DETERMINANTS OF FINANCIAL DISTRESS FACING LOCAL AUTHORITIES IN SERVICE DELIVERY IN KENYA

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(Business Administration)

JOMO KENYATTA UNIVERSITY OF AGRICULTURE AND TECHNOLOGY

2013

Determinants of Financial Distress Facing Local Authorities in Service Delivery in Kenya

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A Thesis Submitted in Partial Fulfillment for the Degree of Doctor of Philosophy in Business Administration in the Jomo Kenyatta University of Agriculture and Technology

2013

DECLARATION

This thesis is my original work and has not been presented for a degree in any other university.

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DEDICATION

To my wife Millicent; children, Caroline, Lisday and Martin, for their support and patience while writing this thesis.

ACKNOWLEDGEMENT

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ABBREVIATIONS AND ACRONYMS

ATMS	Automated Teller Machines
FRSB	Financial Sustainability Review Board
ICT	Information Communication and Technology
IEA	Institute of Economic Affairs
KPI	Key Performance Indicators
LA	Local Authorities
LAIFOM	Local Authority Integrated Financial Operating
LATF	Local Authority Transfer Fund
LGI	Local Government Key Indicators
IT	Information Technology
MAV	Municipal Association of Australia
MIS	Management Information Systems
MOLG	Ministry Of Local Government
PDAs	Personal Digital Assistants
POS	Point of Sale
PWC	Price Waterhouse Coopers
PWC	Price Waterhouse Coopers
WALGA	Western Australian Local Government Association

DEFINITION OF TERMINOLOGIES

Local Government/Local Authority:

Is as a system of government whereby the state allows the establishment of Local units of government with powers and Authority to make Local decisions on matters that affect the Local communities and to mobilise Local resources for implementation or execution of the decisions made (Mcluskey and Fransen, 2005).

Financial Distress

It is a condition where a company cannot meet or has difficulty paying off its financial obligations to its creditors as they come due (Business Dictionary, 2010). A state when a firm's business deteriorates to the point where it cannot meet its financial obligations, the firm is said to have entered the state of financial distress. The first signals of distress are usually violations of debt covenants coupled with the omission or reduction of dividends (Miring'uh and Mwakio, 2006).

Corporate Governance:

Corporate governance refers to mechanisms that are concerned with ways in which all parties interested in the well-being of the firm (the stakeholders) attempt to ensure that managers and other insiders take measures or adopt mechanisms that safeguard the interests of the stakeholders (Mutero, 2007).

Financial management

Financial management is the planning, directing, monitoring, organizing, and controlling of the monetary resources of an organization (Business dictionary, 2010)

Human Resource Management

Human resource Management (HRM) is a set of tools to help you organize, plan, and implement personnel practices in organizations (Mathew, 2007).

Information Technology

Information technology is defined as technologies that ensure a more accurate and cost effective knowledge to support decision making, reduces mental and physical efforts in solving certain tasks; reduces or eliminates inefficient practices, it rivals the manual system and improves services rendered to customers (Awe, 1997).

Government Regulation

Government regulation is defined as a rule of order having the force of law, prescribed by a superior or competent Authority, relating to the actions of those under the Authority's control (West's Encyclopedia of American Law, 2008)

ABSTRACT

The purpose of this research was to investigate the determinants of financial distress facing Local Authorities in service delivery in Kenya. Local Authorities are often unable to meet their financial obligations including payment of salaries. In order to meet their short term financial obligations they are forced to operate on overdrafts which attract high interest rates hence compounding their financial distress problem. The presence of financial distress in Local Authorities leads to poor service delivery and loss of valuable assets to creditors due to inability to service their debts.

The study population comprised of the 175 Local Authorities in Kenya. A descriptive research design was used to conduct the study. A sample of 20 Local Authorities was selected using a stratified random sampling technique. A questionnaire was used to collect data from both the Local Authorities officers and customers of Local Authorities. The data collected was analyzed using descriptive and inferential statistics. Qualitative responses were analyzed using content analysis.

Results indicated that the causes of financial distress include financial management practices, corporate governance practices, human resource management practices, information technology and government regulation. Financial management practices, human resource management practices, and corporate governance practices were found to have a negative and significant relationship with financial distress. This implies that an

increase in the effectiveness of these variables leads to a decrease in financial distress in Local Authorities and vice versa. Government regulations were found to have a positive relationship with financial distress implying that ineffective government regulation leads to high levels of financial distress.

The study recommends that best practices in the area of financial management, human resource management, corporate governance and information technology need to be considered as measures of addressing financial distress of Local Authorities and that Government regulations on formation of parallel institutions should be critically reviewed as it may result to unintended consequences. The study recommendations may be critical to the successful financial management of the county governments.

CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Study

The terms Local Governments and Local Authorities are used interchangeably in this thesis so as to avoid being bogged down by terminological quagmires. Local government means an intra-sovereign governmental unit within the sovereign state dealing mainly with Local affairs, administered by Local Authorities and subordinate to the state government (Khan & Ara, 2006; Jahan, 1997).

Local government is also defined as a political sub – division of a nation or state which is constituted by law and has substantial control of Local affairs, including the power to impose taxes or to enact prescribed purpose (Ajayi, 2001). Wanjohi (2003) and Institute of Economic Affairs (2009) too defined Local Government as an institution whose operations addresses the needs and aspiration of the citizenry and also extends the administrative and political control to the community. These two definitions form the accepted view of LAs for the purpose of this study.

Local Authorities according to Institute of Economic Affairs (IEA, 2009) constitute one of the layers of Government. The other layers of Government are Regional Government, Central or National Government and where applicable the Federal Government. Local Authorities derive their mandate from powers delegated to it by legislation or directives

of the higher level of government (Central government or federal government) (IEA, 2009). The nature of Local Authorities differs from country to country.

The formation of Local government may have been motivated by the need to reduce bureaucracy and the growth of institutional power to the detriment of the citizens. This is exemplified by the quote from a letter from Thomas Jefferson to J. Cabell.

> "The way to have good and safe government is not to trust it all to one, but to divide it among the many, distributing to everyone exactly the function he is competent to. Let the National Government be entrusted with the defense of the nation and its foreign and federal relations; the State governments with the civil rights, laws, police, and administration of what concerns the State generally; the counties with the Local concerns of the counties, and each ward direct the interests within itself" (Thomas, 1816).

1.1.0 The Mandate of Local Authorities

The mandate of Local Authorities is to bring governance closer to the people as advocated by the decentralization theorem which states that each public service should be provided by the jurisdiction having control over the minimum geographic area that would internalize benefits and costs of such provision (Oates, 1972; Stigler, 1957). They provide cultural; educational; management, research, commerce and political services. They also offer employment, best health facilities and boost the country's economy

(United Nations -HABITAT, 2004). For instance, the City Council of Nairobi, the largest Local Authority in Kenya, produces more than half of the country's Gross Domestic Product (IEA, 2009).

The Cities' Alliance Report by Menkveld and Cobbett (2007) and Local Authority services (Cap 265, Chapter 3 Section 5), describes Local Government as providing platforms for productivity, entrepreneurship and economic modernization, poverty reduction and practicing good governance. Local Authorities also are mandated to enable administrative convenience and expediency as advocated by Stigler's menu theorem. The presence of financial distress in Local Authorities leads to poor service delivery and makes a Local Authority not to meet its mandate (Freire & Polese, 2003). Poor service delivery has its consequences which include a growing dissatisfaction of the community to the point that they form Local associations to voice their concerns; a good example is the Karengata Resident Association (Omamo, 1995). On the extreme side, residents may withhold the rates owed to the Local Authorities as a measure to enforce compliance with service delivery (IEA, 2009).

1.1.1 Global Outlook of Financial Distress Facing Local Authorities

Dollery (2009) investigated the emergence of acute financial distress in all Australian Local government state and territory jurisdictions. The study by Dollery (2009) was motivated by the frequent national and state based inquiries into the financial

sustainability of Local councils in the dawn of the new millennium. The central focus of the study was to establish the extent and degree of financial distress in Australian Local Authorities.

The study also noted that there were various policies that had been recommended for dealing with financial unsustainability in Australian Local governments. These policy recommendations were: structural reforms in form of forced amalgamation of councils and internal reforms, increased fiscal transfers from central government to Local government, increased borrowings by Local councils inform of fixed interest bond issues, and relaxing rate capping regulations and the introduction of additional revenues sources such as environmental taxes.

A study by Capalbo, Grossi, Ianni & Sargiacomo (2010) attempted to investigate the nature of financial distress in Italians Local governments. In order to understand the nature of financial distress and the attitudes of central government towards distressed Local governments, Capalbo, Grossi, Ianni & Sargiacomo (2010) adopted various approaches. First, the study proposed a synthetic outline of the national legislative framework on financial distress of Italian Local governments through analyzing data on the number, dimension, and geographical position of distressed Italian Local governments.

Secondly, the study focused on the causes of financial distress in Italian Local governments by reviewing sample based scholarly studies and also by referring to comprehensive analysis done by the court of auditors. Thirdly, the study analyzed the level of the central government involvement in addressing the financial distress of Local governments through a review of legislative measures, the extent to which legislative interventions have changed. After reviewing the scholarly articles on causes of financial distress in Local governments, Capalbo, Grossi, Ianni & Sargiacomo (2010) noted that the main causes of financial distress could be grouped in to two approaches, the social economic decline approach and the Local management approach.

A study by Honadle (2006), sought to establish the role that the state play in dealing with Local government financial crisis in United States. The study also attempted to explain the state policy formation as a response to Local government financial crisis. The overriding objective of the study was to establish whether states are more rational – comprehensive or incremental in their approaches to dealing with Local government financial crisis. Honadle (2006) concluded that an incremental approach was the most approach used by states to develop policies aimed at stemming Local financial crisis. The results also indicated that policy entrepreneurs need to find the right balance between a "technical fix" and politics in order for their proposals to be adopted.

1.1.2 Financial Distress in Local Authorities in Developing Countries

Shah and Shah (2006) noted that Local Authorities in developing countries continue to play a small role in public service delivery with a few notable countries such as a China and Brazil. The role of Local Authorities in these countries (China and Brazil) has progressively increased. The small role played by the Local Authorities in developing countries may be as a result of heavy regulation of the Local Authority activities and inadequacy of financial resources (Smoke, 2001). This implies that Local Authorities have limited autonomy in expenditure decisions and hardly any in revenue-raising decisions (Shah & Shah, 2006).

Wunsch (2001) carried out a literature based study and attempted to understand why decentralization has failed in Africa Local Authorities. He argued that although many African countries have pursued decentralization reforms, these reforms have not managed to bring about effective governance. This study concludes that failure in reforms occurs in four areas which inhibit distribution of substantial resources. These four areas are planning and capital investment, budgeting and fiscal management, personnel systems and management, plus finance and revenue. Schoeman (2011) investigated fiscal performance in terms of own-revenue collection and sustainability of Local municipalities in South Africa. This study noted that a large number of municipalities do not comply with the requirement that a "reasonable" amount of current expenditures be financed by means of own resources. Furthermore, Local governments finances are

featured by substantial variance as far as collection of own income is concerned.

Fjelstad, Henjewele, Mwambe, Ngalewa and Nygaard (2004) attempted to analyze changes in Tanzanian Local Authorities' capacity for financial management and revenue enhancement, and changes relating to governance, including accountability and responsiveness of the Local government. The study concluded that there is a causal relationship between financial management of Local Authorities and governance. Another study by Sennoga (2004) on relationship between Local government revenues and expenditures in Uganda noted that increases in revenues lead to less than proportionate increases in Local government expenditures which then lead to credence of the flypaper effect.

Jonga and Chirisa (2009) observed that it was lamentable that the messy reality of governance in Zimbabwe and the economic meltdown in the country has rendered most of the councils un-creditworthy to Local and international banks, leaving the borrowing powers by urban councils in the hands of central government to the detriment of rapid decision-making let alone service delivery. The researcher further asserted that almost all towns and cities in Zimbabwe have been grappling with raising sufficient revenues for capital and recurrent expenditures. Ekwubi (2010) investigated the problems of effective utilization of revenue available to Local government in Nigeria. The study revealed that ineffective utilization of revenue in the Nigerian Local government had created a

negative impact in Aninri Local Government Area in terms of service delivery.

De Visser, Steytler and Machingauta (2010) assert that given Zimbabwe's overall perilous financial state, Local governments have not been spared. Furthermore, almost all Local Authorities have faced insurmountable challenges in raising enough funding to ensure effective service delivery ever since independence. He further shows that most of the challenges revolve around the failure to ensure effective financial management systems resulting in levying sub-economic tariffs, the failure to ensure cost recovery on essential services, the failure to recover debts in a hyper-inflation environment, and the lack of skilled staff.

1.1.3 Financial Distress in Kenyan Local Authorities

The evolution of Local Authorities in Kenya dates back to the 19th century (Omamo, 1995). In 1902, the first form of Local Authority, the Village Headman Ordinance, was created. These units (Village Headman Ordinance) were managed by chiefs who were appointed by colonial administration. In 1903, the colonial administration established some form of municipalities in Kenya with Nairobi and Mombasa being the first townships that served the European settlers (IEA, 2009). The Local Authorities were used as a tool to control the Local communities and their structure consisted of Governor, Provincial Commissioner (PC), District Commissioner (DC), Division Officer (DO) and the Chief. By 1919 Local Authorities experienced some changes where Nairobi

Municipality had a mixed race council even though Africans were excluded from the council (IEA, 2009; SNV, 2006).

Africans were chosen as Councilors in 1937 for the first time ever (IEA Report, 2009). The functions of the Local Authority were changed in 1950 to include representation for decision making, resources mobilization, agency for central government and a link between Local community and central government, just as they are today (Omamo, 1995). The Local Government Bill of 1962 led to the formation of the Municipal, County, urban and Local Councils (the system that we have today) (Omamo, 1995).

A study done by Institute of Economic Affairs (2009) called understanding Local Government systems in Kenya gives in details the concept and structure of Local Government in Kenya including the historical perspective. This study addresses Local Authorities as they are and clearly shows analogy of events in government regulation of Local Authorities since independence. The current study borrows heavily from this study in getting actual statistics as they are in Kenyan Local Authorities. The paper by IEA (2009) however, does not explain the causes of the current status of Local Authorities in Kenya.

Muganda and Belle (2009) addressed the adoption of e-government by Kenya's Local Authorities and concluded the greatest impediment to adoption of e-government in

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Kenyan Local Authorities include weak financial base and incompetent personnel that are even skeptical of losing jobs if this is introduced. This was also noted by Waema & Mutullah (2006) who lamented of poor financial management in Local Authorities due to lack of adoption of ICT by Local Authorities. The two studies basically mentioned of financial distress in Local Authorities without addressing the causes of the same.

While the Local government regulations of 1963 described the role and functions of the Local Authorities to include the provision of basic socio-economic services, another structure in form of provincial administration existed parallel to the Local Authorities. These dual structures of governance exist up to date as claimed by Muia (2005). Muia (2005) further asserts that the dual structure may be partly responsible for the poor governance and service delivery among Local Authorities in Kenya.

However, Miring'uh and Mwakio (2006) assert that there is overwhelming evidence that recent reform measures, including Rapid Results Initiative (RRI) have failed to stop immense hemorrhage of revenue at the City Hall. A recent damning forensic report by the Kenya Anti-Corruption Commission, states that City Hall continues to lose a huge portion of parking fees, land rates or rent to corrupt officials exploiting weak financial management systems (KACC, 2007). According to this report also perpetrators of the rip-off at the Council had devised a complex system to block evidence of unremitted money estimated to be worth millions of shillings. Key to the racket is concealment of the paper

work involving such money, including bouncing cheques, tempering with the numbering of parking fees receipts and the filing of fraudulent expenditure claims at the council's cash office (Osiche, 2007; Adero, 2007; KACC, 2007).

Generally, some of the few studies on Local Authorities done in Kenya (Omamo, 1995; Osiche, 2007; Adero, 2007; Muia, 2005; Waema & Mutullah, 2006; IEA, 2009, and Muganda & Belle, 2009), mentions of presence of financial distress in Kenyan Local Authorities but do not specifically discuss the determinants of financial distress in these Local Authorities and how to mitigate them.

1.2 Statement of the Problem

Financial distress in Local Authorities exists in various forms (Walker & Jones, 2007). For instance Local Authorities are often unable to pay current liabilities such as salaries and short term obligation to creditors (Omamo, 1995). In order to meet their short term financial obligations they are forced to operate on overdrafts with high interest rates. Local Authorities are also unable to meet long term liabilities such as bank loans. An example of such financial distress include those currently being experienced by Mombasa City council which is staggering under heavy borrowing as it owes the creditors a whooping Ksh 1.9 billion according to Mombasa City Council Budget of 2011, while City Council of Nairobi owes its creditors Kshs 5.3 billion (CCN budget, 2011), just to mention but a few.

Furthermore financial distress exist in the form of revenue deficits forcing the Authorities to always rely on the central government for fiscal transfers such as Local Authority Transfer Fund (LATF) and bank overdrafts (Omamo, 1995). Also other studies (Mcluskey & Fransen, 2005; Gachuru & Olima, 1998 and Muia, 2005), noted that the financial and budget deficits in Local Authorities in Kenya were growing and that there was urgent need to arrest the situation. Consequently a number of councils had their employees demonstrate due to unpaid salaries and salary arrears that have gone for several months (Muia, 2005, Muganda & Belle, 2009).

Financial distress in Kenyan Local Authorities has been a persistent phenomenon. For example, it was recorded in the Kenya Parliamentary sessions that Local Authorities were facing financial challenges due to a weak financial base (ROK, 2001). This led to the introduction of Local Authority Transfer Fund (LATF) as a move to strengthen the financial base. However, these policy instruments together with internal sources of revenue have not mitigated the occurrence of financial challenges in Local Authorities. The persistence of this problem is exemplified in the quote from the Kenya Parliamentary session by ROK (2000) which went on to record that;

> "Mr. Speaker Sir, the Nairobi City Council is in a state of chronic financial distress. It has been spending beyond its means, and it has debt payments arrears that exceed its annual income, before even taking into account its large future debt repayment obligations". Kenya Parliamentary Hansard 15th June 2000, pg.1095.

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The financial health of Local Authorities in any country is crucial in ensuring the sustainable delivery of services to the community (Capalbo, Grossi, Ianni & Sargiacomo, 2010). The Presence of financial distress in Local Authorities such as inability to pay salaries leads to staff demotivation (IEA, 2009; Muganda & Belle, 2009). This is manifested through increase in shirking, laziness and corruption among the staff. This manifestation negatively affects the revenue collection which further compounds the problem of financial deficits (Institute of Economic Affairs, 2009).

However, other studies (Institute of Economic Affairs, 2009; Omamo, 1995; Mcluskey & Fransen, 2005; Gachuru & Olima, 1998 and Ekwubi, 2010) on Local Authority financial distress in developing countries in general, and Kenya in particular are inadequate because they do not exhaustively address the determinants of financial distress in Local Authorities. These studies acknowledge the presence of financial distress in Kenyan Local Authorities, which they claim inhibit service delivery but fails to address the causes of the same.

In addition, such studies are lacking in depth assessment and give generalized conclusions of the presence of financial distress in Kenyan Local Authorities without analyzing the causal relationship between financial distress in Local Authorities and its determinants. In fact no adequate studies have been conducted specifically to establish the factors that contribute to financial distress facing Local Authorities in Kenya. This

study therefore sought to bridge this evident research gap by investigating the determinants of financial distress facing Local Authorities in Kenya.

1.3 Objectives

1.3.1: General Objective

This study sought to establish the determinants of financial distress facing Local Authorities in service delivery in Kenya

1.3.2: Specific Objectives

The specific objectives were to:

1. Investigate whether financial management practices lead to financial distress facing Local Authorities in Kenya.

2. Establish if corporate governance practices lead to financial distress facing Local Authorities in Kenya.

3. Determine the contribution of Information Technology adapted to financial distress facing Local Authorities in Kenya.

4. Establish whether human resource management practices contribute to financial distress of Local Authorities in Kenya

5. Investigate if Government regulations contribute to financial distress facing Local Authorities in Kenya

1.4 Research Hypothesis

H1: Financial management practices do not significantly contribute to financial distress facing Local Authorities in Kenya?

H2: Corporate governance practices have insignificant contribution to financial distress that Local Authorities face in Kenya?

H3: Adoption of Information Technology does not significantly contribute to financial distress facing Local Authorities in Kenya?

H4: Human resource management practices do not significantly contribute to financial distress facing Local Authorities in Kenya?

H5: Government regulations do not significantly contribute to financial distress facing Local Authorities in Kenya?

1.5 Justification of the Study

1.5.1: Policy Makers

The findings of this study may be used to influence policy in the area of management of Local Authority resources with a specific motive of ensuring that financial challenges are addressed. In addition, the findings may influence policy on the management of the newly formed counties by ensuring that the current pitfalls causing financial challenges in Local Authorities are not replicated in the newly formed counties. The failure by Local Authorities to recognize the necessity of establishing and implementing policies aimed at protecting the going concern is a trend that is worrying policy makers and stakeholders.

1.5.2: Local Authorities

It was argued in this study that lack of effective management mechanisms in enhancing the going concern and service delivery of Local Authorities may be responsible for the financial distress facing Local Authorities. This mechanism relate to financial management, governance, information technology, human resource practices and regulations. Specifically, it is hypothetically argued in this study that poor financial management, poor governance, inadequate information technology and ineffective regulation may be determinants of financial distress facing Local Authorities. The results of this study may therefore be used by Local Authority management to turn the around the financial fortunes of Local Authorities.

1.5.3 Government Planners

The study findings may be of use to the National Government as it may highlight the financial challenges facing Local Authorities and which also impact negatively on service delivery. The achievement of Vision 2030 is heavily dependent on the performance of Local governments. The findings of this study may guide the central government on shortcomings of Local Authorities' financial management to help avoid the duplication of the same inefficiencies in the County Governments to be created in the new constitution dispensation era. This may ensure sustainable growth of devolved institutions structures and achievement of vision 2030.

1.5.4: Residents of a Local Authority

The residents of Local Authorities may find the results of this study useful as the results may shed light on the financial challenges that Local Authorities are contending with. Residents of Local Authorities are expected to pay their dues to the Local Authorities in order for them to experience effective service delivery. This report highlighted the need for residents to comply with the payment of rates and other fees and charges to the Local Authorities that may boost the Local Authorities resources and enhance service delivery.

1.5.5: Investors

Investors may find the results useful since the current study will highlight the financial challenges that face Local Authorities. They may therefore make appropriate decisions on whether to invests in Local Authority bonds or invest directly in Local Authority infrastructure such as schools, roads and hospitals. Depending on the nature of financial challenges facing Local Authorities, investors may make decisions on whether to engage Local Authorities in trade through supplies and purchase of tenders that payment may not be forthcoming. This justification will actually be realized if Local Authorities financial challenges are fully addressed and mitigated.

1.5.6 Scholars, Researchers and students

The findings of this study may be a value addition to literature review. Therefore, students of finance, public management, governance, information technology, human

resource management, and law may find this research finding critical in terms of broadening their minds in this area.

1.6 Scope

From a contextual point of view, the study is on the factors leading to financial distress facing Local Authorities in Kenya. The study attempted to establish whether financial management, corporate governance, human resource practices, Management information system and Government regulation contribute to financial distress facing Local Authorities in Kenya. The study restricted itself to the 175 Local Authorities in Kenya. The Local Government system in Kenya is divided into four categories that are Cities, Municipal, County and Town Councils (IEA, 2009). Currently the Local Authority system has 175 Local Authorities composed of three city councils, forty three municipal councils, sixty seven county councils and sixty two town councils (see table 1.1).

Table 1. 1: Classifications of Local Authorities

Local Authority	Total Number
City Councils	3
Municipal Councils	43
County Councils	67
Town Councils	62
Grand Total	**175**

Source; Ministry of Local Government (2011)

1.7 Limitations of the Study

Several limitations were experienced in this study, for example resistance from respondents primarily because they were suspicious of the study intentions although they were assured of their anonymity and the findings were to be used purely for academic purposes. The accuracy of the results depended on the honesty of the respondents, though with the assurance given to officers it is the hope of the Researcher that honest responses were given.

CHAPTER TWO

LITERATURE REVIEW

2.1: Introduction

The entire chapter reviews the literature related to the key study variables as depicted in the conceptual framework. The chapter also looks into the linkages in addition to establishing the existing relationships amongst these variables. Empirical studies related to the study variables were reviewed in the chapter in order to lay down ground for research. The chapter also attempts to justify the study in addition to reinforcing and underpinning the conceptual framework.

In the final analysis, the chapter gives a brief summary of the entire activities that were previously captured. The chapter comprises of; theoretical review, critical review of theories; review of theoretical and empirical studies and their implications and gaps in knowledge.

2.2 Theoretical Review

The theoretical underpinning of this study is enriched by a number of theories that basically informed the various study variables. These theories include Financial Distress Theory which greatly enriched and established the independent variable, while the Agency theory, Motivation Theory, Systems Theory and Regulation Theory informed my Independent variables.

2.2.1 Financial Distress Theory

Financial distress can be subdivided into four sub-intervals: deterioration of performance, failure, insolvency, and default. Whereas deterioration and failure affect the profitability of the company, insolvency and default are rooted in its liquidity. Theoretically, the outcome of each interval can be positive, implying that the company breaks the downward trend, or negative indicating the continuing deterioration of the firm value and a movement downwards from one sub-interval of the spiral to another. In many real cases, when entering financial distress, the company traverses all the stages of decline (Mueller, 1986).

Financial distress is characterized by a sharp decline in the firm's performance and value (Opler & Titman, 1994). This part of the overall process has two important characteristics; moving down the spiral from one phase to another the sharp decline accelerates, whereas the length of each stage becomes shorter and shorter. Obviously, this decline of performance can continue longer than the economic failure of the company. The length of insolvency depends on the maturity structure of the firm's debt, whereas default is dependent on the date of maturity followed by renegotiation and turnaround or liquidation and is, therefore, the shortest stage of financial distress.

The biggest challenge in financial distress is to recognize adverse processes as early as possible in order to gain more time for response. The later financial distress is

anticipated, the more time pressure and the more questionable is the success of counter measures (Opler & Titman, 1994). The theory of financial distress may be useful in explaining the causes of financial challenges facing Local Authorities. In addition, it may be used to give indicators of financial distress in Local Authorities and how the challenges can be resolved.

2.2.2: Agency theory

Agency theory addresses the Agency issue in which one party (the principal) delegates work to another (the agent), who performs that work (Jensen & Meckling, 1976). There is an agency relationship when the actions of one individual affect both his welfare and that of another person in an explicit or implicit contractual relationship. The individual who undertakes the actions is the agent and the person whose welfare (utility), measured in monetary terms, is affected by the agent's actions is called the principal (Akaranga, 2010).

The typical case of agency relationship is the one that exists between an employer (the principal) and his employee (the agent). In an agency relationship, the principal wants the agent to act in the principal's interest. However, the agent is expected to have his own interest and consequently, he may not act in the principal's best interests. An agency relationship is a contract under which one or more persons (the principal), engage another person (the agent) to perform some service on their behalf which involves delegating

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some decision making Authority to the agent. If both parties to the relationships are utility maximizers, there is a good reason to believe that the agent will not always act in the best interests of the principal (Jensen & Meckling, 1976).

Then, the principal's problem is consequently to design an incentive contract that induces the agent to undertake actions that will maximize the principal's welfare. However, both the principal and agent are confronted with uncertainty. This uncertainty may appear in various ways. First, the principal is uncertain about actions undertaken by the agent and/or information held by the agent. The mainstream-economic theory terms the principal's uncertainty state asymmetric information. There is a state of asymmetric information because the agent holds information that the principal does not have.

Second, uncertainty bears on the outcomes of the agent's actions. An agent is uncertain about the outcomes of his actions. For the principal, this latter phenomenon manifests itself more precisely in the fact that the principal is uncertain about the causality between agent's actions and the outcomes. This state of uncertainty and the resulting state of asymmetric information that exists between the principal and his agent impose certain constraints which complicate the forming of the contract (Artley, 2001; United Nations, 1999; Akaranga, 2010)

Agency theory may be useful in explaining the financial distress facing Local Authorities. For instance, the theory could explain how the selfish actions of Local Authority management (agents) affect the welfare of residents (principals). Their actions include how they misappropriate the funds of the Local Authorities and also how they make non optimal decisions as far as utilization of financial and non financial resources are concerned (Muranda, 2006; Kloha, Weissert, & Kleine, 2005)

2.2.3 Motivation Theory

Abraham Maslow published "Theory of Human Motivation" in 1943 and he is considered the father of needs based motivation theory and his theory is "one of the best-known and most widely cited works on motivation" (Artley, 2001). Maslow (1946) proposed a five level hierarchy of needs which he outlined as necessary for the achievement of a completely satisfied individual; or in his terms, a self-actualized being. Those needs are: physiological, safety, love, esteem, and self-actualization.

Physiological needs can be described as the most basic of human needs; those needed for human survival. These include breathing, water, food, and shelter. Safety needs are those needs which create stability and predictability in our lives: personal and financial security, health and well-being, and employment and access to resources. Love/belonging needs are centered on social interactions and interpersonal relationships: friendship, family, and intimacy. Esteem needs reflect our desires for respect, self-esteem and the

need to belong (Gagne, 2003; Frederick-Recascino, 2002; Deci, Koestner, & Ryan, 2001).

Finally, self-actualization is the state which the individual achieves when all other needs have been meet. Maslow identifies fifteen attributes that self-actualized individuals experience, and thus the exact definition of being "self-actualized" is difficult to summarize. Some of the characteristics include: the acceptance of self, others and nature; spontaneity; autonomy independent of culture and environment; and the mystic experience (Chirkov, Ryan, Kim, & Kaplan, 2003; Brown & Ryan, 2003; Barron & Harackiewicz, 2000 and Baard, 2002).

Feelings of limitless horizons opening up to the vision, the feeling of being simultaneously more powerful and also more helpless than one ever was before, the feeling of ecstasy and wonder and awe, the loss of placement in time and space with, finally, the conviction that something extremely important and valuable had happened, so that the subject was to some extent transformed and strengthened even in his daily life by such experiences (Brown & Ryan, 2003 and Barron & Harackiewicz, 2000).

Each need, or level, is fulfilled in sequence and serves as motivation until all the needs of the individual are meet in self-actualization. While Maslow emphasized that individuals will generally be motivated to seek each need in the order described, he also stated that

the order of his hierarchy is "not nearly as rigid as we may have implied" and that in some individuals will seek needs in different order (Barron & Harackiewicz, 2000).

It is important to remember that Maslow himself realized that his hierarchy of needs was more theoretical than normative: The present theory then must be considered to be a suggested program or framework for future research and must stand or fall, not so much on facts available or evidence presented, as upon researches yet to be done, researches suggested perhaps, by the questions raised in this paper (Brown & Ryan, 2003). As such, a number of authors have expanded upon Maslow's work (Frederick-Recascino, 2002; Deci, Koestner & Ryan, 2001).

The theory of motivation may be used to explain the soft elements that contribute to the financial distress facing Local Authorities. For instance, the theory may use the reward structure to explain why the human resource/work force employed to manage the financial and non financial resources do not put extra effort in addressing the financial challenges facing Local Authorities, but always contribute to financial distress facing Local Authorities.

2.2.4 Systems Theory

Systems theory springs from biology and its content free and applicable to many fields of study. Systems theory can be defined as "a working hypothesis, the main function of

which is to provide a theoretical model for explaining, predicting, and controlling phenomenon" (Bertalanffy, 1962). One common element of all systems is described by Kuhn (1974) as knowing one part of a system enables us to know something about another part. The information content or a "piece of information" is proportional to the amount of information that can be inferred from the information (Kuhn, 1974). Systems can be either controlled (cybernetic) or uncontrolled. In controlled systems information is sensed, and changes are effected in response to the information. Kuhn (1974) refers to this as the detector, selector, and effector on functions of the system.

The detector is concerned with the communication of information between systems. The selector is defined by the rules that the system uses to make decisions, and the effector is the means by which transactions are made between systems. Communication and transaction are the only intersystem interactions. Communication is the exchange of information, while transaction involves the exchange of matter-energy. All organizational and social interactions involve communication and/or transaction.

Kuhn's model stresses that the role of decision is to move a system towards equilibrium. Communication and transaction provide the vehicle for a system to achieve equilibrium. "Culture is communicated, learned patterns... and society is a collective of people having a common body and process of culture". A subculture can be defined only relative to the current focus of attention. When society is viewed as a system, culture is seen as a pattern

in the system. Social analysis is the study of "communicated, learned patterns common to relatively large groups (of people)"(Kuhn, 1974).

System theory is crucial in explaining financial distress facing Local Authorities in Kenya. For instance, it may be argued that a failure in one department could lead to a failure in the financial department, collection department or the budgeting departments. Communication hitches in Local Authority departments may lead to disconnect in the way the departments interact with one another.

2.2.5 Regulation Theories

The first group of regulation theories account for regulation from the point of view of aiming for public interest. This public interest can be further described as the best possible allocation of scarce resources for individual and collective goods. In western economies, the allocation of scarce resources is to a significant extent coordinated by the market mechanism. In theory, it can even be demonstrated that, under certain circumstances, the allocation of resources by means of the market mechanism is optimal (Arrow, 1985).

These conditions are frequently not adhered to in practice hence the allocation of resources is not optimal and a demand for methods for improving the allocation arises (Bator, 1958). One of the methods of achieving efficiency in the allocation of resources is

government regulation (Arrow, 1970; Shubik, 1970). According to public interest theory, government regulation is the instrument for overcoming the disadvantages of imperfect competition, unbalanced market operation, missing markets and undesirable market results.

In the first place, regulation can improve the allocation by facilitating, maintaining, or imitating market operation. The exchange of goods and production factors in markets assumes the definition, allocation and assertion of individual property rights and freedom to contract (Pejovich, 1979). The guarantee of property rights and any necessary enforcement of contract compliance can be more efficiently organized collectively than individually. Furthermore, the costs of market transactions are reduced by property and contract law. The freedom to contract can, however, also be used to achieve cooperation between parties opposed to market operation.

Agreements between producers give rise to prices deviating from the marginal costs and an inefficient quantity of goods is put on the market. Antimonopoly legislations aimed at maintaining the market operation through monitoring the creation of positions of economic power and by prohibiting competition limiting agreements or punishing the misuse thereof (Shubik, 1970). Imperfect competition can also result from the special characteristics of the production process in relation to the magnitude of the demand in the

market. At a given magnitude of demand average total costs would be minimized if the production were to be concentrated in one company.

In that case a natural monopoly exists. If several companies produce the same total quantity of goods, the unit costs of production rise. An example of how such a situation arises is when the production process requires a great deal of capital. In that case, the fixed costs can continue to decline as production increases. Especially in the case of modest marginal costs that hardly rise, if at all, average total costs may persistently fall (Baumol, 1977). In such cases it is desirable, from the point of view of productive efficiency, to concentrate the production in a single company. A monopolist striving for maximization of profits will, however, set a price that deviates from the marginal costs. The stimulation of productive efficiency in the production process then acts to the detriment of the aim for allocative efficiency.

Natural monopolies are then either put under control of the state, as happens in many European countries, or highly regulated, as for example in the United States. In the latter case, regulation consists of barring entry to the market and the enforcement of price rules that promote efficient allocation (Braeutigam, 1989). In this way, the market results of perfect competition are stimulated. Examples of companies assumed at some time to have possessed the characteristics of a natural monopoly are railways, electricity distribution, gas and oil pipelines, telecommunication networks and drinking water distribution.

The government regulation on Local Authorities has contributed to their financial distress as regulation has led to formation of parallel institutions like Provincial Administration, Constituency Development Fund, and District Development Committees to mention but a few that have contributed to loss of focus on Local Authorities on issues of development and devolution. The regulation by government dictates devolution of state funds through the parallel institutions thus depriving LAs financing by the state which leads to financial distress in these LAs.

2.2.6: Conceptual Framework

Smith (2004) defines a conceptual framework as a framework that is structured from a set of broad ideas and theories that help a researcher to properly identify the problem they are looking at frame their questions and find suitable literature. A conceptual framework is described as a set of broad ideas and principles taken from relevant fields of enquiry and used to structure a subsequent presentation (Reichel & Ramey, 1987).

A conceptual framework is a group of concepts that are broadly defined and systematically organized to provide a focus, a rationale, and a tool for the integration and interpretation of information (Cooper & Schindler, 2006). Usually expressed abstractly through word models, a conceptual framework is the conceptual basis for many theories, such as communication theory and general systems theory. Conceptual framework

according to the same medical dictionary, also provide a foundation and organization for the educational plan in schools of nursing.

This section defines the various types of variables which include dependent variable and independent variables. There is nothing very tricky about the notion of independence and dependence. But there is something tricky about the fact that the relationship of independence and dependence is a figment of the researcher's imagination until demonstrated convincingly. Researchers hypothesize relationships of independence and dependence. They invent them and then they try by reality testing to see if the relationships actually work out that way (Cooper & Schindler, 2011). A dependent variable is a variable that is measured, predicted, or otherwise monitored and is expected to be affected by manipulation of an independent variable (Cooper & Schindler, 2006; Chandran, 2004; Kothari, 2004; Kumar, 2005).

Independent variable is a variable that is manipulated by the researcher, and the manipulation causes an effect on the dependent variable (Chandran, 2004; Kothari, 2004). Moderating variable (also known as interaction variable) is a second independent variable that is included because it is believed to have a significant contributory or contingent effect on the original independent variable–dependent variable relationship (Chandran, 2004; Kothari, 2004; Kumar, 2005).

