AUDIT COMMITTEE AND FINANCIAL PERFORMANCE OF QUOTED INSURANCE COMPANIES IN NIGERIA (2008-2014)

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ABSTRACT

The study examined audit committee and financial performance of quoted insurance companies in Nigeria (2008-2014) with the objective of finding out the extent to which audit committee can affect return on asset (ROA) and Return on Equity (ROE) of the listed companies. In order to achieve the purpose of the study, secondary data regarding the corporate governance practices and financial performance was collected from ten (10) insurance companies listed on the Nigeria Stock Exchange. The data was sourced from the annual reports of the concerned insurance companies. The collected data which was secondary in nature was analyzed using regression analysis. The findings of the study showed that audit committee does not significantly affect the Return on asset of insurance companies. The findings further indicate that Audit committee size does not significantly affect the return on equity of insurance companies in Nigeria. Based on the findings it was concluded that audit committee size does not affect the financial performance of listed insurance companies in Nigeria. Given the findings and conclusion, it is recommended that the enabling laws guiding the code of practice on audit committee and corporate governance should be amended to include that only qualified accountants should constitute the audit committee. Furthermore, the audit committee should be empowered to the extent that their advice and recommendations are given priority attention.

Keywords: Audit committee, Return on Assets, Return on Equity, Insurance companies, Financial performance.

INTRODUCTION

The highest challenge to human being on this earth from time past has been issues arising from risks and uncertainties. This challenge has remained in areas of science and technology over the years. In a bid to address this challenge, insurance which is a product of human mind has been accepted worldwide as an important element in the safeguard of any national economy because it is believed that no current economy can do well in this modern age without fully having the support of a viable and well organized insurance industry.
The insurance sector is understood to be the prime mover of the economy of any nation including Nigeria through its operations. It is the desire of the National Insurance Commission (NAICON) that the sector will unveil those good qualities that would enhance Nigeria economic growth. A good response to this request is the introduction of good corporate governance for the insurance industry.

Corporate governance is referred to as the manner in which companies are directed and managed or controlled. It includes the manner by which the Board and Senior members of the management team are held liable for their actions which are corporate transparency, discipline, social responsibility. Adding to this, Muriithi (2009), corporate governance is the manner in which organizations are controlled, directed and managed. It is an association between company directors, shareholders and other interested members in issues concerning powers of directors, minority interest, employees' rights and creditors' rights. Corporate governance is seen as method adopted to handle business activities of company so as to promote progress with the aim of achieving shareholders long-term value as they take cognizance of the welfare of their stakeholder (CMA Act, 2002). In the views of Jrairah (2014), the audit committees are seen as one of major arms of corporate governance, which have an important duty in ensuring the reliance of the financial statements, enhancing the smooth running of internal control systems and internal audit duties, strengthen the efficiency and autonomy of the external auditor thereby adding to the restoration of confidence on the insurance companies. While Okolie (2014) see audit committee as a mechanism that focuses the company on issues that are important to verify and protect the integrity of the company's financial reporting. It promotes communication between internal audit, external audit and company's board. Again, audit committee is part and parcel of the board which showcases the audit observation and makes these observations to the board in order to ensure fairness and transparency.

However, some studies must have been conducted on audit committee and financial performance of listed insurance companies in western industrialized economics like United States, France, Canada, United Kingdom and Japan, but, to the best of the knowledge of the researchers, there is no study on audit committee and financial performance of quoted insurance companies in Nigeria (2008-2014). Thus, this study fills the gap in literature.

Research Problem

In Nigeria, poor corporate governance practices have made several insurance companies to go out of business, while some have been acquired or merged due to poor performance (Olajide, 2013). There is doubt in the way and manner audit committees discharge their duties because in Nigeria today, there are mass failures of corporate governance that has been noticed in corporate failures. Many companies that have failed have been linked to the non-presence of committed corporate governance element which is audit committee. Several reasons can be said to be responsible for proper impact of the audit committee in fueling good corporate governance in insurance companies and other quoted institutions. Few among them

are; the law did not make provision for any qualifications to membership of shareholder representatives, the consequence being that those who cannot understand or interpret a financial statement get elected to the committee and thereby rendering no value to any committee meeting. There is also no legal restriction on the ratio of the team from the company directors as between executive and non-executive directors. Since it is not clear on who produces the chairman, as a consequence, the practice differs considerably from company to company. National Electric Power Authority (NEPA), Nigerian Telecommunications Limited (NITEL), Nigeria Cement Company Nkalagu, Asaba Textile Industry, Nigerian Railway Corporation (NRC), Cadbury Plc, Leventis Plc. and Benue Cement Company Gboko, as well as several banks are good examples of recent failures in corporate governance linked with audit committee ineffectiveness. Based on this problems noted, there is need to carry out this study on corporate governance audit committee and financial performance of quoted insurance companies in Nigeria from 2008-2014.

