FACTORS AFFECTING THE EFFECTIVENESS OF FINANCIAL REGULATIONS IN KENYA'S PUBLIC SECTOR: A CASE OF GOVERNMENT MINISTRIES AND STATE OWNED ENTERPRISES

BY

KIMATHI PATRICK NKABU

D61/60063/2010

A RESEARCH PROJECT PRESENTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS OF MASTER OF BUSINESS ADMINISTRATION DEGREE, SCHOOL OF BUSINESS, UNIVERSITY OF NAIROBI.

SEPTEMBER 2014

DECLARATION

STUDENT'S DECLARATION

I declare that this Research Project is my original work and has never been submitted for a degree in any other university or college for examination/academic purposes.

Signature: ……………………… Date: ………………………

Kimathi Patrick Nkabu **Reg: D61/60063/2010**

SUPERVISOR'S DECLARATION

This Research Project has been submitted for examination with my approval as the University Supervisor.

Signature………………………………………..….Date……………………………….

MR. JAMES NG'ANG'A

DEDICATION

I take this opportunity to express my appreciation to my supervisor, Mr. James Ng'ang'a for persevering with me throughout the time of the project and without whose patience and guidance I would not have delivered this project.

ACKNOWLEDGEMENT

I dedicate this paper to my late father, M'Nkabu M'Mwereria whose words of wisdom have taught me innumerable lessons in life, guided me over the years and consistently helped me keep perspective on what is important in life and shown me how to deal with reality. To my mother for single handedly seeing me through high school and college despite the challenges, and my wife and sons for their emotional support during the home stretch and whose encouragement was in the end what made this project possible.

TABLE OF CONTENTS

DECLARATION .... **ii**
DEDICATION .... **iii**
ACKNOWLEDGEMENT .... **iv**
LIST OF TABLES .... **vii**
ACRONYMS/ABBREVIATIONS .... **viii**
ABSTRACT .... **ix**
CHAPTER ONE **1**
INTRODUCTION **1**
1.1 Background of the Study 1
1.1.1 Financial Regulations 3
1.1.2 Factors Affecting Effectiveness of Financial Regulations 4
1.1.3 Government Ministries in Kenya 5
1.1.4 State Owned Enterprises 6
1.2 Statement of the Problem 6
1.3 Objectives of the Study 8
1.4 Significance of the Study 8
CHAPTER TWO **10**
LITERATURE REVIEW **10**
2.1 Introduction 10
2.2 Theoretical Review 10
2.2.1 Keynesian Theory of Macroeconomics 10
2.2.2 Public Interest Theory 12
2.2.3 Private Interest Theory 13
2.2.4 Microprudential Regulation Theory 14
2.3 Factors affecting the Effectiveness of Financial Regulations 15
2.3.1 Political Will 15
2.3.2 Regulatory Framework 16
2.3.3 Resources Availability 18
2.3.4 Legitimacy and Credibility 20
2.4 Empirical Review 22
2.5 Summary of Literature Review 23

CHAPTER THREE **25**
RESEARCH METHODOLOGY **25**
3.1 Introduction 25
3.2 Research Design 25
3.3 Target Population 25
3.4 Data Collection 26
3.5 Validity and Reliability 26
3.6 Data Analysis 27
CHAPTER FOUR **29**
DATA ANALYSIS, PRESENTATION AND INTERPRETATION **29**
4.1 Introduction 29
4.2 Determinants of Effectiveness of Financial Regulations 29
4.3 Political Will 30
4.4 Regulatory Framework 32
4.5 Resources Availability 34
4.6 Legitimacy and Credibility 36
4.7 Regression Analysis 37
CHAPTER FIVE **41**
SUMMARY OF FINDINGS, DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS **41**
5.1 Introduction 41
5.2 Summary of Findings 41
5.3 Discussion 42
5.4 Conclusions 45
5.5 Recommendations 46
5.6 Limitations of the Study 47
5.7 Suggestion for Further Research 47
REFFERENCES **49**
APPENDICES **52**
Appendix 1: Research Questionnaire 52
Appendix II: State Owned Enterprises in Kenya 56

LIST OF TABLES

Table 4. 1: Effectiveness of the implementation of various financial regulations in government ministries in Kenya and state owned enterprises 30

Table 4. 2: Extent that commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector..31

Table 4. 3: Extent of agreement with the following statements of financial regulations in Kenya's public sector...32

Table 4. 4: Extent to which regulatory framework affect effectiveness of financial regulations in Kenya's public sector..33

Table 4. 5: Extent that various factors of regulatory framework affect effectiveness of financial regulations in Kenya's public sector..33

Table 4. 6: Extent that resources availability affect effectiveness of financial regulations in Kenya's public sector..34

Table 4. 7: Extent that various factors of resources affect the effectiveness of financial regulations in Kenya's public sector..35

Table 4. 8: Extent that legitimacy and credibility affect effectiveness of financial regulations in Kenya's public sector..36

Table 4. 9: Model Summary 37

Table 4.10: Summary of One-Way ANOVA results 38

Table 4. 11: Regression coefficients of the relationship between implementation of financial regulations and the four predictive variables 39

ACRONYMS/ABBREVIATIONS

APRA - Australian Prudential Regulation Authority

ASIC - Australian Securities and Investments Commission

CEBS - Committee of European Banking Supervisors

CEIOPS - Committee of European Insurance and Occupational Pensions Supervisors

CESR - Committee of European Securities Regulators

GAAP - Generally Accepted Accounting Principles

GoB - Government of Botswana

GoK - Government of Kenya

IOSCO - International Organization of Securities Commissions

MS - Micro Soft

MTEF - Medium Term Expenditure Framework

PCA - Prompt Corrective Action

PFM - Public Finance Management

SPSS - Statistical Package for the Social Sciences

ABSTRACT

Governments are fundamentally different from business enterprises because they have different purposes, processes of generating revenues, stakeholders, budgetary obligations and propensity for longevity. These differences require separate accounting and financial reporting standards in order to meet the needs of the stakeholders who assess the government's ability for accountability and socio-economic development. The study sought to determine the factors for effective implementation of financial regulations in government ministries in Kenya. This study was conducted through the use of a descriptive design. The target population of the study were the heads in the finance and accounting departments in the 18 ministries and the 47 state owned enterprises in Kenya that are non-commercial. The study used questionnaires for primary data collection. The questionnaires were administered through drop and pick-later method to the sampled population. Data collected was purely quantitative and it was analyzed by descriptive analysis. The descriptive statistical tools such as SPSS V 21.0 and MS Excel helped the researcher to describe the data and determine the extent used. Tables and charts were used to summarize responses for further analysis and facilitate comparison. In addition, the researcher conducted a multiple regression analysis so as to determine the effects of each of the independent variables. The study revealed that commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector. The study also revealed that availability of finances for the regulator, sufficiency of capacity to deal with the regulated entities, poor remuneration of employees and employees being biased towards the regulated with interests of future employment affect financial regulations in Kenya's public sector. The study concluded that political interference, poor relations between the regulating agencies and the regulated entities, state infringing on regulatory jurisdiction and appointment of non-autonomous individuals affect the effectiveness of financial regulations in Kenya's public sector. The study recommends that the government should ensure the establishment of strong regulatory agencies that are independent. The study further recommends that all the employees in the regulatory agencies should be remunerated well. This study focused on the factors for effective implementation of financial regulations in government ministries in Kenya. Another study could be done to establish the challenges faced in the implementation of financial regulations.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Governments are fundamentally different from business enterprises because they have different purposes, processes of generating revenues, stakeholders, budgetary obligations and propensity for longevity. These differences require separate accounting and financial reporting standards in order to meet the needs of the stakeholders who assess the government's ability for accountability and socio-economic development. Kenya's Public Sector Reforms (GoK, 2003) have among others focused on the need to have a transparent, reliable and efficient budgeting and financial regulatory framework that would guarantee provision of effective and efficient services to the Kenyan public.

The Constitution of Kenya provides various statutes and subsidiary legislation such as financial regulations and procedures to provide a detailed legal framework that governs collection of government revenues, allocation and utilization. As noted in the Government Financial Regulations and Procedures (Ministry of Finance, 1989) collection of government revenues and their subsequent expenditures must follow the laid down procedures and should focus on creating value to the public. The introduction of the Medium Term Expenditure Framework (MTEF) was aimed at tying budget votes to specific activities mapped for implementation on a three year rolling budget operationalized on a half yearly basis as a way of enhancing tracking of the said budget votes. This has enhanced clarity of roles and responsibilities in the budgeting process. The enactment of the Government Financial Management Act of 2004 and the subsequent release of the Treasury Circular No. 13/2005 of 1st August

2005 provided guidelines for implementing the budget by public officers. The Circular in part notes ‘Accounting Officers should as part of the efforts aimed at strengthening internal financial controls strengthen their audit committees, and promptly take action on the audit reports which should be submitted to the Treasury at least quarterly’ (Ministry of Finance Circular, 2005). This circular is essentially aimed at implementing financial regulations so as to realize the intended budgetary and financial objectives of government.

