

EXECUTIVE COMPENSATION AND FIRM PERFORMANCE: EVIDENCE FROM NIGERIA FIRMS

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Abstract

The focus of this paper is to theoretically examine the relationship between executive compensation and firm performance among Nigeria firms. This conceptual paper examines the issue using a library-based largely on the review of extant literature. The findings from majority of the studies show that the executive compensation has a significant effect on firm performance. However, we observed several gaps based on the literature review conducted. For studies conducted in developed economies we find that a clear gap exists in terms of the sensitivity of empirical findings for the relationship between executive compensation and firm performance to the type of compensation that is used. Where cash or equity is used, the findings appear to vary. For studies conducted in developing economies, we notice that, in most of these studies only accounting measures of firm performance are used ignoring market measures such as stock price and the Tobin Q measure. Again, it appears that most of the studies are based on cash compensation without much consideration to equity compensation schemes. For Nigeria, it appears that not much has been done empirically in these areas and just as in the case of studies in developing countries, only accounting measures of firm performance are used ignoring market measures such as stock price and the Tobin Q measure. Finally, only cash compensation is examined while equity compensations are ignored by studies in Nigeria. The study concludes that there is the need for further studies to address this gap.

1.0 Introduction

The relationship between a firm's performance and executive compensation has dominated accounting and finance research for almost three decades gaining increasing momentum progressively though without consensus on the steady state of the relationship. To understand this, one has to recognize the sources of the initial problem. Agency principal theory states that a problem exists when an agent (executives) has established an agenda, which conflicts with the interests of the principal (shareholder) (Attaway, 2000). This problem stems in part from the top executives behavior towards aversion to risk. This behavior induces manager to reduce his "personal" risk by engaging in activities that lessen the firm's risks; hence, manager actions negatively affect the shareholders wealth. According to economists, the dominant approach in dealing with this problem is for the board of directors to design a compensation scheme that provides the executive with proper incentives to maximize the shareholders' value. Holstrom (1979) has suggested that varying executive compensation to firm's performance will motivate the executive to make more value-maximizing decisions for the stockholders.

Executive compensation is a term that is straight forward and this has accounted for its simple definition. In clear terms, managerial compensation deals with the various manner and packages in which management is remunerated. The aim of executive compensation is to incentivize and reward appropriate performance and risk management behavior. A well-defined compensation policy will link the terms of performance and behavior to the company's strategy, continuity and long-term stable value creation. Given the strategic role of managers, it is also important that compensation levels are such as to attract, retain and motivate directors of the appropriate quality and caliber required (Bhatnagan & Trimm, 2011). Thus, executive compensation packages have been viewed as important in mitigating the conflict of interest between managers and shareholders in corporations. It has been widely recognized that compensation packages could potentially play an important role in motivating top managers. A number of corporate governance codes recommend that a significant proportion of remuneration should be performance-related (Bhatnagan & Trimm, 2011). Broadly speaking, executive compensation can either be in cash or in terms of equity, though both can have several other derivatives.

So far, there has not been any dominant alternative perspective or theoretical expectations that suggest that executive compensation could have an adverse effect on firm performance. However, in practice, recent events such as the stock market bubble, the series of corporate malfeasances and accounting scandals which drove policy markets to develop a set of anti-fraud/corporate government legislation reforms (notably the Sarbanes-Oxley Act

of 2002), and the financial shocks and recession of 2008-2009, the confidence of policy makers and their constituents that management is in control and working for enhanced returns to investors has been shattered. The tenet that incentive driven executive compensation, especially CEO compensation, for public companies enhances shareholder wealth and thus societal wealth is viewed with now greatly enhanced skepticism by the general public, the media, and policy makers. Numerous demands for the reform of compensation practices of senior executives of public companies have been called for (Michaud & Gai, 2009).

Consequently, the focus of this study is to examine conceptually, the relationship between executive compensation and firm performance.

2.0 Literature Review

2.1 Executive Compensation

According to Shin, Lee and Joo (2009), executive compensation is composed of the financial compensation and other non-financial awards received by an executive from their firm for their service to the organization. It is typically a mixture of salary, bonuses, shares of or call options on the company stock, benefits and perquisites, ideally configured to take into account government regulation, tax law, the desires of the organization and the executive, and rewards for performance. Executive compensation is a broad term for the financial compensation awarded to a firm's executives. Executive compensation packages are designed by a company's Board of Directors, typically by the compensation committee consisting of independent directors, with the purpose of incentivizing the executive team, who have a significant impact on company strategy, decision-making, and value creation as well as enhancing Executive Retention.

