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REPORT OF THE STANDING COMMITTEE ON FINANCE AND BUDGET

ON

THE DIVISION OF REVENUE BILL (NATIONAL ASSEMBLY BILLS NO. 7 OF 2021)

PAPERS LAID	
DATE	13/04/2021
TABLED BY	SEN. OCHILO
COMMITTEE	FINANCE & BUDGET
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PARLIAMENT OF KENYA
<u>NAIROBI</u>

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PREFACE

Mandate and Functions of the Committee

Article 124 of the Constitution of Kenya, provides for the establishment of Committees by either House of Parliament. Committees are central to the workings, roles and functions of Parliament as set out in Article 94 and more specifically in Article 96 of the Constitution in regard to the Senate.

Parliamentary Committees consider policy issues, scrutinize the workings and expenditure of the national and county governments and examine proposals for legislation. The end result of any process in Committees is the report, which is tabled in the House for consideration.

The Standing Committee on Finance and Budget is established pursuant to standing order 218(3) of the Senate Standing Order and is mandated –

a) *To investigate, inquire into and report on all matters relating to coordination, control and monitoring of the county budgets and to examine –*
   i) *the Budget Policy Statement presented to the Senate;*
   ii) *report on the Budget allocated to Constitutional Commissions and independent offices;*
   iii) *the Division of Revenue Bill, County Allocation of Revenue Bill, and cash disbursement schedule for county governments.*
   iv) *to consider all matters related to resolutions and Bills for appropriations, share of national revenue amongst the counties and all matters concerning the National Budget, including public finance and monetary policies and public debt, planning and development policy; and*

b) *To pursuant to Article 228 (6) of the Constitution, to examine the report of the Controller of Budget on the implementation of the budgets of county governments.*

Further, the public Finance Management Act, 2012 section 8 (1)(b) on the responsibility of the Senate Budget Committee in public finance matters provides that- *The Committee of the Senate established to deal with budgetary and financial matters has responsibilities to review the County Allocation of Revenue Bill and the Division of Revenue Bill in accordance with Article 218(1)(b) of the Constitution at least two months before the end of the financial year*.

Membership of the Committee

The Standing Committee on Finance and Budget was constituted by the House on Thursday, 14th December, 2017 during the First Session of the Twelfth Parliament. The Committee was later reconstituted on Wednesday, 24th June, 2020, during the Fourth Session of the Twelfth (12th) Parliament. The Committee as currently constituted, comprises the following Members-

1. Sen. Charles Kibiru, MP - Chairperson
2. Sen. (Dr.) Ochillo Ayacko, MP, - Vice Chairperson
3. Sen. Wetang'ula Moses Masika, EGH, MP - Member
4. Sen. Kimani Wamatangi, MP - Member
5. Sen. Mutula Kilonzo Junior, CBS, MP - Member
6. Sen. Aaron Cheruiyot, MP - Member
7. Sen. Rose Nyamunga, MP - Member
8. Sen. CPA Farhiya Haji, MP - Member
9. Sen. Milicent Omanga, MP - Member

BACKGROUND AND EXECUTIVE SUMMARY

Article 218 of the Constitution provides for introduction of Division of Revenue Bill and the County Allocation of Revenue Bill to Parliament, at least two months before the end of each financial year.

The Budget Policy Statement (BPS), is the precursor to the Division of Revenue Bill, sets the fiscal framework underpinning the sharing of revenue between the two levels of government. The adoption of the 2021 BPS Report paved way for the publication and subsequent introduction of the Division of Revenue Bill to the House.

The Division of Revenue Bill (National Assembly Bills No. 7 of 2021 was published and introduced in the National Assembly. The National Assembly passed the Bill on 23rd March, 2021. Following the passage by the National Assembly, the Bill was submitted to the Senate for concurrence.

The Bill was read a First Time in the Senate on Tuesday, 30th March, 2021, and thereafter stood committed to the Standing Committee on Finance and Budget pursuant to standing order 140 (1) of the Senate Standing Orders for consideration and facilitation of public participation.

Pursuant to Article 118 (1) (b) of the Constitution and standing order 140(5) of the Standing Orders of the Senate, the Standing Committee, in its consideration of the Bill, invited key stakeholders, including the National Treasury, the Attorney General, the Council of County Governors, the Commission on Revenue Allocation, County Assembly Forum to submit their views on the Bill. The Committee also invited other non–state actors and the general public who similarly participated and submitted their memoranda on the bill.

The Bill provides for the division of nationally raised revenue between the two levels of government, allocation to the Equalization Fund as well as setting out specific resources to be provided to counties as conditional grants from national government share of revenue and from proceed of loans and loans from development partners. In addition, the Bill is accompanied by an explanatory memorandum pursuant to Article 218(2) of the

Constitution. The memorandum sets out the explanation of revenue allocation as proposed by the Bill along with the evaluation of the Bill in relation to the criteria provided under Article 203(1) of the Constitution. It also provides a summary of any significant deviation from the recommendations from the Commission on Revenue Allocation with an explanation for each such deviation.

The enactment of the Division of Revenue Bill is critical in setting the stage for the preparation of the national government budget and publication of County Allocation of Revenue Bill. It also informs on the preparation of respective county governments' budget documents in a manner that is timely and enable fiscal clarity and planning.

The Bill proposes-

a) Shareable revenue Kshs. estimated at Kshs 1,775.624 billion which is proposed to be shared as below
    i) National Government Kshs. 1,398.798 billion of which Kshs. 7.532 billion is given to counties as conditional allocations;
    ii) County Equitable Share Kshs 370.0 billion which is 27.3% of the Financial Year 2016/17 audited and approved revenue;
    iii) Equalization Fund – Kshs 6.825 billion;
b) Additional Conditional allocations (loans & grants from Development Partners) Kshs. 32.343 billion

Cognizant of the High Court Ruling in Petition No. 252 of 2016, the Committee considered the Bill and further held two consultative meetings with the National Treasury, the Attorney General, the Council of County Governors, the Commission on Revenue Allocation. The consultations were mainly to achieve an amicable mechanism to deal with the provisions of the Bill while respecting the High Court Ruling.

Committee's Recommendations

The Committee recommends that the Division of Revenue Bill (National Assembly Bills No. 7 of 2021) be approved with the amendment to the schedule. The new schedule should provide for the following four items only-

a) Total sharable revenue;

b) National Government share;

c) Equalization fund; and

d) County equitable share.

This recommendation is in compliance with the Ruling in High Court Petition No. 252 of 2016, where the court held that it cannot be permissible to provide for conditional grants in the Division of Revenue Act and therefor it follows that conditional grant cannot be proposed in Division of Revenue Bill.

Acknowledgements

The Committee acknowledges the Commission on Revenue Allocation, the Institute of Certified Public Accountants (ICPAK), the International Budget Partnership (IBP), the National Treasury, the Attorney General, the Council of County Governors, the and members of the public who made insightful contributions and recommendations. Further, the Committee thanks the Offices of the Speaker and Clerk of the Senate for the support extended to the Committee in execution of its mandate.

Appreciations to the Members of the Committee for their patience, sacrifice and commitment to public service, which enabled the Committee complete the assigned task within the stipulated time.

It is now my pleasant duty and privilege, on behalf of the Standing Committee on Finance and Budget, to present to the Senate, this Report of the Committee on the Division of Revenue Bill (National Assembly Bills No. 7 of 2021).

SIGNATURE: ____________________________

SEN. CHARLES KIBIRU, MP.

(CHAIRPERSON, STANDING COMMITTEE ON FINANCE AND BUDGET)

DATE: 12th April, 2021

CHAPTER ONE

1.0 VERTICAL ALLOCATION OF REVENUE FOR FINANCIAL YEAR 2021/22

HIGHLIGHTS OF THE DIVISION OF REVENUE BILL, 2021

1. Article 218 of the Constitution provides for the submission of the Division of Revenue Bill and the County Allocation of Revenue Bill to Parliament, at least two months before the end of a financial year. The Division of Revenue Bill divides revenue raised by the national government among the two levels of government. The Division of Revenue Bill further sets out specific resources to be provided to counties as conditional grants, and the Equalization Fund.
2. In addition, section 191 of the Public Finance Management (PFM) Act, 2012, provides that each year when the Budget Policy Statement (BPS) is introduced, the Cabinet Secretary shall submit to Parliament a Division of Revenue Bill and County Allocation of Revenue Bill prepared by the National Treasury for the financial year to which that Budget relates.
3. The adoption of the 2021 BPS Report by both Houses paved way for the publication and subsequent introduction of the Division of Revenue Bill, 2021 in National Assembly.
4. The Division of Revenue Bill (National Assembly Bills No. 7 of 2021) was published on 8th March, 2021 and passed by the National Assembly on 23rd March, 2021. The total shareable revenue for the FY 2021/2022 is estimated at Kshs 1,775.62 billion proposed to be allocated as shown in table 1;
5. In addition, several conditional allocations (loans & grants) from development partners allocated to the County Governments for the FY 2021/22 have been listed as memo items in the Bill. The total allocation for these conditional grants amounts to Kshs. 32.34 billion.

Table 1: Allocation of revenue raised nationally between the national and county governments for the financial year 2021/22.

Type/level of allocation	Amount in Ksh.	Percentage (%) of 2016/17 audited and approved Revenue i.e. Ksh. 1,357,698 Million
A. Total Sharable Revenue	1,775,624,173,860	
B. National Government	1,398,798,856,427	
C. Equalization Fund	6,825,317,433	0.50%
D. County equitable share	370,000,000,000	27.3%

1.1 Equitable Share of Revenue

6. Pursuant to Article 202 (1) of the Constitution, the nationally raised revenue is shared equitably among the national and county governments. Article 203 (2) further stipulates that the equitable share of the revenue raised nationally that is allocated to county governments shall be not less than fifteen per cent of all revenue collected by the national government and shall be calculated on the basis of the most recent audited accounts of revenue received, as approved by the National Assembly. The proposed Equitable Share for FY 2021/22 is Kshs. 370 billion which is equivalent to 27.3 percent of the last audited accounts **(Kshs. 1,357,698 million for FY 2016/17)** as approved by the National Assembly.

7. In calculating the County Governments' equitable revenue share allocation for FY 2021/22, the following factors have been put into consideration;
    a) Growth in the County Governments' equitable share for 2020/21 of Kshs. 316.5 billion by Kshs. 36.1 billion or 11.4 %. This growth derived from anticipated improvement in revenues raised nationally in FY 2021/22. This increase is expected

to facilitate post covid-19 economic recovery at the counties as well as ensure sustained service delivery by the devolved governments.

b) Conversion of some of the ongoing county governments' additional conditional allocations with no contractual obligations to equitable share. The converted conditional grants amount to Kshs. 17.4 billion.

1.2 GOK Conditional Allocations to County Governments

8. The Division of Revenue Bill 2021, proposes to allocate Kshs. 7,537 million from the National Government shareable revenue for the following conditional allocations to support specific national policy objectives to be implemented by County Governments-
    a) Conditional Allocation to facilitate the leasing of medical equipment of **Kshs. 7,205 million**. The grant is in its seventh year of implementation.
    b) Conditional allocation to supplement county allocation for the construction of county headquarters of **Kshs. 332 Million** in five counties. The five counties facilitated under this grant are Lamu, Nyandarua, Tana River and Tharaka Nithi. The allocation is in the fourth year of implementation.

1.3 Equalisation fund

9. Kshs. 6.8 billion has also been set aside for the Equalization Fund in FY 2021/22 which translates to 0.5 per cent of the last audited revenue accounts of governments, as approved by the National Assembly. This Fund is used to finance development Programmes that aim at reducing regional disparities among beneficiary counties.
10. The operationalization and administration of the Equalization Fund was suspended in 2016 with the annulment of the guidelines by the High Court due to their unconstitutionality. The National Treasury should fast-track processing and submission of the Public Finance Management (Equalization Fund) Regulations to Parliament for approval to ensure that the marginalized areas access equalization funds as there is a danger of the fund lapsing having not achieved its objective.

1.4 Conditional grants from loans and grants from development partners

11. The bill proposed several conditional grants from loans and grants from development partners. These conditional grants are-

i) IDA-Kenya Devolution Support Program (KDSP) ("level 2") Grant of Kshs. 4.60 billion;

ii) IDA-Transforming Health Systems for Universal Care Project, World Bank credit of Kshs. 2.23 billion;

iii) DANIDA-Primary Health Care in Devolved Context Kshs. 701.25 million;

iv) IDA-National Agricultural and Rural Inclusive Growth Project (NARIGP), World Bank credit of Kshs. 6.39 billion;

v) EU-Instruments for Devolution Advice and Support (IDEAS) grant of Kshs. 230.73 million;

vi) IDA (World Bank) - Kenya Climate Smart Agriculture Project (KCSAP) of Kshs. 7.84 billion;

vii) World Bank- Kenya Informal Settlement Improvement Project II (KISIP II) of Kshs. 2.80 billion;

viii) IDA – Water and Sanitation Development Project (WSDP) World Bank Credit of Kshs. 5.00 billion;

ix) Sweden Agricultural Sector Development Support Programme (ASDSP) II- Kshs. 1.30 billion;

x) Drought Resilience Programme in Northern Kenya (DRPNK) - Kshs. 370 million;

xi) Emergency Locust Response Project (ELRP), World Bank Credit of Kshs. 800 million;

xii) UNFPA - 9th Country Programme Implementation: - Kshs. 73.9 million.

CHAPTER TWO

2.0 SUBMISSIONS FROM STAKEHOLDERS

This Chapter presents the deliberations of the Committee with various stakeholders. It highlights the views and recommendations submitted to the Committee.

Submission by the National Treasury and Planning

12. The Committee invited the Cabinet Secretary, National Treasury and Planning to deliberate on the proposed Division of Revenue Bill, 2021, in light of the High Court Ruling on Petition No. 252 of 2016 on Division of Revenue Act, 2016. The Cabinet Secretary submitted as follows:

On the proposed Division of Revenue Bill, 2021

13. The Division of Revenue Bill (DoRB), 2021 proposed to allocate to County Governments Ksh.409.88 billion in the financial year (FY) 2021/22, which relative to the financial year 2020/21 allocation, reflected an increase ofKsh.53.5 billion or 16.9%. That allocation comprises: equitable share ofKsh.370 billion; additional conditional allocations from the National Government share of revenue raised nationally amounting to Ksh.7.53 billion; and additional conditional allocations from proceeds of loans and grants from development partners amounting to Ksh.32.34 billion.

County Governments ' Equitable Share

14. The bill proposed to allocate County Governments an equitable share of revenue raised nationally for the financial year 2021/22 of Ksh.370 billion. That was premised on Parliament having approved the Third Basis for allocation of the share of national revenue among the County Governments in September, 2020 on condition that the formula's implementation would be preceded by a Ksh.53.5 billion increase in the Counties' equitable revenue share.

15. The proposed County Governments' equitable share of revenue raised nationally for the financial year 2021/22 was arrived at by:

i. adjusting the Counties' FY 2020/21 allocation (i.e., Ksh. 316.5 billion) by Ksh 36.1 billion or 11.4 percent. That growth was premised on the anticipated improvement in revenues raised nationally in FY 2021/22 when the effects of Covid-19 pandemic were expected to ease. That increase was expected to facilitate post Covid-19 economic recovery at the Counties as well as ensure sustained service delivery by the devolved governments; and,

ii. converting four existing conditional grants to County Governments into unconditional grants, and allocating the respective amounts totaling Ksh. 17.4 billion towards the Counties' FY 2021/22 equitable revenue share. The four conditional allocations are: Road Maintenance Levy Fund (RMLF); the level-5 hospital grant; the compensation for user fees foregone; and, the grant funding rehabilitation of village polytechnics.

16. Conversion of the four conditional allocations to Counties equitable revenue share as proposed above had several advantages. Firstly, it would afford the Counties more autonomy to budget and prioritize allocation of resources.

17. Secondly, it would achieve a more consolidated approach to funding of devolved functions- while also enabling the tracking of performance and attribution of outcomes. Thirdly, it would help to address a number of challenges that were experienced including suboptimal absorption of conditional allocations; and failure by Counties to allocate sufficient resources in areas receiving supplemental funding by the National Government through conditional allocations.

18. Moreover, the fact that the approved Third Basis for allocation of the share of national revenue among the County Governments effectively linked resources to devolved functions (specifically with weighted parameters for health, roads and agriculture) meant that it was now possible to achieve policy objectives of some conditional grants directly through the equitable share in health and agriculture, for instance. The new parameters to be used in distributing the equitable revenue share among Counties closely resembled those that were being used to distribute sectoral conditional allocations. In addition, the approved revenue distribution criteria contained a parameter, 'population' with a weight of 18% which was specifically designed to reflect costs of 'other County Services' including village polytechnics.

19. The position at the time was besides the composite of equal share, the allocation criteria for the rehabilitation of village polytechnics conditional grant was also based on total trainee enrolment in the respective county governments, which was similar to the use of population parameter in the Third Basis for Revenue Sharing among Counties. That meant that village polytechnics being a devolved function, and also a composite of the population parameter of the formula should be directly financed from each County's equitable share of revenue.

20. After making the above adjustment, County Governments' equitable share of revenue in the financial year 2021/22 was estimated to be Ksh. 370 billion

21. The above proposed equitable share for FY 2021/22 ofKsh370 billion was equivalent to 27.3 percent of the last audited accounts (Ksh.1.358 billion for FY 2016/17) as approved by Parliament. The proposed allocation met the requirement of Article 203(2) of the Constitution that equitable share allocation to counties should not be less than 15 per cent of the last audited revenue raised nationally, as approved by the National Assembly.

Additional Conditional Allocations

22. 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.

23. Accordingly, and in addition to the equitable share of revenue raised nationally, the National Treasury proposed that County Governments received additional conditional allocations amounting to Ksh. 39.88 billion. That reflected a decrease of Ksh 13.52 billion. That decrease was occasioned by the proposal to convert some of the ongoing additional conditional allocations to county governments, amounting to Ksh. 17.4 billion to the equitable share in FY 2021/22. That comprised: i) additional conditional allocations from the National Government share of revenue raised nationally amounting to of Ksh 7.54 billion and, ii) conditional allocation from proceeds of external loans and grants amounting to Ksh. 32.34 billion.

The Inclusion of Conditional Grants in the Division of Revenue Bill

24. The National Treasury had proposed an allocation of Ksh. 39.88 billion as additional conditional allocations to county governments. The allocation comprised of: -

(a) Ksh. 7.5B billion as additional conditional allocations to county governments financed from the national government share of revenue raised nationally to finance: - i). Leasing of Medical Equipment at Ksh.7.2 billion; and ii) Supplement for construction of county headquarters at Ksh. 332 million. Those additional conditional allocations, were not converted into equitable share of County Governments because they had ongoing contractual obligations.

(b) Ksh. 32.3 billion as additional conditional allocations to County Governments financed from proceeds of loans and grants by development partners.

Treatment of the additional conditional allocations in the Division of Revenue Bill

25. The National Treasury treated the above additional conditional allocations as memo items to the Schedule of the Bill.

26. They averred that the memo items were not part of the main Division of Revenue Bill and was intended as a disclosure to the public of additional allocation of revenue from the national government share of revenue and loan & grants from development partners.

27. Division of revenue are:

i. Item A: Total Sharable Revenue Ksh. 1,775,624,173,860

ii. Item B: National government share of revenue raised nationally amounting to Ksh. 1,398,798,856,427 of which 7,537,0000 shall be transferred to County Governments as additional conditional allocations pursuant to Article 202 (2) of the Constitution.

iii. Item C: Allocation to Equalisation Fund (pursuant to Article 204) amounting to Ksh. 6,825,317,433; and,

iv. Item D: County equitable share amounting to Ksh. 370,000,000,000

Alternative Mechanism for Disbursement of Conditional Grants to Counties if they were to be Omitted in the Bill

28. Article 96 (3) of the Constitution provides that the Senate is responsible for determining the allocation of national revenue among Counties and exercising oversight over national revenue allocated to the County Governments;

29. Article 114 (3) of the Constitution excludes the Division of Revenue Bill and County Allocation of Revenue Bill from the definition of a money Bill. Article 218(1) (b) requires a County Allocation of Revenue Bill be introduced in Parliament to divide among Counties the revenue allocated to the County level of Government.

30. Section 191 (1) as read with Section 25 of the Public Finance Management Act (PFMA), 2012 provides that, *each year when the Budget Policy Statement is introduced, the Cabinet Secretary responsible for finance shall submit to Parliament a Division of Revenue Bill and County Allocation of Revenue Bill as provided in the PFMA for the financial year to which that Budget relates.*

31. Section 191 (3) of the PFMA also provides that, *'the County Allocation of Revenue Bill shall specify— (a) each county's share of that revenue under subsection (2) and (b) any other allocations to the counties, from the national government's share of that revenue, and conditions on which those allocations shall be made.*

32. The import of paragraph 24 was that any additional conditional allocations to County Governments should be contained in County Allocation of Revenue Bill and approved by Parliament.

33. They argued that pursuant to Regulation 24 and 25 of the Public Finance Management (National Government) Regulations, 2015, National Government Accounting Officers could issue Authority to Incur Expenditure to respective accounting officers of the respective county governments. Particularly, Regulation 25 (1) of PFM(NG) Regulations 2015 also provides *An accounting officer may authorize a public officer under their national government entity to be an Authority to Incur Expenditure Holder (AIE).; while regulation 25 (2) provides that, An Accounting Officer who finds it necessary to authorize a public officer in another Ministry or county government to incur official expenditure on his or her behalf, shall do so b) issuing an Authority to Incur expenditure addressed to the Accounting Officer of the national government or county government entity.*

34. However, Regulation 25 (3) and (5) gives clarity that designation of AIE Holder shall be in writing in the form prescribed by the National Treasury; and *Where an Accounting Officer delegates this authority, the accounting officer shall remain responsible for any expenditure incurred as a result or that delegation.*

35. In the doctrine of separation of powers under devolved system of government, emphasis is placed on independence of the two levels as envisaged in Article 189 of the Constitution, However, is this option visible and how can the doctrine be respected?

