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Using Structural Equation Modeling to Relate Enforcement and Board Performance

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Abstract: *Purpose*: Enforcement is reported as key to effective corporate governance. But in an emerging nation like Nigeria, where structures and enforcement mechanisms have been reported weak, there is the need to examine factors responsible. This paper takes steps towards developing a stakeholder perspective to examine any relationship between enforcement structures and board performance for effective corporate functioning. Methodology: Based on survey perceptions of 154 respondents from the Nigerian regulatory enforcement agencies and sampled public firms, the study employs confirmatory factor analysis (CFA) in a structural equation modeling (SEM) approach; a model that relates three enforcement structure variables to board performance is proposed. *Findings*: Building upon enforcement structure construct based on stakeholder framework, the study found the dimensions of regulatory capacity, monitoring compliance, and enforcement mechanisms as the valid measures. The study concludes that enforcement has significant effect on board performance. However, regulatory capacity indicators correlate as valid measures. Hence, confirmed through CFA and the structural model (SEM). *Originality*: The paper explores new research idea on board and focus on strenghtening regulatory framework by Nigerian enforcement agencies. This adds to knowledge, enhances regulatory capacity and reduce conflicts of interests. The SEM approach exposes firms to an appropriate and efficient legal, regulatory and institutional foundation upon which all market participants can rely in establishing their contractual relations for effective functioning.

Key words: Enforcement Structure · Regulatory Capacity · Monitoring Compliance · Stakeholder Theory · Board Performance

INTRODUCTION

As a result of prevailing reported cases of unethical practices in corporate entities, attributable to poor governance and weak enforcement that led to many corporate failures; countries, multilateral organizations and professional bodies seek ways of checkmating the ugly menace. Nations review existing regulations and codes, enacting new laws and new regulations and instituting more proactive steps to strengthening compliance with accounting and governance rules [1]. Though countries may differ in establishing their corporate statutory frameworks, the general pattern has been the government regulations and professional bodies.

On this interest, [2] encourage broader theoretical perspectives, methodological approaches, accountability mechanisms, sector analysis, developing economy studies and time horizon. The authors affirm that regulation is a mechanism of governance, and is usually studied at the country level [3] or the firm. They adopt an analytical frame of reference, and locate seven studies in the special issue in a framework of analysis showing how each one contributes to the field. Some are relevant to the focus of this paper. For example, using stakeholder theory, [4] focuses on regulators, lenders and tenants as other dimensions of corporate governance.

In this respect, perhaps influenced by the common-law similarities or a case of forceful/voluntary legal transplant, the Nigerian Companies and Allied Matters

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Act 1990 (CAMA) is largely modeled on the UK Company Act 1948. According to Rashidah and Mohammed (2010), the imposition of colonial laws is an example of forced transplant, while borrowing of laws for the purpose of legal harmonization is an example of voluntary transplant. In the area of corporate governance, concepts and ideas, as well as laws and regulations are freely borrowed between jurisdictions [5-8]. Hence, countries once colonized by the British would adopt UK Companies Act. Under the Nigerian CAMA, section 310-312 allows minority shareholders to seek redress in court against any governance malfunction. However, Amao & Amaeshi (2007) observe that despite the statutory provisions; communication gap, lack of timely and inappropriate AGM information, apathy, and weak judicial court system to check management excesses, all hinder coordinated board progress.

In addition, [9] assert that in many developing and transition countries, few of the traditional corporate governance mechanisms will be effective because the general enforcement environment is weak and specific enforcement mechanisms function poorly. They affirm that enforcement more than regulation or voluntary code is the key to effective corporate governance. They provide a framework for linkage, as they affect firms' ability to commit to outside investors and other stakeholders. In line with their findings, specific Nigerian studies found governance structure characterized by weak compliance and enforcement [10] & Wilson, 2006), which could hinder board performance.

In this circumstance, policymakers normally focus on increased deterrence, which in practice usually means more enforcement. After all, if compliance is 100%, there will be less need for enforcement. Therefore, this necessitates that; Nigerian firms ought to strengthen internal enforcement mechanisms to complement the public regulatory enforcement bodies and empower them with full capacity to monitor and enforce compliance with governance rules for optimum benefits [10]. Though effective enforcement requires a lot of expenditure, it is assumed that the benefits the economy yields may outweigh the cost. Therefore, dimensions of enforcement structures could explain effective board performance.

As a motivation for this paper, the voluntary status of the Nigerian code means legal sanctions are not provided for non-compliance. However,[9] report that enforcement more than voluntary code is the key to effective corporate governance in transition and developing countries. In addition, [10] reports Nigerian regulatory enforcement bodies lack the capacity to enforce compliance with regulations, coupled with very low penalties for major offences (Okike, 2007). This is not desirable in a lower middle income country craving for local and foreign investments to boost economy. Thus, the need for functional structures and managerial control to protect outside investor. In this regard, Doidge Kardyi & Stulz (2007) report that, the presence of legal and regulatory protections for investors explain up to 73% of the decision to invest. By implication, gaining investor confidence through coordinated board performance can help Nigeria come up in the rankings, which will lead to increased foreign investments, employment generation, enforcing contracts and less cost of monitoring.

The paper proceeds with the review of relevant literature and hypothesis development in section 2. How the research was conducted is explained in the methodology section. Data analysis and the research findings are presented in section 4. The paper discusses the findings, relates implications for theory, practice and regulatory policy, and finally conclusion is presented with agenda for future research in section 5.

Literature Review and Hypothesis Development: The subject of enforcement has attracted increased attention in recent years. Berglof and [11] opine that enforcement more than regulations or voluntary codes is the key to effective corporate governance, at least in transition and developing countries. Corporate governance and enforcement mechanisms are intimately linked as they affect firms' ability to commit to their stakeholders, in particular to external investors. The authors further observe that when the general enforcement environment is weak and specific enforcement mechanisms function poorly, as in many developing and transition countries, few of the traditional corporate governance mechanisms are effective. In other words, effective industry (internal) and regulatory agencies (external) enforcement mechanisms can mitigate the potential costs that come along with these structures if the goals are to be achieved.

