EFFECT OF CORPORATE GOVERNANCE ON FRAUD MITIGATION AMONG MICROFINANCE BANKS IN KENYA

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NOVEMBER 2023

DECLARATION

I declare that this dissertation is my original work that has not been published before nor has been submitted elsewhere for a degree award. I can also confirm that it contains no material written or published by other people with the exception of areas in which their work has been duly referenced and the authors acknowledged.

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ABSTRACT

Microfinance banks in Kenya play a critical role in providing financial services to low-income individuals and small businesses, many of whom are underserved by traditional financial institutions. However, like any financial institution, microfinance banks in Kenya are also susceptible to fraud, which can have significant consequences for both the institution and its clients. The main aim of this research study was to assess the effect of corporate governance on fraud mitigation among microfinance banks in Kenya. The specific objectives of the study were to; determine the effect of executive compensation on fraud mitigation, analyse the effect of board independence on fraud mitigation, to establish the effect of independent risk committee on fraud mitigation and to assess the effect of code of conduct on fraud mitigation. The research adopted the agency theory, stakeholder theory and the stewardship theory. A descriptive research design was used in this research. The target population was the 349 management employees working at the 14 microfinance banks in Kenya and stratified sampling technique was used. The employees were classified according to their cadre. The sample size was 186 arrived at using Yamane formula. The study utilized primary data that was collected using a questionnaire. The administration of the questionnaire was done through Google form. The collected data was converted into quantitative format and analysed using descriptive and inferential statistics. The descriptive statistics involved mean and standard deviation while inferential statistics comprised of both correlation and regression analysis. The results of the study were presented in tables and figures followed with pertinent interpretation. Regression results revealed that executive compensation, board independence, independent risk committee, and code of conduct together account for 93.1% of the variation in the fraud mitigation among microfinance banks in Kenya. The explanatory power of the model was statistically significant as the p value was 0.000. Further the results revealed that executive compensation ($\beta = 0.312$, $p = 0.000$); board independence ($\beta = 0.352$, $p = 0.000$); independent risk committee ($\beta = 0.232$, $p = 0.000$); and code of conduct ($\beta = 0.732$, $p = 0.000$) had a positive and significant effect on fraud mitigation among microfinance banks in Kenya. Based on the findings, the study concluded that effective corporate governance, manifested through equitable executive compensation, autonomous and diverse boards, proficient and independent risk committees, and robust codes of conduct, substantially contributes to fraud mitigation in microfinance banks. The recommendations emphasize the refinement of corporate governance structures and practices, continuous monitoring and evaluation of governance policies, and the integration of advanced technological solutions to enhance fraud detection and prevention capabilities. Future research is encouraged to explore the intricate relationships between different corporate governance components and their collective impact on fraud mitigation, with a focus on uncovering universally applicable insights and practices in varied organizational and geographical contexts.

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You've all offered me incredible support.

DEDICATION

I dedicate this dissertation to my family. I love you deeply with all my heart. To my wife Carol, and Son, Tendai you have been listeners and supporters of all my endeavors. Your partnership, steadfastness, and love sustain me.

I equally dedicate this dissertation to my Parents who have been my source of inspiration and have always continued to provide their moral and spiritual guidance.

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ABBREVIATIONS AND ACRONYMS

CBK	Central Bank of Kenya
CEO	Chief Executive Officer
CLRM	Classical Linear Regression Model
EU	European Union
LR	Likelihood Ratio
MFB	Micro Finance Banks
MFI	Micro Finance Institution
ROA	Return on Assets
ROE	Return on Equity
US	United States

DEFINITION OF TERMS

Board independence	The degree to which the board of directors is composed of individuals who are not directly affiliated with the company's management or major shareholders (Rostami & Rezaei, 2022).
Code of conduct	A set of rules, guidelines, or principles that outline expected behavior and ethical standards for individuals or members of a particular group, organization, profession, or community (Almashhadani & Almashhadani, 2022).
Corporate governance	A framework of policies, procedures, and structures that define the roles and responsibilities of various individuals and groups within the company, and the mechanisms for oversight and accountability (Naimah & Hamidah, 2017).
Executive compensation	The financial and non-financial rewards offered to senior managers and executives inside a firm (Girau, Bujang, Paulus Jidwin, & Said, 2022).

Fraud mitigation	Denotes processes and strategies used to deter, detect, and respond to fraudulent activities (Turner, 2017).
Independent risk committee	A group of individuals who are responsible for overseeing the company's risk management policies and practice (Ramly & Nordin, 2018)

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Fraud mitigation is extremely important in a financial institution. Financial institutions, such as banks, microfinance banks, credit unions, and investment firms, deal with large amounts of money and personal information on a daily basis, making them an attractive target for fraudsters (Mansour, Ahmi, Popoola, & Znaimat, 2022). Fraud can take many forms, including identity theft, account takeover, phishing scams, and more. The consequences of fraud can be severe, including financial losses for both the institution and its customers, damage to the institution's reputation, and legal liabilities (Mangala & Soni, 2023).

Implementing policies and practices that are intended to prevent and identify fraud as well as responding swiftly and effectively to any suspected or proven fraud events are all necessary for effective fraud mitigation (Sood & Bhushan, 2020). This could entail actions like checking account activity for odd patterns or behaviours, confirming client identities, putting multi-factor authentication into place, and instructing staff on how to spot and handle possible fraud. Effective fraud mitigation can assist to preserve confidence in the financial system as a whole in addition to safeguarding the institution and its clients. As such, it is a crucial component of the functioning of financial institutions and needs to be treated seriously (Sinha, 2021).

A financial institution's culture of accountability and openness can make it harder for fraud to occur by fostering effective corporate governance (Bhasin, 2016). Corporate governance frameworks may make sure that each employee in the company is aware of their responsibilities in preventing and identifying fraud. This might contain certain policies

and procedures that specify how staff members are supposed to react to possible fraud. A sound corporate governance structure may aid in developing an ethical culture inside the company. Employees may be encouraged to disclose any suspected fraud-related incidences as a result, which can help deter fraudulent activity (Onesti & Palumbo, 2023).

Corporate governance systems frequently incorporate oversight tools that can assist detect and resolve possible areas of fraud risk, such as independent auditors or compliance committees (Suh & Shim, 2020). Furthermore, financial organizations with sound corporate governance frameworks frequently place a high priority on disclosure and openness. To stakeholders including investors, regulators, and clients, this might entail routine reporting of financial performance and suspected fraud occurrences (Kavadis & Thomsen, 2023).

A growing amount of attention has been placed on microfinance institutions' (MFIs') corporate governance and fraud prevention procedures in recent years. A series of high-profile scandals involving MFIs, which resulted in losses for both investors and borrowers, are partly to blame for this (Almashhadani & Almashhadani, 2022). Effective corporate governance helps ensure that MFIs prioritize the best interests of their clients, many of whom are financially vulnerable. It ensures that fair lending practices are followed, interest rates are transparent, and clients are not subjected to predatory lending practices or over-indebtedness (Rostami & Rezaei, 2022).

Around the world, governments and regulatory authorities are acting to solve these issues. As an illustration, the Reserve Bank of India has updated its rules for microfinance organizations, requiring them to adopt a more stringent approach to risk management and fraud prevention (Pramuki & Agustine, 2023). Similar to this, the UK's Microfinance Association has started a new accreditation scheme for MFIs that shows their dedication to

moral and responsible behavior. Many MFIs are improving their corporate governance and fraud prevention procedures in addition to these required requirements. This entails strengthening internal controls, boosting transparency, and carrying out routine audits to spot possible flaws before they develop into significant difficulties (Ali, Ramakrishnan, Faisal & Ullah, 2022).

In Sub-Saharan Africa, microfinance institutions in Nigeria have placed a substantial emphasis on corporate governance and the prevention of fraud. This is partly attributable to a number of well-publicized MFI fraud incidents that resulted in large losses for investors and borrowers. The Nigeria Central Bank has put in place a variety of regulatory measures to improve corporate governance and lower fraud in the microfinance industry in order to allay these worries (Bagudu, 2022). Numerous MFIs in Nigeria are engaged in improving their corporate governance and fraud mitigation procedures in addition to the statutory requirements. This entails strengthening internal controls, enhancing accountability and transparency, and incorporating best practices from other industries (Eko, 2022).

In East Africa, microfinance institutions are putting more of an emphasis on corporate governance and reducing fraud. For MFIs, several East African nations have put in place licensing and regulatory frameworks that mandate that they adhere to standards for capitalization, governance structure, and risk management (Nandaula, 2022). Industry groups have also created self-regulatory bodies to support ethical behavior and good governance. Additionally, a lot of organizations in the area provide training and capacity-building programs to assist MFIs in establishing better risk management and governance procedures. To increase transparency and lower the risk of fraud, several MFIs are also

implementing technology-based solutions, including as digital platforms and executive remuneration (Owiti, Ogara & Rodrigues, 2022).

In Kenya, microfinance institutions are essential for providing low-income people and small enterprises with financial services, many of whom are underserved by traditional financial institutions (Maengwe & Otuya, 2016). However, as per Wairimu and Mwilaria (2017) like any financial institution, microfinance banks in Kenya are also susceptible to fraud, which can have significant consequences for both the institution and its clients. Some common forms of fraud in microfinance institutions in Kenya include loan fraud, account takeover, and identity theft. The Central Bank of Kenya, which regulates financial institutions in the country, provides guidance on fraud mitigation measures that microfinance banks and other financial institutions should implement. These guidelines include requirements for internal controls, fraud risk assessments, and corporate governance mechanisms (Omino, 2015).

1.1.1 Corporate Governance

Corporate governance refers to set procedures, tenets, and values that guiding how a firm is managed and controlled, including its stakeholders' relation like shareholders, clients, workers, and regulators (Naimah & Hamidah, 2017). Corporate governance typically involves a framework of policies, procedures, and structures that define the roles and responsibilities of various individuals and groups within the company, and the mechanisms for oversight and accountability. This framework is designed to guarantee that the firm operations is ethical, transparent, and consistent with the interests of its stakeholders (Bhasin, 2016). Another definition of corporate governance denotes rules, practices, and processes by which a firm is directed and controlled. This includes the way in which the company's objectives are set and attained, the way in which risk is monitored and assessed,

and the way in which performance is measured and reported (Micklethwait & Dimond, 2017).

Effective corporate governance is vital since it aids promote accountability, transparency, and integrity within a company. It ensures that decision-making processes are fair and ethical, that conflicts of interest are managed appropriately, while identifying and managing risks in a responsible manner (Michelon, & Parbonetti, 2019). Corporate governance is also important because it helps to develop trust and confidence among stakeholders, including investors, employees, customers, and the wider community. Companies may improve their reputation, draw in and keep stakeholders who share their values by displaying a dedication to ethical business practices. In addition, effective corporate governance can help to reduce the likelihood of financial fraud, corruption, and other unboard independence that can have significant negative consequences for both the company and its stakeholders (Almashhadani & Almashhadani, 2022).

In regard to operationalization, researchers have identified some mechanisms of corporate governance that can mitigate fraud. According to Girau, Bujang, Paulus Jidwin, and Said (2022) executive compensation has been highlighted as a technique for bringing executives' interests into line with those of the business and its stakeholders. In addition to being open and equitable, compensation plans should be created to recognize performance that advances the organization's long-term objectives and core values. Board independence has also been identified as a mechanism to mitigate fraud. Independent directors convey external viewpoints and expertise to the board and can aid guarantee that the board is acting in the best interests of the organization and its stakeholders (Rostami & Rezaei, 2022).

As Ramly and Nordin (2018) observed, an independent risk committee can also provide valuable oversight and advice on risk management issues. This committee should

be composed of independent directors with relevant expertise in risk management and should have sufficient resources and authority to carry out its responsibilities. Ethical standards and codes of conduct also help mitigate fraud. They should be established and communicated to all employees, and appropriate mechanisms put in place to monitor compliance and address violations (CIMA Report, 2019). The current research operationalized corporate governance in terms of executive compensation, board independence, independent risk committee and code of conduct.

1.1.2 Fraud Mitigation

The methods and tactics used to stop, catch, and deal with fraudulent activity are referred to as fraud mitigation (Turner, 2017). Fraud is any intentional deception or misrepresentation made for personal gain or to cause harm to others. In the context of business or financial transactions, fraud can include activities such as identity theft, embezzlement, and falsifying financial documents (Cooper, Dacin, & Palmer, 2019). Another definition of fraud mitigation is the procedure of minimizing the impact of fraud on an organization's operations and finances. Effective fraud mitigation requires a proactive and ongoing approach that involves all levels of an organization, from senior management to front-line employees. By appropriate measures implementation, businesses and organizations can lower the risk of fraud and protect themselves and their customers from financial losses and reputational damage (Kaveri, 2019).

The goal of fraud mitigation is to protect an organization from financial losses, reputational damage, and legal liability resulting from fraudulent activity (Opiyo, 2017). This can be particularly important for businesses that handle sensitive financial or personal information, as well as those that operate in high-risk environments, such as the financial services and healthcare industries. By implementing effective fraud mitigation strategies,

organizations can reduce the risk of fraud and ensure the smooth operation of their business (Roy & Prabhakaran, 2022).

Fraud mitigation measures can include: Risk assessment which encompasses identifying potential fraud risks and determining the likelihood and probable impact of every risk. Internal controls which is about implementing policies and procedures that reduce the risk of fraud by ensuring that transactions are properly authorized, recorded, and reconciled (Akinbowale, Mashigo & Zerihun, 2023). Training and awareness which involves educating employees on the risks of fraud and providing guidance on how to detect and report fraudulent activities. Monitoring and surveillance which is about monitoring transactions and other activities to identify unusual patterns or behaviors that may indicate fraud. Response planning is another measure which is a plan for responding to suspected or confirmed fraud, including notifying law enforcement, conducting an internal investigation, and implementing corrective measures to prevent future occurrences (Sood & Bhushan, 2020).

