



EFFECTS OF CORPORATE GOVERNANCE ON DIVIDEND PAYMENT AMONG SAVINGS AND CREDIT CO-OPERATIVE SOCIETIES IN KENYA

ROBERT ASUMANI SAMUEL, DR. FLORENCE MEMBA

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¹Robert Asumani Samuel, ²Dr. Florence Memba

¹Student, Jomo Kenyatta University of Agriculture & Technology (JKUAT), Kenya

²Lecturer, Jomo Kenyatta University of Agriculture & Technology (JKUAT), Kenya

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Abstract

The determinants of firms' dividend policies have long been a puzzle for Savings and Credit Co-operative Societies. The purpose of this study was to determine the effects of corporate governance on dividend payment among Savings and Credit Co-operative Societies in Kenya. The study was informed by signaling, Stakeholders', Agency and Resource dependency theories of dividends. This study employed explanatory research design. The study targeted two respondents in the form of board members and accountant or general manager from each of the 60 Deposit Taking Societies in Nairobi City County registered under SASRA. Since the target population was small in number 120, this study was a census of one board member and accountant or general manager from each of the 60 Deposit taking Societies operating in Nairobi. The study collected both primary and secondary data. Both descriptive and inferential statistics was used to analyze data. Inferential statistics included in the study was Pearson Correlation and multiple regression analysis. The study concludes that board tenure determines dividend pay-out ratios. Corporations with longer board tenures provide higher dividends but the firms with shorter board tenures provide significantly lower dividends. Board independence and independence of sub-committees has a positive influence on dividend payout with a view to reducing free cash flow. Age heterogeneity improves the ability of directors to solve tasks with high complexity such as issues of debt and equity financing. The study recommends that organization and especially SACCOs need to take the issue of board tenure seriously because it affects dividend payment. They need to put in place members on longer board tenures. It is recommended that companies and specifically SACCOs need to consider board diversity issues since companies with the best diversity score high against their dividend payment. It is recommended that SACCOs should ensure that there are independent directors who facilitate continual monitoring of the firm by the market participants.

Keywords: Corporate governance, Dividend payment, Board tenure, Board gender Diversity, Board independence and Board age diversity

INTRODUCTION

Dividend policy has an effect on the performance of the firms (Mitton, 2004). Thus, the SACCOs should pay dividends to ensure that they have a positive outlook in the future. Since the share market is positively responsive to the dividend announcement, companies should always strive to pay dividend consistently for their shares to perform well. SACCO Societies contend that there are a number of challenges ranging from poor governance and poor investment decisions. That dividend payment is hampered by poor financial stewardship, under-capitalization of co-operative enterprises, high cost of funds, and delayed member payments.

Governance in Kenyan SACCOs is typically weak because of their 'Management Board' system which results in the absence of clear division between roles of the board and management. The boards and management capacity of most SACCOs is weak with board membership largely seen as a stepping-stone into politics. This causes board membership to be occupied by individuals not necessarily interested in enhancing member interests in Kenya (Owen, 2007). Okwee (2011) found that a significant number of SACCOs comply less with corporate governance guidelines which may explain the relatively poor financial performance of these SACCOs in Uganda.

Among SACCOs in Kenya the issue of dividend payment is a concern to the members. Various studies have been carried on this area for example a study by Lari (2009) argued that mismanagement and corruption were two significant challenges facing SACCOs in Kenya today and has an effect on the dividend payment to be made to members. Bwana and Mwakujonga (2013) did a study on the effect of SACCOs' Board of Directors (BOD) and

employees on dividend payment. They argued that SACCOs' Board of Directors (BOD) and employees have an effect on dividend payment.

Mitton (2004) in his study shows that firms with higher corporate governance ratings have higher dividend payout. While these studies have covered on dividend payment they did not specifically look at variables such as board tenure, board gender diversity, board independence and board age diversity and how they affect dividend payment. There was need for further research on dividend payment among SACCOs. Thus this was the knowledge gap that the current study sought to fill. Therefore the current study assessed the effect of corporate governance on dividend payments among SACCOs in Kenya.

Objective of the study

The main aim of the study was to determine the effect of corporate governance on dividend payment among SACCOs in Kenya. The specific Objectives of the study were:

- To determine the effect of board tenure on dividend payment in SACCOS in Kenya.
- To establish the effect of board gender diversity on dividend payment in SACCOS in Kenya.
- To find out the effect of board independence on dividend payment in SACCOS in Kenya.
- To determine the effect of board age diversity on dividend payment in SACCOS in Kenya.