The establishment of budget implementation committees in all Ministries which is one of the essential provisions of the Treasury Circular was meant to execute the provisions of the Government Financial Management Act of 2004 which among others include; conducting regular reviews of the ministerial cash plan and communicate the same to Treasury, review utilization of departmental expenditures and utilization of cash limits, review and approve the submission of expenditure returns for the ministry and, review the commitments of the ministry including pending bills and recommend necessary solutions. The Establishment of the Office of the Controller of Budget (Kenya Constitution, 2010) and the subsequent Circular No. 3 of 2012 requires all ministries to submit budget implementation reports for every financial year for assessment by the Office. This is meant to promote accountability on the part of utilization of budget votes by public entities for the benefit of the Kenyan public.

In August 2012, Parliament enacted the Public Finance Management Act, 2012 to provide for the effective management of public finances by the national and county governments; the oversight responsibility of Parliament and county assemblies; the different responsibilities of government entities and other bodies, and for connected purposes (PFM Act, 2012). The Act has taken care of the envisaged changes in the

new governance structure of Kenya’s public sector and it’s expected to meet the anticipated thresholds of measuring Financial Performance in the public sector namely Efficiency, Economy and Effectiveness.

1.1.1 Financial Regulations

Financial regulation is a form of regulation or supervision, which subjects financial institutions to certain requirements, restrictions and guidelines, aiming to maintain the integrity of the financial system. This may be handled by either a government or non-government organization. Financial regulation has also influenced the structure of various sectors, by decreasing borrowing costs and increasing the variety of financial products available. Financial regulators ensure that listed companies and market participants comply with various regulations under the trading acts. The trading acts demands that listed companies publish regular financial reports, ad hoc notifications or directors' dealings (Samarajiva, 2000). Whereas market participants are required to publish major shareholder notifications. The objective of monitoring compliance by listed companies with their disclosure requirements is to ensure that investors have access to essential and adequate information for making an informed assessment of listed companies and their securities.

In most cases, financial regulatory authorities regulate all financial activities. But in some cases, there are specific authorities to regulate each sector of the finance industry, mainly banking, securities, insurance and pensions markets, but in some cases also commodities, futures, forwards, etc. For example, in Australia, the Australian Prudential Regulation Authority (APRA) supervises banks and insurers, while the Australian Securities and Investments Commission (ASIC) is responsible for enforcing financial services and corporations laws (Baldwin and Cave, 2003).

Sometimes more than one institution regulates and supervises the banking market, normally because, apart from regulatory authorities, central banks also regulate the banking industry. For example, in the USA banking is regulated by a lot of regulators, such as the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, the National Credit Union Administration, the Office of Thrift Supervision, as well as regulators at the state level. In addition, there are also associations of financial regulatory authorities. In the European Union, there are the Committee of European Securities Regulators (CESR), the Committee of European Banking Supervisors (CEBS) and the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), which are Level-3 committees of the EU in the Lamfalussy process. And, at a world level, we have the International Organization of Securities Commissions (IOSCO), the International Association of Insurance Supervisors, the Basel Committee on Banking Supervision, the Joint Forum, and the Financial Stability Board. The structure of financial regulation has changed significantly in the past two decades, as the legal and geographic boundaries between markets in banking, securities, and insurance have become increasingly "blurred" and globalized (Bitran & Serra, 2001).

1.1.2 Factors Affecting Effectiveness of Financial Regulations

Financial regulations can be greatly affected by political will in a country. This refers to the commitment by the relevant ministry to creating a strong, efficient capable regulatory agency. Successful reform requires a strong regulator who is able to balance the demands of different interest groups. Abdala (2000) states that, a state may come up with weak regulatory agencies to serve the interests of a few. The regulatory framework may also contribute to the effectiveness of financial regulations. Naidu (2010) posits that in Malaysia independent agencies exist though

they are under the influence of ministers in certain ministries thereby comprising the autonomy of the agencies.

The availability of resources and the legitimacy and credibility of regulating agencies also affect the effectiveness of financial regulations. An agency that is perceived as under-resourced will find it difficult to assert its autonomy and will also struggle to gain legitimacy (Sappington and Stiglitz, 1987). This has an effect on the effectiveness of the undertakings of the agency. Joskow (1998) states that giving parties the option to take matters up for judicial review can also enhance the credibility of the regulatory framework. This however should not lead to a second layer of regulation, with the judiciary becoming unreasonably involved in technical, sector-specific matters. If this happens then the effectiveness of the financial regulation agencies is compromised.

1.1.3 Government Ministries in Kenya

A ministry is the basic functional unit of government which translates government policies into action. It is headed by a Cabinet Secretary who is in charge of policy formulation and the Principal Secretary who is the Accounting Officer in charge of all administrative core functions and activities of the ministry. Every ministry has service or support departments such as human resource, finance, procurement, administration, audit and technical departments in charge of the core functions of the ministry. Appointments of cabinet secretaries and Principal Secretaries are vested in the president subject to approval by parliament. The Cabinet Secretary must not be member of Parliament. All the other employees are civil servants employed by the Public Service Commission.

A ministry discharges its mandate as prescribed by the President in line with the Executive Order No.2 of 2013 on the Reorganization of Government, and is allocated a budget from the National Treasury every financial year.

1.1.4 State Owned Enterprises

A state owned enterprise is a legal entity that is created by the government in order to partake in commercial activities on the government's behalf. A state-owned enterprise (SOE) can be either wholly or partially owned by a government and is typically earmarked to participate in commercial activities. The defining characteristics of SOEs are that they have a distinct legal form and they are established to operate in commercial affairs. While they may also have public policy objectives, SOEs should be differentiated from other forms of government agencies or state entities established to pursue purely non-financial objectives. State owned enterprises are common with natural monopolies and infrastructure such as railways and telecommunications, strategic goods and services (mail, weapons), natural resources and energy, politically sensitive business, broadcasting, demerit goods (alcohol) and merit goods (healthcare).

1.2 Statement of the Problem

Financial regulation effectiveness is dependent on authorities which regulate all financial activities. But in some cases, there are specific authorities to regulate each sector including banking, securities, insurance and pensions markets, but in some cases also commodities, futures, forwards. The structure of financial regulation has changed significantly in the past two decades, as the legal and geographic boundaries between markets in banking, securities, and insurance have become increasingly "blurred" and globalized (Bitran and Serra, 2001).

Governments worldwide are faced with the challenge of meeting the expectations of the citizenry. A number of studies have been conducted on Financial Regulations and public sector budgeting (World Bank, 2007; European Commission, 2008 and GoB, 2004). The Research on government accounting procedures in the United Kingdom (European Commission,2008) found out that government Finance Officers and Accountants recorded transactions and prepared statements in accordance with the Generally Accepted Accounting Principles (GAAP). A world Bank research on the effectiveness of public sector accounting in Sri Lanka (2007) found out that while financial regulations existed, they did not have the force of the law and therefore were not always complied with and thus the oversight of government accounting outcomes were lacking.

In Africa, emerging economies such as Botswana and Ghana have embraced Financial Regulations as the hall mark of modern day public budgeting and financial management. The effective implementation of Financial Regulations in Botswana led to a reduction in government spending by close to US$ 4 Million (GoB, 2004). In Ghana, implementation of Financial Regulations reduced donor dependence in budgeting by 9.2% (World Bank, 2007).

Financial regulations were adopted in Kenya in 1989 (Ministry of Finance, 1989) to provide a framework of the administration, budgeting and utilization of government finances. The regulations were based on the Constitution of Kenya, the Exchequer and Audit Act and the Paymaster-General's Act and Regulations which all contained relevant provisions regarding the control and management of government finances. The enactment of the Government Financial Management Act of 2004 and the PFM Act, 2012 augmented the aforementioned efforts towards realization of an effective

and efficient Public Financial Management System and supportive of public service delivery and socioeconomic development.

Notwithstanding the above achievements, the existence of scandals involving misappropriation and wastage of public resources on one hand and on the other the inability by government ministries to timely meet their budgetary obligations raises serious issues on the adequacy and effectiveness of financial regulations. Moreover, a research by Mugwe (2011) on the challenges of budgeting in government ministries recommended the need to reform the financial regulations for success in budgeting. Other related studies have been conducted by Wabwoba (2012) on the impact of oil price regulation on the financial performance of national oil corporation of Kenya and Okwachi (2009) who conducted an evaluation of the effectiveness of state regulation of the insurance industry in Kenya. To the best of the researcher knowledge the government, as part of the public sector reforms, has put in place a framework for budgeting and budgetary controls which, in line with the new constitution ought to function as required. This study therefore seeks to investigate the effectiveness of financial regulations in government ministries.

1.3 Objectives of the Study

The objective of this study was to determine the factors for effective implementation of financial regulations in government ministries in Kenya.