The current study considered several conceptual frameworks by other scholars on the causes of financial distress in Local Authorities. The reviewed conceptual frameworks were critiqued and various variables were incorporated in the conceptual framework of the current study while others were discarded. The first model was from Park (2004) as illustrated in figure 2.1.
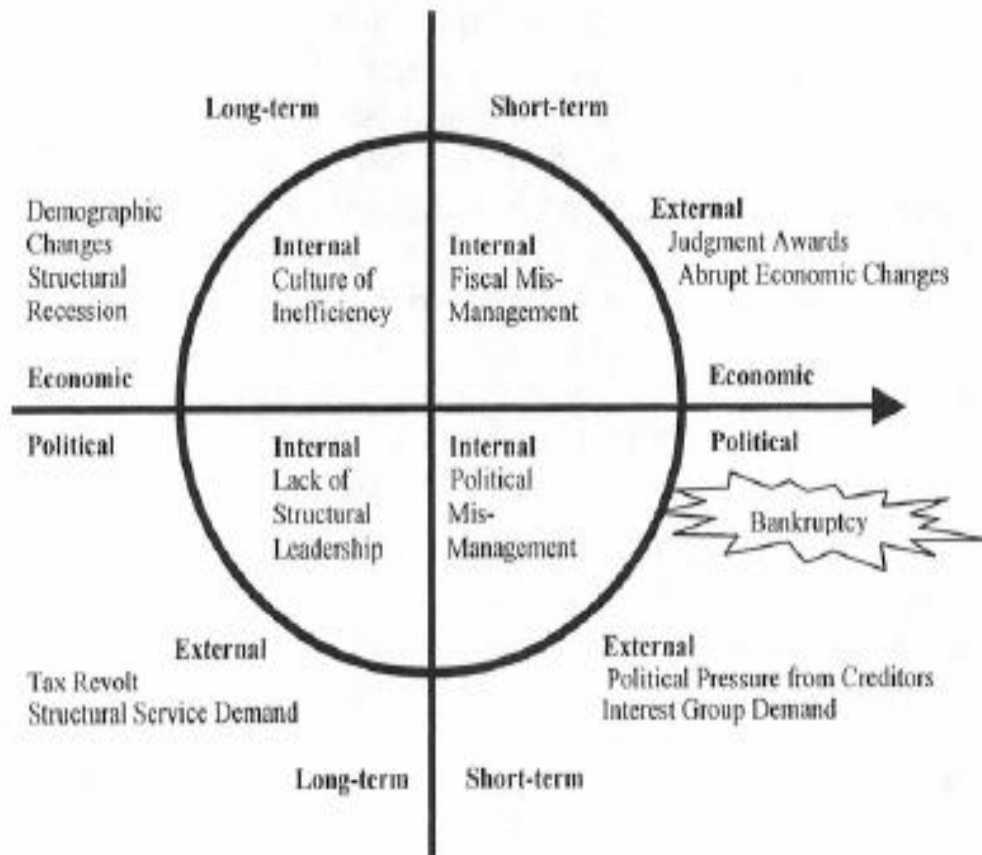
Source: Financial Distress Model by Park, 2004

Figure 2. 1: Park Model

The second reviewed model was by Capalbo, Grossi, Ianni and Sargiacomo (2010), which noted that the main causes of financial distress could be grouped into two approaches, the social economic decline approach and the Local management approach. The social economic decline approach assumes that causes of financial distress are external to Local Authorities and that they are beyond the control of Local government officials. Such causes include: contraction of economic growth, movement of city dwellers to outskirts of the major cities, demographic changes such as increase in population, reduction in Local business activity, unemployment and tax base erosion, bureaucracy and poor legislation.

The Local government approach assumes that incorrect managerial practices such as poor accounting and budgeting methods, incompetence and corruption among Local government officials, sub-division of Local governments into unviable political units and procedures and vulnerability of special interest groups. In conclusion, Capalbo, Grossi, Ianni and Sargiacomo (2010) argues that financial distress does not arise because of one set of factors but arises due to a mix of both external and internal factors.

Carmeli (2008) shows that the sources of financial distress of Local governments in Israel, may be classified into three major groups: structural or fixed (consists of Local Authorities' size, residents' socioeconomic status, and governmental resource allocation), organizational (consists of performance evaluation, transparency, and the role of the

Local government's management), and hybrid (consists of the relationship between the central and the Local governments) factors.

Incorporating the variables of Park (2004), Capalbo, Grossi, Ianni and Sargiacomo (2010) and Carmeli (2008), the current study came up with a conceptual framework. The final conceptual framework for this study is presented in figure 2.2 which indicates that the independent variables for the study included Financial Management Practices, Corporate Governance Practices, Information Technology, human Resource Management Practices and Government Regulations while the dependent variable for the study was financial distress facing Kenyan Local Authorities.

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┌─────────────────────────────────────────────┐
│ Financial Management Practices              │
│                                             │
│   1.  Internal controls                     │
│   2.  Audited accounts                      │
│   3.  Financial reports                     │
│   4.  Budgets                               │
└─────────────────────────────────────────────┘

┌─────────────────────────────────────────────┐
│ Corporate Governance Practices              │
│                                             │
│   1.  Accountability                        │
│   2.  Transparency                          │
│   3.  Corruption/ client characteristics    │
└─────────────────────────────────────────────┘

┌─────────────────────────────────────────────┐
│ Information Technology                       │
│   1.  Reliability  and relevance of information │
│   2.  User friendliness                     │
│   3.  Potential for growth                  │
│   4.  Hardware-Interaction with POS. ATMS   │
└─────────────────────────────────────────────┘

┌─────────────────────────────────────────────┐
│ Human Resource Management Practices         │
│   1.  Employee selection                    │
│   2.  Training & development.           .   │
│   3.  Performance appraisal and compensation │
└─────────────────────────────────────────────┘

┌─────────────────────────────────────────────┐
│ Government Regulations                      │
│   1.  1969-Transfer of functions act        │
│   2.  1974- Abolition of Graduated Personal │
│       Tax                                   │
│   3.  2003 Constituency Development Fund    │
│       Act.                                  │
└─────────────────────────────────────────────┘
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Influence →

┌─────────────────────────────────┐
│   Financial Distress   │
│   facing Kenyan Local   │
│   Authorities   │
└─────────────────────────────────┘

Independent variables   **Dependent variable**

Figure 2. 2: Conceptual Framework

2.3 Empirical Review

2.3.1 Financial Distress

According to Baldwin and Scott (1983), when a firm's business deteriorates to the point where it cannot meet its financial obligations, the firm is said to have entered the state of financial distress. The first signals of distress are usually violations of debt covenants coupled with the omission or reduction of dividends. Financial distress is a term in Corporate Finance used to indicate a condition when promises to creditors of a company are broken or honored with difficulty. Sometimes financial distress can lead to bankruptcy.

Financial distress can also be defined as a reaction, such as mental or physical discomfort, to stress about one's state of general financial well being. In particular, this includes perceptions about one's capacity to manage economic resources (such as income and savings), pay bills, repay debts, and provide for the needs and wants of life (Barbara, et al, 2006). Beaver (1966) defined financial distress as any of the following events: bankruptcy, bond default, bank account overdrawn, or nonpayment of a preferred stock dividend. On the other hand, Lau (1987) classified a firm into a five-state financial distress, that is, state 0: financial stability; state 1: omitting or reducing dividend payments more than 40% below previous year; state 2: technical default and default on loan payments; state 3: protection under the Bankruptcy Act; and state 4: bankruptcy and insolvency.

A study by Dollery (2009) indicated that financial distress in Local Authorities is hard to evaluate because of several reasons. Firstly, different state Local government systems employ 'mixed approaches to measuring and recording financial data' with significant 'inconsistencies' between different states. Secondly, asset valuation was both infrequent and typically made different assumptions about the longevity of Local government assets. Finally, 'incomplete' financial and asset management records, especially in smaller councils, rendered accurate comparisons impossible.

As a consequence, the PWC Report (2006) adopted two separate methods in their evaluation of the financial viability of Local councils. In the first place, the PWC Report applied financial ratio analysis to a sample of 100 Local councils weighted by the number and type of Local council in each state. Secondly, the PWC Report uses descriptive statistics, surveys, interviews and data from questionnaires to analyse the financial viability of LAs.

The Financial Sustainability Review Board (FSRB) of 2005 advanced a quadrilateral set of key financial indicators 'for assessing a council's financial sustainability'. These indicators were: (a) net financial liabilities as the 'key indicator of the council's indebtedness to other sectors of the economy'; (b) operating surplus or deficit as the 'key indicator of the intergenerational equity of the funding of the council's operations'; (c) net outlays on the renewal or replacement of existing assets as the 'key indicator of the

intergenerational equity of the funding of the council's infrastructure renewal or replacement activities'; and (d) net borrowing or lending as the 'key indicator of the impact of the council's annual transactions – both operating and capital – upon the council's indebtedness to other sectors of the economy'.

According to Local Government Index (LGI) of 2006 key performance benchmarks such as Net Debt, Net financial liabilities, Net borrowing /lending and net interest expense as illustrated in appendix (IX) may be used to assess financial distress/challenges in Local Authorities. A study by Boex and Muga (2009) used the following measures of financial performance to indicate the level of financial health of Tanzania Local Authorities; a) expenditure outrun ratio (or budget performance ratio), b) The annual audit opinion that is issued by the National Audit Office for each Local government, c) the percentage of expenditures questioned by the NAO during the audit process. This study concluded that one can hypothesize that Local Authorities' financial management performance in Tanzania is a positive function of Local administrative and managerial practices. For the purpose of the current study, the Key Performance Indicators identified by Boex and Muga (2009) shall be used to measure financial challenges facing Local Authorities in Kenya.

Given a likert scale of 1 to 5, Local Authorities scoring a   mean of 0 to 1.65 were rated as lowly distressed Local Authorities, those scoring above 1. 65 to 3.335 were termed as

moderately distressed Local Authorities while those Local Authorities with a mean score of over 3.335 were described as highly distressed. However, the magnitude of the demarcation/classifications may change according to the weighting system.

2.3.2 Financial Management Practices

Financial management is found in both private sector and public sector as it is an important activity in the management and sustainability of an institution. The definition of financial management depends on the type of institute on and varies depending on whether it is a donor, the government or the private sector. However, the majority for the activities and the objectives of financial management appear to cut across all organizations. According to Lee, Lee and Lee (2009), there are two possible approaches in defining financial management, a descriptive one; and an analytical and operational one. From a descriptive standpoint, financial management is composed of three of the major policies of a firm: its investment, financing, and dividend policies.

However, from an operational standpoint, financial management includes both short term financial management and long term financial management. Short term financial management includes the management of working capital items such as cash management, inventory management, accounts receivable management and the like (Lee et al , 2009). On the other hand, long term financial management is defined as financial management that encompasses essentially all decision making that has an impact over a

period of one year or more (Lee et al, 2009).

According to the business dictionary (2010), Financial management is the "The planning, directing, monitoring, organizing, and controlling of the monetary resources of an organization". According to Working Party on Aid Effectiveness, Joint Venture on Public Financial Management (2008) public financial management is generally understood to "include all components of a country's budget process – both upstream (including strategic planning, medium-term expenditure framework, annual budgeting) and downstream (including revenue management, procurement, control, accounting, reporting, monitoring and evaluation, audit and oversight)"

Financial management can be defined as the management of the finances of an organization in order to achieve the financial objectives of the organization and consists two aspects namely; financial planning and financial control (Whonderr-Arthur, 2009). Harif and Osman (2006) define financial management as an activity that comprises of six components, namely, "financial planning and control, financial accounting, financial analysis, financial accounting, capital budgeting, and working capital management". For the purpose of this study the researcher undertook to investigate the effect of financial management on financial challenges facing Local Authorities in Kenya. The researcher addressed the components of financial management according to Harif and Osman (2006).

Boex and Muga (2009) asserted that Local financial management practices are measured based on assessments of the Local budgeting system, strategic planning system, fall-back system, accounting/reporting system, internal control system, and the Local financial leadership system. While Singer (2004) finds statistically significant (albeit moderate) correlations between Local financial conditions and Local financial management practices among the U.S. municipalities in her sample, regression analysis fails to indicate any statistically significant relationship between a Local government's financial performance and financial management practices after controlling for governance and socioeconomic factors. The studies by (Capalbo, Grossi, Ianni & Sargiacomo, 2010; Carmeli, 2008; Deal, 2007; Frank & Dluhy, 2003; Kloha, Weissert, & Kleine, 2005 and Watson, Handley & Hassett, 2005) confirmed that financial mismanagement contributes to financial distress in Local Authorities.

The current study adopted the following variables of financial management practices in Local Authorities that may lead to financial distress; internal control processes, financial governance, financial reporting/ tracking and control systems, capital budgeting and the annual budgeting process.

2.3.3 Corporate Governance

Sanda, Mikailu and Garba (2005) defines corporate governance as mechanisms that are concerned with ways in which all parties interested in the well-being of the firm (the

stakeholders) attempt to ensure that managers and other insiders take measures or adopt mechanisms that safeguard the interests of the stakeholders. The Cadbury report (1992) defines corporate governance as the system by which companies are directed and controlled. According to Claessens (2003), corporate governance is the set of processes, customs, policies, laws, and institutions affecting the way a corporation (or company) is directed, administered or controlled. Corporate governance comprises the long-term management and oversight of the company in accordance with the principles of responsibility and transparency.

Claessens (2003) also defines corporate governance as the range of institutions and policies that are involved in these functions as they relate to corporations. On the other hand, Shleifer and Vishny (1997) also define corporate governance as "mechanisms of economic and legal institutions that can be altered through political process".

O'Toole (2005), in exploring community governance in Victorian Local government tested the extent to which councils were using new governance ideas. The context was the policy decision by the Blacks Labor government, following the defeat of the Kennett Liberal government in 1999, to redefine good governance and to embrace engagement by the community in the governing process. He reviewed council annual reports to determine how they were reporting on governance and the extent to which they referred to external governance. He found that over half the respondents had some section which

referred explicitly to the term governance, but the term community governance was rarely used if at all used. However 18% of the councils reported on community participation through different council forums and committees. This may be seen as a form of community governance.

A study by Muranda (2006) assessed the role of corporate governance on financial distress in Zimbabwean Banks. The author observed that in all cases of pronounced financial distress, either the chairman of the board or the chief executive wields disproportionate power in the board. The disproportionate power emanates from major shareholding. The overbearing executive overshadows other directors, executive and non-executive, thus creating power imbalance in the board. A study by Joh (2001) attempted to examine how ownership structure and conflicts of interest among shareholders under a poor corporate governance system affected firm performance before the crisis. Findings indicated that Controlling shareholders expropriated firm resources even when their ownership concentration was small. Firms with a high disparity between control rights and ownership rights showed low profitability.

Studies done by Moreno (2005); Frank and Dluhy (2003), demonstrate the contribution of corporate governance to good financial management practices of Local Authorities. The authors found a positive relationship between corporate governance mechanisms and good financial management practices. Literature by Boex and Muga (2009); Kloha,

Weissert, and Kleine (2005) also assert that organizations that uphold tenets of corporate governance also reduce the risk of financial distress.

Specifically, the following aspects of corporate governance were investigated by the current study; Transparency through display of performance results; transparency through audited accounts; Accountability through signing the performance contract and adhering to service delivery charter; leadership structure that supports governance; corruption cases and community participation in decision making.

2.3.4 Information Technology

The value of information technology in Local governments cannot be overemphasized. In this case, Pradhan (2002) attempted to define information technology as "all computing and communication technologies". Organizations such Local governments would not afford to lag behind in adopting information technology. Information technology is that critical that it facilitate collection, storage and retrieval of information. Authors such as Odedra (1996) again concluded that information technology can be defined as "a tool of socio-economic development" and he was of the opinion that use of information technology enhances faster and broader communication of information.

Awe (1997) was of the view that information technology is defined as " technologies that ensure a more accurate and cost effective knowledge to support decision making,

reduces mental and physical efforts in solving certain tasks; reduces or eliminates inefficient practices, it rivals the manual system and improves services rendered to customers". Finally, International Foundation for Information Technology (IF4IT) also defines Information technology as "the study, design, development, implementation, support or management of computer-based information systems, particularly software applications and computer hardware". Information technology is used by many organizations such as Local governments to facilitate effective and efficient provision of services to citizens. Implementation of Information technology leads to increased efficiency and effectiveness of services and as a result there is occurrence of cost reduction (Schelin, 2006).

Waema and Mitullah (2007) conducted a study on E-governance in Local Authorities in Kenya. The authors concluded that ICTs are at an infancy stage in Kenya and ICTs have potential of reversing the trend of ineffective governance and improving participation, transparency, accountability, responsiveness, effectiveness and efficiency which are major governance constructs. The authors further observed that (Local Authority Integrated Financial Operations and Management System) LAIFOMS was limited to financial management and that it was still to penetrate other aspects and engagement with citizens. They also observed that Access to computers and internet was limited and hope for ICT application lies on mobile phones.

A study by Jensen (2002) observed that Local municipalities in Africa are a fertile ground for the application of ICTs. They are at the front lines of government in their service-oriented interaction with the public and business, often in transaction based systems with many, interlinked components. As such, municipalities have considerable potential to assist in the process of integration of ICTs into the daily lives of its citizens. Municipal operations from an information technology perspective can be divided into three areas – 1) internal, 2) intra-governmental, and 3) external (with the public). This study concluded that ICT adoption in African Local Authorities would substantially improve their financial fortunes.

The current study endeavored to demonstrate how the common components of ICT have been adopted in Kenyan Local Authorities and how this state of affairs has contributed to financial challenges facing Local Authorities. These components included people, hardware, software, data, and information procedures (Jensen, 2002; Waema & Mitullah, 2007 and Schelin, 2006).

2.3.5 Human Resource Management

According to Mathew (2007), Human resource Management (HRM) is a set of tools to help you organize, plan, and implement personnel in organizations. Human resources include paid staff, volunteer staff and members of the board. The author further observes that the tools used in HRM fall into six areas: a) Staffing b) Employee and Labour

Relations c) Total Compensation d) Workplace Health and Safety e) Organizational Learning, Training and Development f) HR Information management. Johnson (2000) describes best practice or high performance work practices as HR methods and systems that have universal, additive, and positive effects on organisational performance. Mess (2004) outlines five (5) best practices of human resource management which includes 1) Training and development 2) Teams 3) Employee selection 4) Performance Appraisals 5) Communication.

The aim of training and development within an organization is to provide staff with the necessary skills and knowledge to fulfill the organization's corporate and business plan (Johnson, 2000). This however, is not simply related to specific training for a work practice, as training of any type is essential as it creates a learning ethos (Pfeffer, 1996). In many instances training and development is seen as a frill, rather than a necessity, even though it has been proven that training can provide a competitive advantage to those firms who have the wisdom to use it (Pfeffer & Veiga, 1999). The area of employee selection details the benefits that approaching this function as a best practice has to the organization.

O'Leary, Lou Lindholm, Whitford, and Freeman (2002) state that the most successful organizations of the future will attract, engage, retain and develop the best and brightest employees. Recently there has been an increased use of performance appraisal and

compensation as a means of increasing overall commitment toward the organization (Enz & Siguaw, 2000). There are many methods of performance appraisal that are used within organisations today, such as operational performance and productivity benchmarking for example, performance appraisals with management, average sales figures, organisational performance, and turnover to name a few.

Capalbo, Grossi, Ianni and Sargiacomo (2010) identified incompetence and corruption among Local government officials as major determinant of financial distress in Local Authorities in Italy. Wunsch (2001) noted that in the area of personnel management and human resources, civil servants especially those with technical qualifications get confused as to their Authority and status which further affects their ability to deliver. The current study outline parameters of human resource management practices that have contributed to financial distress in Local Authorities, such as lack of relevant training, no performance rewards and sanctions, increased corruption, just to mention but a few .

2.3.6 Government Regulations

Harris and Carnes (2011) define regulation as administrative legislation that constitutes or constrains rights and allocates responsibilities. It can be distinguished from primary legislation (by Parliament or elected legislative body) on the one hand and judicial decisions on the other hand. West's Encyclopedia of American Law (2008) defines government regulation as a rule of order having the force of law, prescribed by a superior

or competent Authority, relating to the actions of those under the Authority's control. Hertog (1999) defines regulation as taken to mean the employment of legal instruments for the implementation of social-economic policy objectives.

Several regulations that have affected the financial and non financial capacity of Local Authorities have been formulated and implemented in Kenya. According to the Institute of Economic Affairs (2009), government regulations that have a direct impact on the financial operations of Local Authorities include the Transfer of Functions Act (1969) which saw the central government take over key responsibilities from Local Authorities. The second regulation was the abolition of the Graduated Personal Tax in 1974 which took away the major source of revenues to Local Authorities. The third significant regulation was the passing of the constituency Development Act Fund Act (2003) which initiated the mechanism for financing community projects at constituency level in competition with Local Authorities thus further weakening the focus on councils as the primary channel for service delivery at the Local level.

Boex and Muga (2009) investigate the determinants of quality financial management in Local Authorities in Tanzania and concluded that government regulation can have both positive and negative effects on the financial performance of Local Authorities. A study by Capalbo, Grossi, Ianni and Sargiacomo (2010) attempted to investigate the nature of financial distress in Italians Local governments and concluded that bureaucracy and poor

legislation are major causes of financial distress in Local Authorities.

The current study tried to investigate the extent to which government regulations among other factors has contributed to financial distress facing Local Authorities in Kenya. Other studies by (Carmeli, 2008; Deal, 2007; Frank & Dluhy, 2003; Kloha, Weissert, & Kleine, 2005 and Watson, Handley & Hassett, 2005) confirmed that the government regulation on Local authorities and lack of government support contributes to financial distress in Local Authorities.

2.4 A Critique of the Past Studies/Empirical Review

This section discusses the empirical literature. It reviews previous studies on the discourse of determinants of financial challenges in Local Authorities. Studies on this area will be compared and contrasted in terms of methodology, objectives, variables, conclusions and research gaps.

Dollery (2009) investigated the emergence of acute financial distress in all Australian Local government state and territory jurisdictions. The study by Dollery (2009) was motivated by the frequent national and state based inquiries into the financial sustainability of Local councils in the dawn of the new millennium. The mainstay of this study was to establish the extent and degree of financial distress in Australian Local Authorities. The study used a literature based methodology by analyzing the findings of

the PWC (2006) report. The second approach of Dollery (2009) was to critique the policy recommendations that have been advanced by various published sources on ways to curb financial un-sustainability in Australian Local Authorities.

The study by Dollery (2009) noted that there were various policies that had been recommended for dealing with financial unsustainability in Australian Local governments. These policy recommendations were; (a) structural reforms in form of forced amalgamation of councils and internal reforms (b) Increased fiscal transfers from central government to Local government (c) increased borrowings by Local councils inform of fixed interest bond issues. Finally, the study also note that there were other possibilities for curtailing financial un sustainability such as relaxing rate capping regulations and the introduction of additional revenues sources such as environmental taxes.

This study significantly differs from the present study in the following ways; the present study adopts a field based methodology and investigates the determinant of financial challenges whereas Dollery (2009) attempted to explain the extent and degree of financial distress in Australian Local Authorities. Lastly, the two studies differs because Dollery (2009) was conducted in Australia (developed country) while the present study is conducted in Kenya (developing country).

A study by Capalbo, Grossi, Ianni and Sargiacomo (2010) investigated the nature of financial distress in Italians Local governments. In order to understand the nature of financial distress and the attitudes of central government towards distressed Local governments, Capalbo, et al (2010) adopted various approaches. First, the study proposed a synthetic outline of the national legislative framework on financial distress of Italian Local governments through analyzing data on the number, dimension, and geographical position of distressed Italian Local governments.

Secondly, the study focused on the causes of financial distress in Italian Local governments by reviewing sample based scholarly studies and also by referring to comprehensive analysis done by the court of auditors. Thirdly, the study analyzed the level of the central government involvement in addressing the financial distress of Local governments through a review of legislative measures, the extent to which legislative interventions have changed. After reviewing the scholarly articles on causes of financial distress in Local Governments, Capalbo, et al (2010) noted that the main causes of financial distress could be grouped in to two approaches, the social economic decline approach and the Local management approach.

The social economic decline approach assumes that causes of financial distress are external to Local Authorities and that they are beyond the control of Local government officials. Such causes include: contraction of economic growth, movement of city

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dwellers to outskirts of the major cities, demographic changes such as increase in population, reduction in Local business activity, unemployment and tax base erosion, bureaucracy and poor legislation.

The Local government approach assumes that incorrect managerial practices such as poor accounting and budgeting methods, incompetence and corruption among Local officials, division of Local governments in terms of political size and procedures and vulnerability of special interest groups. In conclusion, Capalbo, et al (2010) argues that financial distress does not arise because of one set of factors but arises due to a mix of both external and internal factors.

Further, the researchers found that there was a shift of attitude by Italian central government from general form of intervention to specific form of intervention especially in the case of big cities. The above study compares well with the present study where both studies focus on the causes of financial distress. On the other hand, the study differs from the present study in terms of methodology. Whereas Capalbo, et al (2010) mostly focuses on literature review to conclude on the aims and objectives, the current study adopts a field study based approach. In addition, the present study uses statistical modeling in the form of regression analysis while Capalbo et al (2010) is only descriptive.

Study by Kimhi (2008) discussed the legal remedies for financial crisis facing Local Authorities. This study reviewed three remedies that have been developed to address financial crisis in Local Authorities which included; creditor's remedies, the bankruptcy code and state financial boards. Using a literature based methodology; the study compared and contrasted the merits and demerits of the three legal remedies. The study identified that the most superior legal remedy was state financial board. The researcher concluded that timely state intervention in form of state financial boards should be emphasized as a remedy to financial crisis.

Finally, the study recommended the enactment of proactive ex-ante state approach which enables Local Authorities to improve their credit ratings and reduce the cost of borrowings. This study contrast significantly with the present study which looks at the determinants of financial distress in Local Authorities. Another point of contrast is that the present study concentrates on Kenya which is a developing country while Kimhi (2008) focuses on cities such as Miami, Philadelphia, New York which is from a developed country.

A study by Honadle (2006), sought to establish the role that the state play in dealing with Local government financial crisis in United States. The study also attempts to explain the state policy formation as a response to Local government financial crisis. The overriding objective of the study was to establish whether states are more rational –comprehensive

or incremental in their approaches to dealing with Local government financial crisis. The study used data from a telephone survey consisting of 10 questionnaires administered to members of National Association of State Auditors, Comptrollers and Treasurers from 50 states.

Using a survey based methodology, the study attempted to answer the following research questions namely (a) Are states comprehensive in their approach (b) At what point in the "life" of a crisis do states get involved (if at all)?, and (c) When states opt to make changes to their policies relative to Local government fiscal crises, how (in what fashion) are states' policies evolving to deal with crises? Research findings by Honalde (2006) concluded that an incremental approach was the most approach used by states to develop policies aimed at stemming Local financial crisis. The results also indicated that policy entrepreneurs need to find the right balance between a" technical fix" and politics in order for their proposals to be adopted. This study contrast with the current study in that it focuses on the role that the state play in dealing with Local government financial crisis in United States while the current study focuses on the determinant of financial challenges of Local Authorities in Kenya

A study by Wunsch (2008) carried out a literature based study and attempted to understand why decentralization has failed in Africa. Wunsch (2008) argued that although many African countries have pursued decentralization reforms, these reforms

have not managed to bring about effective governance. Wunsch (2008) indicates that failure in reforms occurs in four areas which attract substantial resources are distributed. These four areas are planning and capital investment, budgeting and fiscal management, personnel systems and management, and finance and revenue.

In the area of planning and capital investment, the study noted that even though planning is touted as a part of decentralization, it has consumed Local government resources, eroded their credibility, demonstrate their lack of Authority and sustained both national and Local levels of grass roots disempowerment. In the area of budgeting and fiscal management, the study noted that Localities have a serious problem in managing their affairs through effective budgeting mainly because they have insufficient technical personnel to undertake budgeting activities. In addition, the interference from central government in the budgeting process is another contributor to poor budget and fiscal management.

Wunsch (2008) noted that the countries where such patterns were found included Kenya, Ghana, Uganda, Nigeria and Swaziland. In the area of personnel management and human resources, civil servants especially those with technical qualifications get confused as to their Authority and status which further affects their ability to deliver. Wunsch (2008) also noted that the area of finance and revenue is plagued by many issues such as the instability of national grants and transfers, limited sources of Local Authorities to raise

revenue, and conflict between Local governments and Local units such as the provincial administration. The study by Wunsch (2008) compares well to the present study since both refer to Local governments in developing countries. However, the two studies differ in the methodologies. Wunsch (2008) used literature based methodology to infer the results while the current study uses statistical modeling to derive the determinants of financial distress among Local Authorities in Kenya.

The report by Institute of Economic Affairs (2009) attempted to demystify the concept of Local governance by analyzing principles of good governance, importance, objectives and mandate of Local governments. It also described how revenues are raised and spent and the revenue challenges facing Local Authorities. It was also in this report that resource mobilization was discussed as an important element of enhancing Local Authority revenue and service delivery. The main similarity of this report to the present study lies in the choice of Local Authorities in Kenya as the scope. In addition, the report also highlighted the problem of financial distress in Local Authorities by emphasizing that despite increase in Government revenue transfers the Local Authorities are unable to cover the cost of increased demand for services and inflation (IEA, 2009).

The report also highlighted the problem of poor collection of revenue as a contributor to financial distress in Local Authorities and this was exemplified in the following extract from the report.

"Collection of revenue is a big challenge to Local Authorities. For example there is a very high rate of land rate defaulters. For instance, the city council of Nairobi by the 3rd quarter of the FY 2007/2008 had collected KShs. 3,737,477 against the budgeted Ksh. 6,600,000. This means that the City may implement only 50% of the programmes they had planned the money for City Council of Nairobi" (IEA, 2009).

Finally, the report alluded to the insufficiency of Local Authority transfer fund as a source of revenue for Local Authorities. It was observed that the main purpose to which the Local Authority transfer fund was applied to was debt resolution, leaving the Local Authorities without enough finances to fund the provision of basic services. Other than the insufficiency of LATF, the Institute of economic Affairs report (2009) identified the gradual removal of some functions of Local Authorities to the central governance as a major hindrance to the financial sustainability of Local Authorities. The gradual removal of the functions and its consequence on declining revenue is idealized in the following extract;

"The Graduated Personal Tax (GPT) was removed from municipalities in 1973. This was followed with the removal of grant system from county councils. The GPT was replaced with specific grants to cover certain services. In 1989, the specific grants were replaced by service charge. This was a charge levied to business premises and employees in formal and informal sector. Again the service

charges was abolished and in its place, the Local Authorities Transfer Fund Act (LATF 1998) was introduced" (IEA, 2009 pp 22).

Despite the results of Institute of Economic affairs report (2009) bearing a striking resemblance to the present study, it did not address the role played by the adoption or non adoption of information technology on the declining revenue and financial distress.

In an attempt to critically analyze the Rapid Results Approach to Local service delivery in Nairobi City Council, Osiche (2007) using literature based methodology observed that some amount of progress was seen to be made in the area of the financial management. Set criteria leading to disbursement and accessing of scarce council funds were strictly followed despite the limited time of the RRI implementation. The study noted that there are institutional capacity and other problems whose persistence are binding constraints to RRI implementation and can only be resolved if there is a re-think about putting in place an enabling governance, policy, legal and cultural environment to avoid institutional bottlenecks .

Osiche (2007) concluded that implementation of RRI practices in Nairobi City council may impacts positively to service delivery and right outcomes. In terms of revenue collection, the council collected a record Kshs. 7 million more in parking fees between October and December, 2006, compared to the same period in the previous calendar year

(Adero, 2007). This report did not address some key practices such as the role of strategic planning in the financial decline of Local Authorities which may have a bearing to the level of financial distress being witnessed by Local Authorities in Kenya.

However, Miring'uh and Mwakio (2006) assert that there is overwhelming evidence that recent reform measures, including RRI have failed to stop immense hemorrhage of revenue at the City Hall. A recent damning forensic report by the Kenya Anti-Corruption Commission, states that City Hall continues to lose a huge portion of parking fees, land rates or rent to corrupt officials exploiting weak financial management systems (KACC, 2007). According to KACC (2007) says perpetrators of the rip-off at the Council had devised a complex system to block evidence of unremitted money estimated to be worth millions of shillings. Key to the racket is concealment of the paper work involving such money, including bouncing cheques, tempering with the numbering of parking fees receipts and the filing of fraudulent expenditure claims at the council's cash office.

Schoeman (2011) investigated fiscal performance in terms of own-revenue collection and sustainability of Local municipalities in South Africa. The study used Local government revenue data on 237 municipalities as reported in the South African national Treasury and adopted conventional Uctum and Wickens model. This study noted that a large number of municipalities do not comply with the requirement that a "reasonable" amount of current expenditures be financed by means of own resources. Furthermore, Local

governments finances are featured by substantial variance as far as collection of own income is concerned. The two studies differ in the methodologies. Whereas Schoeman (2011) adopted conventional Uctum and Wickens model to estimate the extent of fiscal performance in terms of own-revenue collection and sustainability of Local municipalities in South Africa, the current study uses simple regression to derive the determinants of financial distress among Local Authorities.

Fjelstad, Henjewele, Mwambe, Ngalewa and Nygaard (2004) attempted to analyze changes in Tanzanian Local Authorities' capacity for financial management and revenue enhancement, and changes relating to governance, including accountability and responsiveness of the Local government. The study used data on expenditures, finances and financial management for the period 2000-2003 for six Tanzanian Local Authorities, combining both quantitative and qualitative methodologies. Using a survey design collected data from 1260 respondents. The study concluded that there is a causal relationship between financial management of Local Authorities and governance. Whereas this study uses expenditures, finances and financial management as its main variables, the current study uses more variables such as corporate governance, human resource management, ICT, government regulations and financial management practices.

Jonga and Chirisa (2009) attempted to explore the criticalness of decentralized governance as a solution towards service delivery challenges experienced by

Zimbabwean urban centers. This study observed that it was lamentable that the messy reality of governance in Zimbabwe and the economic meltdown in the country has rendered most of the councils un-creditworthy to Local and international banks, leaving the borrowing powers by urban councils in the hands of central government to the detriment of rapid decision-making let alone service delivery.

The study used 52 respondents who were subjected to a simple random sampling. Data was collected through interviews, questionnaires and documentary reviews and the findings asserted that almost all towns and cities in Zimbabwe have been grappling with raising sufficient revenues for capital and recurrent expenditures. This study differs from the current study in that it used interviews, questionnaires and documentary reviews to collect data while the latter uses only questionnaires to both Officers of the Councils and the customers to these Councils.

Another study by Sennoga (2004) on relationship between Local government revenues and expenditures in Uganda, where a Granger-causality test was conducted and estimation was done via a vector autoregressive model using data from fifty six (56) districts for the period 2001 to 2003. The study findings revealed that the management of Local government finances in Uganda conforms to the tax-spend hypothesis where Local governments raise tax revenue and/or request for or receive grants before engaging in new expenditures. Further, the study showed that increases in revenues lead to less than

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proportionate increases in Local government expenditures which lend credence to the flypaper effect. While this study uses Granger-causality test to examine the interrelationships between government revenues and expenditures, the current study uses a simple regression to establish the factors that contribute to financial distress among Local Authorities.

Carmeli (2008) conducted a study on the financial distress of Local governments in Israel. Using case studies and hard (accounting and statistics) data, the author attempted to provide a critical analysis of the financial distress affecting Local governments throughout Israel and the potential remedies for the observed financial distress. These findings clearly indicate that the Local Authorities in Israel are in a state of financial distress.

The findings further show that the sources of financial distress of Local governments in Israel can be classified into three major groups: structural or fixed (consists of Local Authorities' size, residents' socioeconomic status, and governmental resource allocation), organizational (consists of performance evaluation, transparency, and the role of the Local government's management), and hybrid (consists of the relationship between the central and the Local governments) factors.

The above study compares well with the current study as far as conceptualization is

concerned. Both studies investigate the causes of financial distress. However, the context and the methodological aspects are different. While the current study was done in Kenya the above study was done in Israel. The current study will be a survey while the above study used case studies. The conceptual framework differs somewhat with the current s study since it employs a three latent variable framework as causes of fiscal distress (structural/fixed factors, organization factors and hybrid factors). While the current study will use primary data to measure fiscal distress, the above study used hard accounting data.

Deal (2007) carried out an examination of municipal finance reform regarding municipal bankruptcies in the United States. The study used a case study methodology by selecting nine Alabama municipal bankruptcies. The research design for the case studies included documentary analysis, which is a combination of the documentation and archival records. The authors conducted interviews in order to gain a better understanding of the most recent municipal bankruptcies that occurred at the county, city and town levels of government in Alabama.

The study found that the overall contributing factors found were a mixture of financial mismanagement by public officials and the economic decline of the municipalities from loss of businesses and demographic changes. The current study compares well with Deal (2007) since both address financial challenges facing Local Authorities. However the

studies differ since the current study uses a survey methodology while Deal (2007) uses a case study methodology in addition the studies differ since they were done in different countries.

Frank and Dluhy (2003) studied the fiscal decline of Miami, Florida during the period of 1996-2001. Their intent was to draw lessons from this financial crisis that municipalities could utilize in their future planning to avoid such a crisis themselves. The authors found that the financial practices previously employed by Miami city management were not up-to-date, did not promote good stewardship of the city's finances through internal checks, and were not current in the accounting procedures. Frank and Dluhy (2003) concluded that Miami's fiscal crisis could have been avoided if management practices, especially those in the accounting and budgeting areas, had been implemented and if the government officials had been held accountable by the voters of the Miami area. This study just like the current study uses accountability and transparency as independent variables. The two studies differ in terms of scope and period of study.

