



Institute of Economic
Affairs—Kenya

Budget 2005/2006

A Guide for MPs

June 2005

On Wednesday June 8th 2005, the Minister for Finance presented a much awaited for budget speech to the House. The budget reading was brought forward from the original date of June 16th, to comply with the East African Community guidelines. In addition to the budget speech, the Minister tabled the Finance Bill 2005, the Government's Financial Statement for 2005, the Retirement Benefits (Amendments) Bill, 2005, the Estimates of Revenue for the financial year beginning in July 2005 and the Budget Strategy Paper. For his third budget speech, the Minister for Finance chose the theme, "*Reorienting Expenditure to Achieve Rapid Economic Growth and Poverty*

BUDGET 2005/06: GOOD BUT OPAQUE

BACKGROUND

Macroeconomic Framework

12-month overall inflation rate: 16 % (April 2005, Central Bank of Kenya)

Exchange rate: Kshs 76.1 to US \$1 (April 2005, Central Bank of Kenya)

Total unemployment rate: In rural areas, 9.4% and in urban areas, 25.1% (1998/99 Labour Force Survey Report). In 2004, 92% of the 474,000 jobs created were generated by the informal sector.

Investment levels: 13.4% of Gross Domestic Product (2004, Central Bank of Kenya)

Savings: 9.8% of Gross Domestic Product (2004, Central Bank of Kenya)

Fuel prices: Kshs. 72 per litre of Regular or Super and Kshs. 62 per litre of Diesel as of June 2005.

Growth rate: 4.3% in 2004 (Economic Survey 2005)

Despite an impressive growth rate of 4.3%, poverty levels increased and the inequality gap widened. Given this paradox, the Minister for Finance (hereafter referred to as the Minister) will need to explain how the Executive arrived at this figure to Parliament. If the Minister can provide a compelling argument, waning public confidence in official data and statistics is likely to be restored.

The Theme

Against this backdrop, the Minister for Finance chose to **reorient expenditure to achieve rapid economic growth and poverty reduction**. This theme suggests that the executive arm of government intends to alter the expenditure patterns to ensure shared growth and reduced poverty prevalence in the country. The gap between the present growth rate and poverty levels confirms that tackling poverty requires more systematic and deliberate efforts. Furthermore, in light of corruption allegations that emerged last year, the Minister needs to stay true to his promise of greater responsibility in the management of public resources as an indicator of better governance and enforcement of the rule of law.

Tax Collector, Borrower and Spender

If the Minister's theme is to be taken to its conclusion, then the containment of public expenditure is imperative. However, it is noteworthy that the public expenditures for this year have reached a record of Kshs. 508 billion surpassing last fiscal year's



- **BUDGET DOCUMENTS**
- Budget Speech
- Economic Recovery Strategy for Wealth and Employment Creation.
- Financial Statement. Expected movements in the Exchequer Account for the current financial year, forecast for the coming year and a summary of the revenue proposals in the Finance Bill.
- Estimates of Revenue. Detailed breakdown of revenue collections.
- Finance Bill 2005. Provisional Collection of Taxes and Duties Act: Legislation to provide for the collection of taxes until Finance bill is passed
- Retirement Benefits—Amendment Bill 2005. This contains amendments that allow provision to increase tax deductible on pension schemes.
- Estimates of Recurrent Expenditure. Proposed recurrent expenditure by Vote and Consolidated Fund Services.
- Estimates of Development Expenditure. Proposed development expenditure and detailed listing of external (donor) funding.

Budget Strategy Paper which determined indicative overall resource envelop

record mark of Kshs. 431 billion. It appears that having expanded the expenditures by Kshs. 45 billion during the last financial year, the Minister envisages a further expansion of Kshs. 71 billion in the next financial year. With the exception of the partially disputed growth rate of 4.3% and record tax collections from the Kenya Revenue Authority (KRA), the Minister has little positive news in terms of reductions in the poverty levels or overall welfare gains for Kenyan citizens.

In all, this implies that the Minister will have overseen an expansion in expenditure of Kshs. 116 billion within two financial years. This does not appear to be cautious and prudent management of the public purse. Hence Parliament ought to caution the Minister for his tendency of rapidly expanding public expenditures. Such increases in expenditure should only be conditional on the dedication of funds to investments. However with recurrent expenditures taking up 79.5% of the total expenditure, this is not the case. The parliamentary committee on Finance, Trade and Planning and Parliament in general must ask the Minister to make a statement in which a firm commitment to the containment of expenditures, and in particular recurrent expenditure, is made.

Related to the matter of rapidly expanding expenditures is the fact that the Minister has had to resort to substantial borrowing to supplement resources from taxes. During the Budget Speech, the Minister informed Parliament that he will seek authority to borrow Kshs. 25.3 billion from domestic sources to meet the expenditures that have been proposed. This proposed level of borrowing from domestic sources represents a significant increase in the domestic borrowing. The financial statement presented together with the Budget Speech shows borrowing from domestic sources for last year amounted to Kshs. 18 billion. In essence, the Minister is alerting Parliament of the intention to expand the amount of borrowing for the next financial year by 40.5%. Though the Minister's theme suggests that he intended to reorient expenditure, this analysis reveals that he made no difficult choices that required substantial cuts in expenditure and went for the soft option of expanding the domestic debt. Under no single vote head has the Minister proposed cuts and reductions of more than 5% of the expenditure. This also contravenes his earlier promise to cut ministerial spending as in actual fact, the estimates reveals that the

only ministry which saw a cut was the Ministry of Livestock Development and Fisheries.

