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COMMISSION ON REVENUE ALLOCATION

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**RECOMMENDATION ON THE SHARING OF REVENUE
RAISED NATIONALLY BETWEEN THE NATIONAL
AND COUNTY GOVERNMENTS FOR THE FINANCIAL
YEAR 2016/2017**

17TH DECEMBER 2015

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COMMISSION ON REVENUE ALLOCATION

Our Ref: CRA/P&S/VOL

DATE: 17th December 2015

**Clerk of the Senate
Clerk of the National Assembly
Cabinet Secretary, National Treasury
Clerks of County Assemblies
Governors, County Governments**

Dear Sir/Madam

**RE: RECOMMENDATION ON SHARING OF REVENUE FOR
FINANCIAL YEAR 2016/17**

Pursuant to Article 216 (1)(a), the Commission on Revenue Allocation is mandated to make recommendations concerning the basis for the equitable sharing of revenue raised by national government between national and county governments.

Article 216 (5) requires the Commission to submit its recommendations to the Senate, National Assembly, the National Executive, County Assemblies and County Executives. Accordingly, the Commission hereby recommends that Ksh.331,765 million be allocated to county governments as equitable share and Ksh.45,752 million as conditional grants for 2016/17.

The equitable share of revenue for each county government for financial year 2016/17 has not been included in this document. This is because the second formula for sharing revenues, among county governments, had not been approved by the Senate at the time of releasing this recommendation.

Yours Sincerely,

Micah Cheserem

CHAIRMAN

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ACRONYMS AND ABBREVIATIONS

AG	Auditor-General
CBK	Central Bank of Kenya
CDA	Coast Development Authority
CoB	Controller of Budget
CRA	Commission on Revenue Allocation
DANIDA	Danish International Development Agency
EACC	Ethics and Anti-Corruption Commission
ENNDA	Ewaso Nyiro North Development Authority
ENSADA	Ewaso Nyiro South Development Authority
GDP	Gross Domestic Product
ICT	Information Communication Technology
IEBC	Independent Electoral and Boundaries Commission
IPOA	Independent Policing Oversight Authority
JSC	Judicial Service Commission
KBRR	Kenya Bankers Reference Rate
KeRRA	Kenya Rural Roads Authority
KNCHR	Kenya National Commission on Human Rights
KURRA	Kenya Urban Roads Authority
KVDA	Kerio Valley Development Authority
LBDA	Lake Basin Development Authority
MDAs	Ministries, Departments and Agencies
NG&EC	National Gender and Equality Commission
NLC	National Land Commission
OSR	Own Source Revenue
PAYE	Pay As You Earn
PSC	Public Service Commission
RDA	Regional Development Authorities
SRC	Salaries and Remuneration Commission
TARDA	Tana and Athi Rivers Development Authority
TSC	Teachers Service Commission
VAT	Value Added Tax

EXECUTIVE SUMMARY

In accordance with the provisions of Article 216(1)(a) and Article 203(1), the Commission recommends that out of the shareable revenue of Ksh. 935,653 million for the financial year 2013/2014, Ksh. 331,765 million be allocated to county governments as equitable share and Ksh. 45,752 million as conditional transfers for financial year 2016/17. The equitable share allocation to county governments is equivalent to 35.5 percent of the shareable revenue for 2013/14 amounting to Ksh. 935,653 million.

In making this recommendation, the Commission uses the allocation to county governments for financial year 2015/16 of Ksh. 259,775 million as the base. This base has been increased by Ksh. 39,200 million using a three year revenue growth rate of 15.09 percent. The years considered are 2012/13; 2013/14 and 2014/15.

The Commission further recommends that Ksh 27,790 million be allocated to counties for construction and rehabilitation of county roads, and Ksh. 5,000 million for public participation. The equitable share allocation may increase by Ksh. 4,732 million if devolved functions currently being performed by the Waters Services Board and the Regional Development Authorities are unbundled and transferred by the Transition Authority before the County Allocation of Revenue Bill 2016 is enacted.

The recommendation on conditional allocation has two components:

1. An adjustment to the current conditional allocations on Level 5 Hospitals, Maternal Health Care, Compensation for User Fees Foregone and Leasing of Medical Equipment by the three year average revenue growth of 15.09 percent. The Allocation on Road Fuel Levy Fund is based on 15 percent of the actual realized for the Fund for 2014/15 amounting to Ksh.31,707 million.

2. Provision for new conditional grants from the national government equitable share amounting to Ksh. 25,691 million to:
 - a. Cushion County governments on the huge wage bill,
 - b. Construction of headquarters for five counties, namely: Lamu, Tharaka Nithi, Nyandarua, Tana River and Isiolo.
 - c. Rehabilitation of primary and secondary schools,
 - d. Rehabilitation of village polytechnics, and
 - e. Establishment of Emergency Funds in 47 counties.

Table 1 provides a summary of the Commission recommendation on the equitable share to counties for financial year 2016/17. The equitable share due to national government is presented in Table 4.

Table 1: Equitable Share to County Governments

	ITEM	2015/16 Ksh. Million	2016/17 Ksh. Million
A	EQUITABLE SHARE TO COUNTIES		
1	Latest Audited Accounts	2012/13	2013/14
2	Shareable Revenue based on Audited Accounts	776,858	935,653
3	Equitable Share (Baseline)	259,775	259,775
4	Adjust by the three year average revenue growth of 15.09 percent		39,200
5	Add Allocation for County Roads		27,790
6	Add Allocation for Public Participation	-	5,000
7	Total Equitable Share to Counties¹	259,775	331,765
8	Percentage Share to Counties	33.44%	34.53%
B	CURRENT CONDITIONAL ALLOCATIONS	2015/16	2016/17²

¹ The Equitable Share to County Governments may increase by Ksh. 4,732 million if devolved functions currently performed by the Waters Services Boards; and those performed by the Regional Development Authorities

² Allocation of conditional grants to County Governments for financial year 2015/16 have been adjusted by the three year revenue growth rate of 15.09 percent

	ITEM	2015/16 Ksh. Million	2016/17 Ksh. Million
9	Level 5 Hospitals	3,600	4,143
10	Free Maternal Health Care	4,298	4,947
11	Compensation for user fees forgone	900	1,036
12	Leasing of medical equipment	4,500	5,179
13	Road Fuel Levy Fund (15% of Actual 2014/15)	3,300	4,756
14	Sub Total	16,598	20,061
C	NEW CONDITIONAL GRANTS		
15	Personnel emoluments for devolved staff	-	5,196
16	Construction of headquarters in five Counties ³	-	4,000
17	Rehabilitation of primary and secondary schools	-	5,000
18	Establishment of County Emergency Funds (2% of Equitable Share: Ksh. 259,775 Million)	-	5,196
19	Rehabilitation of village polytechnics	-	6,300
20	Sub Total New Conditional Grants	-	25,691
21	Total Conditional Grants	16,598	45,752
D	Total Transfer to Counties for 2016/17	276,373	377,517

Source: CRA 2015

³ This conditional allocation will be used to build headquarters for the following five counties: Lamu, Tharaka Nithi, Nyandarua, Tana River and Isiolo

1.0. INTRODUCTION

1.1 Background Information

Article 216(1)(a) of the Constitution of Kenya mandates the Commission on Revenue Allocation (CRA) to make recommendations concerning the basis for the equitable sharing of revenue raised nationally between the national and county governments. The constitution further stipulates in article 203(1) the criteria to take into account when determining the equitable share between the two levels of Government, they include:

- (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 county governments are able to perform the functions allocated to them;
- (e) developmental and other needs of counties;
- (f) the desirability of stable and predictable allocations of revenue; and
- (g) the need for flexibility in responding to emergencies and other temporary needs, based on similar objective criteria.

The Commission has over the past three years made its recommendation on the division of revenue through a consultative process. This process has given valuable input into the preparation of the recommendations which informs the Division of Revenue Bill prepared by the National Treasury for debate in Parliament.

During the financial year 2013/14, county governments received Ksh. 190 billion, which translated to 31 percent of the total shareable revenue based on the Audited Exchequer Accounts of 2011/2012. In 2014/15, a total of Kshs. 259.8 billion was allocated to counties compared to Kshs. 226.7 billion allocated in 2014/2015. This represented an increase of 14.6 percent in funds allocated to county governments. The allocation to

counties for 2014/15 is equivalent to 33.4 percent of the shareable revenue for financial year 2012/13 amounting to Ksh. 776, 858 million.

1.2 Legal Framework for Revenue Sharing

1. The Constitution of Kenya 2010 provides for a devolved system of government in which the sovereign power of the people is exercised at the national and county levels, (Article 6).
2. Article 202 (1) stipulates that revenues raised nationally be shared equitably among the national and county governments.
3. Article 202 (2) stipulates that county governments may be given additional allocations from the national government's share of revenue, either conditionally or unconditionally.
4. Article 203(1) stipulates the criteria to be taken into account in determining the equitable shares between the national government and the county governments.
5. Article 203(2) stipulates that for every financial year, the equitable share of revenue raised nationally that is allocated to county governments shall be no less than fifteen percent of all revenue collected by the national government.
6. Article 205 (1) stipulates that when a bill that includes provisions dealing with the sharing of revenue, or any financial matter concerning county governments is published, the Commission on Revenue Allocation shall consider those provisions and may make recommendations to the National Assembly and the Senate.
7. Article 205 (2) stipulates that any recommendations made by the Commission on Revenue Allocation shall be Tabled in Parliament, and each House shall consider the recommendations before voting on the Bill.
8. The Commission, under Article 216 (1) (a) of the Constitution is mandated to make recommendations concerning the basis for equitable sharing of revenue raised by the National Government between the national and county governments.

9. Article 218 stipulates that at least two months before the end of each financial year, there shall be introduced in parliament 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 the Constitution. The Bill shall be accompanied by a memorandum setting out a summary of any significant deviation from the Commission on Revenue Allocation's recommendations, with an explanation for each deviation.
10. Article 219 provides that a county share of revenue be transferred to the county without undue delay and without deduction.

