The Institute of Certified Public Accountants of Kenya

ICPAK SUBMISSIONS

ON

THE DRAFT BUDGET POLICY STATEMENT 2021

PARAGRAPH OF BPS 2020	ISSUE OF CONCERN	ICPAK RECOMMENDATIONS
Para 9 and 10: Domestic Economic Development	The outbreak and spread of the Covid-19 Pandemic and the ensuing containment measures have devastated both global and local economies alike. The effect as demonstrated by the data from the Kenya National Bureau of Statistics is as follows; • The global economy is projected to contract by 4.4 percent in 2020 from a growth of 2.8 percent in 2019 • The Sub-Saharan African region has not been spared the negative impact of the pandemic with the region projected to contract by 3.0 percent in 2020 from a growth of 3.2 percent in 2019 • Growth in the East African Community (EAC) region is estimated to slow down to 1.0 percent in 2020 compared to a growth of 6.2 percent in 2019. • In Kenya, the economy is estimated to slow down to around 0.6 percent in 2020 from a growth of 5.4 percent in 2019. It is further projected to recover and grow by about 6.0 percent in the medium term. The BPS further outlined the following risks: **a. Inflation** Inflation rate expected at 5.0 percent which is within the Government target range. The economy is expected to remain competitive in the external market with the exchange rate against major currencies remaining stable even amid COVID-19 pandemic. Overall average monthly inflation between March and December 2020 remained stable at 4.9 percent due to favourable weather	Although this projection is consistent with World Bank's data of to 5.9% in 2020 and 6.0% in 2021, the challenge of this growth premise is that it doesn't seem to adequately incorporate the impact of the COVID crisis and the post COVID economic recovery strategy remains unclear. There is need to lower our expectations due to the following factors: ▪ Impact of locust invasion to food security in the medium term is yet to subside ▪ Continued charged political climate as a result of ongoing campaigns for Building Bridges Initiative (BBI) and early 2022 political campaigns ▪ Changing and unpredictable weather patterns given that Kenya still relies heavily on rainfed agriculture. ▪ The recovery of Kenya's economy from the effects of the COVID-19 pandemic is predicated on normal weather supportive of agricultural output and a swift and well targeted policy response to COVID-19. ▪ According to the Kenya Economic Update by the World Bank, the pandemic increased poverty by 4% or an additional 2 million poor) while the unemployment rate increased sharply, approximately doubling to 10.4 % as measured by the KNBS Quarterly Labor Force Survey. ▪ Emerging and developing markets face a health crisis from the pandemic in addition to severe demand shock, tightening in global financial conditions and a plunge in commodity prices Falling demand and revenues, reduced input supply, tightening of credit conditions, and increased uncertainty. The damage is aggravated

	conditions and lower international oil prices. With the revision of the tax measures instituted by the government during the COVID-19 period, inflation is likely to increase, but is expected to remain within the target range. **b. Interest Rates** The uncapping of interest rates in 2019 was expected to expand the private sector and stimulate business growth and overall performance of the economy. The growth in credit to the private sector, however, slowed down in 2020 due to measures undertaken by global and the national governments to contain the spread of COVID-19 pandemic. Private sector credit grew by 8.1 percent in the 12 months to November 2020 compared to a growth of 7.3 percent in the year to November 2019 **c. Exchange Rates** Exchange rate fluctuations have an effect on current account balance and the amount of debt service repayable on foreign denominated loans. The Kenya shilling weakened against major currencies in 2020. An increasing current account deficit occasioned by a reduction in exports and increased imports will lead to further depreciation of the Kenya Shilling. This is expected to lead to costly foreign debt repayment obligations in servicing of foreign denominated loans in the medium term.	by the presence of a large informal sector, high poverty rate and unemployed youth population ▪ IMF estimates show that the level of estimated GDP at the end of 2021 in both advanced and emerging markets is expected to remain below the pre-virus baseline, highlighting the long-term effects of the pandemic. ▪ For Kenya, according to the World Economic Outlook, IMF, 2020, it is estimated that economic growth could contract to 1.0% comparable to the 0.2% of post-election violence, drought and global financial crisis. ▪ Decline in international trade, travel and domestic consumption is further projected to suppress revenue from consumption taxes on which the majority of low- and middle-income countries rely ▪ Further outlined risks with regard to Inflation, interest and exchange rates coupled with increase in fuel prices is expected to have a negative tall on the economy Recommendations The Institute recommends as follows; a) Boost local production and manufacturing: The country has an opportunity to boost local manufacturing industries. PPEs for the protection of frontline healthcare workers as well as the general public, many apparel manufacturers including SMEs in the Textiles and Apparel sector have taken to producing fabric masks and protective gowns to deal with the pandemic. b) Notably, RIVATEX in Eldoret and KICOTEC in Kitui have stepped up production of face masks and are receiving support from the government through the COVID-19 fund to enable continued production
Para 11: value of Per Capita	According to the Draft BPS 2021, Per capita income rose from Ksh 113,539 in 2013 to Ksh 204,783 in 2019, a compounded annual	Since majority of Kenyans are employed in the informal sector, the Institute recommends as follows;

