SCANNED

HARAMBEE

REPUBLIC OF KENYA

12TH PARLIAMENT - THE SENATE

THE SENATE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION

A REPORT ON THE COMMITTEE CONSIDERATION OF THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, LEGAL NOTICE NUMBER 89 OF 2022

CLS

Recommended for approval for tabling.

14/06/2022

Hon. Speaker

You may approve for tabling.

14/6/22

Approved

14/9/2022

The Senate,
Clerk's Chambers,
Parliament Buildings,
P.O. Box 41842-00100,
NAIROBI, KENYA

JUNE, 2022

PAPERS LAID	
DATE	14. JUNE 2022
TABLED BY	Sen. Faki
COMMITTEE	Delegated. L.
CLERK AT THE TABLE	M. Adjibodoi

DC-EG

Recommended & Forwarded for Approval

14/06/22

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Establishment of the Committee

Honourable Speaker,

The Senate Sessional Committee on Delegated Legislation is established under standing order 221 of the Senate Standing Orders. The Committee is mandated to scrutinize statutory instruments laid before the House to ensure that they are consistent with the provisions of the Statutory Instruments Act, 2013.

Membership of the Committee

Honourable Speaker,

The Senate Sessional Committee on Delegated Legislation is comprised of the following Senators-

Sen. Mwinyihaji Mohammed Faki, MP - *Chairperson*
Sen. Agnes Kavindu Muthama MP - *Vice Chairperson*
Sen. Samuel Poghisio, EGH, MP
Sen. Farhiya Ali Haji, CPA, MP
Sen. Judith Pareno, MP
Sen. Mary Seneta, MP
Sen. Abshiro Halake, MP
Sen. Prof. Samson Ongeri, EGH, MP
Sen. Anwar Loitiptip, MP

Executive Summary

Honourable Speaker,

The Public Finance Management (National Government) (Amendment) Regulations, Legal Notice Number 89 of 2022 were tabled in the Senate on 7th June, 2022 and committed to the Sessional Committee on Delegated Legislation for scrutiny.

Honourable Speaker,

Some of the key observations made by the Committee were as follows-

a) The ratio of Debt to GDP ratio is currently increasing which indicates that it may not be sustainable in future. However, the National Treasury is optimistic that the Post Covid 19 recovery program supported by the IMF will increase the rate of growth of GDP and therefore the ratio of debt to GDP will begin to decline going forward.

b) Economic factors for example, a depreciating shilling and increasing price levels may pose challenges in the sustainability of debt both in the medium term and in the future. This is majorly caused by external forces and perceived artificial shortages of the dollar. However, this is projected to stabilize since the country has enough foreign exchange reserves of up to five months import cover.

c) The instability of the Kenya's debt accumulation process is not conducive for investors who prefer a predictable business environment and are scared of sudden fiscal changes to address debt problems.

d) Public debt is serviced out of government revenues of which taxation is a major source of revenues. Recently, the country has experienced increased tax rates partly arising from IMF conditions. Growing the debt levels too fast may eventually result to increased taxes in the future.

e) The National Treasury has been slow in shifting to a higher ratio of cheap concessional debt in comparison to expensive commercial debt.

f) A high debt ceiling may give the National Treasury leeway to increase debt at a fast rate leading to huge debts in the future and the challenge of high levels of debt is the increase in vulnerabilities in the event of shocks similar to Covid 19.

g) The realized deficit has always been higher than the projected deficit and thus the deficit may continue to increase other than decline. The size of the deficit is driving the growth of public debt despite the fact that parliament has the power to determine sustainable deficit levels.

Honourable Speaker,

The Committee further observed that-

h) The National Treasury needs to put enough effort to build confidence with regards to public debt management and sustainability in the country. It was noted that 'the mere fear of non-sustainability, makes non-sustainability a reality'.

i) The new limit of ten trillion will be beyond the debt carrying capacity IMF /world bank benchmark of 55% for Kenya(DEC,2021) however, due to the post covid 19 recovery programs supported by the IMF the debt to GDP ratio is expected to decline towards the debt carrying capacity level in the medium term.

j) The National Treasury committed in 2019 that the debt ceiling of 9 trillion will be enough after 2024, however, a number of unfavourable events have taken place that have led to the depletion of the ceiling. The events include the Covid 19 pandemic and the Ukraine war and the resultant appreciation of the dollar.

k) The deficit in the budget estimates for 2022/23 and the medium term shall not be fully financed and development partners may stop funding ongoing projects if the debt ceiling is not increased.

l) The National Treasury has a number of policies aimed at addressing the macroeconomic pressures caused by increased expenditure demands and promoting fiscal consolidation. These include-

i. Plans to use more of EPC (Engineering, Procurement and Construction Contracts) project financing. The EPC project financing method transfers all the risks associated with design, procurement and construction to the contractor. This type of contracts are efficient and reduce project costs and also attractive to lenders and thus low borrowing costs.

ii. Efforts to ensure public debt sustainability that include; the enactment of the Public Private Partnership Act, 2021 that has enabled the undertaking of development projects outside the budget framework a case in point is the Nairobi Express way. All government projects currently undergo a feasibility study and considered whether they can be undertaken through PPP framework before they are factored in the budget.

iii. Automation of government procurement for all common user items and link it to IFMIS. The system is currently being developed by the National Treasury and will soon be rolled to Ministries and departments. This will ensure that no procurement is done outside the budget and therefore

Recommendation

Based on the foregoing observations and pursuant to Section 205 (4) of the PFM Act, Number 18 of 2012, the Senate Sessional Committee on Delegated Legislation presents its Report on the consideration of the Public Finance Management (National Government) (Amendment) Regulations, 2022, and recommends to the Senate that the Public Finance Management (National Government) (Amendment) Regulations, Legal Notice Number 89 of 2022, be approved.

SEN. MOHAMED MWINYIHAJI FAKI, MP,

CHAIRPERSON,

SESSIONAL COMMITTEE ON DELEGATED LEGISLATION.

DATED: 13TH JUNE, 2022

ADOPTION OF THE REPORT OF THE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION

We, the undersigned Members of the Senate Sessional Committee on Delegated Legislation do hereby adopt this Report at a Virtual Meeting held on 13th June, 2022 at 11.00 a.m.

Sen. Mwinyihaji Mohammed Faki, MP	**- Chairperson**
Sen. Agnes Kavindu Muthama MP	**- Vice Chairperson**
Sen. Samuel Poghisio, EGH, MP	
Sen. Farhiya Ali Haji, MP	
Sen. Judith Pareno, MP	
Sen. Abshiro Halake, MP	
Sen. Mary Seneta, MP	
Sen. Prof. Samson Ongeri, EGH, MP	
Sen. Anwar Loitiptip, MP	

DATED: 13TH JUNE, 2022

CHAPTER ONE

1.0 BACKGROUND

The National Treasury in accordance with section 12(b) of the Public Financial Management Act, 2012 has the responsibility of managing the level and composition of public debt, national guarantees and other financial obligations of the country and also develop a framework for sustainable debt control.

It is on the basis of the above that the National Treasury is proposing the Regulations to provide for the mechanisms to manage and ensure that government priorities are funded while ensuring that public debt is sustainable.

1.1 OVERVIEW OF THE REGULATIONS AND THE DEBT STATUS

1.1.1 Objectives of the Regulations

The National Treasury and Planning seeks to amend the PFM (National Government) Regulations, 2022, to increase the debt ceiling to a maximum of ten trillion shillings from the current nine trillion shillings.

The Regulations are published under Legal Notice Number 89 of 2022.

1.1.2 Historical debt ceiling amendments

Table 1: Summary table of debt ceiling amendments, 2013 - 2019

Amendment Year	Kenya External Loans Act, Chapter 422	2013	2014	2015	2019

Ceiling	650 Million Pounds Repealed by the PFM Act	USD 10 Bn to USD 14 Bn	USD 14 Bn to USD 28 Bn	USD 28 Bn to 50% of GDP (NPV)	50% of GDP (NPV) to Kshs. 9 Tn
Debt Capped	External Debt	External Debt	External Debt	Total Debt	Total Debt

1.1.3 Kenya's Public Debt Stock &Fiscal Deficit

a) Public Debt Servicing expenditures (interest payments and redemptions), required to finance the repayment of Kshs. 8.2 trillion[1] public stock of debt – composed of Domestic Debt, Kshs. 4.032 trillion and External Debt, Kshs. 4.174 trillion.

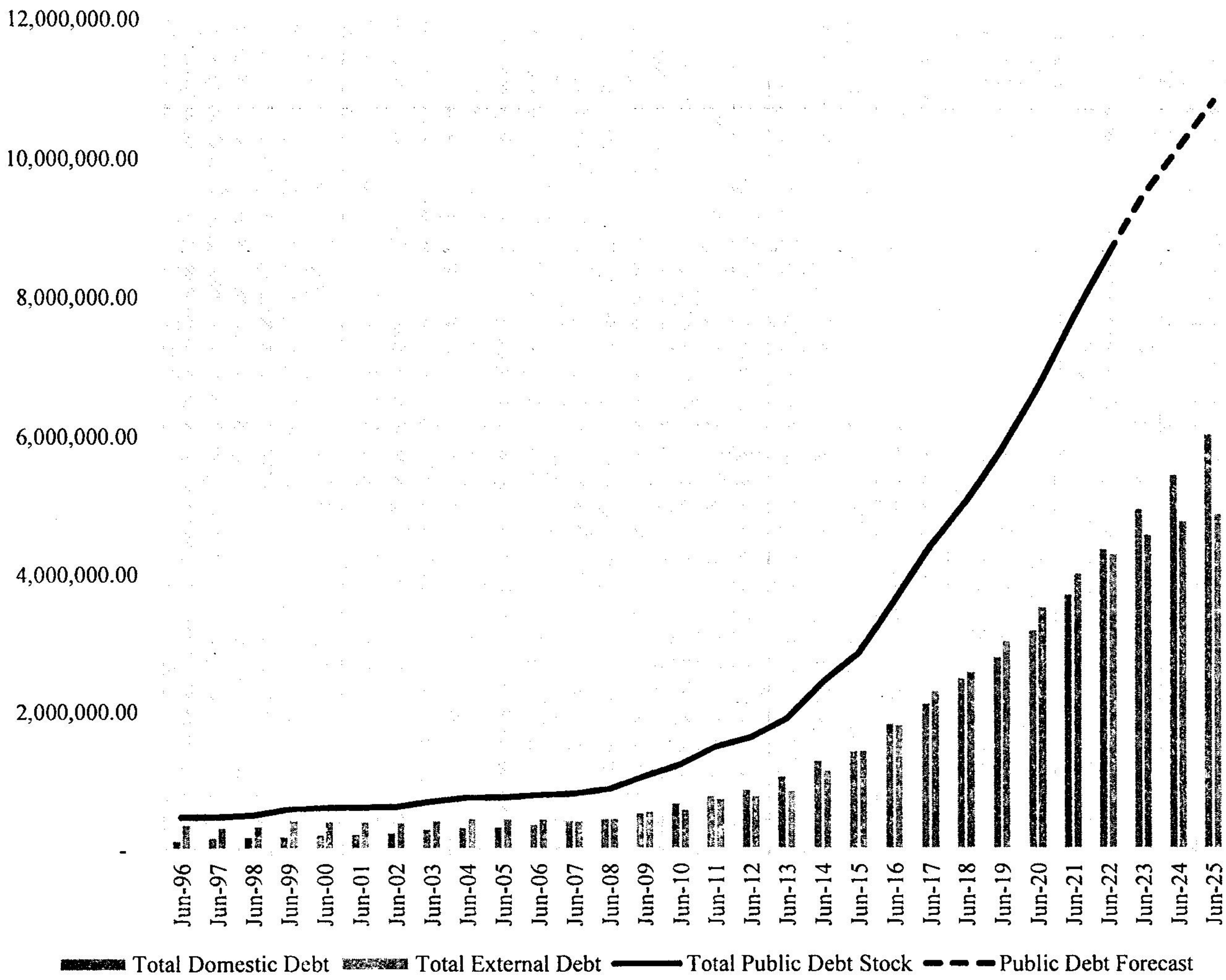
b) The total public debt is projected to reach Kshs. 11.5 trillion[2] by June 2025 on account of expanding fiscal deficit and without subsequent restructuring of public debt, Public Debt Service expenditures will continue to increase over the medium term. Notably, is the rise of use of Domestic debt which while accounting for 49% of total debt stock, it accrues up to 73% of total debt servicing expenditures.

c) The forecasts by the National Treasury and the Parliamentary Budget Office indicate that by June 2022, the debt stock will range between Kshs. 8.6 trillion and Kshs. 8.8 trillion. Further, it is estimated that by the end of 2024, the public debt stock will have crossed the Kshs. 10 trillion mark.

d) Thus, without an amendment to the ceiling, the government would have to maintain a balanced budget over the medium term. Taking into account the existing expenditure needs with no significant increase in revenue collection, an amendment to the ceiling may be necessary in order to ensure that these needs are met.

