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DOES OPTIMAL BOARD STRUCTURE INFLUENCES DIVIDEND POLICY OF THE NIGERIAN DEPOSIT MONEY BANKS?

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Abstract

This study examines whether optimal board structure influences dividend policy of the Nigerian Deposit Money Banks (DMBs). Optimal board structure in the contest of this study is defined in term of appropriate board size with greater proportion of independence. It postulated that the board of directors comprises of executive and non-executive directors and its size depends on the complexity of their business. The study relies on agency and resource dependency theory of corporate governance to explain the inconsistency in the board structure of an organisation. Several literatures were reviewed to justify the reality of governance as critical factors that may influence dividend policy. The paper utilized panel data approach and stata software package was used to analyse the data collected from 8 deposit money banks spinning from 2010 to 2019. Findings from the result suggest that executive directors positively drive dividend policy but not significant while non executive director is negative but significantly influence dividend policy. The earnings per share is positive and also significant. The study also confirms that optimal board sizes represented by dummy variables are not significant in the Nigerian banking sector. The study recommends that commercial bank should fix their board size in line with their circumstances and policy should be directed to improve the independence and quality of non-executive directors present in the board.

Keywords: Board Structure, Dividend Policy, Executive Directors, Earnings Per Share

1. Introduction

Several researches have been carried out on board structure and firm's performance without considering dividend policy. Some authors also focus on firm's specific factor that affects dividend policy. Little is known about the board of directors, its size, independence and appropriateness as a mechanism for board effectiveness to alleviate payment of dividend to shareholders who invested their hard earned incomes in the organisation. Generally, the board of directors' focuses on approving strategic goals and plans of the corporation, setting general policies, guiding corporate affairs, and approving major expenditures. In addition the code of corporate governance issued in 2006 for bank in post consolidation period in Nigeria, which was further revised in 2014 and harmonised with other sector by financial reporting council in 2020; recognised that the board of directors particularly commercial banks is expected to comprise qualified individuals that are familiar with the oversight functions with high degree of independence from management, individual, shareholders and must be responsible for effective control of the banks. In order to allow for independence, the code of corporate governance in Nigeria permits the number of non-executive directors in the board to be greater than the executive directors up to maximum of 20 board members.

Dividend policy is the decision of the board to pay dividend to the shareholders or retain the earning in the organisation for further investment in profitable project. Dividend itself is defined as part of organisation profit after the obligation of all fixed income holders has been met (Olowe 2010). It is usually payable at the end of financial year after the final accounts are ready and the

amount of distributable profits is available. Normally, it is distributed among the shareholders in proportion to the amount of paid-up shares capital. Dividend for a financial year of the company is called final dividend and payable only if it is declared by the company at its annual general meeting on the recommendation of the board of directors. Sometimes interim dividends are also paid by the board of directors between two annual general meetings without declaring them at an annual general meeting. Thus board of directors play significant role on the recommendation, approval and payment of dividend to the stockholders. This further suggests that the actions and attitudes of board of directors determine dividend policy. Consequently, there is need for effective board of directors to promote strong governance in the interest of shareholders and enhance dividend payment in the hand of the shareholders. Without strong governance, performance would be low and the expectation of the shareholders in term of dividend payment may be misplaced. (Awotundun, Arewa & Yunisa 2017)

The nexus between optimal board structure and dividend policy is based on agency and resource dependency theory of corporate governance. The proponent of agency theory particularly Jensen & Meckling (1976), Jensen (1993), Ghosh (2003) appear to favour smaller board of directors while advocate of resource dependency such as Dalton, Daily, Joihanson, & Ellstrand (1999) tilt toward large board size. Thus the inconsistency between these theories pose question whether optimal or appropriate board structure that would improve payment of dividend to shareholders exists. To the best of my knowledge the question appears not to be adequately answered particularly within the content of Nigerian banking sector. The main objective of this study is to test whether optimal board structures that influence dividend policy of commercial banks in Nigeria exist. The rest of this paper is divided into conceptual theoretical and empirical review, methodological approach, data analysis, discussion of finding, summary, conclusion and recommendation.

