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Review Article

Exploring the Role of Independent Non-Executive Directors in Corporate Governance Under Nigerian Law

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Abstract

A company's success hinges significantly on its board's effectiveness in providing strategic leadership and promoting independence in its stakeholder relationship. To achieve this, the board must have independent non-executive directors with the necessary qualifications, responsibilities, and appointment processes. However, determining who qualifies as an independent non-executive director and establishing their true independence remain critical in corporate governance. This article aims to provide comprehensive answers to these questions and to offer a deeper understanding of independent non-executive directors under the Companies and Allied Matters Act 2020 and the Nigerian Code of Corporate Governance 2018. The article proposes that to ensure the true independence of independent non-executive directors, their appointment and removal should involve a more rigorous process that includes a special resolution. Dissenting members should have the right to question appointments or removals to ensure that the appointed person protects the rights of the minority and other stakeholders. By emphasising the importance of independent non-executive directors and advocating for a more robust appointment and removal process, this article contributes to the scholarship on corporate governance and promotes best practices for board independence.

Keywords: Nigeria Corporate Laws, independent non-executive directors, corporate governance and board composition.

INTRODUCTION

According to Lord Denning's observation in *Bolton (Engineering) Co. Ltd. v Graham & Sons,* [1] a company can be compared to a human being with a brain and nerve centre that controls its actions and hands that carry out those actions as directed by the nerve centre. The hands of the company are the employees who serve the company, while the brain and nerve centre are the directors and managers who represent the company's directing mind and will and control its actions.

This article discusses the importance of an Independent non-executive director (INED) in corporate governance. It does so by delving into the criteria for qualification, role, appointment, and removal of INEDs as provided in the Nigerian Law of Corporate Governance 2018 (NCCG 2018) and Companies and Allied Matters Act 2020. By doing so, the paper significantly contributes to corporate governance scholarship, promoting and emphasising best practices in the board's independence.

Legal Regime

CAMA 2020 refers to a company director as a person duly appointed by the company to direct and manage the company's business. "Director" includes any person occupying the position of director by whatever name called and consists of any person by whose directions or instructions the company's directors are accustomed to act. [2]

In the case of Baffa v. Odili, [3] the Court of Appeal, while distinguishing between a director and an alternate director, defined a director while referring to CAMA 1990 as this;

> *"Section 244 of CAMA has defined "directors" as "persons" duly appointed by the company to direct and manage the business of the company..."* [4]

[1] (1957) 1 Q. B 159
[2] Section 868 CAMA 2020
[3] (2001) 15 NWLR (Pt. 737) 709
[4] Now Section 269 CAMA 2020

The Supreme Court has highlighted the statutory duty of the Company Director to his company in the case of ***Artra***

Industries (Nig.) Ltd. V. N.B.C.I.[5] as:

> *"In exercise of the management powers and duties conferred upon them by Section 63(3) of the Companies and Allied Matters Act 1990, the Directors of a company must adhere strictly to the statutory provision which enjoins them to consider the company's interest as paramount. In the instant case, the Directors of the respondent bank showed that they were alert to their responsibilities to the bank by refusing to exercise their discretion in favour of the appellant, which would have the effect of diluting the respondent's security when the appellant was already in breach of its previous undertaking."*

Types of Directors

There are various types of directors as enshrined in CAMA 2020; these are:

i. Executive or special directors: These types of directors are employed or appointed from among the company directors to oversee the company's day-to-day affairs. They manage the company's affairs daily; hence, they are full-time employees entitled to salaries. They are to work for the company to the exclusion of any other job. They have a letter of appointment, which ordinarily should contain their conditions of service. [6]

ii. Non-executive directors are appointed under the provisions of CAMA and the company's memorandum and articles. As they are not company employees, they are not entitled to salaries or remuneration except for out-of-pocket expenses. [7]

