

Public Finance under Kenya's new Constitution



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Njeru Kirira



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Constitution Working Paper No. 5

Published by:

Society for International Development (SID)
Regional Office for East & Southern Africa
Britak Centre, First Floor
Ragati/Mara Road
P.O. Box 2404-00100
Nairobi, Kenya
Tel. +254 20 273 7991
Fax + 254 20 273 7992
www.sidint.net

© Society for International Development (SID)

ISBN No: 978-9966-029-04-1

Printed by:

The Regal Press Kenya Ltd.
P.O. Box 46166
Nairobi, Kenya

Design & Layout:

Sunburst Communications Ltd.
P.O. Box 43193-00100
Nairobi, Kenya
Email: info@sun.co.ke

Abstract

Kenya's new Constitution has introduced fundamental changes in the management of public finance, changes that unfortunately received little attention prior to the referendum and the subsequent promulgation of the Constitution. Kenyans need to appreciate that public finance affects how power and influence are shared among key players and affects their daily lives. Indeed, Kenyans need to appreciate that in public finance nothing is free. Every benefit must be paid for by somebody, either in the form of taxes or debts.

This paper examines the new Constitution and its implications for public finance, particularly the nature of Kenya's public finance and administration system, the short-comings of the new legal framework and its likely impact in the new Constitutional order. It takes a historical and comparative approach.

The paper, through an examination of the experiences of other developing states, makes policy and legislative suggestions on how to remedy the short-comings of the new system of public finance. The paper argues that all current public finance laws and regulations need to be overhauled, but this should be preceded by legislation on the role of the Treasury and the Parliament. Moreover, Kenya needs to build new institutional and administrative structures to manage public finance, and the new Constitution presents this opportunity. However, this is not the time to experiment. Kenya does not need reinvent the wheel. Kenya can learn from the experiences of some developing countries, without carbon-copying their systems.

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The SID Constitution Working Paper Series

In 2010, on the cusp of Kenya's new constitutional dispensation, the Society for International Development (SID) embarked on a project called '*Thinking, Talking and Informing Kenya's Democratic Change Framework*'. Broadly stated, the objective of the project was both historical and contemporary: that is, to reflect on Kenyans struggles for a democratic order through a book project, and to examine the significance of a new constitutional order and its legal and policy imperatives, through a Working Paper Series.

Consequently, SID commissioned research on some of the chapters or aspects of the new constitution that require further policy and legislative intervention, culminating in ten Working Papers. These papers, mostly by Kenyan academics, are intended to help shape public discussions on the constitution and to build a stock of scholarly work on this subject.

These papers seek to contextualize some of the key changes brought about by the new constitutional order, if only to underscore the significance of the promulgation of the new constitution on August 27, 2010. The papers also seek to explore some policy, legislative and institutional reforms that may be necessary for Kenya's transition to a democratic order.

The Working Papers explore the extent to which the new constitution deconstructs the Kenyan post-colonial state: how it re-calibrates the balance of power amongst branches of government and reforms government's bureaucracy; redraws the nature of state-individual relations, state-economy relations, and state-society relations; and deconstructs the use of coercive arms of the government. Lastly, the papers examine some of the limitations of the new constitution and the challenges of constitutionalism.

In the first set of papers, **Dr Joshua Kivuva**, **Prof. Ben Sihanya** and **Dr. Obuya Bagaka**, separately examines how the new constitution has re-ordered nature of Kenya's post-colonial state, especially how it has deconstructed the logic of state power and rule, deconstructed the 'Imperial Presidency', and how it may re-constitute the notorious arm of post-independent Kenya's authoritarian rule: the provincial administration.

The next set of papers in this series, by **Dr. Othieno Nyanjom** and **Mr. Njeru Kirira**, separately looks at the administrative and fiscal consequences of Kenya's shift from a unitary-state to a quasi-federal state system. Whereas Dr. Nyanjom examines the anticipated administrative and development planning imperatives of devolving power; Mr. Kirira examines the anticipated revenue and expenditure concerns, which may arise in a state with two-tier levels of government. Both discussions take place within the context of a presidential system of government that the new constitution embraces.

The paper by **Dr. Musambayi Katumanga** examines the logic of security service provision in post-colonial Kenya. Dr. Katumanga argues that Kenya needs to shift the logic of security from regime-centred to citizen-centred security service provision. However, despite several attempts in the recent past, there are still several challenges and limitations which Kenya must redress. The new constitution offers some room for instituting a citizen-centric security reforms.

The paper by **Prof. Paul Syagga** examines the vexed question of public land and historical land injustices. It explores what public land is, its significance and how to redress the contention around its ownership or use. Similarly, the paper examines what constitutes historical land injustices and how to redress these injustices, drawing lessons from the experiences of

other states in Africa that have attempted to redress similar historical land and justice questions.

The papers by **Dr. Adams Oloo**, **Mr. Kipkemai arap Kirui** and **Mr. Kipchumba Murkomen**, separately examines how the new constitution has reconfigured representation and legislative processes. Whereas Dr. Oloo examines the nature of the Kenya's electoral systems, new provisions on representations and its limitations; arap Kirui and Murkomen look at the re-emergence of a bicameral house system and the challenges of legislation and superintending the executive.

If the other nine papers examine the structural changes wrought by the new constitution; the tenth paper, by **Mr. Steve Ouma**, examines the challenges and limitations of liberal constitutional order, especially the tensions between civic citizenship and cultural citizenship from an individual stand point. Perhaps Mr Ouma's paper underscores the possibility of a self-defined identity, the dangers of re-creating ethno-political identities based on old colonial border of the Native Reserves - the current 47 counties and the challenges of redressing social exclusion and the contemporary legacies of Kenya's ethno-centric politics.

The interpretation of the constitution is contested; so will be its implementation. We hope that this Working Paper Series will illuminate and inform

the public and academic discussions on Kenya's new social contract in a manner that secures the aspiration of the Kenyan people.

SID would like to sincerely thank all those who have made the publication of these papers possible, especially those who participated in the research conceptualization meeting and peer-reviewed the papers such as: **Dr. Godwin Murunga**, **Prof. Korwa Adar**, **Ms. Wanjiru Gikonyo**, **Dr. Joshua Kivuva**, **Dr. Richard Bosire**, **Dr. Tom Odhiambo**, **Ms. Miriam Omolo** and **Dr. Mutuma Ruteere**, for their invaluable input.

Lastly, we would like to acknowledge the invaluable support of the SID staff: Hulda Ouma, Irene Omari, Gladys Kirungi, Jackson Kitololo, Aidan Eyakuze, Edgar Masatu, Stefano Prato, and Arthur Muliwo; as well as Board members Sam Mwale and Rasna Warah. Similarly, we would like to thank the Swedish International Development Cooperation Agency (Sida) for their financial support. Our gratitude also goes to the Swedish Ambassador to Kenya H. E. Ms. Ann Dismorr; and Ms. Annika Jayawardena and Ms. Josephine Mwangi of Sida for supporting this project.

Working Papers Series Coordinators

Jacob Akech
Duncan Okello

Contents

Acronyms	viii
1.0 Introduction	1
2.0 Public Finance in Kenya: How The Past Shaped The Current Constitutional Provisions	1
2.1 The Kenyatta years	1
2.2 The second era: The Moi presidency	2
2.3 The Kibaki administration	4
2.4 Public finance in the new Constitution	4
3.0 Constitutional Changes and the Legal Regime on Public Finance	5
4.0 Implications of some of the key changes	7
4.1 Countering parliamentary licence	7
4.2 Shoring up parliamentary authority	8
5.0 Other Country Experiences	9
5.1 Indonesia	9
5.2 Decentralization in Africa: The case for South Africa and Uganda	10
5.2.1 South Africa	10
5.2.2 Uganda	11
6.0 Revenue Sharing	12
6.1 Commission for Revenue Allocation	14
6.2 Review of allocation criteria for counties	14
6.3 Sharing the revenue base	15
7.0 Collection, Custody and Management of Public Funds	16
7.1 Taxation and tax privileges	16
7.2 Budget process	17
7.3 The role of the Treasury	19
7.4 Transparency and accountability in the new regime	20
7.5 Public debt	20
7.5.1 Dealing with contingent liabilities	20
7.5.2 County borrowing	21
8.0 Other Significant Changes	22
8.1 The Salaries and Remuneration Commission	22
8.2 The Central Bank of Kenya and its functions	23
8.3 Changes to existing laws	23
9.0 Conclusion	23
10.0 References	25
11.0 Annex A Comparison between “Old” and “New” Constitutional Provisions	26
Annex B Phases of Kenya’s Budget Process	35
SID’s Constitution Working Papers Series	37

Acronyms

CAG	Controller and Auditor General
CBK	Central Bank of Kenya
CDF	Constituencies Development Fund
COB	Controller of Budget
COMESA	Common Market for Eastern and Southern Africa
CRA	Commission for Revenue Allocation
EAC	East African Community
ESP	Economic Stimulus Programme
GDP	Gross domestic product
ICT	Information and communication technology
IFMIS	Integrated Financial Management Information System
KANU	Kenya African National Union
KRA	Kenya Revenue Authority
LATF	Local Authorities Transfer Fund
MP	Member of Parliament
MTEF	Medium-term expenditure framework
NARC	National Rainbow Coalition
PBO	Parliamentary Budget Office
PETS	Public Expenditure Tracking Surveys
SRC	Salaries and Remuneration Commission
UK	United Kingdom
USA	United States of America

1.0 Introduction

Public finance is critical to relations between the governed and the governors because without resources, nothing gets done. Finance gives meaning to powers and lies at the heart of the political and institutional structures of every nation. Indeed, taxation and the use of public funds shaped politics and institutional structures of leading democracies, like the United Kingdom (UK) and the United States of America (USA). In the case of the UK, the Magna Carta, signed in 1215, fundamentally influenced the pace and direction of England as a constitutional monarchy when the landed gentry refused to pay taxes on the grounds that they were not represented. Similarly, the American War of Independence (1775–1782) was partly triggered by resentment that originated from taxation without representation. Strong sentiments continue to arise from the imposition of taxes and how the money raised is allocated and used. The choice of taxes to be imposed and who decides how mobilized resources are to be used still play critical roles in 21st century politics and generate debate irrespective of the ideology of the ruling elite.

Kenya's 2010 Constitution has introduced fundamental changes in the management of public finance, changes that unfortunately received little or no attention prior to the referendum and the subsequent promulgation of the Constitution. As implementation starts, issues that were ignored have to be dealt with and solutions found to the problems and challenges that continue to emerge. It is unfortunate that Kenyans do not yet appreciate that a constitution is a vital document – especially on matters of public finance – that affects the way the country is governed, how power and influence are shared among the key players, and the fact that these relations will affect their daily lives. As a living document reflecting the fears and concerns of the past and aspirations for the future, the 2010 Constitution will have significant impacts on relations between the citizens and those given responsibility to govern.

This chapter examines the new Constitution and its implications for public finance, particularly the nature of Kenya's public finance and administration system, the shortcomings of the new legal framework, and the likely implications for the new constitutional order. In so doing, the chapter refers to experiences of other countries, the challenges that some of those countries have faced, and the solutions and options available to Kenya as it implements its new Constitution. As we examine the possible implications, it is necessary to appreciate some of the factors that have informed both the content and the structure of the new Constitution.

2.0 Public Finance in Kenya: How the past shaped the current constitutional provisions

With independence in 1963, Kenya inherited the colonial system of public finance based on command and control structures. The independence Constitution (1963) divided public finance powers among the three branches of the government, but the executive soon moved to accumulate more influence than the other two. To achieve this, that original Constitution was amended over 30 times, in the process reducing the National Assembly to little more than a parliamentary rubber stamp of the executive.

2.1 The Kenyatta years

When Jomo Kenyatta took over the instruments of power from the colonial authorities as the prime minister, the country was centrally governed from Nairobi. The ruling party, Kenya African National Union (KANU), favoured a unitary system with a strong presidency. One of Kenyatta's early actions

was to call for a constitutional amendment abolishing the position of prime minister and creating the position of president, which he then assumed. The executive under a strong presidency led the budget process, with more powers added by Article 48 of the Constitution (1963), which prohibited Parliament from introducing bills related to money or making any amendments to increase taxes or expenditure. It could only amend what was proposed, thus leaving the executive to run the show. Parliament, ostensibly the representatives of the citizenry, had no powers to influence the manner in which resources were mobilized and allocated.

The fiscal structure and institutions of public finance were designed to give the executive and ruling elite maximum control. Sessional Paper No. 1 of 1965, on African Socialism, set out the country's preference for a mixed economy in which the private sector played a critical role in economic development. Nevertheless, the government remained actively involved in economic activities. This strategy was at variance with those of the other two partner states of the East African Community (EAC), Tanzania and Uganda, which chose more socialist-oriented development approaches with the public sector being the lead player. The tax system imposed by the colonial government was retained in Kenya with minor changes introduced to remove overtly racial connotations and the privileges conferred on the white settler community. The changes allowed very little room for the citizens to influence decisions on how resources were mobilized, allocated and used. However, these changes sowed the seeds of discontent that have characterized post-independence Kenya.