Sun Xianging and Huang (2013) define executive compensation as remuneration packages paid to senior leaders in business, most commonly the CEO. Executive compensation packages differ from employee remuneration both in scale and the benefits offered. Stock option form an integral part of most executive compensation packages, as well as a large basic salary, although many will offer a low basic salary and more favourable stock options to reduce the tax burden.

2.2 Measures of Executive Compensation

2.2.1 Salary

CEO salaries are usually set on an annual basis. Moreover, it is a stylized fact that firm's size is associated with base salary (Murphy, 1999). In a static setting, during any particular year, salary's sensitivity to price movement is zero. Barring an implicit bonus scheme in which subsequent salary is adjusted according to reported earnings, it appears unlikely that there is salary-related explanation for earnings management. As argued above, both logic and empirical evidence suggest that earnings management is a costly behavior, with the costs increasing in the degree of earnings management, e.g., due to increasing litigation risk. It follows that a manager on straight salary, who received at best a fixed benefit from earnings management, would have an incentive to reduce the extent of earnings management, and so reduce the costs. We expect a non-positive relationship between the role

of salary in compensation and the use of discretionary accruals as a tool of earnings management.

2.2.2 Percent Bonus

Firms reward managers' bonuses based on the current-year firm performance. Executives have incentives to either increase or decrease firm earnings, depending on the structure of a bonus plan whether earnings can be manipulated to trigger a raise in bonuses (Holthausen, Larcker, and Sloan, 1995). The payoff schemes of CEO bonuses in relation to firm earnings have the shape of a typical call spread curve. More precisely, when earnings are beyond a certain upper threshold or below a lower bound where performance-based compensation is not possible, a manager would have incentives to make earnings-decreasing decisions. In contrast, when firm earnings are in-between a range where bonuses are positively associated with firm earnings, a manager would implement earnings-increasing practices

2.2.3 Restricted Stock held

This variable denotes restricted stocks currently owned by managers, who can choose to sell or continue to hold them. Contingent on the managers' stock holding preferences, they would make different earnings management decisions. Executives who prefer to sell restricted stocks are likely to implement earnings-increasing practices (i.e., under-reserve) so that the current firm value is maximized. By contrast, those who prefer to hold restricted stocks are anticipated to carry but earnings-decreasing policies (i.e., over-reserve) in order to shift favorable firm performance to the future when they decide to sell the restricted stocks (Eckles and Halek, 2010). Restricted Stock Held is defined as the value of the CEO's restricted stock held as a percentage of total compensation.

2.2.4 Stock Option Exercised

Stock options can only be exercised when they are in-the-money. Whether and so what degree stock options are in the money depends on the performance and value of the firm when option are exercised. Since earnings-increasing policies could increase the intrinsic value of option in the current year, managers would have incentives to under reserve. Holthausen, Larcker, and Sloan (1995) document that option exercised by managers indicates solely earnings-increasing discretionary behaviors. Thus, we predict a negative coefficient on stock option exercised, which is calculated as the value of the CEO's stock option exercised as a percentage of total compensation.

2.2.5 Long –Term Pay

Long-term incentive pay remunerates executives based on firms' cumulative performance over past few years; the motivations driven by long-term incentive plans to manipulation earnings similar to those of bonus rewards. In addition, Eckles and Halek (2010) point out that such plan give managers a bias toward under-reserving losses incurred in the last year covered by the incentive plan, since they may want to "catch up" in the last

year. Long-term incentive plans are calculated by the percentage of the CEO's total compensation awarded as long-term incentive pay.

