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Nexus between financial reporting practices and corporate governance in Kenya: A case of the Nakuru County government

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Abstract
This study sought to explore the nexus between financial reporting practices and corporate governance at the Nakuru County Government, Kenya. This study delves into the critical role of financial controls within the realms of corporate governance and devolved governments. The study used descriptive and correlational research designs to guide the research methodology. The target population was 81 employees in the finance department of the Nakuru County Government. A census was conducted since the target population was less than 200, as required in research. Data was gathered using a questionnaire containing closed and open-ended questions. Reliability and vali

dity tests confirmed that the questionnaire was suitable to achieve the study's objective. Qualitative data collected was analysed using the study's themes, and the results were presented using narratives. The Statistical Package for Social Sciences (SPSS) computer software was employed in analysing the quantitative data that was collected using the close-ended questions. Descriptive statistics and inferential statistics, including percentages and frequencies, Pearson correlation and regression analysis, were used in this study. The findings were presented in the form of tables. The study found and concluded that there was a statistically significant relationship between financial reporting practices and corporate governance ($p<0.01$). The study recommends that a similar study be conducted in other counties in Kenya to establish the nexus between financial reporting practices and corporate governance.

Key terms: Corporate Governance, Devolved Governments, Financial Controls, Financial Reporting, Public Sector Management

INTRODUCTION

Corporate governance, a cornerstone of sound organisational management, relies heavily on financial controls to foster economic performance and ensure transparent resource utilisation. These controls empower authorities to navigate financial challenges effectively while upholding principles of accountability and stewardship (Jalal & Nmili, 2020). This article also highlights the genesis of corporate governance, notably brought to prominence by the Cadbury Committee in 2007, as rules governing relationships between stakeholders (Mahrani & Soewarno, 2018).

Financial controls, at their core, are instruments that organisations employ to govern their financial affairs. They serve the crucial purpose of regulating expenditures and safeguarding the intended use of financial resources (Dollery et al., 2020). In the public sector, financial controls encompass realistic budgeting, rigorous audits, and transparent financial reporting, all of which contribute to transparency and responsible stewardship of public funds. Effective financial controls involve the establishment of processes, procedures, and policies that align with an entity's financial goals, thereby enhancing operational efficiency and transparent resource management.

Openness in public services, an imperative for good governance, is achieved through robust financial controls. These controls ensure that financial resources are allocated and utilised as intended, resulting in operational efficiency and effective resource management (De Alwis, 2020). Additionally, Kibor (2019) underscores the importance of financial controls in aiding devolved governments to identify and settle outstanding obligations to suppliers.

Universal corporate scandals underscore the paramount importance of corporate governance in an organisation's operations, emphasising the need for mechanisms that monitor and enhance governance (Kasztelnik, 2019). Corporate governance, in essence, ensures that rights and responsibilities are shared equitably among stakeholders, thereby balancing the forces that drive organisational activities.

Importantly, corporate governance intersects with financial controls, as both are inextricably linked. Financial controls serve as a practical means to achieve the principles of corporate governance, aligning individual and organisational goals. However, challenges such as inadequate financial reporting, budgeting inefficiencies, and liquidity problems may hinder this symbiotic relationship, potentially exposing organisations to risk (Ahmed & Nganga, 2019). Furthermore, limited human resources in certain contexts may hamper the implementation of essential controls, creating opportunities for resource misappropriation.

Devolved governments, both globally and in specific regions such as Africa and England, have pursued financial control strategies to enhance corporate governance. In response to budget constraints, local governments have sought alternative methods of service delivery, emphasising financial management reforms that incorporate budgeting and auditing practices (Ferry et al., 2018). In developing countries, fiscal decentralisation reforms have aimed to address public service needs at the grassroots level. However, these initiatives have encountered challenges, including local elite capture and fiscal control deficiencies, leading to poor financial reporting practices (Dollery et al., 2020).

African countries, like Kenya, have initiated financial control systems and reforms to combat corrupt practices and improve financial resource management (Lassou et al., 2021). In Kenya, financial reforms have been ongoing since the 1970s, with a strong focus on financial controls, budgeting, and auditing to enhance public service delivery (Omollo, 2018). Reports from the Auditor General have highlighted corporate governance challenges in county governments, often stemming from inadequate financial reporting practices and transparency issues (Kibor, 2019). Recommendations have included staff training and stricter authorisation processes for financial control to mitigate fund misappropriation and resource wastage.