[1]Central Bank of Kenya Weekly Bulletin.
[2] Budget Summary April 2022

Figure 1: Public Stock of debt, June 1996 – June 2025



Source: National Treasury Official Documents

e) An analysis of the country's stock of debt indicate that it has grown from Ksh.466 billion in 1996 and is projected to reach Ksh.8.6 trillion by June,2022 as shown in figure 1.The debt is projected to reach Ksh.10.8 trillion by June,2025.

f) A review of the public debt characteristics indicates that costs and risks of debt burden will remain elevated primarily as a result of worsening domestic debt portfolios' risk & cost characteristics[3]. As such, prudent debt management has never been more critical as these risks coupled with the frequency and increasing

[3]Domestic debt in general shows a higher interest rate and refinancing risk compared to external debt portfolio.

size of debt servicing, could affect medium term fiscal sustainability and slowdown the pace of economic recovery.

g) It is therefore critical for national and county governments to prioritize the following-
   i. Fiscal consolidation,
   ii. enhanced transparency,
   iii. enhanced effectiveness of resource allocation,
   iv. efficiency in use of diminishing resources,
   v. fiscal discipline and fiscal commitment.

h) **Cost and Risk Profile of Kenya's public debt stock**

Domestic debt risk characteristics continues to worsen and the overall risk profile of the stock of debt is dependent on favorable external debt risk profile. The domestic debt portfolio has a higher refinancing risk and interest rate risk exposure, despite shifting borrowing from short-term debt instruments to using medium term to long-term instruments.

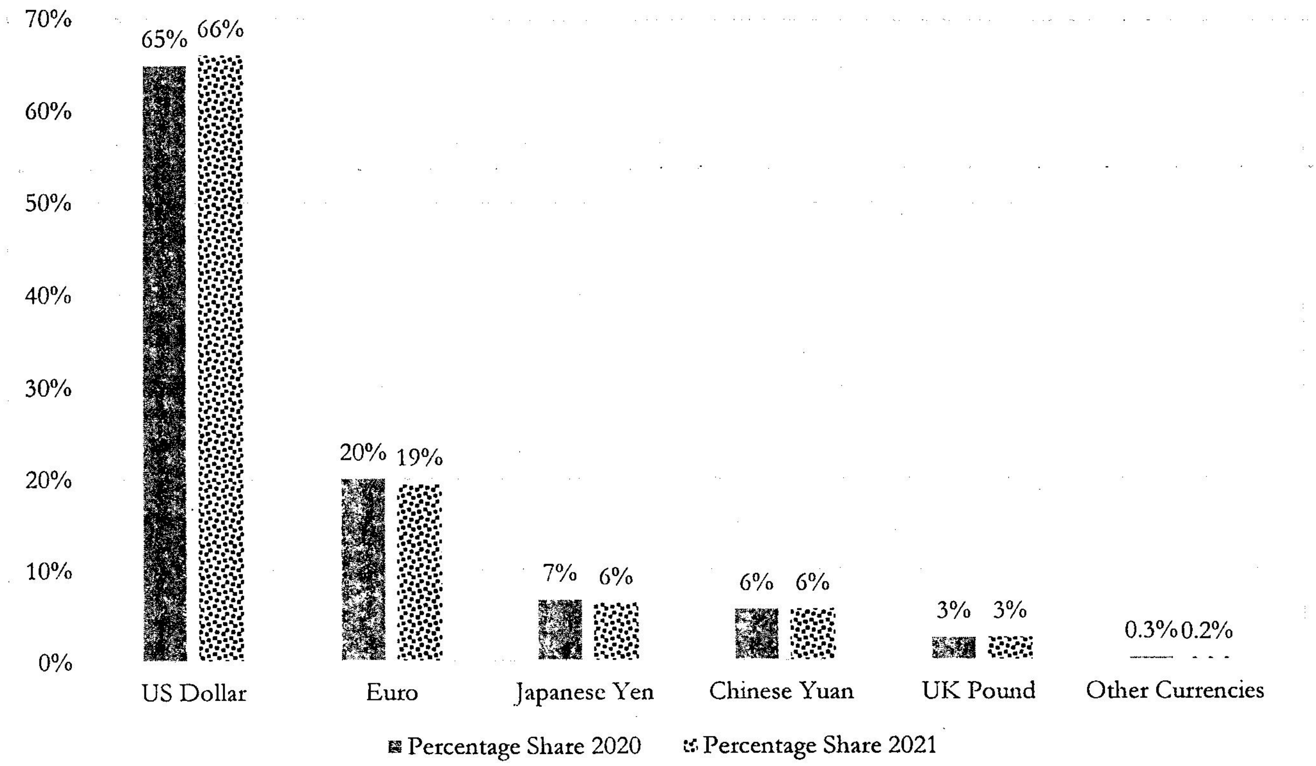
This is illustrated by: i) domestic debt having a much lower Average Term to Maturity (6.9 years) compared to External debt (10.8 years), ii) a higher rate of debt maturing in within one year (25.9%) compared to for external debt (5.2%), and iii) a higher Weighted Average Interest Rate (at 11.1%), compared to that of the external debt portfolio (2.9%).

i) **Currency Composition:**

Exchange rate risk relates to the impact of exchange rate fluctuation on external debt which is determined by both level and composition of external debt. As shown in figure 2,External debt accounted for 51.3% of total debt stock as of June 2021, and changed on marginally (from 51.2% - June 2020), indicating relative stability. The currency composition is as follows: USD , Euro and Japanese Yen at 66%, 19% and 6% respectively, and is as a result of reliance on certain creditors and/or market segments.

Nevertheless, it is the movements of the exchange rates related to these three currencies that have the highest impact on the amounts borrowed but also in year external debt servicing and thus illustrating the importance of a fiscal-monetary policy coordination framework.

Figure 2: Currency composition of External Debt



Source: 2021 MTDS

1.1.4 <u>Fiscal Deficit – Why Does the Stock of Debt Increase?</u>

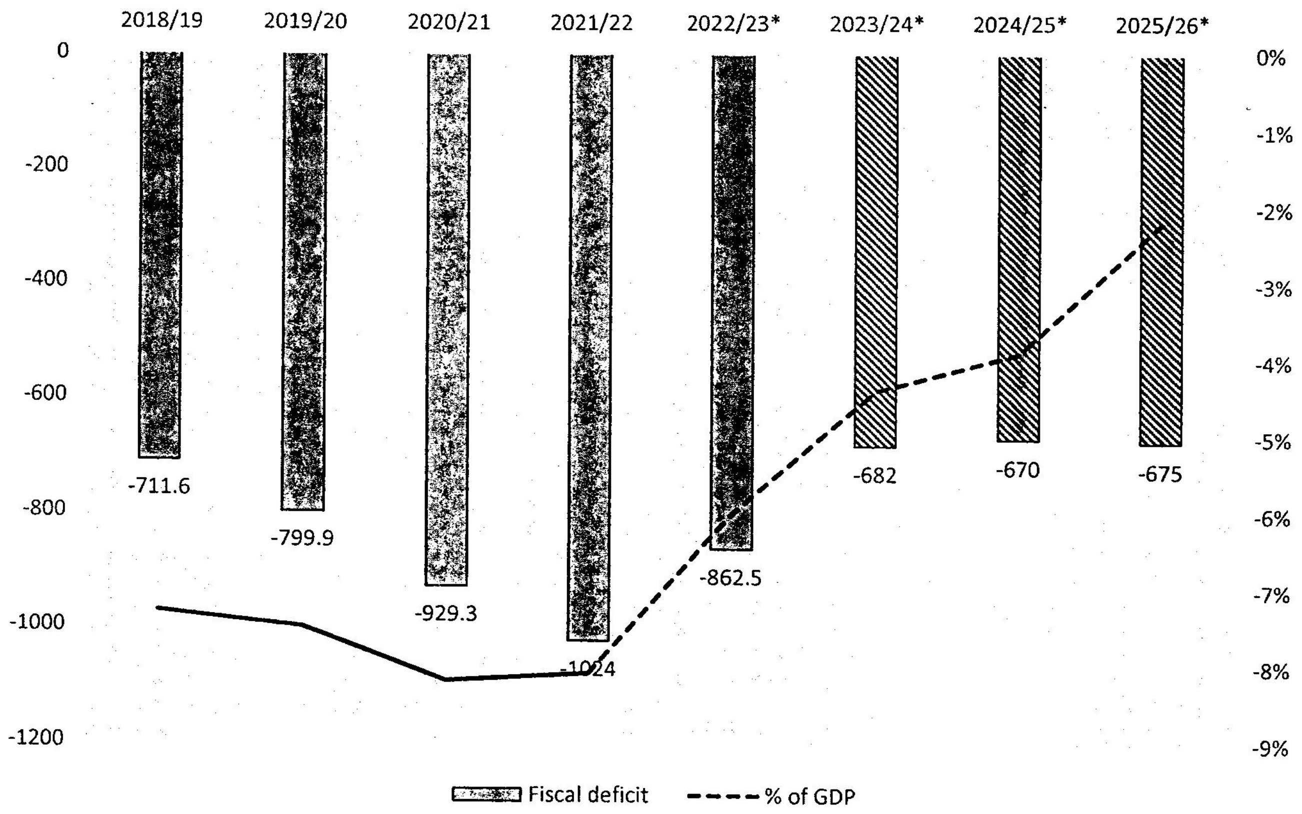
a) The fiscal deficit, which facilitates the accrual of public debt, is estimated to persist but decline into the medium term.Growing from 711.6 billion in 2018/19 reaching to Kshs. 862.5 billion in FY 2022/23 as shown in figure 3.It estimated to decline to Kshs. 675 billion by the end of the medium term[4] as illustrated in figure 3.

b) Whilst initially, the fiscal deficit prompted by large infrastructure related expenditures, the increase in debt servicing expenditures alongside critical expenditures (such as implementation of the economic recovery strategy, national

[4] 2022 Budget Policy Statement

election related expenditures), is expected to play a greater role in the stickiness of the fiscal deficit over the medium term, and determine the pace of debt stock growth.

