CORPORATE GOVERNANCE PRACTICES AND FIRM FINANCIAL PERFORMANCE: THE CASE OF PENSION SCHEMES IN KENYA

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DECLARATION

This research project is my original work and has not been presented for a degree award to any other university

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I pay gratitude to my supervisor for guidance in the course work and the mock research project which became the foundation of my research. I also wish to thank my supervisor for support, patience and understanding throughout the research period.

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DEDICATION

To my family and all those who supported in the completion of this project writing.

Thank you and God bless you abundantly.

ABSTRACT

Corporate governance can be defined as the stewardship responsibility of corporate directors to provide oversight for the goals and strategies of a company and to foster their implementation. Good corporate governance practices was nurtured and encouraged to evolve as a matter of best practice but certain aspects of operation in a body corporate were of necessity and required minimum standards of good governance. Pension was an arrangement to provide people with an income when they were no longer earning a regular income from employment. Among the various recommendations for regulation and supervision, one of the highest priorities was joining the International Organization of Pension Supervisors (IOPS) to benefit from international experience as well as developing policies and practices in two areas: the development of a better system for capturing, managing, and analyzing data, and moving to a more risk-based approach to supervision. Citizens needed to know the depth to which corporate governance practices had been entrenched in the firms that managed their very important contributions. Scholars and academicians also wished to use the findings of this study as a basis for further research on this subject. The specific areas covered included corporate governance in emerging economies, the interaction of different governance mechanisms, international organizational of pension scheme (IOPS), best practices, corporate governance index, corporate governance and stakeholders' participation, role of corporate governance and relationship between governance mechanism and firm performance. The survey design was able to give results that were representative of a larger population. Primary data from the field was collected using semi-structured questionnaires. The researcher carried out a pilot study to pre-test and validate the questionnaire. The data was then coded to enable the responses to be grouped into various categories. The study concludes that corporate governance practices and firm financial performance were practiced in the case of pension schemes in Kenya. This study recommends that the government encourage various people to join the pension scheme since the aim of setting pension was to provide people with an income when they were no longer earning a regular income from employment.

TABLE OF CONTENTS

DECLARATION ..... **ii**
ACKNOWLEDGEMENT ..... **iv**
DEDICATION ..... **v**
ABSTRACT ..... **vi**
TABLE OF CONTENTS ..... **vii**
LIST OF FIGURES ..... **ix**
LIST OF TABLES ..... **x**
CHAPTER ONE **1**
INTRODUCTION **1**
1.1 Background of the Study 1
1.1.1 Background to Pension Schemes in Kenya 3
1.2 Statement of the Problem 5
1.3 Objective of the Study 7
1.4 Importance of the study 7
CHAPTER TWO **8**
LITERATURE REVIEW **8**
2.1 Introduction 8
2.2 Theoretical Review 8
2.2.1 Shareholder Perspectives 8
2.2.2 Stakeholders Perspectives 9
2.3 Corporate Governance in Emerging Economies 11
2.4 The Interaction of Different Governance Mechanisms 13
2.5 International Organizational of Pension Scheme (IOPS) 13
2.6 Best Governance Practices 15
2.7 Corporate Governance Index 17
2.8 Corporate Governance and Stakeholders' Participation 17
2.9 Role of Corporate Governance 19
2.10 Performance Measurement 20
2.11 Relationship between Governance Mechanism and Firm Performance 22
2.11.1 Board Composition 22
2.11.2 Leadership Structure 23

2.11.3 Board Ownership 23
2.11.4 Institutional Holdings 23
2.11.5 Committee Composition 23
2.12 Empirical Review 24
2.13 Conclusion 24
CHAPTER THREE 26
RESEARCH METHODOLOGY 26
3.1 Research design 26
3.2 Population and Sample 26
3.3 Data collection 26
3.3.1 Validity and Reliability 27
3.4 Data analysis 28
CHAPTER FOUR 29
DATA ANALYSIS AND INTERPRETATION 29
4.1 Introduction 29
4.1.1 Response Rate 29
4.2 Disclosure on Corporate Governance 31
4.3 Ethics and Conflict of Interest on Corporate Governance 32
4.4 Sound Governance Practices 33
4.5 Corporate Governance Practices 34
CHAPTER FIVE 36
SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS ... 36
5.1 Introduction 36
5.2 Summary of the Findings 36
5.3 Conclusion 37
5.4 Recommendations 38
5.5 Recommendation for Further Studies 38
5.6 Limitations of the Study 39
REFERENCES 40
APPENDICES 54
Appendix I: Introductory Letter 54
Appendix II: Research Questionnaire 55

LIST OF FIGURES

Figure 4.1: Education level of the Respondents 29
Figure 4.2: Age of the Respondents 29
Figure 4.3: Gender of the respondents 30
Figure 4.4: Period that the respondents have been working in the organization 31

LIST OF TABLES

Table 4.1: Disclosure on corporate governance 31
Table 4.2: Ethics and Conflict of Interest on corporate governance 32
Table 4.3: extent that the following factors enable pension scheme to maintain sound governance practices 33
Table 4.4: extent that the following corporate governance practices are focused 34
Table 4.5: level of agreement with the following statements that relate to corporate governance at your scheme 35

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

In the broadest sense, corporate governance can be defined as the stewardship responsibility of corporate directors to provide oversight for the goals and strategies of a company and to foster their implementation. Gourevitch and Shinn (2005) however defined it as the process and structure used to direct and manage business affairs of the company towards enhancing prosperity and corporate accounting with the ultimate objective of realizing shareholders long-term value while taking into account the interest of other stakeholders. Corporate governance was thus perceived as the set of interlocking rules by which corporations, shareholders and management governed their behavior. These rules referred to individual firm attributes and the factors that allowed companies to maintain sound governance practices even where public institutions are relatively weak. Such factors included a corporation's ownership structure, its relationships with stakeholders, financial transparency and information disclosure practices as well as the configuration of its managing boards.

While there existed numerous approaches to assess the quality of the legal and institutional framework of countries (e.g. Kaufmann *et al.*, 2003), investors had shown a growing demand for a global benchmark of good corporate behavior, which helped create shareholder value regardless of the particular system (Gompers *et al.*, 2003). Corporate governance processes mattered to workers because they shaped: the creation of wealth and its distribution into different pockets; the portfolios of pensioners and retirees, the claims of the rich and the poor rewards to entrepreneurial initiative; the incentives firms had to invest in their labor force and social welfare, health, and retirement plans (Gourevitch and Shinn, 2005, p. 3).

Good corporate governance practices was nurtured and encouraged to evolve as a matter of best practice but certain aspects of operation in a body corporate were of necessity and required minimum standards of good governance (Jones, 1995). There were a number of principles that were essential for good corporate governance practices which had been identified as representing critical foundation and virtues of good corporate governance practices. Corporate governance best practices were, by their very design, intended to

enhance board members' ability to discharge their responsibilities – responsibilities to shareholders, the company, and each other. Corporate governance best practices had historically focused on issues that included the composition of the board (i.e. the proportion of inside directors to outside directors), whether the CEO concurrently held the position of board chairperson, the size of the board, the level and type of director equity held in the company, and the composition of the various board committees.

Researchers increasingly realized that there was not a single agency model that adequately depicted corporate governance in all national contexts (Lubatkin et al., 2005). The predominant model of corporate governance was a product of developed economies (primarily the United States and United Kingdom), where the institutional context lend itself to relatively efficient enforcement of arm's-length agency contracts (Peng, 2003). In developed economies, because ownership and control were often separated and legal mechanisms protected owners' interests, the governance conflicts that received the lion's share of attention were the Principal–Agent (PA) conflicts between owners (principals) and managers (agents) (Jensen and Meckling, 1976). However, in emerging economies, the institutional context made the enforcement of agency contracts more costly and problematic (Wright et al., 2005). This resulted in the prevalence of concentrated firm ownership (Dharwadkar et al., 2000).

Concentrated ownership, combined with an absence of effective external governance mechanisms, resulted in more frequent conflicts between controlling shareholders and minority shareholders (Morck et al., 1988). This led to the development of a new perspective on corporate governance, which focused on the conflicts between different sets of principals in the firm. This came to be known as the principal–principal (PP) model of corporate governance, which centred on conflicts between the controlling and minority shareholders in administrators of pension schemes (Dharwadkar et al., 2000).

The complementarity of pension and corporate governance reforms resulted from the fact that policy-making was influenced by special interest groups that had political power to block the reforms. Publicly traded firms in developing countries were typically owned by a handful of powerful groups that had the incentive to influence the government and determine the level of investor protection in capital markets according to their interests. Similarly, workers and

labor unions were powerful enough to block pension reforms. In this environment, reforms only occurred if the relevant interest groups benefit from them (Calomiris and Beim, 2001). Pension reforms were followed by legal reforms aimed at improving investor protections in capital markets, and second, the governments restrict pension funds to hold domestic securities.

1.1.1 Background to Pension Schemes in Kenya

Pension was an arrangement to provide people with an income when they were no longer earning a regular income from employment. When looking at pension, retirement plan or superannuation term arose which referred to a pension granted upon retirement. Retirement plans were set up by employers, insurance companies, the government, or other institutions such as employer associations or trade unions (Government of Kenya 1997).

i. The pension schemes sector in Kenya amounts to approximately KShs 200 billion, or the equivalent of 23% of Grosse Domestic Product (GDP) part of which was held by National Social Security Fund (NSSF) which was a mandatory national security scheme.

ii. Savings for retirement in Kenya were currently operated by statutory contributions under National Social Security Fund (NSSF) and sponsor-led schemes

iii. Formal retirement benefit sector covers approximately 11% of the labour force.

iv. The Government of Kenya had recognized the importance of the retirement funds industry in boosting economic growth and in accelerating domestic savings which currently stands at a rate of 13%.

v. The legal framework of the industry was governed by the Retirement Benefits Act 1997 which then was the regulator for the industry

vi. The RBA objectives included raising of retirement coverage and to boost domestic savings to 25%.

