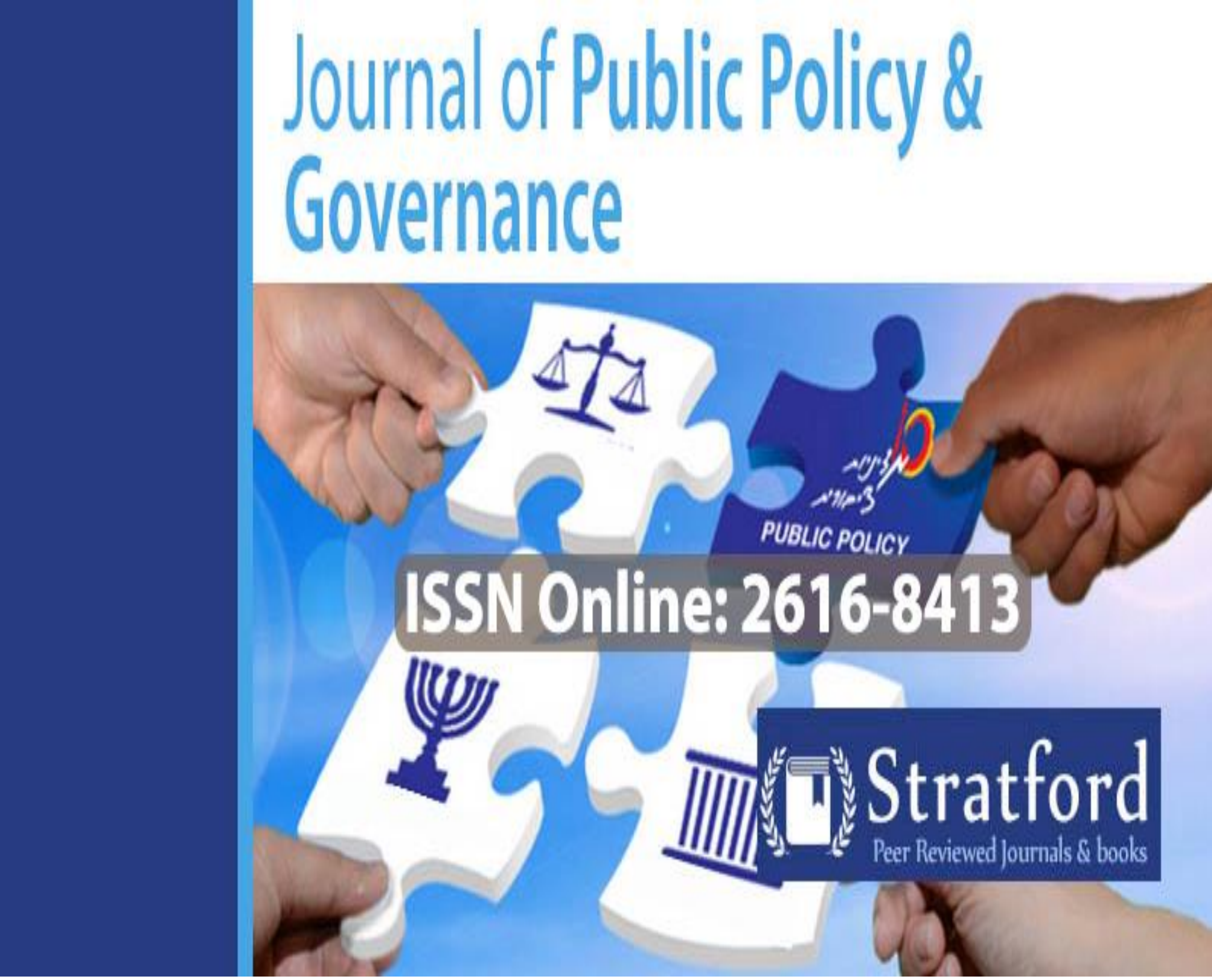

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ISSN: 2616-8413

Stratford Peer Reviewed Journals and Book Publishing
Journal of Public Policy & Governance
Volume 4||Issue 1||Page 29-52||August ||2020|
Email: info@stratfordjournals.org ISSN: 2616-8413

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***How to cite this article*: Mwasi, A., K. & Nyasaka, V., N. (2020). Corporate Governance Practices in Micro-Finance Institutions in Nairobi, Kenya, *Journal of Public Policy & Governance,* Vol. 4(1), 29-52.**

Abstract

Governance is about achieving corporate goals. For most MFIs, dual goals exist particularly the social and economic perspectives. In Kenya, good governance involves effective guidance of the board of MFIs to manage the management team by implementing the regulatory framework of the Microfinance Act of 2006 and developing systems and procedures. The regulators in Kenya have provided a clear directive which focuses on governance and management by introducing strict licensing and minimum capital requirements; capital adequacy rules; fiduciary responsibilities and standards regarding owners, directors and executive managers of MFIs; providing guidelines on risk management and related policies. Despite the efforts of the regulators, many of the MFIs have given very little attention to corporate governance and risk management, which affects their entire performance. MFIs face problems related with governance, emanating from internal and external factors that threaten their operational and financial sustainability. This paper established that most stakeholders are outsiders. This paper recommends that a competent and motivated board together with institutional capacity is critical to advancing CG in the microfinance sector. There is need to investigate expansion of the scope to cover new areas and clients considering MFIs already control a segment of the money market considered risky by main stream banks and the efforts of these MFIs in adopting best CG practices. Further investigation on how legal frameworks can be adapted so as to allow well-performing MFIs to mobilize savings while integrating governance systems and understanding their impact within the financial sector may be conducted

Key Words: *Corporate Governance practices, challenges, Microfinance Institutions, Kenya*

Stratford Peer Reviewed Journals and Book Publishing
Journal of Public Policy & Governance
Volume 4||Issue 1||Page 29-52||August ||2020|
Email: info@stratfordjournals.org ISSN: 2616-8413

1.1 Introduction

The importance of corporate governance lies in its contribution both to business prosperity and to accountability. Public companies are now among the most accountable organizations in society. They publish trading results and audited accounts; and they are required to disclose much information about their operations, relationships, remuneration and governance arrangements (Abdulazeez, Ndibe & Mercy, 2016). But the emphasis on accountability has tended to obscure a board's first responsibility to enhance the prosperity of the business over time. Business prosperity cannot be commanded, however, people, teamwork, leadership, enterprise, experience and skills are what really produce prosperity. There is no single formula to weld these together, and it is dangerous to encourage the belief that rules and regulations about structure will deliver success (Adams, Hermalin & Weisbach, 2010). Any definition of corporate governance needs to encompass fundamental values of transparency, accountability, fairness, and responsibility. The Association of Chartered Certified Accountants (ACCA) defines three main purposes of corporate governance, which are to ensure the board, as representatives of the organization's owners, protects resources and allocates them to make planned progress towards the organization's defined purpose, to ensure those governing and managing an organization account appropriately to its stakeholders, to ensure shareholders and, where appropriate, other stakeholders, can and do hold boards to account (Thomsen & Conyon, 2012).