Kloha, Weissert, and Kleine (2005) developed and tested a composite model to predict Local fiscal distress in hopes of developing an early warning system that will enable state and local government officials to be proactive rather than reactive to fiscal distress situations. The authors used a sample of 97 cities and 53 townships in Michigan, totaling 15 Local governments, during the time period of 1991-2001 for cities and the 1994-2001

time periods for townships. The data were comprised of financial information from comprehensive annual financial reports and audits of those reports as well as socioeconomic data from the U.S. census and labor statistics.

Kloha, Weissert, and Kleine (2005) developed a 10-point scale of fiscal stress using a pre-set standard on the nine variables that distinguished "good" from "bad" performance indication. The authors concluded that this particular 10-point scale achieved their major objective of predicting fiscal stress before it occurred in the Local government. The two studies are similar in terms of conceptualization since they both focus on financial distress of Local Authorities. However the studies differ in terms of modeling and Operationalization of variables, for instance above study used Ratios to measure financial distress while the current study will use both ratios and non-financial indicators.

Watson, Handley and Hassett (2005) have also studied the causes of financial stress, including the municipal bankruptcy that was filed by Prichard and Alabama in 1999. The authors identified five socio-economic conditions they believe were significant contributors to fiscal stress in Local governments. These are financial mismanagement, decline in population, rising per capita costs, structural change in the economic base, natural or man-made disasters, and civic distrust. The authors cited financial mismanagement as the most common factor and echoed by Frank and Dluhy (2003) findings that these problems occurred gradually and a lack of strategic planning

contributed greatly toward the overall effect. This study by Watson et al (2005) is similar to the current study since they both studied the causes of financial distress. The studies differ since current study will be done in a developing country while the above study was done in a developed country.

2.5 Summary

The above chapter reviewed the various theories that explain the independent and dependent variables. The reviewed theories are then critiqued for relevance to specific variables. The chapter also explored the conceptualization of the independent and the dependent variables by analyzing the relationships between the two set of variables. In addition, an empirical review was conducted where past studies both global and Local is reviewed in line with the following criteria, title, scope, methodology resulting into a critique. It is from these critiques that the research gap was identified.

2.6 Research Gaps

A critical review of past literature showed that several conceptual and contextual research gaps existed in the discourse of factors causing financial distress in Local Authorities. For instance, the studies by Watson, Handley and Hassett (2005); Kloha, Weissert, and Kleine (2005); Frank and Dluhy (2003); Deal (2007); Carmeli (2008) ; Capalbo, Grossi, Ianni and Sargiacomo (2010) investigated the factors contributing to financial distress in Local Authorities. However, all the above studies were carried out in developed and

emerging countries such as USA, Italy and Israel. It is therefore possible to argue that the socio economic conditions of developed and emerging economies are somewhat different from those of a developing economy like Kenya.

In addition, the reviewed literature indicates that few studies on causes of financial distress in Local Authorities in developing economies in general and Kenya in particular have been done. The reviewed Local studies (Jonga & Chirisa, 2009; Fjelstad, Henjewele, Mwambe, Ngalewa & Nygaard, 2004; Schoeman, 2011; Miring'uh & Mwakio, 2006; Adero, 2007; Osiche, 2007 and Wunsch, 2008) did not critically address the determinants of financial distress in Local Authorities which the current study critically examines.

CHAPTER THREE

RESEARCH METHODOLOGY

This chapter provides a discussion on the design and methodology that was used to carry out this study. This comprises of type of research design, population, target population, sampling frame, sample, sample size, sampling technique, instruments to be used, pilot test and data analysis.

3.1. Research Design

Research design refers to how data collection and analysis are structured in order to meet the research objectives through empirical evidence economically (Chandran, 2004). According to Cooper and Schindler (2007) research design is the plan and structure of investigation so conceived as to obtain answers to research questions. According to Kerlinger (1986) research design is the plan and structure of investigation so conceived so as to obtain answers to research questions. According to Kothari (2004), a research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure.

Social science research approaches are classified as descriptive, exploratory or explanatory (Kothari, 2004). Descriptive research aims at producing accurate representation of persons, events and situations and the exploratory research aims at

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seeking new insights into phenomena, ask questions, and assess the phenomena in a new light (Torochim, 2006; Winter, 2000 and Sekaran, 2006). On the other hand explanatory research focuses on studying a situation or a problem in order to explain the relationships between variables (Saunders, Goldenberg & Gallimore, 2008 and MacNeill, Cavanagh & Silcox, 2005).

Therefore, descriptive research is the first research about an issue, exploratory research is an attempt to investigate a social phenomenon without a clear anticipation or expectation and explanatory research involves seeking to identify the causes and effects of a social phenomenon and to predict how one variable will change in response to variation in another variable. The nature of the study whether it is exploratory, descriptive or explanatory depends on the stage to which knowledge about the research topic has advanced (Sekaran, 2006).

The current study took a descriptive design, which required analysis of the factors contributing to financial distress facing Local Authorities in Kenya. Descriptive research, also known as statistical research, describes data and characteristics about a population of phenomenon being studied. It answers research questions who, what, where, when and how is the problem. It is used for frequencies, averages and other statistical calculations (Saunders *et al.,* 2009). Descriptive research is used to obtain information concerning the current status of the phenomena to describe "what exists" with respect to variables or

conditions in a situation (Key, 1997). It also describes the characteristics or behaviour of a given population in a systematic and accurate version (Sekaran, 2006).

In the present study, the quantitative research paradigm was followed for the following reasons. Firstly, deductive reasoning was used to formulate research questions. Secondly, these research variables were operationalized and tested. Thirdly, the outcomes of the inquiry were examined and the theory modified in light of the findings. Lastly, it ensured that the empirical results confirm the theory that started with premises and leads to empirical generalization. These steps manifested a quantitative research approach according to Sekaran (2006), Cooper and Schindler (2006) and Saunders *et al.* (2009). Njuguna (2010) adopted a similar research design while investigating the strategies to improve pension funds in Kenya and the findings stood the test of validity and reliability.

3.2 Population

Population is a large collection of individuals or objects that is the main focus of a scientific query. It is for the benefit of the population that researches are done (Castilo, 2009). A population also refers to an entire group of individuals, events or objects having a common observable characteristic. Hence it's an aggregate of all that conforms to a given specification (Mugenda & Mugenda, 2003; Hyndman, 2008). It is also known as a well defined collection of individuals or objects known to have similar characteristics (Sekaran, 2003).

In this study there are two types of population. These are target population and accessible population. Accessible population refers to the population in research to which the researchers can apply their conclusions (Saunders et al., 2009). Target population refers to the entire group of individuals or objects to which researchers are interested in generalizing the conclusions (Castilo, 2009). According Gall, Gall and Borg (2007), target population consists of all members of a real or hypothetical set of people events or objects from which a researcher wishes to generalize the results of their research while accessible population consists of all the individuals who realistically could be included in the sample.

For the purpose of this study the target population comprised of all 175 Local Authorities in Kenya, which included 3 cities, 43 Municipal Councils, 67 County Councils, and 62 Town Councils. The list of local Authorities is given at the appendix VII. Due to considerations in time and money, a representative sample was selected from which conclusions were drawn. This was known as the accessible population (Mugenda & Mugenda, 2003). The accessible population was determined by the sampling frame and discussion with the researcher's supervisor.

3.3. Sampling Frame

A sampling frame is a list of population from which a sample was drawn (O'Leary, 2001). It is the source material or device from which list of all elements within a

population that can be sampled is drawn (Särndal, Swensson & Wretman, 1992) and may include individuals, households or institutions. It's a published list in which or a set of directions for identifying a population (Gall, Gall & Borg, 2007). Jessen (1978) highlights its importance based on features such as single representation of each and every element, numerical identifiers, contact information, maps, location and other relevant information presented in a logical and systematic fashion and exclusion of elements outside the population of interest (Sapsford & Jupp, 2006; Bernstein, 1998; Kish, 1995). Examples in real life would be electoral registers, attendance registers and so on.

A sampling frame facilitates formation of a sampling unit that refers to one member of a set of entities being studied which is the material source of the random variable (Bailey, 2008; Klaus & Oscar, 2008; Cochran, 1977 and Särndal, Swensson & Wretman, 1992). Common examples of a unit would be a single person, animal, plant, or manufactured item that belongs to a larger collection of such entities being studied. For the purpose of this study, sampling frame of 175 Local Authorities was source from the ministry of Local government as at 31st December, 2011 appendix VI.

3.4 Sample and Sampling Technique

A sample is a subset of population (Hyndman, 2008). Marczyk, DeMatteo & Festinger (2005) defined a sample as a subset of the population to be studied. It is a true

representative of the entire population to be studied (Leary, 2001). Similarly sampling is the selection of a subset of individuals from within a population to yield some knowledge about the whole population, especially for the purposes of making predictions based on statistical inference (Scott & Wild, 1986; Black & William, 2004). Its main advantages are cost, speed, accuracy and quality of the data (Adèr, Mellenbergh, & Hand, 2008). A good sample should be truly representative of the population, result in a small sampling error, viable, economical, and systematic, whose results can be applied to a universe with a reasonable level of confidence (Kothari, 2004). The sample of 20 Local Authorities was drawn from the 175 Local Authorities in Kenya.

In qualitative research, especially where purposeful sampling has been used among the sampling methods the goal is to select cases that are information rich with regard to the purposes of the study (Patton, 2002). It is for this reasons the study selected a sample of 20 Local Authorities. For each selected LA, 10 questionnaires was distributed to the relevant departments such as Administration, Treasurer, Audit, Human Resource Management, Works, ICT, Accounts and Public Relations depending on the council's establishment.

Sampling can be probabilistic or non-probabilistic. Probabilistic sampling refers to non-zero probability for selecting any element from the sampling frame. Non-probabilistic sampling occurs where the probability of selecting any particular element is unknown

(Kothari, 2004). According to Trochom (2000), non probabilistic sampling does not involve random sampling but a sampling technique where the samples are gathered in a process that does not give all the individuals in the population equal chances of being selected (Castillo, 2009). In probabilistic sampling every unit in the population has a chance of being selected in the sample, and this probability can be accurately determined.

The methods here are simple random, systematic, stratified and multi stage sampling. In simple random sampling all such subsets of the frame are given an equal probability and each element in the frame has an equal chance of selection (Mugenda & Mugenda, 2003). Systematic sampling relies on arrangement or order schemes coupled with selection of elements at regular intervals i.e. a random start and selection of every kth element from then onwards. In this case, k = (population size/sample size) (Kothari, 2004).

Stratified sampling divides a heterogeneous population into a number of distinct categories or strata of independent sub population from which individual elements can be randomly selected (Trochom, 2000). Cluster or multistage sampling involves two or more levels of units embedded in one another. The first constructs the groups (clusters) while the second randomly selects units from each group (cluster). It applies when the total area of interest is big and needs to be divided into smaller areas with the ultimate goal of drawing the sample from the smaller units (Kothari, 2004).

Non probabilistic sampling is where some elements of the population have *no* chance of selection or their probability of selection can't be accurately determined. It involves selection based on assumptions on the population that forms the criteria for selection (Gall, Gall & Borg, 2007; Mugenda & Mugenda, 2003).

The methods available here are convenience, quota sampling and snowballing. Convenience sampling also known as deliberate, purposive or judgmental sampling involves selecting a sample from that part of a population that's readily available and convenient. In quota sampling, the population is segmented into mutually exclusive sub-groups and then judgment is used to select the elements from each segment based on specified proportions (Kothari, 2004). Snowballing entails the use of a few subjects who direct the researcher to others who possess similar characteristics. It's useful when populations with particular characteristics aren't well known (Mugenda & Mugenda, 2003).

This study used mixed sampling techniques, specifically both stratified random sampling and simple random sampling. The choice of the techniques described here is based on the fact that Local Authorities are classified as one, Cities two, Municipal Councils three, Town Councils and four County Councils (MOLG, 2009). Therefore, stratification was based on the classification of Local Authorities. Stratified random sampling was preferred because; the population to be sampled was divided into homogenous groups

based on characteristics considered important to the indicators being measured. This method also helped to achieve gain in precision, flexible in the choice of the sample design for different strata and finally one is able to get estimates of each stratum in addition to the population estimate (Kothari, 2004).

Since the number of Local Authorities are scattered all over the country, this presented the study with a logistical problem. To select the sample of 20 Local Authorities, stratified random sampling was used. Specifically, the study used lottery method recommended by Kothari (2004) to pick ten percent of Local Authorities in every category. However, a 100% of city councils were picked. The study therefore used a sample of 20 Local Authorities selected as follows;

Table 3. 1: Population and Sample

Local Authority	Total Number	Sample	Sample Percentage
City Councils	3	3	100%
Municipal Councils	43	4	10%
County Councils	67	7	10%
Town Councils	62	6	10%
Grand Total	**175**	**20**	

The study targeted the town clerk of each of the 20 Local Authorities. The study also incorporated the views of middle level management from five departments in each Local Authority namely; 1) Treasury 2) Social Services, housing and public health 3) works/engineering 4) Environment 5) Others. The choice of middle level management was to act as a control for the response of the town clerks and because of their perceived lack of bias, impartiality in answering the study questions. In addition, they were more preferred than junior officers, since junior officers are perceived to be unaware of the pertinent issues affecting the Local Authorities.

The Local Authority customers were also included in the study to give a customer oriented perspective of the financial challenges facing Local Authorities. Six customers were purposively picked from the Local Authority area of jurisdiction. There was no restriction as to the type of customer and all customers were considered equal. For the purpose of this study, a Local Authority customer is any individual who contributes revenue or uses the resources of the Local Authority. He/she could be a parking space user, an open air market retailer, a hawker, a shopkeeper, a large sized, medium size or small size business. Therefore, such an approach was to yield 120 customers drawn from the 20 Local Authorities as demonstrated in table 3.2.

Table: 3. 2: Population Sampling Frame

Local Authority Department		Total Number
i.	Town clerk	20
ii.	Treasury (middle managers)	20
iii.	Social Services, housing and public health(middle managers)	20
iv.	Works/Engineering(middle managers)	20
v.	Environment(middle managers)	20
vi.	Others (middle managers)	100
vii.	Customers	120
Grand Total		**320**

3.5 Data Collection Instruments

The instruments of data collection were through questionnaires with both open-ended and close-ended questions. A questionnaire is a method of data collection in which respondents provide written answers to written questions (Gall, Gall & Borg, 2007). It's also defined as a research instrument consisting of a series of questions and other prompts for the purpose of gathering more information from respondents (Schilder, 2011). Questionnaires that contain open ended, closed ended and matrix type of questions were administered to the respondents through hard copies (Mugenda & Mugenda, 2003).

The instrument of data collection for this research was a questionnaire principally in the

English language which was targeting the respondents of each Local Authority. Further, the content of the questionnaires mirrored the key issues for follow up in the independent variables. The key areas of questioning were on the level of financial challenges/ distress, financial management practices, corporate governance, information technology, human resource practices and government regulations.

3.6 Data Collection Procedures

Data collection refers to the process of gathering raw and unprocessed information that can be processed into meaningful information, following the scientific process of data analysis (Gall, Gall & Borg, 2007). The questionnaires were sent to the respondents under a questionnaire forwarding letter accompanied by an introductory form the University. A qualified research assistant who had been trained on handling data collection was tasked with the delivery and collection of questionnaires.

3.7 Pilot Test

According to Project Star (2008), pilot testing is a trial run of procedures and instruments that one plans to use in carrying out a research. The main purpose of pilot testing is to catch potential problems before they become costly mistakes, provide an indication of time required for actual field work and possible modifications of the instrument and modality of data collection. The advantages of conducting the pilot test include enhancing the training of field staff, review of the instrument, prevention of wasteful

expenditures on a full blown survey whose results may not be applicable. The advantages outweigh the disadvantages of costs and the attendant possibility of redesign of both the survey and instrument (Creswell, 2003).

Pilot Testing ensures and that the field staffs have a common understanding of the instrument and guidelines provided alongside the questionnaire (Creswell, 2003). Cooper and Schilder (2011) indicated that a pilot test is conducted to detect weaknesses in design and instrumentation and to provide proxy data for selection of a probability sample. According to Babbie (2004), a pilot study is conducted when a questionnaire is given to just a few people with an intention of pre-testing the questions.

Pilot test is an activity that assists the research in determining if there are flaws, limitations, or other weaknesses within the interview design and allows him or her to make necessary revisions prior to the implementation of the study (Kvale, 2007). The subjects participating in the pilot study shall not be included in the final study to avoid survey fatigue. The rule of the thumb is that 1% of the sample should constitute the pilot test. This was applied in this study as it is. Therefore 2 Local Authorities participated in the pilot study (Kiambu and Ruiru Local Authorities).

3.7.1 Validity and Reliability

Creswell (2003) asserts that validity is strength of qualitative research, although other researchers prefer to substitute validity with terms such as trustworthiness, credibility,

transferability, dependability, and conformability (Gall, Gall & Borg, 2007). Validity exists when the knowledge sought is arrived at through descriptions that make possible an understanding of the meanings and essences of experience (Castillo, 2009). According to Seidman (2006), if the interview structure works to allow them to make sense to themselves, as well as to the interviewer, then it will have gone a long way towards validity.

Weber (1990) states that to make valid inferences from the text, it is important that the classification procedure be reliable in the sense of being consistent: Different people should code the same text in the same way. To make the study most valid, the content analysis is based on the conceptual framework in Chapter 2. Strategies for validating the accuracy of research findings offered by Creswell (2003) included obtaining data from three different sources of information or triangulation, member checking, which involves having the research participants review final reports to determine accuracy, and documentation using rich, thick descriptions.

Other methods used to validate qualitative research require that the researcher acknowledges and clarifies bias, provides discrepant information, and spends prolonged time in the field (Creswell, 2003). External reviews can also support validation of qualitative research. Creswell suggested that a colleague and/or an external auditor could provide additional insight into the study and research findings, and as proposed the

researcher shall form a working group drawn from senior management officers to ensure validity the findings of this research.

Reliability may be internal or external reliability. Internal reliability refers to the consistency of results within a particular site, and the plausibility of data within that site. External reliability refers to the consistency and duplicative attributes of data across the sites (Castillo, 2009). To ensure the internal reliability, low inference descriptors were used in the qualitative research stage in order to create a careful audit trail, by recording the data and interviews using an appropriate device (with permission). In quantitative research, reliability deals with an indicator's dependability, which means that the information provided by indicators does not vary as a result of the characteristics of the indicator, instrument, or measurement device itself (Gall, Gall & Borg, 2007).

To maximize reliability of the instrument used, the survey was constructed as follows: 1) a pilot survey was conducted to ensure the reliability of the questionnaire; 2) each question was framed succinctly to reduce ambiguity and minimize bias, thereby ensuring the high statistical value of the data; and, 3) each participant in the pilot survey was asked to state their job position to make sure participation was at senior-manager level. In short, the pilot test sought to demonstrate convergent and indiscriminate validity for all the constructs and reveal that all the scales meet or exceed the reliability thresholds for more established research (Castillo, 2009).

3.8: Data Processing and Analysis

Data analysis is a practice in which raw data is ordered and organized so that useful information can be extracted from it (Gall, Gall & Borg, 2007). Descriptive statistics such as mode, median, mean, standard deviation were used to perform data analysis. These measures were calculated using Statistical Package for the Social Sciences (SPSS 17.0) software. This is because it is user friendly and gives all the possible analysis. A qualified statistician helped to run the statistical tests (Castillo, 2009).

Descriptive statistics were used to determine the main determinants of financial challenges facing Local Authorities in Kenya following responses from the raw data. These statistics includes mean, median, mode, skewedness, range, standard deviation, kurtosis and percentages. The data was presented in form of tables, pie charts, column and bar graphs. The relationships in the research questions, was determined using the following Ordinary Least Squares (OLS) regression model as prescribed by various Scholars (Faraway, 2002; Cohen, West & Aiken, 2003 and Kline, 1998).

The use of ordinary Least Squares Regression is preferred due to its ability to show whether there is a positive or a negative relationship between independent and dependent variables (Castillo, 2009). In addition, OLS is useful in showing linear elasticity/sensitivity between independent and dependent variables (Cohen, West & Aiken, 2003). For instance, the current study would like to know the percentage by which

responses on financial distress increases or decreases when responses on financial management practices, human resource management practices, corporate governance practices, government regulations and information technology change by 1 percent. Furthermore, OLS was useful in showing whether the identified linear relationship is significant or not.

The output of OLS consists of an R squared, F statistic and regression coefficients. Lomax (2007); Tabachnick, Barbara and Fidell (2007); Wichura (2007) assert that a high F statistic indicates that the null hypothesis of lack of joint fit is rejected. Everitt, (2002); Nagelkerke, (1992); Glantz and Slinker, (1990) asserts that the coefficient of determination R^2 is used in the context of statistical models whose main purpose is the prediction of future outcomes on the basis of other related information. It therefore indicates the proportion of variability in a data set that is accounted for by the statistical model. It also provides a measure of how well future outcomes are likely to be predicted by the model.

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \varepsilon$$

Where Y= Financial Distress

α = constant (intercept)

β = slope (gradient) showing rate dependent variable is changing for each unit change of
        the independent variable.

X_1= Financial Management practices

X_2 = Corporate governance

X_3 = Information Technology

$X_{4=}$ Human Resource Management Practices

$X_{5=}$ Government regulations

ε = Error/disturbance

Creech (2011) asserts that one-factor ANOVA, also called one-way ANOVA is used when the study involves three or more levels of a single dependent variable. One factor ANOVA was preferred because this study had three levels of financial distress namely low, moderate and highly distress. This categorization was arrived at from the observation that the local authorities were not at the same level of financial distress. Some were more financially distressed than others. The study therefore required an assessment of whether the means of the independent variables differ across the three levels of financial distress exhibited by Local Authorities. This made ANOVA gain superiority to Ordinary Least Squares Regression because OLS does not compare means.

In addition, ANOVA, unlike other parametric tests such as t-tests, is quite robust against some deviation from the assumptions in parametric analysis. Specifically, ANOVA is robust against the parametric assumption that 1) the residuals (deviations from group means) have a normal distribution, 2) the variation is the same in each group. According to Box (1953), Markowski and Markowski (1990) and Sawilowsky (2002), an F test is useful in ANOVA and is used to assess whether the expected values of a quantitative

variable within several pre-defined groups differ from each other. The F statistic tends to be greater when the null hypothesis of independence is not true. The P value is crucial in ascertaining the probability that the null hypothesis is true. In this case, Box (1953), Markowski and Markowski (1990) and Sawilowsky (2002) assert that p values of less than 0.005 indicates that the F statistic is high and that the null hypothesis of independence needs to be rejected since it is not true.

In this study, financial distress was decomposed into three levels a) severely distressed Local Authorities/low financial health b) moderately distressed /moderate health Local Authorities c) weakly distressed/high financial health. Given a likert scale of 1 to 5, Local Authorities scoring a mean of 0 to 1.65 were rated as lowly distressed Local Authorities; those scoring above 1.65 to 3.335 were termed as moderately distressed Local Authorities while those Local Authorities with a mean score of over 3.335 were described as highly distressed. However, the magnitude of the demarcation or classifications of Local Authorities changed according to the weighting system.

The study expectations were that highly distressed/low financial health Local Authorities may exhibit low scores of financial management, corporate governance, information technology, human resource practices. The expectations of the study are that lowly distressed/high financial health Local Authorities may also exhibit high scores for financial management, corporate governance, information technology, human resource

practices. The study expectations were that highly distressed Local Authorities should also score highly on the ineffectiveness of government regulation.

Therefore, to achieve the first objective, the sign of the regression coefficient of financial management practices (X_1), corporate governance (X_2), Information Technology (X_3), Human Resource Management Practices (X_4) was checked whether it is consistently negative as expected in the study. The significance of the coefficient was also verified by checking the calculated p value against the conventional p value of 0.05 (Castillo, 2009). A p value of less than 0.05 indicated that the independent variables (financial management practices (X_1), Corporate governance (X_2), Information Technology (X_3), Human Resource Management Practices (X_4)) are significant determinants of financial distress facing Local Authorities.

Analysis of Variance (ANOVA) was conducted to check whether the mean response for the independent variables significantly differed across the three categories of financially distressed Local Authorities. If they did, then the study checked whether the means are largest for lowly distressed Local Authorities and least for severely distressed Local Authorities. Similarly, to achieve the fifth objective, the sign of the regression coefficient of Government regulations (X_5) was checked whether it was consistently positive as expected in the study. The significance of the coefficient was also verified by checking the calculated p value against the conventional p value of 0.05.

A p value of less than 0.05 indicated that Government regulations are a significant determinant of financial distress facing Local Authorities. To support the finding, Analysis of Variance (ANOVA) was conducted to check whether the mean response for Government regulations significantly differed across the three categories of financially distressed Local Authorities. If they did, then the researcher checked whether the means are larger for lowly distressed of Local Authorities and least for severely distressed Local Authorities.

Content analysis was also used to address the qualitative information obtained from both officers and customers. As one of today's most extensively employed analytical tools, content analysis has been used fruitfully in a wide variety of research applications in information and library science (ILS) (Allen & Reser, 1990). Similar to other fields, content analysis has been primarily used in ILS as a quantitative research method until recent decades.

Qualitative content analysis has been defined as a research method for the subjective interpretation of the content of text data through the systematic Local Authorities classification process of coding and identifying themes or patterns (Hsieh & Shannon, 2005). Content analysis has also been defined as an approach of empirical, methodological controlled analysis of texts within their context of communication, following content analytic rules and step by step models, without rash quantification

(Mayring, 2000), and any qualitative data reduction and sense-making effort that takes a volume of qualitative material and attempts to identify core consistencies and meanings (Patton, 2002).

These three definitions illustrate that qualitative content analysis emphasizes an integrated view of speech/texts and their specific contexts. Qualitative content analysis goes beyond merely counting words or extracting objective content from texts to examine meanings, themes and patterns that may be manifest or latent in a particular text (Mayring, 2000). It allows researchers to understand social reality in a subjective but scientific manner (Hsieh & Shannon, 2005).

The current study preferred qualitative content analysis since it addresses some of the weaknesses of the quantitative approach. Quantitative approaches of data analysis such as regression, correlation and descriptive statistics may be too mechanical and may be unable to unearth the feelings, emotions and subjective responses evidenced in social studies (Patton, 2002). Furthermore, in line with Mayring (2000), Patton (2002), Hsieh & Shannon (2005) qualitative content analysis was preferred in the current study as it allows researchers to understand social reality in a subjective but scientific manner.

The qualitative responses were analyzed along some pre-determined themes. For instance, answers to qualitative questions such as "what are the causes of financial

distress?" yield answers such as "inadequate staff for collecting revenue, unqualified officers in the docket of finance, low morale and motivation from officers in charge of finance administration". These answers were grouped under one theme of poor human resource management practices. Answers such as "nobody audits the fraudulent schemes that happen in Local Authorities, there is no proper records, therefore financial mismanagement can't be detected, the management manipulate the accounts, the management does not stick to budgets" were grouped under one theme of poor financial management practices. Others themes were identified and grouped accordingly.

CHAPTER FOUR

RESEARCH FINDINGS AND DISCUSSION

4.1: Introduction

The chapter presents the empirical findings and results of the application of the variables using techniques mentioned in chapter three. Specifically, the data analysis was based on specific objectives where patterns were investigated, interpreted and implications drawn on them. The chapter starts with a preliminary analysis of the data before analyzing the study variables.

4.1.2 Response Rate

The number of questionnaires that were administered were 320, out of these, 200 was administered to senior officers/employees and 120 were administered to customers of the sampled Local Authorities. A total of 295 questionnaires were properly filled and returned, which included 188 questionnaires from the officers and 107 questionnaires from the customers. This represented an overall successful response rate of 92%. According to Mugenda and Mugenda (2003), a response rate of 50% or more is adequate. Babbie (2004) also asserted that return rates of 50% are acceptable to analyze and publish, 60% is good and 70% is very good.

Table 4. 1: Response Rate

	Successful	Unsuccessful	Total
Officers/Employees	188 (94%)	12(6%)	200
Customers	107 (89%)	13(11%)	120
Total	295 (92%)	25(8%)	320

4.1.3 Reliability of the Results

Reliability refers to the extent to which a measuring instrument contains variable errors, that is errors that appear inconsistently from observation to observation during any one measurement attempt or that vary each time a given unit is measured by the same instrument (Sekaran, 2003 and Castillo, 2009). The current study pilot tested the questionnaire on two Local Authorities namely Kiambu county council and Ruiru municipal council.

A total of 21 questionnaires (11 from Kiambu county council and 10 from Ruiru municipal council) were obtained. Reliability tests were conducted using SPSS. Reliability results for all the 6 constructs representing the independent and dependent variables attracted a cronbach alpha statistics of more than 0.7. A cronbach alpha of 0.7 indicates that the data collection instrument is reliable (Sekaran, 2003). The reliability statistics are presented in appendix VIII.

4.1.4 Normality Test for the Dependent Variable

Results presented in appendix VIII reveal that skewedness' coefficient for financial distress is between -0.5 and 0.5. The kurtosis coefficients indicates that the dependent variable were platykurtic, implying that the distribution curve was flatter than the Gaussian distribution (normal curve). The skewedness' and kurtosis coefficients indicated that the dependent variable was normally distributed. Consequently such data is good for undertaking all manner of inferential and parametric statistical analysis since the probability of outliers is minimal (Sekaran, 2003). Furthermore, it implied that the data was ideal for all type of analysis, including parametric analysis for causal relationship between the dependent variable and the independent variables.

4.2: Demographic data

This section analyzes the demographic characteristics of the respondents.

4.2.1: Category of Local Authority

As demonstrated in figure 4.1, a majority (51%) which is slightly more than half the respondents were from municipal councils. Twenty-three percent (23%) were from county councils, 14% were from town councils, and 12% were from the three city councils. The findings imply that the study respondents were well spread across all categories of Local Authorities (representative of the population) and this may have a positive effect on the generalization, application and representativeness of the data**.**
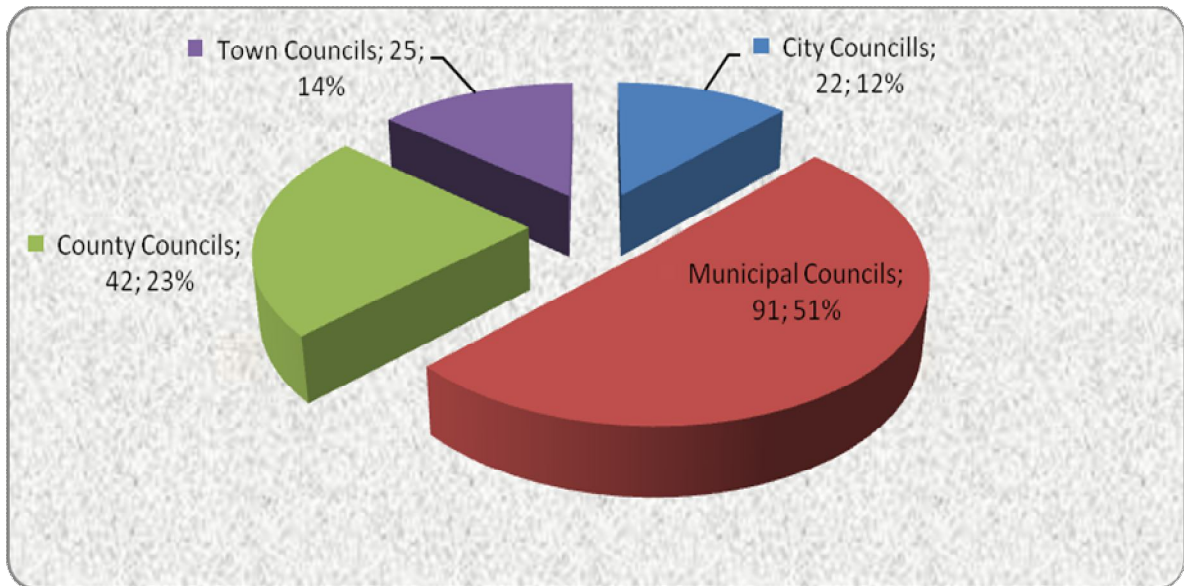
Figure 4. 1: Category of Local Authority

4.2.2: Gender of Local Authority Officers

Figure 4.2, illustrates that a majority (57%) which is slightly more than half of the respondents were males. Females formed 43% of the total number of respondents. The findings reflect the fact that the Local Authority is a male dominated field.

According to Ellis, Cutura, Dione, Gillson, Manuel and Thongori (2007), in spite of women being major actors in Kenya's economy, and notably in agriculture and the informal business sector, men dominate in the formal sector citing the ratio of men to women in formal sector as 74%:26%. Perhaps the gender disparity may have an implication on the level of financial distress in Local Authorities. This is supported by

(Stevenson and St-Onge, 2005; Gakure, 1995; Gakure, 2001; Gakure, 2003) who argued that women are more prudent in resource management compared to their men counterparts.
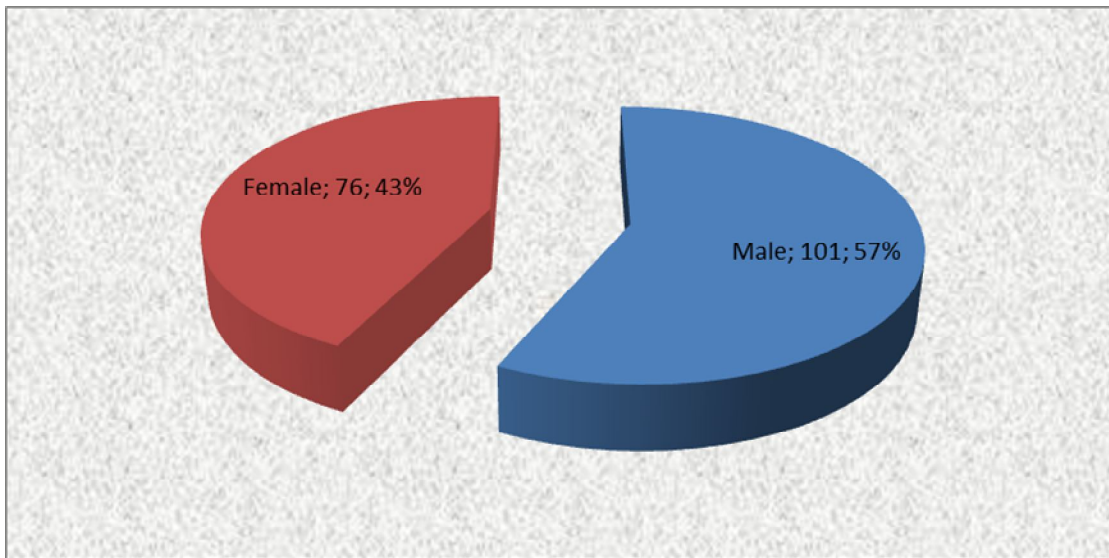
Figure 4. 2: Gender of Local Authority Officers

4.2.3: Age Bracket of Respondents

As revealed in Figure 4.3, a third of the respondents were aged between 31 to 40 years, 61, (33%) which was followed by 41 to 50 years, 60, (32%), 21 to 30 years, 42, (23%), over 50 years, 17, (9%) and 18 to 20 years, 5, (3%). The findings concur with those of Watson Wyatt Worldwide Study (2006) which asserted that the aging workforce exists in many countries including the U.S. and many European countries. The study by Watson also found that by 2050, Asia Pacific will be home to most of the world's elderly with

998 million people aged 60 and over. The findings also concur with Mwendo (2009) who reported that local governments have an aged workforce which has resulted from increasing the mandatory retirement age in Kenya from 55 to 60 years to alleviate succession crisis.

The findings are consistent with expectations as majority of those in Local Authority employment are at their career peak or just preparing to go for retirement in the next decade (Mwendo, 2009). The age of the Local Authority staff may have an important implication for succession planning and decision making on the overall strategic direction of the Local Authorities.
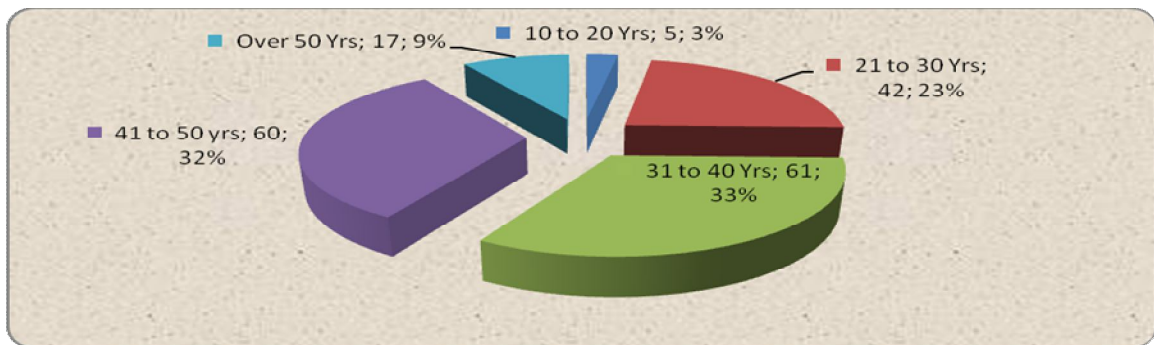
Figure 4. 3: Age Bracket of Respondents

4.2.4: Length of Service

Figure 4.4 reveals that a majority (54%), which was slightly more than half the respondents, had worked for the Local Authorities for a period of over 10 years. It was also observed that 24% of the respondents had worked for the Local Authorities for 1 to 5

years, followed by those who had worked for the Local Authorities for 5 to 10 years (15%). Only (7%) of respondents had worked for the Local Authorities for less than 1 year.

