

## EFFECT OF PUBLIC FINANCIAL MANAGEMENT REFORMS IN THE EFFECTIVE MANAGEMENT OF PUBLIC FUNDS IN KENYA: A CASE STUDY OF THE NATIONAL TREASURY

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### ABSTRACT

Public sector was rampant with corruption and inefficiencies and therefore poor management of public fund; this therefore called for reforms in the public sector. PFM reforms introduced not just a different way of managing public services, but also the need for different financial management tools and techniques. Introduced initially in response to widespread public criticism of the public service, the overall ethos of the reforms is greater public sector efficiency and has two key tenets: allowing managers to manage and making managers accountable and therefore ensuring better management of public funds. The goal of financial management in government is to ensure that safeguard and use available funds and other scarce resources in the best interest of the people. This study sought to establish the effect of reforms in budgeting, enhanced revenue collection, revision of procurement laws, and IFMIS reform in the management of public funds in Kenya National Treasury. The study used descriptive research design. The study targeted employees in top managers, middle level managers and lower level managers. The study adopted a stratified random sampling approach to get a study sample of 30% from within each stratum. A semi-structured questionnaire was used to collect data. Pilot test was conducted to enhance the instrument validity and reliability. Data collected was analyzed through SPSS and Microsoft Excel and presented in tables and charts to summarize responses for further analysis and to facilitate comparison. The study also employed a regression model and correlation to study the relationship between factors. The study found that procurement reforms had the greatest effect on the effective public fund management followed by budgeting reforms, then mentoring adoption of IFMIS while tax revenue administration had the least effect to the effective public fund management. The study recommended that recommends that the government should work together with all the stakeholders in ensuring that the procurement laws are implemented and followed effectively. The study also recommends that the government should work with all the relevant ministries to ensure successful adoption of IFMIS.

**Keywords:** *Effect of Public Financial Management Reforms*

### Introduction

According to Hedger and Renzio (2010), government budgets are key areas of public action by which policy objectives are chosen and acted upon and the necessary resources collected, allocated and spent. Government budgeting systems are also important to donor agencies

because of their role in providing fiduciary safeguards, helping to ensure, for example, that foreign aid funds remitted as direct budget support are properly used for their intended purpose. Pauw, Woods, Van der Linde, Fourie and Visser (2002) in their study to establish the role of budgeting on performance of organizations in United Kingdom found out those strong budgeting systems also contribute to better overall standards of public sector governance. In recent years, donor-supported Public Financial Management (PFM) reform programmes have covered a range of initiatives to strengthen the rules and procedures that underpin budget processes in aid recipient countries. Standard interventions have focused on: improving the comprehensiveness of budget operations; building better links between annual allocations and medium-term policy objectives; introducing performance indicators and management systems; computerizing budget management and expenditure control (McThomas, 2003). According to McThomas (2003), budgeting, supply chain management, movable asset management and control are essential areas of financial management practices that sound financial management, be it in the public or private sector, is vested in the timely, efficient, effective and economical attainment of objectives by managers. The Public Financial Management Reform by the Government is considered by the National Treasury as contributing significantly towards the improvement of financial management in the broader public sector (South Africa National Treasury, 2004).

### Statement of the Problem

According to Transparency International Kenya (2013), in Corruption Perceptions Index 2012 Kenya is ranked 139th out of 176 countries for corruption. However, the country scores 49 out of 100 in the 2010 Open Budget Index, which indicates that the government provides some information to the public, but this is insufficient for citizens to fully hold the government accountable for its management of public resources (International Budget Partnership, 2010). Kenya has been struggling with corruption cases and mismanagement of public funds (Transparency International Kenya, 2013). Corruption drew from public coffers over 600 million dollars in Goldenberg scandal and a further loss in Anglo leasing scandal (Transparency International Kenya, 2013). There are regular reports of tax evasion and high-level government officials using their positions and influence to obtain tax exemptions for themselves or their relatives (Global Integrity, 2011). Corruption and tax evasion has greatly crippled functioning of the national treasury in that; it has influenced the inflow of cash through taxation and effectiveness of use of budgetary allocation.

Various studies have been done in the area of public financial management. Mathiba (2011) did a study to evaluate financial management practices in the department of correctional services in South Africa. Lawson (2012) in a study Commissioned by Sida, Danida and AfDB did an evaluation of public financial management reforms in Burkina Faso, Ghana and Malawi for a period between 2001 and 2010. Further, Wyk (2003) did a study to determine a performance measurement approach to improve financial management in provincial governments in South Africa. Locally, Gathuya (2010) conducted a survey of factors that influence local authority's financial management taking a case of City Council of Nairobi. However, there lacks an empirical study done to investigate the success of these reforms to achieve the set objectives. Therefore this study seeks to establish the effect of reforms in budgeting, enhanced revenue collection, revision of procurement laws, and IFMIS reform in the management of public funds in Kenya National Treasury.

