Paper Laid

By vice-chairperson, Standing Committee on Finance, Commerce and Budget.

16/02/2016

REPUBLIC OF KENYA

THE NATIONAL TREASURY

Division of Revenue Bill, 2016

A Legislative Proposal for submission to Parliament

THE DIVISON OF REVENUE BILL, 2016

ARRANGEMENT OF CLAUSES

Clause

A Bill for

AN ACT of Parliament to provide for the equitable division of revenue raised nationally between the national and county governments in 2016/17 financial year, and for connected purposes.

ENACTED by Parliament of Kenya, as follows—

PART I— PRELIMINARY

Short title.

1. This Act may be cited as the Division of Revenue Act, 2016.

Interpretation.

2. In this Act, unless the context otherwise requires—

"Cabinet Secretary" means the Cabinet Secretary for the time being responsible for matters relating to finance;

"revenue" has the meaning assigned to it under section 2 of the Commission on Revenue Allocation Act, 2011;

No. 16 of 2011.

"State Organ" has the meaning assigned to it under Article 260 of the Constitution; and

"Wasteful expenditure" has the meaning assigned to it under section 2 of the Public Finance Management Act, 2012.

No. 18 of 2012.

Object and purpose of the

3. The object and purpose of this Act is to provide for

Act.

the equitable division of revenue raised nationally between the national and county levels of government for the financial year 2016/17 in accordar ce with Article 203 (2) of the Constitution.

Allocations to national and county governments.

4. Revenue raised by the national government in respect of the financial year 2016/17 shall be divided among the national and county governments as set out in the Schedule to this Act.

Variation in revenue.

5. (1) If the actual revenue raised nationally in the financial year falls short of the expected revenue set out in the Schedule, the shortfall shall be borne by the national government.

(2) If the actual revenue raised nationally in the financial year exceeds the projected revenues set out in the Schedule, the excess revenue shall be apportioned between the national government and county governments on a prorate basis in accordance with the criteria set out in the Schedule.

Resolution of disputes and payment of wasteful expenditure.

6. (1) Any State Organ involved in an intergovernmental dispute regarding any provision of this Act or any division of revenue matter or allocation shall, in accordance with Article 189 of the Constitution and before approaching a court to resolve such dispute, make every effort to settle the dispute with the other State Organ concerned, including exhausting all alternative mechanisms provided for resolving disputes in relevant legislation.

(2) If a court is satisfied that a State Organ, in an attempt to resolve a dispute has not exhausted all the mechanisms for alternative dispute resolutions as contemplated in section 35 of the Intergovernmental Relations Act, 2012 and refers the dispute back for the reason that the State Organ has not complied with subsection (1), the expenditure incurred by that State Organ in approaching the court shall be regarded as

No. 2 of 2012.

wasteful expenditure.

(3) The costs in respect of such wasteful expenditure referred to in subsection (2) shall, in accordance with a prescribed procedure, be recovered without delay from the person who caused the State Organ not to comply with the requirements of subsection (1).

SCHEDULE (s.4)

Allocation of revenue raised nationally between the national and county governments for the financial year 2016/17

Type/level of allocation	Amount in Ksh.	Percentage (%) of 2013/14 audited Revenue i.e. Ksh. 935,653 Millions
National Government	1,093,899,000,000	
Of which:		
Free maternal healthcare	4,121,029,353	
Leasing of Medical Equipment	4,500,000,000	
Compensation for user fees forgone	900,000,000	
Level 5 hospitals	4,000,000,000	
Special Purpose Grant supporting access to emergency medical services	200,000,000	
Equalization Fund	6,000,000,000	0.64%
County equitable share		

	280,300,000,000	30%
Total shareable revenue	1,380,199,000,000	

Memo items

County equitable share	280,300,000,000	
Additional allocations:		
Free maternal healthcare	4,121,029,353	
Leasing of Medical Equipment	4,500,000,000	
Compensation for user fees forgone	900,000,000	
Level 5 hospitals	4,000,000,000	
Special purpose grant supporting access to emergency medical services	200,000,000	
Allocation from Fuel Levy Fund (15%)	4,306,807,629	
Conditional allocations (Loans & grants)	3,870,679,737	
Total County Allocations	302,198,516,719	32 %

MEMORANDUM OF OBJECTS AND REASON

The principal object of this Bill is to provide for the equitable division of revenue raised nationally among the national and county levels of government as required by Article 218 of the Constitution in order to facilitate the proper functioning of county governments and to ensure continuity of county services.