Figure 3: Fiscal Deficit, 2020/21 & the Medium term



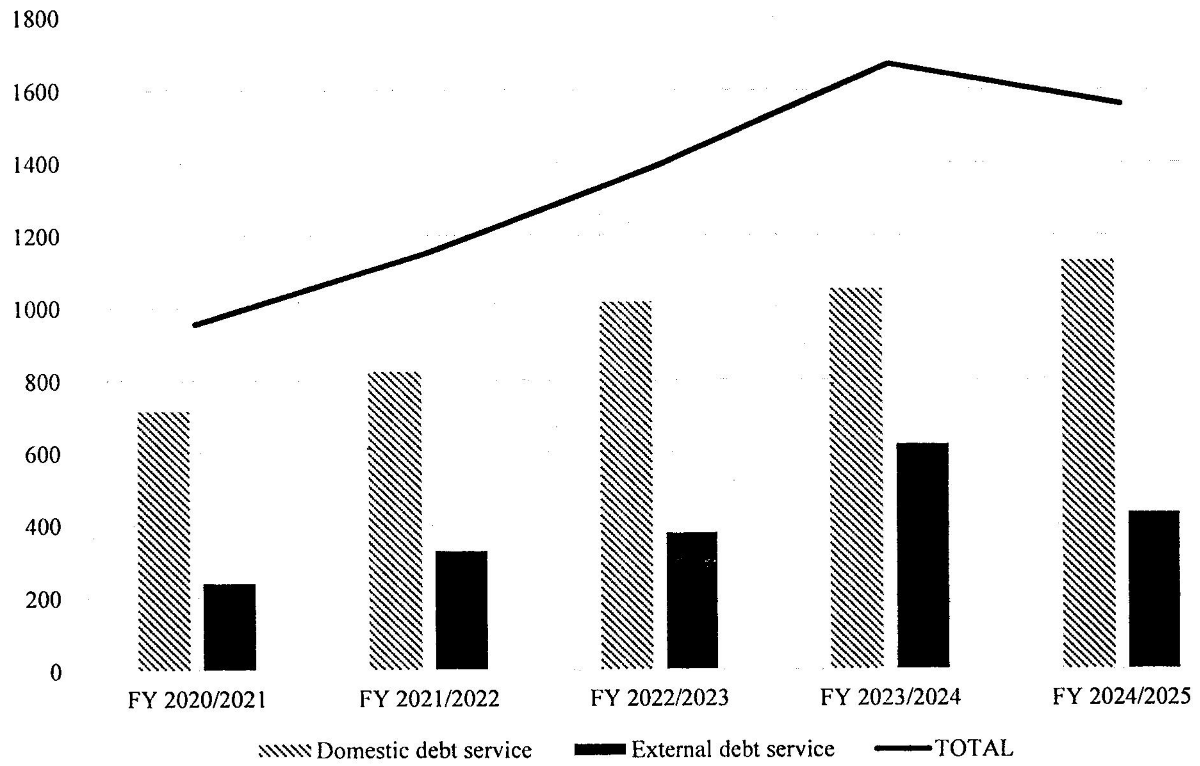
Source: 2021 MTDS

1.1.5 <u>Public Debt Servicing</u>

a) The stock of public debt continues to increase and with it, the increasing level of macroeconomic effort required to maintain debt at sustainable levels. In FY 2022/23, debt servicing expenditures will amount to Kshs 1.39 trillion (a Kshs 241.8 billion or 21% increase from Kshs. 1.15 trillion - FY 2020/21).

b) The growth trend is projected to peak at Kshs 1.67 trillion in FY 2023/24 due to the payment of Kshs 241.75 Billion related to the 2018 International Sovereign Bond (USD 2.0 BN). Despite this, increase in domestic debt servicing expenditures continue to be the main driver of public debt servicing expenditures.

Figure 4: Comparison of Domestic & External Debt Service Expenditures (Ksh. Billions)



Source: FY 2022/23 Budget Estimates

i. ***Domestic Debt Service:*** Figure 4 indicates that at At Kshs. 1.015 trillion (FY 2022/23) domestic debt service expenditures are the largest component of public debt service expenditures, by accounting for 73% of total debt service expenditures. Domestic debt service is largely driven by interest expenditure (Kshs. 553 billion and accounts for 80% of total interest expenses) indicating the high cost of borrowing from the domestic market.

ii. ***External Debt Service****: Figure 4 also indicates that,* external debt service will amount to Kshs. 378.3 billion in FY 2022/23 and account or 27% of total debt servicing expenditures. This low debt service expenditure is on account of the high concessionality qualities of Kenya's external debt (which attract favorable borrowing terms such as longer grace periods and low interest rate) and the positive impact of Debt Service Suspension Initiative (DSSI) provided by critical creditors, low income countries to enable them fight the effects of the Covid-19 pandemic, with the guidance of the World Bank and the International Monetary Fund.

1.1.6 Public Debt Sustainability Analysis

a) Debt sustainability analysis, compares debt burden indicators to thresholds over a 20 -year projection period, if a debt burden indicator exceeds its indicative threshold then it would suggest that a risk of experiencing some form of debt distress exists. The objective of Debt Sustainability Analysis (DSA) is to evaluate a country's capacity to finance its policy agenda, and service the ensuing debt without unduly large adjustments that may compromise its macroeconomic stability and/or that of its economic partners.

The DSA framework consists of two complementary assessments of the sustainability of the following-

i) Total public sector debt DSA and

ii) Total external debt DSA.

b) The overall DSA indicates that Kenya's debt (public & publicly guaranteed debt) totaling to Kshs. 8.2 trillion, is gradually moving towards breaching all the sustainability thresholds, indicating increasing likelihood of debt distress in the future.

Breached thresholds include-

i. PV of Public Debt-to-GDP ratio;

ii. PV of Public debt-revenue and grants ratio;
iii. PV of PPG External Debt-to-Exports ratio; and
iv. PPG debt service-to-exports ratio.

This indicates that both solvency and liquidity sustainability ratios are presumed to be permanently breached and will require concerted effort of fiscal consolidation to bring them back to sustainable levels.

Table 2: Debt Sustainability Analysis

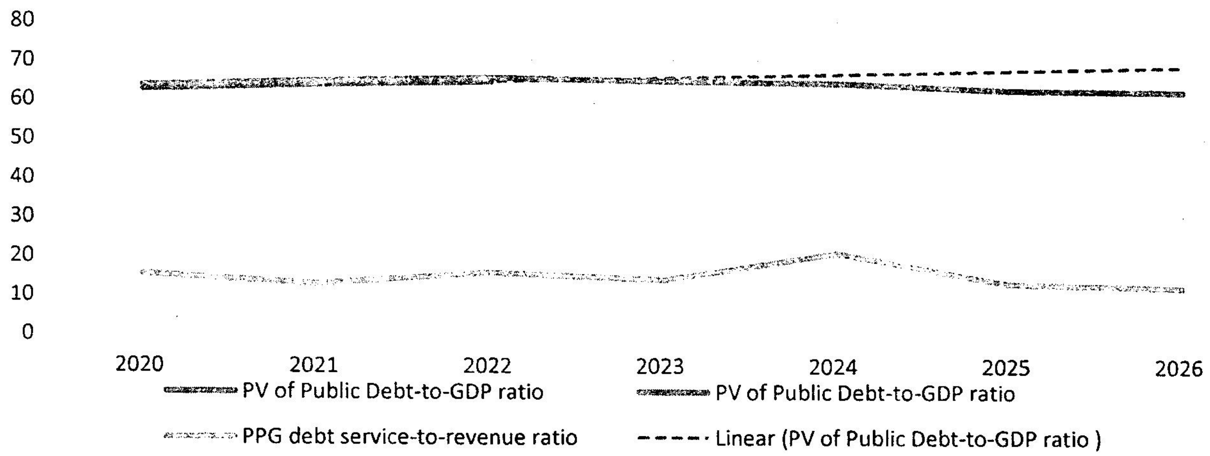
Indicator	**Threshold**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
PV of Public Debt-to-GDP ratio	**55**	**62.7**	**63.9**	**64.6**	**63.8**	**63.3**	**61.5**	**61.1**
PV of Public debt-revenue and grants ratio	**300**	**360**	**372.6**	**370.8**	**348.**	**339.2**	**324.0**	**309.3**
PV of PPG External Debt-to-GDP ratio	**40**	28.7	28.7	28.3	27.3	26.3	25.7	25.2
PV of PPG External Debt-to-Exports ratio	**180**	**288.3**	**255.8**	**239.20**	**219.8**	**204.2**	**193.6**	**188.5**
PPG debt service-to-exports ratio	**15**	**26.5**	**19.1**	**22.70**	**20.1**	**29.7**	**18.4**	**17.1**
PPG debt service-to-revenue ratio	**18**	15.50	13.00	15.80	14.00	**21.00**	13.10	12.10

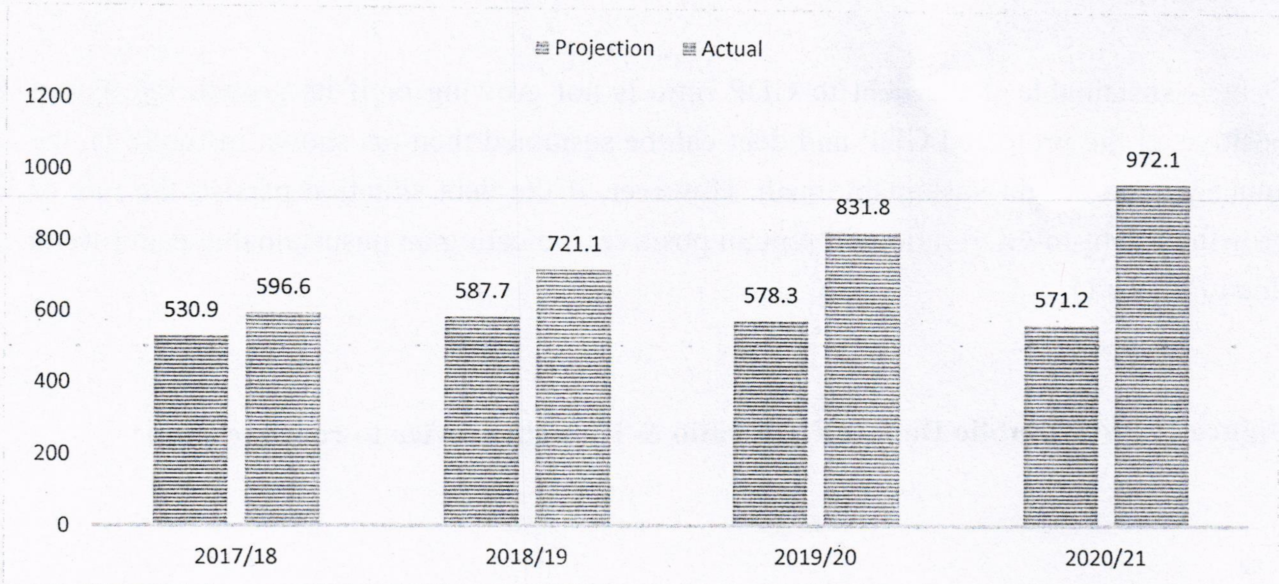
1.1.7 The Debt to GDP Ratio

As shown in table 2,The present value of debt to the Gross domestic product ratio is on average 63.7%. It is projected to increase to 64.6% in 2022 and thereafter decline to 61.1% by 2026. This implies that debt has grown faster than GDP, but the trend is expected to reverse in the medium term, with GDP expanding faster than debt (National Treasury projections). The table also indicates that the present value of public debt to revenue and grants ratio together with the PV of Public and publicly guaranteed external debt to GDP ratio has been breached in comparison to the threshold.

Debt is sustainable if the debt to GDP ratio is not growing or if its growth rate is not positive. If the projected GDP and debt can be sustained then (as shown in figure I), the country is on a debt sustainable path. However, if the debt situation persists,the rate of growth of debt-to-GDP ratio will remain positive, indicating an unsustainable path (trend line in figure 1).

Figure 1: PV of Public Debt to GDP ratio & PV debt service to revenue ratio





The proposed limit of ten trillion represents approximately 80% of the current estimated GDP of twelve trillion. The new limit of ten trillion will be by far off the debt carrying capacity IMF /world bank benchmark of 55% for Kenya(DEC,2021). However, the debt can only be sustainable if the projected GDP can be realized and the deficit declines.

The challenge of having a larger debt limit is that it will give the National Treasury a chance to grow the level of debt at a faster rate leading to a build-up of the debt stock. Huge amount of debt may be at sustainable levels, however in the event of shocks that affect serviceability, it exposes the country to the risk of default.

