
DIRECTORS' COMPENSATION AND PERFORMANCE OF SELECTED QUOTED FIRMS

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Abstract: This study focused on examining the relationship between directors' compensation and firm performance using selected general insurance companies as a case study. The main objective was to investigate the relationship that exists between directors' compensation and firm performance. Eight general insurance companies which were listed in Nigeria Stock Exchange (NSE) were studied. The study covered a five (5) years period of 2009-2013. The time frame used considered the recapitalization in the insurance industry that occurred in 2007. The research made use of secondary data which were collected from the published annual reports of the eight (8) general insurance companies under study. The data was analyzed using the regression analysis. The results from the analysis led to the major findings of the study. Return on Assets (ROA) and net claims paid (NC) were used to establish a relationship between with directors' compensation. The results show that there is a significant relationship between annual directors' compensation and firm performance of the general insurance companies under study. The relationship with return on assets showed a significant but negative relationship, while that of net claims paid was significantly positive. The study suggests that efforts to improve the payments of claims should focus on compensation directors satisfactorily. However, proper care should be taken in making such decisions as the

shareholders; value may be affected due to the negative relationship between directors' compensation and return on assets.

Keywords: Investment, Profitability, Decision, Maximization, Finance

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INTRODUCTION

Complexity of directors' compensation continued to be a source of concern to researchers and academicians as they continue to dedicate time and effort to understand the numerous factors underlie top management compensation and how it is related to firm profitability (Sarker & Jafar, 2012; Yablon, 1999). Obasan (2012) is of the view that compensation strategy is one of the most important strategies in the human resources management functions as it influences the productivity and growth of an organization. Yatim (2012) opines that remuneration and incentive systems have been shown to play a key role in influencing risk-taking behaviours of managers in recent years. Improvement of corporate governance standards and disclosures has been at the lead of international debate in recent times, and compensation of directors and executives is one of the key concerns in this debate. The insurance industry is becoming increasingly important to economic stability and development of many nations as it helps to reduce the burden of risks of individuals and businesses. Growth in insurance industry therefore remains one of the major indices for measuring the level of development of a nation' wealth plays very significant roles in the mobilization of investible resources of an economy and gives greater security to the fortunes of the common people among the whole society. However, in Nigeria today, there is a concern and public outcry over some challenges that seem to be plaguing the insurance industry. It is a

common complaint that insurance companies in Nigeria are performing below expectation as compared to companies of other industries in Nigeria. There is also a public outcry that insurance companies in Nigeria do not settle claims promptly when due, and in most cases only with the intervention of the regulatory bodies.

This is substantiated with Business Day (2014) publication of 17th July 2014 on the successful facilitation of 83 claims payment by NAICOM between January 2014 and June 2014 but the outstanding complaints standing at 189. This must be a most visible effect of an underlying problem. Board compensation is an important area to look at as the major of directors is to monitor management and create wealth and value for the company while the directors in turn are compensated for this fiduciary function. The questions that plague the mind of the researcher include: Are directors of insurance companies in Nigeria suitably compensated to motivate them to carry out their oversight functions? Could there be a link between directors' compensation and firm's performance? Given the challenge above, this research work was carried out to find out if director's compensation in general insurance companies in Nigeria are significantly related to the profitability of the industry.

Research Objectives

The broad objective of this study is to examine the relationship between directors' compensation and firm performance in selected general insurance companies in Nigeria.

However, in more specific terms, the study seeks to accomplish the following objectives is to:

1. Investigate if there exists a significant relationship between directors' annual compensation and return on assets in Nigeria general insurance companies.
2. Examine if a significant relationship exist between directors' annual compensation and annual net claims paid in Nigeria general insurance companies.

3. Evaluate if there exists a significant relationship between directors' annual compensation and net annual premium earned in Nigeria general insurance companies.
4. Examine if there is any significant relationship between directors' annual compensation and earnings per share in Nigeria general insurance companies.

Research Questions

To achieve the aim of the research, this study seeks to answer the following questions:

1. Is there any significant relationship between directors' annual compensation and Return on Assets in Nigeria general insurance companies?
2. Is the relationship that exists between directors' annual compensation and annual net claims paid in Nigeria general insurance companies?
3. Is there any significant relationship between directors' annual compensation and net annual premium earned in Nigeria general insurance companies?
4. To what extent does the directors' annual compensation affect the earning per share in Nigeria general insurance companies?