2.3 Firm Performance

The definition of firm performance could vary, depending on the context of its use (Marimuthu, Arokiasamy & Ismail, 2009). A wide variety of firm performance definitions have been introduced in the literature (Barney, 2007). Firm financial performance is generally defined as a measure of the extent to which a firm uses its assets to run the business activities to revenues. It examines the overall financial health of a business over a given period of time and can be used to contract the performance of identical firms in similar industries or between industries in general (Atrill et al. 2009). The main source of data for determining firm financial performance is the financial statement, the product of accounting which consists of the balance sheet which shows the assets liabilities and equities of a business, the income statement that records the revenues, expenses and profits in a particular period, the cash flow statement which exhibits the sources and uses of ash in period, and the statement of changes in the owners' equity that represents the changes in owner's wealth. Firm financial performance is commonly reflected in the calculation of financial ratios that show the link between numbers in the financial statement. The financial ratios may include the computation of the profitability, efficiency, liquidity, gearing, and investment of a particular firm. Moreover, firm financial performance generally may also be reflected in market-based (investor returns) and accounting-based (accounting returns) measures (Griffin & Mahon, 1997).

Examples of market-based indicators to measure firm financial performance are price per share and Tobin's Q which indicate the market value or the share of the firm as well as the financial prospect of the firm in the future. Additionally, what the shareholders have perceived from the returns distributed by the firm is also the driver of the share price. This price may lead to the market value of the firm. Alternatively, accounting-based measures, including profitability, efficiency, liquidity, gearing, and investment ratios, are calculated using the figures from the financial reports and may represent a firm's financial performance. According to Atrill et al. (2009), the ratios that may be utilized to calculate the firm's profitability and the return on assets (ROA), return on equity (ROE) and return on investments (ROI). These ratios express the success of a firm in generating profits or returns from the resources owned. In contrast, the market-based measure is believed to be more objective because it relines one market responses to particular decision made by a firm (Griffin & Mahon 1997). The choice of whether to use accounting or market-based calculations for measuring a firm's financial performance depends upon the specific aims of the research.

2.4 Review of Prior Studies

2.4.1 Studies in Developed Economics

Campbell (2015) in a paper examined the complex relationship between compensation levels of the Top management team (TMT) and firm performance. A core objective of the study was the comparison of executive compensation and company

performance for United States based companies. Data was collected from a random sample of the 2013 fortune 500 list of largest United States based companies. For the study, the value of the options granted was determined using the Modified Black Scholes method. The statistical procedure employed in the study was ordinary least squares (OLS) regression analysis. OLS regression analysis for the study utilized SPSS 22.0. Findings from the study revealed that a significant relationship exists between CEO compensation and the accounting based measure of performance which accounted for 11.4% of the variance observed in the accounting based measure of performance. The results also showed that levels of Vice President Compensation have a stronger direct relationship with firm performance than CEO compensation.

Bhatnagan and Trimm (2011) in a study explored the Agency managerial power theories to explain the relationship among the various components of executive compensation, firm performance and unsystematic risk in the US financial sector. Institutions in the financial sector listed on the NASDAQ that have been in existence from the pre-financial crisis period January 03, 2006 to the post financial crisis December 27, 2009 are examined. We find that the Agency theory does not fully explain the behavior of executives and their risk appetite. Managerial power theory fares better in this regard, as managers are focused mostly on their base salary. The date analysis shows that stock options are not significantly influenced by unsystematic risk; instead the base salary of executives has been significantly influenced by market risk and firm performance.

Nulla (2014) in a study investigated the effect of CEO roles with accounting performance towards CEO compensation in the New York Stock Exchange (NYSE) companies from the periods 2005 to 2010. This study selected one hundred and twenty companies through stratified sampling method. This study demanded the characteristics of numerical and objectivity as such the quantitative research methodology was applied. The research question for this study was: is there a relationship between CEO compensation, CEO & chairman dual role, and CEO role? It was found that, there was relationship between CEO salary, CEO bonus, CEO total commendation, and accounting firm performance, under both roles.

Kato and Long (2005) in a paper provided evidence on how executive compensation relates to firm performance in listed firms in China. Using comprehensive financial and accounting data on China's listed firms from 1998 to 2002, augmented by unique data on executive compensation and ownership structure, they find for the first time statistically significant sensitivities and elasticity's of annual cash compensation (salary and bonus) for top executives compensation and that Chinese executives are penalized for making negative profit although they are neither penalized for declining profit nor rewarded for rising insofar as it is positive.