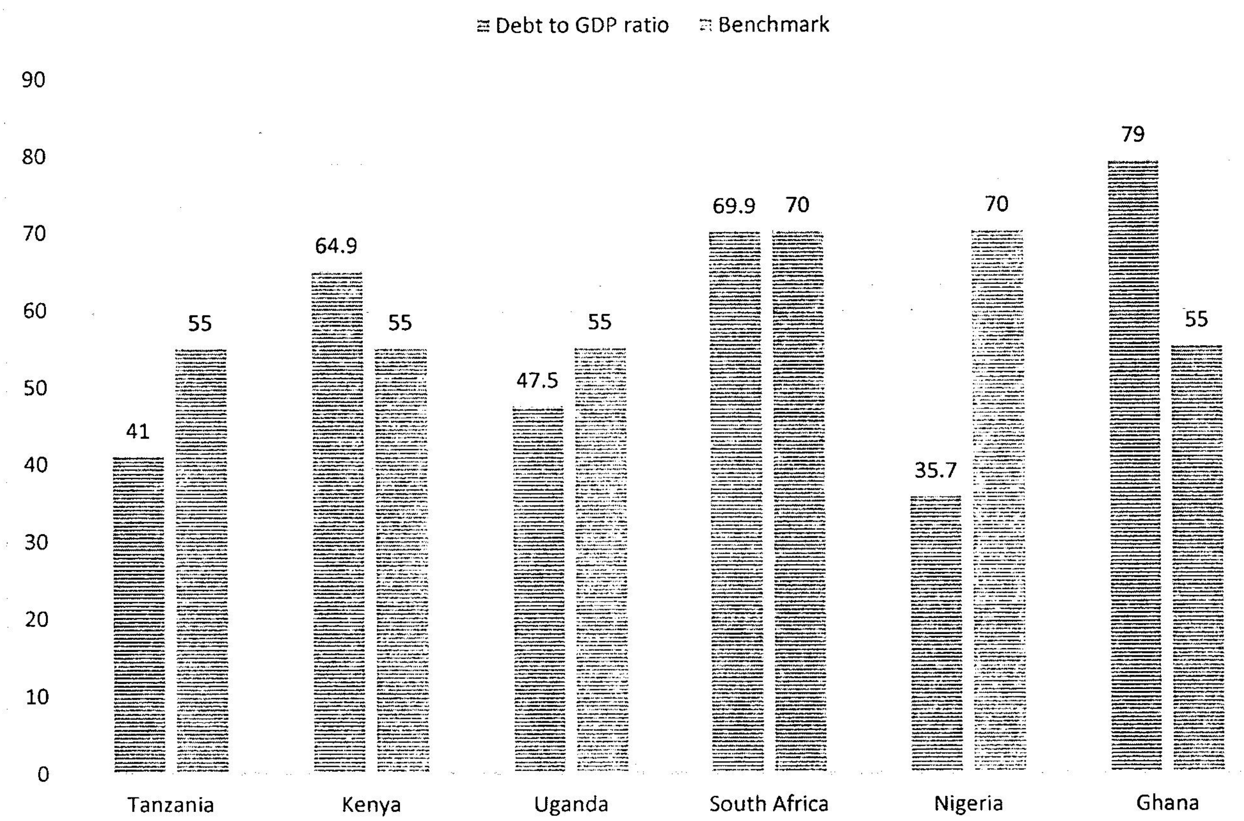
1.1.8 <u>Country Comparison</u>

Figure 2 shows the performance of Kenya in terms of debt to GDP ratio in comparison to other African countries. As indicated Kenya has borrowed highly in comparison to its GDP alongside South Africa and Ghana. The ratios have been compared with the respective debt carrying capacity.

The debt carrying capacity is established to determine the debt threshold that will apply when assessing the extent of risks. Countries are classified using a composite indicator derived from the country specific information.

The debt carrying capacity can be categorized as weak, medium or strong depending on the characteristic of the composite indicator. Each category has a benchmark for the debt to GDP ratio as follows: weak 35%, medium 55% and strong 70%.

Figure 2: Comparison with other selected countries.



CHAPTER TWO

STAKEHOLDERS' ENGAGEMENT

2.0 Consultations with Stakeholders

The Sessional Committee on Delegated Legislation considered written and oral submissions from the following stakeholders:

(1) The Cabinet Secretary for National Treasury and Planning
(2) The Governor, Central Bank of Kenya
(3) The Commission on revenue Allocation
(4) The County Assemblies Forum
(5) The International Budget Partnership
(6) The Institute of Economic Affairs

2.1 COMMENTS BY STAKEHOLDERS

The following is a summary of the submissions from stakeholders on the Regulations:

2.1.1 The Cabinet Secretary, National Treasury and Planning

The Cabinet Secretary Submitted that-

a) As at the end of June 2021, public guaranteed and non-guaranteed debt stood at Kshs.7.7 trillion against a statutory ceiling of Kshs.9 trillion. At the beginning of the FY 2021/22, the available borrowing space was Kshs.1.3 trillion.
b) The projected level of public debt at end of June 2022 is Kshs.8.7 Trillion which is within the legal limit of Kshs. 9 trillion leaving a borrowing space of Ksh.300 billion .This borrowing space continues to shrink due to the strengthening of the US dollar against the Kenya Shilling.
c) The available borrowing space will note be adequate to cover planned borrowing of Ksh.846 billion in FY 2022/23 budget and projected borrowing over the medium term as per the 2022 Budget Policy Statement.
d) Over the last 10 years ,the Government has implemented measures to strengthen overall public debt management

e) The appreciation of the dollar has increased the cost of debt servicing by Ksh.300 billion in 2021/22.

f) There has been efforts meant to ensure public debt sustainability that include; the enactment of the Public Private Partnership Act, 2021 that has enabled the undertaking of development projects outside the budget framework a case in point is the Nairobi Express way. All government projects currently undergo a feasibility study and considered whether they can be undertaken through PPP framework before they are factored in the budget.

g) Further to manage expenditure, the National Treasury is in the process of automating government procurement for all common user items and link it to IFMIS. This will ensure that no procurement is done outside the budget and therefore reducing loss of funds through procurement.

h) The National Treasury also plans to use more of EPC (Engineering, Procurement and Construction Contracts) project financing. The EPC project financing method transfers all the risks associated with design, procurement and construction to the contractor. This type of contracts are efficient and reduce project costs.

i) To reduce the cost of debt, the National Treasury has increased the share of concessional loans to 75% from 65% in 2019 and reduced the share of commercial debt to 25% from 35% in 2019.

j) The Post Covid 19 recovery program supported by the IMF is projected to improve GDP in the medium term and therefore the debt to GDP ratio will begin to decline in the medium term.

k) The National Treasury committed in 2019 that the debt ceiling of 9 trillion will be enough after 2024, However a number of unfavourable events have taken place that have led to the depletion of the ceiling. The events include the Covid 19 pandemic and the Ukraine war.

2.1.2 Submissions from the Governor, Central Bank of Kenya

The Central Bank of Kenya made a written submission generally agreeing with the proposed amendments.

The CBK cites the following reason as to why it supports the proposed amendments to the regulations-

a) Any debt ceiling has to be considered in the context of other applicable measures to contain debt and;
b) A striking balance between debt sustainability and financing investments needs.

2.1.3 Submissions from the Commission on Revenue Allocation

The Commission on Revenue Allocation submitted that the following with regards to the proposed regulations and the general status of public debt in the country:

a) The Commission notes with concern the review of the absolute debt ceilings from its current level of Ksh.9 trillion to Ksh.10 trillion .Given that the Gross Domestic Product is estimated at Ksh.12.4 trillion ,the revised debt ceiling translates to 80.6% of GDP .The commission observes that this is a significant increase.
b) Kenya's economy is rated to have a medium debt -carrying capacity .Global best practice recommends that the public debt is maintained at a level not exceeding 55 per cent of GDP in Present Value Terms. The commission therefore notes that, the debt ceiling at 80.6% exceed the debt carrying capacity for Kenya.
c) The frequent presentation of the debt ceiling in nominal terms will occasion frequent amendments to legislation when, the ceiling is surpassed, the economy expands and has capacity to carry more debt. Frequent amendment of legislation undermines principles of prudent fiscal management and that the ceiling should be set as a percentage of GDP.
d) The country is undergoing a political transition. This transition is likely to come with changes in fiscal and monetary stance. The amendment should therefore be delayed until the change of government.

2.1.4 Submissions from the County Assemblies Forum (CAF)

CAF presented a written submissions and submitted that the Regulations would address the challenges of public debt in the country and enable financing of government priorities.

However CAF has proposed amendments with the following objectives;-

a) The need to provide for a mechanism for the Public Debt Management Office to independently advice parliament and make the advice final with regards to public debt.

b) The proposal to use a nominal figure of Ksh.10 trillion is not the solution to the public debt challenge since the National Treasury will reach the ceiling and still come back for another ceiling.

2.1.5 Submissions from the International Budget Partnership

The International Budget Partnership submitted as follows-

a) The growth of public debt has been significantly high compared to the growth of GDP and this has been driven by an ever increasing budget deficit.

b) The challenge of public debt in the country does not lie in the size of the ceiling but rather it is a governance problem. This has led to increased deficit financing that does not match the language of fiscal consolidation. The borrowed funds are sometimes diverted to recurrent expenditure which has less return on investment.

c) The deficit is growing while incomes are generally reducing and the country needs to budget within its means.

d) A rise of the debt ceiling to Kes 10 trillion in order to allow for deficit financing implies that the debt stock will be over 70% of GDP exceeding the sustainability index of 55%.

e) Debt servicing is taking more and more of revenue and currently stands at 65% of ordinary revenue while revenue projections and actual growth remains erratic while debt repayment is on an upward trend.

2.1.6 Submissions from the Institute of Economic Affairs

The Institute of Economic Affairs Submitted as follows-

a) The debt servicing in the country is competing with the social sector expenditure and has led to relatively reduced expenditure on social services over the years.

b) The borrowed funds may not be viable for projects that have multiplier effects in the economy and some of the borrowed funds may have gone to paying recurrent expenditure.

CHAPTER THREE

COMMITTEE OBSERVATIONS

3.0 Committee Observations

The Committee observed that-

a) The ratio of Debt to GDP ratio is currently increasing which indicates that it may not be sustainable in future, However the National Treasury is optimistic that the Post covid 19 recovery program supported by the IMF will increase the rate of growth of GDP and therefore the ratio of debt to GDP will begin to decline going forward.

b) Economic factors for example, a depreciating shilling and increasing price levels may pose challenges in the sustainability of debt both in the medium term and in the future,however this is majorly caused by external forces and perceived artificial shortages of the dollar.This is projected to stabilize since the country has enough foreign exchange reserves of upto five months import cover.

c) The instability of the Kenya's debt accumulation process is not conducive for investors who prefer a predictable business environment and are scared of sudden fiscal changes to address debt problems.

d) Public debt is serviced out of government revenues of which taxation is a major source of revenues. Recently the country has experienced increased tax rates partly arising from IMF conditions. Growing the debt levels too fast may eventually result to increased taxes in the future.

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h) It is noted that 'the mere fear of non-sustainability, makes non-sustainability a reality'. The National Treasury has to put enough effort to build confidence with regards to public debt management and sustainability in the country.

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k) The deficit in the budget estimates for 2022/23 and the medium term shall not be fully financed and development partners may stop funding ongoing projects if the debt ceiling is not increased.

l) The National Treasury has a number of policies aimed at addressing the macroeconomic pressures caused by increased expenditure demands and promoting fiscal consolidation.

