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## CONTRIBUTION OF GOVERNMENT REGULATIONS TO FINANCIAL DISTRESS FACING LOCAL AUTHORITIES IN KENYA

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# CONTRIBUTION OF GOVERNMENT REGULATIONS TO FINANCIAL DISTRESS FACING LOCAL AUTHORITIES IN KENYA

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## Abstract

**Purpose:** The purpose of this study was to establish the contributions of Government regulations to financial distress facing Local Authorities in Kenya.

**Methodology:** A descriptive research design was used to conduct the study. The study population comprised of the 175 Local Authorities in Kenya. 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:** 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.

**Unique contribution to theory, practice and policy:** The study recommended that, 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. Further regulations and amendments to the existing laws should be critically examined to avoid watering the revenue base of the newly formed county governments.

**Keywords:** Government regulations, financial distress, Local Authorities

## 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 forms 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 Central government, national government or (where applicable) 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).

## **1.2 Problem Statement**

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 whopping 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 15<sup>th</sup> June 2000, pg.1095.

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 contribution of Government Regulations to financial distress facing Local Authorities in Kenya.

### **1.3 Research Objective**

The objective of this study was to determine the contribution of Government Regulations practices to financial distress facing local authorities in Kenya.

## **2.0 LITERATURE REVIEW**

### **2.1 Theoretical Review**

#### **2.1.1 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 Empirical Review**

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.

### **3.0 RESEARCH METHODOLOGY**

A descriptive research design was used to conduct the study. The study population comprised of the 175 Local Authorities in Kenya. 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.

### **4.0 RESULTS AND DISCUSSIONS**

#### **4.1 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.

**Table 1: Response Rate**

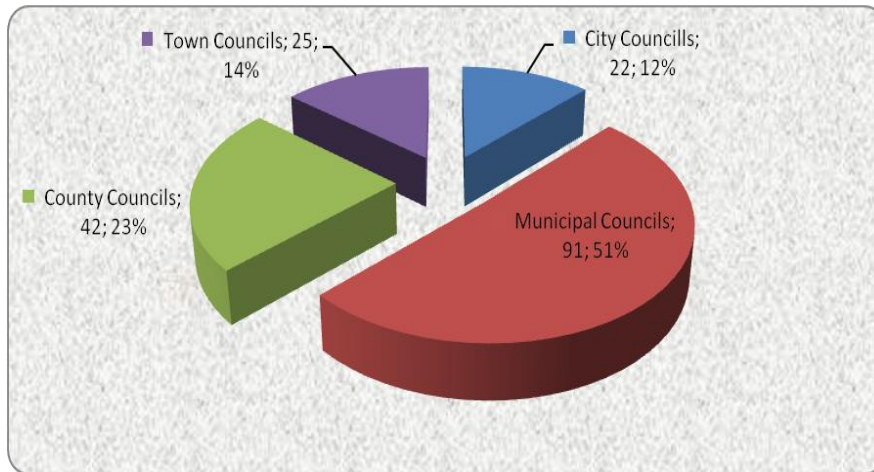
	<b>Successful</b>	<b>Unsuccessful</b>	<b>Total</b>
Officers/Employees	188 (94%)	12(6%)	200
Customers	107 (89%)	13(11%)	120
Total	295 (92%)	25(8%)	320

A total of 295 questionnaires were properly filled and returned, which included 188 questionnaires from the officers and 107 questionnaires from the customers.

#### **4.2: Demographic data**

##### **4.2.1: Category of Local Authority**

Figure 1 presents results on category of local authority of the respondents

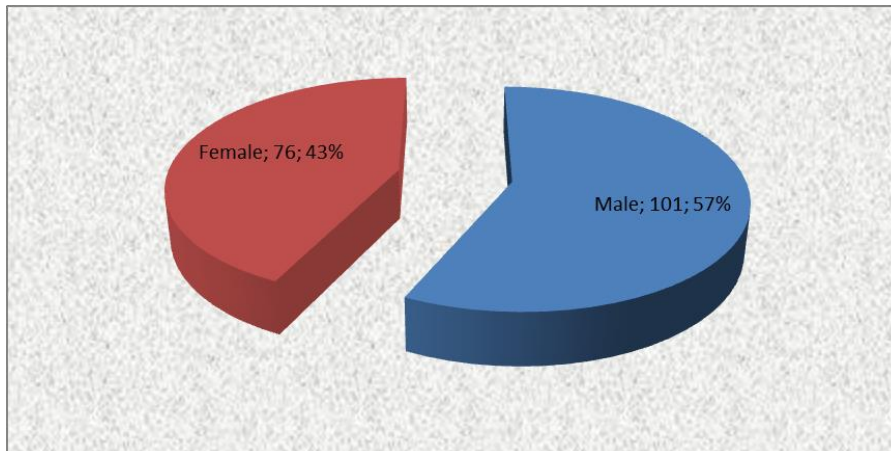


**Figure 1: Category of Local Authority**

As demonstrated in figure 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.

