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Corporate Governance in Nepalese Insurance Company

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Abstract

Corporate governance is one of the best systems by which corporate organizations are guided and managed, Nepalese corporations are realizing the need to initiate good corporate governance practices to create enterprise value. The thrust of this paper was to understand the magnitude and direction of transparency, fairness, accountability, and reliability on corporate government issues of Nepalese insurance companies. Accomplished the quantitative paradigm of study as a blend of guided literature reviews. The study has been carried out based on the primary data with a structured questionnaire. All the stakeholders of insurance companies of Nepal are a population of the study and seventy-two respondents from different sectors are taken as a sample with stratified sampling method. Measurement of corporate governance issues measured on a five-point Likert scale method. The primary data is examined by descriptive as well as inferential statistics methods. Findings show that there is a significant impact of transparency, fairness, accountability, and reliability on the corporate governance issues of Nepalese insurance companies. However, transparency of the activities is a major key element in maintaining corporate governance issues.

Keywords: Corporate governance, Transparency, Fairness, Accountability, Reliability

Introduction

Corporate governance is the mechanisms, processes, and relations by which corporations are controlled and directed. It comprises the rules and procedures for making decisions in corporate affairs and the processes through which corporations objectives are set and pursued in the context of the social, regulatory, and market environment. Governance mechanisms consist of, monitoring the policies, practices, and decisions of corporations, their agents, and other stakeholders. Governance structures and principles identify the distribution of rights and responsibilities among different participants in the corporation such as the board of directors, managers, shareholders, creditors, auditors, regulators, and other stakeholders. Corporate governance (CG) is fully based on the four fundamental keystones of transparency, fairness, accountability, and reliability. Corporate governance refers to the set of organizational rules, policies, practices, and defined processes that coordinate and direct the functioning of the organization. Naimah (2017) has elaborated corporate governance as a way of directing, organizing, and controlling the organization based on the pillars of transparency, responsibility, accountability, independence, and fairness.

Corporate governance includes ownership of responsibilities, duties, and rights by different stakeholders for the pay of performance (Cornett, Marcus & Tehranian, 2008). Likewise, it helps to provide means to monitor managers' behavior to ensure corporate accountability and provide for reasonably cost-effective protection of investors and society's interests (Oman, Fries & Buiter, 2003).

Raut (2003) has stated corporate governance is the set of processes, customs, policies, laws, and institutions affecting the way a company is directed, administered controlled, and regulated. It also includes maintaining relationships with its stakeholders at various levels. Poor corporate governance can drive corporations to lose confidence and ineffectiveness, and even invite risks (Macro & Fernandez, 2009). Strong corporate governance might provide for better access to capital and facilitate economic growth and also has extensive organizational and social aspects similarly, good corporate governance ensures that the business environment is fair and transparent, and the organizations are accountable, and good corporate governance might establish a sustainable and optimal business performance and ensures the social impact in the society (Al-Azzam et al., 2015).

The Banking and Financial Institution Act (BAFIA) 2016 is the umbrella act to govern all the banks and financial institutions in Nepal. The main objective of this act is to strengthen the banking and financial system of the country and promote the trust of the general public in the overall banking and financial system of the country. Similarly, this act aims to protect and promote the rights and interests of depositors and provide quality and reliable banking and financial intermediary services to the general public through healthy competition among banks and financial institutions.

Organization for Economic Cooperation and Development (OECD–1999) was incorporated as basic principles of corporate governance which includes protection of shareholder's rights entailing that the shareholders' rights must be maintained at all times ensuring the continuous flow of needed capital. Equitable treatment should be provided to shareholders, all the investors may be minor, and major should be given equitable preference. Clear, consistent accurate, and timely information must be disclosed by corporations during good times or bad times. Board members should be selected diligently and board elections should be free from political interference. Board members should exercise their duties and responsibilities persistently. OECD principles, amended in 2015 ensure the basis for an effective corporate governance framework -- through legalmonitoring procedures, clear division of responsibilities and the board's implied power and integrity to achieve their duties. Transparency on issues regarding finance, ownership, performance, and governance of the company is to be made. Corporate governance is important because it creates a system of rules and practices that determines how a company operates and how it aligns with the interests of all its stakeholders.

Insurance is a way to minimize and provideprotection against those risks that are beyond human control. It is a way to indemnify those unpredictable losses. Thus, insurance is the transfer of the risk of loss from one entity to another in exchange for a premium and can be taken as guaranteed compensation for a probable loss. The main goal of insurance is to protect the life, wealth, and assets of human being insurance is one of the main fields of the service sector, it is part of the financial system, and perform six basic functions such as pooling financial resources, facilitating capital transformation, making efficient pricing mechanism, risk hedging, facilitating trade and commerce, and acting as an agent to deal with the asymmetric information and moral hazard issues to improve the economic well-being.

