31 March 2015

THE CLERK
SENATE BUDGET, COMMERCE AND ECONOMIC AFFAIRS
KENYATTA INTERNATIONAL CONFERENCE CENTER
NAIROBI, KENYA

Dear Ms. Emmy,

RE: INTERNATIONAL BUDGET PARTNERSHIP KENYA'S SUBMISSION TO SENATE

KEY QUESTIONS ON DIVISION OF REVENUE 2015

As the Senate debates the Division of Revenue Bill 2015, there are a number of issues that should be considered to improve fairness in revenue sharing in 2015/16.

1. **The proposed equitable share to counties for 2015/16 is a slight decrease in the share of total shareable revenues compared to what counties received in 2014/15.** The Senate should consider whether this level of funding demonstrates adequate support for devolution. As overall revenues rise, should national government be taking more of that increase than counties?

	2014/15 (Billions)	**2015/16 (Billions)**
Total Shareable Revenue	1,026.31	1,242.70
County Equitable Share	227	258
Percentage	**22.10%**	**20.76%**

2. **Is there enough money for Level 5 Hospitals and are counties allocating matching funds to ensure the facilities maintain services?** The conditional grant allocated for these facilities in 2015/16 is Ksh 2.064 billion, which is a slight increase compared to what was allocated last year. However, this is still significantly lower than the Ksh 7.7 billion in recurrent funding allocated to provincial hospitals in 2012/13. From the first Division of Revenue Bill 2013, it has been assumed that the gap between what facilities require and what is provided by the conditional grant is being filled by counties. The logic of this arrangement is that counties hosting L5 facilities are providing regional services and should not bear the cost of those services alone, but at the same time, the host counties also benefit disproportionately from the services and must bear some of the cost themselves. How do we ensure that these facilities are receiving adequate funding? It is possible to require host counties to match the funding from the conditional grant (up to a certain percentage) in order to ensure that counties are filling this gap, but this has never been done. Given the importance of these facilities, it is time to ask whether enough is being done to ensure that they are fully financed.
3. **More broadly, what are the actual conditions that guide the conditional grants in the Division of Revenue Bill (DORB) 2015**? When funds are

devolved to counties for specific uses, the conditions should be indicated and a mechanism of enforcement provided. Conditional grants are currently given for two reasons. One reason is that some funds need to be transferred to counties using a distribution that is different from the main revenue sharing formula guiding the "equitable share." Another reason to give a grant is to ensure that certain national priorities are funded at the county level. All conditional grants should therefore either be distributed in a manner that is different from the formula, or they should come with conditions for how the funds are to be used, or both. From the DORB 2015, it is not entirely clear what conditions or distributional criteria apply to the conditional grants. For example, the medical leasing scheme appears to be financing equipment in two facilities per county, which suggests that this is a conditional grant that is not distributed according to the formula. But it is also likely that this is a conditional grant that can be used only for medical leasing. Are there other conditions attached to the grant? We cannot tell (in fact, this may not be a grant at all; it may be funding entirely managed by national government). As another example, the road maintenance grant appears to be given conditionally to ensure that it is used for road maintenance; it is not clear what the distributional criteria are, but it may be that they follow the CRA formula. This is, however, highly questionable, given that the formula has no parameter related to roads and tends to redistribute funding to areas with fewer roads. Giving a grant that can only be used for road maintenance to areas with few roads may not be sensible. Parliament should interrogate the rationale for the distribution and conditions associated with all conditional grants.

4. **Continuing with the issue of conditional grants, many of these grants are not actually devolved to counties directly, but they are mixed with those grants that are actually given to counties, creating confusion.** The DORB mentions that the loans and grants in the "conditional allocations section" will be included in the National Government budget and managed at that level. Therefore, why is this included as part of the county revenue in 2015/16? Moreover, these are among several funds that may not be given directly to counties, from what we are able to conclude from other sources. For example, it does not appear that the medical leasing funds will be given directly to counties. It is not clear whether the free maternity funds are given directly to facilities or pass through county government; if the latter, the notes in DORB 2015 suggest that this may be replaced by an insurance modality which would likely be facility-based. For purposes of transparency and to help inform county budgeting, it should be clear which conditional allocations are actually conditional grants to the counties, and which are not.
5. **The decision to bring more conditional grants into the Division of Revenue Bill is commendable, as these grants should all be considered together; however, this requires a careful comparison with last year to understand what is actually happening to total county revenues.** The table below compares conditional grants between the two years, showing that the total grants last year were much higher than normally reported, because these grants were not included in the DORB last year. Thus the increase in funding is much smaller this year than it might otherwise appear. Coupled with the decline in the counties' share of the total shareable revenue, this implies that county revenues are growing slowly.

Conditional Grants	2014/15 (Ksh) (Billions)	2015/16 (Ksh) (Billions)
Level 5 Hospital Grant	1.85	2.06
Free Maternity*	4.00	4.30
DANIDA Health Grant	0.73	0.85
World Bank Health Grant**		0.51
Medical leasing*	3.30	4.50
RMLF Grant (Road maintenance)		3.30
Health User Fee Grant*	0.70	0.90
Totals	**10.58**	**16.41**
Funds managed by national for counties **Total "conditional allocations"** **Total equitable share+conditional allocations** **Percent of shareable revenue**	**13.17** **23.75** **250.4** **24.4%**	**9.32** **25.73** **283.73** **22.8%**

***Funds were not part of DOR last year and were not counted as a conditional grant though it was distributed through the budget**

