



THE SENATE
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Hon. Speaker

TO : THE CLERK OF THE SENATE

THRO' : DEPUTY CLERK, SENATE - EG
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THRO' : DIRECTOR, COMMITTEE SERVICES
Forwarding and recommended for approval for tabling 07/09/2021

FROM : CLERK ASSISTANT

DATE : 7TH SEPTEMBER, 2021

SUBJECT : REPORT ON THE PUBLIC FINANCE MANAGEMENT (SINKING FUND) GUIDELINES, 2021

You may approve
Walter
8/9/21

The above matter refers.

The Public Finance Management (Sinking Fund) Guidelines, 2021 are made by the Cabinet Secretary, National Treasury and Planning pursuant to regulation 206(3) of the Public Finance Management (National Government) Regulations, 2015, and are intended to be applied to the management of the Sinking Fund established under regulation 206(1) of the Regulations.

The Guidelines were committed to the Sessional Committee on Delegated Legislation for consideration pursuant to section 15(2) of the Statutory Instruments Act, 2013. Herewith attached, please find a Report conveying the recommendation of the Committee in respect to the Public Finance Management (Sinking Fund) Guidelines, 2021, for your review and consideration for processing.


B.M. Kiambi

Approved
8/9/21

Approved

8/9/2021

PARLIAMENT OF KENYA



cos

Recommended for approval for tabling.

8/08/21

Hon. Speaker

You may approve for tabling.

8/9/21

12TH PARLIAMENT - THE SENATE

SENATE SESSIONAL COMMITTEE ON DELEGATED LEGISLATION

A REPORT ON THE CONSIDERATION OF THE PUBLIC FINANCE MANAGEMENT (SINKING FUND) GUIDELINES, 2021

PAPERS LAID	
DATE	08/09/2021
TABLED BY	Vice Chair
COMMITTEE	Delegated
CLERK AT THE TABLE	Deputy

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

September, 2021

DC-EG
Forwarded recommended for approval for tabling
8/07/2021

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ABBREVIATIONS AND ACRONYMS

MP	-	Member of Parliament
Sen.	-	Senator
PFM	-	Public Finance Management
CBK	-	Central Bank of Kenya
CS	-	Cabinet Secretary
COB	-	Controller of Budget
CFS	-	Consolidated Fund Services
FY	-	Financial Year
MP	-	Member of Parliament
DG	-	Director General
PDMO	-	Public Debt Management Office

PREFACE

Honourable Speaker,

Establishment of the Committee

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

Membership of the Committee

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

Sen. Mwinyihaji Mohammed Faki, MP	- Chairperson
Sen. Agnes Kavindu Muthama MP	- Vice Chairperson
Sen. Samuel Poghiso, EGH, MP	
Sen. Farhiya Ali Haji, CPA, MP	
Sen. Erick Okong'o Omogeni, SC, MP	
Sen. Judith Pareno, MP	
Sen. Mary Seneta, MP	
Sen. Abshiro Halake, MP	
Sen. Anwar Loitip, MP	

Honourable Speaker,

Executive Summary of the Report

The Public Finance Management (Sinking Fund) Guidelines, 2021 were published by the Cabinet Secretary, the National Treasury, on 25th May, 2021 pursuant to regulation 206(3) of the Public Finance Management (National Government) Regulations, 2015 and are intended to be applied to the management of the Sinking Fund established under regulation 206(1) of the Regulations.

The Guidelines were submitted to the Senate by the Cabinet Secretary, National Treasury on 3rd June, 2021 pursuant to section 11(1) of the Statutory Instruments Act, 2013. The Guidelines were then tabled before the Senate by the Senate Majority Leader on 6th July, 2021 and subsequently committed to the Senate Sessional Committee on Delegated Legislation. Pursuant to section 15(2) of the Statutory Instruments Act, the Committee is required to scrutinize the Guidelines and make a report to the House with a resolution that a statutory instrument that was referred to the committee be revoked.

The Sessional Committee on Delegated Legislation considered the Guidelines and received submissions from the National Treasury and the Central Bank of Kenya.

Honourable Speaker,

Some of the key observations by the Committee on Public Finance Management (sinking fund) Guidelines, 2021 were as follows: -

- (a) According to the Debt Management Strategy 2021, Debt redemptions are projected to jump from KSh. 499.7 billion as at the end of FY 2020/21 to KSh 990.7 billion in the FY 2023/24, an increase of by 98% in a span of two fiscal years.
- (b) Kenya set up the first sinking fund in the 1960s under the Internal Loans Act, Chapter 420. The fund remained dormant and the process of winding up the fund is currently before the National Assembly.
- (c) Kenya presently pays the public debt from the Consolidated Fund Services (CFS). Section 50 (6) of the Public Finance Management Act which provides that ***public debt incurred by the National Government is a charge on the Consolidated Fund, unless the Cabinet Secretary determines, by regulations approved by Parliament, that all or part of the public debt is a charge on another public fund established by the national government or any of its entities.***
- (d) The Consolidated Fund Services also caters for other obligatory payments such as pension and salaries for independent constitutional office holders.
- (e) Section 50 (8) of the Public Finance Management Act permits the Cabinet Secretary in charge of Treasury, with the ***approval of Parliament, (to) establish such sinking fund or funds for the redemption of loans raised under this Act by the national government.***

