

SUSTAINABLE BUSINESS & CORPORATE GOVERNANCE

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EASE OF DOING BUSINESS

If a country does not have a reputation for strong corporate governance practices, capital will flow elsewhere. If investors are not confident with the level of disclosure, capital will flow elsewhere. If a country opts for lax accounting and reporting standards, capital will flow elsewhere. All companies in that country – regardless of how steadfast a particular company's practices may be – suffer the consequences.

Arthur Levitt

Longest serving Chairman

Champion of the individual investor

U.S. Securities & Exchange Commission

(1993 – 2001)

EASE OF DOING BUSINESS

Ranking Indicators

(Political Governance vs. Corporate Governance)

- 1 Ease of Doing Business
- 2 Starting a Business
- 3 Dealing with Construction Permits
- 4 Getting Electricity
- 5 Registering Property
- 6 Getting Credit
- Protecting Minority Investors
- *** 7
- 8 Paying Taxes
- 9 Trading across Borders
- 10 Enforcing Contracts
- 11 Resolving Insolvency

Doing Business is a series of annual reports investigating the regulations that enhance business activity and those that constrain it. Nigeria is ranked 145 in Ease of Doing Business which is one of the eleven ranking indicators, many of them anchored on political governance. But the most critical of these and relevant to CG - protecting minority investors – has been ignored by the 2018 Code even though, ease of doing business is touted as the philosophy underpinning the Code.

The word minority is mentioned only (2) in the body of the 2018 Code and 19 in the 2016 Code.

FUNDAMENTAL MYTHS IN CG IN NIGERIA

1. CG & Law the same: No not the Same: 2(PHds)
2. Example of Statute (USA & INDIA CA 2013))
3. Compliance Frameworks:
 - 3.1 Comply or Explain (wide dispersal)
 - 3.2 Comply or Else (near Mandatory)
 - 3.3 Mandatory Compliance (all Nigerian Codes)
 - 3.4 Apply and Explain; 2018

Question:

Explain to whom? → Controlling shareholders explaining to themselves!!

Baroness Hogg: FRC UK (2012)

FUNDAMENTAL PURPOSE OF CG ACROSS THE WORLD TODAY!

When ownership is separated from control, there tends to emerge a managerial economy in which the interest of managers tends to diverge from the interest of owners.

What, if ownership has not separated from control or has only partially separated as in many Nigerian companies, and also characterized by very significant concentration?

You now have dominant conflicts of concentration (controlling/minorities) rather than those of wide dispersal (shareholders/managers (1 + 1)). Wide dispersal gives you the '*principal-agency*' problem while concentration gives you '*principal-principal agency*' problem (2 + 2).

Question:

Unitary Board Suitability?

Duality Board to the Rescue?

FUNDAMENTAL PURPOSE OF CG ACROSS THE WORLD TODAY!

Some definitions describe corporate
governance as:

Ways in which suppliers of finance to corporations
assure themselves of getting a return on their
investment (Shleifer and Vishny, 1997) or system
by which companies are directed and controlled
(Sir Adran Cadbury Report, 1992, parag. 2.5).

But the fundamental purpose of CG across the
world today is to push the frontiers of good
business beyond law and address the dangers
posed by both shareholder primacy and
shareholder value in the face of competing and
overwhelming stakeholder capital.

NIGERIAN BANKS AS EXAMPLE

There is no Nigerian bank whose equity value is more than 18% to 20% of aggregate assets. Last research puts it at 18% .

What that means is that non-equity holders contribute 82% of capital towards assets, while the controlling shareholders contribute only 18% and use 18% to control assets value of 100%. This is done to the exclusion of the stakeholders, owners of 82% capital.

The 18% can still be reduced by minority 20% free float which gives you 14.4% controlling equity as a percentage of aggregate assets resulting in minorities and stakeholder aggregate capital of 85.6% of aggregate assets.

The controlling shareholders are therefore majority equity owners but minority capital providers, not majority as in the case of stakeholders. Corporate governance definition of '*suppliers of finance who should be assured of getting return on their investment is relevant here*'.

$$\text{Privatization: } 18\% \times 60\% = 10.8\%$$

$$\text{Less Free Float 20\%: } 18\% \times 80\% = 14.4\%$$

CHIEF POLICEMAN: INDEPENDENT NON-EXECS
LEAD INDEPENDENT NON-EXECUTIVE DIRECTOR

Sec. 31 & 32(e) King IV
Sec. 3.1.1 & 3.1.2 of 2018

31. The governing body should elect an independent non-executive member as chair to lead the governing body in the objective and effective discharge of its governance role and responsibilities.
32. The governing body should appoint an independent non-executive member as the lead independent to fulfill the following functions:
- a. To lead in the absence of the chair.
 - b. To serve as a sounding board for the chair.
 - c. To act as intermediary between the chair and other members of the governing body, if necessary.
 - d. To deal with shareholders' concerns where contact through the normal channels has failed to resolve concerns, or where such contact is inappropriate.
 - e. To strengthen independence on the governing body if the chair is not an independent non-executive member of the governing body (King IV: P. 53 (32e)).
 - f. To chair discussions and decision-making by the governing body on matters where the chair has a conflict of interest.
 - g. To lead the performance appraisal of the chair.