Income and Job creation	growth rate of 11.5 percent. This enabled generation of around 827,000 new jobs per year in the period 2013 - 2019 up from 656,500 new jobs per year in the period 2008 -2012 This demonstrates that the informal sector is the greatest employer in Kenya. This brings to the fore the problem of shadow economy whereby taxes are not paid, and regulations not strictly followed for cash transactions. A report by Financial Sector Deepening (FSD) shows that 96% of businesses in Kenya receive their payments in cash. This could be alluded to two things: One, the fact that 95% of the country's businesses and entrepreneurs operate within the informal sector and only 34.4% of them owning a bank account to run the business. The result, only 19% of registered trade is transacted digitally. Second, the preference for cash transactions with no receipts as a way of increasing profit margins through tax evasion and competitive edge over formal sector, supported by low detection rates of such violations. Data from KRA also shows that only 4 million Kenyans are registered taxpayers against a working population of 31 million. There is need to lessen the tax burden placed on a small proportion of the population to run this economy for profitability, wealth creation and poverty alleviation.	a) 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. b) Consider limiting cash-based transactions as a means to capture all business activities in the economy. c) KRA to device mechanism 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. d) Since the informal sector is growing at a rapidly faster rate than the formal sector, more research needs to be done to establish feasible data the sector's potential can be harnessed for economic growth. e) There's need to address MSMEs(firms) liquidity pressures by continued efforts to accelerate VAT refunds f) Ensure prompt payment of pending bills by Ministries, Departments, Agencies and County Governments to MSMEs to boost growth.
Para 41-43 Revenue Performance	According to the BPS 2021, revenue collection to December 2020 declined by 12.9 percent compared to a growth of 17.1 percent in December 2019. This decline is attributed to the difficult operating environment due to the Covid-19 pandemic which has adversely affected revenue performance from March 2020. As at end December 2020, the cumulative total revenue - inclusive of Ministerial Appropriation in Aid (AiA) amounted to Ksh 810.6 billion against a target of Ksh 907.7 billion, with shortfalls recorded in both ordinary	The Institute recommends the following: a) **Predictable Tax Regime through an overarching tax policy:** for sustained revenue collection b) **Revenue collection:** there is need for stronger strategies to enhance revenue collection such as sealing existing tax loss loopholes and widening the

revenues (Ksh 75.8 billion) and Ministerial A-I-A (Ksh 21.3 billion).

Further analysis of performance per tax head, indicated a drop in corporate tax confirming sluggish economic growth. Over the years, contribution of corporation tax to total tax revenue has been on a decline as highlighted below:

Contribution to total tax revenue

FY	Estimated Ordinary Revenue (in KES billion)	Actual Ordinary Revenue (in KES billion)	Deviation (in KES billion)	% Deviation of actual ordinary revenue from original estimates
2015/16	1,184.37	1,152.54	31.83	2.7%
2016/17	1,311.32	1,306.57	4.75	0.4%
2017/18	1,489.63	1,365.06	124.57	8.4%
2018/19	1,588.13	1,499.76	88.37	5.6%
2019/20	1,615.38	1,573.42	41.96	2.6%
2020/21	1,523.50	NA	NA	NA
Average				3.9%

Source: Quarterly Economic and Budget Review 4th quarter 2020 and BROP 2020

Lower corporate profits, declining consumption & increases in unemployment will cause declines in revenue from corporate income taxes, goods and services taxes and personal income taxes

The measures taken in response to the Covid-19 pandemic are expected to contribute further to a decline in taxes on income, profits and capital gains (income tax).

tax base. This may ensure that the country can comfortably be able to service its public debt as well as meet the revenue targets.

c) **Green" the Tax System:** Use the tax system to promote sustainable & equitable growth esp.in the context of the COVID-19 crisis & increased impact of global warming and climate change