Characteristics of good governance

Good governance has 8 major characteristics. It is participatory, consensus oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive and follows the rule of law. It assures that corruption is minimized, the views of minorities are taken into account and that the voices of the most vulnerable in society are heard in decision-making. It is also responsive to the present and future needs of society.

Participation

Participation by both men and women is a key cornerstone of good governance. Participation could be either direct or through legitimate intermediate institutions or representatives. It is important to point out that representative democracy does not necessarily mean that the concerns of the most vulnerable in society would be taken into consideration in decision making. Participation needs to be informed and organized. This means freedom of association and expression on the one hand and an organized civil society on the other hand.

Rule of law

Good governance requires fair legal frameworks that are enforced impartially. It also requires full protection of human rights, particularly those of minorities. Impartial enforcement of laws requires an independent judiciary and an impartial and incorruptible police force.

Transparency

Transparency means that decisions taken and their enforcement are done in a manner that follows rules and regulations. It also means that information is freely available and directly accessible to those who will be affected by such decisions and their enforcement. It also means that enough information is provided and that it is provided in easily understandable forms and media.

Responsiveness

Good governance requires that institutions and processes try to serve all stakeholders within a reasonable timeframe.

Consensus oriented

There are several actors and as many view points in a given society. Good governance requires mediation of the different interests in society to reach a broad consensus in society on what is in the best interest of the whole community and how this can be achieved. It also requires a broad and long-term perspective on what is needed for sustainable human development and how to achieve the goals of such development. This can only result from an understanding of the historical, cultural and social contexts of a given society or community.

Equity and inclusiveness

A society's well-being depends on ensuring that all its members feel that they have a stake in it and do not feel excluded from the mainstream of society. This requires all groups, but particularly the most vulnerable, to have opportunities to improve or maintain their well-being.

Effectiveness and efficiency

Good governance means that processes and institutions produce results that meet the needs of society while making the best use of resources at their disposal. The concept of efficiency in the context of good governance also covers the sustainable use of natural resources and the protection of the environment.

Accountability

Accountability is a key requirement of good governance. Not only governmental institutions but also the private sector and civil society organizations must be accountable to the public and to their institutional stakeholders. Who is accountable to whom varies depending on whether decisions or actions taken are internal or external to an organization or institution. In general an organization or an institution is accountable to those who will be affected by its decisions or actions. Accountability cannot be enforced without transparency and the rule of law.

Objectives of the Study

The basic objective of the study is to discuss, examine, and evaluate the relationship between corporate governance and factors affecting corporate governance. This study will be conducted to achieve the following objectives.

To access the relationship among corporate governance, transparency, fairness, accountability, and reliability of insurance companies in Nepal

To examine the impact of determinant factors of governance on corporate governance

Review of Literature

Rujitha (2018) studied regulatory issues in corporate governance and found that the loopholes in the provisions have to be removed. Companies should not be left to escape by taking advantage of the limitations of clause 49 of the listing agreement. The function of the audit committee has been expanded to include oversight of risk management control systems to create an environment for adherence to the practices of good corporate governance.

Aggarwal (2019) examined the impact of corporate governance on the financial performance of the firm in an Indian context through different statistical tests and inferred that the governance rating of a company has a significant positive impact on its financial performance.

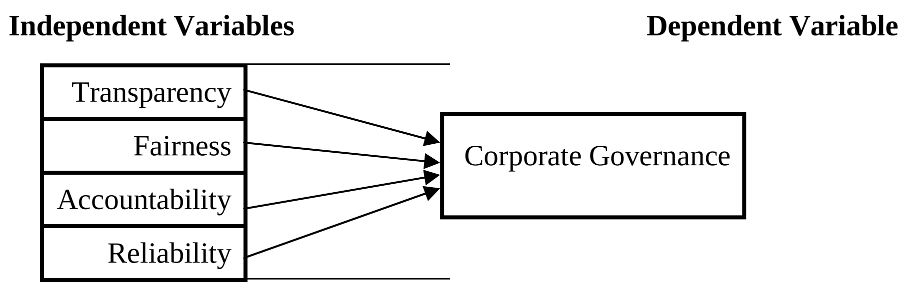
Marco &and Fernandez (2021) definecorporate governance as the set of processes, customs, policies, laws, and institutions affecting how a company is directed, administered, controlled, and regulated. It also includes maintaining relationships with its stakeholders at various levels. Poor corporate governance can drive corporations to lose confidence and ineffectiveness, and even invite risks.