Dewing and Russell (2008) examine corporate governance regulation from the individual regulated. They use content analysis to examine the Financial Services Authority (FSA) in the UK, they also interview high-level individuals in the financial services industry and by way of illustration, they analyze the outcome of FSA enforcement actions against individuals. Similarly, [12] examines the regulatory reform of US SOX to normalize the behavior of managers and accountants.

In a related development, [13-14] observe that, the goals are less likely to be achieved without regulatory oversight that promotes rigorous monitoring and consistent enforcement of applicable accounting standards. This means that governance standard setting is futile in the absence of enforcement, and as such, the extents to which governance standards are enforced and violations prosecuted are as important as the standards themselves. Furthermore, Saudagaran & Diga (1997) opine that, "the best accounting standards are only as good as the effectiveness of the regulatory process". They affirm that, in an emerging capital market, systematic inquiry needs to be made regarding the strength of the regulatory mechanisms, and factors limiting their effectiveness. They further opine that, the enforcement stage in emerging capital markets should be given to the entity equipped with the power to enforce, which is the government. Government agencies will perform functions similar to the SEC in the US: formulating rules for issuance of securities, approving offers of securities and listings, and defining the overall direction (governance) of capital market development.

Conversely, as the emerging capital market reach a particular size and attain a greater number of well trained professionals, regulators may allow the private sector, i.e. stock exchanges to play more active role in enforcing governance standards since in many developing countries enforcement is a big problem. This is because corporations, akin with human behavior are likely to take advantage if nobody takes action when rules are breached; the result is that the rules remain requirement only on paper [15].

A definition of enforcement has been provided by the Committee of European Securities Regulators [16]. "Enforcement is monitoring compliance of financial information with the reporting framework and taking action in the case of infringements." This means that, for any enforcement body or mechanism to function effectively, it must have a quality reporting framework issued and developed by experts in accounting and auditing. Enforcement differs significantly across countries, even being non-existent in some countries. However, even in the EU and other regions across the world, several countries do not have an oversight system. The several EU countries needed to set up enforcement mechanisms or extend the activities of existing enforcement bodies [16]. A study conducted by [13] explore matters regarding uniform enforcement in the EU. They reviewed activities in France, Germany, the Netherlands and the UK in setting up and modifying enforcement bodies before 2005. They tested current developments against the Federation des Experts Comptables Europeens [17] recommendations and against the principles for effective enforcement proposed in [16]. They conducted 23 interviews to representatives of the countries' enforcement bodies. To complement their data, they gathered views from top four big audit firms, the IASB, FEE and EFRAG about the challenges of achieving effective uniform enforcement. They found that, since enforcement remains the responsibility of each EU member state, the goal of uniform enforcement raised a particular challenge, namely the coordination of enforcement activities and sanctions and that uniform international standards can only be maintained if interpretation advice emanates from a central source, in this case the IASB and IFRIC.

The FEE (2002) [17] essential features for an effective enforcement body are: support for high quality corporate governance and external audit; high quality, expert, globally consistent decisions on important issues; freedom from bias; transparency and clear procedures; confidentiality and speed of action; avoidance of making detailed accounting rules; focusing resources; rectification of defective financial information; and finally, sanctions.

In addition, the principles guiding effective enforcement recommended by [16] are: the purpose of enforcement; definition of enforcement; competent enforcement bodies; delegated responsibility; compliance with the standard; features of enforcement bodies; powers; responsibilities; application; documents; ex-post enforcement; ex-ante enforcement; procedures; interim procedure; extent of review; material misstatement; and enforcement actions.

In the foregoing, this means that a country's judicial system might be functioning well but enforcement of regulations lacking. It is difficult, however, to think of a situation in which the judicial system in general works poorly (as the case in Nigeria) but enforcement of standards is strong. The assessment of judicial efficiency produced by the country-risk rating agency Business International Corporation "may be taken to represent investors' assessment of conditions in the country in question" [3]. The second component of enforcement, rule of law, as seen in [15] assesses a country's law and other tradition [3]. If no one cares, regulations covering the content of financial reports are not likely to be effective. Assessments of tradition for law and order are produced by the country-risk rating agency 'International Country Risk'.

While academics and practitioners agree on the importance of enforcement as an essential element of the corporate governance infrastructure, there has been little research on enforcement in an international setting. One potential explanation for this is that it is not easy to measure enforcement across countries [14-13-15]. Likewise, it is also difficult to measure enforcement on firm-level components but it remains an important constituent of corporate governance especially in emerging Nigerian market.

In Nigeria, [10] reports enforcement to be weak. The team stated that powers of the regulatory enforcement bodies are important because of the relatively inefficient court system. The perception in the market is that while the court system is actively used to resolve shareholder disputes, it takes many years to receive a judgment. Therefore, a lot depends on the powers granted to the regulatory bodies, such as the SEC, CBN, NAICOM and the NASB. As earlier stated, according to [10] report, the SEC does not have an effective mechanism for monitoring compliance or for punishing issuers that violates the rules since no effective regulatory mechanisms exist to impose sanctions on managers and boards. The only current penalties are fines and de-listing. However, since the number of listings is seen as a measure of the success of the stock exchange, relative to its international competitors, the de-listing penalty is rarely applied.