1.4 Significance of the Study

This study will be of importance to the government employees especially those working in the Finance department as the information from this study will be useful in their quest to discharge their functions efficiently. The Office of the Controller of Budget will find information out of this study beneficial especially in the process of

restructuring and aligning operations to conform the requirements of the devolved system of government.

To the scholars especially academicians engaged in research in finance, investment and public budgeting the study will be useful as it will provide more information on financial regulations specifically in the Kenya’s public sector.

Consultants in the area of finance and investment will find this report expedient in their quest to provide appropriate, feasible and informed advice to both public and private sector organizations and players.

Researchers and students particularly those pursuing postgraduate studies in finance, Economics and Accounting will find this study useful in their quest to understand budgeting and budget control in the public sector. The study will also form a basis for further researchers who may want to do studies in the similar field. The recommendations for future studies that will be proposed by the study will also be useful to researchers who will have an easier time identifying the areas they can explore further. The findings of the research will also provide rich literature for future studies.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter covers literature review of the main variables of the study. The sections included in this chapter include the theoretical review, determinants of effectiveness of financial regulations, financial regulations, organizational performance and effects of financial management practices on performance. In addition a summary have also been provided at the end of the chapter.

2.2 Theoretical Review

2.2.1 Keynesian Theory of Macroeconomics

The theory was developed by Keynes (1930) to significantly depart from the classical assumption of perfectly flexible prices and develop models based on the assumption that there are constraints on the flexibility of some prices. A central argument in the Keynesian theory of macroeconomics is that the government could counter a recession through fiscal policy by either reducing taxes to spur consumer or investment spending, or directly increasing its own spending, even if this could result in deficit spending. This implies in a period of deep recession, the government can, for example, engage in deficit spending by providing funds to financial institutions if it is deemed that such action could spur lending, increase private spending and investment and thus increase aggregate demand in the economy. The downside of government intervention through injection of funds into the financial system is that not only does it compromise the independence of the financial institutions but also could result in politically motivated forbearance, thereby posing challenges to

effective regulatory governance. For example, in the United States, government injection of capital to rescue financial institutions has led to government ownership of substantial shares of many of these institutions at least in the short run. As stated earlier, the lack of independence of the Japanese financial supervision function within the ministry of finance is widely believed to have contributed to financial sector weaknesses. Although there was probably little direct pressure on the ministry of finance to exercise forbearance, the system lacked transparency and was known for widespread implicit government guarantees of banking sector liability (Udaibir, Quintyn & Taylor, 2002).

The argument here is that while effective intervention is necessary for the proper functioning of the free market system, such policies should be implemented with caution as ill thought out intervention could be ineffective, and result in higher than socially efficient cost of such intervention. In the process of using state intervention to complement market forces in achieving high economic activity, many western countries engaged in massive deficit financing, with potential adverse impact on the economy. Large fiscal deficits result in higher real rates of interest or larger stocks of international debts, with consequent negative effects on investment expenditures, capital stocks, and future per capita national income levels. Larger fiscal deficits also tend to lead, frequently, to higher rates of inflation in the long run and undermine the stability of a nation's economic system if the deficit is financed by selling bonds to the central bank, i.e., by printing money (Mishra, 2001). This could, in turn, lead to massive decreases in government revenues and mounting budget deficits, and force western governments to reduce public expenditure on social programs and regulatory monitoring.

Historical evidence suggests that mounting deficits and the arrival of stagflation all over the western capitalist world in the 1970s threw the Keynesian economics into disarray and the welfare state lost its ideological as well as material basis (Kethineni, 1991). The stagflation in the 1970s was overcome at very high cost. While the world economy expanded at about 5.1% during the period 1960-1973, it grew at much slower 3.2% during the period 1973-1989, due mainly to worldwide squeeze on profits and restrain on investments, jobs and growth caused by tight energy supplies (Sachs, 2008).

With the discredit of Keynesianism, laissez-faire economics gained a new impetus and re-metamorphosed into neo-classical monetarism with the call for cut in government spending on social services, privatization, new public management, liberalized financial markets, tax concession to the rich, decreasing the role of the state and public expenditure, and the free play of the market forces in the economy (Brown, 1984).

2.2.2 Public Interest Theory

Public interest theory is an economic theory first developed by Pigou (1932) that holds that regulation is supplied in response to the demand of the public for the correction of inefficient or inequitable market practices. Regulation is a mechanism to insist that public purposes be respected by businesses and other nongovernmental institutions in their operations (Lehne, 2006). Our understanding of the role of regulation in the relationship between government and private institutions is dominated by two basic theories – the public interest theory and the private interest theory (Mitnick, 1980). According to the public interest theory, regulation is instituted for the protection and benefit of the public at large or some large subclass of the public. Most analysis based on this view present regulation as a response to market

failure (Bernstein, 1955) by, for example, seeking to achieve the benefits of market place competition for consumers and society in situations in which competition does not occur.

The theory of market failure is concerned with establishing the conditions under which competitive market allocations will be inefficient. The theory suggests that under certain conditions, the production and distribution of a good or service through a competitive market in which all the relevant agents are pursuing their own self-interest will result in an allocation of that good or service that is socially inefficient. This implies in the situation where companies have power to fix prices or limit competition, consumers lack the information needed to make the best product choices, market exchanges affect people who are not party to the transaction, the structure of an industry creates barriers to entry (Lehne, 2006), or market allocations result in inequities in the distribution of income and wealth, a market failure has occurred and government can put in place appropriate institutional and regulatory framework to correct it.

2.2.3 Private Interest Theory

The theory is based on the work of Stigler (1971) who states that regulation is one means by which state power can be exercised to the benefit of specific groups. Regulation is supplied by utility-maximizing politicians and regulators in response to the demand for regulation by interest groups. The private interest perspective of regulation views it as a means to pursue private interest, and nothing more than an effort to use government authority to redistribute income from one group to another. For example, a company with less than optimal profit can invest in lobbying effort to secure beneficial regulatory action (Owen & Braeutigam, 1978), and members of

Congress can benefit by transforming regulation into pork barrel politics (Posner, 1969). The need for good regulatory governance as part of a broader effort to prevent or better manage financial crisis and ensure economic stability stems from the fact that a financial system is only as strong as its governing practices, the financial soundness of its institutions, and the efficiency of its market infrastructure. Just as market participants in the financial system should establish good governance practices to gain the confidence of their customers and to help ensure a stable economy, regulators have fiduciary responsibility to follow sound governance practices in their operations to maintain credibility and moral authority in their oversight responsibilities. This requires the establishment of appropriate economic and regulatory policies to prevent political and institutional interference in the regulatory supervision of financial institutions, as well as to prevent regulatory forbearance, regulatory arbitrage and regulatory capture.

2.2.4 Microprudential Regulation Theory

At the risk of caricature, traditional microprudential regulation of institutions can be said to be based on the following logic. Insititutions finance themselves with government-insured deposits. While deposit insurance has the valuable effect of preventing institutions runs (Diamond and Dybvig, 1983), it also creates taxpayer exposure and an accompanying moral hazard problem for institutions managers. The goal of capital regulation is to force institutions to internalize the losses on their assets, thereby protecting the deposit insurance fund and mitigating moral hazard. Thus if the probability of the deposit insurer bearing losses is reduced to a low enough level, microprudential regulation is by definition doing its job.

If the regulator can check up on the bank at discrete intervals, say once a quarter. Suppose the volatility of the institutions assets is such that with probability 99.5%,

they do not decline in value by more than 6% in a quarter. Then if the goal of policy is to reduce the probability of institutions failure and the associated losses to the deposit insurance fund to 0.5%, this can be accomplished by requiring the institutions to hold capital equal to 6% of its assets as a cushion against losses. Note that in this setting, the exact form of the capital cushion is not important it can be common equity, but it can equally well be preferred stock, or subordinated debt, as long as these instruments are not explicitly or implicitly insured, i.e., as long as they will in fact bear losses in a bad state of the world. An important element of capital regulation as it is implemented in practice is the principle of prompt corrective action (PCA), which requires that institutions take immediate steps to restore its capital ratio in the wake of losses.

2.3 Factors affecting the Effectiveness of Financial Regulations

2.3.1 Political Will

One of the most important determinants of the success of a regulatory agency is political will. This is the commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency. Successful reform requires a strong regulator who is able to balance the demands of different interest groups. Yet the state may find it to be in its own interest to create a weak regulatory agency, allowing it to favour the interests of certain interest groups, sometimes at the expense of the public interest (Abdala, 2000).

In a study of the financial regulation in Ghana it was clearly demonstrated how a lack of political will can undermine the capabilities of a regulatory agency. Ghana set out to liberalize telecommunications with the hopes of achieving greater competition in the market, efficiency in service provision, private sector led expansion and improvement of services nationwide and the establishment of a modern, transparent

regulatory framework (Republic of Ghana, Investor Presentation, 2009). The need for an effective regulator was acknowledged very early in the process of regulatory reform, signaling a good start to the process. Yet some government may fail to act according to its own stated objectives by delaying the appointment of the Board that governs the regulatory agency.