In addition, Regulation 206 (3) of the Public Finance Management (National Government) Regulations, 2015 mandates the Cabinet Secretary *to publish in the Kenya Gazette the guidelines for the management of the Fund. Conflict with the Public Finance Management Act, 2012 and its regulations*

- (f) Despite the foregoing, Regulation 206 (2) of the Public Finance Management (National Government) Regulations, 2015 limits the scope of the fund to **payment of expenses of, or incidental to, redemption of an issue of Government securities and the redemption of an issue of Government securities.**
- (g) The Committee notes with concern that despite the limitation above, the guidelines as currently drafted, as per guideline 3 (2), expand the scope of the fund to include national government loans that are not envisaged under Regulation 206 (2) of the Public Finance Management (National Government) Regulations, 2015.

Honourable Speaker,

History of Debt Repayment and tools already in use

- a) The Committee confirmed from the Central Bank of Kenya that the country already has a myriad of effective tools at its disposal to ensure that debt is sustainably managed. These tools include: the ability to roll over previous debt, the option of switching between creditors; the option to lengthen maturity debt; refinancing of external debt through borrowing and offsetting older debt; the executives' overdraft facility with the CBK.
- b) The Committee concurred that committing funds to a sinking fund would essentially lend those funds idle.

Honourable Speaker,

Conflict with the Central Bank of Kenya Act

- (h) Section 4A (1) of the Central Bank of Kenya Act mandates the Central Bank of Kenya to *formulate and implement foreign exchange policy and hold and manage its foreign exchange reserves.* It further observed that guideline 5 (e) of the guidelines provides that one of the sources of the Fund shall consist of *foreign exchange gains from external loans to the National Government.* The Committee noted that the National Treasury is not mandated to hold foreign

exchange reserves and as a result guideline 5 (e) of the guidelines is inconsistent with section 4A (1) of the Central Bank of Kenya Act.

- (i) The Committee further noted that the Guidelines failed to take into consideration Clause 4A (1) (e) of the CBK Act which mandates the CBK to be the fiscal agent of the government.
- (j) The Committee observed that it was unclear how foreign exchange gains from external loans to the National government will be realized when the sinking fund is comprised of local currency. This observation was made on the basis that the Central Bank of Kenya informed the Committee that whereas the sinking fund is in local currency (Kenya Shillings) the guidelines under guideline 5 (e) provide for the realization of foreign exchange gains from external loans to the National government. The Committee was further informed that realization of foreign exchange gains from external loans to the National government would not ordinarily happen unless the amount of local currency accumulated was more than that needed to offset the external obligations at the prevailing exchange rate.
- (k) The guidelines propose the establishment of a Sinking Fund Advisory Committee which is proposed to consist of the Principal Secretary in charge of finance as the Chairperson; the Director General, Public Debt Management Office as the Secretary; the Director -General, Accounting Services and Quality Assurance and the Director -General Public Investment and Portfolio Management. The Committee observed that the Central Bank of Kenya is not a member of the Committee yet under Section 4A (1) (e) of the Central Bank Act, the Bank is the fiscal agent of the government.

Other observations

The Committee also observed that as currently drafted the Guidelines—

- (i) Don't provide for strong oversight of the Fund. There is need to enhance the oversight role of Parliament in the Fund, this can be done by requiring that regular periodic financial and non-financial reports prepared by the Fund administrator are submitted to Parliament for scrutiny.
- (ii) Do not ring-fence the funds. There is need to ensure that the funds are ring-fenced so that it is only used for the set objective of redemption of public debts.

- (iii) Do not provide a mechanism for controlling the administrative expenditure. There is need to establish a mechanism of controlling the administrative expenditures to ensure that there is no wastage of public funds.

Honourable Speaker,

This Report provides detailed observations and the findings of the Committee on specific provisions of the Guidelines which offend section 13 of the Statutory Instruments Act, 2020 as follows-

- a) **The Objects and Purpose of the Fund can be achieved within the existing laws.**
- b) **Paragraph 5 (e) of the Guidelines indicates that the sources of funds will include “Foreign exchange gains from external loans to the National Government.” Which Conflicts the understanding that the Sinking Fund in is Kenya Shillings and also Contradicts CBK’s statutory mandate on foreign exchange, including “hold and manage foreign exchange reserves” under Section 4A (1) of the CBK Act.**

Honourable Speaker,

After consideration of the Public Finance Management (Sinking Fund) Guidelines 2021, pursuant to section 15 (1) of the Statutory Instruments Act and Standing Order 221 (4) (b), the Sessional Committee on Delegated Legislation recommends that the Senate resolves that the Public Finance Management (Sinking Fund) Guidelines 2021 be annulled.

Acknowledgement

The Committee wishes to thank the Offices of the Speaker and the Clerk of the Senate as well as the Secretariat for the support extended to it in the conduct of the public hearings and in fulfilling its mandate.

Further, the Committee wishes to thank the stakeholders who made both written and oral submissions during the consideration of the Public Finance Management (Sinking Fund) Guidelines 2021.

