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KENYA

Report on the Observance of Standards and Codes (ROSC) Fiscal Transparency Module

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January 29, 2008

Executive Summary

This report provides an assessment of fiscal transparency practices in Kenya in relation to the requirements of the IMF Code of Good Practices on Fiscal Transparency based on discussions with the authorities and other organizations, the authorities' response to the IMF fiscal transparency questionnaire, and other sources of information, including the 2006 PEFA assessment. The IMF Manual on Fiscal Transparency (http://www.imf.org/external/np/fad/trans/manual/) should be consulted for further explanation of the terms and concepts discussed in this report.

Kenya has made significant progress since 2003 in improving fiscal transparency and accountability. The introduction of key legislation establishes some important building blocks for the construction of a sound fiscal management system. These and other initiatives and practices have helped Kenya comply with some of the requirements of the fiscal transparency code. However, a great deal more is needed to conform with best international practices.

Regarding *clarity of roles and responsibilities*, fiscal roles of the branches of government and among different levels of government are clearly defined in law and practice. However, the blurred line between general government and the rest of the public sector makes it difficult to accurately establish the full extent of extra-budgetary spending or to clearly define general government. Also, the very limited coverage of the Government Financial Management Act (GFMA) has weakened the Ministry of Finance's ability to ensure adherence to financial regulations.

On *open budget preparation, execution and reporting*, progress in developing the MTEF has contributed to an annual budget process that is generally open. The medium-term fiscal objectives are clearly stated in budget documents but there is no analysis of contingent liabilities, in particular those related to government pension schemes. Improvements are visible in revenue administration, cash-flow planning, and procurement. However, the accounting and reporting system is still evolving and data sharing and coordination is lacking, and the internal audit function is weak.

On *public availability of information*, fiscal information on central government is fairly comprehensive and readily available to the public but there is no "citizen's guide" to the budget. Local government reports are untimely, but local authorities have begun to hold public hearings on their budgets to enhance local community involvement.

In terms of *assurances of integrity*, the Kenyan National Audit Office (KENAO) is independent of the executive. The timeliness in the submission of audit reports has improved but backlogs pertaining to local governments persist. Reviews of audit reports by Parliament are still conducted with delays of 3-4 years, which dilutes their effectiveness.

Main recommendations:

- Put in place the building blocks for PFM reform by: (i) revising the GFMA and financial regulations; (ii) giving budget execution, accounting and internal audit a firmer legal and institutional basis; (iii) consolidating the Exchequer Account to function as a Treasury Single Account; (iv) clarifying the concept of general government and embodying it in the law; and (v) tracking and carefully managing the growth of autonomous agencies and funds.
- Enhance the effectiveness of the external audit function by reducing backlogs and ensuring that the follow-up of audit findings are timely and sustained.
- Quantify contingent liabilities and implement policies to mitigate their impact, and establish a legal and institutional framework for PPPs and develop appropriate capacities to assess risks in PPP arrangements.

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ABBREVIATIONS

AGD	Accountant General Department
AIAs	Appropriations-in-Aid
BOPA	Budget Outlook Paper
BSD	Budget Supplies Department
BSP	Medium-Term Budget Strategy Paper
CAG	Controller and Auditor General
CBK	Central Bank of Kenya
CDF	Constituency Development Fund
DGIPE	Department of Government Investment and Public Enterprises
DMD	Debt Management Department
DPM	Department of Personnel Management
EAD	Economic Affairs Department
EBF	Extrabudgetary Fund
ERD	External Resources Department
FA	Fund Account
IAGD	Internal Auditor General Department
IFMIS	Integrated Financial Management Information System
IPPD	Integrated Payroll and Personnel Database
GDDS	General Data Dissemination Standard
GFMA	Government Financial Management Act
GFRP	Government Financial Regulations and Procedures
GFS	Government Finance Statistics
KACC	Kenya Anti-Corruption Commission
KIPPRA	Kenya Institute for Public Policy Research and Analysis
KENAO	Kenya National Audit Office
KNBS	Kenya National Bureau of Statistics
KPLC	Kenya Power and Lighting Corporation
KRA	Kenya Revenue Authority
LATF	Local Authorities Transfer Fund
MoF	Ministry of Finance
MTEF	Medium-Term Expenditure Framework
NFI	Non-Profit Institution
NGOs	Non-Governmental Organizations
NSSF	National Social Security Fund
PAA	Public Audit Act
PAC	Public Accounts Committee
PAYE	Pay-as-You-Earn
PFM	Public Financial Management
PIC	Public Investment Committee
PPP	Public-Private Partnership
PS	Permanent Secretary
QBR	Quarterly Economic and Budget Review
QFAs	Quasi-Fiscal Activities
RBA	Retirement Benefits Authority
ROSC	Reports on the Observance of Standards and Codes
SAGAs	Semi-Autonomous Government Agency
SDDS	Special Data Dissemination Standard
TARDA	Tana and Athi Rivers Development Authority
TIN	Taxpayer Identification Number

I. DETAILED DESCRIPTION OF PRACTICE[1]

A. Clarity of Roles and Responsibilities

Definition of Government Activities

1. **In Kenya, general government is not defined consistently with Government Finance Statistics (GFS) principles**. *1.1.1*
Central and local government is well defined in law and in practice. However, most government-owned non-profit institutions have traditionally been classified together with state-owned enterprises in Kenya under the State Corporations Act (1986), leading to lack of clarity between government and public sectors. These non-profit institutions include a wide range of semi-autonomous government agencies (SAGAs), such as universities and hospitals, as well as a number of extrabudgetary fund (EBF) operations, such as the Kenya Roads Board, or the Constituency Development Fund (CDF). In addition, over the years, a variety of fund accounts (FAs) have been set up to channel earmarked revenues for specific operations, many of which are undertaken by SAGAs. The need for clarity in this area is understood by the Ministry of Finance (MoF), particularly in the context of the MTEF reforms. Box 1 provides the key features of general government in Kenya.

2. **Relationships between central government and public nonfinancial and financial corporations are generally clearly defined**. *1.1.4*
Nonfinancial and financial corporations in which the government has majority controlling interest are regulated under the State Corporations Act. More than half of the public nonfinancial and financial corporations are also incorporated entities under the Companies Act. The State Corporations Act calls for the Minister of Finance and the Minister of the parent ministry to be represented on the Board, and makes the management of the state corporation accountable to its Board. Since 2005/06, all state corporation Boards have signed performance contracts with their parent ministry, cosigned by the MoF. To some extent, public corporations are engaged in quasi-fiscal activities (see paragraph 4 below), but they receive no preferential treatment vis-à-vis the private sector.

3. **Government holdings of fully-owned corporations and equity are moderate; the management of state assets is clearly defined**. *1.1.5, 2.1.4*
Of the more than 40 financial corporations specializing in general and specialized banking services, and insurance, 12 have government participation, of which nine are

[1] This report was prepared by a Fiscal Affairs Department (FAD) team comprising Messrs. M. Katz (head), and D. Last, Ms. G. Everaert, and Mr. V. Ramachandran (PFM Resident Advisor AFRITAC East). Discussions were held with the Minister of Finance, Governor of the CBK, Deputy Mayor of the City of Nairobi, members of Parliament, senior officials in the Ministry of Finance, Planning and National Development, Local Government, Roads and Public Works, Health, the CBK, KRA, DPM, Public Service Commission, KENAO, Kenya Roads Board, Kenyatta National Hospital, Kenya Railways, KIPPRA, NSSF, RBA, TARDA, KPLC, the World Bank and the PFM Development Partner Group.