36. Article 226 (2) of the Constitution provides that, *"The accounting officer or a national public entity is accountable to the National Assembly for its financial management, and the accounting officer of a county public entity is accountable to the county assembly for its financial management".*

37. Accordingly, the Article suggests that that arrangement posed a challenge not only on accountability mechanism if an AIE were to be issued by a National Government Accounting Officer to a County Government Accounting Officer, but would also offend principles of the Constitution on independence of County Governments.

38. It was for the above reason that the National Treasury was of the considered opinion that the only legal instrument to disburse allocations to County Governments was

the County Allocation of Revenue Act, which must be approved by the Senate, and as such allocations should be disclosed in the Division of Revenue Act as memo items.

The increased Allocation to the Conditional Grant on the Leasing of Medical Equipment Programme

39. That additional conditional allocation which was in its seventh year of implementation, was proposed to increase from Ksh.6.205 billion in FY 2020/21 to Ksh.7.205 billion in FY 2021/22 and was intended to facilitate the payment of lease amounts in respect of modern specialized medical equipment in at least two health facilities in each County Government over the medium term. That would facilitate easy access to specialised health care services and significantly reduce the distance that Kenyans travel in search of such services today.

40. The significant increase in allocation was to cater for pending bills related to MES programme occasioned by lack of provision in previous years. For instance, in FY 2019/20, Ministry of Health closed with pending bills of Ksh. 1.17 billion which was treated as a first charge in FY 2020/21 from the allocation to MES of Ksh. 6.02 billion.

41. Accordingly, the balance would not be adequate to cater for the current year's contractual obligations, unless additional resources were provided in the supplementary. Secondly, the next FY being the final year of the project, there was need to make a full provision to ensure all contractual obligations were met before closure of the project so as not to attract pending bills and subsequent interest which would occasion loss of public funds in the long run.

The High Court Ruling on Petition No. 252 of 2016 on Division of Revenue Act, 2016

42. The National Treasury was cognisant and in agreement with the High Court Ruling on Petition No. 252 of2016 on Division of Revenue Act, 2016 as it related to the

Division of Revenue Bill, 2021 and submitted as follows with regards to compliance with the findings that: -

(a)the National Government cannot allocate itself funds for and undertake devolved functions, without first executing intergovernmental agreements required by Article 187 of the Constitution;

43. The Division of Revenue Bill, 2021 had not allocated any funds to the National Government to undertake any of the Devolved functions as contained in part II of the Fourth Schedule of the Constitution. The only additional conditional allocation whose expenditure would be made by the National Government on behalf of respective county governments was on Leasing of Medical Equipment. There existed duly signed Intergovernmental Agreements pursuant to Article 187 of the Constitution between the Ministry of Health (on behalf of the National Government) and the respective county governments to this effect.

(b)in accordance with Article 202 (2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be netted from national government's share of revenue and not from the overall revenues raised nationally;

44. The National Treasury had proposed allocation of Ksh. 7.5 billion additional conditional allocations to county governments financed from the national government share of revenue raised nationally to finance: - i). Leasing of Medical Equipment at Ksh.7.2 billion and ii) Supplement for construction of county headquarters at Ksh. 332 million.

(c)in accordance with Article 202(2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be disbursed to the Counties through the County Revenue Fund;

45. The National Treasury submitted that they shall- except for the leasing of medical equipment conditional allocation, disburse all allocations to county governments to their respective County Revenue Fund Accounts as contained in the proposed County Allocation of Revenue Bill, 2021, which was before Parliament.

(d)funds christened as 'national interest' in the Division of Revenue Act 2016 or any other Division of Revenue Act enacted to implement the provisions of Article 202 and 203 of the Constitution cannot be apportioned on devolved functions without the same being channeled to the Counties as conditional or unconditional grants.

46. The National Treasury, through the Division of Revenue Bill, 2021 had not proposed an allocation christened "National Interest", Pursuant to Article 203, to the National Government, for functions devolved to county governments.

47. The National Treasury urged the Committee to consider and reinstate the definition of revenue under section 2 of the Bill to read that ""revenue" has the meaning assigned to it under section 2 of the Commission on Revenue Allocation Act, 2011; and *includes Roads Maintenance Levy Fund allocation under this Act.*

Submission by the Commission on Revenue Allocation

In accordance with the requirements of Article 205 of the Constitution, the Commission on Revenue Allocation considered the provisions of the Division of Revenue Bill (National Assembly Bills No. 3 of 2020) and made the following observations:

48. Inclusion of conditional grants in DORB: In line with the Court ruling on Petition no. 252 of 2016, conditional or non-conditional grants are not items to be provided for under the Division of Revenue Act. Implications of the ruling:

a) The Division of Revenue Act should only reflect the equitable share allocations between the two levels of government, and

b) That conditional and unconditional grants have to be provided for through an alternative intergovernmental transfer framework

49. Alternative Mechanisms for disbursement for Conditional Grants: Based on the following rulings (Petition no. 252 of 2016):

a) That the national government cannot allocate itself funds and undertake devolved functions without first executing intergovernmental agreements under Article 187 of the Constitution,

b) That following from (a) above, the national government's accounting officers' cannot spend money for conditional grants directly in the Counties to undertake devolved functions unless there is an agreement transferring functions under Article 187, 189 or 190 of the Constitution and section 21 of the County Governments Act,

c) That there ought to be a framework stating the purpose, the goal and the mechanism for the issuance of the conditional grant,

d) that all funds under Article (202) (2) of the Constitution (conditional or non-conditional) must be channeled through the County Revenue Fund (CRF) to the specific counties for the specific functions outlined by the national level of government,

e) The said funds should be channeled directly to the activities in question and accounted for, and

f) that conditional and unconditional funds cannot be appropriated by the County Assembly through a County Appropriation Bill.

50. Implications of the rulings:

a) That the relevant Ministry, Department or Agency under which the grants are accounted for should provide a schedule of disbursement to each of the county governments based on an agreed intergovernmental transfer framework

b) That the National Assembly has to approve the appropriation of the conditional and unconditional grants given that funds are being channeled directly to the activities in question and accounted for by the national government.

51. Increased allocation to Leasing of Medical Equipment Scheme: The Commission was not part of the signed contractual obligations between the National

Government, County Governments and the provider of the Medical Scheme. Thus the Council of Governors, the Ministry of Health and the National Treasury were better placed to provide more information on why the allocations for the payments kept on varying from one year to another. The Commission's understanding was that whilst the contracted amount remained the same, the annual variations could be informed by the nature and the number of equipments that were availed by the provider each year.

Submission by the International Budget Partnership, Kenya (IBP-Kenya)

52. Country Manager IBP appeared before the Committee on 6th April 2021 raising the following key concerns:

i. The allocations to counties were declining, and that would affect services. Parliament needed to address that situation so as not to lose the gains already made through devolution of public services.

ii. Public debt, pensions and other charges of the consolidated fund services were crowding out the amount available for sharing and hurting counties allocation.

iii. Unrealistic revenue projection had negatively affected revenue sharing.

iv. Lack of transparency, accountability and meaningful public engagement was affecting the division of the revenue process

53. Despite devolution being a key aspect of service delivery in Kenya, the allocations to county governments were declining. While the growth in national revenue remained stable over time, except for FY 2020/2021 and FY 2021/2022 due to the COVID-19 pandemic, the amounts approved to counties as a proportion of national revenue were declining. However, 2021/22 would see a 17% per cent growth in allocations despite a projected decline of 4% in ordinary revenue. They therefore observed that that did not reflect a realistic situation and proposed that parliament arrests that state.

54. **There was no clear growth factor on the division of revenue allocation basis. This was left to individual actors in the national government to decide how much should be allocated to county governments.** Except for FY 2015/2016, Commission on Revenue Allocation (CRA) and the National Treasury have always used different factors to determine how the share of county governments should grow. Of great concern was the allocation for FY 2021/2022 which was arbitrary and had no basis given the declining ordinary revenue occasioned by the Covid-19 pandemic. As much as the increase of Ksh. 53.5 billion was a condition for the approval of the Third Basis for Revenue Allocation, there was no explanation on how it was arrived at. IBP therefore proposed that as Parliament considered the Division of Revenue Bill 2021, the growth factor or the criteria for determining the same be established and made clear. They suggested that as a minimum, allocations to county governments should be informed by the three-year average growth of ordinary national revenue.

55. **Public debt, pensions and other charges of the consolidated fund services were crowding out the amount available for the division of revenue and hurting counties allocation.** Total debt service was growing at a very high rate and that was limiting allocation to devolved services. The growth in county allocation over the years was very minimal which affected service delivery. They also noted that the growth in ordinary revenue was very marginal. More importantly, while public borrowing has a direct impact on the size of the sharable revenue, the National Treasury was the only body deciding on that vital national instrument. They therefore recommended that counties and the Senate should be involved in the discussion on national borrowing as that has an impact on the revenue that is shared between the two levels of government.

56. **Pensions and other CFS Services have equally grown, and their administration was of concern.** Pension was a non-discretionary obligation that had a bearing on

the size of revenue that was eventually shared between the two levels of government. The higher the share of ordinary revenue that is taken up by these national obligations, the lower the sharable revenue and allocations to counties. An analysis of government expenditure on pensions between 2016-2021 indicated an increasing trajectory over time, as illustrated below

Government Fiscal Framework- Pension and other CFS

Year	2016	2017	2018	2019	2020	2021
Pension and other CFS	43,429 Millions	60,169 Millions	91.1 Billions	109.5 Billions	118.7 Billions	137.0 Billions

Source: Budget Policy Statements 2016-2021

57. **Recommendations by CRA on harmonization of functions should be used to justify adjustment of equitable share.** CRA recommended harmonization of functions as provided for in the Fourth Schedule of the Constitution to be used as a basis for increasing the equitable share. IBP welcomed the recommendation and urged Parliament to consider that approach as it would ensure that funds follow functions that are assigned to the county governments.
58. **Conditional Grants for construction of county headquarters needed to be clarified**. The Division of Revenue Bill 2021 allocated Kshs. 332 million towards the construction of county government headquarters for five counties namely, Isiolo, Lamu, Nyandarua, Tana River and Tharaka Nithi. There was need for clarity on the criteria used to identify the counties and the amount to be allocated to each. From the bill, it was clear the five counties received a similar grant in the previous financial years. For instance, the Division of Revenue Bill 2020 allocated Kshs. 300 million to these counties. How far has their construction gone? An annexure of the same should provide the requisite information that indicated the progress made over

the years. They therefore urged the Senate to compel the National Treasury to provide an annex with detailed information on the above.

59. **Lack of transparency, accountability and meaningful public engagement was affecting the division of the revenue process.** Although Parliament had embraced public participation in the legislative process and made efforts towards facilitating public participation, public engagement in the division of revenue process was not effective but tokenistic and inconsequential in the ultimate decision-making process. In some instances, parliament did not explain its actions or give reasons for certain decisions. For instance, on 9th March 2021, parliament approved to reduce the publication time of the Division of Revenue Bill from 7 days to 1 day. Although that may be well within the Standing Orders of Parliament, such actions needed to be explained for the public to understand why the decision was made.

60. **The realism of revenue forecast remained a gamble.** Revenue forecasts at both national and county level were ambitious and often led to budget deficits. This was exacerbated by the failure by the Tax Authority to meet the set targets over the years. That would need to be further revised due to the effect of COVID-19 to Kenya's economic productivity. A trend analysis of revenue growth was critical in informing revenue projections for the coming years. Kenya's budget process had inadequately facilitated accurate forecasts for resource collection. The common tendency was, therefore, to make overly optimistic revenue projections leading to increased uncertainty of resource flows. An analysis of total revenue collection including Appropriation in Aid (A.i.A) showed shortfalls in each financial year since 2015.

Performance of Total Revenue including A-i-A (Figures in Billions of Kshs)

Year	Dec-15	Sep-16	Nov-17	Nov-18	Dec-19	Feb-21
Target Revenue	642.9	328	611	677	1059.3	907.7
Actual	575.2	313.6	558.4	633.7	920.6	810.6
Shortfall	67.7	14.4	52.6	43.3	138.7	97.1

Submission by the Institute of Certified Public Accountants of Kenya

61. **Basis for revenue projections:** Kenya has consistently registered a positive growth in its revenue collection with it doubling from Ksh. 0.7 Trillion in FY 2011/12 to Ksh. 1.5 Trillion over a seven-year period (2018/19) (KRA, 2019). However, the actual revenue receipts have continuously fallen below the targets (KNBS, 2020). Coming from a global pandemic that necessitated most governments, the Kenyan one included, to adopt expansionary fiscal policy measures, it is highly unlikely that in the coming FY 2021/22, the Kenyan economy will have rebounded. The Government should therefore conduct a trend analysis of revenue growth to inform revenue projections for the subsequent years. The ambitious revenue forecast has among other ramifications contributed to budget deficits which have in turn worsened the pending bills problem.

62. **Inadequate utilization of the Leased medical equipment:** The conditional allocations are tied to the implementation of specific national policies, and are mainly from both government and donor community. One of the items catered for is the leasing of medical equipment, which has been receiving allocation from the FY 2015/16. However, a Senate report on 'The Managed Equipment Service (MES) Project' indicates that the equipment has been under-utilized owing to inadequate health personnel and insufficient infrastructure (water and electricity).
63. The report also highlights the exaggerated cost of equipment supplied in comparison to prevailing market rates. There is need to provide capacity strengthening sessions to the health personnel and fast-track the development of the required infrastructure in the respective health facilities.
64. **Conditional Grants for construction of county headquarters need to be clarified and accounted for:** In the FY 2017/18, 5 counties (Isiolo; Lamu; Nyandarua; Tana River and Tharaka Nithi) were identified as being the only counties that did not inherit adequate office space for county headquarters and thus

would be allocated funds to construct their headquarters over the span of three financial years (between 24-32 months).

65. According to a report on County Infrastructure by the Senate Standing Committee on Finance and Budget, the State Department of Public Works submitted that the implementation of this project would be carried out through the Ministry with the National Government contributing 70% of the amount while counties contribute the remaining 30%. The first disbursement of the agreed Ksh 518 million for construction of their headquarters was received in FY2017/18 therefore, the final disbursement should have been in the FY 2019/20. Despite this, DORB 2020 and 2021 still allocated the counties the amounts Ksh 300 million and Ksh 332 million respectively as shown in the table below.

66. ICPAK thus proposed that there was need for an implementation report on the same to justify the continued allocation. Further, there was need for an indication on completion of this project.

67. Consider conditional Allocation to support ECDE: In a Devolution Survey 2020 conducted by the Institute, several challenges were documented that were impeding the successful delivery of educational services, especially at the county level:

- high turnover rates for Early Child Development Education (ECDE) teachers
- low funding for ECDE, inadequate investment in succession planning within departments, low and unclear scheme of service for ECDE teachers,
- Inadequate infrastructure to support the learning of children living with disability; and
- inadequate number of trained instructors in most polytechnics.

68. ICPAK proposed that there was need to provide conditional allocation to ECDE for purposes of the following:

a) increasing capitation for ECDE teachers
b) Employment of skilled and qualified instructors in polytechnics;
c) To support development of adequate monitoring and assessment of performance (quality assurance) of learning at that level.

69. **Public debt repayment crowding out the amount available for division of revenue and hurting counties allocation:** Public borrowing has a very direct impact on the size of the sharable revenue as shown in the table below. On average, public debt servicing growth was higher at 30% than the growth in both the shareable revenue (7%) and the county allocation (5%).

70. The Institute thus called on the National Treasury to contract more loans from the multilateral lenders than from commercial lenders who are usually more expensive as compared to the former.

71. Further, since the National Treasury was the only body deciding on that vital national instrument, ICPAK recommended that counties through the Senate should be involved in the discussion on national borrowing as that had an impact on the revenue shared between the two levels of government.

Growth in Public debt, ordinary revenue and counties allocation

FY	Public Debt Service (Ksh. Billions)	Ordinary Revenue (Ksh Billions)	Counties Allocation (Ksh Billions)	Growth in Public Debt Service	Growth in Shareable Revenue	Growth in County Allocatio
2017/18	462.24	1365.06	302.00			
2018/19	641.51	1499.76	304.96	39%	10%	1%
2019/20	538.80	1573.42	310.00	-16%	5%	2%
2020/21	829.91	1574.01	316.50	54%	0%	2%
2021/22	1174.01	1775.62	370.00	41%	13%	17%
Average				**30%**	**7%**	**5%**

Source: Division of Revenue Bill 2021

72. **Actual public debt service figures have always been higher than the projections:** public debt repayment projections contained in the division of revenue bills were always been lower than what was contained in the programme-based budget documents. These figures have further been lower than the actual ones contained in the national government implementation review reports. In addition to this, the deviation of the projected amounts as contained in the division of revenue bills from the actual show an increasing trend which shows that the projections are highly underestimated.

Public debt projections vs actual

FY	Division of Revenue Bills (Ksh. Millions)	Programme Based Budget (Ksh. Millions)	Office of the Controller of Budget (Actual in Ksh. Millions)	Deviation of the actual from the projections in the DORB (Ksh. Millions)	% growth
2017/18	462,243	649,396	517,161	54,918	12%
2018/19	641,514	850,011	826,202	184,688	29%
2019/20	538,802	696,554	707,892	169,090	31%
2020/21	829,906	904,000	-		

Source: Controller of Budget, National Treasury and Planning

73. This implies that additional borrowing has to be incurred or provision of quality services would be compromised. There was need for more accurate projections for proper planning purposes as well as observance of transparency in public debt contracting

74. **Pensions and other CFS Services have equally grown, and their administration is of concern:** As shown in the table below, servicing of non-discretionary CFS had grown at a high rate and that was limiting how much wass available for allocation to devolved services. The institute commended the National Treasury for rolling out

the super annuity Scheme for all civil servants below the age of 45 to ease the burden of pension payments in future.

Government Fiscal Framework- Pension and other CFS

Year	2016	2017	2018	2019	2020*
Pension and other CFS (Ksh billion)	64.0	65.1	70.8	89.6	123.4

Source: National Treasury and Planning -BPS 2019.2020,2021

75. The Institute also noted with concern that the payout amounts to retirees was below the budgeted amount. For instance, data from the National Treasury indicated that pension and gratuities paid to the retirees in the six months to December was 42.8 billion that represented 38.5% of the current year's retirements payouts budget pointing to delays in processing the claims. The Institute therefore recommended as follows;

- There should be transparency and accountability in processing and payment of pension and gratuities for the retirees as per the budget. Accurate schedule and proper records of retired personnel and amounts disbursed should be fast-tracked to aid early disbursement of such funds to the retirees who require them to better their livelihoods.
- Following the trend of budget for the payment of pensions and gratuities, it was projected that this cost could go even higher in the next five years. There was need for the management and administration of retirement benefits for employees to be transferred to the respective employment commissions. For instance, the pension for public servants should be administered by the Public Service Commission while that for teachers should be administered by the Teachers Service Commission, etc.

76. Progress of the Equalization Fund: Article 204 of the Constitution of Kenya 2010 establishes an equalization fund to provide basic services such as water, roads, health facilities and electricity to the marginalized areas as identified by the

Commission on Revenue Allocation. The fund has a 20-year period within which it should be operational. Time is thus a key factor in as far as the success of the fund is concerned. According to a report on the Consideration of the Equalisation Fund Bill by the Departmental committee on Finance and National Planning, the current composition of the Equalisation fund oversight Board was not been effective in administering the Fund. To this end, progress implementation reports should be publicly availed to provide the status of the projects financed by the Fund.

77. **Way forward for Nairobi City County:** There was need for clarity on how revenue would be allocated considering the transfer of four crucial functions (County Health Services; County Transport Services; County Planning and Development Services; and County Public Works, Utilities and Auxiliary services) to Nairobi Metropolitan Service. This was important to curb any stand-off between the County and NMS that could derail service delivery.

78. **Budget Transparency was critical for objective division of revenue:** The lack of a clear definition and objective criteria for determining national interest has been exploited by national government to starve counties of resources. Additionally, the framework for the management of conditional grants continues to be weak, and indeed does not meet the constitutional requirements for fiscal prudence and transparency.
    - The Division of Revenue bill should include performance and accountability information on conditional grants to adhere with constitutional and statutory requirements. For example, categorization of conditional grants in terms of their type, nature, administration and trends in allocations.
    - Prudent utilization of grants and access to information. Include key accountability information on conditional grants.
    - Establish explicit principles which inform conditional grants or transfers which are subject to specific conditions that may include; targets use, by sector or purpose; requirement for matching (i.e. matching grants) which require recipients to contribute part of costs; requirement to meet specified targets,

outputs or results; one off-funding or over a period, may be open ended, like the case with LATF but with requirements to achieve specified performance ratios e.g. debt, revenue etc

- On Performance evaluation there is a need to ensure that funds are traceable to avoid double funding and blurring of reporting. National departments must report to Parliament the outcome of grants allocated for specific purpose.

79. **Fiscal Accountability:** There was need to strengthen the fiscal accountability structures across both the national and county governments. The recommendations from oversight bodies including the Controller of Budget and the Auditor General should be followed so as to ensure prudent use of public funds. These include full compliance with the Public Financial Management Act (2012).

Submission by Mr. Robert Wakungwi Sakwa, Senior Medical Laboratory Scientist, Masinde Muliro University

80. Mr. Sakwa observed that considering the government focus on universal health coverage and enhanced reproductive health to the citizenry, and in view of the COVID 19 pandemic it would be wise to have sufficient man power to improve on evidence based medicine that is more objective as opposed to curative.

81. There have been efforts to engage intern Doctors, nurses and clinical officers but the engagement of medical laboratory personnel under the same arrangement for one year has not been forthcoming due to lack of attendant resources budgeting compromising diagnostic services across public health facilities.

82. He therefore proposed that the internship of medical laboratory personnel be considered and implemented this time round now that the SARS COV 2 transmission was actively in the community. The presence of intern diagnostic personnel within the community on a continuous basis as they work under mentorship and gain competence would assist in having youth develop skills to venture into the private sector later in case they fail to be absorbed into public service.