1.3 Performance of the Economy

Kenya's Gross Domestic Product (GDP) grew by 5.3 percent in 2014 compared to 5.7 per cent recorded in 2013. The economic sectors recorded growth of varying magnitude except the hotels and restaurants whose growth contracted during the period. The slow growth in the hotel and restaurant industry was mainly attributed to reduced activities in the tourism sector occasioned by both internal and external shocks mainly, insecurity concerns and negative travel advisories by some key tourist source countries.

The main drivers of the GDP growth on the demand side during the period included: Government and private consumption; Low oil prices; increase in exports; and, stability of the Kenya Shilling against major currencies, despite slight depreciation against the US dollar.

The main drivers on the supply side included improved performance in: mining and quarrying (14.2 percent); information and communication (13.4 percent); construction (13.1 percent); financial and insurance activities (8.3 percent); real estate (5.6 percent); transport and storage (5.0 percent); and, Agriculture, forestry and fishing (3.5 percent). The manufacturing sector benefited from an improved economic

environment during the review period. Some of the factors that positively influence the industry include: slightly cheaper and stable electricity supply; restrained inflation; and, resilient domestic demand.

1.3.1 Inflation

The rate of inflation maintained its single digit level rising from 5.7 percent in 2013 to 6.9 percent in 2014 and eventually dropping to 6.6 percent during the first quarter of 2015. The Central Bank of Kenya (CBK) adopted monetary policy measures in 2014 that contributed to the easing of inflationary pressure. Through these policies, relative price stability was achieved with inflation rate remaining close to the target of 5.0 percent. The CBK retained the Central Bank Rate (CBR) at 8.50 percent throughout the period in an effort to anchor inflationary expectations.

1.3.2 Interest Rate

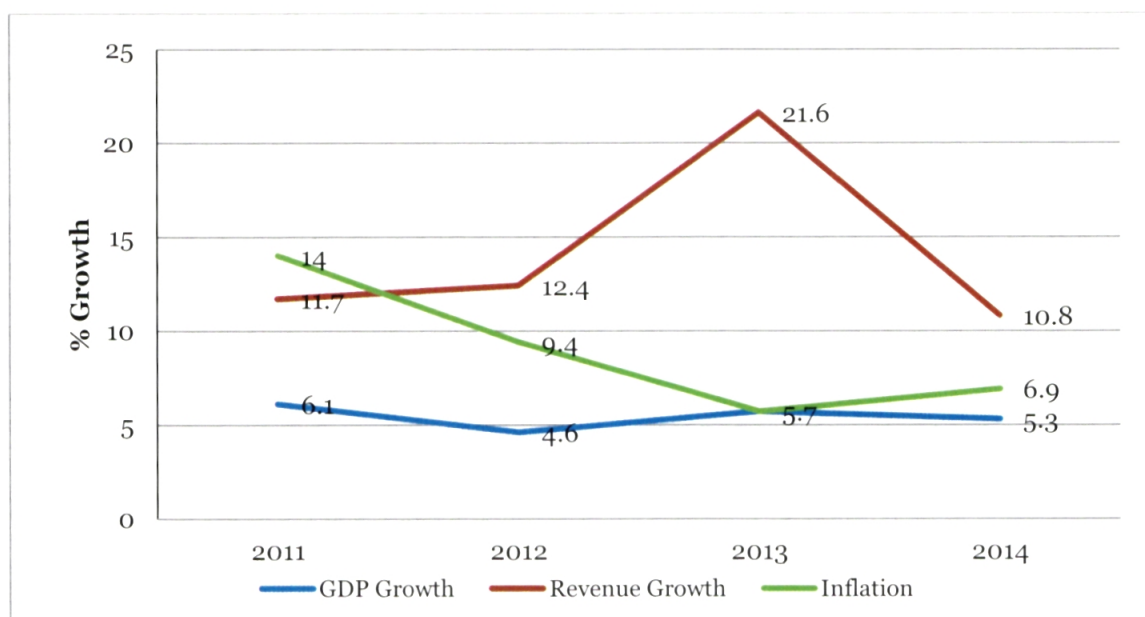
During the review period, interest rates remained stable, with the 91-day Treasury bill rate settling at 8.58 percent in December 2014. Broad money supply (M3) grew by 19.0 percent which was close to the policy target over the period. Commercial banks credit to the national government declined with its share in total credit dropping from 22.7 percent in December 2013 to 9.7 percent in December 2014. The share of the banks' credit going to private sector increased from 61.2 percent of total domestic credit to 80.2 percent.

The Kenya Bankers Reference Rate (KBRR) initially set at 9.13 percent in July 2014 was reviewed down to 8.54 percent in January 2015. The average yield rate for the 91-day Treasury bills, which is a benchmark for the general trend of interest rates, continued to increase from 10.56 percent in July 2015 to 11.54 percent in August 2015. Similarly, the inter-bank rates increased to a level of 18.63 percent in August 2015 (Economic Survey, 2015).

1.3.3 Exchange Rate

The Kenya Shilling weakened by 0.9 percent against major world currencies as reflected in the overall Trade Weighted Index which deteriorated from 107.06 in 2013 to 107.98 in 2014. This was mainly attributed to depreciation of the Kenya Shilling against the currencies of major trading partners. The currency depreciated against the US dollar to Ksh. 97.7 in June 2015 from Ksh. 87.92 in June 2014, mainly due to the global strengthening of the US Dollar on the international market, and high dollar demand by importers in the domestic market. Within the East Africa Community, the Kenya Shilling depreciated against the Rwandese francs and Ugandan Shilling by 3.1 percent and 1.7 percent respectively in 2014. The Kenya Shilling however appreciated by 7.4 percent against the Tanzanian Shilling during the same period. Figure 1 presents trends of the gross domestic product, revenue growth and inflation over the last five years.

Figure 1: GDP, Revenue and Inflation Rate



Source: Kenya Economic Survey, 2015

The overall macroeconomic outlook remains unfavorable following the depreciation of the Kenya shilling and the spiraling effect of lending rates by commercial banks. This is likely to be compounded by increased recurrent expenditures by both national and county governments.

1.4 Public Debt

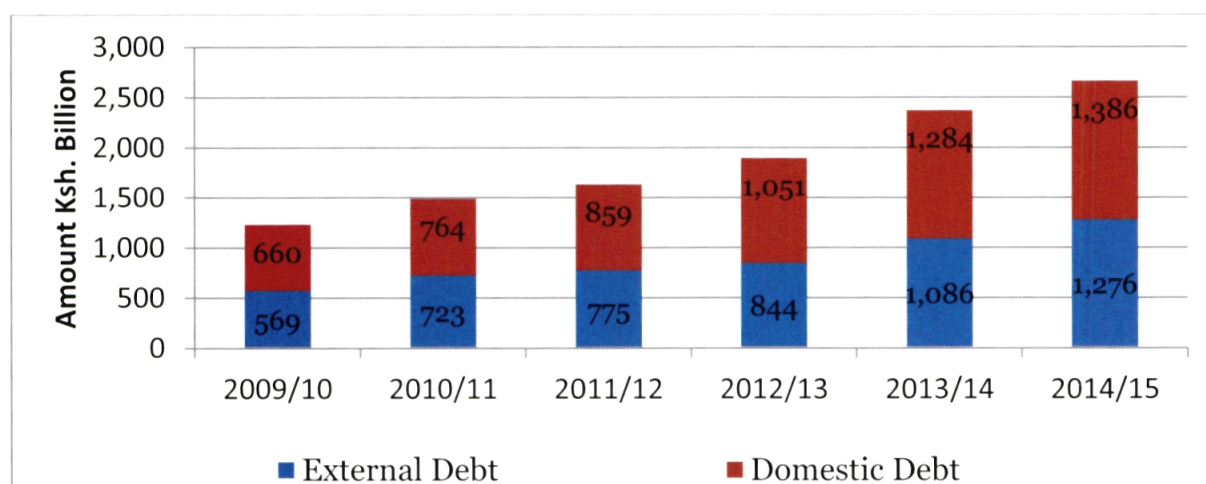
Kenya's public and publicly guaranteed debt rose by Ksh. 458.9 billion to close at Kshs. 2,829.1 billion (52.8 percent of GDP) in June 2015 from Kshs. 2,370.2 billion (44.2 percent of GDP) in June 2014 comprising of 50.05 percent of external debt and 49.95 percent of domestic debt. The net public debt increased by Kshs. 384.1 billion from June 2014 to June 2015. Total gross domestic debt stock increased by 10.6 percent from Kshs. 1,284.3 billion as at end-June 2014 to KShs. 1,420.4 billion by end-June 2015. The total external debt stock, including the International Sovereign Bond, stood at Kshs. 1,423.3 billion at the period ending June 2015.

The debt stock comprised of multilateral debt (48.1 percent), bilateral debt (31.3 percent), Export Credit debt (1.2 percent) and 19.5 percent for Commercial banks' debt - including International Sovereign Bond. Cumulative interest and other charges on domestic debt for the FY 2014/15 amounted to Kshs. 139.8 billion (or 2.6 percent GDP) compared with Kshs. 108.8 billion (or 2 percent GDP) during a similar period of the FY 2013/14. Total external debt service for the FY 2014/15 amounted to Ksh 104.5 billion (or 1.95 percent GDP), comprising Kshs. 81.9 billion in principal repayments and Kshs. 22.5 billion in interest payments (Quarterly Economic and Budgetary Review, 4th Quarter, 2015).

The successful issuance of the international sovereign bond largely contributed to the increase in total external debt. The issue comprised of US\$ 500 million at an interest rate of 5.875 percent with a five year maturity and US\$1.5 billion at an interest of 6.875 percent with a

maturity of 10 years. Most of Kenya’s external debt remains on concessional terms, although its commercial component has increased exponentially over the past three years. The increase in bilateral debt stock is because of the disbursements from China and France meant for financing infrastructural projects. Other changes were attributed to debt service and exchange rate revaluations. Figure 2 provides a trend in Kenya’s public debt.