The Retirement Benefits Act was introduced in 1997 aimed specifically at regulating a market which had heretofore lacked a harmonised legal framework (Government of Kenya (1997). Under the Act, a Retirement Benefits Authority was formed with the following specific objectives:

i. To regulate and supervise the establishment and management of retirement benefit schemes

ii. To protect the interest of members and sponsors of retirement benefits schemes

iii. To promote the development of the retirement benefit sector

iv. To advise the Minister of Finance on the national policy to be followed with regard to the retirement benefits sector.

Under the Act, registered pension schemes were obliged to appoint: a board of trustees, one third of whom were elected by the scheme members; professional managers to manage the scheme assets and a custodian to hold the assets in safe-keeping.

Additionally, schemes were obliged to produce audited accounts on an annual basis. Direct benefit schemes were further obliged to undergo actuarial review every 3 years.The Government had introduced a funded Contributory Pension Scheme in the Public Service in Kenya that made adequate retirement provisions for its employees. The new scheme took effect from 1st July 2006.

Statutory contributions to the NSSF were set at 10% of an employee’s pay, half of which was paid by the employer and half by the employee. There was a monetary ceiling on the maximum combined contribution to the NSSF of currently K Shs 400 per month (or at only 1.3% of average monthly formal sector earnings in Kenya of Kshs 31,357). There have been only two adjustments to the statutory ceiling on contributions since the inception of the NSSF (i.e. an increase from Kshs 80 to K Shs 160 in 1977 and from K Shs 160 to 400 in 2001).

In Kenya, the provision and management of retirement benefits for public service employees (Public Service Pension Scheme; PSPS) was governed under a Pensions Act and Regulations. Certain provisions of the Constitution of Kenya were also relevant especially in the context of

considering reform options for the current arrangements. The Pension Scheme covered approximately 406,000 civil servants, teachers and police and prison staff and just over 180,000 pensioners. It provided a pension of 2.5% of final basic salary for each year of service on retirement from service at 55. Unreduced pensions were payable on retirement at or after 50 with the parent Ministry's consent or earlier on ill health retirement. The pension fraction targeted a retirement pension of 75% of basic salary after thirty years of service (or an average of 50% of total remuneration for all categories of public service employees). A higher pension fraction applied for armed forces and military personnel. Retiring staff opted to take up to 25% of their pension in the form of lump sum with a generous uniform commutation factor of 20:1 applying. No guaranteed pension increases had applied in the past; there had only been four pension increases in the forty years to 2004 with the last increase having been in 1991. Modest pension increased at 3% every two years had been introduced since 2005. Benefits vested after ten years of service and there was no portability of benefits and individuals who resigned from service before retirement were not entitled to any benefits (Raichura., 2008).

1.2 Statement of the Problem

Corporate governance practices had received increasing attention since the 1990s, with influential reports issued by the Cadbury Committee (1992), Greenbury Committee (1995), Hampel Committee (1998), and Turnbull Committee (2003) and Higgs Derek (2003). These reports resulted in various corporate governance codes and recommendations, the most recent being the Combined Code on Corporate Governance, July 2003.

Some recent studies had used a broader measure of corporate governance through a composite corporate governance rating, including Gompers et al. (2003) for the U.S., Klapper and Love (2004) for fourteen emerging markets, Durnev and Kim (2002) for twenty seven countries, Bauer et al. (2003) for the EMU and the U.K.. These studies generally found a positive relationship between governance standards and firm value.

Baure et al. (2003) and other studies were based on ratings of one or two years only, assuming that governance ratings remained constant for a number of years. However some studies show otherwise — there was a significant upward trend for the corporate governance

scores over the time. Without time series data, researchers could not study how firms adjusted their governance structure over time, or analyzed the causality between governance and firm performance found in Black et al. (2002). A recent study by Klapper and Love, (2004), found that differences in firm-level contracting environment affected a firm's choice of governance mechanisms, in line with arguments put forth in Himmelberg et al. (1999). However because their governance data had no time variation, they were not able to control the fixed effects and to test the causality.

Currently there were over 1300 registered administrators of pension schemes in Kenya. These pension schemes hold assets of approximately 140 billion Kenya shillings by 2003 alone which was 27% of GDP by that time (Central Bank of Kenya, 2003). In the same years for instance, Kshs59 billion was held by National Social Security Fund (NSSF) which is a mandatory national security scheme. There were about 1110 other registered private pension and provident fund providers countrywide.

Among the various recommendations for regulation and supervision, one of the highest priorities was joining the International Organization of Pension Supervisors (IOPS) to benefit from international experience as well as developing policies and practices in two areas: the development of a better system for capturing, managing, and analyzing data, and moving to a more risk-based approach to supervision. The International Organisation of Pension Organisers (IOPS) had outlined best practises in this sector one of which was the principle of governance. The IOPS asserted that the supervisory authority adhered to its own governance codes and was accountable. There were clearly documented procedures for decision making.

According to some researchers (Demsetz and Villalonga, 2001; Maher and Andersson, 2002) pension schemes had put in place competent corporate governance policies while others held different views (Larcker, Richardson and Tuna, 2004; Foerster and Huen, 2004; Young, 2000). Up to the time of this study; there was no study that determined the extent to which retirement benefits schemes had adopted the corporate governance practices in Kenya. Using the questions that constitute the computation of the Corporate Governance Index, this study makes a potential contribution in this area by analyzing a number of corporate governance mechanisms based on time-varying firm-specific data. It provided a comprehensive measure of the extent to which a company had adopted international best practices in corporate

governance, as disclosed in their corporate governance disclosures. The main objective of the study therefore, was to investigate the corporate governance practises adopted by the pension schemes in Kenya.

1.3 Objective of the Study

The objective of this study was to determine corporate governance practices of pension schemes in Kenya

1.4 Importance of the study

The findings of this study was of interest to the management and trustees of retirement benefit schemes who were able to determine the levels at which they had embraced the corporate governance practices.

The Government of Kenya benefit from the study in its bid to make policies relating to corporate governance practices.

Citizens needed to know the depth to which corporate governance practices had been entrenched in the firms that managed their very important contributions. Scholars and academicians also wished to use the findings of this study as a basis for further research on this subject.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter dealt with the available literature that had been reviewed for the study. The literature was mainly on the corporate governance practices. The specific areas covered included corporate governance in emerging economies, the interaction of different governance mechanisms, international organizational of pension scheme (IOPS), best practices, corporate governance index, corporate governance and stakeholders' participation, role of corporate governance and relationship between governance mechanism and firm performance.

2.2 Theoretical Review

2.2.1 Shareholder Perspectives

There are two main theories of shareholder-oriented governance: the principal-agent or finance model and the myopic market model.

The principal-agent model started from an assumption that the social purpose of corporations is to maximise shareholders' wealth (Coelho *et al.*, 2003; Friedman, 1970). The principal-agent model regards the central problem of corporate governance as self-interested managerial behaviour in a universal principal-agent relationship. Agency problems arose when the agent did not share the principal's objectives. Furthermore, the separation of ownership and control increased the power of professional managers and left them free to pursue their own aims and serve their own interests at the expense of shareholders (Berle and Means, 1932). There were two problems occurring in the agency relationship with which agency theory was concerned. The first was that because it was difficult or expensive for the principal to verify what the agent was actually doing, the principal could not verify that the agent had behaved appropriately. The second problem was that the principal and the agent preferred different actions because of the different attitudes toward risk (Eisenhardt, 1989, p. 58). Those two problems brought about a particular type of management cost incurred as principals attempt to ensure that agents acted in principals' interests: agency cost (Jensen and

Mechling, 1976). To solve those problems, agency theory determined the most efficient contract governing the principal-agent relationship and an optimal incentive scheme to align the behaviour of the mangers with the interest of owners. While the principal-agent model agreed upon the failure of corporate internal control, it denied the inherent failure of market mechanisms, insisting that markets were the most effective regulators of managerial discretion, the so-called efficient market model (Blair, 1995, p. 107).

The myopic market model shared a common view with the principal-agent model that the corporation served the shareholders' interests only, but criticized that the Anglo-American model of corporate governance because of competitive myopia (Hayes and Abernathy, 1980) and its consequent pre-occupation with short-term gains in return, profit, stock price and other performance measures induced by market pressures. The myopic market model holds that what was wrong with corporate governance was that the system encouraged managers to focus on short-term performance by sacrificing long-term value and competitiveness of the corporation. The financial markets often forced managers to behave in a way divergent from the maximization of long-term wealth for shareholders (Blair, 1995). The myopic market view contended that corporate governance reform provided an environment in which shareholders and managers were encouraged to share long-term performance horizons. Shareholders' loyalty and voice increased, whereas the ease of shareholders' exit reduced. Policy proposals for the reform included the encouragement of relationship investing to lock financial institutions into long-term positions, restrictions on the takeover process and on voting rights for short-term shareholders, and the empowerment of other groups such as employees and suppliers that had long-term relationships with the firm (Keasey *et al.*, 1997, pp. 6-7).

2.2.2 Stakeholders Perspectives

There were two main theories of stakeholder governance: the abuse of executive power model and the stakeholder model.