#### 4.2.2: Gender of Local Authority Officers

Respondents were asked to indicate their gender. Figure 2 presents the results.



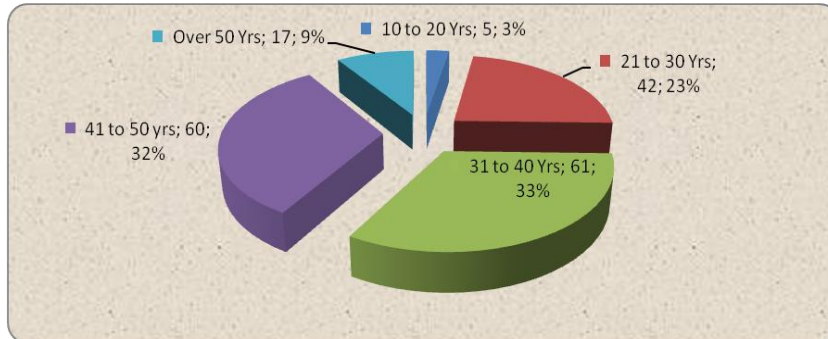
**Figure 2: Gender of Local Authority Officers**

Figure 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.

#### 4.2.3: Age Bracket of Respondents

Respondents were asked to indicate their age bracket. Figure 2 presents the results.

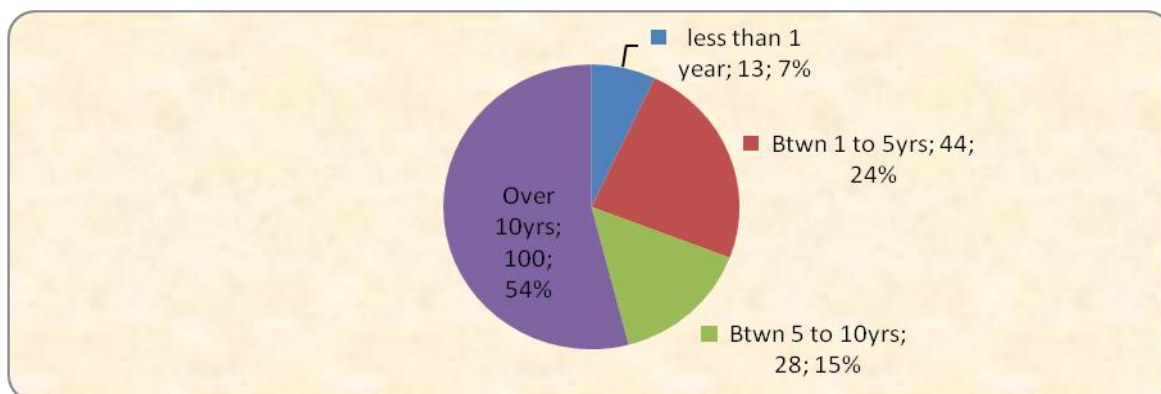


**Figure 3: Age Bracket of Respondents**

As revealed in Figure 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.

#### 4.2.4: Length of Service

Respondents were asked to indicate the length of time in service. Figure 2 presents the results



**Figure 4: Length of Service**

Figure 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.

#### **4.3: 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.

##### **4.3.1 The Transfer of Functions Act (1969)**

Descriptive results in table 2 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.

##### **4.3.2: The Graduated Personal Tax of 1974**

Descriptive results in table 2 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.

##### **4.3.3: The Constituency Development Fund Act of 2003**

Result in table 2 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.