The effectiveness of financial reporting practices in promoting transparent and accountable corporate governance is a topic of concern. Challenges in financial reporting practices in the context of financial controls have raised questions about whether these practices truly contribute to enhancing corporate governance. There is a need to investigate whether there exists a statistically significant relationship between financial reporting practices and the quality of corporate governance within organisations. This inquiry seeks to determine whether financial reporting practices play a pivotal role in shaping the overall governance framework or whether they are merely a component with limited influence.

LITERATURE REVIEW

An empirical review by van Helden and Reichard (2019) on accounting information in the public sector found that financial reporting is an imperative aspect of the public sector. The financial reports provided should be reliable. Financial reliability was encompassed by ensuring that the reports were timely, correct and easily understandable to the users. The review concluded that there was a general shift in financial reporting where most public organisations were moving from a pure accountant's view of reporting to a more balanced way of mixing professional and financial information users' perspectives. By so doing, the public was able to understand the financial information provided because financial reporting was reliable. In the same manner, Redmayne and Vašiček (2021) present that financial reporting transformations in the public sector revived interest in whether individuals who prepare financial reports have the required capacity to comprehend and retort to the needs of financial information users. There was a disconnect found between financial reporting and financial management and control practices. This created obstacles to perceiving the connection between financial reporting practices and corporate governance in the public sector. This is a gap that this current study aimed to investigate to establish the relationship between financial reporting practices and corporate governance in the County Government of Nakuru.

In the local governments of New Zealand, Ehalaiye et al. (2021) examined the significance of financial reporting and found that financial reports contained information that helped to make decisions on investments and funding, which aided in resource management. However, the study recommended the need for the financial reports to be made easier for the users to find and understand the financial information in them. This would help the information to be more reliable for the users to implement and use. In Indonesia, Setyawan and Gamayuni (2020) used a quantitative empirical research design to study financial reporting in local governments. The study found that the robustness of the financial reports focused on the provision and delivery of financial information to stakeholders. Participation and transparency were required to ensure that the financial information provided was relevant and reliable.

Indeed, financial reporting plays a vital role in organisations. A global review by Abed et al. (2020) found that in countries such as the United Kingdom, some companies manipulated their financial reports to counter any impacts that were unfavourable to the companies. In Nigeria, about 90 per cent of companies unfairly reported their operations. The study showed that listed firms used financial reports, and this was impacted by corporate governance practices used in the firms. The financial reports mainly presented information on the financial position and competence of the organisations. The extent of financial reporting and disclosure in the companies determined the extent of investment decisions and valuation for the companies. The financial reports were to be reliable for the organisations. However, this was affected by aspects such as the economic failures of the companies, which raised issues of trustworthiness and dependability of the financial information in the reports. The unethical practices created moral and ethical dilemmas in the corporate governance of the organisations.

In Cameroon, Fossung et al. (2020) used descriptive statistics to study the implementation of the organisation for the Harmonization of Business Law in Africa Act on Accounting and Financial Reporting. The study presented results that indicated that the public sector was in need of proper financial reporting mechanisms. This would help to ensure the unveiling of the financial statements and heighten the quality of financial statement disclosure.

An explanatory study in the State Corporation of Tanzania by Masoud (2022) indicates that there was a lack of openness and accountability, leading to negative significant relationships in the organisation's performance. There were no measures put in place to detect and prevent fraudulent activities and corruption, which meant that fraud and corruption could go undetected in the organisation. Also, important financial and procurement reports were not transparently communicated to the stakeholders, and they did not get communication on time. Kimani et al. (2021) conducted semi-structured interviews to analyse corporate governance in Kenyan corporate organisations. The study revealed that corporate governance concepts were well implemented in organisations. However, there were interferences from patronages and informal networks, which interfered with the work of the managers and hindered their independence. This also created hindrances to accountability and transparency practices in the organisations.

