EFFECTIVENESS OF PERFORMANCE CONTRACTS IN REGULATORY CORPORATIONS IN KENYA

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DECLARATION

This is to confirm that this project was initiated and compiled by myself as original work and that it has not been submitted to any other university for examination.

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LIST OF TABLES

LIST OF FIGURES

ABSTRACT

The importance of performance contracting has been adopted as an instrument to reform state-owned enterprise (SOE), granting SOE managers more operational freedom while holding them accountable for the performance of the enterprises through a system of rewards and sanctions. Performance contracts are being used across all sectors in Kenya in public corporations in order to facilitate efficiency of these corporations.

The role of Regulatory agencies is established primarily to ensure justified pricing, equitable access to infrastructure, good quality service and security of supply. Regulatory agencies are also charged with developing rules and methodologies to provide a level playing field for companies wanting to participate and compete in the sector. The cost of these regulatory agencies is ultimately carried by the society and it is thus in everyone's interest to ensure that these regulatory agencies are efficient and effective. And it's under this premise that this study is looking at how effective are these regulatory bodies have been since signing performance contracts, because poorly designed, poorly implemented, or politically driven regulation can have a significant impact on the efficiency and competitiveness of any sector. Regulation has national and regional economic impacts such as attracting foreign capital into these sectors.

The study was carried out through literature review, interview of Financial, Human Resources and Administrative Managers of 26 state regulatory agencies by administering the questionnaires. 33 questionnaires were responsive out of 52 administered to respondents. Data was analysed using MS Excel and presented in tables, pie-charts and percentages.

From the research findings, it was established that the performance contracting has been effective and efficient because there has been more accountability and transparency which contributed to eradication of corruption. To ensure sustainability of the performance contract strategy as a management tool there is need to have legal framework enacted by parliament.

TABLE OF CONTENTS

ACRONYMS

CEO	Chief Executive Officer
CER	Council of European Regulators
EU	European Union
GOK	Government of Kenya
MOU	Memorandum of Understanding
NPM	New Public Management
OECD	Organisation of Economic Cooperation and Development
PC	Public Corporation
PEU	Public Enterprise Unit
PRS	Public Sector Reforms
PSE	Public Sector Enterprise
SC	State Corporation
SCOPO	Standing Committee on Parastatal Corporation
SEB	Swaziland Electricity Board
SOE	State Owned Enterprise
SPTC	Swaziland Postal and Telecommunication Corporation
SWSC	Swaziland Water Services Corporation
USA	United States of America
KIPPRA	Kenya Institute Of Public Policy Research and Analysis
MTEF	Medium – Term Expenditure Framework

DEFINITION OF TERMS

Agency A subordinate entity (public corporation) in the same hierarchy whose performance is evaluated by the principal (government of Kenya) and is responsible for public policies:

Allocation A designation of appropriations by the government of Kenya through administrative executives that delegates spending regulatory body down the chain of command and for specific line items or categories of expenditure.

Audit A process of scrutinising public spending to ensure financial propriety and monitor compliance with rules and regulations. Spending is evaluated against specified purposes, and reviews done to ensure effective controls to enable attainment of stated objectives.

Board of directors The body empowered to carry out functions relating to the overall direction and management of regulatory agencies under this study

Contract plan management tool designed for Senegal for public sector executives and policy makers to define responsibilities and expectations between the contracting parties to achieve common mutually agreed goals.

Memorandum of understanding management tool designed for India public sector executives and policy makers to define responsibilities and expectations between the contracting parties to achieve common mutually agreed goals.

Parastatal Public enterprise, also known as state corporation or state owned enterprise.

Parent ministry A government ministry under which purview the superintendence of a state corporation falls.

Performance contract Is management tool that help public sector executives and policy makers to define responsibilities and expectations between the contracting parties to achieve common mutually agreed goals.

State Corporation Is a public owned enterprise established under a relevant Act of Parliament and operating under the State Corporations Act, Chapter 446 Laws of Kenya.

CHAPTER ONE: INTRODUCTION

1.1 Background

1.1.1 Performance Contracts and Effectiveness

Performance contracts are management instruments used within the public sector to define responsibilities and expectations between parties to achieve mutually agreed results (Armstrong, 2006). As part of the performance orientation in Kenya, the purpose of performance contracting is to clarify the objectives of service organizations and their relationship with government. Performance contracting is also intended to facilitate performance evaluation based on results instead of conformity with bureaucratic rules and regulations The setting of specific performance targets, in a format that can be monitored, is intended to provide a basis for evaluating performance and improving accountability in the public enterprise sector, (Government of Kenya, 2004).

The term Effectiveness looks at whether the program is logically designed to address all mandated and voluntary requirements (design effectiveness), and whether the program is actually operating as designed (operating effectiveness). In this sense, the evaluation helps to determine if the program is delivering required legal and regulatory outcomes and appropriately reflecting the organization's voluntary promises regarding its approach to governance, risk and compliance. This is the evaluation contemplated by the performance contract guidelines and is a critical process to undertake (Trivedi, 2004).

The relationship between performance contracts and effectiveness is that one of the requirements of performance contracting is to later analyse and gauge the results or the output of the parties who have signed the contract. And this would indicate the effectiveness of the contract as whether the performance was better or poor. So in order to assess the effectiveness of performance contracts, evaluation is necessary. Performance evaluation is the most critical stage in the process of performance contracting. It underlies the all-important paradigm that "what gets measured gets done". It involves assessment of the extent to which public regulatory agencies have achieved agreed performance targets (Trivedi, 2004).

Evaluation of the performance of government agencies falls under the approach which is based on measurement of achievements against targets agreed upon at the beginning of a contract period. Usually it involves a formal agreement and it is most common in professionally run organizations. And the other approach involves measurement of achievement based on the criteria and targets developed at the end of the performance period. It is more comprehensive and useful for future projects (Trivedi, 2004). In this paper performance contracting is used as a management tool to help public sector executives and policy makers to define responsibilities and expectations between the contracting parties to achieve common and mutually agreed goals

1.1.2 Regulatory Corporations

Regulatory agencies or corporations in Kenya are established under the State Corporations Act, Cap 446 of Laws of Kenya. They are responsible with issuing operating licences, supervise, and implement various applicable rules in order to protect and safeguard Kenyan citizens' interests. There are 26 registered regulatory corporations in Kenya. The operations of these corporations seeks Independence in operations from political influences, freehand on enforcement powers or authority on the fields they regulate where by they have been given the mandate to enforce the law without being subjected to legal tussles, Transparency and accountability on how they apply regulatory rules to every entity which falls under their mandate, (Brown, Stern, Tenenbaum, & Gencer, 2006).

Kenya has got independent regulatory agencies with distinctive roles. Thus much is expected of them in service delivery through enhanced accountability. It's due to this subject of performance that this study looks at how effective are performance contracts in enhancing better services. Much of this paper will dwell on counter-analysing regulatory governance arrangements and the benchmarks set by performance contracts. It will investigate whether they have resulted in outcomes that have met the expectations of consumers, operators and investors in Kenya. Have appropriate regulatory models been selected? Has implementation of PC been effective? Ultimately the question is whether regulation facilitates appropriate balance between development and investment outcomes: i.e. are consumer and country benefits advanced while maintaining the financial health of utilities and incentives for further investment?

1.2 Statement of the Research Problem

The importance of performance contracting is to clarify the objectives of service organizations and their relationship with government, and to facilitate performance evaluation based on results instead of conformity with bureaucratic rules and regulations, (Mallon, 1994). Performance contracting between governments and public corporations is increasingly being applied as an instrument for restructuring public corporations and for managing the government-public corporation interface. It is through performance contracting that such autonomous regulatory agencies can be held accountable on their output, (Jones & Khullar, 1994). The use performance contract is one of a number of policy strategy that the government of Kenya has adopted in its efforts to improve the performance of public enterprises as they specify enterprise objectives in terms of the desired socio-economic impact of goods and services; production goals, quantity and quality of services to be provided during the period of the agreement.

The effectiveness of performance contracting of public enterprises lies, inter alia, in maintaining a meaningful balance between autonomy and control. In other words, while operating as autonomous and self-regulating organizational entities, measures should be evolved to ensure that public enterprises conform to specific standards, such as those of efficiency, accountability, responsibility and service to the public (Wamalwa, 1991). It is imperative therefore that contract plans should clarify what public enterprise management may do with or without government approval and what prices enterprises may levy for a variety of goods and services.

