The Effect of Board independence and Audit Committee Independence on Bank Stability in Nigeria (2012-2021)

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Abstract: This study scrutinized the effect of board independence (BIN) and audit committee independence (ACI) on bank stability (BS) in Nigeria from 2012 to 2021 (10years). Secondary data sourced from the annual report of ten commercial bank from the 22 listed commercial banks in Nigeria was used for the study. The study is affixed on the agency theory. The research design employed was ex-post facto. The study analysed the data by the use of multiple regression techniques with the support of econometric view version 9. From the investigation carried out the outcomes revealed that BIN has Positive insignificant effect on BS while ACI had negative significant effect on BS. The study resolves that BIN and ACI has minor effect on bank stability in Nigeria. The study acclaim the need to enlarge the total independent members within the management body so as to enhance stability of banks in Nigeria.

Keywords: Board Independence, Audit Committee, Stability, Banks

1 Introduction

The poor performance of numerous financial firms (banks) is as a result of poor governance practices and the failure of boards of directors to perform their role in the interest of those that have stake in the organisation. This is in line with the assertion of (Aebi et al. 2012; Beltratti and Stulz 2012; Erkens et al. 2012). As cited in Lupu (2015) corporate governance (CG) is significantly important for financial stability and economic growth by ensuring reliability for investors and all stakeholders. Corporate governance will contribute to transparency, disposition to accurate disclosure in accountability and risk management. Corporate governance is the means whereby an organisation is controlled in all entirety so as to achieve its goals and objectives. The term (CG) encompass control mechanism within and outside the organisation that influences how the organisation is run. The internal control mechanism relates to paid persons in the organisation while external control mechanism relates to does that only has administrative interest in the organisation. Aroghene (2021) opined that both internal and external CG mechanisms are used in bank corporate governance. Both the internal and external control mechanism includes ownership structure (OS), CEO duality (CEOD), board size (BOS), board composition (BC), board independence (BI), audit committee size (ACS) etc.

Bank stability (BS) on the other hand refers to how unwavering its operations are over a good number of years. It goes beyond how well it uses its resources to achieve its goals. It has everything to do with its survival in a long period. The continual existence of financial institution (banks) depend on its management. History has it that most institution face instability because of poor management practices by those who are supposed to work in the best interest of the organisation. The failure of numerous banks during the world-wide financial crisis in 2008 led many global institutions comprising World Bank (WB), Organization for Economic Cooperation and Development (OECD) and International Monetary Fund (IMF) and others to focus on the need for the banking sector to improve on its governance framework.

In the case of bank how they manage their asset and liabilities and other decision they make in the institution affects the survival of the bank. As opined by Baker and Powell (2009) the management of bank credit under good CG ensures that shareholders' money is maximised and that banks are stable. The assets of banks comprises loan and advances to customers (both individual, corporate and government) and other interest bearing investment. While its liabilities refers to customers deposits and all other obligations they have to pay. To enhance stability suitable decisions, actions and practices need to adhere to achieve a trade-off between its asset and liabilities. As stated by Eke, Akpanuko and Umofffong (2019) banks were actually struggling financially because the majority of their outstanding loans were non-performing and increased bad debts with little to no provisions for loss. There is also need to adhere to codes governing banks so as to achieve the survival of banks which existence goes a long way in promoting growth in the economy through its intermediation role. Bencharles and Nwankwo (2021) a number of regulations were introduced to prevent executive officers from engaging in financial misconduct and to guarantee banks stability. Thus good (CG) will not only benefit the organisation practising it but also have effect on the economy as well.

Most studies have research on corporate governance mechanism on how it affects banks performance but only few handle the effect of corporate governance on banks stability. Even the few that research on the effect of corporate governance on banks stability, had mixed findings. According to Dong et al. (2017) the faulty application of corporate governance in the banking sector has many negative effects creating higher financial volatility and lower assets quality. Contrariwise, Jiang et al. (2012) find that banks that apply the

principles of corporate governance are more competitive in the long term, because they display a reasonable level of transparency in their financial transactions and accounting and auditing procedures, and this has given them greater financial stability. It is in this regard that this study attempted to use specifically an internal (CG) mechanism (BI) and an external corporate governance mechanism (AC) to evaluate its effect on bank stability.