Para 47-55: Fiscal Policy	The reduction in the fiscal deficit will reduce the pace of growth of the public debt. In FY 2020/21, The BPS 2021 projects fiscal deficit to decline from 7.8 percent of GDP in FY 2019/20 to around 3.6 percent of GDP by FY 2024/25. It is worth noting that the Draft BPS 2021 projects expenditures as a share of GDP to decline from 25.2 percent in the FY 2019/20 to 25.9 percent in the FY 2020/21 and further to 21.6 percent in the FY 2024/25. On the other hand, revenues as a share of GDP are projected at 17.0 percent in FY 2019/20, 16.4 percent in FY 2020/21 and 17.7 percent in FY 2024/25.	The Institute supports the proposals contained in the World Bank's Economic Update: a) There is need to re-ignite private sector led growth and ensure that fiscal consolidation is growth friendly b) 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) c) There is need for Parliament to assess the uptake and impact of already established austerity measures by the National Treasury in 2019
Modernized Income Tax Bill	This matter was captured in the previous Budget Policy Statements for FY 2019/20 and FY 2020/21. However, it has been omitted in the current Budget Policy Statement The Institute is concerned with the delay in the enactment of the Income Tax legislation. This has been pending for the last three years. 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 an overarching Tax policy as a precursor to the review of the law. The Institute is of the opinion that enactment of a modernized Income Tax Legislation is critical due to the following: a) The Kenyan Economy has diversified and grown since 1975	The Institute proposes the following: a) The Bill was at an advanced staged and therefore efforts should be made to expedite tabling of the Income Tax Bill to Parliament. b) Commence initiatives to finalize an overarching tax policy for Kenya.

<table>
<tr><td></td><td>when the current Act was enacted
b) Emergence of digital economy and its implication to tax revenue
c) International taxation issues -such BEPS and transfer pricing
Kenya has a new Constitution and attendant laws that require modernization of income tax</td><td></td></tr>
<tr><td>Para 103: Food and Nutrition Security

The Government will continue to implement measures in the agricultural sector in order to ensure food and nutrition security.</td><td>According to Global Hunger Index (GHI) 2020, Kenya is classified as a food deficit country. The report ranks Kenya at number 84 out of 107 countries with a score of 23.7. This means that Kenya has a level oof hunger which is serious (Alarming 35.0–49.9, Serious 20.0–34.9, Moderate 10.0–19.9, Low ≤ 9.9)

Currently, close to 1 in every 3 Kenyans (14.5 million) suffer from chronic food insecurity and poor nutrition annually. In addition, about 30% of the children countrywide 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.

The Government has been implementing various measures such as the Agricultural Sector Transformation and Growth Strategy, the successful reforming of the Agricultural Inputs Subsidy Programme, expansion of irrigation schemes, supporting large-scale production of staples, implementing programmes to support smallholder farmers and promoting the use of appropriate farming techniques.

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</td><td>The Institute recommends the following:

a) The sector legal, policy and institutional capacity should be strengthened in realization of core mandates.

b) Access to agricultural financing and affordable credit- Lack of finance for agriculture compromises increasing production and investment in value addition activities in agriculture..

c) Continuous training and research in the field of agriculture- Facilitate Refresher training for extension officers/ CPD programmes for staff and farmers supervised by departments of agriculture and cooperatives.

d) Diversification of Agricultural Production: Narrow base of agricultural products, especially exports lead to high vulnerability of incomes to the international market trends. Farmers should be educated on urban farming and support services for agricultural exports.

e) Specialization in areas of comparative and competitive advantage: County specialization in areas of comparative advantage for example Narok specializes on wheat production while Trans-Nzoia on maize farming.</td></tr>
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	of diversified agricultural activities.	f) ***Improving rural infrastructure***: Performance of the sector is affected right from production to marketing domestically and internationally. Rural roads, markets and transport systems that result in high transaction costs for farmers and inaccessibility to input and output markets should be fixed for food security. g) 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
Para 115: Universal Health Coverage	The government has made plausible steps in Universal healthcare. It has rolled out the UHC insurance scheme which will consolidate all the state sponsored schemes into UHC scheme (HISP OVC, Elderly, PWD, Linda Mama, Edu-Afya). As part of the International Health Regulations to contain COVID-19 pandemic, the health sector increased diagnostic capacity for COVID-19Pandemic in twelve counties. At the same time 24,282 complete Personal Protective Equipment (PPEs) were distributed, 7,411 Isolation beds and 319 ICU beds were setup across 47 counties to contribute towards achievement of UHC and medical tourism beyond the COVID-19 pandemic. For the FY 2020/21, the prioritized programs and projects aim at achieving improved accessibility, affordability of health services, and reduction of health inequalities and optimal utilization of health services across the sector. During the MTEF period FY 2021/22-2023/24, the sector has been allocated Ksh 119.9 billion, Kshs.110.3billion and Kshs.121.1billion in the FY 2021/22, 2022/23 and 2023/24 respectively. The recurrent	a) The government needs to supplement the treatment of COVID-19 for all patients. Such a measure will ensure that some of the most vulnerable members of societies such as slum dwellers and low-income earners are guaranteed treatment. The cost of treating COVID-19 is extremely expensive, furthermore, the economic disruption due to the lockdown measures has interfered with the incomes of many people. b) Ensuring that at least 70% of NHIF disbursements go to public health institutions and service providers; with 30% going to the private sector. This will help build capacity of public health institutions as opposed to utilizing public funds to support private entities. According to the Health Financing Reforms Expert Panel (HEFREP) Report, private hospitals received KES 22 billion from NHIF while government and mission hospitals received KES 7 Billion and KES 8 Billion respectively out of the KES 37.7 billion expenditure in FY 2018/19. This implies that government health facilities received only 18.6% allocation of NHIF disbursement in that year.