1.1.3 Microfinance Banks in Kenya

As of December 2022, 14 microfinance banks (MFBs) were operational in Kenya, as per CBK. The MFBs in Kenya are regulated by the Central Bank of Kenya (CBK), which is accountable for licensing and supervising the banks to ensure that they operate in amenability with appropriate laws, regulations, and prudential standards. In Kenya, microfinance banks have the responsibility of providing individuals and small enterprises that might not have access to regular banking services with financial services including loans, savings, and insurance products. In rural locations where traditional banking services may be few or non-existent, MFBs are especially crucial. To assist their clients in

developing their enterprises and improving their financial management, MFBs frequently offer financial training and instruction to them (CBK, 2022).

Kenyan microfinance institutions have taken a number of steps to reduce fraud, a major risk in the financial sector. To identify and stop fraudulent activity, microfinance institutions have established reliable internal control systems (Maengwe & Otuya, 2016). This entails the division of labor, routine audits, and the supervision of risky activity. Additionally, employee training on fraud prevention and detection has been funded by microfinance banks. This involves training employees on how to spot possible fraud and how to report questionable activity. Additionally, in order to stop and catch fraud, microfinance institutions have employed technology solutions. This entails the use of anti-fraud software and techniques, such as real-time transaction monitoring systems and biometric identification systems (Wairimu & Mwilaria, 2017).

Kenyan microfinance institutions use corporate governance to reduce fraud. Implementing risk management frameworks that enable them to recognize, quantify, and manage risks is one of the corporate governance techniques that Kenyan microfinance banks are using to reduce fraud (Mosoti, Wafula & Nyang'au, 2022). Microfinance banks may identify and stop fraudulent activity by putting in place a risk management framework and appointing a board of directors to monitor the institution's general management and strategic direction. To make sure that risks are appropriately managed, continual monitoring and improvement are crucial (Njenga, & Osiemo, 2018). However, the efficacy of these methods differs between institutions.

1.2 Statement of the Problem

Microfinance banks in Kenya play a critical role in offering financial services to low-income persons and small businesses, many of whom are underserved by traditional

financial institutions (Walde & Makori, 2022). The ideal situation in corporate governance context and fraud mitigation among microfinance institutions in Kenya would be one where MFIs have robust corporate governance and risk management practices in place to prevent and detect fraudulent activities. This would include having strong internal controls, an effective board of directors, regular audits and reviews of operational and financial processes, and transparent reporting mechanisms. In such an ideal scenario, investors and borrowers alike would have confidence in the integrity of the microfinance sector and be more willing to participate in microfinance activities (Rizwan & Chughtai, 2022).

However, in the first ten years following the passage of the MFIs Act of 2006, Kenya's microfinance institutions have suffered considerable financial losses. Many of these were brought on by fraud, which impacts not only MFIs but the entire financial industry (Githaiga, 2022). These cases have highlighted the need for stronger corporate governance and risk management practices in the sector. Despite efforts by regulators and industry associations to improve governance and reduce fraud, there are still many MFIs that lack the necessary resources, expertise, and commitment to implement these measures effectively (Mosoti, Wafula & Nyang'au, 2022).

Despite previous research in this field, the focus has mostly been on developed economies (Girau et al., 2022; Chen et al., 2020; Ding et al., 2020). It is obvious that emerging economies experience distinctive challenges from industrialized economies in terms of corporate governance procedures. Compared to industrialized economies, developing economies are more likely to have poorer corporate governance frameworks, which will result in less effective management oversight (Rizwan & Chughtai, 2022). Therefore, it was necessary to do research into the most significant corporate governance factors that have an impact on fraud mitigation. Most of the available studies are among

commercial banks and in the public sector. The current research extended this debate to the Micro-finance banks in Kenya in an effort to offer in the local arena more empirical data.

1.3 Objectives of the Study

The general objective of this study was to determine the effect of corporate governance on fraud mitigation among microfinance banks in Kenya.

The specific objectives were:

i. To determine the effect of executive compensation on fraud mitigation among microfinance banks in Kenya.

ii. To establish the effect of board independence on fraud mitigation among microfinance banks in Kenya.

iii. To find out the effect of independent risk committee on fraud mitigation among microfinance banks in Kenya.

iv. To determine the effect that code of conduct has on fraud mitigation among microfinance banks in Kenya

1.4 Research Questions

The study addressed the following research questions:

i. What is the effect of executive compensation on fraud mitigation among microfinance banks in Kenya?

ii. How does board independence affect fraud mitigation among microfinance banks in Kenya?

iii. What is the effect of independent risk committee on fraud mitigation among microfinance banks in Kenya?

iv. How does code of conduct affect fraud mitigation among microfinance banks in Kenya?

1.5 Significance of the Study

The research conclusions will be instrumental to existing theoretical and empirical literature on corporate governance and financial accountability. This study's results will benefit future scholars on the association between the corporate governance and public fraud mitigation in the financial sector. Future researchers concerned about this topic may want to review further the interconnection between corporate governance and fraud mitigation under different circumstances. The study will therefore act as a reference point in future studies.

The research's conclusions may be important to decision-makers in government and regulatory agencies. The study will help the government make decisions on how to implement policies and how company governance affects fraud prevention. This would aid in pointing up potential areas for policy reform. It will also be useful in assessing how well the various financial institutions are doing in terms of reducing fraud and creating guidelines for doing so.

The results will help management in microfinance institutions better understand how the two variables are correlated. The study is anticipated to be helpful in that it will shed light on the value of corporate governance. The managers are expected to create a clear plan for enhancing the execution of corporate governance. The information can be utilized by other institutions in enhancing fraud mitigation as well as strengthen financial accountability.

1.6 Scope of the Study

This research focused on the effect of corporate governance on fraud mitigation among microfinance banks in Kenya. The research was limited to the executive compensation, board independence, independent risk committee and code of conduct. The target

population was the 349 management employees working at the 14 microfinance banks in Kenya and stratified sampling technique was used. The Yamane formula was used to determine the sample size of 186. The study adopted a descriptive design and relied on primary data obtained via questionnaires. Data was analysed via descriptive as well as inferential statistics. The research was conducted for the period between July and September 2023.

CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction

The empirical literature of academic studies that research how governance arrangements effect fraud mitigation is fully reviewed in this chapter. The chapter also examines the three ideas that serve as the foundation for this research: agency theory, stakeholder theory, and stewardship theory.

2.2 Theoretical Review

The fundamental ideas that were examined in relation to governance frameworks and fraud mitigation will be covered in this section. The ideas that were explored include the agency theory, stakeholder theory, and stewardship theory.

2.2.1 Agency Theory

According to Jensen and Meckling (1976) agency theory, the agent-principal relationship has to be handled for improved value generation when management and company ownership are separated (Moenga, 2015). Divergent perspectives between agents and shareholders need the company to employ different methods. For the business to maintain a sound financial position in such groups, this will result in agency charges. According to this theory, the principal-agent relationship is prone to conflicts of interest because the principal and the agent have different goals and incentives. Contracts and monitoring tools are therefore necessary to balance the interests of the two parties and guarantee that the representative acts in the principal's best interests. According to the hypothesis, any information asymmetry makes it more difficult to acquire, assess, and analyze all records and information related to shareholders' opportunistic managerial conduct (Njau, 2016).

Prominent scholars such Mueller (2010), Gallagher (2004), and Armstrong (2000) endorse the agency thesis, arguing that it plays a crucial role in describing the numerous

interactions in an organizational environment. Agency theory, although being widely used, is not without flaws. It fails to take into account a number of complexities and challenges that agents may run into while carrying out their assigned tasks and obligations on behalf of the principal. According to the agency paradigm, costly control measures are in place. This is the case, according to Segrestin and Hatchuel (2011), since measures taken to safeguard shareholders' interests may impede the implementation of strategic decisions, obstruct company operations, alter investment plans, and give scant attention to the concerns of other stakeholders.

One of the key criticisms of agency theory is that it assumes that people's behaviors are predictable based on incentives and contracts and that their only motives come from self-interests (Alchian & Demsetz, 2017). This viewpoint, according to critics, is oversimplified and fails to take into consideration how complicated and multifaceted human behavior is. Another criticism of agency theory is that it prioritizes monitoring and control mechanisms like performance incentives and contracts over other crucial elements that affect organizational behavior and performance like organizational culture, values, and social norms (Yang & Liu, 2016).

Agency theory is relevant when reviewing the association between corporate governance and fraud mitigation because it provides a framework for understanding the relationships between different stakeholders, particularly the affiliation between the owners (principals) and the managers (agents) of a firm. Agency theory is pertinent to the relationship between corporate governance and fraud mitigation because it highlights the probable interest conflicts that can arise between managers and shareholders, and emphasizes the importance of effective governance mechanisms in aligning their interests and preventing fraudulent behavior.

2.2.2 Stakeholder Theory

According to Fontaine, Haarman, and Schmid (2006), Freeman (1984) is credited with developing the stakeholder theory. According to the stakeholder theory, a company's choices and actions should take into account the interests of all stakeholders, not just its shareholders. Stakeholders are individuals or groups who have an interest in or an influence on the firm's decisions and activities. Stakeholder theory contends that a company's obligations extend beyond maximizing shareholder wealth to include consideration of the interests of a wider variety of stakeholders, such as the environment, the local community, employees, customers, and suppliers. The idea holds that organizations that consider the interests of all of its stakeholders have a greater chance of long-term success because they have a wider range of backers and collaborators (Fontaine, Haarman, & Schmid, 2006).

According to Mudi (2017), organizations that take into account the interests of all of its stakeholders have a higher chance of long-term success because they have the support and cooperation of a wider range of people and organizations. The importance of ethical considerations in corporate decision-making is highlighted by the stakeholder theory, which also recognizes that businesses have obligations beyond maximizing shareholder profit. Stakeholder theory has also drawn criticism. According to Jensen (2016), it might be difficult to implement since the interests of the numerous parties frequently conflict. For instance, there can be a conflict between the interests of investors and employees.

The idea highlights the significance of a company's social and ethical obligations in addition to its financial aims, making it pertinent to the relationship between corporate governance and fraud reduction. The stakeholder theory contends that in order to provide better long-term outcomes for both the business and society at large, firms must act in the best interests of all of its stakeholders. This means that in the context of corporate

governance and fraud mitigation, businesses must take into account how fraudulent activity would affect all of their stakeholders, not just shareholders. According to the stakeholder theory, organizations must strike a balance between their financial goals and their social and ethical obligations, and good governance practices should make sure that this balance is kept. By fostering an environment of openness, responsibility, and ethical conduct inside the business, this can aid in the prevention of fraud.

2.2.3 Stewardship Theory

Donaldson and Davis developed the theory of stewardship in 1991. According to the stewardship concept, managers act as trustees or stewards on behalf of the company's owners and are responsible for making sure that its resources are used ethically and responsibly (Chen et al., 2016). Stewardship theory contends that managers need to prioritize the interests of the business and its stakeholders over their own (Donaldson & Davis, 1991). Stewardship theory holds that managers are accountable for managing the firm's resources, including its human, financial, and physical capital. This requires managers to act responsibly and to prioritize the long-term goals of the company and its stakeholders over short-term gains that can have unfavorable long-term consequences (Muth & Donaldson, 1998).

Stewardship theory, according to scholars Daodu, Nakpodia, and Adegbite (2017), highlights the significance of responsible management, where managers behave in the best interests of the organization and its stakeholders as opposed to pursuing their own self-interests. Better long-term outcomes for the business and its stakeholders may result from this strategy. The stewardship hypothesis is oversimplified and impractical, according to critics like Pastoriza and Ario (2018) since people are prone to acting as stewards for situational as well as psychological reasons. The challenge that arises when there is a

mismatch between the management firm strategy and the psychological traits of the manager is what happens to organizational goals as these foundations do not hold true for all managers. Furthermore, the stewardship theory asserts that acting as a steward simply results from a rational process, yet it is unclear what underlying factors lead a person to make this choice.

The theory is relevant to the connection between corporate governance and fraud mitigation because it emphasizes the importance of a culture of ethical behavior and accountability in preventing fraudulent behavior. Stewardship theory suggests that manager's motivation stem from duty and responsibility sense to the firm and its stakeholders, rather than by financial incentives. This means that managers are more likely to act in the best interests of the company and its stakeholders, and less likely to engage in fraudulent behavior. Stewardship theory acclaims firms ought to adopt governance strategies that encourage managers to act as stewards of the company's resources. This can include mechanisms such as long-term incentive plans, independent board oversight, and regular performance evaluations.

2.3 Empirical Literature

This section evaluated earlier research done by other academics that was concerned with how governance systems impact the fraud prevention of Kenyan microfinance banks.

2.3.1 Executive Compensation and Fraud Mitigation

Executive compensation has been highlighted as a technique for bringing executives' interests into line with those of the business and its stakeholders. In addition to being open and equitable, compensation plans should be created to recognize performance that advances the organization's long-term objectives and core values (Girau et al., 2022). Empirical studies have been conducted in this area but there exist research gaps. This

section provides a discussion of these studies in regard to their objective, methodology, findings, and the existing research gaps.

Chen, Huddart, and Xu (2020) examined the connection between executive compensation and financial statement fraud utilizing a large sample of publicly traded U.S. firms. They focused on the link between executive compensation structure and the likelihood of financial statement fraud occurrence. The study utilized a panel regression model. The results of the study showed a substantial inverse relationship between executive pay and the risk of financial statement fraud. The researchers discovered that greater executive remuneration levels, particularly variable compensation like bonuses and stock options, were associated with a lower risk of financial statement fraud. Higher CEO remuneration, according to the study, aligns the interests of executives with those of shareholders, encouraging them to act morally and take precautions against fraud risks. In addition, the report contends that performance-based pay might give CEOs more incentives to operate in the business' best interests and discourage fraud. The conclusions of this study may not apply to other nations because it primarily focused on publicly traded American companies. Additionally, the research made use of potentially biased client self-reported data.