Ozkan (2011) examined the link between CEO pay and performance employing a data set of 390 UK nonfinancial firms from the FTSE All Share Index for the periods 1999-2005. He included cash and equity-based components of CEO compensation in his analysis. The

results indicated a positive and significant link between CEO cash compensation and performance; however, the link between total compensation and performance was positive but not significant. The findings from the study also suggested that larger firms pay their CEOs higher compensation, which one can interpret as reflecting their demand for higher quality CEO talent. Further, he noted that firms with larger board size pay their CEOs higher level of total compensation and moreover, proportion of non-executive directors on board do not have a significant impact on CEO cash compensation, while non-executive directors share ownership has a significant impact suggesting that ownership can provide incentives for non-executive directors to be more active in monitoring for CEO compensation packages.

Xiang Li (2010) investigated the relationship among corporate governance mechanism, firm performance, and executive compensation within Chinese publicly listed firms and indicated a dysfunctional corporate governance system in China, which cannot bring improved firm performance but grant executives high compensations. So far as the political connections are concerned, results showed that they deteriorate corporate governance mechanism, but do not result in inferior firm performance. Conyon and He (2011) investigated executive compensation and corporate governance in China's public trade firms and found that executive compensation is positively correlated to firm performance. The study showed that executive pay and CEO incentives are lower in State controlled firms and firms with concentrated ownership structures. The study also found that firms with more independent directors on the board have a higher pay-for—performance link.

Doucouliaagos, Askary and Haman (2008) in a paper explored the relationship between directors' and Chief Executive Officer's pay and performance within Australian banking, using panel data for the 1992-2005 periods. Several earnings models are estimated, using different dependent variables, alternate measures of performance and different estimation techniques. The result indicates an absence of a contemporaneous relationship between directors' pay and firm performance, and no association with prior year. However, there is a more distant pay-performance relationship, with total directors' pay having a robust positive association with earnings per share lagged two years, as well as with ROE lagged two years. The pay performance association is stronger and more direct for CEO remuneration than it is for total directors' remuneration.

Gregg, Jewell and Tonks (2011) in paper examined the pay-performance relationship between executive cash compensation (including bonuses) and company performance for a sample of large UK companies, focusing particularly on the financial services industry. The sample utilized for the study considered of 415 companies that were all constituents of the FTSE 350 stock market index over the periods January 1994 to December 2006. The model of the study was estimated using fixed effect regression. Surprisingly, they found that although total board pay and the pay-performance sensitivity between the financial sector and other industries.

Sigler (2011) in a paper examined the relationship of CEO pay and company performance for 280 firms listed on the New Stock Exchange for period from 2006 through 2009. The time frame of the study is a period after the adoption of the Sarbanes Oxley Act and after the SEC approval of the corporate governance rules affecting executives pay for New York Stock Exchange companies. Findings from the study revealed that there is a positive and significant relationship between total CEO compensation and company performance measured by return on equity. The size of the firm appears to be the most significant factor in determining the level of total CEO compensation, according to the results, and the tenure of the Chief Executive Office is another significant variable.

Hassaeen (2015) in a paper examined the effect of CEO compensation on firm performance of French family firm. To investigate the link between executive pay and firm performance, they utilized multiple regression method over a period of four years (2007-2010). Findings from their study revealed that French family companies provide excessive compensation compared to their non-family counterpart, suggesting that families are likely to extract private benefits at the expense of minority shareholders. The findings also show that excess remuneration paid to executives has a negative impact on financial performance. The result confirms the preceding one and suggests that CEO compensation is used by families as a tunneling mechanism that exacerbates agency costs.

Denirer and Yuan (2013) carried out a study to investigate the relationship between executive compensation structure and firm performance in the US restaurant industry. Using executive compensation data for public trade restaurant firms for the periods 1999 to 2010, their results suggest that compensation in the form of bonuses and non-equity affect restaurant firm performance positively. Findings from the study also revealed that compensation in the form of salary affects restaurant firm performance negatively. Findings of this study suggest that restaurant firms should use salary with discretion and use bonuses and deferred pay to increase firm performance.

Sun, Wei and Huang (2013) in a paper examined the relationship between CEO compensation and firm performance proxied by efficiency estimated from data envelopment analysis (DEA) of the US property-Liability (P&L) insurance industry. The study was conducted in two stages. First, they applied DEA models to calculate efficiency scores. In the second stage a translog model was used to correlate the level and structure of CEO compensation and the efficiency for the sample P&L insurance over the period of 2000 to 2006. Findings from the study revealed that firm efficiency is positively and significantly associated with total CEO compensation. While efficiency is associated with CEO cash compensation, cost efficiency is associated with incentive compensation.

