POSITION PAPER ON BUDGET POLICY STATEMENT 2014

February 28, 2014

The Institute of Certified Public Accountants of Kenya ***(ICPAK)*** *is the professional organization for Certified Public Accountants in Kenya established in 1978 by the Accountants Act, CAP 531. ICPAK is dedicated to development and regulation of the accountancy profession in Kenya so as to enhance its contribution and that of its members to national economic growth and development. In this regard, ICPAK wishes to advise the public that an Accountant by Law is an individual who has qualified by passing the three levels of the CPA examinations and is duly registered by the Institute of Certified Public Accountants of Kenya.*

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1.0 OBJECTIVE

This paper reviews and makes various proposals on the Budget Policy Statement (BPS) 2014 in cognizant to the constitutional requirement of public participation and in the latter and spirit of Article 217.2(d) that explicitly requires professional bodies to make submissions on the allocation and division of revenue.

2.0 INTRODUCTION

The National Treasury is required under section 25(2), and (9) of the Public Finance Management Act (2012) to prepare and submit the Budget Policy Statement to Parliament by 15th February each year, and subsequently publish and publicize it not later than 15 days after its submission to parliament. In accordance with section 25(3) the Budget Policy Statement sets out the broad strategic priorities and policy goals that will guide the national government and the county governments in preparing their budgets both for the following financial year and over the medium term.

This yearôs BPS is the first BPS to be prepared under the Jubilee Government and the second under the Public Finance Management Act, 2012. Under the auspice for *Economic Transformation for a Shared Prosperity in Kenya,* the BPS outlines the governmentôs policies, priority programs and strategic interventions intended to address the key challenges facing the country and that would accelerate economic transformation towards the attainment of Vision 2030. It articulates different structural reforms as well as sectoral expenditure programs to be implemented under the Medium Term Expenditure Framework for 2014/15 ï 2015/17 fashioning them towards achieving the governments development goal of economic transformation for a shared prosperity.

3.0 STRUCTURE AND CONTENTS

The BPS 2014 is organized as prescribed under Section 25 (4) of the Public Finance Management Act 2012. It has included an assessment of the current state of the economy and the financial outlook over the medium term, including the macroeconomic forecasts and provided the financial outlook with respect to Government revenue, expenditures and borrowing for the next financial year and over the medium term.

It elaborates on the fiscal responsibility principles and financial objectives over the medium term including limits on total annual debt and provides the proposed expenditure limits for the national government, as well as those of Parliament and the Judiciary. It further proposes the indicative transfers to county governments.

The outlined Government strategy for economic transformation focuses on five broad areas, these are:

i. Creating conducive business environment in order to encourage innovation, investment, growth and expansion of economic and employment opportunities;
ii. Investing in agricultural transformation and food security to expand food supply, reduce food prices, support expansion of agro-processing industries and spur export growth;
iii. Investment in first class transport and logistics hub and scaling investments in other key infrastructure, including roads, energy and water to reduce cost of doing business and improve competitiveness;
iv. Investing in quality and accessible healthcare services and education as well as social safety net to reduce burden on the households and complement and sustain our long term growth and development; and
v. Further entrenching devolution for better service delivery and enhanced rural economic development.

BPS further enumerates the institutional reforms that the government wants to introduce. This includes structural reforms, reforms in governance, Public finance management, asset management, tax and revenue, financial and public sector reforms and fiscal structural reforms among others.