CHAPTER THREE

3.0 COMMITTEE OBSERVATIONS AND RECOMMENDATIONS

3.1 OBSERVATIONS

83. The Committee made the following observations/ findings-

a) That the proposed county equitable share is Ksh. 370 billion. This is in line with the Resolution on the Basis for allocating among the counties the share of national revenue annually allocated to county governments approved by the Senate on 17th September, 2020.

b) That some provisions contained in the Bill contravenes the Ruling in High Court Petition No. 252 of 2016. The ruling paragraph 72 stated-

> *"When allocating funds to the county level of government as either a conditional or non-conditional grant, it is expected that the allocation is made from the national level of government's share. Secondly, it is trite from the language used in Article 202 as read with Article 218(1)(a) of the Constitution,* ***conditional or non-conditional grants are not an item to be provided for under the Division of Revenue Act.*** *Conditional and non-conditional grants can be issued to the county level of government under the auspices of Article 190 of the Constitution or through an agreement between the two levels of government that respects the institutional and functional integrity of the either level of government."*

c) That the increment by Ksh. 1 billion to the MES programme was to cater for pending bills incurred by the Ministry of Health in the FY 2019/20. Thus, to ensure the contractual obligation was fulfilled, additional resources are required since pending bills must be treated as a first charge.

3.2 RECOMMENDATIONS

84. The Committee recommends-

a) the Division of Revenue Bill (National Assembly Bills No. 7 of 2021) be approved with the amendment to the schedule as follows; '*that the schedule to the bill be deleted and substituted therefor with new schedule as attached here below.*'

Type/level of allocation	Amount in Ksh.	Percentage (%) of 2016/17 audited and approved revenue i.e. Ksh. 1,357,698 Million
A. Total Sharable Revenue	1,775,624,173,860	
B. National Government	1,398,798,856,427	
C. Equalization Fund	6,825,317,433	0.50%
D. County equitable share	370,000,000,000	27.3%

This recommendation is in compliance with the Ruling in High Court Petition No. 252 of 2016, where the court held that it cannot be permissible to provide for conditional grants in the Division of Revenue Act and therefore it follows that conditional grant cannot be proposed in Division of Revenue Bill.

b) An enactment of bill to provide for a legal mechanism to enable the transfer of conditional grants to the respective County Revenue Funds (CRFs) and withdrawal from CRFs by county governments. The Bill should also provide a framework for the management, control and accounting for conditional and unconditional grants.

c) That the proposed nascent legal instrument will address the modalities of allocation, expenditure and reporting on conditional grants to county governments. It will therefore be within the purview of Article 110(4) of the Constitution.

APPENDIXES

(a) **Committee Stage Amendments**

(b) **Minutes of the Committee sittings**

(c) **Submission from Public Institutions and Members of Public**

12th April, 2021

The Clerk of the Senate
Parliament Buildings
NAIROBI

RE: COMMITTEE STAGE AMENDMENTS TO THE DIVISION OF REVENUE BILL, NATIONAL ASSEMBLY BILLS NO. 7 OF 2021

NOTICE is given that Sen. Charles Kibiru, MP, Chairperson, Committee on Finance and Budget intends to move the following amendment to the Division of Revenue Bill, National Assembly Bills No. 7 of 2021, at the Committee Stage-

SCHEDULE
THAT the Bill be amended by deleting the schedule and substituting therefor the following new schedule-

SCHEDULE (s.4)
ALLOCATION OF REVENUE RAISED NATIONALLY BETWEEN THE NATIONAL AND COUNTY GOVERNMENTS FOR THE FINANCIAL YEAR 2021/22.

Type/level of allocation	Amount in Ksh.	Percentage (%) of 2016/17 audited and approved Revenue i.e. Ksh. 1,357,698 Million
A. Total Sharable Revenue	1,775,624,173,860	
B. National Government	1,398,798,856,427	
C. Equalization Fund	6,825,317,433	0.50%
D. County equitable share	370,000,000,000	27.3%

Dated **12th April, 2021**

Charles Kibiru,
Chairperson, Committee on Finance and Budget.

International Budget Partnership

Kenya

MEMORANDUM TO THE SENATE ON THE DIVISION OF REVENUE BILL (NATIONAL ASSEMBLY BILLS NO. 7 OF 2021) FOR FY 2021/2022

07 APRIL 2021

This memorandum has been prepared by the International Budget Partnership Kenya (IBP Kenya). 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 focuses 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, generation of evidence, and technical assistance to both governments and CSOs, learning, and networking are integral components of IBP Kenya's work.

Just like the Division of Revenue Bill 2020, the preparation of the Division of Revenue Bill 2021 comes at a time of tight fiscal stress in the country amidst grave effects of the coronavirus pandemic. One year on, the spread of the virus has continued to affect international and local trade directly. Many countries continue to enforce stringent measures that include restrictions on travel, partial and total national lockdowns, and curfews to contain the spread of the virus's new variant strains. The ripple effect has been a decline in critical sectors' performance in affected economies such as tourism and hospitality, transport, capital markets, and trade, among others. Parliament should guide the country in enacting policies that will make life manageable for all Kenyans, especially those in low-income status.

In this memorandum, we raise the following key issues:

1. The allocations to counties are declining, and this will affect services. Parliament needs to address this situation not to lose the gains already made through public services' devolution.
2. Public debt, pensions, and other charges of the consolidated fund services are crowding out the amount available for sharing and hurting counties allocation.
3. Unrealistic revenue projection has negatively affected revenue sharing.
4. Lack of transparency, accountability, and meaningful public engagement is affecting the division of the revenue process.

Submissions

1. **Despite devolution being an essential aspect of Kenya's service delivery, the allocations to the county governments have been declining.** As Table 1 below shows, while the growth in national revenue has remained stable over time, except for FY 2020/2021 and FY 2021/2022 due to the COVID-19 pandemic, the amounts approved to counties as a proportion of national revenue has been declining. However, this year will see a 17% percent growth in allocations despite a projected decline of 4% in ordinary revenue, which does not reflect a realistic situation. We propose that parliament arrests this state.

2. **Conditional Grants for the construction of county headquarters need to be clarified**. We note that the Division of Revenue Bill 2021 has allocated Kshs. 332 million towards the construction of county government headquarters for five counties, namely, Isiolo, Lamu, Nyandarua, Tana River, and Tharaka Nithi. There's a need for clarity on the criteria used to identify the counties and the amount allocated to each. From the Bill, it is clear that these are still the five counties that received a similar grant in the previous financial years. For instance, the Division of Revenue Bill 2020 allocated Kshs. 300 million to these counties. It will be good to know how far have their construction gone. An annexure of the same should provide the requisite information that indicates the progress made over the years. We urge the Senate to compel the National Treasury to provide an annex with detailed information on the above.

3. **There is no apparent growth factor in the division of revenue allocation basis. This leaves it to individual actors in the national government to decide how much should be allocated to county governments.** As Table 1 shows, except for FY 2015/2016, Commission on Revenue Allocation (CRA) and the National Treasury have always used different factors to determine how they share of county governments should grow. Of great concern is the allocation for FY 2021/2022, which is arbitrary and has no basis given the declining ordinary revenue occasioned by the Covid-19 pandemic. Given *Figure 1* below, as much as the increase of Ksh. 53.5 billion was a condition for the approval of the Third Basis for Revenue Allocation; there was no explanation on how it was arrived at. As Parliament considers this Bill, we propose that the growth factor or the criteria for determining the same be established and made clear. Therefore, we propose that as a minimum, allocations to county governments should be informed by the three-year average growth of ordinary national revenue.

Figure 1: Basis for Increase of Equitable Share by Ksh. 53.5 billion

County Governments' Equitable Share

6. The Bill proposes to allocate County Governments' an equitable share of revenue raised nationally for the financial year 2021/22 of Ksh. 370 billion. This is premised on Parliament having approved the third basis for allocation of the share of national revenue among the County Governments in September, 2020 on condition that the formula's implementation would be preceded by a Kshs. 53.5 billion increase in the Counties' equitable revenue share.

Source: Division of Revenue Bill 2021

Table 1: Division of Revenue 2015-2021

	Proposed Growth		Basis for Proposed Revenue Growth							
Year	CRA	National Treasury	CRA	National Treasury	Ordinary Revenue	*Growth in National Ordinary Revenue*	Equitable Share Approved in the DoR (2021/22 is proposed)	Growth in DOR approved Amounts (2021/22 is proposed)	Sharable Revenue (KES Billion)	Equitable share as a % of Sharable Revenue
2014/15							226.66		1,031.80	22%
2015/16	10.4%	10.4%	3-Year average growth in ordinary revenue	3-Year average growth in ordinary revenue	1,152.97	*13%*	259.77	15%	1,251.67	21%
2016/17	15.0%	7.8%	3-Year average growth in ordinary revenue	Not provided	1,306.57	*13%*	280.30	8%	1,380.20	20%
2017/18	15.0%	6.7%	3-Year average growth in ordinary revenue	3-Year average month on month inflation	1,365.06	*4%*	302.00	8%	1,549.41	19%
2018/19	8.5%	4.0%	3-Year average inflation	Not Clear	1,496.93	*10%*	314.00	4%	1,681.07	19%
2019/20	6.9%	2.0%	3-Year average inflation	Not Clear	1,843.81	*23%*	316.50	1%	1,877.18	17%
2020/21	5.7%	0.0%	The country's 3-year (2016-2018) average economic growth	Not Clear	1,856.71	*1%*	316.50	0%	1,857.00	17%
2021/22	3.2%	16.9%	Not Clear	Not clear	1,775.60	*-4%*	370.00	17%	1,775.60	21%

4. **Public debt, pensions, and other charges of the consolidated fund services are crowding out the amount available for revenue division and hurting counties allocation.**
As Table 2 below shows, total debt service has been growing at a very high rate, limiting how much is available for allocation to devolved services. The growth in county allocation over the years has been very minimal, which affects service delivery. We also note that the growth in ordinary revenue has been very marginal. More importantly, while public borrowing directly impacts the size of the shareable revenue, the National Treasury is the only body deciding on this vital national instrument. We recommend that counties and the Senate be involved in the discussion on national borrowing as that impacts the revenue shared between the two levels of government.

Table 2: Servicing of non-discretionary Consolidated Fund Services

Year	Total Debt Service	Ordinary Revenue	Counties' Allocation	Growth in Total Debt Service	Growth in Ordinary revenue	Growth in County Allocation
2014/15	392.2	1,032	226.66			
2015/16	427.6	1,153	259.77	9%	12%	15%
2016/17	463.2	1,306	280.3	8%	13%	8%
2017/18	598.5	1,486	302	29%	14%	8%
2018/19	850.1	1,688	314	42%	14%	4%

2019/20	651.5	1,573	316.5	-23%	-7%	1%
Average				**13%**	**9%**	**7%**

Source: Public Debt Management Report for 2019/2020 and Division of Revenue Acts (2014-2020)

5. **Pensions and other CFS Services have equally grown, and their administration is of concern.** Pension is a non-discretionary obligation that has a bearing on the size of revenue that is eventually shared between the two government levels. The higher the share of ordinary revenue taken up by these national obligations, the lower the shareable revenue and allocations to counties. An analysis of government expenditure on pensions between 2016-2021 indicates an increasing trajectory over time, as illustrated in Table 3.

Table 3: Government Fiscal Framework- Pension and other CFS

Year	2016	2017	2018	2019	2020	2021
Pension and other CFS	43,429 Millions	60,169 Millions	91.1 Billions	109.5 Billions	118.7 Billions	137.0 Billions

Source: Budget Policy Statements 2016-2021

6. **The National interest allocations take a considerable portion of the shareable revenue** and have only substantially declined in 2020/21 and will further decline in 2021/22.

NATIONAL INTEREST ALLOCATIONS (Ksh. Million)										
	2017/18		2018/19		2019/20		2020/21		2021/22	
Ordinary Revenue	1,365,063		1,499,757		1,573,418		1,574,009		1,775,624	
		Share of Ordinary Revenue		Share of Ordinary Revenue		Share of Ordinary Revenue		Share of Ordinary Revenue		Share of Ordinary Revenue
National Interest	82,696	6.1%	84,186	5.6%	94,168	6.0%	86,753	5.5%	83,197	4.7%

Source: Allocation Data - Division of Revenue Bill, 2021

Senate should concern itself with the allocation growth factor of the items within the National interest component. Ordinary revenue has grown by 37 percent from 2015/16, with National interest allocations growing by 10 percent, which is quite significant.

ITEM DESCRIPTION (KSh. Millions)	FY 2015/16	FY 2016/17	FY 2017/18	FY2018/19	FY2019/20	2020/21	2021/22	Growth over years. FY 2016/17	FY 2017/18	FY 2018/19	FY 2019/20	2020/21	2021/22	Growth Between 2020/21 and 2015/16
ORDINARY REVENUE (EXCLUDING AIA)	**1,152,972**	**1,306,568**	**1,365,063**	**1,651,517**	**1,877,176**	**1,574,009**	**1,775,624**	**13.3%**	**4.5%**	**21.0%**	**13.7%**	**-16.2%**	**12.8%**	**37%**
National Interest [Article 203 (I)(a)]	79,189	79,685	82,696	84,186	94,168	86,753	83,197	0.6%	3.8%	1.8%	11.9%	-7.9%	-4.1%	**10%**
Enhancement of security operations (police vehicles, helicopters, defence etc.)	17,700	18,900	20,556	27,800	27,974	24,816	22,261	6.8%	8.8%	35.2%	0.6%	-11.3%	-10.3%	**40%**
National irrigation and fertilizer clearance	12,500	8,700	8,880	11,775	11,103	11,375	11,199	-30.4%	2.1%	32.6%	-5.7%	2.4%	-1.5%	**-9%**
Youth empowerment	17,055	18,544	18,544	7,442	16,226	16,127	14,548	8.7%	0.0%	-59.9%	118.0%	-0.6%	-9.8%	**-5%**
National social safety net - (for older persons, OVC, child welfare, presidential bursary, severe disability)	14,354	16,924	17,305	26,812	26,362	28,832	29,286	17.9%	2.3%	54.9%	-1.7%	9.4%	1.6%	**101%**
Primary school digital literacy program	17,580	13,408	13,408	6,333	8,400	1,500	1,800	-23.7%	0.0%	-52.8%	32.6%	-82.1%	20.0%	**-91%**
School examination fees (KSCE and KCPE)	-	3,209	4,003	4,024	4,103	4,103	4,103	-	24.7%	0.5%	2.0%	0.0%	0.0%	**28%**
COUNTY GOVERNMENT ALLOCATION FROM REVENUE RAISED NATIONALLY, of which;-	273,073	295,020	314,205	322,193	323,911	330,231	377,537	8.0%	6.5%	2.5%	0.5%	2.0%	14.3%	**21%**
a)Equitable Share of Revenue	259,775	280,300	302,000	304,962	310,000	316,500	370,000	7.9%	7.7%	1.0%	1.7%	2.1%	16.9%	**22%**
b)Additional conditional allocations financed from revenues raised nationally	13,298	14,720	12,205	17,231	13,911	13,731	7,537	10.7%	-17.1%	41.2%	-19.3%	-1.3%	-45.1%	**3%**

Source: Allocation Data - Division of Revenue Bill, 2021

The National interest items are not reflective of the inter-county/regional issues. Senate should advocate for regional public service issues to be incorporated herein. Case in point, the third-generation revenue sharing formula uses county-specific parameters to divide resources. Services such as health services at level 5 are to the benefit of regions. Are individual counties expected to foot this bill? Having counties take responsibility for such is not in line with funds following functions. Other issues such as shared inter-county resources, e.g., development of water points, should also be considered under National interests.

7. **Recommendations by CRA on harmonization of functions should be used to justify the adjustment of equitable share.** As highlighted in Figure 2 below, CRA made a recommendation to harmonize functions as provided for in the fourth schedule of the Constitution be used as a basis for increasing the equitable share. We welcome this recommendation and urge Parliament to consider this approach to ensure that funds follow functions assigned to the county governments.

Figure 2: Recommendations of the CRA and the National Treasury

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Table 3: Recommendations of the CRA and the National Treasury (Kshs. Million)

Expenditure Item	CRA	National Treasury	Variance
	A	B	C=(A-B)
1. Equitable Revenue Share in FY 2020/21 (Base)	316,500	316,500	-
2. Adjustment for revenue growth FY 2021 as determined in the Fiscal Framework	-	36,100	(36,100)
3. Conversion of conditional grants to Equitable Share, i.e. Level -5, RMLF, User fees foregone and village Polytechnics	17,020	17,400	(380)
4. Harmonisation of functions in line with the fourth Schedule of the Constitution and Article 187(2)	36,480	-	36,480
TOTAL EQUITABLE SHARE OF REVENUE = (1+2+3+4)	**370,000**	**370,000**	-

Source: National Treasury and Planning

8. **Lack of transparency, accountability, and meaningful public engagement is affecting the division of the revenue process**

Although Parliament has embraced public participation in the legislative process and made efforts towards facilitating public participation, public engagement in the division of revenue process is not effective but tokenistic and inconsequential in the ultimate decision-making process. In some instances, Parliament does not explain its actions or give reasons for certain decisions. For example, on 09 March 2021, Parliament approved to reduce the Division of Revenue Bill's publication time from 7 days to 1 day. This may be well within the standing orders of the Parliament, but such actions need to be explained for the public to understand why the decision was made.

Over the years, civil society organizations have raised concerns on the issues mentioned above, which have never been adequately addressed. There is a need for clear guidance on how the public should engage during the division of the revenue process to influence decisions made and the kind of information that government institutions should provide to enable the citizens to engage accordingly. Besides, a feedback mechanism is required informing on how submissions and inputs from the public are handled. Pursuant to Article 201of the Constitution and Section 35(2) of the Public Finance Management Act, the Cabinet Secretary should enact regulations to provide for meaningful public participation in the national budget and include sanctions for failure to undertake meaningful public participation in the budget process, including division of revenue process.

9. **The realism of the revenue forecast remains a gamble.** We note that revenue forecasts at both the national and county level have been ambitious and often led to budget deficits. We are concerned with the accuracy and the ambitious nature of the National Treasury's revenue projections. This is exacerbated by the failure of the Tax Authority to meet the set targets over the years. This will need to be further revised due to the effect of COVID-19 on Kenya's economic productivity. A trend analysis of revenue growth is critical in informing revenue projections for the coming years. Kenya's budget process has inadequately facilitated accurate forecasts for resource collection. Therefore, the common tendency has been to make overly optimistic revenue projections leading to increased uncertainty of resource flows. An analysis of total revenue collection, including Appropriation in Aid (A. i. A), shows shortfalls in each financial year since 2015, as seen in Table 4 below.

Table 4: Performance of Total Revenue including A-i-A (Figures in Billions of Kshs)

Year	Dec-15	Sep-16	Nov-17	Nov-18	Dec-19	Feb-21
Target Revenue	642.9	328	611	677	1059.3	907.7
Actual	575.2	313.6	558.4	633.7	920.6	810.6
Shortfall	67.7	14.4	52.6	43.3	138.7	97.1

Source: National Treasury- Budget Policy Statements 2016-2021

10. **Conversion of Conditional grants to unconditional grants leaves more questions to be answered –** The four converted conditional grants are being left at the discretion of counties. However, how have the initial directives that were behind the establishment of the conditional grants dealt with? For instance, what will be the impact on actual service delivery in the primary health facilities after scrapping the conditional grant on user fees forgone? This will risk the funds being diverted to other departments since there are no mechanisms put in place to ring-fence the unconditional grants to the counties.

	Grants converted to Unconditional Grants							
	Current Conditional Grants (Billions)	2015/16 DORA	2016/17 DORA	2017/18 DORA	2018/19 DORA	2019/20 DORA	2020/21 DORA	2021/22 DORB
1	Level 5 hospitals	3.6	4.0	4.2	4.3	4.3	4.3	17.4
2	Compensation for user fees forgone	0.9	0.9	0.9	0.9	0.9	0.9	
3	Development of Youth Polytechnics			2.0	2.0	2.0	2.0	

4	Road Fuel Levy Fund (RMLF)	3.3	4.3	11.1	8.3	9.0	9.4	
	Total	***7.8***	***9.2***	***18.2***	***15.5***	***16.1***	***16.6***	***17.4***

The conditional grants to the Level 5 Hospitals will be shared across all 47 Counties. This means that there will be some reduced funding to the 11 counties receiving the grant. The unanswered question is, what will happens to the funding gaps occasioned by this conversion?

Level 5 Hospital Conditional Grants (KShs. Billion)								
	County	2013/14	2014/15	FY 2015/16	FY 2016/2017	FY 2017/18	FY 2018/19	FY 2019/20
1	Embu	0.26	0.19	0.19	0.29	0.30	0.30	0.30
2	Garissa	0.18	0.11	0.36	0.33	0.34	0.34	0.34
3	Kakamega	0.31	0.21	0.34	0.41	0.43	0.43	0.43
4	Kiambu	0.37	0.09	0.33	0.39	0.41	0.54	0.54
5	Kisii	0.21	0.08	0.34	0.40	0.42	0.42	0.42
6	Kisumu	0.40	0.25	0.34	0.35	0.37	0.37	0.37
7	Machakos	0.11	0.16	0.30	0.37	0.38	0.38	0.38
8	Meru	0.18	0.06	0.24	0.36	0.37	0.37	0.37
9	Mombasa	0.41	0.21	0.40	0.37	0.39	0.39	0.39
10	Nakuru	0.60	0.32	0.38	0.36	0.37	0.37	0.37
11	Nyeri	0.38	0.20	0.37	0.39	0.41	0.41	0.41
	Total	**3.42**	**1.87**	**3.60**	**4.00**	**4.20**	**4.33**	**4.33**

Source: County Allocation Revenue Acts

11. A significant proportion of the budget is left to donor grants and loans and for very vital services. Over the past three financial years, donor grants have been above KShs. 30 billion, and there is a need to understand their sustainability plan, specifically assessing the impact on the services under these grants. Further, there is a need to provide the total amount schedule, and the relevant future years should be included in the memoranda to give a complete picture.