## Objectives of the Study

### General Objective

To establish the effect of public financial management reforms in the effective management of public funds in Kenya National Treasury

### Specific Objectives

- i). To establish the effects of budgeting reforms in the effective management of public funds in Kenya National Treasury
- ii). To find out the effect of enhanced tax revenue administration in the effective management of public funds in Kenya National Treasury
- iii). To find out the effect of revision of procurement laws in the effective management of public funds in Kenya National Treasury
- iv). To establish the effects of adoption of IFMIS in the effective management of public funds in Kenya National Treasury

## Literature Review

### Three-Component Theory of Commitment

This theory was proposed by Allen and Meyer in 1990. This model proposes that organizational commitment is experienced by the employee as three simultaneous mindsets encompassing affective, normative, and continuance organizational commitment. Affective Commitment reflects commitment based on emotional ties the employee develops with the organization primarily via positive work experiences. Normative Commitment reflects commitment based on perceived obligation towards the organization, for example rooted in the norms of reciprocity. Continuance Commitment reflects commitment based on the perceived costs, both economic and social, of leaving the organization. This theory of commitment has been used by researchers to predict important human outcomes, including turnover and citizenship behaviors, job performance, absenteeism, and tardiness (Meyer et al., 1993).

### Theory of planned behavior

This theory of planned behavior is a theory about the link between beliefs and behavior. The concept was proposed by Ajzen (1991) to improve on the predictive power of the theory of reasoned action by including perceived behavioral control (Ajzen, 1991). It is one of the most predictive persuasion theories. It has been applied to studies of the relations among beliefs, attitudes, behavioral intentions and behaviors in various fields such as advertising, public relations, advertising campaigns and healthcare. The theory states that attitude toward behavior, subjective norms, and perceived behavioral control, together shape an individual's behavioral intentions and behaviors.

In relation to the study, this theory can be used to explain effectiveness of management of public funds in Kenya National Treasury after budgetary reforms.. This is because budgetary reforms cover a range of initiatives to strengthen the rules and procedures that underpin budget processes. These clearly set rules, procedures and processes in budgeting, will therefore produce certain

desired expected outcomes in the management of public funds; effective management. According to McThomas (2003) Standard interventions have focused on: improving the comprehensiveness of budget operations; building better links between annual allocations and medium- term policy objectives; introducing performance indicators and management systems; computerizing budget management and expenditure control.

### **Institutional-centric theory of finances**

Institutional-centric theory of finances proposed by Stein and Rosefield in 2005 as an alternative to the flawed financial liberalization theory that increased the instability of developing countries during the 90s. Based on the theory of imperfect markets, it acknowledges the existence of imperfect information and informal and formal institutions, which efficiency is the engine of development (Stein & Rosefield, 2005; Dornbusch & Reynoso, 2003). This therefore highlighted the need to have an integrated system that supports real time financial information access. An integration of financial functions was proposed by Demaestri and Guerrero (2003) and theoretically suggests that effectiveness and efficacy are achieved when financial information are integrated.

In relation to this study, adoption of IFMIS in the public sector is aimed at enhancing information access through integration of various functions thereby removing information asymmetry. This as suggested by Demaestri and Guerrero (2003) will enhance effectiveness and efficacy of National Treasury and therefore ensure effective public funds management.

### **Research Methodology**

The study used descriptive research design, to establish the effect of public financial management reforms in the management of public funds in Kenya. The method was chosen since it is more precise and accurate since it involves description of events in a carefully planned way (Babbie, 2004). This research design also portrays the characteristics of a population fully (Chandran, 2004). The research design was both quantitative and qualitative with the aim of determining the relationship between the aspects of PFMR (independent variables) and effectiveness of management of public funds (dependent variables).

A questionnaire was used as the study tool. A questionnaire is a collection of items to which respondents are expected to react, usually in writing (Oso, 2009). The study was concerned with variables which cannot be directly observed such as opinion, perception and feelings of respondents. Such information can best be described through questionnaires (Oso, 2009). The questionnaire was developed in accordance with the research objectives. Questions to address each research question were included. Each variable was operationalised to establish what to use as a measure to it. The questionnaires were administered to the 35 employees of the National Treasury as established in the sample. The purpose of the questionnaire was to collect a lot of information over a short period of time. It was used since the respondents to the study were perceived to be literate. Also, information required could easily be described in writing as indicated by (Oso, 2009).