	expenditure allocation for the same period is Kshs. 70.7 billion, Kshs. 72.6 billion and Kshs. 75.1 billion for recurrent expenditure for financial years 2021/22, 2022/23 and 2023/24 respectively. The development expenditure allocation for the same period is Kshs 49.2 billion, Kshs. 37.6 billion and Kshs 46.0 billion respectively. ***Key concerns*** ▪ According to the Ministry of Health (MoH Kenya) (2019), only 11% of Kenyans are covered by the NHIF insurance program leaving most of the population (89%) without the government-subsidized health plan. With over 70% of the Kenyan workforce working in the informal sector, most of them are either not eligible or cannot be able to afford the premiums set by the government to maintain health insurance provision. ▪ Financing management of communicable and non-communicable diseases such as Malaria, TB, and HIV/AIDS in Kenya is largely dependent on donor funds from international organizations, non-governmental entities, and contributions from other countries. This has led to under-investment of the health sector, weakening health systems and structures, and raising concern as to whether the public health infrastructure can withstand a potential overburden in the wake of the COVID-19 pandemic with the majority of Kenyans facing uncertainty due to lack of health coverage. ▪ The cost of COVID-19 testing in Kenya has not yet been included in the NHIF with only a few people living in hotspots areas receiving free COVID-19 testing with the rest having to pay an estimated cost of US$100 (Ksh 10 825.00) ▪ Kenya's budgetary allocation to health has averagely stood at 9% despite signing the Abuja declaration, which requires signatories to allocate 15% budgetary allocation for health. Most of this is	c) 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. This will go a long way in increasing recruitment and welfare of health personnel to enable efficiency in the health sector. It will also solve the problem of periodic strikes and brain drain that has become a new normal in the health sector by ensuring health workers are well paid, offered proper protective gear that they need to work in a safe environment d) Strengthen accountability in the utilization of funds and resources that are allocated in the health sector. The perpetrators of mismanagement of healthcare provision funds should be brought to book and such funds recovered. e) Invest in Medical Research: Counties should support medical research such as Cancer research and studies on NCDs.

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<td>absorbed as recurrent expenditure leaving little room for the development of health facilities and the acquisition of medicine and equipment.

The greatest challenge is corruption. The most recent case is the mismanagement of Covid-19 funds that produced Covid billionaires including the disappearance of donation from the Chinese Philanthropist, Jack Ma.</td>
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<td>Para 208: Realism of revenue forecast --- it is ambitious and leads to budget deficit</td>
<td>In the FY 2021/22 revenue collection including Appropriation-in-Aid (A.i.A) is projected to increase to Ksh 2,033.9 billion (16.4 percent of GDP) up from the estimated Ksh 1,849.2 billion (16.6 percent of GDP) in the FY 2020/21.

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.

TABLE 1: Comparison In Budgeted And Actual National Government Revenue Between FY 2015/16 AND FY2020/21

<table>
<tr><th>FY</th><th>Estimated Ordinary Revenue (in KES billion)</th><th>Actual Ordinary Revenue (in KES billion)</th><th>Deviation (in KES billion)</th><th>% Deviation of actual ordinary revenue from original estimates</th></tr>
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<tr><td>2019/20</td><td>1,615.38</td><td>1,573.42</td><td>41.96</td><td>2.6%</td></tr>
<tr><td>2020/21</td><td>1,523.50</td><td>NA</td><td>NA</td><td>NA</td></tr>
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<td>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 which the Committee thought of as ambitious and not backed by economic fundamentals.