Honourable Speaker,

It is now our duty, pursuant to section 15 (1) of the Statutory Instruments Act and standing order 221 (4) (b) of the Senate Standing Orders, to present the Report of the Sessional Committee on Delegated Legislation on the Public Finance Management (Sinking Fund) Guidelines 2021.



DATED: 7TH SEPTEMBER, 2021

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

**ADOPTION OF THE REPORT OF THE SESSIONAL COMMITTEE ON THE
PUBLIC FINANCE MANAGEMENT (SINKING FUND) GUIDELINES 2021**

**We, the undersigned Members of the Senate Sessional Committee on Delegated
Legislation do hereby adopt this Report at a virtual meeting held on 7th September,
2021 at 10.00 a.m.**

Sen. Mwinyihaji Mohammed Faki, MP - Chairperson

Sen. Samuel Poghiso, EGH, MP

Sen. Frhiya Ali Hji, MP

Sen. Judith Pareno, MP

Sen. Mary Seneta, MP

DATED: 7TH SEPTEMBER, 2021

CHAPTER ONE

INTRODUCTION

1.0 BACKGROUND

1. This is the second time that Kenya is creating such a fund after the one set up in 1960s under the Internal Loans Act, Chapter 420. The Fund has remained dormant and its winding up is underway, pending before the National Assembly.
2. Presently, the public debt is paid from the Consolidated Fund Services (CFS) which also caters for other obligatory payments such as pension and salaries for independent constitutional office holders.
3. The PFM Act under section 50(6) provides that debt service can be paid from Consolidated Fund Services or any other fund established under an Act of Parliament.
4. According to the Debt Management Strategy 2021, Debt redemptions are projected to jump from KSh.499.7 billion as at the end of FY 2020/21 to KSh 990.7 billion in the FY 2023/24, an increase of by 98% in a span of two fiscal years.

1.1 LEGAL BASIS

5. The Guidelines are made by the pursuant to the Regulation 206(3) of the Public Finance Management (National Government) Regulations 2015 and are intended to be applied to the management of the Sinking Fund established under regulation 206(1) of the Regulations.
6. Section 18 of the Public Finance Management Act 2012 empowers the National Treasury to administer the Fund in accordance to Article 204 of the Constitution. Sections 12 (1) (e) and 205 of the Public Finance Management Act also give the Cabinet Secretary responsible for Finance the powers to make further regulations therein.

1.2 OVERVIEW OF THE GUIDELINES

1.2.1 Purpose of the Fund.

7. A sinking Fund is created and set up purposefully for redemption of government loans and government securities. Certain amount of money is regularly set aside to finance both the principal and interest of a public debt before its maturity date reaches. The objective of the Fund is to mitigate future cash flow challenges arising from heavy repayment of debts whose grace periods have expired.
8. This shall facilitate paying off maturing public debts, buying back bonds when interest is low and retire some of the debts early to avoid higher costs in future.

1.2.2 Capital of the Fund

9. Sources of the fund to include: Consolidated Fund Budget vote for redemption of debts and other debt related expenses from the Exchequer to be remitted to the Fund continuously; monies appropriated by Parliament for the purposes of the Fund; fees and commissions earned by the Public Debt Management Office in execution of its mandate ;income invested from the balances of the Fund; foreign exchange gain from external loans to the National Government; any moneys accruing to or received by the Fund from any other lawful source with approval of the Cabinet Secretary; and any other source provided for by an Act of Parliament.

1.2.3 Expenditures of the Fund

10. Payments out of the Fund shall be for redemption of government loans, and payment of expenses incidental to the loans.
11. Other administrative expenditures shall be on the basis of annual work plans and cost estimates shall be prepared by the Administrator of the Fund, recommended by the Committee and approved by the Cabinet Secretary at the beginning of the financial year to which they relate.

1.2.4 Establishment of Sinking Fund Advisory Committee

12. The Committee membership shall be made up of: PS in charge of finance as the chairperson, Director General, PDMO as Secretary, DG Accounting Services and Quality Assurance, DG Public Investment and Portfolio Management.
13. The Key functions of the Advisory Committee shall include: provide advice on administration of the Fund; provide policy linkages between the Fund and other public management functions, review and recommend for approval of statutory and management reports of the fund before submission to the CS for approval and onward submission to Auditor General and to the COB; review and recommend the annual work plans, annual securities issuance plan, and investment plans to the CS for approval; review and recommend the revenue and expenditure estimates of the Fund to the CS in each financial year.

1.2.5 Fund Administrator

14. Shall be the Head of Public Debt Management Office and whose key functions include: Undertake day to day operations of the fund; borrow and deposit monies into the fund for the purposes of debt redemption on approval by the Cabinet Secretary, supervise and control the administration and management of the Fund

1.2.6 Secretariat to the Fund

15. The CS shall appoint the secretariat to the Fund and ensure that the Fund has the resources and skills to manage the day to day operations of the Fund.

1.2.7 Reporting framework

16. The administrator of the fund shall prepare the annual and non-financial reports in accordance with the Act and Audit Act 2015 and submitted to the Accounting Officer for approval before submission to the Auditor General for audit.
17. In the event of winding up the Fund-
 - i. The administrator of the Fund shall pay any credit balance in the Fund to the National Exchequer Account while the Assets of the Fund shall be transferred to the Ministry for Finance.