****Funds were available in 2014/15 but were not given directly to counties as is planned for 2015/16**

6. **There is a need for Parliament to ask how much money is still held up in the national government budget that could be devolved**. There is still a substantial amount of money held by the national government in the 2014/15 that could be devolved, though this would require some significant state reform. From our analysis, there is about Ksh 65 billion that should be up for discussion, of which some portion could and should be devolved (see Annex). This is inclusive of government grants and local Appropriation in Aid, but excludes any external funding. Reforms in state corporations will play a key role in this discussion, as 73 percent of the Ksh 65 billion consists of allocations to parastatals running county functions. These funds cannot just be devolved without policy reform to cater for corporations that are performing regional functions, corporations that are performing both national and county functions, and corporations performing shared functions (such as energy). There are also some national agencies that were slated for devolution in 2012/13 but have been pulled back that deserve a second look. The Senate should start the debate on how to make adjustments that will ensure each function is run by the right level of government without negatively affecting service provision.
7. **Even if the technical analysis of how much it costs to run functions at their current levels is correct, the DOR is more than an accounting exercise and should also be based on the relative priority we attach to education, security and other national functions versus health, agriculture and other devolved functions.** The "baseline" used in the DORB is

an adjusted and inflated figure based on relative priorities of different sectors in 2012/13, and may not reflect the relative importance of these sectors in 2015/16. Parliament must debate and decide these matters.

8. **What projects/programs are funded by the conditional allocations from loans and grants totalling Ksh 10.7 billion**? The DORB does not provide much information about such projects in terms of locations and individual costs but this has implications on county revenue. This information allows the counties to have an idea of what donors are funding in the counties so that they can avoid allocating money to the same projects or programmes. This should also include the time it will take to implement these donor funded projects. In 2014, the County Allocation of Revenue Bill had some level of detail on projects funded by donors, but we have not been able to access it so far. This information should be made readily available along with the DOR.
9. **Are the national interest priorities under the national government based on a broad national consensus**? The "national interest" mentioned in Article 203 of the constitution as a criteria for revenue sharing should refer to priorities for the country as a whole. It does not refer to national government priorities alone, nor does it refer only to those functions (such as security) carried out by the national government. The "national interest" should be based on a broad social consensus that cuts across both levels of government. For example, a broad social consensus could determine that primary health care was a vital national interest, and that would require counties to have additional funding to support implementation of that function. The 2015/16 DORB is more specific about how the "national interest" has been defined than the 2014/15 DORB. However, it appears that the definition used includes only those funds that will be managed by national government (even for farm inputs, a county function) and there is no evidence that this "national interest," which includes laptops, etc. is the result of any consensus agreement among key stakeholders, including the two levels of government. The choice about what to include in national interest reduces the amount of revenue available for sharing by over Ksh 70 billion, so it is important to consider it carefully.
10. **What are the costs of administrative services in the counties and is the funding given to counties sufficient to manage it?** There has been considerable discussion on how much counties have to spend on administration and whether this is affecting the amount of resources available to run basic services. However, the level of information in the DORB does not really give a full picture of county administrative costs. Over time, the National Treasury and CRA have produced different estimates of administrative costs at county level. These estimates have never been consistent or final, and it is imperative that Parliament demand an updated and complete estimate of all county administrative costs based on the latest notices from the Salaries and Remuneration Commission.

Annex

Resources in 2014/15 budget that should potentially be devolved by source

Categories	Government Grants	Local AiA	External Funding	Total Government Grants+Local AiA+Ext Funding	Sector share to the Total Funding to Functions
Shared Functions	15,350,629,702	3,140,000,000	20,163,000,000	**38,653,629,702**	**48%**
Dominant External Funding	1,803,799,670	-	12,278,894,126	**14,082,693,796**	**17%**
Regional Agencies	5,483,697,778	1,817,238,239	11,056,227,277	**18,357,163,294**	**23%**
Single Unit Running National and County Functions	4,595,299,020	367,000,000	27,985,340	**4,990,284,360**	**6%**
Initially Devolved But Partially or Fully Retained	4,188,743,678	49,675,917	766,000,000	**5,004,419,595**	**6%**
Total Allocation to Shared Functions	**31,422,169,848**	**5,373,914,156**	**44,292,106,743**	**81,088,190,747**	**100%**
Total Allocation to Devolved but Retained Functions	**23,772,910,171**	**4,040,000,000**	**8,178,740,000**	**35,991,650,171**	
Total	**55,195,080,019**	**9,413,914,156**	**52,470,846,743**	**117,079,840,918**	
:of which					
State Corporations	**42,029,282,441**	**4,961,238,239**	**39,032,452,617**	**86,022,973,297**	**73%**

*This table highlights funding in the 2014/15 budget that should be discussed for possible devolution. The categories are:

Shared Functions. These are institutions that are performing functions that are shared in the constitution, such as energy, where it is not clear how much of what they are doing should be devolved.

Dominant external funding. hese are devolved budget heads but they are almost entirely funded by external funds. There is a small amount of local funding that could potentially be devolved, but may also be counterpart funding to secure donor funds. These areas cannot be devolved as they are currently funded, but they represent devolved functions that could eventually be devolved if their funding arrangements changed.

Regional Agencies. Budget heads running devolved functions at a regional level such as the Water Service Boards. Regional bodies may need to be reformed rather than dissolved to ensure regional cooperation continues.

Single Unit Running National and County Functions. Some budget heads are for units that seem to run both national and county functions and it is not clear how these should be split. The National Transport and Safety Authority is an example.

Initially Devolved but Partially or Fully Retained. Another set of vote heads that were marked partially or fully devolved in the 2012/13 budget have remained in the 2014/15 budget for reasons that are not clear. Some may have been devolved in error, but this should be interrogated.

Devolved but Retained. These are budget heads that correspond to devolved functions and there does not appear to be any reason why they should not be devolved.

Further details available upon request.