The findings concur with those by Samuel and Chipunza (2009); Swailes and Fahdi (2010), which asserted that labour turnover, is lower in public institutions, compared to private institutions. The finding is consistent with expectations as it is a well established notion that Local Authorities (just like any other government related officers) have security of tenure.
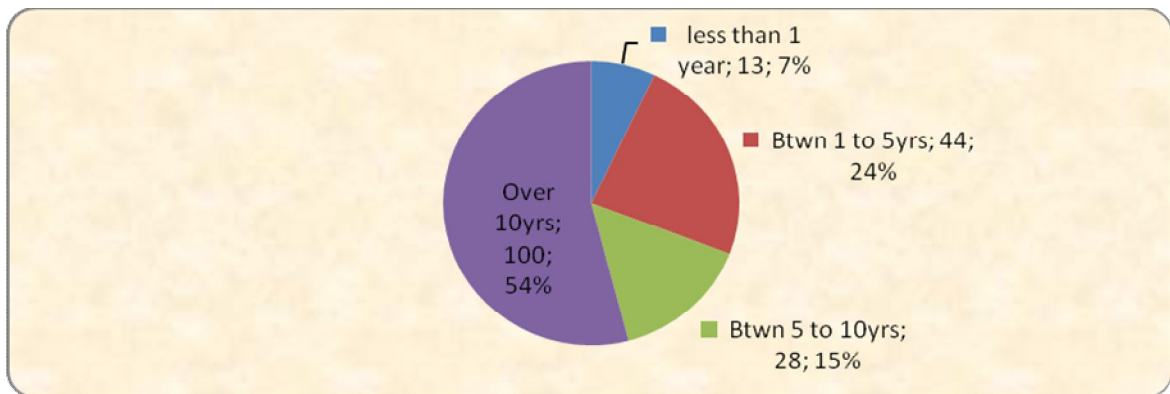
Figure 4. 4: Length of Service

4.3: Determinants of Financial Distress

This section attempts to analyse the findings on the various determinants of financial distress in Local Authorities which includes financial management practices, corporate governance, human resource management practices, information technology and Government regulations.

4.3.1 Financial Management Practices and its Effect on LA Financial Distress

The study sought to establish the effect of financial management practices on the financial distress of Local Authorities in Kenya. Specifically, the study investigated the following aspects of financial management; systems for detecting fraud, internal controls, independent procurement committees, internal audit function, monthly and yearly budget variance analysis, regular financial reporting, preparation of financial statements according to International Financial Reporting Standards (IFRS) and legal requirements,

4.3.1.1 Systems for Detecting Fraud

Results in Table 4.2 indicate that less than half (37.8%) of the respondents in the officers category agreed with the statement that Local Authorities do not have effective systems for detecting fraud. Twenty-two point three percent (22.3%) of respondents in the officer's category also strongly agreed to the statement that Local Authorities suffer from ineffective systems for detecting fraud. This brought to majority (60.1%) respondents who agreed or strongly agreed with that statement. Eleven point seven percent (11.7%) of

the respondents neither agreed nor disagreed with this statement and only 28.2% disagreed with the statement.

The findings corroborate with those of Miring'uh and Mwakio (2006) who asserted that there is overwhelming evidence that recent reform measures, including Rapid Results Initiative have failed to stop immense hemorrhage of revenue at the City Hall. The study results also compare well with those of a recent damning forensic report by the Kenya Anti-Corruption Commission (KACC), which stated that City Hall continues to lose a huge portion of parking fees, land rates or rent to corrupt officials exploiting weak financial management systems.

According to KACC (2007), perpetrators of the rip-off at the Council had devised a complex system to block evidence of unremitted money estimated to be worth millions of shillings. Furthermore, KACC (2007) asserted that key to the racket is concealment of the paper work involving such money, including bouncing cheques, tempering with the numbering of parking fees receipts and the filing of fraudulent expenditure claims at the council's cash office. The findings implies that Local Authorities have not put in place effective systems to detect and prevent fraud and this may have led to the financial distress being witnessed in many Local Authorities in Kenya.

4.3.1.2 Internal Controls

Results in Table 4.2 further indicate that thirty-six point seven percent (36.7%) of respondents in the officer's category agreed with the statement that Local Authorities have insufficient and inappropriate internal controls in place. Sixteen point five percent (16.5%) of the respondents strongly agreed to the statement, bringing to a majority (53.2%) of those officers who agreed or strongly agreed with the statement that Authorities have insufficient and inappropriate internal controls in place. Twelve point eight percent (12.8%) neither agreed nor disagreed while a minority of (34%) disagreed with the statement.

The findings agree with those of (Jonga & Chirisa, 2009; Fjelstad, Henjewele, Mwambe, Ngalewa & Nygaard, 2004 and Schoeman, 2011) who indicate that Local Authorities have poor and insufficient internal controls in place. The findings implies that Local Authorities have not put effective systems and internal controls in place to detect and prevent fraud which leads to fleecing of Councils meager financial resources of which may have led to the financial distress being witnessed in many Local Authorities in Kenya today.

4.3.1.3 Independent Procurement Committees

Results also show that while 29.3% of the officers agreed to the statement that legally constituted procurement committees do not exist, another 13.3% strongly agreed to the

statement, bringing to a total of slightly less than half (42.6%) of those officers who agreed or strongly agreed that Local authorities do not have legally constituted procurement committees. Eighteen point six percent (18.6%) neither agreed nor disagreed with the statement while a minority of (38.8%) disagreed with the statement.

The findings are in conflict with The Public Procurement Act 2005 part IV section 29 subsections 1 to 4 which stipulates that, for every procurement there shall be a legally constituted tender committees and the procuring entity shall use open tendering under Part V or an alternative procurement procedure. Part VI, subsection 2 states that a procuring entity may use an alternative procurement procedure only if before using that procedure, the procuring entity; (a) obtains the written approval from its tender committee; and (b) records in writing the reasons for using the alternative procurement procedure.

Subsection 4 states that a procuring entity shall use such standard tender documents as may be prescribed. Furthermore Part IV section 42 subsections 1 stipulates that no person shall collude or attempt to collude with any other person to make any proposed price higher than would otherwise have been the case.

The finding implies that failure to follow the Procurement Act statute leads to officers entrusted with tender awarding being compromised to award tenders arbitrarily. This has

the implication that the enticed officers inflate prices and get involved in corruption therefore fleecing the Local Authority's their meager financial resource. This may eventually lead to financial distress in Local Authorities.

4.3.1.4 Internal Audit Function

Results in Table 4.2 indicate that 47.3% disagreed while a further 9.6% strongly disagreed bringing to a total majority of slightly more than half (56.9%) of respondents in the officers' category who disagreed with the statement that the internal audit function does exist and it is effective. Twelve point two percent (12.2%) neither agreed nor disagreed while a further 30.9% agreed with the statement.

The findings concur with those by Jonga and Chirisa (2009) which asserted that internal audit departments existed in Local Authorities but were not effective in the performance of their duties due to lack of capacities. The findings imply that internal audit departments may exist in Local Authorities as indicated by a significant proportion of those who disagreed but how effective these internal audit departments are was doubtful. Perhaps, one can infer from the findings on poor internal control and systems of detecting fraud that internal audit department of Local Authorities are ineffective hence unable to check the fleecing of councils financial resources by corrupt individuals thus plunging the LAs into financial distress.

4.3.1.5 Monthly and Yearly Budget Analysis

Results in Table 4.2 indicate that 48.9% of respondents in the officers' category disagreed while a further 10.1% strongly disagreed bringing to a total majority (59%) of respondents who disagreed with the statement that a monthly and yearly budget analysis is done. Sixteen percent (16%) were neutral while a further 25% agreed with the statement.

The findings compare well with those of IEA (2009) and Ekwubi (2010) which argued that budget analysis is not done in Local Authorities. However, Ekwubi (2010) argues that those Local Authorities that practice budget variance analysis rarely follow up on the causes of variances. The Institute of Economic Affairs Report (2009), stipulates that most Councils hold meetings four months to the end of a financial year to legalise mini-budgets due to over expenditure and exhaustion of budget allocations meaning budget variance analysis are not done to identify causes of over-expenditure so as to hedge against such in future.

The findings imply that budget variance analysis is not conducted in Local Authorities, hence, the causes of the variances are not investigated and this may explain the unexplained short fall in revenues and unwarranted rise in expenditures of Local Authorities leading to financial distress.

4.3.1.6 Regular Production of Financial Statements

Results in Table 4.2 indicate that 43.6% of respondents disagreed while a further 12.2% strongly disagreed, bringing to a total majority (55.8%) of respondents who agreed with the statement that financial reports are produced regularly. Neutral respondents were 20.2%, while those who agreed were 23.9%. The findings agree with those of Institute of Economic Affairs (2009); Ekwubi (2010); Miring'uh and Mwakio (2006) which argued that regular financial reporting was done in Local Authorities though in a predetermined template by Ministry of Local Government (MOLG), which may not give the real picture of financial status in these Councils.

The findings imply that Local Authorities in Kenya produce financial reports regularly as indicated by those who agreed. However, the study does not reveal whether the financial reports represent the true and fair view (actual status) of the financial status of Local Authorities since the reporting is on a predetermined template by Ministry of Local Government (MOLG). The study however draws inferences from the state of internal controls and systems of detecting fraud and suggests that the financial reports may not represent the true and fair view because templates of financial statement are issued by ministry of Local Government and they are prepared in an environment of poor controls. An environment of poor internal controls implies that figures can be manipulated as there are no checks and balances to verify the accuracy of such figures.

4.3.1.7 Preparation of Financial Statements in Accordance with International Financial Reporting Standards (IFRS) and Legal Requirements

Results in Table 4.2 indicate that a majority (45.2%) of respondents disagreed while a further 11% strongly disagreed bringing to a total majority of slightly more than half (56.9%) of respondents who disagreed with the statement that financial statements are prepared in accordance with IFRS and legal requirements. Twenty-Two point nine percent (22.9%) neither agreed nor disagreed while a minority total of (20.2%) agreed with the statement.

The findings compare well with those by (Kloha, Weissert, & Kleine, 2005; Frank and Dluhy, 2003; Deal, 2007; Institute of Economic Affairs, 2009 & Jonga and Chirisa, 2009) which revealed that Local governments are audited by the National Audit Office whose objective is to verify whether the financial statements conform to IFRS and legal requirements after which they categorise the financial statements as Unqualified (good accounts) or Qualified (accounts with queries). Furthermore the respondents commented that most financial statements of LAs are qualified and audit queries raised are never addressed. However, Deal (2007), Institute of Economic Affairs Report (2009) and Jonga and Chirisa (2009) also argue that the preparation of financial statements in accordance with the IFRS and legal requirements does not mean that the financial statements are free from errors and misstatements.

The study infers that since financial statements are not prepared in accordance to IFRS and legal requirements, material misstatements and errors exist in those statements because the statements are produced in an environment of poor internal controls and inadequate systems of detecting and preventing fraud. The preparation of such financial statements with material misstatements may have led to financial distress of Local Authorities.

Overall, one can infer from the results that the financial management practices of Local Authorities are inadequate and ineffective which may have played a significant role in the financial distress of Local Authorities in Kenya today.

Table 4. 2: Financial Management Practices

Statement	Strongly disagree	Disagree	Neither agree nor disagree	Agree	Strongly agree
There are no effective systems for detecting fraud	4, 2.1%	49, 26.1%	22, 11.7%	71, 37.8%	42, 22.3%
sufficient and appropriate Internal controls are not in place	5, 2.7%	59, 31.4%	24, 12.8%	69, 36.7%	31, 16.5%
Internal Audit Function does exist	18, 9.6%	89, 47.3%	23, 12.2%	39, 20.7%	19, 10.1%
Monthly and yearly Budget Variance analysis is done	19, 10.1%	92, 48.9%	30, 16.0%	39, 20.7%	8, 4.3%
Financial reports are produced regularly (monthly, yearly etc)	23, 12.2%	82, 43.6%	38, 20.2%	38, 20.2%	7, 3.7%
Financial statements are prepared in accordance with FRS and legal requirements	22, 11.7%	85, 45.2%	43, 22.9%	31, 16.5%	7, 3.7%
Legally constituted Independent procurement committee does not exist	15, 8.0%	58, 30.9%	35, 18.6%	55, 29.3%	25, 13.3%

4.3.1.8: Officers Rating of Financial Management Practices in the Local Authority

Respondents from the officer's category were asked how they would rate the financial management practices in the Local Authority. Results in figure 4.5 indicates that a strong majority (69%) of respondents in the officers category rated the financial management

practices as poor. A minority of (31%) rated the the financial management practices as good.

The findings agree with those of Harif and Osman (2006), Boex and Muga (2009) and Watson, Handley and Hassett (2005) that hold that financial management practices in Local Authorities are poor. This response supported other findings in this study that show that Local Authorities have poor financial management practices.
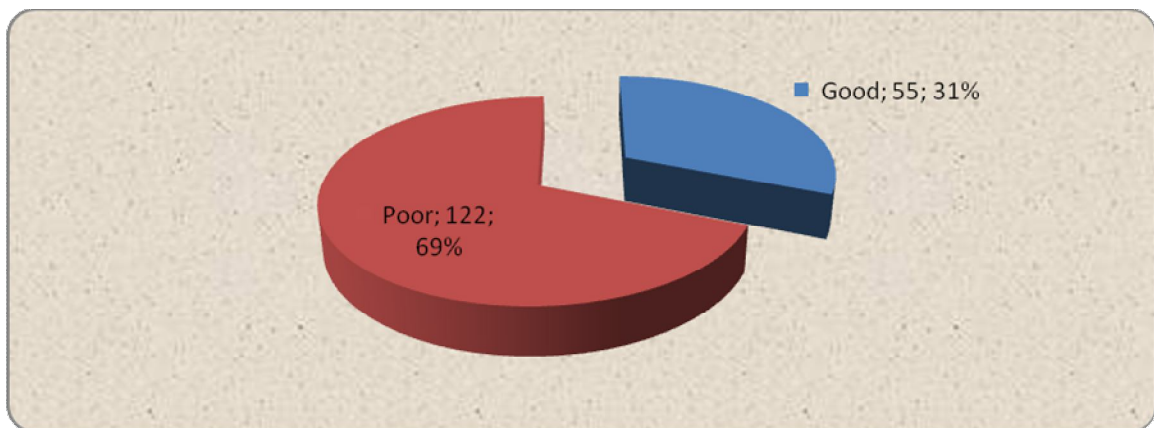
Figure 4. 5: Rating the Financial Management Practices in the Local Authority

Local Authority officers were also asked to explain why they rated financial management practices poorly. The responses were reflected in the following quotations;

> "Funds are expended without adherence to the budget"," Some chief officers do not adhere to approved budget for the LA". "There is no proper management", "Because some of staffs don't have enough skills and experience", " "Because they are not effective", "Because sometimes they don't give the financial records

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in weekly or daily ","" Its poor because of the way they collect their taxes", "No proper control and record keeping", "Audit Department is always Compromised", "Most of the funds Collected don't reach the office"," A lot of Audit Queries", "High Level of Corruption," No Transparency"," No Capacities", "No Professionalism", "Delay in Salary payment and remunerations", "some audit procedures are not followed"," lack of proper budgeting and reporting", "the officers work only under pressure" "the systems are down and cannot detect fraud"," financial books and records are not properly kept"," clerks have autonomous powers".

The results concur with those of Miring'uh and Mwakio (2006), KACC (2007) and Jonga and Chirisa (2009) which asserted that corruption, poor controls and lack of adherence to budgets are elements of poor financial management practices witnessed in Local Authorities.

Content analysis indicated that most of the officers rated the financial management poorly because of lack of internal controls, the ineffectiveness and the lack of independence of the audit department, corruption, lack of independence and political interference from political wing, poor budgeting and lack of adherence to already set budgets, lack of capacity, skills and competence of finance officers, laxity in financial reporting among others.

The Local Authority officers were requested to suggest recommendations for improvement of Local Authorities' financial management practices. Some of the suggested recommendations included;

"I recommend that all Local Authorities to be absorbed by county government to come up with a very strong internal control system"," Decentralization."," Institute a strong financial system for monitoring the funds that is input & output of resources", "Funds collected by Local Authorities should be controlled by people who are not corrupt."," To automate services through LAIFOMS."," Deployment of more staff in internal audit and accounts departments. "To employ staffs who are qualified in financial management skills.", "People Collecting funds Should be taught Something about integrity and money" , "They should invite Auditors from outside for proper checks and balances."

The findings concur with those by (Fjelstad, Henjewele, Mwambe, Ngalewa & Nygaard, 2004; Schoeman, 2011; Deal, 2007; Boex & Muga, 2009 and Miring'uh & Mwakio, 2006) which recommend the institution of proper budgeting practices, proper internal controls and regular financial reports as a panacea to the financial distress seen in Local Authorities.

Content analysis indicates that, the most frequently suggested recommendations for improvements of financial management practices include decentralization and devolution, institution of strong internal controls, address capacity and independence of audit and financial department through training, qualifications based hiring and resistance to interference from political wings. Furthermore, the officers frequently suggested that automation of financial processes and the implementation of LAIFOMS would help to improve financial management practices. In addition, revenue collection methods should be enhanced, diversified, improved and so should the budget practices.

4.3.1.9: Customers' Opinion on Whether Financial Distress Could be Attributed to Poor Financial Management Practices

Customers were also requested to give an opinion on whether poor financial management practices contributed to the financial distress of Local Authorities. Results in figure 4.6 indicated that a majority (54%) of customers strongly agreed with the statement that poor financial management practices such as lack of internal controls, budgeting and reporting contributed to the financial distress of Local Authorities.

The results also indicated that 33% of the customers agreed with the statement that poor financial management practices such as lack of internal controls, budgeting and reporting contributed to the financial challenges of Local Authorities, bringing to a total of an overwhelming majority of (87%) of the customers who agreed or strongly agreed with the statement. Meanwhile, 7% neither agreed nor disagreed with the statement while a further minority total of 6% disagreed with the statement.

The findings agree with those of Boex and Muga (2009) and Miring'uh and Mwakio (2006) which asserted that poor financial management practices such as lack of internal controls, budgeting and reporting contributed to the financial distress of Local Authorities. The findings imply that poor financial management practices such as lack of internal controls, budgeting and reporting contributed to the financial distress facing Local Authorities in Kenya.
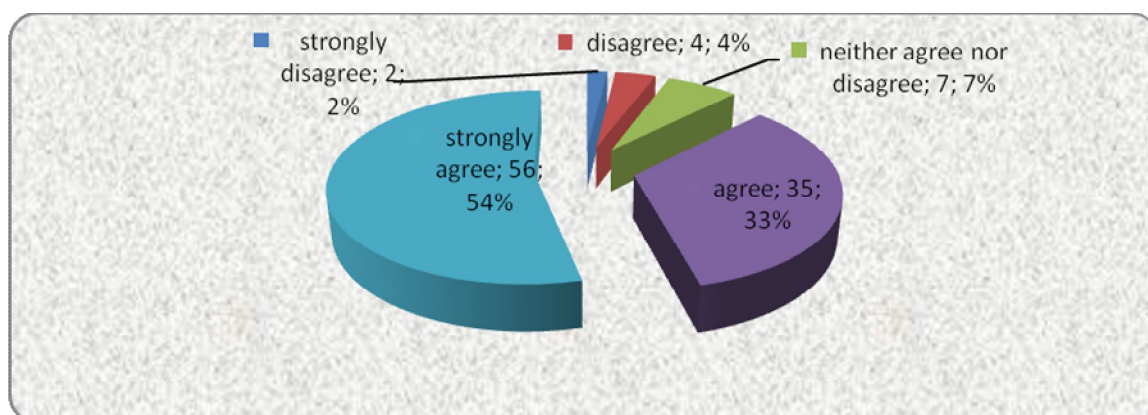
Figure 4. 6: Lack of Internal Controls, Budgeting and Reporting

4.3.1.10: Relationship between Financial Management Practices and Financial Distress

Regression analysis was conducted to empirically determine whether financial management practices were a significant determinant of financial distress in Local Authorities. Regression results in table 4.3 indicate the goodness of fit for the regression between financial management practices and financial distress was satisfactory. An R

squared of 0.977 indicates that 97.7% of the variances in the financial distress in Local Authorities are explained by the variances in the financial management practices. Table 4.3 and figure 4.7 also revealed that the relationship between financial management practices and financial distress is negative and significant (b1=-0.916, p value, 0.000).

Therefore, the results reveal that the null hypothesis which stated that "Financial management practice does not significantly contribute to financial distress facing Local Authorities in Kenya" is rejected at the critical value of 0.05 since the reported p value is 0.000 which is lower. The alternative hypothesis which states that "Financial management practice have a significant contribution to financial distress facing Local Authorities in Kenya is accepted.

The findings agree with those by Schoeman (2011), Boex and Muga (2009) and Frank and Dluhy (2003) which demonstrated that there is a negative relationship between the effectiveness of financial management practices and financial distress in Local Authorities.

This implies that an increase in the effectiveness of financial management practices by 1 unit leads to a decrease in financial distress by 0.916. This further implies that poor financial management practices leads to financial distress in Local Authorities.

The regression equation is as follows;

$$\text{Financial Distress} = 22.995 - 0.916\text{Financial Management Practices}$$

Table 4. 3: Model Summary and Parameter Estimates

	R Squared	Constant	b1
Coefficient	0.977	22.995	-0.916
P Value		(0.00)	(0.00)

The overall model significance is presented in table 4.4. An F statistic of 7993.898 indicated that the overall model was significant. This was supported by a probability value of 0.000. The reported probability of 0.000 is less than the conventional probability of 0.05. The probability of 0.000 indicates that there is a very low probability that the statement "overall model was insignificant" hence showing the strength of the model.

Table 4. 4: ANOVA for Financial Management Practices

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	3372.730	1	3372.730	7993.898	.000
	Residual	78.476	186	.422		
	Total	3451.205	187			

A graphical illustration of the relationship between financial management practices and financial distress was presented in figure 4.7. The findings concur with those by Miring'uh and Mwakio (2006), Carmeli (2008) and Deal (2007) who found a negative relationship between financial management practices and financial distress. The figure revealed that there is a negative relationship between financial management practices effectiveness and financial distress in Local Authorities. An increase in financial management effectiveness leads to a decline in financial distress.

Figure 4. 7: Financial Distress and Financial Management Practices

Group statistics in table 4.5 indicates that highly distressed Local Authorities have a mean score on financial management practices of 7.74. Moderately distressed Local Authorities have a mean score of 12.68 on financial management practices while lowly

distressed Local Authorities have the highest mean score for financial management practices 17.95.

Table 4. 5: Descriptive for Financial Management Practices

	N	Mean	Std. Deviation	Std. Error	95% Confidence Interval for Mean Lower Bound	Upper Bound	Minimum	Maximum
Lowly Distressed	61	17.95	2.281	.292	17.36	18.53	15	23
Moderately Distressed	64	12.68	1.677	.210	12.26	13.10	9	15
Highly Distressed	63	7.74	2.198	.277	7.18	8.29	1	11
Total	188	12.73	4.637	.338	12.07	13.40	1	23

The weighted mean scores for the effectiveness of financial management practices presented in table 4.5 were also presented in the form of a means plot in figure 4.8. Figure 4.8 indicates that lowly distressed local authorities have the highest score on the effectiveness of financial management practices (17.95), followed by moderately distressed local authorities (12.68) with highly distressed local authorities scoring the lowest (7.74). The finding implies that the effective financial management practices may reduce the level of financial distress in a local authority.
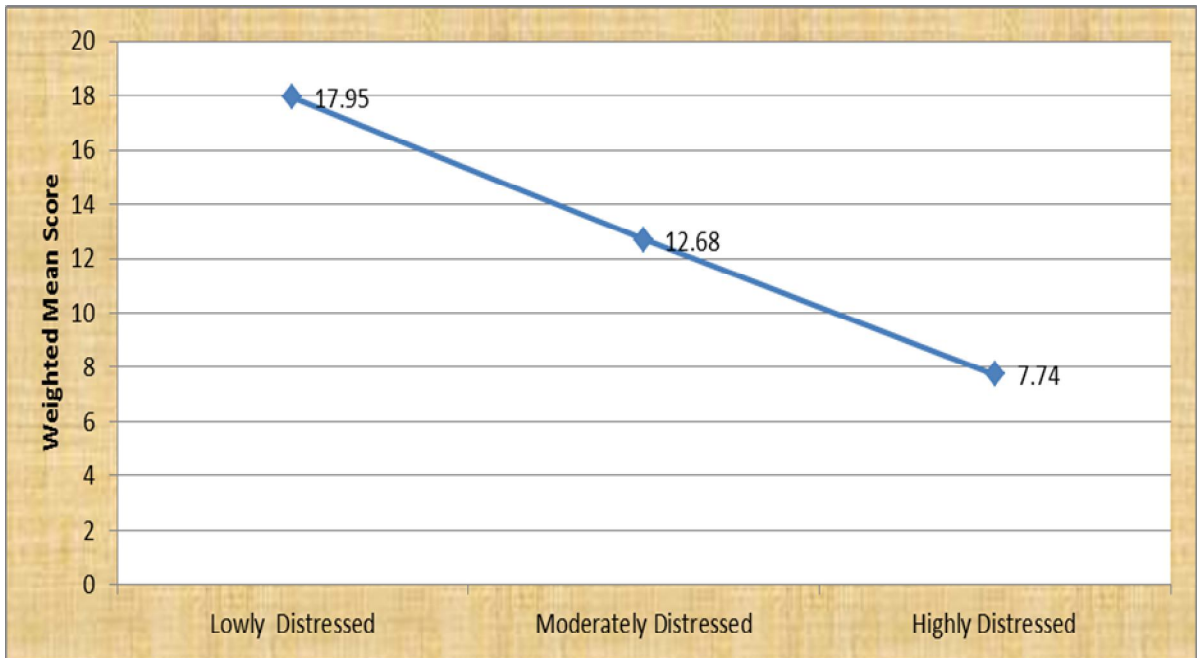
Figure 4. 8: Means Plot for Financial Management Practices

ANOVA results in Table 4.6 indicates that financial management practices differed significantly across the three levels of distressed Local Authorities. The findings were supported by an F statistic of 378.79 and a probability value of 0.000. The findings imply that financial mismanagement practices contribute significantly to financial distress in Local Authorities.

Table 4.6: ANOVA between Groups for Financial Management Practices

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	3231.173	2	1615.586	378.790	.000
Within Groups	789.048	185	4.265		
Total	4020.221	187			

Tests were conducted to verify if there were significant differences in financial management practices across the three categories of financially distressed local authorities. Post hoc tests in table 4.7 revealed that the lowly distressed local authorities had a significantly higher mean score on financial management practices compared to moderately distressed local authorities (p value 0.000) and highly distressed local authorities (p value 0.000). The differences in mean scores of financial management practices in the three categories of Local Authorities were also significantly different (p value 0.000).

Table 4. 7: Multiple Comparisons using Post Hoc Tests

(I) Distress Category	(J) Distress Category	Mean Difference (I-J)	Std. Error	Sig.	95% Confidence Interval	
					Lower Bound	Upper Bound
Lowly Distressed	Moderately Distressed	5.266[*]	.370	.000	4.54	5.99
	Highly Distressed	10.210[*]	.371	.000	9.48	10.94
Moderately Distressed	Lowly Distressed	-5.266[*]	.370	.000	-5.99	-4.54
	Highly Distressed	4.944[*]	.367	.000	4.22	5.67
Highly Distressed	Lowly Distressed	-	.371	.000	-10.94	-9.48
	Moderately Distressed	-4.944[*]	.367	.000	-5.67	-4.22

*. The mean difference is significant at the 0.05 level.

4.3.2 : Corporate Governance and Financial Distress

The current study sought to find out whether the quality and effectiveness of corporate governance practices were determinants of financial distress in Local Authorities in Kenya. Specifically, the following aspects of corporate governance were investigated; Transparency through display of performance results; transparency through audited accounts; Accountability through signing the performance contract and adhering to service delivery charter; leadership structure that supports governance; corruption cases; community participation in decision making.

4.3.2.1 Transparency Through Display of Performance Results;

Descriptive results in Table 4.8 indicate that 26.6% of respondents agreed while another 17.0% strongly agreed bringing to a total of 43.6% of respondents who agreed with the statement that the Local Authority does not ensure transparency through the display of performance results to all stakeholders. Eighteen point one percent (18.1%) neither agreed nor disagreed while a further minority total of (38.3%) disagreed with the statement.

The findings concur with those by Artley (2001) who asserts that the time has come for government to focus on reporting on its organizational and program results. The author further argues that this does not mean that government will always achieve everything it plans. But being clear about intentions, measuring and understanding results, and making adjustments where necessary, would help assure taxpayers that their money is being spent wisely. A focus on results would also help to ensure that limited public resources are being applied in a way that provides the most value for taxpayers.

The findings imply that the Local Authorities do not ensure transparency through the display of performance results to all stakeholders. The failure to display results to some stakeholders may have led to the financial distress in Local Authorities since stakeholders such as anticorruption bodies have no way of knowing the exact amount of financial resources that are going to waste. It also discourages hard working officers because their

effort is never recognized or rewarded. Consequently encourages corrupt practices which fleece the council's meager resources leading to financial distress in Kenyan Local Authorities.

4.3.2.2 Transparency Through Audited Accounts;

Descriptive results in Table 4.8 indicates that 42.1% of respondents in the officers category disagreed while a further 7.9% strongly disagreed bring to majority (50.0%) total of officers who disagreed that Local Authorities does ensure transparency by allowing its books of accounts to be audited. Nineteen point one percent (19.1%) neither agreed nor disagreed while a further minority total of (31.9%) agreed with the statement. The findings concur with those by United Nations (1999) which asserts that it is important to address the issues of accountability and transparency in specific financial management systems by ensuring that accounts are audited regularly.

The findings imply that the Local Authorities in Kenya may have been making attempts to ensure transparency through the audit of accounts. However, the auditing of accounts has not improved the financial status of Local Authorities perhaps because the audited accounts may not necessarily portray the actual financial position of Local Authorities. This is also confirmed by the high number of respondents (32%) who confirmed that there is no transparency in auditing books of accounts.

4.3.2.3 Accountability through Signing the Performance Contract and Adhering to Service Delivery Charter

Descriptive results in Table 4.8 indicate that 46.8% disagreed while a further 10.6% strongly disagreed bringing to a majority (57.4%) total of those respondents who disagreed with the statement that the Local Authority does ensure accountability through signing the performance contract and adhering to the service delivery charter. Meanwhile, 15% of the respondents were neutral while a further minority total of (27.6%) agreed with the statement.

The findings concur with those by Akaranga (2010) who argued that accountability can be enhanced through signing the performance contract and adhering to the service delivery charter. In addition, Akaranga (2010) asserts that performance contracting may improve the financial status of Local Authorities.

The findings imply that majority of Local Authorities have signed performance contracts. However, the signing of the performance contract has not improved the liquidity and financial status of Local Authorities.

4.3.2.4 Leadership Structure that Supports Governance

Descriptive results in Table 4.8 indicate that 33.0% agreed while a further 12.8% strongly agreed, bringing to a total (45.8%) of those officers who agreed with the statement that

the Local Authority does not have good leadership structure which supports corporate governance. Meanwhile, 18.1% neither agreed nor disagreed while a further minority total of (36.1%) disagreed with the statement.

The findings concur with those in literature (Capalbo, Grossi, Ianni & Sargiacomo, 2010; Carmeli, 2008; Deal, 2007; Frank & Dluhy, 2003 and Kamete, 2006) who asserted that strategic and visionary leadership is needed in order to improve the financial fortunes of Local Authorities.

The findings imply that the leadership structure in Local Authorities is not supportive of corporate governance. The failure to separate political leadership from administrative leadership implies that transparency and accountability is threatened in Local Authorities. The lack of leadership structure that supports corporate governance may have led to the financial distress being witnessed in Local Authorities.

4.3.2.5 Corruption

Descriptive results in Table 4.8 indicate that 27.1% agreed while a further 18.1% strongly agreed, bringing to a total (45.2%) of those officers who generally agreed with the statement that the number of corruption cases have not reduced in Local Authorities Sixteen point five percent (16.5%) neither agreed nor disagreed while a further minority total of (38.3%) generally disagreed with the statement.

The finding concurs with those by Boex and Muga, (2009) and Capalbo, et al, (2010) who assert that organizations that have an effective corruption policy also reduce the risk of financial distress. The KACC (2007) report holds that, the increased corrupt cases within Nairobi City Council, has contributed to financial distress that it is encountering today. The findings imply that the Local Authorities have not made progress in reducing the number of corruption cases. The findings further reveal that corruption may have led to financial distress in Local Authorities.

4.3.2.6 Community Participation in Decision-making

Descriptive results in Table 4.8 indicate that 38.3% disagreed while a further 8.0% disagreed, bringing to a slightly less than half total (46.3%) of those officers who generally disagreed with the statement that the Local Authority does encourage frequent community participation in decision making and setting up an Agenda for development. Meanwhile, 18.6% were neutral while a further minority total of (35.1%) generally agreed with the statement.

The findings compare well with those of O'Toole (2005), who in exploring community governance in Victorian Local government tested the extent to which councils were using new governance ideas. The author concluded that although a significant proportion of the councils reported on community participation through different council forums and committees the citizen's views were not prioritized. However, the majority of councils in

Victorian Local government were not using new governance ideas of involving communities in decision making. The findings imply that the corporate governance practices of Local Authorities are ineffective.

Table 4. 8: Corporate Governance and Financial Distress

Statement	strongly disagree	disagree	neither agree nor disagree	agree	strongly agree
The LA does not ensure transparency through display of performance results to all stakeholders	5, 2.7%	67, 35.6%	34, 18.1%	50, 26.6%	32, 17.0%
The LA does ensure transparency by allowing its books of accounts to be audited.	13, 6.9%	79, 42.0%	36, 19.1%	44, 23.4%	16, 8.5%
The LA does ensure accountability through signing the performance contract and adhering to the service delivery charter	20, 10.6%	88, 46.8%	28, 14.9%	39, 20.7%	13, 6.9%
The LA does not have a good leadership structure which supports corporate governance	7, 3.7%	61, 32.4%	34, 18.1%	62, 33.0%	24, 12.8%
The number of corruption cases have not reduced in Local Authorities	10, 5.3%	62, 33.0%	31, 16.5%	51, 27.1%	34, 18.1%
The LA does encourage frequent community participation in decision making and setting agenda for development	15, 8.0%	72, 38.3%	35, 18.6%	38, 20.2%	28, 14.9%

4.3.2.7: Rating the Corporate Governance Practices in the Local Authority

Results in figure 4.9 revealed that a majority of more than half (61%) of respondents in the officer's category rated the corporate governance practices of Local Authorities poorly. Meanwhile, a further 39% rated the corporate governance practices of Local Authorities positively. The findings are in agreement with descriptive results which show that Local Authorities have poor governance practices.
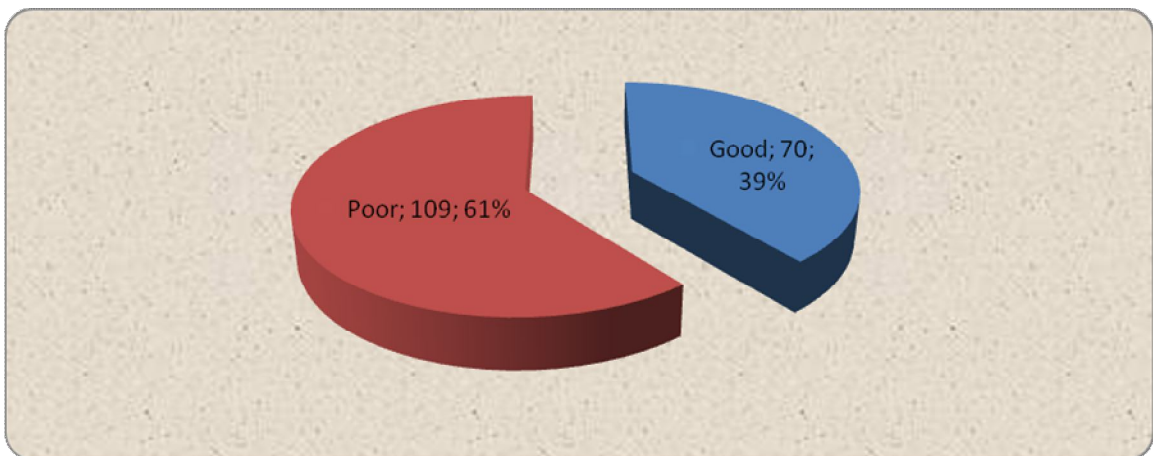
Figure 4. 9: Rating the Corporate Governance Practices in the Local Authority

Local Authority officers were also asked to explain why they rated corporate governance practices poorly. Those officers who rated corporate governance practices poorly explained that;

> "A few people sitting and passing resolution which are detrimental to the welfare
> of the council", "No good governance.", "Because it has bad leadership and no
> transparency.", "It's poor because still, corruption is highly practiced.", "Local

Authority has embraced culture of impunity for a longtime. And they don't normally involve community members when setting agenda for development. They come with their own agenda.", "They are always harsh to their customers.", "Highly Politicized", "Governance is dependent mainly on self interest", "there is poor leadership", "there is no transparency in all departments", "a lot of political interference", "and there is no transparency and accountability."

The findings concur with those of Akaranga (2010), United Nation (1999) and Artley (2001) which identify poor corporate governance practices as a cause of financial distress in Local Authorities. Content analysis indicated that officers rated the corporate governance practices poorly because of corruption, lack of transparency, poor leadership, political interference, failure to institute governance structures and failure to engage the community in setting the development agenda.

The Local Authority officers were requested to suggest recommendations for improvement of Local Authorities' corporate governance practices. Some of the suggested recommendations included;

"The Local Authorities should fully allow community participation in its development programmes", "I should recommend public private partnership", "Involve more stakeholders to participate.", "Civic participation is required in all activities", "Proper Accountability should be adhered to.", "To have good

leadership management and to be transparent and accountable.", "Let the communities set their own agenda for development, because they are the one that knows what problem they are encountering.", "Proper Utilization of Funds, Shun Corruption related Practices and Engage the Community/ Stakeholders in Service Delivery".