Conditional Allocations Loans and Grants -Development Partners (KShs. Billion)			
FY 2018/19	FY 2019/20	FY 2020/21	FY 2021/22
36.9	39.1	30.2	32.3

Source: OCOB Quarter Reports & DORBills

Signed

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COMMISSION ON REVENUE ALLOCATION

OUR REF. CRA/14/Vol.6(21) **DATE:** 06 April 2021

Mr. J. M. Nyegenye,
Clerk of the Senate,
Clerk's Chambers
Parliament Buildings
NAIROBI

Dear Mr. Nyegenye

RE: THE COMMISSION CONSIDERATIONS ON (DIVISION OF REVENUE BILL (THE NATIONAL ASEMBLY BILLS No.7 OF 2021)

The Commission on Revenue Allocation is mandated by Article 216 (1)(a) of the Constitution to make a recommendation concerning the basis for the equitable sharing of revenue between the national and county governments.

In this regard, the Commission in accordance with the provisions of Article 205, has considered the provisions of the National Assembly Bill No. 7 of 2021 on the division of revenue between the national and county governments and in particular, inclusion of conditional grants in the Division of Revenue Bill, the alternative mechanism for disbursement of conditional grants and the increased allocations to the conditional grant on leasing of medical equipment programme, and hereby submit the attached considerations.

Yours Sincerely,

Dr. Jane Kiringai, EBS
CHAIRPERSON

Att//01

Attachment/01

Promoting an Equitable Society

MEMORANDA ON THE DIVISION OF REVENUE BILL (NATIONAL ASSEMBLY BILLS NO. 7 OF 2021)

In accordance with the requirements of Article 205 of the Constitution, the Commission on Revenue Allocation has considered the provisions of the Division of Revenue Bill (National Assembly Bills No. 3 of 2020) and make the follows observations:

1. **Inclusion of conditional grants in DORB**
   In line with the Court ruling on **Petition no. 252 of 2016**, *conditional or non-conditional grants are not items to be provided for under the Division of Revenue Act.*
   Implications of the ruing:
   a) *The Division of Revenue Act should only reflect the equitable share allocations between the two levels of government, and*
   b) *That conditional and unconditional grants have to be provided for through an alternative intergovernmental transfer framework*

2. **Alternative Mechanisms for disbursement for Conditional Grants**
   *Based on the following rulings (***Petition no. 252 of 2016***):*
   a) *That the national government cannot allocate itself funds and undertake devolved functions without first executing inter-government agreements under Article 187 of the Constitution,*
   b) *That following from (a) above, the national government's accounting officers' cannot spend money for conditional grants directly in the Counties to undertake devolved functions unless there is an agreement transferring functions under Article 187, 189 or 190 of the Constitution and section 21 of the County Government Act,*
   c) *That there ought to be a framework stating the purpose, the goal and the mechanism for the issuance of the conditional grant,*
   d) *that all funds under Article (202) (2) of the Constitution (conditional or non-conditional) must be channelled through the*

County Revenue Fund (CRF) to the specific counties for the specific functions outlined by the national level of government,

e) *The said funds should be channelled directly to the activities in question and accounted for, and*

f) *that conditional and unconditional funds cannot be appropriated by the County Assembly through a County Appropriation Bill.*

Implications of the rulings:

a) *That the relevant Ministry, Department or Agency under which the grants are accounted for should provide a schedule of disbursement to each of the county governments based on an agreed intergovernmental transfer framework*

b) *That the National Assembly has to approve the appropriation of the conditional and unconditional grants given that funds are being channelled directly to the activities in question and accounted for by the national government.*

3. Increased allocation to Leasing of Medical Equipment Scheme

a) *The Commission was not part of the signed contractual obligations between the National Government, County Governments and the provider of the Medical Scheme.*

b) *The Council of Governors, the Ministry of Health and the National Treasury are better placed to provide more information on why the allocations for the payments keeps on varying from one year to another.*

c) *The Commission's understanding is that whilst the contracted amount remains the same, the annual variations may be informed by the nature and the number of the equipments being availed by the provider each year.*

ICPAK SUBMISSION ON THE DIVISION OF REVENUE BILL 2021

6TH APRIL 2021

Introduction

The Institute of Certified Public Accountants of Kenya (ICPAK) is a statutory body of accountants established under by the Accountants Act of 1978, and repealed under the Accountants Act Number 15 of 2008, mandated to develop and regulate the Accountancy Profession in Kenya. It is also a member of the International Federation of Accountants (IFAC), the global umbrella body for the accountancy profession. The Institute is further mandated under Section 8 of the Act to advise the Cabinet Secretary on matters relating to financial accountability in all sectors of the economy

The Institute would first and foremost like to appreciate the two Houses and the Executive for reaching a consensus on the 3rd basis of revenue sharing on September of 2020 which has consequently increased the total equitable share. This Bill comes amidst fiscal stress in the country exacerbated by the COVID-19 crisis which has ravaged almost all sectors of the economy including transport, trade, hospitality among others. Some of the issues herein were aptly raised in our earlier memoranda including the DORB 2020 submission.

In this memorandum we raise the following key issues:

1. Basis for revenue projections
2. Leasing of medical equipment
3. Conditional grants
4. Public debt, pensions, and other charges of the consolidated fund services
5. Status of Nairobi City County
6. Equalization Fund
7. Budget transparency and National Interest
8. Strengthen fiscal accountability.

Detailed Submissions

1. Basis for revenue projections:

Kenya has consistently registered a positive growth in its revenue collection with it doubling from Ksh. 0.7 Trillion in FY 2011/12 to Ksh. 1.5 Trillion over a seven-year period (2018/19) (KRA, 2019). However, the actual revenue receipts have continuously fallen below the targets (KNBS, 2020). Coming from a global pandemic that necessitated most governments, the Kenyan one included, to adopt expansionary fiscal policy measures, it is highly unlikely that in the coming FY 2021/22, the Kenyan economy will have rebounded. The Government should therefore conduct a trend analysis of revenue growth to inform revenue projections for the subsequent years.

Table 1: Revenue Projections vs Actual Collections 2012-2019

Year	Total Exchequer Revenue (Ksh millions)	Ordinary Revenue Estimates (Ksh millions)
2013/14	918,982	**1,006,404**
2014/15	1,021,974	**1,070,515**
2015/16	1,136,833	**1,184,368**
2016/17	1,273,060	**1,380,199**
2017/18	1,340,248	**1,560,276**
2018/19	1,474,673	**1,688,492**

Year	Total Exchequer Revenue (Ksh millions)	Ordinary Revenue Estimates (Ksh millions)
2019/20	1,607,000	**1,776,637**
2020/21		**1,883,694**

Source: Kenya Revenue Authority Annual report FY 2018/19 and 2019/20 & the National Treasury – BPS

The ambitious revenue forecast has among other ramifications contributed to budget deficits which have in turn worsened the pending bills problem.

- A special audit by Office of the Auditor General (OAG) verified eligible pending bills by County Governments amounting to Ksh.51.2 billion as at 30th June 2018 and another Ksh.37.7 billion worth of pending bills was found to be ineligible for payment due to lack of documentation to support services rendered or work done.
- A report by the Controller of Budget (CoB) indicates that by 10th November 2020, the Counties had settled Ksh.39.07 billion (76.2% of the eligible pending bills) leaving an outstanding balance of Kshs.12.22 billion.
- According to the Kenya Enterprise Survey 2018, approximately 12% of the 1,001 firms surveyed have had a contract with government that was in arrears.

The government should therefore review realism of revenue forecasts for predictability in expenditure across the two levels of government.

2. Inadequate utilization of the Leased medical equipment:

The conditional allocations are tied to the implementation of specific national policies, and are mainly from both government and donor community. One of the items catered for is the leasing of medical equipment, which has been receiving allocation from the FY 2015/16.

- The grant is managed by the national government and is aimed at facilitating the county governments to acquire modern specialized medical equipment for two level 4 health facilities in each county with a focus on theatre, central sterile services department (CSSD), renal, ICU and radiology equipment. This was expected to ease access to specialized healthcare services at county level as well as reduce travel distances by Kenyans in search of the services.
- However, a Senate report on 'The Managed Equipment Service (MES) Project' indicates that the equipment have been under-utilized owing to inadequate health personnel and insufficient infrastructure (water and electricity).
- The report also highlights the exaggerated cost of equipment supplied in comparison to prevailing market rates.

- There is need to provide capacity strengthening sessions to the health personnel and fast-track the development of the required infrastructure in the respective health facilities.

Table 2: Amounts allocated towards the Leasing of Medical Equipment

FY	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Amount (Ksh. In millions)	3,080	4,500	4,500	9,400	6,200	6,205	7,205

Source: Division of Revenue Acts and Bills 2015-2020

3. Conditional Grants for construction of county headquarters need to be clarified and accounted for:

In the FY 2017/18, 5 counties (Isiolo; Lamu; Nyandarua; Tana River and Tharaka Nithi) were identified as being the only counties that did not inherit adequate office space for county headquarters and thus would be allocated funds to construct their headquarters over the span of three financial years (between 24-32 months).

According to a report on County Infrastructure by the Senate Standing Committee on Finance and Budget, the State Department of Public Works submitted that the implementation of this project would be carried out through the Ministry with the National Government contributing 70% of the amount while counties contribute the remaining 30%. The first disbursement of the agreed Ksh 518 million for construction of their headquarters was received in FY2017/18 therefore, the final disbursement should have been in the FY 2019/20. Despite this, we note that DORB 2020 and 2021 still allocated the counties the amounts Ksh 300 million and Ksh 332 million respectively as shown in the table below.

Table 3: Allocation towards construction of county Headquarters

Financial Year	Allocation towards construction of county HQs (Ksh million)
2017/18	605
2018/19	605
2019/20	485
2020/21	300
2021/22	332

Source: Division of Revenue Bills, 2017 -2021

- There is thus need for an implementation report on the same to justify the continued allocation.

- Need for an indication on completion of this project.

4. **Consider conditional Allocation to support ECDE:**

In a Devolution Survey 2020 conducted by the Institute, several challenges were documented that are impeding the successful delivery of educational services, especially at the county level:

- high turnover rates for Early Child Development Education (ECDE) teachers
- low funding for ECDE, inadequate investment in succession planning within departments, low and unclear scheme of service for ECDE teachers,
- Inadequate infrastructure to support the learning of children living with disability; and
- inadequate number of trained instructors in most polytechnics.

There's need to provide conditional allocation to ECDE for purposes of the following:

a) increasing capitation for ECDE teachers
b) Employment of skilled and qualified instructors in polytechnics;
c) To support development of adequate monitoring and assessment of performance (quality assurance) of learning at that level.

5. **Actual public debt service figures have always been higher than the projections:**

As the table below indicates, the public debt repayment projections contained in the division of revenue bills have always been lower than what is contained in the programme-based budget documents. These figures have further been lower than the actual ones contained in the national government implementation review reports. In addition to this, the deviation of the projected amounts as contained in the division of revenue bills from the actual show an increasing trend which shows that the projections are highly underestimated.

This implies that additional borrowing has to incurred or provision of quality services will be compromised. There is need for more accurate projections for proper planning purposes as well as observance of transparency in public debt contracting.

Table 4: Public debt projections vs actual

FY	Division of Revenue Bills (Ksh. Millions)	Programme Based Budget (Ksh. Millions)	Office of the Controller of Budget (Actual in Ksh. Millions)	Deviation of the actual from the projections in the DORB (Ksh. Millions)	% growth
2017/18	462,243	649,396	517,161	54,918	12%
2018/19	641,514	850,011	826,202	184,688	29%
2019/20	538,802	696,554	707,892	169,090	31%
2020/21	829,906	904,000	-		

Source: Controller of Budget, National Treasury and Planning

6. Public debt repayment is crowding out the amount available for division of revenue and hurting counties allocation: Public borrowing has a very direct impact on the size of the sharable revenue as shown in the table below. On average, public debt servicing growth is higher at 30% than the growth in both the shareable revenue (7%) and the county allocation (5%). We call on the National Treasury to contract more loans from the multilateral lenders than from commercial lenders who are usually more expensive as compared to the former.

Since the National Treasury is the only body deciding on this vital national instrument, we recommend that counties through the Senate should be involved in the discussion on national borrowing as that has an impact on the revenue that is shared between the two levels of government.

Table 5: Growth in Public debt, ordinary revenue and counties allocation

FY	Public Debt Service (Ksh. Billions)	Ordinary Revenue (Ksh Billions)	Counties Allocation (Ksh Billions)	Growth in Public Debt Service	Growth in Shareable Revenue	Growth in County Allocation
2017/18	462.24	1365.06	302.00			
2018/19	641.51	1499.76	304.96	39%	10%	1%
2019/20	538.80	1573.42	310.00	-16%	5%	2%
2020/21	829.91	1574.01	316.50	54%	0%	2%
2021/22	1174.01	1775.62	370.00	41%	13%	17%
Average				**30%**	**7%**	**5%**

Source: Division of Revenue Bill 2021

7. **Pensions and other CFS Services have equally grown, and their administration is of concern:**

As the table 6 below shows, servicing of non-discretionary CFS has been growing at a high rate and that is limiting how much is available for allocation to devolved services. We commend the National Treasury for rolling out the super annuity Scheme for all civil servants below the age of 45 to ease the burden of pension payments in future.

Table 6: Government Fiscal Framework- Pension and other CFS

Year	2016	2017	2018	2019	2020*
Pension and other CFS (Ksh billion)	64.0	65.1	70.8	89.6	123.4

Source: National Treasury and Planning -BPS 2019.2020,2021

The Institute also notes with concern that the payout amounts to retirees is usually below the budgeted amount. For instance, data from the National Treasury indicates that pension and gratuities paid to the retirees in the six months to December was 42.8 billion representing 38.5% of the current year's retirements payouts budget pointing to delays in processing the claims. The Institute therefore recommends as follows;

- There should be transparency and accountability in processing and payment of pension and gratuities for the retirees as per the budget. Accurate schedule and proper records of retired personnel and amounts disbursed should be fast-tracked to aid early disbursement of such funds to the retirees who require them to better their livelihoods.
- Following the trend of budget for the payment of pensions and gratuities, it is projected that this cost could go even higher in the next five years. There is need for the management and administration of retirement benefits for employees to be transferred to the respective employment commissions. For instance, the pension for public servants should be administered by the Public Service Commission while that for teachers should be administered by the Teachers Service Commission, etc.

8. **Progress of the Equalization Fund:**

Article 204 of the Constitution of Kenya 2010 establishes an equalization fund to provide basic services such as water, roads, health facilities and electricity to the marginalized areas as identified by the Commission on Revenue Allocation. The fund has a 20-year period within which it should be operational. Time is thus a key factor in as far as the success of the fund is concerned. According to a report on the Consideration of the Equalisation Fund Bill by the Departmental committee on Finance and National Planning, the current composition of the Equalisation fund oversight Board has not been effective in administering the Fund.

- To this end, progress implementation reports should be publicly availed to provide the status of the projects financed by the Fund.

Table 7: Equalisation fund allocations

Year	2014	2015	2016	2017	2018	2019	2020	2021
Amount (Ksh billions)	3.4	6.0	6.0	7.73	4.7	5.76	6.79	6.83

Source: Division of Revenue Bill 2014 – 2021

9. Way forward for Nairobi City County:

There is need for clarity on how revenue will be allocated considering the transfer of functions four crucial functions (County Health Services; County Transport Services; County Planning and Development Services; and County Public Works, Utilities and Auxiliary services) to Nairobi Metropolitan Service. This is important to curb any stand-off between the County and NMS that could derail service delivery.

10. Budget Transparency is critical for objective division of revenue:

The lack of a clear definition and objective criteria for determining national interest has been exploited by national government to starve counties of resources. Additionally, the framework for the management of conditional grants continues to be weak, and indeed does not meet the constitutional requirements for fiscal prudence and transparency.

- The Division of Revenue bill should include performance and accountability information on conditional grants to adhere with constitutional and statutory requirements. For example, categorization of conditional grants in terms of their type, nature, administration and trends in allocations.
- Prudent utilization of grants and access to information. Include key accountability information on conditional grants.
- Establish explicit principles which inform conditional grants or transfers which are subject to specific conditions that may include; targets use, by sector or purpose; requirement for matching (i.e. matching grants) which require recipients to contribute part of costs; requirement to meet specified targets, outputs or results; one off-funding or over a period, may be open ended, like the case with LATF but with requirements to achieve specified performance ratios e.g. debt, revenue etc
- On Performance evaluation there is a need to ensure that funds are traceable to avoid double funding and blurring of reporting. National departments must report to Parliament the outcome of grants allocated for specific purpose.

11. Fiscal Accountability:

There is need to strengthen the fiscal accountability structures across both the national and county governments. The recommendations from oversight bodies including the Controller of Budget and the Auditor General should be followed so as to ensure prudent use of public funds. These include full compliance with the Public Financial Management Act (2012).

REPUBLIC OF KENYA

THE NATIONAL TREASURY & PLANNING

The Proposed Division of Revenue Bill, 2021

Brief by the Cabinet Secretary, National Treasury and Planning
During a Meeting with the Senate Standing Committee on Finance and Budget

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April 7th, 2021

INTRODUCTION

This brief is informed by the invite to the Cabinet Secretary/ National Treasury and Planning by the Standing Committee on Finance and Budget of the Senate to deliberate on the proposed Division of Revenue Bill, 2021, in light of the High Court Ruling on Petition No. 252 of 2016 on Division of Revenue Act, 2016. The issues for deliberation at the meeting include-

1. The inclusion of conditional grants in the Division of Revenue Bill;
2. The alternative mechanism for disbursement of conditional grants to counties if they were to be omitted in the Bill; and
3. The increased allocation to the conditional grant on the leasing of medical equipment programme.

The brief is also informed by the High Court Ruling on Petition No. 252 of 2016 on Division of Revenue Act, 2016, which among other findings, determined that: -

(a) the National Government cannot allocate itself funds for and undertake devolved functions, without first executing inter-government agreements required by Article 187 of the Constitution;

(b) in accordance with Article 202 (2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be netted from the National Government's share of revenue and not from the overall revenues raised nationally;

(c) in accordance with Article 202(2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be disbursed to the Counties through the County Revenue Fund; and

(d) funds christened as 'national interest' in the Division of Revenue Act 2016 or any other Division of Revenue Act enacted to implement the provisions of Article 202 and 203 of the Constitution cannot be apportioned on devolved functions without the same being channelled to the Counties as conditional or unconditional grants.

THE PROPOSED DIVISION OF REVENUE BILL, 2021

1. The Division of Revenue Bill (DoRB), 2021 proposes to allocate to County Governments Ksh.409.88 billion in the financial year (FY) 2021/22, which relative to the financial year 2020/21 allocation, reflects an increase of Ksh.53.5 billion or 16.9%. This allocation comprises: equitable share of Ksh.370 billion; additional conditional allocations ***from the National Government share of revenue raised nationally*** *amounting to* ***Ksh.7.53 billion***; and additional conditional allocations from proceeds of loans and grants from development partners amounting to Ksh.32.34 billion.

County Governments' Equitable Share

2. The bill proposes to allocate County Governments an equitable share of revenue raised nationally for the financial year 2021/22 of Ksh.370 billion. This is premised on Parliament having approved the third basis for allocation of the share of national revenue among the County Governments in September, 2020 on condition that the formula's implementation would be preceded by a Ksh.53.5 billion increase in the Counties' equitable revenue share.

3. The proposed County Governments' equitable share of revenue raised nationally for the financial year 2021/22 is arrived at by:

   i. adjusting the Counties' FY 2020/21 allocation (i.e., Ksh. 316.5 billion) by Ksh 36.1 billion or 11.4 percent. This growth is premised on the anticipated improvement in revenues raised nationally in FY 2021/22 when the effects of Covid-19 pandemic are expected to ease. This increase is expected to facilitate post Covid-19 economic recovery at the Counties as well as ensure sustained service delivery by the devolved governments; and,

   ii. converting four existing conditional grants to County Governments into unconditional grants, and allocating the respective amounts totaling Ksh. 17.4 billion towards the Counties' FY 2021/22 equitable revenue share. The four conditional allocations are: Road Maintenance Levy Fund (RMLF); the level-5 hospital grant; the compensation for user fees foregone; and, the grant funding rehabilitation of village polytechnics.

4. Conversion of the four conditional allocations to Counties' equitable revenue share as proposed above has several advantages. Firstly, it will afford the Counties more autonomy to budget and prioritize allocation of resources.

Secondly, it will achieve a more consolidated approach to funding of devolved functions, while also enabling better tracking of performance and attribution of outcomes. Thirdly, it will help to address a number of challenges which are currently being experienced including suboptimal absorption of conditional allocations; and failure by Counties to allocate sufficient resources in areas receiving supplemental funding by the National Government through conditional allocations.

5. Moreover, the fact that the approved third basis for allocation of the share of national revenue among the County Governments is now effectively linked to devolved functions (specifically with weighted parameters for health, roads and agriculture) means that it is now possible to achieve policy objectives of some conditional grants directly through the equitable share. In health and agriculture, for instance, the new parameters to be used in distributing the equitable revenue share among Counties closely resemble those currently being used to distribute sectoral conditional allocations. In addition, the approved revenue distribution criteria contain a parameter, 'population' with a weight of 18% which is specifically designed to reflect costs of 'other County Services' including village polytechnics.

6. Currently, besides the composite of equal share, the allocation criteria for the rehabilitation of village polytechnics conditional grant is also based on total trainee enrolment in the respective county governments, which is similar to the use of population parameter in the Third Basis for Revenue Sharing among Counties. This means that village polytechnics being a devolved function, and also a composite of the population parameter of the formula should be directly financed from each County's equitable share of revenue.

7. After making the above adjustment, County Governments' equitable share of revenue in the financial year 2021/22 is estimated to be Ksh. 370 billion (see Table 1).