- ii. The Cabinet Secretary shall pay any deficit in the Fund from the Funds of the National Government in the National Exchequer Account upon approval of Parliament
- iii. The Committee shall prepare final winding up report not later than six months from the date of decision to wind it up and submit financial and non-financial reports to the Auditor General for audit with a copy to the Cabinet Secretary.
- iv. The Cabinet Secretary shall submit a final statement of accounts of the Fund to Parliament.

CHAPTER TWO

STAKEHOLDER ENGAGEMENT

2.0 CONSULTATION WITH STAKEHOLDERS

18. The Sessional Committee on Delegated Legislation received written submissions and held virtual meetings with stakeholders the National Treasury and planning on 1st of September 2021; the Central bank of Kenya on 6th September 2021. The Committee therefore considered the written and oral submissions from the following stakeholders:

- (1) The Cabinet Secretary for Finance vide letter Ref. No. DMD 4/197 “A” dated 30th August, 2021 *copy attached as Annex 1*; and,
- (2) The Governor, Central Bank of Kenya vide letter dated 3rd September, 2021 *copy attached as Annex 2*.

2.1 GENERAL COMMENTS BY STAKEHOLDERS

19. The following is a summary of the submissions from stakeholders on the Guidelines-

2.1.1 The Cabinet Secretary for Finance

20. **The Cabinet Secretary Submitted that;** the Public Finance Management (Sinking Fund) Guidelines are developed pursuant to Regulation 206(3) of Public Finance Management (National Government) Regulations 2015 and are intended to be applied to the management of the Sinking Fund established under Regulation 206(1) of the same regulations.

21. **He stated that; the Object and Purpose of the Fund is** to provide funding for the redemption of government loans, and payment of expenses of, or incidental to, redemption of an issue of national government loans.

22. **The Fund is meant to:**

- a) cushion for amortization of liabilities arising from national government loans;
- b) facilitate debt restructuring and smoothening of the maturity profile;
- c) redeem maturing national government loans to alleviate rollover risks;

- d) build up resources for meeting maturities of loans and securities issued in the domestic and international debt capital markets;
- e) correct any perceived mispricing along the yield curve;
- f) buy back of a national government loan obligations in the debt market;
- g) meet the cost of switches and early redemption of national government loan obligations; and
- h) meet costs incidental to the loans.

23. **The Capitalization of the Fund** shall be as appropriated by Parliament from time to time from the following:

- a) Consolidated Fund Budget Vote for redemption of debts;
- b) Monies appropriated by Parliament;
- c) Fees and commissions earned by the Public Debt Management Office;
- d) Incomes invested from the balances of the Fund;
- e) Foreign exchange gains from external loans to the National Government;
- f) Any moneys accruing to or received by the Fund from any lawful source; and
- g) Any other source to the Fund provided for by an Act of Parliament.

24. **The Cabinet Secretary explained that; there is to be established a Committee known as The Sinking Fund Advisory Committee which shall consist of:**

- a) The Principal Secretary in charge of Finance as the Chairperson;
- b) The Director General, Public Debt Management Office as the Secretary;
- c) The Director General, Accounting Services and Quality Assurance; and
- d) The Director General, Public Investment and Portfolio Management.

25. **The functions of the Advisory Committee shall be to:**

- a) provide advice on the administration of the Fund;
- b) provide policy linkage between the Fund and other public finance management functions;
- c) review and recommend for approval of statutory and management reports;
- d) review and recommend the annual work plans, annual securities issuance plan, and investment plans to the Cabinet Secretary for approval and
- e) review and recommend for approval the revenue and expenditure estimates.

26. **The Cabinet Secretary, National Treasury and Planning further stated that the Advisory Committee shall be holding its meetings as follows:**

- a) In absence of the Chairperson in any meeting of the Committee any member appointed in writing by the Principal Secretary in charge of Finance shall chair the meeting

- b) The Secretary to the Committee may delegate the functions of the secretary to the Director Debt Recording and Settlement from time to time
- c) The Committee may from time to time, co-opt other members as it may deem necessary for the proper and efficient discharge of its functions
- d) The Committee shall meet not less than four times in every financial year
- e) The quorum for the conduct of the meeting of the Committee shall be three members
- f) The Committee shall regulate its own procedures.

27. **The Cabinet Secretary, National Treasury and Planning further stated that the Fund Administrator shall be,** the Head of the Public Debt Management Office in accordance to Regulation 206(1) of the Public Finance Management (National Government) Regulations 2015.

28. **The Administrator of the Fund shall perform the following duties:**

- a) undertake day to day operations of the Fund;
- b) supervise and control the administration and management of the Fund;
- c) prepare the Fund's work plan including, annual securities issuance and redemption plan and investment schedule and submits to the Committee for consideration and recommendation by the Cabinet Secretary;
- d) borrow and deposit monies into the Fund for the purpose of debt redemption;
- e) formulate policies to achieve the objective and purpose of the Fund and submit to the Committee for consideration;
- f) prepare the estimates of revenue and expenditure of the Fund for each financial year and submit to the Committee for consideration and recommendation;
- g) prepare quarterly management reports for review and recommendation;
- h) open any bank account of the Fund in accordance with Section 28 of the Public Finance Management Act 2012 with approval of the Cabinet Secretary;
- i) prepare quarterly management reports in accordance with the provisions of the Public Finance Management Act 2012; and
- j) perform such other duties as may be considered necessary by the Cabinet Secretary from time to time for the proper administration and management of the Fund.