100 percent government-owned, and the remaining three are under direct or indirect government control. There are over 40 public nonfinancial enterprises operating in a variety of sectors, including agriculture, transport, tourism, trade, industry, energy, communications, and education. A number of utilities, such as electricity distribution and fixed landline telephone operations, are state monopolies. According to the Kenya National Bureau of Statistics (KNBS), some 654,200 workers were employed in the public sector in 2005, representing around 36 percent of formally registered wage employment.[2] Since the early 1990s, a significant number of smaller and non-strategic state-enterprises have been privatized. Recent examples of privatizations in strategic public corporations include the floating of 30 percent of shares on the Nairobi Stock Exchange of the power generating company (KENGEN), and 40 percent of shares in a sugar company (MUMIAS). Planned privatization includes the partial sale of shares in Kenya Telkom and its cell phone operator Safaricom, as well as a re-insurance company. The Department for Government Investment and Public Enterprises (DGIPE)[3] is responsible for the overall management and oversight of state assets and approves, on behalf of the MoF, major decisions on subsidies, investment, budgets, and privatization.

Government Relations with Nonfinancial Public Corporations and the Private Sector

1.1.4

4. **Public nonfinancial corporations carry out some quasi-fiscal activities (QFAs)**. *1.1.4, 1.1.5, 2.1.4*

Quasi-fiscal activities do exist—the mission identified QFAs in the agricultural, transport and energy sectors.[4] The public financial sector no longer extends subsidized credit to the public. Examples of QFAs include free transport, subsidized services in the electricity and water sectors, and special projects carried out on behalf of the government.[5] Public corporations are generally compensated for carrying out QFAs, and these are reflected in their budgets but are not visibly presented in the central government's budget as subsidies nor are they clearly distinguished from grants. Moreover, there is no discussion on the total cost of subsidies, as their total value is not readily known at this time (although with

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[2] Formal wage employment in the private and public sector (1.8 million) constitutes only a very small share of total formal and informal employment (8.3 million). Public employment is estimated at 7.9 percent of total employment. Compared to the total labor force (estimated at 11.4 million in 2004), the share of public employment in the total labor force is 5.7 percent. Data are available at http://www.cbs.go.ke/ .

[3] DGIPE was created in the context of the Public Enterprise Reform Program and Privatization Policy Paper of 1994.

[4] The extent of QFAs in other sectors is not known, as the mission was not able to cover all sectors.

[5] Kenya Ferry Services provides free transport to pedestrians, for which it receives compensation according to a formula agreed with government. End-users prices for electricity are regulated at below production cost. A three way arrangement in 2006/07 between KPLC, KENGEN and the government provides for an annual price subsidy of around Ksh 2.6 billion. Tana and Athi Rivers Authority (TARDA) subsidize its fully-owned company that provides drinking water to several towns. Kenya Power and Lighting Corporation (KPLC) manage the rural electrification program on behalf of the government, funded from earmarked revenues and external financing.

considerable difficulty identified QFAs can be aggregated from the central government's budget books).

Box 1. General Government in Kenya

General government in Kenya comprises the following :	Percent of GDP[#] 2007/08
Central Government Units Covered by the Budget	
1. Parliament, president's office, judiciary, 31 ministries, 9 departments, and 3 statutory commissions (approximately Ksh 500.4 billion) *	**24.3**
2. Consolidated Fund Services – public debt, pensions, statutory obligations (Ksh 154.2)	**7.5**
Central Government Units with Individual Budgets	
3. Over 140 fund accounts, semi-autonomous government agencies, extra-budgetary funds, and regional development authorities (estimated at Ksh 60 billion) **	**2.9**
Local Government	
4. 175 local authorities (estimated at Ksh 20 billion, including LATF transfer)	**1.0**
5. Constituency Development Fund (Ksh 10 billion)	**0.5**
Total General Government	**36.2**

[#] GDP projection for 2007/08 is set at Ksh 2,059 billion, according to BSP 2007.
* excluding Consolidated Fund Services, transfers to semi-autonomous government agencies and extra-budgetary funds (estimated), and transfers to local authorities (LATF)
** exact number not available.

5. **Arrangements regulating profit transfers from public financial and nonfinancial corporations to the budget are defined by their respective Boards**. *1.1.5*
The MoF has instructed the Boards of public enterprises to define their individual dividend policies. Annual reports of public corporations provide details on total profit, retained earnings, other uses of profit, and dividend payments. The Central Government's budget records aggregated payments of taxes, royalties and dividends from state corporations.

6. **Privatization, which has until recently been guided by the Privatization Policy Paper of 1994, is now to be managed under clear principles set out in the Privatization Act of 2005**. *1.1.5*
The Permanent Secretary (PS) to the Treasury Incorporation Act of 1963 vests the authority to manage government-owned assets in the PS Treasury, and privatization has been carried out under the Companies Act. The Privatization Policy Paper establishing the Public Enterprise Reform Program, approved by cabinet in 1994, has guided the privatization process until recently. The policy focused on a list of mainly non-strategic enterprises to be privatized, and defines procedures and processes that ensure an open and competitive bidding process, and transparency through publication of notices and outcomes during the tendering and after the awarding process. The interim arrangement is being replaced by the recently adopted Privatization Act, which also includes a

framework for the privatization of strategic public enterprises. The Act envisages the establishment of a Privatization Commission, which will establish a privatization program to be approved by cabinet and submitted to Parliament for information. The Act defines clear modalities for an open and competitive privatization process, and provides for an appeals tribunal. The Act also specifies that privatization receipts are to be paid into the Consolidated Fund.

7. **Kenya ranks in the middle of the World Bank's global ease of doing business indicators and among the highest in Sub-Saharan Africa**. *1.1.5*
The recently established Business Regulatory Reform Unit within the Ministry of Finance is working toward reducing the number of licenses and simplifying procedures.[6] Many of these licenses were introduced by local authorities under the Local Government Act of 1986 and revised in 1998 to raise revenue.[7] Other contributing factors to the cost of doing business include the outdated Companies Act of 1948, but which is currently being reviewed by the Kenya Law Reform Commission, and inefficiencies in the judicial system. Some 118 licenses have been abolished or simplified in the past two years (out of an estimated total of 1,325 business licenses), and proposals are currently in parliament for reducing this number further.[8] The government is developing a Regulatory Reform Strategy, which will subject new regulations to a cost impact assessment, develop regulatory criteria, and establish a consolidated electronic registry of licenses.

