

Effect of Financial Reporting Practices on Budget Absorption in the County Government of Nakuru

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Abstract

Effective budgetary process in the county government is important because it helps the county treasury to estimate revenue and expenditure of the funds received from the national government and funds collected from the county government. However, the budgeting process in the county governments in Kenya has been faced with challenges therefore posing a difficulty in achieving the anticipated development. Therefore, this study sought to determine the effect of financial management practices on budget absorption in the County Government of Nakuru. Specifically, the study sought to determine the effect of financial reporting practices on budget absorption in the County Government of Nakuru. The study was anchored on agency theory. The study adopted descriptive research design with a target population of 80 participants involved in budgeting process. The study adopted census technique to incorporate all the 80 targeted respondents. The study relied on primary data collected through questionnaire. A pilot study was done in Kericho County Government where 8 questionnaires were distributed to officers in the county treasury. Both descriptive and inferential statistics were utilized. Descriptive statistics involved the use of percentages, frequencies, mean and standard deviation. Inferential statistic involved the use of regression analysis. After analysis data was presented in form of a table. The findings revealed a unit increase in financial reporting practices would lead to 0.093 units increase in budget absorption in the county government of Nakuru. The study concluded that there was a positive and statistically significant correlation between financial reporting practices on budget absorption in the county government of Nakuru. From the findings this study recommended that the County Government of Nakuru should strengthen its financial reporting practices by ensuring timely, transparent, and accurate reporting systems that enhance accountability and contribute to improved budget absorption.

Key Words: Financial Reporting Practices, Budget Absorption, County Government of Nakuru.

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I. Introduction

Budget absorption determines the extent to which allocated funds are utilized within a specified period. It is a pivotal aspect of fiscal management, especially within the context of county governments. Efficient budget absorption is essential for the successful execution of planned activities, the achievement of development goals, and the provision of services to citizens. However, the process is often fraught with challenges such as bureaucratic inefficiencies, delays in disbursements, capacity constraints, and political interference. The importance of budget absorption cannot be overstated (Nakitare, 2019). It is a measure of the financial health and administrative efficiency of county governments. High absorption rates indicate that funds are being used as planned, leading to the timely execution of projects and the delivery of services. Effective budget absorption is crucial for several reasons. First, it ensures the effective delivery of services. Numerous services, such as medical care, schooling, infrastructure, and social welfare, fall under the purview of county governments. Efficient use of allocated funds ensures these services are provided effectively to the population (Kipkirui, 2020).

Secondly, efficient budget absorption is essential for achieving development goals. Timely and full utilization of budgets is crucial for the successful implementation of development projects, whether it involves structure roads, enhancing water supply systems, or enhancing public health facilities (Chong & Johnson, 2019).

Proper budget absorption facilitates progress and development. Additionally, high budget absorption rates reflect a government's commitment to transparency and accountability. They establish that funds are being used for their intended purposes, fostering public trust and confidence. Moreover, effective budget absorption can stimulate local economies through job creation, infrastructure development, and improved public services, ensuring that government spending contributes positively to economic growth and stability (Kenis, 2021).

Globally budget absorption remains a key challenge at both the National and County Government. In Sweden, one of the major challenges facing budgetary absorption is the high level of Government debt. According to the Swedish National Debt Office, the central Government debt stood at SEK 1.2 trillion at the end of 2020 (Swedish National Debt Office, 2021). While Sweden has a strong economy, it also has a significant level of public debt, which can limit the funds available for investment and development. The need to service this debt also impact budgetary absorption rates, as it reduces the resources available for other spending priorities. Sweden has a highly decentralized system of Government, which make it difficult to coordinate spending priorities across different levels of Government. Additionally, the budgetary process is time-consuming and cumbersome, leading to delays and inefficiencies that can impact budgetary absorption rates (Fritzell *et al.*, 2020).

Despite these challenges, Sweden has implemented several strategies to improve budgetary absorption rates. One approach is to prioritize investments in key areas, such as infrastructure and innovation that have a high likelihood for economic growth and development. This helps ensure that resources are allocated to projects that have the greatest impact on the economy (Swedish Government, 2020). Sweden has also implemented policies that promote efficiency and reduce waste in Government spending through streamlining administrative processes, reducing bureaucratic red tape, and improving coordination among diverse levels of Government (Swedish Agency for Public Management, 2019). Finally, Sweden has also implemented measures to promote transparency and accountability in budgetary processes through public disclosure of budgetary information, regular audits, and the establishment of independent oversight bodies to monitor the use of funds (OECD, 2018).