Moreover, there is the need to review the current legislation on penalty of fines in the Corporate Affairs Commission (CAC) because [1] observes that if the CAC is to fulfill its role of adequately promoting good corporate governance, its monitoring role needs to be strengthened, and more realistic sanctions applied to erring companies. For example, the penalty for contravening section 19(3) of the Act is N25, the equivalent of $0.16 cents, which is the number of persons that can form a company, association or partnership. Also, the penalty of contravening section 348(1-3) of CAMA 1990 in relation to defective financial statements for companies is N100 ($0.66 cents) and for group financial statements, the penalty is N250 ($1.66). Obviously, companies may opt to pay this token amount and present financial statements that do not give a “true and fair view” since the punishment in the legislation is not sufficient to serve as deterrence. In other words, where compliance with standards is legally required, companies may not comply if it is perceived that the consequences of non compliance are not serious [1].

Similarly, Obazee (2009) reports the need to address institutional issues, especially those relating to enforcement. He observes that, with the confusion created by multiplicity of laws in Nigerian regulatory bodies, enforcement should be clearly vested on one body, such as Financial Reporting Council (consistent with World Bank recommendation) in order to avoid many non-compliance issues passing unnoticed.

Hence, reported weak enforcement affect corporate governance as well, because the Nigerian Accounting Standards Board is also responsible for preparing governance standards and all corporations and enforcement agencies are guided by the same legislation, which has direct effects on Nigerian listed firms. For example, financial statements that lack the required qualities can be considered inaccurate and misleading, which perhaps are prepared with the intention to deceive or conceal some ulterior motives by officers responsible for their preparation. Such deceptions could be, among others, lead to concealment and distortion of accounting records, falsification and/or omission of transactions, deliberate misapplication of governance rules to perpetrate frauds, which indicate consequences of weak enforcement.

Akin to nations with emerged capital markets, there have been so many reported cases of financial scandals in Nigeria. This makes it imperative to overhaul the present regulatory framework as recommended by local and international researchers. As a step-forward, the Nigerian government has started responding to some of the recommendations by establishing a financial reporting council (FRC), in place of the current Nigerian Accounting Standards Board. This is an important policy decision because the establishment of an oversight body such as the FRC is one of the requirements of the European Union to allow financial audit in its jurisdiction. So far only two African countries meet the requirement, South Africa and Mauritius. The Financial Reporting Council in Nigeria is responsible for issuing accounting, auditing and governance standards for both private and public sectors. It is also the only body responsible for licensing, regulating, and ensuring compliance and enforcement of the standards. As an oversight body, it provides a barrier against undue influence by bodies (seven directorates) constituting its establishment ICAN (2009). But its effective functions, in addition to the rules backing it, largely depends on functional enforcement mechanisms.

Also, on behalf of the SEC, the Nigerian Stock Exchange monitors compliance with financial reporting requirements of companies, whose equity or debt

securities are publicly traded. The capacity of SEC to effectively monitor compliance with accounting standards is inadequate, though it is undergoing re-organization. There have been instances where companies have been suspended from the NSE for breach of financial reporting requirements. However, SEC enforcement is weak, and administrative sanctions (e.g. restatement at the cost of the company) and civil penalties are not adequate to deter non-compliance [10].

According to [17] to ensure an efficient corporate governance structure, it is essential that an appropriate and efficient legal, regulatory and institutional foundation be established upon which all market participants can rely in establishing their private contractual relations. The [17] principles of corporate governance further state that a corporate governance framework will typically comprise elements such as legislation, regulation, voluntary commitments, and business practices that are based on a country's specific circumstances such as history and tradition. On the wave of this interest, new experiences are being witnessed even in Africa, judging from the worldwide trend of recognizing other significant stakeholders in governance structures for sustainability, and the changed business circumstances of achieving wider objective functions (King Committee, I; II & III). Therefore, an adjustment in the content and structure of the governance framework in Nigeria may be required.

In this respect, it has been mentioned earlier that [18] is one of the major corporate laws regulating business operations in Nigeria, which provides for the protection of shareholders, functions of directors and audit committee. However, weak regulatory framework, slow legal processes, and high-level corruption have been reported as factors hindering effective corporate governance in Nigeria [10-19-1-20]. Therefore, stakeholder theory view the corporation as an enduring social institution, with personality, character and aspirations of its own, with proper interests of a wide range of stakeholder groups, and with public responsibilities, such as government regulatory and enforcement agencies.

However, the OECD principles assume that all countries have efficient legal system and the means and capabilities to enforce it as obtained in the developed member-nations the organization's principles represent. [12] examines the impact of government, governmental techniques, and regulatory reform to normalize the behavior of managers and accountants. The regulations examined are the US SOX, characterizing the power relationships of government, and the social construction of corporate governance and reforms through autonomous agents, including managers and accountants.

In developing countries, practices of self-dealing and insider trading are widespread. Such offences are usually unpunished because in Nigeria, the penalties are minor [1] and even if there are stiff penalties in theory, enforcement is lax [10-20]. Even the professional auditing associations in Nigeria lack the capacity to impose effective sanctions on their erring members [10-19]. Government departments and independent regulators responsible for monitoring and enforcement are generally weak, and subject to external influence by politicians [19]. Unlike in the UK, community whistle-blowing watchdog organizations such as consumer bodies are not well developed in Africa (Botha, 2001). On the other hand, regulatory structure in relations to board performance, a study in Italy by Zona and Zattoni (2007) indicate that board task performance is higher in regulated industries and listed companies, suggesting that the external context does influence board conduct and may shape the criteria against which board effectiveness can be measured (Pettigrew, 1992). In particular, they suggest that external scrutiny by financial investors as in the case of listed corporations and by regulatory authorities as in the case of companies operating in regulated industries – encourages the boards to accomplish their tasks more effectively. Based on the above assertion, and considering the Italian market is developed and widely held, going by the position of Bebchuk and Hamdani (2009) that arrangement for widely held firms may not be suitable for controlled firms (for example Nigeria). Hence, board role performance is likely to be low in regulated emerging markets, and external context may not be able to influence board conduct and constitute the benchmark or standard against which board competence can be measured. Therefore, it is reasonable to suggest that:

H4: *Regulatory structure as manifested by regulatory capacity, monitoring compliance and enforcement mechanism is not significantly related to board role performance.*

