Effect of Financial Planning On Financial Sustainability of Public Governance Non-Governmental Organizations in Nairobi County, Kenya

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ABSTRACT

Financial sustainability requires that NGOs be able to meet all their resource and financing obligations and remain in existence for unforeseeable future. NGOs also play crucial role in the society. However, just a small number (10 percent) of NGOs that had managed to achieve a desirable level of institutional and financial sustainability. The study sought to establish the effect of financial planning on financial sustainability of public governance NGOs in Nairobi County. The study was guided by resource mobilization theory and fraud theory. Primary data was collected by use of questionnaires. The study adopted descriptive research design. The study target population was the 550 public governance NGOs in Nairobi County dealing with public governance. Systematic sampling technique was used to identify 10 percent of the population as the respondents where every 10th organization was studied. The collected data was analyzed using both quantitative and qualitative data analysis methods. Quantitative method involved both descriptive and inferential analysis. Data from questionnaire was coded and analyzed using Statistical Package for Social Science (SPSS). SPSS was used for data entry, descriptive analysis, reliability analysis, correlation analysis and multiple regression analysis. The study established that the independent variables Financial Control ($r=0.685$, $p<0.05$) had positive and significant effect on NGO financial sustainability. The study concluded that high number of NGOs were not sustainable a problem which could be addressed through NGOs improving their financial planning practices. The study recommended that the management at the NGOs to work towards improving financial management practices with aim of enhancing financial sustainability of the NGOs.

Key Words: *Financial Planning, Financial Sustainability, Public Governance Non-Governmental Organizations, Nairobi County, Kenya*

1. INTRODUCTION

Nongovernmental organizations play key role in the delivery of healthcare, education and other welfare services in many developing countries like Kenya and hence their financial sustainability cannot be ignored. Additionally, NGOs play an important role in creating public awareness on important issues of concern including monitoring the activities of the government, multinational organizations, as well as other entities for the greater good of the community (Goddard & Assad 2006). To achieve the intended objectives, NGOs need to be transparent, accountable and be operated with the highest degree of integrity. This is based on the fact that financial accountability mechanisms employed by NGOs in delivering development objectives affect the effectiveness with which aid funding is deployed in individual aid projects (Agyemang, Awumbila, Unerman & Dwyer, 2009).

Lack of financial accountability is a major feature among nongovernmental institutions globally (USAID, 2010). The challenge is more prevalent in Kenya as supported by empirical findings (Karanja & Karuti, 2014; Njoroge 2013 and Odhiambo, 2013). Non-governmental institutions that have sound financial accountability systems are able to have stable income flows which enable them to fulfil their multiple missions and respond to the current challenges in an increasingly complex and global environment hence leading to their financial sustainability (Anthony & Young, 2003). Further, organisations mostly tend to aim towards financial sustainability by increasing efficiency in the way in which resources are utilised which cannot be achieved without adequate financial accountability mechanisms (Habeeb, 2013). Most NGO in Kenya financial sustainability rests on the donor funding (Odhiambo, 2013) implying the prevalent need for financial accountability. Financial sustainability among NGOs cannot be achieved without the ability to mobilize resources which requires them to be financially accountable. Differential association theory holds that lack of financial accountability leads to employees' dishonesty and infection of honest employees further worsening financial sustainability problem. Resourced based theory on the other hand argue that financial sustainability is a function of internal resources within the organization and how well the resources are applied in generating finances required by the organization (Brinkmann &Henriksen, 2002; Fanning & Cogger, 1998; Cressey, 2003). Driven by this background knowledge, this study will seek to determine the effect of financial accountability on sustainability of NGOs in Kenya.

2. STATEMENT OF THE PROBLEM

The Non-Governmental Organization sector has experienced rapid growth and involvement in achieving increased economic involvement over the last decade (Anheier and Salamon, 2006). These organizations play a vital role in a country including provision of health services, promotion of public governance, economic growth and development by contributing to GDP approximately Ksh. 80 billion per year (NGO Coordination Board, 2014). However, despite the benefits accrued from the NGOs, most of them have been established not to be financially sustainable with only 10% of the NGOs achieving the desired financial sustainability levels (Nuka, 2010). This has resulted with the donor funding reduce significantly by more than 20% and 510 NGOs' licenses being withdrawn due to lack of accountability and dwindling financial sustainability (NGO Coordination Board, 2014).

3. STUDY OBJECTIVE

To determine the effect of financial planning on financial sustainability of public governance NGOs in Nairobi County

4. THEORETICAL REVIEW

NGOs are non-profit making organizations whose existence is well explained by various theories that have emerged over time. The problem of how Local NGOs can ensure their financial sustainability has come into focus in recent years with this dynamic being best explained by various theories. In the past, the problem of financial sustainability was not so acutely felt as there were enough resources to fund projects and programmes. To understand the concept of financial accountability and sustainability of NGOs, various theories are reviewed which include the resource mobilization theory and fraud theory/ differential association theory.

