

Effects of Corporate Governance on Financial Performance of Listed Insurance Firms in Kenya

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Abstract

The main objective of this study was to investigate the effects of Corporate Governance on the financial performance of listed insurance companies in Kenya. Specifically, this study examined board size, board composition, CEO duality and leverage and how they affect the financial performance of listed insurance Companies in Kenya. Firm performance was measured using Return on Assets (ROA) and Return on Equity (ROE). This study adopted a descriptive research design. The study population was all those insurance Companies which were quoted on the Nairobi Securities Exchange as at December 2012. The primary data were collected through the administration of questionnaires to the staff in these listed insurance firms. Stratified random sampling technique was used to obtain the sample staff for the purpose of administering questionnaires. Secondary data were collected using documentary information from Company annual accounts for the period 2007 to 2011. Reliability test was carried out using Cronbach's alpha model. Both descriptive and inferential statistics were used. Data was analyzed using a multiple linear regression model.

The study found that a strong relationship exist between the Corporate Governance practices under study and the firms' financial performance. Board size was found to negatively affect the financial performance of insurance companies listed at the NSE. There was a positive relationship between board composition and firm financial performance. However, the most critical aspect of board composition was the experience, skills and expertise of the board members as opposed to whether they were executive or non executive directors. Similarly, leverage was found to positively affect financial performance of insurance firms listed at the NSE. On CEO duality, the study found that separation of the role of CEO and Chair positively influenced the financial performance of listed insurance firms.

Keywords: Corporate Governance, Insurance firms, Financial Performance

1. Introduction

Corporate Governance is defined as the process and structure used to direct and manage business affairs of the Company towards enhancing prosperity and corporate accounting with the ultimate objective of realizing shareholder long term value while taking into account the interest of other stakeholders (CMA Act, 2002). Corporate Governance is the system by which organizations are directed and controlled. It's a set of relationships between company directors, shareholders and other stakeholder's as it addresses the powers of directors and of controlling shareholders over minority interest, the rights of employees, rights of creditors and other stakeholders (Muriithi, 2009). Corporate Governance is also defined as an internal system encompassing policies, processes and people, which serve the needs of shareholders and other stakeholders, by directing and controlling management activities with good business savvy, objectivity, accountability and integrity (Mang'anyi, 2011). The concept of Corporate Governance has also been defined as "dealing with the ways in which suppliers of finance to corporations assures themselves of getting a return on their investment" (Shleifer and Vishny, 1997). It deals precisely with problems of conflict of interest, design ways to prevent corporate misconduct and aligns the interests of stakeholders using incentive mechanism. Corporate Governance is viewed as ethics and a moral duty of firms. A variety of Corporate Governance frameworks have been developed and adopted in different parts of the world. According to Mulili and Wong (2010), countries that followed civil law (such as France, Germany, Italy and Netherlands) developed corporate frameworks that focused on stakeholders. On the other hand, countries that had a tradition of common law (e.g. Australia, United Kingdom, USA, Canada and New Zealand) developed frameworks that focused on shareholders returns or interests.

Corporate Governance has become a topical issue because of its immense contribution to the economic growth and development of nations. The absence of good Corporate Governance is a major cause of failure of many well performing companies. Existing literature generally support the position that good Corporate Governance has a positive impact on organizational performance; OECD (2009), Gompers, Ishii and Metrick (2003), Claessens,

Djankov and Fan (2002) and others. The economic well-being of a nation is the reflection of the performance of its companies. Thus the low level of development of developing nations is attributed to the low level of good Corporate Governance practices. Hence the emphasis placed on good Corporate Governance in the existing literature as the most important problem facing the development of countries, such as Kenya.

1.1 Corporate Governance in Kenya

Corporate Governance has gained prominence in Kenya as is the case in other countries (Ekadah and Mboya, 2011). This has been caused partly by corporate failure or poor performance of public and private companies (Barako, Hancock and Izan, 2006). The PSCGT Kenya has been the greatest advocate of CG in Kenya. CG framework in Kenya started in 1999 when the Center for Corporate Governance Kenya developed a framework which was voluntary for companies to adopt. The framework was further taken up by the Capital Markets Authority (CMA) in 2000 as draft Corporate Governance practices for listed companies in Kenya. In later years the CMA made it mandatory for the listed companies to adopt those Corporate Governance practices. These Corporate Governance practices mainly dealt with the issues of the board such as board composition, role of audit committee, separation of the role of CEO and the Chair. In addition, they focused on the rights of the shareholders. Listed Companies in Kenya must comply with the Companies Act, the regulations of the Capital Markets Authority and the Nairobi Securities Exchange listing rules. Insurance Companies must also comply with regulations by the Insurance Regulatory Authority which released Corporate Governance guidelines in 2011 to be observed by Insurance Companies.

The insurance industry in Kenya has for almost three decades seen a number of changes being introduced and adopted. It is however, worrying to note that eight insurance firms have either collapsed or have been placed under statutory management; representing an average of one insurance company after every four years. These include: - Kenya National Assurance Company, United Insurance Company, Lake Star Assurance Company, Standard Assurance, Access Insurance Company, Stallion Insurance, Invesco Assurance and Blue Shield Insurance Company. In response to this trend, the government of Kenya responded by establishing the Insurance Regulatory Authority (IRA) which is the prudential regulator of the insurance industry in Kenya. IRA became autonomous on 1st May, 2007 through an Act of Parliament. IRA is also responsible for supervising and developing the insurance industry in collaboration with other stakeholders such as agents and brokers.

Kenya's insurance industry leads within the East Africa Community and is a key player in the COMESA region. The industry employs over 10,000 people. According to Ndung'u (2012), the Kenyan insurance market wrote Kenya Shillings 100 billion of Gross Direct Premiums in the year 2011. It has grown at an average rate of 16% p.a. over the last 5 years. Kenya currently has 45 licensed insurance companies. It is believed that the industry can grow tremendously if the government brings in assets into the industry instead of only playing the role of regulation. AKI forecast further growth of the industry driven by the projected growth of the economy by 5.7 percent, 6.3 percent and 6.5 percent in the next three years respectively. The common market protocol of the East African Community (EAC) creates a big market full of opportunities. According to Ndung'u (2012), the future trend of the insurance and reinsurance market in Africa was to be spread across countries with free movement and with the opportunity to exploit full cross-border growth. The industry should therefore prepare for this eventuality in a timely manner.

1.2 Statement of the problem

It is disheartening to note that no specific study has been undertaken on Corporate Governance and performance of the insurance industry in Kenya despite the fact that insurance industry is an important player in Kenya's economy. Despite tight regulatory framework, Corporate Governance continues to weaken in Kenya (Mang'anyi, 2011). According to Muriithi, (2009), many companies have been characterized by scandals. Directors have acted illegally or in bad faith towards their shareholders. Indeed, the Insurance Regulatory Authority identified poor Corporate Governance in insurance Companies as one of the threats to achieving its strategic plan 2008-2012. This is worrying especially since the industry has witnessed in the past, the collapse of firms such as Kenya National Assurance Company, United Insurance Company, Lake Star Assurance Company, Standard Assurance, Access Insurance Company, Stallion Insurance, Invesco Assurance and Blue Shield Insurance Company. It is possible to attribute their collapse to Corporate Governance practices in the insurance industry. Much needs to be done to sort out this mess otherwise we are likely to see more corporate failures and malfunctions. Whereas there has been renewed interest in Corporate Governance, relevant data from empirical studies are still few. There are therefore limitations in the depth of our understanding of Corporate Governance issues. With such an environment in the background, together with the weak judicial system, the interest of both the minority shareholders and creditors could be compromised. Consequently, performance of such firms might

be compromised. This study sought to bridge this huge gap by investigating the effects of Corporate Governance on the financial performance of listed insurance firms in Kenya in attempt to provide more empirical data in the local arena.

1.3 Objective of the Study

The general objective of the study was to investigate the effects of Corporate Governance on financial performance of listed Insurance Companies in Kenya. The specific objectives of the study were to establish the effect of board size on the financial performance of listed insurance firms, ascertain the effect of board composition on the financial performance of listed insurance firms, examine the effect of CEO duality on the financial performance of listed insurance firms and finally to examine the effect of leverage on the performance of listed insurance firms.

2 Literature

2.1 Theoretical Review

Corporate Governance is defined as the process and structure used to direct and manage business affairs of the Company towards enhancing prosperity and corporate accounting with the ultimate objective of realizing shareholder long term value while taking into account the interest of other stakeholders (CMA Act, 2002). Various theories have been put forward to help us understand the concept of Corporate Governance. Neuman (2006) defines a theory as a system of interconnected ideas that condense and organize knowledge about the world. The agency theory and the stakeholder theory are the main theories underlying the concept of Corporate Governance (Mulili and Wong, 2010). However, other theories were also discussed.