Total revenue collection for the financial year 2004-2005 was Kshs. 396.6 billion and this reflects good performance. Of this sum, the total ordinary revenue amounted to Kshs. 270.9 billion. Most of this was because of improved tax collection by the KRA on account of efficiency and the tax amnesty. Through the tax amnesty that Minister allowed last year, the KRA collected an additional Kshs. 4.8 billion. Having admitted that the one-time amnesty was successful, the Minister ought to have followed up on this success by marking specific funds for tax audits to be carried out by the KRA. Such specific provisions for systematic tax audits should become a constant feature of the allocations to the KRA in order to respond to the individuals who failed to respond to the tax amnesty. The parliamentary committee on Finance, Trade and Planning should insist on the inclusion of specific tax audit funds to sustain the gains from the amnesty.

LEGISLATIVE CALENDAR

Last fiscal year the budget proposed the following legislative developments. To date they have not been passed:

1. Micro Finance Bill
2. Procurement Bill
3. Privatisation Bill
4. NPS and Electronic Transfers Bills
5. Bills of Exchange Act
6. Capital Markets Authority Act (amendment)
7. Insurance Act (amendment)
8. Proceeds of Crime and Anti Money Laundering (Prevention) Bill

This year, the budget speech proposed the following legislation (it is worth noting that 3 bills have been carried over from the last budget speech):

1. Micro Finance Bill – to be tabled
2. Procurement Bill – stuck in Parliament
3. Privatisation Bill – stuck in Parliament
4. SACCOs Bill – to be completed and then tabled
5. Public Officers Ethics Act – to be amended
6. Coffee Act – to be amended
7. Pyrethrum Act – to be amended

8. Retirement Benefits Act – to be amended
9. Higher Education Loans Board Act – to be amended
10. Value Added Tax Act – to be amended
11. Housing Bill- to be introduced after National Housing Policy is completed.

SPENDING PATTERNS

Unlike the past system where particular budget lines were specified, the new system of printed estimates is devoid of details of where and how the money is being spent. This gives rise to a number of shortcomings:

1. Tracking of expenditure can only be implicitly inferred from budget lines such as ‘research, feasibility studies, project preparation and design’ within the development expenditures. This leaves wide scope for financial impropriety and mismanagement.
2. Under the recurrent expenditure, the new system of lumping together allocations to a single heading such as ‘communication supplies and services’ and ‘fuel oil and lubricants,’ makes it difficult to isolate particular budget lines. As such some essential services could easily suffer from insufficient funding.
3. It becomes easier for ministries to go beyond their budget lines under one single heading item as opposed to when budget lines are clearly outlined.
4. There is a risk that pending bills will be sneaked into the estimates. Currently, it is estimated that Kshs 6.3 billion is tied to utilities for recurrent expenditure and Kshs 11.7 billion for development expenditure (Public Expenditure Review, 2004).
5. Parliament should not allow future estimates to be presented in ways that appear to be calculated to obscure important details. Additionally, equally more noticeable and important are the following shortcomings:
 6. It should concern parliament that the Government is absorbing over Kshs. 4 billion in Kenya Railways pensions and retirement benefits. The government should be put to task to explain how the liability arose and why the government should absorb the cost.
 7. The Minister proposed to spend Kshs. 0.2 billion in petroleum exploration. Given that the bulk of

the exploration work is done by foreign firms, Parliament should seek an explanation as to where the money will be spent.

8. The Minister committed to support the expansion of the railway line into Ethiopia and Sudan to open up those markets for local firms. However, he did not back his promise with budgetary allocation and therefore it is not clear how he intends to achieve that objective.
9. Notably, a great proportion (over 50%) of Printed Estimates of Development Expenditure for the fiscal year 2005/6 comprise of expenses that are recurrent, such as, refurbishment of buildings, maintenance of vehicles, etc. In essence therefore the government analysis does not give a true picture of the split between development and recurrent expenditures. Actual development expenditures are actually far much lower than reflected in the budget documents.

Skewed Distribution of Development Budget

The printed estimates demonstrate that past resources have not been distributed equitably to all the districts. The budget allocations do not reflect the level of development or poverty prevalence or access to essential services in the respective districts. A closer scrutiny of the Printed Estimates of Public Expenditure over the years reveal that some districts with favourable economic indicators received a huge development budget as opposed to other districts with relatively higher poverty prevalence levels. The government should ensure that resources are equitably distributed based on the social and economic indicators. Lately, there has been a proliferation of district/constituency development funds and programmes such as the Constituency Development Fund, Constituency & Districts Roads Development Fund, Constituency Aids Fund, Local Authority Development Funds (LATF) and the Rural Electrification Programme (REP).

From budget estimates, it is difficult to tell what amount has been allocated to each of the districts as it is lumped under one heading. Parliament may wish to insist that other ministerial funds earmarked for specific programmes and projects in the districts be distributed on the basis of need as with the CDFs.