Good corporate governance ensures that the business environment is fair and transparent, and the organizations are accountable Good corporate governance might establish a sustainable and optimal business performance and ensures a social impact in society (Al-Azzam et al., 2022).

According tothe International Association of Insurance Supervisors (2004), corporate governance refers to how boards of directors and senior management oversee the insurers' business. It encompasses how members of the board and senior management are held accountable and responsible for their actions. Corporate governance includes corporate discipline, transparency, independence, accountability, responsibility, fairness, and social responsibility. Timely and accurate disclosure of all material matters regarding the insurer, including the financial situation, performance, ownership, and governance arrangements, is part of a corporate governance framework. Corporate governance also includes compliance with legal and regulatory requirements.

Research Framework and Hypotheses Formulation

The article will be prepared on the following research framework. It shows the relationship between independent variables (i.e., determinant factors of corporate governance) and dependent variables (i.e., corporate governance).



Transparency: Transparency is the process of being open, honest, and straightforward about various company operations. Transparent companies share information relating to performance, internal processes, sourcing, pricing, and business values. The transparency of a process, situation, or statement is its quality of being easily understood or recognized, for example, because there are no secrets connected with it, or because it is expressed clearly.Several benefits can come from transparency for both businesses and consumers. Some benefits are improved customer relationships, increased trust, greater employee engagement, enhanced reputation, and better decision-making. According to Insurance Act 2079, Clause 10, Sections 84 and 85,The Insurer shall prepare separate accounts of its income generated fromthe Insurance Business inside Nepal in theform as specified by the Board and submit them to the Board within six months after the expiry of the fiscal year.The Insurer shall have the accounts and records of its Insurance Business audited by an auditor recognized by the prevailing lawand submit a report thereof to the Board no later than ten months from the date expiration of each fiscal year.

Fairness: Fairness in the workplace refers to an aspect of organizational justice about both process and outcome impartiality. Some of the factors that support fair treatment in the promotion of staff, formation of the board of directors, and equal behavior in the workplace with mutual respect, strong interpersonal relationships, and honest communication.

Accountability: Accountability is an acceptance of responsibility for honest and ethical conduct towards others. In the corporate world, a company's accountability extends to its shareholders, employees, government, and the wider community in which it operates. Corporate accountability takes responsibility for any of its actions. This can be for its financial success and, more importantly, in areas like social responsibility and sustainability. This means that companies are accountable not only to their financial stakeholders but also to others, such as their employees, those in the community, and the general public.

Reliability:

Reliability is a method for measuring the probability that a system, product, or service will perform consistently or not. It is related to consistency in delivering goods and services, excellent customer service, and high-quality products &and services. The insurance company's service should be reliable to refund customers' sufficient claim time, investment, and liabilities.

Corporate Governance: Corporate governance refers to the set of organizational rules, policies, practices, and defined processes that coordinate and direct the functioning of the organization. The corporate governance structure in a given country is determined by many factors viz. the legal and regulatory framework, the corporate environment in the country, and each corporation'sarticles of association. Corporate governance is fully based on the four fundamental keystone softransparency, fairness, accountability, and reliability. Based on the above framework, the following hypotheses can be formulated. Hypothesis 1:There is a significant impact of transparency on corporate governance Hypothesis 2:There is a significant impact of fairness on corporate governance Hypothesis 3: There is a significant impact of accountability on corporate governance Hypothesis 4:There is a significant impact of reliability on corporate governance.

Research Methodology

This paper is descriptive in nature. The study has been carried out based on the primary data with a structured questionnaire. All the stakeholders of insurance companies of Nepal are a population of the study and seventy-two respondents (8 insurance agents, 6 life insurance companies' staff, 6 non-life insurance companies' staff, 20 clients, 25 shareholders of insurance companies, 5 tax administrators, and 2 'A' class auditors) are taken as sample with stratified sampling method. Measurement of corporate governance of Nepalese insurance companies measured on a 5-point Likert scale ranging from 1 (strongly disagree) to 5 (strongly agree). The primary data is examined by descriptive aswellas inferential statisticsmethods. The data is examined from the following regression equation.

$$Y_{(CG)} = \alpha + \beta_1 x\, Trans + \beta_2\, x\, fairn + \beta_3 x\, Accou + \beta_4 x\, Relia + e$$

CG = Corporate governance *Trans = Transparency*

Fairn = Fairness *Accou = Accountability*

Relia = Reliability *α = Constant factor*

e = Error term

Result and Discussion

Descriptive and inferential analysis has been made to understand the facts regarding the factors affecting corporate governance from transparency, fairness, accountability, and reliability during the study period with the help of the following table.