Agency Theory

Agency theory is defined as the relationship between the principals, such as shareholders and agents such as the company executives and managers. In this theory, shareholders who are the owners or principals of the company, hires the agents to perform work. Principals delegate the running of business to the directors or managers, who are the shareholder's agents (Clarke, 2004). Agency theory suggests that employees or managers in organizations can be self-interested. The agency theory shareholders expect the agents to act and make decisions in the principal's interest. On the contrary, the agent may not necessarily make decisions in the best interests of the principals (Padilla, 2000). The agent may be succumbed to self-interest, opportunistic behavior and falling short of congruence between the aspirations of the principal and the agent's pursuits. Even the understanding of risk defers in its approach. Although with such setbacks, agency theory was introduced basically as a separation of ownership and control (Bhimani, 2008). The agents are controlled by principal-made rules, with the aim of maximizing shareholders value. Hence, a more individualistic view is applied in this theory (Clarke, 2004).

Indeed, agency theory can be employed to explore the relationship between the ownership and management structure. However, where there is a separation, the agency model can be applied to align the goals of the management with that of the owners. The model of an employee portrayed in the agency theory is more of a self-interested, individualistic and are bounded rationality where rewards and punishments seem to take priority (Jensen & Meckling, 1976).

Stewardship Theory

A steward is defined by Davis, Schoorman & Donaldson (1997) as one who protects and maximizes shareholders wealth through firm performance, because by so doing, the steward's utility functions are maximized. In this perspective, stewards are company executives and managers working for the shareholders, protects and make profits for the shareholders. Stewardship theory stresses not on the perspective of individualism, but rather on the role of top management being as stewards, integrating their goals as part of the organization. The stewardship perspective suggests that stewards are satisfied and motivated when organizational success is attained. It stresses on the position of employees or executives to act more autonomously so that the shareholders' returns are maximized. Indeed, this can minimize the costs aimed at monitoring and controlling behaviors (Daly et al., 2003). On the other end, Daly et al. (2003) argued that in order to protect their reputations as decision makers in organizations, executives and directors are inclined to operate the firm to maximize financial performance as well as shareholders' profits. In this sense, it is believed that the firm's performance can directly impact perceptions of their individual performance. Moreover, stewardship theory suggests unifying the role of the CEO and the chairman so as to reduce agency costs and to have greater

free-riders. They argued that when a board becomes too big, it often moves into a more symbolic role, rather than fulfilling its intended function as part of the management. On the other hand, very small boards lack the advantage of having the spread of expert advice and opinion around the table that is found in larger boards. Furthermore, larger boards are more likely to be associated with an increase in board diversity in terms of experience, skills, gender and nationality (Dalton and Dalton, 2005). Expropriation of wealth by the CEO or inside directors is relatively easier with smaller boards since small boards are also associated with a smaller number of outside directors. The few directors in a small board are preoccupied with the decision making process, leaving less time for monitoring activities.

Vafeas (2000) reported that firms with the smallest boards (minimum of five board members) are better informed about the earnings of the firm and thus can be regarded as having better monitoring abilities. Echoing the above findings, Mak and Yuanto (2003) reported that listed firm valuations of Singaporean and Malaysian firms are highest when the board consists of five members. Bennedsen, Kongsted and Nielsen (2004), in their analysis of small and medium-sized closely held Danish corporations reported that board size has no effect on performance for a board size of below six members but found a significant negative relation between the two when the board size increases to seven members or more. Bhagat and Black (2002), found no solid evidence on the relationship between board size and performance. In an attempt to compare the effects of board structure on firm performance between Japanese and Australian firms, Bonn, Yokishawa and Phan (2004) found that board size and performance (measured by market-to-book ratio and return on assets) was negatively correlated for Japanese firms but found no relationship between the two variables for its Australian counterpart. However, contrary to the Japanese firms the ratios of outside directors and female directors to total board numbers have a positive impact in the Australian sample (Bonn, 2004).

Contrary to the above findings, a positive impact on performance was recorded with larger board size by Mak and Li (2001) and Adams and Mehran (2005); however, in examining 147 Singaporean firms from 1995 data, Mak and Li (2001) support the argument that board structure is endogenously determined when the results of their OLS indicate that board size, leadership structure and firm size have a positive impact on firm performance but their 2SLS regressions do not support this result. Adams and Mehran (2005) found a positive relationship between board size and performance (measured by Tobin's Q) in the U.S banking industry. Adam and Mehran's results suggest that such performance relationship may be industry specific, indicating that larger boards works well for certain type of firms depending on their organizational structures. A meta-analysis based on 131 studies by Dalton and Dalton (2005) revealed that larger boards are correlated with higher firm performance.

Boards with a large number of directors can be a disadvantage and expensive for the firms to maintain. Planning, work coordination, decision-making and holding regular meetings can be difficult with a large number of board members. Generally, Empirical evidence on the relationship between board size and firm performance provide mixed results .While, Ahmadu et al. (2005), Chan and Li (2008), De Andres et al. (2005) and Mustafa (2006) found that larger boards are associated with poorer performance, Beiner et al. (2004), Bhagat and Black (2002) and Limpaphayom and Connelly (2006) found no significant association between board size and firm performance.

Board Composition and firm performance

Boards mostly compose of executive and non-executive directors. Executive directors refer to dependent directors and non-Executive directors to independent directors (Shah et al., 2011). At least one third of independent directors are preferred in board, for effective working of board and for unbiased monitoring. Dependent directors are also important because they have insider knowledge of the organization which is not available to outside directors, but they can misuse this knowledge by transferring wealth of other stockholders to themselves (Beasley, 1996).A board composed of members who are not executives of a company, nor shareholders, nor blood relatives or in law of the family (Gallo, 2005). An independent board is generally composed of members who have no ties to the firm in any way, therefore there is no or minimum chance of having a conflict of interest because independent directors have no material interests in a company. Dalton, Daily, Ellstrand, & Johnson (1998) saw Jacobs (1985) stating that independent directors are important because inside or dependent directors may have no access to external information and resources that are enjoyed by the firm's outside or independent directors (e.g., CEOs of other firms, former governmental officials, investment bankers, Social worker or public figures, major suppliers). Moreover, for advice/counsel inside or dependent directors are available to the CEO as a function of their employment with the firm; their appointment to the board is not necessary for fulfillment of this function.

Staikouras et al. (2007) find that board composition does not affect firm performance although its relationship with performance was found to be positive. These findings were similar to those of Adusei (2010) who found no relationship between board composition and bank performance in Ghana although board composition was found to have positive effect on bank efficiency. At the same time, Alonso and Gonzalez (2006) studied 66 banks in OECD countries from 1996 to 2003. They established an inverted U shaped relation between the measures of bank performance (Tobin's Q, ROA, the annual market return of a bank shareholder) and board size which they posit justifies a large board but imposing an efficient limit on size. According to Jensen and Meckling (1976), boards dominated by outsiders or NEDs may help to mitigate the agency problem by monitoring and controlling the opportunistic behavior of management. The results of previous studies that investigated the relationship between board composition and firm performance are inconsistent. Dehaena et al. (2001), Omar (2003) and Rhoades et al. (2000) found that NED has a positive relationship with financial performance. For example, Krivogorsky (2006), Lefort and Urzúa (2008) and Limpaphayom and Connelly (2006) also found a positive relationship between board composition (the proportion of independent directors on the board) and firm performance. Hasnah (2009) showed that Non Executive Directors is significantly related to firm performance that is measured by ROA. On the other hand, Coles et al. (2001) demonstrated that there is a negative impact of outside directors on firm performance. Erickson et al. (2005) also found a negative relationship between greater board independence and firm value. However, Bhagat and Black (2002) and De Andres et al. (2005) found no significant relationship between the composition of the board and the value of the firm. Based on above discussion and in the light of the agency theory, the following hypothesis can be empirically tested.

CEO Duality and firm performance

The Chief Executive Officer (CEO) of an organization can play an important role in creating the value for shareholders. The CEO can follow and in Corporate Governance provisions in a firm to improve its value (Defond and Hung, 2004). In addition, the shareholders invest heavily in the firms having higher Corporate Governance provisions as these firms create value for them (Morin and Jarrell, 2001). The decisions of the board about hiring and firing a CEO and their proper remuneration have an important bearing on the value of a firm. The board usually terminates the services of an underperforming CEO who fails to create value for shareholders. The turnover of CEO is negatively associated with firm performance especially in developed markets because the shareholders lost confidence in these firms and stop making more investments. It is the responsibility of the board to determine the salary of the CEO and give him proper remuneration for his efforts (Monks and Minow, 2001). The board can also align the interests of the CEO and the firm by linking the salary of a CEO with the performance of a firm. This action was motivate the CEO to perform well because his own financial interest is attached to the performance of the firm.

