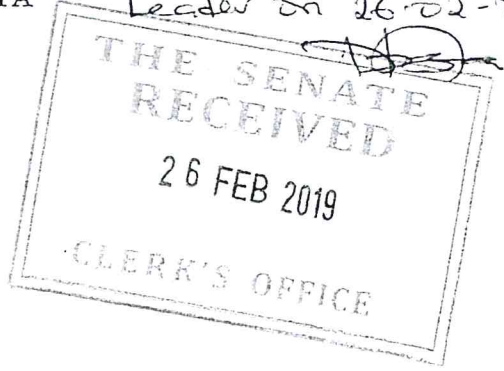


REPUBLIC OF KENYA

Paper laid on the Table
of the Senate by the
Senate Deputy Majority
Leader on 26-02-2019



COs

Recommended for approval
for tabling.

Eg 26/02/19

THE SENATE

Rt-Hon Speaker
You may approve
for tabling.
26/05/19

TWELFTH PARLIAMENT – THIRD SESSION

REPORT OF THE STANDING COMMITTEE ON FINANCE & BUDGET ON THE 2019
BUDGET POLICY STATEMENT AND MEDIUM TERM DEBT MANAGEMENT
STRATEGY

Approved
[Signature]
26/05/2019

PARLIAMENT BUILDINGS

NAIROBI

FEBRUARY 2019

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PREFACE

The Committee on Finance and Budget was constituted by the House on Thursday 14th December, 2017 during the First Session of the Twelfth (12th) Parliament. The Committee as currently constituted, comprises the following members:

- | | |
|--|--------------------|
| 1. Sen. (Eng) Mohamed M. Mahamud, CBS, MP | - Chairperson |
| 2. Sen. (Dr) Isaac Mwaura, CBS, MP | - Vice Chairperson |
| 3. Sen. Wetang'ula Moses Masika, EGH, MP | - Member |
| 4. Sen. Mutula Kilonzo Junior, MP | - Member |
| 5. Sen. Aaron Cheruiyot, MP | - Member |
| 6. Sen. (Dr.) Ali Abdullahi Ibrahim, CBS, MP | - Member |
| 7. Sen. (Dr) Rose Nyamunga, MP | - Member |
| 8. Sen. CPA Farhiya Haji, MP | - Member |
| 9. Sen. Boniface Mutinda Kabaka, MP | - Member |

The Standing Committee on Finance and Budget is established pursuant Section 8 of the Public Finance Management Act, 2012 and standing order 218(3) of the Senate Standing Orders and is mandated to -

- a) 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) *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.*
- b) *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*

The 2019 Budget Policy Statement and Medium term Debt Management Strategy was tabled in this House on 14th February, 2019. Pursuant to standing Order 180(4), of the Senate Standing Orders the Budget Policy Statement (BPS) was committed to Standing Committee on Finance and Budget to deliberate upon and make recommendations. The Finance and Budget Committee hereby tables the report containing its recommendations on the BPS to the House for consideration and approval.

Pursuant to standing order 180(5) of the Standing Orders, the Committee invited the Cabinet Secretary- the National Treasury, Commission for Revenue Allocation (CRA), the Council of Governors and County Assembly Forum (CAF). Further, the Committee invited Senate Standing Committee, which oversight different state departments, to consider respective sector provisions in the BPS and forward the observations and recommendations. Other interested parties like the Institute of Certified Public Accountants of Kenya (ICPAK) and IBP submitted their memorandum.

The Committee in making the recommendations, considered the views of all the stakeholders. The Committees made significant observations on the BPS policy proposals for the 2019/20 and the medium term debt strategy, identifying broad policy issues with great impact on counties and proposals on revenue allocation.

It is significant to mention that the purpose of the approval of this report on the PBS is to communicate the Senate's position on the preparation of all subsequent budget documents for next financial year. These documents include Division of Revenue Bill, 2019 and County Allocation of Revenue Bill, 2019. It is also important to note that Section 25 of the Public Finance Management Act, 2012, stipulates that the resolutions of Parliament, comprising both Houses, on the BPS must inform the preparation of the Annual Estimates. Thus, by extension, this House's resolutions on this report will form the basis of evaluating the 2019/20 estimates for the various spending agencies at both national and devolved level.

Examination of the Medium Term Budget Policy Statement and Debt Management Strategy

Pursuant to Public Finance Management (PFM) Act, 2012 Section 25 (2), the National Treasury submitted the 2019 BPS. Further, pursuant to PFM Act section 25 (7), and standing orders 180 of

the Senate Standing Orders, the BPS was committed to the Standing Committee on Finance and Budget for consideration and recommendation. In considering the 2019 BPS, the Committee held six sittings and a report writing retreat.

The perspective of the Senate Committees and the role of Senate in protecting the interest of counties, the broad issues in the 2019 BPS can be categorized as follows:

- (i) National policies and programmes that have a direct impact on economic performance of counties; and
- (ii) Proposals on division of revenue between the two levels of government and among counties for the 2019/20 financial year.

The 2019 BPS mainly focuses on the “Big Four” which is aimed at Creating Jobs and Transforming Lives. It is important to note that three out of “Big Four” are devolved functions. However, the policy is silent on the role of the counties in accomplishing the ‘Big Four’.

The government targets total revenue collection including appropriation-in-aid of **Ksh. 2,081 billion** for FY 2019/20 compared to **Ksh. 1,832 billion** for FY 2018/19. Ordinary revenue is projected at **Ksh.1,877.20 billion** for FY 2019/20 which is higher than **Ksh.1,652 billion** estimated for FY 2018/19.

According to the 2019 BPS, the projected revenue performance will be underpinned by ongoing reforms in tax policy and revenue administration which are similar to those identified in the 2018 BPS, that include- enhanced scanning to detect concealment and increase efficiency in cargo clearing through procurement of additional scanners and full integration of all scanners, use of Regional Electronic Cargo Tracking System (RECTS) to ensure all goods reach the desired destinations and avoid dumping; the use of third-party information to identify non-compliant property developers and ensure they are included in the tax base; and detection of non-compliance through i-Tax data matching. However, the BPS 2019 does not report on the progress of achievement and how much is expected to raise specifically through these reforms.

Given the sustained underperformance of revenue in the past years, it is very important to ensure that the revenues projected for 2019/20 are realistic. The National Treasury-in collaboration with KRA- should provide clear quantifiable and realistic tax administration measures towards boosting revenue collection.

Economic Growth- the Kenya's economic growth has remained stable in the period 2013 – 2017 at a remarkable at 5.6 percent compared to 4.7 percent (2008 – 2012) percent and 4.6 percent (2002-2007). The economic growth for 2018 is projected at 6.0 percent an increase from 4.9 percent in 2017, the growth was supported by improved weather conditions, improved business activities and easing of political uncertainty. Going forward, the growth projections are 6.2 percent in 2019 and 6.3 percent in 2020.

Indeed, while this is impressive growth, the emerging concern is that these key drivers of economic growth are not anchored on key policy changes but are based on factors beyond the control of policy makers such as favorable weather conditions, security and calm political environment.

Inflation - The overall monthly inflation remained relatively stable at an average of 4.7 percent in 2018 compared to 8.0 percent in 2017. This is attributable to increased food production leading to lower food prices as well as lower energy prices due to increased hydropower generation. Inflation has remained within the target range of 5 ± 2.5 percent. The BPS 2019 projects the inflation will remain within the target range in the medium term supported by lower food prices reflecting favorable weather conditions, reduced electricity tariffs and lower international oil prices. Though currently projected at low levels, fuel prices may go up if the USA imposes sanctions on Venezuela and Iran coupled with the decision by OPEC to cut supply of crude oil ends up limiting oil production. Higher fuel costs will invariably lead to higher transportation costs.

Interest Rates and Private Sector Credit - The Central Bank Rate (CBR) has been adjusted over the past five years to anchor inflation expectations with the most recent adjustment being in July 2018 – from 9.5 percent to 9.0 percent in March 2018 – to ease monetary policy stance in support of economic activity. The outlook in 2019 BPS is that interest rates will remain low and stable supported by improved liquidity conditions and ongoing fiscal consolidation

Exchange Rate & External Sector - The exchange rate was stable against major international currencies in 2018 and beginning of 2019 compared to previous years. The outlook in the 2019 BPS is that it will remain stable supported by improved performance of inflows from exports, continued increase in diaspora remittances and growth in tourism. The foreign exchange reserves remained an adequate buffer for short-term foreign exchange shocks at 5.5 months of import cover above the required threshold of at least 4 months. The risk to the exchange rate is the over-reliance on hot money flows as the main source for foreign reserve stocks. Though diaspora remittances have grown significantly in the past, they are not reliable as a source of foreign exchange. Focus should therefore be on attracting Foreign Direct Investment (FDI) as well as diversifying and growing the country's exports.

Fiscal Policy - Fiscal consolidation is one of the key objectives in the 2019 BPS. It entails the government tightening its belt through expenditure cuts since tax increments are currently not a favorable option for the economy. Analysis indicates that the current fiscal policy is edging towards a contractionary fiscal policy for FY 2019/20 and the medium term as indicated by a fiscal impulse that is slowly edging upwards. While this is commendable, the challenge will be in maintaining a contractionary fiscal path given the prevailing expenditure pressures that mostly increase recurrent expenditures and reduce development expenditures.

County Revenue – over the year counties have received equitable share of Kshs 1,572.80 billion and additional Kshs 194.50 billion in form of conditional grants from the national government share for specific programmes and policies. The annual growth rate of the equitable share allocated to the counties has been reducing from 19.32 percent in financial year 2014/15 to slightly below 4 per cent in FY 2018/19. The 2019 BPS proposes a reduction in county equitable share of Kshs. 310.00 billion from the Kshs. 314.00 billion provided for in the Division of Revenue Act, 2018. The 2019 BPS indicates that the National Policy on supporting enhancement of county government's Own Source Revenue (OSR) was approved by Cabinet in FY 2017/18 and its implementation will assist counties in determining their revenue potentials, revenue forecasting, assist counties in establishing appropriate institutional arrangement for collecting OSR.

Debt Management - Similar to the 2017, 2018 Medium Term Debt Strategy (MTDS), the 2019 MTDS overlooks the importance of listing the projects (both on-going and earmarked) by sector to be implemented using debt in the medium term. Further, the MTDS should have included a detailed current debt servicing information on related projects and the status of their implementation. The borrowing strategy for FY 2019/20 is unclear in terms of the External debt to Domestic debt policy. The 2019 BPS projects that the country will borrow less domestically with a debt policy mix of 47: 53 percent. However, the Medium-term debt strategy (MTDS) indicates that the country will borrow more domestically with a policy mix of 62:38 percent.

The Committee has made several **recommendations** both policy interventions and financial recommendations among them-

- a) Allocation of **Ksh. 335.70 Billion** to the County governments' equitable share for Financial Year 2019/20 be allocated.
- b) Allocation of **Ksh. 55.40 Billion** to the county governments' as Conditional Grants.

- c) Suspension of payment to the Leasing of Medical Equipment Project and removal of the same from the Division of Revenue Bill until full disclosure on the costs is submitted tot Parlaiment..

Acknowledgement

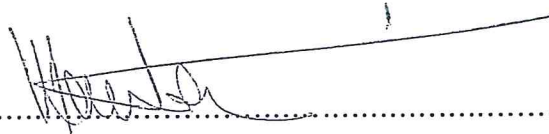
The Committee is also particularly grateful to the Offices of the Speaker and the Clerk of Senate for the support received as it discharged its mandate of examining the 2019 BPS as well as to the Senators who participated in the process.

The Committee is grateful to all the stakeholders who made contributions either through appearing before the Committee and or making written submissions. These includes the Senate Standing Committees, the National Treasury, the Commission on Revenue Allocation (CRA), Council of Governors ICPAK and IBP.

Mr. Speaker Sir,

It is therefore my pleasant duty and privilege, on behalf of the Standing Committee Finance and Budget to table this Report and recommend it to the House for adoption.

Signed

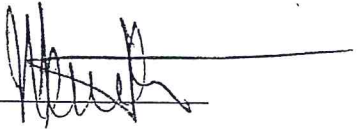


SEN. (ENG) MOHAMED MAALIM MOHAMUD, MP
CHAIRMAN, FINANCE AND BUDGET COMMITTEE

DATE: 26TH FEBRUARY, 2019

Adoption of the Report

Pursuant to standing order 213 (2) of the Senate Standing Orders, the Senate Standing Committee on Finance and Budget Committee adopted the report on Medium Term 2019 Budget Policy Statement (BPS). The Members of the Committee hereby affix their signatures to this Report to affirm the correctness of the contents and support for the Report –

Sen. (Eng) Mohamed M. Mahamud, CBS, MP -Chairperson 

Sen. (Dr) Isaac Mwaura, CBS, MP -Vice Chairperson _____

Sen. Wetang'ula Moses Masika, EGH, MP - Member 

Sen. Mutula Kilonzo Junior, MP - Member 

Sen. Aaron Cheruiyot, MP - Member 

Sen. (Dr.) Ali Abdullahi Ibrahim, CBS, MP - Member 

Sen. (Dr) Rose Nyamunga, MP - Member 

Sen. CPA Farhiya Haji, MP - Member 

Sen. Boniface Mutinda Kabaka, MP - Member _____

I. REVIEW OF THE 2019 BUDGET POLICY STATEMENT AND MEDIUM TERM DEBT MANAGEMENT STRATEGY

- 1) The Budget Policy Statement (BPS) is a policy document that sets out the broad strategic priorities and policy goals that will guide the national and county governments in preparing their budgets for the financial year and over the medium term. The strategic direction of the BPS is informed by the policies outlined in the various government policy documents such as Vision 2030, Ministerial and Sectoral Development Plans among others and is geared towards achieving overall economic growth and development. The growth strategy, revenue and expenditure proposals in a particular financial year should take into account the current state of the global and domestic economy including the outlook of the various macroeconomic variables.
- 2) The 2019 BPS serves as the guide document for key policies, priority programs and reforms which will be implemented over next three years (2019 – 2022). Under a banner titled, “The ‘Big Four’” Plan, the BPS outlines key interventions in manufacturing, agriculture and food security, healthcare as well as housing which will drive the economic transformation agenda towards industrialization, job creation and a general improvement in the quality of life for all Kenyans. To achieve these policies, the BPS also outlines overall expenditure proposals for programmes under various Ministries, Departments and Agencies (MDAs).
- 3) The 2019 BPS is divided into four parts as follows: Part I gives a general overview of the recent economic developments and the medium term outlook; Part II gives the details of the ‘Big Four’ plan including priority initiatives and targets to be achieved by 2022; Part III outlines the revenue and expenditure projections for 2019/20 and the medium term; and part IV discusses the county financial management and division of revenue.
- 4) The document is supposed to set out the broad objectives, policy goals and strategic priorities that guide the National and County Governments in preparing their budgets both for the following financial year and over the medium term. As provided by Section 25 of the Public Finance Management Act, 2012, the key contents of the BPS include the following:
 - i. An assessment of the current state of the economy and the financial outlook over the medium term, including macro-economic outlook.

- ii. Financial outlook with respect to Government revenues, expenditures and borrowing for the next financial year and over the medium term.
 - iii. The proposed expenditure ceilings for the 3 arms of Government and indicative transfers to County Government.
 - iv. The fiscal responsibility principles and financial objectives over the medium term including limits on total annual debt.
 - v. The total resources to be allocated to individual programmes and projects within sector, ministries, departments and agencies indicating outputs expected during the period.
- 5) The role of Senate in the review and approval of government economic and spending policies contained in the BPS are clearly buttressed in the functions of the Senate as set out in Article 96 of the Constitution. The BPS sets out the annual revenue amounts to be raised by the National Government; these are invariably the resources that are allocated to each level of government including counties (Article 203).
- 6) The Senate's role therefore spans protecting the financing of counties, ensuring unified economic policies and prosperity in counties for the benefit of all Kenyans, and to improve national and intra-county business climate. Thus, there is an overwhelming case for the Senate to pronounce itself on any matter it deems fit as articulated in the BPS.

Highlights Of The Budget Ceilings For Financial Year 2019/20

- 7) The indicative expenditure ceilings for FY 2019/20 amount to Ksh. 2,678.87 Billion and include the following proposed allocations-
- | | |
|--------------------------------|----------------------|
| i. National Government | Ksh.1,766.36 Billion |
| ii. Parliament | Ksh.38.50 Billion |
| iii. Judiciary | Ksh. 17.46 Billion |
| iv. Consolidated Fund Services | Ksh.535.75 Billion |
| v. County Equitable Share | Ksh.310.00 Billion |
| vi. Equalization Fund | Ksh.5.80 Billion |
| vii. Contingency Fund | Ksh.5.00 Billion |
- 8) The government targets total revenue collection including Appropriation-In-Aid (A-I-A) of **Ksh. 2,081 billion** for FY 2019/20 compared to **Ksh. 1,832 billion** for FY 2018/19. Ordinary revenue is projected at **Ksh.1,877.20 billion** for FY 2019/20 which is higher than **Ksh.1,652 billion** estimated for FY 2018/19.

- 9) According to the 2019 BPS, the projected revenue performance will be underpinned by ongoing reforms in tax policy and revenue administration which are similar to those identified in the 2018 BPS, that include- enhanced scanning to detect concealment and increase efficiency in cargo clearing through procurement of additional scanners and full integration of all scanners, use of Regional Electronic Cargo Tracking System (RECTS) to ensure all goods reach the desired destinations and avoid dumping; the use of third-party information to identify non-compliant property developers and ensure they are included in the tax base; and detection of non-compliance through i-Tax data matching. However, the BPS 2019 does not report on the progress of achievement and how much is expected to raise specifically through these reforms.
- 10) Given the sustained underperformance of revenue in the past years, it is very important to ensure that the revenues projected for 2019/20 are realistic. The National Treasury-in collaboration with KRA- should provide clear quantifiable and realistic tax administration measures towards boosting revenue collection.

Realism Of The 2019/20 Macro-Fiscal Framework

a) Economic Growth

- 11) Kenya's economic growth has remained stable in the period 2013 – 2017 at 5.6 percent compared to 4.7 percent (2008 – 2012) percent and 4.6 percent (2002-2007). The economic growth for 2018 is projected at 6.0 percent an increase from 4.9 percent in 2017, the growth was supported by improved weather conditions, improved business activities and easing of political uncertainty. Going forward, the growth projections are 6.2 percent in 2019 and 6.3 percent in 2020. The key drivers of growth will be *strong performance in the agricultural and manufacturing activities, favorable weather conditions, strong service sector, ongoing public infrastructural investments, sustained business confidence and stable macroeconomic environment that maybe pegged on security and a calm political climate*. Indeed, while this is impressive growth, the emerging concern is that these key drivers of economic growth are not anchored on key policy changes but are based on factors beyond the control of policy makers such as favorable weather conditions, security and calm political environment. The 10 percent annual economic growth target in Kenya's VISION 2030 therefore remains elusive and the economy needs a significant change in policy direction and budget execution to scale up the country's productive capacity that will promote a higher growth trajectory.

- ♦ **Agriculture:** To boost growth through increased agricultural productivity, there is need to look beyond the prospects of a favourable weather outlook and look into

remedying the quality concerns and inadequate policy implementation that remain a challenge for the sector. Past government interventions to enhance agricultural productivity such as large-scale irrigation, distribution of certified seeds and fertilizer have not enhanced food production as expected mainly due to poor implementation of these projects. It is indicated in 2019 BPS that the sector will focus on land management, livestock resource management, increasing agricultural productivity, water storage, blue economy and agricultural research. However, it is not clear exactly how these priorities will be achieved. Further, given that agriculture is a fully devolved function, there is need for a clear collaborative framework between the two levels of government on how some of these targets will be achieved.

- **Manufacturing:** The manufacturing sector continues to face challenges ranging from shortage of capital due to inadequate access to finances, raw materials and skilled labour in addition to several regulatory challenges. Key areas of focus should be intervention in the expansion and promotion of small-scale industries, reduction of high power tariffs, access to finance and access to preferential markets identified by the State departments for industrialization and trade. County governments could identify specific small-scale industries that can be established in counties to boost local production.
- **Ongoing Infrastructure projects:** Low absorption of development expenditure and reductions during supplementary budgets especially for infrastructure projects is the main risk to infrastructure as a key driver of economic growth. This is because the delayed completion of projects typically adversely affects returns on investment. According to the latest released list of stalled government projects as at the beginning of FY 2018/19, transport infrastructure has the most stalled projects. The general reasons for stalling include delays in obtaining approvals, financial constraints including non-payment to contractors and suspension or termination of some of the contracts. The outstanding budgetary cost for the projects is Kshs. 69.2 Billion as of beginning of FY 2018/19 which translates to 78.7 percent of the estimated cost of the projects.

b) Inflation

- 12) The overall monthly inflation remained relatively stable at an average of 4.7 percent in 2018 compared to 8.0 percent in 2017. This is attributable to increased food production leading to lower food prices as well as lower energy prices due to increased hydropower generation. Inflation has remained within the target range of 5 ± 2.5 percent. The BPS 2019 projects the inflation will remain within the target range in the medium term supported by lower food prices reflecting favorable weather conditions, reduced electricity tariffs and lower international oil prices. Going forward, risks to inflation outlook are likely to emanate mostly from a shift in oil prices. Though currently projected at low levels, fuel prices may go up if the USA imposes sanctions on Venezuela and Iran coupled with the decision by OPEC to cut supply of crude oil ends up limiting oil production. Higher fuel costs will invariably lead to higher transportation costs.

c) Interest Rates and Private Sector Credit

- 13) The Central Bank Rate (CBR) has been adjusted over the past five years to anchor inflation expectations with the most recent adjustment being in July 2018 – from 9.5 percent to 9.0 percent in March 2018 – to ease monetary policy stance in support of economic activity. The outlook in 2019 BPS is that interest rates will remain low and stable supported by improved liquidity conditions and ongoing fiscal consolidation. According to CBK, the lowering of the CBR was aimed at increasing the uptake of credit by the private sector, however, annual growth of credit to the private sector declined from 2.5 percent in 2017 to 2.4 percent in 2018. A likely reason for this could be the crowding out of the credit to the private sector by the government through domestic borrowing given that the net domestic borrowing target for FY 2019/20 has increased to Kshs. 317.1 Billion from Kshs. 268.7 Billion in FY 2018/19. This means that commercial banks may continue lending to government which is less risky at the expense of the private sector. As a result, credit to the private sector may not increase as envisaged.

d) Exchange Rate & External Sector

- 14) The exchange rate was stable against major international currencies in 2018 and beginning of 2019 compared to previous years. The outlook in the 2019 BPS is that it will remain stable supported by improved performance of inflows from exports, continued increase in diaspora remittances and growth in tourism. The foreign exchange reserves remained an adequate buffer for short-term foreign exchange shocks at 5.5 months of import cover above the required threshold of at least 4 months. The risk to the exchange rate is the over-reliance on hot money

flows as the main source for foreign reserve stocks. Though diaspora remittances have grown significantly in the past, they are not reliable as a source of foreign exchange. Focus should therefore be on attracting Foreign Direct Investment (FDI) as well as diversifying and growing the country's exports.

e) Fiscal Policy

- 15) Fiscal consolidation is one of the key objectives in the 2019 BPS. It entails the government tightening its belt through expenditure cuts since tax increments are currently not a favorable option for the economy. Analysis indicates that the current fiscal policy is edging towards a contractionary fiscal policy for FY 2019/20 and the medium term as indicated by a fiscal impulse that is slowly edging upwards. While this is commendable, the challenge will be in maintaining a contractionary fiscal path given the prevailing expenditure pressures that mostly increase recurrent expenditures and reduce development expenditures. It should be noted that in the 2018 BPS, the fiscal deficit for FY 2019/20 was projected at 4.3 percent of GDP but in the 2019 BPS, it is projected at 5.1 percent. This may affect the effectiveness of the budget as a tool for economic growth.

Creating Jobs, Transforming Lives – The Big Four Plan

- 16) The 2019 BPS sets out broad strategic priorities on policies and programmes that are geared towards the realization of the big four agenda and most of these priorities were initiated in the 2018/19 budget. The 'Big Four' plan is targeted at supporting job creation by increasing value addition and the manufacturing sector's share of GDP; enhancing food and nutrition security; providing universal health coverage to all Kenyans and provision of affordable housing.
- 17) The 2019 BPS outlines the Big 4 plan as government's key agenda to be implemented in the medium term and it is expected that counties have substantial role play in actualizing the agenda. However, it's not clear from the proposed allocation and policies on what role counties may be engaged. This is likely to pose risks of duplication and overlaps and there is need for an inter-fiscal framework for implementing the Big 4 Plan and strategically harmonized to guide resource allocation and service delivery to minimize those risks.

County Financial Management & Division Of Revenue For FY 2019/20

a) County Revenue

- 18) County governments have received a cumulative allocation of Kshs. 1,767.30 Billion since the onset of devolution. This comprises of equitable share of Kshs 1,572.80 billion and additional Kshs 194.50 billion in form of conditional grants from the national government share for specific programmes and policies. The main sources of financing to counties are equitable share accounting for over 80 percent, the conditional grants from both national government as well as proceeds from loans and grants from development partners and counties own source revenue mainly raised from several tax streams such as business permits, imposition of property rates, in line with the Article 209 of the Constitution.
- 19) Over the period FY 2013/14 and 2019/20, annual growth rate of the equitable share allocated to the counties has been reducing from 19.32 percent in financial year 2014/15 to slightly below 4 per cent in FY 2018/19. Though the annual allocations in nominal terms has been increasing there has been deaccelerated allocated of the equitable share. The equitable share is calculated on the basis of the most recent audited accounts of revenue received, as approved by the National Assembly. The Approval of the Audited Accounts has been lagging behind to the detriment of the counties. The Division of Revenue for FY 2019/20 will be based on audited revenue for FY 2014/15 of Kshs 1,038 Billion.
- 20) The 2019 BPS indicates that the National Policy on supporting enhancement of county government's Own Source Revenue (OSR) was approved by Cabinet in FY 2017/18 and its implementation will assist counties in determining their revenue potentials, revenue forecasting, assist counties in establishing appropriate institutional arrangement for collecting OSR. To support implementation of the policy, the National Treasury submitted to Parliament a draft legislation on County Governments (Revenue Raising Process) Bill, 2018.

b) County Expenditures

- 21) Total approved county budgets for FY 2017/18 amounted to Kshs 410.50 billion, made up of Ksh 271.00 billion (66%) recurrent expenditure and Kshs.139.81 billion (34%) for development expenditure. In aggregate terms, this level of approvals complied to the fiscal rules stipulating at-least 30% of total county allocation is towards development outlays. However, the actual county expenditure performance translated to 74% of the approved budget with an expenditure of Ksh. 303.83 billion. This expenditure level is also lower compared to the previous FY 2016/17 and FY 2015/16.
- 22) In view of actual expenditure, compliance to fiscal rules deteriorated during budget execution perhaps due to reallocations and virements of allocations between programmes towards

recurrent expenditure. Only nine counties maintained the development – recurrent mix threshold implying in-year approved re-allocations towards recurrent activities that affects creation of asset capacity and pose clear potential risk to county expenditure performance in the medium term.

Pending Bills

23) According to the controller of Budget, County Governments total pending bills for the period under review stood at Kshs 108.41 billion. This translates to an average of 36 percent of the 2017/18 equitable share (Kshs. 302 Billion). This is as compared to the cumulative pending bill of Kshs. 35.84 billion as at end of FY 2016/17, thus increased by approximately 202 percent. Further, some counties did not submit status of their pending bills in the previous years unlike in the FY 2017/18 when the disclosure was done by respective County Treasuries. The total pending bill for FY 2017/18 is composed of 74% recurrent component and 26% development component.

Vertical Allocation Between The National And County Governments For Fy 2019/20

- 24) The 2019 BPS proposes a reduction in county equitable share of Kshs. 310.00 billion from the Kshs. 314.00 billion provided for in the Division of Revenue Act, 2018. In addition, the total conditional grants allocation to counties for FY 2019/20 is Kshs 61.6 billion, of which Kshs. 38.71 Billion is from development partners. Therefore, the total proposed allocation to counties for FY 2019/20 is Kshs. 371.6 billion which is a reduction relative to the total allocation of Kshs. 376.4 billion for FY 2018/19, inclusive of additional conditional allocations from development partners provided in the amendment to DORA, 2018.
- 25) According to the National Treasury the revised base of Ksh. 304.96 Billion is on account of underperformance of revenue that resulted to a downward adjustment of the forecasted revenue for FY 2018/19 by Ksh. 117.7 Billion from Ksh. 1,769 Billion to Ksh. 1,652 Billion. However, this contradicts an estimated favourable growth of 6.1 percent for FY 2018/19. Further, the proposed reduction in equitable share is not based on any law since it has not been approved by Parliament (National Assembly and Senate) and further contravenes section 5(1) of the 2018 DORA in which any shortfall in expected revenue is to be borne out by the national government. In principle, this legal provision is in line with the sum of criteria outlined in the constitution (Art 203 (1)) of ensuring ‘desirability of stable and predictable allocation of revenue’ as highlighted earlier.

26) The Commission on Revenue Allocation (CRA) proposes a County Equitable Share allocation of Kshs. 335.70 Billion for FY 2019/20. The recommendation is based on adjusting the current base of Ksh. 314 Billion by an actual three-year average of annual inflation factor of 6.9 percent. There are inconsistencies in computing the proposed allocation between CRA and National Treasury. While CRA's proposal takes into consideration inflation effect in line with key principles such as desirability of stable and predictable allocation of revenue, the basis for the proposed increase by National Treasury Kshs 304.96 billion to Ksh. 310 billion is not clear.

Medium Term Debt Management Strategy For FY 2019/20

27) The MTDS for FY 2019/20 proposes a borrowing framework of 38 percent from external borrowing and 62 percent for domestic borrowing to finance the national budget deficit. External Debt will be financed through 26 percent from concessional financing, 8 percent from semi concessional financing and 4 percent from commercial financing. As at the end of December 2018, the level of debt in nominal terms reached Kshs. 5.28 trillion making up 52.7 percent of GDP, having risen by 13 percent or 698.4 billion, from Kshs. 4.57 trillion, December 2017. This increase is as a result of increase in disbursement of external loans (Bilateral debt increased by Kshs. 81.5 billion and commercial loans by Ksh. 40 billion) and comprises of debt 48.3 percent in domestic debt and 51.6 percent in external debt. Debt growth is set to continue increase and reach Kshs. 5.7 trillion and Kshs. 6.3 trillion as at the end of FY 2018/19 and FY 2019/20, respectively.

28) The rising debt levels lead to increased debt refinancing requirements and interest payments that shrink the fiscal space in the forward years. Therefore, rising debt servicing commitments was the main reason behind the IMF's reclassification of Kenya's debt distress levels from low to moderate in FY 2018/19. Even though the government indicates the implementation of a fiscal consolidation strategy, its effects cannot be immediately realized given that the trajectory of the fiscal deficit has not changed, and the financing strategy is never adhered to.

29) Domestic debt comprises of Treasury bills and bonds worth Kshs. 899.40 billion and Kshs. 1.55 trillion respectively. While the external debt, comprises of Bilateral debt (Kshs. 894.00 billion), Commercial loans (Kshs. 938.20 billion) and Multilateral debt (Kshs. 874.70 billion). Over the years, the component of commercial debt has increased consistently as the government sought extra resources to finance infrastructure projects under energy, rail, roads etc.