Financial reporting practices involve the process of preparing and presenting financial statements that reflect an organization's financial performance and position. These practices are guided by accounting standards such as the International Financial Reporting Standards (IFRS) or Generally Accepted Accounting Principles (GAAP), ensuring transparency, comparability, and consistency (Bragg, 2021). Effective financial reporting enables stakeholders—such as investors, creditors, and regulators—to make informed decisions (Ross *et al.*, 2021). Timely and accurate financial reports enhance corporate accountability and reduce information asymmetry (Brealey *et al.*, 2020). Poor financial reporting can lead to mismanagement, reduced investor confidence, and legal penalties. Therefore, organizations must adopt robust reporting systems and uphold ethical standards to maintain financial integrity and compliance (Atrill & McLaney, 2019).

II. Theoretical Review

The study was anchored on Agency Theory which was developed by economists Michael Jensen and William Meckling (1983). Agency Theory is a framework that examines the relationship between principals (owners) and agents (managers) in organizations. It focuses on resolving conflicts that arise when agents are entrusted with making decisions on behalf of principals. The theory highlights issues of information asymmetry and misaligned incentives, where agents may act in their own interest rather than in the best interest of the principals. To mitigate these problems, Agency Theory suggests mechanisms such as performance-based incentives, monitoring, and aligning the interests of both parties through contracts (Panda & Leepsa, 2017).

Proponents of Agency Theory argue that it provides a critical understanding of organizational dynamics, particularly in addressing the principal-agent problem. They contend that by recognizing the potential for conflicts of interest, organizations can implement strategies to ensure better alignment between principals and agents (Shogren., Wehmeyer, & Palmer, 2017). These strategies include performance-based compensation, regular monitoring and reporting, and clear contractual agreements that specify the duties and expectations of agents. Proponents believe that these measures not only reduce agency costs (the costs associated with managing and mitigating conflicts) but also enhance organizational efficiency and performance by aligning the interests of managers with those of the owners (Mitnick, 2019).

Despite its widespread application, Agency Theory has faced several critiques. One major criticism is its assumption of opportunistic behavior by agents, which may not always hold true in practice (Vitolla., Raimo, & Rubino, 2020). Critics argue that this view can lead to excessive monitoring and control, which can stifle creativity and innovation. Additionally, the theory tends to focus narrowly on financial incentives and neglects other motivational factors such as job satisfaction, professional ethics, and organizational culture (Mitnick, 2019). Another critique is that Agency Theory often assumes a clear distinction between principals and agents, which can be blurred in many modern organizations where roles and responsibilities are more fluid. Finally, critics point out that the theory's emphasis on control mechanisms can lead to bureaucratic inefficiencies and increased costs.

The theory is relevant in explaining the effect of financial reporting practices on budget absorption in the County Government of Nakuru as it highlights the principal-agent relationship, where government officials (agents) manage public funds on behalf of citizens and oversight bodies (principals). Effective financial reporting practices enhance transparency and accountability, reducing information asymmetry and ensuring that allocated budgets are fully utilized as intended. Accurate and timely financial reports help track expenditures, prevent fund mismanagement, and support informed decision-making, ultimately improving budget absorption. Without proper reporting, inefficiencies, corruption, and poor resource allocation may occur, leading to underutilization of budgets and stalled projects. Thus, financial reporting acts as a mechanism to align agent actions with public interest, ensuring efficient and effective budget implementation.

III. Empirical Review

Santos and Da Silva (2019) conducted a study on the financial reporting practices and budget absorption in Brazil. Employing a qualitative research design, the study selected 200 municipalities in Brazil and conducted semi-structured interviews with finance officials and administrators. Thematic analysis was used to analyze the interview data. The study revealed that municipalities with transparent and timely financial reporting systems experienced higher levels of budget absorption. Effective financial reporting facilitated resource allocation decisions and enhanced accountability, resulting in improved service delivery and infrastructure development.

Ouedraogo and Nwosu (2020) study compared the impact of financial reporting practices on budget absorption between urban and rural states in Nigeria. The study used a mixed-methods approach. The researchers surveyed 150 counties in Nigeria and conducted focus group discussions with finance officials and administrators. Quantitative data were analyzed using descriptive statistics, while qualitative data were thematically analyzed. The study revealed that urban counties with more robust financial reporting systems tended to exhibit higher levels of budget absorption compared to rural counties. Transparent financial reporting enhanced accountability and resource allocation efficiency, resulting in improved service delivery outcomes in urban areas.