CODE 2016 (5 + 1) BOARD COMPOSITION

CODE 2018 (5 + Zero) BOARD COMPOSITION

2016 (5 + 1)	2018 (5 + 0)
1. Controlling Shareholders & Representatives (Shadow)	Controlling Shareholders & Representatives (Shadow)
2. Chairman	Chairman
3. MD	MD
4. EDs	EDs
5. NEDs	NEDs
6. INEDs** oversight committees	Zero *** No oversight
** With a lead, if Chairman is NED.	*** Without a lead, and Chairman is NED, oversight is Zero.

JOINT AUDIT

Multinationality is predicated on concentration. Without concentration, there will be no multinationality because you need the majority equity as a basis for central corporate control – which takes us back to shareholders primacy (1862) and shareholder value.

The need for joint audit in 'concentration' is based on the relatively low value of equity compared to non-equity stakeholder capital. Leaving external audit of significant entities in Nigeria, for example, in the hands of one external auditor using shareholder value and primacy, is leaving audit in the hands of a minority capital providers (equity), to the exclusion of majority capital providers (non equity stakeholders). Multinationality dictates that a secret between two people is a secret, a secret between three people is no longer a secret, hence the abhorrence of a joint audit!!! France disagrees.

The 2018 Committee erred by ignoring joint audit provisions in 2016 Code without a document explaining why, in the form of an Explanation of Material Variations, the sort of document expected from any official Committee in this type of circumstances.

CONTROLLING SHAREHOLDERS CODE 2018 [5+0 CODE]

1. *Committee Remit was to review 2016 Code and make recommendations*
2. *What the Committee did:*
 - 2.1 *It ignored 2016 Code completely and never referred to it once. It ignored its existence.*
 - 2.2 *It re-adopted the 2003 Governance Code as a template, pushing the nation back 15 years*
 - 2.3 *It copied many pages from 2016 Code and never acknowledged it, plagiarism of a particularly bad kind, sending a very bad signal to students in the Universities.*
 - 2.4 *Many academics are on that Committee. I don't know why they allowed or tolerated the plagiarism, whatever the circumstance!*
 - 2.5 *It produced a Code, without tenures, Chairman, MD, ED, NED, no tenure except INEDs that are not wanted, 9 years.*

SUMMARY

1. *Governance Board (2018) is badly structured and skewed towards controlling equity ownership, thus facilitating unchallenged board proposals and strategy.*
2. *Section 359 bundled up, no clarity between Board Audit Committee and Statutory Audit Committee. The Committee did not consider the criticism of Section 359 worldwide.*
3. *Outsourcing of internal audit craftily allowed instead of outright ban (See Carillion, 2018).*
4. *The Code provisions for each of the 3 oversight committees specifically end with 'majority of them should be INEDs, where possible' thus leaving room for majority NEDs on oversight Committees in the country. This does not demonstrate scholarship*
5. *The Chairman of Statutory Audit Committee (SAC) should be selected among its members and should have financial literacy [i.e not necessarily an expert to relate with External Auditors!]*
6. *Minority shareholder protection is nil! All the Code says in Sec. 18.1.3 is that the Board should ensure that 'minority shareholders are adequately protected from abusive actions by controlling shareholders'. No provision to this effect. The word 'minority' is noted in Code 2003 (1), 2016 (19), 2018 (2). 2018 Code seems to derive its template from 2003.*
7. *Where the Regulator is satisfied of abuse of office by Auditor, the word 'Regulator' is now replaced by the word 'Board', and the show of hands voting for auditor removal was deleted and silent to accommodate controlling shareholders who will not remove the auditor anyway.*

CONCLUDING MESSAGE

My own message today can be summarized in these few words: attracting investment requires protecting investors and no country has a divine right to foreign direct investment. In our country today, neither the quality of law nor its enforcement can be said to be very adequate. We do not as a Nation have an enforceable concept of the fiduciary duties that controlling shareholders, directors and managers owe to investors – particularly the minorities. Nigerian companies are increasingly reliant on stakeholder capital, but do everything imaginable to avoid adequate internal or external oversight. Investor protection requires both law and regulation. Investors whether equity or loan will not invest in a country or company regarded as unstable, corrupt or utterly lacking basic protections for their investments and rights. Nigeria needs a very strong Code. The world will see through any weak and deceptive Code. We should not try it!

Victor Odiase

9th July, 2018