iii. Shadow directors are not appointed as first or subsequent directors, and their names are not published as company directors. However, they exert control over the company's directors because they are accustomed to following the shadow director's instructions. This concept is essential to understand as it highlights the potential for influence within a company, even without a formal directorial role. [8]

iv. Life directors: They are called life directors because they do not retire annually like other directors (see Section 285(1) for the rule on retirement of directors by rotation). However, a life director can be removed under s.288 CAMA 2020. [9]

v. Alternate directors and Assignee directors: These types of directors can only be appointed where the company's articles of association provide for them. While a substantive director temporarily appoints an alternate director to represent them at a board meeting, an assigner director permanently replaces a substantive director. [10]

In addition to the above, [11] CAMA 2020 [12] mandates that every public company must have ***INDEPENDENT NON-EXECUTIVE DIRECTORS*** on their board of directors. The Business Facilitation Act 2023 (BFA) [13] which amends some sections of CAMA 2020 stipulates that 1/3 of the board of a public company must be Independent Non-Executive Directors.

This highlights the crucial role played by company directors in the management of companies. [14] In public companies where management is separated from membership, the articles of association often confer broad discretionary powers upon the board of directors. However, there is a concern that these powers may be exercised in the interest of senior management rather than other stakeholders. [15] Therefore, a key aspect of company governance is establishing a framework of rules that prevents the abuse of directorial powers while allowing for the benefits of strong, centralised management. [16] This is where the concept of Independent non-executive directors [17] (INEDs) comes into play, as they provide an additional layer of oversight and accountability in corporate practice in Nigeria.

The Nigerian Code of Corporate Governance 2018 introduced INEDs as a new type of director for companies in Nigeria. [18] Interestingly, the Companies

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5 (1998) 4 NWLR (Pt. 546) 357 at 382

6 Bhadmus, Y.H., "Bhadmus on Corporate Law Practice", 6th ed. (Enugu: Chenglo Limited, 2023) p. 171 and Osamolu, S. A., "Corporate Law Practice in Nigeria", 4th ed. (Abuja: LawLords Publications, 2023).

7 Section 272-274 CAMA 2020; see also Bhadmus, Y.H., "Bhadmus on Corporate Law Practice", 6th ed. (Enugu: Chenglo Limited, 2023) p. 171 and Osamolu, S. A., "Corporate Law Practice in Nigeria", 4th ed.(Abuja: LawLords Publications, 2023).

8 Section 270 CAMA 2020.

9 Section 281 CAMA 2020.

10 See the case of Baffa v. Odili (2001) 15 NWLR (PT 737) 709 at 747; Bhadmus, Y.H., "Bhadmus on Corporate Law Practice", 6th ed. (Enugu: Chenglo Limited, 2023) p. 173

11 Which is not the focus of this article.

12 Section 275.

13

14 Bhadmus, Y.H., "Bhadmus on Corporate Law Practice", 6th ed. (Enugu: Chenglo Limited, 2023) p. 169

15 Davies, P.L & Worthington, S., "Gower & Davies Principles of Modern Company Law", 9th ed. (UK: Sweet and Maxwell, 2012.) p.502

16 Ibid

17 Herein abbreviated as INED

18 Nigerian Code of Corporate Governance was issued by the Financial Reporting Council of Nigeria under the

and Allied Matters Act 2020 [19] (CAMA 2020) also recognised INEDs as a type of director. [20]

Who is an Independent Non-Executive Director?