Current Anglo-American corporate governance arrangements vested excessive power in the hands of management who abused it to serve their own interest at the expense of shareholders and society as a whole (Hutton, 1995). Supporters of such a view argued that the current

institutional restraints on managerial behaviour, such as non-executive directors, the audit process, the threat of takeover, were simply inadequate to prevent managers abusing corporate power. Shareholders protected by liquid asset markets were uninterested in all but the most substantial of abuses. Incentive mechanisms, such as share options, were means through which managers legitimized their abnormal overpayment (viewed by some as a symptom of the breakdown of governance (Keasey *et al.*, 1997, pp. 7-8)). The abuse of executive power was particularly embedded in the problem of executive overpay since executive remuneration had risen far faster than average earnings and there was at best a very weak link between compensation and management performance (Conyon *et al.*, 1995; Gregg *et al.*, 1993). The only restraint on executive pay seemed to be the modesty of executives themselves, and the creation of so-called independent remuneration committees by large companies was not effective. What was worse was that it legitimized self-serving managerial behaviors. The independence was generally a sham, not for restraining excess of pay, but for justifying it (Kay and Silberston, 1995, p. 85, 94). The supporters of this model did not believe that the main lines of corporate governance reform, such as non-executive directors, shareholder involvement in major decisions and fuller information about corporate affairs, were suitable monitoring mechanisms (Kay and Silberston, 1995, p. 94). Instead, they proposed statutory changes in corporate governance, under which hostile takeovers were not possible to effect, since ownership of shares no longer brought the right to appoint executive management. The basic objective of corporate governance in this guise was managerial freedom with accountability, to allow executive management the power to develop the longer term business, while holding them rigorously responsible to all stakeholders involved in the business.

Perhaps the most fundamental challenge to the orthodoxy was the stakeholder model, with its central proposition was that a wider objective function of the firm was more equitable and more socially efficient than one confined to shareholder wealth (Keasey *et al.*, 1997, pp. 8-9). The well-being of other groups such as employees, suppliers, customers and managers, who had a long-term association with the firm and therefore a stake in its long-term success, was recognized. The goal of corporate governance was to maximize the wealth creation of the corporation as a whole. Specifically, a stakeholder was defined as any group or individual who affected or was affected by the achievement of the firm's objectives (Freeman, 1984, p.

25), and this was meant to generalize the notion of stockholder as the only group to whom management needed to be responsive (Freeman, 1984, p. 31). These definition were formulated form the base that modern corporation was affected by a large set of interest groups, including at a minimum shareholders, lenders, customers, employees, suppliers and management, which were often referred to as the primary stakeholders, who were vital to the survival and success of the corporation. To these the corporation added secondary stakeholders, such as the local community, the media, the courts, the government, special interest groups and the general public, that was society in general. From this perspective, corporate governance debates often proceeded with a fixation on the relationship between corporate managers and shareholders, which presupposed that there was only one right answer. In fact, shareholders were difficult and reluctant to exercise all the responsibilities of ownership in publicly held corporations, whereas other stakeholders, especially employees, often too easily exercised their rights and responsibilities associated as owners. This was a compelling case for granting employees some form of ownership.

2.3 Corporate Governance in Emerging Economies

Emerging economies were 'low-income, rapid-growth countries using economic liberalization as their primary engine of growth' (Hoskisson et al., 2000, p. 249). Institutional theory had become the predominant theory for analysing management in emerging economies (Hoskisson et al., 2000; Wright et al., 2005). As an example, seven of the eight papers published in a recent special issue of the Journal of Management Studies on strategy in emerging economies utilized institutional theory (Wright et al., 2005). Institutions affected organizational routines (Feldman and Rafaeli, 2002) and helped frame the strategic choices facing organizations (Peng, 2003). In short, institutions helped to determine firm actions, which in turn determine the outcomes and effectiveness of organizations.

However, the institutions that impacted such organizational actions in emerging economies were not stable. Furthermore, the formal institutions that did exist in emerging economies often did not promote mutually beneficial impersonal exchange between economic actors (North, 1994). As a result, organizations in emerging economies are to a greater extent guided by informal institutions. The theories used by researchers often implicitly assume that the institutional conditions found in developed economies were also present in emerging

economies. Clearly, this was not the case in emerging economies and as a result the organizational activities differred considerably from those found in developed economies (Wright et al., 2005).

To illustrate, in the case of corporate governance, emerging economies typically did not have an effective and predictable rule of law which, in turn, created a 'weak governance' environment (Dharwadkar et al., 2000, p. 650). This was not to say that emerging economies had no laws dealing with corporate governance. In most cases, emerging economies had attempted to adopt legal frameworks of developed economies, in particular those of the Anglo-American system, either as a result of internally driven reforms (e.g. China, Russia) or as a response to international demands (e.g. South Korea, Thailand). However, formal institutions such as laws and regulations regarding accounting requirements, information disclosure, securities trading, and their enforcement were either absent, inefficient, or did not operate as intended. Therefore, standard corporate governance mechanisms had relatively little institutional support in emerging economies (Peng et al., 2003). This resulted to informal institutions, such as relational ties, business groups, family connections, and government contacts, all playing a greater role in shaping corporate governance (Peng and Heath, 1996; Yeung, 2006).

For threshold firms, the transition to professional management was always difficult. Yet it was even more difficult in emerging economies because of the weak institutional environment and it was common for even the largest firms to still be under the control of the founding family. In essence, these firms attempted to appear as having 'crossed the threshold' from founder control to professional management. But the founding family often retained control through other (often informal) means (Liu et al., 2006). Indeed, publicly-listed firms in emerging economies had shareholders, boards of directors, and 'professional' managers, which composed the 'tripod' of modern corporate governance (Monks and Minnow, 2001). Thus, even the largest publicly-traded firms in an emerging economy adopted the appearance of corporate governance mechanisms from developed economies, but these mechanisms rarely function liked their counterparts in developed economies.

In short, the corporate governance structures in emerging economies often resembled those of developed economies in form but not in substance (Peng, 2004). As a result, concentrated

ownership and other informal mechanisms emerged to fill the corporate governance vacuum. While these ad hoc mechanisms solved some problems, they created other, novel problems in the process. Each emerging economy has a corporate governance system that reflects its institutional conditions. However, there are a number of similarities among emerging economies as a group; conflicts between two categories of principals are a major issue.

2.4 The Interaction of Different Governance Mechanisms

Corporate governance comprised many dimensions. Based on the U.K. Code, it can be divided broadly into the role of directors, directors' remuneration, the role of shareholders, and accountability and audit.

Some of the structures were complements while others were substitutes to certain extent. The previous research had found different governance patterns. For example, Peasnell et al. (2001) found evidence of a convex association between the proportion of outside board members and the level of insider ownership in the U.K. corporate control process. Shivdasani and Yermack (1999) observed, using U.S. data, that when the CEO served on the nominating committee or no nominating committee existed, firms usually appointed fewer independent outside directors and more grey outsiders. Similarly, Vafeas (1999) discovered that the likelihood of engaging a nominating committee was related to board characteristics such as inside ownership, number and quality of outsider directors for U.S. firms.

Board structure was an important governance mechanism. Kenneth et al. (1995) note the substitution effects between outside directors, blockholders, and incentives to insiders using eighty one U.S. bank-holding companies in his study. Both Dedman and Elisabeth (2002) and Young (2000) investigated the board structure determinants before and after Cadbury Report. They either found managerial entrenchment reduced or non executive directors were increased following the imposition of new standards of best practice regarding board structure.

2.5 International Organizational of Pension Scheme (IOPS)

The International Organisation of Pension Supervisors (IOPS) is an independent international body representing those involved in the supervision of private pension arrangements. The

organisation currently has around 60 members and observers representing approximately 50 countries and territories worldwide - from Australia to Zambia - covering all levels of economic development and bringing together all types of pension and supervisory systems (Ambrogio and Giacomel, 2008).

The IOPS, formed in July 2004, was instigated by the International Network of Pension Regulators (INPRS), an informal network of regulators and supervisors. It was felt that a more formal, independent, body could better serve as a world-wide forum for policy dialogue and the exchange of information, as well as the standard setting body, promoting good practices in pension supervision. The major goal of the IOPS was to improve the quality and effectiveness of the supervision of private pension systems throughout the world, thereby enhancing their development and operational efficiency, and allowing for the provision of a secure source of retirement income in as many countries as possible (Ambrogio and Giacomel, 2008).

The objective of pension supervision was to protect the interests of pension fund members and beneficiaries and safeguard the stability of the pension industry and financial system as a whole. Given the increasing speed and complexity of financial markets, pension fund supervisory authorities should be alert to developments which posed a challenge to this objective. The increasing use of alternative investment forms, such as (funds of) hedge funds and private equity, were such a development (Conyon, 1997). As pension entities were placing a share of their capital in these types of instrument, the potential risks flowing from these products justified specific attention from supervisory authorities. The way supervisors respond to these risks varied depending on the supervisory approaches adopted. In order to support supervisors as they clarified and articulated these expectations, IOPS had developed a set of best practices, drawing on the knowledge and experience of supervisors However, in many jurisdictions supervisors' responses were based on regulation (Madero., 2007). Compliance by plans and funds with this regulation was then monitored by supervisory authorities, e.g. via off- and on-site supervision and in-depth evaluation of pension funds.