- 30) The national stock of debt also comprises of debt guarantees under Article 213 of the Constitution and Section 58 of the PFM Act, 2012. These form part of fiscal contingent liability i.e. if an institution fails make payments for a guaranteed loan it necessitates the government to step in and shoulder the extra-burden by use already limited financial resources. As at the end of December 2018, a total of Kshs. 147.7 billion worth of guarantees had been provided to 8 institutions and has increased from Ksh. 133.79 (December 2017). This is as a result of increase in guarantees to Kenya Ports Authority, Kenya Broadcasting Corporation and a new guarantee provided to Kenya Power. This could therefore indicate an inconsistency, given that debt guarantees need Parliamentary approval and the last approval was to Kenya Airways. Out of the portfolio, loans worth Kshs. 1.9 billion are non-performing owing to guarantees to Kenya Broadcasting Corporation, Tana & Athi Rivers Development. Authority and East African Portland cement.
- 31) The borrowing strategy for FY 2019/20 is unclear in terms of the External debt to Domestic debt policy mix since the 2019 BPS projects that the country will borrow less domestically with a debt policy mix of 47: 53 percent. However, the Medium-term debt strategy indicates that the country will borrow more domestically with a policy mix of 62:38 percent.
- 32) The Public Debt Sustainability Analysis (DSA) framework that evaluates a country's capacity to finance policy agenda, service ensuing debt without unduly large adjustments that may compromise its macroeconomic stability. The current public sector DSA indicates that the level of debt is still considered sustainable at 60.6 percent of GDP in Net Present Value terms against an IMF threshold of 74 percent. However, the ratio is beyond the 50 percent threshold provided for in the PFM Act Regulations. Other indicators that the country has breached include the ratio of PV of debt service to revenue and the PV of Debt to revenue ratio at 43.7 and 300 respectively compared to a threshold of 30 and 300. This indicates liquidity shocks from debt service which is a first charge and takes up a large amount of the revenue collected.

II. SUBMISSIONS FROM STAKEHOLDERS

- 33) Pursuant to Standing Order 180 (5), the Committee on 15th February, 2019 invited several stakeholders, among them: the Commission for Revenue Allocation (CRA); Controller of Budget (CoB); Institute of Certified Professional Accountants of Kenya (ICPAK); the Council of Governors (CoG); International Budget Partnership of Kenya (IBP); and the Cabinet Secretary, National Treasury and Planning.
- 34) On 21st February, 2019, representatives from the CRA, CoB and ICPAK appeared before the Committee and submitted their views outlined herein. The CoG and IBP submitted a memorandum on the same matter.

The Commission on Revenue Allocation (CRA)

- 35) The Commission was in agreement with the proposed fiscal consolidation in the 2019 Budget Policy Statement as presented by the National Treasury. Fiscal Deficit was projected to reduce from 3.9 per cent to 3.3 per cent of GDP over the medium term; by end of Financial Year (FY) 2021/2022.
- 36) Despite the past trend by the National Treasury of over-projecting revenue collection in the BPS, the actual analysis indicates a growing economy whose expansion is not commensurate with the revenue performance over the last five years. The BPS 2019 projects that the GDP growth rate will be from 6.1 per cent in 2018/19 to 6.2 per cent in 2019/20 FYs. However, the growth is not reflected in the shareable revenue as a percentage of the GDP which remains constant at 16.5 per cent for the 2018/19 and 2019/20 financial years. The analysis also indicates an unstable trend and underperformance of revenues which consequently affects the division of sharable revenue in the long run.
- 37) The BPS 2019 indicates a growth in nominal revenues of more than Kshs. 200 Billion, from Kshs. 1,652 Billion in 2018/19 to 1,877 billion in 2019/20 FYs. The nominal growth in revenues is supposed to be shared equitably as opposed to a proposal indicated in the BPS of Kshs. 310 Billion (county equitable share) which is not justifiable.
- 38) The CRA explained its proposal in the 2019 BPS, the guiding framework for revenue sharing that aligns to the fiscal framework as indicated in the table below.

	Budget Items	Kshs. Billion
1.	Principle for revenue sharing between national and county governments	
	(a) Current level of funding Devolved Functions	314
	(b) Unfunded mandates	
	(c) New Functions	-
	(d) Provisions for sustainability and growth in services	
	i. Adjustment for inflation (3 Year average inflation 6.9per cent)	21.7
	ii. Growth factor (Population growth rate 1.4 per cent)	-
2.	Total equitable share to County government for FY 2019/20	335.7
3.	Equalization Fund (0.5per cent of 2014/15 audited accounts)	5.2
4.	Total equitable share to National Government	1,529.5

39) The Commission indicated that there should be a growth on the sharable revenue between the two levels of government. However, as indicated in the BPS 2019 the National Treasury and Planning indicates a proposal of reduction in the County Government's equitable share but not the National Government. From the proposal of reduction of the County equitable share, this might compromise on service delivery of essential services. In this regard, both the National and County government should rethink on how to reduce the ballooning wage bill which takes more than 70 per cent of the sharable revenue and relook into the criteria used to determine what share of the sharable revenue is allocated to items regarded as the national interest by the national government.

40) Low development spending and wage bill thresh holds in some counties emanates from inherited staff an issue which is still pending at the Summit for resolution.

Controller of Budget

The representatives from the Controller of Budget informed the Committee that:

i. Big Four Plan

- 41) The BPS covers collaboration in two areas namely: Universal Health Coverage and Affordable and Decent Housing. Appropriate clarification in all other areas of collaboration such as Value Addition and Raising the Share of Manufacturing Sector to GDP; and Enhancing Food and Nutrition Security is important. This will enhance effective delivery of priority policies and programmes through devolution and mitigate the risk of duplication and possible intergovernmental conflict that could negatively affect realization of the Big Four Plan.
- 42) In the afore-mentioned the BPS should clarify areas of collaboration with county governments in the Big Four Plan to enable county governments incorporate the same in the County Fiscal Strategy Papers.
- 43) Despite the fact that the manufacturing sector growth is essential through agro-processing and building industries in other sectors, the BPS has not highlighted why the manufacturing sector has not performed optimally in the past, what challenges were experienced and appropriate measures to enhance success.
- 44) Whereas the Government plans to allocate funds for food security in particular to increase maize production, the subsector has recently experienced challenges hence the need for emphasis on accountability.

ii. Revenue Projections

- 45) The BPS 2019 projects revenue to increase by Kshs. 249.4 Billion to Kshs. 2.08 Trillion in FY 2019/20 from Kshs. 1.83 trillion in FY 2018/19. Compared to historical trends, the projected increase may be unrealistic and therefore unachievable. Therefore, it may be necessary to revise this projection to a realistic amount.

iii. Sustainability of debt

- 46) In the BPS 2019, the National Treasury and Planning indicates that the Country's Present Value of Public Debt to GDP was 60.6 per cent in 2018 compared to recognized threshold of 70 per cent. Similarly, the present value of the public debt to revenue was 292 per cent in the same period compared to recognized threshold of 300 per cent. This indicates that the Kenya's risk to debt distress has been raised from low to moderate. Thus, stress test threshold could be breached if there are external shocks or abrupt changes in macro-economic policies. It may be

necessary to consider other public debt indicators such as World Bank Rank Country Policy and Institutional Assessment.

iv. Proposed Allocation of Sharable Revenue

47) The Division of Revenue Act, 2018 allocated Kshs. 314 Billion as equitable share of revenue raised nationally to counties for FY 2018/19, while the 2019 BPS contains a figure of Kshs. 304.96 billion. No explanation is provided for this variance.

The Institute of Certified Public Accountants of Kenya

48) The Institute of Certified Public Accountants of Kenya (ICPAK) raised the following issues and recommendations as shown in the table below:

Issues of Concern	Observations/ Recommendations
a) Per-capita income and job creation	<ul style="list-style-type: none"> • Improve the regulatory environment for the informal sector to support stability and growth of Micro, Small and Medium Enterprises (MSMEs) to overcome start-up challenges and contribute to economic development • Devise mechanisms for identification of informal sector players to contribute to tax revenue. • Formalize the informal sector by limiting cash-based transactions as a means to capture all business activities in the economy
b) Net Foreign Assets	The BPS 2019 indicates Kenya's Net Foreign Assets (NFA) grew by 22.3per cent yet with the increase in public debt and the import bill indicates otherwise. This needs to be revised for clarity.
c) Modernized Income Tax Bill	<ul style="list-style-type: none"> • Legislation, including subsidiary legislation, traces its foundation on an agreed policy framework, to establish the most appropriate approach to resolve a problem. • As such, the review of the Income Tax Act should be predicated on a comprehensive Income Tax policy. • It is therefore the Institute's professional opinion that an income tax policy should be developed to guide the review process of the Income Tax Act. • Further it is important to envisage the entirety of the tax frame and develop an overarching tax policy ahead of any taxation.
d) Real GDP Growth	There's need to consider more realistic growth targets given the economy's vulnerability to shocks. The World Bank (through the Kenya Economic Update 2018) lowers growth rates compared to those given in the BPS 2019, that Kenya's economy is expected to grow by 5.7per cent FY 2018/19, 5.8per cent FY 2019/20 and 6.0 per cent in 2020/21. Since the expected economic growth is a factor

		in subsequent macro-economic and fiscal projections, ICPAK argues for a more prudent approach which does not over-project the state of the economy.
e)	Government Policies to support Fiscal Consolidation	<ul style="list-style-type: none"> • There is need to re-ignite private sector led growth, in this regard, fiscal consolidation must be growth friendly; • Fiscal consolidation needs to be recalibrated towards recurrent spending such as – lowering of transfers to state owned enterprises, cleaning and regular audit of the payroll register, keeping wages, salaries and allowance adjustments in line with recommendations from the Salaries and Remuneration Commission (SRC) • Fiscal policy should geared towards regenerative expenditure not consumptive expenditure
f)	Big Four Plan	<ul style="list-style-type: none"> • MSMEs to further support the manufacturing sector, the Government to continue to promote provision of financial support and credit to Micro, Small and Medium Enterprises • Food Security: - the Government to continue to implement measures in the agricultural sector in order to ensure food and nutrition security including food storage and irrigation services. • Universal Health Coverage (UHC)-the government should complete reconfiguration and digitization of NHIF to ensure the system is ready for roll out before fully implementing the UHC and increase the health budgetary allocation to the recommended 15per cent of the total annual budget as recommended by the African Union under the auspices of Abuja Declaration. • National Housing Development Fund - Consider incentive to businesses by way of either tax credits or allow for the contributions to be treated as tax allowable. This will be a useful relief to businesses which are already doing business. • Other issues that affect the Big Four are:- Monitoring and evaluation system, how to tax idle land , Block chain technology, access to water, sports fund, consolidation of Uwezo Fund, Youth Enterprise Development Fund and Women Enterprise Development Fund, strengthening governance and fight against corruption, realism of revenue forecast as it is ambitious and leads to budget deficits
g)	Own Source Revenue (OSR)	<ul style="list-style-type: none"> • Fast-track implementation of the OSR Policy as developed by the National Treasury for effective revenue management across the Counties, • There is need to integrate the different systems for revenue collection and management. IFMIS has been very vital in entrenching accountability in financial management. • County Treasuries should continuously review the performance of revenue collection vis-à-vis targets and shall

		<p>include a status report in the Quarterly and Annual reports which shall be published in various media</p> <ul style="list-style-type: none"> • The standardized ICT-based system prescribed should provide real time revenue information in a consistent manner to enable consolidation and analysis, as well as periodic reports for use by the National Treasury, the CoB, the CRA and the Office of the Auditor General, and also easily accessible by the general public. • Consider positioning the Kenya Revenue Authority as the collector of county revenues to support revenue collection at that level.
	h) Absorption of Development Funds	<ul style="list-style-type: none"> • The low absorption rates of approved budgets are a pointer to weak budgeting process in relation to: - Over-ambitious and unrealistic revenue projections which become unachieved; As a result of the above, erratic exchequer releases serve to compound the problem. • The need to rethink the budgeting frame work more specifically around revenue projections. This has consequent effect on budget implementation
	i) Pending bills	<ul style="list-style-type: none"> • According to the Auditor General Reports, there has been an increase in pending bills in the recent times. • Globally, under cash accounting, transactions are recognized only when the associated cash is received or paid, and economic events are not reported if there is no immediate exchange of cash. Accrual accounting therefore offers several benefits: accrual-based fiscal reports provide a more comprehensive view of the government's financial performance and the cost of government activities; • focus greater attention on the part of policymakers and the public on the acquisition, disposal, and management of government assets, liabilities, and contingent liabilities • by consolidating not only central government ministries and agencies but all institutional units under government control, accrual accounts provide a more complete picture of the financial position of the public sector as a whole; • by reporting stocks and flows within an integrated accounting framework based on internationally-accepted standards such as IPSAS, accrual accounting can improve the reliability and integrity of government financial data
	j) Absence of audit committees	<ul style="list-style-type: none"> • Continuously lobby County entities to establish audit committees; • Capacity building of established audit committees on their roles; • Support CRA's proposals to have this as a variable under the Fiscal Prudence parameter for revenue share. This will obligate counties to establish and operationalize effective Audit Committees

Council of Governors

- 49) The memorandum from Council of Governors indicated that the Council was against the proposal in the in the BPS 2019 by the National Treasury to have counties equitable share for 2018/19 reduce from Kshs. 314 billion to Kshs. 304 billion against what was approved by Parliament.
- 50) Additionally, according to the Division of Revenue Act, 2018 if the actual revenue raised nationally in any years falls short of projections, the shortfall is to be borne by the National Government to the extent of the threshold prescribed in the Regulations by the Cabinet Secretary. Therefore, this exonerates counties from bearing the burden of revenue shortfalls hence counties revenues should not be reduced. The Council proposes that the revenue base for adjustment for county governments for 2019/ 20 financial year should therefore be Kshs. 314 billion and not Kshs. 304 billion.
- 51) The County equitable share for 2019/20 FY should therefore be Kshs. 343.7 billion comprising of adjustment base of Kshs. 314 billion; with Kshs. 8.7 billion worth of unfunded functions and 6.9 per cent average three year annual inflation. Given the fact that, there are unfunded functions the county governments should be allocated funds on unfunded transferred functions such as the transfer of 31,000 KM of roads and library services amounting to Kshs. 8.7 billion to Counties Governments. The allocation has been pending awaiting Summit's approval of the inter-agency report recommending the same.
- 52) To achieve stability and predictability in implementation of County budgets, there is need to use an average inflation rate. This would ensure the functions of both the national and county governments are not subjected to volatile budgets. The Council recommends the use of an average inflation rate to cater for increase in service costs.
- 53) Currently, nine (9) counties are expected to lose an accumulative amounting of Kshs. 7.3 Billion worth of allocation when 3rd generation revenue formulae is applied against the CRA equitable share proposal of Kshs. 335.7 billion. If the National Treasury proposal of Kshs. 310 billion is adopted, counties would have to lose Kshs. 25 billion before the formula is even applied.

International Budget Partnership Kenya (IBP)

54) The memorandum from IBP Kenya raised key issues and also made the following recommendations:

- i. **Ballooning Wage bill-** The Senate and the National Treasury should take advantage of the current review of the equitable revenue sharing mechanism to help counties address challenges from inherited staff costs;
- ii. **Public Hearings in the Budget Process-** Public Sector Hearings remain centred in Nairobi and should be decentralized and held in different parts of the country;
- iii. **Finalization of spending plans-**Finalization of the detailed budgets should entail scrutiny to curtail spending on non-productive areas and ensure resources are directed to priority programs;
- iv. **County revenue collection potential report should be published and publicized to help inform public debate on county revenue especially in relation to their Finance Bills.** The Own-Source Revenue Potential and Tax Gap Study of Kenya's County Governments provides the first window into fiscal capacity at the county level. This set of information is critical as discussion on having a county own source revenue policy is finalized. In addition, the on-going review of the third equitable revenue sharing formula would benefit from this data as part of how to measure fiscal capacity;
- v. **Revenue targeting seems inconsistent with historical performance and too ambitious.** The 2019 BPS shows that the government projects to collect 14 per cent more revenue in FY 2019/20 compared to the targets set for 2018/19. This would be higher than the projected 8 per cent growth for expenditure. That indicates that the government revenue targets would help in reducing the deficits in 2019/20 which is one key indicator of governments' effort on fiscal consolidation;
- vi. **The revenue growth factor of the county equitable revenue should be more predictable and realistic.** The BPS recommends that counties be allocated Kshs. 310 billion in 2019/20. This is lower than the amount of Kshs. 314 billion approved in 2018/19 and only 2 per cent higher than the revised allocation of Kshs. 304 billion for the same year. In addition, significantly different from the 10 per cent growth in the amount recommended by the Commission of Revenue Allocation, also based

on the revised amount of Kshs. 304 billion. There is need for a clear determinant of how revenue to counties will grow from year to year especially informed by ordinary revenue trends from previous years; and

- vii. There is need for clarity on what is the planning policy informing government budgeting. The BPS 2019 should clearly indicate whether the Big Four Agenda priorities are part of the Medium-Term Plan III or whether they are independent. The BPS 2019 as framed does not give a clear picture of the planning policy in use and what the expected long-term gains will be.
- viii. The BPS 2019 should provide details of major capital projects across sectors. A list of public-private partnership projects. However, The BPS does not explain whether these are the only PPP projects that will be in the 2019/20 budget or explain why the other sectors are not included if there are other projects beyond energy. In addition, this should have details of how capital projects are prioritized especially with revenue challenges as identified in the BPS
- ix. The BPS should provide access to information referred to therein. The BPS makes reference to information, numerous policy and budget related documents that are unavailable in the National Treasury Website or elsewhere. These documents enable readers to reference these documents to understand the proposals therein. This information should be available online and the website link available in the same page that the BPS is published on the National Treasury website.

The National Treasury and Planning

55) The Chief Administrative Secretary (CAS) National Treasury and Planning in his submission to the Committee highlighted as follows:

56) The theme for 2019 BPS is “*Creating Jobs, Transforming Lives- Harnessing the Big Four*”. The policy prioritizes investments in the Big four Agenda, namely: Manufacturing for Job Creation, Food and Nutrition Security, Universal Health Coverage and Affordable Decent Housing.

Overview of the 2019 BPS

57) The policy outlined in the BPS draws from the national development agenda as outlined in the Third Medium Term Plan (MTP III) of the Vision 2030 and targets to attain the Sustainable Development Goals (SDGs) of the United Nations. The policy prioritizes investments in “The

Big Four” Plan, that is: manufacturing for job creation; food and nutrition security; Universal Health Coverage; and affordable housing. In addition, the policy prioritizes creation of a conducive business environment under all the enablers of the “Big Four” Plan.

58) Notable progress has been made on the implementation of the “Big Four” Plan across the four strategic areas:

- (i) To support growth of the manufacturing sector, the Government has scaled up reforms to encourage investment in the sector. In particular, the Government has heightened the fight against illicit trade and contrabands to protect genuine businesses and traders.
- (ii) To enhance food and nutrition security, the Government has aligned all policies under the agriculture sector towards increasing food production, boosting smallholder productivity and reducing the cost of food.
- (iii) To make Universal Health Coverage a reality, the Government has launched the pilot phase of the universal health programme in four Counties namely, Kisumu, Machakos, Nyeri and Isiolo.
- (iv) Finally, on housing, the Government has established the National Housing Development Fund which will be responsible for mobilizing capital to finance the affordable housing project. Additionally, the Government has established the Kenya Mortgage Refinance Company (KMRC) to leverage funds from Development partners and the private sector and provide secure long-term funding to financial institutions thereby increasing the availability and affordability of mortgage loans to Kenyans.

59) The resource allocation for the National Government in the BPS for FY 2019/20 have been realigned to “The Big Four” Plan. Thus, the targeted expenditures will prioritize employment creation, youth empowerment, supporting manufacturing activities, enhancing health coverage, improving food security and enhancing living conditions through affordable housing. The allocations to other critical sectors such as education, infrastructure, energy and social protection will remain protected so as to achieve the targeted objectives

60) **Performance of the Economy:** Despite the fact that the economy is strong and resilient at an estimated growth of 6.2 per cent for 2019/20 up from 6.0 per cent in 2018/19 FYs, the Global Economic Growth is projected to be weakening at 3.5 per cent in 2019. Notably, the Sub-Saharan African Region is expected to register a growth of 3.5 per cent for the same period as a result of commodity prices and access to capital markets. The Exchange Rate remains stable

and competitive against the major international currencies, which has been supported by a low and stable inflation rate. Consequently, short term interest rates have remained fairly low and stable due ample liquidity in the money market.

- 61) Budget Implementation: Implementation of programmes in the first quarter of FY 2018/19 was slow due to budget rationalization to align expenditure priorities to revenues after amendments to the Finance Bill, 2018. The revised total revenue is projected at Kshs. 1,852.6 billion out of which ordinary revenue is projected at Kshs. 1,672.2 billion. The projected total revenue for FY 2019/20 is projected at Kshs. 2,080.9 billion whereas the projected ordinary revenue is projected at Kshs. 1,877.2 billion. The overall expenditure and net lending for FY 2019/20 is projected at Kshs. 2,704.7 billion.
- 62) Reforms to Support Fiscal Consolidation Plan: The fiscal framework supports fiscal consolidation plan that will see a gradual reduction in fiscal deficit from 7.2 per cent in FY 2017/18 to 3.1 per cent of GDP over the medium term in line with the East African Monetary Union Protocol target of 3.0 per cent of GDP. The consolidation will be supported by enhanced revenue mobilization from private sector players, development partners and rationalization of recurrent expenditure. To increase efficiency and effectiveness of public spending, the Government has established the Public Investment and Management (PIM) Unit and adopted the Public Investment Guidelines that will guide appraisal of all projects before their inclusion in the budget
- 63) County Governments Equitable Share FYs 2018/19 and 2019/20: In view of underperformance in revenue raised nationally, the National Treasury proposed a reduction of County Equitable share for 2018/19 by Kshs. 9.04 billion (from Kshs. 314 billion to Kshs. 304 billion). Furthermore, the proposed county equitable share for FY 2019/20 is Kshs. 310 billion. The justification for the downward adjustment of county governments equitable share for FY 2018/19 by Ksh 9.04 billion is informed by shortfalls in national government's revenue raised. The additional conditional allocation from the national government share of revenue amounting to Ksh. 25.5 billion
- 64) Revenue Collection Projection by the Kenya Revenue Authority (KRA) is expected to increase by Ksh. 140 billion though there has been poor performance in collection of corporation tax but had sought technical assistance from the International Monetary Fund (IMF) on ways of improving collection. The Government will strengthen tax administration and compliance through:

- a) Enhanced scanning to detect concealment and increase efficiency in cargo clearing through procurement of additional scanners and full integration of all scanners;
- b) Use of Regional Electronic Cargo Tracking System to ensure all goods reach the desired destinations and avoid dumping;
- c) Use of third-party information to identify non-compliant property developers and ensure they are included in the tax base; and
- d) Detection of non-compliance through i-Tax data matching

65) **Expenditure Projections and Fiscal Deficit:** Overall expenditure and net lending for FY 2019/20 are projected at Ksh 2,704.7 billion (23.8 percent of GDP). These expenditures comprise among others, recurrent of Ksh 1,657.3 billion (14.6 percent of GDP) and development of Ksh 670.9 billion (5.9 percent of GDP). Reflecting on the projected expenditures and revenues, including grants, the fiscal deficit is projected at Ksh 578.3 billion (5.1 percent of GDP) in the FY 2019/20 down from Ksh 635.5 billion (6.3 percent of GDP) in FY 2018/19. The deficit excluding SGR related expenditures in the FY 2019/20 is projected at 4.6 percent of GDP. The fiscal deficit in the FY 2019/20; will be financed by net external financing of Ksh 306.5 billion (2.7 percent of GDP), Ksh 277.5 billion (2.4 percent of GDP) net domestic borrowing and other net domestic receipts of Ksh 5.7 billion

66) **County government own source revenue:** the National Treasury had sought to assist counties to increase their local revenue collection and had commissioned the World Bank (WB) which had undertaken a study which indicated that counties had a potential to collect Ksh, 100 billion.

67) The justification for arriving at the afore-mentioned county equitable share is as shown in the table below:

	Budget Item	Amount in Kshs. Million
A	County Equitable Revenue Share for FY 2018/19	314,000
	<i>Less</i>	
B	Adjustment based on fiscal framework (Shortfall in Revenue performance in FY 2018/19)	9,038

C	Proposed Revised County Equitable Share for FY 2018/19: C=(A-B)	304,962*
	<i>Add</i>	
D	Adjustment based on fiscal framework	5,038
E	Equitable Revenue Share allocation for FY 2019/20 E=(C+D)	310,000

*This proposed Revised County Equitable FY 2018/19 is subject to approval by Parliament

SENATE STANDING COMMITTEES' VIEW ON THE 2019/2020 BPS

Committee on Agriculture	Observation	Recommendation
	<p>There is lack of clarity in the policy interventions relating to excess importation of maize and sugar, procurement of fertilizer, irrigation, revitalization of cash crops and agriculture research fund among others</p>	<p>The BPS for F/Y 2019/2020 should clearly prioritize and address issues relating to the supply of affordable fertilizer, excess importation of sugar and maize and governance issues that have affected production of staple foods.</p>
	<p>Although the overall budget allocation to the Agricultural sector has increased, Kshs. 7.2 billion is conditional grants to counties under World Bank funded programme called National Agricultural and Rural Inclusive Growth Project(NARIGP) which has specific target areas which may not necessarily be in the main areas of focus in the sector.</p>	<p>County governments should receive conditional funds to support the Big Four Agenda particularly in the area of food security and nutrition</p>
	<p>Supplementary budgets have had a negative effect on the implementation of development projects and this contributes to increased pending bills and distortion of budget implementation and reporting.</p>	<p>The government should endeavour to institutionalize proper budgeting and minimize supplementary budgets.</p>
		<p>The Agriculture research fund should receive additional funding because it plays a key role in supporting key areas of production in the Agricultural sector (general recommendation).</p>
	<p>The Mombasa – Nairobi Express Way was to be initiated in FY 2018/19 as was indicated in 2018</p>	<p>No specific recommendation given</p>

Committee on Roads and Transportation	BPS, However, the BPS 2019 indicates that the project started but no indication of the status of implementation is given.	
	The 2018 BPS listed the number of airstrips that were to be constructed and expanded. However, the 2019 BPS does not provide list of airstrips.	The Committee had raised issue with the distribution of the airstrips and subsequently recommended proper distribution of the airstrips across the country giving priority to far flung areas with poor road networks.
	Delivery of the second ferry (MV Safari) is yet to be achieved partly due to a court injunction by a consultant whose contract was terminated.	No specific recommendation given
	The BPS 2019 notes the establishment of the National Housing Development Fund. It is further noted that the Housing Act establishes a national fund. It is unclear as to whether these funds are different or reference is being made to the same fund	
	The BPS 2019, indicates that the government will provide land to investors who will be required to build 20,000 low cost housing units for 100,000 units they construct under a scheme called "Mixed Used Development" scheme.	There is need for clarification on the modalities surrounding the scheme.
	There are 87 stalled projects under the State Departments of Transport, Public Works, and Housing and Urban Development. Some of these projects were near completion before they stalled	There is need for prioritizing to ensure their timely completion

	<p>Based on the analysis of resource requirement versus the ceilings provided, resources are usually limited relative to spending needs.</p>	<p>It is therefore prudent for all state Departments to prioritize their programmes and activities, implement efficiency and productivity measures in order to use the limited resources to achieve the performance targets including supporting four agenda (general observation).</p>
<p>Committee on Health</p>	<p>The proposed FY 2019/20 allocation to the Ministry of Health is Kshs 93 Billion (5.1 percent of the total sectoral allocations). This represents a 3.4 percent increase from the FY 2018/19 allocation of Kshs 90 Billion. Through this allocation, the Ministry and its various Agencies will be implementing five programmes. The allocation is expected to increase to Kshs 99.1 Billion in FY 2021/22. Thus, over the next medium term, the Ministry is expected get an allocation totaling Kshs 288.2 billion.</p>	<p>The Committee is greatly concerned by the amount of resources held by the Ministry of Health, while health is a devolved function.</p> <p>The Committee recommends that any function or programme that does not fall under the National Government be given to the Counties</p>

	<p>The BPS 2019 shows continued support for universal health coverage (UHC), which is one of the big four agenda for the government. The UHC policy aims at ensuring that the entire country has access to affordable and quality health care services by 2022.</p> <p>The government has adopted a phased approach towards implementation of UHC. The pilot phase began in FY 2018/19 and focused on 4 counties and is currently being implemented. According to the BPS, it is envisaged that the next phase which is a full rollout of UHC in the remaining 43 counties will begin in November 2019, in the second quarter of the FY 2019/2020.</p> <p>However, there are still some priorities outlined in BPS 2018 which are yet to take shape such as establishment of referral hospitals</p> <p>An assessment of the health sector priorities outlined in the BPS 2019 indicates that broadly, the priorities enumerated are in line with the key national policy documents such as the Vision 2030 and the MTP III 2018-2022 as well as the Health sector priorities.</p> <p>The total proposed 2019/20 budget for the Health sector amounts to Kshs 93 billion out of which Kshs</p>	<p>The adopted UHC pilot financing model is not unique since a similar model was tried during the initial phases of free maternity programme (Linda Mama Programme) and did not deliver the desired results which necessitated the shift of financing to NHIF based reimbursement model.</p> <p>Additionally the Committee was concerned that Counties will be required to match National Government contribution. The Committee is of the opinion that this process is not sustainable and will create an undue burden to the Counties.</p> <p>As the Health sector is not adequately supported in terms of resource allocation to implement universal health care, the</p>
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	<p>56.3 Billion is for recurrent expenditure while Kshs 36.6 billion is for development expenditure.</p> <p>There is a significant resource gap in the sector as a result of the proposed ceiling in 2019/20 and over the medium term considering the government intention to actualize the UHC by 2022 as one of its big four plan</p> <p>The proposed budget ceiling for Health sector for 2019/20 is less compared to the resource requirement for the sector which stood at Kshs 218.4 Billion. Given the resource requirement of Kshs 218.4 Billion, the sector has been allocated 43 percent of the resource required</p>	<p>sector has to prioritize its programmes given the limited resources available.</p> <p>Further, the Ministry needs to adjust its targets for various performance indicators.</p> <p>As the Ministry of Health intends on implementing five key programmes to deliver on the UHC agenda the Ministry needs to revise the various targets set and also prioritize the various programmes to ensure that the critical deliverables are met in light of the resource gap,</p>
<p>The UHC pilot phase targets 4 counties in the FY 2018/2019 and subsequently being rolled out to cover 47 counties in the FY 2019/2020 and medium term. These targets are ambitious and ambiguous.</p>		<p>The Ministry is over ambitious by targeting to roll out the UHC in all 47 counties by July 2019 since it requires significant resources which have not been adequately provided for in the BPS 2019. Further, there is ambiguity in targeting 100 percent county coverage and not the actual number of population accessing specific health care services free. Free/affordable healthcare for all Kenyans by July 2019 is not achievable. The Committee is of the opinion that this process should be thought through since the funding for UHC</p>

	<p>In the budget allocation for FY 2029/2020 the Linda Mama Programme is classified as development budget whereas the spending under this program is recurrent in nature.</p> <p>The expansion of the Linda Mama program is identified as one of the key areas of spending in the FY 2019/20 and over the medium term. The FY 2019/20 allocation to the Linda Mama program is KShs. 4.3 Billion. Financing under the Linda Mama program is based on an NHIF reimbursement model rather than on direct funding to counties through conditional grants.</p> <p>Counties have experienced various challenges in relation to the NHIF reimbursement model including, <i>inter alia</i>, lack of effective engagement and consultation prior to redesigning the program, barriers to registration of mothers in remote and marginalized areas, low capitation rates leading to non-commensurate compensation for services rendered, marginalization of counties with a low density of registered public health facilities, disproportionate benefits private health facilities</p>	<p>in all 47 Counties is based on revenue that the Government does not have.</p> <p>The Committee recommended that this be corrected and properly classified as recurrent expenditure.</p> <p>The Committee therefore recommends that the Office of the Auditor General undertake a performance audit on the Linda Mama programme from inception to date and that a report on the same be availed to Senate within a specified period of time.</p>
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	<p>Equipping 6,200 health facilities - The government envisages to equip 6,200 health facilities with basic clinical equipment.</p>	<p>The Ministry should provide clear guidelines on-</p> <p>(a) what constitutes basic clinical equipment and what modalities will be used to equip these health facilities considering that most of them are under the purview of the county governments;</p> <p>(b) whether this is a new programme or an expanded MES programme; and</p> <p>(c) names of facilities covered per county.</p>
	<p>Increasing the number of health referral facilities is identified as one of the key areas of spending in the FY 2019/20 and over the medium term. The BPS does not indicate how the health referral facilities shall be identified and what criteria shall be used.</p>	<p>The Committee therefore recommends that the funds set aside for this programme should be given to the Counties as equitable share.</p> <p>The Ministry should provide an implementation plan indicating how the location of the hospitals will be selected and what criteria will be applied. In addition, the plan should clearly state whether the referral hospitals will be established by upgrading existing facilities or building new ones.</p>
	<p>Providing Community Health Volunteers with basic kits is identified as one of the key areas of spending in the FY 2019/20 and over the medium term.</p>	<p>The Ministry needs to clarify what modalities will be used to equip Community Health Volunteers (CHVs) with basic kits considering that health is a devolved function, and that equipping CHVs falls under the purview of the respective county governments.</p>