Research Hypotheses

To accomplish the research objectives and give meaningful answers to the research questions, the following null and alternative hypotheses are to be tested:

Hypothesis 1

H₀: There is no significant relationship between directors' annual compensation and return on assets in Nigerian general insurance companies.

H_A: There is a significant relationship between directors' annual compensation and return on assets in Nigerian general insurance companies.

Hypothesis 2

H₀: There is no significant relationship between directors' annual compensation and annual claims paid in Nigerian general insurance companies.

H_A: There is a significant relationship between directors' annual compensation and annual net claims paid in Nigerian general insurance companies.

Hypothesis 3

H₀: There is no significant relationship between directors' annual compensation and net annual premium earned in Nigerian general insurance companies.

H_A: There is a significant relationship between directors' annual compensation and net annual premium earned in Nigerian general insurance companies.

Hypothesis 4

H₀: There is no significant relationship between directors' annual compensation and earning per share in Nigerian general insurance companies.

H_A: There is a significant relationship between directors' annual compensation and earning per share in Nigerian general insurance companies.

Review of Literature

Compensation can be said to be a reward given to individuals within an organization for the time, strength, intuitive ability and skills that have been contributed for the achievement of organizational goals and objectives. Obasan (2012) explains that compensation is often viewed as direct and indirect monetary and non- monetary rewards given to workers on the basis of the value of the job, their personal for performance can be significant, tend to focus on monetary rewards because individuals are ready to substitute non- monetary for monetary rewards as money represents a generalized claim on resources. Talha Sallehuddin and Masuod (2009) view directors'

compensation as the payment made for services or employment of directors on the board of a corporation. This includes the basic salary and other monetary or non-monetary benefits that an executive receives during his or her tenure. For the non-executive, it includes the allowance that he receives based on his frequency at board meetings, and chairmanship of a committee. The way a company rewards its executive can have a major influence on the company's success in meeting its strategic objectives. It can also have an impact on the company's reputation and its relationship with the stakeholders.

Abdullah, Parj and Haruna (2014) are of the opinion that organizations exist based on conviction of an internal and external party. As an internal party, the board of directors is the highest governing body and the most important component as a workforce in a company to achieve the companies' goals and objectives. Therefore the organizations usually compensate the BODs for their effort diligence in managing the company through salary, bonus, allowances, fees and shares. In today's practice the share option or stock option grants are new instrument of compensation introduced for the board of director in aligning their interest with shareholders. As a result, top management will be motivated to work towards achieving the firms' performance. However there is a major issue as regarding the compensation. This is where the compensation given and the performance or contribution towards the companies are not aligned. Sinclair (2004) examined stock and stock option compensation separately, as the two forms of compensation are likely to differ in their motivational effects. The result of their analysis proposes that there is a relation between stocks based director compensation and firm performance.

Some psychologist and behaviourists are of the view that monetary reward is counters productive. Deci (1972) cited by Obasan (2012) argues that money lowers employee motivation by decreasing the "intrinsic rewards" that employees collect from the job. Slater (1980)

explained that “getting people to chase money produces nothing but people chasing money and thus using money as a motivator leads to a progressive degradation the quality of everything produced. In his article incentives can be bad for business Kohn (1988) offers several reasons why merit pay system is counterproductive. First rewards could act as an encouragement to people to merely focus on a task, to do it as fast as possible, and to take little risks. Second, extrinsic rewards can wear down intrinsic interest. Finally, people could come to see themselves as being controlled by a reward. A second group of merit pay opponents argue that while financial incentive schemes increase productivity in principle, in practice they include adverse side effect that are expensive to employee morale and productivity.