Ding, Jia and Wu (2020) investigated the affiliation between executive compensation, corporate governance, and fraud in Chinese firms. They examined a sample of listed companies in China and analyzed executive compensation and corporate governance mechanisms impact on the likelihood of fraudulent behavior using ordinary least square. The research conclusions discovered that higher levels of executive compensation, particularly equity-based compensation, were associated with a decreased likelihood of fraud. Additionally, the researchers found that strong corporate governance

mechanisms, like independent board directors and audit committees, further enhanced the negative association between executive compensation and fraud. The study suggests that executive compensation aligned with company performance and effective corporate governance mechanisms act as safeguards against fraudulent activities. The study failed to discriminate between the effects of various executive compensation services on fraud prevention and failed to take into consideration any endogeneity problems that could surface throughout the analysis.

Rajabzadeh and Papanastassiou (2020) investigated the relationship between CEO compensation and Iranian corporate performance. According to the research, there is a significant correlation between CEO compensation and company profitability, as shown by the ROA, ROE, and market-to-book ratio. The study also discovered a substantial correlation between CEO pay and business success in businesses with greater levels of management ownership and robust corporate governance. The study also found that the relationship between CEO compensation and firm success was weaker in businesses with larger levels of financial leverage, suggesting that having a lot of debt may work against the positive impacts of executive pay on business performance. Due to its emphasis on Iranian enterprises, which might not be representative of CEO salary patterns in other regions, the research has a contextual gap. Additionally, it did not take into account how CEO remuneration affected the reduction of fraud.

The influence of CEO pay on company performance in the Tunisian context was the main topic of Ghazouani et al.'s (2020) study. According to the analysis, there is a significant relationship between CEO compensation and company success as measured by ROA, ROE, and market value added. The study also discovered that there was a stronger positive correlation between CEO pay and business success in organizations with better

levels of financial performance and stronger corporate governance. Although the study found a limited link between CEO pay and firm success in businesses with high levels of financial risk, this finding may suggest that high levels of financial risk may attenuate the positive impacts of executive pay on company performance. One possible critique of this research is that it only focuses on Tunisian businesses, which may not be representative of CEO wages.

Research on the effect of CEO salary on business performance among European Union (EU) member nations was conducted by Dimitrova et al. (2020). According to the study, there is a connection between executive pay and business performance as shown by ROA and ROE. The study also found that companies with larger company sizes and effective corporate governance had a stronger favorable relationship between CEO remuneration and business success. The results also showed that in companies with high levels of financial debt, the relationship between CEO pay and business performance was weak. Due to its exclusive emphasis on EU member states, which might not be indicative of CEO remuneration patterns or business performance in other nations or regions, this research presents a contextual gap. Further research may be needed in this area because the study did not specifically examine the processes through which executive salary affects fraud mitigation.

In India, Ruparel et al. (2021) investigated the effect of executive salary on business performance. The study found a strong correlation between CEO pay and business success as assessed by return on assets (ROA), return on equity (ROE), and Tobin's Q. The study also discovered that organizations with higher levels of employee ownership and a stronger emphasis on innovation performed better when CEO remuneration was taken into account. Due to its exclusive emphasis on Indian businesses, which might not be indicative of

executive remuneration practices or fraud prevention in other nations or regions, this study has a contextual gap. The different ways executive remuneration affects fraud mitigation is not examined in the study, though.

2.3.2 Board Independence and Fraud Mitigation

Board independence has been identified as a mechanism to mitigate fraud. Independent directors convey external viewpoints and expertise to the board and can aid guarantee that the board is acting in the best interests of the organization and its stakeholders (Rostami & Rezaei, 2022). Empirical studies have been conducted in this area but there exist research gaps. This section provides a discussion of these studies in regard to their objective, methodology, findings, and the existing research gaps.

Balachandran et al. (2021) examined the relationship between board independence and corporate fraud utilizing a sample of Australian firms. They specifically focused on the impact of board independence on financial statement fraud occurrence. The research conclusions revealed that there is a substantial negative link between board independence and the likelihood of corporate fraud. The scholars discovered that higher levels of board independence, indicated by the presence of independent directors on the board, were associated with a reduced financial statement fraud probability. The researchers argued that independent directors bring diverse perspectives, expertise, and greater objectivity to board decision-making processes, which can help mitigate fraud risks. They also highlighted the role of independent directors in providing effective oversight, monitoring management actions, and ensuring ethical behavior within the organization. The study was carried out in Australia, a nation with a distinct cultural and economic environment from Kenya.

Fich and Shivdasani (2022) aimed to examine the impact of board independence on fraud mitigation by investigating whether busy boards (boards with multiple directorships)

affect monitoring effectiveness. The researchers collected data from a large sample of U.S. firms and analyzed the relationship between board independence and fraud incidents. They measured board independence by the independent directors' proportion in the board and evaluated fraud incidents based on publicized cases. The study found that higher levels of board independence were associated with a lower likelihood of fraud incidents. The presence of independent directors was found to improve monitoring effectiveness and reduce the probability of fraudulent behavior. This study might be criticized for concentrating only on widely reported fraud instances, which could not accurately reflect the full scope of fraud activities taking place within businesses. Additionally, the study did not distinguish between different fraud kinds or levels of severity, which might offer additional insights into the relationship between board independence and fraud prevention.

Yermack (2022) sought to investigate the association between board independence and firm valuation, which indirectly reflects the effectiveness of fraud mitigation. The researcher examined a sample of U.S. firms and analyzed the link between board size (a proxy for board independence) and firm valuation. The research utilized regression analysis to assess board size impact on market valuation. The research discovered positive link between board size and firm valuation, suggesting that companies with smaller boards, which typically have a higher proportion of independent directors, tend to have higher market valuations. This suggests that board independence helps make corporate governance procedures, such fraud prevention, more successful. This study might be criticized for measuring board independence's effect on fraud prevention indirectly by using business valuation. Despite the fact that a number of factors might affect a company's valuation, it only serves as an indirect indicator of the performance of the board and does not track fraud incidence or prevention.

In order to better understand the connection between board independence and internal control efficacy, Klein and Zur (2018) undertook this research. The authors examined a sample of 1,700 businesses that from 2010 to 2016 had identified a substantial failure in their internal controls over financial reporting. They carefully examined the traits of the boards of directors of these companies and contrasted them with those of a control group of companies that had not encountered a major deficiency in their internal controls. The study discovered that businesses with more independent boards had better internal controls. They also discovered that the audit committee's independent directors had a notably positive impact on the efficiency of internal controls. The well-designed study by the authors provides compelling evidence that increasing board independence may significantly increase the efficacy of internal controls. It is important to keep in mind that the research is based on a limited sample of businesses, thus the conclusions may not apply to all businesses.

Afzalur (2019) investigates if the board independence among Bangladesh's listed companies has an impact on the firms' economic success. The research employed a simultaneous equation technique in regulating the possible endogeniety problem with the aid of data gathered from 135 listed companies on the Dhaka Stock Exchange, usage of accounting, and market performance measurements. It is concluded that board independence has no beneficial effect on the business success of the company. However, both board independence and the success of the company are considerably and favorably impacted by the size of the board. Board independence has been an essential component of corporate board operations in many industrialized nations, but in Bangladesh it can still be a mirage. The present study will focus on microfinance banks and use firsthand knowledge, whereas the previous research used secondary data and was centered on the companies listed on the Stock Exchange.

The study by Zubeltzu-Jaka et al. (2019) focuses on how boardroom independence of companies affects their financial success. It also discusses how national circumstances influence the relationship between social and institutional surroundings. A meta-regression covering 126 independent samples revealed that boardroom independence of companies has an impact on indicators of accounting and market-based company financial performance in both positive and negative ways. Further research shows that the association between a company's board independence and financial performance is stronger in no communitarian cultures than it is in societies with more sophisticated measures to safeguard non-controlling interest investors. When a variety of model parameters and a number of methodological control elements are used, the results are trustworthy. The results are extremely significant, especially in board composition procedures where it is argued that enterprises should actively rebalance the number of independent directors across diverse social and institutional contexts in order to assure their financial success. The study had a conceptual flaw since it placed more emphasis on company performance than on fraud mitigation.

2.3.3 Independent Risk Committee and Fraud Mitigation

As Ramly and Nordin (2018) observed, an independent risk committee can also provide valuable oversight and advice on risk management issues. This committee should be composed of independent directors with relevant expertise in risk management and should have sufficient resources and authority to carry out its responsibilities. Empirical studies have been conducted in this area but there exist research gaps. This section provides a discussion of these studies in regard to their objective, methodology, findings, and the existing research gaps.

Cheng and Courtenay (2022) aimed to examine the association between board composition, including the presence of an independent risk committee, and voluntary disclosure of risk-related information. The researchers collected data from a sample of Hong Kong-listed companies and conducted regression analysis to assess the impact of board composition, plus the existence of an independent risk committee, on voluntary disclosure of risk information. The study discovered positive relationship between the presence of an independent risk committee and voluntary disclosure level of risk-related information. Firms having independent risk committees were more likely to provide comprehensive and transparent risk disclosures, which can help mitigate fraud risks. This study's emphasis on voluntary risk-related information sharing might be criticized for failing to adequately account for the effectiveness of an independent risk committee in spotting and preventing fraud. The research didn't specifically assess whether fraud occurs or is prevented in organizations.

In order to better understand how outside directors, especially those on risk committees, affect corporate value and fraud prevention, Choi, Park, and Yoo (2021) conducted an investigation. The relationship between the nomination of outside directors, particularly those on risk committees, and company value was explored by the researchers as they looked at a sample of Korean businesses. They used regression analysis and event research techniques to analyze how outside directors affected corporate value and fraud prevention. According to the study, adding outside directors—particularly those who sit on risk committees was positively correlated with rising business value. It has been discovered that the existence of independent risk committees with outside directors enhances corporate governance and lowers the possibility of fraud. The fact that this study largely employs business value as an auxiliary indicator of fraud prevention might be criticized. Firm value does not directly represent the incidence or prevention of fraud within firms, despite the

fact that it can indicate the efficacy of corporate governance procedures, such as independent risk committees.

Aguilera and Vadera (2020) looked examined the relationship between organizational corruption, which includes fraudulent operations, and corporate governance practices, such as independent risk committees. The association between corporate governance procedures and organizational corruption, including fraud, was discovered by the researchers after they performed an extensive examination of the literature and combined the results of previous empirical investigations. They examined a variety of empirical research and case studies from varied situations. According to the report, independent risk committees are crucial as a corporate governance tool for identifying and combating organizational wrongdoing, including fraud. The fact that this study uses case studies and a literature review rather than primary data analysis might be criticized. Although the study offers insightful information on the function of independent risk committees in reducing fraud, the conclusions lack empirical support.

Beasley, Carcello, and Hermanson (2022) intended to investigate the connection between the possibility of financial reporting fraud and the presence of an independent risk committee. The authors examined 468 businesses that had been the victims of financial reporting fraud between 2016 and 2020. They carefully examined the features of the boards of directors of these companies and contrasted them with those of a control group of companies that had not been the victims of fraud. According to the study, businesses with independent risk committees had lower incidences of financial reporting fraud. Additionally, they discovered that when the board of directors was not independent, the existence of an independent risk committee was particularly beneficial in preventing fraud. A well-designed study by the authors shows conclusively that an independent risk

committee is a key element in preventing financial reporting fraud. It is crucial to note that the research is based on a limited sample of businesses, which means that the conclusions could not apply to all businesses.

An accounting restatement is more likely when there is an independent risk committee in place, according to research by Cohen, Krishnamoorthy, and Wright (2018). The authors selected 1,000 companies as a sample from 2007 to 2015 that had submitted an accounting restatement. They looked at the features of the boards of directors of these companies and contrasted them with those of a control group of companies that had not submitted an accounting restatement. The researchers discovered that businesses with independent risk committees had lower accounting restatement rates. They also discovered that, in cases where the board of directors was not independent, the existence of an independent risk committee was particularly useful in averting accounting restatements. Other areas of fraud prevention were not included because the study's focus was on accounting restatements.

2.3.4 Code of Conduct and Fraud Mitigation

Ethical standards and codes of conduct also help mitigate fraud. They should be established and communicated to all employees, and appropriate mechanisms put in place to monitor compliance and address violations (CIMA Report, 2019). Empirical studies have been conducted in this area but there exist research gaps. This section provides a discussion of these studies in regard to their objective, methodology, findings, and the existing research gaps.

In order to determine how the presence of a code of conduct and the possibility of financial reporting fraud are related, Beasley et al. (2022) conducted research. The authors examined 468 businesses that had been the victims of financial reporting fraud between

2016 and 2020. They looked at the traits of the businesses' codes of conduct and contrasted them with those of a control group of enterprises that had not been the victims of fraud. According to the study, businesses with codes of conduct had lower incidences of financial reporting fraud. They also discovered that when the board of directors was not independent, a code of conduct was very beneficial in preventing fraud. The study has a conceptual flaw because it ignores how codes of behavior affect microfinance institutions' efforts to reduce fraud.

Kaptein (2022) sought to investigate how employee responses to perceived misconduct, including reporting fraudulent activities, are influenced by ethical culture, including the presence of a code of conduct. To determine the link between an organization's ethical culture, including the clarity and efficacy of its code of conduct, and the likelihood of reporting misconduct witnessed, the researcher polled workers from a variety of firms. The poll asked questions regarding the leadership's ethical standards, the perception of the ethical climate, and readiness to report dishonest activity. The study discovered that workers' propensity to report witnessed wrongdoing, including fraud, was positively correlated with an organization's strong ethical culture, which is characterized by the presence of an effective code of conduct. This study's reliance on employee self-reported data and impressions, which might be biased or imprecise, is likely to draw criticism. Furthermore, rather than explicitly assessing the efficiency of a code of conduct in preventing or detecting fraud, the research concentrated on the intention to report fraud.