These include;

i. Plans to use more of EPC (Engineering, Procurement and Construction Contracts) project financing. The EPC project financing method transfers all the risks associated with design, procurement and construction to the contractor. This type of contracts are efficient and reduce project costs and also attractive to lenders and thus low borrowing costs.

ii. Efforts to ensure public debt sustainability that include; the enactment of the Public Private Partnership Act, 2021 that has enabled the undertaking of development projects outside the budget framework a case in point is the Nairobi Express way. All government projects currently undergo a feasibility study and considered whether they can be undertaken through PPP framework before they are factored in the budget.

iii. Automation of government procurement for all common user items and link it to IFMIS. The system is currently being developed by the National Treasury and will soon be rolled to Ministries and departments. This will ensure that no procurement is done outside the budget and therefore reducing loss of funds through procurement.

CHAPTER FOUR

COMMITTEE RECOMMENDATION

Based on the foregoing observations and pursuant to Section 205 (4) of the PFM Act, Number 18 of 2012, the Senate Sessional Committee on Delegated Legislation recommends to the Senate that **the Public Finance Management (National Government) (Amendment) Regulations, Legal Notice Number 89 of 2022, be approved.**

ANNEXES

1. The PFM (National Government) (Amendment) Regulations, Legal Notice Number 89 of 2022
2. Submission by the National Treasury and Planning
3. Submission by the Central Bank of Kenya (CBK)
4. Submission by the County Assembles Forum (CAF)
5. Submission by the Commission on Revenue Allocation (CRA)
6. Submission by the International Budget Partnership, Kenya (IBP)
7. Submission by the Institute of Economic Affairs (IEA)

TWELFTH PARLIAMENT |SIXTH SESSION

MINUTES OF THE MEETING OF THE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION HELD ON MONDAY, 13TH JUNE, 2022 ON THE ZOOM ONLINE MEETING PLATFORM AT 11.00 A.M.

PRESENT

1. Sen. Mohamed Mwinyihaji Faki, MP	- **Chairperson *(Chairing)***
2. Sen. Agnes Kavindu Muthama, MP	- Vice Chairperson
3. Sen. Poghisio Samuel Losuron, EGH, MP	- Member
4. Sen. Farhiya Ali Haji, MP	- Member
5. Sen. Judith Pareno, MP	- Member
6. Sen. Mary Yiane Seneta, MP	- Member

ABSENT WITH APOLOGIES

1. Sen. Prof. Samson Ongeri, EGH, MP	- Member
2. Sen. Halake Abshiro, MP	- Member
3. Sen. Anwar Loitiptip, MP	- Member

SECRETARIAT

1. Mr. Boniface Kiambi	- Clerk Assistant - I
2. Ms. Lucy Radoli	- Legal Counsel - I
3. Mr. Jonathan Lemurt	- Fiscal Analyst - 1
4. Ms. Winfred Ocholla	- Audio Officer – III
5. Mr. Patrick Murindo	- Serjeant At Arms- II

MIN. NO. SEN/SCDL/01/032/2022: PRELIMINARIES

The Chairperson called the meeting to order at 11:12 a.m. followed by a word of prayer led by Sen. Mohamed Mwinyihaji Faki, MP.

MIN. NO. SEN/SCDL/ 02/032/2022: ADOPTION OF THE AGENDA

The Committee adopted the Agenda of the Sitting, as set out here below, having been proposed by Sen. Farhiya Ali Haji, MP and seconded by Sen. Mary Seneta, MP : -

AGENDA

1. Prayer.
2. Adoption of the Agenda.
3. Confirmation of the Minutes of Previous Sittings.
4. Report on the Committee Consideration of the Public Finance Management (National Government) (Amendment) Regulations, 2022 (L.N. No. 89 of 2022).
5. Consideration of the Committee Legacy Report for the 12th Parliament.
6. Any Other Business.
7. Adjournment.

MIN. NO. SEN/SCDL/ 03/032/2022: CONFIRMATION OF MINUTES OF THE COMMITTEE MEETING HELD ON FRIDAY, 10TH JUNE, 2022 AT THE HILTON GARDEN INN, MACHAKOS COUNTY AT 9.30 A.M.

The Committee noted that it had held a Consultative Workshop on 10th and 11th June, 2022 in Machakos County, to meet with stakeholders and to deliberate on the Public Finance Management (National Government) (Amendment) Regulations, 2022 (L.N. No. 89 of 2022).

It was observed that during the Workshop, the Committee received and considered written and oral submissions from the following stakeholders:

1. The Cabinet Secretary for National Treasury and Planning
2. The Governor, Central Bank of Kenya
3. The Commission on revenue Allocation
4. The County Assemblies Forum
5. The International Budget Partnership
6. The Institute of Economic Affairs

The Minutes of that Meeting were confirmed as a true record of the deliberations after being proposed by Sen. Farhiya Ali Haji, MP and seconded by Sen. Mary Seneta, MP.

MIN. NO. SEN/SCDL/ 04/032/2022: COMMITTEE REPORT ON ITS CONSIDERATION OF THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMMENDMENT) REGULATIONS, 2022

It was noted that the Committee had recommended to hold a Virtual Sitting on Monday, 13th June, 2022 at 11.00 a.m., to consider its Report upon deliberations on all the submissions made by the stakeholders.

Committee Observations:

Some of the key observations made by the Committee were as follows: -

a) The ratio of Debt to GDP ratio is currently increasing which indicates that it may not be sustainable in future, However the National Treasury is optimistic that the Post Covid 19 recovery program supported by the IMF will increase the rate of growth of GDP and therefore the ratio of debt to GDP will begin to decline going forward.

b) Economic factors for example, a depreciating shilling and increasing price levels may pose challenges in the sustainability of debt both in the medium term and in the future, however this is majorly caused by external forces and perceived artificial shortages of the dollar. This is projected to stabilize since the country has enough foreign exchange reserves of up to five months import cover.

c) The instability of the Kenya's debt accumulation process is not conducive for investors who prefer a predictable business environment and are scared of sudden fiscal changes to address debt problems.

d) Public debt is serviced out of government revenues of which taxation is a major source of revenues. Recently the country has experienced increased tax rates partly arising from IMF conditions. Growing the debt levels too fast may eventually result to increased taxes in the future.

e) The National Treasury has been slow in shifting to a higher ratio of cheap concessional debt in comparison to expensive commercial debt.

f) A high debt ceiling may give the National Treasury leeway to increase debt at a fast rate leading to huge debts in the future and the challenge of high levels of debt is the increase in vulnerabilities in the event of shocks similar to Covid 19.

g) The realized deficit has always been higher than the projected deficit and thus the deficit may continue to increase other than decline. The size of the deficit is driving the growth of public debt despite the fact that parliament has the power to determine sustainable deficit levels.

The Committee further observed that:

h) The National Treasury has to put enough effort to build confidence with regards to public debt management and sustainability in the country. It was noted that 'the mere fear of non-sustainability, makes non-sustainability a reality'.

i) The new limit of ten trillion will be beyond the debt carrying capacity IMF /world bank benchmark of 55% for Kenya(DEC,2021) however due to the post covid 19 recovery programs supported by the IMF the debt to GDP ratio is expected to decline towards the debt carrying capacity level in the medium term.

j) The National Treasury committed in 2019 that the debt ceiling of 9 trillion will be enough after 2024 ,however a number of unfavourable events have taken place that have led to the depletion of the ceiling. The events include the Covid 19 pandemic and the Ukraine war and the resultant appreciation of the dollar.

k) The deficit in the budget estimates for 2022/23 and the medium term shall not be fully financed and development partners may stop funding ongoing projects if the debt ceiling is not increased.

l) The National Treasury has a number of policies aimed at addressing the macroeconomic pressures caused by increased expenditure demands and promoting fiscal consolidation. These include;

i. Plans to use more of EPC (Engineering, Procurement and Construction Contracts) project financing. The EPC project financing method transfers all the risks associated with design, procurement and construction to the contractor. This type of contracts are efficient and reduce project costs and also attractive to lenders and thus low borrowing costs.

ii. Efforts to ensure public debt sustainability that include; the enactment of the Public Private Partnership Act, 2021 that has enabled the undertaking of development projects outside the budget framework a case in point is the Nairobi Express way. All government projects currently undergo a feasibility study and considered whether they can be undertaken through PPP framework before they are factored in the budget.

iii. Automation of government procurement for all common user items and link it to IFMIS.The system is currently being developed by the National Treasury and will soon be rolled to Ministries and departments. This will ensure that no procurement is done outside the budget and therefore

COMMITTEE RECOMMENDATION

Based on the foregoing observations, the Senate Sessional Committee on Delegated Legislation recommends to the Senate that the Public Finance Management (National Government) (Ammendment) Regulations, 2022, be approved.

MIN. NO. SEN/SCDL/ 05/032/2022: COMMITTEE LEGACY REPORT FOR THE 12TH PARLIAMENT

The Committee considered and approved the Committee Legacy Report for the 12th Parliament for tabling before the Senate.

MIN. NO. SEN/SCDL/ 06/032/2022: ADJOURNMENT

Having concluded the business as set out in the agenda, the meeting was adjourned at 12.10 p.m. The next meeting was to be set on notice.

SIGNED: .... **DATE: 13TH JUNE, 2022**

SEN. MOHAMED MWINYIHAJI FAKI, MP
CHAIRPERSON,
SESSIONAL COMMITTEE ON DELEGATED LEGISLATION

TWELFTH PARLIAMENT |SIXTH SESSION

MINUTES OF THE MEETING OF THE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION HELD ON FRIDAY, 10TH JUNE, 2022 AT THE HILTON GARDEN INN, MACHAKOS COUNTY AT 9.30 A.M.

PRESENT

1. Sen. Mohamed Mwinyihaji Faki, MP	- **Chairperson *(Chairing)***
2. Sen. Agnes Kavindu Muthama, MP	- Vice Chairperson
3. Sen. Poghisio Samuel Losuron, EGH, MP	- Member
4. Sen. Farhiya Ali Haji, MP	- Member
5. Sen. Judith Pareno, MP	- Member
6. Sen. Mary Yiane Seneta, MP	- Member

ABSENT WITH APOLOGIES

1. Sen. Prof. Samson Ongeri, EGH, MP	- Member
2. Sen. Halake Abshiro, MP	- Member
3. Sen. Anwar Loitiptip, MP	- Member

SECRETARIAT

1. Mr. Boniface Kiambi	- Clerk Assistant - I
2. Ms. Lucy Radoli	- Legal Counsel - I
3. Mr. Jonathan Lemurt	- Fiscal Analyst - 1
4. Ms. Winfred Ocholla	- Audio Officer – III
5. Mr. Patrick Murindo	- Serjeant At Arms- II

IN ATTENDANCE

1. Dr. Julius Muia, CBS	-Principal Secretary, National Treasury and Planning
2. Dr. Haron Sirma	-Director General, Public Debt Management Office, National Treasury and Planning
3. Mr. Livingstone Bumbe	-Deputy Director, Public Debt Management Office, National Treasury and Planning
4. Mr. Humprey Okusimba	-Public Debt Management Office, National

	Treasury and Planning
5. Mr. Alex Suiji	-Parliamentary Liason Office, National Treasury and Planning
6. Dr. Abraham Rugo	-Country Manager, International Budget Partnership
7. Mr. John Mutua	-Programme Coordinator, Institute for Economic Affairs

MIN. NO. SEN/SCDL/01/031/2022: PRELIMINARIES

The Chairperson called the meeting to order at 9:48 a.m. followed by a word of prayer led by Sen. Mohamed Mwinyihaji Faki, MP.

MIN. NO. SEN/SCDL/ 02/031/2022: ADOPTION OF THE AGENDA

The Committee adopted the Agenda of the Sitting, as set out below, having been proposed by Sen. Farhiya Ali Haji, MP and seconded by Sen. Mary Seneta, MP : -

1. Prayer.
2. Adoption of the Agenda.
3. Consideration of the Public Finance Management (National Government) (Ammendment) Regulations, 2022 and Stakeholder Submissions.
4. Consideration of Legislative Business Pending Before the Committee.
5. Any Other Business.
6. Adjournment.