The findings agree with those by O'Toole (2005), Boex and Muga (2009) and Capalbo, et al (2010) which identifies elimination of corruption, reduction of political interference, enhancing accountability and transparency as ways of improving the corporate governance practices and financial position of Local Authorities.

Content analysis indicates that suggested recommendations for improvements of corporate management practices include; elimination of corruption, reduction of political interference by overhauling Local Government Act Cap. 265 to reduce the powers of the Civic Leaders devolve structures; clearly define boundaries between political and administrative wings, Civic participation in all activities, among others.

4.3.2.8: Customers' Opinion on Whether Financial Distress Could Be Attributed To Poor Corporate Governance Practices

Customers were also requested to give an opinion on whether poor governance practices such as lack of accountability, transparency, corruption, failure to adhere to service

delivery charter contributed to the financial distress of Local Authorities. Results in figure 4.10 indicate that a majority of more than half (59%) of customers agreed while a further 34% strongly agreed, bringing to an overwhelming majority (93%) of those customers who generally agreed with the statement that poor governance practices such as lack of accountability, transparency, corruption, failure to adhere to service delivery charter contributed to the financial challenges facing Local Authorities. Meanwhile, (1%) neither agreed nor disagreed with the statement while a further (6%) generally agreed with the statement.

The results are consistent with those by O'Toole (2005) which concluded that poor corporate governance contributes to financial distress of local authorities.
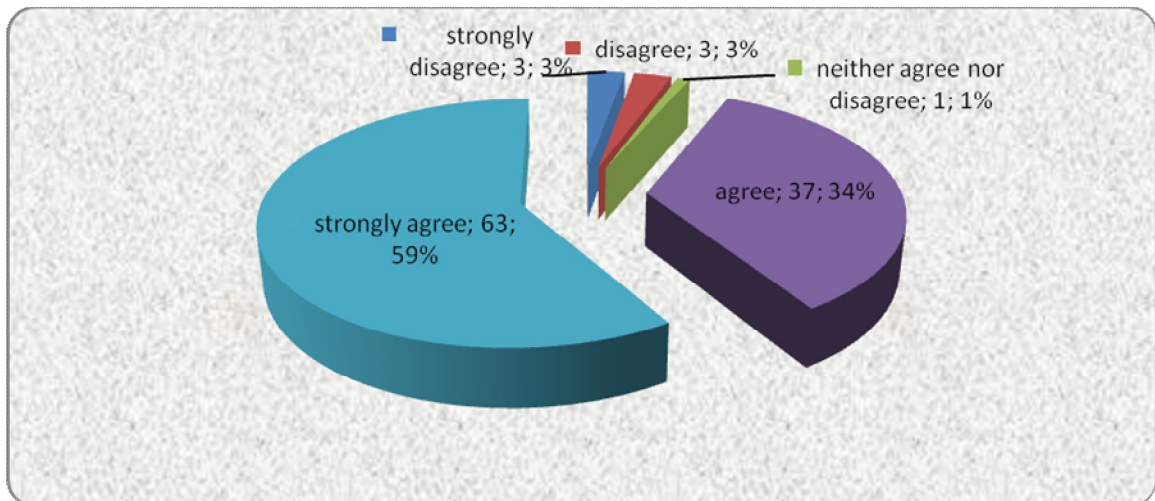
Figure 4. 10: Customers' Opinion on Corporate Governance Practices

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4.3.2.9: Relationship between Corporate Governance Practices and Financial Distress

Regression analysis was conducted to empirically determine whether corporate governance practices were a significant determinant of financial distress in Local Authorities. Regression results in table 4.9 indicate the goodness of fit for the regression between corporate governance practices and financial distress is unsatisfactory. An R squared of 0.441 indicates that (44.1%) of the variances in the financial distress are explained by the variances in the corporate governance practices.

As indicated in table 4.9, the relationship between corporate governance practices and financial distress is negative and significant (b1=-0.703, p value, 0.000). This implies that an increase in the effectiveness of corporate governance practices by 1 unit leads to a decrease in financial distress by 0.703 units.

Therefore, the results reveal that the null hypothesis which stated that "corporate governance practices do not have a significant contribution to financial distress facing Local Authorities in Kenya" is rejected at the critical value of 0.05 since the reported p value is 0.000. The alternative hypothesis which states that "corporate governance practices have a significant contribution to financial distress facing Local Authorities in Kenya is accepted. The regression equation is as follows;

$$\text{Financial Distress} = 19.388 - 0.703\,\text{Corporate Governance Practices}$$

Table 4. 9: Model Summary and Parameter Estimates

	R Square	Constant	b1
Coefficient	0.441	19.388	-0.703
P Value		(0.000)	(0.000)

The overall model significance was presented in table 4.10. An F statistic of 146.979 indicated that the overall model was significant. This was supported by a probability value of 0.000. The reported probability of 0.000 is less than the conventional probability of 0.05. The probability of 0.000 indicated that there was a very low probability that the statement "overall model was insignificant" was true and it was therefore possible to conclude that the statement was untrue.

Table 4. 10: ANOVA for Corporate Governance Practices.

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	1523.386	1	1523.386	146.979	.000
Residual	1927.819	186	10.365		
Total	3451.205	187			

A graphical illustration of the relationship between corporate governance practices and financial distress was presented in figure 4.11. The figure revealed that there is a negative relationship between corporate governance effectiveness and financial distress. The

findings concur with those in literature like Akaranga (2010), United Nations (1999) and Artley (2001) which found a negative relationship between corporate governance practices and financial distress. The findings imply that an increase in corporate governance effectiveness leads to a decline in financial distress.
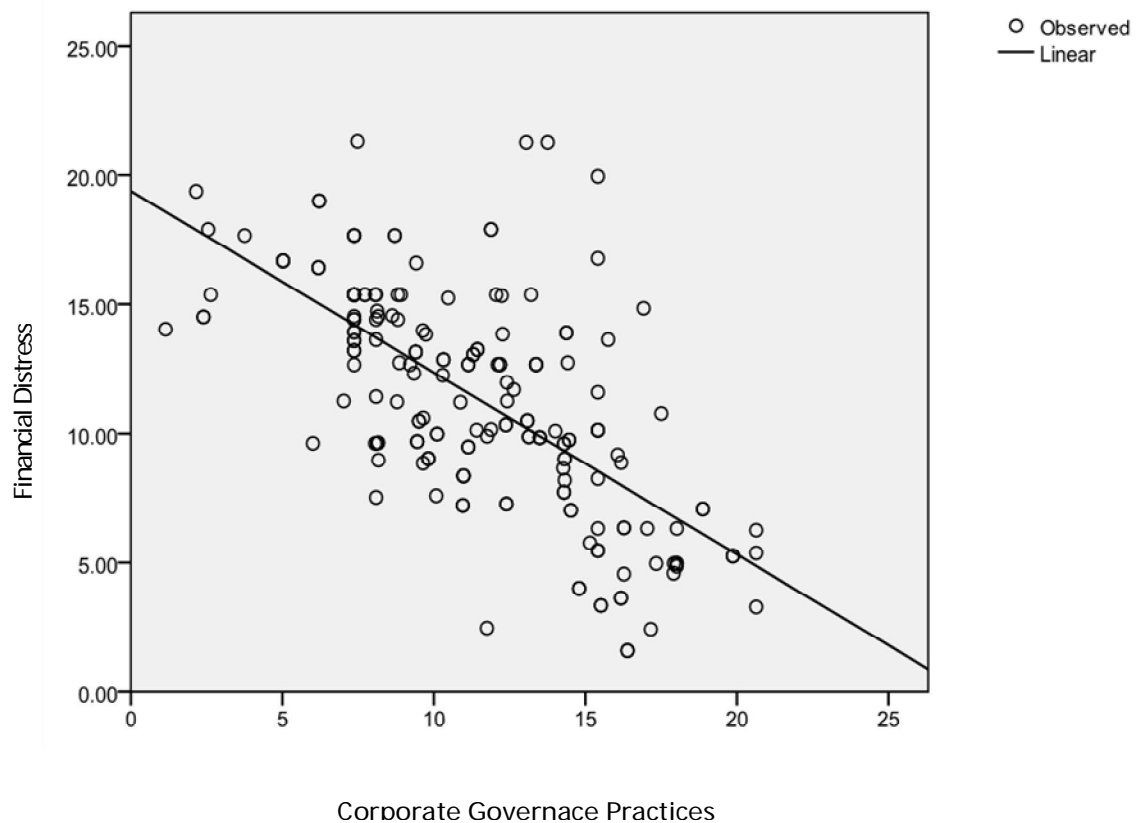
Figure 4. 11: Financial Distress and Corporate Governance Practices

Descriptive statistics in table 4.11 indicate that highly distressed Local Authorities had a mean score of 8.42 on corporate governance practices. Moderately distressed Local

Authorities have a mean score of 11.21 on corporate governance practices while lowly distressed Local Authorities have the highest mean score for corporate governance practices (14.83).

Table 4. 11: Descriptive for Corporate Governance Practices

	N	Mean	Std. Deviation	Std. Error	Lower Bound	Upper Bound	Minimum	Maximum
					95% Confidence Interval for Mean			
Lowly Distressed	61	14.83	3.219	.412	14.01	15.66	8	21
Moderately Distressed	64	11.21	2.540	.318	10.58	11.85	6	18
Highly Distressed	63	8.42	3.529	.445	7.53	9.31	1	17
Total	188	11.45	4.058	.296	10.87	12.04	1	21

The weighted mean scores for the effectiveness of corporate governance practices presented in table 4.11 were also presented in the form of a means plot in figure 4.12. Figure 4.12 indicates that lowly distressed local authorities have the highest score on the effectiveness of corporate governance practices (14.83), followed by moderately distressed local authorities (11.21) with highly distressed local authorities scoring the lowest (8.42). The finding implies that the effective corporate governance practices may reduce the level of financial distress in a local authority.
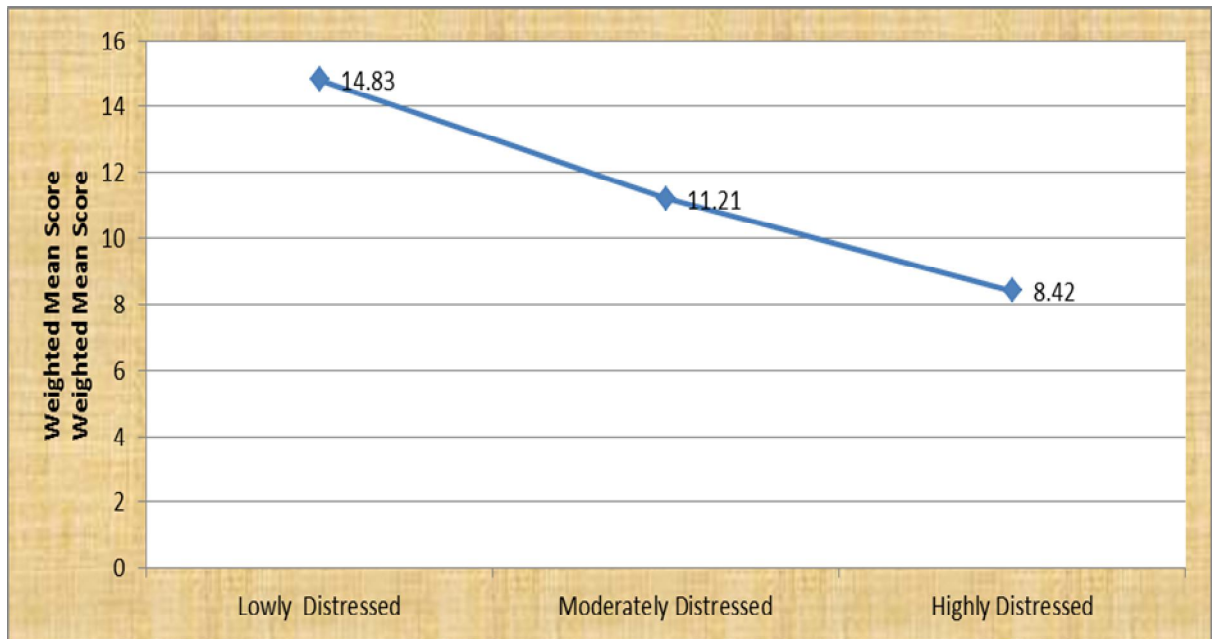
Figure 4. 12: Weighted Means Plot for Corporate Governance Practices

Analysis of Variance (ANOVA) results in table 4.12 revealed that there exists a significant difference in corporate governance practices between the three categories of financially distressed Local Authorities (F=65.706, P value=0.000). This further implies that the effectiveness of quality governance procedures influences the financial distress of local authorities.

Table 4. 12: ANOVA between Groups for Corporate Governance Practices

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	1278.854	2	639.427	65.706	.000
Within Groups	1800.347	185	9.732		
Total	3079.200	187			

Multiple comparisons were done using post hoc test. Multiple comparison results in table 4.13 indicated that there were significant differences in the effectiveness of corporate governance practices across the three categories of locally distressed Local Authorities. The difference in mean score of corporate governance practices between lowly distressed and moderately distressed local authorities was significant (p value =0.000).

The difference in mean score of corporate governance practices between lowly distressed and highly distressed local authorities was significant (p value =0.000). The difference in mean score of corporate governance practices between moderately distressed and highly distressed local authorities was significant (p value =0.000). The findings imply that corporate governance practices contribute to financial distress. The findings compare well with those in Boex and Muga (2009) who asserted that organizations that uphold tenets of corporate governance also reduce the risk of financial distress.

Table 4. 13: Multiple Comparisons

(I) Distress Category	(J) Distress Category	Mean Difference (I-J)	Std. Error	Sig.	95% Confidence Interval Lower Bound	Upper Bound
Lowly Distressed	Moderately Distressed	3.617[*]	.558	.000	2.52	4.72
	Highly Distressed	6.410[*]	.560	.000	5.30	7.52
Moderately Distressed	Lowly Distressed	-3.617[*]	.558	.000	-4.72	-2.52
	Highly Distressed	2.793[*]	.554	.000	1.70	3.88
Highly Distressed	Lowly Distressed	-6.410[*]	.560	.000	-7.52	-5.30
	Moderately Distressed	-2.793[*]	.554	.000	-3.88	-1.70

*. The mean difference is significant at the 0.05 level.

The results from the descriptive statistics, regression analysis and Analysis of Variance (ANOVA), indicate that corporate governance practices are a significant determinant of financial distress in Local Authorities. The findings are consistent with those of a study by Muranda (2006) who assessed the role of corporate governance on financial distress in Zimbabwean Banks. The author observed that in all cases of pronounced financial distress, either the chairman of the board or the chief executive wields disproportionate power in the board. The disproportionate power emanates from major shareholding. The overbearing executive overshadows other directors, executive and non-executive, thus creating power imbalance in the board.

The findings also agree with those of Moreno (2005) and Singer (2004) who demonstrated the contribution of corporate governance to good financial management practices of Local Authorities which resulted into financial health in Portugal. The study found a positive relationship between corporate governance mechanisms, good financial management practices and a consequent reduction in financial challenges. Boex and Muga (2009) also assert that organizations that uphold tenets of corporate governance also reduce the risk of financial distress. The studies by (Capalbo, Grossi, Ianni & Sargiacomo, 2010; Carmeli, 2008; Deal, 2007 and Frank & Dluhy, 2003) also show that that poor corporate governance and leadership contributes to financial distress in Local Authorities.

4.3.3: Information Technology and Financial Distress

The current study sought to find out whether the effectiveness and adequacy of information technology is a determinant of financial distress in Local Authorities. Specifically, the study focused on the following variables; Provision of relevant information by Local Authority Information Management System (LAIFOMS); Reliability of Local Authority Information Management System (LAIFOMS); Local Authority Information Management System in enhancing Growth of Local Authorities (LAIFOMS); Ability of Local Authority Information Management System to incorporate new products and meeting new reporting needs (LAIFOMS); User friendliness of Local

Authority Information Management System (LAIFOMS); Ability of Local Authority Information Management System (LAIFOMS) to interact with applied technologies such as PDAs, POS and ATMS;

4.3.3.1: Provision of Relevant Information by Local Authority Information Management System (LAIFOMS)

Descriptive results in Table 4.14 indicate that 55.3% disagreed while another 9.0% strongly disagreed, bringing to a more than half majority (64.3%) of those respondents under officers category who generally disagreed with the statement that the Management Information System used in Local Authorities does provide relevant information for the right people at different levels of the Local Authority to enable informed decision making. Meanwhile, 14.9% neither agreed nor disagreed while a further minority total of (20.8%) generally agreed with the statement.

The findings agree with those by Jensen (2002), Waema and Mitullah (2007) who assert that Local Authority Information Management System should give relevant information for planning and management purposes as opposed to the current scenario.

The findings imply that Local Authority Information Management System does not provide relevant information for management purposes. Therefore lack of provision of relevant information has translated into increased financial distress in Local Authorities.

4.3.3.2: Reliability of Local Authority Information Management System (LAIFOMS)

Table 4.14 indicated that 53.7% agreed while a further 6.4% strongly agreed, bringing to a more than half majority (60.1%) of those officers who generally agreed with the statement that the information from Management Information System used in Local Authorities is not reliable. Meanwhile, 20.2% neither agreed nor disagreed while a further minority total of (19.7%) generally disagreed with the statement.

The findings agree with those by (Schelin, 2006; Rogers, 1995; Venkatesh, Morris, Davis & Davis, 2003; Venkatesh, 2000) who assert that for an innovation or technology to be adopted, it should have reliability as a quality. Therefore, Local Authority Information Management System should give reliable information for planning and management purposes. Reliable and accurate information is crucial for financial management.

The findings imply that Local Authority Information Management System should provide reliable information for management and planning purposes. However, the provision of unreliable information has compounded problem of financial distress in Local Authorities.

4.3.3.3: Local Authority Information Management System in Enhancing Growth of Local Authorities (LAIFOMS)

Table 4.14 reveals that 55.9% disagreed while a further 10.1% strongly disagreed, bringing to a more than half majority (66.0%) of officers who generally disagreed with the statement that the Management Information System used in Local Authorities is not enhancing the growth of Local Authorities. Meanwhile, 15.4% neither agreed nor disagreed, while a further 18.6% generally agreed with the statement.

The findings agree with those by Rogers (1995), Venkatesh, Morris, Davis and Davis (2003), Venkatesh (2000) who assert that one of the factors determining the adoption and use of a technology or an innovation is the perceived usefulness or relative advantage of the innovation in helping the organization to grow.

The findings imply that Local Authority Information Management System may have a relative advantage over manual systems but it provides little in invigorating the growth of Local Authorities financial base. It is perceived that a relevant information system is useful in the management and planning purposes of the Local Authority. Consequently if the software does not aid growth of an organizations financial base then it leads to increased financial distress in Local Authorities since the cost of installing and maintaining such a system is enormous.

4.3.3.4: Ability of (LAIFOMS) to Incorporate New Products and Meeting New Reporting Needs

Table 4.14 reveals that 56.9% agreed while a further 11.7% strongly agreed, bringing to a more than majority (68.6%) of those officers who generally agreed with the statement that Management Information System used in Local Authorities cannot easily incorporate new products or expand to accommodate new reporting needs. Meanwhile, 14.9% neither agreed nor disagreed while another 16.5% generally disagreed with the statement.

The findings agree with those by Waema and Mitullah (2007) and Venkatesh, Morris, Davis and Davis (2003) who assert that one of the factors determining the adoption and use of a technology or an innovation are the flexibility of the innovation.

The findings imply that Local Authority Information Management Systems is not a flexible system. The Management Information System used in Local Authorities therefore cannot easily incorporate new products or expand to accommodate new reporting needs, hence LA's have no powers to adjust or modify the system to suit their financial reporting needs. This has therefore compounded the problem of financial distress in Local Authorities.

4.3.3.5: User Friendliness of Local Authority Information Management System (LAIFOMS)

Results in Table 4.14 reveal that 59.0% disagreed while a further 8.5% strongly disagreed, bringing to a majority (67.5%) of officers who generally disagreed with the statement that the Management Information System used in Local Authorities is user friendly to staff, that is, easy to understand and operate. Meanwhile, (13.85%) neither agreed nor disagreed, while a further minority total of (18.65%) generally agreed with the statement.

The findings agree with those in Rogers (1995), Waema and Mitullah (2007), Venkatesh, Morris, Davis and Davis (2003) who assert that one of the factors determining the adoption and use of a technology or an innovation is the user friendliness or the perceived ease of use of the innovation.

The findings imply that Local Authority Information Management System is not a user friendly system. The Management Information System used in Local Authorities is therefore considered not easy to use by Local Authority staff. Therefore in the process of evading its use some other employees have become gurus in its use thus using it to fleece the Councils their meager financial resources thus contributing to financial distress in Local Authorities.

4.3.3.6: Ability of LAIFOMS to Interact with Applied Technologies such as PDAs, POS and ATMS

Table 4.14 reveals that 47.3% disagreed while a further 5.3% strongly disagreed, bringing to a slightly more than half majority (52.6%) of officers who disagreed with the statement that the Management Information System used in Local Authorities can interact with any applied delivery technologies, such as handheld computers, point-of-service (POS) terminals, and automated teller machines (ATMs). Meanwhile, 26.1% neither agreed nor disagreed while a further 21.3% agreed with the statement.The findings agree with those by Rogers (1995), Waema and Mitullah (2007), Venkatesh, Morris, and Davis (2003) who assert that one of the factors determining the adoption and use of a technology or an innovation is the compatibility of the innovation to other technologies.

The findings imply that Local Authority Information Management System is not compatible with applied technologies such as personal Digital Assistant (PDAs), Point of Sale (POS) and Automated Teller Machines (ATMS). The Management Information System used in Local Authorities is therefore considered not compatible with other systems. Therefore the non-compatibility of Local Authority Information Management System (LAIFOMS) has contributed to financial distress in Local Authorities, due to the fact that it cannot host e-payment systems effectively.

Overall, the findings imply that Local Authorities have a very optimistic view about information technology and how it has impacted on the operations of the Local Authorities. To reduce levels of corruption and instill efficiency in the operations of LAs there is need to have a software system that is compatible to other innovations in the area of information technologies. Lack of such systems compounds the problem of financial distress in local Authorities in Kenya.

Table 4. 14: Information Technology and Financial Distress

Statement	Strongly Disagree	Disagree	Neither Agree Nor Disagree	Agree	Strongly Agree
The MIS/LAIFOMS does provide relevant information for the right people at different levels of the LA	17, 9.0%	104, 55.3%	28, 14.9%	31, 16.5%	8, 4.3%
The information from LAIFOMS is reliable	12, 6.4%	101, 53.7%	38, 20.2%	33, 17.6%	4, 2.1%
The MIS/ LAIFOMS is enhancing the Growth of Local authorities	19, 10.1%	105, 55.9%	29, 15.4%	29, 15.4%	6, 3.2%
MIS/ LAIFOMS can easily incorporate new products or expand to accommodate new reporting needs	22, 11.7%	107, 56.9%	28, 14.9%	25, 13.3%	6, 3.2%
The MIS/ LAIFOMS is user friendly to staff i.e. easy to understand and operate	16, 8.5%	111, 59.0%	26, 13.8%	26, 13.8%	9,4.8%
MIS/LAIFOMS does interact with any applied delivery technologies, such as handheld computers, point-of-service (POS) terminals, and automated teller machines(ATMs	10, 5.3%	89, 47.3%	49, 26.1%	27, 14.4%	13, 6.9%

Descriptive results in table 4.15 indicated that county councils were the most optimistic about the benefits of Management Information System with a mean score of 11.25 followed by town councils (10.64), municipal councils (10.4) and the city councils spotting the least confidence in the benefits of Management Information System (10.05). The finding implies that larger local authorities such as Nairobi and Mombasa find the level of Information technology or the Local Authority Information and Operation Management System as restrictive and inadequate. It may therefore also imply that smaller local authorities are more likely to find LAIFOMS to be adequate and growth enhancing compared to larger councils such as Nairobi and Mombasa.

The findings are consistent with reality as most town councils and county councils have not implemented the Management Information System yet but have had their staff trained on the use of Management Information System. Therefore, it is likely that the staff of town and county councils have not yet got a reality check on the effectiveness and adequacy of the Management Information System. The city councils have fully implemented the Management Information System but have consistently complained that the systems leave a lot to be desire.

Table 4. 15: Descriptive Statistics for Management Information System

	N	Mean	Std. Deviation	Std. Error	95% Confidence Interval for Mean		Minimum	Maximum
					Lower Bound	Upper Bound		
City Councils	22	10.05	3.629	.774	8.44	11.66	2	18
Municipal Councils	91	10.40	4.322	.453	9.50	11.30	0	23
County Councils	42	11.25	4.544	.701	9.83	12.66	2	18
Town Councils	25	10.64	3.782	.756	9.08	12.20	3	17
Total	180	10.59	4.212	.314	9.97	11.21	0	23

A weighted means score plot was presented in figure 4.13. The highest score on effectiveness of information technology was for county councils (11.25), followed by town councils (10.64), municipal councils (10.4) and city councils (10.05). The findings imply that LAIFOMS is more effective in county councils more than in any other local authority. Perhaps, the reason behind this observation is because county councils are small enough to find LAIFOMS adequate for supporting their growth. On the other hand, municipal councils and city councils are too large and may require amore robust and advanced system. Finally, town councils may find LAIFOMS too advanced due to their small size.
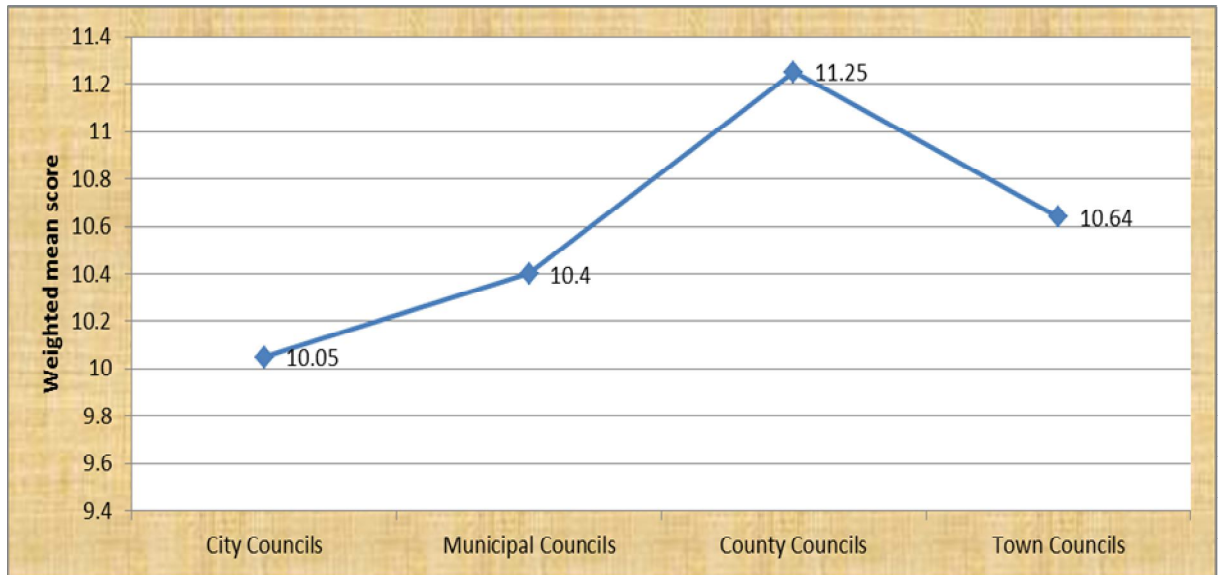
Figure 4. 13: Means Plot for LAIFOMS Comparison across Local Authorities

An ANOVA test was carried out to see whether the category of local authority influenced the level of optimism about Local Authority Information and Operation Management System (Table 4.16). The difference in optimism were not significantly different across the four categories of Local Authorities (F=0.520, p value=0.669). The observation may be explained by the fact that all the local authorities are using the same system (LAIFOMS) and hence have no other system to compare with.

Table 4. 16: ANOVA between Groups for Management Information System

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	27.894	3	9.298	.520	.669
Within Groups	3147.656	176	17.884		
Total	3175.550	179			

4.3.3.7: Rate the Adequacy of Information Technology in the Local Authority

Results in figure 4.14, reveals that majority (59%) of respondents in the officer's category, rated the information technology of Local Authorities as inadequate. Meanwhile, a further 41% rated the information technology as adequate. The findings are in agreement with regression results which show that Local Authorities have inadequate Information technology.
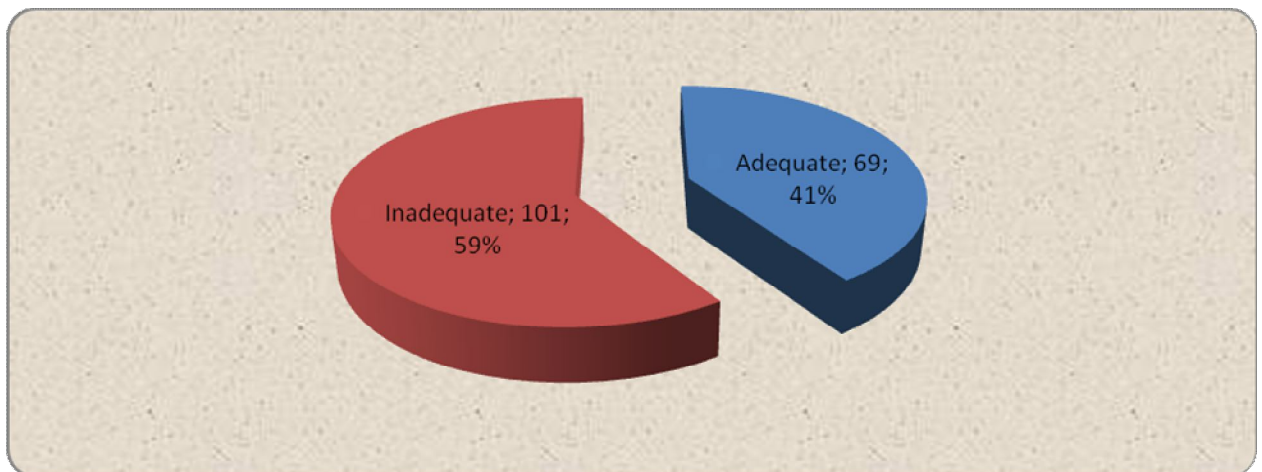
Figure 4. 14. Adequacy of Information Technology in Local Authorities

Local Authority officers were also asked to explain why they rated Information Technology poorly. The officers explained that;

"A bigger percentage of the workforce, are not I.T Compliant", "Lack of LAIFOMS in the L.As.", "The council is not yet on LAIFOMS.", "LAIFOMS are not utilised hence creates loophole for siphoning of funds.", "They need to Purchase Computers.", "IT is yet to be fully developed, LAIFOMS is yet to be fully operationalized", "they do not work effectively as required", "it does not incorporate all the needs of the council", "not all sections are compliant", "more computers", "not all staff members are computer literate", "not all functions have been automated".

Content analysis indicates that most of the officers rated the information technology poorly because of inadequate investment in hardware (computers), software (Implementation of LAIFOMS), and lack of IT skills among the workforce. The Local Authority officers were requested to suggest recommendations for improvement of Local Authorities' information technology. Some of the suggested recommendations included;

"The Government should compel all Local Authorities to implement LAIFOMS as first priority project." All Local Authority should have LAIFOMS to computerize their accounts", "All modules to be fully operationalized and staff training on IT ", "the personnel should be well trained and informed", "People should get education about information technology, chances to reduce illiteracy'.

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"Make the functions to be online compliant.", "Enhancement of capacity building from any development partner."

Content analysis indicates that the suggested recommendations for improvements of information technology include; ICT skills enhancement for Local Authority staff through training, investment in ICT hardware such as computers. Most importantly, the officers recommended that all Local Authorities should prioritize the implementation of LAIFOMS. In addition, those Local Authorities who have already implemented LAIFOMS should ensure that all modules should be fully operationalized, for instance, integration of payroll and statutory deductions with the main accounting system.

4.3.3.8: Customers' Opinion on Whether Financial Distress could be Attributed to Inadequate Information Technology

Customers were also requested to give an opinion on whether information technology and lack of automation contributed to the financial distress of Local Authorities. Results in figure 4.15 indicated that 39% of customers strongly agreed while a further 32% agreed, bringing to a majority total 71% of customers who generally agreed with the statement that lack of automation contributed to the financial challenges facing Local Authorities. Meanwhile, 11% neither agreed nor disagreed while a further 18% strongly disagreed with the statement.

The findings are consistent with those of Waema and Mitullah (2007) who conducted a study on E-governance in Local Authorities in Kenya. The authors concluded that ICTs are at an infancy stage in Kenya and ICTs have potential of reversing the trend of ineffective governance and improving participation, transparency, accountability, responsiveness, effectiveness and efficiency which is the major governance construct.

The authors further observed that (Local Authority Integrated Financial Operations and Management System) LAIFOMS was limited to financial management and that it was still to penetrate other aspects and engagement with citizens. They also observed that access to computers and internet was limited and that hope for ICT application lay on mobile phones.
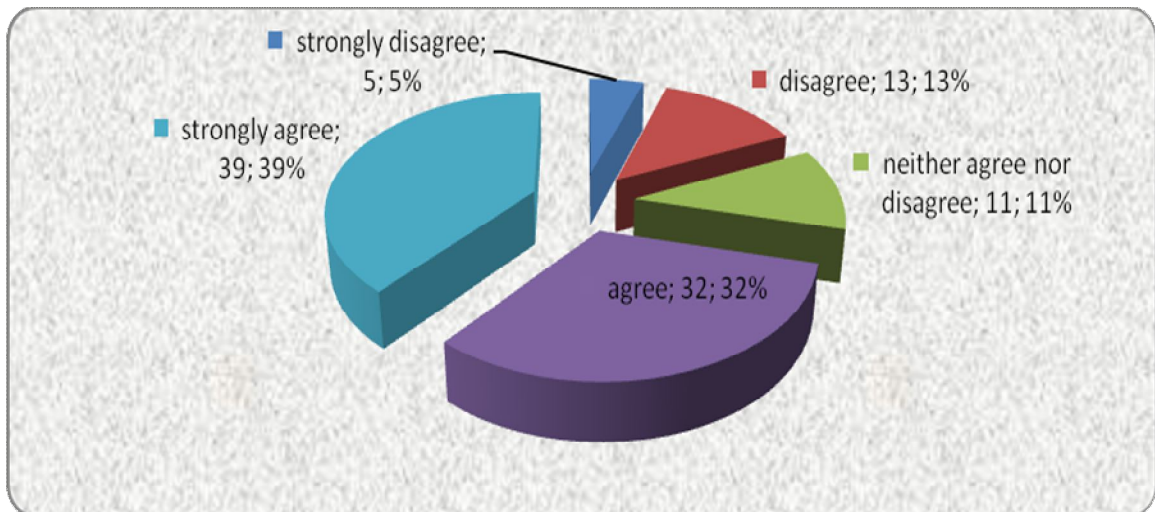
Figure 4. 15: Customers' Opinion on Inadequacy of Information Technology

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4.3.3.9: Relationship between Information Technology and Financial Distress

Regression analysis was conducted to empirically determine whether Information Technology was a significant determinant of financial distress in Local Authorities. Regression results in table 4.17 indicated that the goodness of fit for the regression between Information Technology and financial distress is unsatisfactory. An R squared of 0.224 indicates that 22.4% of the variances in the financial distress of Local Authorities are explained by the variances in the Information Technology.

Table 4.17 reveals that the relationship between Information Technology and financial distress is negative and significant (b1=-0.484, p value, 0.000). This implies that an increase in the effectiveness of Information technology by 1 unit leads to a decrease in financial distress by 0.484 units.

Therefore, the results reveal that the null hypothesis which stated that "Adoption of Information Technology does not have a significant contribution to financial distress facing Local Authorities in Kenya" is rejected at the critical value of 0.05 since the reported p value is 0.000. The alternative hypothesis which states that "Adoption of Information Technology has a significant contribution to financial distress facing Local Authorities in Kenya is accepted. The regression equation is as follows;

$$Financial\ Distress = 16.432 - 0.484 Information\ Technology$$

Table 4. 17: Model Summary and Parameter Estimates

	R Square	Constant	b1
Coefficient	0.224	16.432	-0.484
P Value		0.000	0.000

The overall model significance was presented in table 4.18. An F statistic of 53.707 indicated that the overall model was significant. This was supported by a probability value of (0.000). The reported probability of (0.000) is less than the conventional probability of (0.05). The probability of (0.000) indicated that there was a very low probability that the statement "overall model was insignificant" was true and it was therefore possible to conclude that the statement was untrue.

Table 4. 18: ANOVA for Information Technology.