Trevio, Weaver, and Reynolds (2021) sought to perform a thorough evaluation of the literature on behavioral ethics in companies, including the function of a code of conduct in fostering moral behaviour and reducing dishonest behavior. In order to better understand behavioral ethics in businesses, the researchers evaluated and summarized the current

empirical data, theoretical frameworks, and models. They looked at a variety of factors, such as the effect of codes of conduct on reducing fraudulent behavior, that affect ethical decision-making and behavior. The study discovered that a good code of conduct is a key instrument in influencing ethical behavior inside firms. A code of conduct gives direction on right behavior, establishes clear expectations and standards for employees, and encourages moral decision-making. This study's reliance on a review and synthesis of prior research as opposed to direct data analysis might be criticized, in certain cases. Further empirical research is required to examine the precise effects of various elements of a code of conduct on preventing and detecting fraud in various organizational contexts, even though the research provides insightful information about the role of a code of conduct in promoting ethical behavior and fraud mitigation.

A summary of codes of conduct and their possible applicability in a variety of industries, including financial, is given by Sheth and Dattani (2019). It looks at the advantages and difficulties of using a code of conduct in finance and considers how a code of conduct may change the financial industry. According to the report, financial industry codes of conduct may boost productivity, cut expenses, and boost security. It also emphasizes the necessity of regulatory structures to deal with the difficulties brought on by codes of conduct. Due to the varied social and cultural environments in a mature context like the one this research was conducted in, the conclusions may not be applicable to a developing context like Kenya.

In their study, Klein and Zur (2018) sought to determine how well internal controls function in relation to a code of conduct. The authors utilized a sample of 1,700 businesses that had internal controls over financial reporting that were materially poor between 2010 and 2016. They looked at the features of these companies' codes of conduct and compared

them to the standards set by the boards of directors of a control group of companies that had no major weaknesses in their internal controls. According to the study, businesses with effective internal controls were more likely to have effective codes of conduct. They also found that having independent directors on the audit committee was particularly useful for illuminating the efficacy of internal controls. The well-designed study by the authors provides compelling evidence that improving the efficiency of internal controls depends in large part on the code of conduct. It is crucial to note that the research is based on a limited sample of businesses, which means that the conclusions could not apply to all businesses.

2.4 Summary of Literature Review and Research Gaps

Even though there has been a sizable amount of study on the connection between corporate governance and the reduction of fraud, there are still some research gaps. There was still a need for research that explores how these mechanisms interact with contextual elements including industry type, country, and organizational culture, even though several studies have examined the relationship between certain corporate governance methods and fraud reduction. Understanding how corporate governance and fraud mitigation are context-specific can assist give more nuanced insights into the efficacy of various governance strategies.

Although the relationship between corporate governance practices and fraud mitigation has been the subject of several studies, more work is still needed to understand how these factors affect fraud prevention. Understanding the underlying processes can offer more in-depth insights on the effectiveness of the particular governance systems and how they might be improved.

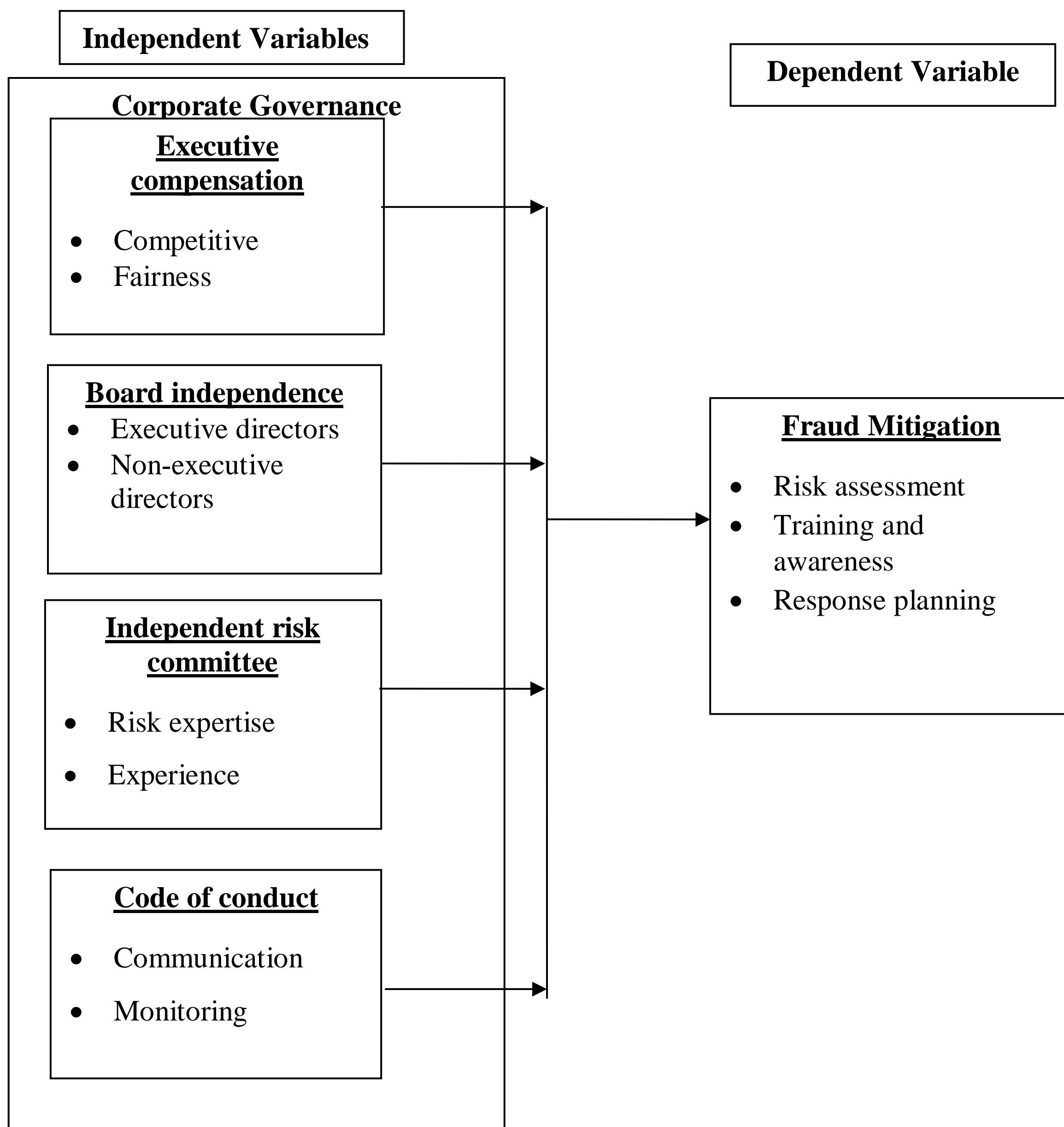
2.5 Conceptual Framework

A diagram showing the relationship between the independent and dependent variables in this study is shown in Figure 2.1. Fraud reduction was the relying factor, whereas executive

compensation, board independence, independent risk committee, and code of conduct were the independent factors. It was theoretically hypothesized that a rise in executive compensation, board independence, independent risk committee or code of conduct would enhance fraud mitigation among microfinance banks in Kenya.

FIGURE 2.1

Conceptual Framework



2.6 Operationalization of Variables

TABLE 2.1

Operationalization of Variables

Variable type	Variable	Indicators	Measurement scales
Dependent	Fraud mitigation	• Risk assessment • Training and awareness • Response planning	Likert/Interval
Independent	Executive compensation	• Competitive • Fairness	Likert/Interval
Independent	Board independence	• Executive directors • Non-executive directors	Likert/Interval
Independent	Independent risk committee	• Risk expertise • Experience	Likert/Interval
Independent	Code of conduct	• Communication • Monitoring	Likert/Interval

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

The research design that was used as a framework for this study is highlighted in this section. The research's target population, the sampling strategy, the tools and processes for gathering data, and lastly the collection and analysis of data as well as the presentation of the results are other parts that were covered.

.3.2 Research Design

The conceptual setting for conducting the survey makes reference to research design. A descriptive cross-sectional research design was employed to address the research issue for the study. According to Cooper and Schindler (2018), descriptive research tries to pinpoint the presence of a phenomena and its specifics, such as what, when, or how it occurs. This methodology was ideal because it allowed the researcher to utilize quantitative data to assess how corporate governance affect Kenyan microfinance institutions' ability to reduce fraud.

3.3 Target Population

According to Kothari (2014), the term "target population" refers to a group of individuals or things that have the same qualities or behaviors. Most people in the population share this characteristic. The research population was the 349 employees in top management, middle management and lower level management in the 14 microfinance institutions that are CBK licensed as shown in Appendix III. The population was as Table 3.1 depicts.

TABLE 3.1

Target Population

Target Population	No. of Employees
Top Level	56
Middle Level	108
Lower Level	185
TOTAL	**349**

Source: Central Bank of Kenya internal data (2023)

3.4 Sample Size and Sampling Procedure

Sampling refers to the complete process of selecting particular individuals or things from a wider group. The term "sampling technique" refers to the method used to choose the sample. Because it enables the researcher to split the sample into appropriate, mutually exclusive strata, stratified random sampling was employed in this study. According to their cadre, the employees were split. According to Cooper and Schindler (2018), this sampling technique increases the sample's statistical efficiency, provides adequate data for analyzing each subpopulation, and enables the use of various study methodologies in various strata. The method, according to Khan (2018), comprises creating a straightforward random sample for each subgroup after segmenting the research population into numerous groups.

The research adopted Yamane (1967) formula with 95% confidence level assumption in estimating the sample size.

$$n = \frac{N}{1 + N(e)^2}$$

Where:

n = sample size

N = population size

e = the level of precision

1 = Constant

$$n = 349/\ 1 + 349(0.05)^2$$

$$= 186.38 \approx 186 \text{ respondents}$$

The sample size for this research was 186 employees after substituting these numbers into the calculation above. Table 3.2 shows the sample size as follows:

TABLE 3.2

Sample Size

Category	Population	Sample size
Top Level	56	30
Middle Level	108	58
Lower Level	185	98
TOTAL	**349**	**186**

3.5 Data Collection Instruments

In order to answer research questions, test hypotheses, and assess results, data collection is a systematic process of acquiring and analyzing data pertaining to certain variables of interest (Burns & Burns, 2018). The types of research instruments to be utilized depend on the information that has to be gathered. To gather primary data, the respondents were asked to complete a questionnaire. The primary data was essential in explaining the actual context of the relationship between the dependent and independent variables. Utilizing questionnaires made sense since they are a quick, low-cost, and productive way to collect data. Closed-ended questions were included in the questions' design. Closed-ended inquiries enabled the researcher to arrive at precise conclusions.

3.6 Data Collection Procedures

Data collection is the process of gathering empirical information to answer the questions that led to the study and to get novel insights into a situation (Khan, 2018). The appropriate authorities were asked for permission before any data was collected. The questionnaire was considered beneficial in data collection since the resource individuals were thought to be sufficiently competent. Google forms were used to administer the survey. There were follow-ups to guarantee a high response rate. All ethical guidelines were followed.

3.7 Pilot Test

The research tool's accuracy and relevance are crucial. A pilot study was carried out in this respect. To determine whether doing a comprehensive investigation was feasible, a pilot study was carried out. A pilot research, with 19 individuals, was carried out on a sample of 10% of the 186 target respondents to verify the validity and reliability of the questionnaire. In order to make the questionnaire more consistent and trustworthy in addressing the study objectives, the researcher provided it to two microfinance institutions and asked for their input on the questions as well as any areas where respondents feel modifications were necessary. The final research did not include the 19 responders in the study.

3.7.1 Validity of Data Collection Instrument

The accuracy with which an instrument can measure a given idea determines the validity of the instrument (Cooper & Schindler, 2018). Contrarily, construct validity is used to assess whether the operational definition of variables corresponds to the concept's intended theoretical meaning. In order to do this in the current study, the researcher adapted an already-existing questionnaire in accordance with findings from earlier investigations. On the other hand, the advice of professional opinion supported the veracity of the material. To guarantee that all research variables were recorded, it was necessary to have study supervisors who carefully reviewed the questionnaire and provided knowledgeable input. Additionally, they verified the study to make sure the theoretical dimensions were given as intended.

3.7.2 Reliability of Data Collection Instrument

According to Cooper and Schindler (2018), reliability is a statistic used to describe the overall consistency of an instrument. When a measurement regularly yields comparable outcomes when used in same situations, it is said to have high dependability. By demonstrating the accuracy of the internal data collection method, Cronbach alpha analysis

helped in assessing the dependability of the research instruments. Cronbach's Alpha is a dependable dependability metric that displays a real "base" score. Even if similar items are included in place of some of the original ones, Cronbach's Alpha is essential to a researcher in determining the validity and reliability of the questionnaire (Khan, 2018). Most people consider a dependability rating of between 0.7 and 0.8 to be adequate, and anything over 0.8 to be excellent. This bar was applied to the study. The reliability test results are as shown in Table 3.3

TABLE 3.3
Reliability Results

Variables	Items	Cronbach Alpha	Remark
Executive compensation	6	.784	Reliable
Board independence	6	.749	Reliable
Independent risk committee	6	.872	Reliable
Code of conduct	6	.798	Reliable
Fraud mitigation	6	.937	Reliable

3.8 Data Analysis and Presentation

Data analysis is the process of modifying and arranging that raw data into a clear, methodical, and scientific form that makes it simple to read and understand (Burns & Burns, 2018). According to Kothari (2014), it comprises a number of intricately related procedures meant to summarize and arrange the acquired data in a way that responds to the research question. The survey results were examined, their quantity counted, and their completeness and sufficiency evaluated by the researcher. Based on their suitability, the questionnaires were sorted. Each question received a different code, which was then scored. After that, the data was input into a computer for examination and summary in order to assess the strength of any emergent themes. The descriptive aspects of the data were analyzed using the mean as a measure of central tendency and the standard deviation as a measure of dispersion, while investigation of the presence of links between and among variables was done using correlation and regression. SPSS version 27 was used.

3.8.1 Model Summary

The regression model below was used:

$$\mathbf{Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon}$$

Where: Y = Fraud mitigation

α =y regression intercept.