Khalid and Nyawira (2022) conducted a longitudinal study to examine the relationship between financial reporting practices and budget absorption in South African municipalities. Using a purposive sampling technique, the researchers selected 250 municipalities in South Africa and collected financial data over a five-year period. Statistical analysis techniques, including panel data regression, were employed to analyze the data. The study findings revealed a positive association between transparent financial reporting practices and budget absorption rates in South African municipalities. Municipalities with consistent and accurate financial reporting demonstrated higher levels of budget absorption, leading to improved service delivery outcomes.

Gonzalez and Amoah (2021) study investigated the impact of financial reporting practices on budget absorption in urban and rural districts in Ghana. Employing a mixed-methods approach, the researchers surveyed 200 districts in Ghana and conducted interviews with finance officials and administrators. Quantitative data were analyzed using regression analysis, while qualitative data were thematically analyzed. The study revealed that districts with transparent financial reporting systems experienced higher levels of budget absorption, leading to improved service delivery outcomes. However, disparities were observed between urban and rural districts, highlighting the need for targeted interventions to enhance financial reporting practices in rural areas.

Matiba and Valma (2022) examined the impact of financial reporting practices on performance of counties within the coastal region. Adopting a mixed-methods approach, the researchers surveyed three counties, across Kenya and conducted in-depth interviews with key stakeholders. The data were analyzed using both quantitative techniques and thematic analysis. The study findings indicated that counties with robust financial reporting practices exhibited higher levels of budget absorption. Transparent financial reporting promoted accountability and informed decision-making, leading to more efficient resource allocation and improved service delivery outcomes.

In Mandera County, Kenya, Hassan (2018) investigated the impact of financial reporting standards on the utilization of allocated funds. The ideas that were examined included the theory of financial control, new public management theory, peacock and Wiseman's theory of expenditure, and differential association theory. A descriptive research design was utilized in this study. One hundred and fifty-five people working in the finance department of Mandera County were the intended participants in this research. Questionnaires were used to collect primary data. The researcher utilized content analysis on the qualitative data that were gathered. To make sense of the numerical data, the researcher turned to inferential statistics, which comprised models for correlation and multiple linear regression. Results showed that the study's descriptive statistics—mean, median, and frequency distribution table—measured central tendency and spread, respectively, using standard deviation and t-tests. The results showed that budgetary absorption was significantly related to financial administration reports.

Odhiambo (2022) conducted a study on the relationship between financial reporting practices and budget absorption in Kenyan Corporations. The study adopted a cross-sectional research design involving 900 corporations and utilizing financial audits and interviews with financial officers, the findings suggested a positive correlation between enhanced financial reporting practices and improved budget absorption. The study concluded by advocating for African corporations to focus on strengthening financial reporting mechanisms to optimize budget absorption.

Diop (2021) conducted a study on the financial reporting and budget absorption in South Africa corporations. The study included 1,200 corporations with randomized cluster sampling, the research centered on financial transparency and its impact on budget absorption in Sub-Saharan corporations. The study revealed that South African corporations with transparent financial practices exhibit a substantial positive impact on budget absorption. Consequently, the study emphasized the crucial role of promoting financial transparency for enhancing budget absorption in South African corporations.

IV. Research Methodology

The study adopted descriptive research design. The total target population was 80 employees who comprised of 7 directors in County treasury, 20 County treasury staff, 14 accounting officers from County entities/department, 28 accountants from County entities /departments and 11 Sub-County administrators. The study adopted census technique to incorporate all the 80 targeted respondents. The study collected primary data using questionnaires. Data gathered in this study were quantitative in nature and was analyzed using SPSS. The researcher then utilized both descriptive and inferential statistics. Descriptive statistics involved the use of percentages, frequencies, mean and standard deviation. Inferential statistic involved the use of regression analysis. Multiple regressions were adopted in the study;

$$Y = \beta_0 + \beta_1 X_1 + \varepsilon$$

Where:

Y = Budget Absorption

β_0 = Constant Term

X_1 = Financial reporting Practices

ε = Error Term

β_1 represents Regression Coefficients for Financial reporting Practices

V. Results and Discussion

The researcher sought to establish the effect of financial reporting practices on budget absorption in the county government of Nakuru.

Descriptive statistics

The findings are as indicated in Table 1.