The tenure of a CEO is also an important determinant of the firm's performance. CEOs are hired on short-term contracts and are more concerned about the performance of the firm during their own tenure causing them to lay emphasis on short and medium-term goals. This tendency of the CEO limits the usefulness of stock price as a proxy for corporate performance (Bhagat and Jefferis, 2002). The management of a firm can overcome this problem by linking some incentives for the CEO with the long-term performance of the firm (Heinrich, 2002). CEO duality plays an important role in affecting the value of a firm. A single person holding both the Chairman and CEO role improves the value of a firm as the agency cost between the two is eliminated (Alexander, Fennell and Halpern, 1993). On the negative side, CEO duality lead to worse performance as the board cannot remove an underperforming CEO and can create an agency cost if the CEO pursues his own interest at the cost of the shareholders (White and Ingrassia, 1992).

Jensen and Meckling (1976) argued that when an individual is holding two top positions there is a tendency on the path of such individual to adopt personal interests' strategies that could be detrimental to the firm as a whole. Sharing the same thought, Mallette (1992) argued that in the combined roles, the chairman of the board has to make decisions potentially leading to the conflict of interest. Moreover, in the combined roles, the CEO can set the board's agenda and can influence (if not control) the selection of directors of the board. They concluded in their paper that CEO duality can challenge a board's ability to monitor executives. However, empirical analyses of the impact of duality on various corporate performance measures have yielded conflicting results. Ahmadu, Aminu and Taker (2005), Bhagat and Bolton (2008), Coles et al. (2001), Feng, Ghoshand and Sirmans (2005), Judge, Naoumova and Koutzevol (2003), Kyereboah - Colemn and Biekpe (2005) and Mustafa (2006) found negative significant relationship between CEO duality and firm performance. In contrast, Carapeto, Lasfer and Machera (2005), Schmid and Zimmermann (2007) and Wan and Ong (2005) found no significant difference in the performance of companies with or without role duality.

Leverage and firm performance

Significant creditors, such as banks, have large investments in the firm, and want to see the returns on their investments materialize. Their power comes in part because of a variety of control rights they receive when firms default or violate debt covenants (Smith and Warner, 1979) and in part because they typically lend short term, so borrowers have to come back at regular short intervals for more funds. As a result, banks and other large creditors are in many ways similar to the large shareholders. Diamond (1984) presents one of the first models of monitoring by the large creditors. Kaplan and Minton (1994) document the higher incidence of management turnover in response to poor performance in companies that have a principal banking relationship relative to companies that do not. DeLong (1991), points to a significant governance role played by J.P. Morgan partners in the companies J.P. Morgan invested in the early 20th century. Gilson (1990), report that U.S. banks play a major governance role in bankruptcies, when they change managers and directors. Weir, Laing and McKnight (2002), hypothesizes that debt financing is an internal governance mechanism whereby increased debt reduces free cash flow and so limits managerial discretion. Debt requires managers to use any excess funds to service company's debts rather than engage in negative net present value projects.

Debt owed to large creditors such as banks is believed to be a useful tool for reducing the agency problem. Large creditors, like large stakeholders, also have interest in seeing that managers take performance-improving measures. Empirical evidence seems to be in support of this assertion. Shleifer and Vishny (1997) in a review article, cite the works of Kaplan and Minton (1994) and Kang and Shivdasani (1995), who found higher incidence of management turnover in Japan in response to poor performance in companies that have a principal banking relationship relative to companies that do not. Leverage has been widely used as a control variable by a number of empirical studies (such as Kyereboah – Coleman, Biekpe, 2006; Alsaeed, 2006) that have examined the relationship between Corporate Governance and financial performance of a Company. In their attempt to justify taking leverage as a control variable, these studies have revealed that the debt has an effect on the financial performance of a Company. Alsaeed, 2006 suggests that firm leverage was measured by dividing total of liabilities by the total of assets.

Another form of agency problem, known as debt agency, arises when there is a conflict of interests between stockholders and debt holders. Debt holders are entitled to claims and these have the tendency to rise at low levels of firm performance, and to remain constant beyond a certain level of that performance. Thus, good performance benefits the stockholders more than it does debt holders, but this is not true when performance is very low. In fact, as the firm moves towards bankruptcy, equity holders face the risk of losing only their shareholdings, passing the burden of such bankruptcy to the debt holders. Taken together, these outcomes encourage managers working to protect the interest of equity holders to embark on risky, high-return projects. This could lead to economic inefficiency since projects that are otherwise profitable may be foregone in exchange for high risk but inferior counterparts. The literature seems to present no unanimous position on the role of debt. Although some see it as having the potential to induce the right steps by the board to protect shareholder interests, other scholars point to the emergence of debt agency and to the need to constitute boards in ways that would protect both shareholder and creditor interests. To achieve this, it is suggested that the board should have a representation from the creditors, as is often the case in Japan and Germany where banks have significant debt holding interests.

Debt purchasers provide finance in return for a promised stream of payments and a variety of other covenants relating to corporate behavior, such as the value and risk of corporate assets. If the corporation violates these covenants or default on the payments, debt holders typically could obtain the rights to repossess collateral, throw the corporation into bankruptcy proceedings, vote in the decision to reorganize, and remove managers. However, there could be barriers to diffuse debt holders to effectively exert Corporate Governance as envisaged. Small debt holders may be unable to monitor complex organization and could face the free-rider incentives, as small equity holders. Also, the effective exertion of corporate control with diffuse debts depends largely on the efficiency of the legal and bankruptcy systems. Large debt holders, like large equity holders, could ameliorate some of the information and contract enforcement problems associated with diffuse debt. Due to their large investment, they are more likely to have the ability and the incentives to exert control over the firm by monitoring managers. Large creditors obtain various control rights in the case of default or violation of covenants. In terms of cash flow, they can renegotiate the terms of the loans, which may avoid inefficient bankruptcies. The effectiveness of large creditors however, relies importantly on effective and efficient legal and bankruptcy systems. If the legal system does not efficiently identify the violation of contracts and provide the means to bankrupt and reorganize firms, then creditors could lose a crucial mechanism for exerting Corporate Governance. Also, large creditors, like large shareholders, may attempt to shift the activities of the bank to reflect their own preferences. Large creditors for example, as noted by Myers (1997) may induce the company to

forego good investments and take on too little risk because the creditor bears some of the cost but was not share the benefits.

Measuring Firm Performance

Firm performance is studied and measured by different researchers (Shah et al., 2011; Matolcsy & Wright, 2011; Yasser et al., 2011) using different measures. Matolcsy & Wright (2011) measured firm performance by ROA (Return on Assets= EBIT / Average total Assets – in book value -), ROE (Return on Equity=net profit / equity - in book value -), Change in market value of equity, Change in market value of equity, adjusted for dividends and risk). Yasser et al. (2011) used return on equity (ROE) and profit margin (PM) for the measurement of firm performance. Market based measures of companies' performance were done by Shah et al. (2011) by Market value of equity divided by book value of equity and Tobin's Q (market value of equity + book value of debt/total of assets - in book value -), whereas financial reporting perspective was measured by ROE and Return on investment (net result + interest) / (equity +total debt). Bhagat & Black (1999) measured dependent variable firm performance by Tobin's Q, Return on assets (Operating income/Assets), Turnover ratio (Sales/Assets), Operating margin (Operating income/Sales), Sales per employee and also by Growth of Assets, Sales, Operating income, Employees and Cash flows. The study was focus on those measures that are strategically important for the success of the company. In that direction, the study would measure the financial performance of the companies by looking at profitability (Return On Assets, Return on Equity and Dividend Yield).

Return on Assets (ROA)

ROA refers to the amount of net income returned as a percentage of total assets. It can be decomposed as follows: Return on Assets= EBIT / Average total Assets – in book value

Return on Equity (ROE)

ROE refers to the amount of net income returned as a percentage of shareholders equity. Return on equity measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested. Each insurance firm's ROE has been obtained for its annual reports. ROE is expressed as a percentage and calculated as: Net Income/Shareholder's Equity * 100 Net income is for the full fiscal year, before any dividends are paid to common stockholders but after dividends are paid to preferred stock. Shareholder's equity does not include preferred shares.