<p>The Ministry needs to clarify what modalities will be used to expand access to essential medicines and supplies considering that health is a devolved function, and that provision of essential medicines and supplies falls under the purview of the respective county governments.</p>	<p>Expanding access to essential medicines and supplies is identified as one of the key areas of spending in the FY 2019/20 and over the medium term.</p>	
<p>Considering UHC will entail delivery of free services at all county referral hospitals including Level 5 hospitals, there is need to review conditional grants to Level 5 facilities.</p> <p>In light of the new and increasing pressures and demands that will fall on county referral hospitals as a result of UHC, there is an urgent need to review and establish legal safeguards for conditional grants to Level 5 hospitals.</p>	<p>The Ministry has proposed a total allocation of KShs. 4.3 Billion as conditional grants to Level 5 Hospitals. This is in comparison to KShs. 4,325,000,000.00 in the FY 2018/19.</p>	
<p>The Cabinet Secretary for Health should finalize the Semi-autonomous Government Agencies (SAGA) constitutive instruments and financial autonomy for Kenyatta University Teaching, Research and Referral Hospital; Mwai Kibaki Teaching and Referral Hospital (formerly Othaya Level 6 Hospital); the National Spinal Injury Hospital and Mathari Mental Hospital to make these facilities under the direct purview and oversight of the Committee.</p>	<p>There exist other national health referrals which are either operating as departments of the Ministry or departments of learning institutions. Such arrangements greatly hamper services delivery in these national health referral institutions.</p>	

<p>The recent Presidential Order placed the Kenyatta University Hospital Teaching and Referral Hospital under the Ministry of Health as a State Corporation.</p>	<p>The Ministry should provide a clarification on whether budgetary allocation has been provided for its operation in the FY 2019/2020.</p>
<p>To drive the UHC goal, the government intends to modernize NHIF systems and improve governance structure through legal and institutional reforms. However, no timelines have been set for these reforms.</p>	<p>The Ministry should provide to the Committee a roadmap for modernization of NHIF to deliver on UHC particularly policy, legislative, & governance reforms. This should be done before any funds are spent</p>
<p>The BPS 2019 indicates that only 5 hospitals have benefitted out of the 37 hospitals targeted to receive CT scans. The allocation for this project which is donor supported was provided in the current financial year.</p>	<p>The Ministry should provide a status report on this project to the Committee which should include the facilities the CT Scans have been delivered to, the procurement process used and cost of the CT Scan</p>
<p>The Managed Equipment Services (MES) project has been allocated a conditional grant of Kshs 6.2 Billion in 2019/20 compared to Kshs 9.4 Billion in 2018/19. The decrease is attributed to advanced implementation status of equipping most of the identified health facilities as well as settlement of previous financial year's arrears.</p>	<p>The Ministry breakdown of the Kshs 6.2 billion allocation need to be provided to the Committee.</p> <p>The Committee recommends that the Auditor-General undertake a performance audit on the MES programme from inception to date. Lessons learnt can be used to inform new programmes or improve the programme.</p>

<p>Additionally, resources set aside for Medical Equipment's Services should be given to Counties through the equitable share.</p>	
<p>There is need to harmonize all these programmes into the UHC programme to avoid duplicity, reduce wastages, and improve on efficiency if the conditional grants to counties.</p> <p>sFurther, the Committee recommends that the Auditor-General undertake programme performance audits of all these programmes to determine their efficacy and efficiency so as to inform the full roll out of UHC.</p>	<p>The national government has channeled significant amount of financial resources to the county governments as conditional grants for roll out of various programmes and projects in the health sector. These programmes were the foundational blocks towards the UHC agenda.</p>
<p>No recommendation given.</p>	<p>The Committee observes that the proposed financing model for UHC is fundamentally flawed in the sense that costing of devolved functions and the appropriate transfer of resources is not factored into the equitable share received by counties. As such, there is a strong possibility that despite the conditional grants that counties will receive under the UHC program, county governments will struggle to implement the program owing to significant resource constraints.</p>
<p>There is need for the Ministry to explore home-grown financing mechanisms for critical projects in the Ministry. The</p>	<p>The health sector capital expenditure is highly dependent on donor financing. In FY 2016/17, the total capital expenditure estimates of Ksh. 31.179 billion was donor financed to the tune of Ksh. 19.77</p>

	<p>billion, representing a donor financing level of approximately 63 percent. In the FY 2018/19 estimates, out of KShs. 40.9 Billion allocation, KShs. 12.7 Billion (31%) was obtained from AIA which is majorly funded by development partners.</p> <p>In view of the expected increased demands for health services that will be occasioned by the implementation of UHC, the government intends to increase the number of health workers from 9:10,000 to 14:10,000 at an estimated cost of KShs. 2.1 Billion. It's not clear from the BPS what proportion of this burden will be borne by National government <i>vis a vis</i> county governments.</p>	<p>funding should be consistent with Kenya's priorities and within broader objectives of universal coverage.</p>
	<p>Funding of additional allowances negotiated under the Collective Bargaining Agreements with doctors, nurses and clinical officers.</p> <p>The combined additional cost of these negotiated allowances to county governments amounts to KShs. 11,806,032,000.00. The BPS, as in the previous year, makes no provision for the allocation of this money yet current industrial action by nurses and clinical officers are related to the failure to implement the respective CBAs.</p>	

Committee on Trade, Industrialization and Tourism	<p>It has been reported that there are a total of 545 stalled projects whose total estimated cost is KSh. 365.9 billion (KSh. 286.9 GoK and KSh. 78.9 billion foreign financing). The Ministry has documented 4 stalled projects, 3 under the state department for industrialization and one under cooperatives.</p>	<p>Cognizant of the fact that delays in completion of projects typically leads to delayed returns on investment the Committee recommends that-</p> <p>(a) a decision be made on the fate of the 545 projects and other projects that may be at the same risk;</p> <p>(b) the possibility of remodeling county governments to be the real economic development centres as opposed to replicating the national government by for instance, an amendment to section 15 of the Public Finance Management Act, 2012 in a bid to stipulate a different percentage of allocation towards capital expenditure</p>
	<p>According to the sector report of 2018, the State Departments for trade, industrialization and tourism have pending Bills of various amounts. If pending bills are not factored into the proposed ceilings, funds may be reallocated to finance the bills and as a consequence impairing the achievement of some programs.</p>	
	<p>A review of the past three financial years indicate a low and declining trajectory in absorption rate of the capital vote of the State Department of Industry and Investment. Low absorption adversely affects the achievement of planned targets such as job creation, enhancing the industrial contribution to GDP and</p>	

	<p>could lead to the reallocations or even budget cuts through supplementary budgets.</p> <p>The government continues to support the manufacturing sub-sector through programmes geared towards improving the manufacturing capacity by expanding access to credit facilities and putting measures in place to reduce the high cost of production.</p> <p>Parastatals under the State Department of Tourism and Cooperatives are many and on duplicating roles;</p>	<p>There is also need to heighten and sustain the fight against illicit trade and contrabands as these lead to unfair competition that may lead to collapse of the established genuine business enterprises.</p>
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III. COMMITTEE OBSERVATIONS AND RECOMMENDATIONS

Observations

The Committee observed the following -

1. The 2018 and 2019 BPS contain similar priorities. However, the 2019 Budget Policy Statement does not provide information on the progress of achievement of the priorities of 2018. The policy document lacks a clear implementation matrix especially with regards to the implementation of the Big Four.
2. The 2019 BPS outlines the Big Four plan as government's key agenda to be implemented in the medium term and it is expected that counties have a substantial role to play in actualizing the agenda. However, it is not clear from the proposed allocation and policies on what role counties should undertake. This is likely to pose risks of duplication and overlaps, with a possible risk of loss of resources and have an adverse effect on costing of functions.
3. Although the National Treasury has indicated commitment towards fiscal consolidation efforts, the challenge will be in maintaining a contractionary fiscal path that entails reduction in government spending given the prevailing expenditure pressures amid a shrinking revenue performance.
4. The ordinary revenue projections of Ksh. 1.87 Trillion for FY 2019/20 are anchored on the same reforms in tax policy and revenue administration as had been set out in the BPS 2018. However, the approved ordinary revenue targets for FY 2018/19 were reduced from Ksh. 1.74 Trillion to Ksh. 1.65 Trillion which led to spending cuts in the supplementary budget. There is over projection in revenues that undermine the set targets rendering the targets unachievable. There is need to set realistic projections to avoid creating fiscal instability and delays in programme implementation
5. The proposed reduction in equitable share of revenue for FY 2018/2019 with a lower base from Ksh. 314 Billion to Ksh. 305 Billion will impact negatively on the amount of county fiscal transfers. This contravenes section 5(1) of the DORA 2018. In addition, the proposed

Kshs. 310.00 billion equitable share to counties for FY 2019/2020 is an unjustified reduction as compared to the Kshs.314.00 Billion allocated in FY 2018/19.

6. The proposal by the Commission on Revenue Allocation through its recommendations to Parliament sets the county equitable share at Kshs 335.70 billion. The recommendation by CRA is based on adjusting the current base to compensate for inflation using an actual three-year average of annual inflation factor of 6.9%. This means that, on a minimum, the proposed amount is to finance the current operational and development expenditure levels and needs across the counties.
7. The National Treasury's proposal on county equitable share is Kshs 310.00 billion which is based on an enhancement from a 'revised fiscal framework that indicates a reduced base of Kshs 304.96 billion. According to the National Treasury, the revised base is because of revenue shortfalls in the current FY 2018/19. However, it does not indicate the basis of arriving at Kshs. 310 Billion.
8. There is an unexplained increase in guaranteed debt as at the end of December 2018 to a total of Kshs. 147.7 billion from Kshs. 133.79 billion in December 2017. There is no evidence that the increase in debt guarantees were subject to parliamentary approval pursuant to Section 58 of the PFM Act, for instance loan guarantee to Kenya Airways.
9. Although the 2019/2020 BPS has given greater focus to food security and nutrition, there is lack of clarity in the policy interventions relating to excess importation of maize and sugar, procurement of fertilizer, irrigation, revitalization of cash crops and Agriculture Research Fund linked with achievement of BIG 4
10. It is observed in the BPS that there is an increase in pending Bills both at the national and county level of government mainly attributed to delayed payments to creditors and suppliers, reallocation of funds during supplementary budgets and other irregular procurement processes outside the approved budget.
11. The consistent over-estimation of revenue has often resulted in missed revenue collection targets that trigger in-year supplementary budgets which have a negative effect on the

- implementation of the budget mainly affecting development projects, at both levels of government.
12. The BPS 2019 indicates that the government has established the National Housing Development Fund. There is a lack of clarity and consistency in the legal instruments enabling the implementation of affordable housing project as set out in the Big Four Agenda. The Housing Act makes reference to a Housing Fund while the Employment Act makes reference to a National Housing Development Fund.
 13. There are a total of 545 stalled projects spread across all sectors with a total estimated cost of KSh. 365.9 billion of which Ksh. 286.9 billion is GoK funded while KSh. 78.9 billion is foreign financed. Some of these projects have been stalled for the last ten years. The Committee notes with concern that delay in completion of projects leads to delayed returns on investment and may result in escalation of project costs and affect debt servicing
 14. There is insufficient information on the manner in which Universal Health Coverage will be achieved including agreements between the county and national governments on the 6200 public health facilities proposed to be equipped with basic clinical equipment. It is also unclear whether this is linked to the MES project.
 15. There is insufficient information on the implementation of the Ajira programme including the project costs, details of the beneficiaries and the specific counties in which the programme has been rolled out.
 16. The criteria for determining 'national interest' is not fully determined. There is an ongoing engagement among the different parties to have the matter resolved spearheaded by the Inter-governmental relations technical committee on the question of the determination of the scope and meaning of "national interest".
 17. The expansion of the Linda Mama program is identified as one of the key areas of spending in the FY 2019/20 and over the medium term. The FY 2019/20 allocation to the Linda Mama program is KSHs. 4.3 Billion. Financing under the Linda Mama program is based on an NHIF reimbursement model rather than on direct funding to counties through conditional grants.

18. With regard to conditional Grants to Level 5 Hospitals, the UHC will entail delivery of free services at all county referral hospitals including Level 5 hospitals, there is no framework for the manner in which level 5 hospitals are identified.
19. There is an increase on the allocations to the Ministry of Health from Kshs. 90 billion in FY 2018/2019 to Kshs. 93 billion (5.1 per cent of the total sector allocations) in FY 2019/2020. This represents a 3.4 per cent increase that targets five programmes in the Health sector. The allocation is expected to increase to in 2020/21 to Kshs 99.1 Billion in FY 2021/2022. Thus, over the next medium term, the Ministry is expected get an allocation totaling Kshs 288.2 billion. There is concern over the huge budget allocation to the Ministry of Health whereas health is a fully devolved function.
20. The Managed Equipment Services (MES) project has been allocated a conditional grant of Kshs 6.2 Billion in 2019/20 compared to Kshs 9.4 Billion in 2018/19. The decrease is allegedly attributed to advanced implementation status of equipping most of the identified health facilities as well as settlement of previous financial year's arrears. However, the allocations to this project have been fluctuating. This is inconsistent with the original agreement and this is a source of concern, making it difficult to ascertain the actual total cost of the project.
21. To achieve UHC there was need for recruitment of additional health workers with view of improving the health workers to patient ratio to 14:10,000. This represents an estimated additional 21,300 health workers. At an average cost of Kshs. 100,000 per health worker, this translates to an estimated cost of Kshs. 2.1 Billion which is not provided in the proposed Budget. Being a national government project, the national government should provide funding for this project.
22. The health sector capital expenditure is highly dependent on donor financing. In the FY 2016/17, the total capital expenditure estimates of Ksh. 31.179 billion was donor financed to the tune of Ksh. 19.77 billion, representing a donor financing level of approximately 63 percent. In the FY 2018/19 estimates, out of a Kshs. 40.9 Billion allocation, Kshs. 12.7 Billion (31%) was obtained from AIA which is majorly funded by development partners. The key projects that are largely under the ambit of donors include: reproductive health commodities; universal health coverage; procurements of vaccines; HIV/AIDS, TB and Malaria among others.

23. The current PFM regulations places a maximum threshold of public debt as a share of GDP in Net Present Value Terms at 50 percent. This has been breached by 9.9% for 2019 and is set to remain above the threshold in the medium term. Other indicators that the country has breached in 2018 include the ratio of PV of debt service to revenue and the PV of Debt to revenue ratio at 43.7 and 300 respectively compared to a threshold of 30 and 300. This indicates liquidity shocks from debt service which is a first charge on the revenue collected. The debt service as a share of ordinary revenue has increased from 24 percent in FY 2016/17 to 34 percent in FY 2017/18 and further to 39 percent in FY 2018/19.
24. Similar to the 2017, 2018 Medium Term Debt Strategy (MTDS), the 2019 MTDS overlooks the importance of listing the projects (both on-going and earmarked) by sector to be implemented using debt in the medium term. Further, the MTDS should have included a detailed current debt servicing information on related projects and the status of their implementation.
25. The borrowing strategy for FY 2019/20 is unclear in terms of the External debt to Domestic debt policy. The 2019 BPS projects that the country will borrow less domestically with a debt policy mix of 47: 53 percent. However, the Medium-term debt strategy (MTDS) indicates that the country will borrow more domestically with a policy mix of 62:38 percent.

Recommendations

A. Policy Recommendations

- 1) The National Treasury should redesign the tax regime to reduce the number of exemptions under the Income Tax Act and the VAT Act. Further, a tax gap analysis should be carried out -to identify tax gaps at the National Government level.
- 2) The National Treasury should submit the national policy on supporting enhancement of county governments' Own Source Revenue to Parliament by 15th March, 2019 so as to guide the revenue administration strategies for FY 2019/20 for the county governments.
- 3) In pursuit of the fiscal consolidation, the fiscal deficit (including grants) of 5.1 percent of GDP should be binding and any increase in spending should be matched with additional revenue collection.
- 4) The National Treasury should come up with concrete measures to reduce the current Debt to GDP ratio in Net Present Value terms to the 50 percent threshold provided for in the PFM Regulations. Further a progress report on the extent to which debt levels have been reduced be submitted to the Senate after six months. This is pursuant to Section 34 of the PFM Act which provides that the National Treasury should provide additional reports when required by Parliament.
- 5) The National Treasury should fast-track adoption of accrual based fiscal reporting by all government entities which provide a more comprehensive view of the governments financial performance and the cost of government activities to avoid pending bills.
- 6) The Anti-counterfeit Agency and the Kenya Bureau of Standards need to enhance and sustain the fight against illicit trade and contrabands as this leads to unfair competition that may lead to collapse of the established genuine business enterprises. The ministry of Trade should critically examine the impact of counterfeits on the economy.

- 7) Parliament should expedite amendment of section 25(7) of the PFM Act 2012 to extend the timelines for the consideration of the Budget Policy Statement by Parliament from 14 days to 28 days. This proposal should extend to the timelines for the consideration of the County Fiscal Strategy Paper by County Assemblies.
- 8) The Ministry of Agriculture must prioritize and address issues relating to the supply of affordable fertilizer, excess importation of sugar and maize and governance issues that have adversely affected production of staple foods. In addition, the Agriculture Research Fund should receive additional funding because it plays a key role in supporting key areas of production in the Agricultural sector.
- 9) The two levels of government should operationalize the framework through which the Big Four Agenda will be achieved as some of the priority areas under the agenda are functions of county governments. Adequate funds should also be provided for these areas.
- 10) The National Treasury should make realistic projections of revenue so as to reduce supplementary budgets which distort budget implementation.
- 11) The national government should pursue the PPP financing model specifically for development projects that qualify for such funding under infrastructure for instance the Mombasa- Nairobi Express project.
- 12) The Senate in consultation with COG and the National Government should develop a framework for determining national referral hospitals and the level five hospitals. There is an urgent need to review and establish legal safeguards for conditional grants to Level 5 hospitals in consultations with the Ministry of Health.
- 13) The Senate with consultation with COG and National Government should undertake to determine the meaning and scope of the term "national interest". To achieve a more effective equitable sharing of revenue between the two levels of government.

- 14) The Office of the Auditor-General should undertake a performance audit on all health initiatives, including the Managed Equipment Service (MES) project and a report on the same be submitted to Senate.
- 15) The Universal Health Coverage should be funded through conditional allocations to county governments, specifically in financing the 6200 public health facilities proposed to be equipped with basic clinical equipment.
- 16) County governments should adhere to strict rules of accountability and prudent management of resources.
- 17) The National treasury should consider exempting the mortgage holders and home owners from making the 1.5 percent contribution on basic pay to the National Housing Development Fund.
- 18) The Senate should be involved in the approval of debt guarantees pursuant to Article 213 and Section 58 of the PFM Act that requires that loan guarantees be approved by Parliament.
- 19) The National Treasury and CRA should expeditiously develop a policy on conditional grants and submit the same to Parliament by 30th May, 2019.
- 20) The conditional grant on Leasing of Medical Equipment should be removed from the Division of Revenue and payment discontinued until such a time when the implementing agency will provide adequate information on the costing of the project.

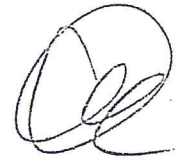
B. Financial Recommendations

The Committee recommends the following financial recommendations: -

- a) That the allocation of revenue to County Governments for FY 2019/20 that is proposed in the 2019 BPS and the draft Division of Revenue Bill 2019, be as follows –
 - (i) Total County Allocation be Ksh. 391.07 Billion of which
 - County Equitable share be Ksh. 335.67 Billion
 - ✓ That the equitable share for FY 2018/19 of Ksh. 314 Billion is adjusted by a three-year average inflation rate of 6.9 percent which is Ksh. 21.67 Billion. This is similar to the proposals by the Commission on Revenue Allocation and the Council of Governors.
 - County Conditional Grants be Ksh. 55.40 Billion which comprises of the following-
 - ✓ Compensation for user fees foregone- Ksh. 0.90 Billion
 - ✓ Level 5 Hospitals- Ksh. 4.326 Billion
 - ✓ Rehabilitation of Youth Polytechnics- Ksh. 2.00 Billion
 - ✓ Supplement for Construction of County HQs- Ksh. 0.485 Billion
 - ✓ Allocation from the Road Maintenance Fuel Levy Fund (15 percent)-Ksh. 8.984 Billion
 - ✓ Allocation from Development Partners as Loans and Grants-Ksh. 38.70 Billion
- b) That the fiscal deficit (on commitment basis including grants) be binding at 5.1 percent of GDP in FY 2019/20.
- c) That the budget ceiling for the Executive for FY 2019/20 be reduced by Ksh. 19.47 Billion. This amount is equivalent to an additional Ksh. 25.67 Billion to the County Equitable Share for FY 2019/20 from Ksh. 310 Billion as proposed in the 2019 BPS to Ksh. 335.67 Billion; and a reduction of Ksh. 6.2 Billion for the conditional allocation for leasing of medical equipment.

APPENDIXES

1. Minutes of the Committee
2. Submission from stakeholders



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20th February 2019

J. M. Nyegenye, CBS
Clerk of the Senate
P.O. Box 41842-00100
Parliament Buildings
Nairobi

**VERY
URGENT**

MEDIUM TERM BUDGET POLICY STATEMENT FOR THE FINANCIAL YEAR 2019/20

Reference is made to your letter referenced SEN/DCS/SCF&B/2019/003 dated 15th February 2019 on the above mentioned subject. The Council of Governors appreciates the work that the Senate does with respect to Article 96 of the Constitution with regards to ensuring that County Governments are adequately resourced.

The Council wants to reiterate that indeed we have looked at the policy statement when it was initially published by the National Treasury and in the spirit of consultation and cooperation between the two levels of governments as emphasized in Article 189 of the Constitution the Council hereby confirms that; Under the Intergovernmental Budget and Economic Council meeting chaired by the Deputy President on 29th January 2019, we did reiterate the need for equity in resource allocation between the two levels of governments.

In our presentation to IBEC and now to the Senate, the Council maintains the following:

1. Rejection of the National Treasury's proposal to have counties equitable share for 2018/19 reduced from the current Ksh.314 billion to Ksh.304 billion.
2. The revenue base for adjustment for county governments for the 2019/20 financial year should therefore be Ksh.314 billion and not Ksh.304 billion.
3. The Counties equitable share of revenues for 2019/20 FY should therefore be Ksh.343.7 billion comprising of adjustment base of Ksh.314 billion with Ksh.8.7 billion worth of unfunded functions and 6.9% average three year average annual inflation.

The reasons for these proposals are:-

1. The current equitable revenues to the Counties is Ksh.314 billion as approved by Parliament and not Ksh.304 billion as proposed by the National Treasury in the Budget Policy Statement 2019.
2. Additionally according to the Division of Revenue Act 2018, Section 5 stipulates that *“if actual revenue raised nationally in any year falls short of projections, the shortfall is to be borne by the National Government, to the extent of the threshold prescribed in Regulations by the Cabinet Secretary.”* This provision therefore exonerates counties from bearing the burden of revenue shortfalls hence counties revenues should not be reduced.
3. There are unfunded functions; The County Governments should be allocated funds on the unfunded transferred functions. Counties were transferred additional 31,000km of roads as well as Library services amounting to Ksh8.7 billion. The allocation has been pending awaiting Summit’s approval of the Inter-agency report recommending the same.
4. To achieve stability and predictability in implementation of county budgets, there is need to use an average inflation rate to cater for increase in service costs. In this case a three year average inflation rate should be used. This will ensure that the functions of both the national and county government are not subjected to volatile budgets.
5. The Council therefore recommends for the use of an average inflation rate to cater for increase in service costs.
6. Currently 9 counties are earmarked to lose an accumulative amount of Ksh.7.3 billion worth of allocation when the 3rd generation revenue sharing formula is applied against the CRA equitable share proposal of Ksh.335.7 billion. If the National Treasury’s proposed allocation of Ksh.310 billion is adopted, counties would have lost Ksh.25 billion before the formula is even applied.

To this end the Council would like to forward to your office our proposals for the Senate’s intervention. Comprehensive memorandum is hereby attached for your reference.

Due to the short notice on the invitation as the letter was received on the evening of 19th February 2019, the Council requests for the rescheduling of its presentation to Monday 25th February 2019 at 2.00 p.m. at your Chambers. The Governors in the Finance Committee shall be present to make the presentation.



Jacqueline Mogeni, MBS
Chief Executive Officer

Copy: All Excellency Governors

All CECs in Charge of Finance



COUNCIL OF GOVERNORS

CoG Recommendations on the 2019 BPS & the proposed vertical sharing of revenues 2019/20

20th February 2019

“Devolution is dying on the vertical sharing of revenues”

2019/2020 vertical share of revenues. Fig 1.

County Governments Equitable Revenue Share 2019/20 FY (Ksh Million)			
Budget item	NT	CRA	CoG
Baseline (i.e allocation in the previous year)	304.00	314.00	314.00
1. Baseline adjustments (Due to additional functions)			
Salaries for Devolved Library staff (33 counties benefiting)	0	0	0.3
Transferred 31,000Km of roads to Counties'	0	0	8.4
Adjusted baseline:	304	314	322.7
1. Adjustment for Revenue Growth. Using 3-year average annual inflation of 6.9% per cent	5.3	21.7	21.7
Computed equitable revenue share allocation	310	335.7	343.7
Percentage allocation against sharing revenue of 1,870.4 trillion	16.50%	17.90%	18.30%

*Both CRA & CoG have used the approved revenue base of Ksh 314 billion as provided for in the 2018 Division of Revenue Act while the National Treasury's base has been reviewed downwards as per the Budget Policy Statement 2019 which intends to revise counties' equitable share from Ksh 314 to Ksh 304 billion in the 2018/19 FY.

The Council of Governors is proposing for an equitable share of revenues to counties in the 2019/20 financial year to be Ksh 343.7 billion.

Reasons for the proposal

1. The current revenue base to counties is at Ksh 314 billion as approved by Parliament through the Division of Revenue Act 2018. The total share of ordinary revenues for which the 2018/19 financial year's county allocation was based on was Ksh 1,688,492,000 million.

2. The revenue sharing framework for the 2018/19 financial year was concluded in February 2018 when the equitable share of revenues to county governments was increased from the ksh 302 billion in the 2017/18 FY to ksh 314 billion. The increment was 4% equivalent to ksh 12 billion shillings.
3. This increment of 12 billion to counties was distributed as follows to cater for county services:-
 - i. 4 billion adjustment of salaries for MCAs following the court case on their salaries,
 - ii. 800 million for the County Executive annual expenditure ceilings,
 - iii. 7.2 billion for enhanced service delivery due to the rising cost of service provision.

Any reduction on this will strongly affect the level of service delivery at the county levels. That will mean that county governments will have to reallocate funds from development votes to recurrent expenditure.

NB:

1. When the revenue sharing framework was finalized in February 2018, Counties allocation of Ksh 314 billion was based on a revenue projection of Ksh 1.68 trillion. By the time the National budget was finalized in June, the National Treasury had revised the projections upwards by Ksh 85 billion to Ksh 1.796 trillion.
2. The revised projections of ksh 85 billion was never shared with the County governments as the total allocation was allocated to National level institutions. The Counties allocations remained at ksh 314 billion. The latest revision of the revenue projections coming in September 2018 revised the projections closer to the revenue framework agreed upon in February at ksh 1.67 trillion. The down ward revision should therefore not affect county governments.
3. The fiscal framework that underpinned the Division of Revenue in February 2018 had not changed, the supplementary budget 2018/19 simply revised the June 2018 budget framework back to the February 2018 framework.
4. The Current legal framework under section 5 of the Division of Revenue Act requires that the National government shall bare the revenue shortfall and in the same manner accrue benefits from over collection.

5. The National Treasury through the BPS has noted that the proposed reductions have also affected commitments on “national Interest” and “other national obligations”. There is need to understand that national obligation include public debt of which the county governments’ have not contributed to. Counties’ are yet to borrow and this should be considered.

Illustration of Counties’ annual increments. Fig 2

	Year	Proposed Growth		Basis for Proposed Revenue Growth		Growth in the Approved Allocations in the Division of Revenue Act	Growth in National Ordinary Revenue
		CRA	National Treasury	CRA	National Treasury		
1	2015/16	10.4%	10.4%	3-Year average growth in ordinary revenue	3-Year average growth in ordinary revenue	14.6%	13%
2	2016/17	15.0%	7.8%	3-Year average growth in ordinary revenue	Not provided	7.9%	15%
3	2017/18	15.0%	6.7%	3-Year average growth in ordinary revenue	3-Year average month on month inflation	7.7%	10%
4	2018/19	8.5%	4.0%	3-Year average inflation	Not provided	4.0%	
	2019/20	10.0%	2.0%				

Key issues

Since the onset of devolution, there has been no agreed revenue growth factor for county governments. The table illustrates that:

1. There has been no uniform approach in developing a growth factor between CRA and National Treasury as the two institutions have increasingly differed in their proposals for the revenue growth save for the 2015/16 financial year when there was an agreed position to use a 3 year average in growth in ordinary revenues.
2. The approved growth rate in all the Division of Revenue Acts have been below the national growth level in ordinary revenues. See table above.

3. For the 2018/19 FY, the approved growth rate was 4.0% from Ksh 302 billion to Ksh 314 billion however Treasury has further proposed through the Budget Policy Statement 2019 to revise the 2018/19 allocation to Ksh 304 billion. This reduction downwards disregards;
 - i. Projected growth in economy. The economy was projected to grow by 5.4% in 2017/18 FY, 6.1 % in the 2018/19 FY and 6.2% in the 2019/20 FY. The trend in the growth of the economy has been on an upward trend save for the 2016/17 and 2017/18 FY due to drought and political activities.
4. The National Treasury has further proposed a 2% revenue increase to county governments' in the 2019/20 FY. This 2% proposal is on the reduced allocation of Ksh 304 billion and not the approved Ksh 314 billion. The Treasury's proposal is therefore earmarked at Ksh 310 billion which is below the current approved allocation to counties of Ksh 314 billion.

Recommendation

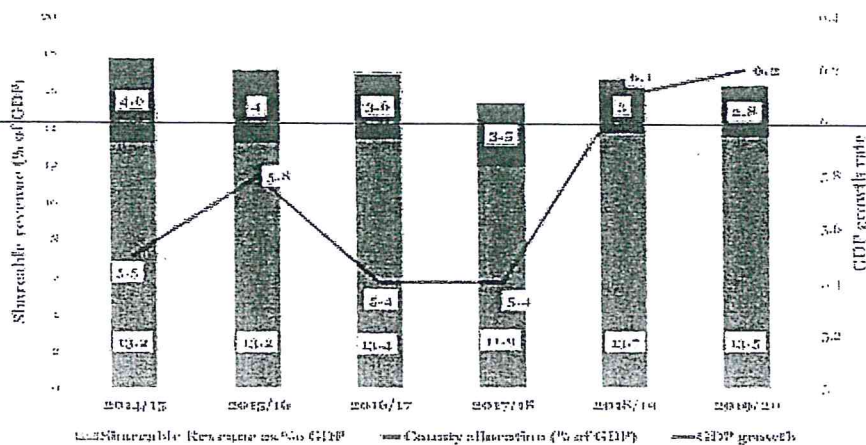
There is no formula or justification as to how the National Treasury arrived at reducing counties' equitable share in the 2018/19 FY from Ksh 314 billion to 304 billion.

There is therefore need for IBEC to agree on a formula moving forward on how to graduate counties' equitable share.

The Council proposes for a formula that will cater for the ever increasing cost of provision of services; that is the inflation cost.

The proposed 2% growth by the National Treasury does not cater for the increased cost of provision of services, and it is also based on a proposed reduction of Ksh 304 billion.