MIN. NO. SEN/SCDL/ 03/031/2022: CONSIDERATION OF THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMMENDMENT) REGULATIONS, 2022 – STAKEHOLDER ENGAGEMENTS

The Public Finance Management (National Government) (Amendment) Regulations, Legal Notice Number 89 of 2022 were tabled in the Senate on 7th June, 2022 and committed to the Sessional Committee on Delegated Legislation for scrutiny.

The Committee thereafter resolved to hold a Consultative Workshop on 10th and 11th June, 2022 in Machakos County, to meet with stakeholders and to deliberate on the Regulations.

During the Workshop, the Committee received and considered written and oral submissions from the following stakeholders:

1. The Cabinet Secretary for National Treasury and Planning
2. The Governor, Central Bank of Kenya

3. The Commission on revenue Allocation
4. The County Assemblies Forum
5. The International Budget Partnership
6. The Institute of Economic Affairs

The following is a summary of the submissions from the stakeholders on the Regulations:

<u>The Cabinet Secretary, National Treasury and Planning</u>

The Cabinet Secretary, National Treasury and Planning Submitted that:

a) As at the end of June 2021, public guaranteed and non-guaranteed debt stood at Kshs.7.7 trillion against a statutory ceiling of Kshs.9 trillion. At the beginning of the FY 2021/22, the available borrowing space was Kshs.1.3 trillion.
b) The projected level of public debt at end of June 2022 is Kshs.8.7 Trillion which is within the legal limit of Kshs. 9 trillion leaving a borrowing space of Ksh.300 billion .This borrowing space continues to shrink due to the strengthening of the US dollar against the Kenya Shilling.

c) The available borrowing space will note be adequate to cover planned borrowing of Ksh.846 billion in FY 2022/23 budget and projected borrowing over the medium term as per the 2022 Budget Policy Statement.

d) Over the last 10 years, the Government has implemented measures to strengthen overall public debt management.

e) The appreciation of the dollar has increased the cost of debt servicing by Ksh.300 billion in 2021/22.

f) There has been efforts meant to ensure public debt sustainability that include; the enactment of the Public Private Partnership Act, 2021 that has enabled the undertaking of development projects outside the budget framework a case in point is the Nairobi Express way. All government projects currently undergo a feasibility study and considered whether they can be undertaken through PPP framework before they are factored in the budget.

g) Further to manage expenditure, the National Treasury is in the process of automating government procurement for all common user items and link it to IFMIS. This will ensure that no procurement is done outside the budget and therefore reducing loss of funds through procurement.

h) The National Treasury also plans to use more of EPC (Engineering, Procurement and Construction Contracts) project financing. The EPC project financing method transfers all the risks associated with design, procurement and construction to the contractor. This type of contracts are efficient and reduce project costs.

i) To reduce the cost of debt, the National Treasury has increased the share of concessional loans to 75% from 65% in 2019 and reduced the share of commercial debt to 25% from 35% in 2019.

j) The Post Covid 19 recovery program supported by the IMF is projected to improve GDP in the medium term and therefore the debt to GDP ratio will begin to decline in the medium term.

k) The National Treasury committed in 2019 that the debt ceiling of 9 trillion will be enough after 2024, However a number of unfavourable events have taken place that have led to the depletion of the ceiling. The events include the Covid 19 pandemic and the Ukraine war.

Submissions from the Governor, Central Bank of Kenya

The Central Bank of Kenya made a written submission generally agreeing with the proposed amendments.

The CBK cites the following reason as to why it supports the proposed amendments to the regulations:

a) Any debt ceiling has to be considered in the context of other applicable measures to contain debt and;

b) A striking balance between debt sustainability and financing investments needs.

Submissions from the Commission on Revenue Allocation

The Commission on Revenue Allocation submitted that the following with regards to the proposed regulations and the general status of public debt in the country:

a) The Commission notes with concern the review of the absolute debt ceilings from its current level of Ksh.9 trillion to Ksh.10 trillion .Given that the Gross Domestic Product is estimated at Ksh.12.4 trillion ,the revised debt ceiling translates to 80.6% of GDP .The commission observes that this is a significant increase.

b) Kenya's economy is rated to have a medium debt -carrying capacity .Global best practice recommends that the public debt is maintained at a level not exceeding 55 per cent of GDP in present Value terms. The commission therefore notes that,the debt ceiling at 80.6% exceed the debt carrying capacity for Kenya.

c) The frequent presentation of the debt ceiling in nominal terms will occasion frequent amendments to legislation when, the ceiling is surpassed, the economy expands and has capacity to carry more debt. Frequent amendment of legislation undermines principles of prudent fiscal management and that the ceiling should be set as a percentage of GDP.

d) The country is undergoing a political transition. This transition is likely to come with changes in fiscal and monetary stance. The amendment should therefore be delayed until the change of government.

Submissions from the County Assemblies Forum (CAF)

The County Assemblies Forum (CAF) presented a written submissions and noted that the Regulations would address the challenges of public debt in the country and enable financing of government priorities.

.However, CAF proposed amendments with the following objectives;-

a) The need to provide for a mechanism for the Public Debt Management Office to independently advice parliament and make the advice final with regards to public debt.

b) The proposal to use a nominal figure of Ksh.10 trillion is not the solution to the public debt challenge since the National Treasury will reach the ceiling and still come back for another ceiling.

Submissions from the International Budget Partnership

The International Budget Partnership submitted as follows:

a) The growth of public debt has been significantly high compared to the growth of GDP and this has been driven by an ever increasing budget deficit.

b) The challenge of public debt in the country does not lie in the size of the ceiling but rather it is a governance problem. This has led to increased deficit financing that does not match the language of fiscal consolidation. The borrowed funds are sometimes diverted to recurrent expenditure which has less return on investment.

c) The deficit is growing while incomes are generally reducing and the country needs to budget within its means.

d) A rise of the debt ceiling to Kes 10 trillion in order to allow for deficit financing implies that the debt stock will be over 70% of GDP exceeding the sustainability index of 55%.

c) Debt servicing is taking more and more of revenue and currently stands at 65% of ordinary revenue while revenue projections and actual growth remains erratic while debt repayment is on an upward trend.

Submissions from the Institute of Economic Affairs

The Institute of Economic Affairs Submitted as follows;

a) The debt servicing in the country is competing with the social sector expenditure and has led to relatively reduced expenditure on social services over the years.

b) The borrowed funds may not be viable for projects that have multiplier effects in the economy and some of the borrowed funds may have gone to paying recurrent expenditure.

COMMITTEE RECOMMENDATION

The Committee recommended to hold a Virtual Sitting on Monday, 13th June, 2022 at 11.00 a.m., to consider its Report upon deliberations on all the submissions made by the stakeholders.

MIN. NO. SEN/SCDL/ 04/031/2022: CONSIDERATION OF LEGISLATIVE BUSINESS PENDING BEFORE THE COMMITTEE

The Committee considered its Report on the following Statutory Instruments that were published by the Ministry of Lands and Physical Planning:

1. The Physical and Land Use Planning (Institutions) Regulations, 2021 (L.N. No .238 of 2021);
2. The Physical and Land Use Planning (Building) Regulations, 2021 (L.N. No. 239 of 2021);
3. The Physical and Land Use Planning (County Physical and Land Use Development Plan) Regulations, 2021 (L.N. No.240 of 2021);
4. The Physical and Land Use Planning (National Physical and Land Use Development Plan) Regulations, 2021 (L.N. No.241 of 2021);
5. The Physical and Land Use Planning (Advertisement) Regulations, 2021 (L.N. No. 242 of 2021);
6. The Physical and Land Use Planning (Planning Fees) Regulations, 2021 (L.N. No. 243 of 2021);
7. The Physical and Land Use Planning (Inter County Physical and Land Use Development Plan) Regulations, 2021 (L.N. No. 244 of 2021);
8. The Physical and Land Use Planning (Development Control for Inter County Projects) Regulations, 2021 (L.N. No .245 of 2021);

9. The Physical and Land Use Planning (Development Control for Strategic National Projects) Regulations, 2021 (L.N. No. 246 of 2021);
10. The Physical and Land Use Planning (Development Control Around Strategic Installations) Regulations, 2021 (L.N. No. 247 of 2021);
11. The Physical and Land Use Planning (Local and Physical Development Plan) Regulations, 2021 (L.N. No. 248 of 2021);
12. The Physical and Land Use Planning (Special Planning Area) Regulations, 2021 (L.N. No. 249 of 2021);
13. The Physical and Land Use Planning (Liaison Committees) Regulations, 2021 (L.N. No. 250 of 2021);
14. The Physical and Land Use Planning (Development Central Enforcement) Regulations, 2021 (L.N. No. 251 of 2021);
15. The Physical and Land Use Planning (Outsourcing of Professional Services) Regulations, 2021 (L.N. No. 252 of 2021); and
16. The Physical and Land Use Planning (Development Permission and Control) (General) Regulations, 2021 (L.N. No. 253 of 2021).

COMMITTEE RESOLUTION

After scrutiny of the Regulations and upon deliberations on the submissions made by the stakeholders, the Committee resolved that the Statutory Instruments by the Ministry of Lands and Physical Planning, Legal Notices Number 238 to 253 of 2021, be acceded to.

MIN. NO. SEN/SCDL/ 05/031/2022: ADJOURNMENT

Having concluded the business as set out in the agenda, the meeting was adjourned at 4.20 p.m. The next meeting was scheduled for Monday, 13th June, 2022 at 11.00 a.m.

SIGNED: .... **DATE: 13TH JUNE, 2022**

SEN. MOHAMED MWINYIHAJI FAKI, MP

CHAIRPERSON,
SESSIONAL COMMITTEE ON DELEGATED LEGISLATION

LEGAL NOTICE NO. 89

THE PUBLIC FINANCE MANAGEMENT ACT

(No. 18 of 2012)

IN EXERCISE of the powers conferred by section 205 of the Public Finance Management Act, 2012, the Cabinet Secretary for the National Treasury and Planning makes the following Regulations—

THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, 2022

1. These Regulations may be cited as the Public Finance Management (National Government) (Amendment) Regulations, 2022. Citation.

2. Regulation 26 of the Public Finance Management (National Government) Regulations, 2015, is amended in subregulation (1) by deleting paragraph (c) and substituting therefor the following new paragraph— L.N. No. 34/2015.

(c) pursuant to the provision of section 50 (2) of the Act, the public debt shall not exceed ten trillion shillings.

Made on the 26th May, 2022.

UKUR YATANI,
Cabinet Secretary for the National Treasury and Planning.

PRINTED AND PUBLISHED BY THE GOVERNMENT PRINTER, NAIROBI

Opening remarks by the Cabinet Secretary, National Treasury & Planning, during Consultative workshop with the Senate Sessional Committee on Delegated Legislation to consider the Public Finance Management (National Government) (Amendment) Regulations, 2022.

Friday, 10th June, 2022

Honourable Chairman of the Sessional Committee on Delegated Legislation,

Hon. Members,

Ladies and Gentlemen:

Good morning,

1. **On 26th May 2022**, tThe National Treasury and Planning had pre- published a legal notice to amend the Public Finance Management (National Government) (Amendment) Regulations, 2019 to **amend the public debt ceiling**.

2. As at **end June 2021 public guaranteed and non-guaranteed debt stood at Kshs 7.7 trillion** against a statutory ceiling of Kshs 9 trillion. At the beginning of the FY 2021/22, the **available borrowing space** was **Kshs 1.3 trillion.**

3. The **projected level of public debt at end June 2022 is Kshs 8.7 trillion** which is within the legal limit of Kshs 9 trillion leaving a borrowing space of Kshs. 300 billion. **This borrowing space continues to shrink due to the strengthening of the US dollar against the Kenya shilling.**

4. The available **borrowing space will not be adequate to cover planned borrowing of Kshs 846 billion in FY 2022/3 budget** and projected borrowing over the medium term as per the 2022 *Budget Policy Statement.*

5. **Honourable Chairman**: The National Treasury had initially sought to amend the Regulations to move away from a nominal debt limit to a ***target debt level*** *of 55% of debt to GDP ratio in Present Value terms.* **This debt target is consistent with debt sustainability level for Kenya.**

6. In addition, ***we had proposed*** that the Cabinet Secretary National Treasury will be required to report to Parliament on **time-bound measures to restore public debt level whenever it rises beyond the set limit.** The reporting requirement seeks to enhance **debt transparency and accountability** in line with the Constitution of Kenya.