Some insurance companies reduce their risk by further insuring themselves through reinsurance companies and so they also receive claims. Net claims paid arise from the total claims paid by an insurance company after deducting the claims received from reinsurance companies insurance commission of western Australia (2008) define net claims incurred as an expenses comprising of claim paid (including claims settlement cost) and the movement in the liability for outstanding claims, net of reinsurance and other amount burden borne by the insurance company. According to Ashturkar (2014a) the most important services that an insurance company gives to its customers is the claim settlement to its policyholders. Tajudeen and Adebowale (2013) took a position that claims management can be seen as an essential tool of image boosting in insurance industry. The excellence in claims handling of an insurance company gives it an edge over its competitors. Atkins and Bates (2007) assert that claims provide an insurer the opportunity to make a favourable impression on the policyholder. Butler and Francis (2010) citing Banjo (1995) indicates that insurers need to take their claim handling function more seriously because if a claim is handled well, it results to higher customer retention but if handled poorly, policyholders will lose confidence in the insurer and this may damage its most cherished reputation. Furthermore, Ashturkar (2014b) explain that claims

settlement even influence the market share of insurance companies. According to the author, growth of the market share of an individual insurance company to a great extent depends upon the attention given by it to the claim settlement process and its proportion.

There has been a collapse of large corporations such as Enron in 2001, Rank Xerox in 2000, global crossing and world com. This is due to certain corporate malpractice. The insurance industry also has similar cases. Momoh and Ukpong (2013) attested to this by noting these scenarios. They stated that Skandia the largest insurance company in Sweden and a world leader in the provision on variable annuities and other savings, had its own share of the corporate fraud in 2003 when three of its top executives were put under investigation for the misuse of corporate assets. Also, in 2007, when recapitalization occurred in Nigeria insurance industry, Lion of African insurance company went into liquidation because its assets could not cover up its liabilities and the board of directors were blamed for this predicament. In the year 2000, the equitable life assurance society, UK collapsed due to the unlawful usage by directors of resources that were targeted towards subsidizing current annuity rate policies. The above incidences and many more have caused a renewed interest of many researchers in the effectiveness of board monitoring and the compensation that directors receive. To this effect, this study is not one of the pioneering works in this field as the issue of whether directors' compensation leads to better performance in corporate firms has met great attention from a wide number of researchers all over the world. Nordin (2008) explored the link between directors' remuneration and firms' performance within the Malaysia's listed companies using data from annual report and data stream for the 2001- 2006 period. The relationship between directors' remuneration and government ownership was also examined. The variables used in this study were directors' remuneration, firms' performance (ROA, ROE, MBR and Tobin & board size), firm size and industry. The study employed regression method in determining the relationship of the variables.

The result showed that there was mixed link between directors' remuneration and firms' performance.

Matowanyika et al (2013) carried out a research with an attempt to discover if the remuneration of directors is aligned with corporate performance as reflected by the prices of corporate shares. Their result indicated a weakening positive correlation between directors' remuneration and corporate performance over two years. To this effect, the research came to the conclusion that directors remuneration in Zimbabwe is not linked to corporate performance. They however, added that the good corporate governance was lacking in most of the companies, and there was a dearth of information as regards directors' remuneration. Matowanyika et al. (2013) citing the work of Dandira (2011) explained further that the investigations carried out in Zimbabwe by the labour and economic development institute of Zimbabwe (LEDDRIZ) indicated that most CEOs received salaries that were above US\$15000 per month in addition to telephone allowance of US\$500 per month, housing allowances that range from US\$300 to US\$2500 and children education allowance of US\$2500 per child for each term for a maximum of three children. The author added that some executive on request are entitled to entertainment allowances while some other receive flat fees, fully funded pensions, hundred percent medical coverage and daily allowance of US\$40 for lunch. As noted by the author some of these companies are struggling for survival.

Jaafar et al (2012) examined the relationship between director remuneration and performance in Malaysia family firm. The proxies of director remuneration include fees, salary, bonuses and benefits of kin. The dependent variables (performance) were measured by ROA and ROE. A panel analysis of 537 firms from 2007 and 2009 found that the relationship between director remuneration and performance is significantly positive. However, the results of some other research works have shown that the compensation of directors, to a great extent, has an impact on the performance of firms. In relation to

Australians banking, Doucouliagos (2007) carried out a research in an attempt to explore the relationship that exists between the pay of directors and chief executive officers (CEOs) and the performance of firms in that sector. To establish a relationship with remuneration, the study used market based measure of performance (Earning per share and Shareholders' Return) vis-à-vis accounting based measures of performance (Return on Assets and Return on Equity) Using a time lag in their analysis, the compensation of Australian directors did not appear to be linked with performance with performance with a one year lag. However, putting a longer time horizon into consideration, their study showed pay- performance relationship for directors arises over time.