There is widespread recognition that strong board aids adequate investor protection, and other relevant stakeholders that can substantially affect public firms, not only in their ability to commit to stakeholders, improve

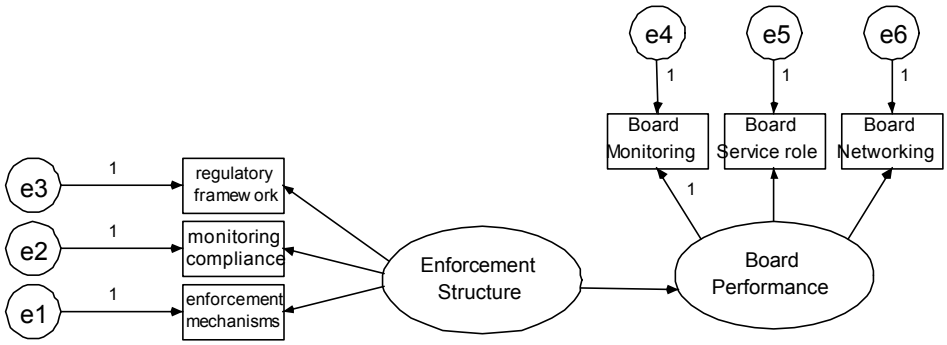

Fig. 1: Theoretical Model

firm value, effective board performance, but also the development of capital markets, monitoring compliance with regulations, improved enforcement stuctures and the growth of the economy in general [21] Bhagat *et al*., 2008, [9-22]. These developments sparked nations, academics and rating agencies develop many dimensions of corporate governance and indices for evaluating the quality of corporate governance practices in public firms. In this regard, Figure 1 presents a theoretical framework model where the exogenous latent constructs enforcement structure represented by three reflective dimensions of enforcement mechanisms, monitoring compliance and regulatory framework, are measured by 8 items. While the endogenous latent construct board performance is measured by 9 items, represented by three dimensions of board monitoring role, board service role and board networking role. This study uses questionnaire instrument to sample the perceptions of relevant market participants, and employs the use of confirmatory factor analysis (CFA) in a structural equation modeling (SEM) approach as the multivariate statistical technique to estimate how the overall model tests the data. In other words, indicators are associated with each latent construct and are specified by the researcher from an established theoretical framework [23].

MATERIALS AND METHODS

Sample: The empirical study was carried out using public listed companies in Nigeria as the sample frame. Since they are certified corporations, listed companies are chosen because they are regulated, easier to obtain data and also more accurate. The population of 318 Nigerian listed companies was targeted for the study, but a sample of 154 was achieved. As a first step, an informal chat with some middle and high level managers and an overview of the study background in the literature confirmed that questionnaire approach was appropriate and logical. All the data for the enforcement structure variables were obtained from responses of 5-points Likert Scale questionnaire. Great care was taken in adapting the questionnaire, which was largely from the findings of previous studies.

Instrumentation and Measurements: As a first step, series of discussions with experts were held, who possess relevant research experience in corporate governance. Thus, based on research findings in the literature, the survey questionnaire items for the construct were adapted and in some instances developed. In addition, the UK Innovation questionnaire largely influenced the adoption of some questionnaire items. Though the researcher have not seen any previous efforts that had attempted to test similar constructs together, however based on the proactive efforts embarked upon, the content validity was deemed adequate.

As a pre-test process, the research instrument was submitted to four senior academics with extensive combined experience in survey research. They were able to provide critical assessment of the content (face) validity of each item, as suggested by Rea & Parker (2005). The experts suggestions during the questionnaire design and revision process helped ensure a close match between the pre-test and final version of the instrument. Piloting of the survey instrument is accomplished by administering the questionnaire to a small sample (30) of respondents in Nigeria whose responses and general reactions are sought and examined. Luckily, all those that participated in the questionnaire pre-test are sufficiently knowledgeable about issues of relevance to the field of inquiry. Among them are nine high-level managers, one company secretary, and one CEO.

The questionnaire contained a total of 21 sets of statements including 4 demographic questions. Each of these sets of questions required a single response (tick as appropriate in the answer options 1-5) for each of a range of items. Each statement was rated by respondents on a range of measures scaled from 1 "strongly disagree" to 5 "strongly agree". Greater scores mean higher level of constructs. Items specific to a given construct were separated from each other in the questionnaire to minimize consistency bias and reduce any sense of repetitiveness. Additionally, each measure included at least one reverse-coded item. The questionnaire cover motivated participation by suggesting the usefulness of the questionnaire as an evaluation tool for reflection on participants' own corporate experience, indicating the amount of time required to complete the survey, and assuring participants of anonymity and confidentiality. The field operation of these variables is discussed below.

RESULTS

Data Analysis: All internal consistency reliabilities based on Cronbach's alphas for the 5-point interval scale measurement items are better than the results in the pilot survey. In the main study, the three manifest variables measuring board performance and enforcement structure are internally consistent with 0.777, 0.842, 0.780 & 0.728, 0.711, and 0.851 respectively. In this paper, the data analysis was conducted in two stages. First, as stated above, the scale reliability coefficient has been calculated for each of the scales used in enforcement structure and board performance. Cronbach's reliability coefficients ranged from 0.777 to 0.851. Since all the figures are above the 0.70 accepted threshold suggested by Hair *et al* (2010), it shows that the items achieved the accepted correlation level to retain them under each scale for further statistical analysis. In this respect, exploratory factor analysis (EFA) using principal component method with varimax rotation were conducted on both board performance and enforcement structure variables to examine their dimensionalties not based on any theoretical underpinning. Five items were removed because of low communality figures (< 0.5). The remaining measured items were confirmed using CFA based on proposed theoretical framework, and the relationships between enforcement structure and board performance constructs were empirically tested using structural equation modelling.