2.3 Empirical Review

Beiner, Drobetz, Schmid and Zimmerman (2004) studied the Corporate Governance and firm valuation by using a broad Corporate Governance index and additional variables related to ownership structure, board characteristics, and leverage to provide a comprehensive description of firm-level Corporate Governance for a broad sample of Swiss firms. The study used Tobin's Q for growth and found a positive relationship between Corporate Governance and growth. An increase in Corporate Governance index by one point caused an increase of the market capitalization by roughly 8.6%, on average, of a company's book asset value. Zheka (2007) studied the effect Corporate Governance on performance by constructing an overall index of Corporate Governance and shows that it predicts firm level productivity in Ukraine. The results imply that a one-point-increase in the index results in around 0.4%-1.9% increase in performance; and a worst to best change predicts a 40% increase in company's performance. Using data on companies in many African countries, including Ghana, South Africa, Nigeria and Kenya, Kyereboah-Coleman (2007) shows that better governance practices are associated with higher valuations and better operating performance. Baker, Godridge, Gottesman and Morey (2007) using a unique dataset from Alliance Bernstein, an international asset management company, with monthly firm-level and country-level governance ratings for 22 emerging markets countries over a five year period, report a significantly positive relation between firm-level (and country-level) Corporate Governance ratings and market valuation, suggesting lower cost of equity for better governed firms.

In Kenya, Wanjiku et al (2011) carried out a study to establish the Corporate Governance practices of firms and its relationship with the growth of Companies listed at the Nairobi Securities Exchange using a causal comparative research design. The study focused on corporate communication, leadership and technology application. The study found a positive linear dependence of growth and Corporate Governance. Ongore and K'Obonyo (2011) conducted a similar study in Kenya to examine the interrelations among ownership, board and manager characteristics and firm performance in a sample of 54 firms listed at the Nairobi Securities Exchange. The findings from this study show a positive relationship between managerial discretion and performance.

However, the relationship between ownership concentration and government on firm performance was significantly negative.

Mang'anyi (2011) carried out a study to explore the ownership structure and Corporate Governance and its effects on performance of firms. His study focused on selected banks in Kenya. His study revealed that there was significant difference between Corporate Governance and financial performance of banks. The study recommended that corporate entities should promote Corporate Governance to send positive signals to potential investors and that regulatory agencies including the government should promote and socialize Corporate Governance and its relationship to firm performance across industries. Miring'u and Muoria (2011) analyzed the effects of Corporate Governance on performance of commercial state corporations in Kenya. Using a descriptive study design, the study sampled 30 SCs out of 41 state corporations in Kenya and studied the relationship between financial performance, board composition and size. The study found a positive relationship between Return on Equity (ROE) and board compositions of all State Corporations.

2.4 Research Gaps

Corporate Governance is important in all organizations regardless of their industry, size or level of growth. Good Corporate Governance has a positive economic impact on the Institution in question as it saves the organization from various losses such as those occasioned by frauds, corruption and similar irregularities. Besides it also spurs entrepreneurial innovation enabling the organization to better seize the economic opportunities that come its way. The main Corporate Governance themes that are currently receiving attention are adequately separating management from the board to ensure that the board is directing and supervising management, including separating the chairperson and chief executive roles; ensuring that the board has an effective mix of independent and non-independent directors; and establishing the independence of the auditor and therefore the integrity of financial reporting, including establishing an audit committee of the board. Good Corporate Governance aims at increasing profitability and efficiency of organizations and their enhanced ability to create wealth for shareholders, increased employment opportunities with better terms for workers and benefits to stakeholders. Thus, the main tasks of Corporate Governance refer to: assuring corporate efficiency and mitigating arising conflicts providing for transparency and legitimacy of corporate activity, lowering risk for investments and providing high returns for investors and delivering framework for managerial accountability.

The studies cited in the literature mostly concentrate on the developed countries whose strategic approach and Corporate Governance systems are not similar to that of Kenya. In Kenya, the studies done in financial services sector have focused on other companies other than insurance service providers in Kenya. For instance, Jebet (2001) conducted a study of Corporate Governance practices among the quoted companies in Kenya, Muriithi (2005) did a study on the relationship between Corporate Governance mechanisms and performance of firms quoted on the NSE, Manyuru (2005) researched on Corporate Governance and organizational performance the case of companies quoted at the NSE while Matengo (2008) did a study on the relationship between Corporate Governance practices and performance: the case of banking industries in Kenya. None of these studies have focused specifically on the relationship between Corporate Governance and financial performance of listed insurance Companies in Kenya. Many other researchers have examined the relationship between variety of governance mechanisms and firm performance. However, the results are mixed. Some researchers examine only one governance mechanism on performance while others investigate the influence of several mechanisms on performance.

3 Research Methodology

3.1 Introduction

This section provides information on the type of research design that was adopted for the study. It gives the population and sample selected for the study. It also show which sample was used in the current research. Furthermore it discusses the data collection, analysis and presentation techniques that were used in the study.

3.2 Research design

Ranjit Kumar, (2005) defined a research design as a procedural plan that is adopted by the researcher to answer questions validly, objectively, accurately and economically. A research design helps a researcher to conceptualize an operational plan to undertake the various procedures and tasks required to complete the study

and to ensure that these procedures are adequate to obtain valid, objective and accurate answers to the research questions.

This study adopted a descriptive research design. According to Mugenda and Mugenda (2003), descriptive research is a process of collecting data in order to test hypotheses or to answer questions concerning the current status of the subjects in the study. A descriptive study determines and reports the way things are. The choice of the descriptive study design was based on the fact that the research was interested on the state of affairs already existing in the field and no variable was manipulated. This study therefore was able to generalize the findings to a larger population. The main focus of this study was quantitative. However some qualitative approaches were used in order to gain a better understanding and possibly enable a better and more insightful interpretation of the results from the quantitative study.

3.3 Population

A population refers to an entire group of individuals, events or objects having common observable characteristics (Mugenda and Mugenda, 2003). Target population is defined as a computed set of individuals, cases or objects with some common observable characteristics of a particular nature distinct from other population. According to Ngechu (2004), a population is a well-defined or set of people, services, elements, events, group of things or households that are being investigated. This definition ensures that population of interest is homogeneous. For this study, the population consisted of all 45 insurance Companies registered under the Insurance Act Chapter 487 Laws of Kenya as per the listing available on the Insurance Regulatory Authority (IRA) website.

3.4 Sampling frame

A sampling frame is a complete list of the units of analysis of interest from which the samples are selected while a sample size is the number of items to be selected from the universe to constitute a sample (Kothari, 2004). The optimum sample size was used to fulfill the requirements of efficiency, representativeness and reliability. Unnecessary large sample size would bring about data duplicity besides having cost and time implications while a smaller sample size would not be representative.

This study sought to investigate the effects of Corporate Governance on performance of listed insurance firms in Kenya. From the entire list of registered insurance firms, the researcher purposely picked only the insurance companies listed on the Nairobi Securities Exchange as at 31st December 2012. This was achieved by obtaining a separate list of all listed insurance Companies from the Nairobi Stock Exchange website as per Appendix IV. Six insurance Companies qualified for study. However, in order to fulfill the requirement of obtaining performance data over a period of five years ending 2011, all companies that were not consistently listed between 2007 to 2011 were eliminated. Thus only two firms were used in the sample actually studied. A sample of the responding staff was drawn from the entire staff population at the Head Offices of the two firms situated in Nairobi. The two Insurance companies had a total 396 employees.

3.5 Sampling Techniques

The study adopted a stratified random sampling technique to come up with the required sample since the population was heterogenous. The goal of stratified random sampling is to achieve desired representation from various subgroups in the population (Mugenda and Mugenda, 2003). Subjects are selected in such a way that the existing subgroups in the population are more or less reproduced in the sample. Mugenda and Mugenda (2003) advises that to use stratified random sampling, one must first decide on the criteria under which the population and hence the sample was stratified and then decide on the size of each stratum in the sample. In this study, however, departments and/or sections already existed hence the first step was already met since each section performs unique tasks and was therefore homogenous within itself but heterogeneous between other sections. The study identified all the sections in each of the firms which formed the different strata before selecting the units from each stratum which were to be included in the sample.