4.0 ICPAK INPUTS & AREAS OF CONCERN

ICPAK commends the proposed reforms that would enhance economic growth and prudence in public finance management. Following a critical analysis of the document, ICPAK is of considered view on the following proposed reforms:

	PROPOSED REFORM		ICPAK COMMENTS
	Pillar I: **Creating a Conducive Business Environment for Employment**		
1.	(14) Governance	ii) economic crime investigation and assets recovery;	The government should come strong on bringing to book those who have grabbed or misappropriated public assets and or grossly violated the set code of conduct.
		(iv) Improving governance in priority areas, of medical supplies, free primary and tuition in schools, public works, national police service, revenue administration, procurement, immigration and lands.	To enhance prudent use of allocated resources, provide for regular audit and professionalism through continued capacity building of professionals in the stated priority areas. Allocate Resources towards the operationalization of the proposed structures in new Procurement Bill ï
		A Kenya Integrity Program (KIP) to be developed in 2014, partly entrenching Code of Conduct and vetting of public officers, starting with those in the above sub-sectors. This is also set to provide a framework for consultation, monitoring and reporting to enhance accountability in the public service.	Strengthen KIP framework and structure for it to live to fulfill its mandate and secure it from mutilation by the forces of impunity in the country. While necessary, vetting alone is insufficient in enhancing integrity; credibility, professionalism and accountability are of essence. Enforcing the code of conduct will be a challenge if the said officers are un-regulated. Making it mandatory for the key officers to be regulated professionals will enhance the

			realization of KIP goals.
2.	**PFM Oversight Institution**	The government plans to enhance efficiency, effectiveness, transparency and accountability in the use of public resources through strengthening the institutional capacity of public finance management oversight agencies. It plans to digitalize its payment transaction by April 2014 to hasten service delivery, reduce transaction cost and safeguard revenue.	While we welcome the digitalization of payment transactions, April 2014 looks a rather ambitious timeline given that most government entities including the county governments lack the necessary structures and the technical know-how to ensure digitalization. Baseline survey should be conducted to establish preparedness and underlying challenges before roll-out The proposed digital platform should be pre-tested and the necessary loop-holes for mismanagement and corruption sealed before roll-out
		Further, it plans to re-structure the National Treasury to align it with its core mandate of economic and financial management and equip it with requisite competencies. The capacity of the oversight institutions will be strengthened, by among others, adoption of modern work environment and training and capacity building in order to enhance their capabilities in audit and financial reporting	Oversight institutions require enhanced resources to be able to do their work effectively ï The Auditor General and the Controller of Budgets need more resources, both human and capital to enhance oversight. Qualified Economists and regulated Accountants should be utilized in ensuring prudent Public financial management in all public entities
3.	**Expenditure Management**	As part of economic transformation and as a measure of improving efficiency and effectiveness in utilization and execution of the budget, the government proposes to deepen	The ever rising wage-bill and public debt call for sturdy austerity measures that would curb the Triggers of increased public expenditure. The recent Auditor General Reports expose a number of gaps in

		public expenditure reforms. This would include ✓ Rationalizing public expenditures to remove overlaps and waste, ✓ Rolling out of leasing of assets in all State Departments and public agencies, ✓ Developing and enforcing cost benchmarks for projects and consumables, ✓ Entrenching performance benchmark of at least 80 percent of the development budget, and strengthening the program budget. ✓ Expenditure tracking and value for money audits undertaken regularly to ensure efficiency in use of resources at both levels of Governments.	expenditure of public funds - imprudent management of imprest and petty cash especially at the county level - tighten their management in the proposed PFM regulations Adoption of more detailed budget lines in the program budget would aid in setting the performance indicators and ease the absorption of budgets by Wanjiku who should also participate in the social audits
4.	**The integrated financial management information system (IFMIS**	The government proposes to make IFMIS fully operational as an end-to-end transaction platform. The Procure-to-Pay which integrates master item lists and cost benchmarks is set to be rolled out in 2014. The integrity and operational capability of the system will be assured, including through regular independent audits, integration with external systems and a state of the art call centre. The Public Finance Management Regulations and a new Procurement law will be submitted to Parliament before August, 2014 in order to	Auditor General should conduct a thorough audit of IFMIS to establish its implementation weaknesses and challenges before full roll-out. Treasury Should fast-track the enactment of PFM regulations and establish tight structures to ensure its full implementation. Treasury and the national government together with professional bodies should ensure the soundness of IFMIS is enhanced via continuous capacity development of county governments and close the available loopholes for corruption.

