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Board Size and Composition and Corporate Performance: the Case of Non- Financial Companies on the Nigerian stock Exchange

Dr. R. O. Ugwoke[1], Dr. E. O. Onyeanu[2] and Dr. N.J.Modebe[3]

1. Dr. Robinson Onuora Ugwoke is of the Department of Accountancy, Faculty of Business Administration, University of Nigeria Enugu Campus.
2. Dr. Edith Ogoegbunam Onyeanu is of the Department of Accountancy, Faculty of Business Administration, University of Nigeria Enugu Campus
3. Dr. Nwanneka J. Modebe is of the Department of Banking and Finance, Faculty of Business Administration, University of Nigeria Enugu Campus

Abstract
The rampant corporate failures in recent times both within and outside Nigeria make corporate governance issue an interesting and important area of research in Accounting. The cases of Enron, Xerox, Adelphia et cetera internationally and Cadbury, NITEL, NEPA, NRC and many banks in Nigeria are very well known. Interestingly the Board of Directors as the top management of these corporate entities is where the bulk stops. The quality of the board, its efficiency and by extension the corporate performance of the entity could be affected by the size and composition of the Board as a critical element of corporate governance. Precisely the question is asked, if at all, to what extent do Board size, Board composition/structure, and frequency of board meetings and regularity of attendance at meetings by board members impact the corporate performance of companies? This paper uses opinions of company administrators and managers to assess their perception on the impact of Board size and composition and the related variables on the financial performance of Non-Financial Companies quoted on the Nigerian stock exchange. A total of 72 companies selected through the Taro Yameni formula were selected and three copies of a structured questionnaire administered to three top ranking managers/accountants in each company to get their perception of the impact of these board characteristics on the corporate governance and performance of these companies. The Micro soft Special Package for Social Sciences (SPSS) was used to analyze the responses presented in a 5-point likert scale. The regression showed that there is a significant positive relationship between the Board size, composition, frequency of meetings, regularity of members' attendance and performance of quoted non financial companies. R, the correlation coefficient which has a value of 0.977, indicates that there is a significant positive relationship between the Board size, composition, frequency of meetings, regularity of members' attendance and performance of quoted companies. R square, the coefficient of determination, shows that (B = -02.0%; C= 80.4%; F= -22.2%; R= 40.7%) of the variation in the performance of quoted companies is explained by the model. More specifically, a higher percentage outside board membership leads to a higher corporate performance and the fewer the overall size of the Board, the higher the corporate performance. It is therefore recommended among others that the Board should not be unnecessarily weighty in size but more importantly, the Board should be composed more of outsiders with proven integrity, acumen, experience and skill in corporate management. This is expected to reduce drastically the spate of corporate failures as good corporate governance is engendered
Key words: Board of Directors, Corporate performance, corporate governance,

1 INTRODUCTION

Wolfenson (1999), and Akinsulire (2006) all agree that corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. This then provides the structure through which the company's objectives are set and communicated, the means of attaining them as well as monitoring performance specified. It is generally also agreed that the Board of Directors (BOD) is central to the corporate governance mechanism in all market economies. In this regard Manne (1965), Alchian and Demtz (1972) and Bonnier and Bruner (1989), assert that, the Board is one of the most important and possibly beneficial internal mechanisms of corporate control being the ultimate stewardship reporter. The board is the primary means through which the shareholders excise control over the affairs of the company. The board is held responsible for all the activities of the company and even for the failure of other elements of the corporate governance chain. The shareholders are helped in this regard by statutory and regulatory provisions and institutions but by far the strength of the internal control mechanism is more germane to the success of the company than all external control measures. Since the internal control mechanism is

