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Board Sub-Committee Effectiveness and Annual Report Readability of Non –Financial Firms in Nigeria

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Abstract
This study examined the effect of board subcommittee and annual report readability of listed non-financial firms in Nigeria. Particularly, this study obtained data from listed non-financial firms in Nigeria from 2013 to 2022. The total population of this study was 109 non-financial firms listed in Nigeria. The study employed a longitudinal research design with a simple filtering technique to select the sample size of 72 firms. A panel regression analysis was employed to analyse data extracted from annual report. The findings of the study showed that board sub-committees' effectiveness when measured in terms of audit committee financial expertise [coef. = -0.774 (0.012)] had a significant negative effect on the FOG index measure of annual report readability of the listed non-financial firms listed in Nigeria. Board sub-committees' effectiveness when measured in terms of audit committee independence [coef. = -0.007 (0.480)] has an insignificant negative effect on the FOG index measure of annual report readability of the listed non-financial firms in Nigeria. The study recommends that an increase in the number of board sub-committees will have a minimal impact on the FOG index measure of annual readability, resulting in a slightly more challenging readability of the annual report for listed non-financial firms in selected Sub-Saharan African countries during the study period.
Keywords: *Board Sub-Committee, Annual Report Readability, Non –Financial Firms*

1.0 Introduction

Effective corporate governance is crucial for firms' success, and board subcommittees play a vital role in ensuring good governance. Annual reports are the key channel for firms to communicate with stakeholder and their readability affects the quality of information disclosed. The board of directors establishes committee primarily to observe the process of financial reporting and deliver financial control regarding corporation economic events. They represent essential part of corporate governance they must have more than simply vague objective and meetings should be well managed (Appah,2022). Committees are usually appointed based on needs, such as audit committee, financial committee, communication committee, Ad-hoc committee, and governance committee (Kiel & Nicholson, 2003). Nigeria as a developing economy is faced with unique corporate governance challenges, non-financial firms in Nigeria face distinct regulatory environments, cultural contexts and stakeholder expectations. Despite the presence of board subcommittees, non-financial firms in Nigeria continue to experience governance laps, suggesting a potential ineffectiveness of these subcommittees in ensuring good governance practices due to composition, meeting, frequency and expertise on the board. Also, annual reports of some of these firms are often characterized by poor readability, making it difficult for stakeholders to understand the firm's financial position. These could be as a result of factors such as language, format, content, which are not optimized for effective communication with stakeholders. Previous studies such as Rama (2019); Rifat et. al. (2022) & Udo et. al. (2023) worked on board sub-committee and firm performance, while some on profitability with less research attention on direct board subcommittee and annual report readability. Therefore, this study examined the effect of board sub-committee effectiveness and annual report readability, drawing samples from non-financial firms in Nigeria. Board sub-committee effectiveness was measured using; number of sub-committee, audit committee financial expertise and audit committee independence while readability was measured using FOG index. The hypothesis of the study was that board sub-committee effectiveness has no significant effect on the annual report readability of listed non-financial firms in Nigeria.

2.0 Conceptual review

Number of Subcommittee; This has to do with the number of smaller groups established in any organization from members of the larger committee to advise the board on specific issues. These groups may be in terms of finance, audit, governance and communication responsible for the day to day activities and urgent issues that cannot wait till business meeting of the firm is held. They must ensure that established guidelines are followed in their discharge of duties. However, in this study number of subcommittee will be measured as number of board subcommittee. (Chairunesia & Bintara, 2019).