7. The National Treasury **carried out public participation and received comments from the general public on the proposed amendments of the Regulations.**

8. **Upon further consultations**, and **after reviewing comments received**, the National Treasury now proposes **amendment of the PFM Regulations to raise public debt limit** from **Kshs 9 trillion to Kshs 10 trillion** to facilitate financing of the FY 2022/3 Budget.

9. The **Legal Notice amending the PFM Regulations was submitted to Parliament** on Friday, 27th May 2022 for consideration and approval.

10. **Hon Chairman:** All the relevant documentations on the proposal to amend the PFM Regulations are submitted herewith for consideration and approval by Senate.

11. **In conclusion, Hon Chairman:**

Over the last 10 years, the Government has implemented measured to strengthen overall public debt management. I want to assure you that public debt remains within sustainable levels.

Honourable Chairman, I beg to move.

Thank you.

HON. (AMB.) UKUR K. YATANI, EGH

CABINET SECRETARY/NATIONAL TREASURY AND PLANNING

Friday, 10th June, 2022

Governor

BANKI KUU YA KENYA

CENTRAL BANK OF KENYA

Haile Selassie Avenue
P.O. Box 60000 - 00200 Nairobi, Kenya
Telephone: +254 20 286 1003

June 10, 2022

Mr. Jeremiah M. Nyegenye, CBS
Clerk of the Senate
Clerk's Chambers
Parliament Buildings
P.O. Box 41842-00100
NAIROBI

Dear Mr Nyegenye,

CONSULTATIVE WORKSHOP OF THE SENATE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION TO CONSIDER THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, LEGAL NOTICE NUMBER 89 OF 2022

Thank you for your letter dated June 8, 2022, inviting me to attend the Consultative Workshop by the Sessional Committee on Delegated Legislation scheduled for 10th and 11th June, 2022 in Machakos, to discuss the Public Finance Management (National Government) (Amendment) Regulations, Legal Notice Number 89 of 2022. Due to the short notice however, I am not able to honour the invite but do wish to share my views below.

We note that Legal Notice No. 89 proposes amendment of Regulation 26 of the Public Finance Management (National Government) Regulations, 2015, to provide that the public debt shall not exceed ten trillion Shillings.

As indicated in our earlier letter of May 24, 2022 (attached), we support the direction of the proposed changes by the National Treasury, including Legal Notice No. 89 of 2022. We reiterate though that any debt ceiling has to be considered in the context of other applicable measures to contain debt, and striking a balance between debt sustainability and financing investment needs.

Sincerely,

Patrick Njoroge

Dr. Patrick Njoroge

Attachment

Tel: 254 (20) 4298000
Email: info@crakenya.org
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Grosvenor Block,
2nd & 3rd Floor
P.O. Box 1310 – 00200
NAIROBI

COMMISSION ON REVENUE ALLOCATION

OUR REF: CRA/14/VOL.6(25)

DATE: 10th June 2022

Mr. Jeremiah M. Nyegenye CBS
Clerk of the Senate
Parliament Buildings
2nd Floor, County House
NAIROBI.

Dear Mr. Nyegenye

RE: CONSULTATIVE WORKSHOP ON THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDEMNET) REGULATIONS, LEGAL NOTICE NUMBER 89 OF 2022

Reference is made to your letter dated June 8th, 2022 on the above captioned matter and your invitation to attend the workshop. Detailed below are our views on the proposed amendment to the Public Finance Management (National Government) (Amendment) Regulations for the Committee's consideration:

1. The Commission notes with concern the review of the absolute debt ceiling from its current level of Ksh. 9 trillion to Ksh.10 trillion. Given that our Gross Domestic Product (GDP) is estimated at Ksh 12.4 trillion; the revised debt ceiling translates to 80.6 percent of GDP significant increase from the current debt level of 69.4 percent of GDP. It is the view of the commission that this is a significant increase.

2. Kenya's economy is rated to have a medium debt- carrying capacity. Global best practice recommends that the public debt is maintained at a level not exceeding 55 percent of GDP in Present Value terms. In this regard the commission notes that the revised debt ceiling at 80.6 % of GDP exceeds the recommended level for an economy the size of Kenya and that it is also at variance with the East African community (EAC) commitment of 50 percent.

3. The continued presentation of the debt ceiling in nominal terms will occasion frequent amendments to legislation when (i) the ceiling is surpassed and (ii) when the economy expands and has a capacity to carry more debt. Frequent amendment of legislation undermines principles of prudent fiscal management. In this regard,

it is the view of the commission that the ceiling should be set as a percentage of the country's GDP an approach which takes into consideration the country's debt-carrying capacity in line with the best practice world over. A debt to GDP anchor will eliminate the need for frequent legislation amendments

4. The country is undergoing a political transition. This transition is likely to come with changes in both fiscal and monetary stance. It is the view of the commission that a delay in this amendment would give the incoming administration an opportunity to reviews and harmonize with their macro -fiscal stance.

5. The Commission submits that any review done to the ceiling on the public debt be considered as a percentage of the country's GDP and not in nominal terms.

Yours sincerely

Dr. Jane Kiringai
CHAIRPERSON

Governor

BANKI KUU YA KENYA

CENTRAL BANK OF KENYA

Haile Selassie Avenue
P.O. Box 60000 - 00200 Nairobi, Kenya
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May 24, 2022

Mr. Jeremiah M. Nyegenye, CBS
Clerk of the Senate
Clerk's Chambers
Parliament Buildings
P.O. Box 41842-00100
NAIROBI

Dear Mr Nyegenye,

RE: SEN/SCDL/CORR/ 2022/042: CONSULTATIVE WORKSHOP OF THE SENATE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION TO CONSIDER THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, 2022 AND THE PUBLIC FINANCE MANAGEMENT (COUNTY GOVERNMENTS) (AMENDMENT) REGULATIONS, 2022

I refer to your letter dated May 16, 2022, on the above captioned matter, and your invitation to attend the consultative Workshop of the *Senate Sessional Committee on Delegated Legislation* to deliberate on the proposed amendments to the Public Finance Management Act and the Regulations. Unfortunately, I cannot appear in person before the committee as requested, due to prior commitments in my schedule. However, I detail below our views, for the Committee's consideration.

At the outset, we support the direction of the proposed changes and note the following:

1. Regulation 26(1) of The *Public Finance Management (National Government) (Amendment) Regulations*, proposes that *"The Cabinet Secretary shall at all times use his best endeavours to maintain the public debt at a level not exceeding 55 percent of Gross Domestic Product in Present Value terms."*

   The proposal represents a shift from a public debt ceiling in nominal terms to a ceiling that is expressed as a ratio of GDP. The objective of any debt ceiling is to enhance fiscal discipline and avoid unsustainable debt. Setting the debt ceiling as a ratio of GDP as proposed links the public debt ceiling to the size of the economy, aligning it to the country's debt-carrying capacity. This conforms to the practice in several other emerging economies. Linking the debt ceiling to the size of the economy allows borrowing for investment in projects that would unlock the economy's growth potential, to the extent that these investments increase the economy's output (GDP).

2. The proposal of a debt ceiling of 55 percent of GDP in Present Value terms brings us closer to alignment with our East African Community (EAC) commitments. The EAC convergence criteria for public debt is set at 50 percent of GDP in Present Value terms. Thus, setting our debt ceiling as a ratio of GDP is welcome, but full alignment will require a lowering of the target in the future.

3. We also support the provisions in the proposed Section 50(2A) of the PFM (Amendment) Act and PFM (National Government) (Amendment) Regulations 26(1)(c), which include a submission for the Cabinet Secretary to report to Parliament as and when the debt ceiling is breached due to fiscal disruptions which include war, health pandemic or natural disasters.

Finally, any debt ceiling has to be considered in the context of other applicable measures to contain debt, and striking a balance between debt sustainability and financing investment needs. In this context, we see the proposed debt ceiling operating in tandem with the other provisions in the PFM Act and Regulations.

With the foregoing in mind, the Central Bank of Kenya supports the proposed amendments.

Sincerely,

Patrick Njoroge

Dr. Patrick Njoroge

REPUBLIC OF KENYA

COUNTY ASSEMBLIES FORUM (CAF)

Flamingo Towers, 5th Floor Wing B, Mara Road, Upper Hill P.o Box 73552- 00200 Nairobi Kenya Tel: 0701 046 933

CAF MEMORANDUM ON

THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, 2022

TO: Mr. Jeremiah Nyegenye, CBS
Clerk of the Senate, Parliament of Kenya.
The Standing Committee on scrutiny of delegated legislation.

FROM: The County Assemblies Forum.

DATE: 9th June 2022.

SUBJECT: CAF Memorandum on the Public Finance Management (National Government) (Amendment) Regulations,2022

REPUBLIC OF KENYA

COUNTY ASSEMBLIES FORUM (CAF)

1.0. INTRODUCTION

1.1. The County Assemblies Forum (CAF) is the coordinating body of the 47 County Assemblies in Kenya. The primary mandate of CAF is to promote networking and synergy among the 47 County Assemblies, coordinate intergovernmental relations and enhance good practice in legislative development. Our Mission is to provide effective leadership and coordination of the 47 County Assemblies and through policy and legislative action, promote a conducive working environment for all its members, and in that way deliver quality services to the people.

1.2. As one of the pillars of the devolved government system CAF is committed to engage in processes that strengthen the Public Finance Management Framework of our Country both at National and County level.

2.0. BACKGROUND

2.1. The PFM (National Government) (Amendment) Regulations 2015 are amended to conform with international best practice in setting debt limits (setting debt limits on basis of payment capacity (GDP) as guided in the IMF public sector statistics. Further to this, there are circumstances under which debt limit may be exceeded such as depreciation of the shillings significant balance of payment imbalances or abrupt fiscal disruptions and therefore there is need to address such eventualities in law.

2.2. The proposed Amendment concerns county governments in terms of Article 110(1)(a) of the Constitution as it contains provisions providing amendments to Public Debt Management framework which will affect Counties at an economic level.

3.0. GENERAL COMMENTS.

3.1. CAF understand the importance of this Amendments as the Country needs robust mechanism to regulate public debts and county debts

3.2. This new proposal for the National Treasury is worrying considering the treasury had submitted yet another approach which would have seen the debt ceiling switch from the current limit of Ksh.9 trillion to a moving figure equivalent to 55 per cent of GDP and present value (PV) terms. Estimates documented in the 2022 Budget Policy Statement (BPS) shows Kenya's debt stock will have surpassed the Ksh.10 trillion mark by June of 2024 with the stock of debt estimated at Ksh.10.1 trillion at the end of the 2023/24 fiscal year.

3.3. In light of the above, its evident The National Treasury may again need to adjust the ceiling, probably as early as next year, to accommodate more borrowing without addressing the real challenge, which is sustainability of debt. International standards require that the public debt be limited to ability to repay it by measuring the stock of loans against the size of an economy. Typically, middle-income economies should not borrow more than 55 per cent of their gross domestic product (GDP) lest they be sucked into a debt crisis.

3.4. Cognizance that the removal of the debt ceiling is not a new thing, having been applied by the Treasury until 2014, when the Public Finance Management Act 2015 came into force, then shifting to debt as a measure of GDP. The removal led to fiscal indiscipline as the Treasury went on a borrowing spree with the justification that the economy was growing and could accommodate more debt. The cap was re-introduced in 2019, at Sh9 trillion, but even that has not stopped the country from borrowing more and shifting the ceiling.