Independent non-executive directors (INEDs) are vital to modern corporate governance. As their name suggests, INEDs are directors who do not have any material relationship with the company and can, therefore, provide an objective "set of eyes" for the functioning of the board and the protection of the interests of the shareholders, particularly minority shareholders. [21] INEDs, therefore, play a crucial role in safeguarding the interests of all stakeholders, including minority shareholders, and in sustaining trust and confidence in the company. [22]

An INED is a director who is independent in character and judgment and whose relationships with the company, its management, or substantial shareholders do not impair their ability to make independent judgments. [23] In addition, an INED is a non-executive director who does not hold a shareholding in the company that exceeds 0.01% of the paid-up capital of the company. [24]

The Companies and Allied Matters Act (CAMA) 2020 provides further guidance on appointing INEDs. According to CAMA 2020, an INED is a director who or whose relatives, either separately or together with him, were not an employee of the company and did not make or receive from the company payments of more than N20,000,000 during the two years preceding the time of their appointment. [25] Moreover, a person to be appointed as an INED must not, during the two years preceding their appointment, own more than a 30% share or other ownership interest, directly or indirectly, in an entity that made or received from the company payments of more than N20, 000,000, or act as a partner, director, or officer of a partnership or company that made or received from the company payments of more than such an amount; and must not have been engaged directly or indirectly as an auditor for the company. [26]

In summary, INEDs are appointed to bring a high degree of objectivity to the board, ensure that decisions are taken in the interest of all stakeholders, and provide an independent perspective on issues facing the company. By fulfilling these roles, INEDs help enhance corporate governance, strengthen shareholder confidence, and promote the company's long-term success.

With the above definitions of INED, it is clear that the only interest an INED has in a company where he is a board member is to be objective in decision-making and give independent judgment on issues of the company in the interest of the company and its stakeholders. He is like a neutral board member who ensures decisions are taken in the interest of all involved.

What are the Roles of Independent Non-Executive Directors?

Independent Non-Executive Directors (INEDs) are crucial in bringing objectivity to the board and upholding stakeholder confidence in corporate governance. INEDs ensure that the company acts in the best interest of all parties, including minority shareholders. This is achieved through rigorous oversight of the company's internal controls and the board's actions to ensure they align with the shareholders' interests. [27]

The board of directors is the highest governing body in the company, and its effectiveness is crucial to the success of the company. According to the Nigerian Code of Corporate Governance (NCCG) 2018,

> *"A successful company is headed by an effective board responsible for providing entrepreneurial and strategic leadership, promoting ethical culture and responsible corporate citizenship. As a link between stakeholders and the Company, the Board is to exercise oversight and control to ensure that management acts in the best interest of the shareholders and other stakeholders while sustaining the prosperity of the Company."* [28]

Federal Ministry of Industry, Trade and Investment. The commencement date was January 15, 2019. The code seeks to institutionalise corporate governance best practices in Nigerian companies. The Code is also to promote public awareness of essential corporate values and ethical practices that will enhance the integrity of the business environment. By institutionalising high corporate governance standards, the Code will rebuild public trust and confidence in the Nigerian economy, thus facilitating increased trade and investment. See the pdf of the code as published in https://pwcnigeria.typepad.com/files/nigerian-code-of-corporate-governance-2018-1.pdf

[19] The law that establishes the Corporate Affairs Commission (CAC) which is the apex regulator of companies in Nigeria. CAMA 2020 repealed CAMA 1990 i.e. cap C 20 LFN 2004.

[20] See section 275 CAMA 2020

[21] Nikunj Mahajan, O.P. Jindal, "Independent directors- A myth or a fact", Indian Journal of Law and Legal Research, Volume IV Issue IV | ISSN: 2582-8878.

[22] See principle 7 NCCG2018

[23] Principle 7 (1) NCCG 2018

[24] Principle 7 (2) (1) NCCG 2018

[25] Section 275 (3) (a & b) CAMA 2020

[26] Section 275 (3) (c & d) CAMA 2020

[27] Nikunj Mahajan, O.P. Jindal. opcit, fn.16

[28] Principle 1 NCCG 2018

Furthermore, the NCCG 2018 emphasises the importance of an appropriate balance of skills, diversity (including experience and gender), competence, independence, and integrity in the board's composition. [29] The board should be composed of a suitable mix of Executive, Non-Executive, and INED members, with most being INED for better governance. [30]

CAMA 2020 stipulates that a public company must have at least one-third of the total number of directors as independent directors, including INEDs. [31] This requirement underscores the significance attributed to INEDs in ensuring that the company operates transparently and accountable, thereby earning the trust and confidence of stakeholders.