Audit committee financial expertise has to do with members of the committee having an understanding of GAAP and financial statements. Experts must have the ability to assess general application relating to financial reporting. Due to agency problems, shareholders require monitoring mechanisms to protect their wealth and interest by establishing audit committee financial expert to help reduce information asymmetry with the use of accounting conservatism to monitor and control managerial issues (Al Lawati & Hussainey ,2021 and Chairunesia & Bintara, 2019). During the audit period, the audit committee is responsible for contacting, communicating, and cooperating with the external auditor (Velte, 2018a). Additionally, audit committees have the responsibility of evaluating internal audit work and guaranteeing that the firm's management applies the internal audit effectively. The audit committee is a permanent committee created to improve firm responsibility by working in conjunction with management and internal auditors to develop a company's accounting and financial reporting (FR) practices and safeguard the behaviour of companies' affairs in maintaining accepted ethical and legal standards (Gaur et al., 2015). Likewise, influential audit committees help reduce mistakes and promote regulatory compliance, internal control systems, and boost voluntary disclosures. Regarding quoted companies, the Security Exchange Commission further enhances the audit committee elements by stipulating the addition of non-executive board members (Velte, 2018b). This particular structure aims to make sure that administration and stockholders are satisfactorily characterized in audit committees seeing the crucial part they undertake and where administration should safeguard the owners' interests by guaranteeing that released (FRs) are a fair exemplification of the condition of a company. In this study, audit committee effectiveness is examined in terms of its size, independence, and gender diversity (Velte,2018b).

In accounting, the size of an audit committee is defined as the total number of individuals who serve as members of the audit committee for a given period of time (Velte, 2018b). A sufficient number of people should be included on the audit committee in order to successfully carry out and coordinate the massive obligations assigned to them. Firms having a large number of members on an audit committee are more likely to provide audit reports on time. According to studies of Bajra & Cadez (2018), who looked at the impact of audit committee qualities on financial reporting quality between 2011 and 2015, showed that audit committee size was found to have a negative and minor impact on financial reporting quality in the selected companies. A similar study by Mohammadi & Naghshbandi (2019) investigated the audit committee attribute and financial reporting quality of Nigerian listed companies and found that the audit committee size negatively and insignificantly affected the financial reporting quality of the sampled firms. Similarly, the study by Kohler Ratzinger-Sakel & Theis (2020), in contrast to the previous findings, showed a positive and negligible association between the size of the audit committee and the quality of financial reporting. The findings of Lennox (2017) showed that the size of the audit committee has a considerable detrimental impact on financial reporting. Studies on the impact of audit committee size on financial reporting quality have yielded conflicting results, as evidenced by the literature review presented above. In this study audit committee financial expertise shall be measured as number of committee members with professional accounting qualification.

Audit committee independence: Independence is a vital elements of an effective corporate governance. As board directors are expected to be independence in their discharge of their duties so are auditors required. To enhance the independence of the audit committee, many codes of corporate governance across the globe recommended that majority of directors on the committee should be an independent non- executive director (Financial reporting council 2016). However, audit committee independence will be measured as percentage of non-directors in the audit committee to audit committee members' size (Chairunesia & Bintara, 2019).

Fog Index

The Gunning's Fog Index (Gunning, 1952) is one of the methods that focuses on the syntactical complexity of the passage and requires that the researcher count words containing three or more syllables, referred to as "hard words." The formula determines the grade level of the passage based on a formula using the percentage of "hard words" and the average sentence length. The fog index is a measure of the readability of a text, based on the average number of words per sentence and the percentage of complex words (those with three or more syllables).

Board sub-committee effectiveness and annual report readability

Cho et al., (2019) often considers audit committee independence an essential and influential feature of audit committee effectiveness in monitoring and presenting financial reporting and suggest that audit committee independence is related to disclosing companies' financial position facing a financial crisis. Previous studies have shown that the independence of audit committee members reinforces the monitoring process for two reasons. First, independent managers do not have economic and mental dependence on company managers that interferes with their ability to examine their actions; and second, maintaining and enhancing the reputation of managers provides incentives for better oversight of independent audit committee members (Blanco et al., 2020 and Chalaki et al., 2012). Beasley (1996) pointed out that non- bound (independent) managers use their management process to signal to foreign markets that are decision-makers, understand the importance of decision control, and can use such controlling systems (for example, the accounting system).

Empirical review

Peter et al., (2020) examined the effect of board attributes and tax planning of listed non-financial companies in Nigeria. Data for the study were collected with the help of audited annual report from 2008-2017.Regession analysis was employed in the study and findings of the study revealed that board independence has a significant negative effect on tax planning. Also profitability has a significant positive effect on tax planning as leverage depicts significant negative effect on tax planning. The study was limited to non-financial companies in Nigeria hence findings were useful to stakeholders of those companies.