In relation to the insurance industry, Tornyeva & Wereko (2012) investigated the relationship between corporate governance and the financial performance of insurance companies in Ghana. The authors collected secondary data from the national insurance commission and the primary data through the administration of questionnaires. Panel data methodology was adopted for the data analysis. The findings of the study showed that large board size, board skill, management skill, longer serving CEOs, size of audit committee audit committee independence, foreign ownership, institutional ownership, dividend policy and annual general meeting are positively associated with the financial performance of insurance companies in Ghana. Yusuf and Dansu (2014) examined the relationship between claims cost and profitability in the non- life sector of the Nigerian insurance industry. The study also developed two linear regression models. Data were generated from the financial statement of ten(10) insurance companies covering a period of ten years (2002- 2011). These data were analyzed using descriptive statistics, coefficient of determination (R²), ANOVA (F), standard error test, test of correlation (T), multiple linear regression and ordinary least square Regression techniques. In addition, two hypotheses were also tested. The results revealed that profitability correlates directly with net claims and ER expense ratio but correlates inversely with Loss Ratio. It also showed

that for every one present increase in net claims, there will be a corresponding increase of 36.7% in LR.

Finally, the study of Tajudeen and Francis (2014) is similar to this study. The authors examined the relationship between claims cost and profitability in the non-life sector of the Nigerian insurance industry. The study covered ten insurance companies covering a period of ten years, from 2002-2011, for which data was gotten from the financial statements. The results revealed that profitability correlates directly with net claims and expense ratio but correlates inversely with loss ratio.

Methodology

This adopt descriptive research design using a five years comparison from 2009 to 2013, this study carried out the analysis of the secondary data collected from the annual report of the eight Nigerian general insurance firms using regression analysis done. This is line with the previous studies of Matowanyinka, et al. (2013), Doucouliagos at al. (2007) and Uwuigbe (2011). Cross sectional data was used as the collection of data will be carried out once. The research method used is quantitative.

Population of the Study

The study population consisted of 8 general insurance companies listed in the Stock Exchange which have been in existence as at the beginning of the time frame used (2009) and whose annual report is available on their corporate website. The time frame considered for the study will be 2009 to 2013. The five year period allowed for possible significant changes that might have occurred over time in the insurance industry due to the recapitalization that was effected in year 2007. Also the time frame chosen considered the introduction of corporate governance codes in the industry as at 2009.

Sampling Techniques

Three criteria are identified for the general insurance companies to be chosen. They must have been identified as general insurance companies on the official website of NAICOM, they must also be listed in the stock exchange and they must have annual reports from the beginning of the time frame (2011). As at the 3rd of March, 2015, there were 58 insurance companies, out of which 30 are general insurance companies. As at the 3rd of March 2015 27 insurance companies were listed in the Nigerian stock exchange. 19 of them are general insurance companies. The researcher did not intend to study all the 19 publicly listed general insurance companies. Only those companies whose annual reports were available and accessible were included in the study. So the study consists of 8 general insurance companies whose annual reports were complete for this study. General insurance companies under the direct control of NAICOM were also left out.

Methods of Data Collection

As a result of the nature of the study to be carried out, this research deals with data from secondary sources. The data used for the study was secondary data derived from the audited financial statement as shown in the annual reports of the general insurance companies. The companies used are listed in the Nigerian stock exchange. They also must have been in existence between the five years period of 2009 and 2013. The annual reports were obtained from their corporate websites and so the financial statements in the published annual reports were gotten from the websites of the companies concerned.

Data Presentation, Interpretation and Analysis

Regression analysis was used to investigate the extent to which directors' compensation is related to the performance of the companies (performance of the companies is proxied by three variables which include net claims, return on assets and net premium).