Table 1. Number and percentage of respondents'viewsabout corporate governance issues

	TRANSPARENCY		FAIRNESS		ACCOUNTABILITY		RELIABILITY	
	No.	%	No.	%	No.	%	No.	%
STRONGLY DISAGREE	0	0	0	0	0	0	0	0
DISAGREE	8	11	15	21	0	0	10	14
UNDECIDED	10	14	12	17	13	18	16	22
AGREE	37	51	33	46	38	53	25	35
STRONGLY AGREE	17	24	12	16	21	29	21	29
TOTAL	72	100	72	100	72	100	72	100

(Source: Survey collection and data processing through SPSS)

The majority of the respondents agree with the corporate governance issues followed by insurance companies in Nepal. Seventy-five percent, sixty-two percent, eighty-two percent, and sixty-four percent of respondents agree in favor of transparency,fairness, accountability, and reliability respectively.On average 18% of respondents are undecided, and 12% of respondents disagree about corporate governance issues.

Table 2. Descriptive Statistics

	Transparency	Fairness	Accountability	Reliability
Mean score	3.67	3.44	3.82	3.63
Std. Deviation	0.69	0.66	0.53	0.78

(Source: Survey collection and data processing through SPSS)

The mean value of accountability is higher and fairness is lower among the five variables. The mean value of all the variables is greater than threeonthe five-point Likert scale. It indicates that Nepalese insurance companiesimplement above-average level corporate governance issues.There is a higher deviation in reliability issues and a lower deviation in accountability issues.

Table 3. Reliability, Validity, and Collinearity Test

<table>
<tr><td>Reliability test of research questions</td><td>Validity test of research questions</td><td colspan="3">Collinearity test of independent variables</td></tr>
<tr><td>Cronbach's Alpha</td><td>Correlation coefficients</td><td>Independent variables</td><td>Tolerance</td><td>VIF</td></tr>
<tr><td rowspan="4">0.789 (15 items)</td><td rowspan="2">r = 0.352 to 0.664
Sig. value = 0 to 0.03</td><td>Transparency</td><td>0.827</td><td>1.209</td></tr>
<tr><td>Fairness</td><td>0.882</td><td>1.133</td></tr>
<tr><td rowspan="2">Critical value at 70 (72 – 2) d. f. at 5% level of significance = 0.232</td><td>Accountability</td><td>0.892</td><td>1.121</td></tr>
<tr><td>Reliability</td><td>0.899</td><td>1.113</td></tr>
</table>

(Source: Survey collection and data processing through SPSS)

Cronbach's alpha above 0.7 indicates that the survey or questionnaire isreliable or acceptable for the research (DeVellis, 2005). Cronbach’s alpha of this study is 0.789 which indicates the research questions are good and reliable.

The validity of a research instrument assesses the extent to which the research questions are effective.The significance value of the correlation of the fifteen research questions is in the range of 0 to 0.03 which is less than 0.05. Similarly, the correlation coefficient of all the fifteen research questions is in the range of 0.352 to 0.664 which is greater than the critical table value of 70 (72 – 2) d. f. at 5% level of significance 0.232. It indicates the research questions are valid.

Multicollinearity refers to a state wherein there exists interrelation between two or more independent variables. The presence of multicollinearity in a dataset is problematic because it causes increased variability in the dataset, and it causes instability in the regression model. Multicollinearity is checked by the tolerance and variance inflation factor (VIF) method. Generally, in good research, a VIF below 4 or a tolerance above 0.25is required (CFI Team, 2022). In this research, all the variance inflation factors (VIF) are less than 4 and tolerance values are above 0.25. So, there is no multicollinearity problem in the independent variables.

Table 4. Model Summary

Model	R	R Square	Std. error of the estimate
	0.746a	0.557	0.488

Predictors: (Constant), Reliability, Fairness, Accountability, Transparency

(Source: Survey collection and data processing through SPSS)

The model summary explains the relationship between dependent and independent variables. ‘R-value’ represents the corporate governance is correlated with aggregate independent variables (i.e. transparency, fairness, accountability, and reliability) by 0.746 or 74.6% of Nepalese Insurance Companies. It shows a good relationship amongfactors because the value of R is more than 0.4 (Jain and Chetty). R – Squareshows the total variation for the dependent variable that could be explained by the independent variables. R - square value greater than 0.5 expresses that the model is effective enough to determine the relationship (Jain and Chetty). Corporate governance issueexplains 55.7% by transparency, fairness, accountability, and reliability and the remaining 44.3% is reliant onother factors.