Exploratory Factor Analysis (EFA): In contrast to CFA, EFA does not require a priori hypotheses about how indicators are related to underlying factors or even the number of factors, hence the term "exploratory"(Kline, 2005). In other words, there is little direct influence on the correspondence between the indicators and the constructs. In this regard, Kline (2005) affirmed that EFA is not generally considered a member of SEM family, though it is a statistical technique used for evaluating a measurement model. In this study, as a first step, EFA has been performed to evaluate the questionnaire items that measure each of the latent constructs through an iterative process.

The exploratory factor analyses were carried out using the principal component analysis and the varimax rotational methods in order to extract the dominant factors and indicators within each factor that share common variance. The direct oblimin rotational method is not selected for this study because of its assumptions that the factors are correlated with one another. It is the correlation of factors that the study intends to confirm for the measurement model (CFA) after exploring for the study measures.

The construct - enforcement structure - was initially measured using an 8-item scale. When performing EFA, two items with factor loadings less than 0.5 were removed from the scale. Employing the principal components factor analysis (PCA), two factors (6 measured items) with an eigenvalue greater than two explained 64% of the variance of enforcement. In Table 2 below, the varimax-rotated factor pattern implies that all the two factors concerned - monitoring compliance (MT) and regulatory framework (RT) with the 8-item scale (α = 0.761, 711; KMO = 0.621; and < .001 @ 5% Sig) measuring the construct present acceptable figures to build the latent construct enforcement structures for further statistical analysis. The result of the EFA is shown in table 2 below.

Similarly, three factors with an eigenvalue greater than five explained 66% of the variance for the endogenous construct board performance using the principal factor analysis. Two items were removed from the scale. The varimax-rotated factor pattern implies that all the three factors concerned – monitoring; service; and networking with the 11-item scale (α = 0.893; KMO = 0.893; and < .001 Sig) measuring the construct present acceptable figures to build the latent construct board performance for further statistical analysis. The result of the EFA is shown in Table 3 above.

Table 1: Reliability of Measurement Items

Regulatory Enforcement (Exogenous Variable):	8 items
Regulatory Framework (3 items)	0.728
Over-regulation create ambiguity, thus a barrier to understanding laws	
Stock market rules are often ignored	
Corruption does not jeopardize performance of regulatory bodies.	
Monitoring (3 items)	*0.711*
Slow legal process jeopardize monitoring and enforcement outcome	
Staff inadequacy does not weaken monitoring action	
Low budget reduces the capacity to monitor compliance with rules.	
Enforcement (2 items)	*0.851*
Periodic evaluation of enforcement agency staff improves outcome	
Minor penalties for major auditing offences undermine enforcement outcomes.	
Board Performance (Endogenous Variable):	
9 Measurement Items	
Cronbach's alpha	
Monitoring (3 items)	*0.777*
The board engage in succession planning for CEO	
The board evaluates the performance of top executives	
The board controls plans and budget.	
Service (4 items)	*0.842*
The board contributes to the implementation of strategic decisions	
The board takes long-term strategic decisions	
Board's suggestions frequently improve strategic decisions	
Board benchmark strategic plan with industry data.	
Networking (2 items)	*0.780*
The board contributes to acceptance of the firm in the environment	
The board provides contacts with relevant stakeholders.	

Table 2: Enforcement Structure (Exogenous Variable)

Measurement Items	Factor Loadin	% of Variance
Slow legal process jeopardizes monitoring & enforcement outcome	0.761	64%
Staff inadequacy does not weaken monitoring action	0.812	
Low budget reduces capacity to monitor compliance with rules	0.813	
Over-regulation leads to ambiguous laws	0.821	
Stock market rules are often ignored	0.813	
Corruption does not jeopardize performance of regulatory bodies	0.779	
Kaiser-Meyer-Olkin Sampling Adequacy	.621	
Bartlett's Test of Sphecity: Appr. Chi-Square	192.243	
df 15		
Sig. .000		
Cronbach's Alpha (α) MT	.761	
Cronbach's Alpha (α) RG	.711	

Table 3: Board Performance

Measurement Items	Factor Loading	% of Variance
Board controls plans and budget	0.788	66%
Board evaluates performance of top executives	0.850	
Board engage in succession planning for CEO	0.696	
Board takes long time strategic decisions	0.680	
Board's suggestions frequently improve strategic decisions	0.860	
Board contributes to the implementation of strategic decisions	0.686	
Benchmark strategic plan with industry data	0.789	
Board contributes to the acceptance of the firm in the environment	0.600	
Board provides contacts with relevant stakeholders	0.762	
Kaiser-Meyer-Olkin Measure of Sampling	.893	
Bartlett's Test of Sphericity: Approx. Chi-Sq	680.081	
	36	
Sig.	.000	
Cronbach's Alpha (α)	.893	

Table 3: Board Performance

Measurement Items	Factor Loading	% of Variance
Board controls plans and budget	0.788	66%
Board evaluates performance of top executives	0.850	
Board engage in succession planning for CEO	0.696	
Board takes long time strategic decisions	0.680	
Board's suggestions frequently improve strategic decisions	0.860	
Board contributes to the implementation of strategic decisions	0.686	
Benchmark strategic plan with industry data	0.789	
Board contributes to the acceptance of the firm in the environment	0.600	
Board provides contacts with relevant stakeholders	0.762	
Kaiser-Meyer-Olkin Measure of Sampling	.893	
Bartlett's Test of Sphericity: Approx. Chi-Sq	680.081	
	36	
Sig.	.000	
Cronbach's Alpha (α)	.893	

Table 4: Composite Reliability (Enforcement Structure)

Latent Variable	Items Code	Factor loading	(Factor loading)^2	Std. Error	(FL)^2 + Std. Error	Composite Reliability
Enforcement	RG1	0.761	0.579	0.042		A/A+B
	RG2	0.812	0.659	0.047		
	RG3	0.813	0.661	0.049		
	MT1	0.821	0.674	0.089		
	MT2	0.813	0.661	0.088		
	MT3	0.779	0.607	0.087		
			A □ 3.841	B □ 0.402	4.243	0.905

In structural equation modeling (SEM), the measurement model is evaluated first to confirm the measurement adequacy of the items for the construct. The second stage involves the evaluation of the structural model, which shows a regression-like relationship between the constructs as shown in the theoretical model (Fig. 1) above. This two-stage approach will overcome the problem of localizing the source of poor model fit associated with other single-step approach (Kline, 1998). However, before proceeding to SEM data analysis, it is necessary to test the validity of the two constructs. Having ascertained both the internal consistency of the items (Table 4), and the EFA test above. Next section discusses construct validity.