2. Conceptual, Theoretical and Empirical Review

Optimal board structure is defined in terms of appropriate board size with greater proportion of independence. The board of directors comprises of executive and non-executive directors and its size depends on the complexity of business and availability of relevant experience La Porta, Lopez-de-Silanes, Shleifer, A.& Vishny (2000). The executive directors consist of inside directors who are key corporate executive of the firm. Non executive directors are outside directors and may include executives from other companies, major shareholders, and national or community leaders (Gitman and Zutter, 2015). Appropriate board structure is also concerned about the issue of board independence. The number of non-executive director present in the board may have an influence on shareholders expectation in form of dividend payment. Independent directors facilitate continual monitoring of the firm by the market participants. Thus effective board may help to minimise the excesses and recklessness of the directors, whereas ineffective board structure may promote unethical behaviours among board members thus diminish firm's performance and dividend payment (Awotundun 2016). Despite number of impressive and quality paper on board of directors the aspect of optimal board structure has been a mirage.

Agency theory stresses that shareholders hire paid managers to run the affairs of the company and as the managers gain control of the corporation, they pursue action that benefit themselves and not the firm owners (Jensen & Meckling, 1976).The principal can minimise conflict of his

interest by establishing appropriate incentives for the agent and by incurring monitoring costs designed to limit the aberrant activities of the agent. In some situations, the agents may expend resources (bonding costs) to guarantee that he will not take certain actions which would harm the principal or compensated the principal if he does take such actions. However, it is difficult for the principal or the agent at zero cost to ensure that the agent will make optimal decisions from the viewpoint of the principal (Jensen & Meckling, 1976). In order to effectively minimise the agency's problems, the theorists advocated board restructuring as an instrument by the owners in subduing the opportunistic behaviour of managers (Stiles & Taylor, 2001). For example Fama and Jensen, (1983) suggested clear separation between management and control. Similarly, Agrawal and Knoeber (1996), Bhagat and Black (2002) and Petrovic (2008) supported greater representation of independent external directors and board size that make management's manipulation difficult.

Resource dependency theory was developed by (Pfeffer, (1973) and further enlarge by (Pfeffer & Salancik,1978). The theory emphasises the important roles played by board of directors in providing access to crucial resources that would enhance the company's performance and protect it against externalities (Tornyeva & Werekó, 2012). It evaluates the board of directors through their expertise, reputation, value added and link to other firms; the proponent of the theory suggests that organisation rely on external board members for provision of resources. Thus resource dependency theory provide for networking relationships among corporate organisation; ensure access to critical resources for organisation survival and emphasis on the role of the board beyond the traditional control stipulated by agency theory; but directed interest to wide board member to attract resources for the organisation (M'ithiria, Musyoki & Shawa 2017).

Early study on dividend policy started with the work of Linter (1956) directed attention on specific factors such as previous dividend and earnings per share as the determinant of dividend policy. Some other study such as the work of Soyode (1975), Nyong (1990), Ade legan (2001) and Musa 2009 found support for Linter (1956) model. Current literatures are now considering elements of corporate governance particularly board structure and it appropriateness. For instance some authors favour smaller board of directors why other argues for large board size. The advocate of agency theory argued that large board size may give rise to excessive compensation, low firm performance, free riding, inefficient decision-making, and weak monitoring (Jensen & Meckling, 1976; Fama, 1980; Ghosh, 2003; Ali & Teulon, 2014; Reddy, Abidin, & You, 2015). Thus chief executive officer could easily manipulate the board to achieve personal interest. The perception of resource dependence theory supports the inclusion of large board size as mean for access toward external resources, greater knowledge, and more vigorous skills to the organization (Dalton, Daily, Johnson, & Ellstrand, 1999). In order to mitigate the inconsistency concerning the optimal board structure, several studies are now examining element board structure and it optimality and on firm performance as well as dividend policy.