Corporate governance is about how an organization is directed and controlled. It is about the structures and processes in place to facilitate and monitor effective management of an organization, including mechanisms to ensure legal compliance and prevent improper or unlawful behavior (Adegbite, 2012). The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources (Cretu, 2012). The aim is to align as nearly as possible the interests of individuals, corporations and society. Good corporate governance leads to development of a framework that provides adequate protection to the interests of stakeholders and reinforces the fiduciary responsibilities of those vested with the authority to act on behalf of the stakeholders (Chen & Wu, 2016). Corporate governance encourages companies and those who own and manage them to achieve their corporate objectives through a more efficient use of resources. Moreover, corporate governance framework should recognize the rights of stakeholders as established by law (Gompers, Ishii & Metrick, 2013). Corporate governance is a significant factor in improving economic efficiency and growth. It has been empirically tested that good governance practices of a company gives a positive signal to investors. With the globalization of markets, international capital flows have become extremely valuable source of external financing.

The performance of micro finance institution is depended on corporate governance structure. It is believed that good governance brings investor goodwill and confidence. Good corporate governance is important in increasing investor confidence and market liquidity that enhance the performance of the firm (Agola, 2014). Good corporate governance practices are important in reducing risk for investors; attracting investment capital and improving the performance of companies (Velnampy & Pratheepkanth, 2012). Corporate-governance mechanisms assure investors in MFIs that they will receive adequate returns on their investments. According to Priyanka Aggarwal (2013), corporate governance rating exerts positive impact on financial performance of firms. In this study, corporate governance practices include board size, board duality, board composition and board independence. CG is therefore, about building credibility, ensuring transparency and accountability as well as maintaining an effective channel of information disclosure that will foster good corporate performance (Labie & Mersland, 2011). Good corporate governance seeks to create an institutional framework that encourages all participants to contribute towards better corporate performance aligned with good governance practices.

Microfinance industry in Kenya is under the umbrella of Association of Microfinance Institutions (AMFI) of Kenya. The Association is a member's institution that was registered in 1999 under the societies Act by the leading microfinance institutions in Kenya to build capacity of the microfinance industry. AMFI presently has 52 member institutions serving more than 2,000,000 poor and middle class families with financial services throughout the country. The main objective of AMFI is provision of general policy guidelines, adherence to ethical practices and direction to the association (AMFI, 2011). Microfinance as it is known today is the provision of a broad range of financial services such as deposits, loans, payments services, money transfer and insurance to the poor and low-income households, and their micro-enterprises. The Microfinance Act authorizes the Central Bank of Kenya to license, regulate, and supervise the activities of formally constituted deposit-taking microfinance institutions in Kenya (Olick, 2015). The Act itself simply empowers the Central Bank as regulator, but specific rules subsequently released by the bank serve to govern microfinance activity in practice (AMFI, 2010). In particular, the Bank has imposed core capital requirements designed to ensure adequate liquidity of depository MFIs, and established minimum corporate governance standards and ownership limits.

In spite of the growth within the formal financial sector, they still do not reach 60% of the Kenyan adult population (FinAccess, 2009). Therefore, even though there are a large number of competitors in the market, the market itself is still under served. This lack of access can be explained by both the high cost of accessing financial institutions as well as the difficulties faced by Banks, SACCOs and MFIs in reaching rural areas not adequately served by existing infrastructure. Figure 1 shows access to financial services in Kenya.

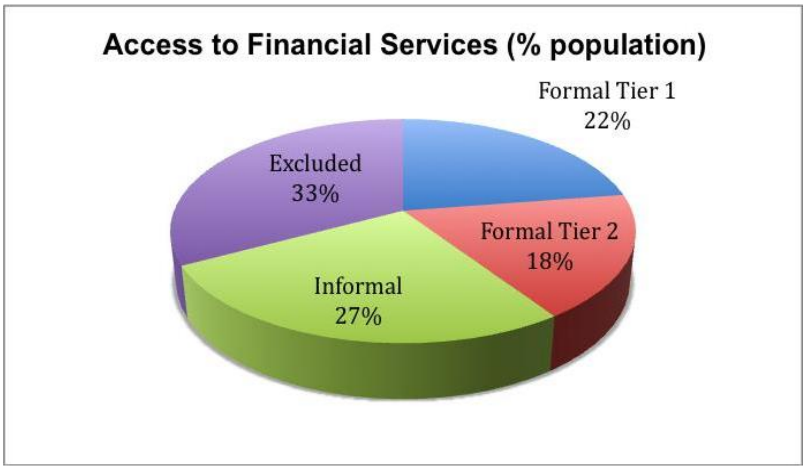

Figure 1 Access to financial services in Kenya

Source: (FinAccess, 2009)

MFIs normally combine a social mission provision of financial services to the lowest- income population possible with a financial objective that drives the institution to achieve self-sufficiency. The extent to which microfinance institutions seek to maintain the dual focus of profitability and outreach to poor clients is directly shaped by the composition of the boards of directors and by the priorities established by the board. These two objectives are not mutually exclusive, and that boards, through their strategic decisions and policies, can move institutions in the direction of achieving superior profitability and reaching an expanding clientele of low-income entrepreneurs.

1.2 Research Problem

Governance is a process that involves a system of check and balances between owners and other stake holders who set the standard and objectives of accountability of a given institution (Vishwakarma, 2015). Implementation and maintenance of good governance facilitates robust decision making and improves strategy, performance, compliance and accountability, and is characterized by ongoing monitoring and evaluation (Durgavanshi, 2014). Effective corporate governance helps an organization to achieve its objectives and desired outcomes and fulfill its obligations through sound Strategic and business planning, Risk management, financial management and reporting, human resource planning and control and compliance and accountability systems.

There are various studies undertaken in relation to the concept of corporate governance. The available studies do not directly address the corporate governance in Microfinance Institutions. Much of the existing research touch on corporate governance on companies listed at Nairobi Stock Exchange (NSE) and cooperative societies. Nandasaba (2010) has focused on corporate governance practices and performance of coffee farmers' cooperative societies in Bungoma, Otieno (2010) has also focused on corporate governance and firm performance in financial institutions for only the case firms listed in NSE and Kimanga (2010) has focused on corporate governance structures and practices at the Kenya revenue Authority. According to Mulili (2011) the international journal of business administration „corporate governance practices in developing countries a case for Kenya's has examined the concept of corporate governance while focusing on public universities in Kenya.

Investigating corporate governance practices in microfinance institutions is important because of the significant resources they leverage in regard to poverty alleviation. The study is also warranted by the scarcity of empirical research about developing strong governance structures within MFIs, where commercialization might increasingly override other governance issues (Momanyi & Ragama, 2017). MFIs have a dual mission of reaching poor clients and being financially sustainable, few MFIs are regulated, and several MFIs still depend on donor funding (Nawaz & Iqbal, 2015). Good corporate governance has been identified as a key bottleneck to strengthen the financial performance of MFIs and increase outreach of microfinance (Chenuos, Mohamed & Bitok, 2014; Hove-Sibanda, Sibanda & Pooe, 2017; Jørgensen, 2011), the influence of corporate governance on the MFIs' performance is not exhaustive.