Measurement Error in SEM: An important question is how do we represent theoretical concepts and then quantify the amount of measurement error? In this paper, the measurement model enabled the researcher to use all the questionnaire measured items to adequately define the two latent constructs, and then the model has been used to assess the extent of measurement error known as the *reliability*. From the stakeholder perspective, enforcement structure is complex, and can have many dimensions. Hence the design of the best 9 items to measure the construct. However, in its most basic form, measurement error is due to inaccurate responses, data entry errors, interpreting questions different from what the researcher intended, or natural degree of respondents' inconsistency when multiple items are used to measure same construct [23]. With the application of CFA, it becomes easier to assess the contribution of each indicator and then measure how well the combined set of indicators represent the latent constructs (reliability and validity). This study has been able to incorporate the extent of the measurement error into the statistical estimation, thus improved the structural model.

Composite Reliability: Reliability is an assessment of the degree of consistency between multiple measurements of a variable. The first measures considered in this paper is the reliability coefficient, which assesses the entire scale, with Cronbach's alpha (Table 1) being the most widely used measure [23]. Generally, reliability is inversely related to measurement error. In other words, as reliability goes up, the relationships between a latent construct and the indicators are greater, meaning that the construct explains more of the variance in each indicator. If reliability is 1, i.e. 100%, then measurement error is 0. But in statistical reality, no indicator items can perfectly define a latent constructs. SEM offers the advantage of automatically accounting for measurement errors. Also available are reliability measures derived from confirmatory factor analysis, such as the composite reliability. In Table 4

Table 5: Composite Reliability (Board Performance)

Latent Variable	Items Code	Factor loading	(Factor loading)^2	Std. Error B	□ (FL)^2 + □ Std. Error	Composite Reliability
Board Performance	MN1	0.788	0.621	0.054		A/A+B
	MN2	0.85	0.722	0.067		
	MN3	0.696	0.484	0.057		
	SV1	0.68	0.462	0.063		
	SV2	0.86	0.739	0.063		
	SV3	0.686	0.471	0.065		
	SV4	0.789	0.623	0.056		
	NT1	0.6	0.360	0.065		
	NT2	0.762	0.581	0.064		
			A □ 5.064	□ 0.554	5.618	0.901

below, the range of the factor loadings for the construct enforcement structure is 0.761 to 0.821. This is the correlation between the original construct and the indicator factors, with higher loadings making the construct representative of the factor. Squared factor loadings indicate what percentage of the variance in an original construct is explained by a factor. For example, the 0.761 loading on item RG1 explains 57.9% of the variance of the construct enforcement structure. In sum, for all practical and statistical significance, factor loadings for the two latent constructs – enforcement structure and board performance exceeded the 0.50 threshold set by Hair *et al*. (2010). Similar with the standard deviation of any set of data values, the standard error is the expected variation of an estimated regression coefficient, but instead denotes the expected range of the coefficient across multiple samples of the data. It is usually useful in statistical tests of significance that test to see whether the coefficient is significantly different from zero. It has been affirmed by Hair *et al*. (2110) that reliability is also an indicator of convergent validity, and that different reliability coefficients do not produce dramatically different reliability estimates, but a slightly different *composite reliability* value. It is computed from the squared sum of factor loadings for each construct and the sum of the error variance terms for a construct as represented by A/A+B. The higher composite reliability values of 0.905 and 0.901 in Table 4 (enforcement structure) and Table 5 (board performance) respectively confirm the assertion that sometimes Cronbach's alpha coefficient understate reliability [23].

Convergent Validity: A measure may be internally consistent (reliable) as above, but not accurate enough to measure a particular construct (valid). Construct validity is the extent to which a set of measured items actually reflects the theoretical latent construct those items are designed to measure [23]. A fundamental assessment of construct validity involves the measurement relationships between items and constructs (i.e., the path estimates linking construct to indicator variables). In CFA application, larger standardized loading estimates confirm that the indicators are strongly related to their associated constructs and are one indication of construct validity. Rules of thumb suggest that standardized loading estimates should be at least 0.5 and ideally 0.7 or higher. Low loadings suggest that a measured variable is a candidate for deletion from the model [23]. A more appropriate idea to discuss construct validity for CFA/SEM is the convergent validity. The items that are indicators of a specific construct should converge or share a high proportion of variance in common, known as convergent validity [23]. One of the important ways available to estimate the relative amount of convergent validity is: high loadings on a factor would indicate that they converge on a latent construct. Since the standardized parameter estimates are constrained to range between – 1.0 and + 1.0, Hair *et al*. (2010) stated that, a good rule of thumb is that standardized loading estimates (R) should have a regression weight 0.5 or higher, and ideally 0.7 or higher. Looking at Tables 6 & 7 below, all the items have R value < 0.5. Also, with the exception of MN1, MN2, and RG2, with R value 0.600, 0.607, and 0.638 respectively, all the other items have R = 0.7. The rationale behind this can be understood in each item's communality, which represents the amount of variance accounted for by the factor solution for each item. In this paper, all the items have been assessed to meet acceptable levels of explanation, i.e. < 0.5. The square of a standardized factor loading represents how much variation in an item is explained by the latent construct and is termed the variance extracted, sometimes referred to as *squared multiple correlation* (SMC). Result of the Tables 6 and 7 below indicate acceptable construct validity because the figure 0.992 for construct reliability is > that of variance extracted, 0.931 for the construct board performance, and 0.971 for construct reliability is > that of variance extracted, 0.919.