Ezat (2019) investigated the impact of corporate governance structure on the readability of Egyptian board of directors' reports in Egypt. The sample included all EGX100 companies listed from 2013 to 2015, and the study used multiple regression analysis to test the main hypotheses. Readability level was measured by applying the LIX formula, which suits the Egyptian context. The results demonstrated that board reports for EGX100 companies were complex and hard to read. In addition, four corporate governance variables, namely separation between CEO and chairman roles, number of board of directors' meetings, foreign board members. and number of audit committee meetings had an impact on the readability level of board reports for EGX100 companies. Further, all control variables except company performance were significantly associated with readability. Greater awareness of the complex style of disclosure reports was crucial for emerging markets to easily convey the required information and enhance communication with stakeholders. Based on the limited literature addressing readability, the study contributed by investigating the impact of corporate governance structure on readability of corporate board of directors' reports in an emerging market. However, this study employed the four mechanisms of corporate governance but had a time frame of three years which is not a good base in research.

Ahmad and Maochun (2019) investigated the issue of readability of Pakistan annual report, which caused the conflict between the shareholders and the management. Annual reports are an integral source of information for the shareholders regarding their investment. To investigate the importance of the readability, they took the data of 21 non-financial companies which were in the KSE-30 index of Pakistan for the 10 years (2008-2017). The findings of the results depicted that

firms whose annual report was more readable as compared to others were facing low problem of the conflict between the shareholders and the management. Further results of this study indicated that under the better-quality measures, relevant audit increase the readability of the annual report which reduces the agency cost. Efretuei (2015) specifically investigated what determined the syntactical complexity of narratives in annual reports by assessing if the experience of the board plays a role in annual report complexity in Nigeria. The study focused on board experience due to the role of the board in governing corporate communications to investors. The study assessed the syntactical complexity of annual report narratives using linguistic features of textual communication, which measure the level of reading difficulty and the tone of communication in annual reports, following the FRC's identification of obscurity and imbalance in communication as the causes of complexity in annual reports. The main findings of the study indicated that the experience of the board determines the level of syntactical complexity of annual report narratives, consistent with the view that the composition of the board affects the integrity of the financial reporting process.
Etuk and Akpan (2023) examined corporate governance mechanisms and annual report readability of listed Oil and Gas firms in Nigeria from 2012- 2021.They study used audit frim type, board size and ownership structure as corporate governance mechanism and annual report readability was proxied using annual report page length. The result showed that board size had a significant effect on annual report readability while audit firm type and ownership concentration had an insignificant effect on annual report readability. The study used only one component of board structure as compared to this study that used all the components of board structure as one variable.

Stewardship theory by Davis, Schoorman, and Donaldson 1997. The stewardship theory was propounded by Davis, et al., (1997). Stewardship theory focuses on psychological and sociological methods of oversight, rather than the economic (pecuniary) tools of agency theory. Stewardship theory posits that, concern for their own reputations and career progression inhibits agents from acting against the interests of shareholders, thus agency costs should be inherently minimized (Donaldson and Davis,1991).

Muth and Donaldson (1998) supported the view that financial gain is not necessarily the sole driver of managerial behaviour, and in addition managers require some discretion to effectively manage business for shareholders. Consequently, separate ownership is not viewed as a weakness in stewardship theory as cooperative behaviours are held to be the latent/intrinsic behaviour of managers (Davis et al., 1997), and they are subject to an array of motives in addition to financial gain (Muth & Donaldson, 1998). The contribution to firm performance of stewards relates to the context in terms of socio-cultural and psychological factors. For example, managers are considered more likely to perform better with greater empowerment and job satisfaction, which is a psychological factor. Socially, managers (along with most personnel in a successful organisation) typically self-identify as organizational representatives and thus they consider the power accorded them by principals to be a tool to enable the organisation and other employees to achieve the organizational goals (Ezat, 2019). In terms of the situational perspective, it is anticipated that managers perform optimally in an environment that is involvement-oriented (in which accomplishment of tasks, control and thinking are combined in a single process). If the organizational culture has a collectivist orientation, this will obviously have implications on the long-term relationship and loyalty managers have towards the firm (Ezat, 2019). Stewardship theory supports that an insider-dominated board is more effective due to more in-depth knowledge of organizational operations, such as access to data and technical expertise (Muth & Donaldson, 1998).