Government Relations with the Central Bank and Public Financial Sector

8. **The Central Bank of Kenya (CBK) Act grants the central bank operational independence and clearly limits its fiscal role**. *1.1.4*
The Act (1966, amended 1996) gives the CBK a principal mandate to achieve and maintain price stability. The CBK is governed by a Board of Directors chaired by the Governor. The Act provides for the appointment of Board members and specifies the condition under which the Governor can be removed from office (by a Tribunal). Nevertheless, the PS for the Treasury is represented as a nonvoting member on the Board, and can indirectly influence its decisions.[9] The bank acts as banker, adviser and fiscal agent of the government, and administers domestic debt on behalf of the government. Financing of the fiscal deficit through the CBK overdraft facility is limited to 5 percent

[6] For instance, in 2006, a cut flower business was required to obtain 60 licenses to operate, while a tour operator was required 11 licenses, seven of which were to be displayed on the vehicle windscreen ("Reducing Business Licenses in Kenya", report by the Working Committee on Regulatory Reforms for Business Activity in Kenya).

[7] Section 148.

[8] The 2007/08 Finance Bill proposes to eliminate 205 licenses and simplify another 371.

[9] The government maintains a direct oversight role in the banking sector through the Banking Act, which empowers the MoF to approve changes to bank charges and fees. The government has proposed changes in the governance structure of the central bank which would establish a Monetary Policy Committee to be chaired by the Governor of the CBK. The Board of Directors would have responsibilities over issues other than monetary policy.

of the gross recurrent revenue of the latest audited Government appropriation accounts, with this facility bearing interest at the Central Bank rate. Government deposits at the central bank are not remunerated. The CBK also issues debt instruments on behalf of the government, but is adequately compensated for these QFAs through a levy which the government pays on all debt issues.[10]

9. **Profit transfers from the CBK are clearly regulated by the CBK Act**. *1.1.4*
Under the CBK Act, any excess profits of the CBK, after taking into account all operating expenses and necessary provisions, including those into the General Reserve Fund of the CBK, are transferred to the government Consolidated Fund, and are clearly identified as transfers from the CBK in government revenue estimates and accounts. At the same time, however, the government must compensate the CBK directly from the Consolidated Fund for any net losses that cannot be met through its General Reserves Fund, irrespective of whether there is any appropriation for this in the budget. Unrealized profits or losses due to exchange rate movements are treated as book operations and are specifically excluded from the above arrangement.

Fiscal Management Relations among the Branches of Government

10. **The fiscal roles of the executive, legislative and judicial branches are clearly defined in the Law**. *1.1.2*
The fiscal roles of the executive, legislature and judiciary are clear and enshrined in the Constitution. Article 48 limits the financial powers of the Parliament to decreasing taxes and/or expenditures in the annual estimates laid before it by the Minister of Finance. The sole exception is the budget of the Parliament itself, which, under Article 45B (5), is prepared by the Parliamentary Services Commission and adopted by the National Assembly.[11] Under Article 99, the Parliament may also enact laws that establish special purpose funds or earmarked (retained) revenues. The Government Financial Management Act (GFMA) of 2004 defines the financial management roles and responsibilities within government, assigning overall responsibility of managing the Consolidated Fund to the Minister of Finance, and specific powers to the Treasury. The GFMA also defines specific duties and responsibilities of Accounting Officers (generally the PSs of ministries or chief executive officers of government agencies). The Public Audit Act (PAA) of 2003 defines the specific oversight powers and responsibilities of the Controller and Auditor General (CAG) as envisaged in the Constitution. Under this Act, the CAG both authorizes withdrawals from the Consolidated Fund and audits the government accounts, which can be interpreted as a conflict of interest. Furthermore, under the PAA, the CAG submits the audit reports to Parliament through the Minister of Finance. The GFMA provides for

[10] The levy is set at 1.5 percent of every debt issue, but with a cap of Ksh 3 billion from this fiscal year onward.

[11] Salaries of members of Parliament are over 200 times per capita GDP—are well above those in neighboring countries, or developed countries such as the U.S., U.K., or Norway. (Source: The Parliamentary and Human Rights Accountability Charter as presented in the vision 2030 presentation.

specific penalties (financial and prison terms) that can be imposed for conviction of public officers found guilty of major contraventions of its provision, implying referral of such cases to the courts.

Fiscal Management Relations among Different Levels of Government

11. **The responsibilities of different levels of government are clearly defined**. *1.1.2*
The Local Government Act of 1986, revised in 1998, clearly defines the expenditure and revenue responsibilities of the 175 Local Authorities in Kenya, which are overseen by a mix of elected municipal, county, town and urban councils. In general, the expenditure responsibilities of Local Authorities in Kenya are limited to the provision of communal and urban planning services, control over trade and transport services, and the maintenance of rural and urban roads.[12] The wealthier seven city councils, which are able to raise significant local revenues (in particular property tax), have also had primary education and primary health services devolved to them. The Minister of Local Government has the power to approve further devolution as revenue capacities of other Local Authorities improve. In 1998, the funding arrangement for Local Authorities was reviewed and formalized under the Local Authority Transfer Fund (LATF) Act of 1998. This provides for a system of formula-based block grants, providing an equitable and transparent basis for determining the distribution of five percent of previous year's national income tax collection earmarked for Local Authorities. The variable part of the formula is based primarily on total population, with urban population as a secondary element of the formula. LATF has provided certainty of funding to Local Authorities as well as confirmed block grant amounts early on in the budget process (around February). In return, Local Authorities have to meet a number of conditionalities before they can receive their grants, including timely submission of budgets and annual revenue and expenditure reports, and proof of clearance of past debts (mainly pensions and health insurance contributions). Under the LATF Act, Local Authorities are also obliged to provide quarterly reports, but since the provision of these is not tied to disbursement of the grant, the reports from some Local Authorities are delayed beyond the 15 day submission limit, and, in a few cases, the reports are not sent at all. Local Authorities are allowed to borrow under the Local Government Act (see paragraph 33).

The Legal and Administrative Framework for Budget Management

12. **The legal and administrative framework for public finance management is neither clear nor comprehensive**. *1.2.1*
As can be seen from Box 2, the backbone of the legal framework for general public finance management rests with the Constitution, the GFMA, and outdated Government Financial Regulations and Procedures. This legal framework has a very limited coverage of key areas of government financial management, and does not take into account

[12] The expenditure and revenue responsibilities of Local Authorities are detailed out in parts IX through XIII of the revised Local Government Act of 1998.

important reforms implemented in recent years, such as the MTEF, new budgetary classifications, new approaches to internal control and internal audit, the introduction of Finance Officers, the design and on-going roll-out of computerized systems,[13] and the production of quarterly budget reports. Implementation issues related to the legal framework are further described in Box 3 below. The Government Financial Regulation and Procedures are currently under review.

Box 2. Legal Framework for Public Finance Management in Kenya

<u>The current PFM legal framework in Kenya includes</u>:

- The **Constitution of 1963**, which sets out the broad responsibilities of the executive and legislature in matters concerning public finance (Chapter VII).
- The **Government Financial Management Act of 2004**, which assigns responsibility for the Consolidated Fund and matters related to public financial management to the Minister of Finance, as well as 'Treasury' responsibilities for public finance management procedures and powers to access documentation. It assigns responsibilities to Accounting Officers for effective, efficient, economical and transparent management of monies appropriated to them by Parliament, and establishes the key offices of Accountant General, Budget Director and Internal Auditor General. The Act focuses on withdrawals from the Consolidated Fund and payments, but does not cover budget formulation and hardly covers budget execution processes. Regulations under this Act have not yet been issued and compliance as well as application of sanctions remain weak.
- **Government borrowing is regulated under 4 separate Acts:** the **External Loans and Credit Act of 1967**, which requires Parliamentary approval for all external loans entered into by the government,[14] the **Internal Loans Act of 1978**, which regulates domestic borrowing, the **Central Bank Act (1966, revised 1996)** which caps government overdraft borrowing to 5 percent of the latest audited revenues, and the **Guarantee (Loans) Act (1961)**, which regulates the ability of government to issue loan guarantees to third parties.
- The **Public Audit Act of 2003,** which provides the legal framework for the external audit oversight function across the whole of the public sector.
- The **Public Procurement and Disposal of Public Assets Act of 2005** which sets out the legal framework for public procurement across the whole of the public sector.
- The **Kenya Revenue Authority (KRA) Act which** establishes the KRA and assigns it responsibilities for revenue administration.
- The **Local Government Act of 1986 (revised 1998)** provides for public finance management within Local Authorities, while the **State Corporations Act of 1986** does the same for SAGAs and EBFs.