β_1, β_2, β_3, β_4= Model coefficients

X_1 = Executive compensation

X_2= Board independence

X_3= Independent risk committee

X_4= Code of conduct

ε =error term

3.9 Pretesting of Multiple Regression Assumptions

Diagnostic checks were performed to make sure that no breaches of the fundamental rules of the traditional linear regression model have taken place before moving on to the equations' computation. Skewed and ineffective model parameters appear when the rules of a conventional regression model are broken. In order to ensure that the regression analysis rules were not broken, diagnostic tests were performed.

3.9.1 Normality Test

Statistical methods such as the Shapiro-Wilk test or the Kolmogorov-Smirnov test were used to examine if the residuals of the response variables are distributed normally around the mean**.**

3.9.2 Multicollinearity Test

The study used a correlation matrix to determine multicollinearity, using an ideal multicollinearity threshold of 0.8 (Cooper & Schindler, 2018). High standard errors occur when multicollinearity is ignored since it leads to endless standard errors and indeterminate

regression coefficients. This has an effect on how precisely the null hypothesis is rejected or not. The estimate procedure is impacted by the multicollinearity's degree. As a result, high multicollinearity is indicated by a correlation coefficient larger than 0.8.

3.9.3 Heteroscedasticity

If heteroskedasticity does occur, it has to be verified and fully taken into account in the CLRM. The CLRM shows that the variance of the error term is constant. The data is said to as homoscedastic if the error variance is not constant. Running a regression analysis without first confirming heteroskedasticity will result in unbiased estimated coefficients and inaccurate standard errors. The Khan (2018) developed Likelihood Ratio (LR) test was used in this work to evaluate heteroskedasticity. The presence of homoscedastic error variance was the null hypothesis for this test.

CHAPTER FOUR

RESULTS AND DISCUSSION

4.1 Introduction

In this chapter, the survey's outcomes are presented. This section of the chapter are general information sections, which include demographic data and the response rate. The chapter also emphasizes the descriptive and inference statistics in relation to the aims of the research.

4.2 Response Rate

In a research study, the response rate is calculated as the number of received replies divided by the number of target participants. The response rate, which is frequently expressed as a percentage, is also known as the completion rate or return rate. Details on the response rate for this research are provided in Table 4.1.

TABLE 4.1
Response Rate

Response Rate	Frequency	Percent
Returned	145	78
Unreturned	41	22
Total	**186**	**100**

Table 4.1 shows that 186 questionnaires were distributed to the managers at each of the 14 microfinance banks in Kenya. Only 145 of the 186 questionnaires dispersed to the target respondents were fully filled and returned, translating to 78 percent study response rate, according to the study's conclusions. This supports Burns and Burns (2018) assertion that analysis and conclusion-drawing are appropriate for studies with a response rate of 70% or more.

4.3 Demographic Characteristics

Demographic information provides a snapshot of the characteristics of the respondents. This information helps to describe the sample or population under study and provides a basis for analyzing and interpreting the data in relation to these demographic variables. It allows researchers to understand the demographic composition of the sample and identify any potential biases or limitations in the data. The first questionnaire segment intended to get data of the general information concerning the profile of the respondents. The segment covered age, gender, highest levels of education and number of years in the current position.

4.3.1 Gender of the Respondents

The target respondents were implored to state their gender. Table 4.2 displays the findings.

TABLE 4.2
Gender Distribution

Gender	Frequency	Percentage
Male	76	52.4
Female	69	47.6
Total	**145**	**100**

Table 4.2 shows that there were a total of 145 respondents in the study, of which 52.4% were male and 47.6% were female. This means that the sample was relatively well-balanced in terms of gender. The descriptive results on the gender of the respondents suggest that women are well-represented in the management workforce at microfinance banks in Kenya.

4.3.2 Age of the Respondents

The study wanted to establish the age of the participants involved in this research. Age is closely tied to the respondent's stage in the lifecycle and their corresponding developmental milestones, responsibilities, and priorities. Different age groups may have different needs, aspirations, and challenges based on their life stage (young adulthood, middle age, or older

adulthood). Knowing the respondents' ages is crucial since a person's age might affect how they respond to the survey. The results are shown in Table 4.3.

TABLE 4.3
Respondents' Age Composition

Age	Frequency	Percentage
21-30 years	6	4.1
31-40 years	28	19.3
41-50 years	72	49.7
Above 50 years	39	26.9
Total	**145**	**100**

The majority of respondents (49.7%) were in the 41-50 age group, followed by the above 50 age group (26.9%), the 31-40 age group (19.3%), and the 21-30 age group (4.1%). This age distribution suggests that the majority of management employees at microfinance banks in Kenya are middle-aged or older. This is likely due to the fact that management positions typically require experience and expertise. The youngest age group (21-30 years) was the smallest group of respondents. This may be due to the fact that this age group is less likely to have the experience and qualifications required for management positions.

4.3.3 Highest Level of Education

The participants were expected to input their highest education level. The finds are illustrated in Table 4.4. The finding shows the highest level of education of the 145 respondents who participated in the study. The majority of respondents (67.6%) had a degree, followed by those with a master's degree (27.6%), a diploma (4.1%), and a PhD (0.7%). This educational distribution suggests that the majority of management employees at microfinance banks in Kenya have a high level of education. This is likely due to the fact that management positions typically require strong analytical and problem-solving skills, which can be developed through higher education.

TABLE 4.4
Highest Level of Education

Education	Frequency	Percentage
Diploma	6	4.1
Degree	98	67.6
Masters	40	27.6
PhD	1	0.7
Total	**145**	**100%**

4.3.4 Years of Experience with the Firm

The participants were requested to designate how long they had been with their current employer. The period spent with an organization can be used to gauge their understanding of internal organizational processes, capabilities, as well as success.

TABLE 4.5
Years of Experience with Current Employer

Number of years	Frequency	Percentage
Less than 1 year	4	2.8
1-3 years	32	22.1
4-7 years	90	62.1
8 years and above	19	13.1
Total	**145**	**100%**

The majority of respondents (62.1%) had 4-7 years of experience with their current employer, followed by those with 1-3 years of experience (22.1%), less than 1 year of experience (2.8%), and 8 years and above of experience (13.1%). This experience distribution suggests that the majority of management employees at microfinance banks in Kenya have a moderate level of experience with their current employer. This is likely due to the fact that microfinance is a relatively new sector in Kenya, and many microfinance banks have been established in the past 10 years. The proportion of respondents with 8 years and above of experience (13.1%) is relatively low. This may be due to the fact that many microfinance banks are still expanding and growing, and may be looking for managers with more experience in the sector.

4.4 Descriptive Statistics

The researcher was able to synthesize and define the key traits, patterns, and distributions of the gathered data using descriptive statistics. Statistical summaries that transmitted crucial information about central tendency, variability, and the shape of the data distribution were supplied by measures like mean and standard deviation. Each variable under study's descriptive data are reported in the subheading as percentages, means, and standard deviations.

4.4.1 Executive Compensation

Table 4.6 gives the mean as well as standard deviation for the definite executive compensation aspects.

TABLE 4.6
Descriptive Statistics for Executive Compensation

Statements	N	Mean	Std. Dev
The executive compensation package in this microfinance bank is better than the other firms in the industry	145	4.32	0.55
Executives in this organization are eligible for an annual bonus or performance-based incentive pay	145	3.99	0.51
Executives in this organization are eligible for long-term incentive pay such as stock options	145	3.88	0.33
The executive compensation has been rising over the years	145	3.99	0.69
I am satisfied with the firm's executive compensation	145	4.23	0.46
The executive compensation in this firm can be described as fair	145	3.86	0.36
Overall mean Score	**145**	**4.05**	**0.48**

From the gathered data, it is evident that respondents generally perceive the executive compensation package within their microfinance banks to be superior to other firms in the industry, with a mean of 4.32 and a standard deviation of 0.55. This indicates a high level of agreement with this statement among the respondents and signifies that the

compensation packages are considered competitive. Regarding the annual bonus or performance-based incentive pay, the mean response was 3.99 with a standard deviation of 0.51, suggesting that executives in these organizations are usually eligible for such bonuses, although there may be some variability across different banks or individual executive contracts.

The response to the eligibility for long-term incentive pay such as stock options had a mean of 3.88 with a relatively low standard deviation of 0.33, indicating that this is a common practice, with low variability in responses, in the microfinance banks under consideration. The statement concerning the rising trend of executive compensation over the years received a mean score of 3.99 and a standard deviation of 0.69. This suggests that there is a general agreement among respondents that executive compensation has been incrementing over the years, with some variation in the extent to which it is believed to have risen.

The level of satisfaction with the firms' executive compensation is high, evidenced by a mean of 4.23 and a standard deviation of 0.46, depicting that most respondents are content with the executive compensation in their respective firms. Similarly, the fairness of the executive compensation in these firms is indicated by a mean of 3.86 and a low standard deviation of 0.36. While this mean is slightly lower compared to other statements, it still represents a positive perception of fairness in executive compensation among the respondents, with a consensus on this view. Finally, the overall mean score of 4.05 with a standard deviation of 0.48 implies a generally positive perception of executive compensation among the surveyed employees in the microfinance banks in Kenya, with moderate variability in responses.

4.4.2 Board Independence

Table 4.7 provides insights into the perception of board independence among respondents in the microfinance banks in Kenya. The gathered data highlights various aspects of board functioning, the role of non-executive directors, the assessment of internal audit functions, and how conflicts of interest are handled within the board. Here is the interpretation of each statement based on the provided descriptive statistics.

TABLE 4.7
Descriptive Statistics for Board Independence

Statements	N	Mean	Std. Dev
In our board, non-executive directors outnumber executive directors.	145	3.71	0.67
The board regularly assesses the effectiveness of the internal audit function.	145	3.75	0.43
On occasion, members submit formal declarations of conflicts of interest to the chair	145	3.41	0.69
The executives of the company do not have any influence over the board's choices.	145	3.87	0.59
The board independently evaluates the findings of internal audits, management's comments, and corrective actions.	145	3.52	0.98
Since their reputations are on the line, external directors are adequately motivated to supervise management.	145	3.17	0.78
Overall Mean Score	**145**	**3.57**	**0.68**

The statement that non-executive directors outnumber executive directors has a mean of 3.71 and a standard deviation of 0.67. This suggests that respondents generally agree that there is a significant presence of non-executive directors on the board, which typically is a good indicator of board independence, but there is also some variability in responses, possibly reflecting differences among the microfinance banks in the composition of their boards. The mean score of 3.75 and a standard deviation of 0.43 for the regular assessment of the internal audit function by the board indicate that respondents largely agree that the boards are proactive in assessing the internal audit function. The

relatively low standard deviation implies that this perception is fairly consistent among respondents.

The mean value for the formal declaration of conflicts of interest is 3.41, with a standard deviation of 0.69. This indicates a moderate level of agreement among respondents that board members do, on occasion, submit formal declarations of conflicts of interest. The higher standard deviation suggests a higher dispersion in responses, possibly due to variations in the practices or experiences of respondents across different organizations. The statement regarding the influence of executives over the board’s choices received a mean of 3.87 and a standard deviation of 0.59. This relatively high mean value implies that respondents generally believe that executives do not significantly influence the board’s decisions, suggesting a perception of independence in decision-making processes within the board.

The independent evaluation by the board of internal audits, management's comments, and corrective actions has a mean of 3.52 but with a relatively high standard deviation of 0.98. This implies a moderate agreement that boards do independently evaluate audit findings but also suggests a substantial variation in responses, indicative of differing perceptions and possibly practices among the surveyed banks. The motivation of external directors to supervise management, given that their reputations are at stake, received the lowest mean score of 3.17, with a standard deviation of 0.78. This suggests that respondents are less convinced about the motivational factors of external directors to supervise management effectively, with varied opinions on this matter among respondents. The overall mean score of 3.57 with a standard deviation of 0.68 illustrates a moderately positive perception of board independence among respondents, with some variability in their responses.

4.4.3 Independent Risk Committee

Table 4.8 sheds light on respondents' perspectives regarding the independent risk committee's composition, compliance, proficiency, and effectiveness within the microfinance banks in Kenya. Each statement's interpretation is as follows, based on the presented descriptive statistics.

TABLE 4.8
Descriptive Statistics for Independent Risk Committee

Statements	N	Mean	Std. Dev
Sources outside of management identify eligible risk committee members	145	3.63	0.69
Members of the risk committee have the necessary financial credentials to carry out the charter's objectives	145	3.53	0.86
The risk committee is well-versed in the industry and has a diverse range of experiences and backgrounds.	145	3.63	0.84
The risk committee's members comply with all relevant independence standards.	145	4.23	0.42
The independent risk committee exhibits honesty, reliability, and trustworthiness, and they are able to deal with problems before they become serious.	145	4.70	0.47
The independent risk committee keeps an eye on adherence to the rules and principles of corporate governance.	145	4.46	0.52
Overall Mean Score	**145**	**4.03**	**0.73**

The statement regarding the sources outside of management identifying eligible risk committee members has a mean of 3.63 and a standard deviation of 0.69. This signifies a general agreement among respondents that the selection of risk committee members is typically independent of management, highlighting an attempt to ensure objectivity and impartiality in risk assessments, but there is also a notable variability in responses, reflecting potential differences in practices among the surveyed banks. The mean value of 3.53 with a standard deviation of 0.86 on the financial credentials of risk committee members suggests that there is a moderate level of agreement among respondents about the committee members having the necessary financial knowledge to fulfill the committee's

objectives. The relatively high standard deviation denotes varied opinions or experiences among respondents, indicating that this is an area where practices may differ significantly across different banks.

For the risk committee being well-versed in the industry and having diverse experiences and backgrounds, the mean score is 3.63 and the standard deviation is 0.84. This implies that respondents generally agree that the risk committees have a considerable understanding of the industry and exhibit diversity in their experiences and backgrounds, but there is also substantial variability in responses, possibly due to differences in the composition of risk committees among the banks. The statement about the risk committee's compliance with all relevant independence standards has a high mean of 4.23 and a relatively low standard deviation of 0.42, showing a strong consensus among respondents that the members of the risk committee adhere to independence standards. This implies a high level of integrity and autonomy in the functioning of the risk committees across the surveyed banks.