The introduction of a de facto one party political system in 1969 strengthened the executive's hand. The Treasury, under the guidance of the presidency, became the lead financial agency as Parliament's role was further reduced to one of ritual approval. In essence, Parliament had lost its oversight function, a situation that undermined governance structures and opened public resources and offices to abuse.

Within the first decade the Constitution (1963) was amended to make provisions for the President to appoint and dismiss senior civil servants without reference to the Public Service Commission (PSC). This led to a situation in which senior civil servants understood that they served at the pleasure of the President (Nyong'o, 2004). Despite this fact, those in the civil service enjoyed significant powers on technical and policy issues – especially the Treasury, which became all-powerful, assuming control over all public resources.

2.2 The second era: The Moi presidency

- What taxes to impose, and the structure and composition of public debt;
- Allocation of public funds, which was often politically manipulated;
- Execution of public programmes and projects; and
- When to prepare and table annual audit reports before Parliament.

Although Parliament approved taxes, rates and expenditure proposals, this was only a formality. Any Member of Parliament (MP) who dared question the government was immediately reprimanded or detained. The executive made all the decisions, including when to report and how much information was to be availed to both Parliament and the public. Members of the legislature could engage in active opposition to government only at their own risk. Whenever they did, they were prone to arrest and, before the re-introduction of multiparty politics in 1992, detention – even if such opposition was expressed within the precincts of Parliament. Consistent with the prevailing socio-political situation, in 1997, for instance, the Parliamentary Estimates Committee, which was responsible for reviewing budgetary allocations proposed by the Finance Minister, was expunged from the Standing Orders for questioning funds allocated to State House. Similarly, although Parliament approved the maximum amount of money government could borrow from both

domestic and external sources, it was provided with limited information on when or how the debt was contracted, the amount borrowed, and what the funds were used for.

Thus, despite the initial constitutional authority granted to Parliament to scrutinize and approve the national budget, the legislature was effectively elbowed aside by the executive, and the Treasury took the lead role. Parliament became little more than a spectator. Add to this the systematic erosion of the Office of the Controller and Auditor General arising from transfers of key officers, a situation that undermined its capacity to perform essential functions and led to accumulated audit arrears. The situation deteriorated so much that by the beginning of 2003, when a new government took over, Parliament was more than five years behind in examination of annual public accounts. This meant that by the time the audits were discussed in Parliament, many of the key witnesses were not available for questioning to validate information necessary for decision making.

One result was gross abuse of public office and mismanagement of finances that culminated in mega scandals. Well-documented incidents of abuse indicate that the government lost billions of shillings to corruption and wastage arising from fiscal indiscipline such as the Goldenberg scandal, along with well-known cases of abuse of public procurement procedures such as the construction of the controversial Eldoret International Airport and the purchase of the presidential jet. At the height of his power, and to ensure full control of both the sole party, KANU, and Parliament, Moi instigated queue-voting to replace the secret ballot, the former being much easier to manipulate and ensure the president's preferred candidates sailed through at the polls. With a weak Parliament and vulnerable legislators, legislative oversight all but disappeared, opening another doorway for abuse of public funds – bogus projects.

Significantly, this involved the accumulation of pending bills. While many of these bills later proved to be forgeries, they were paid, mainly through securitization, a cloak that ensured virtually no Parliamentary scrutiny. The problem with pending bills partly originated from roadside political declarations and directives that allowed the pursuit of projects without regard to public finance laws and procedures. Besides being a conduit for incurring irregular public debt, pending bills or payment arrears were used to siphon public resources into private hands, which added to the clamour for a change of government in 2002. The situation also prompted the legislature to engage in spirited efforts to reclaim its place as the supreme authority in matters of public finance.

By the end of 2002, the country was dotted with a large number of stalled public projects, many of which were started without going through normal procurement procedures. Some of the projects were formalized and approval sought from Parliament through Supplementary Estimates long after implementation had commenced. There were also many nonexistent projects for which the government continued to be billed by so called 'cowboy contractors' as a result of those roadside pronouncements. Conversely, legitimate projects that were properly budgeted for and approved by Parliament were delayed, in some cases for years, in order to accommodate those that were not budgeted and approved. This practice grossly undermined the public financial management system in Kenya, as it was no longer a reflection of government policies and priorities.

The situation was so grave that on assuming power in 2003, the new government (under the banner of the National Rainbow Coalition – NARC) was forced to set up a commission to scrutinize claims of

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pending bills and advise the government on possible solutions. Although the report of this commission has not been made public to date, preliminary findings indicated that a large portion of the claims was false and undeserving of payment. There are also indications that some of the bills that had already been paid were not genuine and therefore the moneys should be refunded.

2.3 The Kibaki administration

The NARC government came to power when the public financial management system had all but broken down. The all-powerful executive had turned

public budgeting into a political tool to reward and punish regions rather than serve the general public. Whatever was decided by the Cabinet passed through Parliament because of the large size of government. Moreover, the low emoluments and allowances paid to MPs meant they had to live on hand-outs to supplement their incomes, thus making it easy for them to be compromised. This encouraged corruption.

Because of such abuses, the general public supported the legislature in its struggle to wrest control of public finances from the executive, especially following the emergence of the Anglo-leasing scandal in 2004 and, more recently, the abuse of maize imports intended for famine relief. The scandals that emerged under the NARC administration dented the government's image to such an extent that restoring public trust continues to be a major challenge.

In response to mounting pressure, a draft budget law was brought before the House in 2005. The bill recognized the need to get the legislature more involved in public financial management. It was strongly resisted by the executive, however, and allowed to lapse by the end of the term of the 9th

Parliament. The 10th Parliament picked up the draft and moved quickly, not only to enact it as the Fiscal Management Act of 2009, but also to establish a Parliamentary Budget Office (PBO). Subsequently, provisions of the new law were mainstreamed in new Standing Orders of Parliament, effective from April 2009. Many of these changes were incorporated into the new Constitution.

2.4 Public finance in the new Constitution

The public finance provisions in the new Constitution were therefore significantly influenced by the need to correct past executive excesses and abuses. Chapter 12 of the new Constitution begins in Article 201 with guiding principles and a framework for public finance, which if strictly adhered to can alter policy formulation and the management of public resources for the better. Among the key principles are requirements that there should be:

- Openness, accountability and public participation.
- Promotion of equity, meaning that the tax burden is shared fairly at both national and county levels.
- Public expenditure that promotes equitable development and addresses marginalized areas and groups.
- Equitable sharing of debt benefits and burden between current and future generations.
- Prudent and responsible use of public resources.
- Responsible financial management with clear fiscal reporting.

The requirement for equity within and between counties has set the stage for Kenyans to take the government to task when communities or areas are perceived to be discriminated against. Previously, the government did deny essential services to some areas on the grounds that they had voted against the ruling party. These regions were cynically advised that bad politics was bad for their lives, i.e. *Siasa mbaya, maisha mbaya* (Kiswahili for "bad politics, bad life") meaning that unless they towed the political line set

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by political leaders, they would suffer discrimination. In future, however, affected communities will have recourse to a constitutional court, a fact that will most likely encourage more responsible political behaviour on the part of leaders.

The provisions of the new Constitution have also enabled the transfer of key public finance responsibilities from the executive to the legislature. Furthermore, some of the oversight institutions have been reorganized and new independent constitutional offices created by splitting the control function of the Controller and Auditor General (CAG), for example, into two, i.e., the Controller of Budget (COB) and the Auditor General (AG) under Articles 228–229. Second, the Constitution extended the role of the COB to monitor budget execution and report on a quarterly basis to Parliament. Third, and perhaps most significant, it overhauled the roles, functions and duties of the Treasury. As a result, the Secretary of Finance (formerly the Minister for Finance) and the Principal Secretary (formerly the Permanent Secretary, Treasury) were relegated to legislation. This is a complete departure from the 1963 Constitution, which, in Chapter VII, gave very clear and distinctive mandates to the Finance Minister, leaving the legislature to deal specifically with matters of approval and oversight.

The other key changes are fiscal decentralization, with county governments empowered to decide on the use of resources allocated to them, and the establishment of the Commission for Revenue Allocation (CRA). The CRA is mandated to oversee the allocation of revenues between national and county governments and advise the legislature. To safeguard the autonomy of county governments, the 2010 Constitution shares both the revenue base and the revenues collected nationally. Similarly, to consolidate fiscal decentralization, the new Constitution establishes a Senate and county legislatures as key institutions on matters of county finance.

One can understand the public frustration and

concerns with past cases of corruption and misuse of public funds, but it would be naive to assume that politicians have higher moral authority than professionals at the Treasury to manage public finances in the absence of some kind of control. As the most recent scandal on maize imported for famine relief demonstrated, the country needs to operate with adequate checks and balances in order to safeguard public interests and the funds. This is clearly not always the case with provisions in the new Constitution. Besides the fact that power corrupts, whether in the legislature or elsewhere, Kenya has a very high turnover of MPs in Parliament. In the last General Election, for example, over 70 per cent of sitting MPs were not returned by the electorate. The newly elected members thus included a large number of first timers, which inevitably creates instability in decision making. This situation requires serious efforts to ensure adequate, competent non-partisan technical support in Parliament to bridge the skills gap among the legislators. To access such skills, there is urgent need to build quickly the capacity of the PBO. It is also necessary for Parliament to access high calibre independent professional services on public finance, as well as other areas as and when needed.

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3.0 Constitutional Changes and the Legal Regime on Public Finance

Following their 20-year struggle for a new constitutional dispensation, Kenyans' expectations are high that the new Constitution will deliver

significant benefits. Key among these is the anticipated change in the behaviour of Kenya's leaders and correspondingly the management of public resources. Many public pronouncements made by politicians in fact stressed that when the 2010 Constitution is implemented, there will be no more abuse of executive power or plunder of public resources.

Unlike the old Constitution (1963), Chapter 12 in the new document includes specific and detailed provisions on public finance issues ranging from guiding principles, modalities for the generation and sharing of revenues between national and county governments, all the way to reporting and accounting. These provisions appear to be based on the belief that past abuses arose from inadequate constitutional provisions, which is not necessarily the case. Some countries, including the UK, do not have formal constitutions yet they have demonstrated good track records of fiscal discipline in the public sector. For this reason, past abuses can be attributed to many other reasons, including:

- **Impunity:** Too many instances of leaders dipping their fingers into the public till and still continuing to hold public offices. In some cases they were simply transferred from one public office to another one of equivalent status.
- **Oversight gaps:** The belief, among those squandering public resources, that they are unlikely to be caught or even punished if found out.
- **Cronyism:** The apparent inability of political leaders to take firm action against offenders. If anything, the leaders bent over backwards to save their colleagues; for example, amending the Constitution (1963) during the first presidency to provide for pardon for election offences.
- **Insufficient public activism:** Lack of public or citizen anger, which could deter looters of public resources. Instead, those stealing from public coffers portrayed themselves as doing it for the good of the communities from which they came (Kituyi, 2011).

It took a long time for the general public to appreciate that looting public finances hurts everyone, including people from the leaders' communities. It creates a precedent for others to follow and eventually entrenches a culture of abuse. Reading through the new Constitution, one gets the impression that there is a belief that if the document provides specifically for what should or should not be done, that in itself will discourage abuse. While the changes detailed in the new Constitution do have the potential to deliver on the expectations, the fundamental problem of abuse of public resources can be dealt with more effectively by making it more expensive for the individuals who get involved. It is necessary to appreciate that what will make those in charge cautious and respectful of the new legal environment is the certain knowledge that they will face serious sanctions should they commit offences related to the abuse of public resources. That is, there is a high likelihood of being punished and that such punishment will be expeditiously undertaken.

A detailed comparison of the public finance provisions of the two constitutions, old and new, is provided in Annex A to this chapter. Substantial authority over public finance has now been transferred from the executive and traditional institutions like the Treasury to elected leaders in both the National Assembly and the county legislatures. Despite the apparent desire to get rid of some of the current institutions and create better ones, however, the transfer has been done without the establishment of the necessary checks and balances to prevent the legislature from introducing changes to government budgets that are not funded. This can expose the country to excessive domestic borrowing as has been seen in countries like the USA. As Anderson (2008) has noted, in such an environment two possible outcomes arise: legislative work on the budget will parallel the government, and may result in either greater cooperation or greater rivalry between the two branches (Anderson, 2008). He adds that the legislature faces tension between the self interest of members to promote their careers by concentrating on their constituents and the collective interest of the

institution to produce sound, coherent legislation. The tendency is for members of the legislature to favour more spending in particular areas without appreciating that they ought to ensure prudent fiscal management, of both revenues and expenditures.