The aims and purposes of IOPS therefore, were summarized as:

i. Serving as the standard-setting body on pension supervisory matters and regulating issues related to pension supervision, taking into account the variety of different private pension systems;

ii. Promoting international co-operation on pension supervision and facilitating contact between pension supervisors and other relevant parties, including policy makers, researchers and the private sector;

iii. Providing a worldwide forum for policy dialogue and exchange of information on pension supervision;

iv. Participating in the work of relevant international bodies in the area of pensions, including joint activities to improve statistical collection and analysis;

v. Promoting, conducting and facilitating the distribution and communication of research, and collecting information in co-operation with relevant international bodies

2.6 Best Governance Practices

The principles of best practice for public pensions funds largely concerned governance, broadly defined, and were intended to ensure that public pension schemes had clear objectives, were free from conflicts of interest, and were operated in as transparent a manner as possible (Carmichael and Palacios, 2004). They also aimed to ensure that the operators of the scheme were accountable to members for their decisions and success or failure in meeting the objectives of the scheme. In short, public pension schemes were operated in the best interests of those who bear the burden of their financial failings. The following principles represented best practices in governance and provided a reference point for considering the present practices (IOPS, 2000):

i. There were clear roles and responsibilities within the pension fund. Clear roles, objectives, and responsibilities are fundamental to transparency (and to accountability). The objectives were set down by government--preferably in law--along with an explicit statement about the promises being made and any government guarantees involved (Carmichael and Palacios, 2004).

ii. The law establishing the management agency provided unambiguous conditions under which members of the governing body of the agency was appointed and removed. Whatever the precise legal form, the members of the governing body of the management agencies operated with a fiduciary responsibility to the members of the scheme, and that single consideration dictated the appropriate terms of appointment and dismissal.

iii. The managing agency was free from inappropriate interference from the government I pursuing its objectives and meeting its responsibilities. The government remained at arm's length from the investment decisions of the fund manager.

iv. The processes for formulating and executing scheme policies were open and transparent. The policy framework and the process of implementation was disclosed and adequately explained.

v. The government established the structure of delegations permitted within the scheme. The essential point was that the structure of delegations was well thought out and transparent to stakeholders. The structure of delegations stated clearly, where responsibility lay in the event of delegation. Responsibility included the explicit requirement for the governing body of the management agency to monitor and review delegated powers.

vi. The management agency was required--by law--to establish internal governance structures and processes designed to minimize corruption, mismanagement, and fraud.

vii. These governance procedures included the mandatory establishment of a risk management and audit committee with appropriate reporting lines. It included a code of conduct for staff and senior executives, detailing how to deal with conflicts of interest. It detailed the roles and responsibilities of the different groups within the agency (board, senior management, audit committee, and so forth) and how they were to account for their actions. It included a quality control process, and it included rigorous documentation, review, and audit requirements for investment decisions and information technology support systems.

viii. The government required the management agency to be regulated and supervised by the same agency that was responsible for regulating private pension providers and, where feasible, to meet the same standards imposed on private providers. Not only was this requirement a matter of good governance, it was compatible with the objective of establishing competitive neutrality throughout the financial system.

2.7 Corporate Governance Index

Corporate Governance Index was built based on four different aspects of the company's governance structure: CEO duality, Size of the board of directors, Managements' holdings and Block shareholders' holding. This index was used as a proxy measure of the effectiveness of the corporate governance mechanism. Black et al, (2006), report strong Ordinary Least Square (OLS) and instrumental variable evidence that overall corporate governance index was an important and likely causal factor in explaining the market value Public Firms.

Using Institutional Shareholder Services (ISS) database, Karpoff et al. (2000) found that cross-sectional performance in related to a simple index of restrictiveness of a firm's governance structure. Consistent with the management entrenchment hypothesis, their result showed that firms with the fewest restrictive provisions relative to other firms in the industry had the best industry-adjusted performance measured by return on assets and market-book-value ratio.

Constructing broad corporate governance Index (CGI) Drobetz et al. (2004) document a strong positive relationship between the quality of firm-level corporate governance and firm valuation. Using dividend yielded as proxies for the cost of capital, they also reported negative correlation between expected stock returns and firm level corporate governance. Finally, during the sample period they documented that an investment strategy (that bought high-CGI firms and shorted low-CGI firms) earned abnormal returns of about 12 percent on an annual basis.

2.8 Corporate Governance and Stakeholders' Participation

Research in strategic management was quick to realize that people who were affected by organizational behavior might have an impact on the achievement of organizational goals and

the definition of stakeholders was born: A stakeholder in an organization was any group or individual who affected or was affected by the achievement of the organization's objectives (Freeman, 1984, p. 46).

Stakeholder theory (Freeman, 1984; Donaldson and Preston, 1995) argued that the corporation was a social entity and affected the welfare of many people. As these stakeholders were instrumental to corporate success and haved moral as well as legal rights (Donaldson and Preston, 1995) their claims were considered by corporate leaders (Blair, 1995). If corporate governance was understood to be the system by which companies were directed and controlled (Cadbury, 2000) it considered stakeholder concerns. Research suggested that the participation of stakeholders in corporate decision-making enhanced efficiency and reduce conflicts (Rothman and Friedman, 2001). A central question of concern was then how do corporations integrate stakeholder concerns into their decision-making structures and conducted business responsibly towards them (Manville and Ober, 2003)? Basically, a reactive or proactive attitude had been distinguished in this regard by Kaptein and Van Tulder (2003) who analyzed various firms on their approach to stakeholder management.

Companies approaching stakeholders in a reactive fashion will not integrate their concerns into corporate decision making and taking responsibility for their claims. The inherent risk of this approach was that organizational goals and stakeholder demands became misaligned and a cause for conflict or corporate irresponsibility (Mackenzie, 2007). Scandals such as Enron had been attributed to a lack of consideration of stakeholder concerns (Turnbull, 2002; Watkins, 2003). To react to a crisis such as the Enron scandal governments set up new regulation in order to align the interests of a broader set of stakeholders with corporate conduct. In the case of Enron and WorldCom the Sarbanes-Oxley Act (SabOx) was passed. Tarnished reputation and the threat of new legislation were often regarded as a key motivation for companies to join the corporate responsibility debate (Paine, 1994). In short, the reactive attitude toward stakeholder concerns contained significant risks and were likely to lead to an antagonistic business in society relationship (Beloe *et al.*, 2004).

More proactive companies seemed to integrate stakeholder concerns into their decision-making processes and establish necessary governance structures (de Wit *et al.*, 2006).

Business for Social Responsibility defined corporate responsibility as a set of policies, practices and programs that were integrated throughout business operations and decision-making processes and intended to ensure the company maximized the positive impacts of its operations on society [1]. Proactive firms took responsibility beyond financial aspects and considered their environmental and social impacts.

2.9 Role of Corporate Governance

To be able to appreciate the role of corporate governance with respect to the relation between capital structure and value, we had to describe this concept. The aim of corporate governance was to ensure that opportunistic behavior did not occur, by mitigating and moderating agency problems that could involve an agent (manager) and various principals (shareholders, debt holders, employees, suppliers, clients etc.) or else a principal (the main entrepreneur) and various agents (managers, employees, investors etc.). Moreover, it facilitated the creation of special skill required in strategic decisions (incentive to firm-specific investment) and limited problems of asymmetric information.

Corporate governance was a broad, complex and problematic concept, which was extremely relevant, while difficult to define, due to the various dimensions that it comprised (Zingales, 1998). The expression corporate governance could take on two meanings, depending on whether greater emphasis was placed on the instruments used to allocate and manage power within a firm, or on the role of external institutions and mechanisms that controlled firm activity efficiency. It was defined as: a system of how decision making power is distributed within the firm, so to overcome problems of contract incompleteness between different stakeholders (managerial or internal corporate governance); and a set of rules, institutions and practices developed to protect investors from entrepreneurial and managerial opportunistic behavior (institutional or external corporate governance). A literature review of those mechanisms that had been traditionally used was offered by Shleifer and Vishny (1997) and by Denis (2001).

In this light, management or internal instruments represent coordination mechanisms that can be used in bilateral contracting processes between management and ownership, or else between management and the other stakeholders. Institutional or external instruments are

mechanisms of collective coordination that operate through the financial markets, through the legal system, the judicial system and the manager job market.

Conflicts of interest and the risk of opportunistic behavior increased the firm's cost of capital. Investors were hesitant to trust management and to thus offer their financial resources to such firms. To the contrary, efficient governance that increased the firm's trustworthiness generated market appreciation and investor trust. This meant that capital could be found more easily and the value creation process was highly favored.

Management participation in the equity of the firm, the presence of external and independent members in the Board of Directors, the presence of institutional investors and the efficiency of the financial system, the legal system and enforcement were only some of the levers of both managerial and institutional corporate governance, that must be integrated together with the role of capital structure so that the firm's ability to create value can be understood.

2.10 Performance Measurement

Whereas the performance measurement concept was deeply rooted in the context of manufacturing, it had to some extent been neglected in service management. However the importance of performance measurement in service industries was widely accepted in literature (Van Biena and Greenwald, 1997).

Performance measurement systems were designed to monitor the implementation of organizations plans and determine when the plans were unsuccessful and how to improve them (Atkinson et al, 1997). They were used to focus attention on the organizations objectives, to measure and report performance and to understand how process performance affected organizational learning (Atkinson et al, 1997). Identifying operational problems, which could be solved by adjusting existing processes, and indicating more fundamental problems, which required an adjustment to strategies of the organization, were further uses of performance measurement.