Illustration of Counties' allocation in a growing economy. Fig 3



- While the economy has continued to grow and on the upward trajectory save for 2016/17 & 2017/18 because of political activities, the Counties' allocation as a percentage of the GDP has continued to dip from 4.6% in the 2014/15 FY to 2.8% in the 2019/20 FY.
- There is no explanation to this downward trend for counties in a growing economy.
- Counties should be allocated resources based an agreed criteria that respects the constitution and promotes equity and is predictable.
- For this reason the Council maintains that Counties equitable share cannot be reduced from the current Ksh 314 billion to Ksh 304 billion. A formula must be developed to provide for a framework for revenue growth for counties.
- The Council also proposes for an allocation of Ksh 343.7 billion as equitable allocation to counties in the 2019/20 based on table 1 above.
- Additionally the Council proposes for the adjustment of the conditional grant for the level five hospitals to cover all the certified level five hospitals across all the counties. There are some counties that are not covered.

Illustration on the allocation towards conditional grants. Fig 4

Current Conditional Grants (Billions)	2017/18 DORA	2018/19 CRA Recommendation	2018/19 National Treasury Recommendation	% Increase of CRA Grants to DORA	% Increase of National Treasury Grants to DORA
Level 5 hospitals	4.2	4.5	4.3	7%	3%
Free maternal health care		3.4	-	-	-
Compensation for user fees forgone	0.9	0.9	0.9	0%	0%
Leasing of medical equipment	4.5	4.5	9.4	0%	109%
Road Fuel Levy Fund	11.1	8.6	8.3	-23%	-25%
Development of Youth Polytechnics	2.0	2.0	2.0	0%	0%
Supplement for construction of county headquarters	0.6	0.6	0.6	0%	0%
Sub-Total*	23.3	24.5	25.5	5%	9%
Conditional allocations (loans and grants)	20.4	-	33.2		63%
Total	43.7	24.5	58.7	13%	34%

Key issues

1. There has been over 100% increase in the allocation towards Leasing on medical equipment from ksh 4.5 billion to Ksh 9.4 billion while zero increment in the allocation towards “Compensation for user fees forgone.”
2. The number of health visits for both outpatient and inpatient increased by 1.5 million persons in 2017 as reported by the Statistical abstract 2018. There is therefore need for consideration for an increment based on the increased cost of provision of services.

Effects of reduction of Counties' Equitable share in the 2018/19 financial year.

CODE	Counties	% Allocation based on 2nd Generation formula	Reduction based on Ksh 9 billion
4460	Baringo	1.62	146,464,200.00
4760	Bomet	1.89	170,874,900.00
4910	Bungoma	2.85	257,668,500.00
4960	Busia	1.90	171,779,000.00
4360	Elgeyo/Marakwet	1.20	108,492,000.00
3660	Embu	1.42	128,382,200.00
3310	Garissa	2.21	199,806,100.00
5110	Homa Bay	2.13	192,573,300.00
3510	Isiolo	1.25	113,012,500.00
4660	Kajiado	1.91	172,683,100.00
4810	Kakamega	3.29	297,448,900.00
4710	Kericho	1.82	164,546,200.00
4060	Kiambu	2.98	269,421,800.00
3110	Kilifi	3.45	311,914,500.00
3960	Kirinyaga	1.31	118,437,100.00
5210	Kisii	2.45	221,504,500.00
5060	Kisumu	2.20	198,902,000.00
3710	Kitui	2.78	251,339,800.00
3060	Kwale	2.40	216,984,000.00
4510	Laikipia	1.31	118,437,100.00
3210	Lamu	1.13	102,163,300.00
3760	Machakos	2.65	239,586,500.00
3810	Makueni	2.27	205,230,700.00
3410	Mandera	3.23	292,024,300.00
3460	Marsabit	2.23	201,614,300.00
3560	Meru	2.55	230,545,500.00
5160	Migori	2.14	193,477,400.00
3010	Mombasa	2.62	236,874,200.00
4010	Murang'a	1.99	179,915,900.00
5310	Nairobi City	5.03	454,762,300.00
4560	Nakuru	3.01	272,134,100.00
4410	Nandi	1.71	154,601,100.00
4610	Narok	2.03	183,532,300.00
5260	Nyamira	1.52	137,423,200.00
3860	Nyandarua	1.57	141,943,700.00
3910	Nyeri	1.60	144,656,000.00
4210	Samburu	1.41	127,478,100.00

5010	Siaya	1.92	173,587,200.00
3260	Taita/Taveta	1.29	116,628,900.00
3160	Tana River	1.77	160,025,700.00
3610	Tharaka - Nithi	1.16	104,875,600.00
4260	Trans Nzoia	1.79	161,833,900.00
4110	Turkana	3.43	310,106,300.00
4310	Uasin Gishu	1.89	170,874,900.00
4860	Vihiga	1.42	128,382,200.00
3360	Wajir	2.70	244,107,000.00
4160	West Pokot	1.57	141,943,700.00
	Total	100.00	9,041,000,000.00

MEMORANDUM TO THE SENATE ON THE BUDGET POLICY STATEMENT 2019

1. The Senate and the National Treasury should take advantage of the current review of the equitable revenue sharing mechanism to help counties address challenges from inherited staff costs. The BPS (Para 277) indicates that the challenge on the wage bill in some counties is a direct result of inherited staff and therefore a cost that was beyond their control. The BPS indicates that only 15 counties complied with the requirement that the wage bill shall not exceed 35 percent of their total revenue. It also indicates that the first two equitable revenue sharing formulas did not have a mechanism to help counties handle their wage bills. However, the National Treasury does not give any specific measures to deal with that challenge right now even in light of the current process of revising the revenue sharing formula. The proposals on helping counties work on plans to meet the ceilings seems inadequate in dealing with a present challenge.
2. Public Sector Hearings remain centered in Nairobi and should be centralized and held in different parts of the country. The 2019 BPS has a section that lists conversations and input from the public. Annex 6 and 7 are an important step in providing feedback to the public on its' input and we applaud the National Treasury for this step, and we hope the Senate will follow suit in its' report. However, the process by which the public is consulted remains quite limiting to the public with the forums only being held in Nairobi and with very limited space for deliberation. Treasury addresses this concern in its feedback to the public but not in a satisfactory way as shown in the snippet below. We believe that the Senate should go a step further and ensure that a system is set up in policy that will ensure that public sector hearings are decentralized. This will see a wider part of society is given the chance to participate in decisions that affect them through the budget.

General comments/ Clarifications/ Corrections.	<ul style="list-style-type: none"> • Correction of grammatical and editorial errors in the document. • Consistency check on the use of the words 'financing' and 'borrowing'. • Repetition of Paragraphs 55 and 56 on the PIM Unit 	<ul style="list-style-type: none"> • All highlighted errors in the BPS were noted and appropriately corrected. • The repeated text has been deleted.
	<ul style="list-style-type: none"> • Consider holding Public Sector Hearings across Counties for adequate representation and participation rather than holding the forums at Nairobi where majority of Kenyans are unable to participate. 	<ul style="list-style-type: none"> • The suggestion is well noted.

3. Justifications for why certain decisions were taken and not others are critical for accountability. Currently, it is hard to tell if the decisions have influenced budget allocations in any way. In addition, paragraph 223 seems to indicate that inputs from

stakeholders will only be taken up once additional resources are available as shown below. The consideration of public input should not just be on what new things can be done but also on proposals from that the government has in the BPS.

Finalization of Spending Plans

223. The finalization of the detailed budgets will entail thorough scrutiny to curtail spending on non-productive areas and ensure resources are directed to priority programmes. Since detailed budgets are scrutinized and the resource envelope firmed up, in the event that additional resources become available, Government will utilize them to accommodate key national strategic priorities. Specifically, the following will receive priority:

- Interventions identified during the stakeholders consultation for the FY 2019/20 budget and over the medium term

4. **County revenue collection potential report should be published and publicized to help inform public debate on county revenue especially in relation to their Finance Bills.** Paragraph 274 indicates that the National Treasury now has information on the revenue potential in each county. The Own-Source Revenue Potential and Tax Gap Study of Kenya's County Governments provides the first window into fiscal capacity at the county level. This set of information is critical as discussion on having a county own source revenue policy is finalized. In addition, the on-going review of the second equitable revenue sharing formula would benefit from this data as part of how to measure fiscal capacity.
5. **Revenue targeting seems inconsistent with historical performance and too ambitious.** The draft BPS shows that the government projects to collect 14 percent more revenue in 2019/20 compared to the targets set for 2018/19. This would be higher than the projected 8 percent growth for expenditure. That indicates that the government revenue targets would help in reducing the deficits in 2019/20 which is one key indicator of governments effort on fiscal consolidation. However, these projections do not consider historical revenue performance as shown in the table.

Financial Year	Total Revenue	Growth	Simulation for a 10% revenue growth in 2018/19
2014/15	1,107.80		
2015/16	1,232.60	11%	
2016/17	1,422.50	15%	
2017/18	1,522.50	7%	
2018/19*	1,831.50	20%	1,674.75
2019/20	2,080.90	14%	24%

*Target for 2018/19

For example, actual revenue growth revenue between 2016/17 and 2017/18 only grew by 7

percent. However, the revenue growth going into 2018/19 is not expected to be much higher than that and the government is already making expenditure cuts to accommodate lower collections. Therefore, a growth of 20 percent between 2017/18 is unlikely when the previous 7 percent growth is considered. The last column shows a simulation of a growth of 10 percent between 2017/18 which may be more realistic. That would mean the government could raise about 1.67 trillion in 2018/19. This would therefore mean that for the government to meet the target of 1.08 trillion for 2019/20 it would have to grow its revenue by 24 percent. This is not realistic, and it means that the current budget could have implicit deficit above the deficit of Ksh 630 billion projected for 2019/20.

6. The revenue growth factor of the county equitable revenue should be more predictable and realistic. The BPS recommends that counties be allocated Ksh 310 billion in 2019/20. This is lower than the amount of Ksh 314 billion approved in 2018/19 and only 2 percent higher than the revised allocation of Ksh 304 billion for the same year. In addition, significantly different from the 10 percent growth in the amount recommended by the Commission of Revenue Allocation also based on the revised amount of Ksh 304 billion. The table below shows that this difference is common and indicative of lack of a clear and predicable methodology in determining growth patterns of revenue to counties. There is need for a clear determinant of how revenue to counties will grow from year to year especially informed by ordinary revenue trends from previous years. In addition, the current lack of clarity has meant that the growth of the equitable share has been much lower than the growth in ordinary revenue as shown in column G.

	A	B		C		D		E	F	G
		Proposed Growth		Basis for Proposed Revenue Growth						
	Year	CRA	National Treasury	CRA	National Treasury			Growth in the Approved Allocations in the Division of Revenue Act		Growth in National Ordinary Revenue
1	2015/16	10.4%	10.4%	3-Year average growth in ordinary revenue	3-Year average growth in ordinary revenue			14.6%		15%
2	2016/17	15.0%	7.8%	3-Year average growth in ordinary revenue	Not provided			7.9%		15%
3	2017/18	15.0%	6.7%	3-Year average growth in ordinary revenue	3-Year average month on month inflation			7.7%		10%
4	2018/19	8.5%	4.0%	3-Year average inflation	3-Year average month on month inflation			1.0%		21%
5	2019/20	10.0%	2.0%		3-Year average month on month inflation					

*Growth projection based on ordinary revenue target for 2018/19 against the actual ordinary revenue for 2017/18

Source: Division of Revenue Acts and Budget Policy Statements 2015-2019, National Treasury

7. There is need for clarity on what is the planning policy informing government budgeting. The BPS should clearly indicate if the big four agenda items are now part of the

Medium-Term Plan III or they are separate and which of the two is guiding budgeting. The BPS as framed does not give a clear picture of the planning policy in use and what the expected long-term gains will be.

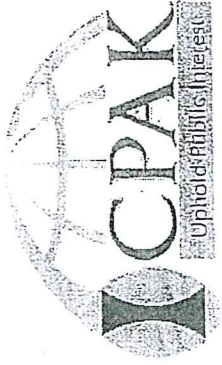
8. **The BPS should provide details of major capital projects across sectors.** Annex Table 5 has details of public-private partnership projects in the energy sector but the same is not provided from other sectors. The BPS does not explain whether these are the only PPP projects that will be in the 2019/20 budget or explain why the other sectors are not included if there are other projects beyond energy. In addition, this should have details of how capital projects are prioritized especially with revenue challenges as identified in the BPS.
9. **The BPS should provide access to information referred to therein.** The BPS makes reference to information, numerous policy and budget related documents that are unavailable in the National Treasury Website or elsewhere. These documents enable readers to reference these documents to understand the proposals therein. We propose that this information should be available online and the website link available in the same page that the BPS is published on the National Treasury website.

Below is a list of information required for better understanding of the BPS

	Information referred to in the BPS but not publicly available	Reference
1.	Universal Health Coverage roadmap and the Universal Health Coverage pilot framework	Para. 97
a.	Under UHC the government will work towards increasing health facility density in 14 counties (Which counties are these?)	Chart 2.3
b.	6200 public health facilities across the country will be equipped with basic clinical equipment (Which counties are these facilities?)	Chart 2.3
2.	National Government agreements with 36 County Governments on housing (where can we read these agreements)	Para. 105
3.	Ajira Programme, the Government has trained about 11,000 youths on online jobs (how much has this cost?)	Para. 179
4.	County Governments' own-source revenue (OSR) policy (Which policy is referred to here)	Para. 168
5.	Justification for the movement of sector ceilings in the BPS and BROP	Para. 97

Signed on February 21, 2019, Nairobi

Abraham Rugo Muriu, PhD.
Country Manager
International Budget Partnership Kenya



The Institute of Certified Public Accountants of Kenya

ICPAK SUBMISSIONS

ON

THE BUDGET POLICY STATEMENT 2019

SUMMARY OF ICPAK SUBMISSION ON BPS 2019

PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
1. Paragraph 12- value of Per Capita Income and Job creation	<p>According to the BPS 2019, The value of goods and services produced raised Per Capita Income from Ksh 113,539 in 2013 to an estimated Ksh 190,521 in 2018, a 67.8 percent increase. This enabled generation of around 840,000 new jobs per year in the period 2013-2018 up from 656,500 new jobs per year in the period 2008-2012</p> <p>According to the Economic Survey 2018, a total of 897.8 thousand new jobs were created in 2017 with 787.8 thousand new jobs created in the informal sector. Employment in the informal sector accounted for 83.4% of total employment in the period under review.</p> <ul style="list-style-type: none"> ▪ How sustainable is employment within the informal sector? ▪ What measures can we put place to spur job creation within the formal and corporate sectors? ▪ Mismatch on data on informal sector- What methodologies/system can KRA use to capture data on informal sector for purposes of tax revenue given that so many jobs are created in this sector yet it isn't considered in the expansion of tax base ▪ How feasible is data on informal sector contribution?? 	<ul style="list-style-type: none"> ▪ Improve the regulatory environment for the informal sector to support stability and growth of MSMEs to overcome start-up challenges and contribute to economic development ▪ Device mechanisms for identification of informal sector players to contribute to tax revenue. ▪ Formalize the informal sector by limiting cash-based transactions as a means to capture all business activities in the economy.

ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
2.	Para 32: Net Foreign Assets (NFA)	The Draft BPS 2019 indicates Kenya's Net Foreign Assets (NFA) grew by 22.3% yet with the increase in external component of the public debt and the import bill indicates otherwise. This needs to be revised for clarity.	The Draft BPS 2019 indicates Kenya's Net Foreign Assets (NFA) grew by 22.3% yet with the increase in public debt and the import bill indicates otherwise. This needs to be revised for clarity.
3.	Para 52- modernized Income Tax Bill	Over the last few years, the reform of Kenya's Tax system has involved policy, legal and administrative reforms aimed at modernizing taxation and simplifying tax administration in Kenya. Recent efforts to modernize the tax regime have yielded a new Value Added Tax 2013, Tax Procedures Act 2015, Excise Duty Act 2015 and Tax Appeals Tribunal Act 2015 without an overarching tax policy.	ICPAK recognizes that legislation, including subsidiary legislation, traces its foundation on an agreed policy framework, to establish the most appropriate approach to resolve a problem. As such, the review of the Income Tax Act should be predicated on a comprehensive n Income Tax policy.
4.	Para 59: Real GDP Growth	In as much as the BPS 2019 projects expansion of the Real GDP by 6.1% in FY 2018/2019, 6.2% in FY 2019/2020, 6.4% in FY 2020/21 and 7.0% FY 2022/23, it fails to put into consideration unforeseen risks and shocks especially in Agricultural sector (unpredictable weather patterns) and the macroeconomic environment that could be affected by external shocks including projected economic slump in leading economies such the US and	It is therefore the Institutes professional opinion that an income tax policy should be developed to guide the review process of the Income Tax Act. It further important to envisage the entire of the tax frame and develop an overarching tax policy ahead of any taxation.
			There's need to consider more realistic growth targets given the economy's vulnerability to shocks. The World Bank (through the Kenya Economic Update 2018) lower growth rates compared to those given in the BPS 2019, that Kenya's economy is expected to grow by 5.7% FY 2018/19, 5.8% FY 2019/20 and 6.0% in 2020/21. Since

PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
	UK	<p>expected economic growth is a factor in subsequent macro-economic and fiscal projections, we argue for a more prudent approach by which we do not over-project the state of the economy.</p>
<p>5. Para 64: Government Policies to support Fiscal Consolidation</p>	<p>The Institute takes note and commends the Government for recognizing the need for fiscal consolidation. However, it will be crucial to carefully determine which expenditures are contained so that the government's "Big Four" Agenda and service delivery are not curtailed.</p> <p><i>capacities to generate</i> <i>business in key</i> <i>countries</i></p>	<p>According to the World Bank's Economic Update:</p> <ul style="list-style-type: none"> ▪ There is need to re-ignite private sector led growth, in this regard, fiscal consolidation must be growth friendly; ▪ Fiscal consolidation needs to be recalibrated towards recurrent spending such as - lowering of transfers to state owned enterprises, cleaning and regular audit of the payroll register, keeping wages, salaries and allowance adjustments in line with recommendations from the Salaries and Remuneration Commission (SRC) ▪ Fiscal policy should geared towards regenerative expenditure not consumptive expenditure.
<p>6. Para 85 MSMEs To further support the manufacturing sector, the</p>	<p>Traditional sources of financing for MSMEs have revolved around personal savings, loans from friends and family, and other informal sources.</p> <p>The Institute notes that for the MSME sector to succeed, it must be supported to overcome key challenges:</p>	<p>The government should consider putting in place programmes to</p> <ul style="list-style-type: none"> ▪ Support financial literacy for MSMEs on areas such as basic record-keeping, cash management, managing customer and supplier payments, tax, insurance and

ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
	<p>Government will continue to promote provision of financial support and credit to Micro, Small and Medium Enterprises (MSMEs)</p>	<ul style="list-style-type: none"> • The regulatory environment • multiple licenses for same business • multiple procedures in registration; • lack of markets; • poor infrastructure (roads, power and water supply) 	<p>other regulatory requirements.</p> <ul style="list-style-type: none"> • At curriculum development level, introduce teaching and learning during formative school years and promoting work experiences for students on MSMEs. • Reform the tax policy to help in the formalization of the informal sector. This can be achieved through: <ul style="list-style-type: none"> a) harmonization of taxes by reducing multiplicity of taxes both at National and subnational levels b) Tax education for taxpayers to understand why they pay. There's also need for sensitization on presumptive tax • Market linkage for MSMEs in Kenya. In addition, there's need to scale-up a programme from micro to small then to medium and large enterprises – to have ready companies to compete at local, regional and global markets. • The government through the MSME authority should consider standardizing and authenticating Kenya products to foster comparative advantage.
7.	Para 86 – Food	According to Global Hunger Index (GHI) 2018, Kenya is classified as a food deficit country. Currently, close to 1 in every	<ul style="list-style-type: none"> • The sector legal, policy and institutional capacity should be strengthened in

PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
<p>Security</p> <p>The Government will continue to implement measures in the agricultural sector in order to ensure food and nutrition security.</p>	<p>3 Kenyans (14.5 million) suffer from chronic food insecurity and poor nutrition annually. In addition, about 30% of the children worldwide are stunted, 13% moderately wasted, while 7% are moderately underweight. Approximately 20% of the population does not attain the minimum dietary requirements to sustain a healthy and productive life.</p> <p>Agricultural sector has faced numerous challenges lowering its productivity in the recent years. Stagnation in productivity has been largely due to frequent droughts in parts of the country, high costs of domestic food production due to high costs of inputs especially fertilizers and farming equipment, rural-urban migration of young energetic population, low purchasing power for large proportions of the population due to high poverty levels, lack of incentives and lack of diversified agricultural activities.</p>	<p>realization of core mandates. This is more so with, regard to devolved functions which require guidelines for implementation.</p> <ul style="list-style-type: none"> • There is need for introduction of subsidies to farmers especially on inputs such as fertilizers and high yield seeds. • Increase funding levels especially to the sectors that contribute to food security such as Agriculture and manufacturing. Exchequer releases should be within the prescribed timeline to facilitate implementation of development programs. Agriculture should be at least 10% as per Maputo Declaration. • Build and improve rural infrastructure to open space for movement of goods and services. • Revisiting policies on trade agreements to boost export of some agricultural products. • Improve access to financial services and credit in agriculture and rural development.
<p>Para 86 – Food Security</p>	<p>Storage facilities and other down-stream efforts for agriculture produce has been a challenge in Kenya. In the 2018 BPS, the government indicated that it will introduce incentives for post-</p>	<p>The Government should consider employing the Ethiopian style warrant age or</p>

ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
	(Storage)	<p>harvest technologies to reduce losses from 20% to 15%. However, this is still a challenge in the sector.</p> <p><i>Stefano</i></p>	<p>inventory credit system.</p> <p>This is a community-based micro credit approach where farmers in partnership with a lending agency (micro-financial institution, NGO, etc.) store their products at harvest in the appropriate established warehouses and are issued with cash loans based on the value of the product deposited, which they could use to address urgent financial needs, participate in collective input purchase or carry out income-generating activities during the off-season.</p> <p>Later, in agreement with the lending institution, the farmers sell the stored produce at higher prices, say after 4-5 months after harvest, when the market supply begins to decline. The cash is then used to pay back the loans with interest.</p> <p>This system has been a success in West African countries like Mali, Niger and Burkina Faso in dealing with poverty/ enhancing rural economic empowerment.</p>
9.	Para 86-Food Security (Irrigation)	<p>The Institute is concerned that for the last two years, a lot of public resources have been invested in irrigation yet the rewards have been minimal. For instance, in BPS 2018, the government placed 700,000 Acres through PPP under maize, potato, rice, cotton, aquaculture and feeds production and formed an Agriculture and Irrigation Sector Working Group to provide coordination of for irrigated agriculture</p>	<ul style="list-style-type: none"> ▪ Monitor progress in implementation of irrigation related projects to determine returns on investment. ▪ Consider reviewing pricing of produce from farmers. For instance, there has been hue and cry from farmers in the coffee,

Progress

Stefano

↑ The value addition in farms produce.

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
		<p>In 2019, the government plans to develop 85,000 acres of irrigation area under National Expanded Irrigation programme and increase area under smallholder irrigation by 1,617 acres</p>	<p>maize and sugar sectors on low prices for their produce</p>
10.	<p>Para 90- Maize Production</p>	<p>Weak monitoring and evaluation systems hamper smooth implementation of the budget and good initiatives started by Government. Its unclear whether agreed targets as enumerated in BPS 2018 have been met under this area. The BPS 2018 had indicated that the government targeted to increase maize production from 40 million 90 kg bags annually to 67 million bags by 2022. To build on these efforts, the government plans (under BPS 2019) to boost maize production by providing subsidized fertilizer to farmers. Already, the Government has spent over Ksh 4.3 billion in acquiring 119,400 metric tonnes of soil friendly fertilizer to subsidize the cost for farmers.</p>	<p>The government should consider supporting standardization and coding of agricultural products to enable competing at the global markets</p>
11.	<p>Para 96- Universal Health Coverage</p>	<p>Its unclear whether agreed targets as enumerated in the BPS 2018 have been met under this area. In 2018, the Government promised to - In particular, the Government will review and amend the NHIF Act to align it to the universal health coverage as well as review the laws governing private insurance companies to encourage investment by private health insurers and bring the cost of cover within the reach of every Kenyan. This has been reiterated in the BPS 2019.</p> <p>Progress in implementing UHC is threatened by persistent labour unrest.</p>	<ul style="list-style-type: none"> ▪ The government should complete reconfiguration and digitization of NHIF to ensure the system is ready for roll out before fully implementing the UHC. ▪ There is need to increase the health budgetary allocation to the recommended 15% of the total annual budget as recommended by the AU under the auspices of Abuja declaration. ▪ Sector players should dialogue to end persistent labour unrest in the sector. Currently, nurses in over 17 counties are on strike to the detriment of services and

ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
12.	Para 97 – Universal Health Coverage	<p>The wording of paragraph 97 connotes free health services,</p> <p>“<i>The residents of these Counties will receive free health care services in all health facilities from their local health centres all the way to the referral facilities. The Government will use the lessons learnt from this pilot to refine and scale up the programme to the rest of the Counties over the next 18 months</i>”, against provisions of the BPS which allude to the fact that a reconfigured contributory NHIF shall be the platform for implementing UHC. This needs to be clarified.</p>	<p>suffering to Kenyans at larger. We urge Labour Unions, National Government and County Governments to work together to address the concerns of the doctors, nurses and other cadres within the health sector.</p> <p>There is need for clarity on whether the Government will be providing free health care services in the long-run under the UHC</p>
13.	Para 102/103	<p>Paragraphs 102 and 103 anticipate investment in health infrastructure including the relevant equipment. However, there is no indication of a commensurate effort to hire competent health personnel to handle the purchased equipment.</p>	<p>Hire and train staff/manpower with relevant skills to handle the purchased equipment (that is, human capital is vital)</p>
14.	Para 107 National Housing Development Fund	<p>Stakeholders have raised concerns on the structure and implementation framework of the National Housing Development Fund.</p>	<p>Consider incentive to businesses by way of either tax credits or allow for the contributions to be treated as tax allowable. This will be a useful relief to businesses which are already of doing business grappling with the high cost of doing business. Such a charge on business is an additional burden.</p>

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
			<ul style="list-style-type: none"> ▪ Increase housing relief for employees: Currently, employees have to cope with numerous statutory deductions from their salaries in the form of taxes. There is need to introduce a housing relief which will help reduce the tax liability. ▪ Access must apply equally for both the public and the private sector: There is need to ensure that access to the benefits of the fund are not only skewed to the public sector in form of salaried government employees but that benefits are also accessible by the private sector. This will give incentives to the private sector to support implementation of the affordable housing agenda. ▪ Administration of the fund: Funds must be utilized only for the intended purpose. Appropriate checks and balances must be put in place to avoid misappropriation of the fund in the form of graft ▪ Mortgage exemptions: The Regulations should provide that employees currently servicing a mortgage should be exempted from contributing to this fund upon proof of mortgage/home ownership loan plan. This will ease the burden of additional tax burden arising from implementation of this policy change.
15.	<p>Housing-General</p>	<p>Its unclear whether agreed targets as enumerated in the BPS 2018 have been met under this area. In 2018, the government</p>	<p>Strengthen monitoring and evaluation systems for the “Big Four” Agenda projects and other</p>

ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
	Comments on M & E systems	<p>earmarked the following projects:</p> <ul style="list-style-type: none"> • Development of a comprehensive housing package that will incentivize the private sector in low cost housing • Established a Taskforce on Expanding Affordable Housing Finance in Kenya • Prioritized review of the National Construction Authority Act, Built Environment Bill, and related legislations to ensure they address matters on sustainable building standards and design procedures, as well as green building codes for sustainability and safety of the housing sub-sector 	government initiatives
16.	Para 110- Idle Land Tax	The Government plans to include allowing strategic land acquisition (Public Land), prohibiting land speculation (Idle Land Tax/Potential Land Tax)	A very encouraging move that will address the pervasive trend of hoarding land, a factor of production, for speculative purposes. It is expected the introduction of this idle land tax which discourage land hoarding and balance off the high cost of land.
17.	Para 147- Blockchain Technology	<p>The Government aims at setting up a taskforce on Blockchain and Internet of Things (IoT) technologies that will study the benefits and challenges associated with the latest digital innovation trends.</p> <p>On contrary, the Taskforce on Blockchain Technology was set up in 2018 and finalized its findings and report.</p>	<p>The economic prosperity of a country is closely linked to the richness of her natural resources of which is a core factor. The push to apply all land into productive use is this a welcome move.</p> <p>It is our considered view that rather than set up another Taskforce, the government needs to implement the Report of the Taskforce on Blockchain Technology to promote accountability within the economy</p>

7	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
18.	Para 152: Access to Clean Water	The Government unveiled plans to implement the strategic water storage program that will increase the number of Kenyans connected to safe piped water by 9 million people by 2022. The Institute supports this proposal.	To further promote realization of Article 43 of the Constitution, we urge all stakeholders to support CRA's proposed 3 rd Revenue Generation formula that has a heavy component on service delivery. Access to water is one of the parameters of the proposed formula.
19.	Para 157: Sports Fund	In order to have a sustainable financing for sports, arts and culture, the Government has established under Public Finance Management Act a Fund with financing mainly from betting taxes and winning. ICPAK is of the opinion that Government should instead offer tax incentives for sport betting companies who spend 40% of their incomes to sponsor sporting activities. In addition, sports tourism and sport development be exempted from corporation tax.	ICPAK is of the opinion that Government should instead offer tax incentives for sports-related betting companies who spend 40% of their incomes to sponsor sporting activities. In addition, sports tourism and sport development be exempted from corporation tax t.
20.	Para 180: Consolidation of Uwezo Fund, Youth Enterprise Development Fund and Women Enterprise Development Fund.	The Government plans to support the youths, women and people with disabilities by reforming and consolidating affirmative action funds such as Uwezo Fund, Women Enterprise Fund, into one robust Fund whose objective is to support enterprises owned by youth, women and persons with disabilities. This is long overdue. The initiative was identified in the 2018 BPS.	There's need to Fastrack this process. CS Rotich indicated in his Budget Speech FY 2018/19 that the Cabinet has approved Biashara Kenya Fund by merging Uwezo Fund, Youth Enterprise Development Fund and Women Enterprise Development Fund.