Hussain, Mahfuzur & Ridzuan (2020) examine the influence of board traits on dividend payout policy in Malaysia. The authors considered elements board structure such as board size and independence as determinant of dividend policy using 336 non-financial firms spanning from 2005 to 2016. Findings show that significant positive relationship exist between board size and dividend policy while negative but insignificant relationship was found between number of independent directors and dividend policy. The authors support larger board size but fail to determine the optimal board size among firms.

Mohammed, Saleh & Islam (2020) investigated board characteristic and firm performance from Palestinian Listed Companies. The study focuses on some attribute of board structure among was the size of the board of directors. The authors utilize 150 observations of non-financial firms listed on the Palestine Security Exchange (PSE) during the period from 2011 to 2016. The results show that the larger the board sizes the better firm's performance. Moreover, the study is limited to board characteristic without considering reasonable board size for non-financial listed firms in Palestine

Suwaidan & Khalaf (2020) investigated the effect of board composition and ownership structure on dividend policy on manufacturing companies listed on the Amman Stock Exchange for the period of 2013 to 2015. The study employed board size, board independence represented by percentage of non executive directors to board size, board gender and duality and earnings per share as its explanatory variables. Panel data comprises of 53 quoted manufacturing companies were utilised. Finding shows that board composition particularly percentage of non executive directors to board size was positive but not significant. The study also finds earnings per share, board size and duality to be significant positive. However the study ignores the issue of optimal board structure.

Naburi & Ndede (2019) Investigated board composition and dividend decisions of companies listed at the Nairobi Securities Exchange Kenya. The study considers board structure particular board independence, director skill and board diversity in their variable dimensions. The authors relied on both primary and secondary data comprises of 64 firms covering 2011 to 2015. Findings from the analysis of the secondary data show that board independence has negative significant relationship with dividend decision while board skill and diversity were positive but significant. However the study is limited to board composition without considering the optimal board structure.

Yahya, Ghazali & Ntim (2017) examined how board governance and dividend policy could influence pay performance link in the capital market of Pakistan. The study use panel data consisting of 219 non-financial firms over the period 2012–2016. Finding confirms that board independence and optimal board size could positively moderates the relationship between operating performance and chief executive officer compensation. However, the study emphasises much on aligning performance to CEO compensation instead of dividend payout to shareholders.

Kurawa and Ishaku (2014) explored the impacts of corporate governance on dividend policy of 5 commercial banks that were listed as at 2014 in the Nigerian Stock Exchange over the period of 2003 to 2012. The study considered elements of board structure such as board size, board independence and board duality in their specification. Findings reveal that all the variables have positive relationship with dividend policy except board independence which exhibited negative sign but was not significant however the study appears to focus on board size, board duality and equity holding but ignore board composition as well as optimal board size in Nigeria.

3. Methodology and Models

The study employs panel data which is made up of time series and cross sectional data. Panel data could be generated by pooling time-series observations across a variety of cross-sectional

units. The sample size comprises of 8 deposit money banks that have record of dividend payment between periods of 2010 to 2019. The study specifies the following model which is consistent to general form of panel data model as follows:

Optimal Board structure and dividend policy

$$dps_{it} = \lambda_0 + \beta_1 \log exd_{it} + \beta_2 \log nexd_{it} + \beta_3 eps_{it} + \beta_1 dumbs_{it} \leq 10 + \beta_2 dumbs_{it} \leq 11 + \dots$$

$$\beta_{19} dumbs_{it} \leq 19 + \mu_{it1} \dots \dots \dots (1)$$

$$dps_{it} = \lambda_0 + \beta_1 \log exd_{it} + \beta_2 \log nexd_{it} + \beta_3 eps_{it} + \beta_1 dumbs_{it} \geq 6 \leq 8 +$$