Performance measurements were also referred to as monitoring and evaluation. Monitoring was aimed at ensuring that the activities of the project were being undertaken on schedule to facilitate implementation as specified in the project design. Any constraints in

operationalizing the design were quickly detected and corrective action taken. Evaluation involved a systematic review or examination of the elements of success and failure in the project experience during the project life to learn how better to plan the project in future. This implied that evaluation was a continuous exercise during the project life and was much related to project monitoring. Monitoring provided the data on which the evaluation was based (Mbeche,2000).

While accounting systems were used to measure performance because they were considered to be reliable and consistent and because they mesh with the primary objective of creating profits, there was a growing concern that concentration on financial measures was inadequate for strategic decision making and indeed for full internal management and control (Atkinson et al., 1997). Long-term survival was linked to organizations chosen strategy, and the strategy determined what must be measured. Measuring only short-term financial results had dysfunctional consequences to its long-term survival (Brignal, 1993). Brignal indicated how measures across six dimensions related to strategy over an extended period were needed to implement strategy in a local government child-care organization.

Government performance needed to measure ‘‘economy, efficiency and effectiveness’’ (Palmer, 1993). Economy is defined as acquiring resources in appropriate quantity and at lease cost. Efficiency is defined as maximizing output for a given set of inputs for a required output. Together, economy and efficiency are consistent with notions of financial accountability in the public sector. Economy and efficiency are usually measured in financial terms, and data such as costs, volume of service and productivity are relatively simple to measure (Palmer, 1993). Measuring economy and efficiency is consistent with Kaplan and Norton’s (1992) categories of resource utilization and financial performance. Effectiveness is defined as the extent to which the defined task has been accomplished (Palmer, 1993).

Notions of public sector accountability became widely used in the 1990’s, with formal systems of accountability being built into Legislation, rules and regulations for government bodies. According to Lee, (2004) the rationale of performance contracts in the public sector in Kenya is to improve on performance that has been consistently poor due to poor management, excessive regulation and controls, political interference, brain drain, multiplicity of principles and bloated staff levels.

2.11 Relationship between Governance Mechanism and Firm Performance

This study borrowed from Himmelberg et al. (1999) who use panel data to show that managerial ownership is explained by key variables in the contracting environment. A large fraction of the cross-sectional variation in managerial ownership is explained by unobserved firm heterogeneity. Moreover, after controlling for both observed firm characteristics and firm fixed effects, changes in managerial ownership did not affect firm performance statistically.

Many other researchers had examined the relationship between variety of governance mechanisms and firm performance. However, the results were mixed. Some examined only the impact of one governance mechanism on performance as Himmelberg et al. did, while others investigated the influence of several mechanisms together on performance. None of them covered a complete set of governance mechanisms. Below, the study briefly reviews some of previous studies on the governance-performance relationship.

2.11.1 Board Composition

It was suggested that higher proportion of non-executive directors in the board helped to reduce the agency cost. Kee et al. (2003) and Hutchinson and Gul (2003) support this view by showing that that higher levels of non-executive directors on the board weaken the negative relationship between the firm's investment opportunities and firm's performance. However, Weir et al. (2002) dispute it by stating that there was no significant relationship between non-executive directors' representation and performance. In contrast, in the U.K., Weir and Laing (2000) found a negative relationship between non-executive director representation and performance. In addition, Yermack (1996) present that small board had a higher market valuation.

Stronger support for the positive impact of non-executive directors came from event study analysis. The studies by Shivdasani and Yermack (1999) showed that the appointment of non-executive directors increased company value.

2.11.2 Leadership Structure

Although corporate governance codes regard separation of the role of CEO and chairman as a sign of good governance, previous empirical analyses did not support it. For example Weir et al. (2002), and Weir and Laing (2000) did not find any significant relationship between CEO duality and performance. Brickley et al. (1997) observe that costs of separation are larger than benefits for most large U.S. firms.

2.11.3 Board Ownership

The findings of the primarily U.S. based literature suggested that management is aligned at low or possibly high levels of ownership but is entrenched at intermediate ownership levels (e.g., Morck et al., 1988; McConnell and Servaes, 1990). U.K. evidence confirms that U.K. management becomes entrenched at higher levels of ownership than their U.S. counterparts (e.g. Faccio et al., 1999; Short and Keasey, 1999). Hutchinson and Gul (2003) report that management share ownership and managers' remuneration weaken the negative relationship between the firm's investment opportunities and firm's performance. In contrast, Coles et al. (2001) do not find any contribution to performance by managerial ownership.

2.11.4 Institutional Holdings

As the U.K. Code encouraged institutions to take an active role in governance, the study expected a positive relationship between institutional holdings and firm performance. Unfortunately, empirical evidence is not supportive of this recommendation. Both Faccio and Lasfer (1999, 2000) failed to find such a significant relationship for U.K. firms. Besides, de Jong et al. (2002) find that major outside and industrial shareholders negatively influence the firm value.

2.11.5 Committee Composition

For U.K. companies, Conyon (1997) provided a thorough review of the workings of remuneration committees and shows that firms with remuneration committees pay directors less remuneration. Conyon & Mallin (1997) observed that U.K. firms have been slow in adopting nominating committees, a symptom of failure of the corporate governance system. By contrast, audit committee use in the U.K. has been widespread (e.g. Conyon, 1994;

Collier, 1993). The results in Forker's (1992) study suggested that the quality of disclosure is only weakly related with audit committees and non-executive directors.

2.11.6 Managers' Remuneration

The empirical work showed that the role of managers' remuneration in coordinating managers' and investors' interests is limited. Hutchinson and Gul (2003) find a positive role for managers' remuneration, while Coles et al. (2001) do not.

2.12 Empirical Review

Many existing studies in good corporate governance had focused on: the roles of non-executive versus executive members of the board (Pass, 2004), the independence of the board of directors (Zandstra, 2002), the role, independence and disclosure of audit committee (Rezaee *et al.*, 2003), the enforcement of compliance and role of internal auditors (Vinten, 1998, 2000, 2002), altogether grouped into underlying values of corporate governance perspectives being the: accountability (Spira, 2001); integrity (Grant, 2003); efficiency (Walker and Fox, 2002); and transparency (Rezaee *et al.*, 2003).

In an effort to develop a proactive approach, best practice guidelines had been developed and prescribed by major organisations such as the Organisation for Economics Co-operation and Development (OECD) (2004a, b) and through a forum of the World Bank and OECD (2002).Good corporate governance researchers had long and repeatedly revealed how best practice traits play a crucial role in sustaining businesses by promoting transparency, accountability, integrity and efficiency (Parker *et al.*, 2002; Zandstra, 2002; Vinten, 1998, 2000, 2002). For some, these sound very much like conceptual frameworks being launched from an ivory tower. It is not the case, apparently. The studies of corporate governance had also unveiled major corporate failures with problems primarily stemming from improper implementation of good governance principles (Zandstra, 2002; Doost and Fishman, 2004; Boyd, 2003).

2.13 Conclusion

From the literature review, it was concluded that in the case of corporate governance, emerging economies typically did not have an effective and predictable rule of law which, in

turn, created a ‘weak governance’ environment. In most cases, emerging economies had attempted to adopt legal frameworks of developed economies, in particular those of the Anglo-American system, either as a result of internally driven reform or as a response to international demands. The corporate governance structures in emerging economies often resembled those of developed economies in form but not in substance.

The principles of best practice for public pension’s funds largely concerned governance, broadly defined, and were intended to ensure that public pension schemes had clear objectives, were free from conflicts of interest, and are operated in as transparent a manner as possible. Corporate Governance Index was built based on four different aspects of the company's governance structure: CEO duality, Size of the board of directors, Managements' holdings and Block shareholders' holding. Companies approaching stakeholders in a reactive fashion will not integrate their concerns into corporate decision making and take responsibility for their claims.

The aim of corporate governance was to insure that opportunistic behaviour did not occur, by mitigating and moderating agency problems that could involve an agent (manager) and various principals (shareholders, debt holders, employees, suppliers, clients etc.) or else a principal (the main entrepreneur) and various agents (managers, employees, investors etc.). Many researchers had examined the relationship between variety of governance mechanisms and firm performance; however, the results were mixed. Most of these studies in the literature were done in the developed countries whose strategy approach was different from that of Kenya. Further, the studies were done in a different context from that of pension schemes. Thus there was a dearth in literature on corporate governance practices within the pension schemes in Kenya. This study sought to fill this gap in literature by investigating the corporate governance practices within the pension schemes in Kenya.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Research design

The design for this study was a case survey design. The survey design was selected because of the fact that the study was interested in investigating corporate governance practices adopted by pension schemes in Kenya. The survey design was able to give results that were representative of a larger population.

3.2 Population and Sample

The population of study included all the over 1300 registered pensions schemes (Central Bank of Kenya, 2003). Out of the over 1300 schemes, multi-stage sampling was done select a sample of 80 schemes. The first stage was based on major cities of which there were four cities; Nairobi, Kisumu, Mombasa and Nakuru. From these cities 20 pension schemes were selected from each. Multistage sampling enhanced the objectivity of the data obtained. These were the schemes which consist of more than 300 members. These are some of the schemes which have satisfied all the rules in the retirement benefits act and are duly registered. The sector was selected given that there had been a lot of activities going on with some of them facing serious corporate governance problems and as such there was need to study whether the quality of corporate governance in these institutions was sound.

3.3 Data collection

Primary data from the field was collected using semi-structured questionnaires. The questionnaire contained questions on the particular pension scheme and was directed at eliciting corporate governance index of the schemes. The questions contained in the questionnaire was first of all obtain confidential matters on respondents and corporate governance adopted by the schemes then direct questions on ethics and conflict of interest to the respondents. The questionnaire was administered using a drop and pick later method from the respondents desks.