There is a need to assess the effectiveness of performance contracting of state regulatory agencies because they have the responsibility to protect Kenyan citizens from various sector malpractices and for that reason they must remain (regulatory agencies) effective by maintaining high standards of responsiveness and the degree to which it delivers business outcomes that go beyond legal and regulatory requirements, and it is the foregoing review that the researcher examines the effectiveness of performance contracting on regulatory state corporations with the hope of recommending more effective performance management practices that would lead to better governance and management.

Some few studies have been done regarding the effectiveness of PCs in Kenya's state corporations in general but not specifically on regulatory corporations. Much of the literature reviewed relate to the research on performance management and agency governance by Balogun, (2003), which is close to study done by Kiringai, and West (2002) on the performance contracting in reviving state corporations; and the Budget Reforms and the Medium-Term Expenditure Framework (MTEF) in Kenya (Working Paper No. 7) by the Kenya Institute of Public Policy Research and Analysis (KIPPRA, 2002). The KIPPRA paper highlights on the importance of MTEF in enhancing corporations' performance evaluation.

There is a near consensus on the main responsibilities of regulators. The research identifies three: to protect consumers from abuse of market power, to support investment by protecting investors from arbitrary action by government, and to promote economic efficiency. But the regulation sector is technically complex, contentious, and politically intricate, to function effectively and achieve goals in such an environment, certain characteristics are desirable for a regulatory agency. These characteristics include: Independence, Enforcement powers, or authority, Transparency, accountability and Competency and as for this case, the study analyses; is performance contracting effective enough in improving service delivery by regulatory state corporations?

1.3 Research Objective

The objective of the study is to assess the effectiveness of performance contracts in regulatory state corporations.

1.4 Significance of the Study

Academically, this study brings forth to scholars the importance of enhancing efficiency through performance contracting as this research tries to gauge the effectiveness it has on the performance of regulatory agencies in Kenya. Also, it highlights to academicians various methods which will help in facilitating new public management systems which will help SOE in Kenya perform effectively.

The research highlights problem areas in performance contracting that require immediate attention by management in state corporations if the strategy is to be most effective. The Kenyan government may also use the research findings to improve the efficiency and effectiveness of management in state corporations in order to meet the expectations of both the public and government.

This study highlights on the shortcomings of performance contracting in regulatory state corporations and recommend most probable way how to enhance performance of regulatory state corporations.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

In this chapter the process involves locating reading and evaluating reports of previous studies, observations and opinions related to the planned study It is a continuous process in a dynamic way, the review helps to clarify, strengthen and direct each stage of the research from formulation of each topic to the mechanism for the dissemination and utilization of the research findings.

2.1.1 Definition of Concepts

The research is based on two concepts that is, performance contracting and effectiveness regarding to regulatory state corporations in Kenya.

A Performance Contract is a freely negotiated performance agreement between Government, acting as the owner of an Agency, and the management of the agency, It is a management tool that organizes corporate objectives into simple, monitor-able and measurable performance criteria, which are measured using clear indicators against negotiated performance targets, at the end a specified contract period (Trivedi, 2004). A performance contract clearly specifies:

- The intentions, obligations, responsibilities and powers of the parties;
- It addresses economic/social/other tasks to be discharged for economic or other desired gain;
- It organizes and defines tasks so management can perform them systematically, purposefully and with reasonable probability of achievement;
- PCs assist in developing points of view, concepts & approaches to determine what should be done and how to go about doing it;
- It imparts operational and managerial autonomy to Government agencies;
- Reduces quantity of controls and enhances the quality of service;

Effectiveness looks at whether the program is logically designed to address all mandated and voluntary requirements (design effectiveness), and whether a performance contract is actually operating as designed (operating effectiveness). In this sense, the evaluation helps to determine if a contract is delivering required legal and regulatory outcomes and appropriately reflecting the corporation's voluntary promises regarding its approach to governance, risk and compliance (Grapinet, 1999). This is the evaluation contemplated by the Performance Contract Guidelines and is a critical process to undertake. So the research will start by looking at why performance contracts were introduced in state corporations and in this case is the poor performance in service delivery.

2.2 Poor Performance of State Corporations

From the outset SOE financial and economic performance generally failed to meet the expectations of their creators and funders. 1965-80 (and beyond) there were SOEs that performed, at least for a time, adequately and sometimes very well, by the most stringent of standards (e.g., Ethiopian Airlines, the Kenya Tea Development Authority, Sierra Leone's Guma Valley Water Company). But the good performers were heavily outnumbered by the bad (Nellis, 2006).

In twelve West African countries, 62 percent of surveyed state owned enterprises (SOEs) showed net losses, and 36 percent were in a state of negative net worth. (Bovat, 1985)By the end of the 1970s, cumulative SOE losses in Mali amounted to 6 percent of GDP. A 1980 study of eight Togolese SOEs revealed that losses in this group alone equalled 4 percent of GDP. In Benin, more than 60 percent of SOEs had net losses; more than three-fourths had debt/equity ratios greater than 5 to 1; close to half had negative net worth, and more than half had negative net working capital, (Grosh & Mukandala, 1994). A 1985 survey of transport sector SOE performance in 18 francophone African countries found that only one-fifth generated revenue sufficient to cover operating costs, depreciation and financial charges. Another fifth covered variable costs plus depreciation but not finance charges; a further 40 percent covered only operating costs, while the final fifth were not even covering these. While few other economic studies undertaken in this period singled out infrastructure SOEs, their relatively large economic and financial size, evidence, suggests that they were major contributors to the low level of general performance

2.3 Causes of Poor Performance

Many studies of this period looked into the causes of poor SOE performance. The diagnosis was that the fundamental problem of SOEs, was multiple and conflicting objectives. Government owners decreed that their SOEs operate in a commercial, efficient and profitable manner, and at the same time insisted that they provide goods and services at prices less than cost-covering levels, serve as generators of employment, receive their inputs from state-sanctioned suppliers, choose plant location on political rather than commercial criteria, etc. The mixing of social with commercial objectives inevitably led to political interference in operational decisions to the detriment of managerial autonomy, commercial performance, and economic efficiency.

2.4 Performance contracting

Despite more than a decade of divestiture and reform, many developing countries continue to have large, poorly performing state-owned enterprises that contribute to fiscal deficits and slow growth. In response, most governments are searching for ways to enhance efficiency and reduce their fiscal burdens. These efforts include rewriting the contract between the government and the firm by changing the explicit or implicit agreement between the government and the enterprise management based on shared expectations about obligations and outcomes, (Shirley M. M., 1996). Performance contracts set targets for SOE managers to attain. Many also provide bonuses for management and workers based on achievement and pledge the government to provide greater autonomy or meet other obligations.

(Larbi, 1999), defines PCs as a management tool to help public sector executives and policy makers to define responsibilities and expectations between the contracting parties to achieve common mutually agreed goals. The new institutional perspective in public sector management is reflected in the public choice theories and in the policy prescriptions. Performance contracting between governments and public corporations is increasingly being applied as an instrument for restructuring public corporations and for managing the government-public corporation interface. Underlying performance contracting and in line with New Public Management (NPM), is the belief that while granting public corporations management operational autonomy, there is a need to hold them accountable for their performance.

Trivedi (2004), further explains that the presence of performance contracts ideally prevents the vicious cycle of the *"Not Me"* syndrome. The syndrome depicts a situation whereby no one wants to be blamed for the management problems facing state corporations. He further explains that in order to break this vicious cycle of blames, a performance contract should be installed to improve the correlation between planning and implementation, coordination between various government agencies, create an enabling public policy environment for other downstream reforms. Trivedi (2004) stresses that an effective performance improvement system should have the following salient features for successful governance of an enterprise.-Performance information system, Performance evaluation system and Performance incentive/sanctions system.

The strongest current performance-oriented trend in the Organisation of Economic Cooperation Development (OECD) countries is to use performance-based management, budgeting, and reporting. Australia and New Zealand were the first to begin the present round of performance management and/or budgeting in the late 1980s, followed in the early to mid 1990s by Canada, Denmark, Finland, France, the Netherlands, Sweden, the United Kingdom and the United States. In the late 1990s to early 2000s, Austria, Germany and Switzerland in their turn introduced versions of these reforms (Trivedi, 2004).