Figure 2: Kenya’s Stock of Public Debt in Ksh. Billions



Source: Quarterly Economic and Budgetary Reviews

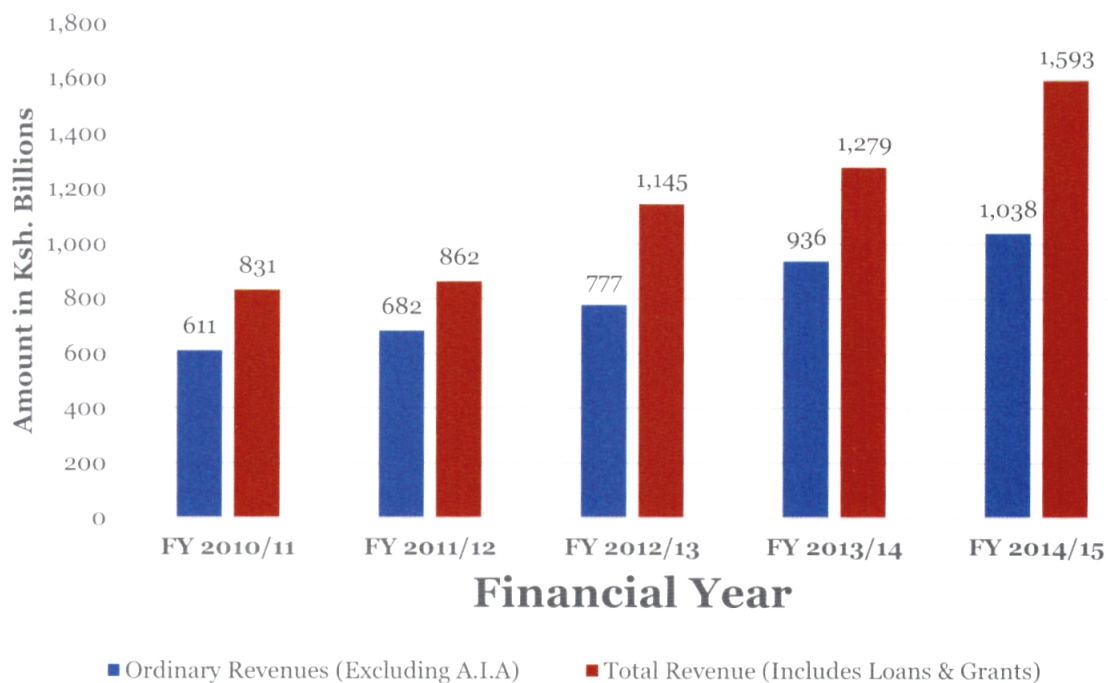
Public debt as a percent of GDP is a measure of a country’s ability to make future payments on its debt, and therefore affects the country borrowing costs and government bond yields. Kenya’s public debt portfolio at 51.7 percent of the GDP in 2014 is growing fast and poses substantial risk to the government’s balance sheet and the country’s financial stability. The national government needs to undertake deliberate measures to ensure debt sustainability. For example, the governments should embark on implementation of major recurrent expenditure reduction measures aimed at drastically reducing recurrent costs to free resources for development.

2.0 FISCAL PERFORMANCE OF GOVERNMENTS

2.1 Ordinary Revenue Analysis

As shown in Figure 3, ordinary revenues performance has been on an increasing trend over the years attributed to various tax reforms. The total revenue collected in 2014/15 including loans and grants amounted to Ksh. 1.6 trillion which is an increase of about 24.6 percent over the previous year. This rapid growth can be attributed to proceeds from the commercial loan for the standard gauge railway and domestic borrowing. The total ordinary revenue collected in 2014/15 amounted to Ksh 1 trillion up from 936 billion collected in 2013/14 which represents a 10.9 percent growth.

Figure 3: National Revenue Growth in Ksh. Billions

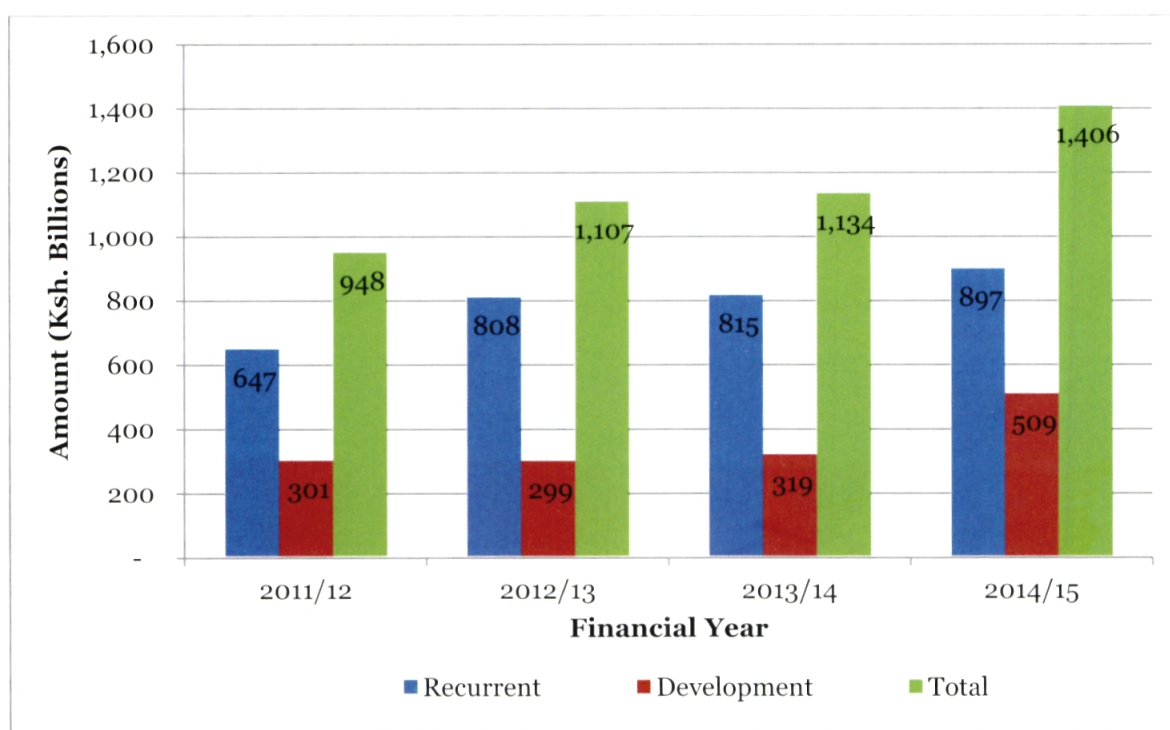


Source: BPS & Exchequer Statements, various Issues

2.2 Expenditure Analysis for National Government

National government Ministries, Departments and Agencies (MDAs), Judiciary and Parliament spent a total of Ksh. 1,406 billion for recurrent and development in 2014/15 against a target of Ksh. 1,625 billion. This is an underperformance of 13 per cent. The recurrent expenditure for 2014/15 totalled Ksh. 897 billion against a target of Ksh. 941 billion. This represented an overall expenditure growth of 24 per cent. The proportion of the funds spent on development by the national government also increased from 28 per cent in 2013/14 to 36% in the 2014/15. Figure 4 presents trends in national government expenditures.

Figure 4: National Government Expenditures, Ksh. Billion



Source: Budget Review and Outlook Papers, Various Issues

The expenditures for national government entities have been on the rise especially recurrent expenditures despite the fact that most of the functions are devolved. In 2012/13 the recurrent expenditure was Ksh. 808.3 billion which increased marginally in 2013/14 to Ksh. 815 billion but rose sharply to Ksh. 897 billion in 2014/15. This expenditure is

projected to continue to increase given that in 2015/16, the national government estimates on recurrent is Ksh. 1,017.5 billion and this will increase further to Ksh. 1,112 billion in 2016/17. Development expenditure is projected at Ksh. 705.6 billion in 2016/17. For the country to realize high and sustainable growth rates needed to achieve Vision 2030, then the national government needs to implement deliberate measures to curb recurrent costs.

2.3 County Revenue Analysis

The total revenue for county governments for the 2014/15 was Ksh. 304.87 billion. This comprised of Ksh. 226.7 billion from equitable share, Ksh. 1.87 billion conditional transfer for level five hospitals, Ksh. 733.65 million grants from DANIDA, Ksh. 41.67 billion from cash balances from 2013/14 and Ksh. 33.9 billion from counties own source revenues.

2.3.1 Analysis of Own Revenue Sources

County governments' effort to raise own revenue to support the budget is very crucial in provision of county services. The county governments in the financial year 2014/15 raised Ksh. 33.9 billion against a target of Ksh. 50.4 billion which is a performance rate of 64 percent. However, this was an improvement of 28 percent from 2013/14 when counties managed to raise Ksh. 26 billion. The improvement in revenue collections in some counties can be attributed to automation of revenue. Continued improvement in collection of own source revenues will enable counties to have sufficient resources to perform optimally the functions assigned to them. Table 2 indicates that Nairobi, Mombasa, Kiambu, Narok, Kiambu, Nakuru and Machakos counties collected the highest own source revenue as a proportion of their total budgets. Most of the marginalized counties collected less than four percent of their total budgets.