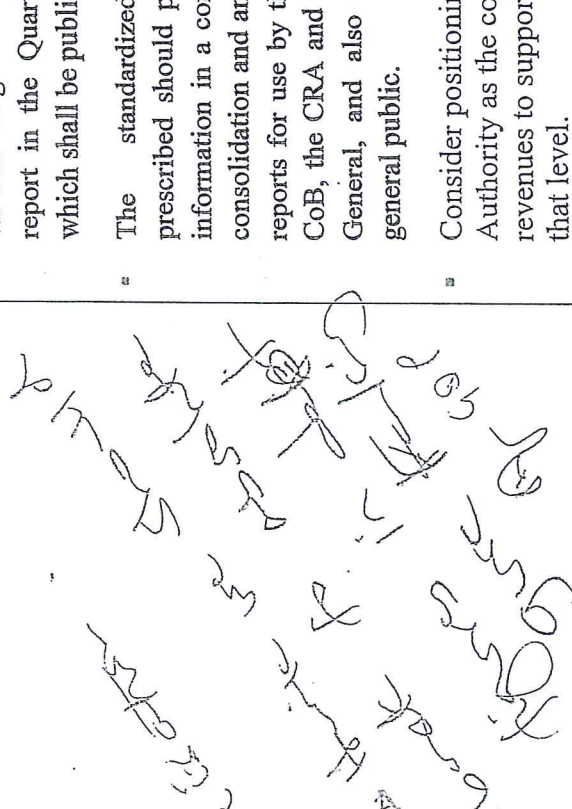
ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS																
21.	Para 181- 185 Strengthening Governance and the Fight against Corruption	Kenya has an elaborate legal architecture on integrity and accountability. This ranges from the Constitutional provisions on leadership and integrity to other numerous related pieces of legislation on public finance management, integrity, bribery and accountability. Nevertheless, we continue to witness myriad cases of financial misappropriation and the numerous reported scandals involving both the public and private entities.	Amend the law and provisions on public finance management, anti-money laundering, leadership and integrity to include: <ul style="list-style-type: none"> • Total blacklisting to public positions for persons culpable • Strengthen asset recovery mechanism, including repatriation of assets 																
22.	Para 205 of realism revenue forecast --- its ambitious and leads to budget deficit .. For instance,	<p>The Institute is concerned with the accuracy and the ambitious nature of National Treasury's revenue projections. This exacerbated by failure by the Tax Authority to meet the set targets over the years.</p> <p>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. The common tendency has therefore been to make overly optimistic revenue projections leading to an increased uncertainty of resource flows.</p> <p>Revenue Projections FY 2017-18- 2019-2020</p> <table border="1" data-bbox="1109 817 1418 1657"> <thead> <tr> <th data-bbox="1109 1451 1173 1657">Fiscal Year</th> <th data-bbox="1109 1249 1173 1451">FY 2017/18</th> <th data-bbox="1109 1025 1173 1249">FY2018/19</th> <th data-bbox="1109 817 1173 1025">FY 2019/2020</th> </tr> </thead> <tbody> <tr> <td data-bbox="1173 1451 1220 1657">Revenue</td> <td data-bbox="1173 1249 1220 1451"></td> <td data-bbox="1173 1025 1220 1249"></td> <td data-bbox="1173 817 1220 1025"></td> </tr> <tr> <td data-bbox="1220 1451 1324 1657">Total Revenue including A-I-A</td> <td data-bbox="1220 1249 1324 1451">Ksh 1,643.1 billion</td> <td data-bbox="1220 1025 1324 1249">Ksh 1,831.5 billion</td> <td data-bbox="1220 817 1324 1025">Ksh 2,080.9 billion</td> </tr> <tr> <td data-bbox="1324 1451 1418 1657">Ordinary Revenue</td> <td data-bbox="1324 1249 1418 1451">Ksh 1,486.3 billion</td> <td data-bbox="1324 1025 1418 1249">Ksh 1,651.5 billion</td> <td data-bbox="1324 817 1418 1025">Ksh 1,877.2 billion</td> </tr> </tbody> </table>	Fiscal Year	FY 2017/18	FY2018/19	FY 2019/2020	Revenue				Total Revenue including A-I-A	Ksh 1,643.1 billion	Ksh 1,831.5 billion	Ksh 2,080.9 billion	Ordinary Revenue	Ksh 1,486.3 billion	Ksh 1,651.5 billion	Ksh 1,877.2 billion	<p>According to ICPAK's, 'Kenya Revenue Analysis Report, 2015'. The role of Parliament is critical in providing oversight over the revenue projections. According to the Parliamentary report on the Budget Policy Statement, the Budget and Appropriations' Committee expressed concerns over the revenue projections provided by the executive in the FY 2014/2015 and by extension, the subsequent revenue projections including the 2019/20 which we also feel are not backed by economic fundamentals.</p> <p>This calls for a holistic approach and a review of economic data and macroeconomic trends when setting revenue targets.</p>
Fiscal Year	FY 2017/18	FY2018/19	FY 2019/2020																
Revenue																			
Total Revenue including A-I-A	Ksh 1,643.1 billion	Ksh 1,831.5 billion	Ksh 2,080.9 billion																
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PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS												
<p>23. Para 210 – Deficit Financing</p>	<p>The government needs to put into consideration efforts to reduce the fiscal deficit.</p> <p>Fiscal Deficit over the years</p> <table border="1" data-bbox="464 806 901 1653"> <thead> <tr> <th>Fiscal Year</th> <th>FY 2017/18</th> <th>FY 2018/19</th> <th>FY 2019/2020</th> </tr> </thead> <tbody> <tr> <td>Fiscal Deficit excluding grants</td> <td>Ksh 581.8 billion</td> <td>Ksh 638.2 billion</td> <td>Ksh 623.8 billion</td> </tr> <tr> <td>Fiscal Deficit including grants</td> <td>Ksh 529.8 billion</td> <td>Ksh 587.7 billion</td> <td>Ksh 572.2 billion</td> </tr> </tbody> </table> <p>This has had an impact on accumulation of public debt</p>	Fiscal Year	FY 2017/18	FY 2018/19	FY 2019/2020	Fiscal Deficit excluding grants	Ksh 581.8 billion	Ksh 638.2 billion	Ksh 623.8 billion	Fiscal Deficit including grants	Ksh 529.8 billion	Ksh 587.7 billion	Ksh 572.2 billion	<p>We take issue with the GDP figures applied in computing fiscal deficit as a function overall GDP. This demonstrates that the projected GDP figures which are subsequently applied to compute economic indicators are grossly overstated and hence cannot be relied upon. THE BPS 2019 presupposes a GDP projection of 11.7 trillion shillings in 2019/20 yet statistics from the CBK which are comparable with globally computed figures put the countries GDP at a modest KES 8.4 trillion. By this overcast in the GDP figures, the BPS has projected a healthier fiscal deficit than it is the case.</p>
Fiscal Year	FY 2017/18	FY 2018/19	FY 2019/2020											
Fiscal Deficit excluding grants	Ksh 581.8 billion	Ksh 638.2 billion	Ksh 623.8 billion											
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<p>24. Para 299- Own Source Revenue</p>	<p>There has been delay in implementing the policy on Own Source Revenue.</p>	<ul style="list-style-type: none"> ▪ Fastrack implementation of the OSR Policy as developed by the National Treasury ▪ For effective revenue management across the Counties, there is need to integrate the different systems for revenue collection and management. IFMIS has been very vital in entrenching accountability in financial management. ▪ County Treasuries should continuously review the performance of revenue collection 												

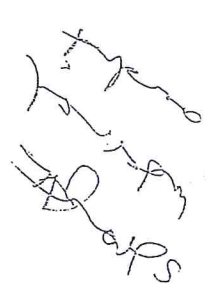
increase income of county treasuries

ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
			<p>vis-avis targets and shall include a status report in the Quarterly and Annual reports which shall be published in various media.</p> <ul style="list-style-type: none"> The standardized ICT-based system prescribed should provide real time revenue information in a consistent manner to enable consolidation and analysis, as well as periodic reports for use by the National Treasury, the CoB, the CRA and the Office of the Auditor General, and also easily accessible by the general public. Consider positioning the Kenya Revenue Authority as the collector of county revenues to support revenue collection at that level.
25.	<p>Para 304 – Absorption of Development Funds</p>	<p>This is a worrying trend at the two levels of government. One of the main causes cited by the Controller of Budget is the delay in Exchequer Releases.</p> <p>For instance, during the Annual report of FY 2015/16, the total exchequer releases towards development expenditure totaled Kshs. 110.4 billion representing 14.3% of the annual net estimates. This is a low percentage considering that at half year, total exchequer releases towards development expenditure should be approximately 50% of the annual net estimates.</p>	<p>The low absorption rates of approved budgets is a pointer to weak budgeting process in relation:</p> <ul style="list-style-type: none"> Over-ambitious and unrealistic revenue projections which become uncollectible; As a result of the above, erratic exchequer releases serve to compound the problem. <p>We need to rethink the budgeting frame more specifically around revenue projections. This has consequent effect on budget implementation.</p>
26.	<p>Para 307/308 –</p>	<p>According to the Auditor General Reports, there has been an increase</p>	<p>Globally, under cash accounting, transactions are</p>

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS						
	<p>Pending Bills</p>	<p>in pending bills in the recent times. The table below illustrates the increase for the national government.</p> <table border="1" data-bbox="406 981 582 1624"> <tr> <td>2013/14</td> <td>16,638,164,142</td> </tr> <tr> <td>2014/15</td> <td>43,212,107,778</td> </tr> <tr> <td>2015/16</td> <td>20,472,313,203</td> </tr> </table> <p><i>Handwritten signature: Atanor</i></p>	2013/14	16,638,164,142	2014/15	43,212,107,778	2015/16	20,472,313,203	<p>recognized only when the associated cash is received or paid, and economic events are not reported if there is no immediate exchange of cash. Accrual accounting therefore offers several benefits:</p> <ul style="list-style-type: none"> ▪ accrual-based fiscal reports provide a more comprehensive view of the government's financial performance and the cost of government activities; ▪ help focus greater attention on the part of policymakers and the public on the acquisition, disposal, and management of government assets, liabilities, and contingent liabilities ▪ by consolidating not only central government ministries and agencies but all institutional units under government control, accrual accounts provide a more complete picture of the financial position of the public sector as a whole; ▪ by reporting stocks and flows within an integrated accounting framework based on internationally-accepted standards such as IPSAS, accrual accounting can improve the reliability and integrity of government financial data
2013/14	16,638,164,142								
2014/15	43,212,107,778								
2015/16	20,472,313,203								
27.	<p>Para 309 – absence of audit committees</p>	<p>BPS 2019 identifies absence and/or ineffectiveness of internal audit committees in line with part XIII of the PFM (County Governments) Regulations, 2015 as one of the county financial</p>	<ul style="list-style-type: none"> • Continuously lobby County entities to establish audit committees 						

ICPAK Submissions on BPS 2019

#	PARAGRAPH OF BPS 2019	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS								
		<p>risks.</p> 	<ul style="list-style-type: none"> Capacity build established committees on their roles Support CRA's proposals to have this as a variable under the Fiscal Prudence parameter for revenue share. This will obligate counties to establish and operationalize effective Audit Committees 								
28.	<p>Para 316- County governments Equitable Share</p>	<p>ICPAK's analysis of the Division of Revenue Process shows that for the past three years, the Division of Revenue Act (DORA) has used FY 2013/14 audited accounts as the basis for equitable share!</p> <table border="1" data-bbox="646 1187 853 1489"> <thead> <tr> <th>Division of Revenue Act (DORA)</th> <th>Audited Financial Statements</th> </tr> </thead> <tbody> <tr> <td>DORA 2016</td> <td>935, 653 million</td> </tr> <tr> <td>DORA 2017</td> <td>935, 653 million</td> </tr> <tr> <td>DORA 2018</td> <td>935, 653 million</td> </tr> </tbody> </table> <p>Therefore, the use of 2013/14 figures affect fairness and equity in the revenue share. These disadvantages county governments given that any surplus accrues to the national government.</p>	Division of Revenue Act (DORA)	Audited Financial Statements	DORA 2016	935, 653 million	DORA 2017	935, 653 million	DORA 2018	935, 653 million	<ul style="list-style-type: none"> It is our considered opinion that in adjudicating of vertical revenue share FY 2019/2020, National Treasury, Commission on Revenue Allocation (CRA) and Parliament should use the most recent audited financial statements as the basis for revenue allocation. The latest audited accounts cover the fiscal year 2016/17 National Assembly to consider, expedite scrutiny and adoption of these reports from the Auditor General. This will enable not only the revenue share to rely on the most recent and approved financial statements, but also enhance accountability of public funds on a timely manner.
Division of Revenue Act (DORA)	Audited Financial Statements										
DORA 2016	935, 653 million										
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REPUBLIC OF KENYA

THE NATIONAL TREASURY AND PLANNING

REMARKS BY THE CABINET SECRETARY/NATIONAL TREASURY AND PLANNING DURING THE MEETING WITH THE STANDING COMMITTEE ON FINANCE AND BUDGET OF THE SENATE ON THE MEDIUM TERM BUDGET POLICY STATEMENT FOR THE FINANCIAL YEAR 2019/20

1. Mr. Chairman, it's my great honour to present to this committee of the Senate, the policy thrust in the the 2019 Budget Policy Statement, the Division of Revenue Bill, 2019 and the County Allocation of Revenue Bill, 2019.

A. 2019 BUDGET POLICY STATEMENT

2. Mr. Chairman, the Budget Policy Statement is prepared in accordance with Section 25 of the Public Finance Management Act, 2012. The law states that: *"(i) The National Treasury shall prepare and submit to Cabinet the Budget Policy Statement for approval; and, (ii) The National Treasury shall submit the Budget Policy Statement approved in terms of subsection (1) to Parliament, by the 15th of February each year"*.

3. Mr. Chairman, in finalizing the BPS and the related documents we consulted a wide range of stakeholders and the general public were also consulted in line with the requirements of the Public Finance Management (PFM) Act and the Constitution.

4. The theme for the 2019 Budget Policy Statement is **Creating Jobs, Transforming Lives - Harnessing the "Big Four"** and it builds on the progress made under the Economic Transformation Agenda to raise productivity and economy-wide efficiency, thereby sustaining high and inclusive growth in line with aspirations of Kenya Vision 2030.

5. The policy outlined in the BPS draws from the national development agenda as outlined in the Third Medium Term Plan (MTP III) of the Vision 2030 and targets to attain the Sustainable Development Goals (SDGs) of the United Nations. The policy prioritizes investments in "The Big Four" Plan, that is: manufacturing for job creation; food and nutrition security; Universal Health Coverage; and affordable housing. In addition, the policy prioritizes creation of a conducive business environment under all the enablers of the "Big Four" Plan.

6. **Mr. Chairman**, notable progress has been made on the implementation of the "Big Four" Plan across the four strategic areas:

- (i) To support growth of the manufacturing sector, the Government has scaled up reforms to encourage investment in the sector. In particular, the Government has heightened the fight against illicit trade and contrabands to protect genuine businesses and traders.
- (ii) To enhance food and nutrition security, the Government has aligned all policies under the agriculture sector towards increasing food production, boosting smallholder productivity and reducing the cost of food.
- (iii) To make Universal Health Coverage a reality, the Government has launched the pilot phase of the universal health programme in four Counties namely, Kisumu, Machakos, Nyeri and Isiolo.
- (iv) Finally, on housing, the Government has established the National Housing Development Fund which will be responsible for mobilizing capital to finance the affordable housing project. Additionally, the Government has established the Kenya Mortgage Refinance Company (KMRC) to leverage funds from Development partners and the private sector and provide secure long-term funding to financial institutions thereby increasing the availability and affordability of mortgage loans to Kenyans.

7. **Mr. Chairman**, as we continue to implement the "Big Four" Plan, we are clearly conscious of our limited fiscal space and will therefore continue to leverage on public

Background by Julie.

private partnerships arrangements. In this regard, the Government will continue to rally the support of both the private sector players and development partners to support for the “Big Four” Plan. Already, many of our development partners are funding projects within the “Big Four” sectors. But in addition to that, and with a view to mobilizing additional resources, they are reviewing the rest of their portfolio to align them with the “Big Four” Plan.

8. Mr. Chairman, resource allocation for the National Government in the BPS for FY 2019/20 have been realigned to “The Big Four” Plan. Thus, the targeted expenditures will prioritize employment creation, youth empowerment, supporting manufacturing activities, enhancing health coverage, improving food security and enhancing living conditions through affordable housing. The allocations to other critical sectors such as education, infrastructure, energy and social protection will remain protected so as to achieve the targeted objectives.

9. Mr. Chairman, allow me to highlight the context in which the 2019 Budget Policy Statement (BPS) has been prepared and the recent economic developments.

10. Mr. Chairman, the 2019 BPS was prepared against a background of weakening global economy. Global growth is projected to slow down to 3.5 percent in 2019 from an estimate of 3.7 percent in 2018 occasioned by weaker economic activities in both the advanced and emerging market economies. However, the Sub-Saharan Africa region is expected to register strong growth of 3.5 percent in 2019 from an estimated 2.9 percent in 2018 largely due to improved commodity prices and capital markets access.

11. **Domestic Economic Performance:** Kenyan economy remains strong and resilient. The economy is estimated to grow by 6.0 percent in 2018 up from 4.9 percent in 2017 and further to 6.2 percent in 2019. Growth continues to be supported by strong agricultural and manufacturing activities underpinned by favourable weather conditions, strong service sector, stable macroeconomic environment, ongoing public infrastructural investments and sustained business confidence.

12. Growth is projected to improve further to 6.2 percent in 2019 and 7.0 percent per annum over the medium term supported by strong agricultural and manufacturing activities underpinned by favourable weather conditions, strong service sector, stable macroeconomic environment, ongoing public infrastructural investments, sustained business confidence and investments in strategic areas under the “Big Four” Plan.

13. **Mr. Chairman**, inflation remains low, stable and within the Government target range of 5+/-2.5 percent as a result of prudent monetary and fiscal policies. Month-on-month overall inflation declined to 4.7 percent in January 2019 from 5.7 percent in December 2018.

14. **Exchange Rate:** The Kenya Shilling exchange rate remained broadly stable and competitive against major international currencies. Against the dollar, the exchange rate has been relatively less volatile exchanging at Ksh 101.6 in January 2019 from Ksh 102.9 in January 2018. Against the Euro and the Sterling pound, the Shilling also strengthened to Ksh 115.9 and Ksh 130.8 in January 2019 from Ksh 125.4 and Ksh 141.9 in January 2018, respectively

15. **Short-term interest rates:** Interest rates have remained fairly low and stable due to ample liquidity in the money market. The interbank rate remained low at 3.5 percent in January 2019 from 6.2 percent in January 2018 while the 91-day Treasury bill rate declined to 7.2 percent from 8.0 percent over the same period.

16. **Mr. Chairman**, annual growth of credit to the private sector grew by 2.4 percent in the year to December 2018, compared to a growth of 2.5 percent in the year to December 2017. In particular, lending to finance and insurance, consumer durables, business services, private households and manufacturing sectors grew by 17.5 percent, 11.0 percent, 8.3 percent, 6.8 percent and 6.0 percent, respectively. We expect private sector credit growth to strengthen in 2019 relative to 2018, with the anticipated higher economic activity and easing credit risk.

17. Mr. Chairman, the foreign exchange market remains stable supported by a continued narrowing in the current account deficit. The current account deficit is estimated at 5.2 percent of GDP in 2018 and is expected to narrow to 5.1 percent of GDP in 2019. This narrowing reflects strong growth in diaspora remittances and tourism receipts, higher tea and horticultural exports, slower growth in imports due to lower food and SGR-related equipment imports and the decline in international oil prices

18. Budget Implementation for the FY 2018/19: Budget execution started on a slow note in the first quarter of the FY 2018/19 but picked up towards the end of the first half. The slowdown was due to budget rationalization to align expenditure priorities to revenues after amendments to the Finance Bill 2018.

19. Mr. Chairman, the revised total revenue for FY 2018/19 is projected at Ksh 1,852.6 billion or 18.5 percent of GDP. Ordinary revenue, the component of our revenues that accrue to the exchequer, is projected at Ksh 1,672.2 billion or 16.7 percent of GDP. These revisions took into account, the weaker than expected revenue outcome for FY 2017/18, the rationalization process during the enactment of the Finance Bill, 2018 and the continued slow pace of revenue recovery in the first half of the financial year.

Revenue Performance by end January 2019

20. Mr. Chairman, total cumulative revenue including A-I-A collected by the end of January 2019 amounted to Ksh 924.8 billion against a target of Ksh 996.3 (Table 1). This performance was below the target by Ksh 71.5 billion.

Table 1: Government Revenue, Period Ending 31st January, 2019

	Jan 2018/19			Jan 2017/18	Jan 18/19	Jan 17/18	Growth Exchequer
	Target	Prel. Issues (Exchequer)	Deviation	Prel. Issues (Exchequer)	Exchequer Rev. % of GDP	Exchequer Rev. % of GDP	
TOTAL REVENUE	996,317	924,807	-71,510	840,619	9.2%	9.5%	10.0%
Ordinary revenue	902,172	847,731	-54,441	783,519	8.5%	8.9%	8.2%
Import Duty	69,087	61,152	(7,934)	58,181	0.6%	0.7%	5.1%
Excise Taxes	130,012	110,267	(19,745)	92,485	1.1%	1.1%	19.2%
Taxes on Income, Profits (Income Tax)	414,447	380,398	(34,049)	377,219	3.8%	4.3%	0.8%
Income Tax from Individuals (PAYE)	227,504	220,074	(7,429)	196,689	2.2%	2.2%	11.9%
Other Income Tax	186,943	160,323	(26,620)	180,530	1.6%	2.1%	-11.2%
Taxes on goods and services (VAT)	245,715	232,444	(13,271)	203,207	2.3%	2.3%	14.4%
VAT (Domestic)	134,471	131,816	(2,655)	115,661	1.3%	1.3%	14.0%
VAT (Imports)	111,244	100,627	(10,616)	87,546	1.0%	1.0%	14.9%
Investment Income	35	24,404	24,370	15,467	0.2%	0.2%	57.8%
Other Revenue	42,877	39,066	(3,811)	36,960	0.4%	0.4%	5.7%
Ministerial Appropriation in Aid	94,145	77,076	(17,069)	57,100	0.8%	0.6%	35.0%
Recurrent	66,597	55,092	(11,505)	43,438	0.5%	0.5%	26.8%
o/w RML	41,638	43,738	2,100	42,993	0.4%	0.5%	1.7%
Transit toll	489	484	(5)	444	0.0%	0.0%	9.0%
Other Recurrent	24,470	10,870	(13,599)	-	0.1%	0.0%	0.0%
Development	27,548	21,984	(5,564)	13,662	0.2%	0.2%	60.9%
o/w RDL	14,110	12,511	(1,599)	12,337	0.1%	0.1%	1.4%
PDL	1,686	1,188	(498)	1,325	0.0%	0.0%	-10.3%
Other Development	11,752	8,284	(3,468)	-	0.1%	0.0%	0.0%
GDP					10,030,206	8,804,905	

Source: The National Treasury

21. **Mr. Chairman**, ordinary revenue amounted to Ksh 847.7 billion by end January 2019, against a target of Ksh 902.2 billion, an under performance of Ksh 54.4 billion. Cumulative ministerial A-I-A collection was Ksh 77.1 billion against a target of Ksh 94.1 billion, an under performance of Ksh 17.1 billion. This performance indicates that growth in total revenue by January 2019, improved to an annual rate of 10.0 percent relative to 8.8 percent in January 2018 but lower than January 2016 levels of 15.2 percent. However, ordinary revenue growth declined to 8.2 percent from 9.0 percent in January 2018.

Reforms to Support the Fiscal Consolidation Plan

22. **Mr. Chairman**, the fiscal framework underpinning the FY 2019/20 budget supports the fiscal consolidation plan. The plan will see a gradual reduction of fiscal deficit from 7.2 percent in the FY 2017/18 to 3.1 percent of GDP over the medium term which is in line with the East African Monetary Union (EAMU) protocol target ceiling of 3.0 percent of GDP. The consolidation will be supported by enhanced revenue mobilization and rationalization of recurrent expenditure while protecting capital expenditure. This will reduce public debt and create fiscal space over the medium term.

23. In the FY 2018/19, the Government implemented a raft of tax policy measures through the tax amendment law and the Finance Act 2018 whose revenue yield is estimated at about 0.9 percent of GDP. In addition, the modernized Income Tax Bill currently undergoing legal drafting, will also ease administrative bottlenecks, improve compliance and boost revenue collection, thereby supporting our fiscal consolidation efforts.

24. To enhance revenue mobilization, the Government continues to implement tax policy and administrative measures. Specifically, under the Revenue Enhancement Initiatives Programme, the Government will strengthen tax administration and compliance through:

- i. Enhanced scanning to detect concealment and increase efficiency in cargo clearing through procurement of additional scanners and full integration of all scanners;
- ii. Use of Regional Electronic Cargo Tracking System to ensure all goods reach the desired destinations and avoid dumping;
- iii. Use of third-party information to identify non-compliant property developers and ensure they are included in the tax base; and
- iv. Detection of non-compliance through i-Tax data matching.

25. In order to increase efficiency and effectiveness of public spending, the Government has established the Public Investment and Management (PIM) Unit and adopted the Public Investment Guidelines that will guide appraisal of all projects before their inclusion in the budget.

26. Mr. Chairman, as a result of these measures, in FY 2019/20, revenue collection including Appropriation-in-Aid (A.i.A) is projected at Ksh 2,080.9 billion (18.3 percent of GDP). Of this Ordinary revenue is projected at Ksh 1,877.2 billion (16.5 percent of GDP). This revenue performance will be underpinned by on-going reforms in tax policy and

revenue administration. Ministerial AiA are projected at Ksh 207.7 billion (1.8 percent of GDP).

27. **Expenditure Projections:** Overall expenditure and net lending for FY 2019/20 are projected at Ksh 2,704.7 billion (23.8 percent of GDP). These expenditures comprise among others, recurrent of Ksh 1,657.3 billion (14.6 percent of GDP) and development of Ksh 670.9 billion (5.9 percent of GDP).

28. **Mr. Chairman,** reflecting the projected expenditures and revenues, including grants, the fiscal deficit is projected at Ksh 578.3 billion (5.1 percent of GDP) in the FY 2019/20 down from Ksh 635.5 billion (6.3 percent of GDP) in FY 2018/19.

29. The deficit excluding SGR related expenditures in the FY 2019/20 is projected at 4.6 percent of GDP.

30. The fiscal deficit in the FY 2019/20, will be financed by net external financing of Ksh 306.5 billion (2.7 percent of GDP), Ksh 277.5 billion (2.4 percent of GDP) net domestic borrowing and other net domestic receipts of Ksh 5.7 billion.

DIVISION OF REVENUE BILL, 2019 AND COUNTY ALLOCATION OF REVENUE BILL, 2019

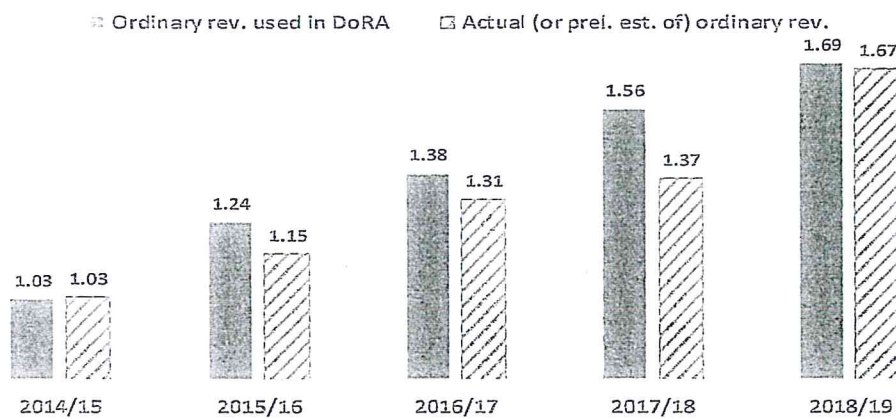
- **PROPOSED REDUCTION IN EQUITABLE SHARE OF REVENUE FOR FY 2018/19**

Underperformance in revenue raised nationally

31. Since FY 2013/14, the Division of Revenue Act (DoRA) has been prepared based on annual estimates of ordinary (shareable) revenue. However, beginning FY 2015/16, ordinary revenue outturn has fallen short of estimates. **(Chart 1)**. The cumulative shortfall now exceeds Ksh 395.5 billion; the largest shortfall of Ksh. 195.2 billion was in FY 2017/18. Ordinary revenue as a share of GDP has also declined since FY 2013/14.

32. In FY 2017/18, revenue performance was exceptionally poor with significant negative growth of 1.7 percent of GDP. Consequently, the revenue forecasting base for FY 2018/19 was overstated by approximately Ksh 136 billion. As reflected in the 2019 BPS, to reflect a lower forecasting base, the National Treasury has revised revenue forecasts for FY 2018/19 and the medium term; the forecast for FY 2018/19 is now Ksh 117.7 billion lower than the original budget estimates.

Chart 1: Estimates of ordinary revenue vs. actual revenue (Ksh trillion)



Note: For FY 2018/19, the data shown in lieu of actual/preliminary is derived from the printed estimates.

33. According to the DoRA, 2018, if actual revenue raised nationally in any year falls short of projections, the shortfall is to be borne by the National Government, to the extent of the threshold prescribed in Regulations by the Cabinet Secretary. This threshold is yet to be prescribed, hence the National Government has solely borne the above shortfalls.

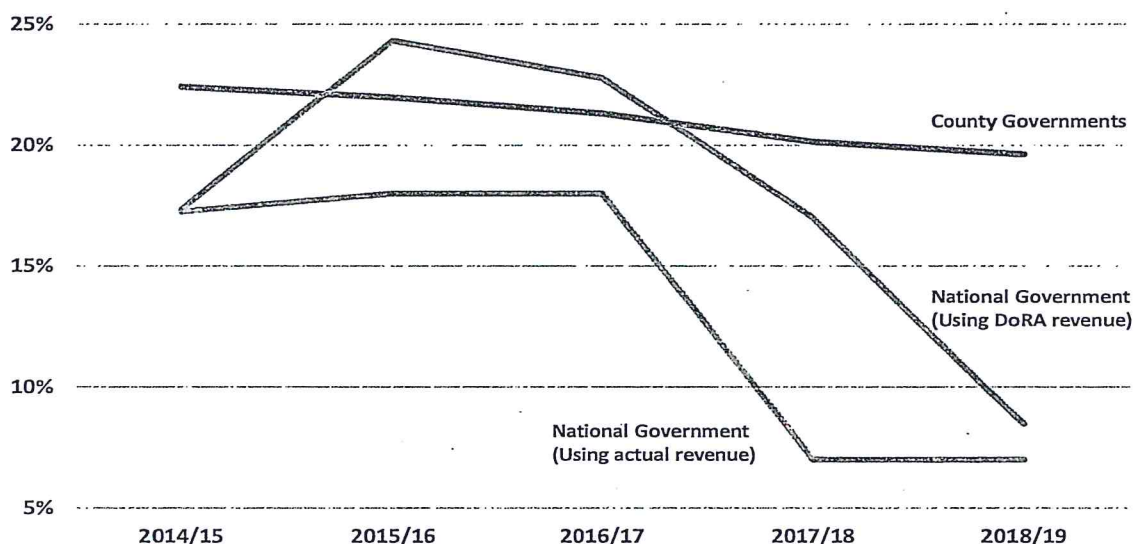
Implications for vertical revenue division

34. County Governments' equitable share grew from Ksh. 259.77 billion in FY 2014/15 to Ksh. 304.96 billion in FY 2018/19. During this period, the Counties' share remained stable at 21 percent of ordinary revenue. (Chart 2).

35. In contrast, the National Government's equitable share after implementing Article 203(1) of the Constitution declined from Ksh. 212.5 billion to Ksh. 201.8 billion over the same period.

36. Based on initial revenue estimates in the DoRA, the National Government's share dropped from 17.3 percent in FY 2014/15 to 8.5 percent in FY 2018/19. When actual ordinary revenue is retrospectively factored in, the difference between the National and the County Governments' equitable revenue share increases even further. This implies a deterioration in the vertical fiscal balance (i.e. a growing fiscal imbalance).

Chart 2: National and County Governments' revenue share as percent of ordinary revenue



Note: The National Government's share is computed after implementing provisions of Article 203(1) of the Constitution.

37. The proposed reduction to County Governments' FY 2018/19 equitable share is therefore further justified by:

- a) **The need to adjust the base for annual computation of the division of revenue:** Between FY 2015/16 and FY 2018/19, the division of revenue base has dropped by Ksh. 395.5 billion, which is the cumulative difference between estimated ordinary revenue as per DoRA and the outturn. **(See Table 1)**. Due to the fact that in FY 2018/19 the printed estimate for ordinary revenue was higher (Ksh 1,769,229 million) than the base used in DoRA (Ksh 1,688,492 million), the cumulative shortfall is actually higher, at Ksh. 476.3 billion. To date, this shortfall has been borne entirely by the National Government, hence the National Treasury's argument that this shortfall needs to be equitable shared by the two levels of Government.
- b) **The need to mitigate potential fiscal risks arising from current and future underperformance in ordinary revenue:** Notwithstanding the National

Treasury's downward adjustment of the ordinary revenue forecasting base for FY 2018/19 (i.e. from Ksh 1,688,492 to Ksh 1,651,517 million as reported in the initial draft of the BPS, 2019), seasonal-based projections show that the outturn is now likely to be even lower, at Ksh 1,534,322 million. Based on the latter forecast, the ordinary revenue shortfall in FY 2018/19 alone could be Ksh 154,170 million, pushing the cumulative shortfall since FY 2015/16 to Ksh 512,742 million. In this context, the proposed reduction in County Governments' FY 2018/19 would -- while barely addressing the larger challenge -- contribute significantly in easing the fiscal pressure on the National Government.

Table 1: Assuming shortfalls in ordinary revenue were distributed fairly, what would Counties' equitable revenue share have been?