Based on the studies conducted in developed economies we find that a clear gap exist in terms of the sensitivity of empirical findings for the relationship between executive compensation and firm performance to the type of compensation that is used. Where cash or

equity is used the findings appear to vary. Also, the measure for financial performance appears to also account for the diversity in the findings.

2.4.2 Studies in Developing Economics

Ghosh (2003) in a paper examined the empirical relationship between board structure, CEO compensation and firm performance in the context of an emerging economy, Indian. Using panel on 462 manufacturing firms from the Indian corporate sector for the periods 1997 to 2002, he explored two issues. First, he examined how the structure of the corporate board in terms of size and proportion of non-executive directors affect the firm performance. Secondly, he examined how the level and different components of executive compensation have an effect on the firm performance. The empirical findings indicate that the relationship between executive compensation and firm performance is found to be non-linear. There is also a saturation level on board compensation, beyond which the performance does not increase. The result suggests that institutional characteristics of emerging economies may support management structures, which are different from those predicted by earlier studies.

Jaafar, Wahab and James (2012) in a study examined relationship between director remuneration and performance in Malaysia family firms. The proxies of director remuneration include fees, salary, bonuses and benefits of kin. The proxy for family firm is a dummy variable that is one (1) if the firm is a family firm and zero (0) is a non-family firm. The dependent variable (performance) is measured by ROA and ROE. A panel analysis of 537 firms from 2007 and 2009 finds that the relationship between director remuneration and performance is significantly positive. This suggests that the remuneration drive board motivation to enhance performance.

Ismail, Yabai and Hahn (2014) in a study investigated the relationship between CEO pay and firm performance (return on asset, return on equity and profit margin) of 100 companies from the consumer product sector in Malaysia listed in Bursa Malaysia from 2006 to 2010. The research question for this study was, will the payment of CEO affects the company's performance? Overall, most of the attestations results were found to have a relationship between CEO pay and firm performance. The correlations and regressions among the sub-variables of the firm performance and the CEO pay were found to be consistently positive ranging from weak positive to the strong positive.

Usman, Akhter and Akhtar (2015) carried out a study aimed at investigating the influence of board effectiveness and firm performance on CEO compensation within the context of developing economy of Islamic Republic of Pakistan. The study uses Partial Least Square (PLS) based Structural Equation Modeling (SEM) techniques to draw the inference using PLS Graph Version 3.0. It uses Karachi Stock Exchange (KSE) 100 index companies as a sample for the period of five years (2007-2011). Before analyzing the structural model, the validity and reliability of the model is confirmed through bootstrapping technique and variance inflationary factor respectively. The structural model results revealed that board effectiveness has negative influence on CEO compensation. Opposite to agency theory and

current studies from developed countries, they found a negative association between the firm performance (firm value and firm profitability) and CEO compensation. These results are due to different business environment of Pakistan and poor corporate governance structure.

Erick, Kefah and Nyaoga (2014) in a paper sought to assess the effect of executive compensation on the financial performance of insurance companies in Kenya. The study considered functional form relationship between the level of executive remuneration and key performance ratios by using a regression model that establishes the relationship between pay and financial performance. The result show that there is a non-significant relationship between executive compensation and financial performance, $P\text{-Value} > 0.05$. The negative correlations suggest the capping of executive compensation to maximize shareholders' returns. This advocates that key performance ratios are not key considerations in determining executive compensation among the insurance companies in Kenya. Hence there is need to sensitize executives to align their payment to accounting performance measures because they are directly linked to shareholders' wealth maximization.

Aduda (2011) examined the relationship between executive compensation and firm performance among commercial banks listed at the National Stock Exchange. The study considered functional form relationship between the level of executive remuneration and accounting performance measures by suiting a regress model that relates pays and performance. He found out that accounting measures of performance are not key consideration in determining executive compensation among the banks in Kenya and that size is a key criterion in determining executive compensation as it was significantly but negatively relates to compensation. The negative correlation suggests the capping of executive compensation to ensure maximization of returns to shareholders.