Clauses 1 and 2 of the Bill provide for the short title of the Bill and the interpretation of terms used in the Bill.

Clause 3 of the Bill contains the provisions on the objects and purpose of the Bill.

Clause 4 of the Bill prescribes the allocations for the national government and the county governments from the revenue raised nationally for the financial year 2016/17.

Clause 5 of the Bill deals with mechanisms for adjusting for variations in revenues emanating from revenue performance during the financial year in which this Bill relates to.

Clause 6 of the Bill contains general provisions which emphasize on alternative dispute resolution before instituting court proceedings and includes provisions on personal liability on public officers who cause a State Organ to incur costs because of referring disputes relating to division of revenue to courts prior to exhausting available alternative dispute resolution mechanism.

Dated the 12th February, 2016

Henry Rotich, EGH
Cabinet Secretary for
The National Treasury

APPENDIX

EXPLANATORY MEMORANDUM TO THE DIVISION OF REVENUE BILL (DoRB), 2016

Background

1. This memorandum has been prepared as an attachment to the Division of Revenue Bill (DoRB), 2016 in fulfilment of the requirements of Article 218(2) of the Constitution and Section 191 of the Public Finance Management Act, 2012.

2. Article 218(2) of the Constitution requires that the Bill be submitted to Parliament every year together with a memorandum explaining:

(a) the proposed revenue allocation set out in the Bill;

(b) the extent to which the Bill has taken into account the provisions of Article 203 (1) of the Constitution; and

(c) any significant deviations from the recommendations of the Commission on Revenue Allocation (CRA).

3. In addition to the above requirements, Section 191 of the Public Finance Management Act, 2012 requires that the Bill be submitted to Parliament together with the Medium Term Budget Policy Statement accompanied by a memorandum which explains;

(a) the extent, if any, of deviation from the recommendations of the Intergovernmental Budget and Economic Council; and

(b) any assumptions and formulae used in arriving at the respective allocations proposed in the Bill.

Explanation of the Allocations to the National and County Governments as Proposed in the Bill

4. The DoRB, 2016 proposes to allocate to County Governments Ksh.302.2 billion in the financial year 2016/17, which relative to the 2014/15 allocation, reflects an increase of Ksh. 20.4 billion or 7 per cent. This allocation comprises of an equitable share of Ksh. 280.3 billion and additional conditional allocations from the share of national government revenue amounting to Ksh. 21.9 billion.

County Governments' Equitable Share

5. The County Governments' equitable share of revenue raised nationally for the financial year 2016/17 is arrived at by growing the County Governments' equitable share for 2015/16 of Ksh. 259.77 by a growth factor of 7.8 percent. This growth has taken into consideration performance of revenue in the past which has not been on target. The equitable share of revenue, thus determined, is an unconditional allocation to the County Governments and therefore County Governments are expected to plan, budget, spend, account and report on the funds allocated independently. This allocation to County Governments takes into account all the functions gazetted for transfer to County Governments by the Transition Authority.

6. After making the above adjustment, County Governments' equitable share of revenue in the financial year 2016/17 is estimated to be Ksh. 280.3 billion **(see Table 1)**. This allocation is above the constitutional minimum of 15 percent of the latest audited revenues for FY 2013/14 (i.e. Ksh. 935.7 billion).

Table 1: Equitable Revenue Share Allocation to County Governments, FY 2016/17

Budget Item	Amount in Ksh. Million
County Equitable Revenue Share for FY2015/16	259,775
Add:	
Adjustment for Revenue Growth (Agreed Revenue growth factor= 7.8 %)	20,225
Equitable Revenue Share allocation for FY 2016/17	**280,300**

Source: National Treasury

Additional Conditional Allocations to County Governments

7. Article 202(2) of the Constitution provides for additional allocation to County Governments from the National Government's share of revenue, either conditionally or unconditionally. Pursuant to this Article, the National Government proposes to allocate the following additional conditional allocations to support specific national policy objectives to be implemented by County Governments:

- **Conditional Grant in support of Free Maternal Health Care of Ksh 4.1 billion.** This grant of Ksh.4.1 billion is to be transferred to County Governments on a reimbursement basis through the respective County Revenue Fund Accounts, upon confirmation that the County Government provided maternal health care services in their health facilities in accordance with agreed specifications. This grant is intended to further facilitate access to free maternal health care in order to reduce the high maternal and child mortality rates in Kenya..