It is also worth noting that while the 2010 Constitution provides for the role of the legislature in public finance processes, Chapter 12 leaves out significant details to be dealt with in subsequent legislation on public finance. A key challenge here is how the role of the legislature will be balanced between oversight, and the actual handling of policy, budget formulation and approval. As Parliament effects changes to budget proposals on taxation or resource allocations as provided under Article 114, issues will arise as to whether it can, at the same time, hold the executive to deliver on previously approved policy commitments. With the provision for public participation, spending priorities should focus on what citizens decide, leaving limited room for the legislature to bring about change. Care must be taken in developing public finance laws that are aligned them with the letter and spirit of the 2010 Constitution.

Also, with the additional authority now conferred on Parliament, it will be necessary for the House to ensure that public finances are managed efficiently and meet the needs of citizens. In so doing, it is essential that fiscal discipline be enforced all round, with firm checks and balances, so that budget implementation is aligned to available resources and those responsible for spending are held to account. In addition, Parliament needs to pay close attention to the planning and implementation of public projects and programmes. To succeed, it will be necessary to identify key institutions, assign them roles and responsibilities, and develop their capacities. Likewise, it will be necessary to ensure that parliamentary involvement in matters of public finance adds value to public financial management. This principle should apply to all the institutions involved in public financial management, without exception.

4.0 Implications of Some of the Key Changes

Clearly, the far-reaching changes introduced in the new Constitution require a complete redesign of the policy and legislative infrastructure and public finance institutions. Of special interest are changes to the provisions of Article 48 of the old Constitution (1963), which prohibited members of the legislature from originating money bills or amending bills before the House to introduce new or additional financial obligations. As noted above, the 1963 Constitution (as amended) further prohibited the legislature from introducing additional taxation or tax waivers, or making commitments to contract, waive or guarantee debt. These prohibitions were intended to separate oversight from execution, leaving Parliament with the mandate to scrutinize proposals and ensure consistency between resource mobilization, allocation and use, and linkages to existing policy. As for debt proposals, Parliament was supposed to scrutinize them and ensure they were within the set limits, consistent with the law, affordable and sustainable. In short, Parliament's role was to avoid reckless public borrowing. Unfortunately, however, this did not happen.

With the provision for public participation, spending priorities should focus on what citizens decide, leaving limited room for the legislature to bring about change. Care must be taken in developing public finance laws that are aligned them with the letter and spirit of the 2010 Constitution.

4.1 Countering parliamentary licence

Many MPs, and sometimes even ministers, have in the past been at the forefront of pressuring the government to write off farmers' loans, e.g., in the coffee, sugar, pyrethrum and milk sectors. They have also exerted considerable pressure for the increase of access to subsidized health care, education and other social services, all of which require additional public resources. Unfortunately, those who advocate for such increased spending do not

suggest that taxes be increased. If anything, some have protested against the introduction of new taxes. For example, there were loud protests by some MPs when Kenya's Finance Minister lowered the import duty on wheat in compliance with an agreement by finance ministers of the EAC. If such experiences are anything to go by, there is a likelihood of increased pressure to spend more – without a commensurate increase in revenue mobilization. Such a practice could lead to fiscal imbalances.

To ensure that legislative changes do not create fiscal or macro imbalances, Anderson (2008) suggests that some parliaments (including those in Europe) permit changes but require that they do not affect agreed pre-determined totals. Any enabling legislation should therefore set clear rules on when and how Parliament may introduce unfunded expenditure commitments. In particular, this should provide for a prior assessment of the fiscal implications and how they will be addressed. And if they cannot be addressed, then questions of how to deal with fiscal problems arising from legislative changes to budget proposals must be anticipated. The preferred position would be to adapt the European parliaments' practices that empower legislatures to effect budget changes provided the aggregate situation remains the same. Such a practice provides a minimum level of checks and balances that leaves the details to be included in the legislation.

4.2 Shoring up parliamentary authority

In the new 2010 Constitution, Parliament has unlimited authority to introduce, amend and alter money bills under Article 114. It can also move motions that have financial or fiscal implications, including matters related to contracting public debt. The only conditions necessary are that:

- A House Committee has made recommendations,
- The legislature receives and considers the views of the Cabinet Secretary for Finance, and
- In the case of public debt, there is equity between current and future generations.

These provisions mean that Parliament now has the authority to introduce new taxes and adjust or introduce new expenditure measures. It is also free to waive taxes, incur public debt or give guarantees. The ability of Parliament to undertake the new roles effectively will present a challenge because:

- Kenya has one of the highest turnovers of MPs in the world. As parliamentarians' terms of service improve and attitudes among professionals regarding politics change, the turnover could rise even further.
- Members and chairs of fiscal committees change frequently, in many cases in every session.
- Kenya has a highly fragmented political party system, which makes it difficult for MPs to agree on crucial matters of policy or principle, such as who should head which House Business Committee.
- Many MPs have limited knowledge on many technical issues, especially public finance.
- Politicians have a tendency to pay more attention to self and vested interests, which may compromise national interests.
- The PBO is new and is yet to consolidate and build the necessary capacity to support the members.

Besides, Kenya has a higher tax effort than its partners in the common market – meaning that the country collects more tax revenues as a ratio of its gross domestic product (GDP) than neighbouring countries, a situation that has led local investors to complain of being more heavily taxed than their counterparts in other EAC member countries. As the EAC becomes more consolidated, this perception, whether real or not, can prompt investors to relocate their activities to neighbouring countries and sell their goods and services to Kenya rather than producing here as well. These factors make Kenya's fiscal policies more complex than those of the other members of the EAC. The policies require constant review by policy makers, and if Treasury is not fully in charge of this process, it will be necessary to have another agency to keep the legislature fully briefed on the possible consequences of wrong decisions in this critical area.

5.0 Other Country Experiences

Countries having similar legislative powers on public finance including the USA runs very high budget deficits, a situation that could present serious fiscal and monetary policy problems if replicated in Kenya. For a country like Kenya, a net importer of capital with a very narrow tax base, an expansionary fiscal policy would pose serious economic management challenges. It is therefore necessary to take adequate measures to reduce risks of escalating public expenditures. Examples of public financial management from a few other countries offer useful lessons for Kenya.

5.1 Indonesia

Fiscal decentralization in Indonesia accelerated after the enactment of fiscal balance laws in May 1999. The shift was driven by a recognition that the people wanted to be more actively involved in management of their daily affairs. Unlike Kenya, the pressure was more from the resource-rich regions. Consequently, decentralization was perceived to give greater control over resources aimed at improving service delivery. The law required that a minimum of 25 per cent of revenues, inclusive of oil and gas receipts, be transferred to regions. A General Allocation Fund, similar to Kenya's County Fund, was established for this purpose. However, special provisions were made to enable regions that produced oil and gas to receive a share of such revenues.

Compared with other international experiences, the Indonesian decentralization has led to improved public goods and services. It has also been associated with more targeted resource allocation, better tailored to local needs. The risk of capture by vested local interests remains real, however. With such capture political pressures and vested interests can lead to poor prioritization and sequencing of public programmes. This experience seems to concur with the Kenyan experience with the Constituencies Development Fund (CDF),

where resource allocations have been significantly influenced by political interests and pressures.

In Indonesia and elsewhere, among the challenges experienced with fiscal decentralization are:

- A tendency for sub-national governments to overspend while paying inadequate attention to raising own revenues.
- A lack of capacity, in both knowledge and skills.
- Failure to establish effective budgeting and expenditure management systems.
- Lack of clarity of functional demarcations between various level of governments, including national, sub-national governments and lower units such as municipal councils.
- Resistance by staff who do not want to be decentralized, and also resistance by sub-national governments to receiving personnel from the centre.
- Poor flow of information between the regions and the centre.

In the early stages of fiscal decentralization, dealing with staff who were originally employed by central government posed serious challenges as many staff resented transfers to what they perceived to be a lower level of government. A corresponding resistance by local politicians was also observed, as they preferred locally recruited personnel, which could also be a problem in Kenya where politicians invariably prefer their 'own people' rather than those from other regions. This has been especially the case where ethnicity is a major factor. Still, fiscal decentralization has been found to be better suited to reorienting public finance to pro-poor initiatives. It is therefore an ideal tool for addressing regional disparities and, when well managed, can be used to promote political harmony.

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5.2 Decentralization in Africa: The case for South Africa and Uganda

Since the 1980s, decentralization has been implemented in several African countries. These efforts aim to achieve such objectives as:

- Bringing public services closer to the people;
- Addressing inequalities;
- Promoting citizen participation; and
- Strengthening democratic institutions.

While all of these issues have been major concerns in Africa, the African experience with decentralization is limited by two factors – late starts and political fragility. Thus recorded evidence is scant. It is recognized, however, that the interests of the

poor, who predominate in the continent, are better addressed when a sustainable decentralized system is in place. This is especially the case when service delivery improves, and planning and resource allocation are then better aligned to local needs as a function of such decentralized governance systems. In such cases, decentralization can be used to address regional and group disparities.

The demand for change has been largely prompted by abuse and misuse of highly centralized systems. It has also been encouraged by the belief that fiscal decentralization encourages the

flow of local information, and that it links citizens' needs more closely to policies and programmes. On the reverse side, there have been concerns that if not well managed, decentralization can lead to capture by local political and self-interested elites who may turn the policies and programmes for their benefit, worsening the situation for the poor. The risks are said to be higher where there are weak democratic institutions, especially electoral systems, and where

the poor, who are less informed, are more likely to vote on the basis of the candidates' campaign spending.

The other risk associated with poorly designed decentralization is an increased culture of dependency. There is also the added risk of lack of balance between social expenditures and capital investments, which may hurt the long-term development of the affected areas. Finally, there is the challenge of the structure of government and the costs associated with it: the more the layers, the higher the cost of running the government.

Among the African countries with longer experience are South Africa, Ethiopia and Uganda, where good progress is reported. Rwanda is a more recent entrant into the decentralization drive. The accumulated experience indicates that decentralization can be used effectively to promote poverty reduction through better linkages between citizen needs and budget allocations. However, it is necessary to recognize the pitfalls associated with decentralization. For Kenya, the way forward may be easier if other country experiences and pitfalls are noted and avoided.

5.2.1 South Africa

The country operates a three-tier unitary system that is regarded as one of the best on the continent. The three levels are national, provincial and municipality. The model does not subordinate the municipality to the provincial, and the national government has the mandate to coordinate sub-national governments. Prior to 1998, South Africa used discretionary transfers for its revenue-sharing model. In 1998/99, however, formula-based transfers were introduced. Under their 1996 Constitution, an equitable share of resources is to be allocated to each layer of government. After extensive debate, it was agreed that the distribution be based on national standards and costing factors.

A total of seven transfers is effected with some, notably for health and education, being

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conditional. This means that the allocated funds must be used for specified purposes in the targeted sectors. The indicators used include population, demographic structure, population eligible for social security, population of school-age children, wage remuneration in a province, etc. It is worth noting that the provinces do not have a specified revenue base. For local authorities, districts and municipalities, however, the revenue base is mainly drawn from property rate collections and user charges. This has led to resistance by taxpayers, and political pressure, all of which make the sources inelastic, often leading to insufficient revenue generation. The South African model requires the sub-national governments to align their operations to national policy, which is similar to what Kenya's new Constitution requires of counties.

5.2.2 Uganda

Uganda has a legally mandated decentralization based on the district as the sub-national unit of government. As in Kenya, Uganda's 1995 Constitution empowers sub-national governments to levy taxes to generate their own revenues. With regard to resource transfers, districts receive conditional and non-conditional grants, estimated to constitute over 80 per cent of sub-national government expenditures. The unspecified grants, which are equivalent to the minimum 15 per cent transfers provided for in the new Kenyan Constitution, are untied and spent at the discretion of the local legislature.

Sources of district revenue include graduated taxes, licences, user charges and producer taxes over which the sub-national governments have the discretion to determine tax rates, but must consult with the Minister for Local Government, a situation that affects their autonomy. Despite this requirement, Uganda has demonstrated a commitment to devolution with checks and balances to promote accountability, transparency and citizen participation.

Three channels are used to enhance accountability:

- External audit by the Auditor General;

- A formal system of Public Expenditure Tracking Surveys (PETS); and
- Citizen involvement in which sub-national governments are required to integrate participatory planning and budgeting based on national guidelines.

In this regard, the sub-national governments are required to engage stakeholders – local leaders, the private sector and professionals. The plans they prepare must address local needs and be consistent with available resources. Although the planning is expected to promote mutual accountability between elected leaders and the public, the mechanisms to apply this downward accountability have been difficult to put in place. To give meaning to the consultative process, sub-national governments are required to prioritize their investments and to hold district budget conferences early in the medium-term expenditure framework (MTEF) process. The district budget is also required to adopt an integrated sector approach that is part of the district plan. This means that various sectoral activities/programmes and projects should be coordinated and harmonized.

District governments are reported to be fairly autonomous, with powers to decide on and plan for the use of their own resources and untied grants. There is, however, concern over the effects of conditional grants that may limit flexibility and decision making at district level and, more importantly, create a measure of unpredictability.¹ As a result, conditional transfers pose the risk of potential changes in resource flows. Finally, Uganda, like other African countries, has assigned unproductive and unsatisfactory taxes to the sub-national governments.