Performance contracting principles are relatively general. All around the world, issues in the reform of regulatory governance include the designation of regulatory authorities, the definition of their powers, of guarantees against unmotivated removal, and of financial autonomy, the choice of the tariff-setting formula, the fora to arbitrate controversies, and the role of the existing antitrust authority in monitoring access to networks and competition in the liberalized markets. In developing countries, agencies may be more permeable to the temptation of kick-backs, as the state is weak and civil servants' salaries are often low in absolute terms and always lower than in regulated firms. The recipe is therefore rather simple: introduce meritocratic recruitment and pay competitive salaries. A final issue concerns the degree of discretion. While clear mandates which

specify limits, either through licenses or through legislation, may reduce the risk of expropriation, rules such as price caps and incentive schemes demand some flexibility in order to adapt to ever-changing technology and demand circumstances (Goldstein & Pires, 2001).

2.5 Empirical Analysis

The role of the regulator with respect to the ministry is more difficult to assess. In general, there is agreement that the ministry will remain in charge of policymaking while the regulator will administer licenses and set tariffs. But clearly, regulators are likely to have valuable input in policy debates and the ministry (or the government) has great interest in tariffs paid by the "voters." Unfortunately, too often governments undermine the regulator on the issue of setting end-user prices. For new regulators trying to establish their legitimacy, this interference can have a lasting negative effect.

2.6 Effectiveness of Performance Contracts

An effective performance of regulators in carrying out their functions is evaluated based on how well they meet their responsibilities. These functions are difficult to evaluate as they are often qualitative and subjective such as: To measure the effectiveness of a regulator, performance evaluation is necessary and it is the most critical stage in the process of performance contracting. It underlies the all-important paradigm that "what gets measured gets done" It involves assessment of the extent to which public regulatory agencies have achieved agreed performance targets. Citizens judge and evaluate government activities in a variety of ways, but the acid test of how well a government is performing is the degree to which citizens gain benefits from the spending and regulatory activities. Ultimately citizens judge government not by intentions but by results (Trivedi, 2004).

Evaluation of the performance of government agencies falls under three broad categories; the Ex-ante versus the Ex-Post; managerial versus agency performance; and results-based monitoring and evaluation system (Trivedi, 2004).

Jones and Khullar, (1994), explain that evaluating the performance of any organization is a notoriously difficult task. The problems are compounded for public enterprises characterized by

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[illegible] and Khullar, (1994), explain that evaluating the performance of any organization is a [illegible]sly difficult task. The problems are compounded for public enterprises characterized by multiple objectives, plural principals and limited autonomy. Performance evaluation is thus both an art and science requiring wisdom and judgment on the one hand and facts and theory on the other. Unlike in private enterprises, in government the system of goals and incentives is different and, with few exceptions, the managers of government agencies have no general indicator of the effectiveness of their choices or the efficiency of their performance comparable to the profit and loss statement. Measures of productivity calculated for individual agencies do reflect the efficiency with which the agencies produce their service output.

2.7 Challenges in Performance Contracting

Performance contracts have not always been an easy process to implement, while the overall design of the contract meets most international standards (and national legal requirements), some challenges have become evident. It should be noted that despite all the efforts and best intentions of all the parties involved in contract implementation and compliance monitoring, there will always be certain conflict situations or risks for which no mitigation measures have been provided in the contract, (Kobia & Mohammed, 2006). A contract cannot regulate every single aspect of such complex relations. Hence, the human factor, such as the parties' willingness to cooperate and find a solution, is important. Nevertheless, the smooth operations and implementation should rely on sound contractual arrangements.

Some of the challenges of performance contracts lie with the difficulties of measuring performance indicators: some performance indicators may not be representative of the real performance of the operator over the service area because the control points are not properly selected. Also there is lack of precision of certain aspects of and terms in the contract: although the contract is rather comprehensive and covers all major issues, numerous amendments have to be made in order to suit a particular objective of the corporation.

According to Kobia and Mohammed, (2006) who did a research on performance contract experiences in Kenya most state corporations are not assigned adequate resources needed to meet performance contract targets. They concluded their research indicating that some of the problems experienced during the implementation of the performance contract include lack of adequate resources, resources not being released on time; some performance targets were highly ambitious and unplanned transfer of staff.

Other instances where performance contracts have failed is in Swaziland. In Swaziland the formulation of contract plans is allowed to be the prerogative and/or domain of outside consultants with little, if any, involvement in the process by enterprise management and staff. This situation is unfortunate, given the fact that, more often than not, the management and staff of public enterprises shoulder the enormous burden of implementing the provisions of performance contract agreements (Musa, 2001). In Swaziland, they used consulting companies to implement performance contracts.

Because of the widespread use of consultants in the formulation of contract plans, including the determination of mechanisms for their monitoring and evaluation, public enterprise management did not develop the necessary sense of ownership and commitment to the success of the enterprise contracts, (Nellis, 2006).

Another problem with regard to the formulation and implementation of contract plans in Swaziland centres around the role and commitment of the contracting partners, especially the fact that the government and/or controlling ministries are the weakest link in the tripartite administrative structure. While public enterprise management appreciate the utility of performance contracts, this is not the case with controlling ministries which often do not show commensurate enthusiasm, thus either delaying the process or frustrating it altogether, much to the detriment of the effective operation of the parastatal sector.

Another impediments to performance contracting is politicising the idea of performance contracts where by politicians and organisations managers and leaders go to lengths to dismiss and question the integrity of performance contracts in order to win the support of the targeted persons by performance contracts, other politicians have argued that performance contracting programs are ill-motives of donor countries trying to manipulate a country's governance to their tune, (Gülen, Makaryan, Volkov, & Foss, 2006) .

2.8 Various Experiences with PCs

Various countries have engaged the premise of performance contracting in order to improve the effectiveness of their state corporations. Such countries include United States of America, France, Ghana, Morocco, Swaziland, Tanzania, Senegal, South Korea, India, Portugal, Denmark, Finland, New Zealand and others. For the purpose of this study, a keen reflection is onto France and New Zealand.

2.8.1 Performance Contracts in France

The concept of performance contracts was first introduced in France in 1967. The initial contracts were drawn between the government and the French Railways (SNCF) and Electricity de France (EDF) in 1969 and 1970 respectively. France went through four phases of the contract system in less than two decades. Some of the reasons cited for the break down of the contracts were unexpected change in macro-economic conditions and political interference whenever it appeared to be convenient (Trivedi, 2004).

This system aimed at improving public sector performance was put in place, using management indicators to measure mission productivity, quality and efficiency. In practice, directorates at local government level are now being managed through performance contracts.

These changes were made possible by giving a freer hand to directors and heads of local services at local government level. In order to encourage initiative, responsibilities were delegated to the decision-making levels closest to staff and users. Every ministry in the French Government is free to use the management methods it deems best suited to its mission and to the structure of its operational services. (Grapinet, 1999).

Despite the successful French experience outlined above, it should be emphasized that the optimal contractual form is the country and cultural specific. This depends on such factors as trust, type of transaction, objectives, legal and administrative limitations, risk management and institutional history. The development levels of socio-cultural, economic and political systems in France, for instance, are not only different but also unique from those in Kenya (Kobia & Mohammed, 2006).

2.8.2 Performance Contracts in New Zealand

Since 1984, New Zealand has undertaken a bold and rapid programme of reforms of both its economic policy and its public sector management systems. Changes to economic policy were driven by a need to address the faltering economy and move away from the pervasive and rigid government interventions and controls in the economy that were its characteristic, particularly in the early 1980s (Shirley & Xu, 1997).Public sector reforms were driven by a growing concern that the government's own management practices were adversely affecting macroeconomic performance and the achievement of its own priorities.

As expressed by (Easterbrook-Smith, 1999), a number of converging factors provided a fertile environment for the changes:

- The economy was faltering. While in the 1960s, New Zealand's per capita income ranked it amongst the highest in the OECD community, by the 1980s it ranked amongst the lowest.
- The 1984 Parliamentary election brought to power a new Labour Government with its new generation of leaders committed to making significant changes to economic and state sector management.
- Concern about the management system was growing within the public sector, particularly amongst managers frustrated by the excessive controls over all aspects of their work. The need for fundamental public sector reform was well identified.