<u>Other PFM regulations</u>:

- ***In practice***, for day to day public finance management staff still refer to the outdated **Government Financial Regulations and Procedures of 1989 (revised in 1992)**, which derive their authority directly from the Constitution or from older fully or partly repealed legislation, notably the Paymaster General Act, and the Exchequer and Audit Act (repealed when the GFMA was adopted), as well as the multitude of treasury circulars which have modified these regulations and procedures over the years.

[13] The Integrated Payroll and Personnel Database (IPPD) has provided decentralized payroll and personnel management systems in most line ministries, while the Integrated Financial Management Information System (IFMIS) is an Oracle-based software package that is currently being rolled out to all line ministries, initially for budgetary and accounting functions.

[14] The External Loans and Credit Act (Cap 422) was amended to effectively increases from Ksh320 billion to Ksh 500 billion the maximum amount the Minister can borrow from external resources. Similarly, the maximum amount under (Cap 461) guaranteed Loans Act, was increased from Ksh 40 billion to Ksh 80 billion in July 1993.

Box 3. Summary of Reforms Since 2003

Prior to 2003, Kenya faced serious weaknesses in institutions, including those in the area of public financial management. The PEM-AAPs, undertaken in 2003 and 2004, showed that Kenya met only 4 out of 16 benchmarks.[1] Governance problems culminated in a number of notorious scandals such as the Goldenberg and Anglo-Leasing scams. **Since 2003, a number of key reforms have been initiated** aimed at improving public financial management and fiscal transparency more generally, although important challenges remain. **The key reforms to address weaknesses in the area of PFM have been**:

Situation in 2003	Key actions taken	Status
1. Outdated PFM legal framework	-*Government Financial Management Act (2004)*: addressed some urgent PFM issues, mainly in accounting, but its coverage remains limited	Revision underway
	-*Public Procurement Act (2003)*: introduced modern procurement processes and standards	Being implemented in 2007
	-*Public Audit Act (2003)*: established independence of National Audit Office	Implemented
2. Limited availability of fiscal information	-strengthened monthly expenditure returns process: significant improvements but still delays of up to two months	On-going
	-improvements in reporting on SAGAs and EBFs: reports more readily available – but information still incomplete and only occasionally published	On-going
	-publication of Quarterly Budget Review on MoF website: available between 2 and 4 months from end of quarter	Implemented, but needs improvement
	-computerization: legacy systems gradually being replaced by modern IFMIS system – roll out to ministries/agencies, districts in second phase	On-going
3. Significant discretionary powers of the Treasury during budget execution	-implementation of stricter limitations on tax expenditures through tightened legal framework and improved controls at KRA	Implemented, but needs monitoring
	-improved cash management: releases based on cash flow projections from ministries/agencies	On-going
	-strengthened accountability of ministries/agencies: less discretionary power at Treasury to make budgetary changes	On-going
4. Significant discretionary powers in personnel policy	-Public Service Commission Regulations 2005: tightened up on qualifications and established procedures for recruitment – greater transparency	Implemented
	-cleanup of payroll: integrated payroll and personnel system introduced, although functioning in decentralized mode	Implemented, but needs further effort
5. Lack of budget realism	-improved fiscal framework: greater reliability of macro-economic forecasts, improved revenue projections, realistic ceilings for budget preparation, MTEF	Good progress made, on-going
	-wider consultation during budget preparation: review of SAGA/EBF budgets, consultation of civil society groups, strengthened budget cycle	On-going

There have also been key reforms in other areas which have helped meet the requirements under the fiscal transparency code. Key legal reforms: (i) the *Public Officer Ethics Act (2003)*, which introduced a code of conduct and compulsory filing of annual declarations of assets and income for public officers; (ii) the *Anti-Corruption and Economic Crimes Act (2003)*, which established the Kenya Anti-Corruption Commission (KACC); (iii) the *Privatization Act (2005)*, which makes a Commission responsible for privatization, thereby increasing accountability and transparency; (iv) the *Statistics Act (2006)*, which established an independent National Bureau of Statistics. In addition, various administrative reforms have been implemented, including outlawing *harambees* (political fund-raising events), establishing a ministerial code of conduct, introducing performance contracts for all SAGAs and SOEs, reforming tax administration (KRA), and simplifying licensing regimes for businesses. **Remaining challenges** include making public the wealth declarations of senior officials, and operationalizing the Privatization Commission and the Pubic Procurement Oversight Authority.

[1]This compared with 8 benchmarks in neighboring Uganda and 11 in Tanzania (www.imf.org).

13. **The overall role of the MoF in fiscal management assigned in both the GFMA and the Constitution is comparatively weak**. *1.2.1*
In particular, the PS for the Treasury is not assigned any significant public financial management (PFM) duties and responsibilities.[15] As a result of this weak position, the MoF has had difficulties over the years in ensuring adherence to the financial regulations, and in particular the Treasury circulars and instructions that it has issued from time to time. To compensate for this weakness, it has developed a consensus and outreach approach to get compliance, which has proved useful in identifying issues. The regulatory framework for new areas such as public-private partnerships (PPPs) has yet to be developed, although this is currently the focus of technical assistance being provided by the World Bank.[16]

14. **Mechanisms for the coordination and management of budgetary and extra-budgetary activities are not adequately defined**. *1.1.3*
There is a significant level of extrabudgetary activity in Kenya,[17] estimated at around 3 percent of GDP (see Box 1), carried out through FAs and SAGAs, some of which, like the Kenya Roads Board or the CDF, are of an extrabudgetary fund nature (Box 4). The number of such entities appears to be increasing for various reasons, including de-linking salary levels from the public service wage constraints and facilitating carryovers for earmarked funding of projects. Many of these entities are established by their own Act of Parliament, with the remainder established by legal notice under the State Corporations Act. SAGAs and EBFs are funded through a mix of transfers from the budget, earmarked taxes, and own revenues. They are governed by their own Boards, on which the Treasury and parent ministry are represented. Since 2004, SAGAs and EBFs have to report their financial operations to the MoF on a quarterly as well as annual basis, although compliance is not complete and the data not widely circulated.[18] Although in principle the budgets of SAGAs are submitted to the MoF well before the finalization of the government budget, and the grants/earmarked funds identified at that stage, they are subject to only limited scrutiny with the main concern being to contain the level of the grants, and not to include them in the policy framework. Another area where spending may not be clearly reported is external grants which provide goods and services in kind, or where payments are made offshore. While these grants are generally reflected in the budget as Appropriations-in-Aid (AIAs), they are not adequately tracked in the accounts, often due to the fact that original documentation is with the donor. The budget documents do not, however, include any annexes summarizing the activities of SAGAs and EBFs.