3.5. We implore the Senate standing committee on scrutiny of delegated legislation to request the National Treasury to address the real problem of unsustainable debt. The treasury needs to be kept in check if we are to avoid a debt crisis

3.6. CAF appreciates the opportunity to contribute to this Bill and on the basis of the foregoing proposes the following amendments:

4.0 SUMMARY MATRIX OF THE PROPOSED AMENDMENTS

THE PROPOSED AMENDMENTS TO CAF MEMORANDUM ON THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDEMENT) REGULATIONS			
NO.	Section	Proposed Amendments	Justification
1.	**Clause 2 of the bill** **Regulation 26 (1) (c)** **2.** Regulation 26 of the Public Finance Management (National Government) Regulations, 2015, is amended in sub regulation (1) by deleting paragraph (c) and substituting therefor the following new paragraph—	Kindly delete and the principal regulations remain as they were.	The provision will enable the National Treasury to exceed the Public Debt Limit as stated. The Forum is concerned with this provision taking into account that the country has not been meeting its debt sustainability indicators. The Forum is categorical that it does not support the regulations as it contrary to international standards on Public Debt Management and the approval of this regulations may jeopardise the economic

	(c) pursuant to the provision of section 50 (2) of the Act, the public debt shall not exceed ten trillion shillings."		stability of the Country as seen in countries such as Sri-Lanka and Pakistan.

Yours sincerely,

JUDY ODUMA WANGALWA
CHIEF EXECUTIVE OFFICER

International Budget Partnership Kenya

SUBMISSION BY THE INTERNATIONAL BUDGET PARTNERSHIP KENYA TO THE SENATE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION

This memorandum has been prepared by the International Budget Partnership Kenya (IBP Kenya) on the Public Finance Management (National Government) (Amendment) Regulations, Legal Notice 89 of 2022 that are under consideration by the Senate. IBP Kenya is a non-profit organization working to advance transparency, accountability, participation, and equity in national and county budgeting processes. IBP Kenya's work is focused on strengthening the impact of citizens and civil society organizations (CSOs) advocacy on budget policies and outcomes at national and sub-national levels of governance. Citizen advocacy, evidence generation, technical assistance to both levels of governments and CSOs, learning, and networking are integral components of IBP Kenya's work.

This memorandum is in response to Letter **Ref. SEN/SCDL/CORR/2022/068**

Overall observation

While we take note and make recommendations on the proposed ammendments, we must underscore that the problem with public debt lays not in the type of threshold, percentage of GDP or an absolute figure, but rather on the prudence in the management expenditure and borrowing. We say so as both past thresholds have been exceeded or nearly reached with minimal explanation and accountability. That budget deficit continues to grow disproportionately to ordinary revenue means the borrowing appetite increases and so does debt servicing and that has put the country in a vicious cycle. We implore on the senate to address this governance problem.

Specific observations and recommendations

1. **Flip flop in decision on ratio or absolute figure:** It is notable that the proposed revision of debt ceiling to an absolute figure of KES. 10 Trillion comes against a background of two other proposals that were published not long ago by the national treasury for reverting to a percentage ratio of 55 and/or 65 per cent respectively. This is such a serious matter to be tossed back and forth especially at this point of increasing risk of debt distress.

2. **There has been no public participation by either the national treasury nor parliament on this new proposal despite it being passed in the national assembly.** This is a violation of the law and portends a serious trend where critical decisions are not presented for consultation. Notable is that the initial proposal for 55 per cent was subjected for public participation.

3. **The problem Kenya faces is on poor governance of public finances and not necessarily the type and level of ceilings for public debt.** Thus, raising the ceiling of debt level will not solve the problem. Kenya looses upward of KES. 700 billion (using the president's figure of KES. 2 Billion per day) to corruption and a further KES. 500 billion on tax expenditures (holidays and breaks) for EPZs.

4. **A raise of the ceiling to KES. 10 Trillion in order to allow for deficit financing of KES 846 Billion deficit technically means that by June 2021 the debt stock to GDP will be over 70 per cent.** This exceeds the sustainability index and further strains the fiscal space that is already. As the table below shows Kenya has already exceeded most sustainability measures.

i. Public Sector Debt DSA

20. The overall DSA indicate that Kenya's debt (public & publicly guaranteed debt) totaling to Kshs. 7.99 trillion, is gradually moving towards breaching the all sustainability thresholds, indicating increasing likelihood of debt distress in the future. Breached thresholds include, i) PV of Public Debt-to-GDP ratio, ii) PV of Public debt-revenue and grants ratio, iii) PV of PPG External Debt-to-Exports ratio, iv) PPG debt service-to-exports ratio. This indicates that both solvency and liquidity sustainability ratios are presumed to be permanently breached and will require concerted effort of fiscal consolidation to bring them back to sustainable levels.

Table I: Debt Sustainability Analysis

	Threshold	2020	2021	2022	2023	2024	2025	2026	2031	2041
PV of Public Debt-to-GDP ratio	55	62.4	63.0	64.2	63.4	62.9	61.1	59.5	45.4	22.6
PV of Public debt-revenue and grants ratio	300	360	372.6	370.8	348.	339.2	324.0	309.3	234.8	110
PV of PPG External Debt-to GDP ratio	40	28.7	28.7	28.3	27.3	26.3	25.7	25.2	22.7	16.8
PV of PPG External Debt-to-Exports ratio	180	288.3	255.8	239.20	219.8	204.2	193.6	188.5	151.5	79.8
PPG debt service-to-exports ratio	15	26.5	19.1	22.70	20.1	29.7	18.4	17.1	16.1	7.9
PPG debt service-to-revenue ratio	18	15.50	13.00	15.80	14.00	21.00	13.10	12.10	12.70	8.30

Source: IMF – March 2021

5. Fiscal deficit is the big problem including its revision during implementation. Table below shows that in some years the revision has been as high as 76 per cent.

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Kenya

Year (Billions)	Deficit in the Approved Budget	Deficit in the Revised Budget	Increase in the deficit within the year
2014/15	-417.0	-732.0	76%
2015/16	-640.5	-732.6	14%
2016/17	-775.0	-871.6	12%
2017/18	-594.3	-670.4	13%
2018/19	-608.1	-760.6	25%
2019/20	-673.6	-789.9	17%

6. Debt servicing is taking more and more of revenue and currently stands at 65 per cent of ordinary revenue. The argument that everything is fine as long as Kenya can pay its debt has to be put into the context of the impact on other facets of budget and government spending. As shown here debt repayment and just a few key government budget tickets will take up all the domestic revenue in 2022. This is even before allocation to other key sectors such as health, agriculture and water access. While the government can borrow to fund capital programmes, there is a real risk of underfunded recurrent budget lines in the near future.

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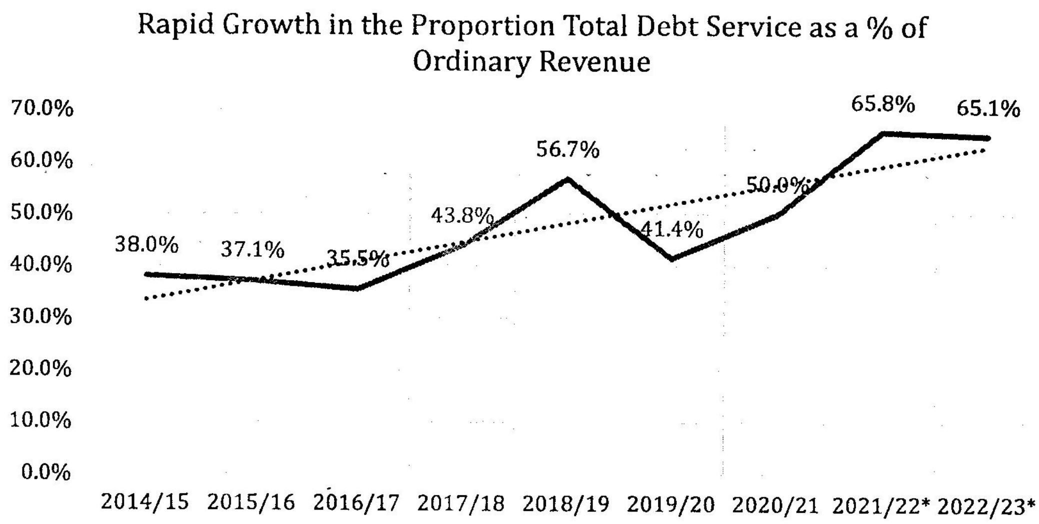

Budget Items	Amount in Billions
Total Revenue	**2,447.0**
Ordinary Revenue	2,141.6
Consolidated Fund Services	**1,571.8**
Of which	
Public Debt	1,393.1
Pensions	171.8
County Equitable Share	**407.0**
Teachers Service Commission	**297.7**
National Defence	**128.4**
Salaries under State Department for Interior	**136.6**
Total Allocation Key Budget Tickets	**2,541.6**
Key Budget Tickets Against Total Revenue	(94.6)

Source: various documents of the national treasury

7. **At the same time revenue projections and actual growth remain erratic while debt repayment is on an upward trend.** The table below shows that public debt and pension have the highest growth. This dwarfs the allocations and spending across other parts of the budget such as the overall budget to ministries, departments and agencies (MDAs) and devolved funds to counties. The overall

budget has not grown at the same rate as public debt and pensions. This means the Consolidated Fund services are now taking a bigger share of the total budget.

(Amount in Billions)	2017/18	2018/19	2019/20	2020/21	2021/22*	2022/23*
Ordinary Revenue	1,365.10	1,498.40	1,575.20	1,568.27	1,775.62	2,141.60
Consolidated Fund Services	582.50	895.00	807.30	878.78	1,327.22	1,571.81
Of which						
Public Debt	516.35	821.30	717.65	765.91	1,169.17	1,393.12
Pensions	62.41	69.30	86.99	110.27	153.64	171.83
Total MDA Spending	1,387.70	1,607.40	1,725.00	1,713.58	1,942.01	2,034.30
County Funding (Equitable Share)	302	314.00	316.50	316.50	370.00	370.00
Total Approved Budget	2,728	3,119.10	3,227.00	3,417.14	3,639.23	4,045.27
	% Change					
Ordinary Revenue		9.8%	5.1%	-0.4%	13.2%	20.6%
Consolidated Fund Services		53.6%	-9.8%	8.9%	51.0%	18.4%
Of which						
Public Debt		59.1%	-12.6%	6.7%	52.7%	19.2%
Pensions		11.0%	25.5%	26.8%	39.3%	11.8%
Total MDA Spending		15.8%	7.3%	-0.7%	13.3%	4.8%
County Funding (Equitable Share)		4.0%	0.8%	0.0%	16.9%	0.0%
Total Approved Budget		14.3%	3.5%	5.9%	6.5%	11.2%

*Approved budgets the rest are actual revenue and expenditure

Source: Office of the Controller of Budget Implmentation Reports 2017-21, National Treasury Programme Based Budget 2022/23

Recommendations

1. Senate must satisfy itself on the steps being taken towards more prudent public expenditure and especially management of deficit and reducing the risk levels that Kenya is exposed too currently.

2. The governance aspects raised above, especially on stopping leakages and outright theft of public funds need to be addressed.

3. Treasury needs to produce the actual picture of public debt as well as the projects where the monies have been spent.

4. Parliament oversight will be central in ensuring fiscal discipline and adherence to documents approved by the house. Therefore, we recommend a more open process of evaluating and approval of supplementary budgets and the Medium Term. This will strengthen the rigour supporting the documents that directly impact deficits and public borrowing.

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5. Parliament considers the Public-Private Partnership model for capital-intensive projects that would save us from many loans. But equity and the impact of such projects on the citizens should be addressed. Further, there is a need for addressing transparency around such projects, with full implementation of the Public Investment Management Guidelines.

Dated 10 June 2022, Nairobi

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