Table 4.1 Regression Statistics for Net Claims

Regression Statistics	
Multiple R	0.965894113
R Square	0.932951437
Adjusted R Square	0.910601916
Standard Error	107878462.6
Observations	5

Source: Author's computation

The results in table 4.1 above indicate that the adjusted R square value is 0.91 thus indicating that 91% of the variation in net claims is accounted for by the variations in directors' compensation

Table 4.2 Analysis of Variance for Net Claims

ANOVA					
	Df	Ss	Ms	F	Significance F
Regression	1	4.85803	4.85803	41.74369	0.00752
Residual	3	3.49133	1.16378		
Total	4	5.20716			

Source: Author's computation

The table for the analysis of variance which is represented in table 4.2 above indicates a calculated F statistics of 41.74 with an asymptotic significance probability of 0.007 thus indicating that the test is significant at a 99% confident level. The implication is that the overall significance of the model is good. In other words, the simple linear model is a good fit for the data

Table 4.3 T – Test and P- value for net claims

	Coefficients	Standard error	T stat	P value	Lower 95%	Upper 95%
Intercept	-149728416.3	157538733.1	-0.9504	0.412	-651086975.3	351630143
DC	22.71535023	3.515798914	6.46094	0.00752	11.52650897	33.9041915

Source: Author's computation

The T-Test for significance of regression parameters represented in table 3 shows a calculated value of 6.460935563 for directors' compensation with an associated asymptotic significance probability of 0.007 thus indicating that the test is significant at a 99% confident level. The T- test shows 149728416.3 as the constant while the coefficient of directors' compensation (DC) is 22.7. This mean that net claims (NC) = 149728416.3 + 22.7 DC. The implication of these results is that the effect that directors' compensation has no net claims is significant.

Table 4.4 Regression Statistics for ROA

REGRESSION STATISTICS	
Multiple R	0.9059313
R Square	0.820712118
Adjusted R Square	0.760949491
Standard Error	1.102701436
Observations	5

Source: Author's computation

The results in table 4.4 above indicate that the adjusted R square value otherwise known as the coefficient of determination is 0.76 this indicating that 76% of the variation in return on asset (ROA) is accounted for by the variations in directors' compensation.

Table 4.5 Analysis Of Variance for ROA

ANOVA					
	Df	Ss	Ms	F	Significance F
Regression	1	16.69848	16.69848	13.7328654	0.034140859
Residual	3	3.647851	1.21595		
Total	4	20.3434			

Source: Author's computation

The analysis of variance table indicates calculated F statistic of 13.73 with an asymptotic significance of 0.03 thus indicating that the test is

significance at a 97% confidence level. This implies that the simple linear regression model is a good fit for the data.

Table 4.6 T- Test and P- Value for Return on Assets

	Coefficients	Standard error	T stat	P value	Lower 95%	Upper 95%
Intercept	9.645	1.1031	5.9893	0.0093	4.51985	14.76933
DC	-1.3318	3.59374	-3.706	0.0341	-2.4755	-1.8808

Source: Author's computation

Table 4. 6 indicate 9.644589933 as the constant of the relationship between ROA and DC. The coefficient of DC is -1.33. This implies that ROA and DC are inversely related. The T- test for significance of regression parameters shows a calculated value of -3.705 with a significant probability of 0.03 thus indicating that the best is significant at a 97% confidence level. The implication is that the relationship between return on assets and directors compensation is significant.

Table 4.7 Regression Statistics for Net Premium

REGRESSION STATISTICS	
Multiple R	0.560450222
R Square	0.314104451
Adjusted R Square	0.085472601
Standard Error	14671654.32
Observations	5

Source: Author's computation

The result in the above table shows that the value of the adjusted R square (coefficient of determination) is 0.085 thus indicating that 8.5% of the variation in net premium accounts for the variation in directors' compensation.

Table 4.8 Analysis Of Variance for Net Premium

ANOVA					
	Df	Ss	Ms	F	Significance F
Regression	1	2.9573	2.9573	1.373843808	0.32576394
Residual	3	6.45772	2.1526		
Total	4	9.41502			

Source: Author's computation

The analysis of variance table shown in table 4.8 above shows a calculated F statistic of 1.37 and a significant probability of 0.32. This shows that the relationship between net premium and directors' compensation is not significant.