Table 1: Equitable Revenue Share Allocation to County Governments FY 2021/22

S/N	Budget Item	Amount in Ksh. Million
A	**County Equitable Revenue Share for FY 2020/21 (Base)**	**316,500**
	Add:	
B	**Adjustment based on fiscal framework (Revenue Growth to county governments in FY 2021/22)**	**36,103**
	Add:	
C	***Converted Conditional allocations (previously financed from National Governments share of Equitable Revenue) to County Equitable share...of which: -***	17,397
	a. User Fee	900
	b. Level 5	4,727
	c. Road Maintenance Levy Fund	9,770
	d. Village Polytechnics	2,000
D	**Equitable Revenue Share allocation for FY 2021/22; D=A+B+C**	**370,000**

Source of data: National Treasury

8. The above proposed equitable share for FY 2021/22 of Ksh.370 billion is equivalent to 27.3 percent of the last audited accounts (Ksh.1,358 billion for FY 2016/17) as approved by Parliament. The proposed allocation meets the requirement of Article 203(2) of the Constitution that equitable share allocation to counties should not be less than 15 per cent of the last audited revenue raised nationally, as approved by the National Assembly.

ADDITIONAL CONDITIONAL ALLOCATIONS

9. 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.

10. Accordingly, and in addition to the equitable share of revenue raised nationally, the National Treasury proposes that County Governments receive additional conditional allocations amounting to Ksh 39.88 billion. This reflects a decrease of Ksh 13.52 billion. This decrease has been occasioned by the proposal to convert some of the ongoing additional conditional allocations to county governments, amounting to Ksh.17.4 billion to the equitable share in FY 2021/22. These comprise: i) additional conditional allocations from the National Government share of revenue raised nationally amounting to of Ksh 7.54 billion;

and, ii) conditional allocation from proceeds of external loans and grants amounting to Ksh 32.34 billion.

THE INCLUSION OF CONDITIONAL GRANTS IN THE DIVISION OF REVENUE BILL

11. As indicated above, the National Treasury has proposed an allocation of **Ksh. 39.88 billion** as additional conditional allocations to county governments. This allocation comprises of:-

(a) **Ksh. 7.5 billion** as additional conditional allocations to county governments financed from the national government share of revenue raised nationally to finance: - i). Leasing of Medical Equipment at **Ksh.7.2 billion** ; and ii) Supplement for construction of county headquarters **at Ksh. 332 million.**

NB: -Its worth noting that these additional conditional allocations, were not converted into equitable share of County Governments because they have ongoing contractual obligations.

(b) **Ksh. 32.3 billion** as additional conditional allocations to County Governments financed from proceeds of loans and grants by development partners.

Treatment of the additional conditional allocations in the Division of Revenue Bill

12. The National Treasury has treated the above additional conditional allocations as memo items to the Schedule of the Bill, which means they are not part of the main Division of Revenue.

13. This is done as a disclosure to the public that besides the equitable share of the County Governments from the revenues raised nationally, Counties would receive additional allocations from the National Government's share of revenue and loans and grants from development partners.

14. By disclosing the additional conditional allocations as memo items, the Division of Revenue Bill provides a complete picture of the resources going to county governments.

15. Thus, the Schedule of the Division of Revenue would appear as shown in Table 2.

Table 2: Allocation of revenue raised nationally between the national and county governments for the financial year 2021/22.

Type/level of allocation	Amount in Ksh.	Percentage (%) of 2016/17 audited and approved Revenue i.e., Ksh.1,357,698 Million
A. Total Sharable Revenue	**1,775,624,173,860**	
B. National Government	**1,398,798,856,427**	
Of which:		
1. Leasing of Medical Equipment	7,205,000,000	
2. Supplement for construction of county headquarters	332,000,000	
C. Equalization Fund	**6,825,317,433**	**0.50%**
D. County equitable share	**370,000,000,000**	**27.3%**
Memo items		
1. County equitable share	***370,000,000,000***	
2. Additional conditional allocations (National Government share of Revenue) of which;	***7,537,000,000***	
2.1. Leasing of Medical Equipment	7,205,000,000	
2.2 Supplement for construction of county headquarters	332,000,000	
3. Conditional allocations (Loans & grants) of which:	***32,343,890,512***	
3.1 IDA-Kenya Devolution Support Program (KDSP) (Level 2 Grant)	4,600,000,000	
3.2 IDA-Transforming Health Systems for Universal Care Project	2,234,664,075	
3.3 DANIDA Grant-Primary Health Care in Devolved Context	701,250,000	
3.4 IDA-National Agriculture & Rural Inclusive Growth Project (NARIGP)	6,394,997,407	
3.5 EU-Instruments for Devolution Advice and Support (IDEAS)	230,730,934	
3.6 IDA (World Bank) - Kenya Climate Smart Agriculture Project (KCSAP)	7,838,338,490	
3.7 World Bank- Kenya Informal Settlement Improvement Project II (KISIP II)	2,800,000,000	
3.8 IDA- Water and Sanitation Development Project (WSDP)	5,000,000,000	
3.9 Sweden Agriculture Sector Development Programme II (ASDP II)	1,300,042,902	
4.0 Drought Resilience Programme in Northern Kenya	370,000,000	
4.1 Emergency Locust Response Project (ELRP)	800,000,000	
4.2 UNFPA- 9th Country Programme Implementation	73,866,704	
Total County Allocations= (1+2+3)	**409,880,890,512**	

16. From table 2 above, its clear that the items of the Division of Revenue are:

(i) **Item A:** Total Sharable Revenue of Ksh. 1,775,624,173,860;

(ii) **Item B:** National Government share of revenue raised nationally amounting to Ksh. 1,398,798,856,427 (of which Ksh. 7,537,000,000 shall be transferred to County Governments as additional conditional allocations pursuant to Article 2020(2) of the Constitution);

(iii) **Item C:** Allocation to Equalisation Fund (pursuant to Article 204) amounting to Ksh. 6,825,317,433; and,

(iv) **Item D:** County equitable share amounting to Ksh. 370,000,000,000.

17. Article 190 (1) of the Constitution provides that, ***"Parliament shall by legislation ensure that county governments have adequate support to enable them to perform their functions."***

ALTERNATIVE MECHANISM FOR DISBURSEMENT OF CONDITIONAL GRANTS TO COUNTIES IF THEY WERE TO BE OMITTED IN THE BILL

18. Article 96 (3) of the Constitution provides that the Senate is responsible for determining the allocation of national revenue among Counties and exercising oversight over national revenue allocated to the County Governments;

19. Article 114 (3) of the Constitution excludes the Division of Revenue Bill and County Allocation of Revenue Bill from the definition of a money Bill.

20. Article 218(1) (b) requires a County Allocation of Revenue Bill be introduced in Parliament to divide among Counties the revenue allocated to the County level of Government.

21. Section 191 (1) as read with Section 25 of the Public Finance Management Act (PFMA), 2012 provides that, each year when the Budget Policy Statement is introduced, the Cabinet Secretary responsible for finance shall submit to Parliament a Division of Revenue Bill and County Allocation of Revenue Bill as provided in the PFMA for the financial year to which that Budget relates.

22. Section 191 (3) of the PFMA also provides that, "the County Allocation of Revenue Bill shall specify— (a) each county's share of that revenue under subsection (2); and ***(b) any other allocations to the counties, from the national***

government's share of that revenue, and <u>any conditions on which those allocations shall be made</u>"

23. The import of paragraph 24 is that any additional conditional allocations to County Governments should be contained in County Allocation of Revenue Bill and approved by Parliament.

24. It may be argued that pursuant to Regulation 24 and 25 of the Public Finance Management (National Government) Regulations, 2015, National Government Accounting Officers can issue Authority to Incur Expenditure to respective accounting officers of the respective county governments. Particularly, Regulation 25 (1) of PFM(NG) Regulations,2015 also provides An accounting officer may authorize a public officer under their national government entity to be an Authority to Incur Expenditure Holder (AIE).; while regulation 25 (2) provides that, ***An Accounting Officer who finds it necessary to authorize a public officer in another Ministry or <u>county government</u> to incur official expenditure on his or her behalf, shall do so by issuing an Authority to Incur Expenditure addressed to the Accounting Officer of the national government or <u>county government entity</u>.***

25. However, Regulation 25 (3) and (5) gives clarity that designation of AIE Holder shall be in writing in the form prescribed by the National Treasury; and ***Where an Accounting Officer delegates this authority, the accounting officer <u>shall remain responsible for any expenditure incurred as a result of that delegation.</u>***

26. In the doctrine of separation of powers under devolved system of government, emphasis on independence of the two levels as envisaged in Article 189 of the Constitution, is this option visible and how can the doctrine be respected?

27. Article 226 (2) of the Constitution provides that, "***The accounting officer <u>of a national public entity is accountable to the National Assembly</u> for its financial management, and the accounting officer <u>of a county public entity is accountable to the county assembly for its financial management</u>***".

28. Accordingly, this Article suggests that this arrangement poses a challenge not only on accountability mechanism if an AIE were to be issued by a National Government Accounting Officer to a County Government Accounting Officer, but would also offend principles of the Constitution on independence of County Governments.

29. It is for the above reason that the National Treasury is of the considered opinion that the only legal instrument to disburse allocations to County Governments is the County Allocation of Revenue Act, which MUST be approved by Senate, and as ***such allocations should be disclosed in the Division of Revenue Act, as memo items.***

THE INCREASED ALLOCATION TO THE CONDITIONAL GRANT ON THE LEASING OF MEDICAL EQUIPMENT PROGRAMME

30. This additional conditional allocation which is in its seventh year of implementation, is proposed to increase from Ksh.6.205 billion in FY 2020/21 to Ksh.7.205 billion in FY 2021/22 and is intended to facilitate the payment of lease amounts in respect 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.

31. The significant increase is to cater for pending bills related to MES programme occasioned by lack of provision in previous years. For instance, in FY 2019/20, Ministry of Health closed with pending bills of Ksh. 1.17 billion which was treated as a first charge in FY 2020/21 from the allocation to MES of Ksh. 6.02 billion.

32. Accordingly, the balance will not be adequate to cater for this year's contractual obligations, unless additional resources are provided in the supplementary. Secondly, the next FY being the final year of the project, there is need to make a full provision to ensure all contractual obligations are met

before closure of the project so as not to attract pending bills and subsequent interest which may occasion loss of public funds in the long run.

The High Court Ruling on Petition No. 252 of 2016 on Division of Revenue Act, 2016

33. The National Treasury is cognisant and in agreement with the High Court Ruling on Petition No. 252 of 2016 on Division of Revenue Act, 2016 as it relates to the Division of Revenue Bill, 2021 and wishes to submit as follows with regards to compliance with the findings that: -

(a) the National Government cannot allocate itself funds for and undertake devolved functions, without first executing inter-government agreements required by Article 187 of the Constitution;

34. The Division of Revenue Bill, 2021 has not allocated any funds to the National Government to undertake any of the Devolved functions as contained in part II of the Fourth Schedule of the Constitution. The only additional conditional allocation whose expenditure will be made by the National Government on behalf of respective county governments is on Leasing of Medical Equipment. There exits duly signed Intergovernmental Agreements pursuant to Article 187 of the Constitution between the Ministry of Health (on behalf of the National Government) and the respective county governments, to this effect.

(b) in accordance with Article 202 (2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be netted from the national government's share of revenue and not from the overall revenues raised nationally;

35. The National Treasury has proposed allocation of Ksh. 7.5 billion as additional conditional allocations to county governments ***financed from the national government share of revenue raised nationally*** to finance: - i). Leasing of Medical Equipment at Ksh.7.2 billion and ii) Supplement for construction of county headquarters at Ksh. 332 million.

(c) in accordance with Article 202(2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be disbursed to the Counties through the County Revenue Fund;

36. The National Treasury shall, except for the leasing of medical equipment conditional allocation, disburse all allocations to county governments to their respective County Revenue Fund Accounts as contained in the proposed County Allocation of Revenue Bill, 2021, which is before Parliament.

(d) funds christened as 'national interest' in the Division of Revenue Act 2016 or any other Division of Revenue Act enacted to implement the provisions of Article 202 and 203 of the Constitution cannot be apportioned on devolved functions without the same being channelled to the Counties as conditional or unconditional grants.

37. The National Treasury, through the Division of Revenue Bill, 2021 has not proposed an allocation christened "National Interest", Pursuant to Article 203, to the National Government, for functions devolved to county governments.

CONCLUSION

38. In processing the Division of Revenue Bill, 2021, the National Treasury request that Senate considers including additional conditional allocations as memo items to the Bill in order to facilitate for purposes of full disclosure of resources going to county governments.

39. We request that the Senate considers the Division of Revenue Act and the County Allocation of Revenue Act as the legislation by Parliament envisaged in Article 190 (1) of the Constitution meant to ensure that county governments have adequate support to enable them to perform their functions.

40. Finally, we request the Committee to consider and reinstate the definition of revenue under section 2 of the Bill to read that, ***""revenue" has the meaning assigned to it under section 2 of the Commission on Revenue Allocation Act, 2011; and includes Roads Maintenance Levy Fund allocation under this Act."***

Hon. (Amb.) Ukur Yatani, EGH
Cabinet Secretary/National Treasury and Planning

Dated: April 7th, 2021

MINUTES OF THE 205TH MEETING OF THE SENATE STANDING COMMITTEE ON FINANCE AND BUDGET HELD ON WEDNESDAY, 31ST MARCH, 2021 AT 9:00 AM VIA ZOOM ONLINE PLATFORM.

PRESENT

1. Sen. Charles Kibiru, MP - Chairperson
2. Sen. (Dr.) Ochillo Ayacko, MP - Vice- Chairperson
3. Sen. CPA Farhiya Haji, MP - Member
4. Sen. Aaron Cheruiyot, MP - Member
5. Sen. Millicent Omanga, MP - Member

ABSENT WITH APOLOGY

6. Sen. Wetang'ula Moses Masika, EGH, MP - Member
7. Sen. Mutula Kilonzo Junior, CBS, MP - Member
8. Sen. Rose Nyamunga, MP - Member
9. Sen. Kimani Wamatangi, MP - Member

SECRETARIAT

1. Mr. Christopher Gitonga - Clerk Assistant
2. Ms. Yunis Amran - Fiscal Analyst
3. Ms. Lucy Radoli - Legal Counsel
4. Mr. Sharon Rotino - Research Officer
5. Ms. Regina Munyao - Legal Counsel
6. Mr. Patrick Murindo - SAA

MIN. NO. 1070/03/2021: PRELIMINARIES

The Chairperson called the meeting to order at 9.15 am and thereafter followed a word of prayer.

MIN. NO. 1071/03/2021: ADOPTION OF THE AGENDA

The agenda of the meeting was adopted after it was proposed by Sen. Millicent Omanga, MP and seconded by Sen. CPA Farhiya Haji, MP.

MIN. NO. 1072/03/2021: MEETING WITH THE GOVERNOR, CENTRAL BANK OF KENYA TO DELIBERATE ON THE STATEMENT REQUESTED CONCERNING QUALITY OF NEW GENERATION CURRENCY NOTES

The Committee considered apology letter requesting from Governor, CBK requesting for rescheduling of the meeting since he was attending Monetary Policy Committee (MPC) meeting.

The considered acceded to the request and resolve that the meeting be held later in the month of April.

MIN. NO. 1073/03/2021: CONSIDERATION OF THE DIVISION OF REVENUE BILL (NATIONAL ASSEMBLY BILLS NO. 7 OF 2021)

The Committee considered the Bill and noted the following-

a) The proposed shareable revenue for the Financial Year 2021/22 was Kshs. 1,775.624 billion.
b) The Bill proposed an allocation of Kshs. 370 billion to county governments, as contained in the Resolution on basis for sharing national revenue allocated to counties, and Kshs. 1,398.79 billion to national government.
c) The allocation to counties which is equivalent to 27.3% of the last audited accounts (Ksh 1,357,698 million for FY 2016/17) as approved by the National Assembly.
d) The proposal for an increased allocation of Kshs. 1 billion to the leasing of medical equipment (MES). The total allocation was Kshs. 7.205 billion.
e) The bill proposed 12 conditional grants from loans and grants totalling of Kshs. 32.343 billion.
f) The implication of the High Court Ruling on Petition No. 252 of 2016 which indicated that conditional grants should not be part of the Division of Revenue Bill.

The Committee resolved to-

a) Hold a consultative meeting with the CRA, the COG, the National Treasury and the Office of the Attorney General on Wednesday, 7th April, 2021.
b) Hold a hearing with ICPAK, IBP and TISA on Tuesday, 6th April, 2021.
c) Request for submission of memorandum from the members of public through newspaper advertisements.

MIN. NO. 1074/03/2021 ANY OTHER BUSINESS

a) The Committee was informed that there was a Petition in the Senate that requested for investigation on financial operations of Wajir County Government Executive. However, the Petition was referred to the standing Committee on Devolution and Intergovernmental Relations whereas its mandate it's not on financial matters. The Chairperson was requested to follow the matter.
b) The Committee noted that the retreat held with Controller of Budget and COG Technical Committee on Finance, Planning and Economic Affairs was fruitful and resolution would be circulated in due course.

MIN. NO. 1075/03/2021 ADJOURNMENT

The time been 10.18 am the Chairperson adjourned the meeting.

SIGNATURE:____________________

(CHAIRPERSON: SEN. CHARLES KIBIRU, MP.)

DATE: 12th April, 2021

MINUTES OF THE 206TH MEETING OF THE SENATE STANDING COMMITTEE ON FINANCE AND BUDGET HELD ON TUESDAY, 6TH APRIL, 2021 AT 9:00 AM VIA ZOOM ONLINE PLATFORM.

PRESENT

1. Sen. Charles Kibiru, MP	- Chairperson
2. Sen. (Dr.) Ochillo Ayacko, MP	- Vice- Chairperson
3. Sen. CPA Farhiya Haji, MP	- Member
4. Sen. Mutula Kilonzo Junior, CBS, MP	- Member
5. Sen. Aaron Cheruiyot, MP	- Member
6. Sen. Rose Nyamunga, MP	- Member

ABSENT WITH APOLOGY

7. Sen. Wetang'ula Moses Masika, EGH, MP	- Member
8. Sen. Millicent Omanga, MP	- Member
9. Sen. Kimani Wamatangi, MP	- Member

SECRETARIAT

1. Mr. Christopher Gitonga	- Clerk Assistant
2. Ms. Yunis Amran	- Fiscal Analyst
3. Ms. Lucy Radoli	- Legal Counsel
4. Mr. Sharon Rotino	- Research Officer
5. Mr. Patrick Murindo	- SAA

INATTENDANCE

International Budget Partnership (IBP) – Kenya Chapter

1. Dr. Abrahams Rugo
2. Ms. Faithann Korir
3. Mr. Abraham Ochieng

Institute of Certified Public Accountants of Kenya (ICPAK)

1. FCPA Philip Kakai
2. FCPA Andrew Tanui
3. CPA Ken Nyamolo
4. CPA Andrew Rori
5. CPA Elias Wakhisi
6. CPA Hillary Onami

MIN. NO. 1076/04/2021: PRELIMINARIES

The Chairperson called the meeting to order at 9.10 am and thereafter followed a word of prayer. The Chairperson welcomed the Members and the stakeholders to the meeting.

MIN. NO. 1077/04/2021: ADOPTION OF THE AGENDA

The agenda of the meeting was adopted after it was proposed by Sen. (Dr.) Ochillo Ayacko, MP and seconded by Sen. Rose Nyamunga, MP.

MIN. NO. 1078/04/2021: PRESENTATION OF MEMORANDUM ON THE DIVISION OF REVENUE BILL, 2021

International Budget Partnership

Upon invitation, the representatives submitted as follows-

a) Despite devolution being an essential aspect of Kenya's service delivery, the rate of growth of allocations to the counties has been declining. However, for FY 2021 the growth is at 17%.
b) Conditional Grants for the construction of county headquarters was to be a three-year grant. However, this conditional grant has existed for over more than five years which raises the question on its effectiveness.
c) There is no apparent growth factor in the division of revenue allocation basis. This leaves it for manipulation by actors in the national government.
d) Public debt, pensions, and other charges on the consolidated fund services are crowding out the amount available for sharing. This eventually negatively affects allocation to counties.
e) Pensions and other CFS Services have equally grown, and their administration is of concern. For instance, Pension is a non-discretionary obligation that has a bearing on the size of revenue that is eventually shared between the two government levels.
f) The National interest allocations take a considerable portion of the shareable revenue and have only been proposed to substantially declined in FY 2021/22.
g) Lack of transparency, accountability, and meaningful public engagement is affecting the division of the revenue process.
h) The realism of the revenue forecast has never been achieved. Revenue forecasts at both the national and county levels of government have been ambitious and often led to budget deficits. The revenue projection is exaggerated because its expenditure driven.