3.3.1 Validity and Reliability

The researcher carried out a pilot study to pre-test and validate the questionnaire. According to Cooper and Schindler (2003), the pilot group can range from 25 to 100 subjects depending on the method to be tested but it does not need to be statistically selected. This was in line with a qualitative research design methodology employed in this research project.

According to Berg and Gall (1989) validity is the degree by which the sample of test items represents the content the test is designed to measure. Content validity which was employed by this study is a measure of the degree to which data collected using a particular instrument represents a specific domain or content of a particular concept. Mugenda and Mugenda (1999) contend that the usual procedure in assessing the content validity of a measure is to use a professional or expert in a particular field.

To establish the validity of the research instrument the researcher sought opinions of experts in the field of study especially the researcher's supervisor and lecturers in the department of educational administration, planning and curriculum development. This facilitated the necessary revision and modification of the research instrument thereby enhancing validity

According to Shanghverzy (2003), reliability referred to the consistency of measurement and is frequently assessed using the test–retest reliability method. Reliability is increased by including many similar items on a measure, by testing a diverse sample of individuals and by using uniform testing procedures (ibid).

The researcher intended to select a pilot group of 10 pension schemes from the target population from the three cities to test the reliability of the research instrument. This was achieved by first stratifying the respondents according to level of management, level of education, number of years worked. The researcher also put in consideration gender equity and geographical background of individuals.

The pilot data was not be included in the actual study. The pilot study allowed for pre-testing of the research instrument. The clarity of the instrument items to the respondents was established so as to enhance the instrument's validity and reliability. The pilot study enabled the researcher to be familiar with research and its administration procedure as well as

identifying items that required modification. The result helped the researcher to correct inconsistencies arising from the instruments, which ensured that they measured what was intended.

3.4 Data analysis

The Corporate Governance Index (CGI) was computed from the recurrence of responses on the data obtained. Each positive answer added one point, so that the final score for each firm ranges from 0 to 15 (worst to best corporate governance quality). The index was built taking into account four dimensions deemed important by the literature to assess corporate governance quality; disclosure, board composition and functioning, ethics and conflict of interest; and shareholder rights. The data was then coded to enable the responses to be grouped into various categories. Data was grouped into frequency distribution to indicate variable values and number of occurrences in terms of frequency. The organised data was interpreted on account of concurrence and standard deviation to objectives using assistance of computer packages especially SPSS and Microsoft Excel to communicate research findings. The results were presented in form of tables. Data was interpreted in terms of mean scores, standard deviations and median.

CHAPTER FOUR

DATA ANALYSIS AND INTERPRETATION

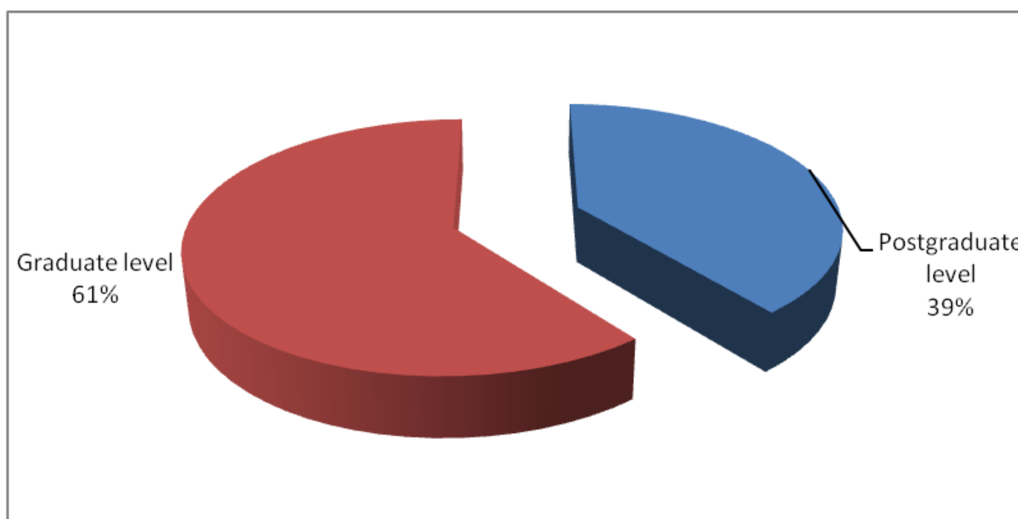
4.1 Introduction

This chapter presents analysis and findings of the study as set out in the research methodology. The study findings are presented on corporate governance practices and firm financial performance the case of pension schemes in Kenya. The data was gathered exclusively from the questionnaire as the research instrument. The questionnaire was designed in line with the objectives of the study.

4.1.1 Response Rate

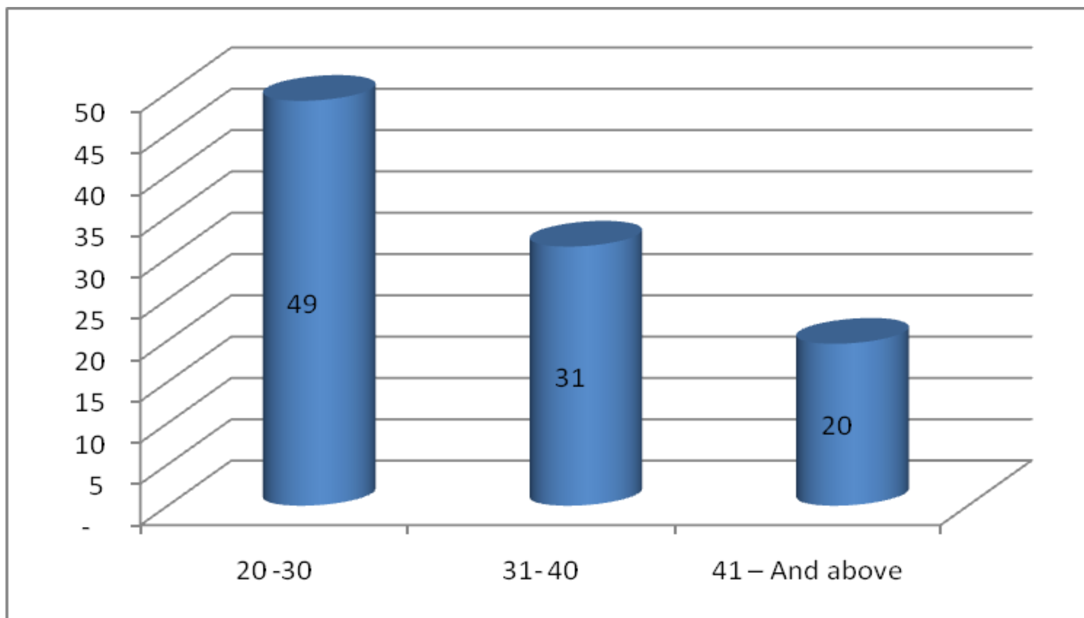
The study targeted 80 respondents in collecting data with regard to corporate governance practices and firm financial performance the case of pension schemes in Kenya. From the study, 51 out of the 80 sample respondents filled-in and returned the questionnaires making a response rate of 63.8%. This reasonable response rate was made a reality after the researcher made personal calls and visits to remind the respondent to fill-in and return the questionnaires.

Figure 4.1: Education level of the Respondents



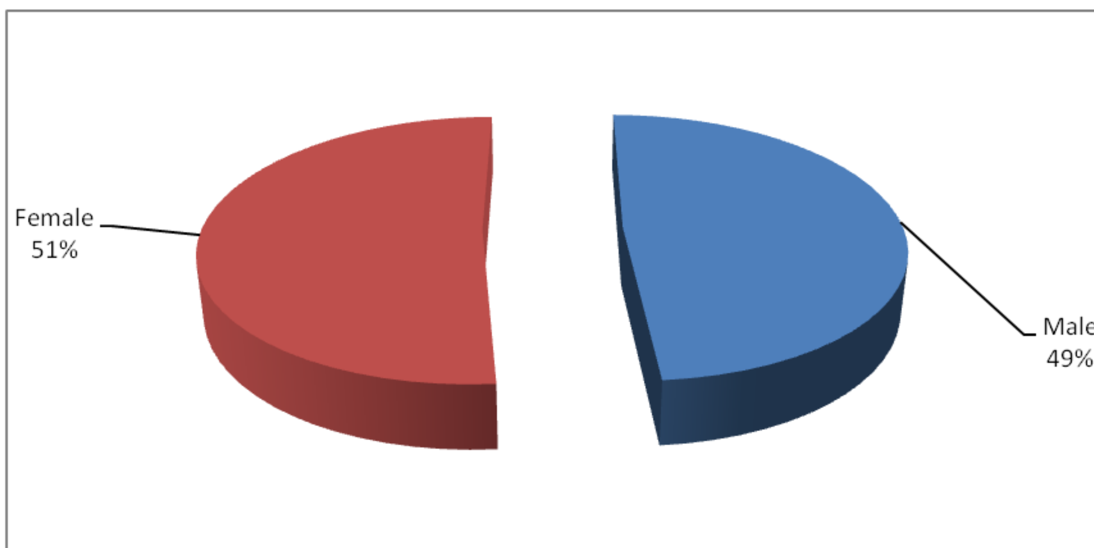
Regarding the highest level of education, that the respondent had achieved, majority (61%) were graduates and 39% had a post graduate degree.