The adoption of stewardship theory in this study is hinged on the fact that, it supports the view that those charged with corporate governance of a company (that is directors) should act in the interest of the owners (shareholders) and others who have a stake in the company. Also stewardship mindset is to prioritize the company's long term interest, leading to more effective decision making and oversight. It helps in active monitoring of managements performance, ensuring accountability and effective governance. It promotes transparent decision making and disclosure, which board subcommittee can ensure through effective reporting and communications. By embracing stewardship theory board subcommittee can enhance their effectiveness, promoting good governance, strategic guidance and sustainable success for the company

METHODOLOGY

Longitudinal research design was employed in this study since the study was to determine the cause and effect relationship between the independent and dependent variables with a view to establishing a causal effect of board effectiveness on annual report readability of listed non-financial firms in Nigeria. The study employed a panel data set which follows the population of interest over an extended time period of 2013-2022 since it was concerned with measuring change over time for the units of analysis within the population. The population of the study consisted of all listed non-financial firms. As at December 2022, 109 non-financial firms listed on the floor of the Nigerian Exchange Group (NGX). Particularly, this study drew data from listed non-financial firms in Nigeria from 2013 to 2022. The period was chosen based on the need to cover a wide range of observations unlike previous studies that used short period of time (Less than 10 years).

The study used the simple filtering technique to select the sample since firms that are included in the sample were based on certain selection criteria. These criteria included firms listed on the Nigerian Exchange Group for 2013-2022; for which access to their annual financial reports were obtained within the period and not firms operating subsidiaries in Nigeria. Newly listed firms and delisted firms were excluded from the study. Thus, only non-financial firms with all relevant data due to continuous existence were included in the sample. The final sample size consisted of 72 non-financial firms as indicated in Table 3.1. This study employed secondary data collection techniques. Secondary data collection is the gathering of information already researched and presented by other scholars or data obtained from other sources. However, data for the study were extracted from; audited annual reports of public quoted firms in the Nigerian exchange groups.

Table: 3.1 Sample size representation

S/N	Industry	Population Size	Newly listed firms after 2013	Suspended Firms (Inactive)	Final Sample Size
1	Healthcare	10	3	3	4
2	Energy	10	2	0	8
3	Industrial	32	3	9	20
4	Consumer Stapples	23	3	3	17
5	Consumer Discretionary	8	0	3	5
6	Information Technology	7	0	1	6
7	Basic Material	10	0	1	9
8	Communication	4	2	1	1
9	Real Estate	5	1	2	2
	Total	**109**	**14**	**23**	**72**

Source: Researcher's Compilation, (2023)

In order to test the hypotheses formulated in the study and to achieve the objectives of the research, the study adopted and modified the model of Xua et al.,(2018). Hence, the model specification of the study was expressed as;

$$FOGI_{it} = \beta_0 + \beta_1 NOSC_{it} + \beta_2 AFEX_{it} + \beta_3 AUCI_{it} + \beta_5 FSIZ_{it} + \mu_{it} \ldots (1)$$

Equation 1 above expressed the fog index being a measure of annual report readability as a function of board subcommittee effectiveness. Specifically, board subcommittee effectiveness was measured in terms of number of subcommittees (NOSC), audit committee financial expertise (AFEX), audit committee independence (AUCI) and firm size (FSIZ)

Table 3.1: Variable measurement

Variables	Measurements	Source	Literature
Annual Report Readability	FOG Index	Annual Report	Xua, Fernando, and Tam (2018)
Board Subcommittee Effectiveness	1. **Number of Subcommittee:** Measured as number of board subcommittees. 2. **Audit committee financial Expertise:** This was measured as the number of audit committee members with professional accounting qualifications. 3. **Audit committee independence:** Audit Committee Independence in percentage was computed as the non-directors in the audit committee to audit committee members' size.	Annual Report	Chairunesia;& Bintara (2019) Chalaki, Didar & Riahinezhad, 2012
Firm Size	Firm size was measured as the natural logarithm of total asset	Annual Report	Hasan & Habib (2023)