3.6 Sample design and sample size

A sample is a small group obtained from accessible population, (Mugenda & Mugenda, 2003). Sampling is the procedure a researcher uses to gather people, places or things to study, (Kombo & Tromp, 2006). It is the process of selecting a number of individuals or objects from a population such that the selected group contains elements representative of characteristics found in the entire group, (Orotho and Kombo, 2002). Stratified random sampling was applied in carrying out the study as per the departments, a sample of 10% of the total population

was used therefore 40 respondents constituted the sample population for the study. According to Gay in Mugenda and Mugenda, (2003), for descriptive studies at least 10% - 20% of the total population is enough. Stratified random sampling ensures inclusion, in the sample, of sub groups, which otherwise would be omitted entirely by other sampling methods because of their small number of population, (Mugenda & Mugenda, 2003).

3.7 Data collection Instruments

The study used both primary and secondary data sources in gathering data for analysis. The primary data source was the use of a semi-structured (matrix) questionnaire consisting of both open and close-ended questions (Mugenda and Mugenda, 2003). Mugenda and Mugenda (2003) posit that when questions are presented in a matrix form, they are easier to complete and hence the respondents are unlikely to put off. The space is also used efficiently and it is easy to compare responses given to different items. This easy comparability is advantageous to both the researcher and the respondent. The researcher can easily detect a trend just by glancing at the responses. Secondary data was collected from published annual reports and websites of the selected Companies. The secondary data provided a reliable source of the information needed by researcher to investigate the phenomenon and seek efficient ways for problem solving situations (Uma, 2003). Primary data collection involved self-administration of questionnaires. The researcher dropped the questionnaires physically at the respondents' places of work. The questionnaires were left with the respondents and were picked up later by the researcher once they were filled up. Each questionnaire was coded and the researcher was the only one who knew which respondent filled it. The coding technique was used only for the purpose of matching returned completed questionnaires with those delivered to the respondents. Secondary data was collected by downloading published annual accounts from these Companies websites. Specifically the data was collected from the portion expounding on corporate information, statement of Corporate Governance as well as the directors' profile. Data on financial performance was collected from final statements such as balance sheets, statements of cash flows, statements of changes in equity and statements of comprehensive incomes provided in the cash flows. Secondary data was easy to collect owing to the ease of availability. The researcher made use of his personal laptop computer that has internet capability.

3.8 Pilot testing of the instrument

A pilot test was conducted on one of the Companies to field test the reliability and the validity of the data to be collected using the questionnaire (Kothari, 2004). The questionnaire was tested to a selected sample which was similar to the actual sample. Subjects in the actual sample was not be used in this pilot study. Same procedures to be used in the actual data collection exercise were used for the pretesting exercise. The pretest sample was 10% of the sample size.

Validity of instruments

According to Kothari (2004) validity is the degree by which the sample of the test items represents the content the test is designed to measure. The study questionnaire was scrutinized for content validity by experts in business research. Factor analysis was employed to test the suitability of the research instrument. The suggestions on the content and structure were included to improve the final draft of the instrument.

Reliability Analysis

Reliability of the questionnaire was evaluated through Cronbach's Alpha which measures the internal consistency. Cronbach's alpha was calculated by application of SPSS for reliability analysis. The value of the alpha coefficient ranges from 0-1 and may be used to describe the reliability of factors extracted from dichotomous and or multi-point formatted questionnaires or scales. A higher value shows a more reliable generated scale. Cooper & Schindler (2008) has indicated 0.7 to be an acceptable reliability coefficient. Table 4.2 shows that CEO duality had the highest reliability ($\alpha=0.848$) followed by board Size ($\alpha=0.821$), then composition of board members ($\alpha = 0.797$) and leverage ($\alpha=0.713$). This illustrates that all the four scales were reliable as their reliability values exceeded the prescribed threshold of 0.7.

Table 4.2: Reliability Coefficients

Scale	Cronbach's Alpha	Number of Items
Board Size	0.821	7
Composition Of Board Members	0.797	9
CEO Duality	0.848	4
Leverage	0.713	3

3.9 Data processing and analysis

Descriptive statistics

The study used the Likert type scale as the rating scale in questionnaires. According to Mugenda and Mugenda (2003), Likert scales are often used with matrix questions. The items that are used in Likert scales are usually declarative in form. Kumar (2005) claims that Likert scales are the easiest to construct and are based upon the assumption that each statement/item on the scale has equal attitudinal value, importance or weight in terms of reflecting an attitude towards the issue in question. The numbers in a Likert scale are ordered such that they indicate the presence or absence of a characteristic being measured. Data collected was mostly quantitative in nature and was analyzed by descriptive analysis techniques using tools such as Statistical Package for Social Sciences (SPSS). Qualitative data was analyzed descriptively. Below is a description of the key characteristics and terms of measurement for each variable. This study focused on Corporate Governance characteristics namely board size, board composition, CEO Duality and Leverage and how they affect performance. Dependent and independent variables were grouped into components; namely, independent variables which consist of board size, board composition, CEO Duality and leverage and dependent variables which consist of performance indicators namely, Return on Assets and Return on Equity. The terms of measurement to be used are described as in table below.

Table 3.3: Summary for terms of measurement

Variables	Terms of measurement
BOS (Board Size)	Total number of directors on the board
BODCOMP (Board Composition)	Ratio of outside directors to total number of directors
CEODUAL (CEO Duality)	Dummy variable 1 if CEO and Chairman are the same person; 0 if CEO and Chairman are different persons
LEVERAGE Leverage %	Ratio of total liabilities to total assets
ROA (Return on Assets)	Amount of net income as a percentage of total assets/Earnings before tax divided by total assets of the Company
ROE (Return on Equity)	Amount of net income returned as a percentage of shareholders equity.

The above terms of measurement were useful in computing the descriptive statistics of the variables of the study which show the mean, median, standard deviation, minimum and maximum.

Correlation analysis

Correlation analysis is the statistical tool that can be used to determine the level of association of two variables (Levin & Rubin, 1998). This analysis can be seen as the initial step in statistical modeling to determine the relationship between the dependent and independent variables. Prior to carrying out a multiple regression analysis, a correlation matrix was developed to analyze the relationships between the independent variables as this would assist in developing a prediction multiple model. Correlation analysis helped to detect any chance of multicollinearity. Correlation value of 0 shows that there is no relationship between the dependent and the independent variables. On the other hand, a correlation of ± 1.0 means there is a perfect positive or negative relationship (Hair et al., 2010). The values were interpreted between 0 (no relationship) and 1.0 (perfect relationship). The relationship was considered small when $r = \pm 0.1$ to ± 0.29 , while the relationship was be considered medium when $r = \pm 0.3$ to ± 0.49 , and when $r = \pm 0.5$ and above, the relationship was considered strong.

Regression analysis

Multiple regression analysis is a statistical method utilized to determine the relationship between one dependent variable and one or more independent variables (Hair et al., 2010). This study employed a multiple linear regression analysis using Return on Assets (ROA) and Return on Equity (ROE) as proxy for the firm's financial performance as dependent variables and independent variables comprising of Board Size, Board Composition, CEO Duality and Leverage.

Normality test

Normality of the variables was examined using the skewness and kurtosis. According to Kline (2011), the univariate normality of variables can be assumed if the skewness statistic is within the interval (-3.0, 3.0) and the kurtosis statistic lying in the interval (-10.0, 10.0).

Multicollinearity test

The issue of multicollinearity may arise if two or more variables was be highly correlated. It may affect the estimation of the regression parameters (Hair et al., 2010). Multicollinearity was tested by examining the correlation matrix.

Multiple regression model

This study employed the following model;

$$Y_{it} = \beta_0 + \beta_1BOS + \beta_2BODCOMP + \beta_3CEODUAL + \beta_4LEVERAGE + e_t$$

Where:

Y_{it} represents firm performance variables which are: Return on Assets and Return on Equity for insurance firms at time t.

BOS represents Board Size,

BODCOMP represents Board Composition,

CEODUAL represents CEO Duality

LEVERAGE represents Leverage as a Corporate Governance variable and

e_t , the error term which account for other possible factors that could influence Y_{it} that are not captured in the model.

Based on the fact that different financial performance proxies were employed, the above model was therefore modified as below to determine the relationship between firm performance and Corporate Governance of insurance firms in Kenya.