2.0 literature Review

2.1.1 Board Independence (BI)

The independency of a board has to do with the neutrality of board members. It relates to the proportion of the board that that is free from influence within the board. Raheja (2005) and dong et al. (2017) had addressed the effect of board independence on the banking sector and found that enabling it results in fewer risky decisions and higher financial performance and stability among banks. For this study it would be measured as the percentage of non-executive director on board.

2.1.2 Audit Committee Independence (ACI)

Auditors are those responsible for evaluating the financial records of institution (banks). For the purpose of this study, we will evaluate the aspect of audit committee that has to do with the external auditors and how their activities influence bank stability. Even if Karamanou and Vafeas (2005) believed that larger audit committees might be best at identifying financial problems, Sun and Liu (2014), established a negative relationship between the size of audit committees and the performance of financial firms. For this study ACI would be measured as the percentage of external auditors to total number of audit committee.

2.1.3 Bank Stability (BS)

BS is the survival of banks on a long term.it has everything to do with how well and how far the bank can operate in spite of challenges. Banking stability is the absence of an unexpected disturbance in the delivery of credit, payment systems, and banking services. (Aroghene & Ikeora 2022). The how well and how far banks can go has a lot to do with its management team (both internal and external). BS is the non-appearance of a disruption in the service provision of banks. Caprio, Levine and Barth (2013) opined that weak regulation or ineffective management can lead to bank instability. Although it is strongly advised, strict management did not increase banking stability. For this study BS would be measured as the addition of capital asset rato and return on assets divided by the return on assets standard deviation.

2.1.4 Corporate Governance (CG)

CG is the way corporation is organised and run. It composed of both internal mechanism and external mechanism used to pilot the affairs of an organisation. In 2006 the apex bank introduced codes by which banks are expected to be run. Adherence to the codes is not only beneficial to the financial institution (banks) both also has impact on the economy. Ahmad, Khai and Mohamed (2016) asserted that CG is a structure used for managing a company's affairs to increase corporate accountability and business prosperity and ultimately accomplish the organization's stated goals.

2.2.0 Theoretical Review

2.2.1 Agency theory (AT)

AT is viewed as the major theory when it comes to corporate governance. Daily, Dalton, and Canella (2003) asserted that the theory refers to shareholders as the principal and managers as agents in an agent to principal relationship. In an organisation the owners (shareholders) often expect their staff (managers) to act in their top interests which they might not be ready to implement. In order to avoid this conflict, there has to be a trade-off between the interest of those who manages the organisation and those that own it.

2.2.2 Shareholders' Theory (ST)

ST has to do with maximising the interest of shareholders in the manner that is not contrary to the laws and norm of the society. Olaoye and Adeyemi, (2021) opined that shareholder value or its company's market value, is the standard at which performance is evaluated.

2.3 Empirical Review

Bencharles and Nwankwo (2021) explored the impact of credit risk management on deposit money banks stability and the moderating role of corporate governance in Nigeria (2009-2019). dependent variable is z-score while independent variable are: nonperforming loans, liquid ratio, capital adequacy ratio, loan loss provisioning, bank size and audit committee independence. Descriptive statistics, unit root tests, co-integration tests, random effect (REM) and fixed effect model (FEM) techniques. The findings revealed that NPL had a negative insignificant relationship with bank stability and a positive insignificant relationship with bank stability when corporate governance was introduced. Gbadebo (2014) examined the implications of corporate governance on the performance of Deposit Money Banks in Nigeria using descriptive research design approach. He found among other things that non-compliance to corporate governance code in the Nigerian banking industry hampers banks performance. Akingunola, Adekunle and Adedipe (2013) examined a sample of five banks in Nigeria between 1992 and 2006. They employed Least Square Regression as a method of analysis. It was discovered that independence, fairness, reliance have less positive effect on bank performance. Corporate governance and stock market liquidity were the subjects of Kim's (2010) empirical investigation. They discovered that organizations with superior corporate governance have tighter spreads, higher market quality indices, smaller trade price impacts, and a decreased likelihood of information-based trading. Adegbie, Akintoye, and Ashaolu (2019) investigated how corporate governance affected the financial stability of Nigeria's deposit money institutions (2007-2016). The research design used for the study was ex-post facto. The 21 deposit banks on the Nigerian Stock Exchange that were listed as of September 2016 made up the study's population. Hausman and cross-section random effect tests were examined after descriptive statistics tests had