In Kenya, Mwambere and Kosimbei (2022) used a descriptive research design to study financial reporting practices in the Taita Taveta County government and found that financial reporting had a positive relationship with the performance of the organisation. However, there was a need for care to be taken during the preparation of financial reports. The reports were to adhere to international accounting standards as well as other professional bodies. There was also a need for the county government to ensure proper implementation of the policy for financial reports to be prepared and disclosed on a regular basis. This would help to ensure proper financial control practices in the organisation.

METHODOLOGY

This study used descriptive and correlational research designs to provide the blueprint for answering the study's objectives, which focus on budgeting, auditing, and financial reporting practices. According to Quinlan et al. (2019), the descriptive design helps to understand, characterise and determine the study phenomenon and the proportion of people behaving in a certain way to aid in making specific predictions. The correlational research design helps to direct the relationship between the study's variables. The research designs used a non-experimental approach that allowed the researcher to data collection from the target audience. Thereby, the researcher broadened the scope of the phenomena by identifying the linkage between the dependent and independent variables. The researcher was able to observe the variables and their relationships as they were devoid of manipulating them.

This study targeted eighty-one employees in the finance department of the Nakuru County Government. This target group was chosen due to the familiarity and involvement of financial aspects in the Nakuru County Government. A census method was used as it allowed the study to use all elements in the target population, which resulted in a high statistical degree of confidence in the data analysis results. Also, all the individuals in the target population participated in the study and were allowed to provide their opinions regarding the study's objectives. The census method provided in-depth and intensive information covering the research's problem, making the conclusions more reliable and accurate (Bougie & Sekaran, 2019). Since the target population was eighty-one employees in the finance department of the Nakuru County government, the number was less than 200 and hence considered small, and a census was deemed as an appropriate method to use as compared to sampling the respondents.

Primary data were collected using structured questionnaires. The questionnaires were used as they are low-cost, and there was no interference emanating from the researcher's bias. The questionnaires helped to collect data in an efficient manner, which would have been challenging if collected by other means. The questions in the questionnaire were presented on a five-point Likert scale ranging from strongly agree to strongly disagree. There were also open-ended questions to allow the respondents to expound on their responses.

Cronbach’s Alpha coefficient verified the questionnaire's reliability, and this helped to assess the extent to which the instrument attains the consistency of the items intended to be measured. The measured items produced results that were similar every time they were measured. In this study, a threshold of 0.7 in the reliability index of Cronbach’s Alpha coefficient was considered. On the other hand, the validity of the questionnaire was ascertained using construct, face and content validities. The construct validity focused on the measures of financial control and corporate governance in the Nakuru County government. The approach used was factor loading, and the minimum loading of the construct measurement of the items that was accepted was 0.4.

Items unable to meet this threshold were either reviewed for completeness or removed. On content validity, the assertion was by assessing whether the questionnaire's content covers all relevant parts of financial control and corporate governance. Finally, face validity focused on identifying whether the items in the questionnaire are suitable for the study and help to realise the study's objectives. The face and content validities were attained using expert assessment by this study's supervisors. This helped to address any ambiguous or challenging aspects of the questionnaire.

Data Analysis

The questionnaires were collected, coded, and cleaned to ensure that the questions were filled as required and that they were fit to be used for this study. The questionnaire contained open and closed questions. The open questions collected qualitative data, which was analysed using themes on the basis of the objectives of this study. This data was presented using narratives. Closed questions collected quantitative data, which was entered into the Statistical Package for Social Sciences (SPSS) computer software (Version 26) for analysis. Descriptive statistics such as frequencies and percentages were used in the analysis, while inferential statistics were analysed using Pearson correlation and linear regression.

The correlation test determined the linear relationship's strength between the study's variables. A coefficient value of +1 deemed a positive relationship, while -1 deemed a negative relationship. Also, a value that lay between .50 and 1 signified a strong relationship. The significance level for the test was 0.05, which was the decision criteria in this study. A linear regression analysis was also performed, and it held the assumptions of linearity and normality tests to establish whether a linear relationship existed between financial reporting practices and corporate governance. The normality test was carried out to ensure that there were no significant outliers in the distribution of the data. The presence of significant outliers would be an indication that the data was distorted and skewed. The multicollinearity test checked whether the variables were highly correlated to each other as it would lead to reduced predictive power.