FY	Ordinary revenue (Ksh m)		Variance in ordinary revenue		Counties' equitable share (Ksh m)	Counties' fair share of revenue shortfall (Ksh m) ³	Counties' <i>would be</i> equitable share (Ksh m)
	Estimate	Actual	Ksh m	%			
A	B	C	D = (C-B)	E = (D/B)	F	G = (15%*D)	H = (F-G)
2014/15	1,026,310	1,031,819	5,509	0.5%	226,660		
2015/16	1,242,700	1,152,972	-89,728	-7.2%	259,715	13,459	246,255
2016/17	1,380,199	1,306,568	-73,631	-5.3%	280,300	11,045	269,255
2017/18	1,560,276	1,365,063	-195,213	-12.5%	302,000	29,282	272,718
2018/19 (a) ¹	1,688,492	1,651,517	-36,975	-2.2%	314,000	5,546	308,454
2018/19 (b) ²	1,688,492	1,534,322	-154,170	-9.1%	314,000	23,126	290,875
TOTAL (a) ¹	6,897,977	6,507,939	(395,547)	-5.7%	1,382,675	59,332	1,096,682
TOTAL (b) ²	6,897,977	6,390,744	(512,742)	-7.4%	1,382,675	76,911	1,079,103

Source of data: BPS, DoRA

Notes:

1. 2018/19(a) uses actual ordinary revenue as contained in the initial BPS, 2019
2. 2018/19(b) uses actual ordinary revenue based on seasonal-based projections
3. On the basis of Art. 203(2) of the Constitution, it is assumed here that Counties' fair share of the shortfall in ordinary revenue is 15 percent. In the Division of Revenue Bill, 2019, it is recommended that the actual proportion of Counties' share of revenue shortfall be directly determined annually by the Cabinet Secretary/National Treasury and Planning

Proposed Way forward

38. In view of the above, the National Treasury proposes a reduction of county equitable share for FY 2018/19 by Ksh. 9.04 billion (i.e. from Ksh 314 billion to Ksh. 304.9 billion). It should be noted that, out of the Ksh 117.7 billion revenue shortfall in FY 2018/19, the National Government has, through various fiscal consolidation measures, absorbed Ksh 108.66 billion (or 92%) of the shortfall. Hence, Counties are only being requested to absorb Ksh 9.04 billion (which is 8%) of the shortfall. A more equitable distribution of the

shortfall would have been 85% (or Ksh 100.1 billion) to the National Government and 15% (or Ksh 17.7 billion) to the County Government, which ratio if be applied in sharing shortfalls in revenue raised nationally, can be linked to Article. 203(2) of the Constitution.

PROPOSED VERTICAL DIVISION OF REVENUE FOR FY 2019/20

39. The DoRB, 2019 proposes to allocate to County Governments Ksh.371.6 billion in the financial year 2019/20, which relative to the 2018/19 revised allocation, reflects an increase of Ksh. 4.4 billion or 1.2 percent. This allocation comprises of an equitable share of Ksh. 310 billion; additional conditional allocations from the share of national government revenue amounting to Ksh. 13.9 billion; Ksh 8.98 billion being 15% of Fuel Levy Fund collections; and, conditional allocations from loans and grants amounting to Ksh 38.7 billion.

County Governments' Equitable Share for FY 2019/20

40. The County Governments' equitable share of revenue raised nationally for the financial year 2019/20 is arrived at by adjusting the base allocation of County Governments' equitable share for 2018/19 of Ksh. 314 billion to Ksh. 304.96 billion; and subsequently growing the revised base for County Governments' equitable share for 2018/19 by Ksh 5.04 billion.

41. The proposed downward adjustment of county governments Equitable Share for the financial year 2018/19 by Ksh. 9.04 billion, by the National Treasury, is informed by shortfalls in national governments' revenue raised nationally since the financial year 2015/16. **(See Chart 1 above)**

42. After making the above adjustment, County Governments' equitable share of revenue in the financial year 2019/20 is estimated to be Ksh. 310 billion **(see Table 2)**. This allocation which represents 30 percent of the latest audited revenues for FY 2014/15 (i.e. Ksh. 1,038, billion) is above the constitutional minimum of 15 percent.

Table 2: Equitable Revenue Share Allocation to County Governments, FY 2019/20

S/N	Budget Item	Amount in Ksh. Million
A	County Equitable Revenue Share for FY2018/19	314,000
	<i>Less:</i>	
B	Adjustment based on fiscal framework (Shortfall in Revenue performance in FY 2018/19)	9,038
C	Proposed Revised County Equitable Share for FY 2018/19 ; C = (A-B)	304,962*
	<i>Add:</i>	
D	Adjustment based on fiscal framework	5,038
E	Equitable Revenue Share allocation for FY 2019/20; E= (C+D)	310,000

Source: National Treasury and Planning

* This proposed Revised County Equitable Share for FY 2018/19 is subject to approval by Parliament.

Additional conditional Allocations

43. In accordance with Article 202(2) of the Constitution, the Bill has provided for additional conditional allocation from the national government share of revenue amounting to Ksh. 25.5 billion, which includes:

- Kshs. 6.2 billion to facilitate the leasing of modern specialised medical equipment.
- Kshs. 4.3 Billion for Level-5 hospitals.
- Ksh. 900 Million to compensate County Health facilities for forgone user fees.
- Ksh. 8.98 Billion from the Road Maintenance Fuel Levy Fund. This allocation is equivalent to 15 percent of the Road Maintenance Fuel Levy Fund.
- Ksh. 2 billion for Rehabilitation of Youth Polytechnics.
- Ksh. 485 Million to supplement County allocation for the construction of headquarters in five counties.

44. In addition, County Governments have been allocated an additional Ksh. 38.7 billion from proceeds of loans and grants from development partners. This brings the total allocation to County Governments in 2018/19 to Ksh. 371.6 Billion or 36 percent of last audited revenue approved by Parliament.

Table 3: Allocation of revenue raised nationally for the financial year 2019/20

Type/level of allocation	Amount in Ksh.	Percentage (%) of 2014/15 audited and approved Revenue i.e. Ksh.1,038,035 Millions
A. National Government*	1,561,416,497,191	
Of which:		
1. <i>Leasing of Medical Equipment</i>	6,200,000,000	
2. <i>Compensation for user fees forgone</i>	900,000,000	
3. <i>Level 5 hospitals</i>	4,455,780,000	
4. <i>Supplement for construction of county headquarters</i>	605,000,000	
5. <i>Rehabilitation of Youth Polytechnics</i>	2,000,000,000	
B. Equalization Fund	5,760,000,000	0.6%
C. County equitable share	310,000,000,000	30%
D. Total shareable revenue	1,877,176,497,191	
Memo items		
1. County equitable share	310,000,000,000	
2. Additional conditional allocations(National Government share of Revenue) of which;	14,160,780,000	
2.1. <i>Leasing of Medical Equipment</i>	6,200,000,000	
2.2 <i>Compensation for user fees forgone</i>	900,000,000	
2.3 <i>Level 5 hospitals</i>	4,326,000,000	
2.4 <i>Supplement for construction of county headquarters</i>	480,000,000	
2.5 <i>Rehabilitation of Youth Polytechnics</i>	2,000,000,000	
3. Allocation from Fuel Levy Fund (15%)	8,984,062,500	
4. Conditional allocations (Loans & grants) of which:	38,655,793,666	
4.1 <i>IDA-Kenya Devolution Support Program (KDSP) Level 1</i>	1,410,000,000	
4.2 <i>IDA-Kenya Devolution Support Program (KDSP) (Level 2 Grant)</i>	4,890,000,000	
4.3 <i>IDA-Transforming Health Systems for Universal Care Project</i>	2,994,247,736	
4.4 <i>DANIDA-Universal Healthcare For Devolved System Program</i>	937,500,000	
4.5 <i>IDA-National Agriculture & Rural Inclusive Growth Project (NARIGP)</i>	7,232,719,940	
4.6 <i>EU-Instruments for Devolution Advice and Support (IDEAS)</i>	492,698,583	
4.7 <i>IDA (World Bank) - Kenya Climate Smart Agriculture Project (KCSAP)</i>	3,643,298,670	
4.8 <i>World Bank- Kenya Urban Support Program(KUSP)- UDG</i>	11,464,702,500	
4.9 <i>World Bank- Kenya Urban Support Program(KUSP)- UIG</i>	396,000,000	
5.0 <i>IDA- Water and Sanitation Development Project (WSDP)</i>	3,500,000,000	
5.1 <i>Sweden Agriculture Sector Development Programme II (ASDP II)</i>	849,626,237	
5.2 <i>EU- Water Tower Protection and Climate Change Mitigation and Adaptation Programme (WaTER)</i>	495,000,000	
5.3 <i>Drought Resilience Programme in Northern Kenya</i>	350,000,000	
Total County Allocations= (1+2+3+4)	371,676,636,166	36%

Source: National Treasury

Table 4: Evaluation of the Vertical Division in Relation to Article 203(1)

ITEM DESCRIPTION (Kshs. Millions)	FY2015/16	FY2016/17	FY2017/18	FY2018/19	FY2019/20
ORDINARY REVENUE (EXCLUDING AIA)	1,152,972	1,305,794	1,486,294	1,683,969	1,877,176
National Interest [Article 203 (1)(a)]	79,189	79,685	82,696	84,186	94,168
<i>Enhancement of security operations (police vehicles, helicopters, defense etc.)</i>	17,700.00	18,900	20,556	27,800	27,974
<i>National irrigation & fertilizer clearance</i>	12,500.00	8,700	8,880	11,775	11,103
<i>Youth empowerment</i>	17,055.00	18,544	18,544	7,442	16,226
<i>National social safety net - (for older persons, OVC, child welfare, presidential bursary, severe disability)</i>	14,354.00	16,924	17,305	26,812	26,362
<i>Primary school digital literacy program</i>	17,580.00	13,408	13,408	6,333	8,400
<i>School examination fees (KSCE & KCPE)</i>		3,209	4,003	4,024	4,103
Public debt (Art. 203 [1][b])	250,390	307,155	453,361	637,396	650,852
Other national obligations (Art. 203 [1][b])	287,240	334,108	359,077	391,878	442,627
<i>Pensions, constitutional salaries & other</i>	54,617	60,169	68,702	90,573	109,526
<i>Constitutional commissions (Art. 248(2)) i.e. CRA, SRC, NLC, NPSC, IEBC, TSC</i>	189,066	208,763	224,623	233,619	261,387
<i>Independent offices (Art. 248(3)) - i.e. AG & CoB</i>	4,720	4,723	5,177	6,412	6,336
<i>Parliament</i>	27,277	31,480	30,915	34,490	36,240
<i>Other constitutional institutions- State Law Office and DPP</i>	6,863	6,359	6,498	7,602	8,765
<i>Other statutory bodies (e.g. EACC, RPP, WPA, CAJ, IPOA, NGEC)</i>	4,697	4,855	5,484	5,724	5,937
<i>Judiciary</i>		17,759	17,678	13,458	14,437
Emergencies [Art. 203 (1)(k)]	7,245	7,245	9,294	6,419	6,418
<i>Contingencies</i>	5,000	5,000	5,000	5,000	5,000
<i>Strategic grain reserve</i>	2,245	2,245	4,294	1,419	1,418
Equalization Fund [Art. 203 (1) (g) and (h)]	6,000	6,000	7,727	4,700	5,765
BALANCE TO BE SHARED BY THE 2 LEVELS OF GOVERNMENT	522,908	571,601	574,139	559,390	677,346
County Government allocation from revenue raised nationally of which:-	273,073	295,020	314,205	322,193	324,160
<i>a) Equitable Share of Revenue</i>	259,775	280,300	302,000	304,962	310,000
<i>b) Additional conditional allocations financed from revenues raised nationally</i>	13,298	14,720	12,205	17,231	14,160
Balance left for the National Government of which :-	249,836	276,581	259,934	237,197	353,186
<i>Other statutory allocations/earmarked funds (e.g. NG-CDF, Affirmative Action)</i>	37,343	37,635	39,512	35,361	40,880

Infrastruc. Ministry

45. **Mr. Chairman**, I wish to thank you and Honourable Senators for giving me this opportunity to share with you the above information.

HENRY K. ROTICH, EGH

CABINET SECRETARY/NATIONAL TREASURY AND PLANNING

February 21, 2019



OFFICE OF THE CONTROLLER OF BUDGET

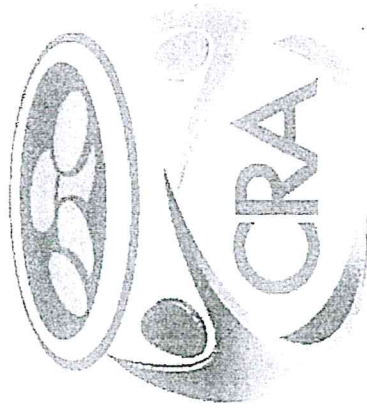
COMMENTS ON THE DRAFT 2019 BUDGET POLICY STATEMENT (BPS)

Page/Paragraph	Details
<p>Page 19; Big Four Plan Preamble and Page.20, Par.77-85</p>	<p>✦ The Government policies and programmes prioritized under the “Big Four” plan partly relate to functions assigned to county governments. Therefore, successful implementation will require collaboration between the two levels of government.</p> <p>While the BPS covers collaboration in two areas, namely; Universal Health Coverage and Affordable and Decent Housing, appropriate clarification of collaboration in all other areas such as; Value Addition and Raising the Share of Manufacturing Sector to GDP; and Enhancing Food and Nutrition Security will be important and will enhance effective delivery of priority policies and programmes through devolution. Further, it will mitigate the risk of duplication and possible intergovernmental conflict that could negatively affect realization of the “Big Four” plan.</p> <p>✦ Recommendation: The BPS should clarify areas of collaboration with county governments in the implementation of the “Big Four” Plan to enable county governments consider and capture the same in County Fiscal Strategy Papers (CFSPs).</p>

Page/Paragraph	Details
Page 20; Big Four "The Manufacturing Sector"	<p>❖ In order to boost the manufacturing sector, the government intends to build textile industries, leather parks, support agro-processing, support production of construction materials, transform the blue economy and re-establish the automobile industry to support job creation.</p> <p>However, the Draft BPS has not highlighted why this sector did not perform optimally in the past. Experience and challenges that faced the sector such as; cheap imports of second hand clothes, food commodities like sugar, maize and fish that have subdued the local industry should be highlighted in order to enhance success. The BPS should also identify appropriate measures to be taken in order to address these challenges.</p>
Page 22, Par.88 and Page 40-41, Part 2.3.6.1	<p>❖ To improve food security, the Government will increase maize production from 40 million to 67 million (90 kg) bags. In addition, the Government has set aside USD.14 million to increase strategic food reserves to 8 million bags in the medium term.</p> <p>Whereas the Government plans to allocate funds for this important activity, accountable use of the funds is paramount. The sub-sector has recently experienced accountability challenges and there may be need to emphasise accountability.</p>
Page 44, Revenue projections	<p>❖ Revenue is projected to increase by Kshs.249.4 billion to Kshs.2.08 trillion in FY2019/20 from Kshs.1.83 trillion in FY 2018/19. Compared to historical trends, the projected increase may be unrealistic and therefore unachievable.</p> <p>It may therefore, be necessary to revise this projection to a realistic amount.</p>

	Page/Paragraph	Details
5	Page 81. Sustainability of debt	<p>✦ Two internationally recognized public debt indicators have been used, which show the country's Present Value (PV) of public debt to Gross Domestic Product (GDP) was 60.6 per cent in 2018 compared to the recognized threshold of 70 percent. Similarly, the PV of the public debt to Revenue was 292 per cent in the same period compared to a recognized threshold of 300 per cent. Further, page 76 of the BPS indicates that Kenya's risk to debt distress has been raised from low to moderate. Thus stress test thresholds could be breached if there are external shocks or abrupt changes in macroeconomic policies.</p> <p>Given the foregoing, it may be necessary to consider other internationally recognized public debt indicators. Other ratios as stated by World Bank's Country Policy and Institutional Assessment (CPIA) include; the PV of PPG</p>
6	Page 70	<p>✦ The Division of Revenue (Amendment) Act, 2018 allocated Kshs.314 billion as equitable share of revenue raised nationally to counties for the FY 2018/19, while the Draft 2019 BPS contains a figure of Kshs.304.96 billion. No explanation is provided for this variance given that that DORA (Amendment), 2018 is still in force.</p> <p>We suggest that you provide an explanation to clarify the variance.</p>

10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36 37 38 39 40 41 42 43 44 45 46 47 48 49 50 51 52 53 54 55 56 57 58 59 60 61 62 63 64 65 66 67 68 69 70 71 72 73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92 93 94 95 96 97 98 99 100 101 102 103 104 105 106 107 108 109 110 111 112 113 114 115 116 117 118 119 120 121 122 123 124 125 126 127 128 129 130 131 132 133 134 135 136 137 138 139 140 141 142 143 144 145 146 147 148 149 150 151 152 153 154 155 156 157 158 159 160 161 162 163 164 165 166 167 168 169 170 171 172 173 174 175 176 177 178 179 180 181 182 183 184 185 186 187 188 189 190 191 192 193 194 195 196 197 198 199 200 201 202 203 204 205 206 207 208 209 210 211 212 213 214 215 216 217 218 219 220 221 222 223 224 225 226 227 228 229 230 231 232 233 234 235 236 237 238 239 240 241 242 243 244 245 246 247 248 249 250 251 252 253 254 255 256 257 258 259 260 261 262 263 264 265 266 267 268 269 270 271 272 273 274 275 276 277 278 279 280 281 282 283 284 285 286 287 288 289 290 291 292 293 294 295 296 297 298 299 300 301 302 303 304 305 306 307 308 309 310 311 312 313 314 315 316 317 318 319 320 321 322 323 324 325 326 327 328 329 330 331 332 333 334 335 336 337 338 339 340 341 342 343 344 345 346 347 348 349 350 351 352 353 354 355 356 357 358 359 360 361 362 363 364 365 366 367 368 369 370 371 372 373 374 375 376 377 378 379 380 381 382 383 384 385 386 387 388 389 390 391 392 393 394 395 396 397 398 399 400 401 402 403 404 405 406 407 408 409 410 411 412 413 414 415 416 417 418 419 420 421 422 423 424 425 426 427 428 429 430 431 432 433 434 435 436 437 438 439 440 441 442 443 444 445 446 447 448 449 450 451 452 453 454 455 456 457 458 459 460 461 462 463 464 465 466 467 468 469 470 471 472 473 474 475 476 477 478 479 480 481 482 483 484 485 486 487 488 489 490 491 492 493 494 495 496 497 498 499 500 501 502 503 504 505 506 507 508 509 510 511 512 513 514 515 516 517 518 519 520 521 522 523 524 525 526 527 528 529 530 531 532 533 534 535 536 537 538 539 540 541 542 543 544 545 546 547 548 549 550 551 552 553 554 555 556 557 558 559 560 561 562 563 564 565 566 567 568 569 570 571 572 573 574 575 576 577 578 579 580 581 582 583 584 585 586 587 588 589 590 591 592 593 594 595 596 597 598 599 600 601 602 603 604 605 606 607 608 609 610 611 612 613 614 615 616 617 618 619 620 621 622 623 624 625 626 627 628 629 630 631 632 633 634 635 636 637 638 639 640 641 642 643 644 645 646 647 648 649 650 651 652 653 654 655 656 657 658 659 660 661 662 663 664 665 666 667 668 669 670 671 672 673 674 675 676 677 678 679 680 681 682 683 684 685 686 687 688 689 690 691 692 693 694 695 696 697 698 699 700 701 702 703 704 705 706 707 708 709 710 711 712 713 714 715 716 717 718 719 720 721 722 723 724 725 726 727 728 729 730 731 732 733 734 735 736 737 738 739 740 741 742 743 744 745 746 747 748 749 750 751 752 753 754 755 756 757 758 759 760 761 762 763 764 765 766 767 768 769 770 771 772 773 774 775 776 777 778 779 780 781 782 783 784 785 786 787 788 789 790 791 792 793 794 795 796 797 798 799 800 801 802 803 804 805 806 807 808 809 810 811 812 813 814 815 816 817 818 819 820 821 822 823 824 825 826 827 828 829 830 831 832 833 834 835 836 837 838 839 840 841 842 843 844 845 846 847 848 849 850 851 852 853 854 855 856 857 858 859 860 861 862 863 864 865 866 867 868 869 870 871 872 873 874 875 876 877 878 879 880 881 882 883 884 885 886 887 888 889 890 891 892 893 894 895 896 897 898 899 900 901 902 903 904 905 906 907 908 909 910 911 912 913 914 915 916 917 918 919 920 921 922 923 924 925 926 927 928 929 930 931 932 933 934 935 936 937 938 939 940 941 942 943 944 945 946 947 948 949 950 951 952 953 954 955 956 957 958 959 960 961 962 963 964 965 966 967 968 969 970 971 972 973 974 975 976 977 978 979 980 981 982 983 984 985 986 987 988 989 990 991 992 993 994 995 996 997 998 999 1000



COMMISSION ON REVENUE ALLOCATION

**Comments on the Budget Policy Statement
(BPS) 2019**

21st Feb 2019

CRA's guiding framework for Revenue Sharing aligns to the fiscal framework but within the Constitutional requirements completely overlooked. (page 65)



	Budget Items	Kshs.bn
1	Principles for revenue sharing between national and county governments	
	a) Current Level of funding of Devolved Functions	314.0
	b) Unfunded Mandates	
	i. County Roads	-
	ii. Salaries for County Library Staff	-
	c) New Functions	-
	d) Provision for sustainability and Growth in Services	
	i. Adjustment for Inflation (3 year average inflation 6.9%)	21.7
	ii. Growth Factor (Population growth rate 1.4%)	-
2	Total equitable share to county government for FY 2019/20	335.7
3	Equalisation Fund (0.5% of 2014/15 audited accounts)	5.2
4	Total equitable share to National Government	1,529.5

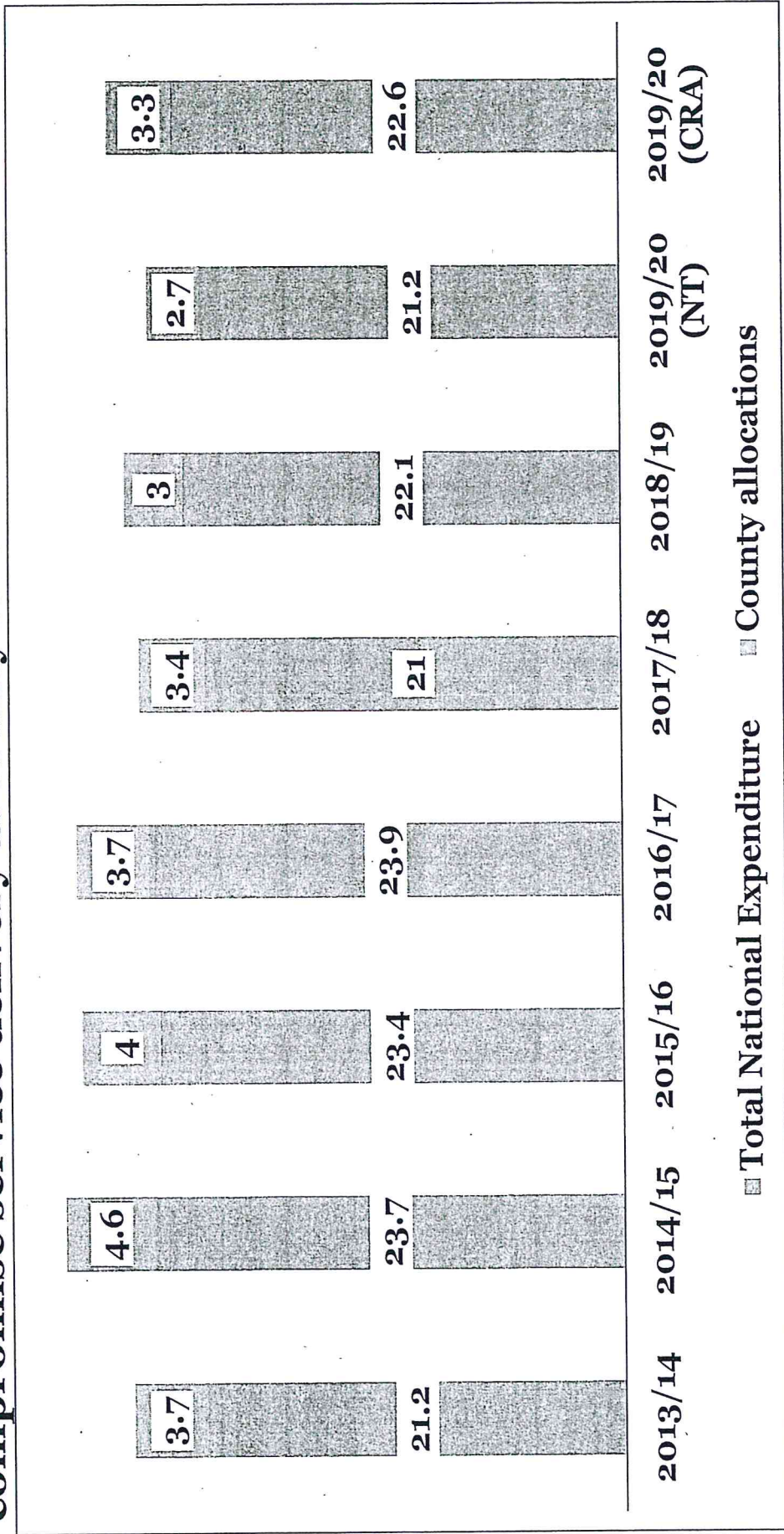
Growth in the shares of revenue to National and County governments...

	2018/19	2019/20
Ordinary revenues	1,651.5	1,877.2
Less: County allocation	305.0	310.0
Interest payment	386.0	426.2
Pension	90.6	109.5
Equalisation fund	4.7	5.8
National government share	865.2	1,025.7
Growth in National government's share		18.6%
Growth in county allocation		1.6%

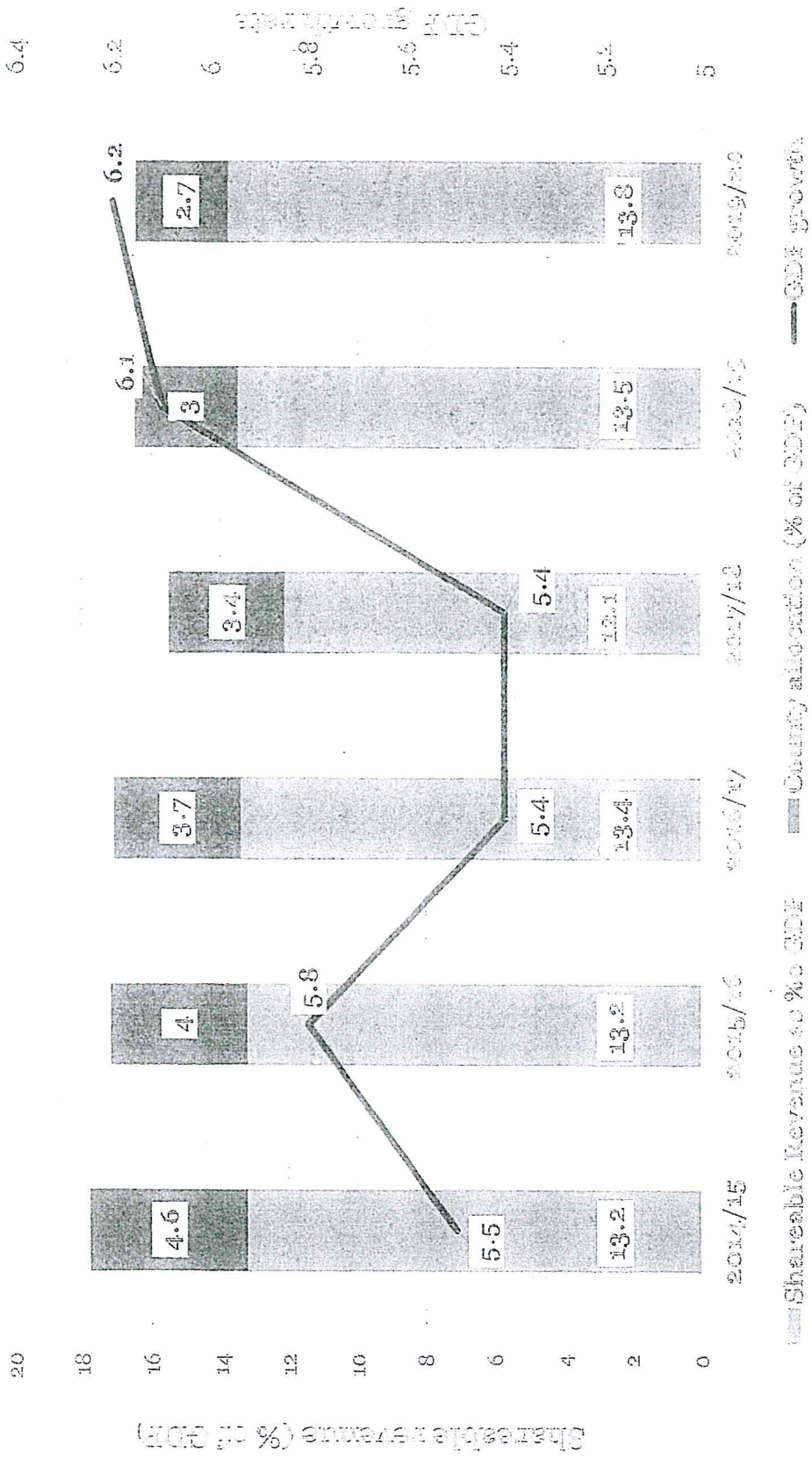
There is need for a more equitable sharing of revenues

Budget items	CRA recommendation	National Treasury: BPS 2019
Adjusted baseline	314,000	305,000
1 County Government	335,666	310,000
2 Equalisation fund	5,200	5,800
3 National government	1,529,534	1,561,200
Projected shareable revenue	1,870,400	1,877,200
Percentage change in county allocation	6.9%	1.6%

An equitable proposal of sharing revenues need not compromise service delivery at county level...



Relative County allocations are declining



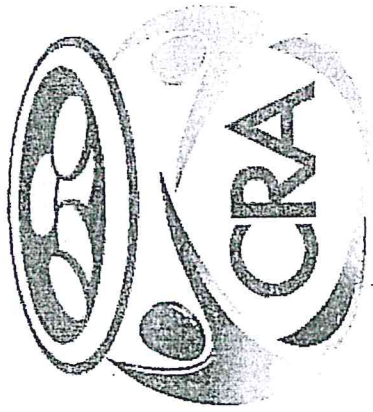
█ Shareable Revenue (% of GDP) █ County Allocation (% of GDP) — Total Allocation (% of GDP)

Other issues

- Pages 38 & 45 (174)
- Low Development spending and wage bill thresholds, in some counties emanates from inherited staff , an issue which is still pending at Summit
- Page 64 chart 4.
- This chart is misleading...if county government share is <20% National government < 20% which government takes the difference
- The correct representation is on page 45 Table 3.1 County governments expenditure is 11% of total expenditure .

Recurrent Expenditure Ceilings

- CRA recommends, for Parliament Approval, recurrent expenditure ceilings for county governments
- Ceilings are largely based on Salaries Remuneration Commission (SRC) determinations on salaries and benefits for County staff
- There is a court ruling on Petition No. 9 of 2018 quashing Gazette Notice 6518 of 2017.
- CRA has analysed growth of recurrent expenditure for counties in relation to growth in the resource envelope.
- CRA is seeking to rationalize the provisions for County Recurrent Expenditure in line with overall growth figures and Fiscal Consolidation policy adopted by the country.



Thank you

MINUTES OF THE 66TH SITTING OF THE STANDING COMMITTEE ON INANCE AND BUDGET HELD ON WEDNESDAY 20TH FEBRUARY 2019 AT COUNTY HALL, GROUND FLOOR BOARDROOM FROM 11:00 A.M.

PRESENT

1. Sen. Mohamed Maalim Mahamud, M.P. - Chairperson
2. Sen. Isaac Mwaura, M.P. - Vice Chairperson
3. Sen. Moses Wetang'ula, M.P. - Member
4. Sen. Mutula Kilonzo Junior, M.P. - Member
5. Sen. (Dr.) Abdullahi Ali Ibrahim - Member
6. Sen. Farhiya Haji, M.P. - Member

ABSENT WITH APOLOGY

1. Sen. Aaron Cheruiyot, M.P. - Member
2. Sen. Boniface Mutinda Kabaka, M.P. - Member
3. Sen. Rose Nyamunga, M.P. - Member

SECRETARIAT

1. Mr. Christopher Gitonga -Clerk Assistant
2. Mr. Charles Ngatia -Clerk Assistant
3. Mr. Martin Masinde -Senior Deputy Director, PBO
4. Ms. Julie Mwithiga -Fiscal Analyst
5. Mr. Charles Atamba -Research Officer
6. Mr. Patrick Murindo -Serjeant-At-Arms
7. Mr. Stephen Nyakuti -Audio Recording Officer

MIN. NO. 320/02/2019:

PRELIMINARIES

The meeting was called to order at 11:10 a.m. and there followed a word of prayer.