Equation 3.1

$$ROA_{it} = f(BOS_t, BODCOMP_t, CEODUAL_t, LEVERAGE_t) \dots \dots \dots (1)$$

$$ROA_{it} = \beta_0 + \beta_1BOS_t + \beta_2BODCOMP_t + \beta_3CEODUAL_t + \beta_4LEVERAGE_t + e_t \dots \dots \dots (2)$$

Equation 3.2

$$ROE_{it} = f(BOS_t, BODCOMP_t, CEODUAL_t, LEVERAGE_t) \dots \dots \dots (3)$$

$$ROE_{it} = \beta_0 + \beta_1BOS_t + \beta_2BODCOMP_t + \beta_3CEODUAL_t + \beta_4LEVERAGE_t + e_t \dots \dots \dots (4)$$

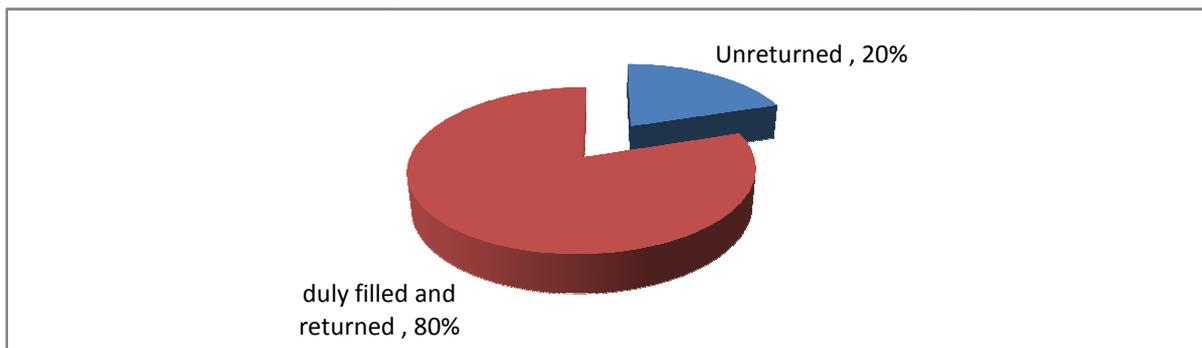
Where: ROA and ROE represents firm performance variables which are: Return on assets and Return on equity for Insurance firms at time t.

4 Data Analysis, Results and Discussion

4.1 Response Rate

To determine the actual number of responses who actively participated in the study, analysis of the response rate was conducted as shown in the figure 4.2 below. The data collection instrument, which was the questionnaires, was sent to 40 employees. However, out of the 40 questionnaires sent, only 32 questionnaires were received back fully completed making a response rate of 80%. This is in agreement with what was indicated by Cooper and Schindler (2003) who indicated that a response rate of between 30 to 80% of the total sample size can be generalized to represent the opinion of the entire population.

Figure 4.2: Response rate

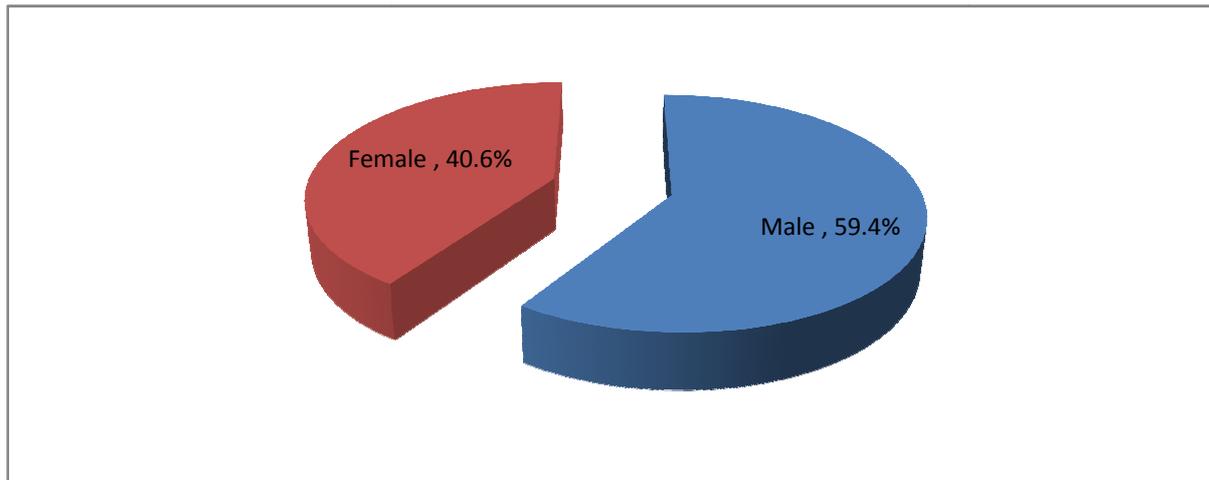


4.2 Quantitative Analysis

Background information

The study sought to establish the background information of the respondents including respondents' gender, duration of work in the organization, position in the organization and number of employees in the organization. From the findings, the study revealed that respondents held various positions namely: quality compliance officer , claims staff, administrators , human resource managers , premium administrators , corporate business administrators, Unit leaders , actuarial managers , accountant, staff , financial managers, risk managers , operation manager, company secretary and unit leader finance .

Figure 4.3: Gender of the respondent



The study also found that both gender were involved in data collection and thus the findings could not suffer from gender biasness. On the number of years the respondents had worked in the company, the respondents had worked in the company between 2 to 11 years, this is an indication that respondents had worked in their organization long enough to give credible information. The study sought to determine the number of employees in this organization, the study revealed that those employed in permanent terms ranged between 9 and 115, those employed on casual ranged between 5 to 50 and those employed on contract ranged between 500 to 700 agents.

Board Size

The study sought to establish the effects of board size on the financial performance of listed insurance firms.

Table 4.4: Effect of board size on the financial performance of insurance companies

	Not at all	Small extent	Moderate extent	Large extent	Very large extent	Mean	Std Deviation
Size of the board affects the financial performance of insurance Companies	6	6	6	12	2	2.9375	1.28938
The board meets regularly during the year to review financial performance and operations of the Company	0	0	4	4	24	4.6250	.71880
The board considers strategic matters and other issues that impact on the Company's performance	0	2	0	4	26	4.6875	.79320

Dialogue and meetings between the board and senior management are held outside formal board meetings.	2	2	14	14	0	3.2500	.85635
Board members usually avail themselves to support management on areas of their expertise.	2	4	6	10	10	3.6875	1.25000
The board is effective at monitoring senior management	0	4	6	12	10	3.8750	1.02470
The board undertakes self-evaluation and review of its performance	0	0	10	16	6	3.8750	.71880

The study found that majority of the respondents rated the following to a very great extent, the board considers strategic matters and other issues that impact on the Company's performance as shown by mean of 4.6875 and the board meets regularly during the year to review financial performance and operations of the Company as shown by mean of 4.6250. Those rated to great extent were; the board undertakes self-evaluation and review of its performance and the board is effective at monitoring senior management as shown by mean of 3.8750 in each case and board members usually avail themselves to support management on areas of their expertise as shown by mean of 3.6875. Those rated to moderate extent, dialogue and meetings between the board and senior management are held outside formal board meetings as shown by mean of 3.25 and size of the board affects the financial performance of insurance Companies as shown by mean of 2.9375. This was supported by low standard deviation, an indication that respondents held similar opinions.

These findings concur with the findings of Hermalin and Weisbach (2003) who argued the possibility that larger boards can be less effective than small boards. Large boards may result to increase in agency problems as some directors may tag along as free-riders. Vafeas (2000) also reported that firms with the smallest boards (minimum of five board members) are better informed about the earnings of the firm and thus can be regarded as having better monitoring abilities. Yokishawa and Phan (2004) found that board size and performance (measured by market-to-book ratio and return on assets) was negatively correlated for Japanese firms. On whether insurance companies have a Corporate Governance policy, the study revealed that insurance companies had Corporate Governance policy as shown by 100% of the respondent who indicated yes. From the findings on whether the insurance companies had board charter the study found that insurance companies had board charter as shown by 100% of the respondent who indicated yes.

Board Composition

In this section the study sought to ascertain the effects of board composition on financial performance of listed insurance firms.