- **Conditional Grant to facilitate the leasing of medical equipment of Ksh 4.5 billion.** This grant is in its second year of implementation and is intended to facilitate the purchase of modern specialised medical equipment in at least two health facilities in each County Government over the medium term. This will facilitate easy access to specialised health care services and significantly reduce the distance that Kenyans travel in search of such services today. This grant will be managed by the National Government on behalf of the County Governments, in accordance with intergovernmental agreements entered into.

- **Conditional grant for level-5 hospitals of Ksh. 4.0 billion.** Level-5 hospitals continue to play a significant role in providing specialised health care services to Kenyans. These hospitals provide specialised health care services to citizens residing outside their host County, usually for complicated cases referred from lower level health facilities. In order to compensate them for the costs incurred in rendering services to neighbouring Counties, the national government proposes to further allocate Ksh. 4.0 billion up from 3.6 billion allocated in FY 2015/2016. This grant will be transferred to County Governments as a conditional grant through the respective County Revenue Fund Accounts.

- **Conditional Grant of Ksh. 900 million to compensate county health facilities for forgone user fees.** It is the intention of government to sustain the Government policy of not charging user fees in public health facilities. In this regard, and in furtherance of this policy, the National Government has allocated Ksh. 900 million in the financial year 2016/17 to compensate county governments for revenue forgone by not charging user fees in the county health facilities.

- **Conditional Grant from the Road Maintenance Fuel Levy Fund of Ksh. 4.3 billion.** This conditional grant which is in its second year of allocation has been increased from an allocation ksh. 3.3 billion in FY 2015/16 to Ksh.4.3 billion in FY 2016/2017. This grant is meant to further enhance County Governments' capacity to repair and maintain county roads and is equivalent to 15 percent of the Road Maintenance Fuel Levy Fund.

- **Special purpose grant supporting specialised medical access of Ksh. 200 million-** Special Purpose Grant of Ksh 200 million has been established to support strengthening of access to emergency medical services in Lamu and Tana River counties which -- because they border Somalia -- are vulnerable to terror attacks, security threats and humanitarian crises. The funds, to be shared equally by the two counties, comprise a conditional grant to reinforce the capacity of two major referral hospitals (Hola and Lamu) to provide emergency medical care to critically-injured patients. The support covers medical surgical equipment and infrastructure e.g. I.C.U, theatre, wards and rehabilitation facilities.

- **Conditional Grant from proceeds of a grant from the Government of Denmark and a loan from the World Bank amounting to Ksh 1.7 billion.** These funds are intended to support the delivery of health services in county health facilities with a view to increase access to health care services by Kenyans and in particular the poor.

- **Conditional allocation financed by other loans and grants received from development partners** and the Government counterpart funding derived from the National Government's share all totalling Ksh 3.8 billion. These conditional allocations which have declined from a total of ksh. 10.7 billion in the FY 2015/16 to the current ksh.3.8 billion relate to loans and grants contracted prior to the establishment of the devolved system of government. This reduction is as a result of winding up of some donor financed projects included in the budget for the financial year 2015/16. These conditional allocations financed by proceeds of loans and grants, however, will not be transferred to County Governments in the financial year 2016/17 due to the following reasons:

    - There exists financing agreements guiding the structures and management framework of all the programmes/projects, the alteration of which would take long and delay implementation of programmes/projects;

    - Loans and grants earmarked for devolved functions are tied to on-going contracts with suppliers, the alteration of which may have legal and cost implications;

    - Some of the programmes/projects funded by loans and grants have agreed implementation structures transcending more than one County and therefore it may not be possible to place the responsibility for their management in one County Government; and

- The financing agreements also specify the funds flow modalities which may not be consistent with what is contemplated under the intergovernmental arrangement.

It is therefore expected that the loans and grants under the existing financing agreement will be included in the budget of the National Government. These funds will be managed by the National Government but with involvement of County Governments in the Project Steering Committees and Project Implementation Units for each programme/project. In addition, reporting arrangements as well as the conditions attached to the implementation of the programme/project will be clearly spelt out in Project Implementation Frameworks to be agreed with County Governments prior to the release of the funds and implementation of the projects.