This calls for a holistic approach and a review of economic data and macroeconomic trends when setting revenue targets.

ICPAK proposes that a clear, consistent and standard forecasting model should be adopted by the country as a basis for determining revenue projections based on either inflationary adjustments or the average revenue performance over the years.

In order to enhance tax administration and seal leakages, the Institute proposes the following:
a) proper controls and monitoring of taxpayer activities through a single identifier will lead to enhanced efficiency in tax administration.
b) Review the penalty system on tax evasion
c) Develop a change management strategy to address</td>
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<table><tr><td>Average</td><td></td><td></td><td></td><td>3.9%</td></tr></table>
Source: Quarterly Economic and Budget Review 4th quarter 2020 and BROP 2020

The table above indicates that the Kenya Revenue Authority has persistently failed to meet its revenue targets, with an average deviation of 3.9%. The highest deviation was experienced in the FY 2017/18 at (8.4%) with the least deviation growth of 0.4% being registered in 2016/17.

The implication of the failure to meet revenue targets is that the national government would either forego offering the services equal to the deviation or incur an unplanned public borrowing hence altering the original plans contained in the annual budgets.
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income tax matters
d) Leverage on simplified technological solutions to enhance integration of taxpayer information systems.
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<td>Expenditure projections: Para 209</td>
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While the Government expenditure as a share of GDP for FY 2021/22 is projected to decline to 24.3 percent, the overall nominal expenditure and net lending is projected at Ksh 3,010.0 billion from an estimated Ksh 2,864.5 billion (25.6 percent of GDP) in the FY 2020/21 budget. The expenditures comprise of recurrent of Ksh 1,986.0 billion (16.0

Key issues of concern

The pandemic has led to a significant fiscal financing gap as revenue collections drops and expenditure pressures increase.

The government has stepped up spending to strengthen the capacity of its healthcare system to cope with COVID-19 infections and to contain the spread of the epidemic. Overall, this has resulted in a large financing gap, estimated at about 1.5 percent of GDP in FY2019/20, and public debt has increased to about 63.2 percent of GDP (from about 62.1 percent of GDP in FY2018/19)

There is need to support these efforts by further expenditure
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The Institute recommends the following:

a) While the COVID-19 crisis persists, the Government of Kenya (GoK) should continue to provide an adequate but temporary expenditure surge to the health sector to meet increased demand for health services and to contain the spread of COVID-19
b) Wage Bill Management; Improved wage bill management and allowances could yield 0.2 percent of GDP in expenditure savings. This includes regular cleaning of the payroll-to eliminate ghost workers, a review and rationalization of the number of allowances, and improved functionality of government payroll management systems could make a significant contribution to reducing expenditure in this area.
c) A review of numerous personal allowances, preventing over-use of travel related allowances, as well as discontinuation of unnecessary allowances forms the bulk of these savings.
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<td>efficiency measures, complemented by additional revenue mobilization and strengthened debt management.</td>
<td>d) Framework agreements and centralized/consolidated procurement for homogeneous goods and services in government procurement could also deliver approximately 0.9 percent of GDP in fiscal savings. This strategy optimizes government's purchasing power and could deliver massive expenditure savings</td>
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<td>Para 210 and 211