29. **He explained that the Secretariat to the Fund** shall be appointed by the Cabinet Secretary in charge of Finance and shall ensure that the Fund has the resources and skills to manage the day-to-day operations of the Fund and that the financial year of the Fund shall run from the 1st July to the 30th June. Monies received in the sinking Fund may be invested in government securities in accordance with the approved cash flow plan. The Fund shall be audited in accordance with the

provisions of the Constitution of Kenya, the PFM Act 2012 and the Public Audit Act 2015.

30. On Reporting Framework the Cabinet Secretary, National Treasury informed the Committee that:

- a) The Administrator of the Fund shall prepare the annual financial and non-financial reports in accordance with the PFM Act 2012 and the Public Audit Act 2015 and submitted to the Accounting Officer for approval before submission to the Auditor-General for Auditing.
- b) The Annual financial and non-financial statements shall be submitted to the Auditor-General for Audit within three months after the end of the financial year in accordance with the Public Audit Act 2015.
- c) The Administrator of the Fund shall prepare an annual general performance report of the Fund.

31. And in the in the event of winding up the Fund, it was noted that:

- a) The Administrator of the Fund shall pay any credit balance in the Fund into the National Exchequer Account to the credit of the National Government while other assets of the Fund shall be transferred to the Ministry responsible for finance.
- b) The Cabinet Secretary shall pay any deficit in the Fund from the Funds of the National Government in the National Exchequer account upon approval of Parliament.
- c) The Committee shall prepare the final winding up report not later than six months from the date of the decision to wind up the Fund.
- d) The Cabinet Secretary shall submit a final statement of accounts of the Fund to Parliament.

32. In light of the above deliberations on the Public Finance Management (Sinking Fund) Guidelines 2021, The National Treasury requested the Committee to adopt the guidelines for further application in Public Debt Management and specifically on debt servicing in Kenya.

33. CONSULTATIONS BEFORE MAKING THE STATUTORY INSTRUMENT

34. As per sections 5 and 5A on proof and demonstration of sufficient public consultation, the National Treasury, in the explanatory memorandum indicated that it had invited interested members of the public to submit written comments on the draft guidelines.

35. The National Treasury did not however provide proof of the consultations made in the development of the guidelines.

2.1.2 SUBMISSION FROM THE GOVERNOR, CENTRAL BANK
OF KENYA, DR. PATRICK NJOROGE

36. The Governor, Central Bank of Kenya explained that the overarching objective of strengthening public finances and making repayments as opportunities arise to reduce the overall cost of debt is supported. The Public Finance Management Act and Regulations allow the creation and operation of a Sinking Fund. However, this is quite constrained:

- a) Redemption of Government Securities (Regulations Sec 206). Sinking fund is circumscribed to “pay for a bond, repurchase or early redemption of Treasury Bonds”
- b) He raised concerns about an expanded class of Government debt (e.g. loans), and therefore inconsistency with other laws and architecture of public finance.
- c) Sinking funds bespeak of repayment or financing constraints by the issuer bearing in mind constrains of one revenue stream or a dwindling resource envelope.
- d) Lender requiring greater assurance of repayment, as a condition of lending.
- e) Difficult to reconcile for a sovereign with a good repayment record and strong public financial management. Also does to augur well with efficient use of public resources (including the opportunity costs of the idle funds).

37. **He pointed out Contradiction between Guidelines and CBK Act & Operations as follows; that** clause 5(e) of the Guidelines indicates that the sources of funds will include “Foreign exchange gains from external loans to the National Government.”

- a) Conflicts the understanding that the Sinking Fund in is Kenya Shillings.
- b) Contradicts CBK’s statutory mandate on foreign exchange, including “hold and manage foreign exchange reserves” under Section 4A (1) of the CBK Act. Inadvertent inconsistency with other laws and architecture on foreign exchange.

38. **The Governor stated that;** the draft Guidelines are not consistent with other laws, particularly PFM Act & Regulations, and CBK Act. A detailed review by the Attorney General’s Office is needed.

- a) Since the stated “Objects and Purposes of the Fund” can be achieved currently, the fundamental reasons for this initiative should be probed further.
- b) A Sinking Fund is not the solution (silver bullet) for the critical objective of strengthening public finances and reducing the public debt burden. A wider conversation on public debt is needed.