Hypothesis of the Study

- H₀₁: Board tenure has no significant effect on dividend payment in SACCOS in Kenya
- H₀₂: Board gender diversity has no significant effect on dividend payment in SACCOS in Kenya
- H₀₃: Board independence has no significant effect on dividend payment in SACCOS in Kenya

H₀₄: Board age diversity has no significant effect on dividend payment in SACCOS in Kenya

Empirical literature

Board Tenure

Gugler, (2001) examines the interrelation between internal governance mechanisms of corporate governance and dividend payments in Austrian firms through a panel data set and conjecture that corporate governance mechanism in particular, board tenure determines dividend pay-out ratios. Corporations with longer board tenures provide smooth dividends but the firm's with shorter board tenures provide significantly lower dividends.

Hwang *et al.*, (2004) documented a study on the Korean business group and examine whether companies with longer board tenures pay higher dividends. Their research results were in line with the outcome model of corporate governance and dividend payments. Kim and Lee (2008) also explore the association of dividend payment to board tenure holding external financing opportunity as an impacting variable of selected Korean firms. They conclude that when firms face constraints in external financing they tend to pay lower dividends and again firms are likely to increase their pay-out ratio with an improvement in their corporate governance.

Adjaoud and Amar, (2010) look into the effects of board tenure on dividend policy in Canada taking the sample from Toronto Stock Exchange's listed firms over four years' time period. The firm level governance index incorporates different provisions of governance, including shareholder rights issues. They draw an interesting outcome which supports the outcome model of dividend that means longer board tenure of firm lead to more dividend income for the shareholder. Their study result is also related to the research of La Porta *et al.*, (2000).

Yordying (2013) conducted a study on dividend policy and board tenure with a sample of 1927 observations for a time period of eight years long in Thailand and infer that dividend policy is heavily influenced by board tenure, particularly organizations with the higher percentage of institutional shareholding likely to pay the higher dividend.

Board Gender Diversity

Short *et al.*, (2002) examined the relationship between board diversity and dividend policy for the UK companies. Findings from their study consistently produced a strong support that a positive association exists between dividend payout policy and board diversity. Similarly, Kumar (2003) examined the relationship between board diversity and firm's dividend payout policy for the period 1994-2000. Findings from the study suggested the fact that an association between board diversity and dividend payout policy existed.

The McKinsey report (2007) compared the 89 European listed companies with the best diversity score against their dividend payment. The dividend payment of these companies was found to be greater in cases where there was a diverse board membership.

Lückerath-Rovers (2011) confirmed the positive relationship between women's presence on boards and dividend payment by applying an enhanced methodology of the popular Catalyst (2007) and McKinsey (2007) research on listed firms in the Netherlands. It has sometimes been said that one woman on the board is a token, two is a presence, and three is a voice. In fact, research has showed that having three or more women on a board makes it more effective hence high dividend payment.

Board Independence

Board independence and independence of sub-committees may have positive influence on dividend payout with a view to reducing free cash flow. Similarly they may view that it is in the best interest of firms to pay dividends and thereby signaling the good prospects when firms have good projects available. Independent directors thus facilitate continual monitoring of the firm by the market participants (Kiel, 2003).

In the Australian context, Kiel and Nicholson (2003) survey a sample of 348 large Australian non-financial firms and estimate the average board independence effect on dividend payment. They find a positive relationship between board independence and dividend payment. Henry (2003) analyses the corporate governance practices of a sample of Australian firms for the period 1992 to 2002 and finds that the corporate governance structure is important. According to this study, the impact of corporate governance disclosures on valuation is not evident.

Cortese (2009) traces the characteristics of non-executive directors of 50 large Australian firms and finds that 80 per cent of the board members are independent for the year 2006. Henry (2010) finds board independence reduces the agency costs of individual firms and that this reduction in agency costs leads to higher levels of dividend payments. Brown *et al.*, (2011) reviews the existing literature on corporate governance and highlight the stickiness of governance data and potential endogeneity problems.

Board Age Diversity

A field study was conducted by Wegge *et al.*, (2008) and found out that age heterogeneity improved the ability of directors to solve tasks with high complexity such as issues of debt and equity financing. For groups working on simple tasks,

however, age heterogeneity increased the number of self-reported health problems which in turn indicates that board of diverse ages should be utilized particularly for innovation or solving complex problems.