2.3.2 Regulatory Framework

After liberalization the development of the policy framework is left in the hands of the Ministry whilst implementation becomes the function of the regulatory agency. This normally involves the regulatory agency developing and monitoring guidelines or regulations that will govern the industry, in pursuit of the goals articulated under the policy framework. The relationship between the Ministry and the agency should thus be supportive as the two are governed by a common vision. International best practice calls for the creation of an independent regulatory institution, with its own funding. Various reasons are given for this insistence on independence. The government usually retains a stake in the incumbent thus a conflict of interest may arise if the state then has to regulate its own competitors. Others have argued that regulation by departments will be less likely to be questioned and scrutinized due to its political weight (Ramanadham, 2009).

A high level of political interference in regulatory decisions can also encourage industry to participate in rent seeking activities (Bitran and Serra, 2001). Yet, it should be noted that the lack of formal, legal independence does not necessarily mean that the agency does not have autonomy. A semiautonomous agency within a government can be effective. Similarly, the independence of a regulatory authority does not guarantee its effectiveness. A regulatory agency should have an arm's length relationship with government yet such autonomy should not give way to capture by

industry or to a lack of accountability to the public (Bitran and Serra, 2001). The regulatory framework agency is an important one because any conflict between the two can be exploited by the regulated and can generally be costly. A problematic relationship often arises where the government tries to keep a firm hand over the market by creating a weak regulatory agency. This does not bode well for the development of the sector.

Malaysia has not escaped the difficulties surrounding the relationship between the state and the regulator. In an article on regulation in general, Naidu (2010) argues that although independent agencies exist in Malaysia, the relevant Minister still has 'considerable' influence over the policies of privatised suppliers. Some authors thus paint a disturbing picture of the level of political interference in the Malaysian case. It is not clear if it is a case of excessive interference by a state infringing on regulatory jurisdiction or co-ordination by a strong state. In Ghana, there have also been reports of political interference in purely regulatory matters, such as ministerial intervention in the resolution of interconnection disputes between Ghana Telecom and the second network operator (Atubra and Frempong, 2001). The relationship between the state and the regulatory agency also depends on the type of people that are appointed at senior management and Board levels. A successful agency will require the appointment of autonomous individuals with high integrity.

Regulatory institutions need to enjoy a certain degree of autonomy. Yet, this autonomy should not come at the price of less co-ordination between the policymaker and the regulator or even conflict. The regulated should never be given an opportunity to play the two entities against each other. The line between policymaking and regulation is often blurred. Given the issues that developing countries face, such as

the promotion of universal access, there is no simple way of deciding where this line should be (Naidu, 2010).

2.3.3 Resources Availability

Resources are needed to enable the regulator to carry out its mandate, including the capacity to monitor industry performance and to enforce regulations. The regulator also needs to have sufficient capacity to deal with information asymmetries and strategic behaviour by the regulated firms. Financial resources are less likely to pose an acute challenge as funds are normally raised through license fees. It is with human resources that most countries, especially developing countries, struggle. Regulatory functions often require the exercise of expert judgement, often based on incomplete and shifting information. The issue of resources is closely linked to the legitimacy and independence of the regulator (from the state and the regulated firms). An agency that is perceived as under-resourced will find it difficult to assert its autonomy and will also struggle to gain legitimacy (Sappington and Stiglitz, 1987).

There is a tendency for agencies lacking analytical capabilities to rely on outside expertise through outsourcing. This strategy can alleviate constraints in the short run but does not nurture in-house skills and experience. Implementing a more forward-looking human resources strategy does have its challenges, most notably that of staff turnover. The wages the regulator offers may create incentives for staff to seek employment in the industry. This will erode the negotiating capacity of the regulatory agency. Agency staff may also attempt to increase their chances of future employment in the industry by being biased towards its interests whilst still in the employ of the regulator. This could lead to regulatory capture by the industry. A partial remedy to this could be a 'cooling off' period where former employees of the regulator are

barred from taking up employment in the regulated industry immediately after leaving the agency (Bitran and Serra,

2001).

Malaysia has more resources than Ghana and has had more experience with regulation. Yet competition regulation is new in the country and capacity strains are felt in this area. There are enough skills to deal with the technical (in an engineering sense) aspects of telecommunications and the country has moved from being a recipient to a donor of assistance in that area. The relative weakness of the country in economic regulation should be seen in light of the fact that economic regulation was not a regulatory priority in the past. The important lesson here is that a human resources strategy has to exist to make sure that regulatory priorities can be skillfully executed. Competition is an important goal in South Africa thus the appropriate skills for economic regulation have to be developed if the goals of the policy framework are to be realized (Republic of South Africa, 2005).

Effective regulation requires the regulator to have access to information about the industry and the firm that is being regulated, including information that will enable it to set the correct prices and the correct interconnection fees. There will always be information assymetries as the regulated firm will necessarily have more information about its cost conditions, market conditions and its actions than the regulator. The firm's cost-reducing efforts will not be perfectly known or observable to the regulator. The seriousness of the information problem is related to how fast the environment changes and how fast the regulator learns (Sappington and Stiglitz, 1987).

A study on Chile found that the efficiency gains of privatization were not passed on to consumers in the form of lower prices. This was attributed to the relative weakness of

the regulator i.e limited information and technical capacity in relation to the industry. The regulator was unable to gather precise cost data from companies who were not only better resourced, but had also cultivated political alliances (Bitran and Serra, 2001). The legislation that governs the regulator should give it the necessary legal backing to request information. The scarcity of regulatory resources is one of the main reasons that regulatory institutions take time to strengthen in developing countries. Various approaches can be taken to meet this challenge. The tasks that require analytical capabilities that the agency does not currently possess can be outsourced. This strategy is however, a short term one and if possible, should be executed in a way that skills are transferred to agency staff. The consultants that are used should also be carefully selected and monitored, especially concerning their relationship to the industry. The working conditions of the agency are unlikely to match those of the regulated firms yet opportunities for training and development will go some way towards attracting skilled employees. Finally, the information problem may be addressed by shifting the burden of proof towards regulated firms in processes such as rate reviews.

2.3.4 Legitimacy and Credibility

Agencies should be seen as dispensing non-arbitrary decision-making and due process (Samarajiva, 2000). This is especially important since regulation will inevitably involve a lot of discretionary judgement, as it is more than just applying formulas. More often than not, the regulated firms start appealing to the executive or the legislature on regulatory issues. This could have the effect of undermining the regulatory agency's autonomy and ability to perform core functions.

Legitimacy is often associated with expertise yet a lot of judgment is involved in a situation of imperfect knowledge. Malaysian regulation has tended to emphasize

technical expertise until recently. Yet there is more to legitimacy than being able to dispense with technocratic decision-making. A regulatory agency will gain legitimacy if it has qualified staff and encourages relevant, on-going training. The training efforts of the regulator should be publicized and communicated to the public and industry as a confidence-building exercise. The regulatory agency will also gain legitimacy by being open. All procedures should be open and inclusive. The legislation that governs the regulatory regime or the guidelines that the agency develops should be explicit on the procedures that are to be taken to resolve disputes, to file complaints etc. In a study on Argentina, Abdala (2000) highlights weaknesses such as consumers being unable to file complaints to the regulator due to lack of procedures. There were no internal procedures to make regulatory decisions and there was no auditing or verification on fulfillment of regulatory targets set in licenses.

Due process is very important in a quasi-judicial process such as regulation. The framework will be successful if it pays attention to issues such as equality, fairness, consistency of treatment, participation by the public, consumers and other affected parties. This may slow decision-making, especially where disputes arise over the appropriate mode of participation (Baldwin and Cave, 1999).Yet, the quality of decisions will benefit if the principles of due process are observed.

Giving parties the option to take matters up for judicial review can also enhance the credibility of the regulatory framework. This however should not lead to a second layer of regulation, with the judiciary becoming unreasonably involved in technical, sector-specific matters (Joskow, 1998). Finally, legitimacy is also gained if the agency is seen to act in the public interest. An important point to bear in mind is that legal independence without legitimacy means nothing. Parties will try to bypass the regulatory agency if it does not earn legitimacy.

2.4 Empirical Review

Eisner (1991) examined the impact of regulatory effectiveness on policy change. He found that regulating agencies perceived as being effective were better able to shape their policy environments. Other contributors argued that regulating agencies that stakeholder perceive as being effective are better able to use their knowledge to positively influence the regulatory process (Bendor et al. 1987).

Carpenter (2001) also examined the relationship between regulatory effectiveness and policy innovation. He found that regulating agencies perceived as being effective by Congress are better able to take risks in dealing with emerging problems. Carpenter's research has ramifications for financial services regulators who frequently have been criticized for not taking enough risks in order to understand emerging regulatory problems.