The convergence of these factors provided a unique opportunity in New Zealand for the reforms to proceed in a bold and comprehensive way. Without these factors, reform would probably have been more modest and piecemeal. Instead, changes introduced saw a significant redefinition of the government's role in the economy and society as a whole

As a first stage, government's controls and interventions in the economy were reduced or abandoned. A second stage saw the government begin to withdraw from managing commercial activities. These activities were now established as State-Owned Enterprises operating in commercially competitive markets. New arrangements which empowered boards to run the enterprises and managers to be responsible for their areas of work without regard to public service rules brought dramatic gains in productivity, improvements in customer services, lower prices and higher returns to shareholders.

The success of managerial accountability in State-Owned Enterprises encouraged the reformers to extend the principles to the core State sector. As a next stage to the reforms, comprehensive changes to the systems of government management were introduced. These were influenced by several key principles presented by the Treasury to the Labour Government following its 1987 election victory.

The government responded. Legislation passed in 1988 (the State Sector Act) and 1989 (the Public Finance Act) laid the foundation for a comprehensive management framework which includes performance contracting for its departments and other agencies that make up the state sector. The new regime provided chief executives with broad authority to run their organisations, recruit staff, use appropriated funds to produce agreed outputs, decide on the optimal mix of inputs to deliver those outputs, and report on achievements, (Easterbrook-Smith, 1999).

With this freedom to manage came increased responsibilities and the need to ensure that managers were accountable for these responsibilities. To this end from the late 1980s, performance-contracting arrangements were widely applied throughout the public sector, (Easterbrook-Smith, 1999).

The New Zealand public sector reforms have been concerned not only with structures and systems, but also with roles, responsibilities, and relationships in pursuit of performance improvement. Nearly ten years on, the performance system adopted in New Zealand has shown pleasing results. It continues to be reviewed and adapted to assist managers to improve their performance and that of their organisations in meeting the government's objectives

2.8.3 Desired Characteristics of a Regulator

The sector of regulation is technically complex, contentious, and politically intricate even for experienced regulators let alone newly established ones in developing countries. To function effectively and achieve goals in such an environment, certain characteristics are desirable for a regulatory agency such as independence, enforcement powers or authority, transparency, accountability and competency.

2.9 Conceptual Framework

The key trend in the new public management approach in most states is the increasing resort to performance contracting although different terms are used in different countries for performance contracting. In India, the term *memorandum of understanding* is used (Trivedi, 2004). In Senegal, the term *contract plan* is used, while in Pakistan, *signalling system* is used (Navarro, 1996). Bolivia, Kenya and Ghana use the term, *performance contract*. As part of the performance-orientation in government, the common purposes are to clarify the objectives of service organizations and their relationship with government, and to facilitate performance evaluation based on results instead of conformity with bureaucratic rules and regulations problems of SOEs, divestiture or complete privatization, and restructuring without change of ownership (Mallon, 1994).

Managing the interface between government and state owned enterprises (SOEs) has tended to be problematic in developing countries, reflecting the difficulty of balancing control and autonomy. Excessive controls and frequent political interventions and policy instability are some of the institutional problems of SOEs cited in the literature (Shirley (b), 1989)

In line with the new institutional perspective in public sector management reforms, as reflected in agency and public choice theories, and in the policy prescriptions based on them, performance contracting between governments and SOEs is increasingly being applied as an instrument for restructuring SOEs and for managing the government-SOE interface..

Figure 1 elaborates the conceptualisation of this study as it demonstrates how performance contracts can be used to achieve objectives of a state corporation through the formulation of resource allocation plans, and management of resources within a defined framework.

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Conceptual

Framework

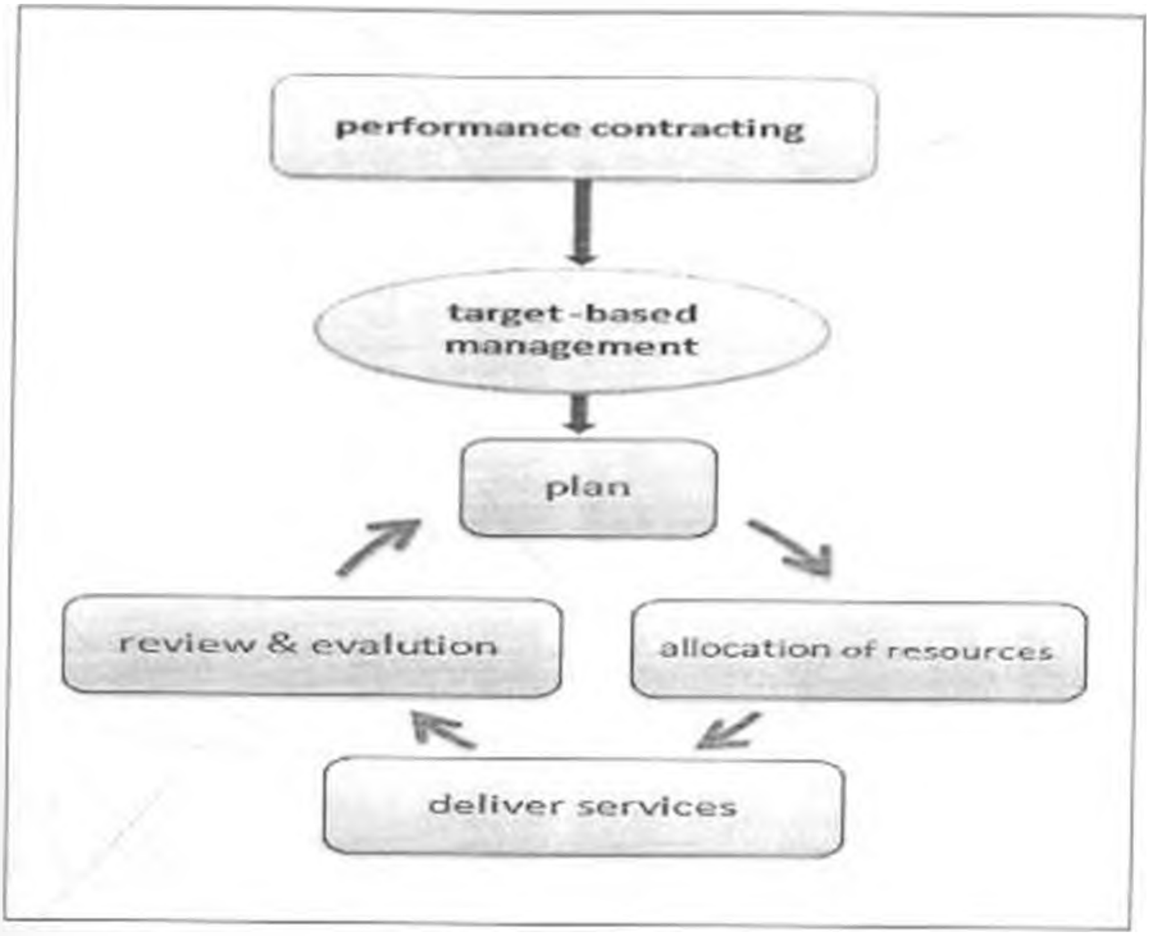


Figure 1; Conceptual Framework

Source; Trivedi 2004

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter profiles process and method to test the proposed research questions of the study. It details the research design and research method adopted which tries to address the goals and objectives of the study as well as the pertinent research questions. Also, the various methods adopted in obtaining information and data from the target respondent are elucidated. For effective interpretation of findings, the data and information generated was subjected to numerical and qualitative analysis.

3.2 Research Design

The research strategy adopted in this study was the survey technique. This strategy was appropriate because of the nature of the research topic which demands the collection of significant amount of data from a meaningful population size in an efficient manner and this method is well understood and perceived as authoritative by people in general. The researcher also used qualitative approach in order to generate in-depth information from respondents to precisely reveal their perceptions, expectations, feelings and beliefs.

3.3 Target Population

The study population comprised of 26 regulatory state corporations currently operating under performance contracting terms and evaluated by the end FY 2007/2008. The choice of population for the study was informed by the need to extract relevant information

3.4 Data Collection

Data was collected through a questionnaire. A sample of the questionnaire is attached (see Appendix I)

The Table 1 shows the desired representation from the regulatory state corporations in the population.