Evaluation of the Bill against Article 203 (1) of the Constitution

8. Article 218(2) of the Constitution requires division of revenue between the two levels of government and across County Governments to take into account the criteria set out in Article 203(1) of the Constitution. The criteria include factors such as: national interest, public debt and other national obligations, needs of the disadvantaged groups and areas etc.

9. Table 2 provides an assessment of the extent to which the requirements of Article 203 (1) have been incorporated in estimating the division of revenue between the National and County levels of Government in the financial year 2016/17.

Table 2: Evaluation of the Bill against Article 203 (1) of the Constitution

	ITEM DESCRIPTION	2015/16	2016/17
		Ksh. Millions	Ksh. Millions
A	**Ordinary Revenue (excluding AIA)**	**1,249,900**	**1,380,199**
B	**National Interest [Article 203 (1)(a)]**	**79,189**	**71,954**
	1. Enhancement of Security Operations (police vehicles, helicopters, defence etc.)	17,700	18,900
	2. National Irrigation & Fertilizer Clearance	12,500	9,500
	3. NYS Re-engineering	17,055	11,620
	4. National Social safety net - (for older persons, OVC, Child Welfare, severe disability, urban food subsidy)	14,354	14,354
	5. Laptops	17,580	17,580
C	**Public Debt (Article 203 [1][b])**	**362,391**	**433,800**
D	**Other National Obligations (Article 203 [1][b])**	**341,744**	**363,162**
	1. Pensions, constitutional salaries & other	54,617	56,115
	3. Constitutional Commissions (Art. 248(2)) - i.e. CRA, CIC, SRC, NLC, NPSC, IEBC, TSC	189,066	208,763
	3. Independent Offices(Art. 248(3)) - i.e. AG & CoB	4,720	4,723
	4. Parliament	27,277	27,705
	5. Other Constitutional Institutions- AG's office and DPP	6,863	6,607
	6. Other Statutory Bodies (e.g. EACC,RPP,WPA,CAJ, IPOA, NGEC)	4,697	4,855

	7. Judiciary	17,161	17,759
	8. Other Statutory Allocations(earmarked funds e.g. Constituency Development Fund, Women Affirmative Action Fund)	37,343	36,635
E	**Emergencies [Article 203 (1)(k)]**	**7,245**	**7,245**
	1.Contingencies	5,000	5,000
	2.Strategic Grain Reserve	2,245	2,245
F	**Equalisation Fund [Article 203 (1) (g) and (h)]**	**6,000**	**6,000**
G	**Balance to be shared between the National and County Government**	**453,331**	**498,038**
H	**County Government Allocation from Revenue Raised Nationally**	**273,070**	**294,021**
I	**Balance Available for National Government Needs**	**180,261**	**204,017**

10. **National Interests:** These are expenditures which relate to projects and programmes that:

- are critical to the achievement of country's economic development objectives;
- potentially will have significant impact of social well-being of citizens;
- are anchored in the Vision 2030 and the Medium Term Plan II (2013 – 2017); and
- have significant resource investment requirements.

These projects and programmes of national interest have also been specified in the 2016 Budget Policy Statement.

These national interests include: activities aimed at enhancing security operations; national irrigation and fertilizer subsidy initiatives; National Youth Service re-engineering; provision of national social safety net for vulnerable groups and provision of laptops to primary school pupils. Revenue allocation for these functions is expected to drop slightly from Ksh. 79.2 billion in 2015/16 to Ksh. 72.0 billion in 2016/17.

11. **Public Debt:** The Bill has fully provided for all public debt related costs. These comprise of the annual debt redemption cost as well as the interest payment for both domestic and external debt. In 2016/17, the revenue allocation for payment of public debt related costs is expected to increase to Ksh. 433.8 billion in 2016/17, up from Ksh. 362.4illion in 2015/16 financial year primarily due to the shift to less expensive debt from international markets.

12. **Other National Obligations:** As provided for under Article 203(1) (b) of the Constitution, the Bill has also taken into account the cost of other national obligations, such as, mandatory pension contributions and/or payments, financing for constitutional offices, including Parliament as well as expenses relating to other statutory bodies and funds. These are estimated to cost Ksh. 363.2 billion in 2016/17 up from Ksh. 341.7 billion in 2015/16.