Lewis (2005) found that regulating agencies generally are motivated more by concerns of reputational risk than by partisan political control. Furthermore, regulating agencies that are motivated by autonomy generally tend to be more effective than other units because the former are able to use their discretion to increase effectiveness. This differs from Hoffmann and Cassell (2010), who analyzed the impact that regulating agency mission has on organizational direction. The latter analyses find that mission relates to recruitment and regulating agency focus. Such factors allow agencies to be more effective in dealing with their constituencies.

The research on government accounting procedures in the United Kingdom (European Commission, 2008) found out that government Finance Officers and Accountants recorded transactions and prepared statements in accordance with the Generally Accepted Accounting Principles (GAAP). A world Bank research on the effectiveness

of public sector accounting in Sri Lanka (2007) found out that while financial regulations existed, they did not have the force of the law and therefore were not always complied with and thus the oversight of government accounting outcomes were lacking.

Balin (2008) presents, analyzes and critiques the effectiveness of the regulatory requirements established by the Basel I and II Accords. He criticizes the fact that the Basel Accords exclude emerging markets from capital obligations and that they do not meet specific needs for emerging markets. Companies in emerging markets are thus put into a difficult position. On the one hand, the adoption of Basel I and II requirements will likely improve banks' status as transparent and controlled institutions. This could help the companies to increase their deposit base, but also lead to excessive risk-taking. On the other hand, being reluctant to adopt the Basel requirements would deteriorate companies' international recognition.

Bawn (2010) and Ferejohn and Shipan (1990) who examined the effect of political control on autonomy are important to this study. Both found that elected officials perceived regulating agencies as being effective are granted greater autonomy from Congress. Scholars such as Carpenter (2000), Kaufman (1976), and Lewis (2006) analyzed the termination of regulating agencies and found that generally agencies that are perceived as being effective were less likely to be terminated.

2.5 Summary of Literature Review

Keynesian theory of macroeconomics argues that the government could counter a recession through fiscal policy by either reducing taxes to spur consumer or investment spending, or directly increasing its own spending, even if this could result in deficit spending. The downside of government intervention through injection of

funds into the financial system is that not only does it compromise the independence of the financial institutions but also could result in politically motivated forbearance, thereby posing challenges to effective regulatory governance. The study will therefore seek to find out the intervention measures that the government has taken in regulating the public sector in Kenya.

Several scholars have done studies in effectiveness of financial regulations (Eisner, 1991; Rainey and Steinbauer, 1999; Carpenter, 2001). Most of these studies are done in other countries whose financial regulations are different from that of Kenya. This study therefore seeks to fill this gap by focusing on the effectiveness of financial regulations in Kenya's public sector.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The chapter describes the research design and methodology that was used to guide the study under the following sub-headings: the research design, target population, sample and sampling design, data collection instruments, data collection procedures and data analysis procedures.

3.2 Research Design

This study was conducted through the use of a descriptive design. A descriptive study attempts to describe or define a subject, often by creating a profile of a group of problems, people, or events, through the collection of data and tabulation of the frequencies on research variables or their interaction as indicated by Cooper and Schindler (2003). Descriptive research portrays an accurate profile of persons, events, or situations (Kothari, 2000). The choice of the descriptive survey research design was made based on the fact that in the study, the research was interested on the state of affairs already existing in the field and no variable was manipulated.

3.3 Target Population

The target population of the study were the heads in the finance and accounting departments in the 18 ministries and the 47 state owned enterprises in Kenya that are nonprofit making specifically 19 in the education and education services, 15 in health and welfare and six development authorities (Appendix II). Mugenda and Mugenda, (2003) explain that the target population should have some observable characteristics, to which the researcher intends to generalize the results of the study. So the study took a census approach.

3.4 Data Collection

This study used questionnaires for primary data collection. The questionnaires were used because they were held to be straightforward and less time consuming for both the researcher and the participants (Owens, 2002). The questionnaires had a number of sub-sections that were sub-divided based on the major research questions except the first sub-section (section A) that was meant to capture the background information of the participants. Other sections covered the main areas of the study. Questionnaires are appropriate for studies since they collect information that is not directly observable as they inquire about feelings, motivations, attitudes, accomplishments as well as experiences of individuals. The questionnaires were administered through drop and pick-later method to the sampled population.

3.5 Validity and Reliability

To ascertain the validity of questionnaire, a pilot test was carried out. This was done by administering the questionnaire onto the pilot group. The content validity of the research instrument was evaluated through the actual administration of the pilot group. In validating the instruments, 20 staffs were selected. Furthermore, to enhance the validity of the instruments, two university lecturers who are experts in the area of financial management were asked to appraise the instruments

Reliability of the questionnaire was evaluated through administration of the said instrument to the pilot group. Reliability was measured through Cronbach's Alpha which measures the internal consistency. The alpha value ranges between 0 and 1 with reliability increasing with the increase in value. Nunnally (1978) stated that reliability of a research instrument can be indicated at a minimal Alpha value of 0.6.

3.6 Data Analysis

Before processing the responses, the completed questionnaire was edited for completeness and consistency. The data was then coded to enable the responses to be grouped into various categories. Data collected was purely quantitative and it was analyzed by descriptive analysis. The descriptive statistical tools such as SPSS V 21.0 and MS Excel helped the researcher to describe the data and determine the extent used. Tables and charts were used to summarize responses for further analysis and facilitate comparison. In addition, the researcher conducted a multiple regression analysis so as to determine the effects of each of the independent variables. The regression equation was: $\mathbf{Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon}$

Where: Y = Effectiveness of financial regulations

β_0 = Constant

X_1 = Political Will (balance of demands of interest groups, strength of regulatory agency and process of appointments)

X_2 = Regulatory Framework (Political interference, appointment of no-autonomous individuals in regulatory agency and relations between the agency and the regulated firms)

X_3 = Resources availability (capacity to deal with the regulated firms, Availability of finances, payment of the regulator agency employees, Access to information about the industry and firm being regulated)

X_4 = Legitimacy and credibility (staff training, regulatory procedures and public's interest)

ε = Error Term

The coefficient of determination (R^2) was used to measure the extent to which the variation in efficiency was explained by the variations in its determinants. F-statistic was also computed at 95% confidence level to test whether there is any significant relationship between financial regulations and its determinants. This analysis was done using SPSS (V 21) software and the findings presented in form of a tables and graphs to aid in the analysis and ease with which the inferential statistics was drawn.

CHAPTER FOUR

DATA ANALYSIS, PRESENTATION AND INTERPRETATION

4.1 Introduction

This chapter discusses the interpretation and presentation of the findings. This chapter presents analysis of the data on the factors for effective implementation of financial regulations in government ministries in Kenya. The chapter also provides the major findings and results of the study.

4.1.1 Response Rate

The study targeted a sample size of 65 respondents from which 58 filled in and returned the questionnaires making a response rate of 88.5%. This response rate was good and representative and conforms to Mugenda and Mugenda (1999) stipulation that a response rate of 50% is adequate for analysis and reporting; a rate of 60% is good and a response rate of 70% and over is excellent.

4.2 Determinants of Effectiveness of Financial Regulations

The study sought to determine how effective is the implementation of various financial regulations in government ministries in Kenya and state owned enterprises. The results are as indicated in Table 4.1.

Table 4. 1: Effectiveness of the implementation of various financial regulations in government ministries and state owned enterprises in Kenya

	Mean	Standard Deviation
Auditor general (corporations) regulations	4.215	1.01102
Procurement and tendering procedures regulations	4.109	1.03468
Budgets and budgetary controls regulations	4.063	0.71522
Stores and supplies regulations	3.346	1.15172
Miscellaneous accounting matters regulations	3.281	0.67955
Internal management audit regulations	3.227	0.65893
Pension benefits regulations	3.194	0.67951
Accounts of state corporations regulations	3.008	1.37445

Regarding the effectiveness of the implementation of various financial regulations in government ministries in Kenya and state owned enterprises the respondents indicated that auditor general (corporations) regulations, procurement and tendering procedures regulations and budgets and budgetary controls regulations were moderately effective as shown by a mean score of 4.215, 4.109 and 4.063 respectively. The respondents also indicated that stores and supplies regulations, miscellaneous accounting matters regulations, internal management audit regulations, pension benefits regulations and accounts of state corporations regulations were effective as shown by a mean score of 3.346, 3.281, 3.227, 3.194 and 3.008 respectively.

4.3 Political Will

The study sought to establish extent that commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector. The results are as shown in Table 4.2.

Table 4. 2: Extent that commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector

	Frequency	Percentage
Very great extent	12	20.0
Great extent	38	65.2
Moderate extent	7	12.2
Little extent	2	2.6
Not at all	0	0.0
Total	**58**	**100.0**

According to the findings in Table 4.2, majority of the respondents (65.2%) indicated that commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector to a great extent, 20.0% to a very great extent, 12.2% to a moderate extent and 2.6% to a little extent.