Institute of Certified Public Accountants of Kenya

Upon invitation, the representatives submitted as follows-

a) Revenue projections - the actual revenue receipts have continuously fallen below the targets/ projections. Aware of the global pandemic it is highly unlikely that in the next FY 2021/22, the Kenyan economy will have rebounded. The Government should therefore conduct a trend analysis of revenue growth to inform revenue projections for the subsequent years.

b) Inadequate utilization of the Leased Medical Equipment- There is need to provide capacity strengthening sessions to the health personnel and fast-track the development of the required infrastructure in the respective health facilities. Allocations to this programme have been fluctuating yet it's a contract with fixed terms.
c) Need for clarity on conditional Grants for construction of county headquarters- The first disbursement for construction of county headquarters was received in FY2017/18 therefore, the final disbursement should have been in the FY 2019/20. Despite this, we note that DORB 2020 and 2021 still allocated the counties the amounts Ksh 300 million and Ksh 332 million.
d) There is need to consider a conditional Allocation to support ECDE- this would assist in increasing capitation for ECDE teachers, enable employment of skilled and qualified instructors, and support development of adequate monitoring and assessment of performance (quality assurance) of learning.
e) Actual public debt service figures have always been higher than the projections- the public debt repayment projections contained in the division of revenue bills have always been lower than what is contained in the programme-based budget documents. These figures have further been lower than the actual ones contained in the national government budget implementation review reports. There is need for more accurate projections for proper planning purposes as well as observance of transparency in public debt contracting.
f) Public debt repayment is crowding out the amount available for division of revenue and hurting counties allocation
g) Pensions and other CFS Services have equally grown, and their administration is of concern- its notable that the pay-out amounts to retirees is usually below the budgeted amount. This is an indication of delays in processing the claims. There should be transparency and accountability in processing and payment of pension and gratuities for the retirees. Secondly, there is need for the management and administration of retirement benefits for employees to be transferred to the respective employment commissions.
h) Equalization Fund- there is need to expedite implementation of the fund since it has a sunset. The time may lapse before its objective is achieved.
i) Nairobi City County- There is need for clarity on how revenue allocated to transferred functions will be transmitted to Nairobi Metropolitan Service. This is important to curb any stand-off between the County and NMS that could derail service delivery.
j) Budget Transparency is critical for objective division of revenue- There is lack of a clear definition and objective criteria for determining national interest. Secondly, the framework for the management of conditional grants continues to be weak, and indeed does not meet the constitutional requirements for fiscal prudence and transparency.
k) Fiscal Accountability- There is need to strengthen the fiscal accountability structures across both the national and county governments. The recommendations from oversight bodies including the Controller of Budget and the Auditor General should

be followed so as to ensure prudent use of public funds. These include full compliance with the Public Financial Management Act (2012).

The Committee noted the need to-

a) review the law to allow management of pension of the civil servants by the approved pension fund institutions.
b) Consult the National Treasury on the proposed increase on allocation for MES.
c) Request for a report on performance of projects funded through conditional grants.

The Committee appreciated the participants for appearing and representing their views on Bill.

MIN. NO. 1079/04/2021 ANY OTHER BUSINESS AND ADJOURNMENT
There been no other business the Chairperson adjourned the meeting at 11.05 am.

SIGNATURE: ____________________

(CHAIRPERSON: SEN. CHARLES KIBIRU, MP.)

DATE: **12th April, 2021**

MINUTES OF THE 207TH MEETING OF THE SENATE STANDING COMMITTEE ON FINANCE AND BUDGET HELD ON WEDNESDAY, 7TH APRIL, 2021 AT 9:00 AM VIA ZOOM ONLINE PLATFORM.

PRESENT

1. Sen. Charles Kibiru, MP - Chairperson
2. Sen. (Dr.) Ochillo Ayacko, MP - Vice- Chairperson
3. Sen. CPA Farhiya Haji, MP - Member
4. Sen. Mutula Kilonzo Junior, CBS, MP - Member
5. Sen. Aaron Cheruiyot, MP - Member
6. Sen. Rose Nyamunga, MP - Member
7. Sen. Millicent Omanga, MP - Member

ABSENT WITH APOLOGY

8. Sen. Wetang'ula Moses Masika, EGH, MP - Member
9. Sen. Kimani Wamatangi, MP - Member

SECRETARIAT

1. Mr. Christopher Gitonga - Clerk Assistant
2. Ms. Phyllis Makau - Director PBO
3. Mr. Martin Masinde - Deputy Director PBO
4. Ms. Yunis Amran - Fiscal Analyst
5. Ms. Lucy Radoli - Legal Counsel
6. Mr. Sharon Rotino - Research Officer
7. Mr. Frank Mutulu - Media Relations Officer
8. Mr. Patrick Murindo - SAA

INATTENDANCE

The National Treasury

1. Hon. (Amb.) Ukur Yatani – Cabinet Secretary
2. Mr. Albert Mwenda - DG, Fiscal, Budget and Intergovernmental Relations
3. Mr. Samuel Kiptorus - Director, Intergovernmental Fiscal Relations
4. Mr. Fred Owegi
5. Ms. Josephine Kanyi
6. Ms. Isabella Kogei

The Commission on Revenue Allocation

1. Dr. jane Kiringai - Chairperson
2. Mr. Humphrey Wattanga - Vice Chairperson
3. Prof. Peter Kimuyu
4. Dr. Irene Asienga

5. Ms. Linet Oyugi
6. Ms. Shaeilla Yieke

The Office of the Attorney General
1. Mr. Fred Mwachi

MIN. NO. 1080/04/2021: PRELIMINARIES

The Chairperson called the meeting to order at 9.06 am and thereafter followed a word of prayer. The Chairperson welcomed the Members and the stakeholders to the meeting.

MIN. NO. 1081/04/2021: ADOPTION OF THE AGENDA

The agenda of the meeting was adopted after it was proposed by Sen. Rose Nyamunga, MP and seconded by Sen. Aaron Cheruiyot, MP.

MIN. NO. 1082/04/2021: CONSULTATIVE MEETING WITH STAKEHOLDERS ON THE DIVISION OF REVENUE BILL, 2021

After introductions, the Chairperson made remarks on the purpose of the meeting, citing the need for the meeting to interrogate the bill to ensure it complies to the law and the High Court ruling on Petition No. 252 of 2016.

All the parties (the Committee, the National Treasury, the Office of Attorney General and the Commission on Revenue Allocation) present in the meeting indicated they were cognizant of the High Court ruling. It was also note that there was need to device a mechanism which would ensure obedience to the ruling as well as ensure public finance structure/ system was adhered to.

After deliberations it was resolved as follows-

a) A technical team comprising of representation from the Senate, National Treasury, the Office of Attorney General, the Commission on Revenue Allocation be constituted.
b) The technical team was mandated to consider the implications of the Ruling in High Court Petition No. 252 of 2016, with respect to conditional grants *vis-a-vis* the Division of Revenue Bill.
c) The technical team should report to the Committee on Friday, 9th April, 2021.
d) A similar meeting comprising of all the stakeholders be held on 9th April, 2021 at 9 am.

On other issues of Division of Revenue Bill, the Cabinet Secretary, National Treasury responded as follows-

a) Increased allocation to MES programme- increment by Ksh. 1 billion to the MES programme was to cater for pending bills incurred by the Ministry of Health in the

FY 2019/20. Thus, to ensure the contractual obligation was fulfilled, additional resources are required since pending bills must be treated as a first charge.

b) Huge budget for national government ministries with performing devolved function (Health and Agriculture)- in developing DORB with county equitable share of Kshs. 370 billion a detailed analysis was done on all the national government entities with concurrent functions. The analysis was able to identify about Kshs. 37 billion which was marked for distribution to counties.

c) Taxation policy- the matter had been raised in other fora and the National Treasury was considering it and information will be provided on the way forward.

The Committee raised concern over several issues that have been pending and require the CS to address. It was further resolved that a meeting be held in future where the Cabinet Secretary, National Treasury would appear before the Committee and respond to all the matters that have been pending.

MIN. NO. 1083/04/2021 ANY OTHER BUSINESS AND ADJOURNMENT

There been no other business the Chairperson adjourned the meeting at 10.31 am.

SIGNATURE: ______________________

(CHAIRPERSON: SEN. CHARLES KIBIRU, MP.)

DATE: **12th April, 2021**

MINUTES OF THE 208TH MEETING OF THE SENATE STANDING COMMITTEE ON FINANCE AND BUDGET HELD ON FRIDAY, 8TH APRIL, 2021 AT 9:00 AM VIA ZOOM ONLINE PLATFORM.

PRESENT

1. Sen. Charles Kibiru, MP - Chairperson
2. Sen. (Dr.) Ochillo Ayacko, MP - Vice- Chairperson
3. Sen. CPA Farhiya Haji, MP - Member
4. Sen. Mutula Kilonzo Junior, CBS, MP - Member
5. Sen. Aaron Cheruiyot, MP - Member
6. Sen. Rose Nyamunga, MP - Member
7. Sen. Millicent Omanga, MP - Member

ABSENT WITH APOLOGY

8. Sen. Wetang'ula Moses Masika, EGH, MP - Member
9. Sen. Kimani Wamatangi, MP - Member

SECRETARIAT

1. Mr. Christopher Gitonga - Clerk Assistant
2. Ms. Phyllis Makau - Director PBO
3. Ms. Yunis Amran - Fiscal Analyst
4. Ms. Lucy Radoli - Legal Counsel
5. Mr. Sharon Rotino - Research Officer
6. Mr. Frank Mutulu - Media Relations Officer

INATTENDANCE

The National Treasury

1. Hon. Nelson Gaichuhie – Chief administrative Secretary
2. Mr. Albert Mwenda
3. Mr. Samuel Kiptorus
4. Ms. Elizabeth Nzioka
5. Mr. Fred Owegi
6. Ms. Josephine Kanyi

The Commission on Revenue Allocation

1. Dr. jane Kiringai - Chairperson
2. Prof. Peter Kimuyu - Commissioner
3. Ms. Linet Oyugi
4. Ms. Shaeila Yieke
5. Ms. Jecinter Hezron

The Office of the Attorney General

1. Mr. Fred Mwachi

The Council of County Governors

1. Hon. Ndiritu Muriithi – Chairman, Technical Committee on Finance, Planning and Economic Affairs
2. Ms. Jackline Mogeni - CEO
3. Ms. Mercy Wangui
4. Ms. Zipporah Muthama

MIN. NO. 1084/04/2021: PRELIMINARIES

The Chairperson called the meeting to order at 9.07 am and thereafter followed a word of prayer. The Chairperson welcomed the Members and the stakeholders to the meeting.

MIN. NO. 1085/04/2021: ADOPTION OF THE AGENDA

The agenda of the meeting was adopted after it was proposed by Sen. Rose Nyamunga, MP and seconded by Sen. Aaron Cheruiyot, MP.

MIN. NO. 1086/04/2021: CONSULTATIVE MEETING WITH STAKEHOLDERS ON THE DIVISION OF REVENUE BILL, 2021

After introductions, the Chairperson made remarks that this meeting was constituted following a resolution made in previous meeting. A technical team had been constituted to consider the implications of the Ruling in High Court Petition No. 252 of 2016, with respect to conditional grants *vis-a-vis* the Division of Revenue Bill, 2021.

Thereafter, he welcomed the technical team to make presentations. The team presented as follows-

a) The team held a meeting and deliberated on the matter and noted the content of the ruling especially paragraph 72 and 67.
b) The team also noted the need to expedite parliamentary approval of the Bill before 30th April so as to pave way for consideration of the budget estimates both at national and county level of governments as well as publication of County Allocation of Revenue Bill
c) The team made the following findings-
    - Conditional grants cannot be contained in the division of revenue bill, not even as memo items.
    - In order to facilitate transfer of conditional grants to County Revenue Fund (CRF), there was need to develop a legal instrument which would be an enabler to this process.
    - There was need for guidelines on management and control of such funds as well as accountability.

d) The team recommended-

- The DoRB, 2021 be amended to drop any reference to conditional and unconditional allocations by deleting the schedule and substituting therefor with a new schedule providing for the following four items only-
  - ✓ Total sharable revenue
  - ✓ National Government share
  - ✓ Equalization fund
  - ✓ County equitable share
- Establish an appropriate legal instrument to enable the transfer of conditional grants to the respective CRFs. This legal instrument should also clarify the framework for the management, control and accounting for conditional and unconditional grants that should be consistent with the ruling and minimize exposure of public funds.

After deliberations, it was resolved that-

a) The recommendations be adopted as proposed. This was adopted after it was proposed by Sen. Aaron Cheruiyot, MP and seconded by Sen. (Dr.) Ochillo Ayacko, MP.

b) A legislation be drafted under Article 190 of the Constitution to cover all the issues canvassed under second recommendation above.

c) The technical team was allowed to take three (3) weeks to develop the legal instrument and submit it to the meeting for consideration.

Further clarifications were made as follows-

a) The proposed legislation mentioned above cannot be classified as money bill;

b) The legislation should have details on management, control and accountability;

c) It should further provide clarity on conditional grant framework between the two levels of government.

d) Appealing the High Court ruling may not be prudent for it may be expensive, time consuming and not yield the much needed outcome.

e) Should clarify on the instrument that the Office of Controller of Budget may apply in authorising withdrawal from respective County Revenue Funds.

MIN. NO. 1087/04/2021 ANY OTHER BUSINESS

a) The CAS was requested to explain the delay experienced on cash disbursement to counties. The CAS informed the meeting that there has been challenges on exchequer flow but the matter was being addressed. In the following week, the National Treasury would disburse some funds to counties. A report on the disbursement would be submitted to the Committee by Friday, 16th April, 2021.

b) It was proposed that the National Treasury should seek to have a 2-month facility with Central Bank of Kenya which would allow transfer to CRFs even when there are challenges in exchequer inflows. The facility would be settled once the exchequer receipts are received. The CAS committed to consider the proposal for adoption.

MIN. NO. 1088/04/2021 ADJOURNMENT

There been no other business the Chairperson adjourned the meeting at 10.55 am.

SIGNATURE: ____________________

(CHAIRPERSON: SEN. CHARLES KIBIRU, MP.)

DATE: **12th April, 2021**

MINUTES OF THE 209TH MEETING OF THE SENATE STANDING COMMITTEE ON FINANCE AND BUDGET HELD ON MONDAY, 12TH APRIL, 2021 AT 9:00 AM VIA ZOOM ONLINE PLATFORM.

PRESENT

1. Sen. Charles Kibiru, MP - Chairperson
2. Sen. (Dr.) Ochillo Ayacko, MP - Vice- Chairperson
3. Sen. Wetang'ula Moses Masika, EGH, MP - Member
4. Sen. CPA Farhiya Haji, MP - Member
5. Sen. Mutula Kilonzo Junior, CBS, MP - Member
6. Sen. Aaron Cheruiyot, MP - Member
7. Sen. Rose Nyamunga, MP - Member
8. Sen. Millicent Omanga, MP - Member

ABSENT WITH APOLOGY

9. Sen. Kimani Wamatangi, MP - Member

SECRETARIAT

1. Mr. Christopher Gitonga - Clerk Assistant
2. Ms. Yunis Amran - Fiscal Analyst
3. Ms. Lucy Radoli - Legal Counsel
4. Mr. Sharon Rotino - Research Officer
5. Mr. Ian Otieno - Audio Officer

INATTENDANCE

MIN. NO. 1089/04/2021: PRELIMINARIES

The Chairperson called the meeting to order at 9.09 am and thereafter followed a word of prayer. The Chairperson welcomed the Members and the stakeholders to the meeting.

MIN. NO. 1090/04/2021: ADOPTION OF THE AGENDA

The agenda of the meeting was adopted after it was proposed by Sen. Mutula Kilonzo Junior, CBS, MP and seconded by Sen. (Dr.) Ochillo Ayacko, MP.

MIN. NO. 1091/04/2021: CONFIRMATION OF MINUTES OF MINUTES

a) The minutes of the 205th meeting held on Wednesday, 31st March, 2021 at 9:00 am were confirmed as a true record of the proceedings of the Committee having been proposed by Sen. (Dr.) Ochillo Ayacko, MP and seconded by Sen. Millicent Omanga, MP.

b) The minutes of the 206th meeting held on Tuesday, 6th April, 2021 at 9:00 am were confirmed as a true record of the proceedings of the Committee having been proposed by Sen. Rose Nyamunga, MP and seconded by Sen. Mutula Kilonzo Junior, CBS, MP.

c) The minutes of the 207th meeting held on Wednesday, 7th April, 2021 at 9:00 am were confirmed as a true record of the proceedings of the Committee having been proposed by Sen. Millicent Omanga, MP and seconded by Sen. Mutula Kilonzo Junior, CBS, MP.

d) The minutes of the 208th meeting held on Friday, 9th April, 2021 at 9:00 am were confirmed as a true record of the proceedings of the Committee having been proposed by Sen. Rose Nyamunga, MP and seconded by Sen. (Dr.) Ochillo Ayacko, MP.

MIN. NO. 1092/04/2021: CONSIDERATION AND ADOPTION OF THE REPORT ON THE DIVISION OF REVENUE BILL (NATIONAL ASSEMBLY BILLS NO. 7 OF 2021)

The Committee considered its report and resolved to recommend-

a) that the Division of Revenue Bill (National Assembly Bills No. 7 of 2021) be approved with the amendment to the schedule. The new schedule should provide for the following four items only-
   - ✓ Total sharable revenue;
   - ✓ National Government share;
   - ✓ Equalization fund; and
   - ✓ County equitable share.

   This recommendation is in compliance with the Ruling in High Court Petition No. 252 of 2016, where the court held that it cannot be permissible to provide for conditional grants in the Division of Revenue Act and therefor it follows that conditional grant cannot be proposed in Division of Revenue Bill.

b) an enactment of bill to provide for a legal mechanism to enable the transfer of conditional grants to the respective County Revenue Funds (CRFs) and withdrawal from CRFs by county governments. The Bill should also provide a framework for the management, control and accounting for conditional and unconditional grants.

c) That the proposed nascent legal instrument will address the modalities of allocation, expenditure and reporting on conditional grants to county governments. It will therefore be within the purview of Article 110(4) of the Constitution.

The report was unanimously adopted having been proposed by Mutula Kilonzo Junior, CBS, MP and seconded by Sen. Millicent Omanga, MP MP.

MIN. NO. 1094/04/2021 ANY OTHER BUSINESS

a) It was reported that the Committee had been invited for a training on Integrated Financial Management Systems: Strategy and Implementation by Development Training International. It was resolved that this training be undertaken in the month of May.

MIN. NO. 1095/04/2021 ADJOURNMENT

The Chairperson adjourned the meeting at 9.58 am.

SIGNATURE: ____________________

(CHAIRPERSON: SEN. CHARLES KIBIRU, MP.)

DATE: **12th April, 2021**

REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

CONSTITUTIONAL AND HUMAN RIGHTS DIVISION

PETITION NO. 252 OF 2016

IN THE MATTER OF ALLEGED INFRINGMENT OF THE PROVISIONS OF ARTICLES 1(1), 1(3), 2(2), 2(4), 3(1), 6(2), 10, 174(G), 175, 183, 185, 186, 186(2), 187(1), 189, 189(1)(C), 203(1)(D), 217, 258 AND 259(1) OF THE CONSTITUTION OF KENYA

BETWEEN

COUNCIL OF COUNTY GOVERNORS..........................PETITIONER

VERSUS

THE ATTORNEY GENERAL...............................1ST RESPONDENT

THE NATIONAL ASSEMBLY...............................2ND RESPONDENT

THE SENATE...3RD RESPONDENT

CABINET SECRETARY,

THE NATIONAL TREASURY...............................4TH RESPONDENT

COMMISSION ON REVENUE ALLOCATION.........5TH RESPONDENT

AND

CONTROLLER OF BUDGET.........................INTERESTED PARTY

JUDGEMENT

THE PETITION

1. The Petitioner; Council of Governors instituted this Petition dated 15th June 2016 on the even date seeking the following reliefs:-

   a) ***A declaration that the National Government cannot allocate itself funds for and undertake devolved functions, without first executing inter-government agreements required by Article 187 of the Constitutions.***

   b) ***A declaration that in accordance with Article 202 (2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be netted from the national government's share of revenue and not from the overall revenues raised nationally.***

   c) ***A declaration that in accordance with Article 202(2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be disbursed to the Counties through the County Revenue Fund.***

d) *A declaration that 'national interest' as stated in Article 203(1) (a) of the Constitution does not necessarily connote functions of the national government as provided in the 4th Schedule of the Constitution.*

e) *A declaration that funds christened as 'national interest' in the Division of Revenue Act 2016 or any other Division of Revenue Act enacted to implement the provisions of Article 202 and 203 of the Constitution cannot be apportioned on devolved functions without the same being channelled to the Counties as conditional or unconditional grants.*

f) *A declaration that, in its entirety, the Division of Revenue Act, 2016 is inconsistent with the provisions of Article 6(2), 10(2)(a), 174(c), (d) and (h), 202(2), 174(g), 175(b), 186, 186(2), 187(1), 189, 189(1) (c), 203(1)(d), 217 of the Constitution.*

g) *An order directing the respondents to take necessary steps to amend the Division of Revenue Act, 2016 to*

conform to the provisions of Articles 202(2) and 203(1) of the Constitution.

BACKGROUND

2. The Petitioner herein; Council of Governors instituted this Petition after parliament went ahead and enacted the ***Division of Revenue Allocation Act in 2016*** to sharing and devolution of power. The Act was assented to by the President on 23rd May 2016 and provides for divisions of revenue modality between the National and County governments.

3. The Division of Revenue Act 2016 hereinafter the "Act" for financial year 2016/2017 provides for the allocation of the following funds to the National Government;

   a) Kshs.4121 Billion for free Maternity Health Care.

   b) Kshs.4.5 Billion for Leasing Medical Equipment.

   c) Kshs.4.5 Billion for level 5 hospitals.

4. All the above are devolved functions yet parliament allocated the funds to the National Government. In an attempt to camouflage the

Constitutional anomaly, the Act made the allocations as a conditional grant. The County Governments aggrieved by the manner in which the National Government was silently taking over devolved functions through allocation of funds to itself filed this Petition seeking the orders hereof as set out in the Petition.

5. The National Assembly, the 2nd Respondent herein subsequently filed a Notice of Preliminary Objection on 25th July 2016 on the grounds that the Petition had not exhausted all the Alternative Dispute Resolution Mechanisms to resolve the dispute before approaching the Court.

6. On 3rd March 2016, Justice Muriithi, allowed the Preliminary Objection and ordered that the Petition be stayed pending reference of the dispute between the Petitioner and the National Government to Alternative Dispute Resolution Mechanism in accordance with ***Article 189(3) of the Constitution*** and the ***Intergovernmental Relations Act***.

