serve as explanations for executive compensation from previous studies in the model could lead to biased results. It is however pertinent to point that it may not be possible to include all explanatory variables in any model.

Prior studies on executive compensation have suggested the inclusion of control variables in the model. For example, Gabaix and Landier (2008) and Jensen and Murphy (1990b) suggest that performance and company size should be considered as part of variables that influence executive compensation. Leverage and growth are additional variables that have equally been suggested by previous researchers as having influence in determining executive compensation (Conyon & He, 2011; Mehran, 1995; Munisi & Mersland, 2013). In consonance with their suggestions, the following are included as control variables for this study: company performance, company size, leverage, growth, and industry.

3.6.1 Company Performance

Performance means different things to different people or group (stakeholders) of the company. To the community; it is about corporate social responsibility and the customers think about adequate service delivery. For the shareholders; their interest centres on wealth maximization and creditors are concerned about the interest and principal repayment. The employees' area of concern is their welfare. It is this conflicting objective that the manager has to contend with to make the company remain a going concern. Among academic researchers from accounting, finance and economics who study executive compensation from the agency theory perspective the area of interest remains the company's financial performance. The financial performance measure is still subject to various definitions as different instruments have been used by prior researchers (Girma, Thompson, & Wright, 2006).

The criticism against excessive executive compensation is not recent as it has been acknowledged several decades ago (Deckop, 1988). It was in the midst of these

criticisms that Jensen and Murphy (1990b) came up with their seminal paper wherein they argue for more incentives pay for executives to make them align their interests with those of the shareholders. In an earlier study by Taussig and Barker (1925), they suggest pay-for-performance relationship as a means for motivating the executives to work more for the interest of the shareholders. Early studies on company performance measure focused on sales or profit as basis for designing executive compensation (Lewellen & Huntsman, 1970; Meeks & Whittington, 1975; Roberts, 1956).

The managerialists' hypothesis supports sales maximization and growth of the firm while the neoclassical economists support profit maximization as the primary objective of the shareholders (Ciscel & Carroll, 1980). Increase in sales volume is dependent on the size of the company, the more the company diversifies to increase its size the more complex it becomes. This decision to expand the company size and not necessarily profit will increase the utility of the CEO at the expense of the shareholders (Ciscel, 1974; Ciscel & Carroll, 1980). Prior studies have also shown that acquisitions lower the acquirer's firm value, such acquisitions however increases firm complexity that makes the CEO to bargain for more pay (Girma *et al.*, 2006; Tosi & Gomez-Mejia, 1989).

Early studies were conducted to find a definitive explanation for executive compensation whether it is the size or profit measure of performance. In times of recession or industry specific crisis, it may be appropriate that executive compensation be based on sales rather than profit as this signals the company is maintaining its share of the market. Size on the other hand is an indication of the

complexity of the company that the CEO manages which will invariably lead to increased executive compensation. Lewellen and Huntsman (1970) investigate the relationship between executive compensation and company performance between 1942 and 1963 under three-year intervals. With a sample of 50 largest industrial companies in the US and using multivariate analysis, they find a positive relationship between profit and executive compensation. Additional support came as Deckop (1988) argues that making executive compensation dependent on firm's sales will make the executive to pursue firm growth instead of profitability to the disadvantage of the shareholders. He finds a positive relationship between executive compensation and profit margin (profit deflated by sales). His finding failed to support the sales for size argument.

On the contrary, Roberts (1956) in his study of the determinants of executive compensation examined between 410 and 939 companies spanning 1945 to 1950 and reports that there is a significant relationship between performance (sales) and executive compensation. Similarly, McGuire, Chiu, and Elbing (1962) in their study of 100 largest industrial companies find support for the sales-executive compensation argument. Ciscel (1974) also document that it is the firm size (sales) and not profit that is the primary determinant of executive compensation.

After removal of simultaneous equations bias, multicollinearity and heteroscedasticity that marred the results of earlier studies, Ciscel and Carroll (1980) in their econometric survey of the determinants of executive compensation report that executive compensation is based on company profit resulting from increased sales or reduced costs. Their finding is straddled between the managerialits and the

neoclassical economists perception of what should be used as measure of company performance. In his paper, Masson (1971) examines the sales-maximization hypothesis in relation to executive motivations. Using a sample of 39 companies from 1947 to 1966, he finds stock performance as a superior measure of company performance to either sales or profit because it takes long-term value of the company into consideration. This study was a follow-up to that of Lewellen and Huntsman (1970) that find profit as a measure for determining executive compensation. Lewellen and Huntsman (1970) find a weak statistical relationship between sales and executive compensation, and documents that market value is a major determinant of executive compensation.

Conclusively, Ciscel and Carroll (1980), show that the results of these early studies were marred by multicollinearity, heteroscedaticity and simultaneous equation bias. The option of what performance measure to adopt for executive compensation research is still open as firm size, accounting-based, and market-based measures of performance are still being used by scholars. In fact, firm size has remained a strong determinant of executive compensation as Tosi *et al.* (2000) document that firm performance is responsible for less than 5% variation in executive compensation.

3.6.2 Company Size

Previous studies have shown existence of strong relationship between company size and executive compensation (Barontini & Bozzi, 2011; Munisi & Mersland, 2013; Reddy *et al.*, 2015; Sakawa *et al.*, 2012; Shin, 2013; Tien *et al.*, 2013; Tosi *et al.*, 2000). The managerial talent theory posits a positive association between company size and executive compensation (Gabaix & Landier, 2008; Cremers & Grinstein,

2014; Falato *et al.*, 2015). This is because large complex organisations require talented managers with appropriate skills to manage them. This in turn translates to higher executive compensation. Tosi *et al.* (2000) find that more than 40% of the variation in executive compensation is traced to firm size.

Consistent with Tosi *et al.* (2000), prior studies report a significant positive relationship between company size and executive compensation (Brunello *et al.*, 2001; Chalmers *et al.*, 2006; Conyon & Murphy, 2000; Van Essen *et al.*, 2015; Zhao, 2000). In another strand of literature, Gabaix and Landier (2008) argue that large complex companies require managers with ability to manage them successfully to deliver value to the shareholders. The managers of such companies are therefore expected to command rent in the labour market. It is also argued that increasing company size is attractive and beneficial to the executives as it is accompanied by prestige, power and increased pay (Tosi *et al.*, 2000). Therefore, executives may likely be inclined to pursue increase in company size at the expense of the shareholders in order to receive higher compensation.

3.6.3 Leverage

The agency theory argues that there is agency cost when a company has debt in its capital structure. This cost will increase in proportion to the level of the debt (Jensen & Meckling, 1976; Meek, Roberts, & Gray, 1995). It is argued that debt may be used as an effective corporate governance mechanism to constrain the manager from exhibiting opportunistic behaviour (Jensen, 1986). Debt holders may therefore take interest to do adequate monitoring of management activities so as to secure interests payment and repayment of principal (Sanda *et al.*, 2005). Brunello *et al.* (2001) argue

that higher debt to equity ratio should lead to lower pay for performance sensitivity as tying pay to performance would be really hurting to the manager. Executive compensation is therefore expected to decrease with leverage.

3.6.4 Growth

The literature suggests that large companies require managers with appropriate skills and talent to manage them effectively (Gabaix & Landier, 2008; Munisi & Mersland, 2013). Core *et al.* (1999) identified growth opportunities as one of the determinants of executive compensation. Growth has been conjectured as a strategy used by executives to grow their pay (Girma *et al.*, 2006). Sales growth could be an indication of increase in the complexity of the company. Increased sales could result from merger activities which also increases companies' complexities (Core *et al.,* 1999; Girma *et al.,* 2006).

3.6.5 Industry

It is assumed that financial sector companies possess characteristics that distinguish them from non-financial companies (Firth *et al.*, 2007; Talmor & Wallace, 2001). The industry classification for this study is grouped into financial and non-financial companies so as to control for the effect of financial sector companies (banks) on executive compensation. This is because empirical studies provide evidence that industry provides explanation for the variation of executive compensation among companies (Reddy *et al.*, 2015; Yermack, 1995). Past studies have examined both the financial and non-financial sectors separately. For example, Firth *et al.* (2007)

examine executive compensation in non-financial companies while Hubbard and Palia (1995) investigate executive compensation in the banking sector.

3.7 Prior Studies on Executive Compensation

3.7.1 Corporate Governance and Executive Compensation

According to Gibson (2003), good corporate governance practice is a necessary requirement that will make foreign institutional investors take delight in investing in emerging economies. Foreign investors therefore expect the board to effectively perform its monitoring role of ensuring that the executives deliver value to the shareholders, and that they do not expropriate the diffused shareholders. Weak corporate governance structure may however lead to increase agency costs as Core *et al.* (1999) report that it will lead to excessive CEO compensation. Duffhues and Kabir (2008) aver that weak corporate governance mechanism could lead to managerial entrenchment where managers extract private benefits in form of excessive compensation to the disadvantage of firm shareholders. This becomes more severe where there is managerial domination over the board. Situations that usually give rise to managerial domination over the board includes long-serving CEOs, insider dominated boards, independent directors appointed by CEOs, CEO and board chair fused into one person. (Core *et al.*, 1999).

Poor corporate governance and inadequate incentives to company top executives could lead to poor performance by companies (Chen *et al.*, 2006). Murphy and Zabojnik (2004) concur that poor corporate governance is one of the likely causes for excessive CEO compensation. In a related study conducted by Basu *et al.* (2007), they find weak corporate governance mechanism to be responsible for excessive

executive compensation in large Japanese companies. This corroborates the finding of Core *et al.* (1999) that US companies with weak corporate governance mechanism will experience greater agency problems that could in turn lead to excessive CEO compensation. They find that independent directors have negative relationship with executive compensation, suggesting that independent directors do adequate monitoring.

3.7.2 Company Performance and Executive Compensation

There is no contention that increasing executive compensation has become a controversial issue (Correa & Lel, 2014; Cremers & Grinstein, 2014; Murphy, 1999). The issue at present is how to limit its perceived excessiveness. The vexing issue in executive compensation research is the statistically weak pay-performance sensitivity that has been reported by researchers. This contrasts the prediction of the agency theory that suggested it to mitigate the principal-agent conflict. Several studies have been conducted all in the bid to find explanation for variations in executive compensation. Tosi and Gomez-Mejia (1989) study executive compensation design in owner-controlled and management-controlled companies and report that company performance explains mostly less than 10% but rarely exceeds 15% of variation in executive compensation. They suggest that focus should be more on the design process of executive compensation and less on the measure of performance. In a related study, Tosi *et al.* (2000) in their meta-analysis report that company performance is responsible for only 5% variation in CEO compensation. These results are not in line with the expectation of the agency theory.

This section considers the relationship between firm performance and executive compensation as suggested by the agency theory. The agency theory anticipates a positive relationship between executive compensation and company performance (Barkema & Gomez-Mejia, 1998). The prediction of the agency theory is that executive compensation should be dependent on firm performance. The underlying assumption is that once the managers are adequately motivated through performance related incentives they will act in the best interest of the principal thus mitigating the agency conflict (Fama & Jensen, 1983b; Jensen & Murphy, 1990b). Acting in the best interest of the principal is to enhance their wealth through better firm performance, and this has been the reasoning behind past focus from literature on firm performance. Numerous research papers have been published by scholars on pay-performance relationship and the results remain inconsistent (Barkema & Gomez-Mejia, 1998; Gomez-Mejia & Wiseman, 1997). In the light of the foregoing, various variables have been used to proxy performance in the literature and such include: sales, profit, firm size, market-based measure, and accounting-based measure as have been discussed previously.

Firth *et al.* (2006) report a positive relationship between firm performance and CEO compensation in China even though with a low sensitivity. However, the ownership structure has influence over this relationship. Where the state owned enterprises are the highest shareholders, the CEO pay is linked to firm profitability while the link is to shareholders wealth where a private blockholder is the major shareholder. They also report a very low pay-performance sensitivity as the CEO gets less than one (1) RMB for one thousand (1000) RMB shareholder wealth increase. They suggest executive stock options be included in the CEO total compensation as an incentive to

align CEO interest to wealth maximization that is the primary interest of the shareholders. Firth *et al.* (2007) show a positive relationship between firm performance and CEO compensation (using accounting-based measure) in China. They report higher pay-performance sensitivity in firms with foreign investors' presence. The explanation for this could be that since these foreign investors are mainly from US and UK where pay-performance is the driving philosophy, they will not be averse to it in China or any other place they hold investments.

Chalmers *et al.* (2006) in their study of Australian companies from 1999 to 2002 show evidence of a positive pay-for-performance relationship in fixed salary, bonus and option compensations. They interpret their result as suggesting that compensation contracts are structured to align managers interest with those of the shareholders. Brunello *et al.* (2001) also document that there is a positive relationship between company performance and executive compensation in their Italian study but with a low sensitivity. They however report that the sensitivity is higher in companies that are affiliated to MNCs or owned by foreigners. They interpret their results as indicative of the conjecture that specific economic environment affects company pay-performance relationship.

In contrast to the above findings, Duffhues and Kabir (2008) in their study of Dutch listed companies fail to find a positive relationship between company performance and executive compensation. They document that weak corporate governance mechanism could lead to managerial entrenchment, where managers extract private benefits in form of excessive compensation to the disadvantage of the company shareholders. This lends credence to the managerial power hypothesis. Girma *et al.*

(2006) report that there is no strong relationship between firm performance and executive compensation in their sample of UK listed companies that were involved in mergers and acquisitions during the period 1981 through 1996. They further provide evidence that acquisitions lead to increase in CEO pay. Zhou (2000) document that for Canadian companies, the relationship between executive compensation and company performance is weak.

3.7.3 Board of Directors and Executive Compensation

After several decades of study on pay-performance relationship with inconsistent results, academic researchers turned their searchlight on the role of board of directors in setting executive compensation (Boyd, 1994). The board, a composition of both inside and outside directors is responsible for the design of a company's executive compensation policy to make it align the interest of the executive with those of the shareholders (Boyd, 1994; Denis & McConnell, 2003; Jensen, 1993). However, a captive board of the CEO will be unable to negotiate compensation contract with the CEO at arm's length (Bebchuk & Fried, 2004; Ozdemir & Upneja, 2012). Hermalin and Weisbach (1998) provide a model wherein executive compensation and board structure is the outcomes of the bargaining process between the board and the CEO. The present executive compensation depends on the perceived CEO ability that is assessed based on his past performance. Consider an outsider CEO that is to be recruited by the board; the negotiation process will centre on his ability to deliver in the uncertain future. The board will therefore rely on his past efforts at managing similar company in drawing up the terms of contract for the present job.

As have been discussed previously, the board remains a key internal corporate governance mechanism in the company (Jensen, 1993). Prior research has shown that it is related to executive compensation. For example, Denis and McConnell (2003) maintain that there is a relationship between the board of directors and executive compensation and as such should be viewed jointly. Chalmers *et al.* (2006) in their study report that governance (board structure) attributes have significant effect in the determination of executive compensation in Australia. Core *et al.* (1999) document that executive compensation is positively related with the following board characteristics: board size, CEO duality, proportion of outside directors appointed by the CEO, proportion of gray outside directors and the proportion of outside directors that are multiple directorship holders. They also report that executive compensation is excessive when proportion of outside directors on board is above age sixty-nine. They conclude that greater agency conflicts are prevalent in companies that have weak corporate governance structure.

Firth *et al.* (2007) document large boards have negative association with CEO pay, and independent boards are inclined to match pay for performance. Independent boards have been adjudged good internal corporate governance mechanism as they will do proper executive monitoring (Fama & Jensen, 1983b). Firm managers have the tendency to exhibit opportunistic behaviour by awarding themselves high compensation. The independent board thus acts as a check by preventing the executives from extracting private benefits since they are independent of the executives. Independent board requirement is now a norm in countries corporate governance reforms (Denis & McConnell, 2003). Chhaochharia and Grinstein (2009) used the US stock exchange's new requirements of independent director majority board, independent nominating committee and independent compensation committee

to examine the role of the board in determining the CEO compensation. They find that there is association between board independence and decrease in CEO compensation. In response to their paper, Guthrie *et al.* (2012) report that Chhaochharia and Grinstein (2009) findings were as a result of outliers in their data sample. After excluding the outliers, they report that independent boards that were made after the reform had no significant influence on executive compensation. In other words, it could be that board independence is associated with higher CEO compensation as documented in past studies (Conyon & He, 2011; Fernandes, 2008; Ozkan, 2007).

Fahlenbrach (2009) shows that entrenched managers do not influence their compensation contracts. Rather, the compensation contract is a means of aligning the interest of the executive to those of the shareholders in a weak corporate governance environment. He addressed this under the governance substitution hypothesis. In contrast, Bebchuk and Fried (2004) argue that entrenched managers may be able to influence their compensation contracts under a weak corporate governance regime to extract private benefits. This is why Bebchuk and Fried (2003) conclude that executive compensation is contributing to the agency problem rather than mitigating it.

The resonating view that CEOs and inside directors could be mischievous if given the opportunity was debunked empirically by Anderson and Bizjak (2003). They document that independent compensation committee has little effect on executive compensation, the CEO and inside directors on the compensation committee neither increases nor decreases the executive compensation. In conclusion, whether the board comprises of more outside directors or inside directors should not be the contentious

issue. Rather, the paramount issue remains the protection of shareholders interest and effectiveness of the board in discharging its statutory responsibility to the shareholders.

3.8 Summary of the Chapter

In this chapter, attempt is made to provide reviews on executive compensation, corporate governance and the different theoretical models. The chapter conducted a review of the agency theory, managerial power theory and managerial talent theory as they affect executive compensation. The agency theory shows the existence of conflicts in companies between shareholders and managers as a result of separation of ownership and control. The corporate governance characteristics and executive compensation as mechanisms for mitigating the agency conflicts were discussed. Table 3.2 presents the summary of selected studies on corporate governance characteristics, company performance and executive compensation.

An examination of prior literature on the relationship between corporate governance characteristics and executive compensation as discussed in this chapter provides equivocal findings. The reasons for these mixed findings could be attributed to country specifics, methodology, and data used for the studies. It is imperative to acknowledge that there are no empirical studies from Nigeria examining the influence of corporate governance characteristics on executive compensation. Specifically, prior studies have ignored the effect of MNCs ownership on executive compensation of their foreign subsidiaries. The present study fills this gap. The next chapter explains the theoretical framework and research methodology of the study.

Table 3.2

Summary of selected Studies on Corporate Governance Characteristics, Company Performance and Executive Compensation

Author and Year	Study Location	Dependent Variable	Main Independent Variables	Sample Size	Analysis Technique	Major Result
Anderson, R. C., & Bizjak, J. M. (2003).	US	CEO compensation	CEO characteristics Compensation committee characteristics	110 firms (1,376 firm-years)	Fixed-effects regression analysis. Difference-in-Difference methodology.	They found little support for the assertion that compensation committee independence will moderate executive compensation. The absence or presence of the CEO on the compensation committee does not affect executive compensation. Rather there is performance-pay sensitivity for large growth opportunity firms.
Balsam, S., Fernando, G. D., & Tripathy, A. (2011).	US	CEO compensation	Differentiation strategy Cost leadership strategy	1,658 firms (11,087 firm-years)	Regression analysis (Fama and MacBeth (1973) method)	Strategy is a strong determinant of executive compensation with strong emphasis on sales.
Basu, S., Hwang, L. S., Mitsudome, T., & Weintrop, J. (2007)	Japan	Top executive compensation	Firm performance Ownership Human capital Governance characteristics	174 firms (1083 executive year observations)	Pooled regression analysis	Directors' ownership is associated with higher top executive compensation. There is no relationship between board size and executive compensation. The presence of outside director shows a negative relationship with executive compensation.
Ben Hassen, R., El Ouakdi, J., & Omri, A. (2015)	France	Executive compensation	Ownership structure: Ownership concentration Discrepancy Manager ownership Family ownership Institutional ownership	388 company-year observations	Probit, Fixed-effects, and Random effects regressions	Negative relationship between ownership concentration and executive compensation. CEO ownership is associated with higher executive compensation. Family ownership shows negative relationship with executive

						compensation. Board independence is associated with lower executive compensation.
Boyd, B. K. (1994).	US	Total cash compensation	Board control: CEO duality Ratio of insiders Board stock ownership Owner representatives Director compensation	193 companies	LISREL model	The level of board control is inversely related to CEO compensation. Firm size is positively associated with CEO compensation
Brick, I. E., Palmon, O., & Wald, J. K. (2006)	US	Cash and total compensation of board members and the CEO.	CEO and Governance Characteristics: CEO age CEO gender CEO experience CEO duality CEO ownership	1163 to 1441 companies	Pooled and Fixed-effects regression	There is a strong positive relationship between CEO compensation and directors' excessive compensation. There is a negative relationship between firm performance and directors' excessive compensation. CEO ownership is associated with lower CEO compensation while CEO duality is associated with higher compensation.
Chalmers, K., Koh, P. S., & Stapledon, G. (2006)	Australia	CEO compensation	Governance and Ownership determinants: CEO duality Board size Board independence CEO ownership Outside directors ownership Substantial ownership	532 firm-year observations	Regression analysis: pooled time-series and cross-sectional multiple regression	There is a positive pay-for-performance relationship. Board size is associated with higher CEO compensation. CEO ownership is associated with lower CEO compensation. There is no significant relationship between board independence, substantial ownership and CEO compensation. Compensation committee is not associated with CEO compensation.

Conyon, M. J. (2014)	US	Executive compensation	Board independence: Affiliated board Affiliated compensation committee	28,259 firm-year observations	OLS and Fixed-effects regressions	There is a negative relationship between affiliated directors and executive compensation. There is no significant relationship between affiliated compensation committee and executive compensation. Executive compensation shows positive association with company performance and company size.
Conyon, M. J., & Leech, D. (1994).	UK	Top directors pay	Performance, Corporate governance, and Ownership structure	294 firms (1,112 firm-year observations)	Regression analysis	Corporate governance structure does not contribute in determining top directors' pay. There is a weak link between company performance and top pay.
Conyon, M. J., & He, L. (2011)	China	Executive compensation	Company performance Board size Board independence CEO duality Largest shareholder Compensation committee	1,342 firms (5,928 firm-year observations)	Pooled OLS, Random effects and Fixed effects regression analyses	Board size, board independence, and CEO duality have no significant relationship with executive compensation. The presence of compensation committee is associated with higher executive compensation. Share ownership by largest shareholders is significantly negatively related with executive compensation
Correa, R. & Lel, U. (2014)	Multi country study	CEO compensation	Say on Pay Laws Company performance Board size Independent directors CEO duality	More than 89,000 firm-year observations	Panel data regression: Fixed-effects regression. Tobit regression	There is a significant negative relationship between Say on Pay Laws and CEO compensation. Independent director is associated with higher CEO compensation. CEO compensation is higher when the board size is large. CEO duality is significantly negatively

						related to CEO compensation.
Deckop, A. R. (1988)	US	CEO compensation	Sales Profit	Between 108 and 119 firms (335 firm-year observations)	Regression: Fixed-effects and Random - effects regressions	There is a positive relationship between profit measured as a percentage of sales and executive compensation. There is no significant relationship between sales and executive compensation.
Duffhues, P., & Kabir, R. (2008)	The Netherlands	Executive compensation	Company performance: Return on Assets Return on Sales Annual Stock return Tobin's Q	500 to 532 firm-years observations	OLS regression analysis	There is a significant negative relationship between company performance measured as Tobin's Q and executive compensation.
Fernandes, N. (2008).	Portugal	Executive compensation	Company performance Board size Board independence	51 companies (142 firm-year observations)	OLS and Fixed effects regression analysis	When non-executive members dominate the board the executive pay is higher. Non-executive board members do not have a strong monitoring role. Board size is not significantly related to executive compensation
Firth, M., Fung, P. M., & Rui, O. M. (2006)	China	CEO compensation	Company performance: Return on Sales Annual Stock Return	549 companies and 1,647 firm-year observations	OLS regression	The two measures of company performance do not show any statistically significant relationship with CEO compensation.
Firth, M., Fung, P. M., & Rui, O. M. (2007)	China	CEO compensation	Company performance Board size Board composition CEO duality	549 companies and 1647 firm-year observations	Fixed-effects regression	There is a significant positive relationship between company performance and CEO compensation. There is high pay-performance sensitivity in companies with the presence of foreign investors. Large board has association with lower executive compensation.

						Independent boards are inclined to match pay for performance.
Girma, S., Thompson, S., & Wright, P. W. (2006).	UK	Executive compensation	Company performance: Operating profits Return on capital	472 acquisitions (Between 9,000 and 11,000 firm-year observations)	Fixed-effects regression analysis	Acquisitions lead to increase in CEO pay. There is no strong relationship between company performance and executive compensation. Increase in sales has significant positive relationship with CEO pay.
Graham, J. R., Li, S. & Qiu, J. (2012)	US	Executive compensation	Firm performance Managerial attributes	25,586 managers	OLS regression and Fixed-effects regression analyses	Firm and manager fixed effects are vital for explaining variations in executive compensation.
Gregory-Smith, I. (2012)	UK	CEO pay	Board of directors Remuneration committee	More than 3,000 firm-years	OLS regression, Fixed-effects, and Generalized Methods of Moments regressions.	Increased board independence does not prevent the CEO from extracting higher compensation.
Hubbard, R. G., & Palia, D. (1995).	US	CEO compensation	Shareholder wealth	147 banks	Fixed-effects regression analysis	There is a stronger positive relationship between performance and CEO pay under interstate banking deregulation than when interstate banking was not allowed. On the whole they found evidence to support managerial talent hypothesis.
Kato, T. (1997).	Japan	CEO compensation	Financial corporate group Return on Assets	154 companies	OLS regression analysis	The CEOs of independent firms earn more than those of financial group firms.

Kato, T., Kim, W., & Lee, J. H. (2007).	Korea	Executive compensation	Company performance: Stock returns	246 companies (543 firm-years observations)	OLS regression analysis	There is a significant positive relationship between stock market performance and Executive compensation. Chaebol group businesses are run to profit the group and not necessarily the minority shareholders. As a result no pay-performance sensitivity was found for Chaebol group firms whereas it existed in non-Chaebol firms.
Lee, J. (2009)	Australia and Singapore	CEO compensation	Financial performance Board independence Substantial shareholders Independent directors on board Independent directors on compensation committee CEO duality Directors shareholding	150 companies	Fixed-effects regression analysis Two Stage Least Squares regression	CEOs will receive enhanced performance-pay when their companies experience improvement in their financial performance. This is unlikely in performance declining firms. Proportion of performance based pay is associated with large companies and sales revenue becomes the parameter for such pay. Independent directors on both the board and its compensation committee do not have influence on the CEO compensation. CEO duality is associated with higher CEO compensation. There is no significant relationship between directors shareholding and CEO compensation.