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¹ In addition, there is also concern about the high proportion of transfers going to personnel emoluments.

Such experiences provide useful background for Kenya and should be used to design a more effective model. For example, if conditional transfers are used, the government should ensure that there are funding mechanisms to finance operating costs once transfers stop. Failure to provide for such arrangements may pose problems with sustainability.

6.0 Revenue Sharing

Kenya's 1963 Constitution did not provide for revenue sharing between national and sub-national governments, a situation that led to under-provisioning at these lower levels of government, affecting their service delivery. This position has been reversed in the new Constitution, which entrenches fiscal devolution that provides for sharing of both the revenue base and the nationally collected revenues. In addition, the 2010 Constitution sets out criteria to be followed when sharing the revenues vertically; among other things the Constitution requires the following:

- Prioritizing national interest, specifically national debt obligations;
- Addressing the needs of the national government while ensuring counties deliver on functions allocated to them and meet their development needs;
- Maximizing fiscal capacity and efficiency of county governments;
- Addressing disparities between and within counties together with incorporation of affirmative action for disadvantaged areas and groups;
- Optimizing county economic potentials;
- Ensuring stable and predictable revenue allocations; and
- Maintaining flexibility and ability to respond to emergencies.

The 2010 Constitution goes ahead to set the

aggregate minimum transfer to counties at 15 per cent of centrally collected revenues, a threshold that will be based on the latest audited national revenue receipts. The Constitution also mandates additional transfers depending on functions delegated to counties. In addition, the Government is required to establish an Equalization Fund, financed by 0.005 per cent (one-half per cent) of nationally collected revenues, to be reserved for marginalized areas to finance basic services like water, roads, electricity etc. The fund is to be maintained for an initial 20 years at least, and may be extended by the National Assembly. The Constitution provides that a bill to appropriate money out of the Equalization Fund be prepared and scrutinized by the Revenue Sharing Commission, which is required to advise the two Houses of the National Assembly. Unfortunately, the Constitution does not indicate who is responsible for preparing this bill. In the view of the author, this provision should be detailed in the appropriate law.

With the clarity on revenue sharing provisions that provide for a minimum quantum of resources set aside for counties, the possibility of conflicts between the legislature and the executive and between the national government and the counties has been minimized. Some politicians have created confusion, however, by giving their constituents the impression that the 15 per cent allocation from the central government will be given in addition to what they are already getting from the Local Authorities Transfer Fund (LATF) and the CDF. Ideally, there should be no confusion because the Constitution makes it clear that counties should be given adequate funds to fulfil their mandates. There is an urgent need to move fast to delineate the functions of the two levels of government and eliminate duplication. Depending on which functions are devolved, it will be much easier to determine whether 15 per cent is adequate or not. If it is not adequate, the Constitution requires that more resources be transferred to match the increased functions of the county governments.

Some confusion has arisen from the continued agitation by politicians not only to retain the CDF,

but also to increase it. Obviously, this will be unaffordable, and will in all likelihood introduce competition between funds such as the Equalization Fund and other mandated transfers. There is also a need to ensure coordination between the fiscal activities of the two levels of government, on the one hand, and the activities of other government agencies and funds, on the other. There is already enough wastage of public funds because of the lack of coordination in the fiscal operations of the local authorities, the line ministries and the CDF. A clear, legally-based sharing of mandates between the two levels of government would ensure policy clarity and direction so that sufficient resources can be allocated to meet their functions and eliminate duplications by funds like the CDF.

Another key concern at lower levels is the sharing of base revenues to the counties. Under the LATF, funds are shared and disbursed to all local authorities on the basis of transparent, objective and equitable criteria. This mechanism makes it possible to disburse funds directly to the counties without their having to pass through intermediate call stations. Once the local authority qualifies for allocation, the money is transferred directly to its commercial bank account.

Yet even as the focus remains on the resources that will be transferred to the counties, it is necessary to pay attention to capacity building at the county level. Experience shows that many of the current local authorities do not have the capacity to handle what they are already doing, even without the additional new responsibilities. Lack of financial resources may be at least partially to blame for the poor performance, but the quality of personnel and political leadership is also a major challenge. Councils have been characterized by public quarrels, frequent fighting and poor revenue mobilization, with some failing to pay their staff for months, a situation that presents valuable lessons. In the 1980s, the government introduced the Local Authority Service Charge as a source of revenue for this level. Unfortunately, most local authorities could not manage assessment and

collection and the service charge was abolished. All these factors suggest an urgent need to conduct a skill gap analysis to establish the current capacity of county governments and identify what needs to be done to ensure counties start on a more positive note than did the local authorities.

An orderly transition to the new constitutional dispensation requires a transparent and predictable horizontal fund allocation and transfer systems so that the public can hold county governments accountable for service delivery. The responsibility for horizontal revenue sharing criteria has been delegated to the CRA. The CRA will benefit from the managerial experiences of the LATF, under which funds can be withheld if a local authority fails to perform or to account for funds already disbursed. In this regard, the LATF has been fairly successful in that allocations are gazetted every quarter to inform the recipient authorities and the citizens so that they know and can plan programmes and projects for implementation. One of the most important lessons learnt from managing the LATF, and one that is corroborated by other country experiences, is that when something goes wrong and funds are withheld, it is the citizens who suffer and not the council officials who may have failed in performing their duties. To avoid victimizing the citizenry, there is a need for better targeted sanctions so that non performing public officers bear responsibility. This means that withholding transfers to sub-national governments should be a last resort measure; the law must make this clear and specify the corrective action required to avoid any negative effects upon the citizenry.

To promote citizen participation and enhance accountability, it is strongly suggested that transparent systems be used for all levels of government. This will give citizens an opportunity to check if revenue sharing, whether at national or county levels, complies with the principles stipulated in Article 201. If not, they can challenge those responsible to ensure that equity and all other aspects detailed in these principles are also applied at lower levels and

used for the benefit of the target groups, in counties, municipalities and town councils.

6.1 Commission for Revenue Allocation

The 2010 Constitution provides a very clear basis for revenue sharing predicated on fairly solid principles. Conversely, it establishes institutional arrangements that are heavily politicized and could lead to operational problems. The chair of the CRA is to be nominated by the President in consultation with the Prime Minister and approved by Parliament. Two of the other seven members will be nominated by political parties in the National Assembly and five by political parties in the Senate. The only non-political member will be the principal secretary for Finance. Although these nominees should not be sitting members of the National Assembly or the Senate, the composition will most likely introduce politics into revenue allocations.

If past experience is anything to go by, the nomination process could give rise to political conflicts, especially if those appointed perceive themselves as being there to serve or promote the interests of the nominating parties. Political intrigues have in the past interfered with decision making in Parliament as members paid more attention to their political party than to the national interest. This could emerge as a factor in the CRA and hinder its operations. It would have been preferable to leave the composition to legislation, which would be much easier to amend as and when new situations emerge. To entrench the CRA in the 2010 Constitution and make it overly political may undermine its objectivity.

An additional challenge arises from the wide mandate given to the CRA, which includes making recommendations on public financial management at the county level and advising on revenue enhancing measures at the national level. These mandates need to be clarified in an appropriate law to avoid potential conflicts with existing institutions like the Kenya Revenue Authority (KRA).

6.2 Review of allocation criteria for counties

The Senate is required to review the basis of revenue allocation every five years according to the provisions and criteria set out in Article 203. In so doing, it will receive recommendations from the CRA, consult with county governors and the Secretary for Finance, and invite professional bodies to make submissions. Such consultations were not provided for under the old Constitution (1963): Government consultations were done in much the same way as budget hearings – at the discretion of the executive and only by invitation. With citizen participation in public financial management stipulated by the new Constitution, stakeholders will have the opportunity to influence fiscal policy on both taxation and resource allocation. Hopefully, this participation will improve accountability, efficiency and outcomes.

Once the Senate arrives at a resolution, it will be required to submit the statement to the National Assembly within ten days, where it may be approved, amended or rejected by a two-thirds majority vote. Should the National Assembly not approve the Senate Resolution within 60 days, the resolution will be deemed approved. The Senate, on the other hand, may amend its resolutions at any time. This institutional arrangement factors in the nation's political diversity, a situation that will clearly improve and entrench democracy. It may also pose serious challenges to formulating and managing fiscal decentralization policy in the early stages, however, as stakeholders adjust to the new environment, especially with regard to timing and coordination. More importantly, citizens can participate effectively only when they have access to adequate, accurate, relevant, up-to-date information. For this reason, the pending legislation ought to provide for public consultations on dissemination of public finance.

Against the existing culture of secrecy in the management of public affairs, fundamental adjustments will be required to build capacity all-round for public officers and citizens. It will also

be necessary to entrench equity and fairness into revenue sharing laws in order to avoid unnecessary controversy and recourse to the Constitutional Court. The institutional arrangements in the new Constitution are designed to avoid discretionary decision making and a repeat of past abuses, so as to reduce the influence of political and vested interests in resource allocations. For example, in the 2010/11 Budget, funds for the Economic Stimulus Programme (ESP) were shared equally among the constituencies, irrespective of variations in population and poverty levels, which would be open to questions under the principle of equity. Money for employment of teachers was similarly allocated equally to each constituency. In both cases, no attempt appears to have been made to assess the actual needs on the ground, for example, the number of schools per constituency. In the case of teachers, some constituencies have fewer than ten secondary schools in total while others have more than 50. To allocate equal funds for teacher employment is to fan taxpayer resentment, which encourages tax evasion and avoidance.

It is important to appreciate that any time the people feel short changed, their willingness to pay taxes is negatively affected. The new Constitution acknowledges this by making the equitable sharing of the tax burden one of the principles of public finance. If this principle is strictly observed, it will make sharing of revenue receipts more acceptable and hence sustainable. Unfortunately, politicians have shied away from discussing matters of the tax burden and concentrated on preaching the gains to be made in resource sharing. Therefore, a lot remains to be done to make Kenyans appreciate the fact that, in public finance, nothing is free. Every benefit must be paid for by somebody, in the form of taxes or debt.

6.3 Sharing the revenue base

In an attempt to avoid unreasonable tax competition within and between national and sub-national governments, the new Constitution categorizes

taxes for each of the two levels. Income taxes, value added tax, excise duties and customs tariffs will be imposed only by the national government. On their part, counties will be able to levy property rates, entertainment taxes and other rates authorized by legislation. The national government is prohibited from taxing the areas set aside for counties, while counties are barred from imposing taxes that can interfere with or prejudice national economic activities and policies, in particular taxes that hinder movement of goods and services.

For the first time, Kenya's constitutional document recognizes the lower levels of government and carves part of the revenue base for them. This is a major change from the old Constitution (1963), which left local authorities at the mercy of the centre on matters of revenue or taxation. Indeed, sub-national governments were not recognized and therefore their existence depended on the goodwill of the political establishment. The missing link in the new Constitution is that no reference is made to levels of government below counties, for example cities, municipalities and town councils. In addition, there is no mention of how these can be established or funded. This omission will have significant implications for the survival and operations of municipalities and town councils, which are normally hotbeds of social, economic and political problems.

Already one can perceive a serious problem in the sharing of the revenue base between counties, on the one hand, and municipalities and town councils, on the other. The heart of the tax structure allocated to counties, that is, property rates and licences, is also the main source of revenue for urban-based local authorities, as it is in the urban areas that most real estate development takes place and where most of the businesses that pay taxes are located. Consequently, with local governments falling

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under the counties, there is bound to be severe competition for the control of the resource base that has been ceded to counties. The reality is that property rates are currently applied only in towns and municipalities and not on rural properties, which are either freehold or community owned.

Still, certain aspects of the implications of the new Constitution remain unclear. The new constitutional dispensation may see the elimination of levels of government below the county, thus doing away with this challenge. Yet, there is a need to retain sub-governments to deal with rapidly increasing urbanization, together with its associated social and economic problems. Article 184 of the new Constitution provides for this to a degree (for urban areas and cities). To the extent that they experienced special problems, they will need targeted attention. If they are retained, it will be necessary to enact a law, providing them with a revenue base, and ensuring accountability and definite governance structures. Otherwise, when it comes to resources, competition between the two sub-national governments can lead to conflicting taxes and multiple licences, which may affect economic activities in these critical areas. In the meantime, it is critical for those concerned to undertake fact finding on best practices and begin preparing appropriate legislation. Ideally, the Constitution should not have specified taxes for each level, but left it for inclusion in a legislation which is easier to change in case of problems.

7.0 Collection, Custody and Management of Public Funds

This aspect of public finance remains largely the same except for the introduction of the COB and the expansion of the control function to include

oversight of budget implementation, in addition to approving the release of funds from the Consolidated Fund and other public funds, including county funds. Under the 1963 Constitution, the CAG did not oversee budget implementation or get involved in local government expenditures. The change effectively means that in future the county budgets will be supervised by the COB. In addition:

- Money received by or on behalf of counties will be deposited in a County Revenue Fund and the COB will approve the release of money from this Fund.
- Money from the County Fund will be withdrawn only when authorized by an Act of Parliament or the county legislature.