been run. All corporate governance factors were shown to have both a positive and a negative impact on capital sufficiency in the investigation.CEO/Chairman duality has partial significant impact on firm performance. Board size also did not show significant relationship with firm performance. Firm age has showed significant results except in terms of net profit margin. Firm size has significant results in respect of all measures of firm performance. Mohamed, Hany and Israa (2021) explored how internal governance affect banks' financial stability in Egypt (2010–2019). Z-score was used as the dependent variable meanwhile board size, board meetings, board gender, board education, ownership of shares by directors, board independence and audit committee meetings acted as independent variable. GMM regression analysis was used. Findings showed that the level of banks' financial stability is positively associated with board size, board meetings, and board gender. In contrast, the results show that board education and the ownership of shares by directors are negatively associated with banks' financial stability. More interestingly, our results demonstrate that higher financial stability is significantly associated with lower board independence, the presence of CEO duality, and fewer audit committee meetings. Wang, Lu and Lin (2012) investigated the Relationship of corporate governance with performance of firms in banking sector in US (2005-2010). The explained variable are capital adequacy, asset quality, management, earnings and liquidity whereas the explanatory variables are Board sizes, average age of directors, outside directors, chairman duality, number of committee and auditors. Data envelopment technique and truncated regression was used. The study found that average age of directors, board size, outside directors and chairman duality showed negative relationship with firm performance, while number of committee and auditors showed positive relationship with firm performance.

3.0 Research Methodology

The design used for this study is ex post facto (EPF). EPF design offer solution to the investigations related to a particular research problem. The study's population are the eighteen deposit money bank listed in the NSE as at August 31, 2021 from CBN press release. From which ten banks would be used as the sample. Data were for the period of 2012 to 2021 (10 years). Method of data analyses includes descriptive statistics, multicollinearity test and correlation matrix.data were regressed by the support of 9.0. version of e-view.

3.1 Variables Measurement

The explanatory variables used are board independence (BIN) and Audit committee independence (ACI) whereas bank stability proxied by Z-score was the explained variable.

3.2 Model specification

Mohamed, Hany and Israa (2021) study was engaged to develop the regression model. The model is defined as follows: BS= f (BIN, ACI)

The function model was incorporated econometrically into the regression model as:

BS= β_0+ β_1BIN + β_2ACI+ ϵ

Where;

BS= Bank Stability

BIN = Board Independence

ACI = Audit Committee Independence

ϵ = Error Term

β_0 = Intercept

β_1–β_2 = Coefficient of the Independent Variables.

The a priori expectation is β_1, β_2, is lesser or greater than 0.

4.0 Data Analysis

4.1 Descriptive Statistics

The descriptive statistics are summarized on Table 4.1 below:

	Z_SCORE	**BIN**	**ACI**
Mean	1.414940	0.512748	0.503000
Median	1.414795	0.500000	0.500000
Maximum	1.418281	0.857143	0.750000
Minimum	1.414269	0.100000	0.400000
Std. Dev.	0.000560	0.185034	0.038152
Skewness	3.816164	0.326916	5.109661
Kurtosis	19.81036	2.624220	36.93415
Jarque-Bera	1420.170	2.369611	5233.171
Probability	0.000000	0.305806	0.000000
Sum	141.4940	51.27480	50.30000
Sum Sq. Dev.	3.11105	3.389520	0.144100
Observations	100	100	100

Source: Econometric Views Version 9 (2022).

From table 4.1 above the BS proxied by Z-score shows an average and Std. Dev values of 1.4149 and 0.0006 which indicates that there is slight disparity in the designated banks' stability as seen by their max. and min. values of 1.418 and 1.414. BS is positively skewed (3.82) with a leptokurtic value of (19.81) which shows the actuality of variations within the period reviewed.

The BIN from the table above depicts a mean of 0.5127 and Std. Dev of 0.1850 which connotes slight difference in the independency of board of the banks under review as shown by the maximum value of 0.8571 and the minimum value of 0.1000. This implies that the number of non-executive director to total number of board members differs slightly across banks under review. BIN is positively skewed (0.33) with a platykurtic value of (2.62) which affirms the existence of variants in the period under review.

Also, from the table above ACI has a mean of 0.5030 and 0.0382 as the Std. Dev. The maximum and minimum value stood at 0.7500 and 0.4000 with positive skewness of 5.11 with a leptokurtic value of (36.93)which implies that there is a noticeable variation in the ratio of the number of independent auditor to total number of audit committee of the various bank under study.