The study also sought to find out the extent the respondents agree with various statements of financial regulations in Kenya's public sector. The results are as indicated in Table 4.3.

Table 4. 3: Extent of agreement with the following statements of financial regulations in Kenya's public sector

	Mean	Standard Deviation
Government create weak regulatory agency that favor certain interest groups	4.403	0.67554
A regulating agency should balance the demands of different interest groups	4.194	0.67955
The government delays the appointment of boards that govern the regulatory agency	3.537	1.03468

Regarding the extent of agreement with various statements of financial regulations in Kenya's public sector the respondents agreed to a great extent that government create weak regulatory agency that favor certain interest groups, a regulating agency should balance the demands of different interest groups and the government delays the appointment of boards that govern the regulatory agency as shown by a mean score of 4.403, 4.194 and 3.5373 respectively.

4.4 Regulatory Framework

The study sought to find out the extent to which regulatory framework affect effectiveness of financial regulations in Kenya's public sector. The results are as indicated in Table 4.4.

Table 4. 4: Extent to which regulatory framework affect effectiveness of financial regulations in Kenya's public sector

	Frequency	Percentage
Very great extent	6	10.4
Great extent	44	76.5
Moderate extent	5	7.8
Little extent	3	5.2
Not at all	0	0.0
Total	**58**	**100.0**

According to the findings, the majority of the respondents (76.5%) indicated that the regulatory framework affect effectiveness of financial regulations in Kenya's public sector to a great extent, 10.4% to a very great extent, 7.8% to a moderate extent and 5.2% to a little extent.

The study further sought to determine the how various factors of regulatory framework affect effectiveness of financial regulations in Kenya's public sector. The results are as indicated in Table 4.5.

Table 4. 5: Extent that various factors of regulatory framework affect effectiveness of financial regulations in Kenya's public sector

	Mean	Standard Deviation
Political interference	4.373	0.65893
Poor relations between the agency and the regulated firms.	4.057	0.71522
State infringing on regulatory jurisdiction	3.955	1.17335
Appointment of non-autonomous individuals in the regulatory agency	3.914	1.01102

According to the findings in Table 4.5, the respondents indicated that political interference, poor relations between the agency and the regulated firms, state

infringing on regulatory jurisdiction and appointment of non-autonomous individuals in the regulatory agency affect the effectiveness of financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.373, 4.057, 3.955 and 3.914 respectively.

4.5 Resources Availability

The study sought to find out to what extent that resources availability affect effectiveness of financial regulations in Kenya's public sector. The results are as indicated in Table 4.6.

Table 4. 6: Extent that resources availability affect effectiveness of financial regulations in Kenya's public sector

	Frequency	Percentage
Very great extent	2	3.5
Great extent	47	81.7
Moderate extent	8	13.0
Little extent	1	1.7
Not at all	0	0.0
Total	**58**	**100.0**

According to the findings in Table 4.6, majority of the respondents (81.7%) indicate that resources availability affect effectiveness of financial regulations in Kenya's public sector to a great extent, 13.0% to a moderate extent, 3.5% to a great extent and 1.7% to a little extent.

The study also sought to find out the extent that various factors of the resources availability affect the effectiveness of financial regulations in Kenya's public sector. The results are as indicated in Table 4.7.

Table 4. 7: Extent that various factors of resources affect the effectiveness of financial regulations in Kenya's public sector

	Mean	**Standard Deviation**
Availability of finances for the regulator	4.403	0.67554
Sufficiency of capacity to deal with the regulated firms	4.194	1.32929
Poor payment of the regulator agency employees	3.572	0.67955
Employees being biased towards the regulated with interests of future employment	3.528	1.15172
Access to information about the industry and firm being regulated	3.059	1.03468

The results in Table 4.7 indicate that availability of finances for the regulator, sufficiency of capacity to deal with the regulated firms, poor payment of the regulator agency employees and employees being biased towards the regulated with interests of future employment affect financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.403, 4.194, 3.572 and 3.528 respectively. The respondents also indicated that access to information about the industry and firm being regulated affect financial regulations in Kenya's public sector to a moderate extent as shown by a mean score of 3.059.

4.6 Legitimacy and Credibility

The study sought to determine the extent that legitimacy and credibility affect effectiveness of financial regulations in Kenya's public sector. The findings are as presented in Table 4.8.

Table 4. 8: Extent that legitimacy and credibility affect effectiveness of financial regulations in Kenya's public sector

	Frequency	Percentage
Very great extent	2	4.3
Great extent	45	77.4
Moderate extent	9	15.7
Little extent	2	2.6
Not at all	0	0.0
Total	**58**	**100.0**

From the study findings portrayed in table 4.6, most of the respondents (77.4%) indicated that legitimacy and credibility affect effectiveness of financial regulations in Kenya's public sector to a great extent, 15.7% to a moderate extent, 4.3% to a very great extent and 2.6% to a little extent.

The study also wanted to determine the extent of agreement with various statements on legitimacy and credibility. The findings are as presented in Table 4.9.

	Mean	Standard Deviation
Poor payment of the regulator agency employees	4.492	0.82555
Availability of staff and encouragement of training of the regulator staff	4.237	0.63552
Being open in all the procedures of the regulatory agency	4.126	0.68253
Regulator should act on the public's interest	3.831	0.74327
Regulatory firms undermine regulatory agency autonomy by appealing to the judiciary or the executive	3.671	0.78441

From the findings, the respondents agreed that poor payment of the regulator agency employees, availability of staff and encouragement of training of the regulator staff, being open in all the procedures of the regulatory agency, regulator should act on the public's interest and regulatory firms undermine regulatory agency autonomy by appealing to the judiciary or the executive affect the effectiveness of financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.492, 4.237, 4.126, 3.831 and 3.671 respectively.

4.7 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 21.0) to code, enter and compute the measurements of the multiple regressions

Table 4. 9: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.8662	0.7503	0.6902	0.1325

R-Squared is a commonly used statistic to evaluate model fit. R-square is 1 minus the ratio of residual variability. The adjusted $R^{2,}$ also called the coefficient of multiple determinations, is the percent of the variance in the dependent explained uniquely or jointly by the independent variables. 69.02% of the changes in the implementation of financial regulations in government ministries in Kenya could be attributed to the combined effect of the predictor variables.

Table 4.10: **Summary of One-Way ANOVA results**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	9.223	4	2.306	3.334	0.015
	Residual	42.876	53	0.692		
	Total	52.099	57			

The probability value of 0.015 indicates that the regression relationship was highly significant in predicting how political will, regulatory framework, resources availability and legitimacy and credibility affect the implementation of financial regulations in government ministries in Kenya. The F calculated at 5% level of significance was 3.334 since F calculated is greater than the F critical (value = 2.55), this shows that the overall model was significant.

Table 4. 11: Regression coefficients of the relationship between implementation of financial regulations and the four predictive variables

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	1.053	0.217		2.889	5.31E-03
	Political Will	0.599	0.196	0.234	4.255	7.19E-05
	Regulatory Framework	0.682	0.149	0.613	5.309	1.58E-06
	Resources availability	0.763	0.091	0.138	3.989	1.78E-04
	Legitimacy and credibility	0.701	0.181	0.149	3.210	2.10E-03

As per the SPSS generated table above, the equation ($\mathbf{Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \varepsilon}$) becomes:

$Y = 1.053 + 0.599X_1 + 0.682X_2 + 0.763X_3 + 0.701X_4$

The regression equation above has established that taking all factors into account (political will, regulatory framework, resources availability and legitimacy and credibility) constant at zero the implementation of financial regulations in government ministries in Kenya will be 1.053. The findings presented also show that taking all other independent variables at zero, a unit increase in the political will would lead to a 0.599 increase in the scores of the implementation of financial regulations in government ministries in Kenya and a unit increase in the scores of regulatory framework would lead to a 0.682 increase in the scores of the implementation of financial regulations in government ministries in Kenya. Further, the findings shows that a unit increases in the scores of resources availability would lead to a 0.763 increase in the scores of the implementation of financial regulations in government

ministries in Kenya. The study also found that a unit increase in the scores of legitimacy and credibility would lead to a 0.701 increase in the scores of the implementation of financial regulations in government ministries in Kenya.

Overall, resources availability had the greatest effect on the implementation of financial regulations in government ministries in Kenya, followed by legitimacy and credibility, then regulatory framework while political will had the least effect to the implementation of financial regulations in government ministries in Kenya. All the variables were significant ($p<0.05$).

CHAPTER FIVE

SUMMARY OF FINDINGS, DISCUSSIONS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presented the discussion of key data findings, conclusion drawn from the findings highlighted and recommendation made there-to. The conclusions and recommendations drawn were focused on addressing the objective of the study.

5.2 Summary of Findings

The study sought to determine the factors for effective implementation of financial regulations in government ministries in Kenya.