$$\beta_2 dumbs_{it} \geq 9 \leq 11 + \beta_3 dumbs_{it} \geq 12 \leq 14 + \beta_4 dumbs_{it} \geq 15 \leq 17 + \beta_2 dumbs_{it} \geq 18 \leq 20 + \mu_{it1} \dots \dots \dots (2)$$

$$\mu_{it1} = \mu_i + \mu_t + \varepsilon_{it1} d \dots \dots \dots (3)$$

Where

dps_{it} = dividend per share denote total dividend divided by total shareholding outstanding
 $\log exd_{it}$ = executive directors represents number of executive directors present in the board,
 $\log nexd_{it}$ = non executive directors represents number of non executive directors present in the board and denote board independence

(eps_{it}) = represent the earnings per share and it is the control variable.

$dumbs_{it} \leq 10, dumbs_{it} \leq 11 \dots \dots dumbs_{it} \leq 19$ = are various level of optimal board size for the study. Optimal board size denotes by dummy where board size fall within the values and ranges specified it is one otherwise it zero. The dummy is specified as a whole number in equation (1) while equation (2) specified the dummy as a range of value.

μ_{it1} is a normal distributed random error which is decomposed into unobserved heterogeneity effect between banks μ_i and the time effect μ_t while ε_{it1} represents time varying error term.

$\beta_1, \beta_2 \dots \dots \beta_{19}$ are set of parameters to be estimated, subscript i is denoted by banks and time period is denoted by t. The a priori expectation $\beta_1, \beta_2 \dots \dots \beta_{19} > 0$

The data sets for the study were obtained from the annual reports and statement of accounts of DMBs in Nigeria for the period of 10 years beginning from 2010 to 2019. The data collected are on dividend per share, executive directors, non executive directors and earnings per share while dummy were used to define various level of optimal board size.

4. Results and Findings

The descriptive statistics show the mean, standard deviation, minimum and maximum values of the variable series specified for the study. The summary of these statistics are presented in table 1 as follows:

Table 1: Descriptive Statistical Values

Variables	Dps	Exd	Ned	Eps
Mean	0.5279018	5.330357	8.276786	0.8773357
Std deviation	0.5898002	2.085507	1.781839	2.103986
Minimum	0	1	2	-13.57
Maximum	2.8	9	12	8.74

Source: STATA Output, 2020

Table 1 reveals that all the variables dps, exd, ned and eps have positive mean value exhibit increasing tendency throughout the sampling period. The average value of dividend per share (dps) is approximately 0.53; while that of earnings per share (eps) is 0.88. It is obvious that

banks paid dividend out of profit to shareholders. In addition, dividend per share ranges between 0 to 2.8 revealing that there are instances where dividends are not paid and the maximum dividend paid during the period of investigation is 2.8 kobo per share. Earnings per share also range between -13.57 to 8.74. Showing evidences of losses and gains in the banking sector. In addition, the earnings per share (eps), executive directors (exd) and non executive directors (ned) appear to be more volatile with standard deviation of 2.10, 2.09, and 1.78 respectively than the dividend per share (dps). This suggests that the independence variables are frequently changes but dividend payment to shareholders is fairly static. This implies that some banks pay same dividend over years. Again the executive directors (exd) ranges from minimum of 1 to 9 at maximum while the non executive directors (ned) comprises of minimum of 2 to maximum of 12. This confirm that the non executive directors present in the board is greater the executive directors and is in agreement with provision of code of corporate governance.

The study conducts Breuesch and Pegan Langrangian Multiplier test to check for appropriate model between pool and random effect .

Table 2: Breuesch Pegan Langrangian multiplier test for random effects estimated results

Var	Sd=.Sqrt(var)	
Dps	0.3478643	0.5898002
E	0.1344417	0.3666629
U	0	0

Test: var(u) = 0

Chibar2 (01) = 0.00

Probability > chibar2 = 1.000

Table 2 reveals the result of Breuesch and Pegan Langrangian multiplier test between pool and random effects. The chibar2 statistics has probability value of (1.000) which is greater than 5%. This confirm that pool effects model is appropriate than the random effects. Thus the study relies on the result of the pool model to explain the relationship between optimal board structure and dividend policy as shown in table 3.