The regression used the following model;

$Y= \beta_0 + \beta_1 X_1 + \varepsilon$

Where: Y was Corporate Governance

β_0 was Constant

X_1 was Financial Reporting Practices

ε was an Error term

β1 was the regression coefficient of independent variables.

The quantitative findings were presented in the form of tables and charts.

RESULTS AND FINDINGS

Financial Reporting Practices

The aim of this study was to assess the relationship between financial reporting practices and corporate governance at the Nakuru County Government, Kenya. The data were analysed and recorded in Table 1.

Table 1 Financial Reporting Practices

No.	Statements	SD (%)	D (%)	N (%)	A (%)	SA (%)	Total (%)
1.	In this organisation, there are proper financial reporting tools	0.0	0.0	0.0	100.0	0.0	100
2.	In this organisation, financial reports are up-to-date	0.0	0.0	0.0	86.7	13.3	100
3.	In this organisation, financial reports are properly developed	0.0	0.0	0.0	82.7	17.3	100

4.	In this organisation, financial reports are easily accessible to the stakeholders	0.0	0.0	0.0	100.0	0.0	100
5.	In this organisation, financial reports are written in a language that all stakeholders of the organisation can understand	0.0	0.0	0.0	86.7	13.3	100

The results show that all the respondents agreed that there were proper financial reporting tools in the organisation. Most of the respondents, 86.7 per cent, agreed that financial reports were up-to-date, while 82.7 per cent agreed that financial reports were properly developed. Moreover, all the respondents agreed that the financial reports were easily accessible by the stakeholders, while 86.7 per cent of the respondents agreed that the financial reports were written in a language that all stakeholders of the organisation could understand.

These findings are congruent with the findings by van Helden and Reichard (2019), who found that it was important for public organisations to have correct, timely and easily understandable financial reports. This made financial reporting in the organisation appear reliable. On the contrary, Redmayne and Vašiček (2021) found that there were disconnects between financial management and financial reporting in public organisations due to inadequate capacity to respond to the needs of financial information users.

Furthermore, in this current study, the respondents were asked if the stakeholders of the organisation have an interest in the financial reports. Most of the respondents indicated that the stakeholders of the organisation had an interest in the financial reports. One of the respondents indicated;

> “The financial reports help the stakeholders to know that as an organisation, we are transparent and accountable for the financial actions that we take. This means that stakeholders such as the public, interested investors and our suppliers are able to understand the overall financial stability and sustainability of the county. For the employees, they are able to understand the importance of adhering to ethical standards and practices.” (Respondent 5, research data 2023)

Interestingly, when asked whether the financial reports were effective, there were mixed reactions, with some respondents agreeing and others disagreeing. Respondents stated;

> "No, I don't think so. For me, the financial reports are just a formality. Maybe some of the stakeholders may have an interest, but only those in the opposition and maybe some of the investors. Otherwise, preparation of the reports is just a formality for the organisation.” (Respondent 29, research data 2023)

Yet another respondent indicated;

> "Yes, the stakeholders have an interest in the financial reports as they view them as a way of understanding and evaluating how the county government is governed financially. From this, they can make decisions on whether the county government is being managed properly in terms of the finances and risks, and they can understand the overall financial health of the county government." (Respondent 72, research data 2023)

These findings resonate with the findings of Ehalaiye et al. (2021), who found that financial reports helped to make investment decisions in public organisations. This was important for resource mobilisation and management processes. However, there were gaps in ensuring that the reports were made easier for stakeholders to find and understand.

Corporate Governance

The dependent variable for this study was corporate governance, and the data on this was analysed and recorded in Table 2.

Table 2 Corporate Governance

No.	Statements	SD (%)	D (%)	N (%)	A (%)	SA (%)	Total (%)
1.	In this organisation, providing financial reports on time helps to achieve financial accountability	0.0	0.0	13.3	69.3	17.3	100
2.	In this organisation, ensuring that financial reports are understandable by all stakeholders helps to ensure that there is transparency in the organisation's operations	0.0	34.7	0.0	65.3	0.0	100

The findings show that 69.3 per cent agreed that providing financial reports on time helps to achieve financial accountability. A large portion of the respondents (65.3 %) agreed that ensuring that financial reports are understandable by all stakeholders helps to ensure that there is transparency in the organisation's operations.