These provisions will bring financial management at county level under the control of a constitutional office, which may help improve performance of these important units of government. To be effective, however, it will be necessary for the COB to build capacity and infrastructure in the 47 counties and establish offices at county headquarters.² This will include developing a system similar to the integrated financial management information system (IFMIS) currently being implemented for the national government.

7.1 Taxation and tax privileges

Among the landmark provisions of the new law, and another major departure from the past, is the prohibition of tax exemptions for any public officer. Previously, constitutional office bearers, MPs, senior public servants and university lecturers enjoyed enormous tax privileges – privileges that were managed without transparency. While some of these benefits were designed to compensate for the low emoluments paid to holders of these key offices, the lack of transparency encouraged abuse and misuse of such exemptions. Besides, the benefits were neither costed to determine the impacts on revenue, nor taken into account when the affected public officers agitated for salary increases. More importantly,

² It is recognized that while this may be good for accountability, it may also present operational challenges and increase costs.

access to these benefits was inequitable, because some of them, like exemptions on motor vehicles, depended on the cost of the vehicle and not the services rendered or the position of the officers. Officers who bought more expensive vehicles got more benefits than those who could only afford cheaper ones. An officer who could not afford a car got no benefits at all.

This practice also encouraged low pay, which negatively affected pension benefits, leading to inadequate provision for retirement. Moreover, such hidden benefits camouflaged the real personnel costs in the public sector. What the 2010 Constitution seeks to do is to ensure that public officers' pay and benefits are transparent and equitable, which is in the best interest of accountable and transparent public finance management. To ensure those affected are no worse off than they were before the new Constitution took effect, it may be necessary for the new Salaries and Remuneration Commission (see section 8, below) to add the loss value to the emoluments as it seeks to harmonize pay and benefits in the public sector.

Besides privileges to public officers, there have been massive abuses of tax remissions, exemptions and write-offs, all of which were availed at the discretion of the ministers in charge. As a general rule, these benefits were mainly enjoyed by well-informed and/or connected persons (including ministers) and continued largely unreported. In only in a few cases were some of the remissions questioned, generating public debate, and these were mainly instances of complaints by people who had sought similar privileges but did not get them.

The spirit of the new Constitution should not be based simply on the need to remove or eliminate waivers and other tax benefits. On the contrary, the intention should be to ensure that when benefits are granted, this is done transparently and accountably. In this context, it is important to appreciate that tax privileges should in general be granted only on the "principle of public interest", that is when a person

extends support to beneficiaries who should have been the responsibility of the government or the community. Examples include support to charities, the aged and destitute, health and medical services to the disadvantaged in the community, or assistance proffered during a humanitarian crisis. Unfortunately, this has not been the case in the past. Those who accessed tax benefits, exemptions and waivers were the politically connected or were associated with bad governance, such as corruption.

To seal such loopholes and make the system transparent, the 2010 Constitution requires that:

- Full details of tax waivers and exemptions be fully recorded;
- Reasons for the waivers be fully explained; and
- A report be availed to the Auditor General.

These provisions are consistent with the principles of transparency and accountability, which are expected to discourage the continuation of past abuses of public offices. The provisions should also encourage best practices, which require that employment compensation be transparent and subject to tax.

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7.2 Budget process

On budget preparation and expenditure management, the old Constitution (1963) left most of the decisions to the executive. The new legal framework changes these processes quite substantially, particularly for the role of Parliament (see diagrams in Annex B). Parliament now has constitutional authority to increase or reduce tax rates without the recommendation of the President as was the case with the 1963 Constitution (Article 48). Significant changes have also been made in revenue allocation and expenditure management. To begin with, the transfer to the counties of 15 per cent of the nationally collected revenues will be budgeted for without reference to the national

government or Parliament. The budget itself is to be submitted, not presented, at least two months before the new fiscal year starts. It is to take a disaggregated form showing:

- Separate allocations for development and recurrent expenditures;
- Details of how the deficit will be financed; and
- Details of net increase in public debt.

Perhaps one of the most fundamental changes that may have escaped public attention is that the Principal Secretaries (formerly permanent secretaries), who are also the accounting officers, will account to the National Assembly not to the executive as before. Under the old Constitution (1963) the accounting officers were appointed by

the Permanent Secretary to the Treasury who could also cancel the appointment in case of gross misconduct. The change reflects one of the significant adjustments to the role of Treasury and will pose challenges to the role of the Secretary of Finance and the Principal Secretary, because, previously, the minister was the face of government in Parliament. With the new Constitution, the Cabinet secretaries will not be members of Parliament and therefore the Secretary of Finance will not present the budget proposals to Parliament, a change

that will necessitate a redesign of the accountability system and working relations between the two.

The implication is that the government will be required to establish new structures for discussion and approval of the budget once it gets to Parliament. To cope with the new arrangements, Kenyans will need to get used to not experiencing budget days and the attendant long speeches. It is important to appreciate that the proposed budget system can be highly politicized, as demonstrated in the USA where the Congress occasionally fails to

approve the budget on time, leading to the closure of government offices, as happened in 1996. On this occasion, because of differences between the President and Congress, the Budget could not be approved on time and government offices shut down from 14 to 15 November 1996. Similar disagreements arose in 2010, mainly on account of social spending. Such interruptions may not have much effect in the USA where the national government plays a minor role in delivery of basic social services. In Kenya, however, the situation is different and such an incident would cause a lot of suffering to citizens who depend on publicly provided basic services.

While there is nothing inherently wrong with borrowing from the US's (or other) system, it is essential to recognize that the two societies are not the same. And even though the US system has been tried and tested for over 200 years, it still experiences occasional hiccups. The lesson for Kenya is to tread carefully and roll out change in a manageable way. Some adjustments and creation of alternative arrangements or customization of borrowed concepts will be needed before they can be expected to work well in Kenya. There is need to start early to build the necessary budget and public finance structures so that there are no last minute disruptions as Kenya moves into full gear in implementing the new Constitution.

On the annual estimates of expenditure, the Constitution specifies that these will be submitted in several parts:

- Estimates of national government expenditures including estimates of expenditures for the Judiciary and Parliament.
- Estimates of allocations from the Equalization Fund for marginalized groups and regions.
- County specific revenue allocations.

It is not clear why this fragmentation is necessary. If not properly managed, it could lead to complications and lack of coordination. Ideally, all government expenditure should be consolidated

Ideally, all government expenditure should be consolidated so that a common ranking criterion is used to decide priorities—which should be consistent with the agreed national strategy, such as Vision 2030 together with its medium-term plans.

so that a common ranking criterion is used to decide priorities— which should be consistent with the agreed national strategy, such as Vision 2030 together with its medium-term plans. When the budget is fragmented in the manner provided for in the new Constitution, additional efforts will be needed to ensure that all the proposals are consistent with policy priorities and that all public programmes and agencies compete for resources at the budget table and on equal terms. More importantly, budget proposals need to be constrained by the available resource envelope. Unfortunately, with proposals originating from three different sources without a single coordinating office, it may be much more difficult to agree on ranking, especially when there is need to reduce budget proposals to fit within the available resources.

The fragmented approach provided in the new Constitution will be especially challenging to the PBO and legislature. It will therefore be necessary to move quickly and enact a law mandating the alignment of annual estimates to agreed priorities, as required by the new Constitution. In addition, the law should provide details of how Parliament will ensure that public expenditure remains sustainable to meet the objectives of the principles detailed in Article 201.

It is expected that the extra lead time availed to Parliament by early submission of budget proposals will be used to scrutinize expenditure proposals more critically to ensure they are affordable, realistic and consistent with the needs of citizens. Currently, the budget is submitted to Parliament only a few weeks to the new financial year, which means the fiscal year starts before the estimates are scrutinized and approved. Under the new Constitution, there is room for Parliament to have a more effective impact on resource allocation. If any of the House committees feels that the proposed estimates will not serve the intended purpose, it will be possible to propose adjustments in the House before the fiscal year starts. In the event Parliament does not approve the estimates before the start of the new

financial year, Article 222 provides for provisional approval of up to 50 per cent of the amounts in the printed estimates, which is similar to what happens today.

To cope with the more active parliamentary involvement in budget preparation, the executive will need to strengthen its own capacity, particularly in order to respond quickly to issues raised by parliamentary committees. This is especially necessary because, as a result of the changes, lobby groups will most likely emerge to canvass directly on behalf of key economic operators, as happens in countries such as the USA. In the last Parliament, for example, there were open signs of active lobbying of Parliament by plastic manufacturers following an announcement by the Finance Minister of the intention to levy heavy excise duties on plastic bags. Doubtless there is other, less overt, lobbying taking place as well. A surge in lobbying activities, on both the taxation and the resource allocation sides of the budget, as Parliament assumes more fiscal responsibilities, will put pressure on the executive to improve its ability to face challenges and argue its case to convince the House committees to pass its proposals.

7.3 The role of the Treasury

Among the greatest “losers” in the new legal framework is the Treasury; in fact, the Treasury's traditional functions do not feature in the 2010 Constitution. Treasury has lost much of its control over public resources to the legislature and the COB, while its previous functions of monitoring and reporting on budget execution have been partly transferred to the office of the COB. The COB seems to combine constitutional and operational functions, because, besides being in charge of releasing funds, it will also monitor and report on execution. This will be a new experience for public sector managers who will need to adjust. It could also provide grounds for potential conflicts between Treasury and the Controller of Budget. Thus the role and functions of the Treasury will have to be detailed in an Act of Parliament that is yet to be prepared.

While it is not clear what the intentions of these changes were, it is important to note that in the USA (the model Kenya seems to copy), the Treasury does not prepare the Annual Budget. This is done by the Office of the President. This new system may lead to less attention being given to links between the budget and the policy strategy. As Kenya re-designs its systems and infrastructure for public financial management, it will be important to ensure that the linkages are made.

7.4 Transparency and accountability in the new regime

The new Constitution includes provisions for enhanced transparency and expenditure controls, including one of the most significant provisions – the power to withhold the transfer of funds to counties that engage in persistent breaches of financial procedures.

For Parliament to support the decision to withhold up to 50 per cent of funds to counties, the COB will need to submit a report and recommend such action. The affected county, however, will be given an opportunity to defend itself. Thus, the Constitution has in-built sanctions, which if enforced effectively can lead to improvements in public financial management, enhancing service delivery.

The new Constitution changes all that, however, and requires that government borrowing be subject to greater legislative scrutiny and transparency.

As for financial accountability, among the most important elements in the new Constitution is the categorical provision that heads of government organizations or entities will be accountable to Parliament. Another is that members of the Cabinet (the department secretaries) will no longer be sitting MPs. In the past, there have been many instances when heads of public agencies and corporations claimed they were given irregular directives by ministers. The combined effect of delinking the Cabinet from Parliament, and making heads of public entities accountable to Parliament, is likely

to be a positive impact on financial management. In particular, it will minimize the discretion exercised by politicians and enhance transparency and accountability.

Still, the need for vigilance remains. In as much as it can be argued that decentralization increases transparency and efficiency, while reducing corruption, in practise it merely shifts the location where the latter takes place. Without strong systems of oversight and accountability, incidents of misuse and abuse of public resources could increase commensurately with the increased number of players. To militate against such risks, there is need for strong controls coupled with an appropriate and expeditious system of sanctions.

7.5 Public debt

Article 103 of the old Constitution (1963) provided generally for servicing public debt with no specific reporting requirements. The new Constitution changes all that, however, and requires that government borrowing be subject to greater legislative scrutiny and transparency. Among the new requirements is legislation to provide for:

- Reporting requirements;
- Cabinet Secretary to present details of loans and guarantees to a House Committee;
- Intended use of debt resources and debt services; and
- Reports of progress on loan repayments.

In addition, the 2010 Constitution requires that the public debt maintain inter-generational equity, that is, between current and future generations. This is a new feature that is expected to preclude reckless borrowing and improve debt management.

7.5.1 Dealing with contingent liabilities

The government is now required to publish an annual report on all guarantees within two months after the end of the fiscal year, a measure that is bound to be of great benefit to Kenyan taxpayers who bear a heavy burden for irregularly procured debts. In particular,

making borrowing by state corporations subject to mandatory reporting and parliamentary oversight is bound to improve their financial performance. More importantly, it will facilitate early detection of exposure to contingent liabilities and the taking of corrective action. It may be recalled, for example, that the NARC government, on behalf of various state corporations, paid out a large sum of money that had been borrowed irregularly and used inappropriately, to the extent that the affected corporations could not service their loan obligations. This was done on account of pressure by various political interests, some of which were direct beneficiaries.