MIN. NO. 321/02/2019:

ADOPTION OF AGENDA

The agenda of the meeting was adopted after it was proposed and seconded by Sen. Farhiya Haji, M.P. and Sen. Moses Wetang'ula, M.P. respectively.

MIN. NO. 322/02/2019:

CONSIDERATION OF 2019 BUDGET POLICY STATEMENT (BPS)

The Chairperson informed the Committee that the purpose of the meeting was to consider the 2019 BPS. Thereafter, the Secretariat briefed the Committee on the provisions of the 2019 Budget Policy Statement (BPS).

**MIN.NO. 329/02/2019: MEETING WITH STAKEHOLDERS TO DELIBERATE
ON 2019 BPS**

After introductions, The Chairperson welcomed the representatives from Commission on Revenue Allocation (CRA) to make their presentation.

CRA informed the Committee as follows-

- a) The draft BPS proposed a fiscal consolidation which would reduce the fiscal deficit to -3.3% of GDP by 2021/22 while public debt would reduce to 46.4% of the GDP.
- b) There was a concern over the projected economic growth (projected 6.2%) while the revenue performance was on decline. GDP growth in 2018/19 was 6.1% while projected 2019/2020 would be 6.2% whereas the revenue growth would be at constant growth of 16.5% of the GDP.
- c) The targeted 2018/19 shareable revenue was Kshs. 1.652 trillion while projected for 2019/2020 was Kshs. 1.877 trillion. However, the growth in equitable share for counties was (not proportional) marginally increased.
- d) The Commission had developed a framework which may be adopted for determining the vertical division of revenue. The framework adjusts the baseline by adding unfunded functions and 3 year average inflation which was 6.9%.
- e) The BPS was erroneous in indicating the county equitable share for 2018/19 as Kshs 305 billion whereas the DoRA, 2018 was clear it was Kshs 314 billion. Secondly, Kshs 310 billion to counties was not based on any parameter.
- f) The relative county allocations compared to GDP had been on declining trend. 2017/18 it was 3.4%, 2018/19 it was 3% and the BPS proposal would further reduce it to 2.7%.
- g) Noting that the projected revenue would be Kshs. 1.877 trillion, the proposal of Kshs. 310 billion would grow the national share by 18.6% while county equitable share would grow by 1.6%.
- h) The Commission recommendation was that the county equitable share baseline (Kshs. 314 billion) be adjusted by 3-year average of 6.9% that would translate to Kshs. 335.666 billion.
- i) The low development expenditure in counties was attributable to inherited staff, a matter which was pending before the Summit.

- j) There was need for definition on what '*National Interest*' entails, since some of the devolved functions may also constitute the national interest whereas some national government were been categorised as national interest.
- k) The Commission recommend that recurrent expenditure ceilings for county government should remain unchanged for the FY 2019/2020 with a view of rationalisation of the provisions for county recurrent expenditure with overall growth figures and fiscal consolidation policy adopted by the country.

Office of the Controller of Budget

The representatives informed the Committee as follows-

- a) The BPS did not clarify the areas of collaboration between the national government and county government noting that 'Big Four Agenda' was basically on some devolved functions. There was risk of duplication and intergovernmental conflict which would hinder the realisation of the Big four plan.
- b) The manufacturing sector was not achieving its target. The BPS should have identified the challenges and appropriate measures to address the sector.
- c) There was a proposal to increase maize production from 40 million to 67 million (90Kg) bags. Further, about 1,400 million had been set aside to increase strategic food reserves to 8 million bags in the medium term. However, there was need to address issues of accountability and governance in the sub-sector.
- d) The projected revenues for 2019/20 was unrealistic, it may be unachievable based on the historical trends
- e) The public debt indicators used (present Value of public debt to GDP and present value of public debt to revenue) were not adequate. There was need to consider use of other indicators such as World Bank's Country Policy and Institutional Assessment (CPIA).
- f) The DoRA, 2018 allocated Kshs. 314 billion to counties but the BPS had unsubstantiated figure of Kshs. 305. The variance was not substantiated.

ICPAK- The Institute of Certified Public Accountants of Kenya

The representatives made their presentation on 2019 BPS as follows-

a) Per-capita income and job creation

- i) The value of goods and services produced raised per capital income from Kshs. 113,539 in 2013 to 2013 to an estimated Ksh 190,521 in 2018, a 67.8 percent increase. However, there was mismatch on data on informal sector. There was need for methodologies/system for KRA to use in capturing data on informal sector for purposes of tax revenue. That would enable the expansion of tax base.
- ii) They recommended improvement of the regulatory environment for the informal sector to support stability and growth of MSMEs to overcome start-up challenges and contribute to economic development.
- iii) Further, device mechanisms for identification of informal sector players to contribute to tax revenue. Formalize the informal sector by limiting cash-based transactions as a means to capture all business activities in the economy

b) Net Foreign Assets

The DBPS 2019 indicates Kenya's Net Foreign Assets (NFA) grew by 22.3% yet with the increase in public debt and the import bill indicated otherwise. That required to be revised for clarity.

c) Modernized Income Tax Bill

Legislation, including subsidiary legislation, traces its foundation on an agreed policy framework, to establish the most appropriate approach to resolve a problem.

As such, the review of the Income Tax Act should be predicated on a comprehensive n Income Tax policy. The income tax policy should be developed to guide the review process of the Income Tax Act. Further, it was important to envisage the entire of the tax frame and develop an overarching tax policy ahead of any taxation.

d) Real GDP Growth

There's need to consider more realistic growth targets given the economy's vulnerability to shocks. The World Bank (through the Kenya Economic Update 2018) gave lower growth rates compared to those given in the BPS 2019, that Kenya's economy is expected to grow by 5.7% FY 2018/19, 5.8% FY 2019/20 and 6.0% in 2020/21. Since expected economic growth is a factor in subsequent macro-economic

and fiscal projections, there was need for a more prudent approach to avoid over-projecting the state of the economy.

e) Government Policies to support Fiscal Consolidation

There is need to re-ignite private sector led growth, in this regard, fiscal consolidation must promote economic growth. Further, fiscal consolidation needs to be recalibrated towards recurrent spending such as – lowering of transfers to state owned enterprises, cleaning and regular audit of the payroll register, keeping wages, salaries and allowance adjustments in line with recommendations from the Salaries and Remuneration Commission (SRC). In addition, fiscal policy should be geared towards regenerative expenditure and not consumptive expenditure.

f) Big Four Plan

To support the manufacturing sector, the Government should continue to promote provision of financial support and credit to the Micro and Small Medium Enterprises (MSMEs).

To attain food security, the Government should continue to implement measures in the agricultural sector that would ensure food and nutrition security including food storage and irrigation services.

To achieve Universal Health Coverage (UHC) the government should complete reconfiguration and digitization of NHIF to ensure the system is ready for roll out before fully implementing the UHC and increase the health budgetary allocation to the recommended 15% of the total annual budget as recommended by the AU under the auspices of Abuja declaration.

The government should consider incentive to businesses by way of either tax credits or allow for the contributions made to National Housing Development Fund, for instance it may be treated as tax allowable. This will be a useful relief to businesses which were already to conduct business.

Other issues that affect the Big Four were Monitoring and evaluation system, idle land tax, Block chain technology, access to water, sports fund, and consolidation of Uwezo Fund, Youth Enterprise Development Fund and Women Enterprise Development Fund. There was need for strengthening governance and fight against corruption. Further, realism of revenue forecast its ambitious and leads to budget deficits

g) Own Source Revenue

There was need to fast-track implementation of the OSR Policy as developed by the National Treasury for effective revenue management across the Counties. Secondly, integration of the different systems of revenue collection and management. IFMIS has been very vital in entrenching accountability in financial management.

The County Treasuries should be continuously review the performance of revenue collection vis-à-vis targets and shall include a status report in the published Quarterly and Annual reports. There should be a standardized ICT-based system which should provide real time revenue information in a consistent manner to enable consolidation and analysis, as well as periodic reports for use by the National Treasury, the CoB, the CRA and the Office of the Auditor General, and easily accessible by the general public. Consideration of positioning the Kenya Revenue Authority as the collector of county revenues to support revenue collection should be done through proper mechanisms.

h) Absorption of Development Funds

The low absorption rates of approved budgets were a pointer to weak budgeting process in relation to over-ambitious and unrealistic revenue projections which were unachievable. As a result of the above, erratic exchequer releases serve to compound the problem. There was need to rethink the budgeting frame more specifically around revenue projections since this had consequent effect on budget implementation.

i) Pending bills

The Auditor General Reports, had noted a continuous increase in pending bills in the recent times. There was need of adopting proper accounting standards. Globally, under cash accounting, transactions are recognized only when the associated cash is received or paid, and economic events are not reported if there is no immediate exchange of cash. Accrual accounting therefore offers several benefits: accrual-based fiscal reports provide a more comprehensive view of the government's financial performance and the cost of government activities. Accrual accounts provide a more complete picture of the financial position of the public sector as a whole;

Further, reporting stocks and flows within an integrated accounting framework based on internationally-accepted standards such as IPSAS, accrual accounting can improve the reliability and integrity of government financial data.

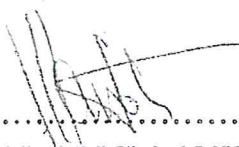
There was need of focusing greater attention on the part of policymakers and the public on the acquisition, disposal, and management of government assets, liabilities, and contingent liabilities.

j) Absence of audit committees

There was need to continuously lobby County entities to establish independent audit committees. Capacity building/ enhancement of established audit committees on their roles should be emphasized. The CRA's proposals of a variable under the Fiscal Prudence parameter in the revenue sharing formula should be encouraged. This will obligate counties to establish and operationalize effective Audit Committees.

MIN.NO. 330/02/2019: DATE OF THE NEXT MEETING AND ADJOURNMENT

There being no other business the meeting was adjourned at 1:05 pm.

SIGNATURE.....
(CHAIRPERSON: SEN. (ENG) MOHAMED MAALIM MAHAMUD)

DATE.....

List of In-attendance Stakeholders

Commission on Revenue Allocation

- | | | |
|---------------------------|---|---------------------------------|
| 1. Dr. Jane Kiringai | - | Chairperson |
| 2. Mr. Kishanto Ole Suuji | - | Commissioner |
| 3. Mr. George Ooko | - | CEO/ Secretary |
| 4. Ms. Sally Yagan | - | Deputy/ Director Fiscal Affairs |
| 5. Ms. Naomi Mathenge | - | Manager Research |
| 6. Ms. Jecinta Hezron | - | P.A Chairperson |

Controller of Budget

- | | | |
|-----------------------|---|---------------------------------|
| 1. Mr. Joshua Musyimi | - | Director, Research and Planning |
| 2. Mr. Martin Musau | - | Research Officer |

Institute of Certified Professional Accountants of Kenya

- | | | |
|-----------------------|---|--------------------|
| 1. Ms. Dorcus Gichira | - | Branch Coordinator |
| 2. Mr. Evance Juma | - | PPR Analyst |
| 3. Mr. David Isiye | - | ICPAK |
| 4. Mr. Elias Wakhisi | - | ICPAK |
| 5. Mr. Fred Riaga | - | ICPAK |
| 6. Mr. Hillary Onami | - | ICPAK |

MINUTES OF THE 68TH MEETING OF THE SENATE STANDING COMMITTEE
ON FINANCE & BUDGET HELD ON FRIDAY, 22ND FEBRUARY, 2019 AT
SIMBA LODGE, NAIVASHA AT 9:00 AM.

PRESENT

1. Sen. (Eng) Mohamed M. Mahamud, CBS, MP - Chairperson
2. Sen. (Dr) Isaac Mwaura, CBS, MP - Vice Chairperson
3. Sen. Moses Wetangula, MP -Member
4. Sen. (Dr) Ali Abdullahi Ibrahim, CBS, MP - Member
5. Sen. CPA Farhiya Haji, MP - Member

ABSENT WITH APOLOGY

1. Sen. Aaron Cheruiyot MP -Member
2. Sen. Mutula Kilonzo Junior, MP - Member
3. Sen. (Dr) Rose Nyamunga, MP - Member
4. Sen. Boniface Mutinda Kabaka, MP - Member

IN-ATTENDANCE

SENATE SECRETARIAT

1. Mr. Njenga Njuguna - Director, Committee Services
2. Mr. Martin Masinde - Deputy Director, Budget Office
3. Mr. Fredrick Muthengi - Chief Fiscal Analyst
4. Mr. Christopher Gitonga - Clerk Assistant
5. Mr. Charles Ngatia - Clerk Assistant
6. Ms Lucy Radoli - Legal Counsel
7. Ms. Julie Mwithiga - Budget Officer
8. Mr. Elly Atamba - Researcher
9. Mr. Patrick Murindo - Sergeant At Arms
10. Mr. Stephen Nyakuti - Audio Officer

IN-ATTENDANCE-NATIONAL TREASURY AND PLANNING

1. Hon. Nelson Gaichuihie - CAS
2. Mr. Fred Owegi - Advisor
3. Mr. Samuel Kiiru - DCE
4. Mr. John K. Njera - DCE
5. Mr. Musa Kathanje - Director

MIN. NO. 331/02/2019: Preliminaries

The Chairperson called the meeting to order at 9.57 am and there followed a word of prayer. He welcomed Members to the meeting and informed them that officials from the National Treasury would make a presentation on the 2019 Budget Policy Statement (BPS).

MIN.NO. 332/02/2019: Presentation by the National Treasury on the 2019 BPS

The Chief Administrative Secretary (CAS), Hon. Nelson Gaichuhie, conveyed the apologies of the Cabinet Secretary for The National Treasury and Planning who was engaged in other official duties.

The CAS presented the remarks of the Cabinet Secretary for The National Treasury and Planning on the 2019 BPS which highlighted the following issue-

1. The theme for 2019 BPS is “*Creating Jobs, Transforming Lives- Harnessing the Big Four*”. The policy prioritizes investments in the Big four Agenda, namely: Manufacturing for Job Creation, Food and Nutrition Security, Universal Health Coverage and Affordable Decent Housing.
2. **Performance of the Economy:** Despite the fact that the economy is strong and resilient at an estimated growth of 6.2 per cent for 2019/20 up from 6.0 per cent in 2018/19 FYs, the Global Economic Growth is projected to be weakening at 3.5 per cent in 2019. Notably, the Sub-Saharan African Region is expected to register a growth of 3.5 per cent for the same period as a result of commodity prices and access to capital markets. The Exchange Rate remains stable and competitive against the major international currencies, which has been supported by a low and stable inflation rate. Consequently, short term interest rates have remained fairly low and stable due ample liquidity in the money market.
3. **Budget Implementation:** Implementation of programmes in the first quarter of FY 2018/19 was slow due to budget rationalization to align expenditure priorities to revenues after amendments to the Finance Bill, 2018. The revised total revenue is projected at Kshs. 1,852.6 billion out of which ordinary revenue is projected at Kshs. 1,672.2 billion. The projected total revenue for FY 2019/20 is projected at Kshs. 2,080.9 billion whereas the projected ordinary revenue is projected at Kshs. 1,877.2 billion. The overall expenditure and net lending for FY 2019/20 is projected at Kshs. 2,704.7 billion.
4. **Reforms to Support Fiscal Consolidation Plan:** The fiscal framework supports fiscal consolidation plan that will see a gradual reduction in fiscal deficit from 7.2 per cent in FY 2017/18 to 3.1 per cent of GDP over the medium term in line with the East African Monetary Union Protocol target of 3.0 per cent of GDP. The consolidation will be supported by enhanced revenue mobilization from private sector players, development partners and rationalization of recurrent expenditure.
5. **County Governments Equitable Share FYs 2018/19 and 2019/20:** In view of underperformance in revenue raised nationally, the National Treasury proposes a reduction

of County Equitable share for 2018/19 by Kshs. 9.04 billion (from Kshs. 314 billion to Kshs. 304 billion). Furthermore, the proposed county equitable share for FY 2019/20 is Kshs. 310 billion. The justification for the downward adjustment of county governments equitable share for FY 2018/19 by Ksh 9.04 billion is informed by shortfalls in national government's revenue raised.

6. Revenue collection projection by the Kenya Revenue Authority (KRA) is expected to increase by Ksh. 140 billion though there has been poor performance in collection of corporation tax but had sought technical assistance from the International Monetary Fund (IMF) on ways of improving collection.
7. The National Treasury had sought to assist counties to increase their local revenue collection and had commissioned the World Bank (WB) which had undertaken a study which indicated that counties had a potential to collect Ksh, 100 billion.

Committee Observations on the Presentation by the National Treasury

1. There was a serious mismatch of projection in economic growth and projection in revenue collection.
2. The component of national interest in budgeting ought to be clearly defined and should be a consultative process between the two levels of government.
3. The National Treasury should increase the tax collection base especially by reducing the tax exemptions given.
4. The Committee disagreed with the proposal to reduce the equitable share to counties by Ksh. 9.04 billion in FY 2018/19 noting that the justification for the reduction was a shortfall in revenue collection which pursuant to section 5 of the Division of Revenue Act, 2018, was to be borne by the national government.
5. The Debt management strategies being applied by National Treasury were not sustainable despite the justification given.
6. Concern that the recommendations of the Senate incorporated in the 2019 BPS may not be implemented by the National Treasury.

MIN.NO. 333/02/2019: ADJOURNMENT AND DATE OF NEXT MEETING

There being no other business the meeting was adjourned at 1:30 p.m. until Friday 22nd February, 2019 at 2:30 p.m.

SIGNATURE.....

(CHAIRPERSON: SEN. (ENG) MOHAMED MAALIM MAHAMUD)

DATE.....25/02/2019

MINUTES OF THE 69TH MEETING OF THE SENATE STANDING COMMITTEE
ON FINANCE & BUDGET HELD ON FRIDAY, 22ND FEBRUARY, 2019 AT
SIMBA LODGE, NAIVASHA AT 2:30 P.M.

PRESENT

1. Sen. (Eng) Mohamed M. Mahamud, CBS, MP - Chairperson
2. Sen. (Dr) Isaac Mwaura, CBS, MP - Vice Chairperson
3. Sen. Moses Wetangula, MP -Member
4. Sen. (Dr) Ali Abdullahi Ibrahim, CBS, MP - Member
5. Sen. CPA Farhiya Haji, MP - Member

ABSENT WITH APOLOGY

1. Sen. Aaron Cheruiyot MP -Member
2. Sen. Mutula Kilonzo Junior, MP - Member
3. Sen. (Dr) Rose Nyamunga, MP - Member
4. Sen. Boniface Mutinda Kabaka, MP - Member

IN-ATTENDANCE

SENATE SECRETARIAT

1. Mr. Njenga Njuguna - Director, Committee Services
2. Mr. Martin Masinde - Deputy Director, Budget Office
3. Mr. Fredrick Muthengi - Chief Fiscal Analyst
4. Mr. Christopher Gitonga - Clerk Assistant
5. Mr. Charles Ngatia - Clerk Assistant
6. Ms Lucy Radoli - Legal Counsel
7. Ms. Julie Mwithiga - Budget Officer
8. Mr. Elly Atamba - Researcher
9. Mr. Patrick Murindo - Sergeant At Arms
10. Mr. Stephen Nyakuti - Audio Officer

MIN. NO. 334/02/2019: PRELIMINARIES

The Chairperson called the meeting to order at 2.42 pm and there followed a word of prayer. The Chairperson informed Members that the Council of Governors had requested for a meeting with the Committee on Monday 25th February, 2018.

**MIN.NO. 335/02/2019: CONSIDERATION OF SUBMISSIONS FROM
STAKEHOLDERS**

1. Submission by Council of Governors (COG)

The Secretariat took the Committee through the submission from the COG which underscored the following issues in the 2019 Budget Policy Statement (BPS)-

- (a) The base figure for equitable share to the counties in should be Kshs. 314 billion and not Ksh. 304 billion;
- (b) Any shortfall in revenue raised nationally ought to be borne by the National Government as provided for in the Division of Revenue Act, 2018
- (c) The County equitable share for FY 2019/20 should therefore be Kshs. 343.7 billion comprising of adjustment base of Kshs. 314 billion; with Kshs. 8.7 billion worth of unfunded functions (such as transfer of 31,000 Km of roads and library services) and 6.9 per cent average of three year annual inflation.
- (d) To achieve stability and predictability in implementation of County budgets, there is need to use an average inflation rate. This will ensure the functions of both the national and county governments are not subjected to volatile budgets. The Council recommends the use of an average inflation rate to cater for increase in service costs.
- (e) Nine (9) counties were expected to lose an accumulative amount of Kshs. 7.3 Billion worth of allocation when 3rd generation revenue formulae is applied against the CRA equitable share proposal of Kshs. 335.7 billion. If the National Treasury proposal of Kshs. 310 billion is adopted, counties would have lost Kshs. 25 billion before the formula is even applied.

Committee Observations on the Submission by COG

- (a) There is need for increase in equitable share to the counties, however, the increase should be support by good governance and prudent use of the funds in the counties.
- (b) There was need to review the Public Finance Management (PFM) Act so as to clarify on the trigger/initiator of the process of stoppage of funds to counties;
- (c) The Committee resolved to meet with the COG on Monday 25th February, 2019 at 12 noon to engage on the 2019 BPS.

2. Submission by International Budget Partnership (IBP)

The Secretariat took the Committee through the submission of the IBP. The memorandum highlighted key issues and made the following recommendations:

- (a) **Ballooning Wage bill-** The Senate and the National Treasury should take advantage of the current review of the equitable revenue sharing mechanism to help counties address challenges from inherited staff costs;
- (b) **Finalization of spending plans-**Finalization of the detailed budgets should entail scrutiny to curtail spending on non-productive areas and ensure non-productive areas and ensure resources are directed to priority programs;
- (c) **County revenue collection potential report** should be published and publicized to help inform public debate on county revenue especially in relation to their Finance Bills. The Own-Source Revenue Potential and Tax Gap Study of Kenya's County Governments provides the first window into fiscal capacity at the county level. This set of information is critical as discussion on having a county own source revenue policy is finalized. In addition, the on-going review of the second equitable revenue sharing formula would benefit from this data as part of how to measure fiscal capacity;
- (d) **Revenue targeting** seems inconsistent with historical performance and too ambitious. The 2019 BPS shows that the government projects to collect 14 per cent more revenue in 2019/20 compared to the targets set for 2018/19. This would be higher than the projected 8 per cent growth for expenditure. That indicates that the government revenue targets would help in reducing the deficits in 2019/20 which is one key indicator of governments' effort on fiscal consolidation;
- (e) **The revenue growth factor of the county equitable revenue** should be more predictable and realistic. The BPS recommends that counties be allocated Kshs. 310 billion in 2019/20. This is lower than the amount of Kshs. 314 billion approved in 2018/19 and only 2 per cent higher than the revised allocation of Kshs. 304 billion for the same year. In addition, significantly different from the 10 per cent growth in the amount recommended by the Commission of Revenue Allocation also based on the revised amount of Kshs. 304 billion. There is need for a clear determinant of how

revenue to counties will grow from year to year especially informed by ordinary revenue trends from previous years; and

- (f) **There is need for clarity on what is the planning policy informing government budgeting.** The BPS 2019 should clearly indicate whether the Big Four Agenda priorities are part of the Medium-Term Plan III or whether they are independent. The BPS 2019 as framed does not give a clear picture of the planning policy in use and what the expected long-term gains will be.

Committee Observations on the Submission by IBP

- (a) The Committee sought to understand how the fourteen (14) counties that would benefit from increase in health facilities density were identified and how the other counties that were left out would be considered.

The Committee noted that there were gaps in information on-

- (b) The Universal Health Coverage (UHC) roadmap and UHC pilot framework;
- (c) The equipping of 6,200 health facilities with basic clinical equipment;
- (d) Agreements between the National Government and thirty six (36) County Governments on affordable housing;
- (e) The cost of Ajira Digital Programme which has trained 11,000 youth on online jobs;
- (f) The policy on own source revenue collection by County Governments; and
- (g) Justification for the movement of sector ceilings in the BPS and Budget Review Outlook Paper (BROP).

MIN. NO. 336/02/2019: PRESENTATION AND CONSIDERATION OF OBSERVATIONS AND RECOMMENDATIONS FROM SENATE STANDING COMMITTEES

Standing Committee on Agriculture, Livestock and Fisheries.	Observation	Recommendation
	There is lack of clarity in the policy interventions relating to excess importation of maize and sugar, procurement of fertilizer, irrigation, revitalization of cash crops and agriculture research fund among others	The BPS for F/Y 2019/2020 should clearly prioritize and address issues relating to the supply of affordable fertilizer, excess importation of sugar and maize and governance issues that have affected production of staple foods.

	Although the overall budget allocation to the Agricultural sector has increased, Kshs. 7.2 billion is conditional grants to counties under World Bank funded programme called National Agricultural and Rural Inclusive Growth Project(NARIGP) which has specific target areas which may not necessarily be in the main areas of focus in the sector.	County governments should receive conditional funds to support the Big Four Agenda particularly in the area of food security and nutrition
	Supplementary budgets have had a negative effect on the implementation of development projects and this contributes to increased pending bills and distortion of budget implementation and reporting.	The government should endeavour to institutionalize proper budgeting and minimize supplementary budgets.
		The Agriculture research fund should receive additional funding because it plays a key role in supporting key areas of production in the Agricultural sector (general recommendation).

Committee Observations

The Committee adopted the recommendations of the Standing Committee on Agriculture, Livestock and Fisheries.

	Observations	Recommendations
Standing Committee on Roads and Transportation	The Mombasa – Nairobi Express Way was to be initiated in FY 2018/19 as was indicated in 2018 BPS, However, the BPS 2019 indicates that the project started but no indication of the status of implementation is given.	No specific recommendation given
	The 2018 BPS listed the number of airstrips that were to be constructed and expanded.	The Committee had raised issue with the distribution of the airstrips and subsequently recommended proper

	However, the 2019 BPS does not provide list of airstrips.	distribution of the airstrips across the country giving priority to far flung areas with poor road networks.
	Delivery of the second ferry (MV Safari) is yet to be achieved partly due to a court injunction by a consultant whose contract was terminated.	No specific recommendation given
	The BPS 2019 notes the establishment of the National Housing Development Fund. It is further noted that the Housing Act establishes a national fund. It is unclear as to whether these funds are different or reference is being made to the same fund	
	The BPS 2019, indicates that the government will provide land to investors who will be required to build 20,000 low cost housing units for 100,000 units they construct under a scheme called "Mixed Used Development" scheme.	There is need for clarification on the modalities surrounding the scheme.
	There are 87 stalled projects under the State Departments of Transport, Public Works, and Housing and Urban Development. Some of these projects were near completion before they stalled	There is need for prioritizing to ensure their timely completion
	Based on the analysis of resource requirement versus the ceilings provided, resources are usually limited relative to spending needs.	It is therefore prudent for all state Departments to prioritize their programmes and activities, implement efficiency and productivity measures in order to use the limited resources to achieve the performance targets including supporting four agenda (general observation).

Committee Observations

The Committee adopted the recommendations of the Standing Committee on Trade, Tourism and Industrialization.