The budget outturn is shown in the table below.

Budget Outturn 2005/06 in Kshs. In Millions				
	Revised Estimates 2004/5	Printed Estimates 2005/06	Actual Change	% Change
TOTAL	295,045	326,031	30,986	10.5%
Ordinary Revenue	267,453	296,096	28,643	10.7%
Custom & Excise	72,811	81,289	8,478	11.6%
Income Tax	95,667	109,820	14,153	14.8%
VAT	72,291	78,603	6,312	8.7%
Others Taxes	26,684	26,384	-300	-1.1%
Recurrent AIA	25,855	27,069	1,214	4.7%
Development AIA	1,737	2,866	1,129	65.0%
TOTAL EXPENDITURE	431,059	508,512	77,453	18.0%
1. Consolidated Fund Services	131,995	147,269	15,274	11.6%
Domestic Debt-Interest	28,077	26,890	-1,187	-4.2%
External Debt-Interest	5,328	9,012	3,684	69.1%
Domestic Debt-Redemption	60,747	64,318	3,571	5.9%
External Debt-Redemption	18,076	23,678	5,602	31.0%
Pension & Gratuities	17,821	17,199	-622	-3.5%
Electoral Commission of Kenya	102	3,107	3,005	2,946.1%
Const. of Kenya Review Comm.	400	1,461	1,061	265.3%
Others	1,444	1,604	160	11.1%
Recurrent	227,082	257,023	29,941	13.2%
Development	71,982	104,220	32,238	44.8%
DEFICIT BEFORE GRANTS	(136,014)	(182,481)	-46,467	34.2%
Grants	20,869	27,866	6,997	33.5%
DEFICIT AFTER GRANTS	-115,145	-154,615	-39,470	34.3%
FINANCING	115,145	154,615	39,470	34.3%
Project Loans	14,160	28,976	14,816	104.6%
Programme Loans	0	9,563	9,563	
Privatization Proceeds	0	8,000	8,000	
Debt Rescheduling	9,726	8,513	-1,213	-12.5%
Refinancing Bank Restructure	0	5,000	5,000	
Securitisation of Domestic Arrears	10,092	4,868	-5,224	-51.8%
Domestic Debt Rollover	58,787	64,318	5,531	9.4%
Domestic Borrowing Requirement	22,380	25,378	2,998	13.4%

Source: Financial Statement 2005

A closer scrutiny of the budget documents reveals **some discrepancies** in the figures reported in the Estimates of Revenue report. For example, the 2004/5 Revised Estimates of Ordinary Revenue report and the Financial Statement for the fiscal year 2005/6 had a variance of Kshs. 3.48 billion, while development expenditure reflected a variance of Kshs. 84 million. This therefore means that the levels of domestic debt could have been higher than Kshs. 18 billion as reported in the 2005/6 Financial Statement. Parliament should seek clarifications about these glaring discrepancies and ask the Minister to confirm the true position regarding the level of domestic borrowing during the financial year 2004/5.

The budget outturn also indicates that the **ordinary revenue** grew by 11.6% mainly due to KRA's efforts towards enforcing tax compliance and widening the tax base. However, given that the levels of investment have not peaked, the future scope to collect more taxes may be threatened.

Public Spending & Domestic Debt:

A review of the last two successive budgets indicate that the Minister has opted for the softer option of increasing public spending and financing the resultant deficit by raising domestic debt. Public expenditure grew by 29%, hitting the Kshs. 400 billion mark in 2004/5 and grew yet again by 18% in 2005/6 to hit the Ksh 500 billion mark. The IEA-Kenya estimates that domestic borrowing during the fiscal year 2004/5 will be Kshs. 22.380 billion. It is expected to grow by 13.4% to Kshs. 25.378 billion in 2005/6. It should concern Parliament that the appetite for public spending is being sustained by expanding domestic debt. The government must also go for the hard choices of rationalising government and minimising ongoing wastage through debt write offs and transfers to inefficient and sustainable Local Authorities and Public Enterprises.

Allocations to the Electoral Commission of Kenya and the Constitution of Kenya Review Commission also grew substantially in readiness for the finalisation of the National constitution review process. Parliament must support and advocate for the speedy conclusion of the review process to save on scarce public resources.

ANALYSIS OF SOME BUDGET SPEECH PROPOSALS

Public Enterprises

Public enterprises are significant avenues for waste of public resources and this is known to the Minister. Parliament should demand a statement stating a timeframe for the closure of non-essential and wasteful agencies. It is clear that the immense pressure on public funds will not be eased without the prompt closure of some of these institutions. Significant savings for public investments could also come from the closure of local authorities which not only fail to meet their obligations but are perpetually reliant on support from central government. In this regard, reducing the amount of monies given to institutions that perform well, will not resolve the problem. A better starting point for the Minister is to assess the public costs of maintaining poorly performing agencies.

Capital Transfers to Public Financial and Non-Financial Institutions and Enterprises

Parliament needs to seek details of the monies earmarked for capital transfers to public financial institutions and enterprises totalling to Kshs. 0.59 billion. The Minister should also give details and elaborate on the capital transfers to non-financial institutions amounting to Kshs 1.6 billion. What are these financial and non-financial institutions, how much money will go to each one and for what purpose?