Table 6: Consrtuct Reliability & Variance Extracted: Board Performance

Items code	Std. loading	(Std. loadin)^2	(□ Std. loading)^2	□ (Std. loadin)^2	Std. Error	□ Std. Error	Constr Relibty: A/A+B	Variance Extractd C/C+B
MN 1	0.600	0.360			0.034			
MN 2	0.607	0.368			0.053			
MN 3	0.709	0.503			0.003			
SV 1	0.700	0.489			0.038			
SV 2	0.725	0.526			0.036			
SV 3	0.727	0.529			0.038			
SV 4	0.740	0.548			0.027			
NT 1	0.757	0.573			0.036			
NT 2	0.730	0.533			0.037			
	□ 6.294		39.614 (A)	4.427 ©		0.329 (B)	0.992	0.931

Table 7: Construct Relaibility and Variance Extracted: Enforcement Stucture

Variable & Items code	Std. loading	(Std. loadin)^2	(□ Std. loadin)^2	□ (Std. loadin)^2	Std. Error	□ Std. Error	Constr Relibty: A/A+B	Variance Extractd: C/C+B
Enforcement								
RG 1	0.814	0.663			0.044			
RG 2	0.638	0.407			0.039			
RG 3	0.591	0.349			0.041			
	□ 2.043		4.174 A	1.419 C		0.124 B	0.971	0.919

Table 8: Squared Multiple Correlations: (Group number 1 - Default model)

	Estimate
Board Role_Performance	.850
ntwrk2	.533
ntwrk1	.573
serv4	.547
serv3	.529
serv2	.526
serv1	.489
mntrg3	.503
mntrg2	.369
mntrg1	.360
reg3	.349
reg2	.407
reg1	.662
reg1 <--- Enforcement	.814
reg2 <--- Enforcement	.638
reg3 <--- Enforcement	.591

The Enforcement Structure Measurement Model (CFA): In a CFA model, the Squared Multiple Correlation (SMC) values represent the extent to which a measured variable's variance is explained by a latent construct. The rules provided for the factor standardized loading estimates tend to produce the same diagnostics because SMC are a function of the loading estimates regardless of whether the researcher is estimating in a congeneric measurement model, CFA or path model with latent constructs (Holmes-Smith *et al*., 2006). In addition, a major component of construct validity is convergent validity- items that are indicators of a specific construct should converge or share a high proportion of variance in common. Factor loadings, variance extracted (or SMC), average variance extracted (AVE) and construct reliability are some of the available ways to estimate the relative amount of convergent validity. In general, researches report at least one of the three models-based estimates of reliability: construct reliability, SMC or VE (Bollen, 1989). In this paper, I estimate the relative amount of convergent validity because both construct reliability and variance extracted are shown (Table 6 and 7 above) and also the SMC loadings have been used to measure the construct validity. As mentioned earlier, the SMC for a measured variable is the square of the indicator's standardized loadings. In other words, from the default outputs in the SEM figures below, it is estimated that the predictors of reg1 (indicator) explain 81.4% of its variance (i.e., the error variance of reg1 is approximately 18.6% of the variance of reg1 itself). Thus, the SMC value threshold of a good observed variable should be .5 and above [23]. Nevertheless, 0.3 indicates an acceptable item variable (Holmes-Smith *et al*., 2006) especially when the indicators for a construct are not more than 3 provided other constructs have higher indicators. A standardized factor loading of 0.7 for an observed variable is roughly the equivalent of 0.5 SMC. From the CFA analysis of the enforcement model, six items present offending estimates. The remaining 3 items of reg1, reg2, and reg3 are retained based on the AMOS modification indices output, as shown below.

DISCUSSION AND CONCLUSION

This paper began by arguing that significant enforcement agencies are a major stakeholder in business organizations. Like other contractual stakeholders, stake-keepers (regulators) help in instituting the required legal framework, and monitoring compliance using the appropriate enforcement mechanisms approved by country or firm law as a code of conduct for the organizations. Though a number of reports have used other factors to raise the importance of enforcement in the corporate governance structure; a typical example is the well-known survey in the transition economies viewpoint by [9], and the specific [10] report on Nigeria. A central claim of this paper is that board performance is a key mechanism of corporate governance that is shaped by the structural forces of sharing a firm's enforcement structures by statutory regulators as the stake-keepers, as argued by [22]. In this context, the country's regulatory framework or the firms' conventional norms are the major of considerations. Though it is difficult to say which of the approaches is superior to the other, but it can be rightly affirmed that both internal and external enforcements are key to effective corporate governance [9].

An important finding in this study is that the proposed manifest variables of the latent construct enforcement structure (exogenous variable) – regulatory framework, monitoring compliance, and enforcement mechanisms have been confirmed to be acceptable measures of enforcement structure. Similarly, for the construct board performance (endogenous variable), the proposed indicator variables – board monitoring, board service, and board networking have been confirmed to be good measures of the construct. However, board service items are stronger because three items are retained after all the modification processes to achieve model fit. In addition, after performing the CFA, only three items in the dimension regulatory framework were retained.