Lastly, the Jarque-Bera Probability of the variables showed that BS and ACI are not normally distributed since their probability value is less than 0.05 which can be attributed to

the large range of data. From the table only BIN show normal distribution with a probability value of 0.3058.

4.2 Multicollinearity Test
This is presented in table 4.2 below:

Variance Inflation Factors
Date: 09/26/22   Time: 15:30
Sample: 1 100
Included observations: 100

Variable	Coefficient Variance	Uncentered VIF	Centered VIF
C	5.66E-07	197.2807	NA
BIN	8.61E-08	8.907727	1.017262
ACI	2.02E-06	179.6269	1.017262

Source: Econometric Views Version 9 (2022).

From table 4.2 above, the centered variance inflation factors (VIF) for BIN and ACI are 1.017 and 1.017 which is greater than 0.1 but less than 10. The centered VIF shows that the data set does have multi-collinearity problems.

4.3 Heteroskedasticity Test: Breusch-Pagan-Godfrey

F-statistic	1.897067	Prob. F(2,97)	0.1555
Obs*R-squared	3.764241	Prob. Chi-Square(2)	0.1523
Scaled explained SS	26.29631	Prob. Chi-Square(2)	0.0000

Source: Econometric Views Version 9 (2022).

From table 4.3 above, the Prob. Chi-Square (2) stand at 0.1523 which is greater than 0.05. The aforementioned probability indicates that the data set has homoscedascity and is suitable for prediction.

4.4 Correlation Matrix
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	Z_SCORE	**BIN**	**ACI**
Z_SCORE	1.000000		
BIN	0.144216	1.000000	
ACI	-0.305732	-0.130266	1.000000

Source: Econometric Views Version 9 (2022).

From table 4.4above, BIN is positively related to BS proxy by Z-score with a coefficient of 0.144. This means that rise/fall in BIN will lead to rise/fall in BS. While ACI is negatively related to BS with a coefficient of -0.3057.This implies that increase/decrease in ACI will result to decrease/increase in BS. Also from the table BIN and ACI has negative correlation with one another. Consequently the coefficient values reflect the absence of multi collinearity among the data set.

4.5 Regression Result
This is presented in Table 4.5 below:

Dependent Variable: Z_SCORE
Method: Least Squares

Date: 09/26/22   Time: 15:35
Sample: 1 100
Included observations: 100

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1.416931	0.000752	1883.936	0.0000
BIN	0.000321	0.000293	1.095821	0.2759
ACI	-0.004286	0.001423	-3.012188	0.0033

R-squared	0.104557	Mean dependent var	1.414940
Adjusted R-squared	0.086094	S.D. dependent var	0.000560
S.E. of regression	0.000535	Akaike info criterion	-12.19729
Sum squared resid	2.78E-05	Schwarz criterion	-12.11914
Log likelihood	612.8645	Hannan-Quinn criter.	-12.16566
F-statistic	5.663137	Durbin-Watson stat	1.149455
Prob(F-statistic)	0.004719		

Source: Econometric Views Version 9 (2022).

5 Discussion of findings
From the regressed result in table 4.5, BIN has a positive coefficient of 0.0003 with an insignificant value of 0.2759. This indicates that BIN has minor effect on the stability of banks in Nigeria. This outcome agrees with the result of Akingunola, Adekunle and Adedipe (2013) and Uwalomwa, Dahunsi and Okeme (2021) but differs from the finding of Israa (2021) and Wang, Lu and Lin (2012).

Also from the table, ACI has a negative coefficient of 0.0043 with an associated probability value of 0.0033. This indicates that ACI has negative significant effect on bank stability in Nigeria. The aftermath agrees with that of Gbadebo (2014) and Vasile and Gheorghe (2013) but varies to that of Bencharles and Nwankwo (2021).

Lastly, from the regression result the r-square is 0.1046 while the adjusted r-square is 0.0861 which therefore infers that 10% of the independent variables explained the dependent variable (BS) while the remnants is captured by the disturbance term (ε). The Durbin-Watson stat. is 1.1495 which expressed that the regression model is statistically fit and reliable.

6 Conclusion
The study investigated the effect of board independence (BIN) and Audit committee independence on bank stability in Nigeria from 2012 to 2021. From the analysis it suffice to conclude that both have little impact on the stability of banks in Nigeria.

7 Recommendations
The study recommend as follows:
i   That more variable should be employed to enable in-depth research
ii The need to enlarge the total independent members within the management body

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