essentially established by the Board, the Board thus exercises utmost control over the safety, correct and most economic use of the resources of the enterprise. Though, all stakeholders responsible for promoting sound corporate governance, not just the Board, but also the management, audit committee and regulators, are challenged and compelled to ensure that sound corporate governance exist (Williams, 2001). But the issues of structure/composition and size of the BOD as a corporate governance mechanism has continued to receive considerable attention from academics, market participants and regulators. This is premised on the expectation that these issues would exert considerable influence on the overall efficiency of the BOD and by extension the quality of corporate governance and firm performance. However going beyond mere expectation, it is germane to evaluate the extent to which BOD size actually affects the bottom line of the firm on one hand and assess the impact of BOD composition/structure on corporate performance in Nigeria. These are tasks set for itself by this paper. It therefore asks such questions as: to what extent does BOD size affect corporate performance? And, does the percentage of outside directors significantly boost corporate performance? The paper tests hypotheses; that there is a negative relationship between BOD size and corporate performance and that there is a strong correlation between BOD composition and corporate performance. The paper is organized in five parts. . Part one of the paper introduces the work, part two contains the literature review, part three the methodology, while part four presents and discusses the findings and part five concludes.

2 LITERATURE REVIEW

2.1. Board of Directors (BOD)

The Companies and Allied Matters Act (CAMA) (1990) S. 244(1) stipulates that the Directors of companies are persons duly appointed by the company to direct and manage the business of the company. S. 63(3) of the Act puts it simply that ''the business of the company shall be managed by the Board of Directors''. By managing the business of the company therefore, the BOD is expected to control and direct, to administer and to take charge of, and to carry on the concerns of the business establishment. Good corporate governance demands that the Directors do this stewardship assignment transparently and accountably by adhering to company fiduciary duties and ethics (Adekoya, 2011). After all, it is the Principal- Agency theory that creates the relationship between the Shareholders and the BOD. The separation of ownership and control, which occurs as a result of the introduction of external investors, brings to the fore the agency challenge requiring the protection of the principal, in this case the shareholders, through an efficient oversight function by the agent (the BOD). It is presumed that the BOD's effective performance of this monitoring role could be influenced by its composition and quality, its size and diversity, information asymmetries and the board culture (Brennam, 2006). This becomes more critical in the face of a growing trend in the composition of independent BODs and critical corporate committees containing a strong representation of non-executive (outsider) directors, (Baysinger and Hoskisson, 1990; Mallette and Fowler, 1992; and Daily and Dalton, 1994). Cho and Kim (2007) describe the outside director as one who does not have any affiliation with large investors or the management of the company. They neither work for nor have professional relationships with the corporation they govern. Pass (2002), describes outsider- directors also known as non-executive directors as persons who take on numerous responsibilities in the company on a part-time basis. They may sit on various key company committees such as the nominations committee, the remuneration committee and the audit committee. The internal directors are the opposite; they may be the core or large investors or their representatives or those who represent management or labor. What values does each category of directors bring to the table and what should be the ideal mix of internal and outside membership of the BOD? According to the Securities and Exchange Commission (SEC) code of best practices of corporate governance in Nigeria 2003, the BOD should be composed in such a way as to ensure diversity of experience without compromising compatibility, integrity, availability and independence; members of the BOD must possess upright personal characteristics, relevant core competencies, knowledge on board matters, a sense of accountability and commitment to the task of corporate institutional building.

The outside directors ideally focus on the financial performance, seen as the benchmark of efficient and effective monitoring. They are more likely to dismiss poor performing CEOs than inside directors. They protect their personal reputations as they are given the incentive to monitor the affairs of the company. Hence their presence strengthens corporate governance by enhancing BOD independence from top management, greater objectivity, representation of multiple corporate perspectives and accountability. Along this line, Johnson et al insist that from the agency point of view, outsiders are more likely to carry out their responsibilities more effectively than insiders because the latter is likely to be reluctant to confront a CEO in a Boardroom situation. On the contrary, insiders would not be keen to raise the sensitive topic of CEO performance because they may in all likelihood be beholden to the CEO for their jobs (Zajac and Westphal, 1996).