Vafeas (2003) found research suggesting that long-term director engagement was associated with greater competence, experience and commitment, because long-term directors have more knowledge of the firm and its business environment and that helped a firm to adopt the best governance structures in their transactions with potential suppliers of funds. By expanding the age diversity on the board of directors, Debt policy and equity ownership ideas are maximized.

Age diversity has the potential to enhance board performance, because directors of different ages will, to some extent, have different backgrounds, skills, experiences and social networks. Several examples of the benefits of a more age diverse board of directors come to the authors' minds. For example, different age groups have varied access to information and expertise about capital structure of a firm (Dagsson *et al.*, 2010).

Today's younger generations have grown up with computers and Internet at home, and may be better informed and more experienced on the subject of online business and better ideas on debt and equity financing. The older generation may, however, be more experienced dealing with the business offline, as they have greater experience in this field through their career. Today more and more businesses have both online and offline services, so experience of both types of business is of importance to many firms. Carter *et al.*, (2010) stated clearly when they argued that "diversity holds the potential to improve the information provided by the board to managers due to the unique information held by diverse directors."

RESEARCH METHODOLOGY

This study employed explanatory research design. According to Cooper and Schindler, (2000) explanatory research focuses on why questions. In answering the 'why' questions, the study was involved in developing explanations. The explanations argue that phenomenon Y (dividend payment) is affected by variable X (corporate governance). According to Ngechu (2004), a population is a well-defined set of people, services, elements, events, group of things or households that are being investigated. The study targeted two respondents in the form of board members, accountant or general manager from each of the 60 DTS registered under SASRA operating in Nairobi City County. Upagade and Shende (2012) refer to a sampling frame as a source list containing all names of the universe. The sampling frame of this study was derived from the database of SASRA which regulates and licenses deposit taking SACCOs in Kenya. Since the target population was small in number 120, this study was a census of one board member, accountant or the general manager from each of the 60 SACCOs operating in Nairobi as recommended by Cooper and Schindler (2000). The study used both the questionnaire and the secondary data collection sheet to collect data. The questions in the questionnaire were formulated according to the study objectives with similar order and content for all the questions. The researcher used both closed and open ended questions. This helped elicit rich information that was not captured when only one of the instruments was used. Data collected was edited first to identify the items that were wrongly responded to and any blank spaces left unfilled, the information was categorized into topics. Responses received were thereafter coded and processed by computer through the Statistical Package for Social Science (SPSS) software version 22.0. Descriptive statistics such as frequency, mean standard deviation and percentage were largely

applied for all the research objectives. The data was presented in a tabular form, bar graphs and pie charts. Both descriptive and inferential statistics were used to analyze data. Inferential statistics included in the study was Pearson Correlation and multiple regression analysis. Pearson correlation assumed the data is linear, and shows the relationship or association between the dependent variable and independent variable. This data was first analyzed for correlation using coefficient of correlation r for association and coefficient of determination R^2 to establish the extent to which corporate governance account for changes.

RESEARCH FINDINGS AND DISCUSSION

Board Age Diversity

The study was interested in finding out from the respondents their age bracket. From the study findings, majority of the respondents were in the age category of between 41-50 years representing 62% followed by those in the age category of over 50 years at 21%. The study findings indicated that those in the age category of between 31-40 years were represented by 16% and those below 30 years were represented by 1%.

Board Tenure

The study sought to find out from the respondents the number of years that the respondents had served in the organization. The study findings indicate that most of those who responded stated that they had been with the organization for a period of 1-3 years representing 38% while those who had been with the organization for a period of 4-6 years were represented by 30%. The study findings show that 20% of the respondents had been with the organization for between 6-9 years. In addition the study findings indicate that 12% of

the respondents had worked for a period exceeding 9 years.

The study sought to establish from the respondents how often they held elections for board members. The respondents indicated that they are expected by regulations to hold annual general meeting to elect a third of the board members who retire annually but can be reelected.

In relation to how elections of board members were conducted. The study findings showed that most of the respondents representing 86% indicated that elections of board members were conducted in the organization democratically whereas 14% of those who responded stated that elections of board members in their organization was controlled by regulatory authorities but were supported by members.