The highest mean score of 4.70, coupled with a standard deviation of 0.47, is attributed to the reliability, honesty, trustworthiness, and proactivity of the independent risk committee in dealing with problems before they escalate. This overwhelmingly positive response indicates a high level of trust and confidence in the effectiveness and integrity of the risk committees among the respondents. Regarding the independent risk committee's role in monitoring adherence to corporate governance principles and rules, the mean is 4.46 with a standard deviation of 0.52. This high mean score with moderate variability indicates a strong agreement among respondents that the risk committees are vigilant and effective in ensuring compliance with corporate governance norms. The overall mean score for the independent risk committee is 4.03, with a standard deviation of 0.73, reflecting a generally

positive perception of the independent risk committees' role, competence, and effectiveness among the respondents, with some variation in individual responses.

4.4.4 Code of Conduct

Table 4.9 provides valuable insights into the perceptions and experiences of respondents regarding the ethical conduct and responsible practices in microfinance banks in Kenya. Here is the interpretation for each statement provided in the table, based on their respective mean and standard deviation.

TABLE 4.9
Descriptive Statistics for Code of Conduct

Statements	N	Mean	Std. Dev
All employees are familiar with the organization's ethical code of conduct	145	4.12	1.02
Employees have received training on the ethical code of conduct	145	3.99	0.98
The organization's ethical code of conduct is clearly written and easy to understand	145	3.88	0.92
Employees feel comfortable reporting behaviour that they believe is in violation of the ethical code of conduct	145	3.87	1.03
This microfinance bank ensures that its loan terms and conditions are clearly communicated to borrowers	145	3.64	0.97
This microfinance bank promotes responsible lending practices, considering the borrowers' ability to repay.	145	4.21	0.67
Overall Mean Score	**145**	**3.95**	**0.89**

The mean score of 4.12 and a standard deviation of 1.02 for familiarity with the organization's ethical code of conduct suggest that the majority of employees are well-acquainted with the ethical standards set by their organization. However, the relatively high standard deviation indicates a variation in responses, implying that experiences with and understanding of the ethical code may differ significantly among employees. Employees' training on the ethical code of conduct has a mean value of 3.99 and a standard deviation of 0.98, indicating that most respondents agree that adequate training is provided. However,

the high standard deviation implies a noticeable disparity in the training received by different employees, suggesting inconsistency in training dissemination.

The clarity of the organization's ethical code of conduct received a mean of 3.88 and a standard deviation of 0.92, showing that the code is generally perceived as clearly written and understandable. However, the variability in the responses hints at differing opinions on the clarity and comprehensibility of the ethical code among different respondents. The statement regarding employees' comfort in reporting behavior they believe violates the ethical code has a mean of 3.87 and a standard deviation of 1.03. This denotes that, generally, employees feel at ease reporting unethical conduct, but the elevated standard deviation signifies diverse experiences and comfort levels among respondents in reporting such behavior.

The clear communication of loan terms and conditions to borrowers received a lower mean of 3.64, with a standard deviation of 0.97, implying a lesser agreement among respondents on the organization's effectiveness in communicating loan terms. The high standard deviation reflects a substantial variation in perceptions, potentially indicative of inconsistencies in communication practices across different banks or individual cases. The promotion of responsible lending practices considering borrowers' ability to repay has a high mean value of 4.21, coupled with a lower standard deviation of 0.67. This suggests strong agreement among respondents that their microfinance bank promotes responsible lending, with relatively consistent experiences and perceptions across respondents in this regard. The overall mean score of 3.95 and a standard deviation of 0.89 indicate a generally positive perception and experience with the ethical code of conduct and responsible lending practices among the respondents, with some variation in individual experiences and perceptions.

4.4.5 Fraud Mitigation

Table 4.10 portrays the respondents' awareness, training, and the measures in place in the microfinance banks in Kenya to detect, prevent, and report fraudulent activities. Below is an interpretation of each statement provided in the table, utilizing their mean and standard deviation values.

TABLE 4.10
Descriptive Statistics for Fraud Mitigation

Statement	N	Mean	Std. Dev.
I am aware of the organization's policies and procedures for detecting and preventing fraud	145	4.34	0.69
Employees have received training on how to detect and prevent fraud in their job function	145	3.75	0.94
There are channels or hotlines available to report any fraudulent activity	145	3.87	1.03
The organization encourage employees to report any suspected fraud or unethical behaviour	145	3.96	0.98
The organization conduct a risk assessment to identify areas vulnerable to fraud	145	3.88	0.67
The organization conducts regular internal audits to assess the effectiveness of its fraud prevention controls	145	4.33	0.53
Average	**145**	**4.02**	**0.85**

With a mean of 4.34 and a standard deviation of 0.69, the responses suggest a high level of awareness among employees about the organization's policies and procedures for detecting and preventing fraud. However, the presence of some degree of variation in the responses as indicated by the standard deviation implies a few disparities in the level of awareness among the respondents. The training on how to detect and prevent fraud scored a mean of 3.75 with a standard deviation of 0.94. While the majority of the respondents have received training on fraud detection and prevention, the high standard deviation reveals considerable variation in the responses, hinting at inconsistencies in the dissemination of training among the employees.

The statement regarding the availability of channels or hotlines to report any fraudulent activity has a mean of 3.87 and a standard deviation of 1.03. This suggests that while there are generally known avenues available for reporting fraudulent activities, the high standard deviation highlights a substantial variation in the experiences or perceptions of their availability among different respondents. The organization's encouragement to employees to report any suspected fraud or unethical behavior scored a mean of 3.96 and a standard deviation of 0.98, reflecting that employees generally feel encouraged to report unethical behavior or suspected fraud. However, the fairly high standard deviation indicates divergent perceptions or experiences in the encouragement received to report such behaviors.

The conduct of a risk assessment to identify areas vulnerable to fraud received a mean value of 3.88 and a standard deviation of 0.67, revealing that respondents generally believe that the organization undertakes risk assessments to spot vulnerabilities. The moderate standard deviation implies moderate variability in responses, suggesting some differing opinions or experiences regarding the thoroughness or frequency of such risk assessments. The organization's regular conduct of internal audits has a high mean of 4.33 and a low standard deviation of 0.53, indicating strong agreement among respondents on the frequent and effective execution of internal audits to assess the robustness of its fraud prevention controls, with relatively uniform perceptions across respondents. The overall average mean score of 4.02 with a standard deviation of 0.85 implies a generally positive perception and confidence in the fraud mitigation measures implemented by the microfinance banks, but with some level of variability in individual experiences and perceptions.

4.5 Diagnostic Tests

Assuming that the data follows all the assumptions of ordinary least square when performing statistical modus operandi such as correlations, regression, t-tests, and variance analysis. These analyses need to be verified since they include statistical flaws. To check for these statistical mistakes, this study checked for normalcy, multicollinearity, and heteroskedasticity. This was done to see whether the data set could be effectively modelled. To test normality, we used Shapiro-Wilk's test. Variance inflation factors and tolerance were used to examine multicollinearity and Levene's test was used to examine heteroskedasticity. The outcomes of various statistical tests are shown in this subsection.

4.5.1 Tests of Normality

The Shapiro-Wilk test was used to look for normalcy. This test looks for skewness, kurtosis, or both to evaluate how normal the data are. The Shapiro-Wilk statistic has a range of 0 to 1, and values higher than 0.05 are indicative of normal data. The data significantly deviates from the normal distribution when it is less than 0.05. Data normality was verified using the Shapiro-Wilk test, and the results indicated that all variables had a p-value larger than 0.05 ($p > 0.05$). The notion that the sample distribution of the mean is normal is referred to as "normality". The results of the normalcy test are shown in Table 4.11.

TABLE 4.11
Test of Normality

	Shapiro-Wilk		
Study variables	Statistic	Df	Sig.
Executive compensation	0.734	145	0.165
Board independence	0.799	145	0.183
Independent risk committee	0.803	145	0.187
Code of conduct	0.792	145	0.178
Fraud mitigation	0.933	145	0.224

Table 4.11's findings show that all of the p values are higher than the threshold value of 0.05, supporting the theory that the data came from a population with a regularly distributed distribution.

4.5.2 Tests of Multicollinearity

Multicollinearity is the term for when there is a considerable amount of correlation between independent variables. To examine multicollinearity, one uses the variance inflation factor (VIF). The VIF counts the amount that the estimated coefficient's variance is exaggerated in the absence of any connection between the independent variables. If there is no correlation between two independent variables, all VIFs will be 1. A VIF of 5 indicates some multicollinearity, whereas a VIF of 10 indicates severe multicollinearity. The variance inflation factor (VIF), which was used to this study's multicollinearity test, is displayed in the results. The opposite of variance inflation factor, tolerance measures the effect of one independent variable on all other independent variables. Table 4.12 displays the test outcomes.

TABLE 4.12
Test of Multicollinearity

Variable	VIF	Tolerance
Executive compensation	4.327	0.231
Board independence	2.332	0.429
Independent risk committee	1.487	0.672
Code of conduct	3.275	0.305
Mean VIF	2.855	

All of the variables had a VIF between 1.487 and 4.327, according to the results in Table 4.13, and tolerance values ranged from 0.231 to 0.672. This demonstrated the absence of multicollinearity in the independent variables.

4.5.3 Tests of Heteroscedasticity

When the variance of the errors in the dependent variable is not constant over the whole set of data, heteroscedasticity takes place. It happens when the values of the independent variables change the variance of errors. Heteroscedasticity in regression analysis is a systematic change in the dispersion of the residuals over the spectrum of measured values. Ordinary least squares regression makes the assumption that residuals come from a population with constant variance. High levels of heteroscedasticity in this regression can significantly skew the outcomes, undermine the analysis, and increase the likelihood of a type 1 error. In this study, homogeneity was assessed using heteroscedasticity Breusch-Pagan/Cook-Weisberg test. The variances between groups are unequal if the Breusch-Pagan/Cook-Weisberg test for heteroscedasticity is statistically significant = 0.05. It is a test to examine if the scores in the variables have about the same dispersion. The outcomes are displayed in Table 4.13.

TABLE 4.13
Test of Heteroscedasticity

Breusch-Pagan / Cook-Weisberg test for heteroscedasticity		
chi2(1)	=	0.5632
Prob > chi2	=	0.4165

Table 4.13 demonstrates that the null hypothesis of homoscedastic error terms is not rejected with a p-value of 0.4165.

4.6 Correlation Analysis

Table 4.14 presents the correlation results between the dependent variable, Fraud Mitigation, and various independent variables such as Executive Compensation, Board Independence, Independent Risk Committee, and Code of Conduct. The Pearson correlation coefficient ranges between -1 and 1, with 1 indicating a perfect positive

correlation, -1 indicating a perfect negative correlation, and 0 indicating no correlation. A correlation marked with ** is significant at the 0.01 level, denoting a statistically significant relationship between the variables.

TABLE 4.14
Correlation Results

		Fraud mitigation	Executive compensation	Board independence	Independent risk committee	Code of conduct
Fraud mitigation	Pearson Correlation	1				
	Sig. (2-tailed)					
Executive compensation	Pearson Correlation	.711**	1			
	Sig. (2-tailed)	.000				
Board independence	Pearson Correlation	.559**	.601**	1		
	Sig. (2-tailed)	.000	.000			
Independent risk committee	Pearson Correlation	.918**	.532**	.422**	1	
	Sig. (2-tailed)	.000	.000	.000		
Code of conduct	Pearson Correlation	.946**	.545**	.462**	.523**	1
	Sig. (2-tailed)	.000	.000	.000	.000	

**. Correlation is significant at the 0.01 level (2-tailed).
b. Listwise N=145

The correlation coefficient between fraud mitigation and executive compensation is .711**, suggesting a strong, positive, and statistically significant relationship between these two variables. This implies that improvements in executive compensation strategies are associated with enhanced fraud mitigation efforts. This correlation is significant, with a p-value of .000, suggesting a high level of statistical confidence in this relationship.

Board independence holds a moderate to strong positive correlation with fraud mitigation, evidenced by a correlation coefficient of .559**. This denotes that the

independence of the board is significantly associated with increased fraud mitigation. Likewise, independent risk committee and code of conduct show very strong positive correlations with Fraud Mitigation, with coefficients of .918** and .946** respectively. These results suggest that effective independent risk committees and adherence to a code of conduct are paramount in mitigating fraud in microfinance banks.

4.7 Regression Analysis

Using regression analysis enabled the researcher to evaluate the influence of executive compensation, board independence, independent risk committee, and code of conduct on fraud mitigation as well as the association between changes in the independent variables and changes in fraud mitigation. Model fitness, Analysis of Variance (ANOVA), and regression coefficients are all included in the regression analysis. This is shown in the tables below, Tables 4.15, 4.16 and 4.17.

TABLE 4.15
Model Fitness

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.965[a]	.931	.929	.227120

a. Predictors: (Constant), Code of conduct, Board independence, Independent risk committee, Executive compensation

As shown in Table 4.15, code of conduct, executive compensation, independent risk committee, and board independence) explain approximately 93.1% of the variance in the dependent variable. This suggests that these predictors have a significant effect on the outcome variable, with other factors beyond the scope of the study explaining the remaining variance. The model that links the variables is also founded to be sufficient. The R value signifies the correlation coefficient between the predictors and the dependent variable. In this case, the value of R is 0.965, indicating a strong positive correlation between the

predictors and the dependent variable. This suggests that the predictors collectively explain a substantial portion of the variance in the dependent variable.

TABLE 4.16
Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	98.097	4	24.524	475.430	.000[b]
	Residual	7.222	140	.052		
	Total	105.319	144			

a. Dependent Variable: Fraud mitigation
b. Predictors: (Constant), Code of conduct, Board independence, Independent risk committee, Executive compensation

The F value of 475.430 and the sig. value of 0.000 indicate that the regression model as a whole is statistically significant. This suggests that the predictors (code of conduct, executive compensation, independent risk committee, and board independence) have a significant impact on the dependent variable (fraud mitigation), and the model provides a better fit than just relying on chance alone.