		entrench prudent public finance management.	
5.	**Asset Management:**	Efficient management of Government assets will be given priority as part of expenditure reforms. The National Treasury will undertake an asset registration exercise and establish an updated Asset Registry for all Government assets. Leasing of assets will be rolled out in all State Departments and state corporations to cover such assets as equipment, plants and machinery, motor vehicles and ICT hardware, among others. All existing fleet of Government motor vehicles will be fitted with fleet management system to ensure optimal utilization and management.	The government should prioritize and allocate necessary resources to quickly finalize the development and digitization of the asset register. Further, the Transition Authority and Auditor General, through the Integrated National and County Assets Register Centre (INCAR) should strive to finalize the Interim assets register and avail the Report to the Public Scrutiny. The leasing out policy should be developed to curb any malpractices that may be as a result of leasing of assets Asset Tagging system should be introduced in all government entities for continuous monitoring of their movement Proper Asset valuation should be done to all public assets and their current value regularly updated in Asset Register Proper stewardship of public assets should be encouraged
6.	**Tax and Revenue Reforms**	The strategy for strengthening revenue efforts and improve ease of doing business will prioritize measures to simplify tax systems, leverage automation, expand the tax base, rationalize tax incentives and exemptions, expand tax net to capture the informal sector and make operational the two inter-dependent revenue agencies ï the Inland Revenue Agency and Customs and Border Control Agency. Reflecting the impact of new	Kenyaœ̂s economy is fragile and must be cushioned against external incursions by cheap imports. Our taxation policies must be structured to offer that support, a vital step in reforming the tax system for efficiency and effectiveness of the economy. Impact of the proposed VAT reforms should be evaluated in consideration of the social-economic impact on Wanjiku Tax Appeals Tribunal Act - the gazettement of this should be

		law, broad base effect and a more effective VAT administration, the VAT revenue effort will be increased by at least 4 percent as a share of GDP by 2017. To further simplify and modernize tax legislations, a new Excise Management Bill, Extractive Industry Tax regime (Income Tax Amendments), and a Tax Procedure Bill will be developed and submitted to Parliament in 2014. In the course of FY2014/15, a review and modernization of the Income Tax law will commence and completed in the course of 2015.	prioritized Administrative reforms on the system of VAT remissions should be undertaken and an objective system clearly spelt within the VAT Law to rule out indiscretion and abuse of the system
7.	**Financial Sector Reforms**	The objective of financial sector reforms is to create a vibrant, accessible, efficient and a stable globally competitive financial sector that promotes high level of savings to finance Kenyaós overall investment needs. Building on the progress made thus far, the establishment of the Nairobi International Financial Centre, enactment of a new Central Bank of Kenya law, re-organization of financial regulators under a Financial Service Council will be given priority in the course of 2014	SACCOs regulation ï The sector has grown immensely on both Assets and Liabilities hence, not a mean sector to be left on its own. The Financial Sector reforms should realign and prepare the financial sector towards the East-African regional single monetary dream ï A strategic plan should be populated Partner with other stakeholders to enhance financial literacy in the country. The national strategy for financial education should ensure that financial education is engraved in curriculum from the basic education
8.	**Public Sector Reforms**	It is proposed that for the public sector to play its facilitative role more effectively, the Government will rationalize and consolidate the civil service to eliminate overlaps and duplications of functions, reduce pressure on wage bill and	This is a welcome move however, it must be guided by objective review of matching skills to work and where necessary adopt the suitable system ï manual or digital. The government must conduct head counts through an