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2.2 Corporate Performance

The capacity and ability of a firm to use its assets to generate revenue from its primary mode of business depict its overall financial health. When this is measured periodically, it forms the basis for both horizontal and vertical analysis and comparison. According to Demsetz and Lehn (2004), financial performance involves measuring a firm's policies and operations in monetary terms which are depicted in the firm's return on investment, return on assets, value added, *et cetera.* That is, accounting profit ratios proxy corporate performance. Corporate governance has been found to correlate positively with corporate performance, (Attiye and Robina, 2007) both seen from these accounting ratios of the firm and the movement of its price in the stock market. While the accounting profit ratios are measured by the Accountant constrained only by the standards set by his profession, the performance as reflected by the movement of its price in the stock market is measured by the investors constrained by their acumen, information, optimism or pessimism and general psychology. In either case however, Young (2000) suggests that best governance practices exert a positive influence on firm performance since it prevents management and controlling investors from taking initiatives to expropriate minority investors. This, it is argued impacts positively on the firm's goodwill and ability to attract equity capital from prospective marginal investors. Hence in considering approaches to measurement of firm level financial performance, Sanda *et al* (2003), insist that this is found in social science research based on market prices, accounting ratios and total factor profitability where market prices are readily obtained from national stock exchanges for all listed firms. While profit is a flow concept, profit margin measures the flow of profits over some period compared with revenue and costs and thus there could be gross profit margin, operating profit margin, return on equity *et cetera*. The relationship between corporate governance and firm's financial performance stems from the understanding that economic value is driven by governance mechanisms such as the legal protection of capital, the firm's competitive environment, its ownership structure, CEO-Duality, board composition and size, (the focus of this paper), existence of Audit Committee and financial policy (Uadiele, 2010). In this light, Gompers *et al* (2003) find that stock returns are higher for firms with strong shareholder rights as compared to firms with weak shareholder rights. This suggests that firms with stronger or better corporate governance provisions outperform those with poor governance provisions in terms of profits, capital acquisition and sales growth. They also add that there is substantial evidence showing that weakly governed firms experience lower performance based on operating performance measures, lower sales growth and net profit margins. This has been corroborated by Khatab *et al* (2011) from a study of twenty listed firms in the Karachi Stock Exchange in Pakistan.

2.4 Assessment of Current Corporate Governance Issues and Corporate Performance in Nigeria.

Whereas in the United Kingdom approaches to best practices in corporate governance reflect a deep appreciation that governance should promote both accountability to shareholders and the board's ability to manage the company effectively and efficiently the situation in Nigeria has been different. For instance, the key features of the UK best practices codified by the country's company law and the listing rules demand inter alia; a unitary board with members collectively responsible for leading the company; division of powers at the apex of the company hierarchy, emphasizing the distinction between running the board by the Chairman and running the company by the CEO; a balance of executive and independent non-executive directors where for larger companies, at least 50% of the board members should by independent non-executive directors and for smaller companies at least two independent directors; formal and transparent procedures for appointing directors, with all appointments ratified by shareholders; regular evaluation of the effectiveness of the board and its committees; formal and transparent procedures for setting executive remuneration, including a remuneration committee made up of independent directors and an advisory vote for shareholders; and a significant proportion of executive remuneration linked to performance. The illicit activities and insider dealings of most Nigerian Bank Chief Executives and directors as revealed by the Governor of the Central Bank of Nigeria in 2009 shows a striking different scenario and summarize the level of decadence in corporate governance in Nigerian companies. Corporate governance is yet at a rudimentary stage in Nigeria with less than 40% of quoted companies including banks having recognized the codes of corporate governance, (CBN, 2006). But Nganga et el (2003) insist that corporate governance is a crucial ingredient in the process of encouraging domestic investment as well as inflow of foreign direct investment in Nigeria. They further lament that corporate governance practices in Nigeria reflect systemic governance problems including the inability to ensure effective capacity, constraints by administrators and ineffective implementation of laws. This leads to limited economic growth (Suberu and Aremu, 2010). And in realization of the need to align with international best practices, the Securities and Exchange Commission (SEC) in collaboration with the Corporate Affairs Commission (CAC), inaugurated a seventeen (17) member committee in June 2000 in Nigeria headed by Atedo Peterside, to review and identify weaknesses in the current corporate governance practices in Nigeria and make recommendations for improvement. According to Inyang (2009), the members of the committee were selected to cut across relevant sectors of the economy including members of professional organization, the private sector and regulatory agencies. The committee submitted a draft code, which was widely publicized throughout the country and