39. **Finally on the history of debt repayment, the Governor informed the Committee that—**

- a) Kenya is a sovereign with good repayment record and strong public finance management and therefore there is no need for a sinking fund.
- b) The country already has a myriad of effective tools at its disposal to ensure that debt is sustainably managed. These tools include: the ability to roll over previous debt, the option of switching between creditors; the option to lengthen maturity debt; refinancing of external debt through borrowing and offsetting older debt; the executives' overdraft facility with the CBK.
- c) Committing funds to a sinking fund would essentially lend those funds idle which is in contravention of efficient use of public resources. In addition, the country is likely to suffer opportunities costs associated to idle funds.
- d) Zambia had set up a sinking fund as a tool for debt management but since the macros of the economy of Zambia were wrong to begin with, the sinking fund proved ineffective in assisting Zambia out of the debt quagmire it has found itself in due to amongst other things an unsustainable debt to GDP ratio.

CHAPTER THREE

COMMITTEE FINDINGS

3.0 Committee Observations

40. The Sessional Committee on Delegated scrutinized the Public Finance Management (Sinking Fund) Guidelines 2021, against the Constitution of Kenya, 2010, the Public Finance Management Act of 2012, Central Bank of Kenya Act of 1966, and the Statutory Instruments Act (No 23 of 2013) and pursuant to Standing Order 221 (4) (b) of the Senate Standing Orders.
41. On specific provisions of the Public Finance Management (Sinking Fund) Guidelines 2021, the Committee made the following observations; -
- c) According to the Debt Management Strategy 2021, Debt redemptions are projected to jump from KSh. 499.7 billion as at the end of FY 2020/21 to KSh 990.7 billion in the FY 2023/24, an increase of by 98% in a span of two fiscal years.

Current framework for payment of debts

- d) Kenya set up the first sinking fund in the 1960s under the Internal Loans Act, Chapter 420. The fund remained dormant and the process of winding up the fund is currently before the National Assembly.
- e) Kenya presently pays the public debt from the Consolidated Fund Services (CFS). Section 50 (6) of the Public Finance Management Act which provides that ***public debt incurred by the national government is a charge on the Consolidated Fund, unless the Cabinet Secretary determines, by regulations approved by Parliament, that all or part of the public debt is a charge on another public fund established by the national government or any of its entities.***
- f) The Consolidated Fund Services also caters for other obligatory payments such as pension and salaries for independent constitutional office holders.
- g) Section 50 (8) of the Public Finance Management Act permits the Cabinet Secretary in charge of Treasury, with the ***approval of Parliament, (to) establish such sinking fund or funds for the redemption of loans raised under this Act by the national government.***

- h) In addition, Regulation 206 (3) of the Public Finance Management (National Government) Regulations, 2015 mandates the Cabinet Secretary *to publish in the Kenya Gazette the guidelines for the management of the Fund.*

Conflict with the Public Finance Management Act, 2012 and its regulations

- i) Despite the foregoing, Regulation 206 (2) of the Public Finance Management (National Government) Regulations, 2015 limits the scope of the fund to **payment of expenses of, or incidental to redemption of an issue of Government securities and the redemption of an issue of Government securities.**
- j) The Committee notes with concern that despite the limitation above, the guidelines as currently drafted expand the scope of the fund to include national government loans that are not envisaged in Regulation 206 (2) of the Public Finance Management (National Government) Regulations, 2015.

History of Debt Repayment and tools already in use

- k) The Committee confirmed from the Central Bank of Kenya that the country already has a myriad of effective tools at its disposal to ensure that debt is sustainably managed. These tools include: the ability to roll over previous debt, the option of switching between creditors; the option to lengthen maturity debt; refinancing of external debt through borrowing and offsetting older debt; the executives' overdraft facility with the CBK.
- l) The Committee concurred that committing funds to a sinking fund would essentially lend those funds idle.

Conflict with the Central Bank of Kenya Act

- m) Section 4A (1) of the Central Bank of Kenya Act mandates the Central Bank of Kenya to *formulate and implement foreign exchange policy and hold and manage its foreign exchange reserves.* It further observed that clause 5 (e) of the guidelines provides that one of the sources of the Fund shall consist of *foreign exchange gains from external loans to the National Government.* The Committee noted that the Treasury is not mandated to hold foreign exchange reserves and as a result clause 5 (e) of the guidelines is inconsistent with section 4A (1) of the Central Bank of Kenya Act.

- n) The Committee further noted that the Guidelines failed to take into consideration Clause 4A (1) (e) of the CBK Act which mandates the CBK to be the fiscal agent of the government.
- o) The Central Bank of Kenya informed the Committee that whereas the sinking fund is in local currency (Kenya Shillings) the guidelines under clause 5 (e) provide for the realization of foreign exchange gains from external loans to the National government. The Committee was further informed that realization of foreign exchange gains from external loans to the National government would not ordinarily happen unless the amount of local currency accumulated was more than that needed to offset the external obligations at the prevailing exchange rate.
- p) Due to the foregoing, the Committee observed with concern and acquiesced that it is unclear how foreign exchange gains from external loans to the National government will be realized when the sinking fund is comprised of local currency.
- q) The guidelines propose the establishment of a Sinking Fund Advisory Committee which is proposed to consist of the Principal Secretary in charge of finance as the Chairperson; the Director General, Public Debt Management Office as the Secretary; the Director -General, Accounting Services and Quality Assurance and the Director -General Public Investment and Portfolio Management. The Committee observed that the Central Bank of Kenya is not a member of the Committee yet under Section 4A (1) (e) of the Central Bank Act, the Bank is the fiscal agent of the government.