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	773.254	1	773.254	53.707	.000
Residual	2677.952	186	14.398		
Total	3451.205	187			

A graphical illustration of the relationship between Information Technology and financial distress was presented in figure 4.16. The figure reveals that there is a negative

relationship between information technology effectiveness and financial distress. The findings concur with those of Akaranga (2010), United Nations (1999) and Artley (2001) which found a negative relationship between information technology and financial distress. The findings imply that an increase in information technology effectiveness leads to a decline in financial distress.
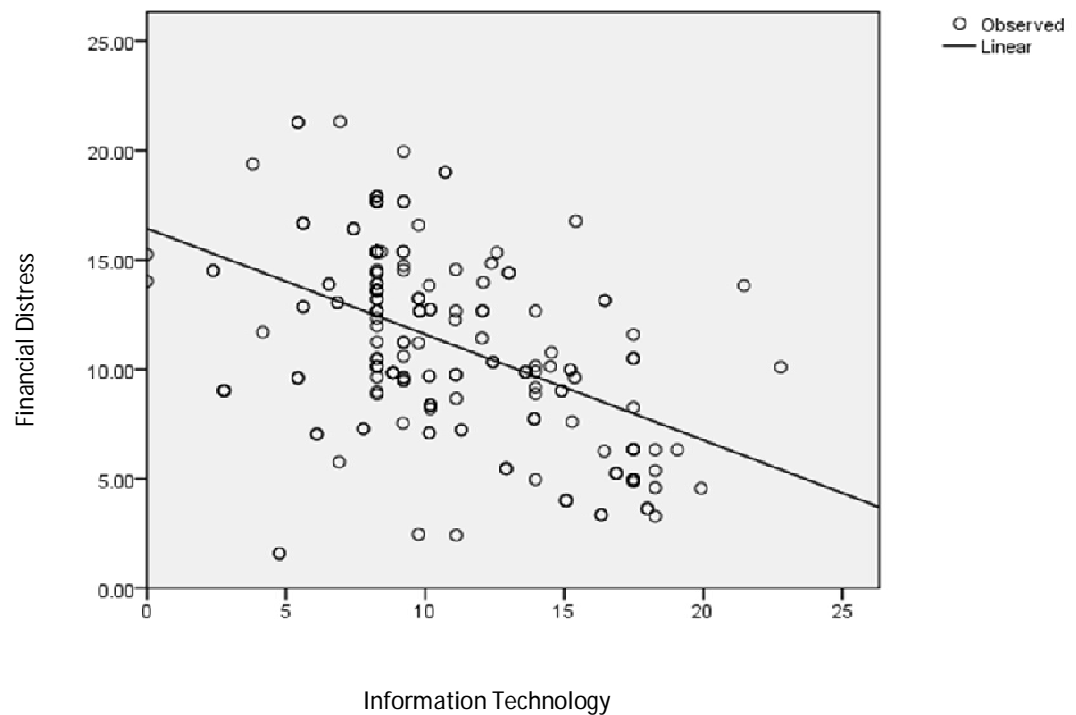
Figure 4. 16: Financial Distress and Information Technology

Descriptive statistics in table 4.19 indicates that highly distressed Local Authorities have a mean score on Information Technology adequacy (8.38). Moderately distressed Local Authorities have a mean score of 10.79 for Information Technology while lowly

distressed Local Authorities have the highest mean score for Information Technology adequacy (12.53).

Table 4. 19: Descriptive Statistics for Information Technology

	N	Mean	Std. Deviation	Std. Error	95% Confidence Interval for Mean		Minimum	Maximum
					Lower Bound	Upper Bound		
Lowly Distressed	61	12.53	4.818	.617	11.30	13.77	3	20
Moderately Distressed	64	10.79	3.449	.431	9.93	11.65	4	23
Highly Distressed	63	8.38	3.172	.400	7.58	9.17	0	21
Total	188	10.55	4.206	.307	9.94	11.15	0	23

The results in table 4.19 were also presented in the form of a weighted mean score plot (figure 4.17). The highest score on effectiveness of information technology was for lowly distressed local authorities (12.53), followed by moderately distressed local authorities (10.79), and highly distressed local authorities (8.38). The findings imply that LAIFOMS is more effective in lowly distress local authorities compared to moderately and highly distressed local authorities.

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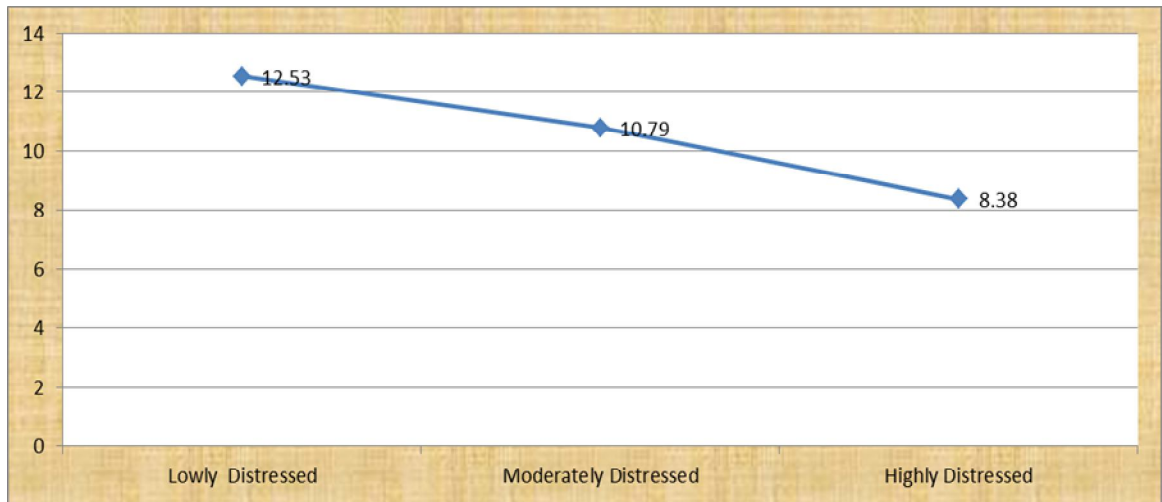
Figure 4. 17: Means Plot for Effectiveness of Information Technology

Analysis of Variance (ANOVA) results in table 4.20 indicates that there exists a significant difference in the adequacy of Information Technology among the three categories of financially distressed Local Authorities (F=18.116, P value=0.000).

Table 4. 20: ANOVA between Groups for Information Technology

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	541.693	2	270.847	18.116	.000
Within Groups	2765.841	185	14.950		
Total	3307.534	187			

Post hoc tests were carried out to establish if significant differences in information technology adequacy exist across different categories of financial distress. Multiple comparison results in table 4.21 indicated that significant differences in Information Technology adequacy exist between lowly distressed and moderately distressed local authorities (probability value = 0.013).Significant differences in Information Technology adequacy exist between lowly distressed and highly distressed local authorities (probability value = 0.00). Significant differences in Information Technology adequacy exist between moderately distressed and highly distressed local authorities (probability value = 0.00).

The finding revealed that information technology adequacy differs across all categories of financially distressed local authorities. The findings imply that Information Technology inadequacy contributes to financial distress in Local Authorities. The findings further imply that those Local Authorities that score lowly on the adequacy of the Information Technology also face higher levels of financial distress.

Table 4. 21: Multiple Comparisons

(I) Distress Category	(J) Distress Category	Mean Difference (I-J)	Std. Error	Sig.	95% Confidence Interval Lower Bound	Upper Bound
Lowly Distressed	Moderately Distressed	1.743*	.692	.013	.38	3.11
	Highly Distressed	4.158*	.695	.000	2.79	5.53
Moderately Distressed	Lowly Distressed	-1.743*	.692	.013	-3.11	-.38
	Highly Distressed	2.416*	.686	.001	1.06	3.77
Highly Distressed	Lowly Distressed	-4.158*	.695	.000	-5.53	-2.79
	Moderately Distressed	-2.416*	.686	.001	-3.77	-1.06

*. The mean difference is significant at the 0.05 level.

The regression results and ANOVA results indicate that information technology is a significant determinant of financial distress among Local Authorities. The findings are consistent with those of a study by Jensen (2002) who observed that Local Municipalities in Africa are a fertile ground for the application ICTs. They are at the front lines of government in their service-oriented interaction with the public and business, often in transaction based systems with many, interlinked components which can be achieved

through e-payment. As such, municipalities have considerable potential to assist in the process of integration of ICTs into the daily lives of its citizens.

Municipal operations from an information technology perspective can be divided into three areas – 1) internal, 2) intra-governmental, and 3) external (with the public). The study by Jensen (2002) concluded that ICT adoption in African Local Authorities would substantially improve their financial fortunes. The findings are also congruent with Waema and Mitullah (2007) who concluded that ICTs are at an infancy stage in Kenya and ICTs have potential of reversing the trend of ineffective governance and improving participation, transparency, accountability, responsiveness, effectiveness and efficiency not forgetting financial base of Local Authorities.

4.3.4: Human Resource Management Practices and Financial Distress

The current study attempted to find out whether the quality and effectiveness of human resource management practices were determinants of financial distress in Local Authorities. Specifically, the following elements of human resource practice were analyzed;

4.3.4.1: Investment in Workforce Training and Development

Descriptive results in Table 4.22 reveals that 54.8% disagreed while a further 4.8% strongly disagreed, bringing to a more than half majority total of (59.6%) of officers who

generally disagreed with the statement that Local Authorities have invested in training and development. Meanwhile, 8.5% neither agreed nor disagreed, while a further minority total of (31.9%) generally agreed with the statement.

The findings are consistent with those of Johnson (2000) and Goleman, Boyatzis, and McKee (2002) who asserts that the aim of training and development within an organisation is to provide staff with the necessary skills and knowledge to fulfill the organisation's corporate and business plan.

The findings imply that Local Authorities may have invested in work force training and development. Perhaps what is lacking is the management of performance since training efforts may go to waste if the performance of the workforce is not properly managed through appraisal and reward techniques.

4.3.4.2: Sponsorship to College and University Courses

Results in Table 4.22 revealed that 45.7% disagreed while a further 6.9% strongly disagreed, bringing to a slightly more than majority total (52.6%) of those officers who generally disagreed with the statement that Local Authority has sponsored its staff for college and university courses. Meanwhile, 18.6% neither agreed nor disagreed while a further minority total (28.8%) generally agreed with the statement.

The findings are consistent with those by Johnson (2000), Brown and Ryan (2003), Barron and Harackiewicz (2000), Baard (2002) who asserts that the aim of academic and advanced training is in line with motivation theory and the need to meet self actualization, self efficacy and adequacy among other goals. These academic courses are also crucial within an organization since they provide staff with the necessary skills and knowledge to fulfill the organization's corporate and business plan.

The findings imply that Local Authorities may have not invested in self development of employees and meeting employee's higher needs of self actualization. However, it may also follow that the efforts of highly qualified individuals in the workforce are also misdirected at maintaining the sorry state of poor service delivery and the resultant financial distress. An environment which encourages dynamism and innovation may be best placed to extract the best performance out of these qualified individuals.

4.3.4.3: Conducting Comprehensive Interviews before Hiring

Results in Table 4.22 revealed that 27.2% agreed while a further 17.9% strongly agreed, bringing to a total of slightly less than half majority (45.1%) of officers who generally agreed with the statement that Local Authorities do not conduct comprehensive interviews before hiring. Meanwhile, 15.8% neither agreed nor disagreed while a further minority total of (39.1%) disagreed with the statement.

The results compare with those in literature like O'Leary, Lou Lindholm, Whitford, and Freeman (2002) and Enz and Siguaw (2000) who assert that the area of employee selection has potential benefits if it is approached from a best practice point of view. Further more, the authors state that the most successful organizations of the future will attract, engage, retain and develop the best and brightest employees.

The finding indicates that best practice in recruitment and selection is not followed by Local Authorities. This has the potential of jeopardizing service delivery. In addition, a poorly recruited workforce may contribute to the financial distress of Local Authorities as they may endeavor to satisfy their appointing authority at the expense of performance.

4.3.4.4: Consideration of Experience and Qualifications in Hiring and Promotion

Results in Table 4.22 reveals that 29.3% agreed while a further 18.5% strongly agreed, bringing to slightly less than half majority total (47.8%), who generally agreed with the statement that Local Authorities do not consider experience and qualifications during hiring and promotions. Meanwhile, 17.9% neither agreed nor disagreed while a further minority total of 34.3% generally disagreed with the statement.

The findings concur with those in Wunsch (2008) who noted Local Authorities have poor recruitment policies. Other studies identified in literature (Carmeli, 2008; Deal, 2007; Frank & Dluhy, 2003; Kloha, Weissert, & Kleine, 2005 and Watson, Handley & Hassett,

2005) argued that that Local Authorities are known to have poor human resource recruitment and selection practices.

The findings imply that Local Authorities have poor recruitment and selection practices. The poor recruitment and selection practices may have led to the poor financial status of Local Authorities since a poorly recruited workforce is less productive in financial management.

4.3.4.5: Conducting Performance Appraisals

Results in Table 4.22 reveals that 36.4% disagreed while a further 11.4% strongly disagreed, bringing to a slightly less than half majority total (47.8%) of those respondents who generally disagreed with the statement that Local Authority does not conduct performance appraisals at least twice a year. Meanwhile, 21.7% neither agreed nor disagreed, while a further minority total (30.5%) agreed with the statement.

The findings concur with those by Zheng, Mark, and O'Neill (2006) and Ahmad & Schroeder (2003) who advocated for performance appraisal as a high performance practices. The author's further link high individual performance practices to superior performance of firms.

The findings implied that Local Authorities do conduct performance appraisals with the hope of boosting productivity of staff. However, conducting performance appraisals has not improved the financial position perhaps because of failure to link performance appraisal with rewards and sanctions.

4.3.4.6: Supporting Performance Appraisals with Rewards

Results in Table 4.22 revealed that 28.3% agreed while a further 28.8% strongly agreed, bringing to a slightly more than half majority total 57.1% of those officers who generally agreed with the statement that performance appraisals are not supported by rewards. Meanwhile, 19.0% neither agreed nor disagreed while a further minority total (23.9%) generally disagreed with the statement.

The findings concur with those by Zheng, Mark, and O'Neill (2006), Ahmad and Schroeder (2003) and Collins and Smith (2006) who argued that performance appraisals should be linked to rewards. This ensures effectiveness of human resources as human resources become highly motivated.

The findings reveal that the Local Authorities have not linked performance appraisal to rewards. This may have resulted into a demotivated workforce. A demotivated workforce may not effectively ensure proper collection of revenue and the management of financial resources.

Table 4. 22: Human Resource Management Practices

Statement	strongly disagree	disagree	neither agree nor disagree	agree	strongly agree
LA has invested in training and development of workforce	9, 4.8%	103, 54.8%	16, 8.5%	48, 25.5%	12, 6.4%
LA has sponsored its staff for college and university courses	13, 6.9%	86, 45.7%	35, 18.6%	45, 23.9%	9, 4.8%
LA doesn't conduct comprehensive Interviews before hiring	9, 4.9%	67, 36.4%	29, 15.8%	50, 27.2%	33, 17.9%
LA doesn't consider experience and qualifications during hiring and promotions	7, 3.8%	60, 32.6%	33, 17.9%	54, 29.3%	34, 18.5%
LA does conduct performance appraisals at least twice a year	21,11.4%	67, 36.4%	40, 21.7%	34, 18.5%	26, 14.1%
Performance Appraisal are not supported by rewards	6, 3.3%	42, 22.8%	35, 19.0%	52, 28.3%	53, 28.8%

4.3.4.7: Rating the Human Resource Management Practices in the Local Authority

As revealed in figure 4.18, a more than half majority (62%) of respondents in the officer's category rated the human resources management practices of Local Authorities poorly. Results further indicate that 38% of officers rated human resource management practices rated as good. The findings imply that Local Authorities have poor human resource management practices.
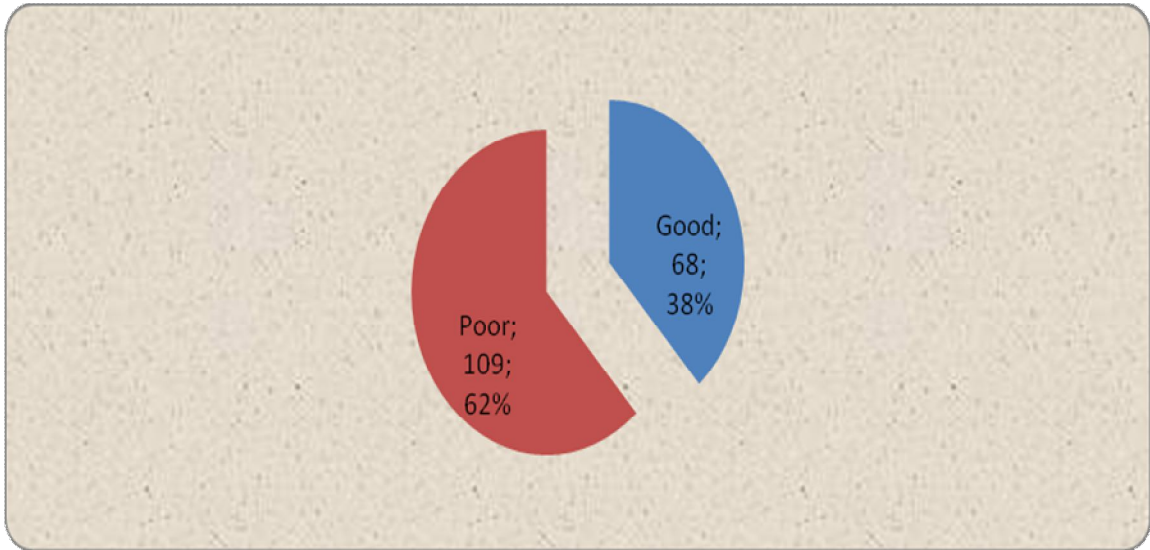
Figure 4. 18: Human Resource Management Practices in Local Authorities

Local Authority officers were also asked to explain why they rated human resource management practices poorly. Those officers who rated human resource management practices poorly also had the following explanations for such a rating;

"Local Authority staff do not do practically what they have learned in class instead they are deployed to do other duties.", "Because when employing and promoting staffs they don't consider experience and academics so much.", "The management lacks proper ways of dealing with its stress.", "Poor supervision, commitment to work is poor", "There is lack of proper job description and deployment is done on political lines.", "They are Politically Influenced.", 'There is a lot of corruption in hiring and Stagnancy in one Scale without promotion.

People being hired at a better Scale while Old employees are not being promoted.", "Poor Training.", "Something is wrong.", "The Worst Department", "Most Corrupt Department.", "its source of worker suffering", "there are appraisal but no rewards or motivation", "no interviews are conducted, politicians sneak in their people without competitive interviews".

The findings concur with those by Kloha, Weissert, and Kleine (2005), Watson, Handley and Hassett (2005) Johnson (2000) and Enz and Siguaw (2000) who argued that that Local Authorities are faced by poor human resource management practices. Content analysis indicates that the officers rated the human resource management poorly because of poor practices in recruitment where recruitment is influenced by corruption and politicians, poor training, poor performance management as job descriptions and deployment is done on political lines, lack of best practice in appraisal and rewarding performance.

The Local Authority officers were requested to suggest recommendations for improvement of Local Authorities' human resource management practices. Some of the suggested recommendations included;

'Staffs should be assigned duties as to what they have trained for." "Training of human resource personnel.", "Training and enforcement of code of conduct", "When hiring and promoting staffs to consider academic qualification and work

experience", "Promotion, Training, Compensations, Fair Remuneration, Improved Work Environment", "Public Service to employ and promote Directly "implementation of job rationalization report as the starting point", 'the question will be best handled once counties come in", "HR department needs to be given a hand to formulate and implement policies and to be fully supported by the executive and the political wing", "involve the mother ministry when hiring and promoting staff", "carry out comprehensive skill audit', "the staff should take responsibilities for their work",.

The findings corroborates with those in literature by Johnson (2000), Enz and Siguaw (2000), O'Leary, Lou, Lindholm, Whitford, and Freeman (2002), Wunsch (2001) and Carmeli (2008) which recommend best practice in human resource management as a way of improving the value derived from Local Authority human resources.

Content analysis indicated that the suggested recommendations for improvements of human resource management practices include; Improvement in hiring practices by ensuring that hiring practices are not politically motivated. In addition, hiring should be done in line with qualifications.

To improve hiring practices, the independence of the human resource department need to be supported by the executive and political wing. A comprehensive skill audit was

recommended. Frequent performance appraisals supported by awards were also recommended. Training and capacity was recommended for both the Human Resource Department and also the staff. The implementation of the rationalization report was also recommended as a way to improve the human resource management in Local Authorities.

4.3.4.8: Customers' Opinion on Whether Financial Distress Could be Attributed to Poor Human Resource Management Practices

Customers were also requested to give an opinion on whether poor human resource management practices such as hiring incompetent staff, failure to train staff, failure to compensate and motivate staff contributed to the financial distress of Local Authorities. Results in figure 4.19 indicated that 39% of customers strongly agreed while a further 30% agreed, bringing to a more than half majority total (69%) of customers who generally agreed with the statement that poor human resource practices such as hiring incompetent staff, failure to train staff; failure to compensate and motivate staff contributed the financial challenges facing Local Authorities. Meanwhile, 22% neither agreed nor disagreed while a further 9% generally disagreed with the statement.

The findings concur with those in literature by Kloha, Weissert, and Kleine (2005), Watson, Handley and Hassett (2005), Johnson (2000) and Enz and Siguaw (2000) which argued that that Local Authorities are faced by poor human resource practices. The findings imply that customers confirmed that Local Authorities have poor human

resource management practices.
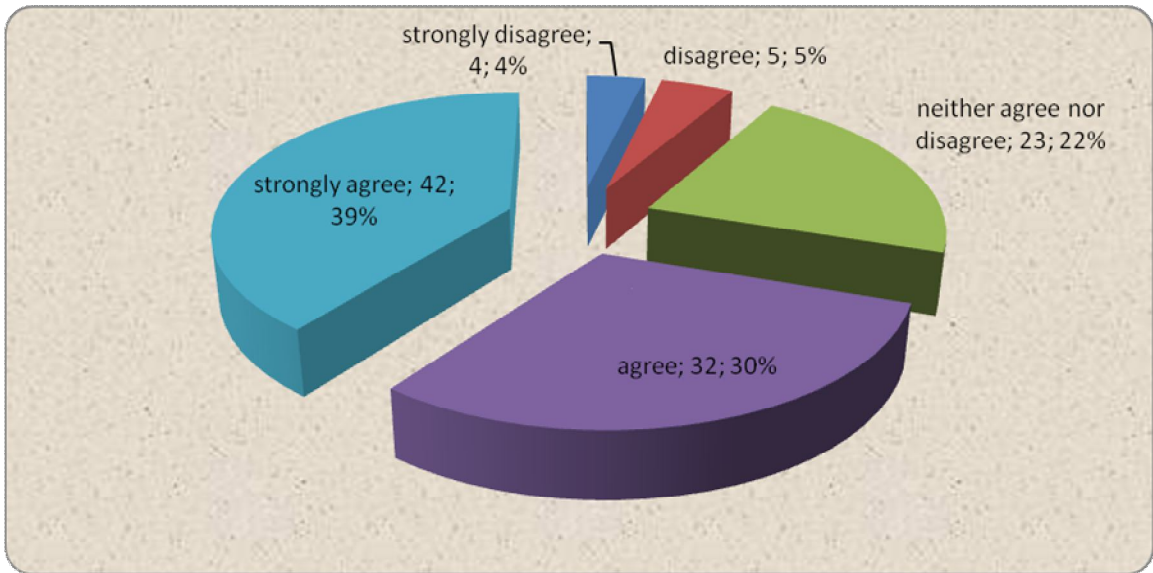
Figure 4. 19: Customers' Opinion on Human Resource Management Practices

4.3.4.9: Relationship between Human Resource Management and Financial Distress

Regression analysis was conducted to empirically determine whether human resource management practices were a significant determinant of financial distress in Local Authorities. Regression results in table 4.23 indicate the goodness of fit for the regression between human resource management practices and financial distress is unsatisfactory. An R squared of (0.291) indicated that (29.1%) of the variances in the financial distress are explained by the variances in the human resource management practices.

The relationship between human resource management practices is negative and significant (b1=-0.693, p value, 0.000). This implies that an increase in the effectiveness of human resource management practices by 1 unit leads to a decrease in financial distress by 0.693 units.

Therefore, the results reveal that the null hypothesis which stated that "human resource management practices do not have a significant contribution to financial distress facing Local Authorities in Kenya" is rejected at the critical value of 0.05 since the reported p value is 0.000. The alternative hypothesis which states that "human resource management practices have a significant contribution to financial distress facing Local Authorities in Kenya is accepted. The regression equation is as follows;

$$Financial\ Distress = 19.383 - 0.693 Human\ Resource\ Managment\ Practices$$

Table 4. 23: Model Summary and Parameter Estimates

	R Square	Constant	b1
Coefficient	0.291	19.383	-0.693
P Value		0.000	0.000

The overall model significance was presented in table 4.24. An F statistic of (76.316) indicated that the overall model was significant. This was supported by a probability

value of (0.000). The reported probability of (0.000) is less than the conventional probability of (0.05). The probability of (0.000) indicated that there was a very low probability that the statement "overall model was insignificant" was true and it was therefore possible to conclude that the statement was untrue.

Table 4. 24: ANOVA for Human Resource Management Practices.

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	1004.063	1	1004.063	76.316	.000
Residual	2447.143	186	13.157		
Total	3451.205	187			

A graphical illustration of the relationship between human resource management practices and financial distress was presented in figure 4.20. The figure revealed that there is a negative relationship between human resource management practices effectiveness and financial distress. The findings concur with those by Kloha, Weissert, and Kleine (2005), Watson, Handley and Hassett (2005) which found a negative relationship between human resource management practices and financial distress. The findings imply that an increase in human resource management practices effectiveness leads to a decline in financial distress.

Figure 4. 20: Financial Distress and Human Resource Management Practices

Descriptive statistics in table 4.25 indicated that highly distressed Local Authorities have a mean score on human resource management practices of (9.54). Moderately distressed Local Authorities have a mean score of (11.71) for human resource management practices while lowly distressed Local Authorities have the highest mean score for human resource management practices (13.66).

Table 4. 25: Descriptive Statistics for Human Resource Management Practices

	N	Mean	Std. Deviation	Std. Error	95% Confidence Interval for Mean		Minimum	Maximum
					Lower Bound	Upper Bound		
Lowly Distressed	61	13.66	2.964	.380	12.90	14.42	9	19
Moderately Distressed	64	11.71	2.702	.338	11.04	12.39	6	19
Highly Distressed	63	9.54	3.044	.384	8.77	10.30	5	21
Total	188	11.61	3.343	.244	11.13	12.10	5	21

The results in table 4.25 were also presented in the form of a weighted mean score plot (figure 4.21). The highest score on effectiveness of human resource management practices was for lowly distressed (13.66), followed by moderately distressed (11.71), and highly distressed (9.54). The findings imply that human resource management practices are more effective in lowly distressed local authorities compared to moderately and highly distressed local authorities.
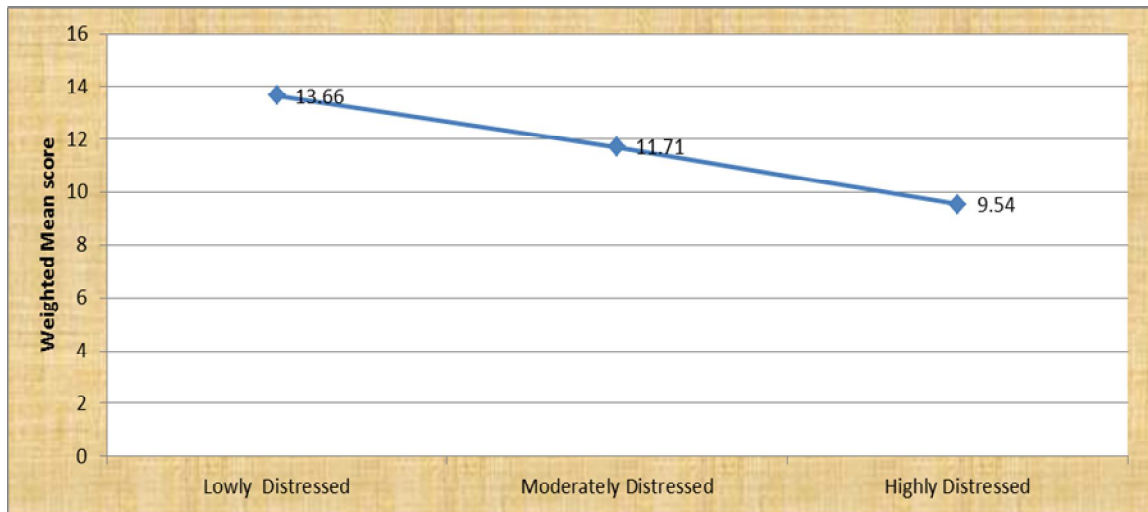
Figure 4. 21: Weighted Mean Plot of Human Resource Management Practices

ANOVA results in table 4.26 revealed that there exists a significant difference in human resource management practices between the three categories of financially distressed Local Authorities (F=31.279, P value=0.000).

Table 4. 26 : ANOVA between Groups for Human Resource Management Practices

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	528.102	2	264.051	31.279	.000
Within Groups	1561.752	185	8.442		
Total	2089.854	187			

Multiple comparisons in table 4.27 revealed that significant difference in human resource management practices existed between lowly distressed and moderately distressed Local Authorities (p value of 0.000). Significant differences between lowly distressed and highly distressed Local Authorities also existed as far as human resource management scores were concerned (p value of 0.000). Findings further revealed that human resource management scores also differed significantly between lowly distressed and highly distressed local authorities (p value of 0.000). The findings imply that human resource management practices contribute to financial distress.

Table 4. 27: Multiple Comparisons

(I) Distress Category	(J) Distress Category	Mean Difference (I-J)	Std. Error	Sig.	95% Confidence Interval Lower Bound	Upper Bound
Lowly Distressed	Moderately Distressed	1.950[*]	.520	.000	.92	2.98
	Highly Distressed	4.124[*]	.522	.000	3.09	5.15
Moderately Distressed	Lowly Distressed	-1.950[*]	.520	.000	-2.98	-.92
	Highly Distressed	2.175[*]	.516	.000	1.16	3.19
Highly Distressed	Lowly Distressed	-4.124[*]	.522	.000	-5.15	-3.09
	Moderately Distressed	-2.175[*]	.516	.000	-3.19	-1.16

*. The mean difference is significant at the 0.05 level.

The results from the descriptive statistics, regression analysis and Analysis of Variance (ANOVA) indicated that human resource management practice is a significant

determinant of financial distress in Local Authorities. The findings are consistent with those of Capalbo, Grossi, Ianni and Sargiacomo (2010) who identified incompetence and corruption among Local officials as major determinant of financial distress in Local Authorities in Italy.

4.3.5: Government Regulation and Financial Distress

The current study sought to find out whether government regulation is a determinant of financial distress in Local Authorities. Specifically, the study focused on the following areas of government regulation; The Transfer of Functions Act (1969); The transfer of Graduated Personal Tax in 1974 to central government; The Constituency Development Fund Act.

4.3.5.1: The Transfer of Functions Act (1969)

Descriptive results in Table 4.28 indicated that 38.8% agreed while a further 13.3% strongly agreed, bringing to a slightly more than half majority (52.1%) of those respondents who generally agreed with the statement that The Transfer of Functions Act (1969) has greatly eroded the revenue base of the Local Authorities. Meanwhile, (28.2%) neither agreed nor disagreed while a further minority total of (19.7%) generally disagreed with the statement. The findings collaborates with those by Institute of Economic Affairs (2009), which revealed that government regulations that have a direct impact on the financial operations of Local Authorities include the Transfer of Functions

Act (1969) which saw the central government take over key responsibilities from Local Authorities.

The findings revealed that there The Transfer of Functions Act (1969) may have eroded the revenue base of Local Authorities and this may have contributed to the financial distress of Local Authorities.

4.3.5.2: The Graduated Personal Tax of 1974

Descriptive results in Table 4.28 indicates that 41.0% agreed while a further 8.0% strongly agreed, bringing to a slightly less than half majority (49.0%) of those officers who generally agreed with the statement that that the transfer of Graduated Personal Tax in 1974 to the central government has greatly eroded the revenue base for Local Authorities. Meanwhile, 31.9% neither agreed nor disagreed while further minority of 19.1% generally disagreed with the statement.

The findings agree with those by Institute of Economic Affairs (2009), which revealed that government regulations that have a direct impact on the financial operations of Local Authorities including the transfer of the Graduated Personal Tax in 1974. The findings imply that the transfer of graduated personal tax took away sources of revenue from Local Authorities. This may have contributed to the financial distress being witnessed in Local Authorities today.

4.3.5.3: The Constituency Development Fund Act of 2003

Result in Table 4.28 reveals that 39.9% agreed while a further 11.7% strongly agreed, bringing to slightly more than half majority (51.6%) of those respondents who generally agreed with the statement that the Constituency Development Fund Act (2003) has diverted the development agenda from Local Authorities to constituencies. Meanwhile, 25.0% neither agreed nor disagreed while a further minority total (23.4%) generally disagreed with the statement.

The findings are consistent with those by Institute of Economic Affairs (2009) which argues that there are several regulations that have affected the financial and non financial capacity of Local Authorities enacted by the government since independence.

The findings revealed that the passing of the Constituency Development Fund Act (2003) which initiated the mechanism for financing community projects at constituency level in competition with Local Authorities led to the weakening of the focus on councils as the primary channel for service delivery at the Local level. This may have led to the weakening of the financial base of Local Authorities.

Table 4. 28: Government Regulation and Financial Distress

Statement	strongly disagree	disagree	neither agree nor disagree	agree	strongly agree
The Transfer of Functions Act (1969) has greatly eroded the revenue base of the local authority	9, 4.8%	28, 14.9%	53, 28.2%	73, 38.8%	25, 13.3%
The Graduated Personal Tax in 1974 has greatly eroded the revenue base for local authorities	7, 3.7%	29, 15.4%	60, 31.9%	77, 41.0%	15, 8.0%
The Constituency Development Act Fund Act (2003) has diverted the development agenda from Local authorities to constituencies	16, 8.5%	28, 14.9%	47, 25.0%	75, 39.9%	22, 11.7%

4.3.5.4: Rating the Adequacy of Government Regulation in the Local Authority

As revealed by figure 4.22, a majority (66%) of respondents in the officer's category rated the government regulation of Local Authorities as inadequate. Meanwhile, 34% of officers rated the government regulation as adequate. The findings are in agreement with descriptive and inferential results which show that Local Authorities have been affected by unfavourable regulation.
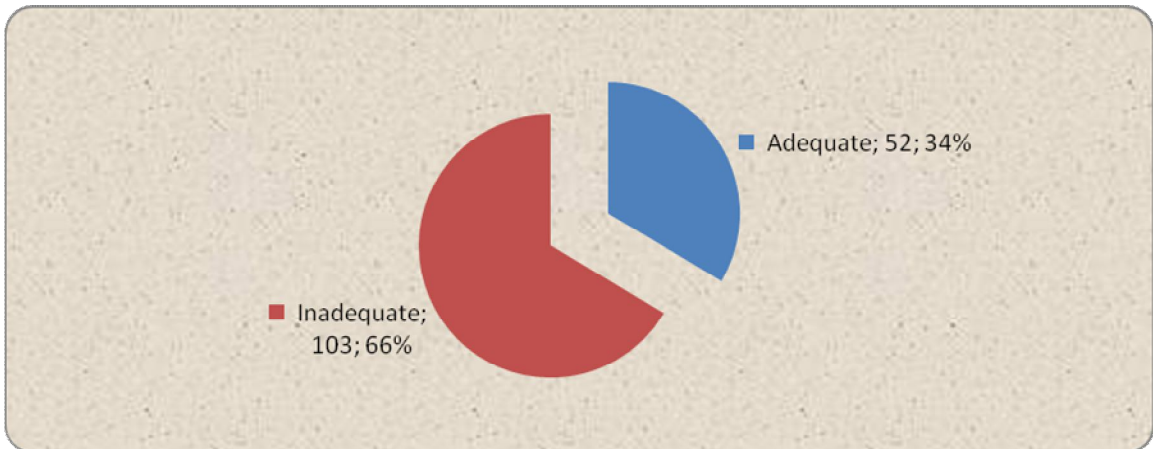
Figure 4. 22: Adequacy of Government Regulation in Local Authorities.

Local Authority officers were also asked to explain why they rated government regulation as inadequate. Some of the explanations included;

"They sometimes contradict those of the council especially those affecting traders SBP". "The government regulates Local Authority budget ceilings". "There are no strict measures in regulating Local Authority by the government". "Sources which were taken by central Government from LA have made / minimized L.As Revenue Margin"." Government is reluctant in regulating LA". "Not much is known about the above Acts". "The government has concentrated funding on constituencies rather than Local Authorities". "Only LATF binds government with Local Authorities". "Regulation does not take into account the LA need". "There has never been adequate consultation". "Much interference from central government"." the Local Authority is supposed to be autonomous".

The findings agree with those in Davey (2012) which asserted that government regulation may be harmful if it doesn't take into account the flexibility needs of the Local Authority. In addition, Davey (2012) asserts that regulation that stifles the efficiency and effectiveness of Local Authorities in service delivery may lead to financial distress of Local Authorities.

Content analysis indicated that the officers rated the government regulation poorly because of three schools of thought on government regulation; overregulation, under regulation and ineffective regulation. Those officers who indicated that there is too much interference from central government and that the Local Authority's are supposed to be autonomous seem to propose that Local authorities are over regulated. Those officers who think that government is reluctant to regulate Local Authority's, only LATF binds government with Local Authorities, and that there are no strict measures of regulating the Authority, seem to think that Local Authorities are under regulated.

However, those officers who cite parallel bodies, regulations that sometimes contradict those of the council especially those affecting traders, that sources which were taken by central Government from Local Authority has minimized Local Authorities Revenue Margin, that the government has concentrated funding on constituencies rather than Local Authorities, that regulation does not take into account the Local Authority need, seem to belong to the " ineffectiveness of government regulation" school of thought.