4.1 Fraud Theory/ Differential Association Reinforcement Theory

The theory is attributed to the work of Burgess and Akers (1966). Differential association theory is based on the belief that the behaviours of an individual are influenced and shaped by other individuals they associate with. The primary reference group is that of the nuclear family, which the individual lives and grows up with. These interactions formulate the individuals understanding of societal norms and values. It is then assumed that if the individual is capable of learning what is acceptable in society, they are also not capable of learning what is considered unacceptable.

To the field of finance, the theory explains why people engage in fraud and other activities which affect financial sustainability of an organization. Researchers and practitioners in different fields that involve the study of fraud acknowledge three key factors associated with the probability of whether an individual will commit fraud. The three factors, which constitute the fraud model, are perceived pressure facing the person, perceived opportunity to commit fraud, and the person's rationalization or attitude. The fraud model was recently advanced by Harrison *et al*., (2011). According to Cressey (2003), dishonest employees are likely to influence the honest employees. A non-sharable financial need affects the behaviour of one who violates a trust to commit fraud. What is deemed non-sharable is in the eyes of the offender. These “non-sharable” needs are divided into six basic types: violation of ascribed obligations, problems resulting from personal failure, business reversals, physical violation, status gaining, and employer-employee relations (Cressey, 2003). Elements of fraud include false representation of a material fact; and representation made with knowledge of its falsity. As Harrison *et al*. (2011) pointed out; management fraud represents one instance of the agency problem where managers are interested in increasing their own wealth at the expense of the shareholders.

Implications of the theory to the study is that accountability systems reduce the chances of committing fraud and hence safeguarding organization’s financial sustainability. Internal audit and management as well as the board of directors and the audit committee code of corporate governance have a key role to play in uplifting accountability. As far as the role of the audit committee is concerned, according to Brinkmann and Henriksen (2002), it improves the capacity of the board to act as a management control by providing them with detailed information and knowledge on the financial statements. As Fanning and Cogger (1998) stated, the board of directors assumes internal monitoring, and their viability is enhanced by having independent non-executive directors on the board. However, fraud prevention and detection is a role that ought to be jointly accepted by the board, senior management and internal auditing. In relation to the study, the theory holds that an organization without accountability mechanisms encourages dishonesty and fraud which in turn reduces donor confidence in the NGO leading the organization being financially unsustainable.

4.2 Resource Mobilization Theory

Resource mobilization theory emerged in the 1970s and is associated with the work of resource mobilization theorists McCarthy and Zald (1977). The theory argues that affluence and prosperity tend to foster social activities. Prosperous societies generate a number of resources that can aid resource mobilization (McCarthy and Zald, 1977). In resource mobilization theory, mobilization is the process of forming crowds, groups, associations, and organizations for the pursuit of collective goals. Organizations do not "spontaneously emerge" but require the mobilization of resources (Lin *et al*., 2003). Resource based theory focuses on a set of contextual processes (resource management decisions, organizational dynamics and political changes) that condition the realization of this structural potential. It takes the issues, the actors and the constraints as given, and focuses instead on how the actors develop strategies and interact with their environment in order to pursue their interests. The theory, therefore, employs a ‘purposive model’ of action and explains organization actions in reference to the strategic-instrumental level of action (Filly, 2005).

The theory stresses on the ability of an organization to acquire resources and to mobilize people towards accomplishing organization’s short term and long term goals. In nongovernmental organizations, a resource in the form of ‘money’ is the most important and crucial for organization financial sustainability. Without this resource, organizations cannot activate the other resources in their possession to achieve sustainability. The success of any community organization agency lies in its ability to raise enough funds (monetary resources), or to convert other resources in such a way that it can be exchanged for the money, or to plan its activities into fundable projects (Tam & Kiang, 2012). Critics of resource mobilization theory point out that it fails to explain social movement in communities, which are large networks of individuals and other groups surrounding NGOs, and providing them with various services. The theory fails to explain how organizations with limited resources can succeed in achieving their objectives and bringing social change (Ludwig & Pemberton, 2011). The theory implications to the study is that NGO financial sustainability depends on how well the NGOs mobilize resources. However, sustainable resource mobilization cannot be achieved nowadays since the donors have become more concerned on how the mobilized resources are applied; this requires financial accountability. If resources are mobilized from large pool of donors who contribute insignificant portions, then they may not be concerned on financial accountability aspect. The proposition of the theory is that the main determinant of financial sustainability in the NGOs is its resource mobilization and utilization effectiveness. Hence, under this circumstance, financial accountability will not affect financial sustainability of NGOs directly.