Table 2: Analysis of County Government Revenues (Ksh. Millions)

No.	County	Equitable share	Own Source Revenue	Total	% of Own Source Revenue to Total Revenue
1	Nairobi City	11,337	11,500	22,837	50
2	Mombasa	4,534	2,493	7,027	35
3	Narok	4,613	1,639	6,252	26
4	Kiambu	6,510	2,111	8,621	24
5	Nakuru	7,080	2,200	9,280	24
6	Machakos	5,904	1,357	7,261	19
7	Kajiado	3,849	786	4,635	17
8	Kisumu	4,956	971	5,927	16
9	Uasin Gishu	4,528	801	5,329	15
10	Nyeri	3,881	681	4,562	15
11	Laikipia	3,009	400	3,410	12
12	Murang'a	4,672	562	5,234	11
13	Embu	3,348	401	3,749	11
14	Kericho	3,930	414	4,343	10
15	Kirinyaga	3,086	312	3,398	9
16	Meru	5,664	539	6,204	9
17	Kilifi	6,491	545	7,036	8
18	Bungoma	6,695	505	7,200	7
19	Taita/Taveta	2,887	217	3,104	7
20	Migori	5,091	355	5,447	7
21	Trans Nzoia	4,448	301	4,750	6
22	Kakamega	7,771	517	8,287	6
23	Busia	4,746	315	5,061	6
24	Baringo	3,873	250	4,123	6
25	Nyandarua	3,757	241	3,998	6
26	Samburu	3,099	196	3,294	6
27	Kwale	4,471	254	4,725	5
28	Kitui	6,339	320	6,660	5
29	Bomet	4,106	206	4,312	5
30	Isiolo	2,666	134	2,800	5
31	Kisii	6,188	297	6,485	5

No.	County	Equitable share	Own Source Revenue	Total	% of Own Source Revenue to Total Revenue
32	Nandi	4,148	193	4,341	4
33	Elgeyo/Marakwet	2,853	129	2,981	4
34	Tharaka -Nithi	2,737	116	2,853	4
35	Makueni	5,207	215	5,423	4
36	Lamu	1,790	62	1,852	3
37	Vihiga	3,377	116	3,493	3
38	Siaya	4,357	143	4,501	3
39	Homa Bay	4,915	158	5,073	3
40	Nyamira	3,624	104	3,728	3
41	West Pokot	3,763	104	3,867	3
42	Garissa	5,035	131	5,165	3
43	Marsabit	4,527	99	4,626	2
44	Wajir	6,309	108	6,417	2
45	Turkana	9,141	127	9,267	1
46	Mandera	7,812	88	7,900	1
47	Tana River	3,476	33	3,509	1
	Total	226,600	33,743	260,343	13

Source: Budget Implementation review Report 2014/15

2.4 Expenditure Analysis for County Governments

County governments spent Ksh. 258 billion in 2014/15, of which Ksh. 167.56 billion was spent on recurrent and Ksh. 90.44 billion on development. Analysis from Table 3 indicates that county governments improved their overall utilization of funds on development from 17 percent in 2013/14 to 30 percent in 2014/15. The aggregate expenditure of all counties represented an absorption rate of 15 percent of the total revenues transferred to counties for 2014/15. Though expenditure on development has improved between 2013/14 and 2014/15, recurrent costs of counties estimated on aggregate at 55 percent need to be substantially reduced to free resources for development.

Table 3: Analysis of County Government Revenue and Expenditure, Ksh. millions

Year	Total County Revenue	Actual Expenditures		Total Expenditure	Absorption of Funds
		Recurrent	Development		
2012/13	22,976	14,531	1,695	16,226	71%
2013/14	216,300	132,800	36,600	169,400	78%
2014/15	304,780	167,560	90,441	258,001	85%

Source: County Budget Implementation Review Reports, Various issues

Absorption of funds by county governments has improved steadily over the last three years. Though on aggregate counties have a high absorption rate, a number of counties have low uptake of funds for both recurrent and development. This has been attributed to delayed transfers from the national governments, poor budgeting by counties and low capacities of some counties to utilize development funds. With the support from the national government and development partners, counties have been assisted to develop capacities to effectively undertake functions assigned to them.

3.0 FUNCTIONAL ASSIGNMENT

3.1 Functional Assignment to National and County Governments

The Constitution establishes two levels of government that are distinct and interdependent. The functions of national and county governments are listed under the Fourth Schedule of the Constitution. Transition Authority transferred the first batch of functions from the national government to county governments through Legal Notice no. 16 of February 2013. Additional functions were transferred in August 2013 to county governments under Special Gazette Supplement No. 116. The other remaining county functions are to be transferred to county governments within the transition period in line with Article 262 (15) of the Constitution.

Concurrent functions that are performed by more than one level of government and residual functions will remain a responsibility of the national government. The functions as articulated in the Fourth Schedule points out that the national government is largely assigned policy, regulatory, technical assistance and capacity building functions while county governments are mainly responsible for service delivery. Where a function cannot be explicitly distinguished as exclusive or concurrent, it is classified as residual and therefore a national government function.

Implementation of the devolved government system has practical and inherent risks and challenges in performing the functions assigned to either level of government. The key challenges include: conflicts between the national and county governments; structural overlaps between national and county governments; management of cross county planning and service delivery as a result of spillover effects; inadequate human resource and institutional capacity in counties to execute their mandates; and political resistance to devolution commonly exhibited in delays in

transfer of funds by the national government to the counties, among others.

Article 187 (2) of the Constitution also 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 in line with the principle of '*funds follow functions*.' This invariably requires clear linkages between assigned functions, planning, budgeting, and resource allocation at either level of government.

In the last three financial years there has been a debate regarding whether the resources allocated for either level of government is sufficient to perform the assigned functions. The national government has not fully devolved some of the functions assigned to counties in the Fourth Schedule and attendant resources. Some of the devolved functions are either being performed by line ministries or various corporations that existed before devolution. In making this recommendation the Commission has taken note of devolved functions that need to be unbundled and transferred to counties with attendant resources.

3.2 Funding of National Government Functions

In line with the objects of devolution, the Fourth Schedule assigns policy-related functions to the national government. The national government in performing its functions' provided to spend a total of Ksh. 1,505,492 million for FY2015/16. It is estimated that the national government expenditure for financial year 2016/17 will increase slightly by 1.4 percent to Ksh. 1,526,067. This is summarized in Table 4.

Table 4: Financing of National Government Functions in Ksh. millions

	Sector/State Department	Printed Estimates 2015/16	BROP Projection 2016/17
1	Agriculture, Rural & Urban Development Land, Housing and Urban Development, Agriculture, Livestock, Fisheries, NLC	79,692	69,347
2	Education: Education; Science and Technology; TSC	336,252	359,365
3	Energy, Infrastructure and ICT: Infrastructure; Transport, ICT; Energy and Petroleum)	404,670	358,276
4	Environmental Protection, Water and Natural Resources: Environment & Natural Resources; Water & Regional Authorities; Mining	63,001	77,011
5	General Economic and Commercial Affairs (GECA): Industrialization & Enterprise, East African Affairs; Commerce & Tourism)	21,296	19,359
6	Governance, Justice, Law and Order (GJLOS): Interior; Coordination of National Government; Attorney General & Justice; The Judiciary; EACC; DPP; CIC; Registrar of Political Parties, KNCHR, IEBC, JSC, NPSC; NGEC; IPOA	154,047	175,766
7	Health	59,184	61,492
8	Public Administration and International Relations: Presidency; Planning; Devolution; Foreign Affairs & International Trade; National Treasury, Parliamentary Service Commission, CRA, PSC, SRC, AG, CoB & CAJ)	243,354	256,191
9	The Social Protection, Culture and Recreation: Sports, Culture and Arts; Labour Social Security and Services	31,483	31,998
10	National Security: Defence, National Intelligence Services)	112,513	117,262
11	Sub Total	1,505,492	1,526,067
12	Other Government obligations Loan repayments, pension and other expenses	509,308	576,333
13	Total	2,014,800	2,102,400

Budget Review Outlook Paper (BROP) 2015

3.3 Financing of County Governments Functions

The Fourth Schedule stipulates the functions and powers of county governments. In February 2013, the Transition Authority transferred the first batch of functions from the national government to county governments through Legal Notice No.16. The Transition Authority in August 2013 transferred additional functions to county governments under Special Gazette Supplement No. 116. The outstanding functions will be transferred to county governments in line with Article 262 (15) of the Constitution. Some of the functions being performed by Water Services Boards and Regional Development Authorities are earmarked to be transferred by the Transition Authority early 2016. Once this is actualized, more resources will be transferred to county governments.

Table 5: Financing of County Functions in Ksh. Millions

No.		Allocation to Counties		
		2014/15 Actual	2015/16 Actual	2016/17 Recommendation
A. Devolved Functions				
1	Health Services	62,780	69,706	85,132
2	Planning & Development	54,091	56,255	64,693
3	Agriculture, Livestock and Fisheries	16,103	19,020	25,579
4	Culture, Public Entertainment & Public Amenities	2,849	2,992	4,039
5	Youth Affairs and Sports	3,380	4,531	6,570
6	Trade, Cooperative Development & Regulation	4,404	4,624	6,757
7	Roads & Transport	38,164	39,339	65,698
8	Lands, Housing and Public Works	5,868	6,015	8,722
9	Water, Natural Resources & Environmental Conservation	6,734	6,902	8,353
10	Pre-Primary Education	2,059	2,265	3,398
B. Sub Total Devolved Functions		196,433	211,649	278,941
11	New County Structures	30,233	48,127	52,824
C. Total Devolved Functions⁴		226,666	259,776	331,765
D. Conditional Allocations				
12	Level 5 Hospitals	1,800	3,600	4,143
13	Free maternal Health Care	-	4,298	4,947
14	Compensation for user fees	-	900	1,036
15	Leasing of medical Equipment	-	4,500	5,179
16	Road Fuel Levy Fund	-	3,300	4,756
17	Personnel Emoluments for Devolved staff	-	-	5,196
18	Construction of Headquarters in five Counties	-	-	4,000
19	Rehabilitation of Primary and Secondary Schools	-	-	5,000
20	County Emergency Fund	-	-	5,196
21	Rehabilitation of Village Polytechnics	-	-	6,300
E.	Total Conditional Allocations	1,800	16,598	45,752
TOTAL		228,466	276,373	377,517

Source, CRA 2015

⁴ The equitable share to counties may increase by Ksh. 4,502 million if devolved functions being performed by the WSBs and RDAs are unbundled and transferred by the Transition Authority before the CARB 2016 is enacted

4.0. APPROACH FOR REVENUE SHARING

In making the recommendations for sharing of revenue between the national and county governments, the Commission has taken into account the functions assigned to each level of government and the growth in nationally raised revenue. Further, the Commission considered the cost of new structures and conditional grants to address specific objectives. This will ensure that there is no mismatch between the resources and service delivery on responsibilities assigned to the national and county governments.