Parliament should also enquire into the Kshs. 3 billion and 5 billion earmarked for other operating expenses and principal repayments on guaranteed debt taken over by the government respectively. Whereas principal repayments on guaranteed debt taken over by the government would be thought to be recurrent expenditures, the Minister has reflected them in the development budget. Most likely, this money will be used towards paying non performing loans belonging to public enterprises. Privatisation of state owned banks will only address the problem from the side of the financial institution. There is still a need to address the problem from the debtors' angle - and one such way would be to close down public enterprises that are unable to operate within their budget. In addition to pressing this point, Parliament need to insist that the Minister gives a timeframe within which the banks should be privatised so that this proposal becomes a reality.

The Wage Bill

The Minister allocated a total of Kshs. 7 billion for wage increments for teachers and other public sector workers. Of this sum, Kshs. 4.9 billion has been dedicated to fulfilling the promise to award teachers a salary rise. Whereas the Minister must be commended by Parliament for making these funds available for improving the pay of teachers and public sector workers, it is still essential for the House to take issue with his failure to commit the Executive to the containment of the rapidly increasing expenditures. Presently, the wage bill consumes up to 40% of total ordinary revenues. Added to the other non-discretionary expenditures such as debt service payments and pension obligations for civil servants, these together take up close to two thirds of the revenues available to government. Thus they leave little scope for wider public investment to generate desired growth and employment. This puts the nation in the position where the development of a national wage policy for the public sector is imperative. Not only would a policy provide the rationale for providing wage increments, but it would also provide guidelines for sustainable wage increments that translate into higher productivity.

Privatisation

When the Minister presented the Budget Speech last year, he mentioned that he expected to present a Privatisation Bill for debate in parliament. Subsequently, a bill was brought to the house but it did not pass as was expected. A similar undertaking has been made this year. The Minister will require the broad support of the legislature to pass this bill. However, Parliament should stress that the bill should be comprehensive and competently drawn in order to ensure its passage. Similar to last year, the Minister has factored in up to Kshs. 8 billion as the expected proceeds of the privatisation process. The implication of this is the confidence that the Privatisation Bill will be presented and passed in time. However, the House and the parliamentary committee on Finance, Trade and Planning should seek clarification from the Minister on the basis of this figure and the entities whose impending privatisation have informed this arbitrary valuation.

Energy

The Minister appreciated that reliable and cost-effective supply of energy to households and private sector firms

is imperative for increased productivity and export competitiveness. Noting that the national capacity for hydro-based power is exhausted, the Minister suggested that the national energy policy would be focused upon maintaining the development of geo-thermal power sources. However, given the poor state of the national grid and distribution system, the mere expansion of supply will not achieve the goal of regular and cost-effective power supply. Investment in the national grid is imperative and the Minister must provide the Kenya Power and Lighting Company (KPLC) Limited with sufficient funds to enable it to improve the national grid and ensure the reliability of supply. On the other hand, the Minister must be given credit for confirming that the executive branch of government has commenced preparations for the privatisation of the Kenya Electricity Generation Company (KenGen). However it is important to note that in the absence of a clear privatisation law and policy, the preparations are not sufficiently transparent to allow for public scrutiny and comment.

Housing

Owning a house in Kenya, particularly in Nairobi is expensive for many. For this reason, the mortgage relief of Kshs 150,000 granted by the Minister although a little low is highly welcomed. To address the larger problems concerning housing such as poor planning, inadequate amenities and low construction standards, Parliament needs to insist on the completion of a National Housing Policy that will provide guidelines on priority areas and quality requirements.

Judiciary

The Minister correctly noted that the key problems facing the judicial system are an outdated information system, the inadequate numbers of judicial officers and the poor state of courts. At present, access to information such as title deeds is slow and cumbersome as many of the records are stored manually. In some cases, information seekers therefore expect or are expected to give a bribe if they want to speed up the process. This means that potential revenues are lost somewhere along the way. Automating the court registry as proposed by the Minister is therefore critical and it needs to be listed as a separate budget item. Increasing the number of magistrates serving in both the criminal and commercial law courts is also important in order to clear the backlog of cases. Lastly, rehabilitating our courts is essential. At present, most

high courts house magistrate courts. However we also have courts in areas especially outside major towns that solely house magistrate courts. Parliament should move to have majority of the funds allocated towards rehabilitating the courts at the lower levels both in and outside Nairobi. The budget estimates allocate 77% of the funds for rehabilitation under the Judicial Department towards rehabilitation of the high courts. Parliament should clarify whether this means that the funds once received by the high courts, will then be disbursed to lower courts that are not housed in high courts.

Water

The Minister's proposal to sink 4 boreholes in each district within arid and semi-arid lands (ASALs) is very commendable. This will result in better food security, health and cut down on time spent—especially by women—accessing water. To implement this initiative, the Minister allocated Kshs 1.5 billion which is fair and reasonable. However, the estimates do not show where these boreholes will be sunk. Furthermore, measures to encourage water storage were not mentioned in the budget speech or reflected in the budget estimates. Parliament should seek clarification on these areas.