5. EMPIRICAL REVIEW

Financial planning is an essential tool, whether in paper or computerized form. Financial plans enable organizations to identify all the major activities required to achieve the research objectives. Financial plans enable identification of the specific person responsible for ensuring that the objectives are completed successfully and within the estimated time. Financial planning involves budget control, having ceilings on overheads, financial reporting, analysis of financial proposals, and stakeholders' participation (Hassan & Forhad, 2013). In recognition of the importance of financial planning in ensuring organization financial sustainability, Juma (2012) examined the factors affecting sustainability of donor funded community development projects in Bungoma County using a descriptive research design. The study sought to establish how audit, financial systems, technology, computerized operations, stakeholders' involvement, donor policies and management systems affected sustainability. The study established that project finance system affected project sustainability to a very great extent where auditing was done quarterly. The study also established that adoption of information technology affected sustainability of the project to a very great extent and that accounting systems, records management, communication and technical operations were computerized to assure adequate information. Stakeholders' involvement in donor funded project affected its sustainability to a very great extent. Finally, the study concluded that donor policy affected sustainability of the project at very great extent. The study recommended that adequate finance be allocated by the project donor in order to ensure effective sustainability of the project and that those authorized to manage and supervise community projects be 'trustworthy and avoid corruption and embezzlement of the funds. Further, the study recommended that for the organization to be fully effective on data management and storage proper systems of information management must be embraced; and stakeholders to be involved in the conception, design, implementation and management of such projects to ensure sustainability.

Further, Obo (2009) studied microfinance sustainability in Ethiopia using descriptive research design. The study sought to determine the measures put in place to ensure that the institutions were sustainable. The study found that microfinance institutions mission and vision were not clearly articulating the need for sustainability. However, strategic plans were directing to MFI self-sustainability indicating that the institutions can be sustainable by having the right structures. The study concluded that Ethiopia MFIs are not operationally and financially self-sufficient except for government owned. Recommendation was that regulatory framework to be made more flexible and merging of MFIs to be encouraged. Ayom (2013) studied internal controls and performance in NGOs in South Sudan. The study followed a descriptive research design and dependent variable; performance of management Science for Health's and independent variables; internal control in nongovernmental organizations sector. The study found out that the payment procedures followed by Management Sciences for Health's. Attracted a positive response with majority acknowledging it performed well. The internal audit function attracted a relatively fair response with some agreeing and others not meanwhile majority of respondents gave a negative view about the procurement process indicating it was fraud, likewise they didn't appreciate the budgeting process.

6. CONCEPTUAL FRAMEWORK

The conceptual framework in figure 1 below shows that financial planning affects financial sustainability of the organization as indicated by self-sufficiency and borrowing level.

Independent Variables → ***Dependent Variable***

Financial Planning

- Budget control
- Ceilings on overheads
- Financial reporting
- Analysis of financial proposals
- Stakeholders' participation

→

Financial Sustainability

- Deficit/Surplus
- Diversification in funding
- Donor dependency ratio
- Debt Ratio

Figure 1: Conceptual Framework

7. RESEARCH METHODOLOGY

The study adopted the descriptive design. The study was done using a survey approach. To show the relationship between financial and NGO financial sustainability, correlation research design was used. The target population was 550 public governance NGOs with offices in Nairobi County as at December 2014. The collected data was analysed using both quantitative and qualitative data analysis methods. Quantitative method involved both descriptive and inferential analysis. Data from questionnaire was coded and analysed using Statistical Package for Social Science (SPSS). SPSS was used for data entry, obtaining the variable descriptive statistics, reliability coefficient, correlation coefficient and multiple regression. Primary data was collected by use of questionnaires which were self-administered to the respondents. The target respondents were the finance managers since they are best placed to provide the required study information.

8. RESEARCH FINDINGS

The study sought to determine the extent of adoption of various financial planning practices among NGOs. A likert scale of 1 to 5 was used to rate their responses, where 1 is no extent, 2 is small extent, 3 is moderate extent, 4 is large extent and 5 is a very large extent. The findings obtained are as shown by Table 1.

Table 1: Financial Planning

Financial Planning	NE	SE	ME	LE	VLE	Mean	Std. Dev
Annual budgets preparation	0	2.6	18.2	58.4	20.8	3.97	0.70
Regular comparison of actual and budget	2.6	10.4	24.7	40.3	22.1	3.69	1.01
Expenditure outside the budget requires directors approval and justification	6.5	10.4	36.4	22.1	24.7	3.48	1.16
Ceilings on administration and overheads expenditure	7.8	9.1	24.7	32.5	26	3.6	1.19
Full and accurate financial reporting	20.8	7.8	14.3	28.6	28.6	3.36	1.49
Financial planning advise sought	3.9	14.3	18.2	37.7	26	3.68	1.12
Financial proposals analysis and discussion	14.3	19.5	19.5	23.4	23.4	3.22	1.38
Stakeholders' participation in budgetary process.	10.4	24.7	13	36.4	15.6	3.22	1.27