The government assumed responsibility on the basis of letters of awareness that had been issued without following the formal procedures, including an assessment of ability to pay or to utilize such loans productively. Although the loans were not legally guaranteed by the government, when the creditors failed to pay and information got to the public, pressure increased for disclosure of the actual defaulters as state-owned commercial banks faced imminent collapse. Had the government-owned commercial banks been allowed to collapse, the main losers would have been innocent depositors. Once the defaulting companies were made public, thereby revealing their political connections, there was an instant public outcry to protect depositors whose funds had been siphoned away by these entities. As the problem threatened the entire financial sector, the government was forced to bail out the public financial institutions to avert a political crisis and the attendant high costs to the taxpayer. The provisions for a more transparent system of reporting on debt guarantees will minimize such risks and are in the best interests of taxpayers and the economy.

To ensure the orderly management of public debt guarantees, the new Constitution requires Parliament to enact a law that should enable the Treasury to issue guidelines on the procedures and the types of loans that may qualify for government guarantees. Such a law should also provide regulations on overall financial management by all state corporations so

that they, too, are subject to the new constitutional principles. In this regard, special attention should be given to organizations considered strategic (such as universities and other public training and research institutions, or public health bodies), which may need protection from liquidation in case of financial default. To ensure the guarantees are sustainable, it may be necessary to provide for a ceiling on total debt guarantees that the government can hold. The proposed legislation should actually be more comprehensive and cover various aspects of management of state corporations, with a clear separation of the roles of cabinet secretaries in appointments of corporation directors so that boards have full responsibility to run their corporations. Past abuses occurred because the ministers who appointed the board members continued to give directives on matters of management, especially on finance, procurements, appointments, etc. The separation of powers is critical to the successful performance of state corporations and is used by countries such as New Zealand.

7.5.2 County borrowing

The counties are prohibited from borrowing unless the loans are guaranteed by the national government after approval by the county legislature. Yet, requiring every loan to be guaranteed by the national government undermines the autonomy of the counties and introduces unnecessary political pressure on the national government. In addition, heavy controls expose the Treasury to unnecessary contingent liabilities.

Like the central government, county leaders should be encouraged to exercise prudent financial management and to take political responsibility and accountability for their decisions. They should not be subject to micro management, as this would give them an excuse to blame the national government for their failure to be innovative in the delivery of public services. The restrictions on borrowing will, in fact, likely present a serious hindrance to the operations at lower levels of government, especially when all they need is a bank overdraft. Ideally, counties should be

able to borrow subject to complying with the law, and provided they have the necessary security. If the concern is that they may borrow too much and risk being liquidated, their borrowing can be restricted to specified sustainable levels. For example, if a county wishes to borrow to build rental houses, appropriate law should allow them to use such assets as security. They may also be required to comply with prescribed procedures, for example accumulating surplus to fund down payments, etc.

For the first time, Kenya's Constitution requires the public sector to maintain a sustainable wage bill, attract and retain skills, and promote productivity and performance. These provisions are expected to minimize disharmony in the public sector and encourage orderly wage and benefit negotiations.

The new Constitution should have borrowed from the experiences of public universities, which only a few years ago were so controlled that they became like dinosaurs, threatened with extinction. Once given the space to assess their potential and make decisions, they engaged in various initiatives funded by commercial bank debts and without government guarantees. So far no university has experienced problems that require the intervention of the central government. For counties,

therefore, the more appropriate option would be for the government to enact a law and provide guidelines for borrowing so that there are adequate controls on borrowing. It is not in the interest of either the counties or the national government to insist that every loan be guaranteed even in cases where a county has the resources and can prove its ability to pay.

8.0 Other Significant Changes

The 2010 Constitution incorporates two significant provisions that have been of public interest: procurement of goods and services, and the

introduction of a Salaries and Remuneration Commission (SRC). On procurement, the new law requires state organs to ensure their systems are fair, competitive, transparent and cost-effective. In addition to requiring Parliament to enact an appropriate procurement law, it also provides for preferences that protect persons previously discriminated against and disadvantaged. Moreover, it incorporates sanctions against contractors and persons who act unprofessionally, default or engage in corruption, which is a reflection of past government failures to take action against well-connected contractors.

8.1 The Salaries and Remuneration Commission

On its part, the SRC is expected to harmonize pay and remunerations across the public sector, and to advise both national and county governments on remuneration and other benefits. The composition of this commission is to include representatives of all constitutional commissions, the Senate and the county governments, along with the Principal Secretary for Finance and a representative of the Department of Public Service.

In the past, wages in the public sector varied according to the political influence of the chairs and chief executives of government organizations. They were also often out of sync with the prevailing economic situation. For the first time, Kenya's Constitution requires the public sector to maintain a sustainable wage bill, attract and retain skills, and promote productivity and performance. These provisions are expected to minimize disharmony in the public sector and encourage orderly wage and benefit negotiations. They are also expected to ensure the public sector reviews its wages and benefits regularly to be consistent with current economic realities. Despite its attractiveness, however, and given the variety of organizations anticipated, the SRC will have a hard job laying the ground rules, especially since the current classification, pay and benefit schemes have no rational basis.

8.2 The Central Bank of Kenya and its functions

The Central Bank of Kenya (CBK) has been upgraded to a constitutional institution. The change is consistent with best practices in other countries, but the provisions deal only with monetary policy. Other central bank functions, such as that of regulator of the financial sector, are not specified, allowing for the possibility of creating a separate financial services regulator. The CBK's current role as the government banker is also not specifically mentioned. As can be appreciated, the CBK is a key player in matters of public finance, a situation that is bound to continue, particularly with regard to mobilization of domestic debt.

Upgrading the CBK to a constitutional entity will help address the potential for abuse of this important institution. In the past, the CBK was misused to divert public resources for personal gain as was so starkly demonstrated by the Goldenberg scandal. In addition, the appointment and removal of CBK governors has been based mainly on political considerations, leaving the governor vulnerable to political pressures. That the appointment of such a high profile position was the purview of a single individual made it difficult for governors to remain politically neutral in the management of the CBK.

To address the missing links on CBK's functions, it will be necessary for a new law to be enacted providing more elaborately for the CBK's monetary and fiscal responsibilities. In particular, it should provide for government access to overdraft facilities at the CBK. More fundamentally, the autonomy granted by the new Constitution gives the Bank more leeway when dealing with the Secretary for Finance, whose role has been significantly reduced.

8.3 Changes to existing laws

Kenya's 2010 Constitution introduces such significant changes that most, if not all, current public finance systems will need to be completely revamped. As demonstrated above, public finance under the old law was centred on the Treasury – under the direction of

the executive – as the key player in the management and control of public funds. New legislation needs to be enacted sooner rather than later to allocate and demarcate operational functions among the affected institutions – whether new or old. In particular, the new laws should focus on the operations of the Commission on Revenue Allocation, the Salaries and Remuneration Commission, and the Controller of Budget. More specifically, the laws should spell out the role of the Treasury and its links with the newly established public finance institutions.

Many other existing laws will need to be amended or repealed as well, and new ones enacted. Among them are:

- The Fiscal Management Act 2009
- The Central Bank Act 1984
- Public Audit Act, 2003
- Internal Loans Act 1979
- External Loans and Credit Act 1979
- Constituencies Development Fund Act 2003
- Local Government Act 1998
- Local Government Loans Act 1984
- Local Authorities Transfer Fund Act 1988
- Public Procurement and Disposal Act 2005
- Government Financial Management Act 2004

9.0 Conclusion

Clearly, the promulgation of the new Constitution marked the beginning of a long and difficult process of redesigning the legal and institutional infrastructure consistent with the new dispensation. Combined with new laws and regulations, the Constitution will enhance the integrity, certainty and predictability of public financial management and strengthen the links between the national budget and government policies. This will be achieved through laws that set out rules for the various phases and players in the budget processes (both national and county), specifying the roles and responsibilities of both state and non-state actors involved in each phase of the

budget process. These rules should have sufficient authority to ensure compliance with the principles laid out in the Constitution. The necessary budget laws should also cover such important aspects as macroeconomic stability and transparency, and they should allow for the reform of the budget processes based on a continuous process of learning about what works. Alternatively, one comprehensive law could be enacted to cover the budget process all the way from policy formulation and budget preparation to approval and oversight.

In fact, given the structure and content of the new constitutional order, all current public finance laws and regulations need to be overhauled, but this should be preceded by legislation on the role of the Treasury and that of relevant committee in Parliament. The new Constitution presents an ideal opportunity for reviewing many of these laws, many of which have not been changed since independence. Among these are some of the most misused acts, such as the Local Government Act, which was applied politically to dissolve councils and appoint 'politically correct' commissions. There is an urgent need to build new institutional and administrative structures to manage public finances without necessarily being driven by the Treasury as was the case before.

Other key issues requiring attention include:

1. Clearly delineating the structure of the central government together with its roles and functions and how these will affect revenue mobilization as well as allocation of both the revenue base and the revenues collected centrally. Steps are needed to:
 - a. Enact appropriate laws to provide for the delegation of functions assigned to central government departments and its agencies, as well as to the counties on the basis of their capacity to handle added responsibilities. Such provisions should provide avenues for collaboration in an effort to minimize competition, duplication and the costs to the public of the two levels of government.
 - b. Build in performance as the basis of

delegation, so that if a county fails to deliver, the responsibility falls back to the principal agency.

2. Formalizing structures and institutions of fiscal decentralization, between national government and counties, and between counties and lower levels, so as to:
 - a. Address the particular concern for the need to provide a legal framework for dealing with counties and lower levels that fail, whether because of lack of capacity or other reasons.
 - b. Make adequate provisions to ensure that transfers do not discourage efforts by counties and lower levels from maximizing their own revenue mobilization.
3. Designing new oversight arrangements and sharing of responsibilities between Parliament and the Senate, on the one hand, and between these two and the county legislatures, on the other.

In the meantime, Kenya should be busy identifying best practices and success cases of a devolved system and learn from them, especially those in the developing world. It would be a mistake to start reinventing the wheel when dealing with such a complex matter when there are examples that have already got it right elsewhere. Although Kenya does not need to carbon copy other country systems, there is no time to experiment.

10.0 References

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11.0 Annex A

Comparison between “Old” and “New” Constitutional Provisions

Old	New
<p>1. Article 48: Money bills proposed only by the executive, upon recommendation of the President, including:</p> <ul style="list-style-type: none"> • Imposition or alteration of taxation, other than by reduction • Imposition of any charge on the Consolidated Fund or any other fund or its alteration other than by reduction • Payment or withdrawal of any money from any public fund • Contracting or remission of debt resulting from government priorities • Proceeding with a motion that touches on any of the above 	<p>1. Article 114: Money bills</p> <ul style="list-style-type: none"> • National Assembly may proceed on a money bill subject to: <ul style="list-style-type: none"> – Recommendations of a relevant House committee, – Taking into account views of Secretary of Finance • National Assembly may proceed on money bills except the Bill on Division and Allocation of Revenue under Article 218. This makes it possible for the legislature to originate money bills. “Money bill” means a bill dealing with: <ul style="list-style-type: none"> – Introduction of new taxes or increasing tax rates – Imposing charges on any public fund, variation or repeal – The appropriation, receipt, custody, investment or issue of any public money – The raising or guaranteeing of any loan or its repayment or matters incidental thereto <p>Clause (3) Article 114,</p> <ul style="list-style-type: none"> • “Taxes”, “public money” or “loan” do not include any of those raised by a county
<p>2. No principles or framework to guide public financial management existed in the old constitution. Public finance implemented using finance and appropriation laws, e.g., Government Finance and Management Act, Public Procurement and Disposal Act, financial regulations, and Treasury circulars, which had no legal basis</p>	<p>2. Article 201: Principles of public finance Provides for guiding principles and framework to guide public finance, which include:</p> <ul style="list-style-type: none"> • Openness, accountability and participation • Promote an equitable society, and ensure <ul style="list-style-type: none"> – Tax burden is shared fairly – Nationally raised revenues are shared equitably between national and county governments – Public expenditure promotes equitable development in the country; and provides for disadvantaged groups and marginalized areas <p>Article 202</p> <ul style="list-style-type: none"> • Calls for equitable sharing of debt burden between present and future generations • Articulates prudent and responsible use of public funds, and • Stipulates responsible management with clear reporting
<p>3. No provision for share of revenues raised nationally with sub-national governments</p>	<p>3. Article 202 : Equitable sharing of resources between national and county governments</p> <ul style="list-style-type: none"> • Revenues are to be shared equitably among national and county governments • County governments to get additional allocations from national government with or without conditions
<p>4. No criteria for sharing of revenues, however</p> <ul style="list-style-type: none"> • Priority given to national debt • No consideration for disadvantaged areas, or groups 	<p>4. Article 203: Equitable share and other financial laws Criteria for revenue sharing to take into account:</p> <ul style="list-style-type: none"> • National interest and provisions for national debt obligations • Needs of national government