Lin, D., Kuo, H. C., & Wang, L. H. (2013)	US	CEO compensation	CEO age CEO tenure CEO shareholding Board size	903 companies (3,612 firm-year observations)	Fixed-effects regression	There is a negative relationship between CEO shareholding and executive compensation. CEO tenure is not related to CEO compensation. CEO age show association with higher compensation. There is no relationship between board size and CEO compensation.
Melis, A., Carta, S., & Gaia, S. (2012)	Italy	Executive remuneration	Board independence: Independent ratio Independent chairperson Independent directors on the remuneration committee Beneficiary on the remuneration committee Minority directors ratio Minority directors on the remuneration committee	155 observations	Logistic regression analysis	Rent extraction theory explains the relationship between stock option plans for executive directors and board independence in blockholder dominated firms. The presence of representatives of minority shareholders on the board shows positive association with optimal stock options plans design. Board size and Board independence do not show association with executive remuneration Independent remuneration committee is associated with higher executive remuneration.
Mobbs, S. (2013)	US	CEO compensation	Talented inside directors Non-talented inside directors Talented outside directors 60% Independent outside directors	6,701 firm-year observations	Fixed-effects regression analysis	There is a significant negative relationship between talented inside directors and CEO compensation. No significant relationship between non-talented inside directors and CEO compensation. There is a significant negative relationship between talented outside

						director and CEO compensation.
Ozdemir, O. & Upneja, A. (2012)	US	CEO compensation	Board structure: Board size Board independence Busy directors Directors age CEO duality	64 firm-year observations	OLS regression analysis	Board independence is associated with higher CEO compensation. CEO duality is positively related to CEO compensation. Board size, busy director, and directors age are not significantly related to CEO compensation.
Ozkan, N. (2007).	UK	CEO compensation	Institutional ownership Board size Board independence Block-holder ownership CEO ownership Directors' ownership	414 companies	OLS regression and Tobit regression analyses	Institutional ownership is associated with lower CEO compensation Board size is significantly positively related to CEO compensation CEOs receive higher compensation in firms where the non-executive directors dominate the board Block-holder ownership constrains the CEO from extracting higher compensation CEO ownership is found not to have influence on CEO compensation There is significant negative relationship between directors' ownership and CEO compensation
Reddy, K. Abidin, S. & You, L. (2015)	New Zealand	CEO compensation	Ownership, board and insider characteristics: Board size Board composition Block shareholding Director shareholding Director compensation	390 company-year observations	GLS regression	The internal corporate governance mechanism influences CEO compensation more than the external mechanism. Board size is associated with higher CEO compensation. There is no relationship between board composition, block shareholding, director shareholding and CEO

						compensation. The presence of the CEO on board is associated with higher CEO compensation. Directors pay is positively related to CEO compensation.
Sun & Cahan, (2012)	US	Compensation committee quality (CCQ)	CEO ownership CEO tenure Institutional shareholdings Growth opportunities Firm size	844 firm-years observations	Fixed-effects regression	CEO ownership does not influence CCQ CEO tenure, Institutional shareholdings, Growth opportunities and Firm size are all associated with lower CCQ.
Tien, C., Chen, C. N., & Chuang, C. M. (2013)	US	CEO pay	CEO power: CEO duality CEO directorship CEO tenure Composite power	More than 400 observations	Cross-sectional Time series regression	There is a significant negative association between CEO duality and CEO total pay. There is no significant association between CEO directorship, CEO tenure, composite power and CEO total pay.

CHAPTER FOUR

THEORETICAL FRAMEWORK AND RESEARCH METHODOLOGY

4.0 Introduction

This chapter presents the methodology adopted in examining the relationship between the predictor variables and the dependent variable in the study. The first part focuses on the research framework. The second part focuses on the development of research hypotheses. The third part is the population and sample of the study. Part four centres on data collection procedures and part five focuses on data cleaning. The sixth part provides the operational definition of the study variables. Part seven discusses the empirical methodology adopted for the study. The model specification is presented in part eight and the last part is the summary of the chapter.

4.1 Research Framework

The diffused nature of shareholders in modern companies has made the separation of ownership and control inevitable (Fama & Jensen, 1983a, 1983b; Jensen & Meckling, 1976). Different mechanisms have been suggested as means of creating harmonious relationship between the shareholders and the professional managers of companies. This serves to avoid the inherent conflict that is associated with such separation because of the misalignment of interests. Among such mechanisms are monitoring and incentives as projected by the agency theory (Jensen & Meckling, 1976). The board is assigned the duty of monitoring the executives to prevent them from exhibiting self-serving behaviour and also negotiating appropriate compensation with them at arm's length so as to align their interests with those of the shareholders

(Boyd, 1994; Connelly *et al.*, 2010; Jensen, 1993; Jensen *et al.*, 2004). Different theories are used to explain means of mitigating this conflict. Among such theories are agency theory (Jensen & Meckling, 1976), stakeholder theory (Freeman, 1984), and stewardship theory (Donaldson & Preston, 1995). The agency theory is used as the underpinning theory to study the relationship between the shareholders and the managers. Under the agency theory, divergence of interest between the shareholders and managers exists because both of them are utility maximizers.

The conjecture of the agency theory is that the board of directors will do adequate monitoring of management activities to prevent managers from exhibiting opportunistic behaviour to the disadvantage of the shareholders (Jensen & Meckling, 1976). Under this theory, the executive compensation is a means of mitigating the agency problem once it is appropriately designed to align the interest of the manager with those of the shareholders (Barkema & Gomez-Mejia, 1998; Fama & Jensen, 1983b). Jensen and Murphy (1990b) argue that executive compensation that is linked to company performance will make the managers work for the enhancement of shareholders wealth. It is argued that executive compensation is the outcome of negotiations between the board of directors (shareholders representatives) and the CEO at arm's length (Hermalin & Weisbach, 1998). This is described as optimal contracting where the interest of the manager is aligned with those of the shareholders thereby making the manager work for the interest of the diffused shareholders.

On the contrary, managerial power theory posits that managers have influence over the determination of their own compensation (Bebchuk & Fried, 2003, 2004). The unarguably excessive compensation received by the CEOs has lent credence to the

managerial power view along with the low pay-performance sensitivity reported in past research (Jensen & Murphy, 1990b). To corroborate this view, Core *et al.* (1999) document that weak corporate governance leads to increased agency problems and higher executive compensation. This could be through entrenchment resulting from long tenure of the CEO, or managerial power where the CEO is the chairman of the board (Core *et al.*, 1999). It is argued that the board that is supposed to monitor the activities of the management often fails to do so because of the board culture that does not allow for antagonism (Brick *et al.*, 2006; Jensen, 1993). Under such circumstance, it is likely such boards will not be able to negotiate executive compensation with the CEO at arm's length on behalf of the shareholders. Connelly *et al.* (2010) argue that company ownership is another mechanism that can be used to monitor and control the behaviour of managers besides the board of directors. However, their diverse nature makes them to have diverse investment objectives (Colpan & Yoshikawa, 2012) that may likely influence their behaviour towards the executive compensation policy of the company.

As illustrated in Figure 4.1, this study investigates the relationship between corporate governance characteristics (board size, board composition, CEO duality, gender diversity, compensation committee, independent compensation committee, CEO ownership, directors' ownership, blockholders' ownership, and MNCs ownership) and executive compensation. Past studies find that executive compensation is explained by company characteristics such as company performance (Sakawa, Moriyama, & Watanabel, 2012), company size (Barontini & Bozzi, 2011), leverage (Van Essen *et al.*, 2015), growth (Colpan & Yoshikawa, 2012), and industry (Reddy

et al., 2015). These company characteristics are therefore included as control variables in this study.

Independent Variables **Dependent Variable**

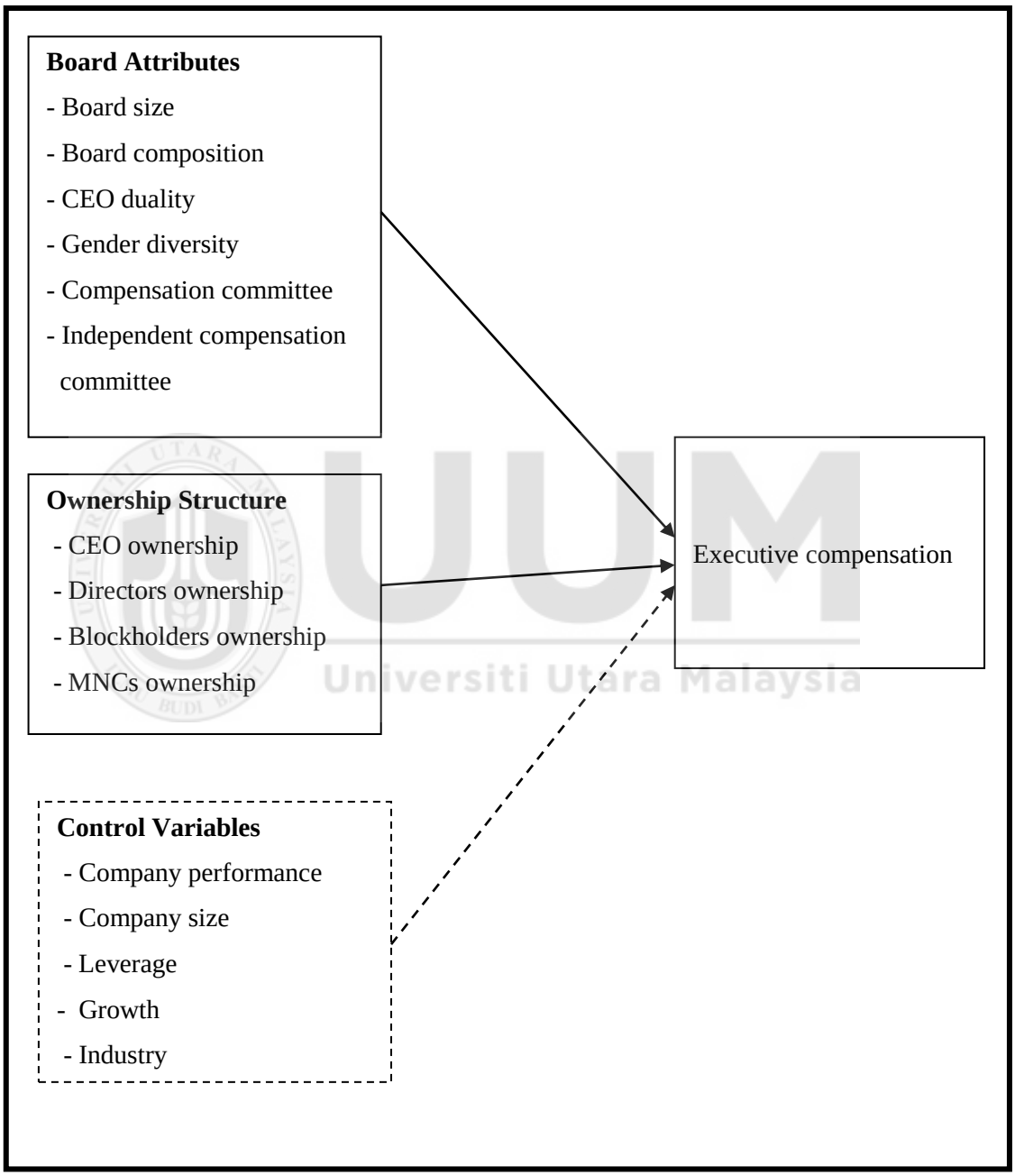

Figure 4.1
Research Framework

4.2 Hypotheses Development

This section presents the argument that supports the development of the study hypotheses. Section 4.2.1 provides the hypotheses about board attributes and executive compensation, while section 4.2.2 concentrates on the hypotheses about ownership structure and executive compensation.

4.2.1 Board Attributes and Executive Compensation

The present study uses six board attributes as part of corporate governance characteristics to examine the relationship between corporate governance characteristics and executive compensation in NLCs. These six board attributes were used to develop six of the ten study hypotheses so as to ascertain their influence on executive compensation. These board attributes are board size (BDS), board composition (BDC), CEO duality (CEOD), gender diversity (GEND), compensation committee (CCOM) and independent compensation committee (CCINDP). Past studies have considered these variables as either independent or control variables that are likely to influence the determination of executive compensation (Adams & Ferreira, 2009; Ben Hassen *et al.*, 2015; Correa & Lel, 2014; Ozdemir & Upneja, 2012; Reddy *et al.*, 2015; Tien *et al.*, 2013). Drawing from relevant theories and past studies, hypotheses development from the above variables are discussed hereunder.

4.2.1.1 Board Size

It is argued that board size influences the extent of power play in companies between the CEO and the board members (Cheng, 2008; Jensen, 1993; Yermack, 1996). Jensen (1993) argues that the board size is a major board attribute that determines the

effectiveness of the board. Several studies provide support for large boards (Abor, 2007; Anderson *et al.*, 2004; Coles *et al.*, 2008; Zahra & Pearce, 1989) as they argue that large boards serve as resource pool for the company to meet its advisory needs and do adequate monitoring of the management. In contrast, Boyd (1994) lends support for small board size as this allows for stronger control of the company. Cheng (2008) argues that CEO becomes powerful and is able to exercise control over the board as the board size increases. He documents that decision making in large boards is laden with compromises that tend to lower variability of firm performance. Elkinawy and Stater (2011) argue that large boards will be associated with higher compensation because of their association with greater agency problems. Yermack (1996) also supports the argument for small board size as he found small boards to be effective monitors in his study of large industrial companies in the US. He further reports that smaller boards are associated with CEO receiving performance incentives as component part of his total compensation. He suggests that increasing board size diminishes the board's ability to set appropriate executive compensation.

Further, Cahan *et al.* (2005) argue that cohesion on large boards will be low just as Jensen (1993) in his criticism of large boards suggests a board size of seven or eight will make for board effectiveness. Past studies show that large boards are likely to have coordination problems and hard to reach consensus (Cahan *et al.*, 2005; Cheng, 2008; Yermack, 1996). It is therefore likely that the difficulty of coordination and reaching consensus in decision making associated with large boards will make the CEO have control over the board, and thus appropriate private benefits in form of excessive executive compensation (Jensen, 1993).

Past empirical studies that investigated the relationship between board size and executive compensation provide evidence that large board is associated with higher executive compensation. For example, Cahan *et al.* (2005), Chalmers *et al.* (2006), and Core *et al.* (1999) report a positive relationship between board size and executive compensation. Reddy *et al.* (2015) provide evidence that when there is increase in number of board members, the CEO will receive higher pay. Van Essen *et al.* (2015) report that when the board size is large, CEOs tend to receive higher total compensation. Consistent with the small board size argument, Correa and Lel (2014) provide additional support when they report that executive compensation is lower when the board size is small.

In Nigeria the CG Code 2011 sets the minimum board size at five (5) without stipulating any maximum. This allows the companies to have boards that are appropriate to their operational needs. Sanda *et al.* (2005) in their study on corporate governance mechanisms and company performance in Nigeria suggests a board size of 10. The equivocal results from prior studies suggest there is no one size fits all approach as there could be advantages and disadvantages for adopting either the large or small board size. Consistent with the prediction of the agency theory and prior studies (Correa & Lel, 2014; Jensen, 1993; Jensen & Meckling, 1976; Van Essen *et al.*, 2015), this study expects that small board size will be effective in monitoring of management as to prevent the CEO from extracting excessive compensation while executive compensation will be higher in large boards. The following hypothesis is therefore developed to test the relationship in this study.

H1: There is a positive relationship between board size and executive compensation.

4.2.1.2 Board Composition

Hillman *et al.* (2000) argue that the insider and outsider classification of board composition as used by previous scholars is sufficient for examining the role of the board under the agency theory. Under the agency theory framework, it predicts that board independence will prevent the managers from exhibiting opportunistic behaviour in form of extracting excessive compensation (Fama, 1980). The proposition of the agency theory is predicated on the assumption that independent boards will be effective monitors of management. The composition of the board is argued determines the power swing between the CEO and other board members. Bebchuk and Fried (2004) in their thought provoking book recommend the independence of the board as a means of diminishing the power of the CEO. A board that is composed of higher number of outsiders is expected to do intense monitoring of the executives, restrain the CEO from extracting higher compensation and add value to the shareholders wealth. Faleye *et al.* (2011) provides empirical support for this argument as they document that intense board monitoring leads to decrease in excess compensation.

The empirical evidence from past studies on the relationship between board composition and executive compensation remains mixed. Incongruous to the outside directors' effective monitoring argument, prior studies have documented a positive relationship between board independence and executive compensation (Core *et al.* 1999; Correa & Lel, 2014; Fernandes, 2008; Ozdemir & Upneja, 2012; Ozkan, 2007). These findings suggest that independent boards are not effective monitors of management and as such cannot adequately represent the interest of the shareholders. For example, Correa and Lel (2014) report that executive compensation is higher

when there is greater board independence. In contrast to the above findings and in support of the agency theory, some other scholars report that independent boards are effective monitors of management (Basu *et al.*, 2007; Chhaochharia & Grinstein, 2009). They report a negative relationship between board independence and executive compensation. Similarly, Firth *et al.* (2007) report that independent boards are inclined to match pay for performance.

Another strand of literature provides empirical evidence of insignificant relationship between board independence and executive compensation (Beiner *et al.*, 2011; Chalmers *et al.*, 2006; Conyon & He, 2011; Conyon & Peck, 1998; Reddy *et al.*, 2015). Beiner *et al.* (2011) in a panel study of Swiss companies report an insignificant relationship between the proportion of outside directors and the fraction of equity-based to cash compensation. Similarly, Chalmers *et al.* (2006) in a panel study of Australian firms find an insignificant relationship between the proportion of outside directors and total compensation. Recently, Guthrie *et al.* (2012) and Mobbs (2013) find that the requirement for outside director dominated boards may not always lead to reduction in excess executive compensation. These findings contrasts the line of reasoning that independent boards will do adequate managerial monitoring, control the CEO and constrain managerial excesses.

In spite of the mixed findings from prior studies, regulators from several countries are demanding for outside director majority boards in the corporate governance codes (Denis & McConnell, 2003) as indicating good corporate governance practice. The CG Code 2011 requires that the board be composed of majority outside directors with at least one independent director. This is an effort at making the board to be free from

the perceived grip of the CEO, and exercise control over his actions. In his study on the relationship between corporate governance and company performance in NLCs, Ehikioya (2009) find no relationship between outside directors and company performance just as Sanda *et al.* (2005) document an insignificant negative relationship between outside directors and company performance in NLCs. The implication is that outside directors are ineffective monitors of management in NLCs. These studies were conducted before the publication of the CG Code 2011 and did not consider the relationship between board independence and executive compensation. Based on the incongruent result from past studies, the above arguments lead to the presentation of the following non-directional hypothesis.

H2: There is a significant relationship between outside director dominated boards and executive compensation.

4.2.1.3 CEO Duality

CEO duality is when both the position of the CEO and the chairman of the board are occupied by an individual. It has been argued under the agency theory framework that separation of the post of the chairman from that of the CEO is a sign of good corporate governance practice (Jensen, 1993). It is also argued that concentrating the dual positions in an individual may make for opportunistic behaviour to the detriment of the shareholders (Jensen & Meckling, 1976). It is argued that combination of the dual roles in an individual will make the CEO powerful and exert influence over the board when negotiating for his pay contract (Van Essen *et al.*, 2015). In examining the relationship between CEO duality and executive compensation, Boyd (1994) argues that a CEO that is also the board chair will be able to evade board control and increase his compensation. Brick *et al.* (2006), Core *et al.* (1999) and Lee (2009)

provide empirical support to show that CEO duality leads to higher executive compensation. In a recent study from China, Chen and Al-Najjar (2012) document that CEO duality will increase CEO's bargaining power. These are consistent with the argument that powerful CEOs will exert influence over the board when bargaining for their compensation (Bebchuk & Fried, 2004).

Sanda *et al.* (2005) argue that the position of the CEO and the chair should be separated in NLCs. In support of Sanda *et al.* (2005) in his examination of corporate governance structure and company performance from Nigeria, Ehikioya (2009) argue for the separation of the CEO and chair positions. He finds CEO duality to have negative effect on company performance. In Nigeria, there are no previous studies on the relationship between CEO duality and executive compensation. The CG Code 2011 requires separation of the board chair from the CEO so as not to concentrate power in an individual. It is therefore argued that CEO duality may allow for managerial entrenchment that allows the CEO to exert influence over the board when determining his compensation contract. To remain consistent with agency theory, regulators and prior studies, this study presumes that CEO duality may likely make the CEO evade board control and extract higher compensation. The following hypothesis is therefore presented.

H3: There is a positive relationship between CEO duality and executive compensation.

4.2.1.4 Gender Diversity

Board gender diversity refers to the presence of women in directorship positions in companies. Under the resource dependency theory, it is argued that a diverse board

will consist of members with various attributes whose presence will enhance the company's performance (Şener *et al.,* 2011). Past studies show that gender diversity seems to significantly influence the quality of board governance (Adams & Ferreira, 2009; Gul *et al.,* 2011), and an effective board is assumed will do effective monitoring of managerial activities. As a proof that women directors could be really resourceful, Norway and Spain have enacted laws that require listed companies in their countries to reserve 40% of board positions for women (Adams & Ferreira, 2009; Gul *et al.*, 2011). Gender diversity can affect the quality of board decisions which in turn can invariably affect the executive compensation policy of the company.

There are previous literature on gender diversity and executive compensation (Elkinawy & Stater, 2011; Lam *et al.,* 2013) whose results have shown that gender should not be overlooked in corporate governance matters. Gul *et al.* (2011) argue under the resource dependence theory that gender diversity in the board would encourage more disclosure by companies. Adams and Ferreira (2009) show that women directors have a significant impact on board inputs and firm outcomes as they are more inclined to link equity-based compensation to stock performance. Their further finding indicates that boards with higher proportion of women do adequate monitoring of the CEO and tend to align more with the interest of the shareholders. Since gender diverse boards do more effective monitoring of managerial activities, it is therefore argued that the CEO may not have influence over such boards as to extract excessive compensation. To remain consistent with the resource dependency theory and prior studies, this study therefore examines the following hypothesis.

H4: There is a negative relationship between women directors and executive compensation.

4.2.1.5 Compensation Committee

The compensation committee is a committee of the board that is responsible for designing, advising on executive compensation matters, and making recommendations to the board (Anderson & Bizjak, 2003; Boivie *et al.*, 2012; Klein, 1998; Sun & Cahan, 2009, 2012). The agency theory predicts that executive compensation optimally contracted will align managers' interests with those of the shareholders (Jensen & Meckling, 1976). It is further argued under the agency theory that the presence of compensation committees in companies indicates good corporate governance practice as they contribute to effective monitoring of managerial behaviour (Allegrini & Greco, 2013). The concept of the compensation committee evolved as a result of the desire to whittle the power of the CEO in the determination of his compensation. However, past research shows that the compensation committee does not influence the level of executive compensation. For example, Chalmers *et al.* (2006) find that compensation committee does not determine executive compensation in Australia. Similarly, Conyon and Peck (1998) document an insignificant relationship between the existence of the compensation committee and executive compensation. It is however interesting to note that Conyon and He (2011) provide evidence of a significant positive relationship between the compensation committee and executive compensation in China suggesting that their presence serves the interest of the CEO.

The corporate governance codes and the listing requirements of various exchanges now require the compensation committee be comprised of independent directors. The effectiveness of this committee in performing this important function has come under question by scholars (Bebchuk & Fried, 2003; 2004; Klein, 1998; O'Reilly & Main, 2007). In fact, some scholars report that the composition of the committee has no effect on executive compensation (Anderson & Bizjak, 2003; Chhaochharia & Grinstein, 2009; Newman & Mozes, 1999; O'Reilly & Main, 2007). Independent compensation committee has been shown not to have any influence in reducing excessive executive compensation. Chhaochharia and Grinstein (2009) find that the requirement for independent compensation committee does not influence the executive compensation policy of companies in the US. They explained further that the board has influence over the composition of the compensation committee and its recommendation is subject to the board's approval. In the UK, the composition of the compensation committee is shown not to have influence on the level of executive compensation (Gregory-Smith, 2012). In contrast to the above findings and in support of the agency theory, Vafeas (2003) shows that inside directors on the compensation committee exhibit self-serving behaviour in the pay setting process. In another study, Laksmana (2008) provides empirical evidence of a positive relationship between independent compensation committee and disclosure of executive compensation.

Nigeria's CG Code 2011 recommends that the compensation committee be comprised of all outside directors. The underlying assumption which is consistent with the agency theory is that non-executive directors are capable of doing proper monitoring of the executives at ensuring managerial accountability. Interestingly, there are

empirical evidences that do not support this proposition. As a result of the mixed findings from previous studies, this study is unable to provide directional hypotheses. The following hypotheses are therefore proffered.

H5: The presence of compensation committee has significant association with executive compensation.

H6: There is a significant relationship between independent compensation committee and executive compensation.

4.2.2 Ownership Structure and Executive Compensation

This study further tests the influence of ownership structure variables as part of a company's corporate governance mechanism on executive compensation. Four additional hypotheses are developed from the four ownership structure variables considered in this study. These variables are CEO ownership (CEOO), directors' ownership (DIRO), blockholder ownership (BLKO), and MNCs ownership (MNCO). This study includes additional ownership variable (MNCO) to examine its influence in the determination of executive compensation. This variable is included because it is argued that the agency conflicts that exist between the MNCs and their foreign subsidiaries should stimulate the MNCs to be involved in the determination of executive compensation of their foreign subsidiaries (Fey & Furu, 2008; Roth & O'Donnell, 1996). The next sub-section discusses the hypotheses development concerning the ownership structure variables.

4.2.2.1 CEO Ownership

CEO ownership in shares is argued to align the CEO's interest with those of the shareholders under the agency theory (Ben Hassen *et al.*, 2015; Core & Guay, 1999; Jensen & Meckling, 1976). In support of this argument, Renneboog and Zhao (2011) suggest that CEO ownership may prevent excessive executive compensation. The convergence of interest or alignment hypothesis holds that as the proportion of shares held by the CEO increases he will be inclined to align his interest with those of the shareholders (Jensen & Meckling, 1976). Previous studies find that when CEOs own shares in their companies it constrains them from extracting private benefit of higher compensation (Core *et al.*, 1999; Hubbard & Palia, 1995; Lin *et al.*, 2013; Shin & Seo, 2011). These findings support the convergence of interest hypothesis.

The contrasting argument is from the entrenchment or rent extraction hypothesis under the managerial power theory that argues against increased shareholding by managers as this will enable them exert undue influence in the determination of their compensation contract. Shleifer and Vishny (1989) argue that entrenched managers have the capability to make decisions that guarantees them higher compensation. Grabke-Rundell and Gomez-Mejia (2002) show that executive stock ownership confers ownership power on the executive, which is used to exert influence when negotiating his compensation contract. Past studies document a positive relationship between CEO ownership and executive compensation, suggesting rent extraction by the CEO (Khan *et al.*, 2005; Li, Moshirian, Nguyen, & Tan, 2007). Consistent with the rent extraction hypothesis, Ben Hassen *et al.* (2015) document that executive compensation increases in relation to increase in managers' shareholding.

Some studies also report an insignificant relationship between CEO ownership and executive compensation (Gregory-Smith, 2012; Ozkan, 2007; Sanders & Carpenters, 1998). Since the extant literature produced equivocal results and the CEO faces conflict of interest, he will be inclined to take actions that will fetch him private benefits. Based on these mixed findings, the following hypothesis is therefore examined.

H7: There is a significant relationship between CEO ownership and executive compensation.

4.2.2.2 Directors Ownership

Agency theory predicts that share ownership by directors will cause them to increase their monitoring duty over the activities of management (Beatty & Zajac, 1990; Jensen & Meckling, 1976). This is consistent with the alignment of interest hypothesis. Since the directors are responsible for the design of executive compensation policy, their shareholdings provide them with incentives to inhibit the manager from extracting excessive compensation. Yakasai (2001) argues that substantial shareholdings by directors will make them align their interests with those of the shareholders as poor company performance will hurt them personally. Bhagat and Bolton (2008) argue that shareholding by directors will incentivise them to do adequate monitoring of the management. However, under the entrenchment or expropriation hypothesis, the directors may be inclined to align with the interest of the managers to jointly expropriate the minority shareholders.

Prior executive compensation studies suggest that there is an association between directors' ownership and executive compensation (Boyd, 1994; Cheng & Firth, 2005;

Firth *et al.*, 1999; Ozkan, 2007) even though the results remain incongruous. Boyd (1994) reports that directors' ownership increases board control over executive compensation. Firth *et al.* (1999) find that directors' ownership has moderating effect on the pay-performance relationship in Hong Kong. On the contrary, Ozkan (2007) documents a positive relationship between director ownership and executive compensation, while Core *et al.* (1999) report that outside directors' ownership does not have any relationship with executive compensation. Similarly, Lee (2009) finds no significant relationship between directors' shareholding and executive compensation.