Police

The Minister mentioned three aspects as pertinent to improving police service; improved crime prevention, investigation and prosecution capacity, community policing and better welfare for officers. Unfortunately, other than the allocation of funds towards the purchase of Mazingira building which will house the CID forensics operations, allocations towards more communications equipment and computerisation is not clearly visible. In addition, for community policing to work, the government will need to allocate monies towards this initiative to reduce the financial burden on the communities and simultaneously launch a campaign that builds public trust in the police service.

Devolved funds such as Constituency Development Funds (CDFs) and Local Authority Transfer Funds (LATFs) for development work have strengths and weaknesses. A strong advantage is that they create an opportunity for citizen participation. Unfortunately this is undermined by a system that is in need of greater transparency in the prioritisation, approval and auditing of funds. Giving out Kshs. 5.6 billion to

LATF and Kshs. 7.2 billion to the CDF where funds are not managed well is cause for some concern to taxpayers.

Coffee

This year the Minister has proposed amendments to the Coffee Act that if (promptly) implemented, will benefit the coffee industry. Firstly, he mentions separating the non-regulatory functions of the Coffee Board of Kenya. This will strengthen the industry's institutional framework. The second proposed amendment is to allow the direct sale of coffee outside the auction house. This will liberalise the market and thereby increase the number of players (hopefully local) that engage in the industry. Lastly, the speech proposes to amend the Act to streamline the licensing procedures. This will remove some of the existing barriers to entry. In light of the benefits that will derive from amending the Coffee Act, Parliament needs to push for the bill to be tabled in the House.

Empowering Small & Micro Enterprises (SMEs)

The SME sector generated 92% of the 474,000 jobs created last year. This shows the significance of the sector in impacting economic growth in the nation. A fair number of women own and work in SMEs and this positively impacts on their ability to feed, clothe and house their families as more and more women now head homes as single parents. It is therefore imperative that the Sessional Paper of 2004 on "Development of Micro and Small Enterprises for Wealth and Employment Creation for Poverty Reduction" be passed and implemented as soon as possible. Some of the ways that the sector can benefit would be through the passing of the Micro Finance Bill, introducing vocational training to impart or upgrade skills, reducing licensing procedures required to open and run a business and increasing accessibility to infrastructure such as roads and clean water.

Education

The government has been hailed for its policy on Universal Primary Education which is of benefit to the student and society at large. The Minister has however correctly noted that girls, street children and children living in ASALs do not have equitable access to the free primary education. UNICEF estimates that 1.5 million children of school going age are not in school and this

(Continued on page 9)