In its broadest sense, corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources with the aim being to align as nearly as possible the interests of individuals, of corporations, and of society. The incentive to MFIs and to those who own and manage them is to adopt internationally accepted governance standards that will assist them to achieve their aims and to attract investment. This proposal aims to analyze governance mechanisms on a wide range of performance and risk measures using a unique data set spanning in 52 MFIs. This research seeks to addresses these challenges with an emphasis on the impact of governance mechanisms through strategic decision making processes in microfinance institutions (MFIs) dual missions of financial sustainability and providing banking services to micro-enterprises and low-income families.

1.3 Objectives of the Study

1. To establish the Corporate Governance practices adopted by Microfinance Institutions in in Kenya
2. To determine the challenges of implementing corporate governance best practices in the Microfinance Institutions in Kenya.

2.0 Literature Review

2.1 Corporate Governance Theories

This paper reviews the theoretical perspectives of a board's accountability that is relevant for this study. It draws on agency theory, stewardship theory, stakeholder theory, social contract theory, legitimacy theory and resource dependency theory.

2.1.1 Agency Theory

Jensen and Meckling (1976) developed the agency theory advancing that the agency relationship is a contract under which one or more persons (the principal) engages another person (the agent) to perform some services on their behalf.. Since the early work of Berle and Means (1932), corporate governance has focused upon the separation of ownership and controls which results in principal-agent problems arising from the dispersed ownership in the modern corporation. They viewed corporate governance as a mechanism where a board of directors is an essential monitoring device to minimize the problems brought about by the principal-agent relationship (Darus, & Mohamed, 2011). In this context, agents are the managers, principals are the owners and the board of directors act as the monitoring mechanism (Kiel & Nicholson, 2013). Furthermore, literature on corporate governance attributes two factors to agency theory. The first factor is that corporations are reduced to two participants, managers and shareholders whose interests are assumed to be both clear and consistent.

A second notion is that humans are self-interested and unwilling to sacrifice their personal interests for the interests of the others (Daily, Dalton & Cannella, 2003). The firm is not an individual but a legal fiction, where conflicting objectives of individuals are brought into equilibrium within a framework of contractual relationships. These contractual relationships are not only with employees, but with suppliers, customers and creditors (Jensen & Meckling, 1976). The agency role of the directors refers to the governance function of the board of directors in serving the shareholders by ratifying the decisions made by the managers and monitoring the implementation of those decisions. According to the perspective of agency theory the primary responsibility of the board of directors is towards the shareholders to ensure maximization of shareholder value.

2.1.2 Stewardship Theory

In contrast to agency theory, stewardship theory presents a different model of management, where managers are considered good stewards who will act in the best of the owners (Donaldson & Davis, 1991). The fundamentals of stewardship theory are based on social psychology, which focuses on the behavior of executives. The steward's behavior is pro-organizational and collectivistic, and has higher utility than individualistic self-serving behavior and the steward's behavior will not depart from the interest of the organization because the steward seeks to attain the objectives of the organization (Davis, Schoorman &

Donaldson, 1997). According to Smallman (2004) where shareholders wealth is maximized, the steward's utilities are maximized too, because organizational success will serve most requirements and the stewards will have a clear mission. He also states that, stewards balance tensions between different beneficiaries and other interest groups. Therefore stewardship theory is an argument put forward for firm performance that satisfies the requirements of the interested parties resulting in dynamic performance equilibrium for balanced governance.

2.1.3 Stakeholder Theory

Research into corporate governance also discusses the stakeholder theory in relation to firms' responsibility to the wider community. A stakeholder is any group of individuals who can affect or is affected by the activities of the firm, in achieving the objectives of the firm (Freeman, 1984). A similar view has been put forward by the World Business Council for Sustainable Development (1999), which also identifies stakeholders as the representatives from labor organizations, academia, church, indigenous peoples, human rights groups, government and non-governmental organizations and shareholders, employees, customers/consumers, suppliers, communities and legislators.

According to Ansoff (1965), a firm's objective could be achieved through balancing the conflicting interests of these various stakeholders. Therefore, a fundamental aspect of stakeholder theory is to identify the stakeholders an organization is responsible for. Any stakeholder is relevant if their investment is, in some form, subject to risk from the activities of the organization (Clarkson, 1995). The moral perspective of stakeholder theory is all stakeholders have a right to be treated fairly by an organization, and managers should manage the organization for the benefit of all stakeholders, regardless of whether the stakeholder management leads to better financial performance (Deegan, 2004).

2.1.4 Resource Dependency Theory

Lawrence and Lorsch (1967) link the resource dependency theory to corporate governance. They state that successful organizations possess internal structures that match environmental demand, which links to Pfeffer's (1972) argument that board size and composition is a rational organizational response to the conditions of the external environment. Furthermore, directors may serve to connect the external resources with the firm to overcome uncertainty (Hillman, Cannella & Paetzols, 2000), because coping effectively with uncertainty is essential for the survival of the company. According to the resource dependency role, the directors bring resources such as information, skills, key constituents (suppliers, buyers, public policy decision makers, social groups) and legitimacy that will reduce uncertainty (Gales & Kesner, 1994).

Thus Hillman *et al.* (2000) consider the potential results of linking the firm with external environmental factors and reducing uncertainty is the reduction of transaction cost associated with external linkage. This theory supports the appointment of directors to multiple boards because of their opportunities to gather information and network in various ways.

Social contract theory is rooted in two opposing perspectives concerning human nature and justifications for the origin of the democratic political state. The social contract framework began in the seventeenth century with the individualist political theories of Hobbes (1651/1996) and Locke (1690/1980). These two social contract political philosophers argued for the primacy and advantages of political liberty, individual autonomy, self-interest, and individual rights over traditional expositions of political and economic obligations innately owed to sovereign and ecclesiastic authorities.

The social contract theory sees society as a series of social contracts between members of society and society itself (Gray, Owen & Adams, 1996). There is a school of thought which sees social responsibility as a contractual obligation the firm owes to society (Donaldson, 1983). Social contract theory was developed by Donaldson and Dunfee (1999) as a way for managers to make ethical decision making, which refers to macro- social and micro-social contracts. The former refers to the communities and the expectation from the business to provide support to the local community, and the latter refers to a specific form of involvement.

2.1.5 Legitimacy Theory

Another theory reviewed in corporate governance literature is legitimacy theory. Legitimacy theory is defined as "a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate with some socially constructed systems of norms, values, beliefs and definitions" (Suchman, 1995). Legitimacy theory is based upon the notion that there is a social contract between the society and an organization. A firm receives permission to operate from the society and is ultimately accountable to the society for how it operates and what it does, because society provides the authority to own and use natural resources and to hire employees (Deegan, 2004). The emphasis of legitimacy theory is that an organization must consider the rights of the public at large, not merely the rights of the investors. Failure to comply with societal expectations may result in sanctions being imposed in the form of restrictions on firms operations, resources and demand for its products (Deegan, 2004).