Previous studies from Nigeria centre on the relationship between directors shareholding and company performance (Ehikioya, 2009; Sanda *et al.*, 2005). Sanda *et al.* (2005) find a significant negative relationship between directors' shareholding and company performance in NLCs. On the other hand, Ehikioya (2009) found no significant relationship between directors' shareholding and company performance in NLCs. This could be an indication that the directors are captives of the CEO. These earlier studies on Nigeria did not consider the extent of the relationship that exists between directors' ownership and executive compensation. Resulting from the mixed findings from past studies that are consistent with the conflicting theories, directors could therefore use their shareholdings to either constrain the CEO from extracting higher compensation or award him with higher compensation. This leads to the development of the following hypothesis.

H8: There is a significant relationship between directors' ownership and executive compensation.

4.2.2.3 Blockholders Ownership

Blockholders ownership is argued substitutes for board monitoring in a weak corporate governance environment and helps mitigate agency conflicts, and their presence has been shown to be associated with lower executive compensation (Becker, Cronqvist, & Fahlenbrach, 2011; Cheng & Firth, 2005; Chhaochharia, Kumar, & Niessen-Ruenzi, 2012; Core *et al.*, 1999; David *et al.*, 1998; Firth *et al.*, 2007; Khan *et al.*, 2005; Ozkan, 2007). These findings imply that block shareholders are good monitors of managerial activities and are consistent with the efficient monitoring hypothesis. Another strand of literature however shows that block shareholders have incentives to expropriate the minority shareholders (La Porta *et al.*, 1999; Lemmon & Lins, 2003), suggesting that agency conflicts exist between block shareholders and the minority shareholders that is addressed as the principal-principal problem (Allegrini & Greco, 2013; Young, Peng, Ahlstrom, Bruton, & Jiang, 2008). Contrary to the efficient monitoring hypothesis, Goldman and Strobl (2013) in their examination of how the presence of a large institutional shareholder affects the complexity of corporate investments provide evidence of large shareholders exhibiting opportunistic behaviour.

The heterogeneous nature of blockholders makes their interests to diverge one from another (David *et al.*, 1998). The resultant effect is that they may not all be interested in doing adequate monitoring of managerial actions because of their divergent interests. While the pressure sensitive blockholders may align with the CEO when designing his compensation contract, the pressure resistant blockholders may likely constrain him from extracting excessive compensation. Further, short term blockholders may not be inclined to take interest in executive compensation matters

as they have alienable rights to their shares. On the other hand, long term blockholders may engage in proper monitoring of executives to safeguard their long term investment goals. Consistent with the above argument, Khan *et al.* (2005) report that dispersion in institutional ownership is positively related with executive compensation. This is consistent with the argument of Li *et al.* (2007) that the identity of large shareholders may affect their behaviour towards company performance and executive compensation. Recently, Shin and Seo (2011) report that the presence of pressure resistant institutional investors leads to higher executive compensation. However, when they are separated into mutual fund ownership and public pension fund ownership the result indicates that they have opposite significant effect of executive compensation.

In contrast, other studies report a positive relationship between blockholder ownership and executive compensation (David *et al.*, 1998; Shin & Seo, 2011). The positive relationship is in congruence with the report by Lemmon and Lins (2003) and La Porta *et al.* (1999) that block shareholders have incentives to expropriate the minority shareholders. Another strand of literature found insignificant relationship between blockholders ownership and executive compensation (Chalmers *et al.*, 2006; Lee, 2009). For example, Chalmers *et al.* (2006) find that block shareholders are not determinants of executive compensation as they report an insignificant relationship between the variables. Consistent with Chalmers *et al.* (2006), Lee (2009) shows that ownership concentration is not a strong determinant of performance-pay component of executive compensation in Australia and Singapore. Since block shareholders could either align with the shareholders or expropriate the minority shareholders, this study provides the following non-directional hypothesis.

H9: There is a significant relationship between blockholders ownership and executive compensation.

4.2.2.4 Multinational Companies Ownership

It has been argued that there exists the transfer of knowledge in multinational companies (Harzing, Pudelko, & Reiche, 2015; Michailova & Mustaffa, 2012). Since MNCs involve in knowledge transfer between the headquarters and their foreign subsidiaries, there is the likelihood that they may be involved in the executive compensation design of those subsidiaries (Fey & Furu, 2008; Kostova & Roth, 2002) as part of their control efforts (Gatignon & Anderson, 1988). It is also argued that companies that are subsidiaries of MNCs are inclined to match pay for performance (Brunello *et al.*, 2001) as they would want reduced agency costs. It is also likely that MNCs appoint CEOs for their foreign subsidiaries, since these subsidiaries rely on the headquarters for resources and administrative guide (Rosenzweig & Singh, 1991) and also for knowledge sharing (Fey & Furu, 2008).

Sanda *et al.* (2011) provide evidence that foreign CEOs show better company financial performance than their domestic counterparts that is likely to make them earn more than their domestic counterparts. Roth and O'Donnell (1996) argue that there is agency relationship between the MNC and her foreign subsidiaries. The agency theory predicts matching of pay with performance as a means of mitigating the agency problem. This study therefore expects that MNCs are more likely to constrain the CEO from extracting higher compensation. The following hypothesis is therefore presented.

H10: There is a negative relationship between MNCs ownership and executive compensation.

4.3 Population and Sample of the Study

The sample population consists of all the companies listed on the NSE. The NSE has a total of 198 listed companies as at December 31, 2013. This information was obtained from the official website of the NSE. Since it will not be possible to examine all the companies, a representation of the population is selected. To maintain balanced panel dataset, purposive sampling technique is used to select the sample companies for the study period (2009 - 2013). The initial sample consists of 112 companies with a total of 408 company-year observations after excluding the Insurance companies. After excluding companies that failed to disclose the highest paid director, the sample was reduced to 75 companies with 327 company-year observations.

Additional screening was done that eliminated companies without annual report for any of the 5-year study period. The final sample consists of 43 companies with 215 company-year observations that constitute a balanced panel dataset. The DCOMs constitute 132 company-year observations while the MNCs comprise of 83 company-year observations. The sample comprises 8 different sectors that include consumer goods, services, conglomerates, industrial goods, oil and gas, construction and real estate, financial services, and agriculture. The detail of this is provided in section 5.1. The five year period is considered since it provides enough data unlike cross-section studies. The period of study (2009 – 2013) coincides to two years before and two years after the publication of the CG Code 2011. It is therefore considered

appropriate for this study as it enables the pre and post study of the effectiveness of the new code as it affects executive compensation.

Table 4.1
Sample Selection Procedure

Sample Characteristics	**Number of companies**	**Number of company-year observations**
Total companies listed on the NSE as at December 31 2013	198	
Companies whose annual reports could not be accessed and the Insurance companies	86	
Initial sample	112	408
Companies without highest paid director disclosure	37	81
Companies with highest paid director disclosure	75	327
Companies with incomplete 5 year annual report	32	112
Final sample	43	215

For robustness checks, the sample is further organized into four subgroups on the basis of whether they are subsidiaries of foreign MNCs or DCOMs, and based on their position before and after the introduction of the CG Code 2011. A company is categorized as a subsidiary of a MNC if a company with headquarters in a foreign country is a substantial shareholder that holds a controlling interest, otherwise it is regarded as a domestic company. Examples of such MNCs include Unilever Nigeria Plc, Guinness Nigeria Plc, and Cadbury Nigeria Plc. The next stage is the sorting of the companies into before (2009 - 2011) (PreCG) and after (2012 - 2013) (PostCG) the introduction of the CG Code 2011.

4.4 Data Collection Procedures

The researcher hand collected the data for all variables from the annual reports of the companies that constitute the sample size since there are no database service providers in the country that have the required data for this type of study. Previously, Nigerian researchers have used the annual report as source of extracting financial and corporate governance information for their studies (Adegbite, 2012; Adelopo, 2011; Sanda *et al.*, 2005). The annual reports were accessed from the NSE Library, financial websites such as resourcedat.com, africanfinancials.com, investinafrica.com, and company websites. The annual reports span the period from 2009 to 2013.

The following criteria have to be met by a company to qualify for inclusion in the final sample size. First, it must not be an insurance company because of the peculiarity of insurance operations. Past research shows that companies that are subject to extra regulations may influence the level of executive compensation (Firth *et al.*, 2007). Second, the five year annual report from 2009 to 2013 must be available with relevant information (Ehikioya, 2009; Reddy *et al.*, 2015). Third, the highest paid director must be disclosed in the annual report (Conyon & He, 2011; Firth *et al.*, 2007). Fourth, similar to Conyon and He (2011) and Reddy *et al.* (2015) all the corporate governance characteristics and control variables must be disclosed in the annual report by the company to avoid the issue of missing data. The above criteria helped to obtain a balanced panel dataset for the study analysis.

The process involves conducting search of each annual report during the study period to ascertain if there is disclosure of the highest paid director. It is after establishing the availability of this variable that search for other variables were conducted. In any

year that highest paid director is not disclosed, the examination of the immediately following year is made to check if the highest paid director of the preceding year is disclosed. Where this is established such company-year is included in the sample. The unit of analysis is the Nigerian Listed Companies.

4.5 Data Cleaning for Multiple Linear Regression Analysis

STATA 12 statistical package was used for the statistical analysis of the panel data set. Descriptive analysis was carried out to provide the mean, median, standard deviation, minimum, and maximum for all the variables of study. For parametric tests to be conducted in statistics, certain assumptions need to be satisfied as inability to satisfy these assumptions could lead to biased results (Hair, Black, Babin, & Anderson, 2010). These assumptions are now discussed in turn for the purpose of the regression analysis.

4.5.1 Normality

This is the assumption that the error term is distributed normally with zero mean and constant variance (Gujarati & Porter, 2009), as failure of this assumption could lead to flawed analysis (Tabachnick & Fidell, 2007). Ordinarily, the skewness and kurtosis statistics show that the data are not normally distributed. However, with large samples of 200 or more cases the skewness and kurtosis do not have significant effect on the analysis (Tabachnick & Fidell, 2007). The literature suggests that normality will not pose any problem when the sample size is up to two hundred or more (Hair *et al.*, 2010). For this reason, normality is not an issue in this study as the sample

consists of two hundred and fifteen observations. Further, the histogram of residuals in Figure 4.2 shows that data is normally distributed.

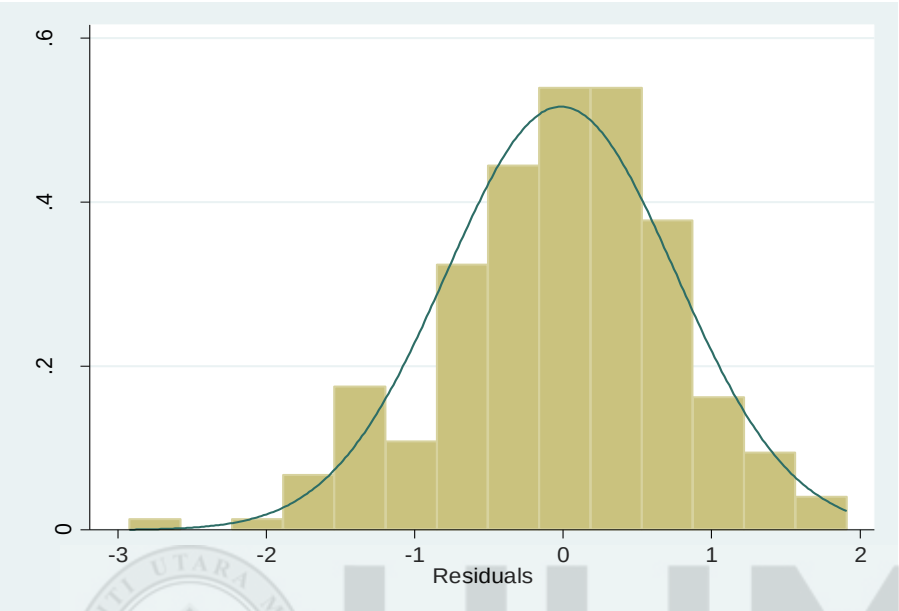

Figure 4.2
Histogram of Residuals

4.5.2 Linearity

This is the assumption that there is a linear relationship between the study variables. A linear relationship is said to exist when the variation in the dependent variable remains constant at different values of the independent variable (Hair *et al.*, 2010). If the relationship is non-linear the assumption of linearity will not be able establish any relationship. Since quadratic polynomial is appropriate for examining a curvilinear relationship between dependent and independent variables (Hair *et al.*, 2010), additional analysis was conducted by including the squared term of MNCs ownership. This enables an examination of whether there is a curvilinear relationship between it and executive compensation. Further, if standard deviation of the dependent variable is greater than the standard deviation of the residual then linearity is not likely to pose

any problem (Hair *et al.*, 2010). Table 4.2 shows that the standard deviation of LnCOMP is in the same range with the standard deviation of the residuals. Therefore linearity is not expected to be a problem in this study.

Table 4.2
Standard Deviation of the Dependent Variable and the Residuals

	Standard Deviation
LnCOMP	1.056
Residuals	1.061

4.5.3 Multicollinearity

This is the condition when there is high intercorrelation between two or more variables (Rencher, 2002). In situations that there is multicollinearity, it becomes difficult to identify the effect of the highly correlated independent variables separately on the dependent variable (Hair *et al.*, 2010). High multicollinearity between independent variables will give a flawed result of the relationship between the independent variables and the dependent variable. The two methods that are generally used for detecting the presence of multicollinearity are the correlation matrix and the variance inflation factor (Gujarati & Porter, 2009; Hair *et al.*, 2010; Tabachnick & Fidell, 2007). A correlation coefficient of 0.80 is assumed to be high and shows that there is the problem of multicollinearity (Gujarati & Porter, 2009). However, Tabachnick and Fidell (2007) suggest a coefficient of 0.90 to be evidence of high correlation. Variance inflation factor that has a value greater than 10 is considered as signal for the presence of multicollinearity (Hair *et al.*, 2010).

4.5.4 Homoscedasticity

The variance of the error term for all the independent variables is assumed to be constant for all values of the dependent variable (Gujarati & Porter, 2009). In situations that there are variations in the variance of the error term for the independent variables, there is said to be heteroscedasticity. The presence of heteroscedasticity in OLS regression produces a biased estimator of variance. This renders the t and F tests invalid. For panel data, the xttest3 command is used to conduct the Modified Wald test for groupwise heteroscedasticity in fixed effect regression model in STATA. A *p*-value < 0.05 rejects the null hypothesis of homoscedasticity (i.e. the homogeneity of the variance of the residuals) and concludes the presence of heterocedasticity. A *p*-value > 0.05 fails to reject the null hypothesis and concludes the presence of homoscedasticity. When the variables are not uniformly skewed, it may result to heteroscedasticity. The data for this study are not uniformly skewed and as such there is likelihood of the presence of heteroscedasticity. When the presence of heteroscedasticity is established, the robust option in STATA is used to correct the standard errors which in turn affect the t-statistics and the *p*-value. It is also suggested that heteroscedasticity can be corrected by transforming the dependent variable (Hair *et al.*, 2010; Tabachnick & Fidell, 2007). Consistent with this suggestion and past studies this study transformed the dependent variable of study.

4.5.5 Serial Correlation or Autocorrelation

Another assumption is that there is no serial correlation or autocorrelation between the error terms. The premise of this assumption is that the disturbance term relating to one observation is independent of the other whether for time unit or cross sectional

unit. The estimates of the error variance will be too small when the autocorrelation is positive and will be too large when the autocorrelation is negative (Tabachnick & Fidell, 2007). The resultant effect is the overstating of the Type 1 error rate and loss of power respectively. The presence of autocorrelation makes the OLS estimators to become biased and inefficient and so may no longer be best linear unbiased estimator (BLUE) (Gujarati & Porter, 2009). The xtserial command is used to conduct the Wooldridge test for autocorrelation in panel dataset in STATA. A *p*-value < 0.05 indicates the presence of autocorrelation in the panel dataset and reject the null hypothesis of no first-order autocorrelation in panel data. A *p*-value > 0.05 fails to reject the null hypothesis and concludes that there is no first-order autocorrelation in the dataset. The robust option in STATA is used for correcting the presence of serial correlation. However, this study does not have the problem of serial correlation.

4.5.6 Outliers

Outlier is a data point that is at extreme compared to other data points (Hair *et al.*, 2010). The presence of influential outliers in the dataset will produce erroneous statistical results. Like other assumptions, outliers can be detected through the use of statistical and graphical methods. Several tests were conducted to test for outliers before deciding on whether to remove or retain any outliers. For this study, mean leverage is 0.065 with a minimum of 0.018 and maximum of 0.892. Cook's D has a minimum of 0.000 and maximum 0.233 with 0.006 as average. Studentized residual average is -0.005 ranging from -3.710 to 2.488. Tabachnick and Fidell (2007) suggest that when standardized score for any case is greater than 3.29 or less than -3.29 is an indication it could be an outlier. Examination of the studentized residual shows a case that has a value of -3.71. When this case was excluded from the regression the result

remained qualitatively similar. This case was therefore retained so as not to limit the generalizability of the results.

4.6 Operational Definition and Measurement of Variables

4.6.1 Dependent Variable

The dependent variable for this study is executive compensation. This is the pay incentive reward to the manager for his managerial effort at managing the activities of the company. For this study, the measure of executive compensation is the highest paid director. This is the extent of disclosure made by the companies in the annual reports. There is no information regarding the equity-based component of executive compensation, if any, in the annual reports. This is consistent with the finding of Odewale and Kamardin (2015a) that listed companies in Nigeria do not disclose the long-term incentives plan and share options to the CEO in the annual reports. Highest paid director has been used in previous studies as proxy for CEO compensation (Cheng & Firth, 2005; Conyon & Peck, 1998; Conyon & Leech, 1994; Firth *et al.*, 2007; Girma *et al.*, 2006). Consistent with previous studies that used the natural logarithm of executive compensation (Conyon & He, 2011; Graham *et al.*, 2012; Gregory-Smith, 2012), this study adopts the natural logarithm of the highest paid director.

4.6.2 Independent Variables

4.6.2.1 Board Size

The board of directors consists of both inside and outside directors. Board size is commonly used to determine the monitoring effectiveness of the board as to whether

the CEO will be able to exert influence over it or otherwise (Jensen, 1993). The recommendation of the CG Code 2011 is a minimum board size of five directors while the maximum is to depend on the complexity of the company's operations. Consistent with past studies, this study measures board size as the total number of directors on the board (Chalmers *et al.*, 2006; Coles *et al.*, 2008; Correa & Lel, 2014; Kamardin & Haron, 2011; Ozdemir & Upneja, 2012; Reddy *et al.*, 2015; Yermack, 1996).

4.6.2.2 Board Composition

The CG Code 2011 recommends that the board should comprise of majority non-executive directors with at least one independent director. Board composition or independence is a measure of the extent of managerial power that CEO has over the board (Hillman *et al.*, 2000; Hossain *et al.*, 2001; Jensen, 1993). Agency theory posits that independent board will be able to do adequate monitoring of the CEO and constrain him from extracting rent for his private benefits (Fama, 1980). In this study, board composition is measured as the proportion of outside directors to the total number of directors as used by prior studies (Chalmers *et al.*, 2006; Chhaochharia & Grinstein, 2009; Correa & Lel, 2014; Ozdemir & Upneja, 2012; Reddy *et al.*, 2015; Sakawa *et al.*, 2012).

4.6.2.3 CEO Duality

CEO duality is a measure of managerial power. CEO duality is when both the position of the CEO and the chairman of the board is occupied by an individual (Chalmers *et al.*, 2006; Core *et al.*, 1999; Ozdemir & Upneja, 2012; Shin, 2013; Tien

et al., 2013). The CG Code 2011 recommends that separate individuals be appointed to the positions of the board's chairman and CEO so as to avoid power concentration in an individual. Consistent with past studies, CEO duality is measured by dichotomous variable, when the CEO is also the chairman of the board '1' and '0' otherwise (Conyon & He, 2011; Correa & Lel, 2014; Lee, 2009; Ozdemir & Upneja, 2012; Tien *et al.*, 2013).

4.6.2.4 Gender Diversity

Prior studies provide evidence that the presence of women on boards increases board quality and enhances board monitoring (Adams & Ferreira, 2009; Gul *et al.*, 2011). To remain consistent with prior studies, this study measures gender diversity as the proportion of women to total number of directors on board (Campbell & Mínguez-Vera, 2008; Gul *et al.*, 2011; Singh *et al.*, 2008).

4.6.2.5 Compensation Committee

Compensation committee is a committee of the board that is saddled with the responsibility for designing the compensation of the executive directors (Conyon & He, 2011; Klein, 1998). The compensation committee is considered as the most significant committee of the board that may serve to constrain the CEO from extracting higher compensation. The CG Code 2011 recommends the establishment of a wholly non-executive directors' compensation committee. Consistent with measures used by past studies, this study assigns '1' for the presence of a compensation committee and '0' otherwise (Chalmers *et al.*, 2006; Conyon & He, 2011; Conyon & Peck, 1998). Additional measure is also used, the compensation committee that has more outside directors in its membership is regarded as an

independent compensation committee and is assigned the value of '1', and '0' if inside directors are dominant members.

4.6.2.6 CEO Ownership

CEO ownership is used to determine whether the CEO will align his interest with those of the shareholders or otherwise. Following past studies, this study measures CEO ownership as the percentage shareholding by the CEO to the total number of shares outstanding (Ben Hassen *et al.*, 2015; Chalmers *et al.*, 2006; Conyon & He, 2011; Lin *et al.*, 2013; Shin & Seo, 2011).

4.6.2.7 Directors Ownership

Directors' ownership represents the shareholdings by the directors. To remain consistent with past studies, the measure of this variable is the proportion of directors' shareholdings to the total number of company shares (Bhagat & Bolton, 2008; Ehikioya, 2009; Firth *et al.*, 1999; Ozkan, 2007; Reddy *et al.*, 2015; Sanda *et al.*, 2005).

4.6.2.8 Blockholders Ownership

Blockholders ownership is a measure of the level of ownership concentration in companies. Blockholders could either use their power to protect or expropriate the minority shareholders (Firth *et al.*, 2007; Lemmon & Lins, 2003; Ozkan, 2007; Shin & Seo, 2011). For this study, blockholders ownership is measured as the total shareholding by shareholders that own minimum shares of 5% in the company (Derrien *et al.*, 2013; Kim, 2010; Mitton, 2002; Odewale & Kamardin, 2015a).

4.6.2.9 Multinational Companies Ownership

A multinational company is one that is a member of a group of companies with headquarters in a foreign country (Hannon *et al.*, 1995; Rosenzweig & Singh, 1991). This is the first study to examine the influence of MNCs ownership on executive compensation of their foreign subsidiaries as such there is no past empirical work to follow for measurement purpose. However, similar to the measure of other ownership variables, MNCs ownership is measured as the proportion of shares held by the MNC in its foreign subsidiary. Consistent with Brunello *et al.* (2001) and Le *et al.* (2013), to distinguish between MNCs and DCOMs a dummy variable is assigned a value of '1' if it is a multinational company and '0' if it is a domestic company.

4.6.3 Control Variables

This sub-section presents the operational definition of the control variables used in this study. This includes company performance, company size, leverage, sales growth, and industry. These are now discussed in turns.

4.6.3.1 Company Performance

Even though performance has been shown to account for about 5% of variation in executive compensation (Tosi *et al.*, 2000), it is still included as a control variable because of its extensive use in previous studies (Andjelkovic *et al.*, 2002; Barkema & Gomez-Mejia, 1998; Brick *et al.*, 2006; Buck, 2008; Chalmers *et al.*, 2006; Firth *et al.*, 2006; Girma *et al.*, 2006; Gomez-Mejia & Wiseman, 1997; Kato *et al.*, 2007; Sakawa *et al.*, 2012; Zhou, 2000).

Table 4.3
Measurement of Variables

Variables	Acronyms	Operational Definition	Source of Information
Dependent Variable			
Executive Compensation	LnCOMP	Log of highest paid director	Annual report
Independent Variables			
Board Size	BDS	The total number of directors on the board.	Annual report
Board Composition	BDC	The proportion of outside directors to the total number of directors.	Annual report
CEO Duality	CEOD	A dichotomous variable that takes the value of '1' if the CEO is the chairman of the board and '0' otherwise.	Annual report
Compensation Committee	CCOM	A dichotomous variable that is assigned '1' for the presence of a compensation committee and '0' otherwise.	Annual report
Independent Compensation Committee	CCINDP	Independent compensation committee is assigned the value of '1', and '0' if inside directors are dominant members.	Annual report
Gender Diversity	GEND	Gender diversity is the proportion of women to total number of directors on board.	Annual report
CEO Ownership	CEOO	CEO ownership as the percentage shareholding by the CEO to the total number of shares outstanding.	Annual report
Directors Ownership	DIRO	The proportion of directors' shareholdings to the total number of company shares.	Annual report
Blockholders Ownership	BLKO	The total shareholding by shareholders that own minimum shares of 5% in the company.	Annual report
MNCs Ownership	MNCO	The proportion of shares held by the MNC in its foreign subsidiary. The second measure is a dichotomous variable that takes the value of '1' if it is a MNC and '0' otherwise.	Annual report
Control Variables			
Company Performance	ROA	This is earnings before interests and taxes deflated by the total assets.	Annual report
Company Size	SIZE	Log total assets	Annual report
Leverage	LEV	The total liabilities deflated by total assets.	Annual report
Growth	GRT	The proportional increase in total sales of one year over the preceding year.	Annual report
Industry	IND	A dichotomous variable that takes the value of '1' if the company is from the financial sector and '0' for non-financial companies.	

Return on Assets (ROA) is the proxy for company performance used for this study. ROA is measured as earnings before interests and taxes deflated by the total assets as used by prior researchers (Barontini & Bozzi, 2011; Conyon & He, 2012; Firth *et al.*, 2007; Luo & Jackson, 2012; Sakawa *et al.*, 2012). ROA is an accounting-based measure of firm performance for evaluating manager's ability at managing company assets (Odewale & Kamardin, 2015b) with its attendant limitations (Krivogorsky, 2006). Krivogorsky (2006) points that; it is affected by accounting conventions for recognising revenue and assets valuation.

4.6.3.2 Company Size

Logarithm of total assets as a size variable is included to control for size effect on executive compensation as firm size has been reported to account for about 40% of the variation in executive compensation (Tosi *et al.*, 2000). This measure is used in order to remain consistent with prior studies (Barontini & Bozzi, 2011; Beiner *et al.*, 2011; Chalmers *et al.*, 2006; Hazarika, Karpoff, & Nahata, 2012; Shin, 2013).

4.6.3.3 Leverage

Prior study suggests that debt holders have the incentives to do proper monitoring of managerial actions to constrain them from extracting higher executive compensation (Munisi & Mersland, 2013). In this study, leverage is measured as the total liabilities deflated by total assets similar to past studies (Albuquerque *et al.*, 2013; Beiner *et al.*, 2011; Barako, Hancock, & Izan, 2006; Brown & Lee, 2010; Munisi & Mersland, 2013; Van Essen *et al.*, 2015).

4.6.3.4 Growth

Core *et al.* (1999) identified growth opportunities as one of the determinants of executive compensation. Growth has been conjectured as a strategy used by executives to grow their pay (Girma *et al.*, 2006). In this study, growth is measured as the proportional increase in total sales of one year over the preceding year as used by Colpan and Yoshikawa (2012), Hazarika *et al.* (2012) and Tien *et al.* (2013).