4.1 Criteria for Revenue Sharing

Article 203 stipulates criteria to be taken into account in determining the equitable shares among the national and county governments. These are:

- (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 county governments are able to perform the functions allocated to them;
- (e) the fiscal capacity and efficiency of county 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 optimization of each county and to provide incentives for each county to optimize 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.

The criteria in article 203 (1) applies partly to the basis for determining the equitable sharing of revenue raised by the national government between the national and county governments and partly to the basis for determining the equitable sharing of revenues among the county governments.

The Commission submits that the following six of the eleven criteria of Article 203 (1) (a)(b)(c)(d)(f)(k) are pertinent in determining the vertical sharing of revenue. The remaining five, Article 203 (1)(e)(g)(h)(i)(j) are relevant to the sharing of revenues among the county governments. The section below discusses the Commission's interpretation of Article 203(1) that is relevant to the equitable sharing of revenue between the national and county governments.

4.2. The National Interest

The term national interest refers to agreed policies, goals, priorities, and resultant programs which have fiscal implications and benefit the whole country. Decisions on national interest priorities do have financial implications on the functions of either level of government. National interest is not synonymous with National government functions. Programmes and projects necessitated by national interest considerations can be implemented by either the national or the county governments.

The list of the national interest policies and priorities that the country will undertake over a period of time should be agreed through a consultative process. Consultations on these national interest priorities should ideally be at the Summit. The national interest policies and priorities once agreed by both levels of government should be clearly set out in the Medium Term Expenditure framework, clearly outlining the policy priorities and the timelines for their implementation. They should inform the Budget

Review Outlook Paper, the Budget Policy Statement and the County Fiscal Strategy Papers. The consultative discussions should include an agreement on the mode in which the functions will be performed and therefore funded. In an ideal set up, the implementation shall be through inter-governmental frameworks/agreements that will provide the manner in which implementation will be effected. The options for implementation of national interest policies and priorities are:-

- (a) By either levels of government which will perform them as part of their constitutional mandate
- (b) By County governments but through conditional grants by the national government from its allocated share of revenue as part of their obligation to implement national policy.
- (c) By either levels of government where it is deemed the policy will be more effectively performed. The implementation should be through inter-governmental agreements that will provide the manner in which the implementation will be undertaken.

The budgetary provision necessary to accomplish national interest should be determined through the process outlined in the Public Finance Management Act which provides for involvement of the Intergovernmental Budget and Economic Council.

In the absence of agreed policies, goals, priorities by the Summit, the Commission submits the following as comprising the national interest. These priorities have been defined in the second Medium Term Expenditure Framework (2013-2017), and the Budget Review Outlook Paper 2015. The two policy documents are prepared by the national government through a participatory process which involves the county governments. National government priorities include:-

- (a) Quality and accessible Education and Healthcare services
- (b) Infrastructure Development, especially energy, roads and ICT

- (c) Security
- (d) Food Security
- (e) Youth and Women Empowerment

The revenue allocation to both levels of government, and indeed the budgets of both levels of government should be aligned with the above priorities to spur overall development in the country.

4.3. The Public Debt and Other National Obligations

4.3.1. Public Debt

The term public debt is defined in Article 214 as all financial obligations attendant to loans raised or guaranteed and securities issued or guaranteed by the national government. Article 203(1) provides for consideration of public debt during revenue sharing.

The level of indebtedness that the Country will go into and the application of the funds borrowed is an issue that must be discussed through a consultative and cooperative process that involves both levels of government. This is critical because the level of debt incurred by the National Government has direct implications:

- (a) On equitable share,
- (b) On the borrowing component, out of the total debt ceiling, available to the national governments, and
- (c) On the borrowing component, out of the total debt ceiling, available to the County governments.

On the basis of Article 214, the Commission considers public debt repayment by the national government as expenditure to be taken into account when the respective needs of the two levels of government are considered in subsequent sections.

4.3.2. Other National Obligations

National obligations refer to those obligations that the National government may have and which affect the entire country. Excluded from these criteria are those obligations that arise as part of the National government's functions. The obligations that are outside the National government functions include the funding of

- (a) The cost of shared institutions including the Judiciary, Parliament, and constitutional commissions; and
- (b) The cost of other national obligations which do not directly relate to the functions under the Fourth Schedule. These other national interests needs full disclosure by the national government and should be discussed at the Summit.

5.0. SHAREABLE REVENUE

The shareable revenue as stipulated under Article 202(1) of the Constitution requires that the revenues raised nationally shall be shared equitably among the national and county governments. The shareable revenue excludes internal and external loans borrowed by the national government. The allocation to counties is based on shareable revenues defined in the Constitution and Section 2 of the Commission on Revenue Allocation Act, 2011 as follows:

“all taxes imposed by the national government under Article 209 of the constitution and any other revenue (including investment income) that may be authorized by an Act of Parliament, but excludes revenues referred to under Articles 209 (4) and 206(1)(a)(b) of the Constitution”.

Table 6 below presents a summary of the revenues raised nationally, the shareable revenue and the non-shareable revenues for financial years 20012/13 to 2014/15.

Table 6: Shareable and Non-Shareable Revenues

No.	PARTICULARS	2012/13	2013/14	2014/15
		Ksh. Millions		
1.	Opening Balance	1,159	496	162
2.	Income Tax from Individuals (P.A.Y.E)	199,790	249,873	279,796
3.	Income Tax from Corporations	173,296	199,717	228,785
4.	V.A.T. on Domestic Goods & Services	92,772	105,888	127,905
5.	V.A.T. on Imported Goods & Services	92,144	126,911	131,781
6.	Excise Taxes	85,660	102,029	115,872
7.	Licenses under Traffic Act	2,431	3,323	2,825
8.	Customs Duties	57,650	67,555	74,048

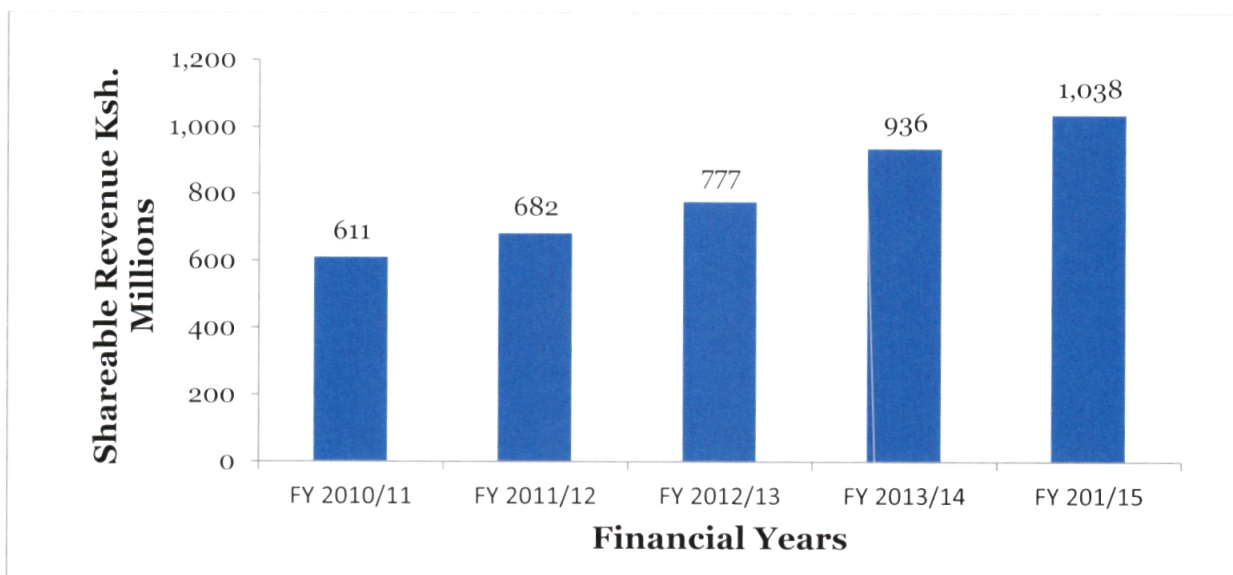
No.	PARTICULARS	2012/13	2013/14	2014/15
		Ksh. Millions		
9.	Other Taxes from International Trade & Transactions	24,163	26,678	26,993
10.	Stamp Duty	8,538	9,987	11,468
11.	Interest Received	1,356	586	1,609
12.	Profit & Dividends from CBK	1,500		
13.	Other Profits and Dividends	13,764	10,181	12,873
14.	Rent of Land	1,789	1,588	1,774
15.	Immigration Visas and Other Consular Fees	2,688	775	2,509
16.	Work Permit Fees	4,277	1,121	1,489
17.	Passport Fees	502	170	11
18.	Fishing Rights	171		211
19.	Betting Control	112		3
20.	Registration Services	247	129	505
21.	Fines, Penalties & Other Charges	1,465	1,443	2,491
22.	Others	2,136	1,023	678
23.	Miscellaneous Revenue	9,245	26,180	14,249
SUB TOTAL-SHAREABLE REVENUE		776,858	935,653	1,038,035
24.	Recurrent Recovery Over Issues 2008/09 & 09/10		66	
25.	Development Recovery Over Issues 2008/09 & 2009/10		17	
26.	Grants from Foreign Govt. through Exchequer	5,188	6,431	6,631
27.	Contribution from Govt. Emp. To S.&W.S within Govt.			120
28.	Loans from Foreign Govt. through Exchequer	23,569	28,432	30,310
29.	Loans to Non-financial Public Enterprises	2,035	1,148	2,695
30.	Loans to Financial Institutions	66	119	203
31.	Domestic lending-T/Bills	99,400		37,000
32.	Domestic lending-T/Bonds	232,430	160,660	255,680

No.	PARTICULARS	2012/13	2013/14	2014/15
		Ksh. Millions		
33.	Grants from International Organizations	5,826		3,843
34.	Borrowing from International Organizations			3,454
35.	Commercial loan		34,648	215,470
36.	AMISON Grants		4,695	
37.	Net Domestic Borrowing (CBK)		106,700	-
SUB TOTAL -NON SHAREABLE		368,515	342,917	555,405
GRAND TOTAL		1,145,373	1,278,570	1,593,440

Source: Audited Exchequer Accounts, Various Issues

The ordinary revenues raised nationally has increased overtime from Ksh. 611 billion in 2010/11 to Ksh. 1,038 billion in 2014/15. This is shown in Figure 5.