Old	New
<ul style="list-style-type: none"> Fiscal capacity and efficiency not a measure 	<ul style="list-style-type: none"> Ensure county governments are able to deliver services Fiscal capacity and efficiency of county governments Ensure developmental needs of counties are met Ensure economic disparities within and between counties are remedied Ensure affirmative action for disadvantaged areas and groups Need to optimize economic potential and capacity of counties Ensure stable and predictable revenue allocations, Need for flexibility to respond to emergencies and similar other temporary needs A minimum of 15% to be allocated to counties based on the latest audited government revenue receipts
<p>5. No fund to address special needs of marginalized groups and areas</p>	<p>5. Article 204: Creation of Equalization Fund</p> <ul style="list-style-type: none"> Equalization Fund funded by "one-half per cent" of revenues collected nationally set aside each year based on most recent audited accounts of revenue receipts Money to provide basic services to marginalized communities, e.g., water, roads, health care and electricity Expenditure from Equalization Fund to be used according to the Appropriation Bill; can either be direct or indirect as conditional grants to counties with marginalized communities The Commission on Revenue Allocation (CRA) is to be consulted and its recommendations considered before Appropriation Bill passed in Parliament and money appropriated Balances of unspent money be retained in the Fund at fiscal year end Equalization Fund expires after 20 years if not extended by more than half the members of National Assembly. Life of fund may extend for a fixed period if Parliament enacts a legislation to extend it Withdrawals from the Fund must be approved by the Budget Controller
<p>6. Counties did not exist</p>	<p>6. Article 205: Consultation on financial resources affecting counties</p> <ul style="list-style-type: none"> Bills on revenue sharing and other financial matters to be allocated by the CRA that will make recommendations to both Houses (National Assembly and Senate) Each House to consider the CRA recommendations before voting on the Bill
<p>7. Article 99: Consolidated Fund All government revenues be paid into Consolidated Fund, from which:</p> <ul style="list-style-type: none"> No money shall be withdrawn unless authorized by the constitution or an act of Parliament or by vote on account under Article 101 	<p>7. Article 206: Public Funds All national government receipts paid into Consolidated Fund, with the exception of:</p> <ul style="list-style-type: none"> Money excluded by an act of Parliament for specific purpose, or authorized to be retained by state organs to defray expenses of the state organ Money withdrawn from Consolidated Fund only When authorized by an appropriation act, or an act of Parliament or

Old	New
<p>Parliament may authorize money to be paid into other funds established for specific purposes</p> <ul style="list-style-type: none"> • Such money be spent as authorized by law • Money charged to Consolidated Fund be paid to the persons authorized • Parliament prescribes the manner of withdrawals from Consolidated Fund and other funds <p>Article 101 applies to withdrawals based on Vote on Account, being total of 50% of the net estimates for the year laid in Parliament to meet expenditure</p>	<ul style="list-style-type: none"> • Authorized by the National Assembly to be spent for the purpose of meeting expenditure in order to carry on services of the National Government as prescribed in Article 222 <ul style="list-style-type: none"> – Money withdrawn shall not exceed one-half of amount included in estimates of expenditure for the year laid in the National Assembly – Money may not be withdrawn from the Consolidated Fund unless authorized by the Budget Controller
<p>8. Revenue Fund for each county did not exist</p>	<p>8. Article 207: County revenues Revenue Fund established for each county into which:</p> <ul style="list-style-type: none"> • All moneys received or raised on behalf of each county shall be paid into unless excluded by an act • Money shall be withdrawn from that fund only as a charge against the Fund, or as provided by Parliament, or county legislature <ul style="list-style-type: none"> – Withdrawals from the Fund to be authorized by Controller of Budget – Legislation may make provision for withdrawal from a Revenue Fund or establish other funds
<p>9. Article 102 Established the Contingencies Fund</p> <ul style="list-style-type: none"> • Fund was under the control of Finance Minister • Minister authorized advances from the Fund • Advances made from the Fund during the year presented to Parliament in a Supplementary Appropriation Bill to replace the amount so advanced 	<p>9. Article 208: Contingencies Fund</p> <ul style="list-style-type: none"> • To be established by an act of Parliament • Provides for advances from the Fund if Secretary of Finance is convinced there is an emergency to be funded for which no other provision or authority exists
<p>10. Article 48: Revenue raising powers and public debt</p> <ul style="list-style-type: none"> • Revenue raising powers were the prerogative of the Executive • Public debt had its own Article 103 	<p>10. Article 209: Revenue raising powers and public debt Article shares responsibility as follows:</p> <ul style="list-style-type: none"> • National government to impose: <ul style="list-style-type: none"> – Income tax – Value added tax – Customs tariff (import as well as export duties) – Excise taxes • Counties to impose: <ul style="list-style-type: none"> – Property rates – Entertainment taxes – Any other tax authorized by law > National government prohibited from levying any taxes on areas set aside for counties > Counties not to impose any taxes that prejudice national economic policies or activities or hinder movement of goods and services, or labour or capital

Old	New
11. Waivers, Exemptions, Variations <ul style="list-style-type: none"> Not provided in constitution. Provided under specific tax legislations (income tax, VAT, Customs & Excise Acts) 	11. Article 210: Waivers, Exemptions, Variations <ul style="list-style-type: none"> No exemptions for public office holder Taxes imposed, waived, exempted or varied as provided by law Record of each waiver and reasons to be maintained Each waiver reported to Auditor General
12. Article 103 National Debt/Borrowing <ul style="list-style-type: none"> Debt and other charges were provided under sub-section 2 of Article 103 	12. Article 211: National Debt/Borrowing Parliament to enact law on: <ul style="list-style-type: none"> National government borrowing, including terms and reporting Secretary of Finance to report to either House of Parliament within seven days if so requested by resolution and relevant committee and to include details on: <ul style="list-style-type: none"> Extent of total indebtedness; principal and interest How debt resources used or will be used Debt servicing (or repayment schedule) Progress so far in repayments of the debt
13. No provision for county guarantees in the constitution <ul style="list-style-type: none"> Borrowing by sub-national governments not in the constitution 	13. Article 212: Borrowing by counties County governments to borrow only if: <ul style="list-style-type: none"> Guaranteed by national government Approved by the county assembly
14. Guarantees by national government <ul style="list-style-type: none"> Guarantees by national government were not embodied in the constitution but in legislation 	14. Article 213: Guarantees by national government <ul style="list-style-type: none"> Parliament to enact a law and prescribe how national government may guarantee loans Within two months of fiscal year end, national government to publish a report on all guarantees issued during past year
15. Article 103 Public Debt <ul style="list-style-type: none"> Provides for all public debt charges and other Expenditure connected with raising of loans to be met directly from the Consolidated Fund 	15. Article 214: Public Debt Constitution authorizes public debt to be charged to Consolidated Fund, however: <ul style="list-style-type: none"> Parliament may make provision for all debt or part thereof to be charged to other public funds Public debt constitutes all financial obligations attendant to loans raised or guaranteed, or securities issued or guaranteed
16. Commission for Revenue Allocation (CRA) did not exist nor did the functions	16. Article 215: Commission for Revenue Allocation (CRA) Provides for establishment of a CRA composed of <ul style="list-style-type: none"> Chair nominated by President and Approved by the National Assembly Two persons nominated by political parties represented in National Assembly on a proportionate basis Five persons nominated by political parties in Senate on a proportionate basis The Principal Secretary, Finance <ul style="list-style-type: none"> These persons may not be sitting members of the legislature and must have extensive knowledge of finance and economics Important to note is that composition of membership may pose some risks and politicize revenue sharing Functions of CRA are provided in Article 216

Old	New
<p>17. Division of Revenue</p> <ul style="list-style-type: none"> No revenue sharing formula Only LATF and CDF existed by acts of Parliament ; and funds deposited in a dedicated account in Central Bank or other designated bank and paid directly to each local authority account or CDF account in a designated bank based on annual budget allocations 	<p>17. Article 217: Division of revenue between counties</p> <ul style="list-style-type: none"> To be reviewed by Senate every five years through a resolution to determine basis for allocation using: <ul style="list-style-type: none"> The criteria in Article 203 (1) The recommendations of a Revenue Sharing Commission Outcome of consultations with county governors, organizations within county and Cabinet Secretary for Finance, and Submissions by stakeholders and professionals Within ten days of Senate resolution, the Speaker (Senate) to refer it to Speaker of the National Assembly. <ul style="list-style-type: none"> If National Assembly does not vote on resolution within 60 days, resolution to be considered approved without amendment Resolution approved if two-thirds of the members of Parliament support it; rejected if two-thirds of members vote against it. Within 60 days, the National Assembly may consider the resolution and vote to approve it with or without amendments or reject it National Assembly may: <ul style="list-style-type: none"> Refer the matter to a Joint Committee of both Houses; if approved the resolution is binding.
<p>18. No provisions existed for division and allocation of revenues</p>	<p>18. Article 218: Annual division and allocation of revenues (between counties and the national government)</p> <ul style="list-style-type: none"> Two months before end of financial year, Division of Revenue Bill introduced in the National Assembly to <ul style="list-style-type: none"> Divide revenue raised among national and county governments County allocation revenue bill to divide among county levels of government in accordance with Article 217 Bills required by clause (1) to be accompanied by: <ul style="list-style-type: none"> Memorandum explaining revenue allocation proposed in the bill An evaluation of the bill using criteria in Article 203(1) Summary of deviations, if any, from the recommendations of the CRA, with an explanation for each deviation Article 219 requires transfer of county's share of revenues without undue delay or deduction unless transfer is stopped on account of material breach by a county under Article 225
<p>19. Article 100: Authorization of expenditure from consolidated fund and by appropriation</p> <ul style="list-style-type: none"> Finance Minister tabled details of expenditure in Parliament <ul style="list-style-type: none"> Proposals made under separate votes with details of recurrent and development votes Details and purpose of expenditure 	<p>19. Article 220: Budgets and Spending</p> <ul style="list-style-type: none"> Requires that budgets shall contain: <ul style="list-style-type: none"> Estimates of revenue and expenditure in two categories, recurrent and development Proposals of how budget deficit will be financed Details of net increase of government debt National legislation to prescribe: <ul style="list-style-type: none"> The structure of county budgets, and their development plans When the budgets and plans shall be laid in county assemblies

Old	New
<ul style="list-style-type: none"> Minister also tabled Supplementary Estimates (Article 100 (3)) to fund expenditure shortfalls and any emergencies funded through Civil Contingency Fund (Article 102) 	<ul style="list-style-type: none"> Details of consultation held between the two levels of government when preparing the plans and budgets
<p>20. Article 100 (1)</p> <ul style="list-style-type: none"> Old Standing Orders provided estimates of revenue and expenditure to be laid in the House before 20 June each year for expenditures of the following financial year Estimates of Parliamentary Service Commission and those of Chief Registrar, Judiciary were part of revenue and expenditure estimates 	<p>20. Article 221: Budget estimates and annual Appropriation bill</p> <p>Two months before end of each financial year the Secretary for Finance to submit to National Assembly estimates of revenue and expenditure of the national government for next financial year, to include expenditure from Equalization Fund in form and accordance with procedure prescribed by an Act of Parliament.</p> <ul style="list-style-type: none"> National Assembly to consider estimates together with estimates submitted by Parliamentary Service Commission and Chief Registrar of the Judiciary A committee of National Assembly to review and consider the estimates of revenue and expenditure before consideration by the National Assembly Committee to seek representation of public and make recommendation to National Assembly Once estimates of the Parliamentary Service Commission and the Judiciary are approved by the National Assembly, to be included in the Appropriation Bill for approval to authorize withdrawals of money from Consolidated and other funds
<p>21. Article 102</p> <ul style="list-style-type: none"> Vote on account taken before 26 June If approved government to access up to 50 per cent of money included in the estimates of revenue and expenditure laid in the House 	<p>21. Article 222: Expenditure before the budget is passed</p> <p>National Assembly to authorize withdrawal of one-half of the net amount included in the estimates of expenditure for that year to carry on services of national government until such time the Appropriation Act is assented to</p>
<p>22. Article 100 (3)</p> <ul style="list-style-type: none"> Provided for supplementary estimates or statement of excess to appropriate additional sums to meet shortfalls or excesses or make good money withdrawn from the Contingencies Fund 	<p>22. Article 223: Supplementary appropriation</p> <ul style="list-style-type: none"> Provides for supplementary appropriation to meet needs of national government that arise because of shortfalls in expenditure and for which no provision exists or money is withdrawn from the Contingencies Fund Approval to be sought within the first two months after the first withdrawal If Parliament is not sitting or adjourns before approval within two weeks after it next sits An Appropriation Bill must be approved for the money to be spent Supplementary estimates not to exceed 10 per cent of the budget in any financial year, unless in special circumstances Parliament approves a higher percentage
<p>23. County budgets did not exist, nor division of revenue</p>	<p>23. Article 224: County appropriation bills</p> <p>Based on Division of Revenue Bill, approved by Parliament under Article 218, each county to prepare and adopt its own annual budget and appropriation in the form and according to procedure prescribed</p>