Table 5. Coefficient of Correlation

	Transparency	Fairness	Accountability	Reliability	Corporate Governance
Transparency	1				
Fairness	0.338	1			
Accountability	0.239	0.130	1		
Reliability	0.227	0.115	0.270	1	
Corporate Governance	0.664	0.066	0.363	0.378	1

Correlation is significant at the 0.05 level (2-tailed)

(Source: Survey collection and data processing through SPSS)

Transparency is a high degree positively correlated but accountability, and reliability are low degrees positively correlated with corporate governance. The data shows that the relationship between fairness and corporate governance is low.Respondents indicate that Nepalese insurance companies are low degree fair in internal management issues.

Table 6. Coefficients

Model	Unstandardized Coefficients Beta	Sig p-value	Hypothesis supported or not
(Constant)a	0.345	-	
Transparency	0.657	0.000	Supported
Fairness	-0.212	0.025	Supported
Accountability	0.240	0.040	Supported
Reliability	0.188	0.019	Supported

Dependent Variable: Corporate Governance

Coefficientsat 0.05 level of significance

(Source: Survey and data processing through SPSS)

Hypothesis Analysis

H_1: There is a significant impact of transparency on corporate governance.

The above table shows that the p-value of transparency is 0.000 which is less than the significance level of 0.05. This result directs the positive effect of transparency on corporate governance. The beta coefficient indicates that with a 1% improvement in transparency, corporate governance will also improve by 0.657% and vice-versa.

H_2: There is a significant impact of fairness on corporate governance.

The above table shows that the p-value of fairness is 0.025 which is below the significance level of 0.05. The null hypothesis is rejected and the alternative hypothesis is accepted. This result expresses that there isa positive effect of fairness on corporate governance. The beta coefficient indicates that with a 1% upsurge in fairness, corporate governance will diminution by 0.212%.

H_3: There is a significant impact of accountability on corporate governance.

Thetable no. 6demonstrates that the p-value of accountability is 0.04 which is less than the significance level of 0.05. The alternative hypothesis (H3) is supported and this result leadsto the positive outcome of accountability on corporate governance. The beta coefficient specifies that with a 1% improvement in accountability, corporate governance will also improve by 0.24% and vice-versa.

H_4: There is a significant impact of reliability on corporate governance.

Table no. 6displays that the p-value of reliability is 0.019 which is below the significance level of 0.05. The alternative hypothesis (H4) is supported and this result guides the positive effect of reliability on corporate governance. The beta coefficient indicates that with a 1% rise in reliability, corporate governance will also rise by 0.188%.

Fitting of the regression line:

$(Y_{CG}) = \alpha + \beta_1 x\, Trans + \beta_2\, x\, fairn + \beta_3 x\, Accou + \beta_4 x\, Relia + e$

= 0.345 + 0.657 Transparency - 0.212 Fairness + 0.24 Accountability + 0.188 Reliability

Major Findings

The mean value of all the variables is greater than three (3.44 to 3.82) on the five-point Likert scale. It indicates that Nepalese insurance companies implement above-average level corporate governance issues. The majority (average 70%) of the respondents agree with the corporate governance issues followed by insurance companies in Nepal.

Corporate governance is correlated with aggregate independent variables by 74.6% of Nepalese Insurance Companies. Corporate governance issue explains 55.7% (R – Square) by transparency, fairness, accountability, and reliability. Transparency is a high degree positively correlated but accountability, and reliability are low degrees positively correlated with corporate governance. The data shows that the relationship between fairness and corporate governance is markedly low.

Significant or p-value of predictors transparency, fairness, accountability, and reliability are 0.000, 0.025, 0.04, and 0.019 correspondingly. These values are below 0.05. So, the hypothesis result shows that there is a significant impact of transparency, fairness, accountability, and reliability on the corporate governanceissues of Nepalese insurance companies. Impact or beta coefficient of transparency, fairness, accountability, and reliability on corporate governance are 0.657, -0.212, 0.24, and 0.188 respectively.

Conclusion

Good corporate governance leads to ethical business practices, which leads to financial viability.In the process of good corporate governance,organizations may have to maintain some critical issues. The finding shows that Nepalese insurance companies implement above-average level corporate governance issues.Transparency is a high degree positively correlated but accountability, and reliability are low degrees positively correlated with corporate governance. There is a significant impact of transparency, fairness, accountability, and reliability on the corporate governance issues of Nepalese insurance companies. However, transparency of the activities is a major key element in maintaining corporate governance issues.

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