Research Aim/Objectives

The aim of this study is to explore how audit committee can affect the financial performance of quoted insurance companies in Nigeria. Accordingly, the main objectives of this study are:

1. Identify the extent audit committee size affects return on asset (ROA)
2. To find out the extent audit committee size affects return on equity (ROE)

Research Questions

1. What is the nature of the relationship between audit committee size and Return on Asset (ROA)?
2. To what extent does audit committee size affect Return on Equity (ROE) of Insurance companies in Nigeria?

Research Hypotheses

Ho_1: Audit committee size does not significantly affect return on assets.
Ho_2: Audit committee size does not significantly affect return on equity.

Theoretical Framework

This study was based on the following theories: theory of inspired confidence and credibility theory.

Theory of Inspired Confidence

This theory came into light in the late 1920s by a Dutch, Theodore Limperg (Hayes et al., 2010). Limperg's theory looks at the demands for and supply of audit services. According to Limperg, the demand for audit services is the direct consequence of the participation of outside stakeholders in the company. These stakeholders need accountability from the management, in return of their contribution to the company. Sometimes, information that is brought by the management may be biased; a possible divergence between the interests in information is required.

With regard to the level of audit assurance that the auditor should provide, Limperg adopts a normative approach. The auditor's job should be carried out in such manner that the expectations of a rational outsider are not thwarted. Hence, given the possibilities of audit technology, the auditor should ensure to meet with public expectation.

Credibility Theory

This theory sees the primary duties of auditing to be the addition of credibility to the financial statements. Audited financial statements are used by management (Agent) in order to enhance the principal's faith on the agent's stewardship and reduce the information asymmetry. Porter (1993) in conclusion say that audited information does not form the primary basis for investor's investment decision. On the other hand, it is seldomly said that financial statements have a duty of confirming the message that was previously issued (Hayes et al., 1999).

Stakeholder Theory

Following the views of Wheeler et al (2002) stakeholder theory was gotten from the amalgamation of sociological and organizational disciplines. Stakeholder theory is seen to be any group or individual who has the ability to affect or is affected by the outcome of organization's objectives. Stakeholder theorists are of the opinion that managers in organizations have chains of people to serve which are employees, and business partners and suppliers, which was further argued that, these chains of people seem to be more important than owner-manager-employee association that is in agency theory. Further, Sundoram and Inkpen (2004) say that stakeholder theory tries to handle the members of stakeholder seeking the attention of the management.

Conceptual Framework

Corporate Governance

Corporate governance is a way by which organizations are handled or controlled which focuses on institutions accountability and transparency with the aim of making stakeholders, employees and consumers satisfied with the operations. Mensah (2003) corroborated by saying that, corporate governance is an arrangement in institution that creates room to checkmate the wrong doings of the managers that are controlling the affairs of organizations and anyone found guilty of any wrongdoing is disciplined. While Lemo (2010) view corporate governance as a body of rules by which companies are administered and controlled by board of directors so as to safeguard the affairs and financial stakeholders that are not part of the management of the firm. Therefore, corporate governance in the insurance companies means adequate internal control measures and rules made by the board of Directors and carried out by effective management with skilled personnel.

Why Good Corporate Governance in Nigeria Insurance Company?