Table 1: Regulatory states corporations' representation

Population category	Respondents from each SOE	Registered regulatory state corporation	Sub-total of respondents
Management	2	26	52
Total	2	26	52

3.4.1 Questionnaire

A questionnaire designed contained both open and closed ended semi-structured questions, which was to be administered to the target respondents. The main advantage of using this method for collecting primary data was its versatility. It allows collection of large amount of data from the target respondents. It's also fast and saves time. The open-ended question allows the respondent to give in-depth information on the subject of interest

In order to improve on the value of the survey results, the questionnaire and interview schedules were be pre-tested in order to gauge the following:

- Respondent Interest--It is important to discover the respondent reactions to the questions.
- Meaning — Are the wordings of the questions meaningful and readily understood by respondents?
- Continuity and Flow--Questions should read effortlessly and flow from one to another and from section to section.

3.4.2 Respondents

The research identified the managers as the respondents since they are the ones who prepare and implement performance contract. Therefore the respondents, who serve in any managerial position such as in finance, human resource, administration, procurement, operations, communications, research and development, compliance departments and others were interviewed. It was the target of the research at least to get two responses from the identified managerial departments from the 26 regulatory corporations.

3.5.3 Questionnaire Administration

The questionnaires needed face-to-face administration The author identified the most appropriate way of contacting the various respondents for example booking a prior appointment if it was required or the questionnaires were sent to their respective locations for the respondents to answer the questions at their own appropriate time and then the research will collect the questionnaires upon completion.

3.6 Data Analysis

The data collected in the study was both quantitative and qualitative and which was later summarized and analysed. The data was interpreted during which a description of results was undertaken and the results presented in the form of pie charts and tables.

All the returned questionnaires were checked for reliability and verification by continuity and flow of respondent's response to the questions in the questionnaire. The researcher generated information by analyzing data using qualitative and quantitative techniques. This involves reducing accumulated data to a manageable size by developing summaries, looking for patterns and applying statistical techniques and then use pie charts, percentages, graphs and tables among others where applicable.

CHAPTER FOUR: DATA ANALYSIS AND PRESENTATION

4.1 Introduction

This chapter presents the findings of the study based on the research questions. It is divided into sections and presents analysis an

d findings of the research study. The findings reflect the opinions of respondents regarding the effectiveness of performance contracting. The respondents were the personnel working in managerial positions. The data emerging from the study is descriptively presented with the aim of offering a detailed analysis of the information collected regarding the impact of performance contracting in Kenya's state corporations.

The objective of the study was that to find out the effectiveness of performance contracting in state corporations which are involved in the regulating the market and to help in the realizing the objectives the study did a field research whereby the managers of various departments were interviewed on their opinion regarding to effectiveness of performance contracts. The research target population comprised of 52 managers trickling down to two managers from each corporation The responses are elaborated below;

Table 2: Response Rate

The targeted population and the responses obtained	
Target respondents	actual respondents
52	33

The research managed to get responses from 33 managers and their opinions and responses have been analysed below in terms of tables and charts. The responses were analysed and summarised basing on the questions expressed in the questionnaire. Some responses on some questions were combined in order to achieve a simplified synopsis of the whole research.

4.2 Understanding Performance Contracts

The respondents were asked whether they understood clearly what performance contracts were and to the extent of knowing what the requirements are in terms of the goals and objectives. All of the 33 managers said that they understood what performance contracts were and what's expected of them in terms of goals and objectives. When the respondents were asked further whether the measures expressed in the performance contracts were well defined and easy to understand, 24 respondents said Yes, 7 respondents said they Some-How understood the measures while the remainder of 2 respondents said No. Their responses are illustrated in table 3 and figure 2.

Table 3: Understanding Performance Contracts

Understanding the measurement of performance contracts			
Yes	Some how	No	Total
24	7	2	33

Figure 2: Understanding Performance Contracts

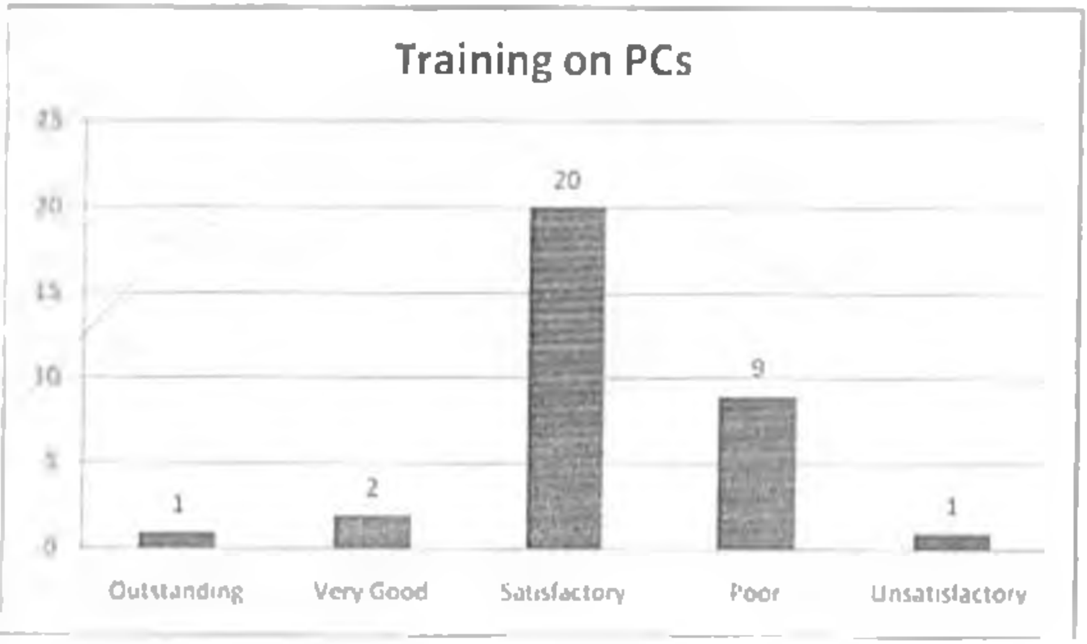
4.2.1 Training on Performance Contracts

The research sought to find out whether the managers have gone in any training regarding to how to handle performance contracts and how to utilise the requirements of the same contracts in their management of operations within their respective agencies. All the respondents said they have undergone some training on the requirements of performance contracts The question further asked them to rate the level of the training they received and one respondent said it was Outstanding, 2 said it was Very Good, 20 of the respondents said the training was Satisfactory, 9 said it was Poor while the remaining person (1) said it was Unsatisfactory.

Table 4: Training on Performance Contracting

Training on Performance Contracts					
Outstanding	Very good	Satisfactory	Poor	Unsatisfactory	Total
1	2	20	9	1	33

Figure 3: Training on Performance Contracts



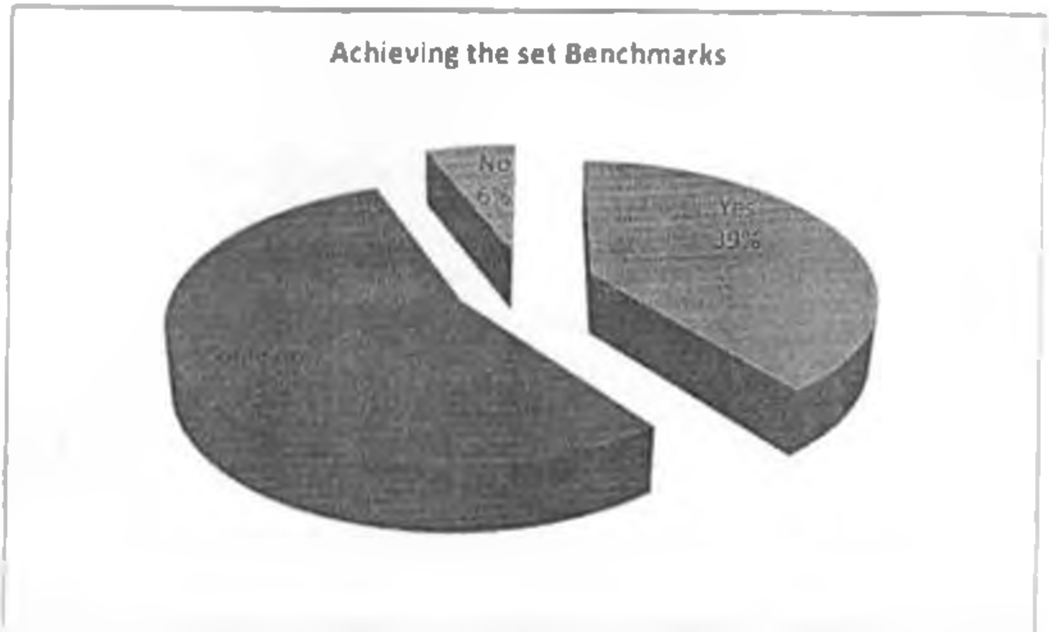
4.2.2 Achieving the Set Benchmarks

The research asked the respondents whether the indicators that are expressed in the performance contracts do really reflect achievable benchmarks in their agency and the following results were obtained from 33 respondents.