The Local Authority officers were requested to suggest recommendations for improvement of Local Authorities' government regulation. Some of the suggested recommendations included;

> "The government should be directly involved in the practices of Local Authorities", 'the government regulation should be 100%'', "They Should Revert back all Sources of revenue which were taken by Central government to L.A,S.", "Restructure, Management in Utilization of Funds & Review Some of the ACTS That Divert Funds to other Ministries/ Departments", "government to give close supervision", "Local Authority be given power to impose revenue collection", "setting up anti corruption committee", " more finances to be channeled through LA", "to consider LA when setting regulations", "Divorce Politics from Local Councils.","" Before the government passes any regulation affecting the council, it should liaise with it first.", "More supervision needed.".

The findings agree with those in James (2012) which asserts that Central government's primary mechanism for influencing and supporting good Local government is the legal framework within which councils operate. If this mechanism is properly focused, savings and efficiencies can be achieved across councils. Achieving the necessary conditions to improve Local government efficiency requires a coherent package of actions – no single

action will change the culture and the settings in Local government and improve efficiency.

Content analysis indicated that the suggested recommendations for improvements of government regulation include an increase in regulation of Local Authorities where the government closely monitors the activities of a Local Authority. The sources of revenue that were taken away from the Local Authorities should be reverted back to them. Officers also suggested that some of the Acts that divert funds to other ministries/departments should be reviewed. The Local Authorities also need to be given more powers to increase their sources of revenue.

It was also recommended that perhaps the law should be amended to enable the setting up of an anticorruption committee at the Local Authority level. In addition, it was suggested that cap 265 should be amended so as to divorce politics from Locals. Most importantly, it was recommended that the government should liaise with the Local Authorities and conduct comprehensive consultation on how a certain law would affect them before passing it.

4.3.5.5: Customers' Opinion on Whether Financial Distress Could be attributed to Poor Government Regulation

Customers were also requested to give an opinion on whether poor regulation contributed

to the financial distress of Local Authorities. Results in figure 4.23 indicated that 36% of customers strongly agreed while a further 31% strongly agreed bringing to a majority (67%) of those customers who generally agreed with the statement that statement that poor regulation contributed to the financial challenges facing Local Authorities. Meanwhile, 7% neither agreed nor disagreed while a further minority (26%) generally disagreed with the statement.
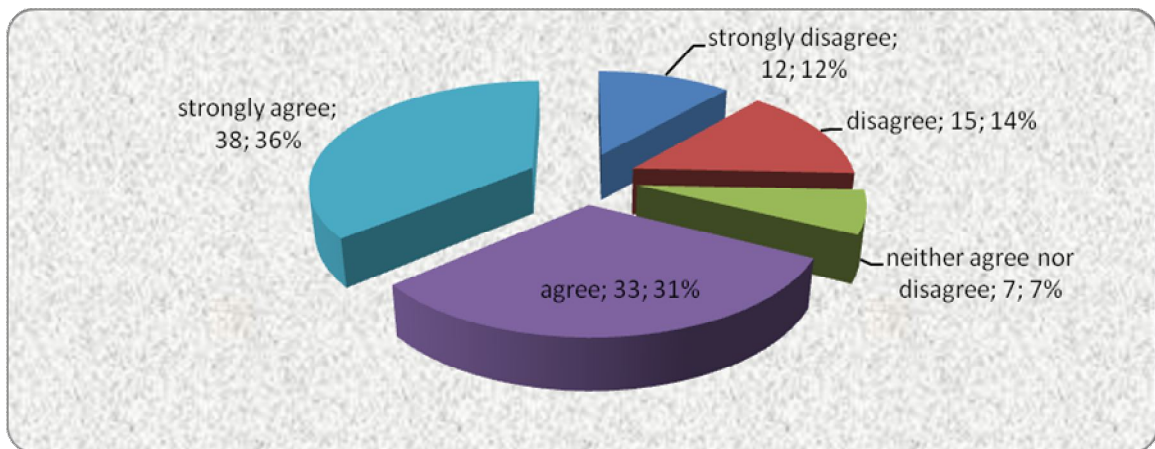
Figure 4. 23: Customer's Opinion on Government Regulation

4.3.5.6: Relationship between Government Regulation and Financial Distress

Regression analysis was conducted to empirically determine whether government regulation was a significant determinant of financial distress in Local Authorities. Regression results in table 4.29 indicate the goodness of fit for the regression between government regulation and financial distress is unsatisfactory. An R squared of 0.809

indicates that (80.9%) of the variances in the financial distress are explained by the variances in the government regulation.

As revealed in table 4.29, the relationship between government regulation and financial distress is positive and significant (b1=1.575, p value, 0.000). This implies that an increase in the ineffectiveness of government regulation by 1 unit leads to an increase in financial distress by 1.575 units.

Therefore, the results reveal that the null hypothesis which stated that "government regulation does not have a significant contribution to financial distress facing Local Authorities in Kenya" is rejected at the critical value of 0.05 since the reported p value is 0.000. The alternative hypothesis which states that "government regulation has a significant contribution to financial distress facing Local Authorities in Kenya is accepted. The regression equation is as follows;

Financial Distress = 4.492 + 1.575 Government Regulation

Table 4. 29: Model Summary and Parameter Estimates

	R Square	Constant	b1
Coefficient	0.809	4.492	1.575
P Value		0.000	0.000

The overall model significance was presented in table 4.30. An F statistic of (789.649) indicated that the overall model was significant. This was supported by a probability value of (0.000). The reported probability of (0.000) is less than the conventional probability of (0.05). The probability of (0.000) indicated that there was a very low probability that the statement "overall model was insignificant" was true and it was therefore possible to conclude that the statement was untrue.

Table 4. 30: ANOVA for Government Regulation.

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	2793.259	1	2793.259	789.649	.000
Residual	657.946	186	3.537		
Total	3451.205	187			

A graphical illustration of the relationship between Government Regulation and financial distress was presented in figure 4.24. The figure revealed that there is a positive relationship between unfair government regulation and financial distress. The findings concur with those in Institute of Economic affairs (2009) which found a positive relationship between particular government regulation such as the CDF Act (2003) and financial distress. The findings imply that an increase in unfair government regulations leads to an increase in financial distress.
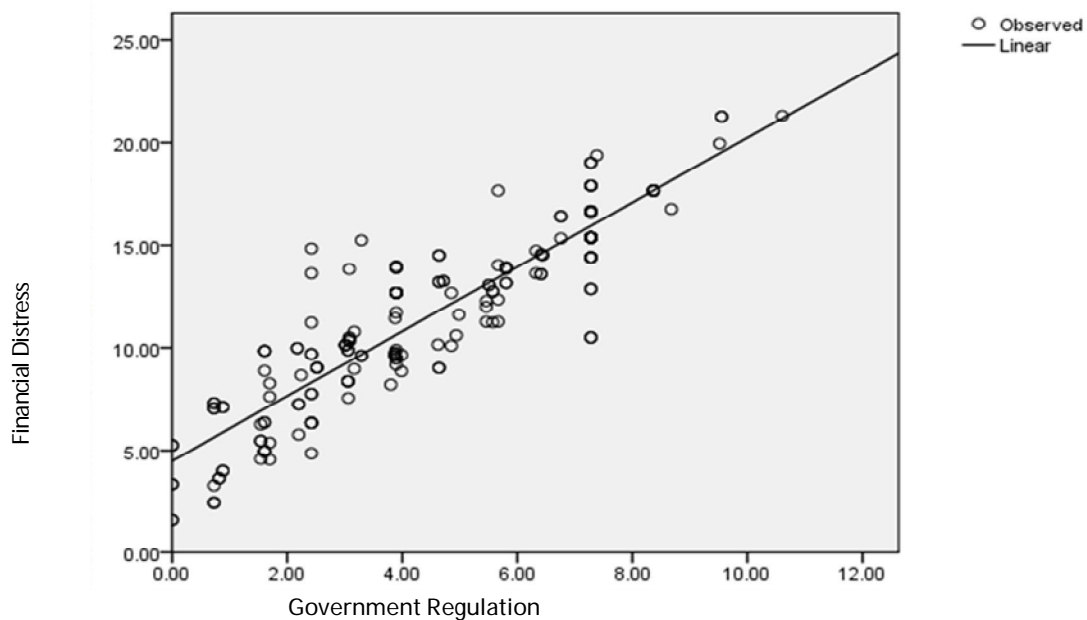
Figure 4. 24: Financial Distress and Government Regulation

Descriptive statistics in table 4.31 indicated that highly distressed Local Authorities have a mean score of 6.803 on government regulation. Moderately distressed Local Authorities have a mean score of 4.251 for government regulation while lowly distressed Local Authorities have the lowest mean score for government regulation (1.902).

Table 4. 31: Descriptive Statistics for Government Regulation

	N	Mean	Std. Deviation	Std. Error	95% Confidence Interval for Mean Lower Bound	95% Confidence Interval for Mean Upper Bound	Minimum	Maximum
Lowly Distressed	61	1.9021	1.21094	.15504	1.5920	2.2123	.00	4.64
Moderately Distressed	64	4.2516	1.42451	.17806	3.8958	4.6074	1.61	7.28
Highly Distressed	63	6.8031	1.63439	.20591	6.3915	7.2147	2.42	10.61
Total	188	4.3443	2.45460	.17902	3.9911	4.6975	.00	10.61

The results in table 4.31 were also presented in the form of a weighted mean score plot (figure 4.25). The highest score on the ineffectiveness of government regulation was for highly distressed local authorities (6.8031), followed by moderately distressed (4.2516), and lowly distressed local authorities (1.902). The findings imply that government regulation is more ineffective in highly distressed local authorities compared to moderately and lowly distressed local authorities.
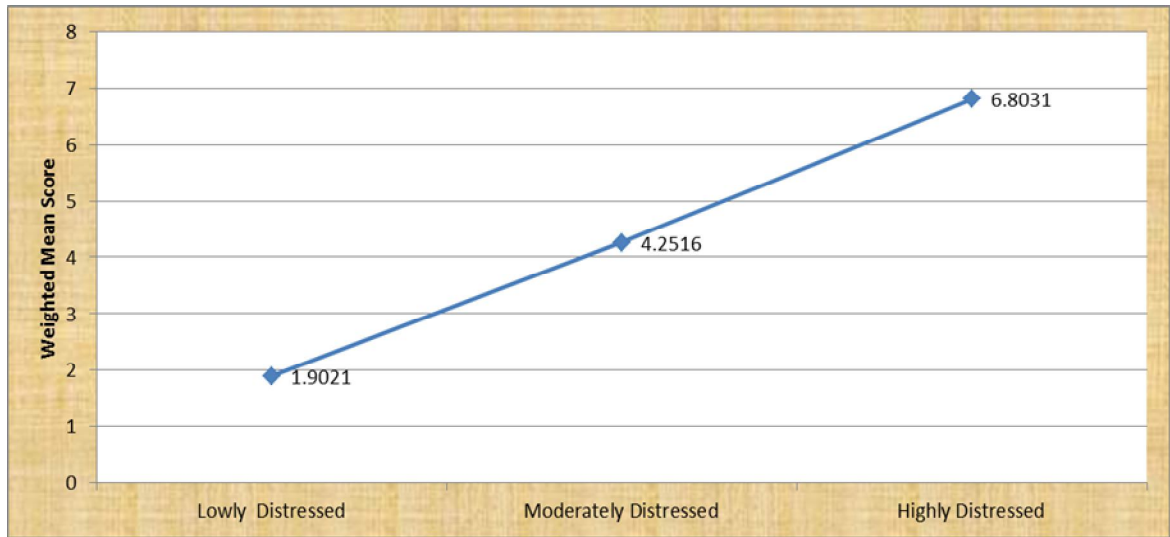
Figure 4. 25: Weighted Mean Plot of Government Regulation

Analysis of Variance (ANOVA) results in table 4.32 indicated that there exists a significant difference in the adequacy and effectiveness of government regulation between the three categories of financially distressed Local Authorities (F=180.725, P value=0.000).

Table 4. 32: ANOVA between Groups for Government Regulation

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	745.249	2	372.625	180.725	.000
Within Groups	381.439	185	2.062		
Total	1126.688	187			

Multiple comparison results in table 4.33 indicated that adequacy of government regulation significantly differs between lowly distressed and moderately distressed (p value of 0.000). Results indicated that adequacy of government regulation significantly differs between lowly distressed and moderately distressed (p value of 0.000). Results further indicated that adequacy of government regulation significantly differs between moderately distressed and highly distressed (p value of 0.000).

The findings imply that government regulation causes a higher level of distress in some Local Authorities than in others. The findings further imply that those Local Authorities that score highly on the inadequacy of the government regulation also face higher levels of financial distress.

Table 4. 33: Multiple Comparisons

(I) Distress Category	(J) Distress Category	Mean Difference (I-J)	Std. Error	Sig.	95% Confidence Interval Lower Bound	Upper Bound
Lowly Distressed	Moderately Distressed	-2.34948*	.25694	.000	-2.8564	-1.8426
	Highly Distressed	-4.90099*	.25793	.000	-5.4098	-4.3921
Moderately Distressed	Lowly Distressed	2.34948*	.25694	.000	1.8426	2.8564
	Highly Distressed	-2.55151*	.25484	.000	-3.0543	-2.0487
Highly Distressed	Lowly Distressed	4.90099*	.25793	.000	4.3921	5.4098
	Moderately Distressed	2.55151*	.25484	.000	2.0487	3.0543

*. The mean difference is significant at the 0.05 level.

The results from the descriptive statistics, regression analysis and Analysis of Variance (ANOVA) indicated that government regulation is a significant determinant of financial distress in Local Authorities. The findings are consistent with those of Boex and Muga (2009) who investigated the determinants of quality financial management in Local Authorities in Tanzania and concluded that government regulation can have both positive and negative effects on the financial performance of Local Authorities. The findings are consistent with a study by Capalbo, Grossi, Ianni and Sargiacomo (2010) that attempted to investigate the nature of financial distress in Italians Local governments and concluded

that bureaucracy and poor legislation are major causes of financial distress in Local Authorities.

4.4: Multiple Regression Analysis for the Determinants of Financial Distress

A multiple regression analysis was conducted to investigate the joint causal relationship between the independent and dependent variables. Regression results in table 4.34 indicated that the goodness of fit for the regression of independent variables and financial distress is satisfactory. An R squared of (0.980) indicated that (98%) of the variances in the financial distress are explained by the variances in the determinants of financial distress.

The regression equation was as follows;

$$
\begin{aligned}
Financial\ Distress \\
&= 21421 - 0.831 Financial\ Management\ Practices \\
&+ 0.031 Human\ Resource\ Management\ Practices \\
&- 0.014\ Corporate\ Governance\ Practices \\
&+ 0.156 Government\ Regulation - 0.037 Information\ Technology
\end{aligned}
$$

Table 4. 34: Model Fit for Determinants of Financial Distress

Model	R	R Squared	Adjusted R Squared	Std. Error of the Estimate
	.990	.980	.979	.62060

ANOVA results were presented in table 4.35. The results indicated that the overall model was significant, that is, the independent variables were good joint explanatory variables/determinants for financial distress (F=1755.763, P value =0.000).

Table 4. 35: ANOVA for the Determinants of Financial Distress

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	3381.109	5	676.222	1755.763	.000
Residual	70.096	182	.385		
Total	3451.205	187			

Regression results in table 4.36 indicated that the relationship between Financial management practices and financial distress was negative and significant (b1=-0.831, p value, 0.000). The findings agree with those by (Kloha, Weissert, & Kleine, 2005; Frank & Dluhy, 2003; Deal, 2007; IEA, 2009 and Jonga & Chirisa, 2009) who link financial mismanagement to financial distress.   This implies that an increase in the effectiveness

of financial management practices by 1 unit leads to a decrease in financial distress by 0.831 units.

Regression results in table 4.36 indicated that the relationship between Information technology and financial distress was negative and significant (b1=-0.037, p value, 0.006). The findings agree with those in Waema and Mitullah (2007) and Jensen (2002) which link inadequacy of Information technology to financial distress. This implies that an increase in the effectiveness and adequacy of Information technology by 1 unit leads to a decrease in financial distress by 0.037 units.

Regression results in table 4.36 indicated that the relationship between Government Regulation and financial distress was positive and significant (b1=0.156, p value, 0.000). The findings agree with those by James (2012), Davey (2012) and Institute of Economic Affairs (2009) which link ineffective government regulation to financial distress of Local Authorities. This implies that an increase in the inadequacy and ineffectiveness of regulation by 1 unit leads to an increase in financial distress by 0.156 units.

Regression results in table 4.36 indicated that human resource practices and corporate governance practices are not significant determinants of financial distress. However, these results contradicted univariate regression results in table 4.7 and in table 4.19 obtained using curve estimation as well as ANOVA results in other parts of this study

that concluded that human resource practices and corporate governance practices are significant determinants of financial distress. The current study adopted the univariate regression and ANOVA results on the strength of the goodness of fit (0.980) and the F statistic for joint explanatory power (F=1755.763, P value =0.000).

Table 4. 36: Model Summary and Parameter Estimates

Model	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	21.421	.494		43.379	.000
Financial management practices	-.831	.023	-.897	-35.658	.000
Human Resource Management Practices	.031	.018	.024	1.689	.093
Corporate Governance Practices	-.014	.017	-.013	-.802	.423
Government Regulation	.156	.043	.089	3.637	.000
Information Technology	-.037	.013	-.036	-2.787	.006

4.5: Analysis of Financial Distress in Local Authorities

The study attempted to confirm whether Local Authorities were under financial distress. Specifically, the study focused on the following elements of financial distress; Local Authority budget out run ratio, salary to total operating revenue ratio, net debt to total

operating revenue ratio, interest expense to total operating revenue ratio, council financial statements are frequently qualified (meaning that they are frequently not given a good bill of health) and National Audit Office queries a large percentage of expenditures during the audit process (meaning that there seems to be expenditures that demonstrate fiscal stress).

4.5.1: Local Authority Budget out run Ratio (Meaning that the Local Authority Always Spends more than it has Budgeted)

Results in Table 4.37 reveal that 49.5% agreed while a further 28.2% strongly agreed, bringing to a more than half majority (77.7%) of respondents from the officers category who generally agreed with the statement that the Local Authority budget out run ratio is high, meaning Local Authorities spend more money than budgeted. Meanwhile, 7.4% neither agreed nor disagreed while a further minority (14.9%) generally disagreed with the statement.

The finding concur with those in Western Australian Local Government Association (WALGA) (2006) which asserted that Local governments in Western Australia were in a state of financial distress as shown by the high budget outrun ratio. The findings also agree with Boex and Muga (2004) who argued that Tanzania Local Authorities were in poor financial health. The findings therefore imply that Local Authorities are facing financial distress.

4.5.2: Salary to Total Operating Revenue Ratio (Meaning that the Salary Expense Take More than 70% Portion of the Operating Revenue)

Findings in Table 4.37 indicate that 44.7% agreed while a further 18.1% strongly agreed, bringing to a more than half majority (62.8%) of officers who generally agreed with he statement that the salary to total operating revenue ratio is high (meaning that the salary expense take more than 70% portion of the operating revenue). Meanwhile, 15.4% neither agreed nor disagreed while a further minority total (21.8%) generally disagreed with the statement.

The finding concur with those in Western Australian Local Government Association (WALGA) (2006) which asserted that Local governments in Western Australia were in a state of financial distress as shown by the high salary to total operating revenue ratio. The findings also corroborate with those of Boex and Muga (2004), Price Waterhouse Coopers, (2006), Capalbo, Grossi, Ianni and Sargiacomo (2010) and Carmeli (2008) who argued that Local Authorities face cash flow problems leading to financial distress. The findings therefore imply that Local Authorities in Kenya are facing financial distress.

4.5.3: Net Debt to Total Operating Revenue Ratio (Meaning the Local Authority is Highly Indebted)

Results in Table 4.37 also indicate that 48.9% agreed while a further 14.9% strongly agreed, bringing to a more than half majority (63.8%) of officers who generally agreed

with the statement that net debt to total operating revenue ratio is high (meaning the Local Authority is highly indebted). Meanwhile, 16.0% were neutral while a further minority (20.2%) generally disagreed with the statement.

The finding concur with those in Western Australian Local Government Association (WALGA) (2006) which asserted that Local governments in Western Australia were in a state of financial distress as shown by the high Net debt to total operating revenue ratio. The findings also agree with (Watson, Handley & Hassett, 2005; Honadle, 2006; Wunsch, 2008; IEA, 2009; Schoeman, 2011; Jonga & Chirisa, 2009 and Sennoga, 2004) which assert that Local Authorities were in poor financial health because of high levels of loans taken to pay salaries and other outstanding creditors . The findings imply that Local Authorities in Kenya are facing financial distress due to the high levels of indebtness.

4.5.4: Interest Expense to Total Operating Revenue Ratio (Meaning that the Local Authority may be over Reliant on Overdrafts).

Results in Table 4.37 also indicated that 46.3% of respondents agreed while a further 19.1% disagreed, bringing to a more than half majority (65.4%) of officers who generally agreed with the statement that the interest expense to total operating revenue ratio is high (meaning that the Local Authority may be over reliant on overdrafts and also defaulted payment of other statutory obligations which attract interests penalty). Meanwhile, 16.5% neither agreed nor disagreed; while a further minority (18.1%) generally disagreed with

the statement.

The finding concur with those in Western Australian Local Government Association (WALGA) (2006) which asserted that Local governments in Western Australia were in a state of financial distress as shown by the high interest expense to total operating revenue ratio. The findings also agree with (Carmeli, 2008; Deal, 2007; Frank & Dluhy, 2003; Kloha, Weissert, & Kleine, 2005; Watson, Handley & Hassett, 2005 and Honadle, 2006) who argued that Local Authorities were in poor financial status. The findings imply that Local Authorities in Kenya are facing financial distress.

4.5.5: Council Financial Statements are Frequently Qualified (Meaning that they are Frequently not Given a Good Bill of Health)

Results in Table 4.37 reveals that 50.5% of respondents agreed while a further 8.5% strongly agreed with the statement, bringing to a more than half majority (59%) of officers who generally agreed with the statement that council financial statements are frequently qualified (meaning that they are frequently not given a good bill of health by Kenya National Audit Office). Meanwhile, 23.9% neither agreed nor disagreed while a further minority (17.1%) generally disagreed with the statement.

The finding concur with those in Western Australian Local Government Association (WALGA) (2006) which asserted that Local governments in Western Australia were in a

state of financial distress as shown by the frequent qualification of council financial statements due to unexplained expenditures. The findings also agree with Boex and Muga (2004) who argued that Tanzania Local Authorities were in poor fiscal health.

The findings imply that Local Authorities in Kenya are facing financial distress.

4.5.6: National Audit Office Queries a Large Percentage of Expenditures During the Audit Process (Meaning that there Seems to be Expenditures that Demonstrate Financial Stress)

Results in Table 4.37 revealed that 51.6% agreed while a further 13.8% strongly agreed , bringing to a more than half majority (65.4%) of those offices who generally agreed with the statement that that the National Audit Office queries a large percentage of expenditures during the audit process (meaning that there seems to be expenditures that demonstrate fiscal stress). Meanwhile, 21.3% neither agreed nor disagreed while a further minority (13.3%) generally disagreed with the statement.

The findings concur with those in Western Australian Local Government Association (WALGA) (2006) which asserted that Local governments in Western Australia were in a state of financial distress as shown by the National Audit Office queries a large percentage of unpaid expenditures during the audit process. The findings also agree with Boex and Muga (2004) who argued that Tanzania Local Authorities were in poor financial health. The findings further compare well with those by Dollery (2009) and

Price Waterhouse Coopers (2006) which found evidence of financial distress in Local Authorities due to incurring huge expenditures without the ability to meet such expenditures. These findings imply that Local Authorities in Kenya are in a state of financial distress since majority of the Local Authorities' overcommit themselves through the tendering process. Table 4.37 presents the detailed findings.

Table 4. 37: Financial Distress in Local Authorities

Statement	strongly disagree	disagree	neither agree nor disagree	agree	strongly agree
The local authority budget out run ratio is high (meaning The Local Authority always spends more than it has budgeted).	1, 0.5%	27, 14.4%	14, 7.4%	93, 49.5%	53, 28.2%
The salary to total operating revenue ratio is high (meaning The salary expense take more than 70% portion of the operating revenue)	9, 4.8%	32, 17.0%	29, 15.4%	84, 44.7%	34, 18.1%
The net debt to total operating revenue ratio is high (meaning The LA is highly indebted)	6, 3.2%	32, 17.0%	30, 16.0%	92, 48.9%	28, 14.9%
The Interest expense to total operating revenue ratio is high (meaning The LA may be over reliant on overdrafts)	1, 0.5%	33, 17.6%	31, 16.5%	87, 46.3%	36, 19.1%
The council financial statements are frequently qualified (meaning they are frequently not given a good bill of health)	6, 3.2%	26, 13.8%	45, 23.9%	95, 50.5%	16, 8.5%
The National audit office queries a large percentage of expenditures during the audit process (meaning there seems to be expenditures that demonstrate fiscal stress)	5, 2.7%	20, 10.6%	40, 21.3%	97, 51.6%	26, 13.8%

4.5.7: Critical Analysis of Financial Distress in Local Authorities

Descriptive results in table 4.38 revealed that municipal councils have the highest level of distress (11.758) followed by city councils (11.578), county councils (10.896) and town councils (9.815).

Table 4. 38: Descriptive Statistics for Distress Across Local Authority Categories

	N	Mean	Std. Deviation	Std. Error	95% Confidence Interval for Mean		Minimum	Maximum
					Lower Bound	Upper Bound		
City Councils	22	11.57	3.68200	.78500	9.9463	13.2113	3.35	16.68
Municipal Councils	91	11.57	4.05012	.42457	10.9148	12.6018	1.59	21.32
County Councils	42	10.89	4.60582	.71069	9.4608	12.3313	3.29	19.38
Town Councils	25	9.81	4.17826	.83565	8.0904	11.5398	1.59	17.66
Total	180	11.26	4.18320	.31180	10.6500	11.8805	1.59	21.32

However, as indicated by table 4.39, there is no significant difference in levels of distress among the different types of councils (F=1.589, P value =0.194). The finding implies that financial distress is not a preserve of a specific category of Local Authority but crosscuts across all categories of Local Authorities.

Table 4. 39: ANOVA for Distress Across Categories of Local Authorities

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	82.584	3	27.528	1.589	.194
Within Groups	3049.760	176	17.328		
Total	3132.344	179			

4.5.8: Customers' Awareness that Local Authorities Suffer from Financial Challenges

As illustrated in Figure 4.26, customers for Local Authorities were also asked to express their opinion on whether they were aware that Local Authorities were suffering from financial distress. A majority of customers (70%) indicated that they were aware that Local Authorities were facing financial challenges. Meanwhile, 30% of customers indicated that they were not aware that Local Authorities were suffering from financial distress.
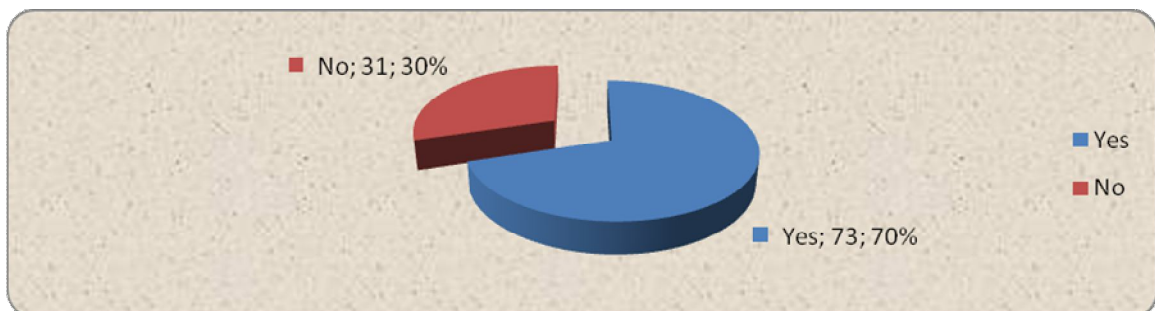
Figure 4. 26: Customers Awareness that LAs Face Financial Distress

The results from officers and customers of Local Authorities indicate that Local Authorities in Kenya suffer from financial distress. The findings are consistent with those in literature (Dollery, 2009; Price Waterhouse Coopers, 2006; Boex & Muga, 2004; Capalbo, Grossi, Ianni & Sargiacomo, 2010; Carmeli, 2008; Deal, 2007; Frank & Dluhy, 2003; Kloha, Weissert & Kleine, 2005; Watson, Handley & Hassett, 2005; Honadle, 2006; Wunsch, 2008; IEA, 2009; Schoeman, 2011; Jonga & Chirisa, 2009 and Sennoga, 2004), which found out that Local Authorities of the countries under study suffered from financial distress.

4.5.9: Poor Service Delivery as a Cause of Financial Distress

The study sought to find out whether customers were satisfied with the services of the Local Authorities. Results in figure 4.27 indicated that an overwhelming majority (83%) of customers were dissatisfied with the service of the Local Authorities. Meanwhile, (17%) were satisfied with the services of the Local Authorities This finding is consistent with those of IEA (2009) which argues that Local Authorities are mandated to enable administrative convenience and expediency as advocated by Stigler's menu theorem and therefore exist to offer services at a decentralized level. However, IEA (2009) argues that majority of Local Authorities have failed in their service delivery mandate which has led to widespread complaints by citizens of poor service delivery.

Legend: Yes; 18; 17%; No; 89; 83%
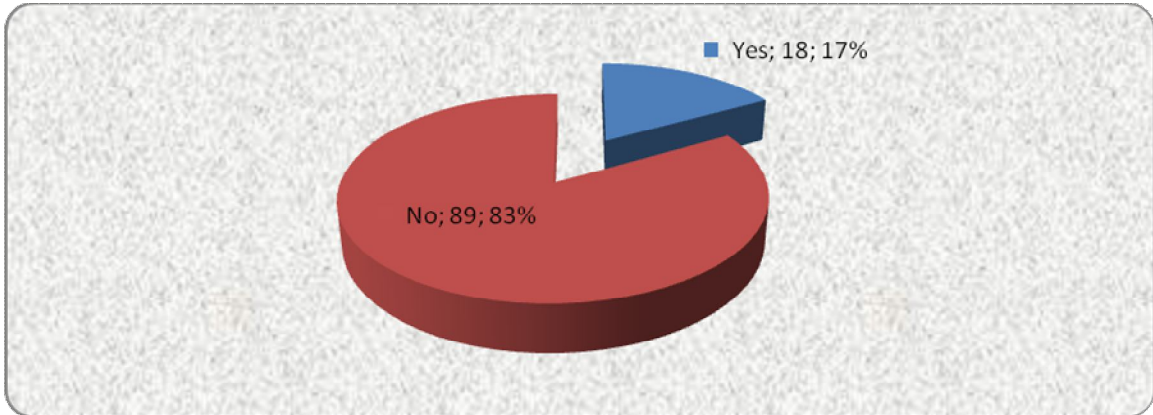
Figure 4. 27: Customers Satisfaction with Service Delivery

Customers were asked whether poor service delivery contributed to the financial distress of Local Authorities. Results in figure 4.28 indicate that a majority (55%) of customers strongly agreed with the statement that poor service delivery to clients contributed to the financial challenges facing Local Authorities. The results also indicated that 28% of customers agreed with the statement that poor service delivery to customers contributed to the financial challenges Local Authorities bring to a total of (83%) the customers who agreed or strongly agreed with the statement. Meanwhile, 4% neither agreed nor disagreed while a further minority (13%) generally disagreed.
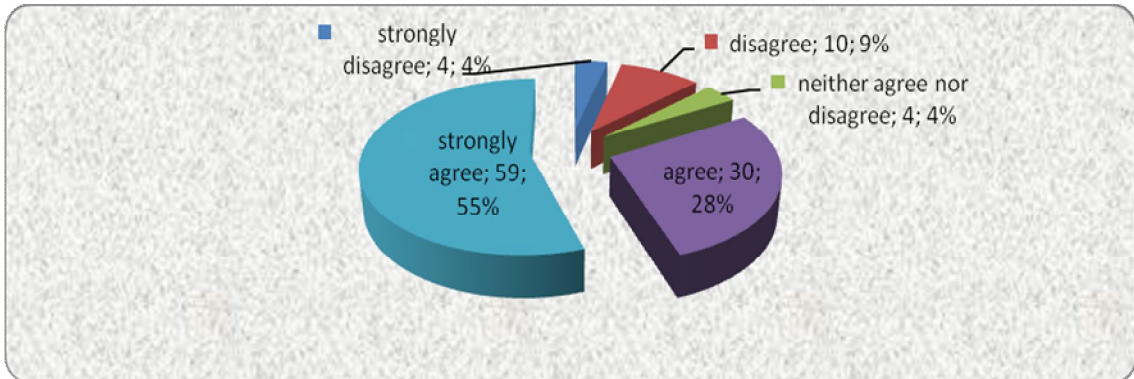
Figure 4. 28: Poor Service Delivery to Customers Causes Financial Distress

Customers were asked whether the level of satisfaction with service delivery influenced their willingness to pay bills, rents and rents to the Local Authority. Results in figure 4.29 indicated that a majority 62% of the customers stated that level of satisfaction with service delivery influenced their willingness to pay bills, rents and rents to the Local Authority. Meanwhile, 38% indicated that level of satisfaction with service delivery did not influence their willingness to pay bills, rents and rents to the Local Authority.

The findings are in agreement with those by Omamo (1995) and IEA (2009) which assert that poor service delivery has its consequences which include a growing dissatisfaction of the community to the point that they form Local associations to voice their concerns. The authors quoted a good example as the Karengata Resident Association. On the extreme side, the authors argued that residents may withhold the rates owed to the Local Authorities as a measure to enforce compliance with service delivery.
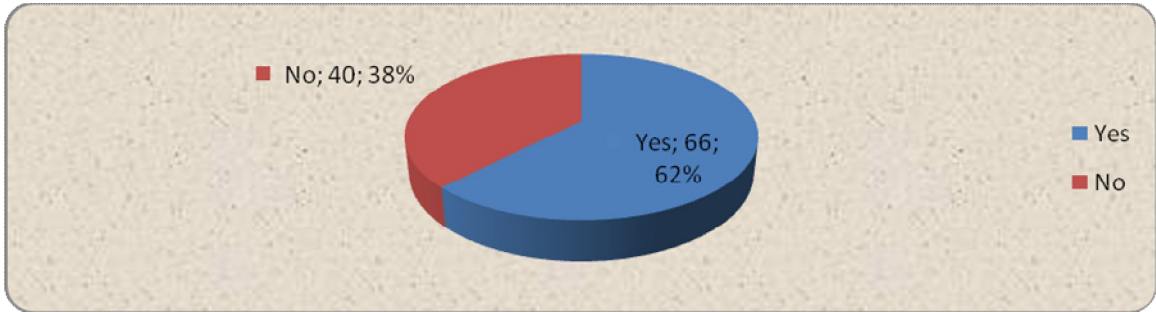
Figure 4. 29: Service Delivery Influence on Willingness to Pay LA Dues

On the question of whether customers contribute to financial distress of Local Authorities, results in figure 4.30 revealed that a majority (50.5%) of the customers agreed that customers contributed to the financial distress of Local Authorities. Meanwhile, a further 49.5% indicated that customers do not contribute to financial distress of Local Authorities.
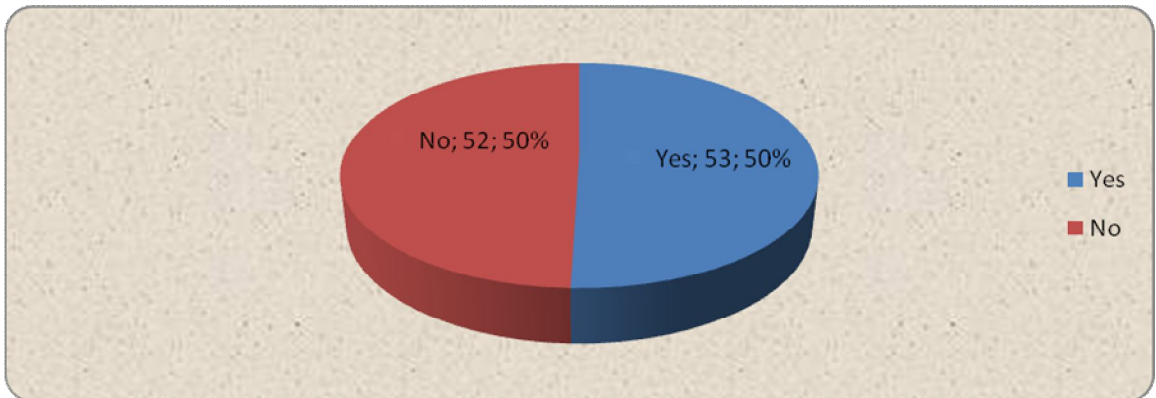
Figure 4. 30: Customers' Contribution to the Financial Distress in Las

The current study sought to investigate the ways in which customers contribute to financial distress. Results in Table 4.40 indicate that 32% of customers agreed that they contribute to financial distress by failing to pay land rates, fees, rent and parking fees. A further 26% of the customer strongly agreed that they contribute to financial distress by failing to pay land rates, fees, rent and parking fees bringing to a total of (58%) of customers who either agreed or strongly agreed with the statement. Meanwhile, 3% neither agreed nor disagreed while a further minority (39%) generally disagreed with the statement.

The findings agree with other results by Miring'uh and Mwakio (2006) and KACC (2007) which revealed that customers contributed to the financial distress of Local Authorities because of their behavior. The two studies identified failure by customers to pay rates as a common contributor to Local Authority financial distress

Results in Table 4.40 indicate that twenty-Five percent, (25%) of customers agreed with the statement that they contributed to financial distress through colluding with Local Authority officers to defraud the Local Authority of its revenue. A further 19% of the customer strongly agreed that they contribute to financial distress through colluding with Local Authority officers to defraud the Local Authority of its revenue bringing to a total of 44% of customers who either agreed or strongly agreed with the statement.