Business operations face on-going change, as do the needs and expectations of stakeholders and society. Therefore, corporations have to manage their strategies and practices in order to retain their perceived legitimacy. Problems arise when organizations become out-of-date with societal values and understandings, or are confronted by a multiplicity of stakeholders with ambiguous, conflicting and inconsistent demands and different interpretations of what are the most appropriate organizational structures and practices (Wilmshurt & Frost, 2000). The studies of Pattern (1992), Deegan (2002) and Ogden and Clarke (2005) identified a range of strategic postures employed by managers (involving assertive, tactic and defensive techniques) to manage stakeholders' perceptions.

2.2 Corporate Governance in Microfinance Institutions

The experience of corporate governance for deposit taking MFIs is drawn from best practices of any organization or share company, particularly commercial banks, which should be customized to features and environment and address the specific problems of these institutions (Adekunle & Aghedo, 2014). Corporate governance is the process by which a board of directors, through management, guides an MFI in fulfilling its corporate mission and protects the institution's assets over time (Cretu, 2012).

Effective governance occurs when a board provides proper guidance to management regarding the strategic direction for the institution, and oversees management's effort to move in the direction of the approved strategy (Alagathurai & Nimalathashan, 2013). The board carries out this function on behalf of a third party, referred to as shareholders in the case of for-profit corporations. Because of there are no owners in non-profit corporations, that third party in not as easily identified to include the corporation's clients, staff board, and donors (Adeusi, 2013). The fundamental to good governance is the ability of individual board of directors to work with each other to accomplish an effective balance between strategic and operational responsibilities (Alimehmeti & Paletta, 2014). The interplay between board and management centers on this relationship between strategy and operation, and assumes that both of these components are essential for the successful evolution of the institution.

Good governance in the Kenyan deposit taking MFIs plays an important role in increasing outreach, improving transparency, accountability, sustainability, profitability, efficiency, effectiveness, responsibility and responsiveness to the changing environments. Effective governance depends on both forms- the structures and processes of control, and content-and the specific individuals involved, particularly in the leadership (Cherotich, 2011). The board, which plays a critical role in ensuring good governance of MFIs, has five major responsibilities, namely: Legal obligations: this includes understanding the regulatory framework of MFIs and compliance with bylaws, procedures, legal requirements which are clearly stated in the microfinance Act (Microfinance ACT, 2006).

Relationship between board and executives which mainly includes operational distance of the board from day to day operations, drawing on the institutional memory of the directors and making binding decisions as a board (Bonna, 2011). Apart from this role, the board must ensure management accountability by bringing competent professionals as executives, establishing clear goals for their performance, monitoring performance closely, and confronting weaknesses when these surface (Labie & Mersland, 2011). Setting policy and providing strategic direction consistent with the MFI, mission, vision and objectives. Fiduciary obligation to ensure that the financial solvency of MFIs is maintained. This is a very serious responsibility of board of especially in the Kenyan context of MFIs, as most MFIs are turning into deposit taking from the public (Momanyi & Ragama, 2017). The board must be able to assess the risks associated with the provision of financial services. Board assessment of its own performance is a major responsibility which should be exercised on regular basis.

According to Baker and Anderson, (2010), the key elements of sound corporate governance in an MFI include: well-articulated corporate strategy against which the overall success and the contribution of individuals can be measured. Setting and enforcing clear assignment of responsibilities, decision making authority and accountabilities that is appropriate for the risk profile. A strong financial risk management function (independent of business lines) adequate internal control system (including internal and external audit function) and functional process design with the necessary checks and balances (Capital Markets Authority, 2011). Corporate values, codes of conduct and other standards of appropriate behavior and effective system used to insure compliance. This includes special monitoring of the risk exposures of MFIs where conflicts of interest are expected to appear (e.g. relationships with affiliated parties). Financial and managerial incentives to act in an appropriate manner offered to the board of management and employees including compensation, promotion and penalties (i.e. compensation should be consistent with the MFIs objective performance and ethical values). Transparency and appropriate information flows internally and to the public.

2.3 Challenges of Implementing Corporate Governance Best Practices

Corporate governance is concerned with the processes, systems, practices and procedures as well as the formal and informal rules that govern institutions, the manner in which these rules and regulations are applied and followed, the relationships that these rules and regulations determine or create, and the nature of those relationships (Bayero, 2018). It also addresses the leadership role in the institutional framework. Corporate Governance, therefore, refers to the manner in which the power of a corporation is exercised in the stewardship of the corporation's total portfolio of assets and resources with the objective of maintaining and increasing shareholder value and satisfaction of other stakeholders in the context of its corporate mission.

Corporate governance implies that companies not only maximize shareholders wealth, but balance the interests of shareholders with those of other stakeholders, employees, customers, suppliers, and investors so as to achieve long-term sustainable value (Bonna, 2011). There is a need for effective and sound regulatory framework for various aspects of corporate governance. There is a need for legislative enactment or decree that establishes a regulatory agency, and indicates its functions, including its enforcement powers. ACCA recognizes that corporate governance evolves and improves over time (Tshipa & Mokoaleli-Mokoteli, 2015). We accept that organizations in different sectors and across the world operate in diverse environments in terms of culture, regulation, legislation and enforcement. What is appropriate, in terms of governance, for one type of organization will not be appropriate to all organizations (OECD, 2004).

The regulatory process consists of setting the rules or standards, monitoring compliance and enforcement (Villanueva-Villar, Rivo-Lopez, & Lago-Peñas, 2016). The regulatory challenge relate to capital adequacy standards for international banks, accounting and auditing standards for corporations, regulations governing business practices etc. A particular difficulty in Africa for example, in designing and implementing appropriate regulatory, enforcement and incentive regime is the lack of skills and institutional capacity to do so. The commitment of government and the leadership is an overriding factor in transition economies where environment conducive to corporate governance has to be created to ensure enterprise sustainability (Vishwakarma, 2015). Where there are companies with controlling shareholders the most effective governance mechanism is for the institution of a set of legal rules that control managerial behaviour and protect minority shareholders.

According to the World Bank's (2003) report on corporate governance, most developing and transition economies have failed to enforce laws, rules, and regulations regarding corporate governance consistently and evenly. This failure was perhaps not anticipated by the OECD principles, which implicitly assume that countries have an efficient legal and regulatory framework in place and those courts and securities regulators have the means and capabilities to enforce it. Practices such as self-dealing and insider trading are widespread. Such offenses mostly go unpunished, even if stiff penalties apply in theory (Xavier, *et al.,* 2015). According to the report, auditing is another major area of weakness in corporate governance enforcement. Most countries delegate the setting of accounting and auditing standards to the accounting association (World Bank, 2003).

However, professional associations usually lack the means to impose effective sanctions on their members. Auditors have been given unqualified opinions, certifying that the accounts audited provide a true and fair picture despite the many defects noted. The penalties for such behavior are minor and enforcement is generally lax. In most countries especially in SSA the capacity to support the implementation of good corporate governance is undermined by the existence of weak monitoring and enforcement (Otobo, 1997). Government departments and independent regulators responsible for monitoring corporate governance do not as yet fulfill their roles as overseers. Many are generally weak and subject to external influence by politicians and lawmakers. Community watchdog organizations such as consumer bodies are not well developed in Africa (Botha, 2001). There is a need for legislative overhaul or decree that establishes a regulatory agency and indicates its functions, including its enforcement powers.