4.6.3.5 Industry

Past studies provide evidence that the industry to which a company belongs has influence on its executive compensation practice (Reddy *et al.*, 2015; Yermack, 1995). The financial sector companies (banks) operate in a regulated environment whose operations are very much different from those companies in the non-financial sector (Firth *et al.*, 2007). For this study, industry is measured as a dichotomous variable that takes the value of '1' if the company is from the financial services sector and '0' for non-financial companies.

4.7 Empirical Methodology

The explanation on the empirical methodology employed for data analysis as used in this study is presented in this section. Panel data methodology is adopted for this study and the sample consists of a balanced panel dataset. Panel data has several advantages over cross-sections or time-series data. An important characteristic of panel data is that it can be used to improve empirical analysis in such a way that cross-section or time-series data cannot do (Gujarati & Porter, 2009). When there are

correlated omitted effects, panel data helps to get consistent estimates of the parameters of interest which is not possible with OLS on individuals' cross sections (Johnston & DiNardo, 1997). Baltagi (2005) lists the benefits of using panel data to include the following: control for individual unobserved heterogeneity, more informative data, more variability, less collinearity among the variables, more degrees of freedom and more efficiency, more suitable to examine dynamic relationships, identification and measurement of effects that cannot be easily detected in pure cross-section or pure time-series data, and enables the study of more complicated behavioural models.

In panel data methodology, the researcher is faced with what choice to make from pooled OLS regression, fixed-effects and random-effects models. The appropriateness of both fixed and random effects models eliminates the option of pooled OLS regression. Hausman test is conducted to determine whether fixed or random effect is more appropriate. Regardless of the conduct of Hausman's test to decide on the appropriateness of fixed or random effects model, Johnston and DiNardo (1997, p. 403) state "...there is no simple rule to help the researcher navigate past the Scylla of fixed effects and the Charybdis of measurement error and dynamic selection. Although they are an improvement over cross-section data, panel data do not provide a cure-all for all of an economctrician's problems."

Following Palia (2001), firm-effects test was conducted that confirmed the existence of firm effects. The time effects test shows no need for time effects. The Breusch Pagan Lagrange Multiplier test confirmed the suitability of the random-effects model. Consistent with Palia (2001) and Conyon and He (2011), the Hausman specification

test was conducted to determine whether the fixed-effects or random-effects estimation is more appropriate. The Hausman test rejects the null hypothesis, thus confirming the appropriateness of the fixed-effects model.

Fixed-effects panel data methodology is therefore used in this study. Fixed-effects panel data methodology is employed to control for unobservable heterogeneity among companies (Conyon & He, 2011; Palia, 2001; Wooldridge, 2002). Conyon and He (2011) argue that there will be misspecification error that will lead to omitted variable bias if there is correlation between firm heterogeneity and the observable variables. This omitted variable bias problem can be addressed with the use of fixed-effects model if the omitted variables are time-invariant (Graham *et al.*, 2012). A fixed effects methodology allows the unobservable heterogeneity (company characteristics) that is time-invariant to be randomly correlated with the explanatory variables (Greene, 2008; Wooldridge, 2002). Recently, Conyon (2014) and Graham *et al.* (2012) show that executive compensation is strongly influenced by company fixed-effects.

In spite of the attendant challenges associated with fixed-effects, the fixed-effects estimators still remain consistent even when it is assumed that the pooled or random-effects model is valid (Gujarati & Porter, 2009; Johnston & DiNardo, 1997). Further, Johnston and DiNardo (1997, p. 397) states that "With fixed effects estimators, we cannot generally recover estimates of any time-invariant explanatory variables. The fixed effects estimator is robust to the omission of any relevant time-invariant regressors." This study therefore adopts the fixed effects approach and it is supported by the Hausman specification test.

4.8 Model Specification

This section presents the model used to test the study hypotheses. The study variables discussed earlier are used to build the model and the empirical examination of the model is conducted in chapter five. The regression model is shown below.

$$LnCOMP_{it} = \alpha + \beta_1 BDS_{it} + \beta_2 BDC_{it} + \beta_3 CEOD_{it} + \beta_4 GEND_{it} + \beta_5 CCOM_{it} + + \beta_6 CCINDP_{it} + \beta_7 CEOO_{it} + \beta_8 DIRO_{it} + \beta_9 BLKO_{it} + \beta_{10} MNCO_{it} + \beta_{11} ROA_{it} + \beta_{12} SIZE_{it} + \beta_{13} LEV_{it} + \beta_{14} GRT_{it} + \beta_{15} IND_{it} + \varepsilon_{it}$$

Where:

LnCOMP	- Logarithm of highest paid director
BDS	- Board size
BDC	- Board composition
CEOD	- CEO duality
GEND	- Gender diversity
CCOM	- Compensation committee
CCINDP	- Independent compensation committee
CEOO	- CEO ownership
DIRO	- Directors' ownership
BLKO	- Blockholders ownership
MNCO	- Multinational companies ownership
ROA	- Return on assets
SIZE	- Company size (Logarithm of total assets)
LEV	- Leverage
GRT	- Growth
IND	- Financial sector
ε	- Error term
i, t	- i is companies 1 – N; t is for years 1 - t

4.9 Summary of the Chapter

This chapter has presented the methodology adopted for this study. The research framework is first presented, followed by the development of ten hypotheses. This is followed by the description of the population and sample of the study. Next is the data collection and data cleaning methods. Operational definition and measurement of variables is then discussed. This study consists of one dependent variable, ten independent variables, and five control variables. Empirical methodology and model specification are then discussed. Following the procedures laid out in this chapter, the next chapter provides the analysis of data and discussion of results.

CHAPTER FIVE

DATA ANALYSIS AND DISCUSSION

5.0 Introduction

This chapter presents the results of data analysis for this study. Sections 5.1 to 5.3 presents the descriptive statistics and univariate analysis of the variables used in the regression model. Correlation analysis and variance inflation factors are contained in section 5.4. Section 5.5 discusses the results of the multivariate analysis. The result of the robustness checks is presented in section 5.6. Finally, section 5.7 discusses the summary of the chapter.

5.1 Sector Distribution of Sample of the Study

Table 5.1 reports the sector distribution of the sample observation. The study covers eight sectors of the NSE over a 5 year period from 2009 to 2013 that consists of consumer goods, services, conglomerates, industrial goods, oil and gas, construction and real estate, financial services, and agriculture. The consumer goods sector provides the highest number of observations that constitute 25.58% of the study sample followed by the services sector that had 20.93%. Financial services sector comprising 35 observations constitute 16.28% of the sample size while industrial goods, and oil and gas constitute 11.63% each. The result shows that 6.98% of the sample companies are from the conglomerates sector while construction and real estate contributed 4.65% to the study sample. Finally, the agricultural sector constitutes the last 2.32% of the sample.

Table 5.1
Sample of Companies according to Sectors

S/No.	Sectors	No. of companies	No. of observations	Percentage of observations
1.	Consumer goods	11	55	25.58
2.	Services	9	45	20.93
3.	Conglomerates	3	15	6.98
4.	Industrial goods	5	25	11.63
5.	Oil and gas	5	25	11.63
6.	Construction and Real Estate	2	10	4.65
7.	Financial services	7	35	16.28
8.	Agriculture	1	5	2.32
	Total	43	215	100.00

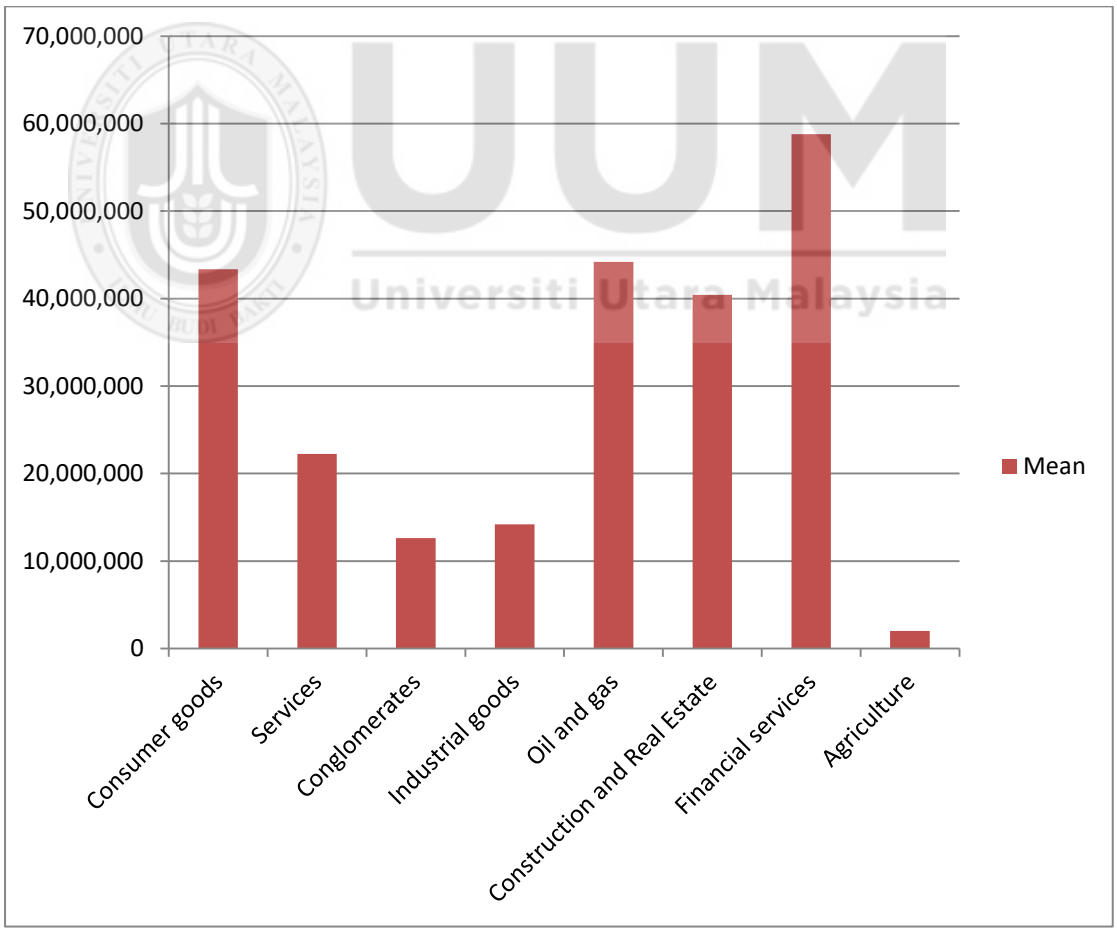

Figure 5.1
Mean of Executive Compensation according to Sectors

Table 5.2
Mean of Executive Compensation according to Sectors

S/No.	*Sectors*	*No. of observations*	*Mean*
1.	Consumer goods	55	43,342,320
2.	Services	45	22,257,760
3.	Conglomerates	15	12,631,670
4.	Industrial goods	25	14,190,360
5.	Oil and gas	25	44,194,200
6.	Construction and Real Estate	10	40,434,900
7.	Financial services	35	58,783,610
8.	Agriculture	5	2,024,800

The result in Table 5.2 shows the financial services has the highest mean executive compensation with ₦58,783,610 (USD293,918), followed by oil and gas sector with ₦44,194,200 (USD220,971). The lowest mean executive compensation of ₦2,024,800 (USD10,124) is from the agricultural sector. The graphical representation is shown in Figure 5.1. The highest level of executive compensation from the financial services sector compared to other sectors could be part of the reasons why some studies have excluded financial companies from their studies (Firth *et al.*, 2007; Hubbard & Palia, 1995). The result shows there are variations in level of executive compensation across industries in Nigeria.

5.2 Descriptive Statistics

This section presents the descriptive statistics and the univariate test results for the data set as used for this study. This section provides suggested answers to the study's first research question on the extent of executive compensation practice in NLCs. The companies were first separated into two groups: the MNCs and the DCOMs. Thereafter, another separation into pre and post CG Code 2011 periods was made.

This separation is imperative as it enables an examination of any variation in executive compensation between them. In addition, the effectiveness or otherwise of the corporate governance variables between them can equally be examined. This is to enable the provision of answers for the first research question on the extent of executive compensation practice in NLCs.

5.2.1 Descriptive Statistics of Executive Compensation

The descriptive statistics of executive compensation defined as the highest paid director is presented in Table 5.3 and depicted in graphical form in Figure 5.2. First, the executive compensation is presented for every year of the study period. This is followed by the full period data. The average executive compensation paid during the period of study was ₦35,383,870 (USD176,919) ranging from ₦620,000 (USD3,100) to ₦183,412,000 (USD917,060). This is an indication of wide range of variations in executive compensation paid by companies to their CEOs in NLCs during the study period. The result indicates a steady rise in executive compensation from an average of ₦28,031,600 (USD140,158) in 2009 to ₦44,003,400 (USD220,017) by 2013. This shows an increase of about 57% over the 5 year period. This compares with the highest paid director that has increased from ₦115,520,000 (USD577,600) in 2009 to ₦183,412,000 (USD917,060) by 2013.

Table 5.3
Descriptive Statistics of Executive Compensation for Full Sample from 2009 to 2013

Year	Obs.	Mean	Median	Minimum	Maximum	Std. Dev.
2009	43	28031.60	20000.00	620.00	115520.00	25170.91
2010	43	29344.00	22013.00	1754.00	80912.00	23434.99
2011	43	33878.26	23526.00	2685.00	159031.00	33333.77
2012	43	41662.12	24738.00	3954.00	168155.00	42616.65
2013	43	44003.40	28067.00	1111.00	183412.00	43878.06
Overall	215	35383.87	23954.00	620.00	183412.00	35014.41

The mean amount of ₦35,383,870 (USD176,919) implies that an average CEO earns over ₦2,900,000 (USD14,500) per month in NLCs. From Figure 5.2, it is evident that the highest paid director decreased from 2009 to 2010 only to show a steady rise from 2010 to 2013. The steady rise could be attributed to scarcity of managerial labour talent in the market. Anecdotal evidence abounds as to how the banks recruited employees from other sectors with higher financial packages before the financial crisis in 2009.

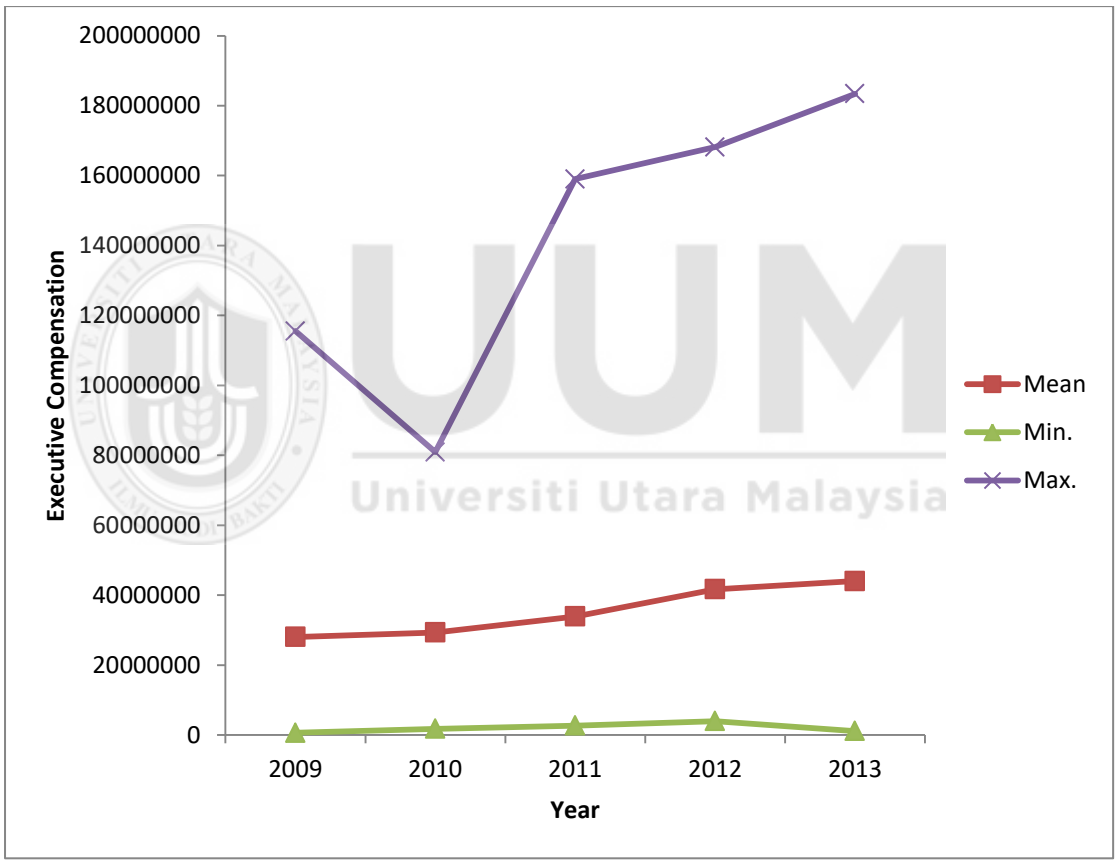

Figure 5.2
Executive Compensation for Full Sample from 2009 to 2013

In Nigeria, there is no regulation mandating companies to make detailed disclosure of their executive compensation in the annual report (Odewale & Kamardin, 2015a). This has hindered empirical research from Nigeria on this issue. The CG Code 2003 recommends the disclosure of the emoluments of the directors, chairman and the

highest paid director in the annual report plus stock options and pension contributions where applicable. The CG Code 2011 went further by recommending the disclosure of the company's compensation policy in the annual report. In addition, the compensation of the CEO and executive directors should include stock options and bonuses that are performance related, all of which are to be disclosed in the annual report. At present, there is no company that makes disclosure of the components of executive compensation on an individual basis in the annual reports. By 2012, some of the companies that hitherto disclosed their directors' emoluments, and that of the chairman and highest paid director failed to do so; instead they disclosed the bulk sum for the Key Management Personnel in compliance with the requirement of IAS 24 Related Party Disclosure. Among such companies are Stanbic IBTC Holdings Plc and Lafarge Cement WAPCO Nigeria Plc. Inadequate disclosure of executive compensation in the annual reports by NLCs is an evidence of information asymmetry as Laksmana (2008) concludes that greater disclosure of executive compensation serves to reduce information asymmetry.

5.2.2 Descriptive Statistics

The summary statistics of variables for the full sample, as presented in Table 5.4 shows that the mean board size is 9.77 with a minimum of 5 and maximum of 20 for a typical sample of NLCs. This satisfies the average board size of 10 recommended for Nigerian listed companies (Sanda *et al.,* 2011) to make it effective in performing its duties to the shareholders. This also finds support from the international literature (Lipton & Lorsch, 1992) that recommends a board size of between 8 and 10. This is however slightly higher than the board size of 7 or 8 recommended by Jensen (1993). It is also higher than the mean board size of 8.81 reported for Ghanaian listed

companies (Abor, 2007) even though both countries are in the same West Africa sub-region. This statistic is however in compliance with the recommendation of the CG Code 2011 that recommends a minimum board size of 5.

Table 5.4
Descriptive Statistics

	Mean	Median	Minimum	Maximum	Std. Dev.	Skewness	Kurtosis
Executive Compensation							
LnCOMP	9.991	10.084	6.430	12.119	1.050	0.289	2.800
Board Attributes							
BDS	9.772	9.000	5.000	20.000	3.011	0.793	3.415
BDC	0.681	0.667	0.200	0.933	0.133	-0.221	3.338
CEOD	0.023	0.000	0.000	1.000	0.151	6.326	41.024
GEND	0.091	0.091	0.000	0.333	0.095	0.715	2.499
CCOM	0.572	1.000	0.000	1.000	0.496	-0.291	1.085
CCINDP	0.460	0.000	0.000	1.000	0.500	0.159	1.025
Ownership Structure							
CEOO	0.033	0.000	0.000	0.400	0.084	2.820	10.251
DIRO	0.130	0.027	0.000	0.910	0.197	1.669	4.760
BLKO	24.699	18.430	0.000	85.880	24.446	0.868	2.741
MNCO	22.651	0.000	0.000	75.000	29.396	0.615	1.548
Control Variables							
ROA	0.111	0.086	-0.927	0.688	0.135	-1.203	19.871
SIZE	17.386	17.302	13.336	22.077	2.129	0.367	2.339
LEV	0.621	0.632	0.115	1.304	0.217	-0.045	2.463
GRT	0.135	0.098	-0.548	6.539	0.483	10.915	145.399
IND	0.163	0	0	1	0.370	1.827	4.337
N	215						

This pooled study sample shows mean board composition of 68.10%. The implication of this is that more than two-third of the board members in NLCs

comprise outside directors; that ordinarily is expected to guarantee the independence of the board. This is consistent with the recommendation of the CG Code 2011 that recommends the board should comprise of more non-executive directors.

The descriptive statistics for CEO duality shows a mean of 2.30%. This is an indication that 97.70% of NLCs have separate roles for both the CEO and Chairman. All the companies that constitute sample for MNCs separate the position of the CEO and that of the Chairman. This again is a substantial compliance with the recommendation of the CG Code 2011. The average number of women that sit as directors in NLCs is 9.10%. This percentage is low, viewed in the light of the suggestion by Adams and Ferreira (2009) that boards with higher proportion of women do adequate monitoring of the CEO and tend to align more with the interests of the shareholders. However, this result is comparable to 10% mean women directors documented by Gul *et al.* (2011) in their US study and improves over Campbell and Mı´nguez-Vera (2008) who reported mean female directors of 3.28% in Spain.

The result shows that 57.20% of the sample companies have compensation committee while 42.80% do not yet have compensation committee. This result is higher than that reported for China (37%) by Conyon and He (2011). It is however inconsistent with the benchmark for international good corporate governance and is inconsistent with the recommendations of the CG Code 2011 that NLCs should establish compensation committees. The average for independent compensation committee is 0.46, the implication is that only 46% of NLCs have majority outside director dominated compensation committee.

The mean CEO ownership is found to be 3.30% with a minimum of 0% and maximum of 40%. Bhagat and Bolton (2008) document mean CEO ownership in their US sample to be 2.92% while Core *et al.* (1999) report average CEO share ownership of 1.52%. Ozkan (2007) reports mean CEO shareholding of 1.71% for UK. This indicates that CEO ownership is low in companies whether from developed or emerging economies.

Directors' ownership ranges from 0% to 91% with an average of 13%. This result is consistent with findings from past studies from Nigeria. For example, Ehikioya (2009) finds the mean directors ownership for their sample of NLCs to be 15.35%. Similarly, Sanda *et al.* (2011) report average directors' ownership in NLCs to be 12%. However, directors' ownership in NLCs is low compared to what obtains in China where Firth *et al.* (1999) document that the mean directors ownership is 44%, and higher than what obtains in UK where Ozkan (2007) report average directors share ownership of 4.19%.

Blockholders ownership in NLCs average 24.70% in the study sample size ranging from a minimum of 0% to as much as 85.88%. The average blockholders ownership in the UK is 27.51 (Ozkan, 2007), this compares with this study's finding. Table 5.4 shows that 22.25% of shares in NLCs are held by MNCs. This ranges from 0% to 75% shareholding.

The average ROA for the sample NLCs during the study period is 11.10%. The minimum ROA was found to be -9.27% with a maximum of 68.80% This is lower than the 13.80% reported by Bhagat and Bolton (2008) for US and compares to the

11.40% for Ghanaian listed companies as documented by Abor (2007). This could be an indication that company performance in emerging economies may be lower than those of the developed countries. The proxy for company size is the natural logarithm of a company's total assets. The result indicates a mean of 17.39 (₦2.91 Billion) (USD14.55 Million) with a minimum of 13.34 (₦619 Million) (USD3.095 Million) and maximum of 22.08 (₦3.87 Billion) (USD19.35 Million).

In terms of leverage, the typical NLC has an average of 0.621 gearing ratio. This shows that the average company in Nigeria is moderately geared. Debt financing in NLCs is higher when compared to the 0.427 obtained by Bhagat and Bolton (2008) for their US samples. The mean value for sales growth reported in this study is 13.50% that ranges from -55% to 654%, which shows a wide variation in sales growth among NLCs. For the industry sector, the companies from the financial sector accounts for 16.30% of study sample and the non-financial companies account for 83.70%.

5.2.3 Mean Descriptive Statistics

Table 5.5 provides the mean descriptive statistics for the study variables for every year covered by the study period. The mean board size is relatively stable during the study period with 9.86 in 2009 and 9.67 in 2013. On the overall the board size in NLCs is about 10 members. There is not much changes in board composition between 2009 and 2012, but it increased to 70.40% by 2013 from 68.30% in 2012. This signifies an indication by companies to comply with the CG code 2011 requirement that the board should be comprised of more outside directors. The separation of the position of the CEO from that of the Chairman is generally seen to

indicate good corporate governance practice. The CEO duality remained constant at 2.3% all through the sample period. This implies that 2.3% of the sample do not comply with the CG code 2011 requirement that the position of the CEO should be separated from the Chairman so that no one individual will have total control of company affairs.

Table 5.5
Mean Descriptive Statistics from 2009 to 2013 for Full Sample

	2009	2010	2011	2012	2013	All
Executive Compensation						
LnCOMP	9.770	9.983	9.977	10.133	10.182	9.991
Board Attributes						
BDS	9.860	9.861	9.698	9.767	9.674	9.772
BDC	0.672	0.670	0.678	0.683	0.704	0.681
CEOD	0.023	0.023	0.023	0.023	0.023	0.023
GEND	0.067	0.089	0.091	0.088	0.120	0.091
CCOM	0.372	0.419	0.628	0.674	0.767	0.572
CCINDP	0.279	0.302	0.465	0.558	0.698	0.460
Ownership Structure						
CEOO	0.038	0.035	0.033	0.031	0.025	0.033
DIRO	0.138	0.128	0.144	0.118	0.123	0.130
BLKO	23.442	23.519	23.797	25.199	27.537	24.699
MNCO	22.756	22.811	23.316	22.255	22.117	22.651
Control Variables						
ROA	0.128	0.133	0.110	0.079	0.107	0.111
SIZE	17.127	17.226	17.410	17.536	17.634	17.386
LEV	0.616	0.588	0.621	0.638	0.644	0.621
GRT	0.170	0.088	0.159	0.095	0.161	0.135
IND	0.163	0.163	0.163	0.163	0.163	0.163
N	215					

The percentage of women directors increased from 6.70% in 2009 to 12.00% in 2013 indicating the admission of more women to directorship positions during the study period. The increase in the proportion of women on the board does not however

translate to reduction in executive compensation during the study period. The mean compensation committee increased progressively from 37.20% in 2009 to 76.70% in 2013. An implication of this is that there was great awareness and desire to establish compensation committees by companies in compliance with the CG codes requirement. Again, their presence does not translate to reduction in executive compensation as expected under the agency theory. The result shows that companies with independent compensation committees increased progressively from 27.90% in 2009 to 69.80% by 2013. There was increased compliance with the CG Code requirement for independent compensation committee, but this does not translate to reduction in executive remuneration as shown in the regression results.

There was a decreasing trend in CEO ownership from 3.8% in 2009 to 2.5% in 2013. This could be an indication that CEOs detest monitoring that made them to shed their shareholdings as a result of the Code's requirement for outside directors' dominated board coupled with whole outside directors' compensation committee. It is observed from the result that there is fluctuation in directors' ownership between 2009 and 2013 that culminated in an overall average of 13.00%. The result indicates a steady increase by blockholders ownership from 23.44% in 2009 to 27.54% in 2013. This suggests that the CG Code 2011 has made the blockholders to develop greater interests in the Nigeria capital market as this increase became pronounced in 2012 and 2013 after the introduction of the CG Code 2011. The MNCs ownership remains relatively stable between 2009 and 2013 averaging 22.65%. The industry classification remained the same all through the sample period with the financial services sector contributing an average of 16.30 % of the study sample.