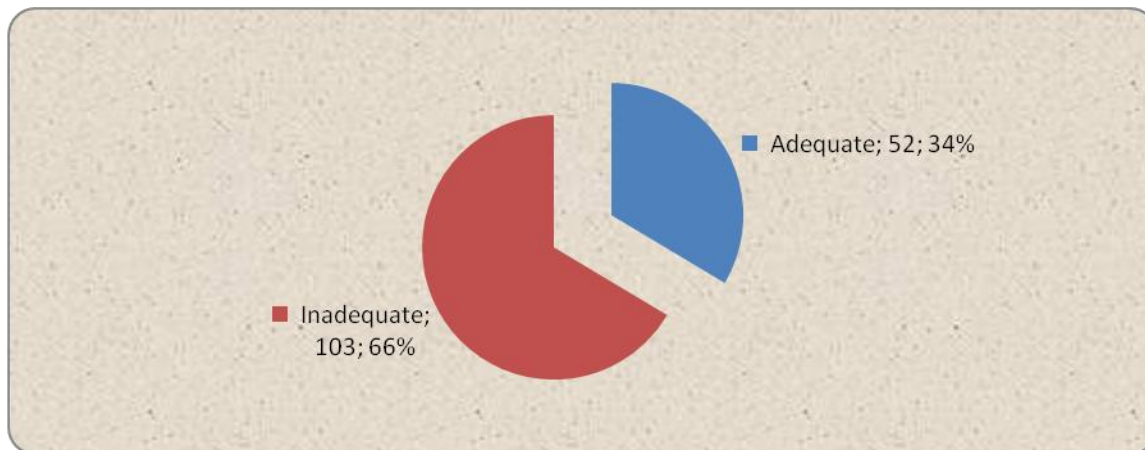
The findings revealed that the passing of the Constituency Development Fund Act (2003) which initiated the mechanism for financing community projects at constituency level in competition with Local Authorities led to the weakening of the focus on councils as the primary channel for service delivery at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

**Table 2: 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 authorities	9, 4.8%	28, 14.9%	53, 28.2%	73, 38.8%	25, 13.3%
The Graduated Personal Tax of 1974 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%

#### 4.3.4: Rating the Adequacy of Government Regulation in the Local Authority

As revealed by figure 5, 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 unfavorable regulation.



**Figure 5: 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.

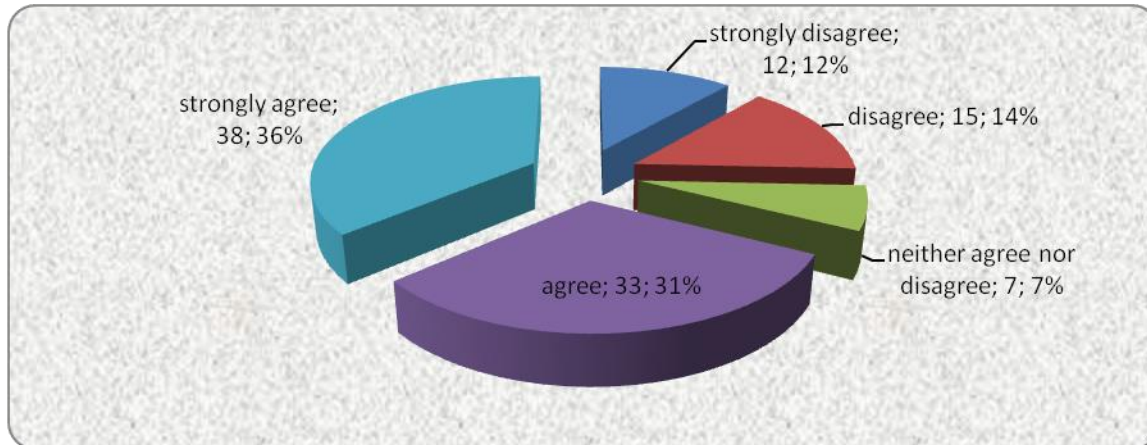
It was also recommended that perhaps the law should be amended to enable the setting up of an anticorruption committee at the Local Authority level. In addition, it was suggested that cap 265 should be amended so as to divorce politics from Locals. Most importantly, it was recommended that the government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

#### **4.3.5: 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 6 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 6: 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 3 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 3, the relationship between government regulation and financial distress is positive and significant ( $b_1=1.575$ ,  $p$  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;

**Table3: 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. 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: 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			

Descriptive statistics in table 4 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 5: Descriptive Statistics for Government Regulation**

	N	Mean	Std. Deviation	Std. Error	95% Confidence Interval for Mean		Minimum	Maximum
					Lower Bound	Upper Bound		
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

Analysis of Variance (ANOVA) results in table 6 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 6: 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 7 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 7: 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 Italian Local governments and concluded that bureaucracy and poor legislation are major causes of financial distress in Local Authorities.

## 5.0 CONCLUSIONS AND RECOMMENDATIONS

### 5.1 Conclusions

The study concluded 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 Recommendations

The study recommended that, 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. Further regulations and amendments to the existing laws should be critically examined to avoid watering the revenue base of the newly formed county governments.

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