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Volume 4||Issue 1||Page 29-52||August ||2020|
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3.0 Research Methodology

This was a descriptive study designed to gather data from Chief Executive Officers in Microfinance Institutions in Kenya in order to understand better corporate governance practices in those institutions and how strategic decision making processes can be adopted. The population of interest in this study was the Microfinance Institutions in Kenya. According to Association of Microfinance Institutions, there are 52 registered Microfinance Institutions in Kenya. In this study, the researcher will use census study of the 52 MFIs located in Nairobi. Census is the method where every member of the population is included in the enumeration. The units of observation were the senior managers or their deputies among the 52 registered MFIs in Kenya. This is because they were the most appropriate to respond to the objectives of this study. The data was collected using a structured questionnaire designed along the objectives of the study. Sources used to gather secondary data were document analysis collected from published and unpublished company documents, subject-relevant literature and internal monthly journals/magazines from the MFIs.

Data obtained was subjected to quantitative analysis. Quantitative data is based on descriptive statistics using non-statistical techniques on subjective statements and explanation. The results of the study were presented using frequency tables, percentages and pie charts.

4.0 Research Findings and Discussions

Out of the targeted 52 MFIs to, all of whom the questionnaires were administered, 23 filled and returned the questionnaires resulting to a response rate of 44.2% which was considered adequate for analysis.

4.1 Corporate Governance Practices in MFIs in Nairobi

One of the objectives of this paper was to establish the Corporate Governance practices in MFIs in Nairobi. To achieve this objective, respondents were presented with descriptive statements of the various Corporate Governance practices and were required to indicate in a 5-point scale the extent to which the statement apply to their institutions. The descriptive statements were adopted from the Corporate Governance code of best practices developed by OECD, CGAP and MFI Act No. 19 of 2006. These Corporate Governance best practices relate to the role and functions of the board: - board membership and committees: appointment, selection, disclosures and removals of directors: evaluation of the board and audit committees.

Good corporate governance seeks to create an institutional framework that encourages all participants to contribute towards better corporate performance aligned with good governance practices. Basically this is a set of relationships between a company's board, management, its shareholders and the society within an institutional framework. These relationships evolve into the corporate governance framework, which is “the system by which companies are directed and controlled.

4.1.1 Role and Functions of the Board

From the findings tabulated in Table 4.5, 70% of the respondents indicated that the board establishes a formal and transparent arrangement for shareholders to effect the appointment of independent auditors at each annual general meeting (a mean of 3.91), 61% stated that the board ensures that the institution will survive, thrive and continue as a viable going concern (mean 4.00); 57% of the respondents either stated that the board ensures that accounts are presented in line with International Accounting Standards (IAS); or the board identifies key risk areas and key performance indicators of the business and monitors these factors with a mean of 4.04 and 4.13 respectively) and 52% of the respondents stated that there is a clear separation of the role and responsibilities of the chairman and chief executive, which ensures a balance of power of authority and provide for checks and balances this had a standard deviation of (0.850).

The board of directors acts as a fulcrum between the owners and controllers of a corporation and is a crucial a link between the shareholders who are providers of capital, and the managers who are the individuals who use that capital to create value (Monks & Minow, 2001). They are elected by the shareholders of the firm and have a fiduciary role in relation to fulfilling their responsibilities towards the shareholders they represent. Their duties and responsibilities involve hiring, firing, compensating employees and advising top management (Denis, 2001). Boards can consist of a mix of inside and outside directors. Inside directors are those that are linked with the controlling shareholders and are those that hold senior positions in the firm. On the other hand, outside directors are not employees of the firm. They owe their position on the board due the specific expertise which they possess in areas that are valuable to firm.

Table 2 Role and functions of the board

Role and the functions of the board	Response	Frequency	Percent	Mean	Std Deviation
The board monitors and evaluates the implementation of strategies, policies, management performance criteria and business plans.	Not at all	0	0	4.17	0.778
	Less extent	1	4.3		
	Moderate extent	2	8.7		
	Large extent	12	52.2		
	Very large extent	8	34.8		
The Board ensures that the institution complies with the relevant laws, regulations and codes of best business practice	Not at all	0	0	4.21	0.850
	Less extent	1	4.3		
	Moderate extent	3	13		
	Large extent	9	39.1		
	Very large extent	10	44%		
There is a clear separation of the role and responsibilities of the chairman and chief executive, which will ensure a balance of power of authority and provide	Not at all	0	0	3.95	0.878
	Less extent	2	8.7		
	Moderate extent	3	13.0		
	Large extent	12	52.2		
	Very large extent	6	26.1		
There is a shareholders participation in major decisions of the Company.	Not at all			3.83	1.114
	Less extent	5	21.7		
	Moderate extent	1	4.3		
	Large extent	10	43.5		
	Very Large extent	7	30.4		
The board serves the legitimate interest of the shareholders and the corporation and account to them fully.				3.91	0.996
	Not at all	0	0		
	Less extent	3	13.0		
	Moderate extent	3	13.0		
	Large extent	10	43.5		
	Very large extent	7	30.4		
The board regularly reviews				4.04	0.878

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Journal of Public Policy & Governance
Volume 4||Issue 1||Page 29-52||August ||2020|
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processes and procedures to ensure the effectiveness of its internal systems of control.	Not at all	0	0		
	Less extent	2	8.7		
	Moderate extent	2	8.7		
	Large extent	12	52.2		
	Very large extent	7	30.4		
The board ensures that accounts are presented in line with International Accounting Standards.					
	Not at all	0	0	4.13	0.757
	Less extent	1	4.3		
	Moderate extent	2	8.7		
	Large extent	13	56.5		
	Very large extent	7	30.4		
The board establishes a formal and transparent arrangement for shareholders to effect the appointment of independent auditors at each annual general	Not at all	1	4.3	3.91	0.900
	Less extent	1	4.3		
	Moderate extent	1	4.3		
	Large extent	16	69.6		
	Very large extent	4	17.4		
The board establishes relevant Committees and delegate specific mandates to such committees as is necessary.	Not at all	2	8.7	7.43	12.037
	Less extent	2	8.7		
	Moderate extent	3	13.0		
	Large extent	10	43.5		
	Very large extent	6	26.1		
The board identifies key risk areas and key performance indicators of the business and monitors these factors.	Not at all			3.88	0.902
	Less extent	3	13.0		
	Moderate extent	3	13.0		
	Large extent	13	56.5		
	Very large extent	4	17.4		
The board ensures that the institution will survive, thrive and continue as a viable going concern.	Not at all	0	0	4.00	0.738
	Less extent	1	4.3		
	Moderate extent	3	13.0		
	Large extent	14	60.9		
	Very large extent	5	21.7		

Regulation and supervision of the microfinance sector; this has led to quality growth, broaden the funding base for MFIs eligible to mobilize and administer deposits, offer credit facilities and other financial services and initiate the process of integrating these institutions into the formal financial process. Omino, (2005) stated that the regulation of the sector enables authorities define procedures for their operations, entrance, exit and ultimately create an environment for fair competition and efficiency in the sector. On the other hand, supervision encompasses all means by which regulators enforce compliance with a given legal and regulatory framework. In supervising MFIs, the line ministries using risk based approach; must understand the risk profile of different financial institutions dealing with different products and clients while ensuring that they have the ability to assess the adequacy of the measures taken to mitigate these risks. This agrees with the world-wide trend of MFIs desire to introduce/offer more products leading to conversion to commercial banking (CGAP, 2006).