Table 3: Optimal Board Structure and Dividend Policy

Variables	Coefficient	Standard error	Z- Statistcs	P-value
Logexd	0.1638005	0.5036423	0.33	0.745
Lognxd	-1.831476	0.8761093	-2.09	0.037
Eps	0.1349505	0.0234116	5.76	0.000
dumbs ≤ 10	- 0.3879642	0.2806251	-1.38	0.167
dumbs ≤ 11	- 0.1514738	0.2756896	-0.55	0.583
dumbs ≤ 12	0.2221298	.2019841	1.10	0.271
dumbs ≤ 13	0.0087748	0.2103381	0.04	0.967
dumbs ≤ 14	-0.080916	0.177653	-0.46	0.649
dumbs ≤ 15	-0.0262282	0.1908443	-0.14	0.891
dumbs ≤ 16	-0.0044943	0.2045932	-0.02	0.982
dumbs ≤ 17	0.1597025	0.3649907	0.44	0.662
dumbs ≤ 18	0.1702716	0.4798082	0.35	0.723
dumbs ≤ 19	-0.2457846	0.4386707	-0.56	0.575

Constant	1.966975	1.352485	1.45	0.146 -
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R- sq = 0.4193

Wald chi2(5) = 70.76

Prob > chi2 = 0.0000

Source: STATA Output, 2020

Table 3 captured the expression that relates optimal board structure and dividend per share. The results confirm that the coefficients of executive directors (logexd = 0.1638005) with p-value of (0.745) indicating that the executive directors paid dividend but not significant. The coefficient of non executive directors (lognexd= -1.831476) with p-value of (0.037) implied that non executive directors significantly diminished payment of dividend. However executive directors conform to prior theoretical expectation while non executive directors did not.

Earnings per share (eps) have a positive coefficient (0.1349) and p-value of (0.000) which is less than 5%. This implies that earnings per share of deposit money banks are positive and significant in determining dividend policy of commercial banks. This again complies with theoretical expectation. The coefficient and the corresponding p-value of optimal board size of dumbs ≤10 (-0.3880 ; 0.167) dumbs ≤11 (-0.1515 ; 0.583) dumbs ≤12 (0.2221 ; 0,271) dumbs ≤13 (0,0088 ; 0.967) dumbs ≤14 (-0.0809 ; 0.649) dumbs ≤15 (-0.0262 ; 0.891) dumbs ≤16 (-0.0045 ; 0.982) dumbs ≤17 (0.1597 ; 0.662) dumbs ≤18 (0.1703 ; 0.723) dumbs ≤19 (-0.2458 ; 0.575). This confirm that optimal board size is positively related to dividend policy with exception of dumbs ≤10, dumbs ≤11, dumbs ≤14, dumbs ≤15, dumbs ≤16 and dumbs ≤19 but none of them is significant in the contest of Nigerian banks. This suggests that optimal board structure do not exist in Nigerian banks. In view of this findings the study further perform additional test by using range of values to represent optimal board size. The result is shown in table 4 below.

Table 4: Optimal Board Structure and Dividend Policy

Variables	Coefficient	Standard error	Z- Statistcs	P-value
Logexd	0.2929312	0.3428573	0.85	0.393
Lognexd	-1.8536	0.6319891	-2.93	0.003
Eps	0.1476349	0.0225773	6.54	0.000
dumbs ≥9≤11	0.256678	0.2255128	1.14	0.255
dumbs ≥12≤14	0.408243	0.2622848	1.56	0.120
dumbs ≥15≤17	0.4129946	0.3203064	1.29	0.197
dumbs ≥18≤20	0.2335595	0.4120717	0.57	0.571
Constant	1.53381	.5525981	2.78	0.006