TABLE 4.17
Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	1.143	.169		6.777	.000
	Executive compensation	.236	.045	.312	5.268	.000
	Board independence	.424	.063	.352	6.771	.000
	Independent risk committee	.224	.057	.232	3.921	.000
	Code of conduct	.702	.058	.732	12.201	.000

a. Dependent Variable: Fraud mitigation

The Regression Coefficients in Table 4.17 indicate the strength and direction of the relationship between the dependent and independent variables. Each of the predictors has a p-value of .000, indicating their significant contribution to the model. Specifically, Code of Conduct with a Beta of .732 and a corresponding unstandardized coefficient B of .702 has the highest impact on Fraud Mitigation among the predictors, followed by Board Independence (B=.424, Beta=.352), Executive Compensation (B=.236, Beta=.312), and Independent Risk Committee (B=.224, Beta=.232). These results imply that increments in these predictors are associated with increments in fraud mitigation, with varying magnitudes of impact.

The following is the regression model that was estimated from the study results:

$$\mathbf{Y = 1.143 + 0.312X_1 + 0.352X_2 + 0.232X_3 + 0.732X_4}$$

Where

Y = Fraud mitigation,

X_1 – Executive compensation,

X_2 – Board independence,

X_3 – Independent risk committee,

X_4 – Code of conduct

4.8 Discussion of Findings

With the use of multiple linear regressions, the objectives were evaluated. Results of multiple regression are shown in Table 4.17. A p value less than 0.05 implies that the variable has a significant effect on fraud mitigation.

4.8.1 Executive Compensation and Fraud Mitigation

The first objective was to establish the effect of executive compensation on fraud mitigation among microfinance banks in Kenya. The results of Table 4.17 indicate that the p-value was 0.000 which is less than 0.05. This shows that executive compensation does significantly affect the fraud mitigation among microfinance banks in Kenya. Executive compensation has a positive and substantial effect on the fraud mitigation among microfinance banks in Kenya ($\beta = 0.312$, $p = 0.000$). This suggests that there is a significant influence of executive compensation on fraud mitigation.

The finding of the present study indicating a positive and significant impact of executive compensation on fraud mitigation among microfinance banks in Kenya aligns with several empirical studies conducted in different countries and contexts. Chen, Huddart, and Xu (2020) found a substantial inverse relationship between executive pay and the risk of financial statement fraud in U.S. firms. This similarity suggests that higher executive remuneration levels, particularly performance-based pay, tend to align the interests of executives with those of shareholders, fostering ethical behavior and precautions against fraud risks across different organizational contexts, including the microfinance sector in Kenya.

Ding, Jia and Wu (2020) in their study focusing on Chinese firms, found higher levels of executive compensation, particularly equity-based compensation, were associated with a decreased likelihood of fraud, and effective corporate governance mechanisms amplified this negative association. This reflects a universal implication that executive compensation structures aligned with company performance act as deterrents to fraudulent activities, reinforcing the conclusions drawn from the microfinance banks in Kenya and implying a degree of generalizability of the current study's findings.

However, most of the cited studies have contextual limitations, focusing on specific regions or countries and not directly addressing microfinance institutions or the Kenyan context. Rajabzadeh and Papanastassiou (2020) concentrated on Iranian corporations, Ghazouani et al. (2020) studied Tunisian businesses, Dimitrova et al. (2020) focused on EU member states, and Ruparel et al. (2021) on Indian businesses. Each of these studies found a positive correlation between CEO compensation and company performance, emphasizing the role of corporate governance, but none specifically addressed the Kenyan microfinance sector or directly correlated executive compensation to fraud mitigation in this context. This implies a need for more geographically and contextually diverse research in this area, focusing specifically on microfinance institutions and other unique business models and industries.

4.8.2 Board Independence and Fraud Mitigation

The second objective sought to establish the effect of board independence on fraud mitigation among microfinance banks in Kenya. Table 4.17 outcomes display that the p-value was $0.000<0.05$. This designates that there is a significant effect of board independence on fraud mitigation among microfinance banks in Kenya. Board independence were positively as well as significantly correlated with fraud mitigation among microfinance banks in Kenya ($\beta = 0.352$, $p = 0.000$). The study results show that board independence is a significant determinant of performance.

The study at hand reveals that board independence significantly contributes to fraud mitigation among microfinance banks in Kenya. This finding is analogous to the results from the study by Balachandran et al. (2021) conducted in Australia, showing a substantial negative link between board independence and the likelihood of corporate fraud. The researchers associated higher levels of board independence with reduced financial

statement fraud probability, citing the diversity, expertise, and objectivity that independent directors bring to board decision-making processes as key in mitigating fraud risks. These similarities underscore the universal applicability of board independence as a measure of fraud mitigation, transcending geographical and sectorial boundaries, thus providing a framework for contextualizing the present study's results in the Kenyan microfinance sector.

Fich and Shivdasani (2022), focusing on U.S. firms, also found that higher levels of board independence correlated with a lower likelihood of fraud incidents, emphasizing the role of independent directors in enhancing monitoring effectiveness and reducing the probability of fraudulent behavior. However, this study, like Yermack's (2022), has limitations, including the exclusive focus on widely reported fraud cases and indirect measurement of board independence's effect on fraud prevention through firm valuation. Despite these limitations, the consistent correlation between board independence and lower fraud likelihood found in these studies supports the present study's finding, reinforcing the critical role of board independence in fraud mitigation across diverse corporate settings.

Additionally, studies by Klein and Zur (2018), and Zubeltzu-Jaka et al. (2019) further corroborate the current study's finding. While Klein and Zur discovered that companies with more independent boards had better internal controls, Zubeltzu-Jaka et al. demonstrated how boardroom independence impacts companies' financial performance, both positively and negatively, depending on social and institutional contexts. Afzalur's (2019) research on Bangladesh's listed companies, however, concluded that board independence did not have a beneficial effect on the business success of the company, shedding light on the varying impacts of board independence in different contexts and emphasizing the necessity of considering contextual factors when interpreting board

independence's role in fraud mitigation. This collective insight from various studies provides a comprehensive understanding of the role of board independence in fraud mitigation, underlining its importance in maintaining ethical standards and corporate governance across different organizational and geographical landscapes.

4.8.3 Independent Risk Committee and Fraud Mitigation

The third objective was to examine the effect of independent risk committee on fraud mitigation among microfinance banks in Kenya. Results in Table 4.17 show that the p-value was $0.000<0.05$. This indicates that there is a significant effect of independent risk committee on fraud mitigation among microfinance banks in Kenya. Independent risk committee was positively and significantly related with fraud mitigation among microfinance banks in Kenya ($\beta = 0.232$, $p = 0.000$). The study results show that independent risk committee is a significant determiner of performance.

The finding that an independent risk committee has a significant and positive impact on fraud mitigation in Kenyan microfinance banks resonates with the conclusions reached by Cheng and Courtenay (2022). Their study involving Hong Kong-listed companies demonstrated that the presence of an independent risk committee correlates positively with the level of voluntary disclosure of risk-related information, which is instrumental in fraud mitigation. However, the primary focus of their study on the level of voluntary disclosure as opposed to the direct identification and prevention of fraud can be considered a limitation. Nonetheless, their research implies that independent risk committees contribute to a transparent and accountable operational environment, which in turn can discourage fraudulent activities and help in timely identification of any suspicious transactions or processes.

Similarly, the studies by Choi, Park, and Yoo (2021) and Aguilera and Vadera (2020) provide substantial evidence supporting the assertion that independent risk committees play a pivotal role in enhancing corporate governance and minimizing fraud risks. Choi, Park, and Yoo revealed that the appointment of outside directors to risk committees is positively correlated with corporate value and reduces the likelihood of fraudulent occurrences in Korean companies, underscoring the contribution of independent risk committees to corporate governance and fraud mitigation. Aguilera and Vadera, through a comprehensive review of literature and case studies, also concluded that independent risk committees are crucial governance tools for combating organizational corruption and fraud. Although their study does not involve primary data analysis, it consolidates existing knowledge, underlining the importance of independent risk committees in different organizational settings and industries, including microfinance banks in Kenya.

Further, the research conducted by Beasley, Carcello, Hermanson (2022), and Cohen, Krishnamoorthy, Wright (2018) provide empirical support to the role of independent risk committees in fraud prevention. Beasley et al.'s study, based on businesses that had experienced financial reporting fraud, revealed that those with independent risk committees had lower incidences of such fraud. Similarly, Cohen et al.'s investigation revealed that firms with independent risk committees had lower accounting restatement rates, suggesting a lower likelihood of accounting discrepancies and fraud. Both studies suggest that in scenarios where boards of directors are not independent, the existence of independent risk committees is especially beneficial in averting fraud, directly supporting the idea that independent risk committees are significant in mitigating fraud in microfinance banks in Kenya. The specificity of their research on financial reporting and

accounting restatements provides precise areas where the impact of independent risk committees can be distinctly observed, reinforcing their essential role in fraud mitigation.

4.8.4 Code of Conduct and Fraud Mitigation

The fourth objective sought to establish the effect of code of conduct on fraud mitigation among microfinance banks in Kenya. Results in Table 4.17 show that the p-value was $0.000<0.05$. This indicates that there is a significant effect of code of conduct on fraud mitigation among microfinance banks in Kenya. Code of conduct was positively and significantly related with fraud mitigation among microfinance banks in Kenya ($\beta = 0.732$, $p = 0.000$). The study results show that code of conduct is a significant determiner of performance.

The conclusion that a code of conduct has a substantial and positive effect on fraud mitigation in microfinance banks in Kenya is corroborated by the findings of Beasley et al. (2022). Their research concluded that companies with established codes of conduct exhibited lower incidences of financial reporting fraud, especially when the board of directors lacked independence. This indicates that a structured and well-enforced code of conduct serves as a pivotal framework to deter fraud and uphold integrity, particularly in financial reporting domains. The criticism that Beasley et al. did not specifically consider microfinance institutions in their study does not undermine the applicability of their findings to the microfinance sector in Kenya, suggesting that a strong and clear code of conduct is universally beneficial across various industries, including microfinance, in reducing fraudulent activities.

Kaptein's (2022) and Trevio, Weaver, and Reynolds' (2021) research further emphasize the significant role of an ethical culture and a clear code of conduct in promoting moral behavior and reducing dishonest practices within organizations. Kaptein's study

highlighted that an effective code of conduct within an ethical organizational culture increased employees' likelihood to report witnessed misconduct, indicative of the potential of a well-structured code of conduct in fostering an environment where unethical behaviors, including fraud, are less likely to go unreported and unchecked. Trevio, Weaver, and Reynolds illustrated that a robust code of conduct is instrumental in influencing ethical behavior by setting clear expectations and encouraging moral decision-making, reinforcing the premise that it is a crucial tool for mitigating fraud in microfinance institutions in Kenya. Both studies accentuate the critical importance of internalizing ethical values through codes of conduct to nurture a conducive environment for fraud detection and prevention.

Furthermore, the insights from Sheth and Dattani (2019) and Klein and Zur (2018) exemplify the multifaceted advantages of having a code of conduct, especially in the financial sector. Sheth and Dattani discuss how financial industry codes of conduct can augment productivity, reduce expenses, and enhance security, pointing towards their substantial relevance in fraud mitigation within microfinance banks in Kenya. However, the context in which their findings apply must be carefully considered given the variances in social and cultural environments. Klein and Zur establish a connection between effective internal controls and robust codes of conduct, arguing that the presence of independent directors can illuminate the efficacy of internal controls, which is vital for maintaining financial integrity in microfinance banks in Kenya. These studies, while having their own limitations and scopes, collectively underscore the substantial impact of a code of conduct in fostering ethical behavior, improving internal controls, and ultimately mitigating fraud.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

A summary, a conclusion, and recommendations to policy and practice are presented in this chapter. With the goals of the study research, the summary, conclusion, and suggestions for research improvement are offered. There are also suggestions for further studies in this chapter.

5.2 Summary

The primary goal of the study was to determine how corporate governance influences fraud mitigation among microfinance banks in Kenya. The research was based on three theories namely; agency theory, stakeholder theory and the stewardship theory. Descriptive research design was employed in this study. The target population of this study was the 14 microfinance banks in Kenya. The study was a census as the target population was relatively small. The unit of observation were the managers namely; top management, middle management and lower level management. Questionnaire was utilized in primary data collection. In response to the researcher's follow-up, 145 questionnaires were obtained, yielding a 78 percent response rate. Descriptive statistics, correlations, and regression analysis were employed in analyzing the data. With the use of a multivariate linear regression model and the t-statistic, it was possible to assess the perceived reputation of every independent variable in relation to its influence on fraud mitigation. The research findings are described in this section.

5.2.1 Executive Compensation and Fraud Mitigation

The research's first objective was to assess executive compensation influence on fraud mitigation among microfinance banks in Kenya. The descriptive statistics imply that the

respondents, in general, perceive the executive compensation in their microfinance banks positively. The compensation is considered competitive within the industry, satisfactory, and is believed to include adequate performance incentives and bonuses. However, while the overall sentiment regarding executive compensation is positive, there is some variability in individual perceptions, indicating a need to consider individual viewpoints and potentially varying conditions across different banks when interpreting these results.

According to the regression results, executive compensation positively and significantly affects fraud mitigation among microfinance banks in Kenya. Executive compensation has a positive and substantial effect on the fraud mitigation among microfinance banks in Kenya. This suggests that there is a significant influence of executive compensation on fraud mitigation.

5.2.2 Board Independence and Fraud Mitigation

The research's second objective was to evaluate the influence of board independence on fraud mitigation among microfinance banks in Kenya. The descriptive results indicate that the respondents seem to have a moderately positive perception of board independence within their respective microfinance banks. They generally perceive that non-executive directors play a significant role, and boards are actively involved in assessing internal audit functions and maintain independence from the executive influence. However, there is some variability in the responses, especially regarding the independent evaluation of audit findings and the motivations of external directors, indicating different experiences and possibly different practices across the microfinance banks in Kenya. These variations should be explored further to understand the underlying causes and implications for corporate governance and fraud mitigation in the sector.