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[15] It is noteworthy that the Fiscal Management Bill currently before Parliament finds it necessary to empower the PS to collect the information required under that Bill.

[16] The consultants contracted by the World Bank have recently submitted their report on the PPP Policy Framework.

[17] The aggregate spending of fund accounts, SAGAs, EBFs, and regional development authorities is estimated at around Ksh 60 billion (over 10 percent of budgetary resources).

[18] Furthermore, as a result of being grouped together with state corporations of a commercial nature, it is also not possible to identify their deposits in the CBK banking sector surveys, or establish their overall sectoral impact in the statistical publications of the KNBS.

Box 4. Extrabudgetary Spending in Kenya

There is significant spending in Kenya which takes place outside the main budgetary management rules and procedures. This spending, for which resources may be partly or wholly reflected in the budget as earmarked revenues or transfers, occurs within semi-autonomous government agencies (SAGAs) as well as through extra-budgetary funds (EBFs) and Fund Accounts (FAs). Spending from these entities is not included in budget execution reporting for central government, nor in the annual accounts of central government. Set up either under their own Acts or created under the provisions of the State Corporations Act, these entities have their own supervisory boards and financial management rules and procedures including audit. Remuneration of staff for these entities is also generally de-linked from the general public service terms and conditions.

SAGAs and EBFs: the authorities reported 101 such entities to the mission, although the list was already out of date, with several new ones either planned or in the process of being created. As illustrated below, they occur in a wide range of government functions. Some entities perform extrabudgetary fund activities, like the Road Fund, which receives earmarked taxes and distributes these on a formula basis to executing agencies performing road maintenance at the national, regional and local levels. Others, like Hospitals and Universities, are classic autonomous entities, whose spending is mainly funded from budgetary transfers topped up with user fees.

Internal security	1	Trade & industry	6	Law	1
Personnel management	2	Justice & constitution	4	Education	15
Planning	3	Gender, sports, culture & social services	5	Information & communications	4
Regional development	6	Livestock & fisheries	2	Aids	1
Agriculture	4	Water & irrigation	14	National heritage	3
Health	5	Environment	4	Science & technology	8
Roads	1	Cooperative development	1	Tourism & wildlife	6
Transport	3	State corporations	1	Home affairs	1

Fund Accounts (FAs): the 42 reported FAs are mainly separate accounting mechanisms established either by a special Act of Parliament or by government decision, into which specific revenues are channeled for defined activities, again not included in budget execution reporting. The difference from an EBF is that the staff running the FAs are generally part of the public service. FAs generally have a supervisory board and are under the control of a specific ministry. Again there is a wide range of FAs across a number of government functions.

President	3	Health	2	Energy	1
Foreign affairs	1	Roads & public works	1	Electoral commission	1
Home affairs	4	Livestock and fisheries	2	Lands & housing	2
Planning	2	Cooperative development	1	Security	1
Finance	13	National assembly	3		
Agriculture	2	Constitution	1		

Among these FAs is the **Constituency Development Fund** (CDF), established by Parliament in 2003 to increase public participation in identifying needs and selecting projects. The size of the CDF allocation has been set in the CDF Act at 2.5 percent of ordinary revenues, which translates to just under US$0.7 million per constituency. At the national level, the CDF is overseen by a board which includes the PS Treasury, with small committees selecting projects at the constituency level, whose execution is then overseen by the District Development Officer. A number of concerns have arisen in implementation, namely: (a) lack of coordination between CDF, local planning and central government planning—no coordination so far with LASDAP and limited involvement of ministries in CDF project decisions; (b) the recurrent costs of CDF projects are not fully taken into account at the time of project selection—while the CDF Act requires that spending be coordinated with parent ministries, the construction and design of some 1000 dispensaries, done in consultation with the District Medical Officers to ensure compliance with standards, has not ensured provision for staff or running costs in the Health Ministry budget; and (c) there is limited oversight provision and few CDF projects have been properly audited so far.

Table 1. Summary of Budgeting and Reporting Status of SAGAs and FAs

		Included in Budget Documents			Regular and Detailed Reporting		
	No.	Transfers	Earmarked revenues	Expenditures	Transfers	Earmarked revenues	Expenditures
SAGAs	101	Yes	Most	None	Annual	Most	Quarterly
FAs	40	Yes	Most	None	Annual	Most	Annual

Source: World Bank 2004 PEM AAP and Ministry of Finance

The Legal and Administrative Framework for Tax Policy and Administration

15. **The legislative basis for taxation is clear and comprehensive**. *1.2.2*
The tax legislation is clear and comprehensive and administrative guidelines are widely distributed. A tax appeal mechanism has been implemented. The laws are regularly reviewed and updated during the annual budget process. Self-assessment has been a prominent feature of the tax system in Kenya since the 1990s, in particular for income tax (from 1993) and VAT (introduced in 1990). Tax administration has been performed by an autonomous agency, the Kenya Revenue Authority (KRA), for the last 12 years. KRA's internal procedures ensure regular technical reviews of tax rulings, as well as of any contentious issues that may arise, and the preparation of technical briefs clarifying tax issues which are then widely circulated to staff and stakeholders. The tax laws expressly limit the scope for discretionary interpretation by tax officials. Each tax law has its own separate tax procedures code, including appeal, tribunal and recourse to the courts. A common and unified tax procedures code is currently under preparation.

16. **Each tax law clearly identifies exemptions that can be applied, and they are generally not subject to discretion**. *1.2.2*
The tax expenditure is not always assessed as part of the exemption procedure. The KRA strictly applies the exemptions provided for in the various laws, and has been known to challenge exemptions granted by the Minister of Finance that do not conform to these laws. Taxes are mostly levied on ad valorem basis with exception of some excise taxes that are based on specific rates. These specific rates are, however, not indexed for inflation but rather reviewed on an annual basis and adjusted as the need arises. *However, the power of the Minister of Finance and the Commissioners to waive penalties and interest, and to write-off of uncollectible debt tax, is discretionary*. Commissioners are empowered to grant a waiver of penalties and interest subject to a limit of Ksh 500,000 while any requests above that limit require the approval of the Minister.[19] There are very

[19] However, the ability of the commission of customs or the Minister of Finance to waive penalties is not recognized under the East African Community Customs Management Act (EACCMA). Nevertheless, the EACCMA contains a provision to grant the commissioner of customs the power to waive penalties and interest that relate to matters before the commencement of the customs union.

generalized guidelines for writing-off of uncollectible taxes, and criteria for guiding decisions on waivers using a weighted waiver template have been developed by the KRA in consultation with the MoF. Overall this discretionary area is subject of potential abuse both at the MoF and at the KRA, given the punitive nature of the penalty rate imposed on unpaid taxes (set two percent per month).