5.2.1 Political Will

The study revealed that commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector to a great extent. The study also found out that to a great extent government create weak regulatory agency that favor certain interest groups, a regulating agency should balance the demands of different interest groups and the government delays the appointment of boards that govern the regulatory agency as shown by a mean score of 4.403, 4.194 and 3.5373 respectively.

5.2.2 Regulatory Framework

The study revealed that the regulatory framework affect effectiveness of financial regulations in Kenya's public sector to a great extent. The study also revealed that political interference, poor relations between the agency and the regulated firms, state infringing on regulatory jurisdiction and appointment of non-autonomous individuals

in the regulatory agency affect the effectiveness of financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.373, 4.057, 3.955 and 3.914 respectively.

5.2.3 Resources Availability

The study found out that resources availability affect effectiveness of financial regulations in Kenya's public sector to a great extent. The study also revealed that availability of finances for the regulator, sufficiency of capacity to deal with the regulated firms, poor payment of the regulator agency employees and employees being biased towards the regulated with interests of future employment affect financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.403, 4.194, 3.572 and 3.528 respectively.

5.2.4 Legitimacy and Credibility

The study established that that legitimacy and credibility affect effectiveness of financial regulations in Kenya's public sector to a great extent. The study also established that poor payment of the regulator agency employees, availability of staff and encouragement of training of the regulator staff, being open in all the procedures of the regulatory agency, regulator should act on the public's interest and regulatory firms undermine regulatory agency autonomy by appealing to the judiciary or the executive affect the effectiveness of financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.492, 4.237, 4.126, 3.831 and 3.671 respectively.

5.3 Discussion

This section sought to discuss the factors that affect the effective implementation of financial regulations in government ministries in Kenya.

5.3.1 Political Will

The study revealed that commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector to a great extent. This is in line with Abdala (2000) who posits that one of the most important determinants of the success of a regulatory agency is political will. He continues to state that political will is the commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency. Successful reform requires a strong regulator who is able to balance the demands of different interest groups. The study also found out that to a great extent government create weak regulatory agency that favor certain interest groups, a regulating agency should balance the demands of different interest groups and the government delays the appointment of boards that govern the regulatory agency as shown by a mean score of 4.403, 4.194 and 3.5373 respectively. This is in agreement with (Abdalla, 2000) who argues that the state may find it to be in its own interest to create a weak regulatory agency, allowing it to favour the interests of certain interest groups, sometimes at the expense of the public interest.

5.3.2 Regulatory Framework

The study revealed that the regulatory framework affect effectiveness of financial regulations in Kenya's public sector to a great extent. The study also revealed that political interference, poor relations between the agency and the regulated firms, state infringing on regulatory jurisdiction and appointment of non-autonomous individuals in the regulatory agency affect the effectiveness of financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.373, 4.057, 3.955 and 3.914 respectively. This is in line with Bitran and Serra (2001) who state that the regulatory framework agency is important because any conflict between the agency

and the government can be exploited by the regulated and can generally be costly. A problematic relationship often arises where the government tries to keep a firm hand over the market by creating a weak regulatory agency. This does not bode well for the development of the sector. Naidu (2010) argues that regulatory institutions need to enjoy a certain degree of autonomy. Yet, this autonomy should not come at the price of less co-ordination between the policymaker and the regulator or even conflict. The regulated should never be given an opportunity to play the two entities against each other.

5.3.3 Resources Availability

The study found out that resources availability affect effectiveness of financial regulations in Kenya's public sector to a great extent. This correlates with Sappington and Stiglitz (1987) who argue that an agency that is under-resourced will find it difficult to assert its autonomy and will also struggle to gain legitimacy thereby being less effective. The study also revealed that availability of finances for the regulator, sufficiency of capacity to deal with the regulated firms, poor payment of the regulator agency employees and employees being biased towards the regulated with interests of future employment affect financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.403, 4.194, 3.572 and 3.528 respectively. The findings also are also in line with Bitran and Serra (2001) the wages the regulator offers may create incentives for staff to seek employment in the industry. This will erode the negotiating capacity of the regulatory agency. Agency staff may also attempt to increase their chances of future employment in the industry by being biased towards its interests whilst still in the employ of the regulator. This could lead to regulatory capture by the industry. A partial remedy to this could be a 'cooling off'

period where former employees of the regulator are barred from taking up employment in the regulated industry immediately after leaving the agency.

5.3.4 Legitimacy and Credibility

The study established that that legitimacy and credibility affect effectiveness of financial regulations in Kenya's public sector to a great extent. The study also established that poor payment of the regulator agency employees, availability of staff and encouragement of training of the regulator staff, being open in all the procedures of the regulatory agency, regulator should act on the public's interest and regulatory firms undermine regulatory agency autonomy by appealing to the judiciary or the executive affect the effectiveness of financial regulations in Kenya's public sector to a great extent as shown by a mean score of 4.492, 4.237, 4.126, 3.831 and 3.671 respectively. This is in line with Samarajiva (2000) who posit that agencies should be seen as dispensing non-arbitrary decision-making and due process. This is important since regulation will inevitably involve a lot of discretionary judgement, as it is more than just applying formulas. Abdala (2000) states that, regulatory agency gains legitimacy if it has qualified staff and encourages relevant, on-going training. The training efforts of the regulator should be publicized and communicated to the public and industry as a confidence-building exercise.

5.4 Conclusions

The study concludes that the government create weak regulatory agency that favor certain interest groups; a regulating agency should balance the demands of different interest groups and the government delays the appointment of boards that govern the regulatory agency which affects the effectiveness of financial regulations Kenya's public sector.

The study also concludes that political interference, poor relations between the agency and the regulated firms, state infringing on regulatory jurisdiction and appointment of non-autonomous individuals in the regulatory agency affect the effectiveness of financial regulations in Kenya's public sector.

The study further concludes that availability of finances for the regulator, sufficiency of capacity to deal with the regulated firms, poor payment of the regulator agency employees and employees being biased towards the regulated with interests of future employment affect financial regulations in Kenya's public sector.

Finally the study concludes that poor payment of the regulator agency employees; availability of staff and encouragement of training of the regulator staff; being open in all the procedures of the regulatory agency and regulatory firms undermine regulatory agency autonomy by appealing to the judiciary or the executive which affects the effectiveness of financial regulations in Kenya's public sector.

5.5 Recommendations

The study recommends that the government should ensure the establishment of strong regulatory agencies that are independent. This will ensure that the agencies do not favor the interests of certain groups and it can fully balance the demands of all the stakeholders. This will ensure great accountability and effectiveness of financial regulations in Kenya's public sector.

The study also recommends that the government should ensure that the regulatory agencies are kept free of political interference. This will ensure that the agencies will be able to deliver on their mandate. However, the government should ensure that there is an independent body mandated to oversight the agencies as too much autonomy may bring some ineffectiveness in the agencies.

The study further recommends that all the employees in the regulatory agencies should be paid well. Employees get motivated by better pay and hence work more efficiently to safeguard their job. With the same, corruption cases go down since the workers' demands are satisfied hence better effectiveness of financial regulations.

The study finally recommends that the regulatory agencies should ensure openness and transparency in all the procedures. This can be achieved by following the provisions of the law and other relevant authorities thereby leading to greater effectiveness of financial regulations.

5.6 Limitations of the Study

The management staffs targeted in this study were very busy and therefore they required a lot of time in order to fill in the questionnaires. The challenge was overcome by giving the respondents the questionnaires at the right time. Inadequate financial resources affected the results of the study.

Getting accurate information from the respondents was one of the major challenges since some of the workers were threatened that the information may be used against them by the management in the terms of performance hence insecurity of their jobs. The challenge was minimized by assuring the respondents of confidentiality of the information they gave and also indicating that the information was to be used for academic purposes only. The researcher carried an introduction letter from the university to authenticate this.

5.7 Suggestion for Further Research

This study focused on the factors for effective implementation of financial regulations in government ministries in Kenya. Another study should be done to establish the challenges faced in the implementation of financial regulations.

This study put emphasis on the regulating agencies; another study should be conducted with an emphasis on the regulated institutions to find out whether the study will yield the same information.

REFFERENCES

Abdala, M. (2000). Institutional roots of post-privatisation regulatory outcomes, *Telecommunications Policy,*24, 645-668

Atubra, W. H. and Frempong, G. K. (2001). Liberalisation of telecoms: the Ghanaian experience',*Telecommunications Policy,* 25, 197-210

Baldwin, R. and Cave, M. (2003). *Understanding Regulation: Theory, Strategy and Practise*. Oxford: Oxford University Press.

Balin, B. J. (2008). *Basel I, Basel II, and Emerging Markets: A Nontechnical Analysis.* 3, 41-56

Bawn, K. (2010). Political Control Versus Expertise: Congressional Choices About Administrative Procedures. *American Political Science Review* , 89(1), 62-73.

Bendor, J. and Taylor, S. et al. (1987). Stacking the Deck: Bureaucratic Missions and Policy Design. *American Political Science* Review, 81(3), 873–896.