The study was interested in establishing from the study findings whether the SACCOs under review had electoral zones. The study findings indicated that most of the respondents representing 68% indicated that they had electoral zones that made it easy for the organization to ensure efficiency. On the other hand the findings indicated that 32% of the respondents stated that they did not have any form of electoral zones but all issues relating to the organization were carried out centrally at a location selected by the members.

The reasons provided by for having electoral zones include consideration for issues such as the size and permanency of membership in an area whose number should not be less than 30, distance between an existing branch and the new branch, availability of banking facility/services and the operational costs effectiveness.

Board Independence

In relation to board independence the study sought to find out how frequent authorities inspect the

organizations. From the study findings it was clear that most respondents indicated that authorities had the power to inspect their organization quarterly being represented by 88% of the respondents whereas 10% felt it was annually whereas 2% indicated that it was monthly.

The study sought to find out how frequent the organizations hold board meetings. The study findings indicated that most of the respondents stated that they hold board meetings monthly at 75% followed by those who stated that they held their board meetings quarterly at 12%. On the other hand another 2% indicated that they held their board meetings annually whereas 10% indicated that they held board meeting whenever there was a good reason to do it and did not have a time frame to do it but at least they did it once every year.

The study was interested in finding out from the respondents whether regulatory authorities influence decision making process in the organization. The study findings showed that majority of the respondents 92% were of the opinion that regulatory authorities influence decision making process whereas 8% did not think regulatory authorities influence decision making process in their organizations.

Those who stated that this was the case argued that authorities and in particular SARSA has the power to inspect the premises and the records of a SACCO and to prescribe enforcement actions in case of deficiencies including the appointment of a statutory manager, non-compliance with legal requirements carries clearly specified penalties and includes removal from office of directors and other responsible officers.

The study wanted to find out from the respondents their opinion on whether the society chairman was the overall decision maker. The study findings indicate that majority of the respondents were of

the opinion that this was not the case representing 73% while other 7% stated that to some extent the chairman was the overall decision maker. From the study findings 20% of those who responded argued that the chairman was part of the group that makes decision but was not the overall decision maker.

Board Gender Diversity

The study sought to find out from the respondents what the board gender diversity was. The study findings indicated that most of the respondents at 82% argued that their board members had majority of male members representing majority and in some instance the board comprised of only male members. This was as opposed to 18% of the respondents who argued that their board members comprised both male and female but indicated that majority were male members. From the study findings it is clear that more than three quarters of the board members were male members as opposed to a quarter and in some instances a lack of female board member.

Dividends Payment

The study findings sought to establish the percentage the organization paid in form of dividend to their members. As shown in the study findings 89% of the respondents indicated that they paid less than 10% in dividends to members. This was as opposed to 11% who stated that they paid more than 10% dividends to members.

In regards to the mode of dividend payment to members all the respondents stated that their mode of payment was cash payment. The study went further to inquire the sources of finances for dividend payment. All the respondents indicated that the only source of finances for dividend payment was accumulated cash reserves arising from profits made by the organizations.

Summary of Descriptive Statistics

On average dividend payment by SACCOS in Kenya was affected by board tenure by almost 22%, while the maximum effect on dividend payment was 207, minimum value was 43% while the standard deviation was 30.19. As for board gender diversity it showed a mean value of 0.22 and standard deviation of 36.7% in relation to how they affect dividend payment. On the other hand the findings shows that board age diversity affect dividend payment to a mean value of 0.595 and standard deviation of .3606.

Research Questions Test and Analysis

In relation to the objectives, the study adopted the following model:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \epsilon$$

The fitted multiple regression model of the variables was presented as follows:

$$Y = 8.357221_{(0.01581)} + 0.690401_{(0.01133)} X_1 + 0.600817_{(0.00210)} X_2 + 0.714664_{(0.0025)} X_3 + 0.641154_{(0.0135)} X_4$$

The fitted model was diagnosed and found that the regression was statistically significant at 5% significance level (regression *FP*-value= .05 > .024415). This shows that the combination of these factors (explanatory variables) significantly affect the response variable (dividend payment of SACCOS). Further, R-square = 75.434%, implying that the explanatory variables accounted for 75.434% of the response variable.

Where; Y is the dividend payment of SACCOS

X_1, X_2, X_3, X_4 : are the Independent Variables

β_0 was the intercept; and reflects the constant of the equation.