5.2.4 Descriptive Statistics of Executive Compensation for Domestic Companies

Table 5.6 presents the descriptive statistics for executive compensation for DCOMs from 2009 to 2013 while Figure 5.3 depicts the trend in graphical form. The mean executive compensation rose steadily ranging from ₦26,712,690 (USD133,563) in 2009 to ₦41,739,780 (USD208,699) by 2013. The maximum highest paid director rose from ₦76,656,000 (USD383,280) in 2009 to ₦183,412,000 (USD917,060) by 2013. The steady rise in executive compensation without a corresponding increase in company performance as shown in Table 5.7 provides evidence that company executives in Nigeria decouple their pay from company performance. In Nigeria, Ayininuola (2007) assert CEOs exert immense influence in the determination of executive directors' compensation. This is consistent with the argument of Tosi and Gomez-Mejia (1989) that CEOs endeavour to decouple their pay from performance, given that this increase is not performance related.

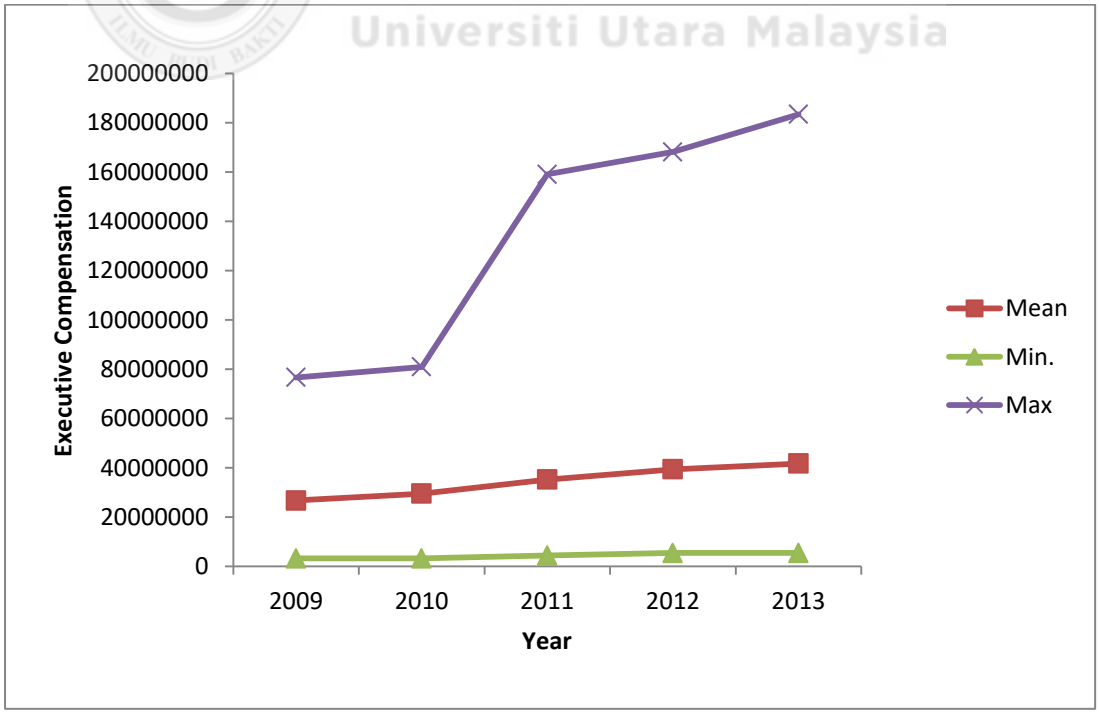

Figure 5.3
Executive Compensation for Domestic Companies from 2009 to 2013

Table 5.6
Descriptive Statistics of Executive Compensation for Domestic Companies from 2009 to 2013

Year	Obs.	Mean	Median	Minimum	Maximum	Std. Dev.
2009	26	26712.69	19187.00	3194.00	76656.00	22782.99
2010	26	29498.58	22005.00	3194.00	80912.00	24350.30
2011	26	35212.31	23740.00	4400.00	159031.00	37428.28
2012	27	39375.11	20500.00	5400.00	168155.00	45731.10
2013	27	41739.78	24952.00	5400.00	183412.00	45085.26
Overall	132	34599.36	22006.50	3194.000	183412.00	36480.90

Overall executive compensation indicates a mean of about ₦34,599,360 (USD172,997) with range from ₦3,194,000 (USD15,970) to over ₦183,412,000 (USD917,060). This wide variation could be as a result of inadequate disclosure of the amount paid to the highest paid director by some of the companies. From the data gathered, some of the companies suppressed the amount disclosed as highest paid director and there was no explanation for such suppression. This finding is consistent with the submission by Ayininuola (2007) that directors in NLCs collude with executives to award hidden compensation to company managers. Moreover, there is no disclosure of executive compensation policy in the annual reports to enable an examination of how executive compensation is determined in Nigeria. This also supports the argument that executive directors in Nigeria receive compensation as benefits-in-kind whose values are higher than those disclosed in the annual report (Ayininuola, 2007). This result provides further evidence of lack of transparent disclosure of executive compensation in NLCs and is consistent with the finding of Odewale and Kamardin (2015a) that report a low average transparency disclosure score of 37.29% for NLCs. This is considered low when compared with transparency disclosure score of 68% for European companies documented by Muslu (2010).

5.2.5 Descriptive Statistics for Domestic Companies

Table 5.7 presents the descriptive statistics for domestic companies as contained in the sample for this study. The number of observations that constitute domestic companies is 132 company-years. Executive compensation has been described under Table 5.6 and as such this description centres on other variables. Beginning with the board size, the average board consists of 9.82 members suggesting that it is within the optimal board size that will make them effective in discharging their monitoring duties. The board composition variable has a mean value of 67.90%. This indicates

Table 5.7
Descriptive Statistics for Domestic Companies

	Mean	Median	Minimum	Maximum	Std. Dev.
Executive Compensation					
LnCOMP	9.998	9.999	8.069	12.119	0.952
Board Attributes					
BDS	9.818	9.000	5.000	20.000	3.404
BDC	0.679	0.667	0.429	0.909	0.118
CEOD	0.038	0.000	0.000	1.000	0.192
GEND	0.094	0.100	0.000	0.333	0.099
CCOM	0.576	1.000	0.000	1.000	0.496
CCINDP	0.477	0.000	0.000	1.000	0.501
Ownership Structure					
CEOO	0.040	0.001	0.000	0.291	0.082
DIRO	0.161	0.070	0.000	0.911	0.194
BLKO	35.541	32.000	0.000	85.880	24.325
Control Variables					
ROA	0.094	0.073	-0.927	0.688	0.152
SIZE	17.279	16.197	13.336	22.077	2.591
LEV	0.633	0.676	0.116	1.304	0.239
GRT	0.105	0.097	-0.548	0.803	0.228
IND	0.265	0	0	1	0.443
N	132				

that the board is dominated by members who are outside directors. CEO duality indicates that 96.20% of the sample has separate individuals occupying the position of the CEO and Chairman (mean = 3.80%). The result shows that 9.40% of women are in directorship positions while the compensation committee has a mean of 57.60%. This indicates that 42.40% of domestic companies in Nigeria are yet to comply with the CG Code 2011 requirement for the establishment of compensation committee. The result shows that 47.70% of the sample companies have independent compensation committees.

The mean CEO ownership is 4% while the mean directors' share ownership is 16.10% with a minimum of 0% and maximum of 91.10%. This is relatively high as it compares to the 16.80% reported by Krivogorsky (2006) for the US. The average blockholders ownership is 35.54% indicating the strong presence of block shareholders in domestic companies in Nigeria. The above summary evidences support for Sanda *et al.* (2011) that documented concentration of share ownership in a few hands in NLCs. For the control variables of executive compensation, the average ROA is 9.40% with a minimum of -9.27% and a maximum of 68.80%. The average for leverage is 63.30% while average growth is 10.50%. For the industry variable, the financial services sector constitutes 26.50% of the domestic companies.

5.2.6 Descriptive Statistics of Executive Compensation for Multinational Companies

Table 5.8 shows the descriptive statistics for executive compensation for MNCs during the period 2009 to 2013 while Figure 5.4 provides the trend. The mean highest paid director for 2009 was ₦30,048,760 (USD150,244) that declined to ₦29,107,590 (USD145,538) by 2010 only to rise steadily to ₦47,823,250 (USD239,116) by 2013.

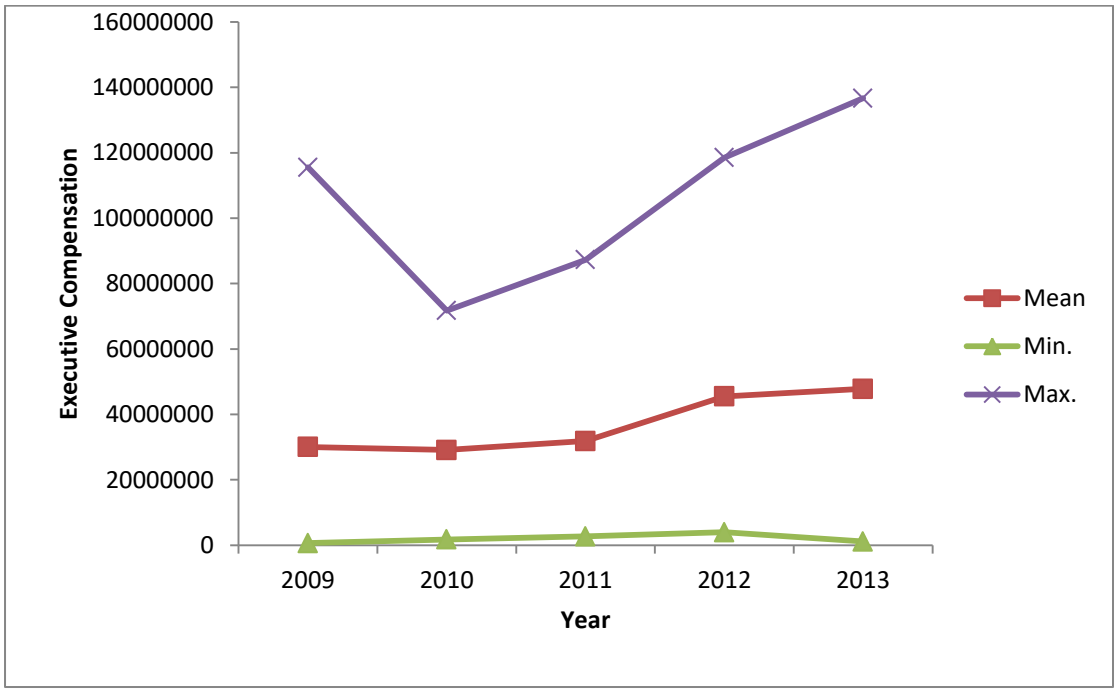

Figure 5.4
Executive Compensation for Multinational Companies from 2009 to 2013

Table 5.8
Descriptive Statistics of Executive Compensation for Multinational Companies from 2009 to 2013

Year	Obs.	Mean	Median	Minimum	Maximum	Std. Dev.
2009	17	30048.760	22972.000	620.000	115520.000	29067.950
2010	17	29107.590	26189.000	1754.000	71732.000	22695.480
2011	17	31837.940	23384.000	2685.000	87289.000	26843.240
2012	16	45521.440	33754.500	3954.000	118500.000	37881.670
2013	16	47823.250	34535.000	1111.000	136691.000	42926.620
Overall	83	36631.540	29232.000	620.000	136691.000	32724.530

It could be that the global shock in 2009 affected the executive compensation in 2010. On the whole the average highest paid director during the period was ₦36,631,540 (USD183,158) with a minimum of ₦620,000 (USD3,100) and maximum of ₦136,691,000 (USD683,455).

5.2.7 Descriptive Statistics for Multinational Companies

The MNCs sample consists of 83 company-year observations and the summary statistics for the study variables excluding executive compensation having discussed it in the previous section is presented in Table 5.8. The result shows that MNCs subsidiaries from the financial services sector are not included in the sample. These subsidiaries of MNCs include Ecobank Plc, Citibank, Stanbic IBTC Bank Plc, and Standard Chartered Bank Plc. They were excluded from the study sample because they failed to meet the criteria for inclusion in the study sample. For example, Citibank is not listed on the NSE while Stanbic IBTC Bank Plc failed to disclose the highest paid director in its 2013 annual report.

The average board size is 9.70 members. The average board consists of 68.60% outside directors. The gender diversity variable (GEND) has a mean of 8.60%. Table 5.9 shows that 56.6% of the observations have a compensation committee and 43.40% have independent compensation committee. The level of CEO share ownership is low; the average CEO ownership is 2.10%. On average, the directors hold 8.10% of MNCs shares while the blockholders hold 7.46% of company shares. Company performance shows average ROA of 13.90% with a minimum of -7.20% and maximum of 39.50%. The average leverage is 0.602 having a minimum of 0.115 and maximum of 0.940. Average sales growth is 18.20%.

Table 5.9
Descriptive Statistics for Multinational Companies

	Mean	Median	Minimum	Maximum	Std. Dev.
Executive Compensation					
LnCOMP	9.980	10.283	6.430	11.825	1.195
Board Attributes					
BDS	9.699	9.000	6.000	15.000	2.267
BDC	0.686	0.700	0.200	0.933	0.154
CEOD	0.000	0.000	0.000	0.000	0.000
GEND	0.086	0.091	0.000	0.286	0.089
CCOM	0.566	1.000	0.000	1.000	0.499
CCINDP	0.434	0.000	0.000	1.000	0.499
Ownership Structure					
CEOO	0.021	0.000	0.000	0.400	0.088
DIRO	0.081	0.004	0.000	0.605	0.194
BLKO	7.455	0.000	0.000	35.450	11.139
MNCO	58.674	60.000	31.400	75.000	10.759
Control Variables					
ROA	0.139	0.114	-0.072	0.395	0.097
SIZE	17.557	17.605	15.389	19.451	1.029
LEV	0.602	0.620	0.115	0.940	0.176
GRT	0.182	0.098	-0.269	6.539	0.722
IND	0	0	0	0	0
N	83				

5.2.8 Descriptive Statistics for Study Sample Before the Introduction of Code of Corporate Governance for Public Companies in Nigeria 2011

Table 5.10 shows summary statistics for the sample before the introduction of the CG Code 2011. The average executive compensation for these sample companies is ₦30,417,950 (USD152,090) (9.880) during the period. On average, the board is made up of 9.81 members with more than two third (67.30%) as outside directors. The finding shows that 2.30% of the sample have same individual occupying the position of the CEO and Chairman concurrently. Regarding gender diversity representation,

Table 5.10
Descriptive Statistics for Study Sample Before the Introduction of Code of Corporate Governance for Public Companies in Nigeria 2011

	Mean	Median	Minimum	Maximum	Std. Dev.
Executive Compensation					
LnCOMP	9.880	9.999	6.430	11.977	1.029
Board Attributes					
BDS	9.806	9.000	5.000	20.000	3.110
BDC	0.673	0.667	0.200	0.933	0.139
CEOD	0.023	0.000	0.000	1.000	0.151
GEND	0.082	0.083	0.000	0.333	0.092
CCOM	0.473	0.000	0.000	1.000	0.501
CCINDP	0.348	0.000	0.000	1.000	0.478
Ownership Structure					
CEOO	0.035	0.000	0.000	0.4000	0.137
DIRO	0.137	0.034	0.000	0.911	0.208
BLKO	23.586	15.450	0.000	85.88	24.188
MNCO	22.961	0.000	0.000	75.00	29.328
Control Variables					
ROA	0.124	0.101	-0.033	0.481	0.107
SIZE	17.254	17.121	13.363	21.767	2.085
LEV	0.608	0.629	0.116	1.304	0.212
GRT	0.139	0.132	-0.508	0.803	0.215
IND	0.163	0	0	1	0.371
N	129				

8.20% of board positions are occupied by women. Less than half (47.30%) of the companies have compensation committee as a board committee and 34.80% of the committees are independent. On ownership structure, the average CEO shareholding is 3.50%. The mean director shareholding during this period stood at 13.70% while the block shareholders hold more than 23% of the companies' equity. On average, 22.96% of the shares are held by MNCs. For the control variables of executive compensation the average ROA is 12.40%, leverage is 60.80% and growth is 13.90%. The companies from the financial services sector constitute 16.30% of the study sample during this period.

5.2.9 Descriptive Statistics for Study Sample After the Introduction of Code of Corporate Governance for Public Companies in Nigeria 2011

Table 5.11 shows the descriptive statistics of the sample after the introduction of the CG Code 2011. The mean executive compensation is ₦42,832,760 (USD214,164) (10.157) with a minimum of ₦1,111,000 (USD5,555) (7.013) and maximum of ₦183,412,000 (USD917,060) (12.119). The average board size is 9.721 with a minimum of 5 and maximum of 18. The mean outside directors is 69.40% with a minimum of 42.90% and maximum of 92.90%.

Table 5.11
Descriptive Statistics for Study Sample After the Introduction of Code of Corporate Governance for Public Companies in Nigeria 2011

	Mean	Median	Minimum	Maximum	Std. Dev.
Executive Compensation					
LnCOMP	10.157	10.136	7.013	12.119	1.065
Board Attributes					
BDS	9.721	9.000	5.000	18.000	2.872
BDC	0.694	0.667	0.429	0.929	0.123
CEOD	0.023	0.000	0.000	1.000	0.152
GEND	0.104	0.100	0.000	0.333	0.100
CCOM	0.721	1.000	0.000	1.000	0.451
CCINDP	0.628	1.000	0.000	1.000	0.486
Ownership Structure					
CEOO	0.028	0.000	0.000	0.400	0.077
DIRO	0.120	0.018	0.000	0.616	0.181
BLKO	26.368	23.740	0.000	85.88	24.876
MNCO	22.186	0.000	0.000	75.00	29.664
Control Variables					
ROA	0.093	0.083	-0.927	0.688	0.168
SIZE	17.585	17.587	13.336	22.077	2.190
LEV	0.641	0.652	0.115	1.211	0.223
GRT	0.128	0.071	-0.548	6.639	0.719
IND	0.163	0	0	1	0.371
N	86				

The CEO duality shows a mean of 2.30%. The average gender diversity is 10.40% from a minimum of 0% to maximum of 33.30%. The finding shows that 72.10% of the sample has a compensation committee in place. The result shows that 62.80% of the compensation committees are independent. The result indicates that the CEOs own 2.80% of the company shares that range from 0% to 40%. The average directors' shareholding is 12% with a minimum of 0% and maximum of 61.60%. Blockholders ownership constitutes 26.37% of the shares while MNCs hold 22.19% of company shares on average. The mean for ROA is 9.30% that ranges from -9.27% to 68.80%. The average for leverage is 64.10% with a minimum of 11.50% and maximum of 121.10%. The average growth rate is 12.80%. The companies from the financial services sector account for 16.30% of the study sample during this period.

5.3 Univariate Analysis

5.3.1 Univariate Analysis Based on Sample of Multinational Companies and Domestic Companies

In Table 5.12, t-test indicates no statistical difference in executive compensation between MNCs and DCOMs. This finding reinforces support for the argument that there will not be any significant difference in executive compensation between MNCs and DCOMs because of their operation in the same environment with low investor protection rights and weak enforcement and compliance mechanism (Okike, 2007; ROSC, 2008, 2011). This is consistent with the argument of Kostova and Roth (2002) that MNCs become isomorphic with the local companies so as to drive and maintain legitimacy in the foreign country.

There are no significant statistical differences between MNCs and DCOMs in the board attribute variables except for the CEO duality. This implies that these attributes are not influenced by the categorization of the company into whether it is a MNC or DCOM. The MNCs and DCOMs have mean board size of 9.7 and 9.8 respectively. Board composition is around this figure (68%) for both MNCs and DCOMs during the study period. All the companies that constitute sample for MNCs maintain separate positions for the CEO and Chairman.

Table 5.12
Univariate Comparisons of Dependent, Independent and Control Variables for Study Sample of MNCs and DCOMs (2009 -2013)

	MNCs	DCOMs	t -test	
	Mean	Mean	t-value	p-value
Executive Compensation				
LnCOMP	9.980	9.998	0.119	0.906
Board Attributes				
BDS	9.699	9.818	0.283	0.778
BDC	0.686	0.679	-0.379	0.705
CEOD	0	0.038	1.799	0.073*
GEND	0.086	0.094	0.567	0.572
CCOM	0.566	0.576	0.136	0.892
CCINDP	0.434	0.477	0.621	0.535
Ownership Structure				
CEOO	0.021	0.040	1.547	0.123
DIRO	0.081	0.161	2.943	0.004***
BLKO	7.455	35.541	9.881	0.000***
Control Variables				
ROA	0.139	0.094	-2.444	0.015**
SIZE	17.557	17.279	0.931	0.353
LEV	0.602	0.633	1.015	0.311
GRT	0.182	0.105	-1.133	0.259
IND	0	0.265	5.447	0.000***
N	83	132		

***, **, * Significant at 1%, 5%, and 10% level respectively.

The average directors' ownership in MNCs is 8.10% and 16.10% for DCOMs. There is a significant difference between the MNCs and DCOMs ($p < 0.01$) for t-test. The directors in the domestic companies in Nigeria own as much as twice their MNCs counterparts. There is however a wide disparity between the presence of blockholders in MNCs and their domestic counterparts as the result shows they hold 7.46% and 35.54% shares respectively. There is a significant statistical difference between these two. This shows a high presence of block shareholders in DCOMs listed on the NSE compared to their MNCs counterpart. There are lesser block shareholders in MNCs because the MNCs hold substantial shareholdings in their foreign subsidiaries in Nigeria. Their minimum shareholding is 31.40% with a median of 60% as indicated in Table 5.9. This study finds significant difference between the ownership structure of MNCs and those of the DCOMs. For the control variables, company performance is significantly different for the two groups while company size, leverage and growth do not show any significant difference between the MNCs and the DCOMs. However, the result shows a significant difference in the financial sector variable between MNCs and DCOMs. This is because the subsidiaries of MNCs from the financial services sector were excluded from the study. The banks with subsidiaries in Nigeria such as Citibank, Ecobank Plc, and Stanbic IBTC Bank Plc were excluded from the study as they failed to satisfy the conditions for inclusion in the study sample. However, 26.50% of the DCOMs are from the financial services sector.

5.3.2 Univariate Analysis based on Sample of Pre CG Code 2011 and Post CG Code 2011

In Table 5.13, t-test is used to ascertain whether there are statistical differences between PreCG and PostCG samples for the executive compensation, board attributes, and ownership structure variables. The result indicates a significant statistical

difference in executive compensation between PreCG and PostCG periods at 10% level. The PostCG samples show higher mean executive compensation than the PreCG period. The explanation for this could be that the CG Code 2011 is not effective in making the board to exercise its oversight function to constrain the CEOs from extracting higher compensation.

Table 5.13
Univariate Comparisons of Dependent, Independent and Control Variables for Study Sample Pre Corporate Governance Code 2011 (2009 -2011) and Post Corporate Governance Code 2011 (2012 and 2013)

	PreCG	PostCG	t -test	
	Mean	Mean	t-value	p-value
Executive Compensation				
LnCOMP	9.880	10.157	1.910	0.058*
Board Attributes				
BDS	9.806	9.721	-0.203	0.839
BDC	0.673	0.694	1.093	0.275
CEOD	0.023	0.023	0.000	1.000
GEND	0.082	0.104	1.641	0.102
CCOM	0.473	0.721	3.698	0.000***
CCINDP	0.349	0.628	4.163	0.000***
Ownership Structure				
CEOO	0.035	0.029	-0.615	0.540
DIRO	0.137	0.120	-0.590	0.556
BLKO	23.586	26.368	0.817	0.415
MNCO	22.961	22.186	-0.189	0.850
Control Variables				
ROA	0.124	0.093	-1.635	0.104
SIZE	17.254	17.585	1.117	0.265
LEV	0.608	0.641	1.092	0.276
GRT	0.1388	0.128	-0.160	0.873
IND	0.163	0.163	0.000	1.000
N	215			

***, **, * Significant at 1%, 5%, and 10% level respectively.

Board size, board composition, CEO duality, and gender diversity show no significant mean difference between the two periods. This implies that the publication of the CG Code 2011 does not impact on these variables in any significant manner, lending credence to the argument that internal corporate governance mechanism remains ineffective in an environment with weak enforcement mechanism. The NLCs have maintained appropriate board size, outside director dominated boards and separation of the position of the CEO from that of the chairman prior to the implementation of the requirements of the CG Code 2011. However, compensation committee presence and independent compensation committee show significant mean differences between the two periods.

There is an increase in the percentage of women directors following the introduction of the CG Code 2011. The CG Code 2011 caused a substantial increase in the number of companies that have established compensation committees. Before the publication of the CG Code 2011 only 47.30% of the companies have compensation committees as part of board committees but this increased significantly to 72.10% during the PostCG period. The independent compensation committee also increased from 34.90% before the CG Code 2011 to 62.80% after the Code. However, the increase in the existence of the compensation committee and independent compensation committee in companies are not justified by the attendant increase in executive compensation during the same period considering the argument by the proponents for its establishment. This is consistent with the argument of O'Reilly and Main (2007) that there is no evidence that corporate governance mechanism such as the presence of compensation committee have provided any explanation for variation in executive compensation.

The study could not find any significant statistical difference in the ownership structure variables between PreCG and PostCG periods. On the control variables, company performance, company size, leverage, growth, and industry sector return insignificant difference.

5.4 Correlation Analysis and Variance Inflation Factor

5.4.1 Correlation Analysis

The Pearson correlation coefficient among the study variables is presented in Table 5.14. Correlation analysis is used to measure the linear association that exists among the variables of study (Gujarati & Porter, 2009). This association could be positive or negative. It is also used to measure the collinearity that exists among the explanatory variables. A correlation coefficient of 0.90 is assumed to be high and shows that there is the problem of multicollinearity (Tabachnick & Fidell, 2007). In that case it is suggested that one of the variables needs to be dropped from the regression analysis so as to avoid the issue of multicollinearity. The correlation matrix shows a high correlation (r = 0.949) between CEO ownership (CEOO) and executive directors' ownership (ExDIRO). On running the OLS regression with all the variables it was found that the *p*-value of ExDIRO (0.884) is higher than that of CEOO (0.448), as such the ExDIRO variable was dropped from the model. Another high r (0.799) is found to exist between CCINDP and CCOM, but the two variables are retained since the r is not more than 0.90.

The result shows there is positive correlation between executive compensation and board size. This correlation result provides support for the argument that large

boards are associated with higher executive compensation. Consistent with agency theory's prediction, executive compensation is negatively correlated with board composition. This is in congruence with the argument that outside directors do adequate monitoring of executives that prevents them from extracting private benefits in form of excessive executive compensation. The correlation between executive compensation and CEO duality is negative and significant suggesting that when the board chairman is also the CEO he/she is more likely to align with the interest of the shareholders. The analysis indicates that executive compensation is positively correlated with gender diversity.

Executive compensation shows positive correlation with compensation committee and independent compensation committee. The bivariate result does not show that the presence of compensation committee and its independence will lead to lower executive compensation. The result indicates that executive compensation is negatively associated with directors' ownership and blockholders ownership. This supports the prediction of the agency theory that directors' shareholding and block shareholding by investors will make them align their interest with those of the shareholders and check the manager from exhibiting opportunistic behaviour. For the control variables, there is a positive association between company size, leverage, industry and executive compensation while growth shows a negative association.