Deficit financing</td>
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The fiscal deficit (including grants), is projected at Ksh 930.0 billion (7.5% of GDP) in FY 2021/22 against the estimated overall fiscal balance of Ksh 966.6 billion (8.7%t of GDP) in FY 2020/21.
The fiscal deficit in FY 2021/22, will be financed by net external financing of Ksh 267.2 billion (2.2% of GDP), and net domestic borrowing of Ksh 662.8 billion (5.3% of GDP).
The Institute is concerned that the debt portfolio continues to balloon and the current borrowing strategy, as indicated under the approved Medium Term Debt Management Strategy 2021, is pegged on the assumption that fiscal consolidation will reduce the overall cost of debt and safeguard debt sustainability.
However, given the impact of Covid-19 pandemic on revenue mobilization, exports, production and other contingent liabilities vis-à-vis increasing expenditure demands, there is a high likelihood that fiscal consolidation measures will be hard to adhere to. Thus the country's debt distress levels could move from moderate to high.
Kenya's net external and domestic borrowing
<table>
<tr><th>Fiscal Year</th><th>FY 2018/2019</th><th>FY 2019/2020</th><th>FY 2020/2021</th><th>FY 2021/2022</th></tr>
<tr><td>Net External financing</td><td>214.7 billion</td><td>306.5billion</td><td>247.3 billion</td><td>Ksh 345.5 billion (2.8 percent of GDP)</td></tr>
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The Institute proposes the following measures;
a) Implementing the budget taking into consideration financial and information requirements required for a successful medium-term fiscal policy implementation,
b) Enhance accountability in public and private sectors to free more resources to development. The government must decisively deal with wastages in utilization of public resources. We must also reign in on corruption that threaten service delivery and could derail realization of the Big Four Agenda.
c) Kenya should diversify its exports and the market for the same to increase its foreign exchange reserves and hence minimize on the exchange rate risk.
d) Rely more on concessional loans and grants rather than on expensive bilateral loans that are non-concessional, thus reduce high interest rates payments, averting possibility of debt overhang.
e) Implement government-to-government partnerships and other Public Private Partnerships (PPP) models based on independent cost-benefit, Cost-Effectiveness and value-for-money studies, to prevent expensive low priority bilateral, donor-led investments funded by debt.
f) Diversifying the currency mix in which debt is denominated to reduce exposure to foreign exchange risks.
g) Enhance debt transparency and accountability in order to enhance management of public debt in Kenya.
h) An audit of current projects is critical to wipe out white
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Net Domestic Borrowing	368.8 billion	277.5 billion	318.9 billion	592.2 billion (4.7 percent of GDP).

BPS 2018/2019/2020/21

Kenya's public and publicly guarantee debt stock is projected to increase over the medium term owing to the impact of low generation of domestic revenue and pressure from expenditure on ongoing programs

Data from the Public Debt Office and the National Treasury indicates that As at June 2020, the national debt stock had reached Kshs. 6.6 trillion (Kshs. 873 billion or 15% increase) and is projected to reach Kshs. 7.5 trillion by June 2021.

Debt servicing expenditures are estimated to utilize up to 49% of ordinary revenues in FY 2020/21. This implies that at best, only approximately 51% of nationally raised revenues will be available for FY 2020/2021 budget implementation.

The Institute is concerned that the current public finance management framework has capped the national debt stock at Kshs. 9 trillion. This means that with the current borrowing rate, it is anticipated that there will be little borrowing space beyond three years.

Public Debt Servicing as a Percentage of Ordinary Revenue For The Period Between *FY 2015/ & FY 2020/21*

FY	Total Public Debt Service (in KES	Ordinary Revenue (in KES billion)	(Public debt service/ordinary revenue) in %

elephant projects. A clear framework for tracing and auditing debt financed projects is needed for equity.

i) **The government should also consider the following measures to enhance public financial management.**

(i) ***Expenditure Vs Revenue:*** In the past few years, public expenditure has been growing at a faster pace than revenue. The major outcome has been huge budget deficits. We should cut wasteful expenditure, increase the efficiency of spending, and free up resources that can be redirected to where they are most needed to combat the crisis and protect livelihoods

(ii) ***Implementation of budget monitoring reports:*** Act on Auditor General and Controller of Budget recommendations in respect to public debt

(iii) ***Audit of the Public Debt Register:*** Establishing the authenticity of the public debt register including the true debt sustainability position is critical. Government sources and the world bank continue to give conflicting statistics of Kenya's debt situation.

(iv) ***Accounting for debt:*** The public is not sure on the accuracy and completeness of the debt register. National Treasury and Central Bank of Kenya have conflicting statistics on national public debt. The Auditor General in its Report for the Financial Year 2017/18 pointed out

	billion)		
2015/16	397.03	1,184.37	33.5%
2016/17	466.51	1,311.32	35.6%
2017/18	621.76	1,489.63	41.7%
2018/19	870.62	1,588.13	54.8%
2019/20	696.55	1,615.38	43.1%
2020/21	904.70	1,523.50	59.4%

Source: Programme Based Budgets 2015/16 -2020/21 and Quarterly Economic and Budget Review 4th quarter 2020

The table above indicates a growing rate of public debt servicing as a percentage of ordinary revenue. It is expected that in the current FY 2020/21, for every KES 100 collected as tax, KES 59 will be used to repay public debt leaving only KES 41 for other national government functions. This indicates that the country is in a vulnerable position due to the high debt repayment.

misstatements and differences between the financial statements and the confirmed balances. Further, Further, a comparison of the statement of receipts and payments and the ledger for the period under review reflected different account balances as indicated below:

Item Description	Financial Statement Balance KSh.	Ledger Balance KSh.	Variance KSh.
Interest Payments on Foreign Borrowings	84,357,487,111	84,725,600,971	368,113,860
Principal Repayment on Domestic Loans	111,700,845,296	294,836,376,343	183,135,531,047
CBK -Pre-1997 Loans	1,110,000,000	2,220,000,000	1,110,000,000
Repayment of Principal from Foreign Lending and On-Lending	141,532,524,729	141,360,882,966	171,641,763
Exchequer Releases	517,161,876,534	-	517,161,876,534

Source: Auditor General Report for National Government-FY 2017-2018

Paragraph 249. Education sector	The Sector has been allocated Ksh 487.7 billion, Ksh 503.9 billion and Ksh 517.4 billion for recurrent expenditure for financial years 2021/22, 2022/23 and 2023/24 respectively. The development expenditure allocation for the same period is Ksh 20.9 billion, Ksh 17.8 billion and Ksh 19.8 billion, respectively. ▪ In a Devolution Survey 2020 conducted by the Institute, several challenges were documented that are impeding the successful delivery of educational services, especially at the county level: ▪ high turnover rates for Early Child Development Education (ECDE) teachers ▪ low funding for ECDE, inadequate investment in succession planning within departments, low and unclear scheme of service for ECDE teachers, ▪ Inadequate infrastructure to support the learning of children living with disability ▪ inadequate number of trained instructors in most polytechnics.	The Institute recommends the following: a) increasing capitation for ECDE teachers b) Employment of skilled and qualified instructors in polytechnics; c) putting in place monitoring and assessment of performance (quality assurance) to ensure there is no laxity on the part of those employed to offer services to the learners
Para 275: County Government's Own Source Revenue	According to the BPS 2021, the County Governments' actual Own Source Revenue (OSR) collection for FY 2019/20 was Ksh. 35.8 billion against a target of Ksh. 54.9 billion representing 65.2 percent of the annual target. This was a drop in absolute terms from Ksh. 40.3 billion collected in FY 2018/19 that was 74.8 percent of the annual OSR target by the Counties. The County Governments Budget Implementation Review Report for FY 2019/20 by the Controller of Budget indicates that only five Counties surpassed their revenue targets in the FY 2019/20. (Homa	The Institute recommends the following to support Own Source Revenue: a) **Revenue forecasting and mapping**: a clear, consistent and standard forecasting model needs to be adopted by the country as a basis for determining revenue projections. There is further need for a comprehensive analysis and mapping of counties' revenue potential. b) **Revenue collection systems**: There is need to standardize revenue collection management systems

Bay, Taita Taveta, Lamu, Machakos and Bomet)

Key Concerns

- Counties collect much less revenue than the estimated revenue base giving them less resources to deliver on required services.
- The shortfall in equitable resources from the National Government and low collection of own source revenue is a major constraint to delivery of services at the county level.
- Devolution has not yet translated to the envisioned equitable overall development in the country and this is partly due to the wastage brought about by inadequate accountability and lack of transparency in the management of resources.
- Over the years, counties have not been meeting their targets in terms of revenue collection. A study by World Bank demonstrates that counties have been collecting way below their potential. There is need to optimize on OSR potential to avoid overreliance on the National Government equitable share allocation.

Counties revenue targets, actual and potential from 2013/14- 2019/20

	Revenue		Potential	
FY	Revenue targets	Actual revenue collection	At 35%	At 94%
2013/14	54,207,798,427	26,296,089,510	35,499,720,838.50	51,014,413,649.4
2014/15	50,376,859,951	34,468,720,354	46,532,772,477.90	66,869,317,486.7
2015/16	50,539,746,840	36,905,771,161	49,822,791,067.35	71,597,196,052.3
2016/17	57,664,858,199	32,522,875,093	43,905,881,375.55	63,094,377,680.4

across counties for uniformity and easy reporting. In addition, counties should strive to automate revenue collection systems to seal loopholes and leakages. This 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 Controller of Budget, the CRA and the Office of the Auditor General, and also easily accessible by the general

c) **Collaboration with KRA**: To enhance efficiency and effectiveness in revenue collection and administration, county units should consider engaging KRA for technical support.

d) **Public Participation in Revenue collection:** Counties should empower citizens with revenue information through revenue clinics- for citizens to understand the importance of taxes and charges to county service delivery.

e) County Treasuries should continuously review the performance of revenue collection vis-à vis targets and shall include a status report in the Quarterly and Annual reports which shall be published in various media.