		enhance its performance accountability. Similarly, state corporations, regulatory agencies and research and training institutions will be rationalized and new organizations strengthened into lean, efficient, effective and accountable agencies to provide better service delivery.	independent body and clean the payroll and the ghost workers. The government should also establish and or review the policy/ criteria/ structures/ available frameworks for promotions in county Enhance the implementation of the service charter in the public sector There should be established an objective criterion for annual percentage salary increment to curb the continued agitation for increased salary from the civil service. Non-practice allowances and other benefits should be reviewed and rationalized to cater for all professionals Complains redress mechanisms should be established and a complaints register instituted in all public offices
	Under Pillar II - V the following proposals are worth noting:		
9.	**Established Funds**	The government establishes **various funds** ï Agri- Business Fund; Uwezo Fund, SME fund and the Social Protection Fund. It further commissions various high level **development projects** in all the key sectors - Million Acre Irrigation project, LAPPSET Project, Standard Gauge Railway, Airway, road and Pipeline expansions and the Laptop Project among others. These are multi-billion projects that necessitate proper accounting and professional management	There should be established a Framework or policy guideline for the establishment of funds- many funds are being introduced by the day The Institute is of the considered opinion that for good governance, transparency and accountability, all the Chief Finance Officers or any other person responsible for finance function and the persons responsible for the internal audit function of all these entities and the said projects, should be professionally regulated accountants.

		of the financial resources invested	Independent Audit committees composed of accounting professionals should be established in all these entities for enhanced accountability of the allocated resources while ensuring value for money and return on investment. Performance reporting / periodic progress reports update should be mandatory.
10.	**The Buy Kenya Policy**	BPS envisions this as a training ground for Kenyan enterprises to expand local production for local and export market and one that encourages the formation of viable enterprises, especially by youth and women, under the Biashara initiative. The small and medium enterprise fund, including Uwezo Fund as well as adherence to at least 30 percent of all public procurement reserved for the youth, women and persons with disability	The institute welcomes this policy direction but recommends a review of successes and challenges of similar programs in the past to ensure that value for money is achieved. Further care should be observed that its implementation especially in terms of taxation and pricing should not be in such a manner that makes the local products more expensive the common man. Critical sectors of the economy that must be cushioned against incursion from cheap imports. Further, inputs to critical but sensitive sectors of the economy should be zero-rated The implementation of 30% reservation should be entrenched to the county level. Public Procurement preference should be given to local contractors and suppliers except where local capacity is not available as per the Public Procurement and disposal amended regulations (2009) Sec. 39 ï Constituents and citizen located and operating in the issuers locale
11.	**National and County Government**	National Government seeks to deepen its support to county governments as the centres for service	Indeed the national government has a key mandate not only in setting the taxation policy but also in protecting public

	Relationship	delivery and economic expansion, especially in the areas of public financial management, good governance practices and supporting the counties to be fully operational. Close collaboration between the two levels of government in terms of implementing the national development agenda, and critical policy initiatives will be encouraged. This will include moderating the zeal by counties to raise additional revenues and safe guarding a thriving business environment supportive of the private sector	interest; ensuring the purchasing power of the citizens is not eroded through continued taxation. Alternative sources of revenue should be pursued and development priorities set to avoid the unfair taxation at the county level. Counties should be assisted in exploring different tax avenues and in the collection of the existing baskets. Capacity building is needed at the county level Digitizing the revenue collection ï Invest in innovative alternatives and technology to collect revenue
	Fiscal Structural Reforms		
12	**Wage Bill;**	The Government sets to institute measures to contain the public wage bill and in order to have more resources for development funding. Some of the measures include payroll cleansing, staff rationalization, identification and trimming off of excess personnel. It is the Governmentôs undertaking to continue offering support and enhance the capacity of county governments and midwife the devolution process so as to encourage proper and transparent use of resources and encourage quality service delivery to Kenyans	Recent audits conducted have revealed a significant percentage of ghost workers in the public entities. This ópayroll cleansingô should be rolled out in all public entities. Given the rising wage bill, the national government should, Instead of employing new staff, re-deploy and capacitate the existing staff to save on the cost of hiring and training even as staff rationalization is undertaken. Concern has been raised on reduction of the salaries of the forwarded/ re-deployed staff- a national policy should be formulated to guide the rationalization process, deployment and re-deployment processes Harmonization of allowances / rationalization of salaries is