reviewed in major financial centers of Lagos, Abuja and Port Harcourt to elicit stakeholders' input prior to finalization. The final report was approved in 2003 by the boards of SEC and CAC. The release of the 2003 code marked a watershed in the development of good corporate governance practices in Nigeria. Essentially, the Code stipulated among other things, the separation of the roles of Chief Executive Officer and Chairman of the Board and most importantly, as stated earlier, that the board should be composed in such a way as to ensure diversity of experience without compromising compatibility, integrity, availability and independence. It remains to be seen how far these provisions are being implemented. It also remains to be ascertained, the extent to which the roles of the board as stipulated in the Code, *to wit*: strategic planning; selection, performance appraisal and compensation of senior executives; succession planning; communication with shareholders; ensuring the integrity of financial controls and reports; ensuring that ethical standards are maintained and that the company complies with the laws of the federation; are being carried out under different sizes and composition of the board.

3 METHODOLOGY

The paper adopts a survey design involving time series and sectional data on the surveyed companies. Secondary sources of data on the performances of sampled companies are used for analysis. The population of the study is made up of all the non-financial companies quoted in the Nigerian stock exchange within the period covered by the study. Though the Nigerian stock exchange record shows a list of 203 companies, the CBN list that purges it of liquidated companies and gives a list of 88 non-financial companies is used as the population. Using the Taro Yameni formula at 95 percent confidence level and error margin of 0.05, a sample size of 72 is selected. Through cluster random sampling, sample elements representing all the sections of the non-financial companies were picked from the sample frame. The dependent variables are corporate financial performance and elements of corporate governance while the independent variables are the sizes and percentage composition of the boards. A regression analysis is performed with the Microsoft Special Package for Social Sciences (SPSS). To enhance the robustness of the findings, an oral interview was conducted on the sampled firms. The interview guide established the effect of size and composition skew in favor of external or internal directors on the following: increased board monitoring, effectiveness of control, reduced financial scandal, investors' confidence, effective communication, information diffusion, fastness of decision making, and financial performance/profitability. Responses were reduced into a 5-point Linkert scale for proper analysis employing regression, correlation, ANOVA, F- statistics and Durbin Watson statistics.

4 PRESENTATION OF FINDINGS AND DISCUSION

4.1 Perceived Impact of Board Size, Composition and Activities on Corporate Governance and Performance of Quoted Companies on the Nigerian Stock Market

Primary data showing the responses of the respondents is shown on table 4.1 in Appendix I

Table 4.1 shows a weighted average of 3.82 from the 5 point linkert scale (which is nearest to 4 in the scale) indicating a general 'Agreement' by the respondents that board size, composition, frequency and regularity of attendance to meetings impacts positively on the corporate governance and performance of the companies listed in the Nigerian Stock Exchange. Increased board size and in particular non executive directorship has had greater positive impact on the corporate governance tone and profitability of the companies as reflected by the higher weighted averages of 4.03, 4.01 and 4.03 respectively for higher proportion of outside directors and positive impact on the company's corporate governance tone and performance, increase in board size and increase in the profitability and efficiency ratios of the companies, and the positive effect of board size on effective communication, coordination and decision making. Curiously, the respondents appeared not to know whether Investors have reacted positively to announcement of outside directors in the companies. The weighted average for this parameter is 3.10 which is closest to 3 in the linkert scale signifying having 'No Idea'. The rest of the parameters received weighted averages closer to '4' (AGREED) from the respondents signifying their agreement to the positive effects of board size, outside directorship composition, and efficient functioning of the board on corporate governance and performance of the companies.

4.2 REGRESSION ANALYSIS

Null hypothesis (H_o): Board Size, board composition, frequency of meetings and members' regularity at meetings do not have any positive significant relationship with corporate governance and performance of quoted non financial companies on the Nigerian Stock Exchange.