These findings mirror those of Kimani et al. (2021), who found that financial reporting practices that were well structured led to great implementation of corporate governance concepts. However, external interferences from patronages led to hindrance of auditors' independence, which in turn hindered accountability and transparency practices.

Additionally, in this current study, all the respondents agreed that financial reporting practices in the organisation are adequate in ensuring proper corporate governance takes place. On the relationship between financial reporting practices and corporate governance (transparency and accountability) in the organisation, there were diverse views provided. One of the respondents indicated;

> "There is a good relationship if financial reports are done in the right way, then, corporate governance is upheld and this leads to financial accountability and transparency." (Respondent 37, research data 2023)

Another respondent indicated;

> "I believe that there is a link between financial reports and corporate governance. When the reports are properly put in place, corporate governance becomes strengthened. Financial resources can be properly monitored and evaluated, and this helps to ensure that the county government makes informed decisions which cater for the needs of the residents of Nakuru County." (Respondent 60, research data 2023)

These findings reinforce those of Ismail et al. (2019), who found that financial reports had a relationship with corporate government. This is because it increased aspects of transparency, accountability, credibility and reliability of the reports. This increased the public's confidence in the reporting process, and there was a reduced likelihood of financial misstatements being produced. This improved the overall financial performance of the organisations.

The Relationship between Financial Reporting Practices and Corporate Governance

To establish the relationship between financial reporting practices and corporate governance at the Nakuru County Government, inferential analysis was conducted by this study, and they consisted of correlations and multiple linear regression. First, diagnostic tests were conducted to test the study's held assumptions.

Diagnostic Tests

The diagnostic tests for this study were linearity, normality and multicollinearity tests.

Linearity Test

To find out whether a linear relationship existed between financial reporting practices and corporate governance, a linearity test was conducted. These findings were recorded in Figure 1.

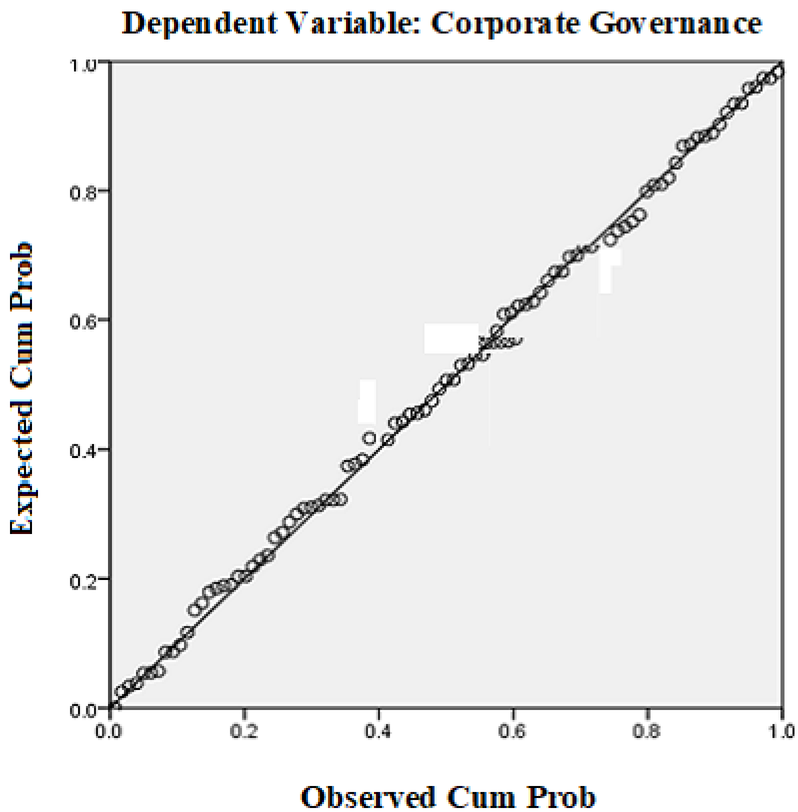

Figure 1: Test of Linearity

Figure 1 shows that the distribution of data was linear. Even though there were small deviations, they were not drastic, and as such, the linearity of the data was upheld.