Table 4.5: Rating the effects of board composition on the financial performance of insurance companies

	Not at all	Small extent	Moderate extent	Large extent	Very large extent	Mean	Std Deviation
Board composition affect the financial performance of a firm	4	4	8	12	4	3.2500	1.23828
Board composition affects the way the board communicates with other stakeholders	0	2	4	16	10	4.0625	.85391
The number of non-executive directors on the board affect the performance of the insurance Companies	0	4	10	16	2	3.5000	.81650
Outside directors are better able to challenge and discipline the CEO and management	0	2	2	12	16	4.3125	.87321
Boards composed of directors with good mix of skills, experience and competences can	0	0	2	8	22	4.6250	.61914

take the business to greater heights							
The board should be responsible for selecting top management staff	0	4	10	6	12	3.8125	1.10868
Boards perform better where expatriates sit on them	4	6	12	8	2	2.9375	1.12361
The work of the board includes active monitoring of the activities of management and resolution of internal conflicts.	4	8	6	10	4	3.0625	1.28938
An expatriate CEO has superior knowledge and is likely to improve the performance of an insurance firm	10	8	8	6	0	2.3125	1.13835

From the findings, most of the respondents rated Boards composed of directors with good mix of skills, experience and competences can take the business to greater heights to a very great extent as shown by mean of 4.6250. Respondents rated the following to great extent; outside directors are better able to challenge and discipline the CEO and management as shown by mean of 4.3125, board composition affects the way the board communicates with other stakeholders as shown by mean of 4.0625, the board should be responsible for selecting top management staff as shown by mean of 3.8125 and the number of non-executive directors on the board affect the performance of the insurance Companies as shown by mean of 3.5, those rated as affecting performance to moderate extent were board composition affect the financial performance of a firm as shown by mean 3.25, the work of the board includes active monitoring of the activities of management and resolution of internal conflicts as shown by mean of 3.0625 and boards perform better where expatriates sit on them as shown by mean of 2.9375. On the item that an expatriate CEO has superior knowledge and is likely to improve the performance of an insurance firm, the respondents rated it to small extent as affecting performance as shown by mean 2.3125.

The findings of the study concur with the findings of Dalton et al., (1998) who states that independent directors are important because inside or dependent directors may have no access to external information and resources that are enjoyed by the firm's outside or independent directors. Staikouras et al. (2007) found that board composition does not affect firm performance although its relationship with performance was found to be positive. Adusei (2010) also found that board composition had a positive effect on bank efficiency.

CEO Duality

The study further sought to examine the effect of CEO duality on the financial performance of listed insurance firms.

Table 4.6: Rating the effects of CEO duality on the financial performance of insurance companies

	Not at all	Small extent	Moderate extent	Large extent	Very large extent	Mean	Std Deviation
Roles of Chairman of Board and CEO should be clearly defined and not vested in the same person	2	0	2	4	24	4.5000	1.09545
CEO tenure should be fixed	10	0	8	10	4	2.9375	1.48183
CEO salary should be linked to performance of the firm	4	0	2	10	16	4.0625	1.34009
The monitoring role of board is weaker when the CEO is also Chair	4	0	2	4	22	4.2500	1.39044

On the respondents rating the effects of CEO duality on the performance of insurance firms listed in the NSE, the study found that majority of the respondents rated Roles of Chairman of Board and CEO should be clearly defined and not vested in the same person to a very great extent as shown by mean of 4.50, those rated to great

extent as affecting performance were the monitoring role of board is weaker when the CEO is also Chair as shown by mean of 4.25 and CEO salary should be linked to performance of the firm as shown by mean of 4.0625 , CEO tenure should be fixed was rated to moderate extent as affecting performance . Bhagat and Jefferis, (2002) found that the tenure of a CEO is also an important determinant of the firm's performance.

Leverage

In this section the study sought to examine the effects of leverage on the financial performance of listed insurance firms

Table 4.7: Effects of leverage on the financial performance of insurance companies

	Not at all	Small extent	Moderate extent	Large extent	Very large extent	Mean	Std Deviation
Debts affect the performance of a firm	0	4	6	6	16	4.0625	1.12361
Firms with huge debts may perform better than firms with little or no debts	8	8	8	4	4	2.6250	1.36015
Large creditors such as banks should be represented on the board of directors	12	4	6	6	4	2.5625	1.50416

From the findings on respondents rating, it was revealed that majority of the respondents rated that debts affect the performance of a firm to great extent as shown by mean of 4.0625, those rated as affecting performance to moderate extent were; firms with huge debts may perform better than firms with little or no debts as shown by mean of 2.6250 and large creditors such as banks should be represented on the board of directors as shown by mean of 2.5625. Shleifer and Vishny (1997) argue that debt owed to large creditors such as banks is believed to be a useful tool for reducing the agency problem. Empirical evidence seems to be in support of this assertion. Shleifer and Vishny (1997) in a review article, cite the works of Kaplan and Minton (1994) and Kang and Shivdasani (1995), who found higher incidence of management turnover in Japan in response to poor performance in companies that have a principal banking relationship relative to companies that do not.

Financial Performance

In this section the study sought to determine other factors affecting the financial performance of insurance Companies

Table 4.8: Corporate Governance practices contribution to annual gross profit

	Frequency	Percent
10 to 20%	4	12.5
21 to 30%	10	31.3
41 to 50%	8	25.0
More than 50%	10	31.3
Total	32	100.0

From the finding on the proportion of annual gross profit attributed to Corporate Governance practices, the study found that those who indicated more than 50% and 21 to 30% were shown by 31.3% in each case, 25% of the respondent indicated to 41 to 50% whereas 12.5% of the respondent indicated 10 to 20 %, this is an indication that more than 20% of annual gross profit could be attributed to Corporate Governance practices.

Table 4.9: Corporate Governance practices contribution to overall goals

	Frequency	Percent
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21 to 30%	12	37.5
41 to 50%	6	18.8
More than 50%	14	43.8
Total	32	100.0

From the finding on the proportion of overall goals achieved attributed to Corporate Governance practices, the study found that most of the respondents as shown by 43.5% indicated more than 50%, 37.5% of the respondent indicated 21 to 30 whereas 18.8% of the respondent indicated 41 to 50%, this is an indication that more than 40% of overall goals achieved in the insurance firms could be attributed to Corporate Governance practices.

Table 4.10: Factors affecting the financial performance of insurance Companies

	Not at all	Small extent	Moderate extent	Large extent	Very large extent	Mean	Std Deviation
Size of the board of directors	4	12	12	0	4	2.6250	1.14746
Composition of the board of directors	0	0	4	20	8	3.8625	9.99979
Separation of the role of CEO and Chairman of the board	0	0	6	6	20	4.5625	12.67527
The willingness of investors and lenders to put their money in the firm	2	0	2	10	18	4.3125	1.07819
Large creditors are represented on the board	8	4	12	4	4	3.8125	4.99625
CEOs salary is linked to performance of the firm	4	6	4	10	8	3.3750	1.40831
Checks and balances	0	2	8	4	18	4.1875	1.04682
Business experience and entrepreneurship skills of the CEO	0	0	4	4	24	4.6250	.71880

The study sought to determine the various factors that affect the financial performance of insurance companies. From the findings, majority of the respondents rated the following as affecting financial performance to a very great extent; business experience and entrepreneurship skills of the CEO as shown by mean 4.6250 and separation of the role of CEO and chairman of the board as shown by mean of 4.5625, those rated to large extent as affecting performance are the willingness of investors and lenders to put their money in the firm as shown by mean 4.3125 ,checks and balances as shown by mean of 4.1875, composition of the board of directors as shown by mean of 3.8625 and large creditors are represented on the board as shown by mean of 3.8125. Those rated to moderate extent CEOs salary is linked to performance of the firm as shown by mean of 3.3750 and size of the board of directors as shown by mean 2.6250.

4.3 Descriptive Analysis

Table 4.11: Descriptive data

	Year	Board Size	Board Composition	CEO Duality	Leverage	ROA	ROE
JUB	2007	8	0.50	0	0.78	0.037	0.184
	2008	8	0.38	0	0.84	0.035	0.248
	2009	8	0.38	0	0.84	0.038	0.270
	2010	8	0.25	0	0.82	0.060	0.360
	2011	8	0.38	0	0.82	0.046	0.285

PAN	2007	7	0.57	0	0.76	0.034	1.650
	2008	7	0.71	0	0.81	-0.016	-0.532
	2009	7	0.67	0	0.82	0.018	0.395
	2010	7	0.57	0	0.83	0.055	1.191
	2011	7	0.71	0	0.84	0.068	1.238

Secondary data was collected from the firms' financial statements and report for the years between 2007 and 2011. The study collected data on Return On Assets which was measured as amount of net income returned as a percentage of total assets, Return On Equity which was measured as the amount of net income returned as a percentage of shareholder equity, the various independent variables were Board Size which was measured by the number of directors, Board Composition which was measured as the ratio of outside directors to total number of directors, CEO Duality which was measured as dummy variable 1 if CEO and Chairman are the same person; 0 if CEO and Chairman are different persons and Leverage which was measured as ratio of total liabilities to total assets. In order to test for multicollinearity the researcher conducted a Pearson Product Moment correlation.