Source: Authors (2023)

RESULTS AND DISCUSSIONS

Table 4.1: Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min	Max
Nigeria Sample					
FOGI	730	6.204	4.96	5	50
NOSC	730	3.168	1.397	0	9
AUCI	730	57.599	22.496	0	100
AFEX	730	.538	.499	0	1
FSIZ	730	7.171	.87	5.24	9.45

Source: Author's Computation (2023)

the mean of FOG index was 6.204 for the under studied firms. It is an indication that on the average, the annual report of the firms under studied in the study area difficult to read. It further shows that a childish report with readability rate range of 8 to 9. The result from the descriptive statistics also shows that the mean number of sub-committees (NOSC) was 3.168 with a standard deviation of 1.397. The result also shows that the mean of audit committee independence (AUCI) was 57.599 with the standard deviation of 22.496. The study further shows that the mean of audit committee financial expertise was 0.699 with the standard deviation of 0.859. Also, the result of the descriptive statistic showed that the mean of audit quality (AFEX) was 0.538 with a standard deviation of 0.499. In the case of the control variable of firm size (FSIZ), the result shows that the mean was 7.171 with a standard deviation of .87.

Table 4.2: Data Normality Test

Variable	Obs	W	V	Z	Prob>z
Nigeria Sample					
FOGI	730	0.627	176.582	12.645	0.000
NOSC	730	0.980	9.339	5.461	0.000
AUCI	730	0.865	64.062	10.167	0.000
AFEX	730	1.000	0.045	-7.565	1.000
FSIZ	730	0.987	6.126	4.430	0.000

Source: Author's Computation (2023)

Table 4.2 shows that FOG index has a z-statistics from the Shapiro-Wilk test as 12.645 with a Probability of Z-statistics as 0.000. The result implies that, the dependent variable of annual report readability when measured in terms of FOG index was not normally distributed across all the study samples since the probability of the z-statistics as shown in Table 4.2 were significant at 1% level. Number of sub-committees had a z-statistics from the Shapiro-Wilk test as 5.461 with a Probability of Z-statistics as 0.000 for the study. Audit committee independence has a z-statistics from the Shapiro-Wilk test as 10.167 with a Probability of Z-statistics as 0.000. Audit committee financial expertise has a z-statistics from the Shapiro-Wilk test as 6.777 with a Probability of Z-statistics as 0.000. Table 4.2 had shown that audit quality has a z-statistics from the Shapiro-Wilk test as -

7.565 with a Probability of Z-statistics as 1.000 for the Nigeria sample. Firm size has a z-statistics from the Shapiro-Wilk test as 4.430 with a Probability of Z-statistics as 0.000

Table 4.3: Correlation Analyses

Variables	(1)	(2)	(3)	(4)	(5)
Nigeria Sample					
FOGI	1.000				
NOSC	0.126	1.000			
AUCI	0.037	0.072	1.000		
AFEX	0.151	0.252	0.195	1.000	
FSIZ	0.381	0.488	0.213	0.206	1.000

Source: Author's Computation (2023)

The result also shows that FOG index was positively associated with the independent variable of number of sub-committees (0.126). FOG index was positively associated with the independent variable of audit committee independence (0.037). The result shows that audit committee financial expertise has a negative association with the dependent variable of FOG (-0.027). The correlation analysis also revealed that FOG index was positively associated with the independent variable of audit quality (0.151). In the case of the control variable, it was found that while FOG index was positively associated with the control variable of firm size (0.381).