WHERE DOES THE MINISTER WANT TO SPEND?:							
A SUMMARY OF THE ESTIMATES in Kshs. Millions							
Details of Vote	RECURRENT		DEVELOPMENT		TOTALS		% Share of Total
	Gross Approved Exp. 2004/5	Gross Estimates 2005/06	Gross Approved Exp. 2004/5	Gross Estimates 2005/06	Gross Approved Exp. 2004/5	Gross Estimates 2005/06	
Office of the President	27,695.79	27,817.94	5,474.92	7,609.08	33,170.71	35,427.02	6.97%
State House	602.09	863.05	250.00	250.00	852.09	1,113.05	.22%
Dir. Of Pers. Management	1,210.79	2,778.49	945.76	273.40	2,156.55	3,051.89	0.60%
Min. of Foreign Affairs & I C.	5,953.7	6,257.00	100.20	100.00	6,053.90	6,357.00	1.25%
OVP and Min. Home Affairs	6,944.05	7,257.57	922.67	1,491.50	7,866.72	8,749.09	1.72%
Min. of Planning & Nat. Dev.	836.57	835.11	1,301.32	2,098.40	2,137.89	2,933.52	0.58%
Min. of Finance	10,997.05	14,179.12	19,952.52	20,933.22	30,949.56	35,112.34	6.90%
Department of Defence	21,218.76	26,651.65	-	-	21,218.76	26,651.65	5.24%
Min Regional Development	630.53	535.46	202.03	609.05	832.55	1,144.52	0.23%
Min Agriculture	3,806.56	5,115.00	2,763.40	3,114.80	6,569.96	8,229.80	1.62%
Min. Health	17,515.86	20,209.67	4,458.01	9,943.17	21,973.87	30,152.84	5.93%
Ministry of Local Government	5,499.49	6,133.83	1,740.62	1,305.79	7,240.10	7,439.61	1.46%
Min of Roads & Public Works	10,344.03	10,937.50	9,127.89	17,750.95	19,471.92	28,688.45	5.64%
Min. of Transport	3,047.93	3,266.35	1,603.96	7,833.13	4,651.89	11,099.48	2.18%
Min. of Labour & HRD	849.67	871.29	123.86	194.00	973.52	1,065.29	0.21%
Min. of Trade & Industry	2,104.60	1,678.14	459.21	825.81	2,563.81	2,503.95	0.49%
Min. of Justice & Cons. Affairs	1,239.21	556.70	1,233.00	922.29	2,472.20	1,478.99	0.29%
Min. Gender, Sports & Culture	1,589.47	1,736.87	163.96	266.52	1,753.43	2,003.38	0.39%
Min. of Livestock & Fisheries	2,291.88	2,476.06	1,039.68	1,380.95	3,331.56	3,857.01	0.76%
Min. Water & Irrigation	2,157.55	2,307.39	4,254.44	7,755.20	6,411.99	10,062.58	1.98%
Min. of Env & Natural Resour.	2,263.43	2,525.11	686.37	604.96	2,949.80	3,130.07	0.62%
Min. Co-operative Development	576.70	713.14	1,467.33	58.90	2,044.03	772.04	0.15%
Min. East African & Reg. Co-op.	528.11	441.83	-	-	528.11	441.83	0.09%
The State Law Office	421.79	666.93	125.00	145.25	546.79	812.18	0.16%
Judicial Department	1,337.57	1,656.20	287.50	281.00	1,625.07	1,937.20	0.38%
Public Service Commission	169.52	183.69	-	-	169.52	183.69	0.04%
National Audit Office	1,096.65	1,105.58	-	-	1,096.65	1,105.58	0.22%
National Assembly	5,499.76	5,556.09	-	-	5,499.76	5,556.09	1.09%
Ministry of Energy	257.73	325.52	5,906.39	8,060.51	6,164.12	8,386.03	1.65%
Min. of Educ. Science & Tech.	78,810.21	88,361.67	5,883.25	8,385.87	84,693.45	96,747.54	19.03%
Min. Inform. & Communication	643.55	757.58	26.84	26.00	670.39	783.58	0.15%
Electoral Commission	1,274.50	1,789.50	-	-	1,274.50	1,789.50	0.35%
Kenya Anti-Corruption Comm.	-	1,200.95	-	-	-	1,200.95	0.24%
Min. of Lands & Housing	1,773.60	2,446.94	268.72	791.75	2,042.32	3,238.69	0.64%
NSIS	4,195.45	5,200.00	-	-	5,409.49	5,200.00	1.02%
Min. of Tourism & Wildlife	1,698.32	1,628.26	1,214.04	1,209.00	1,698.32	2,837.26	0.56%
TOTAL Discretionary Exp.	227,082.46	257,023.19	71,982.85	104,220.49	299,065.31	361,243.68	71.04%
Add Consolidated Fund Services:							
(1) Public Debt	112,227.53	123,847.64			112,227.53	123,847.64	24.35%
(2) Pensions and Gratuities	112	227.53			112	227.53	3.38%
(3) Salaries, Allowances	1,037.91	5,287.07			1,037.91	5,287.07	1.04%
(4) Subscrip.to Int'l Organs.	133.02	133.02			133.02	133.02	0.03%
(5) Miscellaneous Debts	776.29	802.00			776.29	802.00	0.16%
TOTAL CFS	131,995.24	147,268.77			131,995.24	147,268.77	28.96%
TOTAL EXPEN. OUTLAYS.	359,077.70	404,291.96			431,060.55	508,512.45	100.00%

poses a challenge in attaining the Millennium Development Goal of universal primary education. Measures should be put in place to ensure that enrolment is sustained and that obstacles keeping children out of school are addressed. Such measures could include the provision of sanitary towels to girls and ensuring that there are school milk and feeding programmes in ASALs. This would help reduce the level of those without education which stands at 21.6 % of females and 13.8% for men, in 2004 with higher rates in North Eastern province. Additionally, the Minister's proposal to review the bursary scheme (allocated Kshs. 0.88 billion in this budget) should ensure that only students from needy backgrounds receive funds and girls get first priority whether they are bright or not. Lastly, the Minister is fair to state that our universities should be less dependent on the Exchequer. However ways in which to do so were not clearly expressed in the Budget Speech. Therefore Parliament may want request that he explains how he intends to increase their self-reliance.

Health

While it is encouraging to note the development expenditure dedicated to the Ministry of Health increased four fold from previous allocation of Kshs. 2.4 billion to Kshs. 9.9 billion. It is worth noting that details are lacking to track the beneficiaries of these funds.

The current budget seeks to increase funds for immunisation which will reduce infant mortality and allocate resources to address maternal mortality. These measures if implemented correctly will contribute to the achievement of the Millennium Development Goals on reducing child mortality and improving maternal health. It is not clear however where the money will come from under the development budget lines of the Ministry of Health. It would have been better to reflect such funds under a line item titled Reproductive Health which would encompass all reproductive health services including family planning.

Another health concern mentioned in the budget speech includes strategies to reduce HIV prevalence and improve access to affordable drugs. This would

TAX MEASURES

It should concern the MPs that the people they represent (constituents) were not cushioned from the effects of inflation, which peaked up significantly towards the end year 2004. To protect income earners from inflation, the personal relief should have been increased by another 10% and the income tax brackets should have been widened.