Qualification and Criteria for Appointment of Independent Non-Executive Directors

Specific criteria must be fulfilled for a Non-Executive Director (NED) to be appointed as an Independent Non-Executive Director (INED). Firstly, the individual in question is expected to possess an advanced degree in a relevant field that aligns with the company's business, as this will allow for a deeper understanding of the company's industry and business model. A record of ethical behaviour and sound decision-making is also considered when appointing an INED.

Furthermore, an INED must demonstrate a genuine commitment to the company's success and be willing to dedicate the necessary time and effort to the role. Considering the factors that qualify an NED to be nominated as an INED, it is essential to note that the individual must represent a strong independent voice on the Board. This means that they must be independent in character and judgment, and there should be no relationship with the company that could impair their ability to make independent decisions. [32]

Other factors [33] to consider include that an INED should not be a representative of a shareholder with the ability to control or significantly influence management, nor should they have been an employee of the company or group within the last five years. An INED should not be a close family member of the company's advisers, directors, senior employees, consultants, auditors, creditors, suppliers, customers, or substantial shareholders.

An INED should not have had a material business relationship with the company either directly or as a partner, shareholder, director, or senior employee of a body that has or has had such a relationship with the company.[34] They should have served at something other than the directorate level or above at the company's regulator within the last three years. They should only render professional, consultancy, or other advisory services to the company or the group in the capacity of a director. [35]

Additionally, an INED should only receive additional remuneration from the company if a director's fee and allowances are paid. They should not participate in the company's share option or a performance-related pay scheme and should not be a member of the company's pension scheme. Finally, an INED should have served on the Board for at most nine years from the date of their first election. [36]

As per the provisions of CAMA 2020, [37] the criteria that must be satisfied to nominate an NED as an INED require that the INED should have served as a director of the company for two years preceding the time in question, with relatives either separately or together:

1. was not an employee of the company;
2. did not -
   i. make to or receive from the company payments of more than N20,000,000 or
   ii. own more than a 30% share or other ownership interest in an entity that made to or received from the company payments of more than N20,000,000
3. did not own more than 30% of the shares of any type or class of the company, and
4. was not engaged directly or indirectly as an auditor for the company.

Considering specific criteria before being appointed as an INED in a company is essential. INEDs should be able to exercise objective judgment and speak up for minority shareholders in cases where their rights are at risk due to a conflict of interest between the majority and minority shareholders.

Appointment and Term of Office of Independent Non-Executive Directors

The appointment of INEDs is a crucial aspect of corporate governance, as it ensures that the board of directors comprises individuals with the requisite skills, experience, and independence to oversee the company's affairs effectively. However, the process of appointing INEDs can be complex, particularly in cases where there are shareholding qualifications for directors, [38] as exceptions must be made to enable the nomination of INEDs.

[29] Principle 2 NCCG 2018
[30] Principle 2.2 NCCG 2018
[31] See section 275(1) CAMA 2020
[32] Principle 7.1 NCCG 2018
[33] Principle 7.2 (1-9) NCCG 2018
[34] Ibid
[35] Ibid
[36] Principle 7.2 (1-9) NCCG 2018
[37] Section 275 (3) CAMA 2020
[38] See section 277(1) CAMA 2020 for shareholding qualification of a company director where the articles of the company so provide.

Under the provisions of CAMA 2020, [39] the number of directors and their names are determined by the subscribers of the Memorandum of Association or a majority of them. In cases where the articles of association empower anyone, including outsiders, to appoint directors, such persons may also be responsible for nominating INEDs. [40]

The NCCG 2018 recommends the establishment of a committee responsible for nomination and governance, which is tasked with identifying individuals who are suitably qualified to become board members and making recommendations for their nomination and appointment. The committee is also responsible for undertaking an annual assessment of the independent status of each INED.