Table 4.9 T- Test and P- Value for Net Premium

	Coefficients	Standard error	T stat	P value	Lower 95%	Upper 95%
Intercept	332207.56	36700265.72	0.0091	0.9933	-116464417	117128832.6
DC	0.0139	0.01183	1.1721	0.3258	-.02378429	0.051518784

Source: Author's computation

The T- test for significance of the regression parameters shows that the intercept is 332207.5523 while the coefficient of net premium is 0.014. This means that $DC = 332207.6 + 0.014 NP$. The relationship between directors' compensation and net premium is not significant since the P- value is 0.33.

Hypotheses Testing

Earlier two testable hypotheses were formulated on the relationship between directors' compensation and firm performance. It is on these hypotheses that this study is anchored. In this section, the hypotheses are subjected to empirical testing drawing from the results of the statistical analyses. The decision rule is based on the adjusted R square and the T- statistic represented by the P- values. As said by Agbonifoh and Yomere (1999), it can be inferred from a significant t- statistics the extent to which a significant relationship exists.

Hypothesis 1

H₀: There is no significant relationship between directors' annual compensation and return on assets in Nigerian general insurance companies.

H_A: There is a significant between directors' annual compensation and return on assets in Nigerian general insurance companies.

In the first hypothesis, the null and alternative hypotheses were formed. For the null hypothesis, it was assumed that the relationship between directors' annual compensation and return on assets is not significant. For the alternative hypothesis, it was assumed that the relationship between directors' compensation and return on assets is significant. From the analysis on table 4.4, the adjusted R square showed the coefficient of determination as 0.76. It means that 76% of the variation in return on assets (ROA) is accounted for by the variation in directors' compensation (DC). The T- test shows that ROA and DC are inversely related as the coefficient of DC and the T statistic is -1.33 and -3.7 respectively. The P- value is 0.03. Since $p < 0.05$, the relationship is significant. Thus the relationship between ROA and DC is negatively significant. Based on these results, since the negative effect is significant, we therefore reject the null hypothesis and accept the alternate hypothesis which states that there is a significant relationship between directors' compensation and return on assets.

Hypothesis 2

H₀: There is no significant relationship between directors' annual compensation and annual net claims paid in Nigerian general insurance companies.

H_A: There is a significant relationship between directors' annual compensation and annual net claims paid in Nigerian general insurance companies.

In the second hypothesis, the null hypothesis assumed that there is no significant relationship between directors' compensation (DC) and net claims paid (NC). The alternative hypothesis assumed that the

relationship between DC and NC is significant. Table 4.1 indicates that the adjusted R square value is 0.91 thus indicating that 91% of the variation in net claims is accounted for by the variation in directors' compensation. The P- value is 0.007. Since $p < 0.05$, this result implies that directors' compensation has a significant and positive impact on net claims paid. The null hypothesis is rejected and the alternative hypothesis is accepted.

Hypothesis 3

H₀: There is no significant relationship between directors' annual compensation and net annual premium earned in Nigerian general insurance companies.

H_A: There is a significant relationship between directors' annual compensation and net annual premium earned in Nigerian general insurance companies.

In the third hypothesis, the null hypothesis states that the relationship between directors' annual compensation and net annual premium earned is not significant. For the alternative hypothesis, it was assumed that the relationship between directors' compensation and net annual premium earned is significant. From the analysis on table 4.7, the adjusted R square showed the coefficient of determination as 0.09. It means that 9% of the variation in net annual premium earned is accounted for by the variation in directors' compensation (DC). The T- test shows that net annual premium earned and DC are positively related as the coefficient of DC and the T statistic is 0.0139 and 1.172 respectively. The P- value is 0.03. Since $p < 0.05$, the relationship is significant. Thus the relationship between net annual premium earned and DC is positively significant. Based on these results, since the positive effect is significant, we therefore reject the null hypothesis and accept the alternate hypothesis which states that there is a significant relationship between directors' compensation and net annual premium earned.

CONCLUSIONS AND RECOMMENDATIONS

Empirical findings shows the net claims paid are positively and significantly related to the directors' annual compensation. Also directors' compensation and return on assets negatively and significantly related. In addition, empirical findings shows the net annual premium earned are positively and significantly related to the directors' annual compensation. It is therefore recommended that efforts to improve total directors' compensation should focus on the efficiency of claims payment to the insured. It is also recommended care should be taken while increasing directors' annual compensation as it has a negative relationship with shareholders' return on asset.

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