Other observations

The Committee also observed that as currently drafted the guidelines—

- i. Don't provide for strong oversight over the Fund. There is need to enhance the role oversight role of Parliament in the Fund, this can be done by requiring that regular periodic financial and non-financial reports prepared by the Fund administrator are submitted to Parliament for scrutiny.
- ii. Do not ring-fence the funds. There is need to ensure that the funds are ring-fenced so that it is only used for the set objective of redemption of public debts.
- iii. Do not provide a mechanism for controlling the administrative expenditure. There is need to establish a mechanism of controlling the administrative expenditures to ensure that there is no wastage of public funds.

- iv. Did not undergo effective public participation as anticipated under the Constitution and section 5 of the Statutory Instruments Act. From the presentations made by the Central Bank, a key player in the public financial sector with a constitutional responsibility to formulate monetary policy, it was clear that it had not been consulted in the making of the regulations. Whereas the National Treasury indicated that it had carried out consultations, it provided no evidence of such consultations. There is therefore need for effective consultations to be undertaken with, not only key stakeholders but, the general public as anticipated by the Constitution and section 5 of the Statutory Instruments Act.

CHAPTER FOUR

COMMITTEE RECOMMENDATION

Based on the foregoing observations, and pursuant to section 15 (1) of the Statutory Instruments Act, 2013 and in accordance with standing order 221 (4) (b) of the Senate Standing Orders, the Senate Sessional Committee on Delegated Legislation recommends to the Senate that the Public Finance Management (Sinking Fund) Guidelines, 2021 be annulled.

ANNEXES



Annex 1

Letter from the Cabinet Secretary, National Treasury and Planning dated 30th August, 2021 and the Presentation made before the Committee.

Annex 2

Letter from the Governor, Central Bank of Kenya dated 3rd September, 2021.

Annex 3

The Public Finance Management Act No 18 of 2012.

Annex 4

The Kenya Gazette Notice Vol. CXXIII-NO 117 on PFM (Sinking Fund) Guidelines, 2021.

Annex 5

The Central Bank of Kenya Act, Chapter 491.

Annex 6

The Public Finance Management Act Subsidiary Legislation.

Annex 7

Presentation made by the Governor Central Bank of Kenya to the Committee.

Annex 8

The Public Finance Management (Sinking Fund) Guidelines, 2021.



TWELFTH PARLIAMENT | FIFTH SESSION

**MINUTES OF THE THIRTEENTH MEETING SITTING OF THE
SESSIONAL COMMITTEE ON DELEGATED LEGISLATION HELD ON
MONDAY, 6TH SEPTEMBER, 2021 ON THE ZOOM ONLINE MEETING
PLATFORM AT 10:00 A.M.**

PRESENT

- | | |
|--------------------------------------|-----------------------------------|
| 1. Sen. Mwinyihaji Mohammed Faki, MP | - Chairperson (<i>Chairing</i>) |
| 2. Sen. Poghisio Samuel Losuron, MP | - Member |
| 3. Sen. Farhiya Haji Ali, MP | - Member |
| 4. Sen. Judith Pareno, MP | - Member |
| 5. Sen. Halake Abshiro, MP | - Member |
| 6. Sen. Mary Yiane Seneta, MP | - Member |

ABSENT WITH APOLOGIES

- | | |
|--------------------------------------|--------------------|
| 1. Sen. Agnes Kavindu Muthama, MP | - Vice Chairperson |
| 2. Sen. Erick Okong'o Mogeni, SC, MP | - Member |
| 3. Sen. Anwar Loitip, MP | - Member |

IN ATTENDANCE

- | | |
|------------------------|--|
| 1. Dr. Patrick Njoroge | - Governor, Central Bank of Kenya |
| 2. Mr. Erick Abuga | - Director, Office of the Governor Central Bank of Kenya |
| 3. Mr. David Luusa | - Director, Financial Markets |

SECRETARIAT

- | | |
|---------------------|--------------------------|
| 1. Boniface Kiambi | - Clerk to the Committee |
| 2. Ms. Sombe Toona | - Legal Counsel |
| 3. Mr. Tiyon Joseph | - Research Officer |

MIN. NO. SEN/SCDL/034/2021: PRELIMINARIES

The Chairperson called the meeting to order at 10:10 a.m. followed by a word of prayer led by Sen. Poghismo Samuel Losuron, MP.

MIN. NO. SEN/SCDL/035/2021: ADOPTION OF THE AGENDA

The Committee adopted the agenda of the Sitting, as set out below, having been proposed by Sen. Judith Pareno, MP and seconded by Sen. Poghismo Samuel Losuron, MP : -

1. Preliminaries;
 - a) Prayer
 - b) Introductions
2. Adoption of the Agenda;
3. Meeting with the Governor, Central Bank of Kenya to deliberate on the Public Finance Management (Sinking Fund) Guidelines 2021;
4. Any Other Business; and
5. Adjournment.