Standing Committee	Observations	Recommendations
<p>on Health</p>	<p>The proposed FY 2019/20 allocation to the Ministry of Health is Kshs 93 Billion (5.1 percent of the total sectoral allocations). This represents a 3.4 percent increase from the FY 2018/19 allocation of Kshs 90 Billion. Through this allocation, the Ministry and its various Agencies will be implementing five programmes. The allocation is expected to increase to Kshs 99.1 Billion in FY 2021/22. Thus, over the next medium term, the Ministry is expected get an allocation totaling Kshs 288.2 billion.</p>	<p>The Committee is greatly concerned by the amount of resources held by the Ministry of Health, while health is a devolved function.</p> <p>The Committee recommends that any function or programme that does not fall under the National Government be given to the Counties</p>
	<p>The BPS 2019 shows continued support for universal health coverage (UHC), which is one of the big four agenda for the government. The UHC policy aims at ensuring that the entire country has access to affordable and quality health care services by 2022.</p> <p>The government has adopted a phased approach towards implementation of UHC. The pilot phase began in FY 2018/19 and focused on 4 counties and is currently being implemented. According to the BPS, it is envisaged that the next phase which is a full rollout of UHC in the remaining 43 counties will begin in November 2019, in the second quarter of the FY 2019/2020.</p>	<p>The adopted UHC pilot financing model is not unique since a similar model was tried during the initial phases of free maternity programme (Linda Mama Programme) and did not deliver the desired results which necessitated the shift of financing to NHIF based reimbursement model.</p> <p>Additionally the Committee was concerned that Counties will be required to match National Government contribution. The Committee is of the opinion that this process is not sustainable and will create an undue burden to the Counties.</p>

	<p>However, there are still some priorities outlined in BPS 2018 which are yet to take shape such as establishment of referral hospitals</p>	
	<p>An assessment of the health sector priorities outlined in the BPS 2019 indicates that broadly, the priorities enumerated are in line with the key national policy documents such as the Vision 2030 and the MTP III 2018-2022 as well as the Health sector priorities.</p>	
	<p>The total proposed 2019/20 budget for the Health sector amounts to Kshs 93 billion out of which Kshs 56.3 Billion is for recurrent expenditure while Kshs 36.6 billion is for development expenditure.</p> <p>There is a significant resource gap in the sector as a result of the proposed ceiling in 2019/20 and over the medium term considering the government intention to actualize the UHC by 2022 as one of its big four plan</p> <p>The proposed budget ceiling for Health sector for 2019/20 is less compared to the resource requirement for the sector which stood at Kshs 218.4 Billion. Given the resource requirement of Kshs 218.4 Billion, the sector has been allocated 43 percent of the resource required</p>	<p>As the Health sector is not adequately supported in terms of resource allocation to implement universal health care, the sector has to prioritize its programmes given the limited resources available.</p> <p>Further, the Ministry needs to adjust its targets for various performance indicators.</p> <p>As the Ministry of Health intends on implementing five key programmes to deliver on the UHC agenda the Ministry needs to revise the various targets set and also prioritize the various programmes to ensure that the critical deliverables are met in light of the resource gap,</p>
	<p>The UHC pilot phase targets 4 counties in the FY 2018/2019 and subsequently being rolled out to cover 47 counties in the</p>	<p>The Ministry is over ambitious by targeting to roll out the UHC in all 47 counties by July 2019 since it</p>

<p>FY 2019/2020 and medium term. These targets are ambitious and ambiguous.</p>	<p>requires significant resources which have not been adequately provided for in the BPS 2019. Further, there is ambiguity in targeting 100 percent county coverage and not the actual number of population accessing specific health care services free. Free/affordable healthcare for all Kenyans by July 2019 is not achievable. The Committee is of the opinion that this process should be thought through since the funding for UHC in all 47 Counties is based on revenue that the Government does not have.</p>
<p>In the budget allocation for FY 2029/2020 the Linda Mama Programme is classified as development budget whereas the spending under this program is recurrent in nature.</p>	<p>The Committee recommended that this be corrected and properly classified as recurrent expenditure.</p>
<p>The expansion of the Linda Mama program is identified as one of the key areas of spending in the FY 2019/20 and over the medium term. The FY 2019/20 allocation to the Linda Mama program is KSHs. 4.3 Billion. Financing under the Linda Mama program is based on an NHIF reimbursement model rather than on direct funding to counties through conditional grants.</p> <p>Counties have experienced various challenges in relation to the NHIF reimbursement model including, <i>inter alia</i>, lack of effective engagement and consultation prior to redesigning</p>	<p>The Committee therefore recommends that the Office of the Auditor General undertake a performance audit on the Linda Mama programme from inception to date and that a report on the same be availed to Senate within a specified period of time.</p>

	<p>the program, barriers to registration of mothers in remote and marginalized areas, low capitation rates leading to non-commensurate compensation for services rendered, marginalization of counties with a low density of registered public health facilities, disproportionate benefits private health facilities</p>	
	<p>Equipping 6,200 health facilities - The government envisages to equip 6,200 health facilities with basic clinical equipment.</p>	<p>The Ministry should provide clear guidelines on-</p> <ul style="list-style-type: none"> (a) what constitutes basic clinical equipment and what modalities will be used to equip these health facilities considering that most of them are under the purview of the county governments; (b) whether this is a new programme or an expanded MES programme; and (c) names of facilities covered per county. <p>The Committee therefore recommends that the funds set aside for this programme should be given to the Counties as equitable share.</p>
	<p>Increasing the number of health referral facilities is identified as one of the key areas of spending in the FY 2019/20 and over the medium term. The BPS does not indicate how the health referral facilities shall be identified and what criteria shall be used.</p>	<p>The Ministry should provide an implementation plan indicating how the location of the hospitals will be selected and what criteria will be applied. In addition, the plan should clearly state whether the referral hospitals will be established by upgrading</p>

	existing facilities or building new ones.
Providing Community Health Volunteers with basic kits is identified as one of the key areas of spending in the FY 2019/20 and over the medium term.	The Ministry needs to clarify what modalities will be used to equip Community Health Volunteers (CHVs) with basic kits considering that health is a devolved function, and that equipping CHVs falls under the purview of the respective county governments.
Expanding access to essential medicines and supplies is identified as one of the key areas of spending in the FY 2019/20 and over the medium term.	The Ministry needs to clarify what modalities will be used to expand access to essential medicines and supplies considering that health is a devolved function, and that provision of essential medicines and supplies falls under the purview of the respective county governments.
The Ministry has proposed a total allocation of KShs. 4.3 Billion as conditional grants to Level 5 Hospitals. This is in comparison to KShs. 4,325,000,000.00 in the FY 2018/19.	<p>Considering UHC will entail delivery of free services at all county referral hospitals including Level 5 hospitals, there is need to review conditional grants to Level 5 facilities.</p> <p>In light of the new and increasing pressures and demands that will fall on county referral hospitals as a result of UHC, there is an urgent need to review and establish legal safeguards for conditional grants to Level 5 hospitals.</p>
There exist other national health referrals which are either operating as departments of the	The Cabinet Secretary for Health should finalize the Semi-autonomous

	<p>Ministry or departments of learning institutions. Such arrangements greatly hamper services delivery in these national health referral institutions.</p>	<p>Government Agencies (SAGA) constitutive instruments and financial autonomy for Kenyatta University Teaching, Research and Referral Hospital; Mwai Kibaki Teaching and Referral Hospital (formerly Othaya Level 6 Hospital); the National Spinal Injury Hospital and Mathari Mental Hospital to make these facilities under the direct purview and oversight of the Committee.</p>
	<p>The recent Presidential Order placed the Kenyatta University Hospital Teaching and Referral Hospital under the Ministry of Health as a State Corporation.</p>	<p>The Ministry should provide a clarification on whether budgetary allocation has been provided for its operation in the FY 2019/2020.</p>
	<p>To drive the UHC goal, the government intends to modernize NHIF systems and improve governance structure through legal and institutional reforms. However, no timelines have been set for these reforms.</p>	<p>The Ministry should provide to the Committee a roadmap for modernization of NHIF to deliver on UHC particularly policy, legislative, & governance reforms. This should be done before any funds are spent</p>
	<p>The BPS 2019 indicates that only 5 hospitals have benefitted out of the 37 hospitals targeted to receive CT scans. The allocation for this project which is donor supported was provided in the current financial year.</p>	<p>The Ministry should provide a status report on this project to the Committee which should include the facilities the CT Scans have been delivered to, the procurement process used and cost of the CT Scan</p>
	<p>The Managed Equipment Services (MES) project has been allocated a conditional grant of Kshs 6.2 Billion in 2019/20 compared to Kshs 9.4 Billion in 2018/19. The decrease is</p>	<p>The Ministry breakdown of the Kshs 6.2 billion allocation need to be provided to the Committee.</p>

	<p>attributed to advanced implementation status of equipping most of the identified health facilities as well as settlement of previous financial year's arrears.</p>	<p>The Committee recommends that the Auditor-General undertake a performance audit on the MES programme from inception to date. Lessons learnt can be used to inform new programmes or improve the programme.</p> <p>Additionally, resources set aside for Medical Equipment's Services should be given to Counties through the equitable share.</p>
	<p>The national government has channeled significant amount of financial resources to the county governments as conditional grants for roll out of various programmes and projects in the health sector. These programmes were the foundational blocks towards the UHC agenda.</p>	<p>There is need to harmonize all these programmes into the UHC programme to avoid duplicity, reduce wastages, and improve on efficiency if the conditional grants to counties.</p> <p>Further, the Committee recommends that the Auditor-General undertake programme performance audits of all these programmes to determine their efficacy and efficiency so as to inform the full roll out of UHC.</p>
	<p>The Committee observes that the proposed financing model for UHC is fundamentally flawed in the sense that costing of devolved functions and the appropriate transfer of resources is not factored into the equitable share received by counties. As such, there is a strong possibility that despite the conditional grants that counties will receive under the UHC program, county governments will struggle to</p>	<p>No recommendation given.</p>

	implement the program owing to significant resource constraints.	
	<p>The health sector capital expenditure is highly dependent on donor financing. In FY 2016/17, the total capital expenditure estimates of Ksh. 31.179 billion was donor financed to the tune of Ksh. 19.77 billion, representing a donor financing level of approximately 63 percent. In the FY 2018/19 estimates, out of KShs. 40.9 Billion allocation, KShs. 12.7 Billion (31%) was obtained from AIA which is majorly funded by development partners.</p>	<p>There is need for the Ministry to explore home-grown financing mechanisms for critical projects in the Ministry. The funding should be consistent with Kenya's priorities and within broader objectives of universal coverage.</p>
	<p>In view of the expected increased demands for health services that will be occasioned by the implementation of UHC, the government intends to increase the number of health workers from 9:10,000 to 14:10,000 at an estimated cost of Kshs. 2.1 Billion. It's not clear from the BPS what proportion of this burden will be borne by National government <i>vis a vis</i> county governments.</p>	
	<p>Funding of additional allowances negotiated under the Collective Bargaining Agreements with doctors, nurses and clinical officers.</p> <p>The combined additional cost of these negotiated allowances to county governments amounts to KShs. 11,806,032,000.00. The BPS, as in the previous year, makes no provision for the allocation of this money yet</p>	

	current industrial action by nurses and clinical officers are related to the failure to implement the respective CBAs.	

Committee Observations

- (a) The equipping of 6200 health facilities should not be funded under the equitable share of revenue to counties but should be funded under conditional grants.
- (b) There was need to have a clear procedure on how hospitals are categorized in the various levels and recommended that the Standing Committee on Health should take up the matter with Cabinet Secretary for Health.
- (c) The Committee recommended that the 2019 BPS should include Ksh. 11 billion to cater for additional allowances for nurses as a conditional grant.

	Observations	Recommendations
Standing Committee on Trade, Industrialization and Tourism	It has been reported that there are a total of 545 stalled projects whose total estimated cost is KSh. 365.9 billion (KSh. 286.9 GoK and KSh. 78.9 billion foreign financing). The Ministry has documented 4 stalled projects, 3 under the state department for industrialization and one under cooperatives.	<p>Cognizant of the fact that delays in completion of projects typically leads to delayed returns on investment the Committee recommends that-</p> <p>(a) a decision be made on the fate of the 545 projects and other projects that may be at the same risk;</p> <p>(b) the possibility of remodeling county governments to be the real economic development centres as opposed to replicating the national government by for instance, an amendment to section 15 of the Public Finance Management</p>

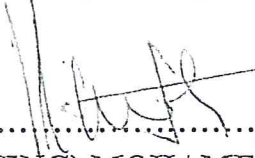
		Act, 2012 in a bid to stipulate a different percentage of allocation towards capital expenditure
	According to the sector report of 2018, the State Departments for trade, industrialization and tourism have pending Bills of various amounts. If pending bills are not factored into the proposed ceilings, funds may be reallocated to finance the bills and as a consequence impairing the achievement of some programs.	
	A review of the past three financial years indicate a low and declining trajectory in absorption rate of the capital vote of the State Department of Industry and Investment. Low absorption adversely affects the achievement of planned targets such as job creation, enhancing the industrial contribution to GDP and could lead to the reallocations or even budget cuts through supplementary budgets.	
	The government continues to support the manufacturing sub - sector through programmes geared towards improving the manufacturing capacity by expanding access to credit facilities and putting measures in place to reduce the high cost of production.	There is also need to heighten and sustain the fight against illicit trade and contrabands as these lead to unfair competition that may lead to collapse of the established genuine business enterprises.
	Parastatals under the State Department of Tourism and Cooperatives are many and on duplicating roles;	

Committee Observations

The Committee adopted the recommendations of the Standing Committee on Trade, Tourism and Industrialization.

MIN.NO. 337/02/2019: ADJOURNMENT

There being no other business the meeting was adjourned at 6:30 p.m.

SIGNATURE.....

(CHAIRPERSON: SEN. (ENG) MOHAMED MAALIM MAHAMUD)

DATE.....25/02/19.....

MINUTES OF THE 70TH MEETING OF THE SENATE STANDING COMMITTEE
ON FINANCE & BUDGET HELD ON SATURDAY, 23RD FEBRUARY, 2019 AT
SIMBA LODGE, NAIVASHA AT 9:30 AM.

PRESENT

1. Sen. (Eng) Mohamed M. Mahamud, CBS, MP - Chairperson
2. Sen. (Dr) Isaac Mwaura, CBS, MP - Vice Chairperson
3. Sen. Moses Wetangula, MP - Member
4. Sen. (Dr) Ali Abdullahi Ibrahim, CBS, MP - Member

ABSENT WITH APOLOGY

1. Sen. Aaron Cheruiyot MP -Member
2. Sen. Mutula Kilonzo Junior, MP - Member
3. Sen. (Dr) Rose Nyamunga, MP - Member
4. Sen. Boniface Mutinda Kabaka, MP - Member
5. Sen. CPA Farhiya Haji, MP - Member

IN-ATTENDANCE

SENATE SECRETARIAT

1. Mr. Njenga Njuguna - Director, Committee Services
2. Mr. Martin Masinde - Deputy Director, Budget Office
3. Mr. Fredrick Muthengi - Chief Fiscal Analyst
4. Mr. Christopher Gitonga - Clerk Assistant
5. Mr. Charles Ngatia - Clerk Assistant
6. Ms Lucy Radoli - Legal Counsel
7. Ms. Julie Mwithiga - Budget Officer
8. Mr. Elly Atamba - Researcher
9. Mr. Patrick Murindo - Sergeant At Arms
10. Mr. Stephen Nyakuti - Audio Officer

MIN. NO. 338/02/2019: PRELIMINARIES

The Chairperson called the meeting to order at 9.30 am and there followed a word of prayer.
The Chairperson welcomed Members to the meeting.

**MIN.NO. 339/02/2019: CONSIDERATION OF THE DRAFT REPORT ON THE
2019 MEDIUM TERM BPS**

The Committee considered the draft report on the 2019 Medium Term Budget Policy Statement and made the following observations-

1. There is little information on the status of implementation and objectives of the programmes that are funded through the conditional grants. It is imperative that the Standing Committees under whose mandate the programmes fall, should engage the implementing agencies to monitor and oversight the programmes.
2. Mortgage holders should be exempted from contributing the 1.5% tax on basic pay to the National Housing Development Fund to support the Big Four Agenda on construction of Affordable Housing.
3. Resolved to request the National Treasury to submit to the Parliament the policy on how counties can enhance own source revenue collection.
4. Resolved to request from the Auditor General to expedite the special audit on the conditional grants to counties especially on Linda Mama programme, Managed Equipment Service and Level 5 hospital to establish the effectiveness and value for money on the grants.
5. Resolved to adopt the proposal for division of revenue as follows-

The Committee recommends the following financial recommendations: -

a) That the County Allocation for FY 2019/20 be as follows –

(i) Total County Allocation be **Ksh. 405.46 Billion** of which

- County Equitable share be **Ksh. 332.06 Billion**

- ✓ That the equitable share for FY 2018/19 of Ksh. 314 Billion is adjusted by an annual inflation rate of 5 percent which is Ksh. 15.70 Billion and an adjustment for growth in development expenditure of 2.5 percent which is Ksh. 2.36 Billion.

Rationale:

- ❖ *The adjustment for inflation is based on the average annual inflation for the previous year.*

* The adjustment for growth in development expenditure of 2.5 percent reflects the minimum growth of capital asset for any institution. The 30 percent minimum for development expenditure is in line with the fiscal responsibility principles as provided in the PFM Act. Based on the equitable share of Ksh.314.00 Billion the minimum development expenditure is Ksh.94.20 Billion.

• County Conditional Grants be Ksh. 73.40 Billion which comprises of the following-

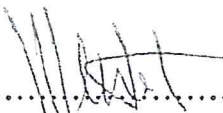
- ✓ Leasing of Medical Equipment- Ksh. 6.2 Billion
- ✓ Compensation for user fees foregone- Ksh. 900 Million
- ✓ Level 5 Hospitals- Ksh. 4.326 Billion
- ✓ Rehabilitation of Village Polytechnics- Ksh. 2 Billion
- ✓ Supplement for Construction of County HQs- Ksh. 485.20 Million
- ✓ Allocation from the Fuel Levy (15%)-Ksh. 8.984 Billion
- ✓ Allocation from Loans and Grants-Ksh. 38.70 Billion
- ✓ Health workers CBA – Ksh. 11.81 Billion

b) That the fiscal deficit (on commitment basis including grants) be binding at 5.1 percent of GDP in FY 2019/20.

The Committee resolved to adopt the report of the Committee on the 2019 BPS during the meeting on Monday 25th February, 2018.

MIN.NO. 340/02/2019: ADJOURNMENT

There being no other business the meeting was adjourned at 2:35 p.m.

SIGNATURE.....
(CHAIRPERSON: SEN. (ENG) MOHAMED MAALIM MAHAMUD)

DATE.....25/02/2019.....

MINUTES OF THE 71ST MEETING OF THE SENATE STANDING COMMITTEE ON FINANCE & BUDGET HELD ON MONDAY, 25TH FEBRUARY, 2019 AT COUNTY HALL, GROUND FLOOR BOARDROOM AT 11:00 AM.

PRESENT

1. Sen. (Eng) Mohamed M. Mahamud, CBS, MP - Chairperson
2. Sen. (Dr) Isaac Mwaura, CBS, MP - Vice Chairperson
3. Sen. Moses Wetang'ula, MP - Member
4. Sen. Aaron Cheruiyot MP -Member
5. Sen. (Dr) Ali Abdullahi Ibrahim, CBS, MP - Member
6. Sen. CPA Farhiya Haji, MP - Member

ABSENT WITH APOLOGY

1. Sen. Mutula Kilonzo Junior, MP - Member
2. Sen. (Dr) Rose Nyamunga, MP - Member
3. Sen. Boniface Mutinda Kabaka, MP - Member

IN-ATTENDANCE

SENATE SECRETARIAT

1. Mr. Christopher Gitonga - Clerk Assistant
2. Mr. Fredrick Muthengi - Budget Office
3. Ms. Julie Mwithiga - Fiscal Analyst
4. Mr. Nixon Mutai - Audio Officer

MIN. NO. 341/02/2019:

PRELIMINARIES

The Chairperson called the meeting to order at 11.10 am and there followed a word of prayer. The Chairperson welcomed Members to the meeting.

MIN. NO. 342/02/2019:

ADOPTION OF THE AGENDA

The agenda of the meeting was adopted after it was proposed by Sen. (Dr) Ali Abdullahi Ibrahim, MP and seconded by Sen. CPA Farhiya Haji, MP.

MIN.NO. 343/02/2019: CONFIRMATION OF MINUTES OF PREVIOUS SITTING

- a) The minutes of the 66th meeting held on Wednesday, 20th February, 2019 at 11.00 am were confirmed as a true record of the proceedings of the committee after they were proposed by Sen. CPA Farhiya Haji and seconded by Sen. (Dr) Ali Abdullahi Ibrahim.

- b) The minutes of the 67th meeting held on Thursday, 21st February, 2019 at 10.00 am were confirmed as a true record of the proceedings of the committee after they were proposed by Sen. Moses Wetang'ula and seconded by Sen. Aaron Cheruiyot.
- c) The minutes of the 68th meeting held on Friday, 22nd February, 2019 at 9.00 am were confirmed as a true record of the proceedings of the committee after they were proposed by Sen. Moses Wetang'ula and seconded by Sen. CPA Farhiya Haji.
- d) The minutes of the 69th meeting held on Friday, 22nd February, 2019 at 2.30 am were confirmed as a true record of the proceedings of the committee after they were proposed by Sen. (Dr) Ali Abdullahi Ibrahim and seconded by Sen. Moses Wetang'ula.
- e) The minutes of the 70th meeting held on Saturday, 23rd February, 2019 at 9.30 am were confirmed as a true record of the proceedings of the committee after they were proposed by Sen. Moses Wetang'ula and seconded by Sen. (Dr) Ali Abdullahi Ibrahim.

**MIN.NO. 344/02/2019: CONSIDERATION OF THE REPORT ON THE
2019 MEDIUM TERM BPS**

The Committee considered the report and made the following financial recommendations-

- a) That the equitable share for FY 2019/2010 be determined by adjusting the FY 2018/2019 equitable share by 3 year average inflation rate (6.9%). This translates to **Kshs 335.67 Billion**.
- b) That the conditional Grant from national revenues be allocated as follows-
 - i. Leasing of Medical Equipment- **Ksh. 6.2 Billion**
 - ii. Compensation for user fees foregone- **Ksh. 900 Million**
 - iii. Level 5 Hospitals- **Ksh. 4.326 Billion**
 - iv. Rehabilitation of Village Polytechnics- **Ksh. 2 Billion**
 - v. Supplement for Construction of County HQs- **Ksh. 485.20 Million**
 - vi. Allocation from the Fuel Levy (15%)-**Ksh. 8.984 Billion**

MIN.NO. 345/02/2019: ADJOURNMENT

There being no other business the meeting was adjourned at 12:25 p.m.

SIGNATURE.....

(CHAIRPERSON: SEN. (ENG) MOHAMED MAALIM MAHAMUD)

DATE.....

MINUTES OF THE 72ND MEETING OF THE SENATE STANDING COMMITTEE ON FINANCE & BUDGET HELD ON MONDAY, 25TH FEBRUARY, 2019 AT COUNTY HALL, GROUND FLOOR BOARDROOM AT 12:30 PM.

PRESENT

1. Sen. (Eng) Mohamed M. Mahamud, CBS, MP - Chairperson
2. Sen. (Dr) Isaac Mwaura, CBS, MP - Vice Chairperson
3. Sen. Moses Wetang'ula, MP - Member
4. Sen. Aaron Cheruiyot MP -Member
5. Sen. (Dr) Ali Abdullahi Ibrahim, CBS, MP - Member
6. Sen. CPA Farhiya Haji, MP - Member

ABSENT WITH APOLOGY

1. Sen. Mutula Kilonzo Junior, MP - Member
2. Sen. (Dr) Rose Nyamunga, MP - Member
3. Sen. Boniface Mutinda Kabaka, MP - Member

IN-ATTENDANCE

SENATE SECRETARIAT

1. Mr. Christopher Gitonga - Clerk Assistant
2. Mr. Fredrick Muthengi - Budget Office
3. Ms. Julie Mwithiga - Fiscal Analyst
4. Mr. Nixon Mutai - Audio Officer

IN-ATTENDANCE

COUNCIL OF GOVERNORS REPRESENTATIVES

List Attached.

MIN. NO. 346/02/2019: PRELIMINARIES

The Chairperson called the meeting to order at 12.40 pm and there followed a word of prayer. The Chairperson welcomed Members to the meeting.

MIN. NO. 347/02/2019: ADOPTION OF THE AGENDA

The agenda of the meeting was adopted after it was proposed by Sen. (Dr) Ali Abdullahi Ibrahim, MP and seconded by Sen. CPA Farhiya Haji, MP.

MIN.NO. 348/02/2019: MEETING WITH COUNCIL OF GOVERNORS

The Chairperson welcomed the representatives from Council of Governor and informed them that the purpose of the meeting was to deliberate on the 2019 Budget Policy Statement (BPS).

After a round of introductions the Chairperson welcomed the representatives from COG to make their presentation.

The representatives informed the Committee as follows-

- a) That there was need for more interactions and engagement between the Senate and the COG to ensure the protection of the interest of counties.
- b) The interest of the COG in the 2019 was mainly the vertical sharing of the revenue of which the baseline was allegedly revised. There were meetings to consider the baseline but no consensus.
- c) At the point of negotiating for Ksh 314 billion as equitable share, the projected revenue was Ksh 1.68 trillion. However, the projection was revised to Ksh 1.79 trillion but the equitable share was not revised upwards. Thus, the revision of the projections back to Ksh 1.6 Trillion should not affect the equitable share.
- d) The counties had budgeted for their allocation from Ksh 314 billion. Revision will trigger preparation of supplementary budget. Further, counties had no other mechanism to shield such shortfall since they cannot borrow.
- e) Though there was a proposal of inclusion of unfunded devolved functions amounting to Ksh 8.7 Billion, (salaries for devolved library staff 300 million and transferred 31,000 km of roads to counties Ksh 8.4 billion) after further consultation, the council was willing to withdraw the proposal.
- f) The proposal to revise the county equitable share downwards for the year 2018/2019 because of revenue shortfall was in contravention of the law, (DORA, 2018).
- g) The Council was in agreement with the Commission of Revenue Allocation (CRA) proposal of adjusting the Ksh 314 by using 3-year average annual inflation of 6.9%. This would translate to Ksh 335.7 billion.
- h) There was need to adjust the baseline using inflation factor to ensure adequate service delivery. There was need to set up a mechanism/ parameters which would determine the annual adjustments in equitable share.
- i) The county equitable allocation in relation to GDP was declining whereas the GDP was growing. This trend indicated that devolution was at stake.
- j) The mandate of tax collection was a national government obligation and counties should not be made to suffer due to over projections of revenue.

Further deliberations ensued as follows-

a) Health workers Collective Bargaining Agreement (CBA)

- At onset of devolution, most of the health workers had stagnated in the job groups. However, there were efforts to ensure they were promoted.
- The 2017 strike, the nurses were requesting for increment in basic salary, annual uniform allowance, and nursing allowance.

- The basic salary was honoured as enshrined in the CBA. However, the other two allowances were contested. The court had directed for mediation/ negotiation on the matter within 60 days. The ministry of Labour had appointed a reconciliatory Committee and the matter was ongoing.
- The SRC were supposed to approve allowances.
- There was hope that the matter will be resolved amicably.

b) **Big Four Agenda**

- The counties were not consulted on the matter and the target areas were devolved functions. There was concern that the national government was taking back some devolved functions especially health.
- There was concern over ever increasing budgets allocated to the ministry of Agriculture and Ministry of Health whereas these functions were fully devolved. Such funds should be allocated to the counties as either equitable share or conditional grants.
- There was a lot of duplication especially the Ministry of Water.
- Projects such as envisioned in the Big 4 should be funded through conditional grants to the county government.

c) **National Interest**

- The Constitution Implementation Commission had initiated the matter of defining the meaning and scope. However, their term lapsed before the conclusion of the matter. COG sought court interpretation, but the matter was referred back for Alternative Dispute Resolution (ADR). This has been ongoing matter.
- IBEC was to deliberate on the matter and then forward to Summit for approval.
- There was need to consider legislation to define the term and the scope.

d) **Leasing Medical Equipment**

- The matter has not been clear on the costs. There was concern over the transparency and accountability of the project. Since there was no transparency the public resources may be misappropriated. Further, the project was undertaken without consultation with the COG.
- The cost of the equipment supplied is always several times higher than the market value.

- The Senate should stop approving the conditional grant for this project until proper explanations on the costs were provided.

e) Pending Bills

- Some counties lack capacity to manage cash flow projections and implementation of the budget. At times procuring more than what is the budget.
- There has been a delay in disbursement of equitable share by the National Treasury. Especially development budgets for first quarter were released in the second quarter.
- There was a tendency of National Treasury releasing almost 50% of the allocation to a county few days to the end of the financial year. Then counties are advised to spend the funds within 5 working days.
- Most of the counties were making the necessary plans to clear or reduce the pending bills.

f) Own Source Revenue

- There were some consultations done on Own Source revenue Policy and the COG gave their views. However, the proposed legislation was not in line with their proposal. Especially provision of notifying the Cabinet Secretary of any proposed fees/ taxes 10 months in advance.
- The counties are only able to collect fees like market fees. Such are not structured and there is a lot of political interference.
- 17 counties had undertaken revenue automation process but were at different levels.

g) Health

- The Funding for Level 5 hospitals had remained the same though there was increase in the number of hospitals.
- Instead of constructing new referral hospitals the National Government should consider improving the existing level 5 hospitals with view of upgrading them to the level of referral hospitals.
- The *Linda Mama* program was doing well though counties have to claim for reimbursement from NHIF.

- There were 6200 health facilities earmarked for equipping by the national government, however, the COG was requesting that the fund for the same be channelled to the counties through conditional grants.
- KEMSA was captured by cartels and were supplying drugs at quite high prices yet it was supposed to be offering at the fairest price. In addition they supplied generic drugs which are expected to be cheaper.

h) Development Expenditure

- At times it's difficult to utilize the funds because of the delayed disbursements. The funds are released towards the very end of the financial year.
- The oversight bodies should be keen to ensure the 30%-70% rule was met at both budgeting and implementation levels.
- The issue of absorption capacity would be dealt with if there was adherence to cash disbursements schedule.

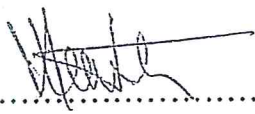
i) Accountability and Governance

- There were concerns over the rate of misuse of the public resources in the counties. The oversight bodies had also increased with view of ensuring public resources were appropriately utilised.
- The Council had developed a mechanism for peer review to deal with governance and corruption issues. A *Maarifa centre* supported by USIU was created to serve as a platform for peer review among the county governors.

The Chair thanked the COG for their submission and noted that their request would be considered.

MIN.NO. 349/02/2019: ADJOURNMENT

There being no other business the meeting was adjourned at 2:25 p.m. Next meeting Tuesday, 26th February, 2019 at 9:00 am.

SIGNATURE.....

(CHAIRPERSON: SEN. (ENG) MOHAMED MAALIM MAHAMUD)

DATE.....

Representatives from Council of Governors

1. Hon. Wycliff Oparanya – Chairperson
2. Hon. Wycliff Wangamati – Chairman, COG Finance Committee
3. Hon. Ndiritu Murithi – Member, COG Finance Committee
4. Ms. Jacqueline Mogeni – COG CEO
5. Ms. Mary Mugwanja – CECM Finance and Education, Nyandarua
6. Mr. David W. Waweru – CECM Finance Muranga
7. Mr. Geoffrey Omulayi – CECM Finance Kakamega
8. Mr. Andrew Sigei – CECM Finance Bomet
9. Mr. Kiama Kaara – Snr Advisor Laikipia
10. Ms. Mercy Wangui
11. Mr. Victor Odanga
12. Ms. Nkatha Koronya
13. Mr. Ronald Odanga
14. Mr. Barbara Awuor
15. Mr. Iyepondi Stanslaus

MINUTES OF THE 73RD MEETING OF THE SENATE STANDING COMMITTEE
ON FINANCE & BUDGET HELD ON TUESDAY, 26TH FEBRUARY, 2019 AT
COUNTY HALL, GROUND FLOOR BOARDROOM AT 9:00 AM.

PRESENT

1. Sen. (Eng) Mohamed M. Mahamud, CBS, MP - Chairperson
2. Sen. Moses Wetang'ula, MP - Member
3. Sen. Aaron Cheruiyot MP -Member
4. Sen. (Dr) Ali Abdullahi Ibrahim, CBS, MP - Member
5. Sen. CPA Farhiya Haji, MP - Member
6. Sen. Mutula Kilonzo Junior, MP - Member
7. Sen. (Dr) Rose Nyamunga, MP - Member

ABSENT WITH APOLOGY

1. Sen. (Dr) Isaac Mwaura, CBS, MP - Vice Chairperson
2. Sen. Boniface Mutinda Kabaka, MP - Member

IN-ATTENDANCE

SENATE SECRETARIAT

1. Mr. Christopher Gitonga - Clerk Assistant
2. Mr. Fredrick Muthengi - Budget Office
3. Ms. Julie Mwithiga - Fiscal Analyst
4. Mr. Charles Atamba - Research Officer

MIN. NO. 350/02/2019:

PRELIMINARIES

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

MIN. NO. 351/02/2019:

ADOPTION OF THE AGENDA

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

MIN.NO. 352/02/2019: CONFIRMATION OF MINUTES OF PREVIOUS SITTING

- a) The minutes of the 71st meeting held on Monday, 26th February, 2019 at 11.00 am were confirmed as a true record of the proceedings of the committee after they were proposed by Sen. Aaron Cheruiyot and seconded by Sen. (Dr) Ali Abdullahi Ibrahim.
- b) The minutes of the 72nd meeting held on Monday, 26th February, 2019 at 12.30 pm were confirmed as a true record of the proceedings of the committee after they were proposed by Sen. Moses Wetang'ula, and seconded by Sen. (Dr) Ali Abdullahi Ibrahim.

**MIN.NO. 353/02/2019: ADOPTION OF THE COMMITTEE REPORT ON 2019 BPS
AND MEDIUM TERM DEBT MANAGEMENT
STRATEGY**

The Committee considered the report and resolved the following

- a) The Parliament should legislate on-
 - The framework of identifying the level 5 hospitals.
 - The definition and scope of '*national interest*'
- b) Removal of conditional grant on Leasing of Medical Equipment (MES project) from the Division of Revenue Bill.
- c) National Treasury to stop payment to the MES project until full disclosure of costs are made to the Parliament.
- d) CRA and The National treasury should develop a policy framework on the conditional grant and submit the same to the Parliament within 3 months.

The Committee made the following financial recommendations.

- a) That the recommendation on the allocation of revenue to County Governments for FY 2019/20 that is proposed in the 2019 BPS and the draft Division of Revenue Bill 2019, be as follows –
 - (i) Total County Allocation be **Ksh. 391.07 Billion** of which
 - County Equitable share be **Ksh. 335.67 Billion**
 - ✓ That the equitable share for FY 2018/19 of Ksh. 314 Billion is adjusted by a three-year average inflation rate of 6.9 percent which is Ksh. 21.67 Billion. This is similar to the proposals by the Commission on Revenue Allocation and the Council of Governors.
 - County Conditional Grants be **Ksh. 55.40 Billion** which comprises of the following-
 - ✓ Compensation for user fees foregone- **Ksh. 0.90 Billion**

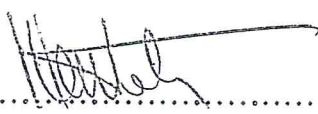
- ✓ Level 5 Hospitals- Ksh. 4.326 Billion
- ✓ Rehabilitation of Youth Polytechnics- Ksh. 2.00 Billion
- ✓ Supplement for Construction of County HQs- Ksh. 0.485 Billion
- ✓ Allocation from the Road Maintenance Fuel Levy Fund (15 percent)- Ksh. 8.984 Billion
- ✓ Allocation from Development Partners as Loans and Grants-Ksh. 38.70 Billion

- b) That the fiscal deficit (on commitment basis including grants) be binding at 5.1 percent of GDP in FY 2019/20.
- c) That the budget ceiling for the Executive for FY 2019/20 be reduced by Ksh. 19.47 Billion. This amount is equivalent to an additional Ksh. 25.67 Billion to the County Equitable Share for FY 2019/20 from Ksh. 310 Billion as proposed in the 2019 BPS to Ksh. 335.67 Billion; and a reduction of Ksh. 6.2 Billion for the conditional allocation for leasing of medical equipment.

The Committee unanimously adopted the report for tabling on 26th February, 2019.

MIN.NO. 354/02/2019: ADJOURNMENT

There being no other business the meeting was adjourned at 10:45 am.

SIGNATURE.....

(CHAIRPERSON: SEN. (ENG) MOHAMED MAALIM MAHAMUD)

DATE.....