Where NE=No Extent, SE=Small Extent, ME=Moderate extent, LE=Large Extent, VLE=Very Large Extent

The findings obtained indicated that NGO were preparing budgets on annual basis to guide spending for the NGO to a large extent (mean of 3.97 and standard deviation of 0.70). This meant that most NGOs had adopted budgets as financial planning tools. The standard deviation was small indicating that the respondents agreed more on the adoption of budgets to large extent. Regular comparison of actual and budget being determined and corrective action taken was being done to large extent (mean of 3.69 and standard deviation of 1.01). Therefore, to a large extent, most NGOs were comparing the actual and budget as a financial planning tool. The standard deviation indicated the variation in the responses. Expenditure outside the budget requiring directors approval and must be fully justified had a mean of 3.48 and standard deviation 1.16. This implied that approval for expenses above the budgets was being done to a moderate extent. Further, the findings indicated that to a large extent, administration and overheads expenditure had a ceiling which was set in relation to expected funding (mean of 3.6 and standard deviation 1.19).

To a moderate extent, for most NGOs, there was a full and accurate reporting on the financial planning to the stakeholders with a mean of 3.36 and standard deviation 1.49. This implied that reporting was accurate but not at all times. In financial planning, management seeks counsel and guidance from professional advisors had a mean of 3.68 and standard deviation 1.12. This implied that to a large extent, NGOs' management sought counsel on the budget matters. Financial proposals are analyzed and debated vigorously by all stakeholders before they are approved and implemented had a mean of 3.22 and standard deviation 1.38. Thus, to a moderate extent, financial proposals were being debated. Stakeholders of the organization participating in budgetary process had a mean of 3.22 and standard deviation 1.27. This implied that stakeholders of organizations participated in budgetary to a moderate extent. The findings implied that most financial planning practices had not been fully adopted by the NGOs. Notably, only budget planning had a large extent of adoption while the rest had moderate extents of adoption with stakeholders' participation having the least extent. Financial plans enable organizations to identify all the major activities required to achieve the study objectives as well as the estimated actual work time. They thus ought to be well formulated and implemented so as to enhance the financial operations in an organization.

On the sustainability of the NGOs, the findings obtained as shown by Table 2 indicate that 56 percent of the respondents stated their organizations to be sustainable while 44 stated that the NGOs were not sustainable. This shows that majority of the NGOs were sustainable.

Table 2: NGO Sustainability

Sustainability	Frequency	Percent
Not Sustainable	34	44.2
Sustainable	43	55.8
Total	**77**	**100**

The study sought to establish the underlying relationships between variables and the extent to which the independent variables influenced the dependent variables. Regression analysis was used to find the relationship between financial planning and NGO financial sustainability. Table 3 gives the relationship between different sets of variables that was obtained.

Table 3: Regression Analysis Results

	R	R Square	Adjusted R Square	Std. Error of the Estimate		
	.438a	0.192	0.181	0.628		
ANOVA(b)						
		Sum of Squares	df	Mean Square	F	Sig.
Regression		7.036	1	7.036	17.836	.000a
Residual		29.585	75	0.394		
Total		36.621	76			
Coefficients(a)						
		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
(Constant)		1.149	0.401		2.865	0.005
Financial Planning		0.472	0.112	0.438	4.223	0.000

a. Predictors: (Constant), Financial Planning
b. Dependent Variable: Financial Sustainability

Regression analysis obtained indicated that financial planning and financial sustainability had a Pearson Correlation of 0.438 and a p-value<0.05. The positive coefficient indicated that financial planning had a positive effect on financial sustainability of NGOs. The p-value<0.05 indicated that the positive effect of financial planning was significant at 95% confidence level. Financial planning had a coefficient of 0.472, p<0.05. Therefore, an NGO that adopts appropriate financial planning practices will significantly improve financial sustainability. These findings compared with those of Juma (2012) who examined the factors affecting sustainability of donor funded community development projects in Bungoma County and concluded that donor policy affected sustainability of the project at very great extent. Ayom (2013) and found out that financial planning procedures positively influenced NGO sustainability.

9. CONCLUSIONS

Based on the findings obtained, the study concludes financial planning practices adopted by the governance NGOs in Nairobi County were relatively low. The study concluded that financial planning practices have a positive and significant effect on financial sustainability of NGOs.

10. RECOMMENDATIONS

The study recommends that NGOs management to adopt proper and effective financial planning mechanisms. These will enable NGOs to gain credibility from financers, they should be accountable by adopting appropriate financial controls and partner with an established NGO or gain sponsorship from a well-known organization. The study recommended that NGOs regulation board to formulate minimum financial planning standards to be met by the NGOs. This will lead to improved accountability and hence more NGOs will be sustainable.

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