Old	New
<p>24. Functions and responsibilities of national Treasury were not provided in the constitution</p>	<p>24. Article 225: Financial control</p> <ul style="list-style-type: none"> • Legislation to provide for establishment, functions and responsibilities of the national Treasury • Parliament to enact law on transparency and expenditure control in all governments, including mechanism for their implementation • Secretary of Finance to stop the transfer of funds to a county or other public entity: <ul style="list-style-type: none"> – For serious or persistent material breach of measures introduced by legislation for not more than 60 days – Not more than 50 per cent of funds due to a county government (stopped) • Lapses retrospectively within 30 days if Parliament doesn't approve it by a resolution of both Houses • Parliament may renew decision to stop transfer but not for more than 60 days at a time <ul style="list-style-type: none"> > Parliament may not approve/renew decision to transfer funds unless: <ul style="list-style-type: none"> – COB submits a report on the issue to Parliament; and or – The affected entity is given an opportunity to present and defend its case before the relevant Committee
<p>25. Article 105 (C) Provided for the audit and report on all accounts of the central and local govt, all courts, commissions and the Clerk to the National Assembly each year.</p>	<p>25. Article 226: Accounts and audit of public entities</p> <ul style="list-style-type: none"> • Legislation to provide for keeping of financial records and auditing of accounts of all government and public entities • Prescribe other measures for efficient, transparent fiscal management • Designate an accounting officer for each entity • Accounting officer of a national public entity accountable to national assembly and county public entity to county assembly • Accounts of the Auditor General be audited and reported on by a professional accountant appointed by National Assembly • Holder of public or political office to be held liable for loss or • Use of public funds contrary to law or instructions and shall make good the loss whether still in office or not
<p>26. Procurement of goods and services was not provided in the constitution</p>	<p>26. Article 227: Procurement of public goods and services</p> <ul style="list-style-type: none"> • Provides for public entity to procure goods and services using a system that is fair, equitable, transparent, competitive and cost-effective • Legislation to prescribe the framework for policies for procurement and asset disposals, and in particular, how to deal with: <ul style="list-style-type: none"> – Categories of preference in allocation of contracts – How to protect disadvantage persons, groups from unfair competition or discrimination – Ensure sanctions for non-performance or poor quality and unprofessional work are in place – Ensure penalties for tax defaulters, corrupt contractors or persons or those who violate employment laws

Old	New
<p>27. Article 105 (1)</p> <ul style="list-style-type: none"> • Controller's duties were performed by Controller and Auditor General • Approved withdrawals from the Consolidated Fund 	<p>27. Article 228: Controller of Budget (COB)</p> <p>Provides for a COB nominated by President and approved by National Assembly, who</p> <ul style="list-style-type: none"> • Must be qualified and posses extensive knowledge of public finance and at least ten years experience • In line with provisions of Article 251, holds office for eight years and is not eligible for re-appointment • Authorizes withdrawals from Public Funds for national and county governments under Articles 204, 206 and 207 • Oversees budget implementation • Must be satisfied withdrawal is in accordance with the law, and to submit to each House a report every four months on implementation of budgets of national and county governments
<p>28. Article 105 (1)</p> <ul style="list-style-type: none"> • Appointed by the President • No specific qualifications or tenure of office was specified • Audited all accounts of government, all commissions, courts and clerk of National Assembly • Once every year carry out audit and report on the accounts of call public entities in Kenya • Submit his report to the National Assembly through Minister for Finance. • Not subject to direction or control of any other person or authority. • Provision was silent on who to audit his accounts 	<p>28. Article 229: Auditor General</p> <ul style="list-style-type: none"> • Nominated by President, approved by National Assembly and appointed by President • Must have extensive knowledge in public finance, or ten years experience in auditing and public finance management • Shall hold office for eight years and not eligible for re-appointment, subject to provisions of Article 251 • Within six months after end of financial year, audit and report on the accounts of: <ul style="list-style-type: none"> – National and county government – All funds and authorities of the national and county governments – All courts – Every commission and independent office – The National Assembly, Senate and county assemblies – Political parties – Public debt, and – Any other entity that is funded from public funds and requires Auditor General to audit • Every audit must confirm public funds have been spent lawfully and effectively • The reports to be submitted to Parliament or the relevant county assembly • Upon receipt of audit report Parliament or the county assembly to consider the report within three months, debate and take appropriate action
<p>29. Salaries and Remuneration Commission did not exist</p>	<p>29. Article 230: Establishment of Salaries and Remuneration Commission</p> <p>Established and appointed by the President to set and review the remuneration and benefits of all state officers and also to</p> <ul style="list-style-type: none"> • Give advice to national and county governments on remuneration of all other public officers • Ensure total public wage bill is fiscally sustainable • Ensure public service attracts and retains qualified personnel with skills • Promote productivity and performance and ensure transparency and fairness

Old	New
30. Central Bank <ul style="list-style-type: none">• Not provided for	30. Article 231: Central Bank of Kenya <p>Established to be responsible for:</p> <ul style="list-style-type: none">• Formulating monetary policy, promoting price stability, issuing currency• Not subject to any direction or control of any person or authority in the exercise of its powers or performance of its functions• Legislation to provide its composition, powers, functions and mode of operation

Annex B

Phases of Kenya's Budget Process

Figure B1: Key phases of the budget process under the old constitution

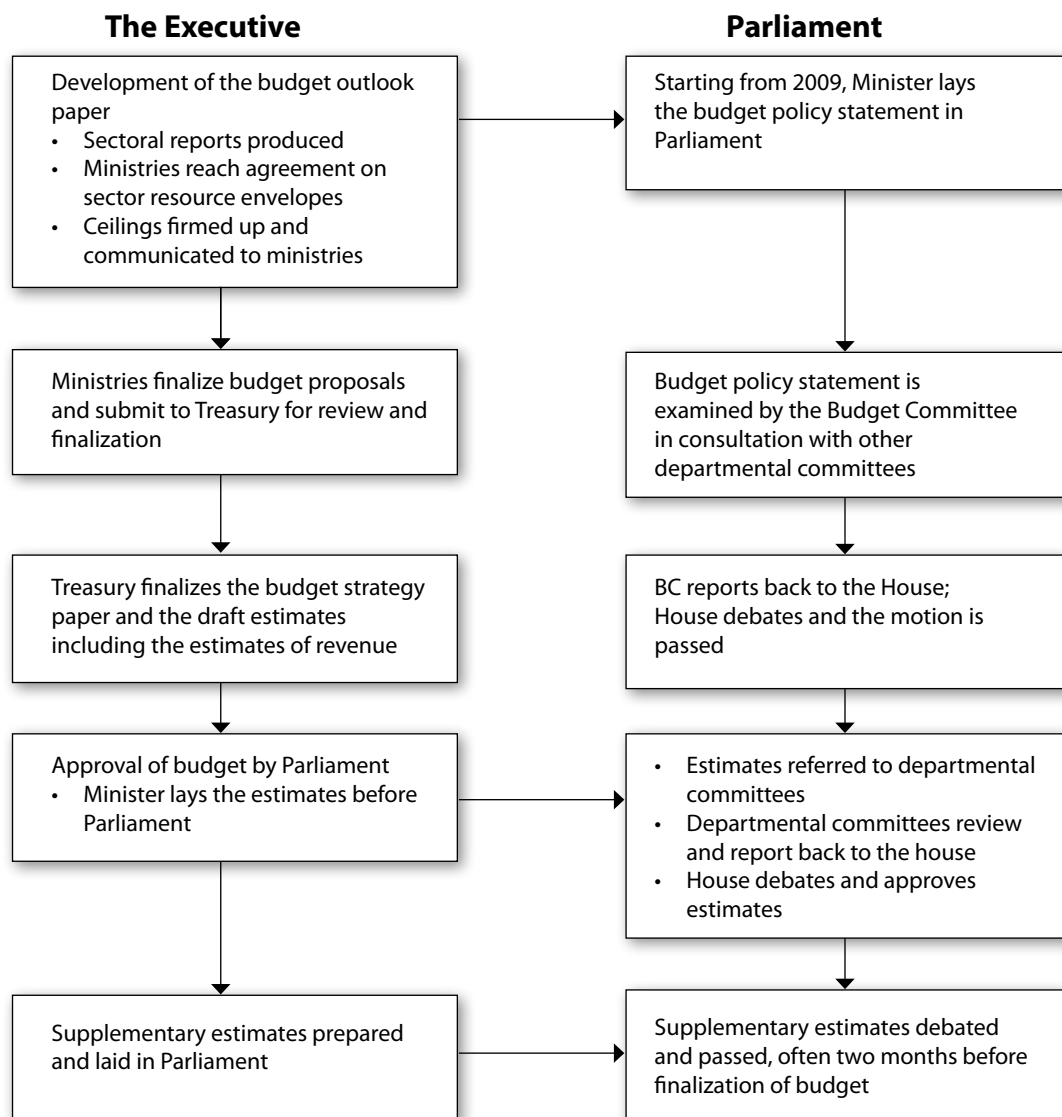
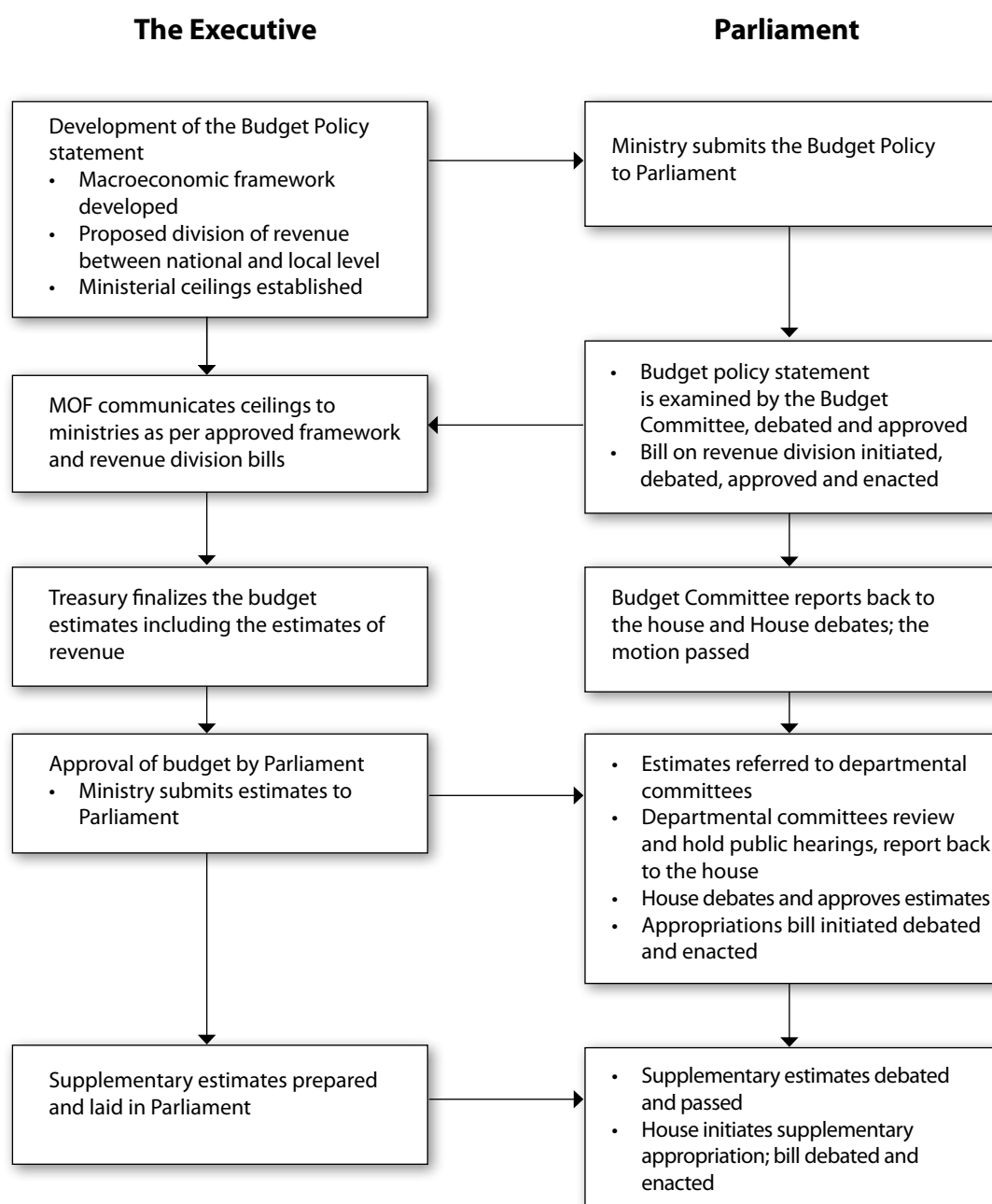


Figure B2: Key phases of the budget process under the new Constitution

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Published by:
Society for International Development (SID)
Regional Office for East & Southern Africa
Britak Centre, First Floor Ragati/Mara Road
P.O. Box 2404-00100 Nairobi, Kenya
Tel. +254 20 273 7991
Fax + 254 20 273 7992
www.sidint.net

ISBN No: 978-9966-029-04-1