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<tr><td>2017/18</td><td>49,219,014,037</td><td>32,491,694,261</td><td>43,863,787,252.35</td><td>63,033,886,866.34</td></tr>
<tr><td>2018/19</td><td>53,863,582,921</td><td>40,304,833,142</td><td>54,411,524,741.70</td><td>78,191,376,295.48</td></tr>
<tr><td>2019/20</td><td>57,824,660,000</td><td>37,380,440,000</td><td>50,463,594,000.00</td><td>72,518,053,600.00</td></tr>
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Source: COB various issues and estimate for 2019/20, World Bank Study
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<td>Para 278: Pending Bills</td>
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A special audit by Office of the Auditor General (OAG) verified eligible pending bills by County Governments amounting to Ksh. 51.2 billion as at 30th June 2018. Another Ksh. 37.7 billion worth of pending bills was found to be ineligible for payment due to lack of documentation to support services rendered or work done.
A report by the Controller of Budget (CoB) indicates that by 10th November 2020, the Counties had settled Ksh. 39.07 billion (76.2% of the eligible pending bills) leaving an outstanding balance of Kshs. 12.22 billion.
According to the Kenya Enterprise Survey 2018, approximately 12 percent of the 1,001 firms surveyed have had a contract with government that was in arrears. Pending bills if allowed to persist, could reduce firm liquidity and cause postponement of new investments. It could also increase firms' default rate (in business to business transactions), which can be associated with a rise in non-performing loans for the banking sector.
As at 24th November 2020, the National Treasury had cumulatively released to County Governments Ksh 71.85 billion as their equitable share of revenue raised nationally and Ksh 5.55 billion as conditional grants for FY 2020/21.
The issue of pending bills is a significant bottleneck facing various sectors of the economy. There is need for the government to continue with the efforts of clearing the legitimate pending bills that were
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The Institute recommends the following:
a) The National Treasury should consider accrual accounting as opposed to cash accounting which presents challenges in terms of monthly and annual financial reporting on pending bills and other liabilities.
b) There is need to develop a database of all owed dues to counties and MDAs, and assess the multiplier effect/impact to the economy
c) The Institute supports recent efforts by the National Assembly to amend the Public Procurement and Assets Disposal Act 2015, compelling the National and County Governments to pay suppliers and contractors within 30 days.
d) Legislative Proposals
The Institute proposes Amendment to 17 of Public Finance Management Act 2012.
Amend 8(b) to read "by inserting the following new subsection immediately after subsection (7)—
"(8) (a) six months prior to a general election, no procurement shall be carried out by the national and county governments, or their respective entities, in respect of their
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	accrued.	*respective development votes unless with the approval of the National Treasury".* *(8) (b) All pending bills incurred by the national and county governments, or their respective entities, in respect of their respective development votes, shall be cleared not later six months prior to a general election* This amendment will help curb pilferage of public resources during an election year and increase of pending bills during the same period.
Para 285: County governments Equitable Share	The Third Basis for the allocation of the National Revenue to the County Government was approved by Parliament in September 2020 on condition that its implementation would be preceded by 53.5 billion increase in counties' equitable revenue share. The National Treasury however proposes moderate adjustment of 10 billion to yield a new baseline allocation of Ksh 326.5 billion. Sustained underperformance in ordinary revenue and economic and fiscal repercussions of the Covid-19 pandemic have been cited for this proposal. In addition, four conditional grants have been converted to unconditional allocations to be disbursed to the counties as part of their equitable share. The Commission on Revenue Allocation recommends that for the financial year 2021/22, out of a projected shareable revenue of Kshs. 1,813.7 billion, and the Road Maintenance Levy Fund revenue projection of Kshs. 65.13 billion, national government be allocated Kshs. 1,443.7 billion and County governments Kshs.370 billion. The Institute commends National Treasury, Commission on Revenue Allocation and Council of Governors for unanimously agreeing on equitable share of Ksh. 370Billion FY2021/222 at the 14th Intergovernmental Budget and Economic Council (IBEC) meeting.	Parliament should consider the following: a) Consider amending Section 37 (9) of the PFM Act 2012 to enable prior enactment of DORA before Appropriations Bill. b) 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. c) The Institute recommends further amendment to Section 191 of the Public Finance Management Act **The National Assembly shall within three months after receiving an audit report adopt and approve the report;** **In the event that the audit report is not adopted and approved by the National Assembly within three months, it shall be deemed as the most recent audited accounts for purposes of determining**

	This will be the first time in many years where we'll not have a contested division of revenue process	**sharable revenue.** Therefore, the National Assembly must expedite its process of considering the audited financial statements as submitted by the Auditor General