Figure 5: Trend of Shareable Revenue, Ksh. Millions



Source: Audited Exchequer Accounts, Auditor General's Reports

The growth of various revenues is presented in Table 7 below. Though the shareable revenues has exhibited a stable growth, increasing overtime,

the growth in total revenues and indeed, non-sharable revenues has fluctuated widely during the last three financial years, revealing shifts in overall financing policy of public expenditures by the national government.

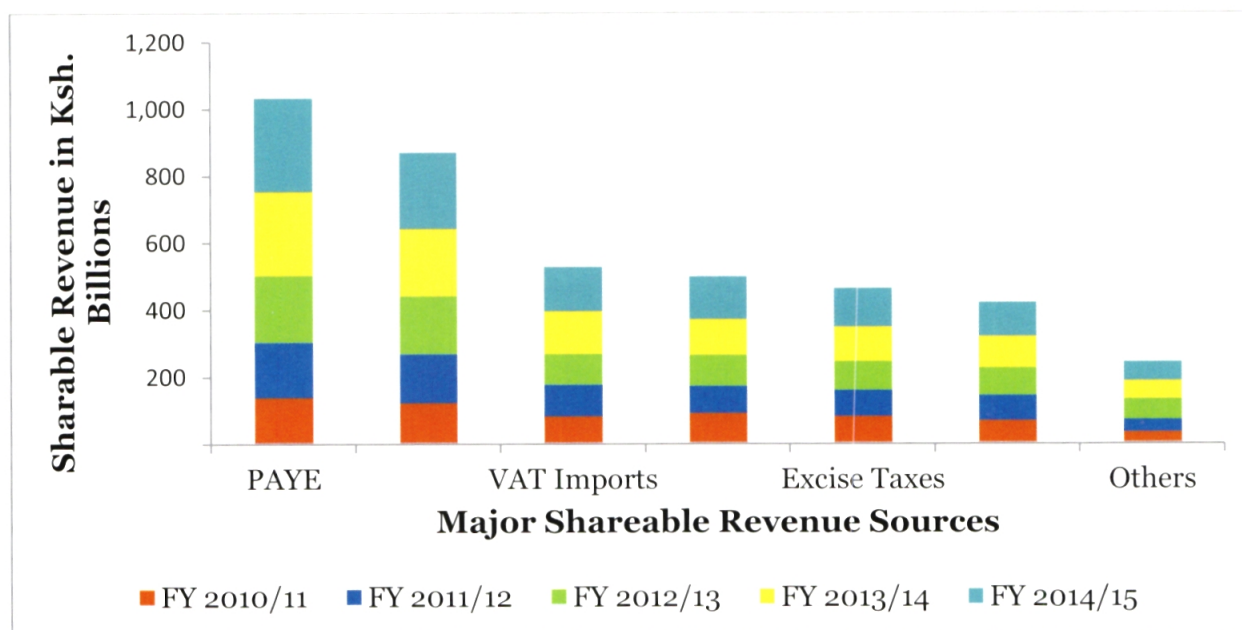
Table 7: Growth in Revenues for FY 2011/12 - 2014/15 (%)

Item	2011/12	2012/13	2013/14	2014/15	Average
Total Revenues	3.7	32.9	11.6	24.6	18.2
Of Which					
1. Sharable Revenue	11.7	13.9	20.4	10.9	14.2
2. Non Shareable Revenue	-18.3	104.8	-6.9	62.0	35.4

Source: Audited Exchequer Accounts, Auditor General's Reports

The stable growth in sharable revenue is as a result of stability of the growth of various revenue streams as revealed in Figure 6 below.

Figure 6: Major Sources of Shareable Revenues for 2010/11 - 2014/15



Source: Audited Exchequer Accounts, Auditor General Reports

6.0 RECOMMENDATION ON SHARING OF REVENUE

6.1 Determination of Equitable Share of Revenue 2016/17

In accordance with the provisions of Article 216(1)(a) and Article 203(1), the Commission recommends that out of the shareable revenue of Ksh. 935,653 million for the financial year 2013/2014, Ksh. 331,765 million be allocated to county governments as equitable share and Ksh. 45,752 million as conditional transfers for financial year 2016/17. The recommended equitable share allocation to county governments is equivalent to 35.5 percent of the shareable revenue for 2013/14 amounting to Ksh. 935,653 million.

In making this recommendation, the Commission uses the allocation to county governments for financial year 2015/16 of Ksh. 259,775 million as the base. This base has been increased by Ksh. 39,200 million using a three year revenue growth rate of 15.09 percent. The years considered are 2012/13; 2013/14 and 2014/15.

The Commission further recommends that Ksh 27,790 million be allocated to counties for construction and rehabilitation of county roads, and Ksh. 5,000 million for public participation. The equitable share allocation may increase by Ksh. 4,732 million if devolved functions currently being performed by the Waters Services Board and the Regional Development Authorities are unbundled and transferred by the Transition Authority before the County Allocation of Revenue Bill 2016 is enacted.

The recommendation on conditional allocation has two components:

1. An adjustment to the current conditional allocation on Level 5 Hospitals, Maternal Health Care, Compensation for User Fees Forgone and Leasing of Medical Equipment by the three year average revenue growth of 15.09 percent. The Allocation on Road

Fuel Levy Fund is based on 15 percent of the actual realized for the Fund for 2014/15 amounting to Ksh.31,707 million.

2. Provision for new conditional grants from the national government equitable share amounting to Ksh. 25,691 million to:
 - a. Cushion County governments on the huge wage bill,
 - b. Construction of headquarters for five counties, namely: Lamu, Tharaka Nithi, Nyandarua, Tana River and Isiolo.
 - c. Rehabilitation of primary and secondary schools,
 - d. Rehabilitation of village polytechnics, and
 - e. Establishment of Emergency Funds in 47 counties.

Table 8 provides a summary of the Commission recommendation on the equitable share to counties for financial year 2016/17. The equitable share due to national government is presented in Table 4.

Table 8: Recommendation on Shareable Revenue to Counties, Ksh. Millions

	ITEM	2015/16 Ksh. Million	2016/17 Ksh. Million
A	EQUITABLE SHARE TO COUNTIES		
1	Latest Audited Accounts	2012/13	2013/14
2	Shareable Revenue based on Audited Accounts	776,858	935,653
3	Equitable Share (Baseline)	259,775	259,775
4	Adjust by the three year average revenue growth of 15.09 percent		39,200
5	Add Allocation for County Roads		27,790
6	Add Allocation for Public Participation	-	5,000
7	Total Equitable Share to Counties⁵	259,775	331,765
8	Percentage Share to Counties	33.44%	34.53%

⁵ The Equitable Share to County Governments may increase by Ksh. 4,732 million if devolved functions currently performed by the Waters Services Boards; and those performed by the Regional Development Authorities

	ITEM	2015/16 Ksh. Million	2016/17 Ksh. Million
B	CURRENT ALLOCATIONS	2015/16	2016/17⁶
9	Level 5 Hospitals	3,600	4,143
10	Free Maternal Health Care	4,298	4,947
11	Compensation for user fees forgone	900	1,036
12	Leasing of medical equipment	4,500	5,179
13	Road Fuel Levy Fund (15% of Actual 2014/15)	3,300	4,756
14	Sub Total	16,598	20,061
C	NEW CONDITIONAL GRANTS		
15	Personnel emoluments for devolved staff	-	5,196
16	Construction of headquarters in five Counties ⁷	-	4,000
17	Rehabilitation of primary and secondary schools	-	5,000
18	Establishment of County Emergency Funds (2% of Equitable Share: Ksh. 259,775 Million)	-	5,196
19	Rehabilitation of village polytechnics		6,300
20	Sub Total New Conditional Grants		25,691
21	Total Conditional Grants	16,598	45,752
D	Total Transfer to Counties for 2016/17	276,373	377,517

Source: CRA

⁶ Allocation of conditional grants to County Governments for financial year 2015/16 have been adjusted by the three year revenue growth rate of 15.09 percent

⁷ This conditional allocation will be used to build headquarters for the following five counties: Lamu, Tharaka Nithi, Nyandarua, Tana River and Isiolo

6.2. Additional Transfers to County Governments

The Constitution in Article 202(2) provides that county governments may be given additional allocations from the national governments share of the revenue, either conditionally or unconditionally. The Commission recommends for the following additional allocations to county governments:

6.2.1 Public Participation

The Constitution under Articles 118(1)(b) and 196(1)(b) provides citizens the right to participate in the decision-making process and other duties of the national and county legislative bodies. Article 174(c) also give powers of self-governance to the people and enhances the participation of the people in the exercise of the powers of the State. Further, The County Government Act section 91 allows the county government to set up modalities and platforms for citizen's participation in the county affairs. To achieve this, the county governments are required to set up necessary structures to enable the public participate effectively in planning, legislation, budgeting and implementation of county affairs. The structures required include but not limited to: setting up of information communication platforms, town halls, establishment of citizen fora among others.

The county governments need to be funded adequately in order to set up the required structures to ensure effective citizen participation. All counties have grossly underfunded public participation resulting in unnecessary litigations. **To streamline public participation in counties, the commission recommends that Ksh. 5 billion be included as part of the equitable share of counties for 2016/17.**

6.2.2 Water Services Boards

The Water Service Boards (WSBs) as currently constituted are agencies of the National Government. The main roles of the WSBs are to: implement government policies related to water services on behalf of the national government; undertake planning and development of national water infrastructure and undertake investment planning and implementation of special projects.