Meanwhile, 15% neither agreed nor disagreed while a further 41% generally disagreed with the statement.

The findings agree with other results by Miring'uh and Mwakio (2006) and KACC (2007) which revealed that customers contributed to the fiscal distress of Local Authorities because of their behavior. The two studies identified collusion between customers as a common contributor to Local Authority fiscal distress.

As revealed by Table 4.40, Thirty-seven percent (37%) of customers agreed with the statement that they contributed to financial distress by failing to properly use the resources of the council. A further 23% of the customer strongly agreed that they contribute to financial distress by failing to properly use the resources of the council bringing to a total of (60%) of customers who either agreed or strongly agreed with the statement. Meanwhile, 4% neither agreed nor disagreed while a further minority (36%) generally disagreed with the statement.

The findings agree with other results by Miring'uh and Mwakio (2006) and KACC (2007) which revealed that customers contributed to the financial distress of Local Authorities because of their behavior. The two studies identified irresponsibility by customers in using the facilities as a common contributor to Local Authority fiscal

distress. For instance, customers littered the streets and failed to keep the city clean through the use of dustbins.

Results in Table 4.40 reveal that approximately half (46%) of the customers agreed that they contributed to financial distress through vandalism of the property of the Local Authority property. The other half (47%) disagreed with the statement. Meanwhile, 7% were neutral with the statement.

The findings corroborate with other results by Miring'uh and Mwakio (2006) and KACC (2007) which revealed that customers contributed to the financial distress of Local Authorities because of their behavior. The two studies identified collusion between customers as a common contributor to Local Authority fiscal distress.

The study results imply that customers of Local Authorities contribute to the financial distress of Local Authorities through their action of omission or commission. The findings further imply that both internal causes and external causes of financial distress exist. Therefore, a policy to address financial distress should not only focus on the internal management but should also focus to change the culture and attitudes of customers towards supporting the Local Authorities.

Table 4. 40: Factors Contributing to Local Authorities Financial Distress

Statement	strongly disagree	disagree	neither agree nor disagree	agree	strongly agree
Failure to pay land rates, fees, rent and parking fees	29, 28%	11, 11%	3, 3%	33,32%	27, 26%
Colluding with local authority officers to defraud the local authority of its revenue	25, 24%	18, 17%	16, 15%	26, 25%	20, 19%
Failure to use the resources of the city properly	23, 22%	16, 15%	4, 4%	39, 37%	24, 23%
Vandalism of the local authority property	27, 27%	20, 20%	7, 7%	26, 26%	20,20%

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECCOMMENDATIONS

5.0: Introduction

This chapter presents the summary of major findings of the study, relevant discussions, conclusions and the necessary recommendations. The study sought to determine the role of financial management practices, corporate governance practices, human resource management practices, management information system, and government regulation to financial distress witnessed in the Kenyan Local Authorities.

The summary is done in line with the objectives of the study and based on the output of the descriptive and inferential statistical analyses guided to test the research hypothesis of the study. Each recommendation traces directly to each conclusion in line with practice and policy.

5.1: Summary of the Findings

5.1.1: Financial Management Practices and their Contribution to Financial Distress Facing Local Authorities in Kenya

One of the objectives of the study was to investigate whether financial management practices leads to financial distress facing Local Authorities in Kenya. Various methods were used to arrive at the findings. These methods included descriptive statistics,

parametric analysis and regression analysis. The findings indicated that Local Authorities had ineffective financial management practices.

This observation was arrived at since the Local Authorities did not have effective systems to detect and prevent fraud. In addition, Local Authorities had poor internal controls, poor budgeting practices, poor procurement practices and poor financial reporting practices, which are signs of ineffective financial management practices that contribute to the financial distress of Local Authorities in Kenya. These findings led to rejection of null hypothesis that financial management practices did not significantly contribute to financial distress facing local authorities in service delivery in Kenya.

5.1.2: **Corporate Governance Practices and their Contribution to Financial Distress of Local Authorities in Kenya**

In order to determine the extent to which corporate governance practices contribute to financial distress of Local Authorities in Kenya, descriptive statistics, regression analysis and analysis of variance (parametric analysis) were conducted. Results indicated that Local Authorities had poor governance practices.

Specifically, Local Authorities did not ensure transparency through the display of performance results to all stakeholders. In addition, the Local Authorities do not have a good leadership structure which supports corporate governance. It was also observed

from the results that the number of corruption cases had not reduced in Local Authorities. The findings implied that the corporate governance practices of Local Authorities are ineffective and this contributed to the financial distress of Local Authorities in Kenya. These findings led to rejection of null hypothesis that corporate governance practices did not significantly contribute to financial distress facing local authorities in service delivery in Kenya.

5.1.3: Information Technology and their Contribution to Financial Distress of Local Authorities in Kenya

The study investigated whether management information system contributes to financial distress in Local Authorities. To meet this objective, descriptive statistics, regression analysis and ANOVA was conducted. Results indicated that information technology was inadequate in Local Authorities. Specifically, results indicated that the management information system used does not provide relevant information for the right people at different levels of the Local Authorities and that the information from Local Authority integrated financial and operating management system (LAIFOMS) was not reliable.

In addition, the management information system was not enhancing the growth of Local Authorities. This was because LAIFOMS, the management information system used by Local Authorities, cannot easily incorporate new products or expand to accommodate new reporting needs. It was also observed that the management information system is

not user friendly to staff , that is, easy to understand and operate .The management information system also does not interact with any applied delivery technologies, such as hand-held computers, point-of-service (POS) terminals, and automated teller machines.

The results further indicated that information technology was a significant determinant of financial distress in Local Authorities. The inadequacy of information technology contributed to loss of finances to corrupt officers and inability to collect fully finances thus contributing to financial distress in Local Authorities. These findings lead to rejection of null hypothesis that information technology did not significantly contribute to financial distress facing local authorities in service delivery in Kenya.

5.1.4: Human Resource Management Practices and their Contribution to Distress of Local Authorities in Kenya

The study attempted to investigate whether human resources management practices contributes to financial distress in Local Authorities. The type of analysis used includes descriptive statistics, regression analysis and parametric analysis. Results indicated that Local Authorities have poor human resource management practices. Specifically, Local Authorities do not conduct comprehensive interviews before hiring nor consider experience and qualifications during hiring and promotions and Local Authority performance appraisals are not supported by rewards.

The finding implies that human resources management practices in Local Authorities are ineffective especially in the area of hiring and recruitment and promotions, and rewarding of performance. Results further indicated that poor human resource management practices contributed to the low morale of staff, unqualified personnel thus contributing to financial distress in Local Authorities. These findings lead to rejection of null hypothesis that human resources management practices did not significantly contribute to financial distress facing local authorities in service delivery in Kenya.

5.1.5 Government Regulation and its Contribution to Financial Distress of Local Authorities in Kenya

In order to determine the extent to which government regulation contribute to financial distress of Local Authorities in Kenya, descriptive statistics, regression analysis and ANOVA were conducted. Results indicated that the government regulation on Local Authority was unfair and ineffective. Results further indicated that the inadequacy or biased government regulation contributed to financial distress in Local Authorities.

Specifically, The Transfer of Functions Act (1969) and The Graduated Personal Tax Act (1974) greatly eroded the revenue base of the Local Authorities. Furthermore, The Constituency Development Act Fund Act (2003) has diverted the development agenda from Local Authorities to constituencies resulting in the weakening of the financial base of Local Authorities thus leading to financial distress. These findings lead to rejection of

null hypothesis that government regulation did not significantly contribute to financial distress facing local authorities in service delivery in Kenya.

5.1.6: Financial Distress in Local Authorities

The study investigated the state of financial distress in Local Authorities and concluded that Local Authorities were highly distressed since majority of the Local Authorities' scored highly on the indicators of financial distress. Specifically, the study found out that the Local Authorities always spend more than budgeted and salaries took more than 70% of the operating revenue.

Moreover, the Local Authorities were highly indebted and relied heavily on over drafts. It was also observed that the financial statements of Local authorizes are rarely given a good bill of health by auditors. Auditors also questioned a large percentage of the expenditures, an indication that the Local Authorities were under financial distress.

5.2: Conclusion

5.2.1: Contribution of Financial Management Practices to Financial Distress

The study concludes that the financial management practices of Local Authorities are poor and ineffective. The poor financial management practices may have led to the resultant financial distress being witnessed in many Local Authorities. Highly distressed local authorities have poor ratings on financial management practices compared to

moderately and lowly distressed local authorities. It can be concluded from this study that there exists a negative significant relationship between financial management practices and the financial distress of Local Authorities.

5.2.2: Contribution of Corporate Governance Practices to Financial Distress

The study concludes that corporate governance practices of Local Authorities are ineffective. Poor corporate governance practices may have contributed to financial distress of Local Authorities. Highly distressed local authorities have poor ratings on corporate governance practices compared to moderately and lowly distressed local authorities. The study concludes that the relationship between corporate governance practices and financial distress is negative and significant.

5.2.3: Contribution of Information Technology to Financial Distress

The study concludes that local Authorities rated the effectiveness of information technology highly however, level of adoption of information technology was rated as inadequate. This indicated that they were optimistic about the information technology and how it can impact on the operations of the Local Authorities but also noted that it is a case of "too little too late" since the adoption of information technology was inadequate. The management information system (MIS) also known as LAIFOMIS has only been introduced in very few Local Authorities and are therefore inadequate. For large councils it is inadequate because it does not give room for expansion and lacks some critical

modules. Majority of the Local Authorities have just been trained on how to use the MIS software and it has not been fully rolled out in majority of the Local Authorities.

Meanwhile, it is also possible to infer that the relationship between Information technology and financial distress is negative and significant. The study shows that there exists a significant difference in the adequacy of Information Technology between the three categories of financially distressed Local Authorities. Information technology inadequacy contributes to financial distress in Local Authorities.

5.2.4: Contribution of Human Resource Management Practices to Financial Distress

The study concludes that the human resource management practices especially in the area of hiring and recruitment, promotions, and rewarding of performance were ineffective. Customers of Local Authorities have a negative view about the quality of human resources employed by local authorities. Highly distressed Local Authorities have a significantly lower mean score on human resource management practices compared to moderately and lowly distressed Local Authorities. The ineffective Human resource management practices contribute to financial distress of local authorities. There is a negative and significant relationship between human resource management practices and financial distress.

5.2.5:   Contribution of Government Regulation to Financial Distress

The study concludes that government regulation for Local authorities is ineffective, unfair and biased. Several government regulations for instance the Transfer of Functions Act (1969), Graduated Personal Tax in 1974 and Constituency Development Act Fund Act (2003) have greatly eroded the revenue base of the Local Authorities. Poor regulation contributed to the financial distress facing Local Authorities. The relationship between government regulation and financial distress is positive and significant which implies that an increase in the ineffectiveness of government regulation leads to an increase in financial distress.

5.2.6:   Financial Distress in Local Authorities

It was possible to conclude from the study findings that local Authorities in Kenya face financial distress. They also spend more than what is stipulated in the budget. Local Authorities have a salary expense that takes more than 70% portion of the operating revenue and are highly indebted. Local Authorities are over reliant on overdrafts and rarely pay their suppliers and creditors (their accounts are always qualified). LAs pay salaries of their employees with difficult. The huge expenditures and debts of Local Authorities that are not paid demonstrate financial distress.

5.3: Recommendations of the Study

The study recommendations are in line with the objectives, findings and conclusions of the study. Both the recommendations from the officers and from the customers were taken into account in formulation of the specific recommendations that would inform decision making.

5.3.1: Improvement of Financial Management Practices

Local Authority officers recommended that various measures need to be put in place in order to improve financial management practices. Some of the recommendations included;

5.3.1.1: Decentralization and Devolution

It was recommended that service delivery to be further decentralized. This would mean that the decentralized structure would be responsible for putting in place effective financial management practices such as stringent controls and adherence to budgets.

5.3.1.2: Address Capacity and Independence of Audit and Financial Department Through Training

The local authorities should put in place measures to safeguard the independence and effectiveness of internal audit departments as this department is crucial in the implementation of internal controls. The finance and revenue collection departments

should also uphold tenets of professionalism, integrity, regularly trained and join professional bodies.

5.3.1.3: Automation of Financial Process and full Implementation of LAIFOMS

Automation of financial processes also called e-payment and the implementation of LAIFOMS would help to improve financial management practices. For instance, there should be an option to pay for the renewal of licenses and other council fees through MPESA and other modern/convenient money transfer methods.

5.3.1.4: Revenue Collection Methods Should be Improved

Old and new debts should be collected aggressively to safeguard against the opportunity cost of holding high levels of account receivables. This can be done by involving professionals in debt collection.

5.3.1.5: Maximization of utilization of resources like Land

Many LAs own very prime land within their areas of jurisdictions which is not put into full capacity utilization. The study recommends that this prime property be leased out or investment is done on it by LAs since recouping capital invested will take a short period, and there after act as a reliable source of revenue.

5.3.1.6: Address the problem of bloated workforce

The wage bill in most LAs takes more than seventy percent of the total budget, and it's recommended that a comprehensive job rationalization needs to be taken and report thereof implemented to ensure optimality of the workforce.

5.3.2: Improvement of Corporate Governance Practices

The officers suggested recommendations for improvements of corporate governance practices such as:-

5.3.2.1: Elimination of corruption

The culture of kickbacks and corruption should be eliminated through a cultural and mind set change. This should be done from the local authority's staff and from customer's side while involving KACC through Integrity Testing Programs

5.3.2.2: Review of Local Government Act Cap. 265, to Reduce the Powers of the Civic Leaders on policy implementation

There should be clearly defined boundaries between political and administrative wings and minimize interference by politicians in the implementation of policies and the recruitment of bureaucrats to ensure efficiency and effectiveness.

5.3.2.3: Civic Participation in all Activities

Letting the communities set their own agenda for development, because they are the ones that knows what problem they are encountering may be a welcome move towards enhancing community governance. In addition, Stakeholders should monitor the corporate governance practices in Local Authorities.

5.3.3: Improvement of Information Technology

Recommendations for improvements of information technology included;

5.3.3.1: Implementation of LAIFOMS

The study also recommends that all Local Authorities should prioritize the implementation of LAIFOMS. In addition, those Local Authorities who have already implemented LAIFOMS should ensure that all modules are fully operationalized, for instance, integration of payroll and statutory deductions with the main accounting system. For large councils relevant software should me adopted to embrace inclusiveness of all operations.

5.3.3.2: Enhanced ICT Training

It is recommended that ICT skills for Local Authority staff should be enhanced through training.

5.3.3.3: Investment in ICT Hardware such as Computers

The Local Authorities should invest in more computers and ICT software as doing so would improve their financial fortunes. This influences the level of networking connectivity and creation of favourable environment for e-payment.

5.3.4: Improvement of Human Resource Management Practices

Suggested recommendations for improvement of human resource management practices included;

5.3.4.1: Improvement in Hiring Practices by Ensuring that Hiring Practices are not Politically Motivated

Hiring should be done in line with qualifications. To improve hiring practices, the independence of the human resource department need to be supported by the executive and political wing. Consequently professional bodies should be used in recruitment.

5.3.4.2: Frequent Performance Appraisals Supported by Awards

Performance appraisals that are supported by rewards and sanctions should be introduced so as to improve the staff morale and attitude towards work.

5.3.4.3: Training and Capacity Enhancements

The implementation of the job rationalization report by Price water house coopers was also recommended as a way to improve the human resource management in Local Authorities. A comprehensive skill audit need also be done so as to identify training gaps.

5.3.5: Improvement of Government Regulation

Recommendations included:

The sources of revenue that were taken away from the Local Authorities should be reverted back to them or the government to increase funding to LA's. Officers also suggested that some of the Acts that divert funds to other ministries/departments should be reviewed. It was also recommended that a portion of corporation tax that is paid to the government should be devolved to LA's.

The Local Authorities also need to be given more powers to increase their sources of revenue. It was also recommended that perhaps the law should be amended to enable the setting up of an anticorruption committee at the Local Authority level. In addition, it was suggested that cap 265 should be amended so as to divorce politics from running of LA's. Most importantly, it was recommended that the government should liaise with the Local Authorities and conduct comprehensive consultation on how a certain law would affect them before passing it in parliament. Further regulations and amendments to the existing

laws should be critically examined to avoid watering the revenue base of the newly formed county governments.

5.3.6: Overall Recommendations

Overall, it is recommended that financial management practices, Corporate Governance practices, Information technology, Human Resource Management practices and Government Regulation should be improved as doing so would reduce financial distress in Local Authorities in Kenya

5.4: Suggested Areas for Further Research

There are several conceptual areas that may need to be researched further. For instance, is financial distress severe in rural or urban LAs? There needs to be awareness on what specific clauses of the cap 265 need to be amended to revive the financial fortunes of LAs. In addition, it would add value to investigate and compare how sister Local Authorities in America, Britain or Italy are addressing the problem of financial distresses.

What specific action plans can be adapted from financially healthy Local Authorities in developed countries? It is also very important to know which of the causes of financial distress need to be prioritized for action. Due to scarcity of resources and the infinite nature of needs to be satisfied, it would be important to find out which causes of financial distress need to be addressed first.

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APPENDICES

APPENDIX I QUESTIONNAIRE FOR LOCAL AUTHORITY OFFICERS

This questionnaire is concerned with assessing the determinants of financial Distress facing Local Authorities in service delivery in Kenya.

Section A: Demographic Information

i)   LOCAL AUTHORITY INFORMATION

1. Name of the L.A (Optional) …………………………….

2. Category type (please tick as appropriate)
   a) City Councils
   b) Municipal Councils
   c) County Councils
   d) Town Councils

RESPONDENTS PARTICULARS

3. Gender: Male ☐   Female ☐

4. Age Bracket
      i. 18-20
      ii. 21-30
      iii. 31-40
      iv. 41-50
      v. Over 50

5. Department
      a. Treasury
      b. Social Services, housing and public health
      c. Works/Engineering
      d. Environment
      e. Others

6. How long have you worked with this Local Authority (tick as appropriate)
    a. Less than 1 yr ☐
    b. Btw 1-5 yrs ☐
    c. Btw 5-10 yrs ☐
    d. Over 10 yrs ☐

Section B: Financial Management

This Section is concerned with assessing whether financial management practices affects financial distress faced by Local Authorities in Kenya. Please mark (x) in the box which best describes your agreement or disagreement on each of the following statements.

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. The Local Authority systems are not effective at detecting fraud					
2. The Local Authority do not have appropriate and sufficient internal controls in place					
3. Local Authority internal audit functions does exist					
4. The Local Authority does conduct monthly and yearly budget variance analysis					
5. The Local Authority does produce daily, weekly, monthly, quarterly and yearly financial reports					
6. The Local Authorities financial statements are prepared in accordance with IFRs, IAS, and other relevant Government requirements					
7. The Local Authority has not constituted an independent procurement committee in accordance with government requirements					

8. How would you rate the financial management practices in the Local Authority?

a) Good ☐ b) Poor ☐

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In consideration of the rating above, please Explain why;

_____

9. What measures would you recommend for the improvement financial management practices in the Local Authority?

...

SECTION C: Human Resource Management Practices
This Section is concerned with assessing whether human resource management practices affect financial distress faced by Local Authorities in Kenya. Please mark (x) in the box which best describes your agreement or disagreement on each of the following statements.

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. The Local Authority has invested in training and development of its work force (computer literacy/ customer care training)					
2. The Local Authority has sponsored its staff for diploma and university courses					
3. The Local Authority does not conducts comprehensive interviews before hiring					
4. The Local Authority does not takes into consideration both work experience and academic qualification before hiring and promoting.					
5. The Local Authority does conduct performance appraisals at least twice in a year					
6. The performance appraisals are not supported by rewards					

7. How would you rate the human resource management practices in the Local Authority?

a) Good ☐ b) Poor. ☐

In consideration of the rating above, please explain why;

_____

_____

8 What measures would you recommend for the improvement of human resource management practices in the Local Authority?

………………………………………………………………………………

SECTION D: Corporate Governance

This Section is concerned with assessing whether Corporate Governance affect financial distress faced by Local Authorities in Kenya. Please mark (x) in the box which best describes your agreement or disagreement on each of the following statements.

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. The Local Authority is not transparent and accountable. It does not ensure transparency by displaying performance results for all stakeholders					
2. The Local Authority is transparent and accountable. It does ensure transparency by allowing its books of accounts to be audited					
3. The Local Authority is accountable. It does ensure accountability by signing the performance contract and adherence to service delivery charter					
4. The Local Authority does not have a good leadership and managements structure which					

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
support corporate governance					
5. The number of corruption cases have not reduced in Local Authorities					
6. The Local Authority does encourages frequent community participation in decision making and setting agenda for development					

a) Good ☐ b) Poor. ☐

In consideration of the rating above, please explain why;

7. How would you rate the corporate governance practices in the Local Authority?

8. What measures would you recommend for the improvement of corporate governance practices in the Local Authority?

……………………………………………………………………………………

SECTION E: Government Regulation

This Section is concerned with assessing whether Government Regulation affect financial distress faced by Local Authorities in Kenya. Please mark (x) in the box which best describes your agreement or disagreement on each of the following statements.

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. The Transfer of Functions Act (1969) has greatly eroded the revenue base of the Local Authority					

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
2. The Graduated Personal Tax in 1974 has greatly eroded the revenue base for Local Authorities					
3. The Constituency Development Act Fund Act (2003) has diverted the development agenda from Local Authorities to constituencies					

4. How would you rate the adequacy of government regulation in the Local Authority?

a) Adequate ☐ b) Inadequate ☐

In consideration of the rating above, please explain why;

_____

4. What measures would you recommend for the improvement of government regulation in the Local Authority?

………………………………………………………………………………

SECTION F: Information Technology

This Section is concerned with assessing whether Information Technology affect financial distress faced by Local Authorities in Kenya. Please mark (x) in the box which best describes your agreement or disagreement on each of the following statements.

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. The MIS/LAIFOMS does provide relevant information for the right people at different levels of the LA					

2. The information from LAIFOMS is reliable					
3. The MIS/ LAIFOMS is enhancing the Growth of Local Authorities					
4. MIS/ LAIFOMS can easily incorporate new products or expand to accommodate new reporting needs					
5. The MIS/ LAIFOMS is user friendly to staff i.e is easy to understand and operate					
6. MIS/ LAIFOMS does interacts with any applied delivery technologies, such as handheld computers, point-of-service (POS) terminals, and automated teller machines(ATMs					

7. How would you rate the adequacy of Information Technology in the Local Authority?

a) Adequate ☐ b) Inadequate ☐

In consideration of the rating above, please explain why;

8. What measures would you recommend to improve the adequacy and use of Information technology in the Local Authority?

………………………………………………………………………………………

SECTION G: Financial Distress

This Section is concerned with assessing the level of financial distress faced by Local Authorities in Kenya. Please mark (x) in the box which best describes your agreement or disagreement on each of the following statements.

Statement	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. The Local Authority budget out run ratio is high (meaning The Local Authority always spends more than it has budgeted).					
2. The salary to total operating revenue ratio is high (meaning The salary expense take more than 70% portion of the operating revenue)					
3. The net debt to total operating revenue ratio is high (meaning The LA is highly indebted)					
4. The Interest expense to total operating revenue ratio is high (meaning The LA may be over reliant on overdrafts)					
5. The council financial statements are frequently qualified (meaning they are frequently not given a good bill of health)					
6. The National audit office queries a large percentage of expenditures during the audit process (meaning there seems to be expenditures that demonstrate fiscal stress)					

1. To what would you attribute financial distress in the Council?
    i._____
    ii._____
    iii._____

2. How do you think the challenges of financial distress can be addressed?
    i.   _____
    ii.   _____
    iii. _____

APPENDIX II   QUESTIONNAIRE FOR CUSTOMERS

This questionnaire is designed with the purpose of generating collaborative evidence in relation to the responses obtained from Local Authority officers.

1. Are you aware that Local Authorities face financial distress?

    a) Yes

    b) No

2. What do you attribute the financial distress to? Please tick appropriately.

Financial distress are caused by;	Strongly disagree	Dis agre e	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. Poor financial management practices such as lack of internal controls, budgeting and reporting					
2. Poor human resource management practices such as hiring incompetent staff, failure to train staff , failure to compensate and motivate staff					
3. Poor governance practices such as lack of accountability, transparency, corruption, failure to adhere to service delivery charter					
4. Poor government regulation					
5. Lack of automation in record keeping					
6. Poor services that they offer to customers					

3. Are residents satisfied with the services that the Local Authority is offering to the residents?

    a) Yes

    b) No

    Explain your answer..

4. If residents are not satisfied with the services, did that influence their willingness to pay bills, rents and rates to the Local Authority?

    a) Yes

    b) No

5. Do customers contribute to the financial distress of Local Authorities?

    a) Yes

    b) No

6. To what extent do you agree that customers contribute to Local Authorities financial distress in the following way;

Customers contribute to Local Authority financial distress through;	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
1. Failure to pay land rates, fees, rent and parking fees					

Customers contribute to Local Authority financial distress through;	Strongly disagree	Disagree	Neither agree not disagree	Agree	Strongly agree
	1	2	3	4	5
2. Colluding with Local Authority officers to defraud the Local Authority of its licensing revenue , parking revenue, land rate revenue among others					
3. Failure to use the resources of the city properly, for instance littering and releasing waste on the highway					
4. Vandalism of the Local Authority property such as seats, cabling and street lights					

5. What reasons make residents to collude with Local Authority officials and refuse to meet their obligations towards the Local Authorities?..

6. What would it take to motivate residents to stop colluding and also motivate them to meet their obligations to Local Authorities?...................................

7. What are your suggestions towards how the financial distress of Local Authorities can be addressed?...

APPENDIX III OPERATIONALIZATION OF THE VARIABLES

Variable	Definition	Operationalization/Measurement
Financial Distress	A state when a company traverses all the stages of decline through deterioration of performance, failure, insolvency, and default.	1. Budget Outrun ratio 2. Salary to total operating revenue 3. Net debt to total operating revenue 4. Interest expense to total operating revenue 5. Qualification of financial statements by auditors 6. Queries on a large percentage of expenditure
Financial management practices	The planning, directing, monitoring, organizing, and controlling of the monetary resources of an organization	1. Internal controls 2. Audited accounts 3. Financial reports
Corporate governance practices	the system by which companies are directed and controlled	1. Accountability 2. Transparency 3. Corruption/ client characteristics
Information Technology	all computing and communication technologies that facilitates collection, storage and retrieval of information	1. Reliability and relevance of information 2. User friendliness 3. Potential for growth 4. Hardware- Interaction with POS,ATMS ,PDAs
Human Resource management practices	It's a set of tools to help you organize, plan, and implement activities in organizations	1. Employee selection 2. Training & development. 3. Performance appraisal and compensation
Government Regulations	Administrative legislation that constitutes or constrains rights and allocates responsibilities.	1. 1969-Transfer of functions act 2. 1974- Abolition of G.P. tax 3. 2003 CDF act.

APPENDIX IV LIST OF LOCAL AUTHORITIES (POPULATION)

Column1	Type	Local Authority Name	Surplus (Deficit)
1	City Council	Mombasa	(2,208,951.00)
2	City Council	Kisumu	24,465,801.00
3	City Council	Nairobi	(8,427,310.00)
1	County Council	Migori	4,133,697.00
2	County Council	Baringo	(202,909.00)
3	County Council	Bomet	4,721,638.00
4	County Council	Bondo	(3,698,329.00)
5	County Council	Bungoma	14,896,815.00
6	County Council	Burere-Mumias	5,216,686.00
7	County Council	Bureti	11,405,634.00
8	County Council	Busia	(565,223.00)
9	County Council	Embu	(34,343,420.00)
10	County Council	Garissa	8,669,800.00
11	County Council	Gucha	(3,874,252.00)
12	County Council	Gusii	(2,366,780.00)
13	County Council	HomaBay	(1,764,509.00)
14	County Council	Ijara	4,285,517.00
15	County Council	Isiolo	(17,540,986.00)
16	County Council	kakamega	15,637,087.00
17	County Council	Keiyo	(5,561,872.00)
18	County Council	Kiambu	17,869,820.00
19	County Council	Kilifi	34,861,472.00
20	County Council	kipsigis	1,034,099.00
21	County Council	kirinyaga	(19,748,891.00)
22	County Council	Kisumu	4,079,177.00
23	County Council	Kitui	19,653,960.00
24	County Council	koibatek	(55,990,764.00)
25	County Council	Kwale	15,687,263.00
26	County Council	Laikipia	6,659,656.00
27	County Council	Lamu	(1,991,696.00)
28	County Council	Liugari	2,944,288.00
29	County Council	Makueni	(37,642,721.00)
30	County Council	Malindi	71,111,103.00
31	County Council	Mandera	3,540,830.00
32	County Council	Maragwa	10,262,806.00

Column1	Type	Local Authority Name	Surplus (Deficit)
33	County Council	Marakwet	5,860,879.00
34	County Council	Marsabit	18,454,637.00
35	County Council	Masaku	64,744,660.00
36	County Council	Mberee	2,070,953.00
37	County Council	Meru	56,957,706.00
38	County Council	Meru south	6,471,317.00
39	County Council	Mount Elgon	(9,442,455.00)
40	County Council	Moyale	8,712,966.00
41	County Council	Murang'a	728,944.00
42	County Council	Mwingi	(19,178,811.00)
43	County Council	Nandi	8,679,785.00
44	County Council	Narok	36,842,944.00
45	County Council	Nyambene	(14,959,253.00)
46	County Council	Nyamira	8,659,244.00
47	County Council	Nyandarua	27,158,442.00
48	County Council	Nyando	3,744,730.00
49	County Council	Nyeri	(7,285,460.00)
50	County Council	Nzoia	(88,140,984.00)
51	County Council	Olkejuado	13,419,773.00
52	County Council	Pokot	5,947,113.00
53	County Council	Rachuonyo	2,423,403.00
54	County Council	Samburu	(4,093,064.00)
55	County Council	Siaya	(245,395.00)
56	County Council	Suba	2,178,282.00
57	County Council	Taita Taveta	15,734,343.00
58	County Council	Tana River	34,582,195.00
59	County Council	Teso	4,921,248.00
60	County Council	Tharaka	9,354,077.00
61	County Council	Thika	47,444,022.00
62	County Council	Trans Mara	(17,952,044.00)
63	County Council	Turkana	5,629,074.00
64	County Council	Vihiga	3,286,162.00
65	County Council	Wajir	46,754,775.00
66	County Council	Wareng	(7,951,550.00)
1	Municipal Council	Limuru	2,864,409.00
2	Municipal Council	Nyahururu	19,923,983.00
3	Municipal Council	Bomet	2,580,250.00

Column1	Type	Local Authority Name	Surplus (Deficit)
4	Municipal Council	Bungoma	8,346,831.00
5	Municipal Council	Busia	14,821,345.00
6	Municipal Council	Chuka	977,777.00
7	Municipal Council	Eldoret	89,208,743.00
8	Municipal Council	Embu	12,254,106.00
9	Municipal Council	Garissa	6,722,646.00
10	Municipal Council	HomaBay	(12,068,151.00)
11	Municipal Council	kabarnet	(2,143,671.00)
12	Municipal Council	kakamega	9,316,922.00
13	Municipal Council	kapenguria	(157,411.00)
14	Municipal Council	kapsabet	(6,917,250.00)
15	Municipal Council	karatini	8,961,221.00
16	Municipal Council	Kehancha	9,129,138.00
17	Municipal Council	Kericho	42,848,456.00
18	Municipal Council	Kerugoya kutus	(6,335,435.00)
19	Municipal Council	Kiambu	9,707,726.00
20	Municipal Council	kimilili	684,847.00
21	Municipal Council	kisii	3,421,300.00
22	Municipal Council	Kitale	49,866,121.00
23	Municipal Council	Kitui	3,119,164.00
24	Municipal Council	Lodwar	3,057,128.00
25	Municipal Council	Machakos	(4,149,457.00)
26	Municipal Council	Malindi	14,514,849.00
27	Municipal Council	Maua	(2,290,957.00)
28	Municipal Council	Mavoko	(1,985,817.00)
29	Municipal Council	Meru	18,553,499.00
30	Municipal Council	Migori	6,114,709.00
31	Municipal Council	Mumias	3,110,823.00
32	Municipal Council	Murang'a	(2,846,748.00)
33	Municipal Council	Naivasha	844,476.00
34	Municipal Council	Nakuru	21,114,934.00
35	Municipal Council	Nanyuki	(771,114.00)
36	Municipal Council	Nyeri	(12,629,042.00)
37	Municipal Council	Ruiru	26,362,035.00
38	Municipal Council	Runyenjes	(798,743.00)
39	Municipal Council	Siaya	2,130,208.00
40	Municipal Council	Thika	91,945,301.00

Column1	Type	Local Authority Name	Surplus (Deficit)
41	Municipal Council	Vihiga	(4,039,965.00)
42	Municipal Council	Voi	8,656,862.00
43	Municipal Council	Webuye	(9,327,048.00)
1	Town Council	Iten-tambach	(2,330,423.00)
2	Town Council	Molo	10,075,013.00
3	Town Council	Ahero	2,622,837.00
4	Town Council	Awendo	3,922,862.00
5	Town Council	Bondo	1,562,378.00
6	Town Council	Burnt forest	5,994,997.00
7	Town Council	chepareria	(530,868.00)
8	Town Council	Chogoria	5,417.50
9	Town Council	Eldama Ravine	(2,407,779.00)
10	Town Council	Funyala	147,771.00
11	Town Council	Kajiado	1,071,287.00
12	Town Council	kandara	876,359.00
13	Town Council	kangema	1,196.71
14	Town Council	kangundo	677,713.00
15	Town Council	karuri	5,938,892.00
16	Town Council	KenduBay	(727,766.00)
17	Town Council	Keroka	(2,570,442.00)
18	Town Council	Kikuyu	(20,881,492.00)
19	Town Council	Kilifi	16,593,328.00
20	Town Council	Kipkelion	(617,550.00)
21	Town Council	Kwale	6,809,813.00
22	Town Council	litein	567,462.00
23	Town Council	Londiani	(10,419,545.00)
24	Town Council	Luanda	(3,251,070.00)
25	Town Council	Makuyu	2,769,716.00
26	Town Council	Malaba	1,717,268.00
27	Town Council	Malakisi	47,396.00
28	Town Council	Malava	7,670,416.00
29	Town Council	Mandera	7,197,401.00
30	Town Council	Maragwa	3,451,325.00
31	Town Council	Maralal	5,852,556.00
32	Town Council	Mariakani	349,196.00
33	Town Council	Masimba	(541,848.00)
34	Town Council	Matuu	230,169.00

Column1	Type	Local Authority Name	Surplus (Deficit)
35	Town Council	Mbita Point	(735,841.00)
36	Town Council	Mtito Andei	5,417,223.00
37	Town Council	Muhoroni	(714,324.00)
38	Town Council	Mwingi	5,692,181.00
39	Town Council	Nakuru	41,086,051.00
40	Town Council	Nambale	4,501,340.00
41	Town Council	Nandi -hills	4,414,861.00
42	Town Council	Narok	1,687,587.00
43	Town Council	Nyamache	2,870,504.00
44	Town Council	Nyamarambe	1,193,412.00
45	Town Council	Nyamira	2,473,622.00
46	Town Council	Nyansiongo	(837,551.00)
47	Town Council	Ogembo	(2,605,994.00)
48	Town Council	Ol' Kalou	2,947,452.00
49	Town Council	Othaya	1,458,950.00
50	Town Council	Oyugis	9,958,221.00
51	Town Council	Port Victoria	(950,475.00)
52	Town Council	Rongo	4,502,173.00
53	Town Council	Rumuruti	873,248.00
54	Town Council	Sagana	(4,043,229.00)
55	Town Council	Sirisia	(911,980.00)
56	Town Council	Sotik	2,085,461.00
57	Town Council	Suneka	33,493.00
58	Town Council	Tabaka	2,905,832.00
59	Town Council	Taveta	10,757,067.00
60	Town Council	Ugunja	36,055.00
61	Town Council	Ukwala	(2,258,304.00)
62	Town Council	Wote	(1,795,788.00)
63	Town Council	Yala	130,190.00

APPENDIX V RELIABILITY OF RESULTS

i) Reliability statistics

Section	questionnaires	questions	Cronbach alpha	Comment
Financial management practices	21	10	0.834	Reliable
Human resource management practices	21	12	0.877	Reliable
Corporate Governance Practices	21	8	0.868	Reliable
Government Regulation	21	3	0.791	Reliable
Information technology	21	8	0.824	Reliable
Financial Distress	21	6	0.827	Reliable

ii) Normality Tests of the Dependent Variable

	N Statistic	Skewness Statistic	Kurtosis Statistic
Distress	188	-.084	-.507

APPENDIX VI   LGI KEY PERFORMANCE BENCHMARKS

Analytical Balances	Definition	Denominator for comparative ratio
Net Debt	Interest- bearing financial liabilities less holding of cash and securities other than externally restricted cash and securities	Total operating revenue
Net financial liabilities	Total liabilities less financial assets net of holdings of externally restricted cash and securities	Non-financial assets plus holdings of externally restricted cash and securities
Net interest expense	Annual interest expense less interest earnings on holdings of cash and securities other than externally restricted cash and securities	Total operating revenue
Operating surplus/deficit	Operating revenue before capital amounts less operating expenses less depreciation expense less net interest expense	Own -source revenue
Net borrowing /lending	Capital expenditure less capital revenues less depreciation expense less operating surplus /deficit	Annual capital expenditure on new or enhanced assets
Annual renewals deficiency	Annual depreciation expense less annual capital expenditure on existing assets	Annual capital expenditure on renewal or rehabilitation of existing assets on new or enhanced assets
Renewals backlog	Cumulative past annual renewals deficiencies	Non- financial assets

Source: LGI (2006, page 272 Table 11.2)