7. On 9th October 2017, the Attorney General in line with the Court's order invited parties to a meeting where the parties resolved to have

the dispute mediated upon by the ***Intergovernmental Relations Technical Committee*** hereinafter the ***IGRTC.***

8. On 16th November 2017, the parties agreed that the following issues arise for determination by the mediation process:-

   i. ***Whether the allocation of conditional grants in the division of Revenue Act, 2016 is made in accordance with Article 202(2) of the Constitution.***

   ii. ***Whether the accounting officer of the national government can spend money for conditional grants directly in the counties to undertake devolved function with the execution of an intergovernmental agreement under Article 187 of the Constitution.***

   iii. ***Which is the scope of an intergovernmental agreement under Article 187 of the Constitution?***

   iv. ***Whether the national interest means the interest of the national government and not of county governments.***

v. ***What is the meaning of national interest as a criteria of revenue allocation as per Article 203(1) (a) of the Constitution?***

vi. ***Whether the national interest means the interest of the national government and not of the county government.***

vii. ***Whether an allocation for national interest ought to be allocated exclusively to the national government.***

viii. ***Whether the national government can use the funds for the national interest directly to undertake devolved functions.***

ix. ***Whether the national government has a constitutional obligation to disburse to counties, as conditional or unconditional grants, money allocated as national interest that are earmarked for devolved functions.***

9. The first Mediation Report prepared by ***Intergovernmental Relations Technical Committee (IGRTC)*** was filed in Court on 14th September 2018 and it had the following conclusions:-

a) That the parties reached a consensus that conditional grants are derived from the National Government's share of the revenue. However, the parties noted that the Act defines conditional allocations as additional resources allocated to County Governments from revenue raised nationally.

b) With regards to issue no 2-4, the parties noted that the same had been addressed in circular no.8/2017 dated 29th August 2017 on Guidelines for management of Intergovernmental Fiscal Transfers in Kenya which addressed the division of revenue.

c) On the meaning of national interest, the parties agreed that the matter is polycentric in nature and this may not be adequately addressed in the mediation process.

10. On 14th October 2018, Hon. Lady Justice Okwany, upon consideration of the Report and arguments raised by the parties was convinced that, that all efforts to resolve the dispute had not failed and consequently ordered that issues No. 5 to 9 be submitted to a second mediation which would be facilitated by either the ***Intergovernmental Budget and Economics Council (IBEC)*** or

the summit for determination in line with provisions of ***Article 189(3) of the Constitution*** and ***Section 35 of the Intergovernmental Relations Act***.

11. The second mediation process was conducted by the ***Intergovernmental Budget and Economic Council (IBEC)*** which filed the Report in Court on 10th June 2020. The report findings on the meaning of national interest (***Article 203(1) of the Constitution)*** is as follows:-

a) In defining the meaning of national interest for the purposes of the COK 2010, one ought to be guided by Article 259 of the Constitution. The Commission on Implementation of the Constitution (CIC) defined the term national interest as: 'a set of agreed policies, goals, priorities and resultant programs which have fiscal implications and which benefit the country as a whole.' This definition was generally agreed upon by the mediation committee.

b) National interests transcends both levels of government as it benefits the entire country. National interest can therefore be the interest of either level of government.

c) Where a function has been earmarked as one being of national interest, an allocation for the same ought to be allocated to the government level that has been assigned the functions under the fourth schedule.

d) Article 187 of the Constitution provides that a function or power of government at one level may be transferred to a government at the other level by agreement between the governments. By virtue of this provision, either level of government can undertake a devolved function where there is existence of an agreement between the two levels.

e) Article 202(2) provides that County Governments may be given additional allocations from the national government's share of revenue, either conditionally or unconditionally.

PETITIONER'S CASE

12. The Petitioner argue that the language used in the Report is that of a possibility yet the diametric of division of revenue between the two levels of government is couched in mandatory terms in the constitution. The Petitioner contend that it is imperative that these

issues are well interpreted by this Honourable Court which is bestowed with jurisdiction under ***Article 165 of the Constitution*** to interpret the Constitution in order to provide a binding judgment to guide parliament in the preparation of future Division of Revenue Acts for the overall good and benefit of devolution.

THE 1ST AND 4TH RESPONDENTS CASE

13. The 1st and 4th Respondents urge that the parties deliberated and settled on the ***Intergovernmental Relations Technical Committee*** to mediate the dispute between the parties. The parties appeared before mediation on multiple occasions unfortunately, the mediation proceedings were upset and the Petitioner sought to have the court determine the very same issues which it had set to mediate.

14. The Parties being unable to agree on the way forward, the Court ordered that mediator do file his report with the Court to enable it make its determination on the extent of compliance with the ruling of Hon. Justice Muriithi. The Court (Hon. Okwany J) upon reading the report and upon hearing the parties issued a ruling, on 28th November 2018 ordering the parties herein, to return to the

mediation Table referring the matter to the Intergovernmental Budget and Economic Committee for determination. The Court ordered further in default of parties reaching an agreement, the matter be referred to summit in accordance with ***Article 189(3) of the Constitution*** for further attempts at alternative disputes resolution with a view to determining the issues in the Petition.

15. Arising out by the Court's Ruling (Hon. Okwany J) the secretariat of the Intergovernmental Budget and Economic Council (hereinafter IBEC) convened a technical committee meeting which deliberated the issues for determination in this matter and thereafter for emergent report presented to the full IBEC which adopted the findings of the committee and issued its report to court by hand of the Office of the Attorney General on 21st January 2020.

16. The Parties herein were able to agree on various working definition and guidelines that are expected to guide the division of revenue and matters on conditional and unconditional grants. The parties herein were also able to, under the guidance of the National Treasurer (4th Respondent) and Commission of Revenue Allocation (5th Respondent herein) determine the proper working definition of

'national interest' as found within ***Article 203(1) of the Constitution of Kenya 2010***.

17. The 1st and 4th Respondents contend that this Court ought to take Judicial notice of the note of the Commission of the same Allocation as established within ***Article 215 of the Constitution***.

18. ***Article 216 of the Constitutions*** sets out the functions of Revenue Allocation and provides as follows:-

"Article 216

(1) The Principal function of the Commission on Revenue Allocation is to make recommendations concerning the basis for the equitable sharing of revenue raised by the national government-

a) Between the national and county governments; and

b) Among the country governments.

(2) The Commission shall also make recommendations on other matters concerning the financing of, and financial

management by, country governments, as required by this Constitution and national legislation."

19. The 1st and 4th Respondents invite the Court to take Judicial notice of the composition of the IBEC as outlined within the Public Finance Management Act and note that almost all parties in this matter are represented within the Council.

THE 5TH RESPONDENT

20. The 5th Respondent urge that upon reference of this matter to the ***Intergovernmental Relations Technical Committee (IGRTC)***; the mediation team distilled the issues for determination and therefore filled a mediation report on 14th September 2018 and gave the findings on each of the 9 issues for determination.

21. The Petitioner was dissatisfied with IGRTC Report for reasons that the same did not solve the questions in contest in the Petition. The Petitioner requested the Court to give directions on the Petition. In a Ruling delivered on 28th November, 2018, this Honourable Court referred the following issues to mediation by the Intergovernmental Budget and Economic Council (IBEC) –

a) ***What is the meaning of national interest as a criteria of revenue allocation as per Article 203(1)(a) of the COK 2010.***

b) ***Whether the national interest means the interest of the national government and not of the country governments.***

c) ***Whether an allocation for national interest ought to be allocated exclusively to the national government.***

d) ***Whether the national government can use the funds for national interest directly to undertake devolved functions.***

e) ***Whether national government has a constitutional obligation to disburse to counties, as conditional or unconditional grans, money allocated as national interest that are earmarked for devolved functions.***

22. The IBEC filed its report in Court on 10th June, 2020. Having participated in the development of the report, the 5th Respondent associates itself with the findings therein.

23. The 5th Respondent contend that the only issue that remains for this Honourable Court's determination is whether the allocation of conditional grants in the ***Division of Revenue Act 2016*** was made in accordance with the Constitution.

ANALYSIS AND DETERMINATION

24. I have carefully considered the pleadings herein, parties rival submissions, and the mediation reports and from the same the issues arising thereto for determination can be summed up as follows:-

a) Whether the allocation of conditional grants in the Division of Revenue Act 2016 is made in accordance with Article 202 (2) of the Constitution and whether the national government can attach terms to funds disbursed as conditional grant?

b) Whether an accounting officer of the national government can spend money from conditional grants directly in the counties to undertake devolved functions without an intergovernmental agreement under Article 187 of the Contitution?

c) What is the meaning of "national interest" in the context of Division of Revenue between the two levels of government and whether what constitutes "national interest" is a justifiable issue for courts to determine?

A. WHETHER THE ALLOCATION OF CONDITIONAL GRANTS IN THE DIVISION OF REVENUE ACT 2016 IS MADE IN ACCORDANCE WITH ARTICLE 202 (2) OF THE CONSTITUTION AND WHETHER THE NATIONAL INTEREST CAN ATTACH TERMS TO FUNDS DISBURSED AS CONDITIONAL GRANT?

25. The Respondent herein, commission on Revenue Allocation is established under ***Article 215 of the Constitution*** and its Principal function is to make recommendations concerning the basis for the equitable sharing of the revenue raised by the National Government between the National and County Governments and among the county Governments as provided in ***Article 216(1) of the Constitution***.

26. ***Article 202(2) of the Constitution*** provides that county government may be given additional allocations from the national

government's share of the revenue, either conditionally or unconditionally.

27. In furtherance of the Constitutional direction enshrined in ***Article 202(2)*** and ***Article 187(2) of the Constitution***, the commission can make recommendations on the conditional allocations to counties. ***Article 203 of the Constitution*** sets out the criteria to be taken into account in determining the equitable shares provided for under ***Article 202 of the Constitution***.

28. ***Article 205(1) of the Constitution*** stipulates that when a bill that includes provisions dealing with the sharing of revenue, or any financial matter concerning country government is published, the commission shall consider those provisions and may make recommendations to the National Assembly and the Senate. On its part, ***Article 203 (2) of the Constitution*** stipulates that any recommendations made by the Commission shall be tabled in parliament, and each House shall consider the recommendations before voting on the Bill. It should be noted that the Senate plays a key role in division of revenue between the two levels of government.

29. The responsibility to control public funds is clearly vested in the National Treasury pursuant to ***Article 225 of the Constitution*** and the ***Public Finance Management Act, 2012*** and the Treasury performs these duties together with parliament.

30. On division of revenue, ***Article 218 of the Constitution*** provides for the manner in which the Senate and the National Assembly should process thus:-

> ***"218. Annual Division and Allocation of Revenue Bills***
>
> ***(1) At least two months before the end of each financial year, there shall be introduced in Parliament—***
>
> ***(a) a Division of Revenue Bill, which shall divide revenue raised by the national government among the national and county levels of government in accordance with this Constitution; and***
>
> ***(b) a County Allocation of Revenue Bill, which shall divide among the counties the revenue allocated to the county***

level of government on the basis determined in accordance with the resolution in force under Article 217.

(2) Each Bill required by clause (1) shall be accompanied by a memorandum setting out—

(a) an explanation of revenue allocation as proposed by the Bill;

(b) an evaluation of the Bill in relation to the criteria set out in Article 203(1); and(c) a summary of any significant deviation from the Commission on Revenue Allocation's recommendations, with an explanation for each such deviation."

31. In dividing the revenue raised nationally, the Senate and the National Assembly rely on the criteria in ***Article 203 of the Constitution*** to determine the amount of revenue that should be allocated to the national and country governments.

32. ***Article 202 of the Constitution*** requires that the criteria be taken into account to determine the equitable share, which clearly means

that the figure is not fixed and varies every year based on the following criteria:-

a) The national interest;

b) Any provision that must be made in respect of the public debt and other national obligations;

c) The needs of the national government, determined by objective criteria;

d) The need to ensure that country governments are able to perform the functions allocated to them;

e) The fiscal capacity and efficiency of country governments;

f) Developmental and other needs of counties;

g) Economic disparities within and among counties and the need to remedy them;

h) The need for affirmative action in respect of disadvantaged areas and groups;

i) The need for economic optimisation of each county and to provide incentives for each county to optimise its capacity to raise revenue;

j) The desirability of stable and predictable allocations of revenue; and

k) The need for flexibility in responding to emergencies and other temporary needs, based on similar objective criteria.

33. It therefore follows that the share revenue to the counties can vary so long as the amount allocated to the County is not less than (15%) of fifteen per cent of all revenue collected by the national government.

34. The Petitioners contend that the division of revenue is a process that concerns the application of national resources to development and indeed how the resources will be allocated. It is urged one of the principles of public finance as embedded in ***Article 201(b) of the Constitution*** is that the public finance system shall promote an equitable society. ***Article 202 (1) of the Constitution*** provides that revenue raised nationally shall be shared equitably among the national and county governments. The legal instruments that elaborates how revenue is to be shared between the two levels of government is the Division of Revenue Act which is enacted yearly by parliament.

35. The focus of this Petition is ***Article 202(2) of the Constitution*** which states that County Government may be given additional

allocation from the national government's share of revenue, either conditionally or unconditionally. The use of the would 'may' in my view connotes that the issuance of conditional or unconditional grants is at the discretion of the national government.

36. ***Article 203 of the Constitution*** as already indicated herein above provides the criteria that shall be taken into account in determining the equitable share for each level of government. It therefore follows the division of revenue between the two levels of governments is partly informed by the role played by each of the government amongst other factors such as fiscal capacity and efficiency of county governments as well as the development and other needs of the counties.

37. Further ***Article 230(1) of the Constitution*** provides that one of the criteria is the need to ensure that country governments are able to perform the functions allocated to them in the Fourth schedule of the Constitution. This provision in my view is intended to promote the principles of development governance set out in ***Article 175(b) of the Constitution*** which provides that County governments shall have reliable source of revenue to enable them to govern and deliver service efficiently.

38. In the instant Petition, the Petitioner contend that the ***Division of Revenue Act*** for financial year 2016/2017 provides for the allocation of funds for devolved functions to the National Government as follows:-

a) Kshs.4,121 Billion for Free Maternal Health Care

b) Kshs.4.5 Billion for leasing Medical Equipments

c) Kshs.4.5 Billion for Level 5 hospitals.

39. The Petitioner contend that in an attempt to cure the above fundamental breach, the ***Division of Revenue Act, 2016*** went ahead to make the allocation as a conditional grant. The allocation of money to the national government to undertake the above devolved functions on paper, it is urged, appears as conditional grant but the Petitioner urges in reality it is the accounting officers of the national government who manage the funds.

40. In respect of ***Revenue Bill 2016***, the ***Commission on Revenue Allocation*** contend that, the commission makes its recommendation of the division of revenue through a consultation process. That in its recommendation; the commission noted, that in accordance with ***Article 187(2) of the Constitution***, which provides

that; if a function or power is transferred from a government at one level to a government at the other level, then arrangements shall be put in place to ensure that the resources necessary for the performance of the function or exercise of the power are transferred. The Commission therefore contend that it is in line with the principle of ***"funds follow functions"*** and invariably requires clear linkages between assigned function, planning, budgeting and revenue allocation either level of government.

41. In the instant Petition the Petitioner has not submitted that the ***Division of Revenue Act 2016*** failed to allocate the counties the minimum 15% of nationally raised revenue and this can be seen from the following statement in the Explanatory memorandum to the ***Division of Revenue Bill, 2016***;

"6. After making the above adjustment, County Governments' equitable share of revenue in the financial year 2016/2017 is estimated to be Khss.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. Kshs.935.7 billion)."

42. From the above it turns out the Parliament did not violate the constitution as it allocated the county governments the minimum of 15% required and therefore, having received more than the constitutionally mandated minimum of 15%. It is not demonstrated that there is a constitution violation to warrant High Court to invoke its jurisdiction under ***Article 165 of the Constitution***.

43. A perusal of the explanatory Memorandum to the ***Division of Revenue Bill, 2016***, the following statements explain the manner in which the revenue raised nationally was divided between the national and the country governments:-

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

4. The DoRB, 2016 proposes to allocate the County Governments Kshs.302.2 billion in the financial year 2016/17, which relative to the 2014/15 allocation, reflects an increase of Kshs.20.4 billion or 7 per cent. This allocation comprises of an equitable share of Kshs.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 Kshs.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."

44. As regards conditional allocations, the Explanatory memorandum is clear that the conditional allocations are drawn from the national government's share of revenue:

"Additional Conditional Allocations to County Governments

7. Article 202(2) of the Constitution provides for additional allocation to County Government 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:"*

45. It therefore follows from the above that, in the financial year 2016/2017, the county governments were allocated the sum of Kshs.280.3 billion from a total national revenue of Kshs.935.7 billion which is 29.95% of the revenue raised nationally. The Petitioner having received then an additional 29.95% of the revenue raised annually, the national government clearly made additional allocation to the country governments as per paragraph 7 of the explanatory memorandum to the ***Division of Revenue Bill, 2016***.

46. In the instant Petition it should be noted the commission took into account that at the time of making conditional allocations, the national government had not fully devolved some of the functions assigned to the country in the Fourth Schedule of the Constitution. Some of the devolved functions were either being performed by the ministers or various corporations that existed before devolution. The Commission thus took into account the functions assigned to each level of government to ensure there is no mismatch between the resources and delivery on responsibilities assigned to the national and country governments. This therefore lead to the commission

making its recommendations pursuant to ***Article 216(5) of the Constitution*** and ***Section 190 of the Public Finance Management Act*** to the Senate, the National Assembly the National Executive, County Assemblies and County Executives.

47. The Commission in arriving at its recommendations was guided by ***Chapter 12 of the Constitution*** which provides for the principles, legal and institutional framement of public Finance; which recommendation were issued in fulfilment of its constitutional role.

48. The 5th Respondent relies on the High Court decision in ***County of Mandera & 2 others v. The Commission on Revenue Allocation & 4 Others [2017] eKLR*** where Mativo J. stated thus:

"One of the most important policy changes ushered in by Kenya's 2010 constitution was an overhaul of the way in which resources are shared across the country. The Constitution took this power away from the executive and created new bodies, including the Commission on Revenue Allocation and the Senate, to lead a more transparent and objective process of deciding how to share resources. Article 216 (1) of the Constitution mandates the Commission on Revenue Allocation

to make recommendations concerning the basis for the equitable sharing or revenue raised by the National Government between the national and county governments, and among the country governments. Article 216(2) mandates the Commission to make recommendations on other matters relating to the financing of, and financial management by, county governments and to encourage fiscal responsibility."

49. Similarly in the case of ***Council of Governors & 47 others v. Attorney general & 3 Others (Interested Parties); Katiba Institute & 2 Others (Amicus Curiae) [2020] eKLR*** where the Court, while holding that the advise of the Commission is not binding on Parliament, the Court nonetheless affirmed the positon of the recommendation of the 5th Respondent as follows:-

"[56] A critical reading of the provisions cited above, leaves no doubt that the Constitution places a very high premium on the recommendations by the Commission for Revenue Allocation. Such recommendations once tabled in Parliament, must be accorded due consideration before a vote takes place in either of the Houses, on the Division of Revenue Bill and the County Allocation of Revenue Bill. This is the unequivocal prescription

in Article 205 of the Constitution. Even where the National Government intends to appropriate money form the Equalization Fund, the Commission must still be consulted, and if following such consultation, it makes recommendations, the National Assembly must consider the same before passing on Appropriation Bill.

[57] In view of the foregoing, it is our considered opinion that, where either of the two Houses passes a Bill envisaged under Article 205 of the Constitution, without considering the recommendations of the Commission on Revenue Allocation, the resultant legislation would be unconstitutional. By the same token, where the National Government appropriates money from the Equalization Fund without consulting the Commission, the resultant legislation would suffer a similar fate. The same result would obtain were the national Assembly passes legislation authorizing the National Government to appropriate money from the Equalization Fund without considering the recommendations, if any, by the Commission on Revenue Allocation."

50. The Commission further contend in accordance with the provisions of ***Article 216(1) (a)*** and ***Article 203(1) of the Constitution***, the Commission recommended that the allocation of the conditional grants should be equitable and their distribution should not compromise the independence of the county governments as regards budgeting, planning and budget execution.

51. The Court while addressing itself to the rationale behind fiscal responsibility in ***Speaker, Nakuru County Assembly & 46 others v. Commission on Revenue Allocation & 3 Others [2015] eKLR***, stated:

"Fiscal reporting mechanisms are clear at the National level and so are they in the County level with the County Executive, County Treasury and County Assemblies each charged with the responsibility of ensuring accountability and transparency in utilization of County resources and specifically, the mandate of approving County Budgets in the responsibility of a County Assembly"

52. The Commission's Constitutional mandate clearly is to encourage fiscal responsibility in the formulation of policy geared towards

ensuring accountability and transparency in the utilization of public finances. The management of intergovernmental transfers, including the duties of the national accounting officer in managing intergovernmental transfers to counties are set out in ***Regulation 130 of the Public Finance Management (National Government) Regulations, 2015*** which includes:-

"a) ensuring that transfers to a county government –

i) are made in accordance with the frameworks governing the conditional and unconditional transfers to county governments; and

ii) are deposited only into the Country Revenue Fund of a County Government; and

iii) are made in accordance with the relevant Act of Parliament unless the allocations are withheld or stopped in terms of Article 255 of the Constitution."

53. Further a national government accounting officer who transfers any conditional allocation to country government shall, in addition to any other requirement in terms of the Act or any other applicable law or framework governing the allocation, monitor and evaluate the

financial and non-financial performance of programmes, fully or partially funded by the allocation and submit to the National Treasury –

a) *A quarterly report within 30 days after the end of each quarter;*

b) *An annual report within three months after the end of the financial year;*

c) *The attendant conditions of any conditional grant to a country accounting officers.*

54. It is further provided that at ***Regulation 130 (4) of the Public Finance Management (National Government) Regulations, 2015***, the reports referred to include information that: -

"a) indicate the total amount of funds transferred to each county government;

b) Indicate the amount of funds withheld or stopped form any county government, the reason for withholding or stopping and the action taken by the national government Accounting

Officer and the county government Accounting Officer to deal with the matters that necessitated the withholding or the stoppage of the transfer;

c) ***Indicate any reductions or additions of conditional or unconditional allocations to county governments authorized by the National Treasury;***

d) ***Indicate the funds, if any, spent by the national government Accounting Officer on the administration of the transfer to the counties; and***

e) ***That may be required under the relevant law or framework governing the transfer by the National Treasury."***

55. The County Government Accounting Officer in accordance with ***Regulation 131 (1) (a) of the Public Finance Management (National Government) Regulations, 2015*** is responsible; for ensuring compliance with the requirements of the relevant law and frameworks governing the management of conditional transfers from the national government.