Bitran and Serra (2001). Regulation of privatised utilities: the Chilean experience' *World Development,* 26 (6), 945-962.

Carpenter, D. P. (2000). Stochastic Prediction and Estimation of Nonlinear Political Durations: An Application to the Lifetime of Bureaus. Political Complexity: Nonlinear Models of Politics. University of Michigan Press.

Carpenter, D. P. (2001). The Forging of Bureaucratic Autonomy: Reputations, Networks, and Policy Innovation in Executive Agencies, 1862-1928. Princeton, NJ: Princeton University Press.

Eisner, M. A. (1991). Antitrust and the Triumph of Economics: Institutions, Expertise, and Policy Change. Chapel Hill, NC: University of North Carolina Press.

Ferejohn, J. and Shipan, C. R. (1990). Congressional Influence on Bureaucracy. *Journal of Law, Economics, and Organization* **6**, 1-43.

Government of Kenya (1989). *Government Financial Regulations and Procedures. Ministry of Finance.* Nairobi: Government Printer.

Government of Kenya (2003). *Economic recovery strategy for wealth and employment creation 2003 – 2007.* Ministry of Planning and National Development. Retrieved from http://siteresources.worldbank.org/KENYAEXTN/Resources/ERS.pdf Accessed on July, 2014.

Government of Kenya (2013). *The public finance (administration and management) regulations.* Nairobi: Government Printer.

Government of Kenya. (2010). *The Constitution of Kenya*. Nairobi: Government Printer.

Government of Kenya. (2012). *The Public Finance Management Act*. Ministry of Finance. Nairobi: Government Printer.

Hoffmann, S. M., and Cassell, M. K. (2010). *Mission Expansion in the Federal Home Loan Bank System*. SUNY Press.

Joskow, P. (1998). *Regulatory Priorities for Reforming Infrastructure in Developing Countries*, Paper prepared for the Annual World Bank Conference on Development Economics.

Kaufman, H. (1976). Are Government Organizations Immortal? . washington, D.C.: Brookings Institution.

Lewis, C. W. (2006). In pursuit of the public interest. *Public Administration Review***.** 66, 694-701.

Lewis, D. E. (2005). Measurement and public service motivation: New insights, old questions. *International Public Management Journal*, *13*(1), 46-55.

Ministry of Finance. *Treasury Circular No.13/2005*

Naidu, G. (2010). Infrastructure' in Jomo, K. S. (ed) *Privatizing Malaysia: Rents, Rhetoric*, *Realities*, Oxford: Westview Press.

Okwachi, E. S. (2009). An Evaluation Of The Effectiveness Of State Regulation Of The Insurance Industry In Kenya. Unpublished MBA project, University of Nairobi.

Rainey, H. G. and Steinbauer, P. (1999). Galloping elephants: Developing elements of a theory of effective government organizations. *Journal of public administration research and theory*, *9*(1), 1-32.

Ramanadham, V.V. (2009). *Privatisation and after: monitoring and regulation*. London: Routledge.

Republic of Ghana (2009). *Investor Presentation: Telecommunications in Ghana*.

Republic of South Africa (2005). *Treasury Regulations for Departments, trading entities, constitutional institutions and public entities*. National Treasury, Retrieved from http://www.treasury.gov.za/legislation/pfma/regulations/gazette_23246.pdf Accessed on July, 2014

Samarajiva, R. (2000). Establishing the legitimacy of new regulatory agencies, *Telecommunications Policy,* 24, 183-187

Sappington, D. E. and Stiglitz, J. E. (1987). Privatization, information and incentives. *Journal of policy analysis and management*, *6*(4), 567-585.

The World Bank. (2007). *Sri Lanka. Public Sector Accounting and Auditing*. Retrieved from http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/SOUTHASIAEXT/0,,contentMDK:21555665~pagePK:146736~piPK:146830~theSitePK:223547,00.html Accessed on July, 2014.

Wabwoba A. (2012). The impact of oil price regulation on the financial performance of national oil corporation of Kenya. Unpublished MBA project, University of Nairobi.

APPENDICES

Appendix 1: Research Questionnaire

Determinants of effectiveness of financial regulations

1. How effective is the implementation of the following financial regulations in government ministries in Kenya and state owned enterprises?

	Very effective	Moderately effective	Effective	Slightly effective	Ineffective
Internal management audit regulations					
Budgets and budgetary controls regulations					
Procurement and tendering procedures regulations					
Stores and supplies regulations					
Pension benefits regulations					
Accounts of state corporations regulations					
Auditor general (corporations) regulations					
Miscellaneous accounting matters regulations					

SECTION A: Political Will

2. To what extent does commitment by the relevant Ministry to creating a strong, efficient capable regulatory agency affect effectiveness of financial regulations in Kenya's public sector?

   Very great extent [ ] Great extent [ ]

Moderate extent [ ] Little extent [ ] Not at all [ ]

3. To what extent do you agree with the following statements of financial regulations in Kenya's public sector?

	Very great extent	**Great extent**	**Moderate extent**	**Little extent**	**Not at all**
A regulating agency should balance the demands of different interest groups					
Government create weak regulatory agency that favor certain interest groups.					
The government delays the appointment of boards that govern the regulatory agency.					

SECTION B: Regulatory Framework

4. To what extent does regulatory framework affect effectiveness of financial regulations in Kenya's public sector?

   Very great extent [ ] Great extent [ ]

   Moderate extent [ ] Little extent [ ] Not at all [ ]

5. To what extent do the following factors of regulatory framework affect effectiveness of financial regulations in Kenya's public sector?

	Very great extent	**Great extent**	**Moderate extent**	**Little extent**	**Not at all**
Political interference					
State infringing on regulatory jurisdiction					
Appointment of non-autonomous individuals in the regulatory agency.					
Poor relations between the agency and the regulated firms.					

SECTION C: Resources Availability

6. To what extent does resources availability affect effectiveness of financial regulations in Kenya's public sector?

   Very great extent [ ] Great extent [ ]

   Moderate extent [ ] Little extent [ ] Not at all [ ]

7. To what extent do the following affect the effectiveness of financial regulations in Kenya's public sector?

	Very great extent	**Great extent**	**Moderate extent**	**Little extent**	**Not at all**
Sufficiency of capacity to deal with the regulated firms					
Availability of finances for the regulator					
Poor payment of the regulator agency employees					
Employees being biased towards the regulated with interests of future employment					
Access to information about the industry and firm being regulated					

SECTION D: Legitimacy and Credibility

8. To what extent does legitimacy and credibility affect effectiveness of financial regulations in Kenya's public sector?

   Very great extent [ ] Great extent [ ]

   Moderate extent [ ] Little extent [ ] Not at all [ ]

9. To what extent do you agree with the following statements on legitimacy and credibility of the regulator?

	Very great	**Great**	**Moderate**	**Little**	**Not at**

	extent	extent	extent	extent	all
Regulatory firms undermine regulatory agency autonomy by appealing to the judiciary or the executive					
Availability of staff and encouragement of training of the regulator staff					
Poor payment of the regulator agency employees					
Being open in all the procedures of the regulatory agency					
Regulator should act on the public's interest					

THANK YOU

Appendix II: State Owned Enterprises in Kenya

Education and education services

1 National Council for Science and Technology (NCST)
2 Public Universities Inspection Board
3 University of Nairobi
4 Moi University
5 Egerton University
6 Jomo Kenyatta University of Agriculture & Technology
7 Kenyatta University
8 Maseno University
9 Kenya National Examination Council
10 Kenya Literature Bureau
11 Jomo Kenyatta Foundation
12 Kenya Institute of Education
13 Kenya Education Staff Institute
14 Commmission for Higher Education
15 Higher Education Loans Board
16 Teachers Service Commission
17 Western University College of Science and Technology
18 Kenya Institute for Public Policy Research & Analysis
19 Kenya National Bureau of Statistics

Health and Welfare

1 National AIDS Control Council
2 National Campaign Against Drug Abuse Authority
3 National Museums of Kenya
4 N.G.O. Co-ordination Bureau
5 Poverty Eradication Commission
6 National Sports Stadia Management Authority
7 National Disability Council
8 Gender Commission
9 Kenyatta National Hospital
10 Kenya Medical Training College
11 National Hospital Insurance Fund
12 Moi Teaching & Referal Hospital, Eldoret
13 Kenya Medical Research Institute
14 Kenya Medical Supplies Agency (KEMSA)
15 Radiation Protection Board

Development Authority

1 Ewaso Ngiro North Devevelopment Authority
2 Ewaso Ngiro South Development Authority
3 Lake Basin Development Authority
4 Coast Development Authority
5 Kerio Valley Dev. Authority

6 Tana and Athi River Development Authority

Others

1 Kenya Institute of Administration
2 Kenya Ordinance Fact. Corp.
3 Betting Control & Licensing Board
4 State Corporations Appeals Tribunal
5 National Housing Corporation
6 Kenya Roads Board
7 Public Complaints Standing Committee