Table 5.14 indicates that when there is an inverse association between DIRO and BDS such companies are more likely to report lower executive compensation. A positive association between CCINDP and BDS may possibly lead to higher executive compensation in companies where such exists. A company with negative association between BLKO and BDS will most likely pay lower executive compensation. The

Table 5.14
Pearson Correlation Matrix

	LnCOMP	BDS	BDC	CEOD	GEND	CCOM	CCINDP	CEOO
LnCOMP	1.000							
BDS	0.415***	1.000						
BDC	-0.160**	-0.197***	1.0000					
CEOD	-0.142**	-0.245***	-0.095	1.000				
GEND	0.330***	0.244***	-0.172**	-0.148**	1.000			
CCOM	0.136**	0.113*	-0.042	0.009	-0.014	1.000		
CCINDP	0.190***	0.126*	0.129*	0.043	-0.024	0.799***	1.000	
CEOO	-0.161**	-0.315***	-0.052	0.466***	-0.206***	-0.136**	-0.053	1.000
ExDIRO	-0.176***	-0.282***	-0.091	0.434***	-0.209***	-0.166**	-0.080	0.949***
DIRO	-0.237***	-0.263***	-0.080	0.194***	-0.226***	-0.027	-0.090	0.661***
BLKO	-0.178***	-0.285***	0.100	0.067	-0.110	-0.104	-0.111	0.323***
MNCO	-0.004	-0.052	0.008	-0.119*	-0.002	-0.041	-0.071	-0.142**
ROA	0.048	-0.113*	0.125*	-0.071	0.105	-0.056	-0.061	-0.225***
SIZE	0.571***	0.690***	-0.223***	-0.178***	0.270***	-0.014	0.012	-0.296***
LEV	0.130*	0.205***	-0.209***	0.204***	-0.014	-0.029	-0.028	0.004
GRT	-0.154**	0.077	-0.029	-0.025	-0.001	0.032	0.031	-0.069
IND	0.284*	0.612*	-0.206*	-0.068	0.150*	-0.077	-0.028	-0.127

Table 5.14 (continued)
Pearson Correlation Matrix

	ExDIRO	DIRO	BLKO	MNCO	ROA	SIZE	LEV	GRT	IND
ExDIRO	1.000								
DIRO	0.664***	1.000							
BLKO	0.317***	0.425***	1.000						
MNCO	-0.146**	-0.223***	-0.581***	1.000					
ROA	-0.237***	-0.256***	-0.053	0.143**	1.000				
SIZE	-0.262***	-0.381***	-0.367***	0.057	-0.155**	1.000			
LEV	0.018	0.026	0.015	-0.089	-0.277***	0.445***	1.000		
GRT	-0.060	-0.068	-0.120*	0.081	0.086	0.084	0.018	1.000	
IND	-0.091	-0.098	-0.036	-0.341*	-0.304*	0.720*	0.501*	0.048	1.000

***, **, * Correlation is significant at 1, 5 and 10 per cent level respectively.

result suggests that large size companies with large board size are associated with higher executive compensation. Large companies with less independent boards pay higher executive compensation. In addition, negative correlation between blockholders ownership and board size invariably leads to lower executive compensation.

The insignificance of other variables does not necessitate their exclusion from the model as the correlation coefficient is only a measure of association between two variables. Besides, excluding such variables could reduce the explanatory power of the model. In addition to the correlation matrix, this study also used the variance inflation factors and tolerance level to check for multicollinearity which is discussed hereunder.

5.4.2 Variance Inflation Factors and Tolerance

Variance inflation factor (VIF) and Tolerance (TOL) are used to check if multicollinearity pose problem in a study. VIF that has a value greater than 10 is considered as signal for the presence of multicollinearity among the regressors (Gujarati & Porter, 2009; Hair *et al.*, 2010). For TOL, a value of less than 0.10 is an indication of the presence of multicollinearity. VIF and TOL results shown in Table 5.15 indicate high collinearity for CEOO and ExDIRO variables that could be a problem in the study. This is similar to the result from the correlation matrix. As discussed in the previous section the ExDIRO variable was dropped to resolve the multicollinearity problem. As can be seen from Table 5.15 the CCOM and CCINDP variables have VIF values less than 4 thus supporting their inclusion in the regression model as multicollinearity is not an issue.

Table 5.15
Variance Inflation Factors and Tolerance for Executive Compensation

	VIF	Tolerance
BDS	2.37	0.421
BDC	1.30	0.770
CEOD	1.62	0.617
GEND	1.19	0.842
CCOM	3.40	0.294
CCINDP	3.34	0.299
CEOO	11.24	0.089
ExDIRO	10.92	0.092
DIRO	2.54	0.393
BLKO	2.21	0.452
MNCO	2.20	0.455
ROA	1.30	0.767
SIZE	4.13	0.242
LEV	1.76	0.568
GRT	1.03	0.967
IND	3.78	0.265
Mean VIF	3.40	

5.5 Multivariate Analysis

The results of the multivariate regression analysis and hypothesis testing as used in this study are presented in this section. This is followed by theoretical and empirical comparisons of the findings with those of prior studies.

5.5.1 Regression Results on Board Attribute and Ownership Structure Variables

The results for Models 1, 2 and 3 are reported in Table 5.16. In Model 1, only the board attributes and control variables are entered in the regression to examine the effects of board attributes on executive compensation. The F-value of 8.33 is significant at 1% level and indicates that there is a minimum of one independent variable that provides explanation for the variation in executive compensation. The

adjusted R^2 (0.1521) shows that the model explains 15.21% of the variations in executive compensation. The result shows that independent compensation committee is significant at 5% level ($\beta = 0.189$; $p = 0.020$) while other board attribute variables show insignificant relationship with executive compensation. Wald test for the joint significance of board attribute variables from Model 1 is significant at 5% level (*p*-value = 0.011). This finding indicates that there are board attribute variables that do not determine executive compensation in an environment with weak enforcement mechanism and low investor protection rights. This is consistent with the argument of Boubakri *et al.* (2005) that the inability of emerging economies to have functional institutions is responsible for their poor corporate governance system. This result is consistent with the findings in Core *et al.* (1999) that poor corporate governance mechanism is associated with higher executive compensation. This result may reflect the argument of Bebchuk and Fried (2004) that CEOs exert managerial power over the board when determining their compensation.

In the second Model, executive compensation is regressed on ownership structure and control variables. The F-value (7.18) is statistically significant at 1% level indicating that the ownership structure and control variables can jointly explain the variations in executive compensation in the study. The adjusted R^2 (0.1488) implies that the Model explains 14.88% of the variations in executive compensation. It is found that directors' ownership and MNCs ownership are significantly related to executive compensation. Executive compensation increases with greater directors' ownership ($\beta = 0.577$; $p = 0.002$), and decreases with increased MNCs ownership ($\beta = -0.024$; $p = 0.000$). The positive relationship is however not consistent with agency theory.

Table 5.16

Test of Board Attributes and Ownership Structure Variables as Determinants of Executive Compensation

Variables	1			2			3		
	Coef.	t-stat	p-value	Coef.	t-stat	p-value	Coef.	t-stat	p-value
Constant	2.968	0.99	0.328	2.527	0.73	0.470	2.933	0.94	0.350
Board Attributes									
BDS	0.033	1.30	0.201				0.020	0.84	0.407
BDC	-0.564	-0.93	0.356				-0.564	-0.96	0.344
CEOD[a]	--	-	--				--	-	--
GEND	0.133	0.24	0.809				0.102	0.21	0.835
CCOM	0.034	0.42	0.673				0.030	0.40	0.693
CCINDP	0.189**	2.42	0.020				0.169**	2.23	0.031
Ownership Structure									
CEOO[b]				1.394	1.20	0.238	1.558	1.46	0.152
DIRO				0.557***	3.39	0.002	0.474***	2.77	0.008
BLKO				0.008	1.38	0.175	0.006	1.17	0.249
MNCO				-0.024***	-5.23	0.000	-0.018***	-3.36	0.002
Control Variables									
ROA	0.298	1.10	0.277	0.214	0.82	0.416	0.287	1.09	0.283
SIZE	0.397**	2.45	0.018	0.433**	2.05	0.047	0.413**	2.39	0.021
LEV	0.077	0.19	0.847	0.248	0.77	0.444	0.139	0.36	0.723
GRT	-0.163***	-4.50	0.000	-0.138**	-2.52	0.016	-0.161***	-4.20	0.000
IND[c]	--	--	--	--	--	--	--	--	--
N	215			215			215		
Adjusted R^2	0.1521			0.1488			0.1820		
F-value	8.33***			7.18***			7.78***		

Wald Test for the Joint Significance	Model 1	F-Statistics	3.43**
		(*p*-value)	(0.011)
	Model 2	F-Statistics	10.02***
		(*p*-value)	(0.000)
	Model 3	F-Statistics	6.74***
		(*p*-value)	(0.000)

***, **, * Significant at 1%, 5%, and 10% level respectively.

Notes: a, CEOD was eliminated in STATA because of collinearity.

b, When EXDIRO was entered into the equation as substitute for CEOO, the result remained qualitatively similar.

c, IND was eliminated in STATA because of collinearity.

The CEO ownership and blockholders ownership both show insignificant relationship with executive compensation. This finding suggests that ownership structure variables are determinants of executive compensation in an environment with low investor protection rights and weak enforcement mechanism. A Wald test for the joint significance of ownership structure variables is significant at the 1% level. The implication is that ownership structure variables are indeed determinants of executive compensation in NLCs.

When all the board attributes and ownership structure variables are entered simultaneously as contained in Model 3 the result remains similar to those obtained in Models 1 and 2. The F-value (7.78) is statistically significant at 1% level with adjusted R^2 of 0.1820. The Wald test for the joint significance of board attributes and ownership structure variables show significance at the 1% level. It can therefore be inferred that the independent variables jointly explain the variations in executive compensation.

5.5.2 Main Regression Results

The regression results for the full sample are presented in Table 5.17. The squared term of MNCs ownership ($MNCO_{sq}$) does not produce any evidence of curvilinear relationship with executive compensation. Therefore, the interpretation centres on the linear specification model. The adjusted R^2 of 0.1820 indicates that the predictor variables explain 18.20% of the variation in executive compensation. The significant value of the F-statistic at 1% shows that the model significantly explains executive compensation.

The result rejects Hypothesis 1, that there is a positive relationship between board size and executive compensation. Even though the result indicates the expected relationship between board size and executive compensation ($\beta = 0.020$; $p = 0.407$), it remains insignificant. The implication of this result is that board size is not a determinant of executive compensation in NLCs. This result does not support the postulation of the agency theory that small board size will be associated with effective managerial monitoring. The result is similar to that of Ozdemir and Upneja (2012) that found no significant relationship between executive compensation and board size in the US lodging industry even though with opposite sign. They interpreted their finding as indication that different industries have different determinants of executive compensation. Conyon and He (2011) and Li *et al.* (2007) also report an insignificant negative relationship between board size and executive compensation.

This result however contrasts previous studies from China where Firth *et al.* (2007) document a significant negative association between board size and executive compensation. In New Zealand, Australia and USA Reddy *et al.* (2015), Cahan *et al.* (2005) and Core *et al.* (1999) respectively report a significant positive relationship between board size and executive compensation. Ozkan (2007) also finds that large boards are associated with higher executive compensation in the UK.

The mean board size in this study is about 10 members, this is conventionally within the range to make the board effective in monitoring managerial actions especially executive compensation. This study's finding could be an indication that the directors lack the requisite skills and expertise to negotiate executive compensation with the CEO. This is what Ayininuola (2007) described as knowledge and skill gaps in the

nomination of directors in NLCs. Another perspective is that the board may not employ the services of remuneration consultants when necessary. Further, the directors may be in the "old boys" network that may make them not to want to rock the boat since there is a board culture that does not allow for antagonism or there could be evidence of cronyism (Brick *et al.*, 2006; Jensen, 1993). Another reason for this finding is the inability of the boards in Nigeria to concentrate on decision making as according to Pierce (2011) in an interview granted the Society for Corporate Governance Nigeria (SCGN) Newsletter:

> If you look at most agendas of board meetings; you will find out that the major items on the agenda are a report from the Chief Executive Officer (CEO), … a report from the Remuneration Committees and probably, half of the time is spent on reviewing reports and been informed rather than the board taking an active, proactive decision making stands …. (p. 4)

Consistent with Pierce (2011), Ayininuola (2007, p. 27) argued that a board that just "trust and endorse" the reports submitted by management cannot provide leadership for the company. Another reason identified by Ayininuola (2007) for the non effectiveness of the boards in Nigeria in the performance of their functions is the non availability of data and the provision of poor quality information to them by management.

Contrary to the prediction in Hypothesis 2, that there is a significant relationship between outside director dominated boards and executive compensation, the result shows an insignificant negative relationship between board composition and executive compensation ($\beta = -0.564$; $p = 0.344$). It indicates that board independence is not a determinant of executive compensation in NLCs. This result is inconsistent with the expectation of the agency theory and the argument of the managerial power theorists. The implication here is that outside directors in NLCs may not after all be

effective monitors of management as envisaged by the Code of Corporate Governance for Public Companies in Nigeria (CG Code, 2003 & 2011) as they are independent on paper.

Recently, Gregory-Smith (2012) document lack of relationship between board independence and executive compensation in their panel study of UK companies from 1996 to 2008. This is consistent with the finding of Chalmers *et al.* (2006) who document an insignificant relationship between board independence and executive compensation in Australia and similar to Conyon and He (2011) that find an insignificant relationship between the variables in China. It is also similar to the finding of Conyon and Peck (1998) and Reddy *et al.* (2015) that document an insignificant relationship between outside directors and executive compensation. Chalmers *et al.* (2006) suggest that their result could be driven by the fact that the directors are in business relationship with the company which could make them become passive as regards to executive compensation matters. This result implies that outside directors may not necessarily align with the interest of the shareholders with respect to executive compensation issues in NLCs. The driving force here could be that they were nominated to the board by the CEO (Boivie *et al.*, 2012) and would want further board appointments in the future.

It is noted that entrenched managers in Nigeria influence the nomination of directors that are neither qualified nor truly independent (Ayininuola, 2007). In addition to the above adduced reasons, it is likely that the outside directors who are retired company executives may require patronage from the CEO and as such do not have the incentives to constrain the CEO from extracting higher compensation. The data for this study shows that some retired company executives sit on their former company's

boards. This is also consistent with Adegbite (2015, p. 23) that reports an interviewee as saying ‘‘I became the chairman after I retired as the CEO’’. Further, Adegbite (2015, p. 23) documents that one of the focus group respondents agrees that ‘‘we still need real board independence’’ in Nigeria.

Table 5.17
Fixed-Effects Panel Regressions (with robust option) for Executive Compensation

Variables	Linear specification			Quadratic specification		
	Coef.	t-stat	*p*-value	Coef.	t-stat	*p*-value
Constant	2.933	0.94	0.350	2.944	0.95	0.347
Board Attributes						
BDS	0.020	0.84	0.407	0.020	0.85	0.402
BDC	-0.564	-0.96	0.344	-0.593	-0.97	0.340
CEOD[a]	--	--	--	--	--	--
GEND	0.102	0.21	0.835	0.667	0.13	0.894
CCOM	0.030	0.40	0.693	0.028	0.36	0.718
CCINDP	0.169**	2.23	0.031	0.168**	2.25	0.030
Ownership Structure						
CEOO[b]	1.558	1.46	0.152	1.565	1.46	0.152
DIRO	0.474***	2.77	0.008	0.471***	2.74	0.009
BLKO	0.006	1.17	0.249	0.007	1.17	0.248
MNCO	-0.018***	-3.36	0.002	-0.025*	-1.92	0.061
MNCOsq				0.000	0.41	0.681
Control Variables						
ROA	0.287	1.09	0.283	0.302	1.10	0.277
SIZE	0.413**	2.39	0.021	0.410**	2.35	0.024
LEV	0.139	0.36	0.723	0.165	0.40	0.691
GRT	-0.161***	-4.20	0.000	-0.161***	-4.16	0.000
IND[c]	--	--	--	--	--	--
N	215			215		
Adjusted R^2	0.1820			0.1790		
F-value	7.78***			7.48***		

***, **, * Significant at 1%, 5%, and 10% level respectively.

Notes: a, CEOD was eliminated in STATA because of collinearity.

b, When EXDIRO was entered into the equation as substitute for CEOO, the result remained qualitatively similar.

c, IND was eliminated in STATA because of collinearity.

Additional explanation for this insignificant relationship is the lacklustre attitude of the regulators to demand greater transparency in the disclosure of executive compensation. This is evident in the lack of adequate executive compensation disclosure matters in the CG Codes. As an evidence of inadequate disclosure of information by companies in the annual report, Pierce (2011, p. 4) notes, "Yes, the level of transparency in all section of the annual report is significantly lower in Nigeria than it is in many other countries, there is an opportunity to greater disclosure, greater transparency and there is a seeming reluctant to do that …." On the part of regulators, the CBN governor in a newspaper interview Komolafe (2010) while he was providing explanation for the removal of the part of the CBN Prudential guidelines on disclosure of executive compensation in the annual reports states "we are dealing with something that has to do with security, and someone says you come out to disclose your salary, the next day, somebody shoots you. So you have to look at that."

Contrary to the insignificant findings, Ozdemir and Upneja (2012) provide evidence of increased executive compensation when the board is comprised of more outside directors in the US lodging industry. Ozkan (2007) also report positive association between outside directors' dominated boards and executive compensation, indicating that outside directors align with managerial interests in the UK. This is consistent with the findings of Correa and Lel (2014) that greater board independence is associated with higher executive compensation. In contrast, Firth *et al.* (2007) find that independent boards are not associated with excessive executive compensation. Similarly, Basu *et al.* (2007) document a negative relationship between board independence and executive compensation.

For gender diversity variable, GEND is found to have no effect on executive compensation (β = 0.102; *p* = 0.835). Hypothesis 4, that there is a negative relationship between women directors and executive compensation is not supported. This finding is consistent with the report of Campbell and Minguez-Vera (2008) of an insignificant effect that the presence of women directors had on company performance. It is however incongruent to the suggestion of Adams and Ferreira (2009) that boards with higher proportion of women do adequate monitoring of the CEO to align his or her interest with those of the shareholders. There could be inherent challenges facing the women on boards such as the few women directorships in NLCs.

The result from Table 5.17 does not show support for Hypothesis 5, that the presence of compensation committee has significant association with executive compensation. The presence of the compensation committee and executive compensation show positive relationship at insignificant level (β = 0.030; *p* = 0.693). The result suggests that the existence of compensation committee does not have any significant influence on executive compensation in NLCs. This is consistent with the argument of O'Reilly and Main (2007) that the presence of compensation committees in companies has not been shown to be a determinant of executive compensation. It is also similar to the finding of Conyon and Peck (1998) where they document an insignificant relationship between the existence of the compensation committee and executive compensation.

The reasons for this disappointing result could be the presence of the CEO on the compensation committee (Anderson & Bizjak, 2003) and inability of the committee to hold meetings as reported by some companies in the annual report. Another

explanation could be the low quality of the compensation committee members (Sun & Cahan, 2009, 2012) that has rendered them ineffective in the performance of their monitoring duty. Ayininuola (2007) shows that some directors in Nigeria lack the requisite knowledge and skills to enable them perform their duty optimally. The implication of this finding is that the compensation committee is not strong and capable of performing its assigned duties. In Nigeria, Ayininuola (2007) shows that committees do not have the needed resources and information required to function effectively. In contrast, Conyon and He (2011) provide evidence of a significant positive relationship between compensation committee and executive compensation in China, suggesting that their presence is associated with higher executive compensation. Consistent with Conyon and He (2011), Main and Johnston (1993) also find a positive relationship between compensation committee and executive compensation in the UK.

Another strand of research finds that the presence of compensation committee is associated with lower executive compensation. For example, Conyon (1997) finds that companies that established compensation committee during the study period report decreased growth in executive compensation. In the Nigerian context, the compensation committee seems not to have justified the essence for its existence as recommended by the CG Codes 2003 and 2011. The result also does not justify the position of agency theory that their presence will check managers' tendency to extract excessive compensation through appropriate monitoring (Allegrini & Greco, 2013).

The result shows that independent compensation committee has a positive and significant relationship with executive compensation at 5% level ($\beta = 0.169$; $p =$

0.031). Therefore, Hypothesis 6 which predicts a significant relationship between independent compensation committee and executive compensation is supported. This finding indicates that CEOs earn more when the proportion of non-executive directors on the compensation committee increases. This finding is consistent with Melis *et al.* (2012) that independent compensation committee is associated with higher stock option plans component of executive compensation in Italy. The result is also similar to the finding of Conyon and Peck (1998). It however contrasts the findings of other scholars who find insignificant association between independent compensation committee and executive compensation (Chhaochharia & Grinstein, 2009; Gregory-Smith, 2012).

The result suggests that independent compensation committees are ineffective in constraining the CEOs from earning excessive compensation. There is no support for the effective monitoring hypothesis of the agency theory as the compensation committee is shown to align with managerial interest. Even though the CG Code 2011 recommends that boards and compensation committee be composed of more non-executive directors to enhance their monitoring effectiveness, the finding of this study suggests otherwise. There is therefore no evidence that the corporate governance reform is about to achieve the intended objective with respect to executive compensation matters. The inability of the independent compensation committee to constrain the CEO from earning excessive compensation could be related to mutual back scratching (Brick *et al.*, 2006), where their nomination to the board was facilitated by the CEO (Ayininuola, 2007; Boivie *et al.*, 2012), or where they are pressure sensitive (David *et al.*, 1998). In Nigeria, CEOs are reported to unnecessarily intervene in important committees (Sanda *et al.*, 2011). Their

intervention in compensation committee matters may likely erode the committees' independent status.

Hypothesis 7 that predicts a significant relationship between CEO ownership and executive compensation is not supported. The result indicates that shareholdings by CEOs show positive relationship with executive compensation at statistically insignificant level ($\beta = 1.558$; $p = 0.152$) suggesting that CEO ownership is not important in determining executive compensation in NLCs. This result is similar to that of Ozkan (2007) who reports an insignificant relationship between CEO ownership and executive compensation in UK even though with a negative sign. This is also consistent with the findings of Sanders and Carpenters (1998). It however contrasts the argument of Hubbard and Palia (1995) and report by Conyon and He (2011) that CEOs equity holdings will align their interest with those of the shareholders.

This finding is neither consistent with the alignment of interest hypothesis nor with the entrenchment hypothesis (Fahlenbrach, 2009; Fama & Jensen, 1983b). For example, it is not in agreement with prior empirical studies (Core *et al.*, 1999; Lin *et al.*, 2013; Shin & Seo, 2011) that CEOs shareholding leads to decrease in executive compensation. It also contrasts the positive association between CEO ownership and executive compensation documented by Ben Hassen *et al.* (2015), Khan *et al.* (2005), and Li *et al.* (2007). In the Sub-Saharan African context, Munisi and Mersland (2013) document a positive relationship between CEO ownership and board compensation. The implication is that increased CEO ownership does not provide them incentives to align with interests of shareholders. However, the finding of this

study indicates that share ownership by CEOs makes them indifferent to executive compensation matters. The possible explanation for this result is the non availability of the equity-based component of the CEO compensation in NLCs. This is evident in the non disclosure of any equity based payment as part of the companies' compensation policy in the annual reports even though such disclosure is required by the CG Code 2011. The low CEO ownership of 3.30% reported in this study remains another contributor for the insignificant relationship with executive compensation as it does not provide them with significant power to influence executive compensation.

This study provides evidence of a significant positive relationship between directors' ownership and executive compensation at 1% level ($\beta = 0.474$; $p = 0.008$). This result provides support for Hypothesis 8 that directors' ownership will be significantly related with executive compensation. It also aligns with the entrenchment hypothesis argument that increased shareholding by directors will make them align with the interests of the manager to extract private benefits (Fahlenbrach, 2009). This result is similar to Basu *et al.* (2007) that find a positive association between directors' ownership and executive compensation in Japan and Munisi and Mersland (2013) that document a positive association between board ownership and board compensation among Sub-Saharan African listed companies.

This is however incongruent with the proposition of the agency theory (Jensen & Meckling, 1976; Fama, 1980; Jensen, 1993) that directors' ownership will align their interests with those of the shareholders. Increased shareholding by the directors does not provide enough incentives for them to constrain the CEO from extracting higher compensation. This result contrasts the finding of Cheng and Firth (2005) where they

document a significant negative relationship between directors' ownership and executive compensation in Hong Kong. Their result was driven by the large proportion of shares held by the directors (40.70%) compared to the 13.01% shareholding by directors in NLCs. The finding of low directors' ownership in this study compares with directors' ownership of 12% reported for NLCs by Sanda *et al*. (2011). Ozkan (2007) also finds a significant negative relationship between directors' ownership and executive compensation. Koh (2003) attributed the insignificant result obtained in his study to the low equity holdings by directors and argued that such low equity holding does not encourage them to mitigate the agency conflict that exists between managers and shareholders. Similarly, Reddy *et al.* (2015) find an insignificant relationship between directors' shareholding and executive compensation in New Zealand.

Nigeria is a country with weak institutions and low enforcement mechanism and this finding reinforces the argument that directors' shareholdings provides them with incentives to diverge their interests from those of the shareholders as increased shareholdings by directors lead to higher executive compensation. This result suggests directors in NLCs are pressure sensitive and may not want to be seen as rocking the boat (Brick *et al.*, 2006; David *et al.*, 1998). Similar to Munisi and Mersland (2013), this study shows that directors' ownership in NLCs makes them to become entrenched and as such use their share ownership influence to make the CEO extract higher compensation. This is an affirmation of the conclusion by Ayininuola (2007) of alleged complicity between board of directors and executives in Nigeria to award executives hidden compensation.

The result indicates that blockholder ownership has an insignificant positive association with executive compensation (β = 0.006; *p* = 0.249). Therefore, Hypothesis 9, which proposed a significant relationship between blockholder ownership and executive compensation, is not supported. There is therefore no support for both the alignment and expropriation hypotheses. The alignment hypothesis predicts that block shareholders have the incentives to do adequate monitoring of the executives to prevent them from exhibiting opportunistic behaviour. On the other hand, the expropriation hypothesis posits that block shareholders will use their power of control to align with the managers to extract private benefits (Shleifer & Vishny, 1986; Young *et al.*, 2008).

This result is similar to Chalmers *et al.* (2006) and Lee (2009). For example, Chalmers *et al.* (2006) find that blockholders ownership is not a determinant of executive compensation. Lee (2009) also documents that ownership concentration is not a strong determinant of performance-pay component of executive compensation in Australia and Singapore. However, there are previous studies that show negative relationship between executive compensation and different classes of block shareholders from different institutional settings (Becker *et al.*, 2011; Chhaochharia *et al.*, 2012; Cheng & Firth, 2005; Firth *et al.*, 2007; Khan *et al.*, 2005; Ozkan, 2007). For example, Firth *et al.* (2007) document a statistically negative relationship between large outside shareholders and executive compensation in China. With evidence from Hong Kong, Cheng and Firth (2005) report a negative relationship that is statistically significant between large directors' shareholders and executive compensation. Ozkan (2007) finds a significant negative relationship between institutional ownership concentration and executive compensation in UK. Khan *et al.* (2005) find a

significant negative relationship between large institutional shareholders and executive compensation in the US.