17. **Tax exemptions are fairly extensive and tax expenditures are not reported**. *1.2.2*

The various tax laws provide for a wide range of exemptions aimed at promoting investment, assisting disadvantaged groups and social causes, and meeting diplomatic obligations. In the customs area, exemptions mainly target food (in particular sugar), while domestic tax exemptions mainly target NGO and charity organizations. These exemptions were estimated by the KRA at about Ksh 15 billion (1.0 percent of GDP) in 2005/06. Conditions that are set and must be met to qualify for exemptions or tax holidays are published and readily available to the taxpayers. Each request for exemptions is individually reviewed by the KRA, to determine whether the set conditions have been met, and discretionary powers are generally limited. The scope for customs exemptions has been limited in recent years by the East African Community Customs Union. While the Commissioners make assessments of the foregone tax for exemptions and tax holidays, only in the case of customs is this done on a systematic basis for forgone tax from exemptions; and this information is not published.

18. **Tax administration is clearly defined and well coordinated with overall fiscal management**. *1.2.2*

There are no limitations in law to tax officials demanding third party information and enforcing collection of arrears. For example, tax officials frequently seek and receive information on banking transactions of taxpayers and this has worked well. The tax administration is functionally-based and is generally in line with best practice recommendations, with the exception of the domestic tax department, which is headed by two commissioners (large taxpayers and other taxpayers).[20] The unique taxpayer identification number (TIN) is used for all taxes and across all revenue departments. For income tax, Kenya has a well established system of Pay-As-You-Earn (PAYE) for government and private sector payrolls, as well as annual income tax returns that are based on self-assessment. Customs and excise duties are reviewed on case-by-case basis. The time taken for KRA to process refunds is variable; also efforts are made to process VAT refunds within 30 days, although refunds that require verification can take up to 60 days. Until recently, the system required each VAT refund to be pre-audited before payment could be made. In July 2007 the KRA moved to a three-pronged approach (payment without audit, payment with post audit, or pre-audit) and is moving to a full risk-based approach for its large taxpayers. The KRA retains part of the take to cover refunds and this was increased from Ksh 900 million to Ksh 1 billion in July 2007. VAT

[20] This creates two accountability centers for the same taxes, and therefore the potential for conflicting rulings. However, this arrangement is seen by the authorities as a means to improve the performance of the offices, allowing for greater specialization and enhanced revenue performance.

withholding arrangements are in place for goods and services delivered to government departments and state corporations, where VAT to be paid to the supplier is instead directly remitted to the KRA.

19. **Tax officials have very limited discretionary authority and there is an elaborate process for handling objections and appeals**. *1.2.2*
Objections/appeals are initially handled by well-established internal mechanisms that are independent of the audit units. Dissatisfied taxpayers can lodge an appeal with independent committees/tribunals (currently each tax has its own appeals committee or tribunal) or go to the courts. The various tax laws set specific time limits for KRA to deal with objections/appeals. A unified tax procedures codes is currently under preparation. KRA has a code of conduct, an internal affairs division that handles matters of integrity and corruption among staff, and a corporate level disciplinary committee. These mechanisms are reported to be working well.

20. **KRA maintains close working relations with the MoF during budget preparation and execution, to ensure effective monitoring of tax revenues**. *1.2.2*
The KRA is a member of the Macro Working Group, and in that function, is closely involved in the formulation of revenue projections in the MTEF. The KRA has a performance contract with the MoF with monthly and tax-specific revenue targets. During the fiscal year, KRA officials regularly meet members of the Economic Affairs Department (EAD) from the MoF to discuss revenue collection so far, and remedial measures if needed. The KRA brings recommendations on tax legislation changes to the attention of the MoF, as needed, for incorporation in the Finance Bill. The KRA is currently funded through a 1.65% fee on tax collections.[21] KRA also acts as a collecting agent for some earmarked and local taxes, for which it charges a two percent fee.

21. **Taxpayers' legal rights are well defined**. *1.2.2*
Taxpayers' rights and obligations are specified in the taxpayers charter. However, this document has no legal standing and therefore has not been a useful tool to protect taxpayers. To ensure coherence in information on the various tax laws provided to taxpayers, as well as to encourage greater taxpayer compliance, taxpayer education, which is seen as an important issue by KRA, has been centralized under the Taxpayer Services Division since 2005. Individual tax laws have their own procedures for administrative review, as mentioned in paragraph 15, including independent committees or tribunals and recourse to the courts. In general, tax administration appears to be applied fairly and the appeals mechanisms seem to be working effectively. The frequency of appeals is low in Kenya. The draft law on tax procedures code, which will provide a unified approach across all taxes, will also entrench some of these rights and obligations in law.

[21] The KRA Act allows for funding up to 2% of collected revenues, but this has been negotiated downwards by MoF.

Public Servants' Code of Behavior and Anti-Corruption Activity

22. **The Public Officer Ethics Act of 2003 establishes a clear legal framework for the ethical conduct of public servants**. *1.2.3*

The Act sets out guiding provisions on ethical conduct, in areas such as improper enrichment, conflict of interest, coerced fundraising (*harambees*), nepotism, and sexual harassment. Ethical behavior of public officers is further governed by the Corruption and Economic Crimes Act which established the Kenya Anti-Corruption Commission (KACC) that is responsible for investigating anti-corruption activities, and for combating corruption in the public service (Box 3). The various Commissions governing government employment[22] are responsible for administering the Act and have codified these provisions into a Code of Conduct and Ethics. The Public Officers Ethics Act of 2003 provides for declaration of assets by senior officers, as well as all persons holding political or judicial function at both national and local level, and board members and chief executives of state corporations. This declaration also extends to their spouses and non-adult children.[23] In addition, wealth declarations of Ministers are subject to verification by the KACC. Failure to comply is made an offence, with provisions for payment of a fine or imprisonment in the Act, and other disciplinary measures are clearly spelled out in the code of regulations. The KACC publishes quarterly activity reports on its website detailing ongoing investigations, court cases and outcomes of completed court cases. It has completed a number of investigations, and cases related to the Goldenberg scandal are currently before the court. The KACC has been slow in concluding the investigation of other prominent cases, including those related to the Anglo-Leasing scandal.[24] The government's overall strategy is elaborated in its Governance Strategy to Build a Prosperous Kenya.

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[22] Commissions include the public service, the teachers, the judiciary, and the parliamentary service. Additional employment groups are members of Parliament, defense, national security and intelligence personnel, and local authority councilors.

[23] A proposal to make public and open to scrutiny the wealth declarations of ministers and senior officials has been made in the form or the Miscellaneous Amendments Bill, but is yet to be passed. Work is ongoing to computerize the information on wealth declarations and link these to income tax returns collected by the tax administration.

[24] The conclusion of investigations into the Anglo-Leasing scandal is waiting closure of foreign investigations, whereas domestic investigations have been finalized.