			necessary across all recognized professions.ï SRC Annual increments should not be bound by bargaining power but on job evaluation and performance evaluation ï Increment factored as a percentage of economic growth, average inflation in a given year. - elimination of ghost workers -
13.	**Development and Net Lending**:	About 47 percent of the development budget will be funded through project loans and grants not tied to conditionalities from development partners. This is expected to be about 4.5 percent of GDP in 2014/15 down from 5.5 percent in the revised budget of 2013/14. With improvement in procurement planning (following the expected review of the Procurement and Disposal Act), the absorption capacity of project funds is expected to increase resulting in a higher investment level in infrastructure activities	Since the success of the absorption is pegged on the yet to be reviewed- Procurement & Disposal Act ï The Institute proposes a quick passage of this Act to law ï
14.	**Overall Deficit and Financing:**	The overall budget deficit (including grants) in 2014/15 is projected to be about KSh 291.5 billion (equivalent to 6.3 percent of GDP). About 34.5 percent of this budget deficit will be covered by net external financing amounting to KSh.100.7 billion (2.2 percent of GDP), leaving about KSh 190.8 billion (4.1 percent of GDP) to be financed through domestic borrowing	The overall deficit is still on a worrying trend. Public Debt to GDP has been on the increase from 49% in 2013 to the projected 52% in 2014. This literally means half of Kenyaös assets are foreign owned since all our development is loaned ï concrete and practical ways of reducing public debt are needed. If not managed, we will continue to experience higher inflation rates and crowding out effect ï which is detrimental especially to the future generations.

15	**Fiscal Discipline**	There lacks clarity on what entails fiscal discipline ï a key component on the equitable share of revenue and a key determinant on CRA formulae.	National government should come up with an objective criteria of measuring fiscal capacity and efficiency and of ensuring fiscal responsibility and discipline Fiscal responsibility principles and indicators should be clear to all for objective measurement and review of county performance

5.0 SECTOR SPECIFIC ALLOCATIONS:

Prioritization and the key sectors

The priority areas of budgetary allocation are derived from Article 202 and 203 of the constitution. On non-discretionary expenditures, the national government has prioritized - Defense and National Intelligent Service (NIS), Parliament, Judiciary, Presidency, Office of the Attorney General Office & Department of Justice, DPP, Police services, TSC, Other constitutional Commissions and IOs and Elections.

The priority social sectors of education and health have a combined allocation of 30.1% of total discretionary expenditures with Energy, Infrastructure and ICT sector receiving the second largest share of resources pegged at 22.5 % of total discretionary expenditures. Other priority areas including internal security, rule of law, youth and development of arid regions which continue to receive adequate resources.

	MTEF SECTORS	2013/2014	2014/2015	% Change	Comment
1	**Agriculture, Rural and Urban Dev. Sector (ARUD)**	54.4	55.60	2.21%	Most functions in the sector are devolved - An increase should reflect in County allocation as a result. The sector composition has not been unbundled making it difficult to follow specific allocations
2	**Energy, Infrastructure & ICT (EII)**	216.5	250.00	15.47%	Some of the functions -public road transport and ferries and harbours etc have been devolved as per Schedule 4
3	**General Economic and Commercial Affairs**		13.80		The sector has been re-bundled hence difficult in ascertaining the exact allocations from the previous year More resources should be allocated to this sector due to its ability to generate revenue and significant contribution to the national grid (GDP)