On CG practices in MFIs in Nairobi, this study establishes that strategic decision makers are often members of board of directors of organizations. This is because one of the roles of the board is formulating strategies for the organizations. From the governance perspective, in order for the board to make strategic decisions, its composition in terms of size and diversity should be taken into consideration. Good composition and execution of the board duties allows the members to bring their expertise and different perspectives to the organization and to aid strategic decisions.

4.1.2 Board Membership and Committees

This study established that the findings were skewed either to a large extent or a very large extent in regard the statement. Hansmann (1996) argues that the difference between ownership types lies in who controls the organization and who receives the profit from it. In a shareholder firm, the shareholders control the organization, decide on how to distribute the profits, and are free to sell their privileges. The governance role of board of directors regards the issue of the separation of company ownership and management of companies which has characterized the modern corporation, while the boards of directors have for a long time been identified as the representatives of shareholders. However, recent observers now concur that the current boards of directors do represent an array of other stakeholders as well. It is due to this representation that the board acts as a governance organ. It has also been observed that the boards of directors have advantage over the other channels of governance, in that they are internally recognized and bear legal authority to oversee the company. Internal controls are designed, among other things, to ensure that each key risk has a process or other measure to help contain or control that risk and that such process or measure is being applied and works as intended. As such, internal controls help ensure process integrity, compliance and effectiveness

Table 3: Board membership and committees

Board membership and	Response	Frequency	Percent	Mean	Std
The organization is managed by a board which has at least two thirds of its members being non-executive	Not at all	2	8.7%	3.85	1.01
	Less extent	3	13.0%		
	Moderate extent	3	13.0%		
	Large extent	9	39.1%		
	Very large extent	6	26.1%		
An audit and credit committees has been constituted	Not at all	2	8.7%	3.64	1.13
	Less extent	3	13.0%		
	Moderate extent	4	17.4%		
	Large extent	9	39.1%		
	Very large extent	5	21.7%		
There is an assets and liabilities committee to drive the strategy for the institution in terms of the mix of assets and liabilities	Not at all	2	8.7%	3.68	1.17
	Less extent	3	13.0%		
	Moderate extent	4	17.4%		
	Large extent	8	34.8%		
	Very large extent	6	26.1%		
The chief executive officer and the chairperson of the board are not a member of the audit committee	Not at all	2	8.7%	3.77	1.19
	Less extent	3	13.0%		
	Moderate extent	3	13.0%		
	Large extent	8	34.8%		
	Very large extent	7	30.4%		
The committee elects a chairperson among	Not at all	3	13.0%	3.76	1.13
	Less extent	2	8.7%		

themselves who is a non-executive director	Moderate extent	4	17.4%		
	Large extent	8	34.8%		
	Very large extent	6	26.1%		
The quorum for meetings are at least two-thirds of the committee members where at least one attendee must be a non-executive director	Not at all	1	4.3%	3.86	1.255
	Less extent	3	13.0%		
	Moderate extent	3	13.0%		
	Large extent	6	26.1%		
	Very large extent	9	39.1%		
Every committee reports to the board at least every three months	Not at all	2	8.7%	3.64	1.22
	Less extent	4	17.4%		
	Moderate extent	3	13.0%		
	Large extent	8	34.8%		
	Very large extent	6	26.1%		
No person shall hold the position of a director in more than one institution, unless the institution are subsidiaries or holding company of the	Not at all	2	8.7%	3.50	1.34
	Less extent	4	17.4%		
	Moderate extent	3	13.0%		
	Large extent	7	30.4%		
	Very large extent	6	26.1%		
The Board has a balanced mix of Executive, Non-Executive and Independent Non-Executive Directors	Not at all	3	13.0%	4.50	4.07
	Less extent	3	13.0%		
	Moderate extent	3	13.0%		
	Large extent	9	39.1%		
	Very large extent	5	21.7%		
The terms of reference of each of committee are restricted and defined.	Not at all	2	8.7%	3.68	1.21
	Less extent	4	17.4%		
	Moderate extent	2	8.7%		
	Large extent	9	39.1%		
	Very large extent	6	26.1%		
There is a formal and transparent procedure in the appointment of directors to the board	Not all	1	4.3%	3.73	1.20
	Less extent	6	26.1%		
	Moderate extent	1	4.3%		
	Large extent	8	34.8%		
	Very large extent	7	30.4%		
The CEO is appointed by the board whose terms and conditions of service are determined by the board in the contract letter	Not at all			3.87	1.25
	Less extent	6	26.1%		
	Moderate extent	1	4.3%		
	Large extent	6	26.1%		
	Very large extent	10	43.5%		
The CEO is not appointed without the prior approval of the Central Bank (in case of deposit taking MFI)	Not at all	1	4.3%	3.59	1.26
	Less extent	7	30.4%		
	Moderate extent	2	8.7%		
	Large extent	6	26.1%		
	Very large extent	7	30.45		
The board formally reviews its composition and performance at least every year to ensure that the mix of	Not at all			3.74	1.18
	Less extent	6	26.1%		
	Moderate extent	1	4.3%		
	Large extent	9	39.1%		

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membership is appropriate	Very large extent	7	30.4%		
The nominations committee recommends to the board qualified, competent fit and proper persons to be nominated for election to the	Not at all	1	4.3%	5.43	8.26
	Less extent	5	21.7%		
	Moderate extent	1	4.3%		
	Large extent	11	47.8%		
	Very large extent	5	21.7%		
Boards appointments are made that provide a mix of proficient	Not at all	0	0	3.69	1.11
	Less extent	5	21.7%		
directors each of whom is able to add value and bring independent judgment to bear	Moderate extent	3	13.0%		
	Large extent	9	39.1%		
	Very large extent	6	26.15		
All persons offering themselves for appointment, as directors disclose any potential area of conflict that may undermine their position or	Not at all	0	0	3.61	1.16
	Less extent	6	26.1%		
	Moderate extent	3	13.0%		
	Large extent	8	34.8%		
	Very large extent	6	26.1%		
All directors submit themselves for re-election at regular intervals and at least once every three years	Not at all	2	8.7%	3.48	1.38
	Less extent	5	21.7%		
	Moderate extent	3	13.0%		
	Large extent	6	26.1%		
	Very large extent	7	30.4%		
Service contracts of executive directors do not exceed three years but these are renewable with the approval of shareholders on the	Not at all	2	8.7%	3.52	1.34
	Less extent	4	17.4%		
	Moderate extent	4	17.4%		
	Large extent	6	26.1%		
	Very large extent	7	30.4%		
All directors disclose in good faith to the board for recording and disclosure to the external auditors, any business of other interests that are likely to	Not at all	1	4.3%	3.61	1.20
	Less extent	4	17.4%		
	Moderate extent	4	17.4%		
	Large extent	8	34.8%		
	Very large extent	6	26.1%		
When a director resigns or is removed from office before the expiry of his term, he discloses to the external auditors and to the shareholders	Not at all			3.57	1.04
	Less extent	5	21.7%		
	Moderate extent	4	17.4%		
	Large extent	10	43.5%		
	Very large extent	4	17.4%		

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Journal of Public Policy & Governance
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4.2.3 Evaluation of the Effectiveness of the Board and Audit Committees

This study sought to find out the various responses on CG practices in relation to evaluation of the effectiveness of the board and audit committees where: 1 represents Not at all; 2- To a less extent; 3- To a moderate extent; 4- To a large extent and 5- To a very large extent. 57% of the respondents indicated that the board's meeting agenda clearly reflects our strategic plan or priorities to a large extent mean= 3.91; 53% of the respondents stated that their organization has a three to five-year strategic plan or a set of clear long range goals and priorities to a large extent; to a less extent, 9% indicated that board members are aware of what is expected of them.