Below is an outline of the budget's proposed tax measures and their implications. Parliament needs to

Customs Duty	
Proposal	Implication
Duty on used clothing reduced from 75% to 45% or US 30 cents per Kg, whichever is higher	This will translate to lower prices for second hand clothes and thus make them accessible to majority of Kenyans, especially the poor. This will also boost small businesses dealing in second hand clothes. Specifically for gender parity, it will positively impact women who are significantly involved in the trade and purchase of second hand clothes.
Removal of import duty on: Pharmaceuticals Sanitary Pads LPG Speed Governors, safety belts Splints for manufacture of matches Media containing computer software Coal	To make health care affordable To make it affordable to women. This will encourage the production of other brands. To encourage use of LPG and reduce encroachment to forests. To enhance public safety among users of road transport. To support Kenyan manufacturers who export to the EAC and COMESA market. This will encourage the purchase and use of computers Hopefully this will translate to lower cost of coal to the manufacturers. Kenya has some coal deposits. Removal of import duty will facilitate exploitation of the coal if other EAC member countries follow suit and lower import duty.
Page 9 Introduced duty remission schemes for input for manufacture of agriculture equipment used in horti-	Budget 2005/06 To support horticulture sub-sector which has been growing and contributing significantly to GDP. This will hopefully accelerate growth of

Excise Duty	
<i>Proposal</i>	<i>Implication</i>
Excise duty on cigarettes and beer increased by 10%.	This will result in higher prices for beer and cigarettes.
Duty on petroleum products to be collected at the point of importation.	This will minimise leakage of revenue and lower costs of collection for KRA. Petroleum marketing companies will now be required to pay duty in advance and where they use borrowed funds to pay duty, result in higher costs of finance. This could be transferred onwards to the consumers in form of higher prices.
All motor vehicles regardless of engine size, will attract excise duty at 20%.	The aim is to check leakages arising from undervaluation. Henceforth vehicles with big engines and some luxurious vehicles will become cheaper.
VAT	
<i>Proposal</i>	<i>Implication</i>
Failure to withhold and remit tax, issue tax certificate or submit a return will attract a penalty of Kshs. 10,000 or 10% of tax due. Persons not registered as withholding tax agents who collect withholding tax shall be liable for a penalty of Kshs. 10,000 or 10% of the tax withheld.	To enforce compliance among withholding tax agent.
VAT on LPG and Sanitary pads zero rated.	To allow input tax deduction and thus facilitate lowering of retail prices. This will impact positively household budget more so for those who were already buyers of sanitary towels before VAT was zero-rated. More basic needs items should become zero-rated.
VAT on milk and maize flour zero rated.	To allow deduction of input tax and thus make these basic food items affordable. This will have positive impact on food security situation in Kenya.
VAT refunds: Funds have been allocated to KRA to clear the backlog and meet current refund claims KRA has been instructed to carry out an audit of claims to ensure that only those which are genuine are paid.	Clearing the backlog will reduce the cost to businesses especially if the audits are done quickly and refunds given promptly.
Income Tax	
<i>Proposal</i>	<i>Implication</i>
Benefit realised on leased vehicles shall be taken as the cost of hiring/leasing or the prescribed rate of benefit, whichever is higher.	To remove ambiguity in the computation of the benefit derived from the use of leased vehicles for purposes tax.
Tax deductible limits for pension/provident/individual retirement funds increased from Kshs. 210,000 to Kshs. 240,000 per annum.	This will encourage savings via retirement benefit schemes thus ensure social security at retirement age.
Allowed married women to file separate tax returns and to include all sources of income in the returns.	To allow married men and women greater freedom in managing their incomes. Previously grossed household meant that a bigger proportion of the income would attract tax at 30%. With separate tax assessment, there might be lesser tax burden at household level.
Disputes in tax assessments to be resolved in 30 days, down from 60 days.	To streamline tax administration.
To amend Income Tax Act and HELB Act to allow HELB to compel KRA to furnish it with beneficiaries' addresses.	To assist HELB in the recovery of loans from past beneficiaries.

Tax allowable Non-cash benefit in respect of employment or services rendered was raised from Kshs. 24,000 to Kshs. 36,000 per annum.	This adjustment is to cater for inflation.
Farm audit fees in respect of Maximum Residual Limits paid to non-resident laboratories and auditors are allowable for tax purposes.	This is to lower farmers costs of complying with the export market requirements e.g. EU. It is not clear why the Minister does not extend the same benefits to local auditors and laboratories. Is he encouraging farmers to use foreign services? Or is it an EU requirement that this service be provided by foreign firms?
Corporation tax on newly listed companies at NSE lowered from 27% to 20% for a period of 5 years on condition that such companies allow local participation of at least 40%.	To encourage new listing and local participation. However, this will not necessarily lead to more companies (especially new ones) listing on the stock market because regulatory barriers still remain.
Home ownership annual mortgage interest relief was increased from Kshs. 100,000 to Kshs. 150,000.	To encourage investment in home acquisition. However, this is still low relative to the market value of homes.
Limit of cost of motor vehicles allowable in the computation of tax deductible depreciation was increased from Ksh 1 million to Kshs. 2 million.	To reflect the general increase in the prices of motor vehicles.
Medical benefits provided to Directors of companies, up to a maximum to be prescribed by the Minister, to be exempt from income tax.	To encourage companies to offer medical covers to directors too.
Eucalyptus, Pine and Cypress trees reclassified as permanent crops so that capital expenditure incurred in their propagation becomes tax deductible.	To promote afforestation campaigns in Kenya. However, the choice of the three species was not justified. Why didn't he include indigenous trees or plants with medicinal value which face the danger of extinction? This may limit the success of afforestation campaigns since these species do not thrive in all regions of Kenya.