The Nigerian insurance companies need good governance framework to promote transparency and efficient markets, as well as map out the division of responsibilities for different stakeholders in the industry because of the importance of the following issues; "Compliance with rules, laws, regulations and principles guiding insurance business. Differences between the board and management giving rise to board squabbles, ineffective board oversight functions, fraudulent and self-serving practices among members of the board management and staff, overbearing influence of chairman or MD/CEO, especially in family controlled business, weak internal controls, passive shareholders, power of controlling shareholder over minority shareholders, ineffective management information system, increasing level of societal awareness of the sector and conflict of interest" ()

Corporate Governance Code in Nigeria

As the corporate challenges all over the world necessitated the need for corporate governance, Nigeria in a bid to address issues arising from corporate governance joined

others in formulating corporate governance codes to handle matters neither specifically nor sufficiently addressed by the previous legislation. In Nigeria, the very early corporate governance code was linked to the code of corporate governance for banks and other financial institution in Nigeria that was brought out by the bankers' committee in August, 2003 (Demaki, 2011; Komolafe, 2007). According to Okene et al., (2010) the weakness noticed in this code is that it was provided by a voluntary association of the chief executives of Nigerian Banks which made it not to have an impact. This code was closely followed by the code of Best practices on the corporate governance in Nigeria, 2003 which was issued by the Securities and Exchange Commission in 2003. In Nigeria today, there are many codes of corporate governance thus:

(i) Central Bank of Nigeria (CMB) code 2006 for banks established under the provision of the bank and other financial institution Act (BOFIA).
(ii) National Insurance commission (NAICOM) code 2009, directed at all insurance, reinsurance, broking and loss adjusting companies in Nigeria and,
(iii) Pension commission (PENCOM) code 2008, for all licensed pension operators.

These codes, though containing the same key elements of corporate governance, have differences in the content of their provisions and enforcement mechanisms (CBN, 2006; PENCOM, 2008; NAICOM, 2009), (Okene et al., 2010, Udomigie, 2010).

Audit Committee in Insurance Companies

Section 359(3) of CAMA (2004) as amended makes provisions for the establishment of audit committees in public companies in Nigeria, whereby the auditor in case of public company makes report to an audit committee which shall be established by the public company. This provision was further strengthened by section 359(4) that provides that membership of the committee shall be composed of equal number of directors and shareholders' representatives so that the maximum number of members of the committee shall not be more than six. The issue of formation of audit committees in public companies in Nigeria was energized in 2003 by the code of best practices of corporate governance in Nigeria, made available by the securities and exchange commission that affect all the public companies in Nigeria. In the views of Nat (2013), the 2013 SEC Code mandate companies to have audit committees as well as directors' representatives in the audit committee. The 2003 SEC code has now been replaced by the code of corporate governance in Nigeria 2011 issued by the securities and exchange commission that become operational from 1st April, 2011, so, taking a clue from the provisions of the 2003 SEC code, the code of corporate governance for insurance companies in Nigeria issued by the regulator of the insurance industry in Nigeria, national insurance commission (NAICOM), provided for the establishment of audit committees in insurance and reinsurance companies operating in Nigeria.

Responsibilities of Audit Committee in Insurance Companies

The code of good corporate governance for the national insurance commission (NAICOM) allows the audit committee to carry out the following responsibilities:
(a) The committee shall have a written mandate and terms of reference.
(b) The committee shall be responsible for the review of the integrity of the data and information provided in the audit and/or financial reports.
(c) The committee shall provide oversight functions with regard to both the company's financial statements and its internal control and risk management function.

(d) The committee shall review the forms of engagement and recommend the appointment or re-appointment and compensation of external auditors to the board and the shareholders.
(e) Review the procedure put in place to encourage honest whistle blowing
(f) The audit committee shall meet at least three times in a year and at least once with the external auditors.
(g) The committee's performance shall be evaluated periodically.

Empirical Reviews

Okolie (2014) in a work titled corporate governance and audit committee in Nigeria. Here a correlation analysis was utilized and it was noticed that corporate governance principles affect audit committee. Again; Mare, Nabeeh (2009) in their study on the role of Audit committee in improving the internal audit job, in the Jordanian insurance companies. The result showed that there is a role for the audit committee to review the internal audit activities in Jordanian insurance companies. Lee, Mande & Ortman (2004) in their study on impact of audit committee and boards of directors on the auditor's independence. The study found that the independence of audit committees and boards of directors lead to serious cooperation with the auditor. In a study on corporate governance and firm performance: Evidence from the insurance sector of Ghana, it was found out that establishment of audit committee would lead to better corporate performance (Tornyera and Wereko, 2012).