Table 4: Evaluation of the effectiveness of the board and audit committees

Evaluation of the effectiveness of the Board and Audit Committees	Response	Frequency	Percent	Mean	Std Deviation
How would you describe the contributions or accomplishments of the Board over the past year?	Not at all	4	17.4%	4.05	.779
	Less	1	4.3%		
	Moderate	2	8.7%		
	To a large	11	47.8%		
	Very large	5	21.7%		
Our organization has a three to five-year strategic plan or a set of clear long range goals and priorities	Not at all	1	4.3%	3.91	.900
	Less	1	4.3%		
	Moderate	2	8.7%		
	To a large	12	52.2%		
	Very large	7	30.4%		
The board's meeting agenda clearly reflects our strategic plan or priorities.	Not at all	0	0	3.91	.900
	Less	2	8.7%		
	Moderate	3	13.0%		
	To a large	13	56.5%		
	Very large	5	21.7%		
The board gives direction to staff on how to achieve the goals primarily by setting or referring to policies	Not at all	0	0	3.87	.919
	Less	2	8.75		
	Moderate	4	17.4%		
	To a large	11	47.8%		
	Very large	6	26.1%		
The board ensures that the organization's accomplishments and challenges are communicated to members and stakeholders	Not at all	0	0	3.87	.815
	Less	2	8.7%		
	Moderate	5	21.7%		
	To a large	10	43.7%		
	Very large	6	26.1%		
The board has ensured that members and Stakeholders have received reports on how our organization has used its financial and human resources.	Not at all	0	0	3.83	.937
	Less	1	4.3%		
	Moderate	6	26.1%		
	To a large	11	47.8%		
	Very large	5	21.7%		
It seems like most board members come to meetings prepared	Not at all	2	8.1%	3.87	9.19
	Less	5	21%		
	Moderate	0	0		
	Large	10	44.0%		

	Very large	6	26.1%		
There is a clear understanding of where the board's role ends and the Executive Director's begins	Not at all	0	0	3.74	1.01
	Less	4	17.4%		
	Moderate	3	13.0%		
	Large	11	47.8%		
	Very large	5	21.7%		
The board has developed formal criteria and a process for evaluating the Executive Directors	Not at all	0	0	3.87	.920
	Less	2	8.7%		
	Moderate	5	21.7%		
	Large	10	43.5%		
	Very large	6	26.1%		
The Chair is skilled at managing different points of view	Not at all	0	0	3.78	.109
	Less	4	17.4%		
	Moderate	4	17.4%		
	Large	8	34.8%		
	Very large	7	30.4%		
Is the board functioning properly; are meetings held regularly and run efficiently, do discussions allow for different viewpoints to be expressed	Not at all	0	0	3.61	.941
	Less	4	17.4%		
	Moderate	4	17.4%		
	Large	12	52.2%		
	Very large	3	13.0%		

On the issue of evaluation of the effectiveness of the board and audit committees, these findings are supported by literature that states, at its best, the internal board auditor provides independent, objective assessments on the appropriateness of the organization's internal governance structure and the operating effectiveness of specific governance activities. This activity should be value enhancing. Policy papers for MFIs stress the importance of internal audit and recommend that the internal auditor reports directly to the MFI board (Steinwand, 2000). Thus, an MFI allowing their internal auditors to report directly to the board should show higher financial performance. Information variables could also include CEO experience and educational background as well as stakeholder representatives. A more experienced CEO is likely to bring better and more relevant information to the board's attention. Likewise, representatives of employees and customers should enhance the MFIs knowledge of its markets, and also, help to align the stakeholders to the MFI mission.

4.2 Challenges of Implementing Corporate Governance Best Practices

From the findings tabulated in Table 4.9 show that the various challenges highlighted were either not in existence or were to a less extent affecting MFIs. The highest mean

2.05 indicated that there was hardly a conflicting role of government. Corporate governance implies that companies not only maximize shareholders wealth, but balance the interests of shareholders with those of other stakeholders, employees, customers, suppliers, and investors so as to achieve long-term sustainable value. There is a need for effective and sound regulatory framework for various aspects of corporate governance. There is a need for legislative enactment or decree that establishes a regulatory agency, and indicates its functions, including its enforcement powers.

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Table 5: Challenges faced in the implementation of corporate governance practices

Challenges faced in the implementation of corporate governance practices	Response	Frequency	Percent	Mean	Std Deviation
Lack of independence within the Board	Not at all	12	52.0%	1.86	1.256
	Less	5	21.7%		
	Moderate	3	13.0%		
	Large	2	8.7%		
	Very large	1	4.3%		
Political interference at the Board level	Not at all	9	39.1%	1.91	1.064
	Less	9	39.1%		
	Moderate	2	8.7%		
	Large	1	4.3%		
	Very	2	8.7%		
Insufficient monitoring regimes by shareholders	Not at all	9	39.1%	1.73	.702
	Less	10	43.5%		
	Moderate	3	13.0%		
	Large	1	4.3%		
	Very	0	0		
Conflicting roles of government	Not at all	7	30.4%	2.05	1.056
	Less	10	43.5%		
	Moderate	3	13.0%		
	Large	1	4.3%		
	Very	2	8.7%		
Lack of commitment and leadership	Not at all	12	52.2%	1.45	.511
	Less	10	43.5%		
	Moderate	1	4.3%		
	Large				
	Very				
Failure by boards to understand the risks the institution is taking	Not at all	10	43.5%	2.05	2.13
	Less	10	43.5%		
	Moderate	1	4.3%		
	Large	2	8.7%		
	Very				
Boards allowing transactions that benefit a few at the expense of the many	Not at all	12	52.2%	1.50	.598
	Less	9	39.1%		
	Moderate	1	4.3%		
	Large	1	4.3%		
	Very	0	0		
Management of conflict of interest and codes of ethics	Not at all	12	52.2%	1.55	.671
	Less	8	34.8%		
	Moderate	2	8.7%		
	Large	1	4.3%		
	Very	0	0		
Incompetent audit committee	Not at all	12	52.2%	1.60	.796