Normality Test

To ensure that there were no significant outliers in the distribution of the data, a normality test was conducted using a histogram. The presence of significant outliers would distort and skew the data's interpretation, which would, in turn, significantly negatively affect the study's results. The normality test was conducted, and the findings were recorded in Figure 2.

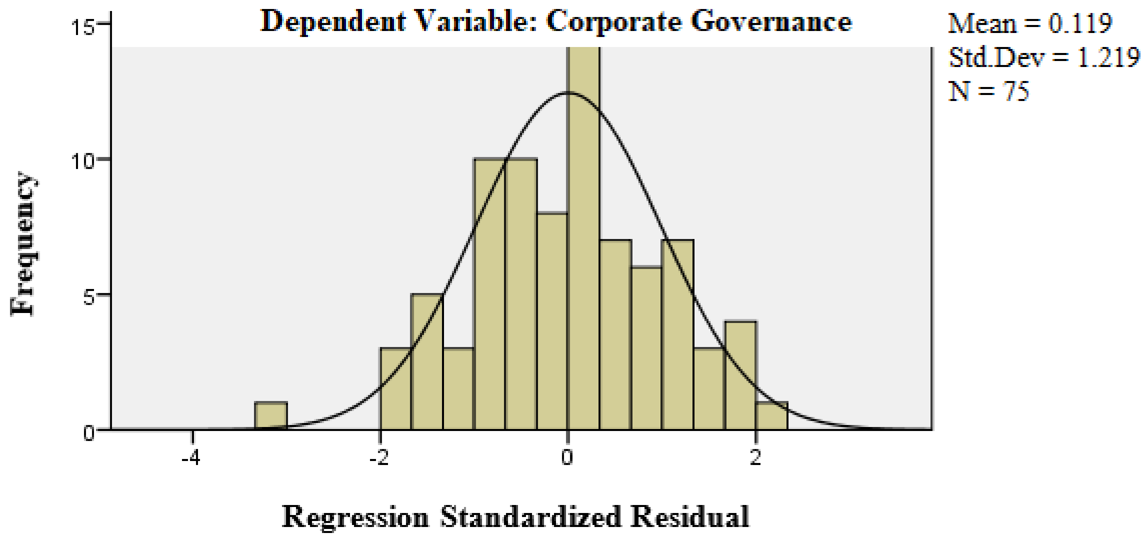

Figure 2: Test of Normality

Figure 2 shows that the data were distributed normally, and the bell-shaped curve is symmetrical. The standard deviation was 1.219, while the mean was 0.119. A mean of 0 and a standard deviation of 1 indicated that there was a normal distribution of data.

Correlation Analysis

A Pearson correlation analysis was employed to establish the relationship between financial reporting practices and corporate governance at the Nakuru County Government. The findings were recorded in Table 3.

Table 3 Correlation Analysis

		Financial Reporting Practices	Corporate Governance
Corporate Governance	Pearson Correlation	.604**	1
	Sig. (2-tailed)	.000	
	N	75	75

**. Correlation is significant at the 0.01 level (2-tailed).

The findings also showed a strong and positive relationship existed between financial reporting practices and corporate governance, with a Pearson correlation value of 0.604 and a p-value of 0.000 (<0.01). Contradictory findings were presented by Abed et al. (2020), who indicated that there was a negative but statistically significant relationship between financial reporting and corporate governance. This was because the companies were not truthful in their financial reports. This raised issues of reliability and credibility of the financial information in the reports. There were many cases of unethical practices reported, which led to the development of corporate governance ethical and moral dilemmas among the organisations that participated in that study.

Regression Analysis

To make inferences based on this study's regression model, a regression analysis was conducted. This study aimed to investigate the nexus between financial reporting practices and corporate governance at the Nakuru County Government, Kenya. The regression analysis resulted in the model summary, ANOVA and coefficient results.

1. Model Summary

The model summary results showed how well the regression model performed and fit in the study. The findings are shown in Table 4.