Methodology

The study utilized simple regression analysis with the aid of Statistical Packages for Social Sciences (SPSS) Version 21, on the study that involves audit committee and financial performance of quoted insurance companies from (2008-2014). The study is limited to 10 listed insurance companies in this period due to availability of data. The dependent variable is measured by (RoA and RoE) while the independent variable is audit committees.

$$y = a + bx + u$$

Where Y = dependent variable (financial performance)

X = Independent variable (audit committee)

U = error term

DATA PRESENTATION AND ANALYSES

Ho_1: Audit Committee Size does not significantly affect Return on Asset of Insurance Companies in Nigeria

Table 1: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.130[a]	.017	.001	.1374823

a. Predictors: (Constant), Audit Committee

The model summary in table 1 above shows that the coefficient of correlation ® is 0.130. This means that the strength of the relationship between Audit Committee Size and the Return on Asset (ROA) is just 13.0%. Furthermore, the coefficient of determination (R^2) gave

a value of 0.017 with the implication that only about 1.7% of the variations in the Return on Assets (ROA) of Insurance Companies can be explained or attributed to variations in the Audit Committee Size of the Insurance Companies.

Table 2: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.332	.325		1.023	.310
	Audit Committee	-.057	.055	-.130	-1.040	.302

a. Dependent Variable: Return On Asset

Table 2 above shows that there is a negative relationship between Return on Asset and Audit Committee Size. This is evident from the value of the coefficient of regression (B) of -0.057 which imply that every unit increase in Audit Committee Size, Return on Asset is predicted to decrease by 0.057 units.

Finally, given the value of the calculated T-statistic of -1.040 for the coefficient of Audit Committee Size, we accept the null hypothesis. This is because the critical t-statistic of 1.67 is greater than the calculated t-statistic of -1.040. Thus, conclude that Audit Committee Size Does not significantly affect the Return on Asset of Insurance companies in Nigeria.

Ho_2: Audit Committee Size does not significantly affect Return on Equity of Insurance Companies in Nigeria

Table 3: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.042[a]	.002	-.014	.1839955

a. Predictors: (Constant), Audit Committee

The model summary in table 3 above shows that the coefficient of correlation (R) is 0.042. This means that the strength of the relationship between Audit Committee Size and the Return on Equity (ROE) is just 4.2%. Furthermore, the coefficient of determination (R^2) gave a value of 0.002 with the implication that only about 0.2% of the variations in the Return on Equity (ROE) of Insurance Companies can be explained or attributed to variations in the Audit Committee Size of the Insurance Companies.

Table 4: Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.198	.434		.456	.650
	AuditCommittee	-.025	.074	-.042	-.336	.738

a. Dependent Variable: Return On Equity

Table 4 above shows that there is a negative relationship between Return on Equity and Audit Committee Size. This is evident from the value of the coefficient of regression (B) of -0.025 which imply that for every unit increase in Audit Committee Size, Return on Equity is predicted to decrease by 0.025 units.

Finally, given the value of the calculated T-statistic of -0.336 for the coefficient of Audit Committee Size, we can conclude that Audit Committee Size Does not significantly affect the Return on Equity (ROE) of Insurance companies in Nigeria. This is because the critical t-statistic of 1.67 is greater than the calculated t-statistic of -1.040.

DISCUSSION OF FINDINGS

From the data analyses results shown in the previous section, audit committee does not significantly affect the financial performance of insurance companies in Nigeria in terms of return on asset and return on equity. This findings imply that beyond providing credibility and inspiring confidence in the activities of firms as propounded in theory (Hayes et al., 2010; Sundoram and Inkpen (2004; Porter 1993), the audit committee does play a role in the decision to invest.

Empirically, the findings is in line with that of Ugwoke and Onyeanu (2013) who show in their study on audit committee and corporate performance of quoted companies that the composition of the audit committee can hardly have any significant effect on financial performance. Although they agree that a wrongly composed audit committee will negatively affect the financial performance of the firm. The implication is that audit committees of insurance companies are performing below expectation in terms of oversight functions over accounting and auditing issues of the companies concerned.

CONCLUSION AND RECOMMENDATION

Our findings indicate that there is a weak relationship between audit committee and the return on asset and return on equity. The findings further show that audit committee does not significantly affect the Return on Asset (RoA) and Return of Equity (RoE) of insurance companies in Nigeria. Based on the findings, we conclude that audit committee is not an important factor in the financial performance of listed insurance companies in Nigeria. Given the findings and conclusions as enumerated above, it was recommended that enabling laws guiding the code of practice on audit committee and corporate governance should be amended to include that only qualified accountants should constitute the audit committee. Furthermore, the audit committee should be empowered to the extent that their advice and recommendations are given priority attention.

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