Transition Authority, in its review of the institutions and unbundling of functions in the water sector has recommended that the function of water and sewerage services provision should be transferred to the County Governments (vide TA Gazette Supplement No. 116). Currently the Water, Bill 2014 proposes that the WSBs be restructured to Water Works Development Agencies to handle national water infrastructure development and the counties handle county works and provision of water services.

The inter-agency task force on determination of the extent to which National Government performs County Governments' functions recommended for formal intergovernmental agreements for managing functions performed by the WSBs in the short term. In the medium term, the boards should be restructured to align them to the devolved system of government and in the long term the task force recommended that relevant legislation should be amended to include county governments in the management structures of the WSBs to align them to the devolved system.

All the Water Service Boards (WSBs) receive both recurrent and development budget from the ministry of Water and Irrigation apart from Athi Water Service Board and Rift Valley Water Service Board who fund their budget using the Appropriations in Aid. Further, a number of Water

Service Providers receive transfers either from the Ministry or from County Governments. Table 9 shows the budget for the WSB for FY2015/16.

Table 9: Budget of Water Services Boards for 2015/16 (Ksh. Millions)

No	Water Service Board	Recurrent Ksh Million	Development Ksh. Million
1.	Athi Water Service Board	-	-
2.	Lake Victoria North WSB	23	179
3.	Lake Victoria South WSB	36	539
4.	Rift Valley WSB ⁸	-	260
5.	Northern WSB	63	510
6.	Coastal WSB	-	180
7.	Tana WSB	13	1,075
8.	TANATHI WSB	19	270
	Total	152	3,013

Source: Budget Estimates 2015/16

Owing to the fact that the Water Bill 2014 is under consideration and that the Transition Authority has recommended transferring the provision of water services to the counties, **the Commission recommends that the budget for the Water Service Boards be rationalized and Ksh. 3,013 million be transferred to county governments as part of the equitable share for 2016/17.**

⁸ The budget for Athi and Rift Valley WSB is funded through Appropriations in Aid

6.2.3 Regional Development Authorities

Regional development is a holistic approach where different regional actors participate in the definition, decision and implementation of the most appropriate development initiatives. In Kenya, there are six Regional Development Authorities (RDAs) charged with the mandate of spurring integrated regional development to address equitable and balanced socio-economic development in the country. Most of the functions that are performed by the RDAs regional are impact on the functions of several counties.

The Transition Authority carried out an analysis of the functions of the Regional Development Authorities (RDAs) and made the following recommendations:

- The RDAs to continue implementing their core mandates on integrated multipurpose development projects and programs that cut across counties. These projects were conceptualized by the Authorities and over the years, the Authorities have built the requisite capacity to effectively implement the projects. In addition, these projects are national flagship projects under Vision 2030. The Authorities have built Public Private Partnerships with support of National Government to deliver these cost intensive projects.
- It is necessary to review and align the RDAs policy, legal and regulatory framework in line with the Constitution. Most of their functions have certain components of devolved county functions including agriculture, fisheries, livestock, irrigation, conservation and forestry among others.
- There is need to establish a collaborative framework that will ensure the creation of synergy, curb wastage through duplication of efforts and ensure proper monitoring and evaluation of both the County and RDA project.

These recommendations are in tandem with those of the inter-agency task force on determination of the extent to which National Government performs County Governments' functions. For the FY 2015/16 the RDAs were allocated a total of Ksh.553 million for recurrent and Ksh. 1,489 million for development budget as shown in Table 10 below.

Table 10: Budget for Regional Development Authorities

No.	Name of RDA	Approved Budget FY2015-16	
		Recurrent Ksh. Million	Development Ksh. Million
1	Kerio Valley Development Authority (KVDA)	113	225
2	Tana and Athi Rivers Development Authority (TARDA)	137	226
3	Lake Basin Development Authority (LBDA)	131	246
4	Ewaso Nyiro South Development Authority (ENSADA)	56	319
5	Ewaso Nyiro North Development Authority (ENNDA)	59	373
6	Coast Development Authority (CDA)	58	100
	Total	553	1,489

Source: Budget Estimates 2015/16

In implementing the Transition Authority recommendations **the Commission recommends that Ksh. 1,489 million be transferred from RDAs to county governments in 2016/17 and be shared equitably among all counties using the revenue sharing formula.**

6.2.4 Allocation for County Roads

Allocation to county governments for construction and rehabilitation of county roads is grossly underfunded. This is because the national government has continued to allocate resources to Kenya Rural Roads Authority (KeRRA) to construct, maintain and manage rural road network in the country classified as D, E & Others and Kenya Urban Roads Authority (KURA) mandated to develop, manage, rehabilitate and maintain roads in all urban areas and cities in Kenya.

KeRRA and KURA are largely doing county functions. This need to be streamlined. **The Commission recommends that Ksh. 27,790 million currently allocated to other roads for 2015/16 budget be transferred to counties as equitable share for 2016/17.**

7.0. RECOMMENDATION ON CURRENT CONDITIONAL GRANTS

The Constitution in Article 202(2) provides that the county governments may be given additional allocations from the national government's share of the revenue, either conditionally or unconditionally. Over the last three financial years, county governments have received conditional allocations to address specific objectives in the health and road sectors.

Whilst conditional grants are important, the Commission urges that their allocation should be equitable and their distribution should not compromise the independence of the county governments as regards budgeting, planning and budget execution. Table 11 shows a summary of the recommendation on the current conditional grants to the county governments.

Table 11: Recommendation on Current Conditional Grants

NO.	ITEM	FY2015/16 Ksh. Million	FY2016/17 Ksh. Million
1.	Level 5 Hospitals	3,600	4,143
2.	Free maternal Health Care	4,298	4,947
3.	Compensation for user fees forgone	900	1,036
4.	Leasing of medical Equipment	4,500	5,179
5.	Road Fuel Levy Fund	3,300	4,756
	Total Conditional Grants	16,598	20,061

Source: CRA 2015

7.1 Level Five Hospitals

These grants are meant to benefit the health referral hospitals whose catchment areas go beyond the boundaries of a specific county. For this reason, a total of Ksh. 3,600 million was set aside in FY2015/16 to compensate the host counties and the funds were shared based on the

percentage bed occupancy per hospital in 2014. **The commission recommends that the grant is retained and be adjusted by the revenue growth rate of 15.09 percent to Ksh. 4,143 million.**

7.1. Free Maternal Health Care

Health care is largely a devolved function. As one of the strategic intervention under health care the counties had a total of Ksh. 4,298 million for the FY2015/16. The grant was shared using a direct reimbursement to health providers based on percentage to contribution to total number of maternity deliveries during the FY2013/14. **The Commission recommends that grant be retained and adjusted by the revenue growth rate of 15.09 percent to Ksh. 4,947 million. The money should be shared based on county's percentage contribution to total number of maternity deliveries during the FY2014/15.**

7.3. Leasing of Health Care Equipment.

The national government provided for a total budgetary allocation of Ksh. 4,500 million in 2015/16 to facilitate the purchase of modern specialised health care equipment in at least two health facilities in each county government. **The Commission recommends that the allocation be retained and revenue growth rate of 15.09 percent to Ksh. 5,179 million for FY2016/17.**

7.4. Compensation of user fees forgone

The national government introduced this conditional grant to compensate the counties for the revenue from the user fees charged by health centers and dispensaries. During the financial year 2015/16, the national government set aside Ksh. 900 million for this purpose. The National Treasury used the annual consolidated facility outpatient attendance workload to share the money to health centers and dispensaries within the county. **The Commission recommends that the conditional allocation be retained and adjusted by the revenue**

growth rate of 15.09 percent to Ksh. 1,036 million. The allocation will compensate counties for user fees forgone and will be share among the counties for the same purpose and shared using annual consolidated facility outpatient attendance workload.

7.5. Road Maintenance Fuel Levy Fund

This fund was established in 1993 through the Roads Maintenance Levy Fund Act to cater for the maintenance of public roads, including the former local authority unclassified roads. This fund a fuel levy on petroleum products and transit toll collections. It is administered by Kenya Roads Board (KRB) and targets maintenance of roads

The national government set aside Ksh. 3.3 billion in FY2015/16 for counties to use to maintain county roads. Sharing of money under this grant is based on the approved revenue sharing formula among county governments. During 2014/15, the Kenya Roads Board received Kshs. 31.7 billion as fuel levy. **The Commission recommends Ksh. 4,756 million, which is 15 percent of the amount collected in 2014/15 to be allocated to county governments based on the approved revenue sharing formula among county governments.**

8.0. PROPOSED ADDITIONAL CONDITIONAL GRANTS

8.1. Personnel Emoluments for county governments

County governments have raised concerns based on the amount of resources they have spent on personnel emoluments for staff for devolved functions and former Local Authorities. The Commission recommends as a short term stop gap measure, to cushion counties against high expenses on salaries as we await the results and implementation of the staff rationalization programme. **The Commission recommends Kshs. 5,196 million to be shared proportionately based on the payroll of the devolved staff as indicated in Table 12.**

Table 12: Sharing of the Conditional Grant on Personnel Emoluments in Ksh. Millions

No.	County	Total Personnel Devolved 2013/14	Allocation Factor based on 2013/14 Devolved Staff	Allocation to Counties 2016/17
1.	Baringo	1,070	0.0227	114
2.	Bomet	397	0.0084	42
3.	Bungoma	1,358	0.0289	144
4.	Busia	871	0.0185	92
5.	Elgeyo/Marakwet	789	0.0168	84
6.	Embu	1,328	0.0282	141
7.	Garissa	695	0.0148	74
8.	Homa Bay	964	0.0205	102
9.	Isiolo	482	0.0102	51
10.	Kajiado	728	0.0155	77
11.	Kakamega	1,744	0.0371	185
12.	Kericho	1,037	0.0220	110
13.	Kiambu	2,628	0.0558	279
14.	Kilifi	1,006	0.0214	107
15.	Kirinyanga	864	0.0183	92
16.	Kisii	1,382	0.0294	147
17.	Kisumu	1,677	0.0356	178
18.	Kitui	997	0.0212	106
19.	Kwale	579	0.0123	62