4.4 Correlation analysis

Table 4.12: Correlations coefficient

		Board Size	Board Composition	CEO Duality	Leverage	ROA	ROE
Board Size	Pearson Correlation	1	.364	.034	.172	-.073	-.402
	Sig. (2-tailed)		.302	.926	.634	.842	.249
	N	10	10	10	10	10	10
Board Composition	Pearson Correlation	.364	1	.594	.148	.396	.178
	Sig. (2-tailed)	.302		.070	.683	.257	.623
	N	10	10	10	10	10	10
CEO Duality	Pearson Correlation	.034	.594	1	.361	.276	.444
	Sig. (2-tailed)	.926	.070		.305	.440	.198
	N	10	10	10	10	10	10
Leverage	Pearson Correlation	.172	.148	.361	1	.264	.213
	Sig. (2-tailed)	.634	.683	.305		.461	.555
	N	10	10	10	10	10	10
ROA	Pearson Correlation	-.073	.396	.276	.264	1	.610
	Sig. (2-tailed)	.842	.257	.440	.461		.061
	N	10	10	10	10	10	10
ROE	Pearson Correlation	-.402	.178	.444	.213	.610	1
	Sig. (2-tailed)	.249	.623	.198	.555	.061	
	N	10	10	10	10	10	10

On the correlation of the study variables, the researcher conducted a Pearson Product Moment correlation. From the findings on the correlation analysis between Return On Assets and various CG practices, the study found that there was positive correlation coefficient between Return On Assets and Board Composition as shown by correlation factor of 0.396, the study also found a positive correlation between ROA and CEO duality as shown by correlation coefficient of 0.276, association between ROA and Leverage was found to have positive relationship as shown by correlation coefficient of 0.264. However, ROA and Board Size were found to have negative correlation with a correlation coefficient of -0.073.

From the finding on the correlation analysis between ROE and various Corporate Governance practices, the study found that there was a positive correlation coefficient between ROE and Board Composition as shown by correlation factor of 0.178. The study also found a positive correlation between ROE and CEO Duality as shown by correlation coefficient of 0.444. Association between ROE and Leverage was found to have positive relationship as shown by correlation coefficient of 0.213. However, ROE and Board Size were found to have negative correlation with a correlation coefficient of -0.402. This is an indication that there was positive relationship between performance of insurance firms and Separation of role of CEO and Chair, Leverage and Board Composition whereas the performance was found to be negatively correlated to Board Size.

4.5 Regression Analysis

In this study, a multiple regression analysis was conducted to test the influence among predictor variables. The research used Statistical Package for Social Sciences (SPSS V 20) to code, enter and compute the measurements of the multiple regressions

Regression analysis on ROA

Table 4.13: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.969 ^a	.939	.921	.01575

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable. From the findings in the above table, the value of adjusted R squared was 0.921, an indication that there was variation of 92.1% on the financial performance (ROA) of insurance companies due to changes in Board Size, Board Composition, CEO duality and Leverage at 95% confidence interval . This shows that 92.1% changes in financial performance of insurance compnies could be accounted for by Board size, Board Composition, CEO duality and Leverage. R is the correlation coefficient which shows the relationship between the study variables. The findings show that there was a strong positive relationship between the study variables as shown by 0.969.

Table 4.14: ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.004	4	.001	3.869	.015 ^b
	Residual	.001	5	.000		
	Total	.005	9			

From the ANOVA statistics in table above, the processed data, which is the population parameters, had a significance level of 0.015 which shows that the data is ideal for making a conclusion on the population's parameter as the value of significance (p-value) is less than 5%. The calculated was greater than the critical value (2.262 <3.869) an indication that Board size, Board Composition, CEO duality and Leverage were significantly influencing financial performance (ROA) of insurance firm in Kenya .The significance value was less than 0.05 an indication that the model was statistically significant.

Table 4.15: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.455	.231		1.973	.106
	Board Size	-.016	.009	-.444	-1.815	.009
	Board Composition	.182	.050	1.231	3.616	.036
	CEO Duality	.053	.017	1.075	3.159	.025
	Leverage	.204	.240	.230	.850	.028

From the data in the above table the established regression equation was

$$Y = 0.455 - 0.016 X_1 + 0.182 X_2 + 0.053 X_3 + 0.204 X_4$$

From the above regression equation it was revealed that Board Size, Board Composition, CEO duality and Leverage to a constant zero , financial performance of insurance companies would stand at 0.455 , a unit increase in board size would lead to decrease in financial performance (ROA) of insurance companies by a factor of 0.016, unit increase in Board Composition would lead to increase in financial performance of insurance companies by a factor of 0.182 , a unit increase in CEO duality would lead to increase in financial performance of insurance companies by a factor of 0.053 and unit increase in Leverage would lead to increase in financial performance of insurance companies by a factor of 0.204. At 5% level of significance and 95% level of confidence, Board Composition had a 0.036 level of significance; Leverage showed a 0.028 level of significance, CEO duality had a 0.025 level of significance while Board Size showed 0.009 level of significance hence the most significant factor is Board Size. Overall Board Size had the greatest effect on the financial performance of insurance companies, followed by CEO duality, then Leverage and Board Composition had the least effect to the financial performance of insurance companies. All the variables were significant (p<0.05).

Regression on ROE

Table 4.16: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.943 ^a	.889	.879	.46258

Adjusted R squared is coefficient of determination which tells us the variation in the dependent variable due to changes in the independent variable, from the findings in the above table the value of adjusted R squared was 0.879 an indication that there was variation of 87.9% on the financial performance (ROE) of insurance companies due to changes in Board Size, Board Composition, CEO duality and Leverage at 95% confidence interval . This shows that 87.9% changes in financial performance of insurance companies could be accounted for by Board size, Board Composition, CEO duality and Leverage. R is the correlation coefficient which shows the relationship between the study variables, from the findings shown in the table above there was a strong positive relationship between the study variables as shown by 0.943.

Table 4.17: ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.625	4	.656	3.366	.025 ^b
	Residual	1.070	5	.214		
	Total	3.694	9			

From the ANOVA statistics in table above, the processed data, which is the population parameters, had a significance level of 0.025 which shows that the data is ideal for making a conclusion on the population's parameter as the value of significance (p-value) is less than 5%. The calculated was greater than the critical value (2.262 < 3.366) an indication that Board Size, Board Composition, CEO duality and Leverage were significantly influencing financial performance (ROE) of insurance firms in Kenya .The significance value was less than 0.05 an indication that the model was statistically significant.

Table 4.18: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.573	.775		2.889	.034
	Board Size	-.509	.253	-.536	-2.013	.011
	Board Composition	3.103	1.482	.776	2.094	.040
	CEO Duality	1.483	.492	1.118	3.016	.030
	Leverage	1.317	7.063	.640	2.168	.032

From the data in the above table, the established regression equation was

$$Y = 1.573 - 0.509 X_1 + 3.103 X_2 + 1.483 X_3 + 1.317 X_4$$

From the above regression equation, it was revealed that Board Size, Board Composition, CEO duality and Leverage to a constant zero, financial performance (ROE) of insurance companies would stand at 1.573. A unit increase in Board Size would lead to decrease in financial performance of insurance companies by a factor of 0.509, unit increase in Board Composition would lead to increase in financial performance of insurance companies by a factor of 3.103 , a unit increase in CEO duality would lead to increase in financial performance of insurance companies by a factor of 1.483 and unit increase in Leverage would lead to increase in financial performance of insurance companies by a factor of 1.317. At 5% level of significance and 95% level of confidence, Board Composition had a 0.040 level of significance; Leverage showed a 0.032 level of significance, CEO duality had a 0.030 level of significance while Board Size showed 0.011 level of significance hence the most significant factor is Board Size. Overall Board Size had the greatest effect on the financial performance of insurance companies, followed by CEO duality, then Leverage and Board Composition had the least effect to the financial performance of insurance companies. All the variables were significant (p<0.05).

5 Conclusions

From the findings on the effects of Board Size on the financial performance of listed insurance firms, the study found that various aspects of board size affect the financial performance of insurance to a great extent. From the regression analysis, board size was found to negatively affect the financial performance of insurance companies listed at the NSE. On the effects of board composition on the financial performance of listed insurance firms, the study established that various aspects of composition of the board affect the financial performance to a great extent. The study thus concludes that composition of the board positively influence the financial performance of insurance companies listed to a great extent. From the findings on effects of CEO duality on the financial

performance of listed insurance firms, the study found that various aspect of CEO duality positively influenced the financial performance of insurance firm listed to great extent. Thus the study concludes that separation of the role of CEO and Chair positively influenced the financial performance of insurance firms listed to great extent. From the findings on effects of Leverage on the financial performance of listed insurance firms, the study established that leverage of the firm positively influenced the financial performance of insurance firms listed in the NSE. The study thus concludes that leverage of the firm positively influenced the financial performance of insurance firms listed in the NSE.

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