Table 5: Achieving the set Benchmarks

Do the set benchmarks set on PCs achievable			
Yes	Some-how	No	Total
13	18	2	33

Figure 4: Achieving the set Benchmarks



From the figures above it shows that 13 respondents think that the benchmarks set in the performance contracts are achievable, 18 respondents said that the benchmarks were Some how achievable while 2 respondents of the 33 respondents said the benchmarks were Not achievable.

4.3 Effectiveness of Performance Contracts

4.3.1 Customers' Confidence on Regulators

The respondents were asked to rate the level they thought customers would place them in regulating the market. In this question, managers were to relate to the trust, integrity, and the confidence that customers have in them in protecting them from various players in the market.

Out of the 33 responses obtained, 12 managers said they feel that customers are satisfied the way they regulate the market, 17 of the respondents said that customers rating would put them at Very Good while the 4 represented those who felt that customers would place their regulatory services at Outstanding performance. But none of the respondents said their performance was poor or unsatisfactory. The responses are illustrated in table 6 and figure 5.

Table 6: Customer's Confidence in regulatory agencies

Customer's confidence in regulatory bodies in performing their duty					
Outstanding	Very good	Satisfactory	Poor	Unsatisfactory	Total
4	17	12	0	0	33

Figure 4: Customers' Confidence in Regulators

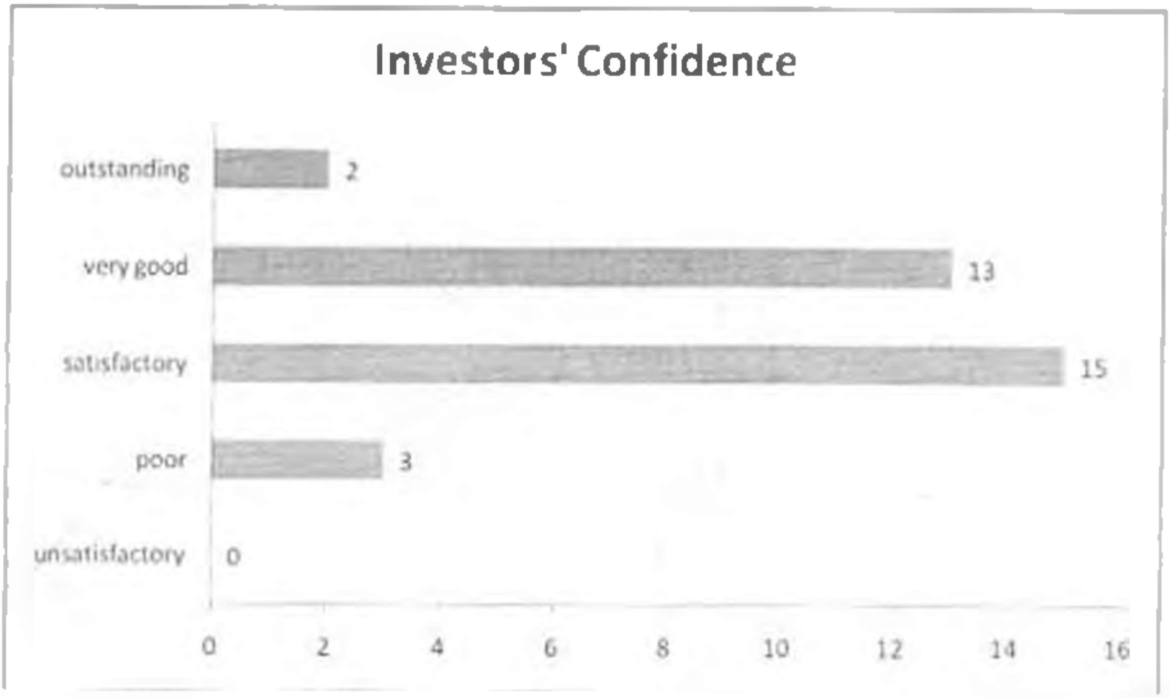
4.3.2 Investors' Confidence

According to respondents who were interviewed, 3 respondents felt that investors would rate their regulatory duties as Poor, 15 thought that investors were Satisfied with the way they regulate the market, 13 placed the investor confidence at Very Good, 2 respondents rated the confidence at outstanding but none of the 33 respondents rated the investors' confidence at Unsatisfactory level. The following table and figure bellow summarises the responses.

Table 8: Investors' Confidence

Investors' confidence in regulatory bodies in performing their duty					
Outstanding	Very good	Satisfactory	Poor	Unsatisfactory	Total
2	13	15	3	0	33

Figure7: Investors' Confidence



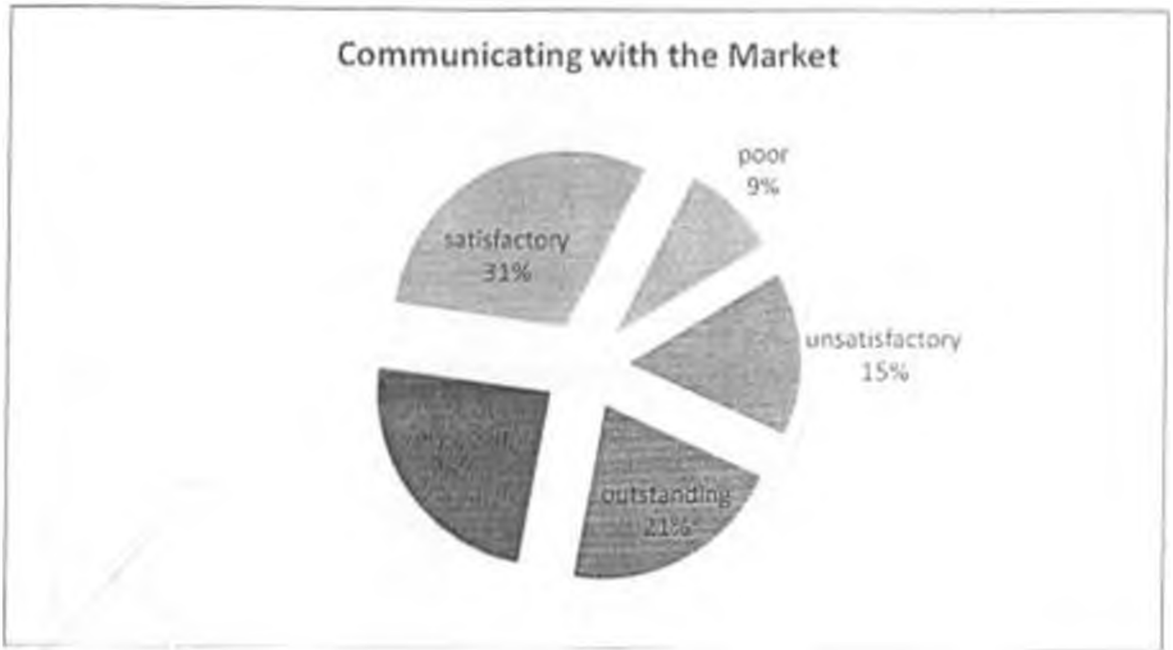
4.3.3 Communicating With the Market

The research sought to find out how managers would rate the progress their agencies have made after signing performance contracts in educating or otherwise informing the market of their activities and how beneficial they are in maintaining fair play in the market. Out of the 33 responses obtained, 5 respondents said their agency's progress was unsatisfactory, 3 respondents rated themselves at Poor, 10 respondents said their progress was Satisfactory, 8 placed their progress at Very good and the remainder of 7 respondents said their progress was Outstanding. The responses are tabled.