13. **Fiscal Capacity and Efficiency of County Governments:** Fiscal capacity for county governments, that is, the potential revenues that can be generated from the tax bases assigned to the counties when a standard average level of effort is applied to those tax bases, has not been assessed fully. It is also still early to measure county governments' fiscal efficiency. As a result, there is no official data on county fiscal capacity and efficiency and therefore this criterion has not been taken into account in the determination of the division of revenue between the national and county governments. However during the FY 206/17 there are plans to come up with a National Framework for enhancing county governments own source revenues.

14. **County governments' ability to perform the functions assigned to them and meet other developmental needs of the county governments:** As explained above, the baseline for the equitable share allocation for the financial year 2016/17 was derived from the Division of Revenue Act, 2015.

15. It should be noted that allocations for devolved functions transferred from the national government were based on the historical cost of those functions as determined through a consultative process that involved the line ministries and other independent commissions and offices.

It is therefore clear that the proposed vertical division of revenue proposed in the Division of Revenue Bill, 2016 takes into account the cost of county governments' developmental needs and therefore it is expected that county governments will have the ability to perform the functions assigned and transferred to them as contemplated under Article 203(1)(f).

16. **Economic Disparities within and among counties and the need to remedy them:** Allocation of the sharable revenue (i.e. equitable share of Ksh. 285.4 billion) among counties is based on the formula approved by Parliament which takes into account disparities among counties and aims at equitable distribution of resources. The formula takes into account population (45%), land area (8%), poverty (20%), a basic equal share (25%), and fiscal responsibility (2%). The equitable share of revenue for county governments in 2016/17 reflects an increase of 10.6 percent compared to the allocation in 2015/16. This means that there is more money in 2016/17 to help remedy economic disparities within and among counties. This formula, however, lapsed in 2015 and the second formula for sharing revenue among county governments waits Parliament's approval. It should also be noted that Ksh. 6.0 billion has also been set aside for the Equalization Fund in 2016/17. This Fund will be used to finance development programmes that aim to reduce regional disparities among counties.

17. **Need for Economic Optimization of Each County:** Allocation of resources to county governments was guided by the costing of the functions assigned to the county governments. The equitable share of revenue allocated to county governments was increased by 7.8 per cent from Ksh. 259.77 billion in 2015/16 to Ksh. 280.3 billion in 2016/17. This is an unconditional allocation which means that the county governments can plan, budget and spend the funds independently. With the additional resources, therefore, county governments can allocate more resources to their priority projects and thus optimize their potential for economic development.

18. **Stable and Predictable Allocations of County Governments' Vertical Share of Revenue:** The county governments' equitable share of revenue raised nationally has been protected from cuts that may be necessitated by shortfall in revenue raised nationally. According to the DoRB 2016, any shortfall in revenue raised nationally is to be borne by the National Government.

19. **Need for Flexibility in Responding to Emergencies and Other Temporary Needs:** Included in the equitable share of revenue for the national government is an allocation of Ksh. 5 billion for the Capital of the Contingencies Fund. This Fund will be used to meet the demands arising from urgent and unforeseen needs in all Counties that suffer from calamities in the manner contemplated under Section 21 of the Public Finance Management Act, 2012. In addition, the Public Finance Management Act, 2012 requires each county government to set up a County Emergency Fund. County governments are expected to set aside part of their allocation for this purpose.

20. It should be noted that after taking into account all the other factors required to be taken into account in sharing revenue between the two levels of government, including the needs of county governments, only Ksh. 204.0 billion is left to finance other National Government needs, such as, defence, roads, energy etc.

Response to the Recommendations of the Commission on Revenue Allocation

21. The Division of Revenue Bill, 2016 proposes to allocate county governments an equitable share of Ksh. 285.4 billion from the shareable revenue raised nationally. The CRA, on the other hand, recommends County Governments' equitable share of revenue of Ksh. 331.8 billion as an unconditional allocation to be shared among county governments on the basis of the formula for sharing revenue approved by Parliament under Article 217 of the Constitution. The difference in the Commission on Revenue Allocation (CRA) recommendation and the National Treasury proposal emanates from the different approaches used to compute the County Governments' equitable share of revenue. These include:

- **Use of different revenue growth factor:** CRA grows the county equitable share revenue by 15.09 percent, which is the average growth rate of audited shareable revenue raised nationally over the past three years. The National Treasury on the other hand uses a revenue growth factor of 7.8 percent. This growth factor has taken into consideration performance of revenues which have not been performing in the past.