Figure 4.2: Age of the Respondents



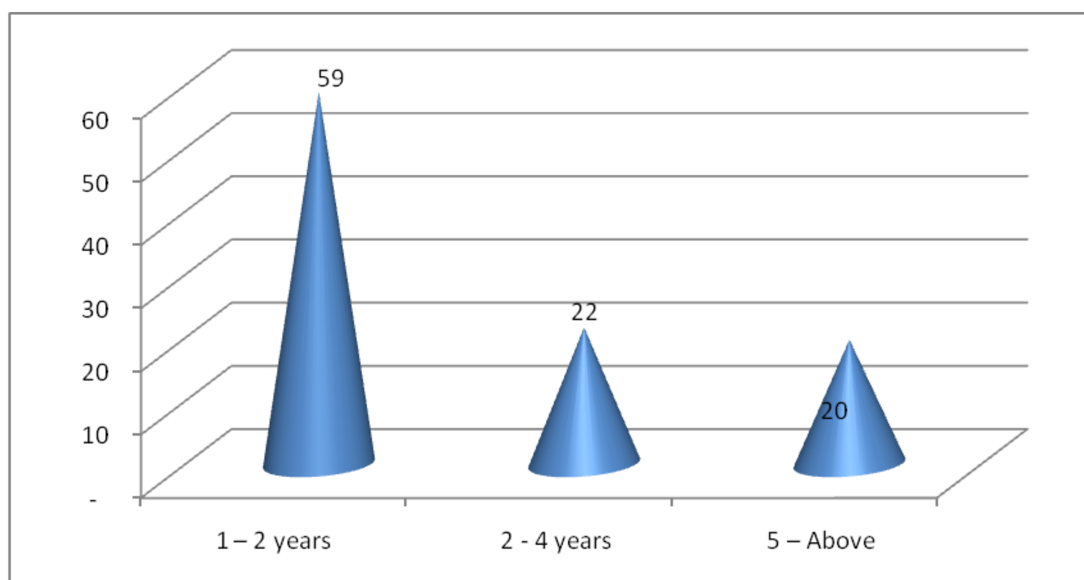
The research sought to find out the age of the respondent. According to the findings 49% of the respondents were aged 20-30 years, 31% were aged 31-40 years and 20% were aged 41 years and above.

Figure 4.3: Gender of the respondents



The research sought to find out the gender of the respondent. According to the findings 51% of the respondents were female while 49% were male.

Figure 4.4: Period that the respondents had been working in the organization



Regarding the period that the respondents had been working in the organization majority (59%) had worked for 1-2 years, 22% had worked for 2-4 years while 20% had worked for 5 and above years.

4.2 Disclosure on Corporate Governance

Table 4.1: Disclosure on corporate governance

CGI questions	**Yes**	**No**
Does the scheme's annual report, website or public disclosure include information about potential conflicts of interest such as related party transactions?	73	27
Does the scheme specify in its charter, annual reports or other means sanctions against management in the case of violations of its desired corporate governance practices?	45	55
Does the scheme produce its legally required financial reports by the required date?	51	49
Does the scheme disclose in its website or annual report compensation information for the CEO and board members?	63	37
Does the scheme have monitoring committees such as a compensation and/or nominations and/or audit committees?	71	29
Is the board of trustees clearly made up of outside and possibly independent trustees?	51	49
Is the board size between 5 and 9 members as recommended by the IBCG Code of Best Practices?	80	20

The study sought to find out the disclosure on corporate governance. According to the findings, 80% of the respondents indicated that the board size was between 5 and 9 members as recommended by the IBCG Code of Best Practices and 73% of the respondents agreed that the scheme's annual report, website or public disclosure included information about potential conflicts of interest such as related party transactions. In addition, 71% of the respondents agreed that the scheme had monitoring committees such as compensation and/or nominations and/or audit committees and 63% of the respondents indicated that the scheme disclosed in its website or annual report compensation information for the CEO and board members. Moreover, 51% of the respondents agreed that the scheme produced its legally required financial reports by the required date and the respondents agreed that the board of trustees was clearly made up of outside and possibly independent trustees. 55% of the respondents disagreed that the scheme specified in its charter, annual reports or other means sanctions against management in the case of violations of its desired corporate governance practices. This implies that corporate governance reports were clearly disclosure.

4.3 Ethics and Conflict of Interest on Corporate Governance

Table 4.2: Ethics and Conflict of Interest on corporate governance

CGI questions	Yes	No
Is the scheme free of any undergoing inquiry regarding governance malpractices	45	55
Is the scheme free of any convictions and/or fining for governance malpractices or other securities law violations in the last five years?	65	35
Does the scheme submit to arbitration in place of regular legal procedures in the case of corporate governance malpractices?	63	37
Does members have a controlling voice in the scheme	55	45
Does the scheme invest funds as per RBA stipulations	65	36
Is there openness in the way books are audited	61	39
Does the scheme has briefings regularly to members	51	49
Do a member has unlimited access to schemes records if he wishes	73	27

The study sought to find out the ethics and conflict of interest on corporate governance. According to the findings, 73% of the respondents indicated that a member had unlimited

access to schemes records if he wished in pension schemes and 65% of the respondents agreed that the scheme was free of any convictions and/or fining for governance malpractices or other securities law violations in the last five years. In addition, 65% of the respondents indicated that the schemes invest funds was as per RBA stipulations and 63% of the respondents indicated that the scheme was submitted to arbitration in place of regular legal procedures in the case of corporate governance malpractices. Moreover, 61% of the respondents indicated that there was openness in the way books were audited and 55% of the respondents agreed that members had a controlling voice in the scheme. Also other 51% of the respondents also agreed that the scheme had briefings regularly to members. Other 55% of the respondents disagreed that the scheme was free of any undergoing inquiry regarding governance malpractices. This implies that pension scheme followed the ethics and conflict of interest on corporate governance.

4.4 Sound Governance Practices

Table 4.3: Extent that the following Factors Enable Pension Scheme to Maintain Sound Governance Practices

Factors	Very great extent	Great extent	Moderate extent	Little extent	Not at all	Mean	Stdev
Corporation's ownership structure	25	71	3.9	0	0	4.2	0.1
Relationships with stakeholders	35	49	13.7	2.0	0	4.2	0.2
Financial transparency	43	51	2.0	3.9	0	4.3	0.4
Information disclosure practices	41	39	15.7	3.9	0	4.2	0.1
Configuration of managing boards	43	39	5.9	5.9	5.9	4.1	0.1

The study sought to investigate the extent to which the following factors enabled pension scheme to maintain sound governance practices. Majority of the respondents indicated that financial transparency enabled pension scheme to maintain sound governance practices to a great extent as shown by a mean score of 4.3 as well as Corporation's ownership structure enabled pension scheme to maintain sound governance practices to a great extent as shown

by a mean score of 4.2. In addition, majority of the respondents also indicated that relationships with stakeholders enabled pension scheme to maintain sound governance practices to a great extent as shown by a mean score of 4.2. Moreover, majority of the respondents indicated that information disclosure practices enabled pension scheme to maintain sound governance practices to a great extent as shown by a mean score of 4.2 and configuration of managing boards enabled pension scheme to maintain sound governance practices to a great extent as shown by a mean score of 4.1. From the findings, it is clear that various factors enabled pension scheme to maintain sound governance practices.

4.5 Corporate Governance Practices

Table 4.4: Extent that the Following Corporate Governance Practices are Focused

Practices	Very great extent	Great extent	Moderate extent	Little extent	Not at all	Mean	Stdev
The composition of the board (i.e. the proportion of inside directors to outside directors)	22	69	2.0		7.8	4.0	0.2
Whether the CEO concurrently holds the position of board chairperson	49	37	5.9	2.0	5.9	4.2	0.2
The size of the board	39	49	7.8	3.9		4.2	0.4
The level and type of director equity held in the company	20	53	27.5			3.9	0.1
The composition of the various board committees	31	51	9.8	3.9	3.9	4.0	0.1

The study sought to investigate the extent to which the following corporate governance practices are focused. Majority of the respondents indicated that the CEO concurrently held the position of board chairperson practice was focused to a great extent as shown by a mean score of 4.2 and the size of the board practice was focused to a great extent as shown by a mean score of 4.2. In addition, majority of the respondents also indicated that the composition of the board (i.e. the proportion of inside directors to outside directors) practice was focused to a great extent as shown by a mean score of 4.0 and the composition of the various board committees practice was focused to a great extent as shown by a mean score of 4.0. Moreover, majority of the respondents indicated that the level and type of director equity

held in the company practice was focused to a great extent as shown by a mean score of 3.9. From the findings, it is clear that various corporate governance practices were focused on in pension schemes in Kenya.

Table 4.5: Level of Agreement with the Following Statements that Relate to Corporate Governance at your Scheme

Statements	Strongly Agree	Agree	Moderately Agree	Disagree	Strongly Disagree	Mean	Std. Dev
Corporate governance best practices at your scheme are intended to enhance board members' ability to discharge their responsibilities – responsibilities to shareholders, the company, and each other.	18	63	17.6	2.0	0	2.0	0.2
Corporate governance is used to direct and manage business affairs of the company towards enhancing prosperity and corporate accounting	25	59	13.7	2.0	0	1.9	0.4
The practices ultimate objective is to realize shareholders long-term value while taking into account the interest of other stakeholders	37	39	15.7	7.8	0	1.9	0.1

The study sought to investigate the extent to which the respondents agreed to the statements that relate to corporate governance at your scheme. From the study, majority agreed that corporate governance best practices at pension scheme were intended to enhance board members' ability to discharge their responsibilities – responsibilities to shareholders, the company, and each other as shown by a mean score of 2.0 and the practices ultimate objective was to realize shareholders long-term value while taking into account the interest of other stakeholders as shown by a mean score of 1.9. In addition, the respondents agreed that corporate governance was used to direct and manage business affairs of the company towards enhancing prosperity and corporate accounting as shown by a mean score of 1.9. This implied that most of the respondents agreed with the statements that relate to corporate governance at your scheme.