In contrast, other studies find a positive relationship between blockholder ownership and executive compensation, providing support for the expropriation hypothesis (David *et al.* 1998; Shin & Seo, 2011). It is reported that several NLCs have controlling shareholders and such concentration is in a few hands (ROSC, 2008; Sanda *et al.*, 2011). The data for this study indicates that a good number of the block shareholders are local and foreign institutional investors who often disposed of their shares during the study period. Thus, the explanation for the insignificant result is that the block shareholders were short term investors that do not have incentives to do proper monitoring of managerial activities (Kim, 2010). Another key explanation for this result is the difficulty in identifying the real owners of shares in Nigerian companies because of lack of transparency in ownership disclosure (ROSC, 2008). In situations that the block shareholders are pressure sensitive and are likely to use their power of control to extract private benefits (David *et al.*, 1998) they may not have the incentives to constrain the CEO from extracting higher compensation.

The findings shown in Table 5.17 indicate a statistically significant negative relationship between MNCs ownership and executive compensation at 1% level (β = -0.018; p = 0.002). This result therefore suggests that increase in percentage shareholdings by multinational companies will lead to lower executive compensation. This result supports the expectation of Hypothesis 10 that predicts a negative relationship between MNCs ownership and executive compensation. This is consistent with the view of the agency theory that shareholders with substantial

ownership have incentives to constrain executives from exhibiting opportunistic behaviour (Filatotchev & Wright, 2011). It supports the assertion that MNCs are interested in the control of their foreign subsidiaries (Gatignon & Anderson, 1988). It is also consistent with the finding that MNCs influence the design of the executive compensation of their foreign subsidiaries (Le *et al.*, 2013). This could also be an indication that headquarters of MNCs are involved in the design of executive compensation for their subsidiaries in Nigeria. Fey and Furu (2008) suggest that design of executive compensation for the subsidiary could be an interest alignment mechanism between the MNCs and their foreign subsidiaries that encourages knowledge sharing within the group.

5.5.3 Control Variables of Executive Compensation

The results in Table 5.17 indicate an insignificant positive relationship between company performance and executive compensation ($\beta = 0.287$; $p = 0.283$). The result shows that company performance does not determine the level of executive compensation in NLCs. This may be an indication that CEOs in NLCs are more likely to decouple their pay from company performance. There is no support for the argument of the agency theory for a link between company performance and executive compensation. This result is consistent with Tien *et al.* (2013) who investigated the influence of CEO power on company performance through CEO compensation in computer industry in the US. Further, it is similar to Munisi and Mersland (2013) who documented that company performance does not have any association with board compensation.

The insignificant relationship between company performance and executive compensation could be attributed to concentrated ownership structure in Nigeria. As indicated earlier, several of the listed companies in Nigeria have controlling shareholders, these shareholders interest may diverge from those of the minority shareholders as they may have other private benefits they extract from the companies. It could also be that the CEOs have friendly boards that may not be inclined to sanction them for poor performance. For example, the finding of this study shows that the directors' ownership is associated with higher executive compensation. Conclusively, this finding aligns with past research that company performance accounts for less than 5% of the variation in executive compensation (Tosi *et al.*, 2000). This result however contradicts Sakawa *et al.* (2012) that document a positive relationship between company performance and short-term incentives component of executive compensation. It is also inconsistent with Ozkan (2011) who finds a significant positive relationship between company performance and CEO compensation.

As shown in Table 5.17, this study finds a significant positive relationship between company size and executive compensation at 5% level ($\beta = 0.413$; $p = 0.021$). The implication is that CEOs of large companies receive higher compensation and is a confirmation of managerial talent hypothesis which posits that large companies require managers with skills and talent to manage them successfully which in turn attracts higher pay (Albuquerque *et al.*, 2013; Cremers & Grinstein, 2014; Falato *et al.*, 2015; Gabaix & Landier, 2008; Hubbard, 2005; Terviö, 2008). The result is similar to Reddy *et al.* (2015) which provide evidence of a positive relationship between company size and executive compensation. In addition, it also supports the

finding of Tien *et al.* (2013) which indicates that managers of large companies receive higher compensation. It can therefore be summarized that the size of the company is a strong determinant of executive compensation in Nigeria. This is because large size companies show the extent of complexity that the manager has to cope with.

The result shows there is no significant relationship between leverage and executive compensation ($\beta = 0.139$; $p = 0.723$) indicating that creditors are not inclined to monitor compensation paid to CEOs in NLCs. This finding is consistent with the report by Reddy *et al.* (2015) that leverage is not associated with the level of CEO pay in New Zealand. The result also supports Munisi and Mersland (2013) who document that there is no association between leverage and board compensation. Accordingly, the level of debt in NLCs does not determine the level of executive compensation. The explanation for this finding could be that the debt covenant does not place such monitoring duty on the creditors. Another plausible explanation is that the creditors could be in business relationship with the company.

The result shows a significant negative relationship between sales growth and executive compensation at 1% level ($\beta = -0.161$; $p = 0.000$). This shows that CEOs of growth companies receive lower compensation. This could be an indication that such sales growth does not add commensurate value to the shareholders wealth as it does not translate to increase in shareholder value. For example, from Table 5.4, the average sales growth of 13.50% translates to ROA of 11.10%. This result is not consistent with Tien *et al.* (2013) that report an insignificant relationship between sales growth and CEO short term pay on one hand, and a significant positive relationship between sales growth and CEO long-term pay and CEO total pay on the

other hand. It also contrasts the report by Munisi and Mersland (2013) that document an insignificant relationship between sales growth and board compensation.

5.6 Robustness Checks

The robustness tests conducted to verify the consistency of the main regression research findings are contained in this section.

5.6.1 Split Sample before and after the introduction of the CG Code 2011

Table 5.18 shows the result of fixed-effects panel regressions (with robust option) for executive compensation for the split sample before and after the introduction of the CG Code 2011. The adjusted R^2 for the PreCG period is 0.003 indicting that 0.30% of the variations in executive compensation can be explained for in the model. The F-statistics of 28.87 at 1% significance means that there is at least one variable in the model that explains variation in executive compensation during the period. For the PostCG period the adjusted R^2 is 0.2620 with an F-statistics of 581.84 at 1% significant level.

The linear specification is used for analysis as there was no evidence of inverted U relationship for MNCs ownership with executive compensation for the split sample before and after the publication of the CG Code 2011. The independent compensation committee variable shows significant positive relationship with executive compensation during the PreCG period at 1% level ($\beta = 0.229$; $p = 0.008$). This provides support for Hypothesis 6. All other board attribute variables produced insignificant relationship with executive compensation during the sample period before the publication of the CG Code 2011. There is no support for Hypotheses 1, 2,

4, and 5. This result remains consistent with that obtained for the full sample as discussed earlier.

For the ownership structure variables, the result does not provide support for Hypothesis 7, indicating that CEO ownership does not affect executive compensation before the introduction of the CG Code 2011. There was a significant positive relationship between directors' ownership and executive compensation (β = 0.556; *p* = 0.000) prior to the introduction of the CG Code 2011. This is consistent with the full sample result. This finding provides support for Hypothesis 8 and shows that directors in NLCs align with the interest of the managers to the disadvantage of the shareholders by rewarding the CEO with higher compensation. There is support for Hypothesis 9 as the blockholder ownership shows a significant positive relationship with executive compensation at 10% level (β = 0.013; *p* = 0.063) supporting the expropriation hypothesis and the principal-principal problem (Young *et al*., 2008). The result conflicts with the prediction of Hypothesis 10 as MNCs ownership was not significant during the PreCG Code 2011 period (β = -0.006; *p* = 0.813). For the control variables, none of them shows any significant relationship with executive compensation during the PreCG period.

As shown in Table 5.18, Wald test indicates that both the board attribute variables and ownership structure variables are jointly significant in explaining variation in executive compensation at 1% in NLCs before the introduction of the CG Code 2011. After excluding the directors' ownership variable the Wald test for joint significance of the ownership structure variables lost its significance implying that the earlier joint significance result was attributable to directors' ownership.

The results in Table 5.18 show that all the board attribute variables during the PostCG period produced insignificant relationship with executive compensation indicating that they do not have effects in the determination of executive compensation after the publication of the CG Code 2011. There is therefore no support for hypotheses 1, 2, 4, 5, and 6. This suggests that the board was not effective in the discharge of its monitoring duties in constraining the CEO from extracting higher compensation as the board remained indifferent. During this period, hypotheses 7, 8, and 9 were also not supported as CEO ownership, directors' ownership, and blockholder ownership show insignificant relationship with executive compensation while the coefficient on MNCs ownership is negative and statistically significant at 10% (β = -0.046; p = 0.055) lending support for the prediction of Hypothesis 10 that there is a negative relationship between MNCs ownership and executive compensation in NLCs. After the publication of the CG Code 2011, MNCs ownership constrained the CEO from extracting higher compensation. This is consistent with the finding of Chhaochharia and Grinstein (2009) that report a decrease in executive compensation after the publication of new regulatory requirement in the US. For the control variables, consistent with the full sample result growth is negatively related to executive compensation at 1% level (β = -0.196; p = 0.000). All the other variables show estimates that are statistically insignificant.

Table 5.18

Fixed-Effects Panel Regressions (with robust option) for Executive Compensation

Variables	PreCG			PostCG		
	Coef.	t-stat	*p*-value	Coef.	t-stat	*p*-value
Constant	9.375	1.630	0.110	3.234	0.280	0.784
Board Attributes						
BDS	-0.003	-0.060	0.951	0.022	0.490	0.630
BDC	-0.243	-0.520	0.603	0.438	0.660	0.511
CEOD[a]	--	--	--	--	--	--
GEND	-0.103	-0.170	0.866	0.533	0.980	0.332
CCOM	0.020	0.180	0.857	0.198	1.370	0.177
CCINDP	0.229***	2.770	0.008	-0.171	-1.400	0.169
Ownership Structure						
CEOO[b]	-0.526	-0.300	0.768	0.488	1.250	0.219
DIRO	0.556***	4.410	0.000	1.080	1.410	0.165
BLKO	0.013*	1.910	0.063	-0.004	-0.830	0.410
MNCO	-0.006	-0.240	0.813	-0.046*	-1.970	0.055
Control Variables						
ROA	0.288	0.240	0.808	0.509	1.040	0.306
SIZE	0.016	0.040	0.966	0.446	0.720	0.477
LEV	0.101	0.100	0.923	-0.910	-0.910	0.370
GRT	0.083	0.580	0.565	-0.196***	-7.710	0.000
IND[c]	--	--	--	--	--	--
N	129			86		
Adjusted R^2	0.0031			0.2620		
F-value	28.87***			581.84***		

Wald Test for the Joint Significance: PreCG	Board Attributes	F-Statistics	4.57***
		(*p*-value)	(0.002)
	Ownership Structures	F-Statistics	5.09***
		(*p*-value)	(0.002)
Wald Test for the Joint Significance: PostCG	Board Attributes	F-Statistics	0.84
		(*p*-value)	(0.532)
	Ownership Structures	F-Statistics	9.03***
		(*p*-value)	(0.000)

***, **, * Significant at 1%, 5%, and 10% level respectively.

Notes: a, CEOD was eliminated in STATA because of collinearity.

b, When EXDIRO was entered into the equation as substitute for CEOO, the result remained qualitatively similar.

c, IND was eliminated in STATA because of collinearity.

Wald test indicates that the board attribute variables are jointly insignificant in explaining variation in executive compensation. The Wald test however shows that ownership structure variables are jointly significant at 1% in explaining variation in executive compensation in NLCs. After excluding MNCO from the ownership structure variables, the Wald test turned insignificant supporting the result that MNCO inclusion was the reason for the joint significance of the ownership structure variables earlier reported.

This finding shows that there was no improvement in the relationship between executive compensation and board attributes in NLCs after the publication of the CG Code 2011. Rather, the board attributes that were jointly significant during the PreCG period lost this significance during the PostCG period. The ownership structure variables remained jointly significant during both periods. Board attribute variables (BDS, BDC, GEND, and CCOM) are found to have insignificant relationship with executive compensation for the PreCG and PostCG samples. This is consistent with the univariate test where the result fails to show any significant difference between the two periods and also with the full sample result in Tables 5.13 and 5.17 respectively.

Directors' ownership variable indicates a positive relationship with executive compensation at significant level for PreCG period, but at an insignificant level for the PostCG period. This implies that the CG Code 2011 could have influenced the decision of directors' shareholders to change their disposition towards executive compensation matters. Another variable, the MNCs ownership shows a significant decrease in executive compensation after the introduction of the CG Code 2011

compared to the insignificant relation during the PreCG period. This suggests that the CG Code 2011 has stirred the MNCs to ensure that CEOs do not earn undeserved compensation to the detriment of the shareholders unlike their indifferent attitude during the PreCG period. The result shows that the blockholders ownership that was associated with higher executive compensation during the PreCG period became indifferent during the PostCG period. In contrast, CEO ownership is found not to be statistically insignificant for both periods.

5.6.2 Split Sample for Multinational Companies and Domestic Companies

Table 5.19 shows the result of fixed-effects panel regressions (with robust option) for executive compensation for the split sample for MNCs and DCOMs separately. The adjusted R^2 for the MNCs is 0.1606 indicating that 16.06% of the variations in executive compensation can be explained for in the model. The F-statistics of 253.35 at 1% significance means that there is at least one variable in the model that explains variation in executive compensation during the period. For the DCOMs the adjusted R^2 is 0.1785 with an F-statistics of 5.15 at 1% significant level. For MNCs, the regression result shows that board size, board composition, gender diversity, and compensation committee do not have any influence on executive compensation. Hypotheses 1, 2, 4, and 5 are thus not supported. However, executive compensation increases in relation to independent compensation committee at 5% level ($\beta = 0.301$; $p = 0.026$). This finding remains consistent with the full sample results on board attributes that supports the prediction of Hypothesis 6. This shows that the compensation committee remains ineffective in constraining the CEO from extracting higher compensation even with its independent status.

Table 5.19

Fixed-Effects Panel Regressions (with robust option) for Executive Compensation

Variables	MNCs			DCOMs		
	Coef.	t-stat	*p*-value	Coef.	t-stat	*p*-value
Constant	0.659	0.130	0.894	0.418	0.150	0.881
Board Attributes						
BDS	0.071	1.310	0.210	0.018	0.560	0.583
BDC	-0.395	-0.520	0.612	-0.114	-0.200	0.842
CEOD[a]	--	--	--	--	--	--
GEND	1.206	1.000	0.333	-0.010	-0.020	0.983
CCOM	0.003	0.020	0.985	0.038	0.420	0.678
CCINDP	0.301**	2.460	0.026	0.104	1.010	0.322
Ownership Structure						
CEOO[b]	0.852	1.250	0.229	2.108	0.830	0.417
DIRO	2.006	1.280	0.217	0.395***	2.920	0.007
BLKO	0.030***	3.080	0.007	0.001	0.300	0.768
Control Variables						
ROA	1.085	0.670	0.515	0.191	0.810	0.426
SIZE	0.421	1.520	0.148	0.537***	3.740	0.001
LEV	1.231	1.010	0.328	-0.083	-0.220	0.831
GRT	-0.153***	-3.290	0.005	-0.208**	-2.360	0.026
IND[c]	--	--	--	--	--	--
N	83			132		
Adjusted R^2	0.1606			0.1785		
F-value	253.35***			5.15***		
Wald Test for the Joint Significance: MNCs	Board Attributes		F-Statistics (*p*-value)	4.64*** (0.008)		
	Ownership Structures		F-Statistics (*p*-value)	9.16*** (0.001)		
Wald Test for the Joint Significance: DCOMs	Board Attributes		F-Statistics (*p*-value)	0.78 (0.573)		
	Ownership Structures		F-Statistics (*p*-value)	5.41*** (0.005)		

***, **, * Significant at 1%, 5%, and 10% level respectively.

Notes: a, CEOD was eliminated in STATA because of collinearity.

b, When EXDIRO was entered into the equation as substitute for CEOO, the result remained qualitatively similar.

c, IND was eliminated in STATA because of collinearity.

The CEO ownership and directors' ownership do not have significant relationship with executive compensation and so fails to support Hypotheses 7 and 8 respectively. The study finds that executive compensation increases with the proportion of shares held by block shareholders. This relationship is significant at 1% level ($\beta = 0.030$; $p = 0.007$). The blockholder ownership finding indicates that the block shareholders may be in business relationship with the company that will make them align their interest with those of the managers to expropriate the minority shareholders. For the control variables of executive compensation, company performance, company size, and leverage show insignificant relationship with executive compensation while the coefficient of sales growth is negative and statistically significant at 1%.

Wald test for the joint significance of the board attribute variables indicates they are jointly significant at 1% in determining executive compensation in NLCs. The ownership structure variables also are jointly significant in determining executive compensation at 1% level.

The regression result for domestic companies shows that none of the board attribute variables is a determinant of executive compensation. There is therefore no support for Hypotheses 1, 2, 4, 5, and 6. This result was further confirmed with the Wald test for joint significance that returned insignificant results for board attribute variables. This result is consistent with the argument by Boubakri *et al.* (2005) that the inability of emerging economies to institute functional institutions will inhibit good corporate governance mechanism. The result supports the contention that the Anglo-American corporate governance system may not after all be good for emerging countries from Africa. For instance, Rwegasira (2000) suggested a combination of the Anglo-

American corporate governance system and the Germany-Japan model for Africa. Under the ownership structure variables, CEO ownership and blockholder ownership do not have significant relationship with executive compensation. Therefore, Hypotheses 7 and 9 respectively are not supported. Directors' ownership indicates a significant positive relationship with executive compensation at 1% ($\beta = 0.395$; $p = 0.007$). Hypothesis 8 is supported as it predicts a significant relationship between the variables. For the control variables of executive compensation, company performance and leverage do not affect executive compensation and this is consistent with the result of the full sample. Similar to the full sample results, company size and sales growth show significant effect in determining executive compensation.

The Wald test of joint significance for MNCs shows that the board attributes are jointly significant in determining executive compensation in NLCs but they are not jointly significant for DCOMs. The result shows further that the ownership structure variables were jointly significant in determining executive compensation for both MNCs and DCOMs. There is no evidence from both the MNCs and DCOMs of any significant relationship between company performance and executive compensation. This suggests that they may not likely take performance into consideration when deciding on the executive compensation policy of the company. This is evident from the annual reports as none of the companies disclosed its executive compensation policy statement. Furthermore, the finding indicating no significant relationship between executive compensation and leverage for both MNCs and DCOMs implies that regardless of the companies' major shareholder, debt holders do not influence executive compensation in a significant way.

5.6.3 Results for OLS Firm-Level Fixed Effects Regression

The result for OLS firm-level fixed effects regression is presented in Table 5.20. It does not support Hypothesis 1 as board size shows insignificant relationship with executive compensation (β = 0.010; *p* = 0.809). Contrary to the prediction of Hypothesis 2, the study finds an insignificant relationship between board composition and executive compensation (β = -0.639; *p* = 0.353). There is no support for Hypothesis 3 as CEO duality shows insignificant relationship with executive compensation (β = -0.212; *p* = 0.761). This variable was earlier omitted due to collinearity under the fixed effects regression model. The result shows insignificant positive relationship between gender diversity and executive compensation (β = 1.558; *p* = 0.109) and as such Hypothesis 4 is equally not supported. Contrary to Hypothesis 5, this study finds an insignificant relationship between compensation committee and executive compensation (β = -0.119; *p* = 0.623). This is consistent with the result in Table 5.17 that documents an insignificant relationship between compensation committee and executive compensation.

Hypothesis 6 is supported as independent compensation committee shows a significant positive relationship with executive compensation at 5% level (β = 0.523; *p* = 0.037). This is similar to the result obtained under the main regression result. None of the ownership structure variables shows a significant relationship with executive compensation. There is therefore no support for hypothesis 7, 8. 9 and 10. For the control variables, company performance, company size, growth, and industry all indicate significant relationships with executive compensation while leverage shows an insignificant relationship.

Table 5.20
OLS Firm-Level Fixed Effects Regression of LnCOMP (with cluster-robust standard error)

	Coef.	t-stat	p-value
Constant	3.038**	2.020	0.050
Board Attributes			
BDS	0.010	0.240	0.809
BDC	-0.639	-0.940	0.353
CEOD	-0.212	-0.310	0.761
GEND	1.558	1.640	0.109
CCOM	-0.119	-0.500	0.623
CCINDP	0.523**	2.150	0.037
Ownership Structure			
CEOO[a]	0.599	0.230	0.816
DIRO	0.294	0.320	0.754
BLKO	0.003	0.530	0.601
MNCO	-0.003	-0.690	0.497
Control Variables			
ROA	1.019*	1.850	0.071
SIZE	0.418***	4.370	0.000
LEV	-0.387	-0.690	0.497
GRT	-0.460***	-7.650	0.000
IND	-0.875*	-1.780	0.082
N	215		
Adjusted R^2	n.a		
F-value	n.a		

n.a , not available

***, **, * Significant at 1%, 5%, and 10% level respectively.

Note: a, When EXDIRO was entered into the equation as substitute for CEOO, the result remained qualitatively similar.

In summary, gender diversity that was not significant in the main regression has now turned significant at the 10% level with positive coefficient. CEO duality that was earlier omitted from the regression now shows an insignificant relationship with executive compensation with a negative coefficient. On the ownership structure variables, directors' ownership and MNCs ownership that were significant under the main regression have now turned insignificant. These findings imply that some of the

corporate governance variables are sensitive to methodology adopted to correct for heteroscedasticity and firm level fixed effects while others are not.

5.6.4 Substituting Blockholders and Multinational Companies Presence for their Percentage Shareholdings

In Table 5.21, the presence of block shareholders and MNCs is substituted for their percentage shareholdings. Their presence is measured as an indicator variable where '1' indicates their presence and '0' otherwise. The result remains qualitatively similar to the main regression results. The board attribute variables show insignificant relationship with executive compensation except for independent compensation committee that remains positively significant at 5% level. CEO ownership remains insignificant while the directors' ownership remains significant similar to the main regression results. The presence of block shareholders shows significant positive relationship at 5% compared to the insignificant result reported for their percentage holding. There is thus evidence that the presence of block shareholders have influence on executive compensation which contrasts with the finding on the proportion of their shareholdings in NLCs. The results also show that the presence of MNCs is negatively associated with executive compensation in NLCs similar to the results obtained for their percentage shareholdings. The effect of the control variables on executive compensation is similar to that of the main regression results.

Table 5.21
Fixed-Effects Panel Regressions (with robust option) for Executive Compensation After substituting Blockholders and MNCs Presence for their Percentage Shareholdings

Variables	Coef.	t-stat	p-value
Constant	2.320	0.800	0.430
Board Attributes			
BDS	0.025	1.020	0.316
BDC	-0.568	-1.010	0.318
CEOD[a]	--	--	--
GEND	0.144	0.290	0.776
CCOM	0.033	0.410	0.687
CCINDP	0.162**	2.180	0.035
Ownership Structure			
CEOO[b]	1.409	1.340	0.186
DIRO	0.457**	2.390	0.021
BLKO	0.200**	2.200	0.034
MNCO	-0.480***	-5.410	0.000
Control Variables			
ROA	0.357	1.290	0.203
SIZE	0.432**	2.680	0.011
LEV	0.167	0.430	0.671
GRT	-0.170***	-4.730	0.000
IND[c]	--	--	--
N	215		
Adjusted R^2	0.1778		
F-value	n.a.		

***, **, * Significant at 1%, 5%, and 10% level respectively. n.a. (Not Available)

Notes: a, CEOD was eliminated in STATA because of collinearity.

b, When EXDIRO was entered into the equation as substitute for CEOO, the result remained qualitatively similar.

c, IND was eliminated in STATA because of collinearity.

5.6.5 Regression Results After Excluding Banks

Next, the study ran another regression after excluding the financial services sector (banks) observations to determine whether their presence have influence on the earlier result. The result is shown in Table 5.22. Previous studies have excluded the

financial sector from their study sample (Firth *et al.*, 2007) while others have studied the banks separately (Hubbard & Palia, 1995). The argument underlying such separation is that the banks are regulated compared to other sectors of the economy.

Table 5.22
Fixed-Effects Panel Regressions (with robust option) for Executive Compensation After Excluding the Banks

Variables	Coef.	t-stat	*p*-value
Constant	3.764	1.160	0.255
Board Attributes			
BDS	0.013	0.350	0.729
BDC	-0.422	-0.620	0.537
CEOD[a]	--	--	--
GEND	0.478	1.090	0.282
CCOM	0.084	1.100	0.277
CCINDP	0.148*	1.840	0.075
Ownership Structure			
CEOO[b]	0.310	0.550	0.585
DIRO	1.286***	2.76	0.009
BLKO	0.017***	3.020	0.005
MNCO	-0.015**	-2.700	0.011
Control Variables			
ROA	0.302	1.140	0.260
SIZE	0.348*	1.840	0.074
LEV	0.141	0.330	0.742
GRT	-0.151***	-3.740	0.001
N	180		
Adjusted R^2	0.2212		
F-value	7.97***		

***, **, * Significant at 1%, 5%, and 10% level respectively.

Notes: a, CEOD was eliminated in STATA because of collinearity.

b, When EXDIRO was entered into the equation as substitute for CEOO, the result remained qualitatively similar.

The study results remain qualitatively similar to the full sample regression except for the addition that blockholder ownership is now significantly positively related to executive compensation. This suggests that the banks and other sectors in the Nigeria

Stock Exchange are isomorphic on matters that relate to executive compensation and corporate governance variables.

5.6.6 Examination of Sector Effect on Executive Compensation

Another potential factor that may likely influence the level of executive compensation is industry classification. Murphy (1999), Reddy *et al.* (2015), and Yermack (1995) argue that industry classification has influence on the level of executive compensation. The result is shown in Table 5.23. Under the fixed-effects regression model, the industry dummy variables are deleted because they are constant across time. Therefore, as a robustness test, following Reddy *et al.* (2015) and Yermack (1995), this study uses the random-effects model to examine the industry effects on the level of executive compensation. The finding indicates that all the sectors except financial services and agriculture show significant association with executive compensation. The consumer sector has the highest coefficient of 2.084 while the lowest coefficient of 0.751 is from the conglomerates sector.

This result indicates that industry classifications explain variations in executive compensation in Nigeria. This is consistent with the findings shown in Table 5.2 and prior studies that find evidence that executive compensation level differs across industries (Reddy *et al*., 2015; Yermack, 1995). It should be noted that the Wald chi2 (Wald $\chi^{2)}$ and F-value were omitted from the random-effects regression. The implication of this finding is that fixed-effects model controls for unobserved heterogeneity among companies and not just for industry sectors and as such the random effects model may not be appropriate. Therefore, the result of entering the industry classification one at a time in the random-effects regression is not presented.

Table 5.23

Fixed-Effects Panel Regressions (with robust option) for Executive Compensation After Including all the Sectors

	Fixed Effects			Random Effects		
Variables	Coef.	t-stat	*p*-value	Coef.	z-stat	*p*-value
Constant	2.933	0.94	0.350	1.069	0.57	0.569
Board Attributes						
BDS	0.020	0.84	0.407	0.021	0.93	0.350
BDC	-0.564	-0.96	0.344	-0.626	-1.09	0.275
CEOD[a]	--	--	--	-1.062**	-2.05	0.040
GEND	0.102	0.21	0.835	0.303	0.64	0.524
CCOM	0.030	0.40	0.693	0.017	0.20	0.839
CCINDP	0.169**	2.23	0.031	0.212**	2.49	0.013
Ownership Structure						
CEOO	1.558	1.46	0.152	1.573	1.63	0.102
DIRO	0.474***	2.77	0.008	0.370	1.43	0.153
BLKO	0.006	1.17	0.249	0.002	0.54	0.588
MNCO	-0.018***	-3.36	0.002	-0.007	-1.48	0.139
Control Variables						
ROA	0.287	1.09	0.283	0.314	1.24	0.213
SIZE	0.413**	2.39	0.021	0.430***	3.96	0.000
LEV	0.139	0.36	0.723	0.016	0.05	0.962
GRT	-0.161***	-4.20	0.000	-0.170***	-5.74	0.000
Sectors						
CONSUMER[b]	--	--	--	2.084***	7.19	0.000
SERVICES[c]	--	--	--	1.753***	5.26	0.000
CONGLOMERATES[d]	--	--	--	0.751**	2.18	0.029
INDUSTRIAL GOODS[e]	--	--	--	1.891***	8.23	0.000
OIL & GAS[f]	--	--	--	1.580***	3.28	0.001
CONSTRUCTION[g]	--	--	--	2.048***	6.17	0.000
FIN. SERVICES[h]	--	--	--	0.508	0.73	0.464
AGRICULTURE[i]	--	--	--	--	--	--
N	215			215		
Adjusted R^2	0.1820					
F-value	7.78***			n.a.		
Wald χ^2				n.a.		