especially impact women who have a higher prevalence rate than males (ratio is 1.9 to 1 as per 2003 Kenya Demographic and Health Survey) and who often take time off from other productive work to take care of the sick. The increasing number of those infected with HIV/AIDS and the resultant number of widows and orphans has increased women's workload and their financial responsibilities significantly. To address this problem in the long term, our local research faculties should focus on developing a vaccine to cure this disease. At present, the Kenya Medical Research Institute (KEMRI) has received Kshs. 0.5 billion under the development expenditure for the refurbishment of buildings and purchase of specialised plant, equipment and machinery and Parliament should ensure that it is used to the benefit of research.

Agriculture

The current budget seeks to support agricultural credit through Agricultural Finance Corporation (AFC). While this is generally good, it is important to realise that financial institutions will usually want collateral which the poor especially women do not have. AFC will need to come up with new ways to address this problem. Additionally, food security remains a major

concern for all Kenyans, particularly women and the children. Parliament needs to push for more extension services and officers under the Kenya Agricultural Research Institute (KARI) to facilitate the diversification of farming and insulate subsistence farmers from weather changes.

CONCLUSION

1. The budget is not as responsive to men and women as it could be. Parliament should call for a budget that is more favourable towards gender through the following:

Requiring departments and line ministries to consider the impact of their budgetary allocations on men and women in the Treasury circular;

Capacity building in line ministries for gender analysis;

Policy and programme analysis for their gender responsiveness;

Establishing disaggregated gender data for financial planning;

Strengthening of Gender Commission; and
Mainstreaming gender in all ministries and departments

through technical and financial support.

Gender responsive budgeting can also be hastened by the prompt release and discussion of the Sessional Paper 2005 on Promoting Gender Equality.

2. Expenditures have not been re-oriented in a prudent manner. If adopted as proposed, the budget will need to borrow to meet its deficit. This will divert funds towards non-core areas and increase interest rates. Additionally, it will further burden the taxpayer.

3. Adoption of the tax measures will help to raise levels of consumption. However to further increase consumption and motivate savings, the Minister should reduce the impact of inflation by widening the tax brackets and increasing tax relief.

4. Tax measures have created good opportunities for some level of investment in certain areas. However investment is more likely to occur within a context of good governance, macroeconomic stability, a fair and swift judicial system and better security.

5. Expenditure estimates are sketchy and this makes it

difficult for Parliament and citizens to track monies disbursed and to what end. This encourages financial indiscipline by ministries and departments. Parliament should insist on more transparency.

Kenya adopted the Mid Term Expenditure Framework (MTEF) approach to budget formulation in 2000/01. The purpose of this idea was to link policy-making to planning and budgeting, maintain fiscal discipline, facilitate expenditure prioritisation and encourage better use of the resources. After reviewing the MTEF in 2003/04, it was found that it remained separate to the budgeting process. To bridge this gap, the MTEF review recommended that a Budget Strategy Paper amongst other documents be prepared to outline priority needs according to the resource envelope..

Although these measures have greatly improved the planning process, it appears from the analysis of the budget 2005/06 proposals, spending patterns and tax measures, that more can be done to connect planning to the context and priority needs.

Budget Calendar

1. Policy Debate (up to 7 days from Thurs 9 June)

Policy Debate. The House will debate the Government's economic policy and strategies as outlined in the budget speech. Do they adequately address the challenges and imperatives facing the country? Official opposition will be given first opportunity to articulate its alternative to the Government's proposals. The Finance Minister will respond at the end of the debate.; *Key Documents: Budget Speech, PRSP, National Development Plan, Economic Survey, Statistical Abstract and this Guide.*

2: Vote on Account (1 day)

Policy debate will be interrupted for the Minister to seek approval for up to 50% of the expenditure to spend up to December 31 pending approval of appropriations during the Committee of Supply: *Key documents: Estimates of Recurrent & Development Expenditures and the summary provided by this Guide.*

3. Committee of Ways and Means (3 days):

Finance Minister will move Motion to constitute House as Committee of Ways and Means. House will debate taxation proposals. Members will have opportunity to amend the proposals during the debate on the Finance Bill.: (*Key*

documents: Budget Speech, Finance Bill, Estimates of Revenue and The Revenue Analysis Section of this Guide).

4. Committee of Supply (Before October 31);

House will debate and approve expenditures on a Ministry-by-Ministry basis. Members will have opportunity to propose nominal reductions on specific items (sub-votes) as a sanction for non-performance. The house will debate 10 votes in Plenary and pass the rest on/or about 31st October, by guillotine. (*Key documents: Estimates of Recurrent & Development Expenditures and the analysis of Expenditures in this Guide).*

This Budget Guide has been produced by the **Budget Information Programme (BIP)** of the Institute of Economic Affairs, a non-partisan, public Affairs forum.

For more information please contact,

Institute of Economic Affairs

5th Floor, ACK Garden House

P O BOX 53989, Nairobi,

Tel: 2717402, 2721262, 2716231

Email: admin@ieakenya.or.ke