Ramadan (2013) carried out a study to test the pay-performance relation for the Jordanian manufacturing firms listed on the Amman Stock Exchange during the periods 2000-2011. Using two regression methods; the ordinary Least Square Method, and the Fixed Effect Method, three models were tested. All three models were tested to lead to a conclusion that there is a positive and significant impact of the CEO remuneration on the Jordanian manufacturing firm's performance. Another finding of the study revealed that due to specific characteristics of each of the companies, the impact of the remuneration varies among the Jordanian Industrial Firms in the magnitude of the impact, and consistent in the direction of the impact. These findings are compatible with the say that the CEO remuneration has a significant role in mitigating the agency problem by granting reasons for CEOs to perform their tasks to the magnification of owner's wealth, and the remuneration should reflect and suit firm's performance.

Krauter and Ferreira de Sousa (2013) carried out a survey to investigate the relationship between executive compensation and the financial performance of companies. The survey data consisted of a secondary and non-probability sample of 44 Brazilian industrial companies. In order to operationalize the independent remuneration variable, the

authors used average monthly salary, average variable salary, and three indices that were created for this survey: benefits, career, and development. These indices measure the access to benefits, mechanisms for stimulating and supporting, careers, and mechanisms to encourage education and professional development that companies offer to their directors, vice president, and Chief Executive Officer (CEOs), who are referred to in the paper by the term “executive”. The remuneration data are from fiscal year 2006. In order to operationalize the finance performance variable, two accounting indicators were used: sales growth and Return on Equity (ROE) for fiscal years 2006 and 2007. The results of a multiple regression analysis do not support the hypothesis that there is a positive and significant relationship between executive compensation and corporate financial performance.

Lone, Hassan and Afzal (2015) in a paper represented the initiative to highlight a developing country’s perspective on justification and thereby identifying the factors affecting CEO compensation. The aim of the paper was to explore the reason for high CEO compensation in Pakistan’s Banking Sector. The paper attempted to use panel data of 22 listed banks in Pakistan for the periods 2006-2013 and explores the relationship between CEO compensation and the following variables: firm performance, Firm Size, CEO from the family, Independence of the board of directors, share held by the board, percentage ownership of financial and non-financial institution. Findings from the study suggest that performance does not play any role in CEO compensation.

Scholtz and Smit (2012) carried out a study to examine the relationship between short-term executive compensation and company performance for a sample of companies listed on the Alternative Exchange in South Africa between 2003 and 2010. The financial sample consisted of 58 companies, but only data available on McGregor BFA for the companies in the sample were used in the regression analysis. Evidence is provided that there is a strong relationship between executive remuneration and some company performance variables, such as total assets, turnover and share price. The corporate governance measures and disclosure requirements application to executive remuneration were also examined.

For studies conducted in developing economies, we notice the following gaps. Firstly, in most of these studies only accounting measures of firm performance are used ignoring market measures such as stock price and the Tobin Q measure. The neglect of market measures may not provide a well-rounded perspective to the firm performance. Secondly, it appears that most of the studies are based on cash compensation without much consideration to equity compensation schemes and also limits the inferential ability of the studies in the context of equity compensations. Thirdly, is the issue of mixed findings in the literature which suggests that the issue is far from resolved empirically?

2.4.3 Studies in Nigeria

Obasan (2012) carried out a study that tried to link compensation with performance using selected firms in Nigeria as a case study. His study specifically covered three conglomerates in Nigeria. The choice of this case study was not unconnected with the fact

that these companies are among the largest employers of labour in the manufacturing industry in Nigeria. A total number of 150 questionnaires (50 for each company) were considered. The questionnaires were distributed among the staff and management of the selected business units. The random sampling techniques were employed in the distribution of the questionnaire. Using the cross-sectional data analysis, the study found that compensation strategy has the potential beneficial effects of enhancing workers' productivity and by extension improving the overall organizational performance. Therefore, the significance of compensation cannot be overemphasized in an organization and is in fact a variable option for attracting, retaining, and motivating employees for improved organizational productivity.

Ayodele (2012) in his paper examined the effect of executive compensation structure and ownership on firm performance. A simple random sampling technique was used to sample 240 personnel from cross-section of banks in Lagos State, Nigeria. A structured questionnaire consisting of 25 items as instrument for data collection was employed. The data were analyzed using chi-square technique. The results of the analysis revealed that there is a significant relationship between management ownership and bank's market value. However, the finding shows that executive compensation structure do not affects bank's market value. The paper also revealed that among larger commercial banks, size is a key criterion in determining executive compensation as it is significantly but negatively related to compensation.