	Less	8	34.8%		
	Moderate	1	4.3%		
	Large	1	4.3%		
	Very	1	4.3%		
Corporate culture which fosters unethical behavior which discourages difficult questions from being asked	Not at all	9	39.1%	1.90	1.064
	To a less	9	39.1%		
	Moderate	2	8.7%		
	Large	1	4.3%		
	Very	2	8.7%		
Influence by mission and vision of mother NGO	Not at all	10	43.5%	1.86	1.082
	Less	8	34.8%		
	Moderate	2	8.7%		
	Large	1	4.3%		
	Very	1	4.3%		
Irregular board meetings placing huge responsibilities on management	Not at all	10	43.5%	1.72	.935
	To a less	10	43.5%		
	Moderate	1	4.3%		
	Large	1	4.3%		
	Very	1	4.3%		
Incompetency of some board members in terms of diversified skills and effectiveness in guiding the senior managers.	Not at all	10	43.5%	1.59	.590
	To a less	11	47.8%		
	Moderate	1	4.3%		
	Large	1	4.3%		
	Very	0	0		
The structure of ownership and governance making the role of regulators much difficult	Not at all	8	34.8%	1.86	.940
	To a less	11	47.8%		
	Moderate	2	8.7%		
	Large	1	4.3%		
	Very	1	4.3%		
Lack of prudential guidelines for Microfinance Institutions	Not at all	6	26.1%	2.00	.925
	Less	12	52.2%		
	Moderate	3	13.0%		
	Large	1	4.3%		
	Very	1	4.3%		
Lack of independence between the chairman of the board and the CEO	Not at all	8	34.8%	1.77	.751
	Less	12	52.2%		
	Moderate	1	4.3%		
	Large	1	4.3%		
	Very	1	4.3%		
Lack of transparency and accountability	Not at all	6	26.1%	1.77	.528
	Less	15	65.2%		
	Moderate	1	4.3%		
	Large	1	4.3%		
	Very	0	0		

Among the key challenges that this study established in regard to challenges while undertaking CG practices were management of conflict of interest and codes of ethics, boards allowing transactions that benefit a few at the expense of the many, lack of commitment and leadership and incompetent audit committees. Regarding challenges of implementing CG best practices, the literature on the performance of MFIs in regard to implementation of CG practices has generally not been concerned with the effect of ownership type. However, Hartarska (2005) in her study on corporate governance in East European MFIs included ownership type as an independent variable in her model. Similarly Cull et al. (2007) included ownership type as a control variable in their study on the influence of lending methodologies on performance. In none of these studies did ownership type have a significant influence on the performance of MFIs due to varying challenges. In another study Hartarska and Nadolnyak (2007) found that regulation affected neither social nor financial performance in MFIs.

This view of failure has found support amongst researchers arguing for effective governance within MFIs (Mersland & Strom, 2009) while others find the microfinance sector to have experienced some major failures where, among other reasons for these failures, the inadequacy of governance practices was to blame (Labie, 2001). In addition to weak governance practices, there has been a tremendous growth and institutionalization process experienced by some organizations that is providing an interesting area for further research (especially in SSA) aimed at improving internal control mechanisms, especially mechanisms linked to board action.

Accordingly, Mersland and Strom (2009) suggest that financial performance improves with local rather than international directors supported by an internal board auditor, while Hardy et al. (2003) argue for a better MFI regulation. MFIs in Kenya through the enactment of the MFI Act 2010 have led to commercialization of MFI operations as a key to sustainable business. The Act has freed MFIs to mobilize public deposits and manage professionally to make profits for sustainable businesses (AMFI, 2010). This is further supported by the fact that in the microfinance literature, the analysis of governance has evolved from a principal-agent theory to a more complex, multi-stakeholder one (Giovanna Pugliese, 2010).

5.0 Conclusion

This study concludes that there is empirical evidence which indicates that MFIs (both for profit and not for profit) have large boards. However because of the dual objective of MFIs, these studies. This study concur with the findings as well as related literature that good corporate governance seeks to create an institutional framework that encourages all participants to contribute towards better corporate performance aligned with good governance practices. This supported by literature indicates that boards of these organisations should be large at least to meet the requirement suggested of eight members by various studies (Hartaska & Mersland, 2008). In this case the board composition will be fair in terms of both the size and diversity.

The most important implication of this study is that while the MFIs study is specific to Kenya, the conditions for successful MFIs can be generalized to other donor-led MFIs elsewhere. A competent and motivated board together with institutional capacity is critical to advancing CG in the microfinance sector. The implication here is that sufficient flows of donor funds are not a guarantee for success. MFIs need good governance that ensures transparency of processes and clear lines of accountability amongst stakeholders in relation to MFI's mission. For this to happen, MFIs boards should be in positions to challenge and act as a check on executives, and have the relevant background experience. In addition, MFIs need to invest in up to date management information systems that are well supported by established business ethics. Considering that there were hardly challenges among the MFIs that were targeted in regard to CG practices, this is a good indication that MFIs in Kenya are on track and this policy should be replicated within other financial and non-financial institutions in the country.

6.0 Recommendations

From the above findings and conclusion the study recommends that in order for MFI to remain profitable while ensuring good corporate governance there is a need to keep up and to strengthen close ties to customers in order to overcome informational asymmetries. However, this should not necessarily be done through group lending as this approach increases costs. A viable MFI needs to be profitable while integrating good CG practices. Thus, as long as donors or governments are not willing to take on a long term obligation to subsidies, good financial performance needs to be accepted, even if this means lower outreach in the short term. Stronger competition among MFIs should be encouraged.

In regard to the second objective where the government hardly interferes with operations of MFIs the role of the state should thus be to foster competition in the MFI field. This is perhaps the major contribution the state can make for microfinance institutions. Some answers in microfinance governance have been found, more questions remain especially on outreach and more about financial performance. Consequently, the similarity of financial and outreach performance in community based organizations, MFI operating under the Act and those operating under Company Act, calls for an investigation into causes for this.

Furthermore, since stakeholders have intrinsic values, they should be viewed instrumentally, as factors potentially affecting the overarching goal of optimizing shareholders' interests especially in entrenching CG practices. By having them in the board, they become source of either organizational goodwill or retaliation. They also represent the diverse interests which may lead the organization to making effective strategic decisions which will in turn lead to better performance. Strategic decisions are the most important for the organization and they chart a direction of the organization. Therefore the groups which can affect that direction must be represented in the boards which imply that they are involved in the process of strategic decision making.

This study also emphasizes the fact that MFIs operate in countries ripe with corruption, where the legal frameworks are mixed, law enforcement is weak, and effective government regulation is uncertain. Therefore, there are good reasons to believe that the effects of some alternative governance mechanisms are more limited in most microfinance markets. Relevant literature expounds that increased levels of competition in microfinance markets induced efficient operations and reduced interest rates. However, as mentioned, competition in most markets is still weak. Adding to this is the challenge related to the lack of managerial capacity in the industry, which reduces managers' incentives to improve performance. Since no better options are available for the owners, managers can continue to produce slack results.

Increased use of incentive pay could solve some MFI governance challenges. However, aligning the interest of MFI managers too much with the interests of owners with economic incentives is problematic in financial institutions since this could induce managers to take higher risks at the expense of depositors and other debt holders.

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