β_1 was the sensitive coefficient of each independent variable ($i=1,2,3,4$).

ϵ was the error term.

In regards to correlation, the study results indicate that the predicting variable generates a positive correlation. The normal probability plot of the correlation standardized residuals is presented in

the plot for analysis which suggests that no major deviation of the variables or the predictors from normality. This then implies a positive correlation for these predictors positively affect the dividend payment in SACCOS.

To assess the statistical significance of the result, it is necessary to look in the table below: ANOVA. This tests the null hypothesis that Regression (R) in the population equals 0. The model presented here reaches statistical significance of 0 i.e, [Sig = .000, this means $p < .0005$

ANOVA^a

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	44.867	31	5.607	32.723	.000 ^b
	Residual	4.122	62	.171		
	Total	48.980	93			

The multiple regression summary table is shown in table below:

Multiple Regression Summary Table

Variable	Coefficient	Std. Error	t-Statistic	Prob.
Constant	8.357221	0.01581	0.28666	0.774
X ₁	0.690401	0.01133	2.16424	0.031
X ₂	0.600817	0.00210	0.93993	0.347
X ₃	0.714664	0.0025	3.42736	0.007
X ₄	0.641154	0.0135	0.55235	0.260
R ²	0.75434			
Adjusted R ²	0.71327			
F-statistic	80.4977			

The T-test at 95% ($\alpha=0.05$) level was used to test the significance of the difference in pre and post dividend payment in relation to board tenure, board gender diversity, board independence and board age diversity. The standard errors (SE) of the coefficients of the explanatory variable of M are given in the parenthesis. In the estimated model coefficients, the SE values were less than .05 (i.e. $0.05 > SE$) implying that the board tenure factors` tested significantly affect dividend payment at 5% significance level. At the 95% confidence level an interval of any value less than 0.05 was acceptable in this study for purposes of interpretations.

In summary all together the effects of explanatory variables captured in the model are significant, and these findings are informative, as they intrigue significant questions regarding the effect of corporate governance on dividend payment among SACCOs.. The regression output showed R-square value of 75.434%. This implies that there could be other factors that contribute to the remaining 24.566% in explaining the variation in dividend payment among SACCOs in Kenya.

Conclusions

The study concluded that board tenure determines dividend pay-out ratios. SACCOs with longer board tenures provide higher dividends but those with shorter board tenures provide significantly lower dividends. SACCOs with the best diversity score against their dividend payment. The dividend payment of these SACCOs is found to be greater in cases where there was a diverse board membership. In summary SACCOs with the best diversity score high against their dividend payment.

Board independence and independence of sub-committees has a positive influence on dividend payout with a view to reducing free cash flow. Independent directors facilitate continual

monitoring of the firm by the market participants. Board independence reduces the agency costs of individual SACCOs and that this reduction in agency costs leads to higher levels of dividend payments.

Age diversity has the potential to enhance board performance, because directors of different ages will, to some extent, have different backgrounds, skills, experiences and social networks. Several examples of the benefits of a more age diverse board of directors come to the author's mind. For example, different age groups have varied access to information and expertise about capital structure of a firm. Age heterogeneity improves the ability of directors to solve tasks with high complexity such as issues of debt and equity financing. For groups working on simple tasks, however, age heterogeneity increased the number of self-reported health problems which in turn indicates that board of diverse ages should be utilized particularly for innovation or solving complex problems.

Recommendations

Owing to the above conclusions the study recommends that organization and especially SACCOs need to take the issue of board tenure seriously because it affects dividend payment. They need to put in place members on longer board tenures. The higher the board tenure quality the higher is the propensity to pay higher dividends and thereby reducing conflict of interest between agents and management.

It is recommended that companies and specifically SACCOs need to consider board diversity issues since companies with the best diversity score high against their dividend payment.

Since board independence and independence of sub-committees has a positive influence on

dividend payout with a view to reducing free cash flow. It is in the best interest of firms to pay dividends and thereby signal the good prospects when firms have good projects available. It is recommended that SACCOs need to ensure that there are independent directors who facilitate continual monitoring of the firm by the market participants.

The study recommends that board membership by SACCOs must ensure that its composition has age diversity because age diversity has the potential to enhance board performance, because directors of different ages will, to some extent, have different backgrounds, skills, experiences and social networks. Different age groups have varied access to information and expertise about capital structure of a firm.

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