Descriptive Statistics

	Mean	Std. Deviation	N
corporate performance of quoted companies	1.4428	.89329	201
Board size	1.2935	.67706	201
Composition	1.2786	.83186	201
frequency of meetings	1.8209	.85893	201
regularity of members attendance	2.2189	1.22957	201

Correlations

		corporate performance of quoted companies	Board size	composition	frequency of meetings	regularity of members attendance
Pearson Correlation	corporate performance of quoted companies	1.000	.884	.910	.847	.835
	Board size	.884	1.000	.831	.753	.781
	Composition	.910	.831	1.000	.812	.620
	frequency of meetings	.847	.753	.812	1.000	.828
	regularity of members attendance	.835	.781	.620	.828	1.000
Sig. (1-tailed)	corporate performance of quoted companies	.	.000	.000	.000	.000
	Board size	.000	.	.000	.000	.000
	Composition	.000	.000	.	.000	.000
	frequency of meetings	.000	.000	.000	.	.000
	regularity of members attendance	.000	.000	.000	.000	.
N	corporate performance of quoted companies	201	201	201	201	201
	Board size	201	201	201	201	201
	Composition	201	201	201	201	201
	frequency of meetings	201	201	201	201	201
	regularity of members attendance	201	201	201	201	201

Model Summary(b)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.977(a)	.955	.954	.19170	.531

a Predictors: (Constant), regularity of members attendance, composition, Board size, frequency of meetings
b Dependent Variable: corporate performance of quoted companies

ANOVA(b)

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	152.389	4	38.097	1036.667	.000(a)
	Residual	7.203	196	.037		
	Total	159.592	200			

a Predictors: (Constant), regularity of members attendance, composition, Board size, frequency of meetings
b Dependent Variable: corporate performance of quoted companies

Coefficients(a)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta	B	Std. Error
1	(Constant)	-.058	.035		-1.662	.098
	Board size	-.020	.048	-.015	-.419	.676
	Composition	.804	.041	.749	19.808	.000
	frequency of meetings	-.222	.041	-.213	-5.439	.000
	regularity of members attendance	.407	.026	.560	15.677	.000

a Dependent Variable: corporate performance of quoted companies

TABLE 4.3 SPSS RESULT ON THE EFFECT OF RCBF ON PQC

Particulars	R	R^2	Adj. R^2	DW	Standard Coefficients		F	Sig
					Beta	T- Value		
All Firms	0.977[(a)]	0.955	0.954	.531	B = -015 C=0.749 F =-213 R = 0.560	- .419 19.808 -5.439 15.677	1036.667	0.000

NOTE:
R = Correlation Coefficient or Beta
R^2 = Coefficient of Determination
Adj. R^2 = Adjusted Coefficient of Determination
DW = Durbin Watson (d) test statistic
T-value = Student t- test Statistic
F = F- test statistic

Interpretation on corporate performance:
The regression sum of squares (152.389) is greater than the residual sum of squares (7.203), which indicates that more of the variation in the dependent variable is explained by the model. The significance value of the F statistics (0.000) is less than 0.05, which means that the variation explained by the model is not due to chance.
R, the correlation coefficient which has a value of 0.977, indicates that there is a significant positive relationship between the Board size, composition, frequency of meetings, regularity of members attendance and performance of quoted companies. R square, the coefficient of determination, shows that (B = -02.0%; C= 80.4%; F= -22.2%; R= 40.7%) of the variation in the performance of quoted companies is explained by the model.
With the linear regression model, the error of estimate is low, with a value of about 0.19170. The Durbin Watson statistics of .531, which is not up to 2 indicates that there is no autocorrelation.
The Board size, composition, frequency of meetings , regularity of members attendance and performance of quoted companies of 0.977 indicates a positive significance between size, composition, frequency of meetings , regularity of members attendance and performance of quoted companies , which some are statistically significant and other are not (B with t = -.4.19; C=19.808;F= -5.439 and R= 15.677). Therefore, the null

hypothesis is rejected and the alternative hypothesis accordingly accepted. We therefore conclude that Board size, board composition, frequency of meetings and regularity of attendance to meetings by members have positive significant effect on corporate performance of quoted non financial companies on the Nigerian Stock Exchange.

Critically, a higher positive effect was seen from board composition and regularity of members' attendance to meetings than just board size and frequency of board meetings. Essentially, the higher the board size, the higher the cost associated therewith. The same applies to frequency of meetings due to associated sitting and transport allowances. These would invariably impact negatively on the profit figures. But these higher costs can be more than counter balanced by a good composition of a board with higher percentage of outside board members with wide interests, experience, professional competence, proven integrity and honesty of purpose. A large sized board with irregularity of attendance by members could by counterproductive. It is therefore not just the frequency of meetings that improves performance but the regularity of attendance by members that make it possible for meaningful contributions from wide array of experience to the board strategic planning, organizing, directing and control of the resources of the company that makes the significant contribution to both corporate governance and performance.