R- sq = 0.3960

Wald chi2(7) = 68.19

Prob > chi2 = 0.0000

Source: STATA Output, 2020

Table 4 provides corroborative evidence of expression of relationship between optimal board structure and dividend policy. The result is similar to what is obtained in table 4.3. The coefficients of executive directors (logexd = 0.2929) with p-value of (0.393) indicates that the executive directors paid dividend but not significant. The coefficient of non executive directors

(lognxd= -1.854) with p-value of (0.003) implied that non executive directors significantly diminished payment of dividend. Earnings per share (eps) remain positive in line with theoretical expectation but significant influence dividend per share of banks. The coefficient and the corresponding p-value of optimal board size at various range are dums $\geq 9 \leq 11$ (0.256678 ; 0.255), dums $\geq 12 \leq 14$ (0.408243 ; 0.120), dums $\geq 15 \leq 17$ (0.4129946; 0.197), dums $\geq 18 \leq 20$ (0.2335595 ; 0.571). This confirms that optimal board size is positively related to dividend policy but none of the range of value is significant in determine dividend policy of Nigerian banks. This again suggested that optimal board structure do not exist in Nigerian banks. The post estimation test of the two model revealed that the R- Square of the first and second model in table 3 and 4 are 0.4193 and 0.3960 respectively are very good. The R-Square indicates the extent to which the explanatory variables explained dividend per share. The probability values of Wald statistics for both models are significant at 5%. Thus confirm both models are well fitted.

4.1 Discussion of Findings

The nexus between optimal board structure and dividend policy revealed mixed reaction. The results of this study revealed evidence of negative but significant relationship between board independence represented by non-executive directors and dividend policy. This result contradict the work of Yahya, Ghazali & Ntim (2017) in Pakistan, Hussain, Mahfuzur, & Ridzuan (2020) in Malaysia and partially supported by Kurawa & Ishaku (2014) in Nigeria but in line with Naburi & Ndede (2019) in Kenya. In addition the study also confirmed positive but significant relationship between earnings per share and dividend policy as suggested by Linter 1956; Adelegan 2003; Musa 2009. The result of dummy variables indicated that none of the board size as well as range of value specified as optimal board structure was significant. Thus the study confirms that optimal board structure does not exist in the Nigerian banking sector. This in fact differ from the perception of advocate of agency theory particularly Jensen & Meckling, (1976) Fama, (1980) Ghosh, (2003) Ali & Teulon, (2014) Reddy, Abidin, & You, (2015) who argued against large board size. The study also contradict the postulate of resource dependency theory such as Dalton, Daily, Johnson, & Ellstrand, (1999) who provided support for large board size. Thus this study suggest that the number of directors present in the board may be small or large depend on the situation that are peculiar to each banks. By implication, Investors should be aware that board size may not be defined in the banking sector and non executive directors appear not to favour the payment of cash dividend. This is obviously another reason why dividends are not paid some of the time.

5. Conclusion and Recommendations

The study examines the relationship between optimal board structure and dividend policy of banking firms. It identifies optimal board structure in term of the executive directors, non-executive directors and reasonable number of director present in the board. It argues that appropriate number of executive and non executive directors present in the board would driver dividend policy. The study was based on agency and resource dependency theory of corporate governance. Several literatures were reviewed to justify the reality of governance as critical factors that may influence the return of the shareholders. The study employed panel data approach and used stata software package to analyse the data collected from commercial banks. Findings from the result suggest that executive directors positively drive dividend policy but not significant while non executive director is negative but significantly influenced dividend policy. The study also confirms that optimal board size that is the number of executive and non executive directors that would influence dividend policy cannot be defined within the contest of

Nigerian banks. Board size is situational among Nigerian banks. On the basis of this conclusion the study recommends that commercial bank should fix the board size in line with their prevailing circumstances and policy should be directed to improve the independence and quality of non executive directors so as to enable them to check the excesses of executive directors and improve dividend policy.

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