***, **, * Significant at 1%, 5%, and 10% level respectively.

Notes: a, CEOD was eliminated in STATA because of collinearity.

b c, d, e, f, g, h, and i were eliminated in STATA because of collinearity.

5.7 Summary of the Chapter

This chapter presents the empirical results of the relationship between executive compensation and corporate governance characteristics that include the board attributes and ownership structure variables from companies quoted on the NSE during the period 2009 to 2013. The main objective of this study is to examine whether the Anglo-American corporate governance system is appropriate for constraining higher executive compensation from an emerging economy like Nigeria given the low investor protection rights and weak enforcement and compliance mechanism that obtains in the country. Executive compensation is proxied by the highest paid director as NLCs do not provide details of executive compensation components such as salary and bonuses, share options, long-term incentives, and pensions. Further, the compensation of the directors is not disclosed on an individual basis. This study provides new evidence of the influence of MNCs foreign subsidiaries in constraining the managers from extracting higher compensation.

Univariate analysis is used for examining the extent of executive compensation practice in Nigeria, while multivariate analysis is used to examine the study's hypotheses. Several robustness checks were conducted and compared to the main regression results to test its validity. The univariate analysis shows significant difference in executive compensation between the PreCG and PostCG periods, but there was no evidence of any difference between MNCs and DCOMs executive compensation. The executive compensation was higher for PostCG period compared to the PreCG period. This supports the view of the ineffectiveness of the new code to address the executive compensation matters in NLCs.

The findings indicate that board size, board composition, CEO duality, gender diversity, and the presence of a compensation committee do not constrain CEOs from extracting higher compensation as there were insignificant relationships between them. In contrast to the expectation of the agency theory, independent compensation committee is found to be associated with higher compensation. On the overall, the board attribute variables do not satisfy the effective monitoring argument put forward for their establishment. Directors' shareholders are found to align with the managerial interests, while CEO ownership and blockholders ownership are found to have no influence on the level of executive compensation. The result however shows that MNCs ownership serves as an effective monitoring mechanism for constraining managers from extracting higher compensation.

The robustness checks show consistency with the main results especially when the banks were excluded from the full sample. The result is however sensitive to the methodology adopted as the OLS company-level fixed effects model result is not very much similar to the main results. All the ownership structure variables became insignificant, while only gender diversity shows positive relationship with executive compensation from the board attribute variables. The publication of the CG Code 2011 does not seem to make any significant impact on executive compensation as indicated in the regression results for the PostCG period. Except for the MNCs share ownership that shows association with lower executive compensation, all other independent variables show insignificant relationship with executive compensation. This provides evidence of weakness in the CG Code even though it was crafted to address the perceived weakness of the CG Code 2003.

This study has been able to provide evidence for the main research objective to show that Anglo-American corporate governance system may not likely be appropriate for an emerging economy like Nigeria considering country specifics like low investor protection rights, weak institutional frameworks, weak enforcement and compliance mechanism (Okike, 2007; ROSC, 2008, 2011). The new variable (MNCs ownership) introduced into the study however shows that it is an effective mechanism for constraining higher executive compensation. Finally, the next chapter presents the summary and conclusions of the study.

CHAPTER SIX

SUMMARY AND CONCLUSION

6.0 Introduction

The summary and conclusion of the study are presented in this final chapter of the thesis. The study sets out to examine how corporate governance characteristics influence the determination of executive compensation in companies quoted on the NSE. The underlying assumption of the Anglo-American corporate governance model that is operational in Nigeria is the promotion of the shareholders interest. The CG Code 2011 in promoting good corporate practice recommends that the board of directors be comprised of more outside directors and wholly outside directors' compensation committee. However, Nigeria, as an emerging economy is fraught with low investor protection rights, weak institutions and weak enforcement mechanisms that may render its corporate governance system ineffective. The remainder of the chapter is structured as follows: Section 6.1 focuses on the summary of the study. The implications of the findings are presented in section 6.2, while the limitation of the study is discussed in section 6.3. Section 6.4 presents the suggestions for further research and section 6.5 concludes the chapter.

6.1 Summary of the Study

It is argued that corporate governance practice and executive compensation are internal mechanisms for mitigating the agency conflict that exists between shareholders and managers in large complex organizations because of the separation of ownership and control (Connelly *et al.*, 2010; Core *et al.*, 1999; Duffhues & Kabir, 2008; Jensen & Meckling, 1976; Munisi & Mersland, 2013; Ozdemir & Upneja,

2012). It is further argued that investors are willing to make their investments at a premium in properly governed companies (Stanwick, 2008). ASX (2014) notes that investors show keen interest on executive compensation matters. For corporate governance mechanism to mitigate the agency conflict it has to be strong, and executive compensation should be optimally contracted. The effectiveness of the corporate governance practice and executive compensation in mitigating the agency conflict remains an issue among company stakeholders whether from developed or emerging economies.

However, weak corporate governance practice in companies is shown to be associated with greater agency problems (Core *et al.*, 1999) and it is argued that excessive executive compensation is exacerbating the agency conflict (Bebchuk & Fried, 2003). Nevertheless, past studies have found that corporate governance characteristics have influence on the executive compensation practice of companies even though with conflicting results (Anderson & Bizjak, 2003; Boivie *et al.*, 2012; Chhaochharia & Grinstein, 2009; Conyon & He, 2011; Core *et al.*, 1999; Fernandes, 2008; Lam *et al.*, 2013; Ozkan, 2007; Tien *et al.*, 2013; Van Essen *et al.*, 2015; Yermack 1996). This study extends this research by examining the influence of corporate governance practice by companies in Nigeria, a country that is quite different from the developed markets, on executive compensation, measured as the highest paid director. Without prior research on Nigeria, this study seeks to empirically examine whether corporate governance characteristics constrain CEOs from extracting excessive compensation in NLCs.

The data for the study was manually extracted from the annual reports of forty-three NLCs from 2009 to 2013 (comprising a total of 215 company-year observations). Unlike previous empirical studies that grouped all companies together in country studies, for robustness checks, this study separates the MNCs from the DCOMs. This separation enables an examination into how corporate governance practice affects executive compensation in MNCs separately from DCOMs. This distinction is important as MNCs have been identified as playing significant roles in Nigeria's economy, in addition to the obvious that they belong to a group of internationally recognised companies. Further distinction was made between the PreCG and PostCG periods. This enables an assessment of the influence of the CG Code 2011 on corporate governance and executive compensation practice. The focus of this study is the concern as to the effectiveness of the board of directors and ownership structure (especially MNCs ownership) in constraining executives from extracting higher compensation. It is argued that board attributes and ownership structure are determinants of executive compensation (Ben Hassen *et al.*, 2015). An understanding of these mechanisms will assist in assessing their effectiveness in monitoring management actions.

As a recap, this study has three main objectives that are restated below. The first objective is to examine the extent of executive compensation practice in NLCs. The second objective is to examine the influence of board attributes (board size, board composition, CEO duality, gender diversity, compensation committee, and independent compensation committee) in determining executive compensation. The third objective is to examine the relationship between ownership structure (CEO ownership, directors' ownership, blockholders ownership and MNCs ownership) and

executive compensation. Two groups of hypotheses were developed to examine the influence of corporate governance characteristics on executive compensation. The first group with six hypotheses examined the relationship between board attributes and executive compensation, while the second group with four hypotheses focused on the relationship between ownership structure and executive compensation.

In line with the objectives of the study, this study sets out to find empirical answers to the three major research questions that are restated as follows: (1) What is the extent of executive compensation practice in NLCs? (2) What is the relationship between board attributes (board size, board composition, CEO duality, gender diversity, compensation committee, and independent compensation committee) and executive compensation? (3) What is the relationship between ownership structure (CEO ownership, directors' ownership, blockholders ownership and MNCs ownership) and executive compensation?

For the first research question, descriptive and univariate analyses were conducted to provide empirical answer. The results indicate that the mean (median) executive compensation during the period is ₦35,383,870 (USD176,919) (₦23,954,000) (USD119,770) that showed an increasing trend from 2009 to 2013 for the full sample. The mean (median) executive compensation for the DCOMs is ₦34,599,360 (USD172,997) (₦22,006,500) (USD110,033), and ₦36,631,540 (USD183,158) (₦29,232,000) (USD146,160) for MNCs. The financial services sector has the highest mean executive compensation with ₦58,783,610 (USD293,918), followed by oil and gas sector with ₦44,194,200 (USD220,971). The lowest mean executive compensation of ₦2,024,800 (USD10,124) is from the agricultural sector.

The univariate result shows that there is no significant difference in executive compensation between MNCs and DCOMs. The result however indicates a significant difference in executive compensation between the PreCG and PostCG periods. There is no evidence of any of the companies providing equity-based compensation to the CEO as there is no disclosure of such in the annual reports.

Table 6.1
Summary of the Results of Hypotheses

Statement of Hypothesis		Exp. Sign	Results	
			Sign	Conclusions
H1	There is a positive relationship between board size and executive compensation.	+	+ (Not Sig)	Not Supported
H2	There is a significant relationship between outside director dominated boards and executive compensation.	?	- (Not Sig)	Not Supported
H3	There is a positive relationship between CEO duality and executive compensation.	+		
H4	There is a negative relationship between women directors and executive compensation.	-	+ (Not Sig)	Not Supported
H5	The presence of compensation committee has significant association with executive compensation.	?	+ (Not Sig)	Not Supported
H6	There is a significant relationship between independent compensation committee and executive compensation.	?	+ (Sig)	Supported
H7	There is a significant relationship between CEO ownership and executive compensation.	?	+ (Not Sig)	Not Supported
H8	There is a significant relationship between directors' ownership and executive compensation.	?	+ (Sig)	Supported
H9	There is a significant relationship between blockholders ownership and executive compensation.	?	+ (Not Sig)	Not Supported
H10	There is a negative relationship between MNCs ownership and executive compensation.	-	- (Sig)	Supported

Notes: Exp. Sign = Expected Sign, Sig = Significant, and Not Sig = Not Significant.

In answering the second research question, the regression results show that board attribute variables do not constrain the CEO from extracting higher compensation. Hypotheses 1, 2, 4, and 5 were not supported. Board size, board composition, gender diversity and compensation committee are not significant determinants of executive compensation. In fact, the independent compensation committee is associated with higher executive compensation in contrast to expectation of the agency theory. Before the publication of the CG Code 2011, the board attribute variables were not significantly related to executive compensation except the independent compensation committee variable that shows a positive relationship with executive compensation. After the publication of the CG Code 2011, none of the board attribute variables indicates any association with executive compensation. The result of Hypotheses 1, 2, 4, 5, and 6 for the MNCs only sample is qualitatively similar to that of the full sample. In all the fixed-effects regressions, the CEO duality and industry were omitted from the regression results because of collinearity. The implication of this finding is that the board attributes considered in this study do not constrain the CEO from extracting higher compensation.

For the third research question, the result indicates two of the ownership structure variables show significant association with executive compensation, while the other two variables show insignificant association with executive compensation. The MNCs ownership variable is associated with lower executive compensation by reporting a significant negative relationship with executive compensation. On the other hand, the directors' ownership shows association with higher executive compensation. The CEO ownership and blockholders ownership show insignificant relationship with executive compensation. In addition, the analysis for the PreCG and

PostCG periods show that MNCs ownership is associated with lower executive compensation after the publication of the CG Code 2011, while directors' ownership and blockholders ownership show positive significant relationship with executive compensation prior to the publication of the CG Code 2011. Out of the four ownership structure variables examined in this study, only MNCs ownership was found to constrain the CEO from extracting excessive compensation. The summary of the results of tested hypotheses is shown in Table 6.1.

6.2 Implications of the Findings

Past studies relate corporate governance characteristics with executive compensation presenting their argument from the agency theory perspective (Ben Hassen *et al.*, 2015; Conyon, 2014; Core *et al.*, 1999; Jensen & Meckling, 1976; Reddy *et al.*, 2015). The results from these studies remain equivocal and inconsistent. Boyd *et al.* (2012) and Munisi and Mersland (2013) noted that even though several studies have been conducted on corporate governance and executive compensation, there is complete absence of empirical studies from emerging economies especially from Sub-Saharan Africa. This study fills this gap. Similar to prior studies, the findings of this study suggests that past studies have neglected the impact of MNCs ownership in the determination of executive compensation of their foreign subsidiaries. This study makes important new contributions to theory, policy makers and stakeholders on corporate governance and executive compensation. It provides new insight to the influence of MNCs ownership in their foreign subsidiaries in constraining CEO from extracting higher compensation with evidence from an emerging economy. It also shows the ineffectiveness of internal corporate governance mechanisms in preventing

the CEO from exhibiting opportunistic behaviour. This could be an indication of weak corporate governance practice. This section presents the theoretical and policy implications of the findings of this study, and also discuss the implications for other company stakeholders.

6.2.1 Theoretical Implications of the Findings

For the first time, the result of this study indicates that the board of directors does not constrain the executive from extracting higher compensation in Nigeria. This contradicts the prediction of the agency theory that the board will do adequate monitoring of the manager and align his interest with those of the shareholders. The board size shows insignificant relationship with executive compensation, and as such does not provide support for the resource dependence theory that board acts as cohesive agent that bonds the interest of stakeholders to that of the executive management (Şener *et al.,* 2011). It does not also support the agency theory that board of directors as representatives of the shareholders will adequately monitor the manager and prevent him from exhibiting opportunistic behaviour (Fame & Jensen, 1983b).

The result shows an insignificant relationship between board composition and executive compensation and did not support the postulation of the agency theory that independent boards remain effective monitors of managerial actions (Fame & Jensen, 1983b). This could be an indication of managerial power influence over the board of directors that is consistent with the managerial power theory. There is no evidence of significant relationship between gender diversity and executive compensation. There is no support for the resource dependency theory that board diversity (gender

diversity) enhances effective board monitoring (Gul *et al.*, 2011). The insignificant relationship between compensation committee and executive compensation is not consistent with the agency theory. The presence of the compensation committee is expected to aid the board in designing effective executive compensation policy that will align managers' interest with those of the shareholders. Again, there is no support for the agency theory regarding the relationship between independent compensation committee and executive compensation. There is therefore no justification for an independent compensation committee as they are shown to be associated with higher executive compensation.

For the CEO ownership, the result shows that shareholding by CEO does not influence executive compensation. This result neither supports the alignment nor the expropriation hypotheses, nor is it consistent with the agency theory. The directors' ownership provides support for the expropriation hypothesis, which suggests that increased shareholdings by directors will diverge their interests from those of the shareholders. It therefore does not provide support for the prediction of the agency theory. Blockholders ownership as an effective monitoring mechanism is not supported as the result turned insignificant in relation to executive compensation. The result does not support both the alignment and expropriation hypotheses. Concerning the MNCs ownership, the result indicates that shareholding by MNCs enhances effective monitoring and prevents the CEO from extracting higher executive compensation. In Nigeria, MNCs ownership therefore serves as a substitute for effective corporate governance mechanism. This supports the argument that there is agency relationship between MNCs headquarters and their foreign subsidiaries and

that executive compensation could be a vital stimulus for mitigating the agency conflict (Roth & O'Donnell, 1996).

This study contributes to corporate governance and executive compensation theories by depicting MNCs ownership as an internal corporate governance mechanism for mitigating the agency conflict and by using the MNCs literature to explain agency relationship between MNCs and their foreign subsidiaries. MNCs exercise significant influence in the Nigerian capital market as they are recognised to control ten (10) out of the twenty (20) most capitalized companies on the NSE as at January 2013 (SECN, 2013b). It is shown that MNCs together with other foreign institutional investors controlled 81% of the total shares on the NSE as at 2011 (Anuforo, 2014). Their presence and influence in Nigeria's corporate environment cannot therefore be ignored.

6.2.2 Policy Implications of the Findings

The result of this study has several attendant implications for regulators of Nigeria's capital market. The regulatory authorities have the responsibility for ensuring adherence to good corporate practice by companies. SECN and other regulatory authorities will find the results of this study useful in drawing up future corporate governance regulatory reforms and executive compensation matters. First, under a low investor protection rights environment with weak enforcement and compliance mechanisms, the Anglo-American corporate governance model may not be sufficiently suitable for constraining the CEO from extracting excessive compensation. The regulatory authorities in Nigeria should therefore design a

corporate governance model that will adequately address the peculiarity of Nigeria's socio-economic environment.

The board does not show any evidence of effective monitoring of management as regards executive compensation matters. This suggests that the recommendations of the CG Codes have not been effective in constraining the CEO from extracting higher compensation. The efforts of SECN and other relevant agencies at strengthening the corporate governance practice in Nigeria do not seem to be yielding the desired expectations with regards to executive compensation issues. The issue of inadequate disclosure of information on executive compensation by companies needs to be properly addressed by both the SECN and the NSE.

The board size shows insignificant relationship with executive compensation. The implication is that executive compensation does not depend on whether the board size is large or small. There should therefore be an inquiry as to why the board has remained indifferent to executive compensation matters. An understanding of the reasons could assist in future corporate governance reforms considering Nigeria's peculiar environment. The result of this study does not justify the recommendation of outside director dominated board in the CG Codes as the result shows insignificant association with executive compensation. There is no evidence that the outside directors bring their experience to benefit the shareholders. There is the need to further examine the attitude of outside directors to executive compensation matters and what could be the challenge confronting the directors when designing executive compensation policy.

Gender diversity is not significantly related to executive compensation. The women directors have not shown any evidence of their presence improving the monitoring duty of the board concerning executive compensation. There may be the need for further inquiry as to ascertain the cause for their ineffectiveness in enhancing good corporate governance practice and show lower association with executive compensation. The finding indicates that the presence of the compensation committee does not constrain the CEO from extracting higher compensation and the compensation committee independence is significantly associated with higher executive compensation. This suggests that the recommendation of the CG Code 2011 for independent compensation committee has not enhanced the effectiveness of the compensation committee. It therefore becomes imperative to examine the difficulties being encountered by this committee in the discharge of its duties.

CEO ownership does not show any association with executive compensation. This suggests that CEO ownership neither aligns nor diverges his interest from those of the shareholders. There is the need to conduct a further investigation to understand this CEO behaviour. The findings show that directors' ownership is associated with higher executive compensation. This implies that directors align their interests with that of the CEO and not those of the shareholders. Further investigation needs to be carried out to ascertain the reason for this behaviour of the directors. Blockholders show indifferent attitude to executive compensation issues. This result could be an indication of expropriation of minority shareholders and requires further inquiry to determine the challenges confronting the block shareholders in constraining the CEO from extracting higher compensation.

The findings of this study indicate that the MNCs ownership is associated with lower executive compensation. This suggests that MNCs ownership in companies ensures adequate monitoring of the CEO and prevents him from exhibiting opportunistic behaviour. The regulatory authorities should therefore encourage more foreign direct investments into Nigeria through the MNCs as their share ownership substitutes for effective monitoring of managerial behaviour. This may likely lead to reduce agency problems between shareholders and managers. Further, DCOMs should be encouraged to adapt the practices from the MNCs that lead to effective monitoring of executive actions.

6.2.3 Implications of the Study for various Company Stakeholders

The results of this study would be of interest to various stakeholders that include shareholders, management, potential investors, academic researchers, and the press as it shows the inherent weakness of the corporate governance mechanism in Nigeria. For the shareholders, the study results show that the board of directors do not properly work for their (shareholders) interest. The insignificant association between board attribute variables and executive compensation indicates indifferent attitude of the board to protecting the interest of the shareholders. It provides the shareholders associations and activists basis for demanding to actually know their company directors. This is because reduced executive compensation would also mean additional company income that may likely translate to increased dividend to the shareholders.

This study results should encourage more empirical research on corporate governance and executive compensation practice in Nigeria to uncover the likely reasons for the

ineffectiveness of the board in aligning with shareholders interest. There is also the need to examine the ownership structure of NLCs so as to determine the identity of the controlling shareholders. This is because of the ROSC (2008) report that there is no transparent disclosure of shareholders in NLCs.

The findings should encourage the press to begin to show much interest in executive compensation matters by providing the public with what is considered as outrageous compensation paid to company executives. They should also investigate the corporate governance practice by companies and make the public to be aware of infractions on the part of the board and management of companies. This will sensitize the investors and put company managers on their watch.

The board of directors will find the result of this study of immense value as it provides them with evidence of ineffectiveness in performing their monitoring duties. The non-executive directors and compensation committee members should therefore be inclined to mind their reputation and show that they are representatives of the shareholders.

The literature shows that investors are willing to invest in properly governed companies at a premium and they show interest in executive compensation matters (ASX, 2014; Stanwick, 2008). The findings of this study might therefore interest them as it provides evidence of executive compensation that is non-related to company financial performance, and a board that is indifferent to executive compensation issues.

Further, optimally designed executive compensation is expected to mitigate the agency problem that exists between shareholders and managers in companies. This will in turn make the company to focus on how to benefit the society through corporate social responsibility such as charitable donations and community development projects.

6.3 Limitations of Study

This study has shown that MNCs ownership is associated with lower executive compensation, while other corporate governance characteristics indicate ineffectiveness in constraining the CEO from extracting higher compensation. Even though this study has made various contributions, it becomes imperative to state that there are also certain limitations that may engage future researchers. This section therefore presents the limitations of this study that should be taken into consideration when interpreting the findings and shows potential areas that require further examination. First, the study is limited to companies listed on the NSE, as private limited companies were excluded since they are not required to comply with the recommendation of the CG Codes. The results may therefore not be appropriate for assessing executive compensation practice among the private limited companies. Further, there is need for caution as the result cannot be generalized for other Sub-Saharan African countries because of differences in codes, legislation, and economic characteristics. In addition, the sample size of 43 companies with 215 company-year observations is considered small even though it is sufficient for statistical analysis.

Second, the highest paid director is used as proxy for executive compensation due to non availability of data on other components of CEO total compensation. The study

is therefore unable to consider other components like bonuses, stock options, long term incentives and other performance related pay. The availability of this data in the public domain could shape the behaviour of the board and provide further insights into the executive compensation issues in Nigeria. In addition, there is no effort to examine top management pay as executive compensation is not disclosed on individual basis.

Third, data from the annual report were hand collected and as such may suffer from subjectivity of the researcher even though much effort has been made to ensure objectivity. Four, no distinction is made in the outside director variable as to whether they are gray directors, independent directors, or a company's former employee. This is because some of the companies do not provide detailed profiles of their directors to enable such data. Identifying directors in their various categories have been shown to have different influence on executive compensation (Core *et al.*, 1999).

This study does not consider the CEO characteristics such as age, tenure, educational experience, and social network which have been reported to have influence in the determination of executive compensation in past studies. No attempt is made in this study to separate blockholders ownership into various components like institutional blockholders, directors' blockholders, and foreign blockholders. Inability to do this separation has the potential of affecting the generalizability of this study as blockholders have different investment objectives that in turn affect their disposition towards executive compensation issues.

6.4 Suggestions for Further Research

Research on executive compensation is of importance to academics, public, investors, press, and policy makers. The excessive compensation received by the CEOs and the decoupling of their pay from performance have attracted much interests contending that their pay should be related to performance. Investors not only have the right to know how much is being paid to the CEO from the company resources but also to make input into such pay package. The results of this study indicate that board attributes are not significant determinants (constraints) of executive compensation in NLCs similar to some of the ownership structure variables. This finding brings to question the efficacy of the Anglo-American corporate governance mechanism in an emerging economy like Nigeria where there is a low investor protection rights cum weak institutions and enforcement mechanism. There are several frontiers that this study can be improved upon. First, the study used the highest paid director as proxy for executive compensation due to unavailability of data. Additional information on executive compensation such as equity-based payments, bonuses, long-term incentives plan, and pension should be incorporated into the CEO total compensation whenever they are available to broaden the understanding on the subject matter.

Second, this study examines the influence of the presence of compensation committee on executive compensation; future studies can examine the compensation committee characteristics such as committee size, directors' experience, age, educational qualification, share ownership, and number of meetings. Third, no attempt is made in this study to separate block shareholders into various groups. Future research can take this into consideration by examining separately institutional blockholders, directors' blockholders, short term blockholders, long term blockholders, and foreign

blockholders. This study is limited only to the CEO pay, further studies can be conducted on top management team compensation once the relevant data are available in Nigeria.

6.5 Conclusion

There is no gainsaying that there is an upsurge in executive compensation and corporate governance research. The bulk of these research concentrate on the developed economies of US, UK, Australia and Continental Europe. In recent times there have been research findings from Asia but this cannot be said of Africa, particularly Nigeria that is regarded as one of the fastest growing economies in Africa. While corporate governance is gradually evolving as a separate academic discipline, executive compensation is gradually becoming a contributor to the agency problem instead of being a part of the solution as posited by the agency theorists. This is why it has attracted much of academic inquiry. The global findings remain equivocal and have left the issue largely unresolved. There are no agreed determinants of executive compensation in the literature.

This study contributes to the executive compensation literature by examining the relationship between corporate governance characteristics and executive compensation in an emerging economy like Nigeria where investor protection right is low coupled with weak compliance and enforcement mechanism (Okike, 2007, ROSC, 2008, 2011). The study shows for the first time that MNCs ownership is effective for constraining the CEO from extracting higher compensation in Nigeria. Therefore, in Nigeria where corporate governance mechanism is weak with low

investor protection rights, MNCs ownership substitutes for effective corporate governance mechanism.

The study provides evidence that board attributes do not show association with lower executive compensation, and ownership structure shows evidence of alignment with managerial interests by directors indicating that directors are entrenched in Nigeria. In Nigeria, the Anglo-American corporate governance model does not seem suitable for constraining the CEO from extracting higher compensation. In spite of the evidence that more than 68% of the directors are non-executive directors, the insignificant association with executive compensation indicates that there is still room for improvement of the CG Code. The CG Codes 2003 and 2011 do not show any improvement in corporate governance practice and executive compensation. The MNCs are isomorphic with the DCOMs as there is not much difference in their board attributes and executive compensation. The implication of the findings of this study is that the board of directors is not effective in monitoring the executives and aligning their compensation with shareholders interest.

The accompanying challenge is to the regulatory authorities in Nigeria so that future corporate governance reforms will consider the country's peculiar characteristics that have made the corporate governance characteristics examined in this study to show insignificant association with executive compensation. There should be capacity building by regulatory authorities to enable them cope with the challenges of enforcing compliance by companies. It is highly suggested that executive compensation disclosure matters should be given adequate attention in future corporate governance reforms while it is also integrated into laws and Listing

Requirements of the NSE. As an indication that the Anglo-American corporate governance system may be ineffective in Nigeria, a member of the drafting committee of the CG Code 2003 made this observation as documented by Adegbite (2013, p. 534), ‘‘. . . The World Bank, IMF and the OECD are very influential in shaping corporate governance in Nigeria. However, some of us wanted us to be more stakeholder oriented like Japan, which is considered to suit our environment better.” It is hoped that these suggested recommendations will assist in strengthening the country’s corporate governance system and executive compensation matters.

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