Table 4 Model Summary

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.596[a]	.356	.328	2.323
a. Predictors: (Constant), Financial Reporting Practices b. Dependent Variable: Corporate Governance				

The findings in Table 4 indicate that the magnitude of the linear relationship between corporate governance and financial reporting practices is 0.596. The coefficient of determination showed that 35.6 per cent of the variance in corporate governance was explained by the predictor of financial reporting practices. These findings suggested a moderate relationship between the predictor and dependent variables. The remaining 64.4 per cent of the variance could be attributed to random variation or factors not considered in the analysis as the study involves invariabilities of human behaviour. These factors can include aspects such as the role of the Nakuru County Assembly in providing oversight, ethics and compliance. As such, the variance in this study was considered to provide valuable insights into understanding the nexus between financial reporting practices and corporate governance.

2. Analysis of Variance (ANOVA)

To further understand the variability levels in the regression model, the ANOVA results were presented. The results of ANOVA are recorded in Table 5.

Table 5 ANOVA Results

ANOVA[a]						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	211.448	3	70.483	13.058	.000[b]
	Residual	383.219	71	5.397		
	Total	594.667	74			
a. Dependent Variable: Corporate Governance						
b. Predictors: (Constant), Financial Reporting Practices						

Table 5 shows that the F-statistic is 13.058, and the p-value is 0.000. This is an indication that the regression model of the study is statistically significant ($p<0.05$). This provides strong evidence that there is a statistically significant relationship between financial reporting practices and corporate governance.

3. Regression Coefficients

The regression coefficient results show the significance of the relationship between financial reporting practices and corporate governance. The results are shown in Table 6.

Table 6 Regression Coefficients

Coefficients[a]

Model		Unstandardised Coefficients		Standardised Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	.3.134	13.915		.225	.822

	Financial Reporting Practices	1.691	.488	.430	3.461	.001

a. Dependent Variable: Corporate Governance

For the regression analysis, the regression model that was used is as follows:
Y= Y= $\beta_0 + \beta_1 X_1 + \varepsilon$

Where: Y was Corporate Governance
β_0 was Constant
X_1 was Financial Reporting Practices
ε was an Error term
β_1 was the regression coefficient of the independent variable.

Therefore, the coefficient findings in Table 6 show that;
Corporate Governance= $3.134+1.691X_3$

The unstandardised coefficient for financial reporting practices is 1.691 and a t-value of 3.461. This implies that, on average, for a one-unit increase in financial reporting practices, corporate governance increases by 1.691 units. The t-value was 3.461, reflecting the magnitude of the relationship between financial reporting practices and corporate governance. The p-value of 0.001 (<0.05) suggests a strong positive relationship between financial reporting practices and corporate governance. In other words, the financial reporting practices were associated with higher levels of corporate governance in the Nakuru County Government. Therefore, this study rejects the research hypothesis that financial reporting practices do not have a statistically significant relationship with corporate governance at the Nakuru County Government.

These findings reinforce the findings by Mwambere and Kosimbei (2022), who indicated that at the Taita Taveta County government, financial reporting had a positive relationship with the performance of the organisation when it came to aspects such as accountability and transparency. However, there was a need for care to be taken during the preparation of financial reports. The reports were to adhere to international accounting standards as well as other professional bodies. There was also a need for the county government to ensure proper implementation of the policy for financial reports to be prepared and disclosed on a regular basis. This would help to ensure proper financial control practices in the organisation.

CONCLUSION AND RECOMMENDATIONS

Conclusion: This study concludes that there are proper financial reporting tools at the Nakuru County Government. The financial reports are up-to-date, properly developed, easily accessible by the stakeholders and written in a language that all stakeholders of the organisation can understand. The stakeholders of the organisation have an interest in the financial reports as the reports help in asserting that the organisation is accountable and transparent in its financial actions. This helps the stakeholders to understand the overall financial stability and sustainability of the county. Additionally, the employees are not sure about the effectiveness of the financial reports, with some of them indicating that the financial reports are effective in aiding decision-making, while others view the development of financial reports as a formality for the organisation. Further, inferences are made that there is a statistically significant relationship between financial reporting practices and corporate governance.

Recommendations: This study recommends that the Nakuru County Government should review and update its financial reporting policies and procedures to make sure that they align with best practices. There should be comprehensive communication with the stakeholders, including the employees, on the organisation's financial reports. There should also be monitoring and evaluation of the effectiveness of the financial reports, and these findings should be communicated to the organisation's stakeholders. A similar study can be carried out in other counties in Kenya to establish the nexus between financial reporting practices and corporate governance.

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