Table 1: Financial Reporting Practices on Budget Absorption

Statements	SA %	A %	U %	D %	SD %	Mean	Std
The county government has adopted transparency financial reporting practices to ensure that public funds are used efficiently.	15.7	65.2	6.7	12.4	0.0	3.8427	.83800
Transparency acts as a deterrent to corruption by making it more difficult for officials to conceal misuse of funds.	20.2	32.6	22.5	24.7	0.0	3.4831	1.07780
Through accurate financial reporting that County government ensures that funds are allocated to priority areas where they are most needed.	28.1	41.6	18.0	12.4	0.0	3.8539	.97177
Through accurate reporting the county government identify areas of inefficiency or overspending, allowing for timely adjustments to budgetary allocations.	22.5	33.7	27.0	15.7	1.1	3.6067	1.04030
Compliance with regulations ensures that the county government adheres to legal requirements and avoids penalties.	30.3	50.6	9.0	9.0	1.1	4.0000	.92932
Compliance with regulations enhances the credibility of financial reports, both internally and externally.	38.2	32.6	15.7	12.4	1.1	3.0112	1.04983

From the findings 15.7% of the respondents strongly agreed that the county government has adopted transparency financial reporting practices to ensure that public funds are used efficiently, 65.2% agreed, 6.7% were undecided, 12.4% disagreed while none of the respondents strongly disagreed with a mean of 3.8427 and a standard deviation of 0.83800. These findings align with those of Santos and Da Silva (2019) who found that transparency in financial reporting enhances the ability of county governments to allocate resources more

effectively and reduce wastage. Transparency ensures that financial records are accessible and verifiable, thereby promoting public trust and budget discipline.

In addition, 20.2% of the respondents strongly agreed, 32.6% agreed, 22.5% were undecided, and 24.7% disagreed that transparency acts as a deterrent to corruption by making it more difficult for officials to conceal misuse of funds resulting in a mean of 3.4831 and a standard deviation of 1.07780. These results are in line with the findings of Ouedraogo and Nwosu (2020) who emphasized that clear and publicly accessible financial reports reduce opportunities for corruption in devolved units. By limiting discretion and increasing oversight, transparency narrows the avenues through which public resources can be misappropriated.

From the findings, 28.1% strongly agreed that through accurate financial reporting that County government ensures that funds are allocated to priority areas where they are most needed, 41.6% agreed, 18.0% were undecided and 12.4% disagreed, with a mean of 3.8539 and a standard deviation of 0.97177. These results support the findings of Khalid and Nyawira (2022), who argued that the accuracy of financial reports guides strategic budgeting decisions and supports timely service delivery. When financial data is accurate, departments can allocate funds more efficiently, aligning budget execution with planning objectives.

Moreover, 22.5% of respondents strongly agreed that through accurate reporting the county government identify areas of inefficiency or overspending, allowing for timely adjustments to budgetary allocations 33.7% agreed, 27.0% were undecided, 15.7% disagreed, and 1.1% strongly disagreed, leading to a mean of 3.6067 and a standard deviation of 1.04030. These findings are consistent with a study by Gonzalez and Amoah (2021) who found that counties that invest in detailed and frequent financial reporting are better able to monitor financial performance and reallocate resources when necessary. Early identification of inefficiencies through reporting enhances the ability of financial managers to stay within budget and improve absorption rates.

From the analysis, 30.3% of respondents strongly agreed that compliance with regulations ensures that the county government adheres to legal requirements and avoids penalties, 50.6% agreed, 9.0% were undecided, and 9.0% disagreed, with a Cronbach mean of 4.0000 and a standard deviation of 0.92932. Lastly, on whether compliance with regulations enhances the credibility of financial reports, both internally and externally, 38.2% strongly agreed, 32.6% agreed, 15.7% were undecided, 12.4% disagreed while 1.1% strongly disagreed with a mean of 3.0112 and a standard deviation of 1.04983. the findings generally align with those of Matiba and Valma (2022) who argued that compliance with statutory guidelines builds trust in financial reports both within the organization and among external stakeholders. Overall, the results confirm that financial reporting practices play a critical role in enhancing budget absorption through transparency, accuracy and regulatory compliance.

Budget Absorption

The researcher sought to determine the budget absorption of county government of Nakuru, Kenya. The findings are as indicated in Table 2.