Within the overall model, the estimates of the structural coefficients provide the basis for testing the proposed hypothesis. As expected, enforcement structure factors are not significantly related to board performance, thus supporting the proposed hypothesis. In other words, the regression weights for enforcement structure in the prediction of board performance is insignificantly different from zero even at 10% level as shown in Table 9 above (0.479). In other words, enforcement structure and board performance show weak path (0.082), and statistically insignificant, but the hypothesis is supported because it goes in line with the proposed theory that found weak enforcement mechanisms in Nigeria In addition, the table confirms the statistical significance of all the 18 measures of the stakeholder model. The three stars *** in the P column indicates that the probability of getting a critical ratio as large as 5.454 in absolute value is less than 0.001. In other words, the regression weight for Enforcement Structure in the prediction of reg2 is significantly different from zero at the 0.001 level (two-tailed). Same with 5.307 in absolute value is less than 0.001. In other words, the regression weight for Enforcement Structure in the prediction of reg3 is also significantly different from zero at the 0.001 level. Same goes with the other endogenous construct (board performance) with all their measured items.

This study findings does not contradict the findings in the literature, which stated that enforcement is key to effective corporate governance especially in emerging markets [9-10-19-20-1]. Thus, the research objective of examining enforcement structure is insignificantly related to board performance have been achieved, answering the research question in the affirmative, consistent with the

Table 9: Hypothesized Regression Weight Among Latent Constructs

	Estimate	S.E.	C.R.	P	Status
Board Role_Performance <--- Enforcement	.082	.116	.708	.479	Not Sig
reg1 <--- Enforcement	1.000				
reg2 <--- Enforcement	.861	.158	5.454	***	par_13
reg3 <--- Enforcement	.827	.156	5.307	***	par_14
*** P value is statistically significant at 0.01 level					
mntrg3 <--- Board Role_Performance	1.000				
serv1 <--- Board Role_Performance	1.340	.174	7.698	***	par_5
serv2 <--- Board Role_Performance	1.365	.176	7.762	***	par_6
serv3 <--- Board Role_Performance	1.343	.179	7.501	***	par_7
ntwrk2 <--- Board Role_Performance	1.200	.172	6.980	***	par_8
*** P value is statistically significant at 0.01 level					

literature. However, not all the items provided in the initial proposed theoretical model actually measures the two constructs – enforcement structure and board role performance. Hence, the reason for deleting such items as suggested by AMOS estimates output in the modification indices.

For Nigerian listed firms in this regard, this means that even when there is in place legitimate regulatory framework, but the capacity to enforce the rules is of vital importance. The subject of enforcement has attracted increased attention in recent years. [9-24-35] opined that enforcement more than regulations or voluntary codes is the key to effective corporate governance, at least in transition and developing countries. Corporate governance and enforcement mechanisms are intimately linked as they affect firms' ability to commit to their stakeholders, in particular to external investors. They further observe that when the general enforcement environment is weak and specific enforcement mechanisms function poorly, as in many developing and transition countries, few of the traditional corporate governance mechanisms are effective.

In Nigeria, the Securities and Exchange Commission (SEC) regulates securities market participants under the Investments and Securities Act of 1999 and the SEC rules and regulations (1999). The Nigerian Stock Exchange, a self-regulating organization established by the NSE Act 1961, supports the SEC, supervises the securities market operations, and regulates second-tier capital market. Occasionally, there are conflicts between the SEC and the NSE with respect to the authority to discipline erring companies; there is a need therefore to review relevant legislation to clarify roles and powers. As a matter of rule, audited financial statements must be filed with the SEC, Nigerian Stock Exchange, and the Corporate Affairs Commission and be approved by the Stock Exchange before publication in newspapers within three months after the year-end. The Investments and Securities Act requires every market participants to maintain accurate and adequate records of its affairs and transactions, but it does not specify the standards to follow in preparation of financial statements, as companies have to comply with CAMA 1990 requirements. This multiplicity of laws may sometimes create a tug of war among the regulatory agencies especially CBN and SEC.

It was reported by World Bank (2005) that, despite the efforts made to minimize inconsistencies among the provisions of these laws, they have led to a situation where several bodies review and approve the audited financial statements of some companies before they are published. In some cases, the regulators have differed in their assessments of their quality of financial statements. There is the need, therefore, to harmonize regulatory arrangements, and codify them as a separate law. This task is likely to be addressed with the latest establishment of the FRC, which has received the President's assent. Therefore, the lack of functional regulatory and enforcement structures to monitor and enforce compliance for Nigerian listed firms can be the barrier that hinder board performance.

In view of the above, an important implication here is that it is doubtful that Nigerian boards in listed firms can be said to be meeting the requirements of the Companies and Allied Matters Act. In other words, the necessary powers given to them to monitor, manage, direct, and supervise the affairs of the firms with focus on equity shareholder protection raise question of the status quo of the code as reflected in the perceptions that the emerging Nigerian market will function better if all inclusive approach of stakeholder perspective is taking into considerations. Limited by the weak legal framework, the board are not able to fully influence key outcomes.

Therefore, boards' emphasis on operational matters as a measure of performance should be reconsidered, because this study has provided the required empirical evidence to substantiate the arguments in the extant literature that operational variables, such as monitoring role are insignificant instruments of monitoring compliance, and enforcement mechanisms but has no much effect on board service role performance. Finally, this study practically conceived that Nigerian firms that understand the different dimensions of enforcement structure as stakeholder dimensions could lead to better utility of boards to maximize their contributions and to impact such dynamics not only on board performance in particular, but also on firm's performance in general.

This study has succeeed in bridging the conspicuously dearth of extensive research on enforcement in relations to corporate governance. Perhaps the insufficient empirical work is possibly due to the difficulty of gaining access to data. As a task, the researcher believes that such a limitation should not be a hindrance for not developing a working model for conceptual analysis. The results in this study seem to suggest that enforcement play a more important role in explaining board performance, thus this study can be expressed in terms of contribution to theory. The combinations of the contractual constituents of stakeholders is also a first attempt that proposed an integrated model linking enforcement and board

performance. On a more practical note, understanding the different dimensions of enforcement could lead to better functioning of boards to maximize their respective tasks towards firm performance. This debate will follow other preceding arguments that portray a misapprehension of the superiority of equity shareholder as the ultimate board role. However, as an agenda for future research, whistle blowing policies for non.

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