5 CONCLUSION

The study was done using both primary and secondary data collected from questionnaire administered to 216 senior management and professionals and 4 years Annual Reports respectively of 72 financial companies quoted in the Nigerian Stock Exchange. Using the Microsoft Special Package for Social Science (SPSS), the data were analyzed and hypothesis tested to find that Board Size, Board Composition, Frequency of Board Meetings and Regularity of attendance at Board meetings all positively and significantly affect corporate governance and company performance of quoted financial companies on the Nigerian Stock Market. There appears to be a general conflict of interest of the shareholders and that of Executive Directors which is inimical to the maximization of shareholders' wealth. Little wonder that shareholders have a disdain for the excesses of Executive Directors and usually prefer a higher proportion of outside directors. Similarly, a larger sized board incorporates not only a greater number of experts from different fields but also accommodates more credible, transparent, selfless and dedicated non executive directors. Arbitrariness, autocratic, intimidation and over bearing attitudes of either the Chairman of the Board or the Chief Executive Officer of the company are usually cubed and checkmated by a large and Non Executive Directors- dominated Board. The probability of the Chairman doubling as Chief Executive Officer of the company is reduced by a larger sized and outside directors dominated board. Essentially this contributes positively to corporate governance through enhanced transparency and accountability. A sound human capital with robust intellect and experience from outside is therefore recommended by this paper for company boards.

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APPENDIX 1

Table 4.1 Perceived Effect of Board Size, Composition and Activities on Corporate Governance and Performance

S/N	Variable	SA=5	A=4	NI=3	DA=2	SDA=1	TOTAL	MEAN
1	A higher proportion of outside directors on the Board of this company could have impacted positively on the company's corporate governance tone and performance	80 (400)	100 (400)	8 (24)	20 (40)	8 (8)	216 (872)	4.03
2	A higher proportion of Non Executive Directors in this company has enhanced effective monitoring of both Board and management leading to increased protection of shareholders' wealth	60 (300)	85 (425)	30 (30)	35 (70)	5 (5)	215 (800)	3.72
3	Higher dividend per share in this company has been positively influenced by a board size and higher percentage of outside directors.	62 (310)	75 (300)	30 (90)	28 (56)	6 (6)	201 (762)	3.79
4	Investors have reacted positively to announcement of outside directors in this company	40 (200)	70 (280)	30 (30)	41 (82)	15 (15)	196 (607)	3.10
5	The overall corporate performance of this company has been positively affected by the size of the Board.	70 (350)	100 (400)	5 (15)	25 (50)	10 (10)	210 (825)	3.93
6	Limited board size has negatively affected the securing of critical resources for expansion and better performance	65 (325)	99 (396)	5 (15)	20 (40)	10 (10)	199 (786)	3.95
7	The profitability and efficiency ratios of this company have significantly risen with increase in its board size.	80 (400)	100 (400)	4 (12)	19 (38)	12 (12)	215 (862)	4.01
8	The size of the board has significantly influenced the effective communication, coordination and decision making.	82 (410)	100 (400)	4 (12)	18 (36)	12 (12)	216 (870)	4.03
9	Frequency of board meetings has positively affected overall efficiency and performance of this company	77 (385)	101 (404)	5 (15)	22 (44)	10 (10)	215 (858)	3.99
10	Regularity of attendance to board meetings by members has had positive impact on corporate governance tone and performance of this company	67 (335)	80 (320)	4 (12)	40 (80)	10 (10)	201 (757)	3.77
11	Both corporate governance tone and performance have been positively influence by Board members' professional qualifications, knowledge, competence, integrity and experience.	75 (375)	80 (320)	4 (12)	34 (68)	22 (22)	215 (797)	3.71
	AVERAGE							3.82

Source: Field survey 2013. SA = Strongly Agree; A = Agree; NI = No Idea; D= Disagree and SD =Strongly Disagree. The weights are 5, 4, 3, 2, and 1 respectively. A total number of 216 respondents were surveyed.

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