4	**Health**		37.90		Most of the functions including payroll have been devolved. This is not reflected in the allocation to counties The Policy document does not spell out the government commitment to various commitments and declarations like the MDG, Abuja declarations among others Allocations for level 5 and referral counties have been omitted in this yearôs allocation
5	**Education**	276.2	296.00	7.17%	Double priority sector between the National and County governments despite clear functional distinction Does the amount factor continued Union negotiations and agreements made between the parties? Given the increased numbers of students unable to join secondary schools due to the increased intake and as a result of free primary education, the Budget should allocate significant resources on revamping, funding and management of payroll of the Pre-primary education, village polytechnics, home craft centres and children facilities left to counties to increase their absorption capacity or at best offer policy guidance on the same. ï Empower tertiary (TIVET) institutions with more resources to cope up with recent developments and absorption capacities of higher education
6	**Governance, Justice, Law and Order (GJLOs)**	123	133.20	8.29%	
7	**Judiciary**	15.1	17.70	17.22%	
8	**Public Administration & International Relations**	121.3	168.00	38.50%	
9	**Parliament**	17.5	19.20	9.71%	

10	**Labour and social services**	20.57971	21.30	3.50%	
11	**Environment Protection, Water & Natural Resources**	57.9	55.00	-5.01%	The only sector with a significant decrease in allocation yet Water as a social-economic right require more resources to meet the minimum provision Most of the functions have been devolved yet significant allocations remain at the national government which continues to roll out programs at the county level In the previous year, this sector included housing and hence difficult to ascertain the exact allocation for the FY 2013/14
12	**National security**	72.5	80.10	10.48%	
13					

6.0 RECOMMENDATIONS

In view of the above we recommend the following:

1. **Priority in resource allocation** ï preference should be given to sectors that contribute significantly to generation of revenue like Trade and Tourism, agriculture, rural and urban development among others

2. **The sectors should be un-bundled/ Demystified** ï The composition of the sectors is unclear and sometimes confusing. A look at the 2013/14 BPS and the 2014/15 underscore this point. For instance where is housing, last year it was under the subsector with Environment and Water, this year it appears under Agriculture, rural and urban development? A list of the various ministries and government entities in a given sector will benefit the readers and would help in reading and analysis.

   Further, in 2013/14, the Jubilee government reduced the number of ministries from the previous 44 to 18 by merging them. Did this cause any significant change in the composition of the sectors? In a nut-shell, it is not possible to follow the trend of allocation especially when this information has not been disaggregated and or differs from the last yearôs allocation/ projection.

3. **Ambiguity of terms- National strategic interventions and presidency -** Presidency and national strategic interventions have been introduced as part of the national interest ï There is no detailed explanation what these strategic interventions ï these are allocated KSh. 5billion. This reduces funds for other priorities. Presidency has also been introduced in this yearôs BPS ï How different is this allocation to that of state-house under public Administration?

4. **Allocation to counties-** Given that funding follows function- and that most of the Schedule 4 functions have been devolved, the Ksh. 221billion allocated to counties does not seem to reflect this reality. In the FY 2013/14 the county allocation was Ksh. 190billion. This was before the un-bundling of functions and proper costing of the functions had been done. We suggest a quick un-bundling of the functions and proper costing of the devolved functions to advise future allocations. Historical costing has been blamed for the existing inequalities and does not reflect on current levels of desired service delivery, digitization and effective and effectiveness in service delivery.

Recent Audit report reveal that county priorities are not aligned to the national priories and as per Schedule 4 of the constitution. Counties are still budgeting and allocating significant resources towards security and education despite these being distinct national government functions.

5. **Emergency kitty-** National preparedness for emergencies has always been questioned. Besides, utilization of the emergency kitty has never been audited to ascertain its usage and sufficiency -given that the allocation to the kitty has remained the same over the last three years. What is the guiding principle on the allocation?

6. **Costing of Functions and Program based budgeting -** Since the historical cost of functions does not capture the current realignment and structure as in schedule four of the constitution and given that the Transitional Authority did not finalize the costing of functions, we recommend that an independent audit be done to establish the current cost to advice future budgets. Historical data on cost should be a base for costing the functions. Further, we recommend that the program based budgeting approach require detailed budget lines to aid in further analysis of the cost of functions, programs and projects.