- **County equitable revenue share adjustment of Ksh. 27.8 billion for additional county roads**: In anticipation of a decision by the Transition Authority (TA) to transfer additional county roads in FY 2016/17, the CRA proposed to gross up the county equitable share of revenue for 2016/17 by an allocation of Ksh. 27.8 billion for construction and rehabilitation of county roads. It should be noted that at the time when CRA recommended the transfer of an additional Ksh. 27.8 billion to County Governments, the TA had not gazetted the decision to transfer additional county roads to County Governments. The National Treasury view is that any additional resources to be transferred to County Governments in respect of county roads function should be supported by a gazette notice by the TA authorising such transfer and a determination of resources, if any, to be transferred to County Governments. It should, however, be noted that as early as FY 2013/14, some resources relating to roads were transferred to County Governments and therefore the county equitable revenue share proposed by the National Treasury for FY 2016/17 already includes an allocation for county roads.

- **County equitable revenue share adjustment of Ksh. 5 billion to cater for public participation**: The CRA has proposed a further adjustment of the equitable revenue share to include an allocation of Ksh.5.0 billion to cater for public participation in FY 2016/17. The National Treasury view is that whilst public participation is a constitutional requirement for both levels of government in carrying out any development agenda, each level of government is required by law to set aside funds for the same function form its resources.

22. Table 3 below analyses the differences between the CRA recommendations and the National Treasury proposal on the division of revenue between the national and county governments in 2016/17.

Table 3: Comparison of Recommendations of the Commission on Revenue Allocation and the National Treasury on the Division of Revenue in 2016/17 (Figures in Ksh. Billions)

Expenditure Item	2016/17		
	CRA (A)	National Treasury (B)	Variance C = (A-B)
Equitable Revenue Share in FY 2015/16	259.8	259.8	0
Add			
Adjustment for revenue growth in FY 2016/17	39.2	20.5	18.7
Adjustment for County Roads	27.8	0	27.8
Adjustment for Public Participation	5.0	0	5.0
TOTAL EQUITABLE SHARE OF REVENUE	**331.8**	**280.3**	**51.5**

Source: National Treasury

23. Further the Commission on Revenue Allocation has in the financial 2016/17 proposed new conditional allocations amounting to Ksh. 25.7 billion that the National Treasury has not included in the Division of Revenue Bill. These have resulted in a significant variance between the National Treasury and the CRA proposals on division of revenue for FY 2016/17. These include;

- **Allocation to cater for emoluments for Devolved staff of Ksh. 5.196 billion:-** CRA has proposed an additional Ksh. 5.196 billion, to be shared proportionately among counties based on payroll of devolved staff. These allocations are intended to act as a short term stop gap measure to cushion counties that inherited a relatively higher number of employees, against expenses on salaries as they await conclusion of the staff rationalization programme. It should, however, be noted that in costing of devolved functions adequate provisions were made to cater for county personnel expenses. Indeed, additional allocations (Ksh. 6.3 billion) to cater for county payroll were included in the equitable share of revenue for FY 2015/16. It should also be remembered that in FY 2013/14 amounts set aside to hold harmless county governments that inherited higher than average wage bills, were shared on the basis of the revenue sharing formula following an agreement among county governments. In the opinion of the National Treasury, at the current level of funding county governments have sufficient resources to cater for the cost of personnel emoluments.

- **Additional conditional allocation for construction of County headquarters of Ksh. 4.0 billion -** CRA proposes an conditional additional allocation of Ksh. 4.0 billion to be shared equally for construction of county headquarters in Tharaka Nithi, Lamu, Nyandarua, Tana River and Isiolo counties. Whilst it is true that the above named counties did not inherit offices that could accommodate the county government, there is no evidence that these counties applied the funds transferred to them by the Transition Authority in FY 2013/14 for the refurbishment of identified headquarters offices. It is felt that the concerned counties should demonstrate commitment first by initiating the construction prior to seeking National Government support. Financing from National Government could then be provided once the financial position of Government improves. Currently, the National Government financial position may not allow for additional fiscal transfers to county governments as proposed by the CRA.