No.	County	Total Personnel Devolved 2013/14	Allocation Factor based on 2013/14 Devolved Staff	Allocation to Counties 2016/17
20.	Laikipia	687	0.0146	73
21.	Lamu	297	0.0063	32
22.	Machakos	1,442	0.0306	153
23.	Makueni	996	0.0211	106
24.	Mandera	239	0.0051	25
25.	Marsabit	447	0.0095	47
26.	Meru	1,445	0.0307	154
27.	Migori	700	0.0149	74
28.	Mombasa	1,533	0.0326	163
29.	Muranga	1,099	0.0234	117
30.	Nairobi	3,792	0.0806	403
31.	Nakuru	2,667	0.0567	283
32.	Nandi	796	0.0169	85
33.	Narok	661	0.0140	70
34.	Nyamira	544	0.0116	58
35.	Nyandarua	982	0.0209	104
36.	Nyeri	1,817	0.0386	193
37.	Samburu	326	0.0069	35
38.	Siaya	713	0.0152	76
39.	Taita Taveta	593	0.0126	63
40.	Tana River	324	0.0069	34
41.	Tharaka Nithi	672	0.0143	71
42.	Trans-Nzoia	916	0.0195	97
43.	Turkana	390	0.0083	41
44.	Uasin Gishu	1,036	0.0220	110
45.	Vihiga	527	0.0112	56
46.	Wajir	321	0.0068	34
47.	West Pokot	515	0.0109	55
Total		47,069	1	5,000

Source: CRA 2015

8.2. Construction of County Headquarters

The County Government's Act gave the Transition Authority powers to identify and gazette the headquarters of all counties and identify the offices for the county assembly and county executive. The Transition Authority carried out an audit for all counties and identified the headquarters and office space for each county. During the transition period, each county received a total of Ksh. 61.6 million to refurbish and buy furniture. However, five counties did not have headquarters. These are: Tharaka Nithi, Nyandarua, Isiolo, Lamu and Tana River. To enable these counties construct headquarters, **the Commission recommends a conditional grant of Ksh. 4 billion to be shared equally among the five counties as shown in Table 13.**

Table 13: Allocation to Counties without Headquarters

No.	County	Allocations Ksh. Millions
1.	Tharaka Nithi	800
2.	Lamu	800
3.	Nyandarua	800
4.	Tana River	800
5.	Isiolo	800
Total		4,000

Source: CRA 2015

8.3 Rehabilitation of Primary and Secondary Schools

Investment in social infrastructure such as basic education which covers primary and secondary education brings many benefits to the economy and contributes to economic growth. Increasing investment and improvement of productivity in the education sector is important for the long-term wellbeing of the economy. Education absorbs a large share of government's wage bill, and so increasing productivity by improving infrastructure is essential.

Despite the robust free primary and secondary school policy, which provides for funding for schools' recurrent expenses, the infrastructure of many primary and secondary schools remains in deplorable condition. This is because building of school infrastructure has been left to parents. Provision of basic education is the national government function. However, county governments are best suited to construct and rehabilitate schools. **The commission recommends that the national government allocates Ksh. 5,000 million as conditional allocation to county governments from its share of revenue for rehabilitation of primary and secondary schools in 2016/17. The grant will be shared among all the counties based on the proportion of a county's population under 18 years.**

8.4 Establishment of County Emergency Fund

It is important that each county government establishes an Emergency Fund. The PFM Act Section 110 (1) provides for the establishment of the County Emergency Fund to manage urgent and unforeseen expenditure needs at the county level. The County Emergency Fund consists of monies appropriated by the County Assembly. The PFM Act Section 113 limits the withdrawal from the County Emergency Fund to two percent of the total audited county government revenue for the previous financial year. Based on the equitable transfer to county governments for financial year 2015/16 amounting to Ksh. 259,775 million, two percent translates to an

Emergency Fund of Ksh. 5,196 million to be shared proportionately using the county total revenues for 2014/15.

8.5 Rehabilitation of Village Polytechnics

The Village polytechnics are devolved functions assigned to county governments under the Fourth Schedule. Although, the national government has historically spent more than 20 percent of its overall budget on education, little has been invested in financing of village polytechnics which are essential in developing skills of the youths who don't transit to higher institutions of learning. Village polytechnics if well-equipped, are good centres of excellence to empower the youth with skills to generate employment opportunities. **The Commission recommends that county governments be allocated a conditional grant of Ksh. 6,300 million from the national government share to build, equip and or renovate the village polytechnics. The grant will be shared among all the counties based on the approved revenue sharing formula.**

9.0. RECOMMENDATION ON EQUITABLE SHARES FOR 2016/17

Pursuant to Article 216 (5), the Commission hereby submits its recommendation to the Senate, the National Assembly, the National Executive, County Assemblies, and County Executives that county governments be allocated Ksh. 331,765 million as shareable revenue. This is equivalent to 23 percent of the projected shareable revenues for financial year 2016/17 amounting to Ksh. 1,444.9 billion as presented in Table 14.

In accordance with the provisions of Article 204(1), the government should also set aside one half percent of all the revenue collected by the national government each year calculated on the basis of the most recent audited accounts for revenue received, as approved by the National Assembly. This allocation to the Equalisation Fund is equivalent to Ksh. 4,236 million. This calculation is based on the revenue collected in 2012/13 amounting to Ksh. 847.2 billion.

Table 14: Shareable Revenue for Financial Year 2016/17

Budget Items		Ksh Billions	Percentage
Projected Ordinary Revenues for 2016/17		1,444.9	100%
<i>Of Which</i>			
1	Equalisation Fund	4,236	0.3%
2	National Government	1,108.9	76.7%
3	County Governments	331,765	23.0%

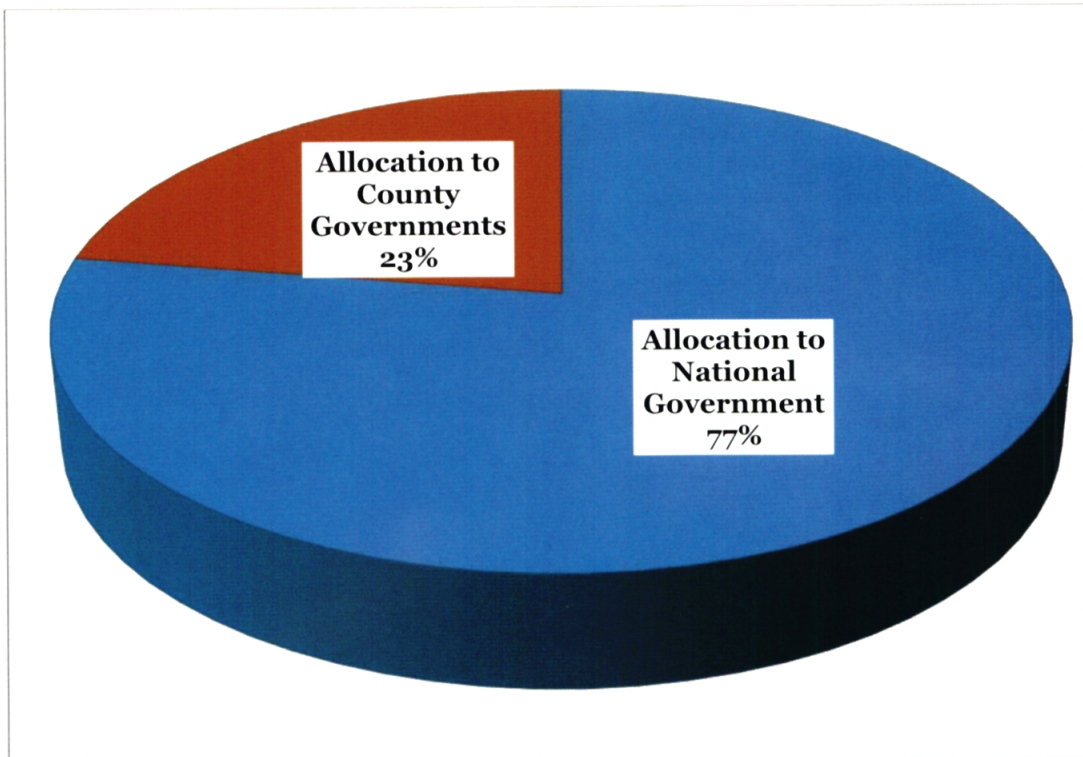
Budget Review Outlook Paper October 2015 & CRA 2015

The Commission, having taken into consideration the shareable revenue for 2013/14 and the level of revenue to be raised nationally for financial year 2016/17, hereby makes the following recommendations for consideration:-

1. That Ksh. 331,765 million be allocated to county governments as equitable share for 2016/17,
2. That Kshs. 1,108.9 billion be allocated to the national government, to meet its obligations and perform its functions,
3. That Ksh. 44.7 billion be transferred to county governments as conditional allocations from the national government share of revenue,
4. That Ksh. 4.2 billion be paid into the Equalisation Fund, being equivalent to one half percent of the revenues for 2012/13, and
5. That Ksh. 4.5 billion be transferred to counties from the national government share of revenue if the Transition Authority transfers functions performed by Water Services Boards and Regional Developed Authorities to the county governments before the County Allocation of Revenue Bill 2016 is enacted.

Figure 7 presents a summary of the aggregate shares to the national and county governments for financial year 2016/17.

Figure 7: Share of Total Revenue to National and County Governments for 2016/17



Source: CRA 2015

In conclusion, the Commission urges the national government to transfer all the devolved functions still being performed by ministries departments and agencies before March 2016 in accordance with the provisions of the Constitution. The national government entities should focus on the functions assigned by the Constitution under the Fourth Schedule, which is mainly regulation and policy formulation and cede implementation of devolved functions to county governments.



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