B. Open Budget Preparation, Execution, and Reporting

The Budget Preparation Process: Clarity and Consistency of Process and Presentation

23. **The annual budget process is generally open**. *3.2.1*
The annual budget cycle, which has been strengthened in the last few years under the MTEF reforms, is well defined and structured, known to budgetary entities, and generally adhered to (Box 5). The process starts early in the fiscal year with ministerial reviews of the budget year just completed. This is then followed by the update of the macro-fiscal framework, discussions on policies and sectoral ceilings, culminating in the preparation of the Budget Outlook Paper (BOPA) in December. Treasury then issues a budget circular, together with the BOPA, which starts discussions in sector working groups on sectoral needs and allocations, which provide the input to sector hearings that will determine the ministerial ceilings that will be formally issued for detailed budget preparation. [25] These, along with the revised macro-economic and macro-fiscal frameworks, are issued in the Medium-Term Budget Strategy Paper (BSP) around April but sometimes even later.[26] The BSP, along with the estimates books, are then submitted to Parliament in June.[27] Since deliberations on the Budget by Parliament start very close to beginning of the fiscal year, following the Westminster tradition, the Budget is not formally adopted until after the start of the fiscal year, sometimes as late as October or November. To cover for this interim period, the Constitution provides for a "vote-on-account", authorizing spending on up to one-half of the submitted budget, which takes place a few days after the budget is submitted. One supplementary budget is typically submitted in the spring to Parliament and voted upon, along with updated estimates' books.

24. **Coordination between development and recurrent budgets is managed through the MTEF process**. *3.2.1*
Ten sector working groups establish recurrent and investment ceilings early on in the budget cycle. Ministry level strategic plans provide an important input into the sector working group deliberations. However, in practice, once the ceilings are established, it is availability of external aid funding that drives many of the development budget decisions, with line ministries negotiating individually with donors to get access to such funds.

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[25] Sector working groups include participation by external stakeholders, such as business groups and NGOs, and also hold an annual public meeting open to any interested member of the public. The sector working group reports are posted on the MoF website (www.treasury.go.ke).

[26] The BSP for 2007/08 was available in June 2007.

[27] Since the reestablishment of the East African Community, the official Budget Day of the founding member countries (Kenya, Tanzania and Uganda) has been synchronized to the second Thursday in June.

Coordination between the two budgets therefore remains a challenge, although progress is being made to improve the coordination, in particular the future recurrent costs of

Box 5. The Budget Preparation Process

Due dates	Activities	Legal basis
The fiscal year is set on a July 1st to June 30th basis by the Constitution. The main steps in the process are as follows:		
August – September	Revision and update of ministerial strategic plans and preparation of ministerial public expenditure reviews	Treasury Regulations and Circulars
September – October	Update of the macroeconomic and fiscal framework, and the preparation of preliminary sector ceilings	’’
October – November	Discussions on policies and ministerial ceilings between the Ministry of Finance and line-ministries and other stake-holders	’’
November-December	Government approval of Budget Outlook Paper	’’
December	Ministry of Finance issues Circular together with the Budget Outlook Paper	’’
January – February	Reports from the Sector Working Groups on funds required for achieving policy objectives	’’
February	Sector hearings with the Ministry of Finance and the Ministry of Planning and Development	’’
February – March	Update of the macroeconomic and fiscal framework	’’
March	Discussion on the revised ministerial ceilings between the Ministry of Finance and line-ministries and other stake-holders	’’
April	Government approval of the Budget Strategy Paper	’’
April	Circulation of the Budget Strategy Paper to line-ministries	’’
April	Submission of itemized budget by line-ministries	’’
April – May	Estimates Working Group review of the estimates for the individual line-ministry	’’
April – May	Budget Procedure Group review of budget estimates	’’
April – May	Budget Steering Committee review of budget estimates	’’
May – June	Submission of budget estimates to Cabinet for possible amendment and final approval	’’
June	Submission of budget estimates book to Parliament and vote on account	Constitution, East African Community
June-Sept/Oct	Parliament debates and approves the budget, usually two or more months after the start of the fiscal year	

investment projects, under the MTEF and the external resource management processes. Although there are separate Ministries of Finance and Planning, the responsibility for preparation of the two budgets is primarily with the MoF, while the Ministry of Planning and National Development focuses on sector planning and monitoring. At the local government level, coordination is achieved through the Local Authorities Service

Delivery Action Plan (LASDAP). There is no coordination, however, between the CDF and LASDAP, and the national budget.[28]

25. **Budget presentation is partly consistent with international standards**. *3.2.1*
The budgetary and accounting classifications include administrative and economic classifications, but do not include functional or program classifications. The economic classifications were upgraded to a GFS 2001 compatible framework in FY 2005/06. The budget includes a sectoral breakdown, but this falls short of a GFS compatible functional classification. Program classification has not yet been developed.

The Macroeconomic Framework and Policy Basis for the Budget

26. **The net domestic financing position and the overall balance of central government are the main indicators of fiscal policy and are closely monitored**. *3.2.3*
Net domestic financing is the government's main indicator of its fiscal policy, and is set in the Budget Outlook Paper during the early preparation stage of the budget. Both the BSP and budget speech clearly indicate the government's target for net domestic borrowing and the overall balance.[29] During the execution stage of the budget, QBRs closely monitor the fiscal situation with an upfront discussion of the overall fiscal deficit, compared to quarterly projections, as well as a detailed discussion on the evolution and composition of the domestic debt and net domestic financing position. Primary and current balances can be calculated from the information in the QBR, and the KNBS publishes, with a delay, annual data on the net operating balance of the central government. However, no reporting takes place on other measures of the fiscal position such as structural or cyclically adjusted balances. No data on the general government balance are available, neither does consolidation with the rest of the public sector take place.

27. **Budget macroeconomic forecasts and underlying macroeconomic assumptions are clearly presented and are generally realistic.** *3.1.3*
The Macro Working Group, which includes representatives of the MoF, Ministry of Planning and Economic Development, CBK, KRA, KNBS and an autonomous government research center, KIPPRA, is responsible for the formulation of a macroeconomic and fiscal framework, typically covering three years. The MoF is the convener of the Macro Working Group meetings and it takes the lead in the preparation of the macroeconomic framework. The Macro Working Group meets as needed, and in the context of the publication of the BOPA and the BSP, where the framework is formulated and subsequently updated and finalized. Members of the working group

[28] Some 1000 dispensaries have been built under the CDF, but these have remained empty due to lack of budget allocation for their operating costs. The Ministry of Health has developed a plan to absorb the recurrent costs from operationalizing these over a three year period, beginning FY 2007/08.

[29] The budget speech, does not mention the public debt target.

present their forecasts using models developed by their respective departments,[30] and a consultative approach leads to the final formulation of the macro-economic framework. This framework is clearly presented in the BOPA and BSP and includes a full elaboration of the real, fiscal, monetary and external sector projections. Assumptions for the upcoming budget are generally realistic, except for those on the implementation rate of foreign-financed development projects. Medium-term projections serve as broad indicators for outer-year budget formulation, but are subject to considerable review. Additional macroeconomic scenarios are included when needed, such as those elaborating the government's Vision 2030. However, supplementary estimates submitted mid-year are not accompanied by an updated macro framework.

Medium-Term Planning and Analysis of Fiscal Risks

28. **A statement on medium-term fiscal policy objectives is included in the budget document, but fiscal sustainability analysis is not presented**. *3.1.1*
The government's medium-term fiscal objective to maintain domestic debt sustainability is clearly stated in all budget documents.[31] The government has so far relied on the joint IMF - World Bank debt sustainability analysis and no long-term financing reports are produced. Recently, however, a draft debt sustainability analysis has been prepared and is currently being finalized.[32] The three-year rolling MTEF is guided by a limit on domestic borrowing, projections for domestic revenues and external resource availability. In this framework, expenditures are limited and sectoral and ministerial ceilings for expenditures are set for year *t*, *t+1* and *t+2*.