- **Additional conditional allocations for Rehabilitation of Primary and Secondary school of Ksh. 5.0 billion-** the proposed new conditional additional allocation by CRA of Ksh. 5.0 billion is meant for building of school infrastructure, a role they say has been left to parents despite the function being a national one. The view of the National Treasury is that these are National government functions and that such a conditional grant can only be initiated by the ministry responsible for primary and secondary education.

- **Conditional additional allocation for the Establishment of County Emergency Fund of Ksh. 5.2 billion: -** CRA has proposed new conditional additional allocation of Ksh. 5.2 billion as seed money towards establishment of County Emergency Funds in line with provisions of PFMA Section 110(1) to be shared proportionately among counties. The National Treasury holds contrary opinion on this proposal because the PFMA anticipates that all governments, both national and county, should set aside funds for the establishment of their respective Emergency Funds. More over a similar proposal was dropped on the above legal basis by the mediation committee of Parliament when making recommendations on the Division of Revenue Bill, 2015.

- **Conditional additional allocation for the Rehabilitation of Village Polytechnics of Ksh. 6.3 billion: -** the CRA has further proposed an additional conditional allocation of Ksh. 6.3 billion from the national government share of revenue to county governments so as to build, equip and renovate village polytechnics. The CRA further argue that these village polytechnics will go a long way to serve as centres of excellence to empower youth with the requisite skills to generate employment. The National Treasury acknowledges this is a devolved function and that the Village Polytechnics are essential in developing skills of the Youth who don't transit to institutions of higher learning. However, due to limitation in resources, the National Treasury recommends that this conditional allocation be done through donor financing within the provisions of the External Resources Policy of the National Treasury. As such, it is proposed that the decision to include it in the budget for FY 2016/17 be shelved until a potential dònor is identified.

24. It's also worth noting that the CRA proposes an increase in the existing conditional additional allocations by a growth factor of 15.09 percent. The existing conditional allocations include allocations for; Level-5 hospitals, Free Maternal Health Care, Compensation for User fee forgone, leasing of medical equipment and county roads with funding from Roads Maintenance Fuel Levy It should be noted that allocations for the various conditional additional allocations are determined through the national MTEF budget process based on the weight attached to the national government policy objectives that the allocations are intended to support.

25. In conclusion, allocation to each level of government has been informed by the costing of functions assigned to each level of government. The proposals contained in the Bill are also intended to ensure that neither a huge financing gap is created nor functions at either level of government are left unfunded or underfunded. In this regard, any additional allocation beyond the cost of functions as proposed in the CRA recommendations specifically county roads and public participation may be considered only if there is demonstrable evidence that the county roads function has been gazetted and attendant resources identified for transfer or the revenue growth has improved. At the moment, the National Treasury has not received a confirmation of additional resources that ought to be transferred to county governments in respect of additional functions transferred. The CRA does not provide such evidence and therefore such proposals should be shelved until the function is gazetted and attendant resources identified It should be noted that any financing gaps created can only be financed through higher taxes that would push up the cost of doing business in Kenya or by way of additional borrowing that would push interest rates up and thereby slow the growth of the economy.

26. It should, however, be noted that the National Treasury's proposed equitable share allocated to county governments in the Division of Revenue Bill, 2016, at 30 per cent of the most recent audited revenue, as approved by the National Assembly, is way above the minimum threshold required under Article 203(2) of the Constitution.

Response to the Recommendations of the Intergovernmental Budget and Economic Council (IBEC)

27. The Intergovernmental Budget and Economic Council (IBEC) recommended that county equitable share of revenue for FY 2016/17 be increased by a growth factor arrived at on the basis of the principles agreed at the IBEC meeting of 11th February 2015. The implementation of this recommendation is, however, not possible given that revenue collection at the national level has been below target.

28. The IBEC further resolved that county governments be allocated additional conditional grants amounting to Ksh. 1.5 billion to support the rehabilitation of village polytechnics. The National Government recognises the critical role played by village polytechnics in contributing to economic development and increasing employment opportunities for the youth. However, given the tight financial position of Government it is not possible to provide this additional allocation to counties in FY 2016/17. This request will be considered when the financial position of Government improves.

29. The IBEC also recommended that the National Government considers allocating some funds for the construction of headquarters for five counties, that is, Lamu, Tharaka Nithi, Isiolo, Nyandarua, and Tana River. As explained at the IBEC meeting of 9th February 2016, this will be funded when discussions with the concerned counties are concluded and subject to availability of funds.