Table 4.5: Regression Result

	Nigeria Sample		
	FOGI Model (Pool OLS)	FOGI Model (Fixed Effect)	FOGI Model (Random Effect)
CONS	-7.289 {0.106}	4.797 {0.139}	-0.421 {0.885}
NOSC	-0.046 {0.722}	-0.048 {0.543}	-0.067 {0.388}
AUCI	0.021 {0.005} **	0.011 {0.001} **	0.010 {0.002} **
AFEX	0.118 {0.582}	0.121 {0.245}	0.121 {0.244}
FSIZ	2.084 {0.000} ***	-0.014 {0.972}	0.742 {0.032} **
N	730	730	730
F-stat/wald stat	25.58 (0.0000)	6.69 (0.0000)	74.18 (0.0000)
R- Squared	0.2664	0.0999	0.0848
VIF	1.42	-	-
Hettest.	1402.79 {0.0000}	-	-
Hausman Test	-		21.62 {0.0639}

Note: (1) bracket {} are p-values: (2) **, *, implies statistical significance at 5% and 1% levels respectively**

Table 4.4 indicated that the pool OLS regression for the FOG index had an R-squared value of 0.2664. This implies that the independent variables of the study were explained only by 27% of the systematic change in the dependent variable of annual report readability when measured in terms of FOG index during the period under study. However, the unexplained part of annual report readability when measured in terms of FOG index was captured by the error term. The results obtained from the mean VIF of the regression models was 1.42 the result from the panel fixed effect showed an F-statistics value of 6.69. The probability value of 0.0000 indicated that on the overall, the fixed effect regression model was fitted for statistical inference. Also, the result indicated that the fixed effect regression had an R-squared value of 0.0999. This implies that the independent variables of the study were explained by only 9% of the systematic change in the dependent variable of annual report readability when measured in terms of FOG index during the period under study.

The Hausman test was based on the null hypothesis that the random effect model was preferred to the fixed effect model. the p-value of the Hausman test of 21.62 [0.005] indicated a significance at 5% level of significance. This implied that the study adopted the random effect panel regression results in drawing the conclusion and recommendations. This also implied that the random effect results tend to be more appealing statistically when compared to the fixed effect. Hence, the null hypothesis that board sub-committee effectiveness has no significant effect on the annual report readability of non –financial firms in Nigeria.

Discussions of Findings

The study found that the effectiveness of board sub-committees, as measured by the number of sub-committees, had a notable positive impact on the FOG index, which measures the annual report readability of listed non-financial firms in selected Sub-Saharan African countries. Board sub-committees' effectiveness, as measured by audit committee financial expertise, had a significant negative impact on the FOG index, which measured the annual report readability of non-financial firms listed in selected Sub-Saharan African countries. When evaluating the audit committee independence of board sub-committees, it had a minimal adverse impact on the FOG index, which measured the annual report readability of non-financial firms in the study area. The study found that the effectiveness of board sub-committees, specifically the audit committee's financial expertise, led to a significant decrease in the FOG index of listed non-financial firms during the study period. Board sub-committees' effectiveness, when measured by the number of board committees, has an insignificant impact on the FOG index of listed non-financial firms during the study period.

Board sub-committees' effectiveness, measured in terms of audit committee independence, had a negligible impact on the FOG index of listed non-financial firms in the Selected Sub-Saharan African countries during the study period. An increase in the number of board of directors with professional qualifications in accounting significantly decreased the FOG index measure of annual readability in the annual reports of listed non-financial firms during the study period. An increase in the number of board sub-committees will have a minimal impact on the FOG index measure of annual readability, resulting in a slight increase in the difficulty of reading the annual reports of listed non-financial firms selected during the study period. An increase in the number of non-executive directors in the audit committee have an insignificant effect on decreasing the FOG index measure of annual readability in the annual reports of listed non-financial firms during the study period.

Conclusion

In conclusion the study revealed that an increase in the number of board sub-committees will have a minimal impact on the FOG index measure of annual readability, resulting in a slightly more challenging readability of the annual report for listed non-financial firms in Nigeria. Also, an increase in the number of non-executive directors in the audit committee will have an insignificant effect on decreasing the FOG index measure of annual readability in the annual reports of listed non-financial firms in Nigeria.

Recommendations

It was recommended that professionals should be introduced into sub-committees and number of sub-committee should be increased in other to enhance effective and efficient achievement of organizational goals and help in making communication easier and report readable.

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