Table 9: Communicating with the market

Progress in communicating agency's activities with the market					
Outstanding	Very good	Satisfactory	Poor	Unsatisfactory	Total
7	8	10	3	5	33

Figure 8: Communicating with the market



4.3.4 Information Flow to the Market

On the same issue of communication, the respondents were asked on how they would rate the information flow and availability to the market to the stakeholders who include consumers, investors and the general public after the introduction performance contracts. In this question respondents were required to pick alternatives of excellent, very good, good, fair and poor.

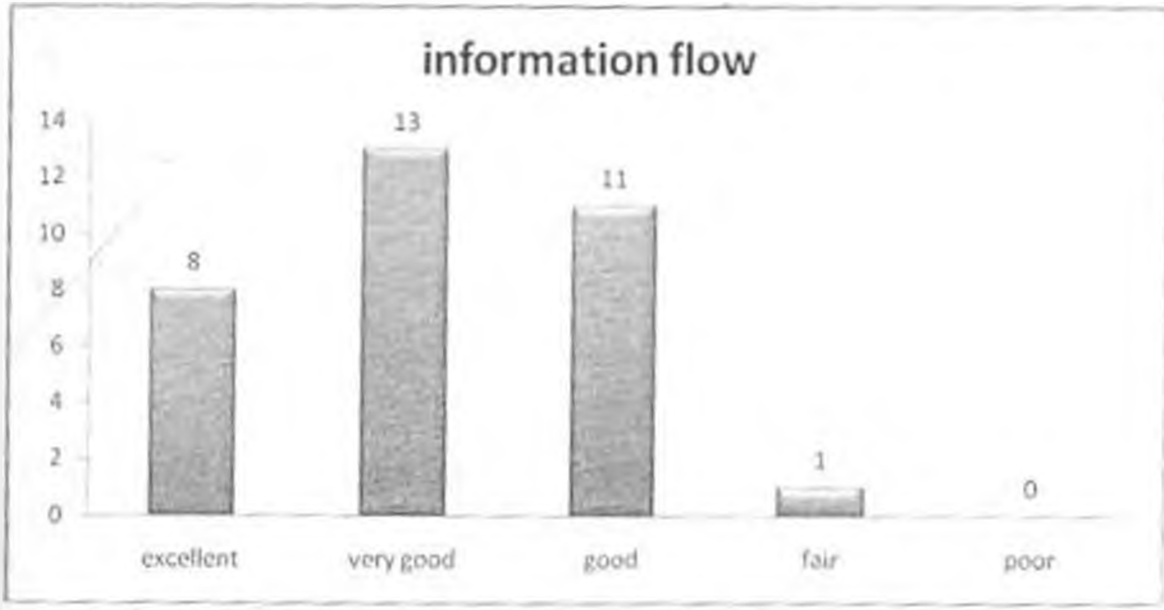
8 respondents said information availability for market players was at excellent level, 13 respondents answered information availability was at Very good level, 11 answered good, one

respondent answered that his agency's information availability was fair and none answered poor. Their responses are as follows.

Table 10: Information flow and availability

Information flow and availability to the market					
Excellent	Very good	Good	Fair	Poor	Total
8	13	11	1	0	33

Figure 9: Information flow and availability



4.3.5 Assessing Performance Indicators

The research identified various indicators to test the performance of regulatory agencies; these indicators include accountability, consumer education, monitoring the market, customer satisfaction surveys, resource allocation, work appraisal and work training. In this case these indicators are supposed to help an agency to find out how they are performing and by getting good results would indicate better overall performance of an agency. Hence the following responses were obtained from 33 respondents on the above indicators and they only tabulated.

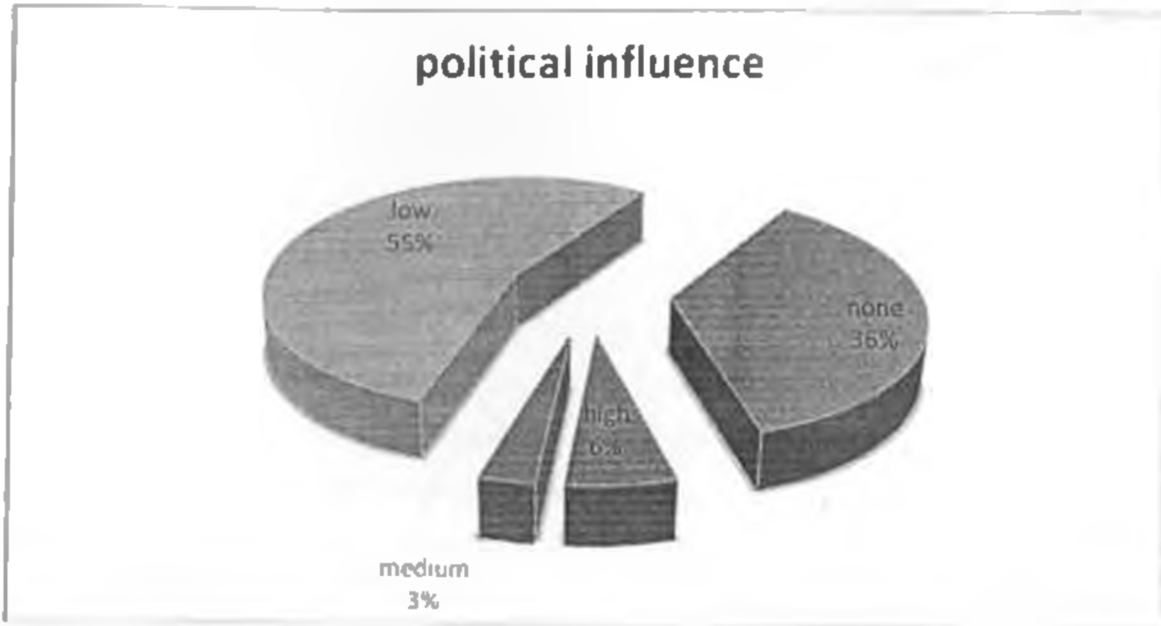
Table11: Performance indicators

	Performance indicators in pursuit of effectiveness					
	Excellent	Very good	Good	Fair	Poor	Total
Accountability	4	8	15	4	2	33
Consumer education	9	11	6	7	0	33
Customer surveys	6	19	4	0	4	33
Monitor the market	3	13	13	1	3	33
Resource allocation	5	6	0	15	7	33
Work appraisal	9	11	8	5	0	33
Work training	9	6	12	3	3	33

4.3.6 Political Influence

The research sought to find out whether regulatory agencies do experience political influences in their operations and to what extent. Of the 33 interviewed respondents, 2 respondents said the political influence in their operations was High, 1 respondent said the influence was Medium, 18 said the influence was Low and 12 said none. The low political influence can be attributed to the multiparty and collision government embrace improved performance thus helping boost economic growth and minimising the bureaucratic rules in regulatory agencies. The responses have been represented in the subsequent pie chart.

Figure 10: Political Influence



CHAPTER FIVE SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.0 Introduction

This chapter give a summary of findings in relation to research questions and draws conclusions and recommendations on the effectiveness of performance contracts.

5.1 Summary of Findings

The research sought to find out the effectiveness of performance contracting in state regulatory corporations using the following main questions in order to realise the research objectives. The questions are; what are the improvements on performance of state corporations after the introduction of performance contracting in the public sector? How the performance indicators are being implemented in order to achieve results? How does the autonomy of state corporations impact on their management?

From the field findings the performance contracts have improved the general performance of state regulatory agencies in the matter of regulating the market and restoring customer and investor confidence in these regulatory bodies in protecting their needs. The use of the performance contracting strategy has led to the realization that it is a very effective and efficient planning tool. Corporate planning and the itemization of annual work plans, adequately supported by budgetary provisions and delineation of lines and levels of responsibility for performance, is a necessary tool for effective and efficient management of public resources.

The findings reveal that regular monitoring of the implementation of the performance contracts is a vital aspect for its effectiveness. Providing feedback on reports and taking corrective action, where necessary, are key ingredients for effectiveness. The strategy captures the current performance and raises expectations for improved future performance. The Strategy also raises motivation, morale and builds confidence of the consumers of the public services. In summary, performance contracts have been effective.