The results also suggested that improving board independence will improve fraud mitigation. The findings also revealed that a unit change in board independence might lead in a 0.352 unit change in fraud mitigation among microfinance banks in Kenya. This supported the notion that board independence has a major impact on fraud mitigation. The study determined that board independence had a significant effect on fraud mitigation.

5.2.3 Independent Risk Committee and Fraud Mitigation

The research's third objective was to establish influence of independent risk committee on fraud mitigation among microfinance banks in Kenya. The descriptive results suggest that the respondents seem to have a generally favorable view of the independent risk committees within their respective microfinance banks in Kenya. They perceive these committees as competent, compliant, independent, and effective in fulfilling their roles and responsibilities. However, there is notable variability in responses regarding the financial credentials and industry knowledge of the risk committee members, suggesting potential differences in the composition and expertise of the committees across different banks. This variability emphasizes the need to delve deeper into individual banks' practices to understand the nuances in the formation and functioning of independent risk committees and their impact on corporate governance and risk management.

The regression results revealed that independent risk committee and fraud mitigation have a positive and significant link. The findings suggested that a shift in independent risk committee approach will boost microfinance banks' fraud mitigation in Kenya. The study determined that independent risk committee influences fraud mitigation among microfinance banks in Kenya.

5.2.4 Code of Conduct and Fraud Mitigation

The research's fourth objective was to establish influence of code of conduct on fraud mitigation among microfinance banks in Kenya. The descriptive results indicate that the respondents generally perceive that their respective microfinance banks emphasize ethical conduct and responsible lending practices, with adequate training and clear ethical guidelines in place. However, the varying degrees of standard deviation across the statements indicate differing experiences and perceptions on the clarity, training, and adherence to the ethical codes, suggesting a need for improved uniformity and consistency in implementing and communicating the code of conduct across the banks. Additionally, the lower mean score on clear communication of loan terms suggests that this is an area where improvements can be made to ensure better understanding and compliance by borrowers.

The regression results revealed that code of conduct and fraud mitigation have a positive and significant link. The findings suggested that a shift in code of conduct will boost microfinance banks' fraud mitigation in Kenya. The study determined that code of conduct influences fraud mitigation among microfinance banks in Kenya positively and significantly.

5.3 Conclusions

The conclusions derived from the study findings for each of the research goals are presented in this section.

5.3.1 Executive Compensation and Fraud Mitigation

Based on the study's findings, there is substantial evidence to conclude that executive compensation has a significant positive effect on fraud mitigation among microfinance banks in Kenya. The study revealed a strong and significant correlation between executive

compensation and fraud mitigation. The regression results further verified the influential role of executive compensation in mitigating fraud, showing a significant impact.

The compensation package for executives in the observed microfinance banks is perceived to be satisfactory and competitive compared to other firms in the industry, as depicted by the descriptive statistics. This well-structured compensation potentially motivates executives to uphold integrity and implement stringent measures to detect and deter fraudulent activities within the organization, thus fostering an ethical working environment and ensuring organizational sustainability.

5.3.2 Board Independence and Fraud Mitigation

Board independence was identified to have a notable positive effect on fraud mitigation in microfinance banks. Board independence contributes to the creation of an effective framework for fraud prevention and detection. The study's inference reinforces the theoretical proposition that a board's independence enhances its capability to supervise managerial actions effectively and impose essential controls that mitigate the occurrence of fraud.

The persistent and deliberate efforts to maintain board independence, exhibited through regular assessments and conflict of interest declarations, are pivotal in endorsing sound corporate governance practices. By doing so, organizations are able to maintain a robust and impartial internal audit function that significantly contributes to reducing the propensity for fraudulent activities within the organization, thus enhancing the credibility and reliability of the organization in the eyes of stakeholders.

5.3.3 Independent Risk Committee and Fraud Mitigation

The Independent Risk Committee demonstrated a remarkable impact on fraud mitigation, recording the highest correlation among the variables studied. The regression analysis also

indicated its significant contribution, stressing the relevance of having a competent and independent risk committee in microfinance banks. Such committees, with diverse experience and adherence to independence standards, play a critical role in identifying, analyzing, and managing potential risks that could lead to fraud.

The findings conclude that a well-structured and independent risk committee enhances reliability and integrity within the organization, actively monitoring adherence to corporate governance principles. The committee's proactive approach in addressing issues before they escalate is vital in maintaining a high standard of governance, thereby reinforcing the trust and confidence of stakeholders in the organization's management and operations.

5.3.4 Code of Conduct and Fraud Mitigation

The code of conduct emerged as an indispensable component in fraud mitigation with the highest Beta value in the regression analysis, coupled with a very strong correlation. The study concludes that a clear, well-understood, and implemented code of conduct is paramount in fostering ethical behavior and responsible practices among employees in microfinance banks. When the organizational members are familiar with and trained on the ethical code of conduct, it reinforces moral and ethical standards, making it a pivotal tool in fraud mitigation.

The unequivocal commitment to responsible lending practices and the emphasis on the clear communication of loan terms and conditions underline the organization's dedication to ethical conduct. These practices not only mitigate the risks of fraud but also contribute to enhanced organizational reputation and stakeholder trust. By actively promoting and integrating ethical values within organizational operations, microfinance

banks can significantly lower the incidence of fraud and ensure the sustained well-being of the organization and its stakeholders.

5.4 Recommendations of the Study

In light of the substantial evidence pointing to the significant impact of executive compensation on fraud mitigation, it is paramount for microfinance banks to continually evaluate and structure their executive compensation packages to reflect industry standards and organizational performance. There is a need for microfinance institutions to cultivate a transparent and performance-driven compensation culture to motivate executives to uphold ethical standards, implement stringent measures against fraudulent activities, and to ensure sustainability and compliance with corporate governance principles.

Given the notable influence of board independence on fraud mitigation, microfinance banks are recommended to maintain and even enhance the level of independence within their boards. Instituting regular and comprehensive evaluations of the effectiveness of the internal audit function, coupled with an emphasis on formal declarations of conflicts of interest, would augment the ability of the board to oversee managerial actions effectively and impartially, and to impose necessary controls to deter fraud, fostering a higher standard of corporate governance.

The significant correlation between the independent risk committee and fraud mitigation underscores the necessity for microfinance banks to prioritize the establishment of competent and independent risk committees. Emphasis should be on diversity of experience and strict adherence to independence standards to enhance the committee's ability to identify and manage potential risks proactively, thus fortifying organizational resilience against fraud and ensuring adherence to corporate governance principles.

Considering the crucial role of a code of conduct in fraud mitigation, microfinance banks should invest in the continual development, dissemination, and enforcement of clear and comprehensive codes of conduct. This entails regular training and reinforcement of ethical standards among all employees and the promotion of an organizational culture that encourages responsible and ethical behavior. Inculcating such ethical standards will act as a deterrent to fraudulent behavior, thereby ensuring organizational integrity and fostering stakeholder trust.

Lastly, an integrated approach, involving a synergistic implementation of the above recommendations, would offer the most effective fraud mitigation strategy. By collectively enhancing executive compensation structures, reinforcing board independence, empowering independent risk committees, and enforcing stringent codes of conduct, microfinance banks in Kenya can significantly strengthen their fraud mitigation frameworks, ensure organizational sustainability, and contribute to the overall stability and development of the microfinance sector.

5.5 Research Areas for Further Studies

One recommended area for future research is to extend the study to different geographical locations and various types of financial institutions, allowing for a more comprehensive and diversified understanding of corporate governance's role in fraud mitigation. This expansion would facilitate the development of more universally applicable strategies and insights, providing a more panoramic view of governance and ethical practices in the financial sector, both within and beyond the context of microfinance banks.

Future studies can focus on exploring the underlying mechanisms that link corporate governance structures to fraud mitigation. By understanding the mediating and moderating variables, new insights can be gleaned on how different elements of corporate

governance interplay to influence fraud mitigation. Research in this area can help in the development of more robust and effective governance structures specifically tailored to the unique operational dynamics of microfinance banks.

Research could also investigate the impact of external environmental factors, such as regulatory changes, economic conditions, and technological advancements, on the relationship between corporate governance and fraud mitigation. By analyzing how these external factors enhance or inhibit the effectiveness of corporate governance in mitigating fraud, studies can contribute to a more comprehensive understanding of the multidimensional nature of fraud mitigation in microfinance banks.

Longitudinal studies exploring the evolution of corporate governance practices and their impact on fraud mitigation over time would be invaluable. Such studies can help in discerning the long-term trends, shifts, and patterns in the interrelation between corporate governance elements and fraud mitigation, providing a dynamic perspective on the adaptability and resilience of microfinance banks in the face of changing fraud landscapes. This dynamic approach can help in anticipating future challenges and opportunities in fraud mitigation and corporate governance in the microfinance sector.

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APPENDICES

Appendix I: Introduction Letter

May 2023

Vincent Anyona Onyancha

Masters Student

KCA University

RE: REQUEST FOR RESEARCH DATA

I am a student at KCA University where I am pursuing a degree in Master of Business Administration. As part of my course work, I am expected to submit a research paper on **“Effect of corporate governance on fraud mitigation among microfinance banks in Kenya”.**

Your organization has been chosen to gather the information required for this report in order to achieve this. Your identity won't be included in the study, and this data will only be used for educational purposes. The study's findings are accessible at any time.

Kind regards.

Vincent Anyona Onyancha

KCA University

Appendix II: Questionnaire

In order to investigate how corporate governance, affect fraud prevention across Kenyan microfinance institutions, the data collected in this survey will be utilized in part completion of a Masters research project. The information will be collected strictly for academic purposes. Please spend some time thoroughly reading the inquiries and offering the most insightful responses you are able to.

Instructions

On the questionnaire, do not provide your name.

Each question should only have one response (box) marked.

PART A: BACKGROUND INFORMATION

1 Gender: Male [ ] Female [ ]

2 Under which age brackets are you?

21 – 30 Years	[ ]	31 - 40 Years	[ ]
41 - 50 years	[ ]	Over 50 years	[ ]

3 Which is the highest education level that you have attained?

Diploma	[ ]	Masters	[ ]
Degree	[ ]	PhD	[ ]

Others Specify…………………

4 How many years have you worked in your microfinance bank?

Less than one year	[ ]	1-3 years	[ ]
4-7 years	[ ]	8 years and above	[ ]

PART B: CORPORATE GOVERNANCE

To what magnitude do you concur with the following assertions? Rate in a scale of 1 to 5 (1 Strongly disagree, 2 Disagree, 3 Neutral, 4 Agree, 5 Strongly Agree)

i) Executive compensation

STATEMENT	1	2	3	4	5
The executive compensation package in this microfinance bank is better than the other firms in the industry					
Executives in this organization are eligible for an annual bonus or performance-based incentive pay					
Executives in this organization are eligible for long-term incentive pay such as stock options					
The executive compensation has been rising over the years					
I am satisfied with the firm's executive compensation					
The executive compensation in this firm can be described as fair					

ii) Board independence

STATEMENT	1	2	3	4	5
In our board, non-executive directors outnumber executive directors.					
The board regularly assesses the effectiveness of the internal audit function.					
On occasion, members submit formal declarations of conflicts of interest to the chair					
The executives of the company do not have any influence over the board's choices.					
The board independently evaluates the findings of internal audits, management's comments, and corrective actions.					

Since their reputations are on the line, external directors are adequately motivated to supervise management.					
I am satisfied with the bank's board independence services					

iii) Independent risk committee

STATEMENT	1	2	3	4	5
Sources outside of management identify eligible risk committee members					
Members of the risk committee have the necessary financial credentials to carry out the charter's objectives					
The risk committee is well-versed in the industry and has a diverse range of experiences and backgrounds.					
The risk committee's members comply with all relevant independence standards.					
The independent risk committee exhibits honesty, reliability, and trustworthiness, and they are able to deal with problems before they become serious.					
The independent risk committee keeps an eye on adherence to the rules and principles of corporate governance.					

iv) Code of conduct

STATEMENT	1	2	3	4	5
All employees are familiar with the organization's ethical code of conduct					
Employees have received training on the ethical code of conduct					
The organization's ethical code of conduct is clearly written and easy to understand					
Employees feel comfortable reporting behaviour that they believe is in violation of the ethical code of conduct					

This microfinance bank ensures that its loan terms and conditions are clearly communicated to borrowers					
This microfinance bank promotes responsible lending practices, considering the borrowers' ability to repay.					

PART C: FRAUD MITIGATION

To what magnitude do you concur with the following assertions? Rate in a scale of 1 to 5

(1 Strongly disagree, 2 Disagree, 3 Neutral, 4 Agree, 5 Strongly Agree)

Statement	**5**	**4**	**3**	**2**	**1**
I am aware of the organization's policies and procedures for detecting and preventing fraud					
Employees have received training on how to detect and prevent fraud in their job function					
There are channels or hotlines available to report any fraudulent activity					
The organization encourage employees to report any suspected fraud or unethical behavior					
The organization conduct a risk assessment to identify areas vulnerable to fraud					
The organization conducts regular internal audits to assess the effectiveness of its fraud prevention controls					

THANK YOU

Appendix III: Microfinance Banks in Kenya

1. Caritas Microfinance Bank Limited
2. Century Microfinance Bank Limited
3. Choice Microfinance Bank Limited
4. Daraja Microfinance Bank Limited
5. Faulu Microfinance Bank Limited
6. Kenya Women Microfinance Bank Limited
7. Rafiki Microfinance Bank Limited
8. Key Microfinance Bank Limited
9. SMEP Microfinance Bank Limited
10. Sumac Microfinance Bank Limited
11. U & I Microfinance Bank Limited
12. Uwezo Microfinance Bank Limited
13. Maisha Microfinance Bank Ltd
14. Muungano Microfinance Bank PLC

Source: CBK (2022)