56. The Regulations envisage that the County Government Accounting Officer has the first mandate to monitor and evaluate the financial and non-financial performance of programmes, fully or partially funded by the allocation and report the same to the national government accounting officer, who subsequently reports to the national treasury.

57. The conditional allocation are drawn from the National Government share. The conditional grant in the Cambridge dictionary is defined as follows:-

"condition noun (Agreed Limit)

An arrangement that must exist before something else can happen."

58. ***Article 202 (2) of the Constitution*** provides ***"County Governments may be given additional allocations from the national government's share of the revenue, either conditionally or unconditionally."*** This in my view means where ***"conditional allocation"*** is made by the national government to the counties, the national government may impose conditions, that it deems fit for disbursement and management of the funds in a

manner that meets the objectives of the national government. It should be noted that the ***"conditional allocations"*** are from the national government share of revenue and as such there is justification for imposing conditions by national government to have its objectives met.

59. I find in the instant Petition, there is no challenge to constitutionality of the various ***Regulations of the Public Finance Management (National Government) Regulations, 2015*** relied upon by the 5th Respondent; as regards the function of monitoring and evaluating conditional allocations to County Governments which, ultimately lies with the National Government.

60. In the case of ***Institute of Social Accountability & Another V. National Assembly & 4 others [2015] eKLR***; the Court held that:-

"Conditional grants are a feature of most fiscally decentralized counties. Through conditional grants, the national government is able to achieve certain national governmental objectives within the decentralized units. What is paramount though is that the nature and design of such grants must respect the constitutional architecture."

61. The Petitioner urge that the ***Division Revenue Act 2016*** defines ***"conditional allocations"*** as ***'additional resources allocated to County Governments <u>from revenue raised nationally.'</u>*** The Petitioners urge that the definition thereto is wrong, contravenes ***Article 202(2) of the Constitution*** and in effect interferes with the County Governments autonomy and undermines devolution.

62. The 1st Mediation report states that Conditional grants are derived from the National Government's share of revenue. It therefore follows that conditional grants are allocated to the counties from the national government's share of revenue and not from the revenue raised nationally. I therefore find that the proper and justifiable way would be for the Act to indicate the additional money allocated to the counties is from the national government's share specifying the conditions for their expenditure. Conditional grants bear conditions and for this reason the national government may impose conditions on how finances advanced to the county governments ***under Article 202(2)*** are to be utilised.

63. I therefore find that it is proper to take the conditional grants as money transfers from one level of government to another, either through competitive ***project grants*** or through more general ***block***

grants which is essentially and annual sum of money that is awarded by a national government to a county government to help fund a specific project. It is noteworthy that a national government places conditions on the use of the transferred funds by the recipient government. The conditions may be either financial or substantive in nature. In other words, the grantor uses these grants to induce certain reactions on the part of the grantee in order to bring a county level of government into line with the national level of government's policy objectives. The greater the conditions placed upon the grant, the less flexible is the program for the recipient government.

64. I am of the view that the nature of conditions should not be constant for all counties but can vary from one county to another. The conditional grants may be materially or non-materially. The conditions may be imposed by the sphere of government allocating the funds, or the two spheres of government may negotiate them. In either case, an important feature of conditional grants is the method used to enforce the conditions. With specific grants, enforcement will typically not be an issue: the grant will only be paid if the recipient government undertakes the specific spending. For block grants, enforcement is more difficult because the conditions are typically rather value and subject to interpretation. The following methods of

enforcement are possible in this scenario that is, the national government may enforce the conditions by penalising the county level of government whose programmes do not meet them or where there may be some dispute settlement mechanisms, possibly the courts, may be used for adjudication.

65. It is expected that if there are any financial conditions imposed on the county level of government, the conditions will usually entail matching requirements, and they are typically stated as a percentage of the conditional grant amount or as a percentage of total project costs, and financial matching requirements must come from local revenues raised by the country level of government or from its non-conditional share. On the other hand, substantive requirement reflect the nature of uses to which the recipient may apply the revenue granted by the national level of government.

66. The extent to which conditional grants are used and their design depend very much on the constitutional, institutional and fiscal circumstances. In the most general sense, the purpose of conditional grants is to influence the fiscal decisions of the county level of government presumably with the express intent of achieving

some objective of the national level of government, including objectives that are stipulated by the Constitution.

67. It is expected that if the conditional funds are allocated to the county level of government, the funds would then be sent through the County Revenue Fund to the specific counties for the specific functions outlined by the national level of government. The effect of a conditional grant is that the funds are channelled directly to the activities in question and accounted for. The funds cannot be appropriated by the County Assembly through a County Appropriation Bill.

68. The Petitioner urge that according to the ***constitutional law expert, John Mutakha Kangu,*** the equitable share is a right of each government and not a discretionary donation by national governments to the County Governments. In his book, ***'Constitutional Law of Kenya on Devolution' at page 252*** he contends that there are three forms of funding for County governments' from revenue raised nationally namely:

   i. An entitlement to an equitable share of revenue raised nationally;

ii. Additional allocations from the national government's share of the revenue raised nationally which is given either conditionally or unconditionally; and

iii. Equalisation funding from the revenue raised nationally.

69. In the submissions by the South Africa's Financial and Fiscal Commission to the South African Parliament to enable the enactment of the South African Division of Revenue Bill of 2002 with Specific Reference to the Conditional Grant System, the Commission stated that:

"Conditional grants are used in most decentralized systems of government to enable <u>specified national objectives. The Constitution states that conditional grants must be provided from the national equitable share and that the division of revenue must recognize the role played by conditional grants within the national equitable share.</u> This implies that there is a trade-off between increasing conditional grants to provinces and municipalities and the total amount available for equitable sharing between the 3 spheres of government.

70. Further according to the submission by the ***South African Commission, "conditional grants"*** are used as an intervention tool for the national level of government where there are concurrent functions. As such, in a bid to protect the respect of the institutional and functional integrity of either level of government, there ought to be an identification of objectives to be achieved and the monitoring of the performance of the various projects the funds are meant for. The two levels of government are also expected to make accountability arrangements and these arrangements clarified upfront. The national level of government is thus expected to have a Conditional Grant Framework with key requirements such as the purpose and conditions of the grant, measureable outputs and delivery indicators, why the objective cannot be met through the Equitable Share mechanisms, the projected lifespan of the grant and that the allocation criteria that must comply with the Constitution.

71. ***Article 202 of the Constitution*** provides for two forms of allocations. ***Article 202(1)*** provides for the ***Division of Revenue Act*** in the sense that it provides for the equitable sharing of the revenue raised nationally between the national level of government and the county level of government as provided for under ***Article***

218(1)(a) of the Constitution. The other allocations provided for under ***Article 202 of the Constitution*** are conditional or non-conditional grants. ***Article 202(2) of the Constitution*** is instructive that the funds used as conditional or non-conditional grants are from the share allocated to the national level of government.

72. When allocating funds to the county level of government as either a conditional or non-conditional grant, it is expected that the allocation is made from the national level of government's share. Secondly, it is trite from the language used in ***Article 202*** as read with ***Article 218(1)(a) of the Constitution***, conditional or non-conditional grants are not an item to be provided for under the ***Division of Revenue Act***. Conditional and non-conditional grants can be issued to the county level of government under the auspices of ***Article 190 of the Constitution*** or through an agreement between the two levels of government that respects the institutional and functional integrity of the either level of government.

73. It is clear from the above that the conditional grants given to counties by the national government must emanate from its own share of the equitable revenue and not directly from the equitable share as contemplated under ***Article 202 (2) of the Constitution***. Secondly,

there ought to be a framework stating the purpose, the goal and the mechanism for the issuance of the conditional grant. Deviating from the set principles in ***Article 203 of the Constitution*** means that the equitable share raised nationally will significantly reduce resulting to a decrease in the equitable share allocated to counties. This would also mean that the decreased equitable share to counties undermines their financial autonomy since it restrains implementation of budgets.

74. In view of the above I find that conditional grants to counties should come from the National Government's share whereas funds for devolved functions should be allocated directly from the nationally raised revenue and not through the national government's share. I am of the view that the definition of ***"conditional allocations"*** used in ***Section 2 of the Division of Revenue Act of 2016*** that ***["conditional allocations" for the purposes of this Act, means additional resources allocated to county governments from revenue raised nationally]*** is not only misleading but patently unconstitutional for going against the provisions of ***Article 202(2) of the Constitution*** which states that ***"additional allocations"*** from the national government's share may be given either conditionally or unconditionally to county governments.

75. In view of my findings herein above, I am of the considered view that it is proper for this Court to adopt the 1st Mediation report with regard to the issue of conditional grants and declare that the ***Division of Revenue Act, 2016*** contravened the provisions of ***Article 202(2) of the Constitution*** by defining that the conditional allocations to counties shall be from the revenue raised nationally instead of the national government's equitable share.

76. I find that the conditional grants in the ***Division of Revenue Act 2016*** were not done in accordance with the Constitution and it is evidently clear it is not in accordance with the law. The ***Division of Revenue Act, 2016*** contravenes the provisions of ***Article 202 (2) of the Constitution*** by defining that the conditional allocation to counties shall be from the revenue raised nationally instead of the national government equitable share. The ***Division of Revenue Act*** is therefore not made in accordance with ***Article 202(2) of the Constitution*** and is therefore unconstitutional.

B. WHETHER AN ACCOUNTING OFFICER OF THE NATIONAL GOVERNMENT CAN SPEND MONEY FROM CONDITIONAL GRANTS DIRECTLY IN THE COUNTIES TO UNDERTAKE DEVOLVED FUNCTIONS WITHOUT AN

INTERGOVERNMENTAL AGREEMENT UNDER ARTICLE 187 OF THE CONSTITUTION?

77. The Petitioner's position on the issue in the 1st Mediation Report is that it is this Court which can determine the functions to be undertaken by the National and County Governments. The issue was unresolved by the Report. The 1st Report recommend that circular No. 8 of 2017 dated 29th August 2017 on Guidelines for Management of Intergovernmental Fiscal Transfer in Kenya should be interpreted by the Court to ascertain on functions.

78. From the above it appears that issues of dual accountability arise where money for devolved functions is allocated to the County Governments through the national government. The issue for consideration is therefore clear that is, who should account for the money? Is it the accounting officer of the national government or the county governments?

79. It appears that at one hand the Principle Secretary to the relevant Ministry is bound to account since it is the equitable revenue shared to the national government while on the other, the accounting officer at the County government is obligated to account for actual

expenditure of the money sent to the County for specified activities. The Petitioner urge this process undermines the principles of Public Finance as envisaged in ***Article 201(a) of the Constitution*** which dictates that there shall be openness and accountability; including public participation in financial matters.

80. The Petitioners further contend that conditional grant cannot be spent at the national level, as it is mainly issued by the national government from its share to the counties. The national government may at its discretion set certain conditions for expenditure. The principal secretary, is obvious cannot spent money designated as conditional grant at the national level, as by doing so, would undermine the functional autonomy of county government.

81. Considering the ***Fourth schedule of the Constitution*** it is clear that, it assigns the two levels of government's specific functions which are outlined in part I and II of the Schedule. The functions are categorised as either exclusive, concurrent or residual functions. ***Article 187 of the Constitution*** provides that a function or power of government at one level may be transferred to a government at the other level by agreement between the governments. By virtue of this provision, the 2nd mediation report recommends that ***either***

level of government can undertake a devolved function where there is existence of an agreement between the two levels.

82. Upon considering the 2nd mediation report recommending that either level of government can undertake a devolved functions where there is existence of agreement between the two levels of government I find this to be a progressive and positive step towards enhancing devolved function and development in counties. I find that it would be in interest of eliminating the issues of dual accountability by adopting the 2nd mediation report recommending that either level of government can undertake a devolved function where there is existence of agreement between the two levels of government.

83. It should be appreciated that the purpose of conditional or unconditional funds is to enable the national government to meet its policy objectives at the County level of government. In doing so, the national government is expected to accede to the provisions of ***Article 189(1) of the Constitution*** by firstly, performing its functions and exercising its powers in a manner that respects the functional and institutional integrity of the county level of government. It also must respect the constitutional status of the county level of

government. Secondly, in the event that there is need for the enhancement of capacity or coordinating policies and administration at the county level of government, the national level of government is expected to liaise with the county level of government in a manner that respects the functional and institutional integrity of the county level of government as stated in ***Article 189(1)(c) of the Constitution.*** Therefore, there is a legitimate expectation that if conditional grants are allocated to the county level of government, the national government must liaise with the county level of government in effecting the policy considerations the grants are intended for.

84. In the instant Petition, it is Petitioner's position that no agreement or any transfer was done between the two levels of governments. The national government allocated money for functions meant for the county level of government without liaising with the county level of government and acted as if those functions are allocated to the national level of government without following the provisions of ***Article 187 of the Constitution***. To this date, the National Government has not executed the requisite inter-governmental agreement as required by ***Article 187 of the Constitution*** with

respect to the mentioned devolved functions on ***free maternal health care, leasing of medical equipment amongst others***.

85. The Respondents have not disputed the Petitioner's contention as stated hereinabove nor have they taken any rebuttal of the same. It therefore turns out that the respondents are in violation of the provisions of the constitution on the basis, that the national government accounting officers chose to directly spend money for conditional grants which was meant for the counties. It appears as if the national government has taken over the devolved functions, which in turn is against the spirit of devolution and contravenes the provisions of ***Article 187 and 189 of the Constitution***.

86. There is no doubt the national government in overlooking the provisions of ***Articles 187 and 189 of the Constitution*** its actions amounts to encroachment on the functions and mandate of county governments with respect to misinterpreting the law and allowing the accounting officer of the national government to spend money for conditional grants meant for counties.

87. The Respondents position is that the function of monetary and evaluating conditional grants to county governments lies ultimately

with the national government. This with due respect is totally wrong for allowing accounting officers of the national government to spend money from conditional grant meant for counties. I find that the national government may only intervene in activities of county governments pursuant to provisions of ***Article 190(3) of the Constitution*** and ***Section 21*** of the ***County Governments Act***. ***Article 190(3) of the Constitution,*** which states that:-

"Parliament may by legislation provide for intervention by the national government if a county government –

a) Is unable to perform its functions

b) Does not operate a financial management system that complies with the requirements prescribed by the national legislation."

88. I have carefully considered parties submissions, the provisions of ***Regulations 130, 131 of Public Finance Management (National Government, Regulations, 2015;*** and ***Articles 187 and 189 of the Constitution*** and find that the law is very clear, that when an accounting officer of the national government spends money for

conditional grants directly in the counties to undertake devolved functions without an intergovernmental agreement under ***Article 187 or 189 of the Constitution***, acts in breach of the Constitution and the Law.

C. WHAT IS THE MEANING OF "NATIONAL INTEREST" IN THE CONTEXT OF DIVISION OF REVENUE BETWEEN THE TWO LEVELS OF GOVERNMENT AND WHETHER WHAT CONSTITUTES "NATIONAL INTEREST" IS A JUSTIFIABLE ISSUE FOR COURTS TO DETERMINE?

89. The "National Interest" as defined in ***Article 203 (1) (a) of the Constitution*** is not a legal question but rather is a political question for the Executive and the Legislature to determine during the extensive yearlong budget process.

90. The Respondents contend that Article 203 permits the revenue allocation to be adjusted based on the criteria in ***Article 203 (1)*** **as long as the total county allocation meets the minimum threshold of 15% of the total revenue raised nationally.**

91. The Petitioner support the 2nd Mediation Report's interpretation of ***"national interest"*** as ***a set of agreed policies, goals, priorities and resultant programs which have fiscal implications, and which benefits the country as a whole*** and pray that the same be adopted as a judgment of this court.

92. The "national interest" is clearly defined under ***Article 203 of the Constitution***. I find that "national interest" is a key backbone in influencing the division of revenue between the two levels of government in line with ***Article 203 of the Constitution***. However, in the past this term has been misused to mean that "National interest" means the ***interest of national government***.

93. In considering whether the "national interest" is expendable, one has to have a look at ***Article 259 of the Constitution*** which the Petitioner seeks to rely on. ***Article 259(1) of the Constitution*** provides:-

> ***"259. Construing this Constitution***
>
> ***(1) This Constitution shall be interpreted in a manner that—***
>
> ***(a) promotes its purposes, values and principles;***

(b) advances the rule of law, and the human rights and fundamental freedoms in the Bill of Rights;

(c) permits the development of the law; and

(d) contributes to good governance."

94. The Petitioner aver seeking that the meaning of ***"national interest"*** must be guided by ***Article 259 of the Constitution***; dealing with construing the Constitution, and agrees with the ***2nd mediation report*** which states that ***"the National interest transcends both levels of government as it benefits the entire country.*** **National interest can therefore be the interest of either level of government**. The 2nd Mediation Report further states that **Where a function has been earmarked as one being of national interest, an allocation for the same ought to be allocated to the government level that has been assigned the function under the fourth schedule"**.

95. The Respondents do not agree and take the ***"national interest"*** as advocated for by the Petitioner as misguided and misinterpretation of the Constitution in submitting that the funds allocated to national interest must not be dedicated before equitable allocation to the counties.

96. The Respondents urges that ***Article 203 of the Constitution*** requires that the criteria therein be a determining factor in allocation of revenue between the national and county government and the 3rd Respondent submits that what constitutes the national interest in each financial year is a political question.

97. ***Article 203(1) of the Constitution*** provides for the criteria to be taken into account in determining the equitable shares provided for under ***Article 202(1) of the Constitution*** and in all national legislation concerning county government enacted in terms of Chapter Twelve of the Constitution. ***"The national interest"*** is one of the criteria to be used for the determination of the equitable share. It is expected that when allocating the equitable share meant for the national government or the county level of government, ***"national interest"*** is taken into consideration.

98. From provision of ***Article 203 of the Constitution*** it follows that equitable share allocated to the county level of government may be increased or reduced based on ***"national interest"***. For instance, if the national interest is the enhancement of health services, more funds will be allocated to the county level of government to meet the goals and purpose of the national interest served by health. In

another instance, where Kenya has been attacked by an external aggressor, the national interest will be defence spending. That means that revenue allocated to the national level of government may increase based upon serving the ***"national interest"*** that is defence of Kenya's borders. The criteria set out in ***Article 203(1) of the Constitution*** is intended to insure equitable sharing of revenue.

99. It is noted however that the ***Division of Revenue Act 2016***, used ***"National Interest"*** as the basis for setting aside revenue in total contravention of the Constitution. It is expected that national interest would only apply in the allocation of revenue under ***ITEM G on Table 2: Evaluation of the Bill against Article 203 (1) of the Constitution***. ***"National Interest"*** cannot be the basis for setting aside revenue from the Consolidated Fund but is a criteria for the allocation of the equitable share under ***Article 202(1) and Article 218(1)(a) of the Constitution***.

100. The ***Division of Revenue Act*** allocated funds for national interest which are deducted from the equitable share before the money is shared equitably between the levels of governments. For instance funds for NYS and security are deemed to be national interest and allocated to the national government way before the revenue raised

nationally is shared between the national government and counties. The national interest is in my view just a factor to be considered before the funds are equitably allocated to each level of government. It does not constitute a separate faction that has to be allocated money.

101. Upon considering the parties submissions and the 2nd Mediation Report which has not been challenged or its contents denied by the Respondents or by any party and which the Petitioners agree with, I find that the ***"National Interest"*** transcends both levels of government as it benefits the entire country. I also find that where a function has been earmarked as one being of national interest an allocation for the same ought to be allocated to government level that has been assigned the function under the fourth schedule. I find the position should be as recommended in 2nd Mediation Report.

102. I further find that what constitutes a ***"National Interest"*** is a justifiable issue for the courts determination and as I have already dealt with what constitutes a ***"national interest"*** hereinabove, I need not say more than already stated hereinabove.

103. ***The upshot is that the Petitioner's Petition is merited and the same is granted in the following terms:-***

a) A declaration be and is HEREBY issued that the National Government cannot allocate itself funds for and undertake devolved functions, without first executing inter-government agreements required by Article 187 of the Constitution.

b) A declaration be and is HEREBY issued that in accordance with Article 202 (2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be netted from the national government's share of revenue and not from the overall revenues raised nationally.

c) A declaration be and is HEREBY issued that in accordance with Article 202(2) of the Constitution all funds christened in the Division of Revenue Act as conditional or unconditional grants should be disbursed to the Counties through the County Revenue Fund.

d) A declaration be and is HEREBY issued that 'national interest' as stated in Article 203(1) (a) of the Constitution does not necessarily connote functions of the national government as provided in the 4th Schedule of the Constitution.

e) A declaration be and is HEREBY issued that funds christened as 'national interest' in the Division of Revenue Act 2016 or any other Division of Revenue Act enacted to implement the provisions of Article 202 and 203 of the Constitution cannot be apportioned on devolved functions without the same being channelled to the Counties as conditional or unconditional grants.

f) A declaration be and is HEREBY issued that in its entirety, the Division of Revenue Act, 2016 is inconsistent with the provisions of Article 6(2), 10(2)(a), 174(c), (d) and (h), 202(2), 174(g), 175(b), 186, 186(2), 187(1), 189, 189(1) (c), 203(1)(d), and 217 of the Constitution.

g) An order be and is hereby issued directing the respondents to take necessary steps to amend the Division of Revenue Act, 2016 to conform to the provisions of Articles 202(2) and 203(1) of the Constitution.

h) I direct that each party do bear its own costs.

Dated, Signed and Delivered at Nairobi on this **3rd** day of **December, 2020.**

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J. A. MAKAU

JUDGE