Idemobi, Onyeizugbe and Akpunonu (2011) in a study examined the extent to which compensation management can be used as a tool for improving organizational performance in a typical public sector organization like the Anambra State of Nigeria Civil Service. Guided by the Vroom's expectancy theory of motivation, this study seek to ascertain if financial compensation has a significant relationship with employee performance in the public service using Anambra State Civil Service as a reference. In pursuance of the objective of the study, the descriptive survey design was adopted. Pearson's product Moment Correlation was used for data analysis and Z-test was also used to test the significance of the coefficient of correlation at 5% level of significance. It was found that financial compensation for staff members in the public service do not have a significant effect on their performance and that financial compensation received are not commensurate with staff efforts.

Olalekan and Bodunde (2015) in a study examined the impact of CEO pay on performance of 11 selected Nigerian quoted banks between 2005 and 2012, using a dynamic Generalized Method of Moments (GMM). The study reveals that the CEO pay exerts significant but negative influence on bank performance in Nigeria. This study therefore concludes that rather than being an important corporate governance mechanism to align the interests of CEO with those of shareholders, the CEO pay of Nigerian quoted banks is indeed part of agency problem in the industry.

For studies conducted in Nigeria, we notice the following gaps. Firstly, it appears that not much has been done empirically in this area. Secondly, just as in the case of studies in

developing countries, only accounting measures of firm performance is used ignoring market measures such as stock price and the Tobin Q measure. The neglect of market measures may not provide a well-rounded perspective to the firm performance. Finally, only cash compensation is examined while equity compensation is ignored by studies in Nigeria.

3.0 Theoretical framework

3.1 Agency Theory

Agency theory is at the core of any research trying to determine whether a correlation exists between performance and executives pay. Theory defines how to best categorize relationships in which one party (the principal, defined as the shareholder) determines the work, which another party (the agent, defined as the Chief Executive Officer) undertakes (Eisenhardt, 1985). Amongst other concepts, the theory argues that under difficult monitoring conditions, such as imperfect information and uncertainty, an agency problem may arise in the form of moral hazard. Moral Hazard problems are common in labour contracting issues. It is the condition under which the principals cannot be sure if the agent has put forth his best effort. Moral Hazard problems can be present any time two parties come into a risk sharing agreement with one another, and where their privately taken actions affect the profitability of the total outcome. If this situation were to arise, optimal risk sharing is generally excluded since it will not yield the proper incentives for making the correct decision. Moral hazard problems can take the shape of compensation structure. Since the executive's compensation will be the same regardless of how much or how little the shareholder will benefit from his work, a fix salary might create a disincentive for taking value maximizing risks and putting forth his best effort. In order to resolve this situation, there needs to be a way to substitute some of the risk sharing where benefits of incentives can be achieved. The action, which is optimal for the agent, will depend on the extent of risk sharing between the principal and the agent (Holstrom, 1979). Incentive contracts can yield the proper stimuli for risk sharing. To entice the top executive to perform to the best of their ability, theory on moral hazard problem suggest replacing fixed wages with compensation that is tied to the profits of the company. The provision of ownership right reduces the incentive for executive's moral hazard since it makes their compensation dependent on their performance (Jensen, 1983).

4.0 Conclusion

Executive compensation packages have been viewed as important in mitigating the conflict of interest between managers and shareholders in corporations. It has been widely recognized that compensation packages could potentially play an important role in motivating top manager. Therefore it is important to understand whether there is a link between compensation and performance. This conceptual paper examines the issue using a library-based approach. The findings from majority of the studies show that the executive compensation has a significant effect on firm performance. However, we observed several gaps based on the literature review conducted. For studies conducted in Nigeria, we notice that first, it appears that not much has been done empirically in this area. Secondly, just as in the case of studies in developing countries, only accounting measures on firm performance are used ignoring market measure such as stock price and the Tobin Q measure. The neglect

of market measures may not provide a well-rounded perspective to firm performance. Finally, only cash compensation is examined while equity compensation is ignored by studies in Nigeria. The study concludes that there is the need for further studies to address this gap.

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