Table 2: Budget Absorption

Statements	SA	A	U	D	SD	Mean	Std
	%	%	%	%	%		
The county government attains its revenue targets in a financial year which has led to improved budget performance.	0	10.3	18.9	40.4	30.4	1.9551	1.11712
The county projects are implemented within the budgetary provisions.	12.4	12.4	16.9	22.5	36.0	2.4382	1.30519
The projects are delivered on timely basis.	0	16.9	18.0	14.6	50.6	1.9292	.93398
Majority of the programs in the budgets have been implemented in the last three years.	20.2	32.6	22.5	24.7	0.0	3.4831	1.07780
Development expenditure always has a high execution rate as opposed to recurrent expenditure hence contributing to higher budget absorption rate.	7.9	2.2	10.1	38.2	41.6	1.9562	1.00408

From the findings none of the respondents strongly agreed that county government of Nakuru attain its revenue targets in a financial year which has led to improved budget performance, 10.3% of respondents agreed, 18.9% were undecided, 40.4% disagreed and 30.4% strongly disagreed that county government attain its revenue targets in a financial year which has led to improved budget performance with a mean of 1.9551 and a standard deviation of 1.11712. In addition, 12.4% strongly agreed, 12.4% agreed, 16.9% were undecided, 22.5% disagreed, and 36.0% strongly disagreed that the county projects are implemented within the budgetary provision with a mean of 2.4382 with a high standard deviation of 1.30519, indicating poor budget adherence.

Regarding whether the projects are delivered on timely basis none strongly agreed, 16.9% agreed, 18.0% were undecided, 14.6% disagreed, and 50.6% strongly disagreed, with a mean of 1.9292 and a standard deviation of 0.93398. This finding is in line with Maina and Wambua (2022), who reported that procurement delays, political interference, and poor monitoring mechanisms often stall project timelines in counties. Delays

reduce the fiscal year's effective execution window, leading to underutilized budgets. When asked whether most programs in the budget have been implemented in the last three years, 20.2% strongly agreed, 32.6% agreed, 22.5% were undecided, and 24.7% disagreed with a mean of 3.4831 and a standard deviation of 1.07780. This supports Kilonzo and Atambo (2020), who found that implementation rates across counties are often skewed, with recurrent projects favored over capital ones. While some programs are completed, systemic inefficiencies still hinder full absorption.

On whether development expenditure always has a high execution rate as opposed to recurrent expenditure hence contributing to higher budget absorption rate 7.9% strongly agreed, 2.2% agreed, 10.1% were undecided, 38.2% disagreed, and 41.6% strongly disagreed with a mean of 1.9562 and a standard deviation of 1.00408. These results reflect the findings of Otieno and Koskei (2021), who emphasized that capital projects are often delayed due to complex procurement processes and limited contractor capacity. Overall, these findings portray a challenging budget absorption environment in Nakuru County, largely due to poor revenue realization, slow project implementation, and inefficiencies in executing development budgets.

Inferential statistics

Regression analysis was conducted to establish the relationship between financial reporting practices and budget absorption. The results are shown in Table 3.

Table 3: Regression coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.425	.341		1.246	.216
Financial reporting practices	.619	.146	.587	4.235	.000

The interpretations of the findings indicated follow the following regression model.

$$Y = 0.425 + 0.619X_1$$

According to the intercept (β_0), holding all the other independent variables constant, a unit increase in financial reporting practices would lead to 0.619 units increase in budget absorption in the county government of Nakuru. The p-value for financial reporting was $0.000 \leq 0.05$. Therefore, the study rejects the null hypothesis and concludes that financial reporting practices have a statistically significant effect on budget absorption in the county government of Nakuru. The study findings are in line with those of Khalid and Nyawira (2022) which revealed a positive association between transparent financial reporting practices and budget absorption rates in South African municipalities. Municipalities with consistent and accurate financial reporting demonstrated higher levels of budget absorption, leading to improved service delivery outcomes. The findings also concur with those of Odhiambo (2022) the findings suggested a positive correlation between enhanced financial reporting practices and improved budget absorption. The study concluded by advocating for African corporations to focus on strengthening financial reporting mechanisms to optimize budget absorption.

VI. Conclusion and Recommendations

The study concluded that there was a positive and statistically significant correlation between financial reporting practices and budget absorption in the county government of Nakuru, ($r=0.566$; $p<0.01$). The study findings are in line with those of Santos and Da Silva (2019) which revealed that municipalities with transparent and timely financial reporting systems experienced higher levels of budget absorption. Effective financial reporting facilitated resource allocation decisions and enhanced accountability, resulting in improved service delivery and infrastructure development. The study recommended that the Heads of departments consistently submit monthly budget utilization reports to promote transparency and inter-departmental accountability. Furthermore, the County assembly public accounts committee was recommended to enhance its oversight role by reviewing and publicizing financial performance audits to increase public trust and pressure for compliance.

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