5.2 Conclusions

It has been found out that

i) Introduction of performance contracts in the management of regulatory agencies has provided sufficient evidence that the management of public resources can be effective and efficient.

ii) As a result of the introduction of the performance contracts strategy, there has been more accountability and transparency and this would ultimately contribute to the eradication of corruption

iii) The process enhances accountability for public resources to the tax payers. The performance contracts strategy, therefore, provides a yardstick and a reliable and valid tool for competitive recruitment and promotion in the public service. It also promotes the principle of meritocracy, reward or sanction.

iv) The continued and persistent use of the performance contracts strategy would help to de-personalize and depoliticize the operations of public regulatory agencies affairs.

v) It is evidence that performance contracting is effective through customer confidence on regulators, raising investors' confidence, communication with market, easy access to performance indicators.

RECOMMENDATIONS

There is a need for developing a customized and coordinated training programme on performance contracting for all involved managers. There is also a need to develop a communication strategy for the performance contracting strategy that clearly spells out methods of packaging, marketing, disseminating information and sensitizing all employees in regulatory bodies.

Capacity building should be extended to the performance evaluation teams. Good quality independent evaluations of government programs can provide information needed to improve the effectiveness and efficiency of performance contracts. Reforms of public enterprises should focus on changing the system rather than people. Unless the Kenyan government (as owner) defines excellence, it can not achieve it. Reforms of public regulatory agencies should focus on results and not on processes. Accountability for results should also trickle down and up.

Lastly, to ensure sustainability of the performance contracts strategy as a management tool, it should be legislated and entrenched in the Laws of Kenya as soon as appropriate. There is therefore need to review the existing legal and institutional frameworks that currently govern the operations of the public agencies in tandem with the requirements of the performance contracts Strategy. The Incentives/Sanctions system should be put in place to reward success and sanction failures.

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QUESTIONNAIRE: APPENDICES

Number ....

INSTRUCTIONS:

This questionnaire consists of items pertaining to effectiveness of performance contracting in state corporations. Please complete each item as per the instructions given. The information collected is purely meant for academic research and will be treated as confidential.

Position ....

Date...............................2008

Address...(Optional)

Name of the
Corporation..

Postal Address of State
Corporation..

Physical address of State

Corporation..

The questionnaire is divided into two sections; **section A and section B** **Section A** has questions which seek to find out how well do regulatory bodies understand the requirements of Performance Contracts and **section B** seeks to find out how effective are Performance contracts

Section A: Understanding Performance Contracts

1. Do you understand what the Performance Contract entails?

    Yes [ ]
    Some- how [ ]
    No [ ]

2. As for your opinion, do the measures expressed in the performance contracts well defined and easy to understand?

    Yes [ ]
    Some- how [ ]
    No [ ]

3. As a public officer, have had any training on Performance Contracting?

    Yes [ ]
    No [ ]

4. If yes, how could you rate the level of training received? (*Tick where appropriate*)

    Outstanding [ ]
    Very Good [ ]
    Satisfactory [ ]
    Poor [ ]
    Unsatisfactory [ ]

5. Do you think the indicators expressed in the performance contract reflect achievable benchmarks performance?

    Yes [ ]

Some-how [ ]

No [ ]

Section B; Effectiveness of Performance Contracts

For each question tick where appropriate and within the brackets or boxes provided

1. At which level would you rate the relationship of trustworthiness, integrity and confidence customers have in you, to regulate the market? (*using a scale of 1; unsatisfactory, 2; poor, 3; satisfactory, 4; very good 5; outstanding*)

   *Level*______________

2. How would you rate the level of confidence the investors have in you in the field of regulating the market after signing performance contracts? (*using a scale of 1; unsatisfactory, 2; poor, 3; satisfactory, 4; very good 5; outstanding*)

   *Level*______________

3. Rating the level of communication with the market of your activities, what kind of progress do you think performance contracts have made? (*using a scale of 1; unsatisfactory, 2; poor, 3; satisfactory, 4; very good 5; outstanding*)

   Level of progress ____________________

4. How do you rate the level of information flow to consumers, investors and the public in general after performance contacts?

   Excellent [ ]

   Very good [ ]

   Good [ ]

Fair [ ]

Poor [ ]

5. The objectives of the contract acts as baseline to indicate your organisation's performance, of the following objectives listed, how would you rate them looking at your agency's pursuit of effectiveness?

Indicators	1 (Excellent)	2 (V. Good)	3 (Good)	4 (Fair)	5 (Poor)
Accountability					
Consumer education					
Customer satisfaction surveys					
Monitoring the market					
Resource allocation					
Work appraisal					
Work training					

6. How would you rate the level of political influence in your operations of regulating the market?

High [ ]

Medium [ ]

Low [ ]

None [ ]

7. Looking at the level of autonomy to run your own operations, how would you rate your freedom in engaging strategies that will improve your effectiveness?

(Using a scale of 1: limited, 2; discouraging, 3; satisfactory, 4; encouraging, 5; unlimited)

Level of autonomy ______________________

Registered Regulatory State Corporation

	Applicable State Corporation	Parent Ministry
1.	Capital market Authority	Finance
2.	Communication Commission of Kenya	Information and Communication
3.	Commission for Higher Education	Education Science and technology
4.	Electricity Regulatory board	Energy
5.	Retirement Benefit Authority	Finance
6.	Coffee Board of Kenya	Agriculture
7.	Council for Legal Education	Justice and Constitutional Affairs
8.	Export Promotion Council	Trade and Industry
9.	Export Processing Zones Authority	Trade and Industry
10.	Investment Promotion Center	Trade and Industry
11.	Kenya Plant Health Inspectorate Services	Agriculture
12.	Kenya Bureau of Standards	Trade and Industry
13.	Kenya Civil Aviation Authority	Transport
14.	Kenya Sugar Board	Agriculture
15.	National Environment Management Authority	Environment and Natural Resources
16.	Tea Board of Kenya	Agriculture
17.	Catering Training and Tourism Development Levy Trustees	Tourism and Wildlife Environment and Natural Resources
18.	Horticultural Crops Development Authority	Agriculture
19.	Kenya Dairy Board	Livestock and Fisheries Development
20.	Kenya Industrial Property Institute	Trade and Industry
21.	Kenya Sisal Board	Agriculture
22.	Maritime Authority	Transport
23.	NGO Co-ordination Bureau	Office of the Vice President/Home Affairs
24.	National Tea Zones Development Authority	Agriculture
25.	National Irrigation Board	Water and Irrigation
26.	Water Service Regulatory Board	Water and Irrigation

Registered Regulatory State Corporation

	Applicable State Corporation	Parent Ministry
1.	Capital market Authority	Finance
2.	Communication Commission of Kenya	Information and Communication
3.	Commission for Higher Education	Education Science and technology
4.	Electricity Regulatory board	Energy
5.	Retirement Benefit Authority	Finance
6.	Coffee Board of Kenya	Agriculture
7.	Council for Legal Education	Justice and Constitutional Affairs
8.	Export Promotion Council	Trade and Industry
9.	Export Processing Zones Authority	Trade and Industry
10.	Investment Promotion Center	Trade and Industry
11.	Kenya Plant Health Inspectorate Services	Agriculture
12.	Kenya Bureau of Standards	Trade and Industry
13.	Kenya Civil Aviation Authority	Transport
14.	Kenya Sugar Board	Agriculture
15.	National Environment Management Authority	Environment and Natural Resources
16.	Tea Board of Kenya	Agriculture
17.	Catering Training and Tourism Development Levy Trustees	Tourism and Wildlife Environment and Natural Resources
18.	Horticultural Crops Development Authority	Agriculture
19.	Kenya Dairy Board	Livestock and Fisheries Development
20.	Kenya Industrial Property Institute	Trade and Industry
21.	Kenya Sisal Board	Agriculture
22.	Maritime Authority	Transport
23.	NGO Co-ordination Bureau	Office of the Vice President/Home Affairs
24.	National Tea Zones Development Authority	Agriculture
25.	National Irrigation Board	Water and Irrigation
26.	Water Service Regulatory Board	Water and Irrigation