CHAPTER FIVE

SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter provides the summary of the findings from chapter four, and it also gives the conclusions and recommendations of the study based on the objectives of the study. The objectives of this study were to establish the corporate governance practices and firm financial performance the case of pension schemes in Kenya.

5.2 Summary of the Findings

The study aimed at investigating the corporate governance practices and firm financial performance the case of pension schemes in Kenya. From 61% of the respondents were graduates who were aged between 20 and 40 years. 51% of the respondents were female while 49% were male. 59% of the respondents had worked in the organization for 1-2 years.

The board size was between 5 and 9 members as recommended by the IBCG Code of Best Practices, the scheme's annual report, website or public disclosure included information about potential conflicts of interest such as related party transactions, the scheme had monitoring committees such as compensation and/or nominations and/or audit committees, the scheme disclosed in its website or annual report compensation information for the CEO and board members, the scheme produced its legally required financial reports by the required date and the board of trustees was clearly made up of outside and possibly independent trustees.

A member had unlimited access to schemes records if he wished in pension schemes, the scheme was free of any convictions and/or fining for governance malpractices or other securities law violations in the last five years, the schemes invest funds was as per RBA stipulations and 63% of the respondents indicated that the scheme was submitted to arbitration in place of regular legal procedures in the case of corporate governance malpractices, there was openness in the way books were audited and 55% of the respondents

agreed that members had a controlling voice in the scheme and the scheme had briefings regularly to members.

Financial transparency enabled pension scheme to maintain sound governance practices, corporation's ownership structure enabled pension scheme to maintain sound governance practices, stakeholders enabled pension scheme to maintain sound governance practices, information disclosure practices enabled pension scheme to maintain sound governance practices and configuration of managing boards enabled pension scheme to maintain sound governance practices.

The CEO concurrently held the position of board chairperson practice was focused, the size of the board practice was focused, the composition of the board (i.e. the proportion of inside directors to outside directors) practice was focused and the composition of the various board committees practice was focused.

Corporate governance best practices at pension scheme were intended to enhance board members' ability to discharge their responsibilities – responsibilities to shareholders, the company, the practices ultimate objective was to realize shareholders long-term value while taking into account the interest of other stakeholders and corporate governance was used to direct and manage business affairs of the company towards enhancing prosperity and corporate accounting.

5.3 Conclusion

The study concludes that corporate governance practices and firm financial performance were practiced in the case of pension schemes in Kenya. These were achieved through disclosure on corporate governance, ethics and conflict of interest on corporate governance, sound governance practices and corporate governance practices which were put in place and followed.

The study concludes that annual reports and legally required financial reports were produced by the required date. The board size of the scheme was between 5 and 9 members as recommended by the IBCG Code of Best Practices. The scheme had monitoring committees to facilitate the disclosure of the pension scheme.

The study also further concludes that ethics and conflict of interest on corporate governance were practiced. This was achieved by member having unlimited access to schemes records if he wished in pension schemes, the scheme being free of any convictions and/or fining for governance malpractices or other securities law violations in the last five years and the schemes invest funds being as per RBA stipulations.

In addition, the study concludes that corporation's ownership structure, relationships with stakeholders, financial transparency, information disclosure practices and configuration of managing boards enabled pension scheme to maintain sound governance practices.

Finally the study concludes that the composition of the board, CEO concurrently holding the position of board chairperson, size of the board, level and type of director equity held in the company and composition of the various board committees were corporate governance practices which were focused in pension scheme. Corporate governance best practices at the pension scheme were intended to enhance board members' ability to discharge their responsibilities – responsibilities to shareholders, the company, and each other.

5.4 Recommendations

This study recommends that the government encourage various people to join the pension scheme since the aim of setting pension was to provide people with an income when they were no longer earning a regular income from employment.

The study also recommends that audit on pensions be done annually to ensure that those who are pensioned are comfortable and their money is safeguarded. The audited accounts should be published in the Kenya Gazette annually.

5.5 Recommendation for Further Studies

This study has reviewed the corporate governance practices and firm financial performance in the case of pension schemes in Kenya and disclosure on corporate governance, ethics and conflict of interest on corporate governance, sound governance practices and corporate governance practices as the practices undertaken in pension schemes to achieve the firm financial performance.

There are other different firms who have opted to adopt corporate governance practices and firm financial performance. To this end therefore a further study should be carried out to establish how other firms adopt corporate governance practices and firm financial performance.

Moreover a study should also be carried out to establish how the pension scheme can participate in improving the corporate governance practices and firm financial performance in Kenya and how the management can be improved in the country as it focuses in the realization of the vision 2030.

5.6 Limitations of the Study

The researcher encountered various limitations that were likely to hinder access to information sought by the study. The researcher encountered problems of time as the research was being undertaken in a short period which limited time for doing a wider research. However the researcher countered the limitation by carrying out the research across all the management levels where respondents were selected which enabled generalization of the study findings on the corporate governance practices and firm financial performance.

The respondents to be approached were reluctant in giving information fearing that the information they give might be used to intimidate them or print a negative image about the organization. The researcher handled the problem by carrying an introduction letter from the University and assured the respondents that the information they gave was to be treated confidentially and it was to be used purely for academic purpose.

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APPENDICES

Appendix I: Introductory Letter

UNIVERSITY OF NAIROBI,

P.O BOX 30197-00100,

NAIROBI

TO WHOM IT MAY CONCERN

Dear Sir/Madam

REF: RESEARCH STUDY

I am a student studying for a Masters in Business Administration student at the University of Nairobi. In partial fulfillment of the requirement to the award of the masters degree, I am required to do and write a research paper. The topic of my research is 'A Survey Of Corporate Governance Practices Within The Pension Schemes In Kenya .

Your organization is one of the main focuses for the study. The choice is based on your strategic importance in the achievement of development goals in the country. I kindly request your assistance by availing time to respond to the questionnaire. Any documentations, reports or journals that you may have that are relevant to this topic of study may be availed to me at your discretion.

A copy of the final report will be made available to you at your request. Your assistance will be highly appreciated. Thank you in advance.

Yours faithfully

Gacheru A.K.

D61/P/8407/2005

Appendix II: Research Questionnaire

Section A: Biographic data

Please fill in the spaces provided with information that is as accurate as is practicable, please tick where appropriate.

1. Please provide your personal information as indicated below.

a) Education level

Postgraduate level [ ]

Graduate level [ ]

Other (specify) [ ]

b) Age: ……………………………………………………………………………….

20 -30 [ ]

31- 40 [ ]

41 – And above [ ]

c) Gender

Male [ ]

Female [ ]

2. What is the name of your pension scheme?

....

3. Designation

…………………………………………………………………………….…………

4. In which department do you work?

…………………………………………………………………………………...

5. How long have you been working in the organization?

   1 – 2 years [ ]

   2 - 4 years [ ]

   5 – Above [ ]

6. Please fill in the following table on corporate governance

Governance Dimension	#	CGI questions	Yes	No
Disclosure	1	Does the scheme's annual report, website or public disclosure include information about potential conflicts of interest such as related party transactions?		
	2	Does the scheme specify in its charter, annual reports or other means sanctions against management in the case of violations of its desired corporate governance practices?		
	3	Does the scheme produce its legally required financial reports by the required date?		
	4	Does the scheme disclose in its website or annual report compensation information for the CEO and board members?		

	5	Does the scheme have monitoring committees such as a compensation and/or nominations and/or audit committees?		
	6	Is the board of trustees clearly made up of outside and possibly independent trustees?		
	7	Is the board size between 5 and 9 members as recommended by the IBCG Code of Best Practices?		
Ethics and Conflict of Interest	8	Is the scheme free of any undergoing inquiry regarding governance malpractices		
	9	Is the scheme free of any convictions and/or fining for governance malpractices or other securities law violations in the last five years?		
	10	Does the scheme submit to arbitration in place of regular legal procedures in the case of corporate governance malpractices?		
	11	Does members have a controlling voice in the scheme		
	12	Does the scheme invest funds as per RBA stipulations		
	13	Is there openness in the way books are audited		

	14	Does the scheme has briefings regularly to members		
	15	Do a member has unlimited access to schemes records if he wishes		

7. To what extent do the following factors enable your pension scheme to maintain sound governance practices?

	Very great extent	Great extent	Moderate extent	Little extent	Not at all
Corporation's ownership structure					
Relationships with stakeholders					
Financial transparency					
Information disclosure practices					
Configuration					

of managing boards					

8. To what extent are the following corporate governance practices focused?

	Very great extent	Great extent	Moderate extent	Little extent	Not at all
The composition of the board (i.e. the proportion of inside directors to outside directors)					
Whether the CEO concurrently holds the position of board chairperson					
The size of the board					
The level and type of director equity held in the company					
The composition of the various board committees					

9. What is your level of agreement with the following statements that relate to corporate governance at your scheme? Use a scale of 1-5 where 1= strongly agree and 5 = strongly disagree.

	1	2	3	4	5
Corporate governance best practices at your scheme are intended to enhance board members' ability to discharge their responsibilities – responsibilities to shareholders, the company, and each other.					
Corporate governance is used to direct and manage business affairs of the company towards enhancing prosperity and corporate accounting					
The practices ultimate objective is to realize shareholders long-term value while taking into account the interest of other stakeholders					