However, the appointment of INEDs raises questions about their loyalty, as they are not connected to any particular shareholder group. As such, it is essential to adopt a mode of appointment that ensures their independence and impartiality. In the absence of specific provisions for the appointment of INEDs under CAMA 2020 or NCCG 2018, the mode of appointment of Non-Executive Directors (NEDs) after nomination can be adopted since INEDs are a "specie" of NED.

Therefore, the following mode of appointment can be adopted;

a. The nomination of an INED shall be by notice in writing signed by a person duly qualified to attend and vote at the meeting of their intention to propose such a person for election as an INED.
b. The nominee must also give written notice, signed by them, of their willingness to be elected.
c. Both notices must be delivered to the company's registered office or head office not less than three nor more than 21 days before the date appointed for the meeting. [41]
d. At the general meeting, an ordinary resolution will be passed to appoint the nominee as an INED.

Retirement and Removal of Independent Directors

INEDs are a specie of NED; therefore, in the absence of specific provisions for the retirement and removal of INEDs, the general provisions provided for the retirement and removal of NEDs will suffice. Concerning the retirement of directors, unless the company's articles provide otherwise, all directors will retire from office at the first annual general meeting of the company, and subsequently, one-third of the directors for the time being, or at the nearest one-third if their number is not a multiple of three, shall retire from office at subsequent annual meetings.[42] This is a recurring event, which is one of the ordinary businesses of companies at an annual general meeting. A retiring director may be re-appointed if they present themselves for re-election, another person is not elected to fill their place, or the meeting does not expressly resolve not to fill the vacancy created by their retirement, or a resolution for their re-election has not been put to the meeting and lost. [43]

Regarding the removal of INEDs, the articles or contracts appointing a director may provide for their removal from office. However, a company may remove a director from office by an ordinary resolution, of which special notice is given. [44] According to the NCCG 2018, it is recommended that the board of directors ensure that the removal of a director is by the law and the company's articles of association and that the process is fair, transparent, and communicated to shareholders. [45] The removal of a director should be done with utmost caution, as it can potentially impact the company's reputation and investor confidence.

CONCLUSION

The NCCG 2018 and CAMA of 2020 have introduced several favourable provisions to ensure the independence of INEDs in serving the interests of minority shareholders and other stakeholders in a company. However, in practice, the question of how independent an INED truly is remains pertinent, especially in light of the mode of nomination, appointment, and removal of INEDs, which is determined by a simple majority (ordinary resolution).

This article posits that when the majority controls the nomination and appointment of INEDs, it becomes challenging for the INEDs to maintain an independent, objective judgment in guaranteeing the protection of minority shareholders. This is because the INEDs are conscious of the annual evaluation by a simple majority, which may lead to their re-election after retirement, or the decision by the majority, which may result in their removal. The knowledge of this fact may impair their independent judgment when dealing with the majority.

To address this challenge, this article recommends that the relevant laws provide for a more stringent mode of appointment and removal of INEDs to ensure that the fear of some set of persons managing the

[39] See section 275 (2) CAMA 2020
[40] See section 46(3) CAMA 2020
[41] See section 285(4) CAMA 200
[42] See section 285 CAMA, see also Osamolu, S. A., Corporate Law Practice in Nigeria, (Law Lords Publishers: Abuja, 2023, 4th ed.) at p.224
[43] See section 285 (3) CAMA 2020.
[44] See generally, the provisions of section 288 CAMA 2020.
[45] Principle 7.4 NCCG 2018

affairs of the company does not impair their objectivity while playing their role as INEDs. Specifically, amendments should require a special resolution for the appointment and removal of an INED, with dissenting members having the right to approach the court to cancel such a resolution where they did not vote in favour. These amendments will go a long way in protecting the independence of INEDs and ensuring that the interests of minority shareholders are adequately represented.