MIN. NO. SEN/SCDL/036/2021: CONSIDERATION OF THE PUBLIC FINANCE MANAGEMENT (SINKING FUND) GUIDELINES 2021

The Governor, Central Bank of Kenya informed the Committee that as follows:

- a) That Kenya is a sovereign with good repayment record and strong public finance management structures and therefore there was no need for a sinking fund.
- b) The country already had a myriad of effective tools at its disposal to ensure that debt is sustainably managed. These tools include: the ability to roll over previous debt, the option of switching between creditors; the option to lengthen maturity debt; refinancing of external debt through borrowing and offsetting older debt; the executives' overdraft facility with the CBK.
- c) The Committee was informed by the Central Bank of Kenya that Zambia had set up a sinking fund as a tool for debt management but since the macros of the economy of Zambia were wrong to begin with, the sinking fund proved ineffective in assisting Zambia out of the debt quagmire it has found itself in due to amongst other things an unsustainable debt to GDP ratio. From the foregoing case study, the Committee surmised that a sinking fund may not be

an effective debt management tool and concurred with the Central Bank that the tools currently in place for purposes of debt management are sufficient.

The Central Bank Governor informed the committee that the guidelines conflict with the Central Bank of Kenya Act in the following ways;

- a) Section 4A (1) of the Central Bank of Kenya Act mandates the Central Bank of Kenya to *formulate and implement foreign exchange policy and hold and manage its foreign exchange reserves*. It further observed that clause 5 (e) of the guidelines provides that one of the sources of the Fund shall consist of *foreign exchange gains from external loans to the National Government*. The Committee noted that the Treasury is not mandated to hold foreign exchange reserves and as a result clause 5 (e) of the guidelines is inconsistent with section 4A (1) of the Central Bank of Kenya Act.
- b) The Committee further noted that the Guidelines failed to take into consideration Clause 4A (1) (e) of the CBK Act which mandates the CBK to be the fiscal agent of the government.
- c) The Central Bank of Kenya informed the Committee that whereas the sinking fund is in local currency (Kenya Shillings) the guidelines under clause 5 (e) provide for the realisation of foreign exchange gains from external loans to the National government. The Committee was further informed that realisation of foreign exchange gains from external loans to the National government would not ordinarily happen unless the amount of local currency accumulated was more than that needed to offset the external obligations at the prevailing exchange rate.
- d) Due to the foregoing, the Committee observed with concern and acquiesced that it is unclear how foreign exchange gains from external loans to the National government will be realised when the sinking fund is comprised of local currency.
- e) The guidelines propose the establishment of a Sinking Fund Advisory Committee which is proposed to consist of the Principal Secretary in charge of finance as the Chairperson; the Director General, Public Debt Management Office as the Secretary; the Director -General, Accounting Services and Quality Assurance and the Director -General Public Investment and Portfolio Management. The Committee apprehensively observed that the Central Bank of Kenya is not a member of the Committee yet under Section 4A (1) (e) of the Central Bank Act, the Bank is the fiscal agent of the government.
- f) The Committee further agreed with the Central Bank of Kenya that the establishment of a sinking fund creates a perception that the country may be unable to meet its debt obligations when they fall due which according to the

assessment of the Committee and the Central Bank is not the case since Kenya has met its debt obligations consistently and has maintained good standards of debt management.

During deliberations, the Committee noted that-

- a) According to the Debt Management Strategy 2021, Debt redemptions are projected to jump from KSh. 499.7 billion as at the end of FY 2020/21 to KSh 990.7 billion in the FY 2023/24, an increase of by 98% in a span of two fiscal years.
- b) Despite the foregoing, Regulation 206 (2) of the Public Finance Management (National Government) Regulations, 2015 limits the scope of the fund to **payment of expenses of, or incidental to redemption of an issue of Government securities and the redemption of an issue of Government securities.**
- c) The Committee notes with concern that despite the limitation above, the guidelines as currently drafted expand the scope of the fund to include national government loans that are not envisaged in Regulation 206 (2) of the Public Finance Management (National Government) Regulations, 2015.
- d) The Committee concurred that committing funds to a sinking fund would essentially lend those funds idle which is in contravention of efficient use of public resources. In addition, there are opportunities costs associated to idle funds that the country is likely to suffer.
- e) The guidelines don't provide for strong oversight over the Fund. There is need to enhance the role oversight role of Parliament in the Fund, this can be done by requiring that regular periodic financial and non-financial reports prepared by the Fund administrator are submitted to Parliament for scrutiny.
- f) The guidelines do not ring-fence the funds. There is need to ensure that the funds are ring-fenced so that it is only used for the set objective of redemption of public debts.
- g) The guidelines do not provide a mechanism for controlling the administrative expenditure. There is need to establish a mechanism of controlling the administrative expenditures to ensure that there is no wastage of public funds.

RECOMMENDATION

After consideration of the Public Finance Management (Sinking Fund) Guidelines, 2021, pursuant to section 15 (1) of the Statutory Instruments Act and Standing Order 221 (4) (b), the Sessional Committee on Delegated Legislation recommended that the

Senate resolves that the Public Finance Management (Sinking Fund) Guidelines 2021 be annulled.

MIN. NO. SEN/SCDL/037/2021: ADJOURNMENT

Having concluded the business as set out in the agenda, the meeting was adjourned at 11.15 a.m. The next meeting would be on notice.



SIGNED:

DATE: 7TH SEPTEMBER, 2021

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