### **Data Analysis/Findings**

#### **Regression Analysis**

In this study, a multiple regression analysis was conducted to test the influence among predictor variables. The research used statistical package for social sciences (SPSS V 21.0) to code, enter and compute the measurements of the multiple regressions

**Table 4.1: Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.822	0.675	0.625	0.450

R-Squared is a commonly used statistic to evaluate model fit. R-square is 1 minus the ratio of residual variability. The adjusted  $R^2$ , also called the coefficient of multiple determinations, is the percent of the variance in the dependent explained uniquely or jointly by the independent variables. 62.5% of the changes in effective management of public funds in Kenya National Treasury could be attributed to the combined effect of the predictor variables. This is in line with De Renzio and Dorotinsky (2007) who state that improving the information base for budget reporting and budget management purposes has been a core part of the Public Financial Management Reform Programme (PFMRP).

**Table 4.2: Summary of One-Way ANOVA results**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	12.223	4	3.056	13.521	4.35E-06
	Residual	5.876	26	0.226		
	Total	18.099	30			

The probability value of 0.001 indicates that the regression relationship was highly significant in predicting the effect of public financial management reforms in the effective management of public funds in Kenya National Treasury. The F critical at 5% level of significance was 13.521 since F calculated is greater than the F critical (value = 2.74), this shows that the overall model was significant.

**Table 4.3: Regression coefficients of the relationship between effective management of public funds in Kenya National Treasury and the four predictive variables**

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	1.492	0.298		5.007	0.033
	Budgeting reforms	0.902	0.171	0.421	4.505	0.015
	Tax revenue administration	0.596	0.163	0.123	3.556	0.031

Procurement reforms	0.883	0.175	0.384	4.046	0.019
Adoption of IFMIS	0.617	0.178	0.326	3.766	0.027

As per the SPSS generated table above, the equation ( $Y = \beta_0 + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \epsilon$ ) becomes:

$$Y = 1.492 + 0.902X_1 + 0.596X_2 + 0.883X_3 + 0.617X_4$$

The regression equation above has established that taking all factors into account (adoption of IFMIS, procurement reforms, tax revenue administration and budgeting reforms) constant at zero effective public fund management will be 1.492. The findings presented also show that taking all other independent variables at zero, a unit increase in the scores of budgeting reforms would lead to a 0.902 increase in the scores of effective public fund management, a unit increase in the scores of level of tax revenue administration would lead to a 0.596 increase in the scores of effective public fund management. The study also found that a unit increase in the scores of procurement reforms would lead to a 0.883 increase in the scores of effective public fund management and a unit increase in the adoption of IFMIS would lead to a 0.617 increase in the scores of effective public fund management.

At 5% level of significance and 95% level of confidence, budgeting reforms showed a 0.015 level of significance, tax revenue administration had a 0.031 level of significance, capability of the procurement reforms had a 0.019 level of significance and adoption of IFMIS had a 0.027 level of significance; hence the most significant factor is budgeting reforms.

Overall, budgeting reforms had the greatest effect on the effective public fund management, followed by procurement reforms, then adoption of IFMIS while tax revenue administration had the least effect to the effective public fund management. All the variables were significant ( $p < 0.05$ ). This is in agreement with South Africa National Treasury (2004) who state that the Public Financial Management Reform by the Government is considered by the National Treasury as contributing significantly towards the improvement of financial management in the broader public sector.

## Discussion

### Procurement Reforms

The study sought to answer the question: To what extent has procurement reforms affected effectiveness in management of public funds in Kenya National Treasury? The study found out that revision of procurement laws has influenced effectiveness of management of public funds in Kenya National Treasury to a great extent. The study also found out that procurement reforms enhance transparency of procurement process, removal of bribery and corruption, accountability, efficient and effective procurement process and competition in the procurement process to a great extent.

### Adoption of IFMIS

The study sought to establish how adoption of IFMIS has affected the effectiveness in management of public funds in Kenya National Treasury. The study deduced that the adoption of IFMIS has led to effective management of public funds in Kenya National Treasury. The study

also revealed that to a great extent IFMIS has enhanced automation of government processes, enhanced reporting, enhanced record keeping, enhanced communication, customization of government processes and integration of government processes. Further it was strongly agreed that IFMIS enhances effectiveness and transparency of financial management system, IFMIS offers a standardized integrated financial management reporting system, IFMIS enhanced financial controls and accountability and IFMIS provide timely and accurate financial information.

### Conclusions

From the findings, the study concludes that budgeting reforms have an effect on effective management of public funds in Kenya National Treasury. The study also revealed that budget management, budgeting process, comprehensiveness, budget execution and budget reporting influence the effectiveness in management of public funds in Kenya National Treasury.

The study also concludes that tax revenue administration influence effectiveness of management of public funds in Kenya National Treasury. The study further found that increased tax collection reduced evasion and increased voluntary compliance affect the effectiveness of management of public funds in Kenya National Treasury.

Further the study concludes that revision of procurement laws influence effectiveness of management of public funds in Kenya National Treasury. The study also concludes that procurement reforms enhance transparency of procurement process, removal of bribery and corruption, accountability, efficient and effective procurement process and competition in the procurement process.

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