29. **Fiscal rules used in the budget process relate to borrowing**. *3.1.2*
Parliament, through a recent sessional paper, has set the limit on the size of external and government guaranteed debt at Ksh 500 billion (27.4 percent of 2006/07 GDP) and Ksh 80 billion (4.3 percent of 2006/07 GDP) respectively but this limit is presently not binding.[33] Under the PRGF arrangement, the government is also committed to refraining from nonconcessional external borrowing. The Fiscal Management Bill, currently with parliament, seeks to limit recurrent expenditure to recurrent revenues of the same year, but this bill has not yet been passed.

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[30] In addition to a financial programming framework used in the MoF, an internal model used by the CBK, KIPPRA uses the KIPPRA-Treasury Macro Model which is a macro-fiscal model that focuses on growth, and the expenditure side of the budget. In addition, macroeconomic assumptions are identified separately, and include assumptions on growth, inflation, changes in the terms of trade, import and export growth, main decisions that affect wage growth, among others.

[31] It is included in the BOPA, BSP and final budget speech.

[32] A debt sustainability workshop took place in May 2007, following which the government is preparing a Debt Management Strategy which includes a debt sustainability analysis, with drafts already circulated for comments.

[33] The Minister of Finance initiates the sessional paper in Parliament. The ceilings were last revised in July 2000.

30. **Estimates of new initiatives and ongoing costs of government policies are not presented in budget documents submitted to parliament, although they are available in sector working group reports which are publicly available**. *3.1.4*
The reports from the sector working groups distinguish between cost of ongoing and new policies, and these are used as inputs into the MTEF. However, while the budget speech highlights the main new budget initiatives, the budget documents submitted to Parliament do not provide detailed quantification of newly introduced tax and expenditure measures. The budget documents also do not include any performance indicators that link budgetary outlays to MTEF objectives, limiting the value of the current MTEF process.

31. **There is a limited discussion in the budget documents on the sensitivity of budget estimates to changes in economic variables and of fiscal risks**. *3.1.5*
The BSP includes a descriptive discussion on risks emanating from changes in macroeconomic and other conditions such as oil prices, weather, investor confidence, delays in the implementation of reforms , political uncertainties, or delays in donor disbursements, but not of other important variables such as lower growth, higher interest rates, or large contingent liabilities that may surface. Risks emanating from delays in privatization and contingency measures are also not consistently included or quantified.[34] The budget does not present a list of externally guaranteed debt, but the annual accounts, audited by the CAG, and reports by the MoF and CBK, as discussed in paragraph 37, do.

Clarity of Control of Budget Execution

32. **Basic accounting and internal control procedures are frequently modified and are not legally enforceable**. *3.3.1*
As indicated in paragraph 12 and Box 2, the provisions in the Constitution related to government financial administration are no longer underpinned by a set of clear and legally enforceable financial regulations. Financial administration is presently governed by a compendium of outdated regulations, known as the Government Financial Regulations and Procedures (GFRP), which date from 1989. Many of the regulations and procedures of the GFRP are no longer followed and the government has made substantial changes in the way it conducts its financial management. Such changes to the regulations as have been introduced have been implemented by circulars issued by the Treasury, which have not yet been codified and which rarely make any reference to the legal authority supporting them, are thus probably not legally enforceable. The current arrangements for budget execution, based on the GFRP, are described in Box 6.

[34] Despite financing of the budget for 2.2 percent of GDP through privatization receipts, the BSP 2007/08-2009/10 does not cite shortfall in privatization proceeds as a risk.

Box 6. Budget Execution Procedures

Issue of budget authority to the spending ministry: After the Appropriation Act is passed, a Presidential Warrant (General Warrant) is issued, which authorizes the Minister of Finance to issue a Treasury Warrant (Annual Estimates Warrant) to the Accounting Officers in the line ministries, which allows them to incur expenditures in respect of the votes for which they are responsible. Treasury Warrants are recorded as Authority-to-Incur-Expenditure (AIE) in the expenditure ledgers maintained for each ministry in the Treasury, and limit commitments (and therefore expenditures) which line ministries may make.

Commitment Control: Commitments are registered in the vote books at the time the line ministry raises a local purchase order (LPO) for the supply of goods and services. The LPO is approved for registration only if the amount proposed for commitment is covered by an AIE. The GFRP (5.5.1 to 5.5.3 and Appendix 15.16.0) prescribes that AIEs are issued for the whole year (in the case of allocations to District AIE) and are to be recorded as commitment in the ministry's account, which is contrary to the procedures being followed by Treasury where AIEs are issued quarterly. Where this is the case, it is unclear which of the two systems is providing internal controls, and whether the systems fully conform to the internal controls currently envisaged in the regulations. Also, annual AIEs and quarterly cash releases may lead to discrepancies which could result in arrears accumulation.

Issue of cash limits: The Treasury transfers cash from the Exchequer Account to the line ministry's account at the CBK to enable them to make payments against commitments. These Exchequer Releases are proposed by the Accountant General and authorized by the CAG. This procedure is different from the one prescribed in the GFRP as the authority to make payments has since been decentralized to Accounting Officers.

Issue of budget authority and cash limits to subordinate offices: Accounting Officers may further devolve budget authority to their offices located in districts by issuing their own AIEs, backed by cash transfers to the commercial bank accounts of their subordinate offices.

Payment: Payment process starts with the receipt of an invoice, which is checked against LPO. Goods received are also verified at this stage. The invoice is approved after exercising the prescribed controls, after which a check is issued. The payment is recorded in the vote book and in the cash book (along with checks details).

Bank reconciliation: The bank sends a statement of cash disbursed against checks presented, and the disbursement is reconciled with the entries made in the cash book.

Computerization: Budget execution is currently complicated by computerized systems running in parallel, as the newer IFMIS is rolled out. There is no clarity as to which system is the basis for exercising internal control during this interim phase.

Source: Ministry of Finance, and GFRP 1989.

33. **While the accounting methodology is generally satisfactory, its application varies across ministries due to weak capacities and an unclear legal framework**. *3.3.1* The reconciliation and clearance of suspense accounts should be completed by the end of the year. However, the Auditor General's findings[35] indicate that there are substantial balances, at the end of the year, in suspense accounts pertaining to outstanding imprest balances with the ministries and departments[36] and district cash fund accounts. The Auditor General has also pointed out instances of discrepancies between the Appropriation accounts and the Statement of Assets and Liabilities submitted by the Vote Holders. The most common irregularities noticed by the Auditor General are poor and inadequately maintained accounting records, material errors in book-keeping such as

[35] The Report of the Controller and Auditor General on The Appropriation Accounts and Accounts of the Funds for the fiscal year 2004/05.

[36] Ksh. 419,770,823 at the end of 2004/05.

double-posting and omission of expenditure from accounts, discrepancies between ledger balances and financial statement figures, lack of analysis of suspense balances, and unidentified balances which are not properly classified.

34. **The legal framework for a Consolidated Fund is in place but the principles of a Treasury Single Account are not being followed**. *3.3.1*
Significant cash balances are still being held outside the Exchequer Account. These are held on accounts managed by line ministries, some 40 public fund accounts[37] (Box 7) and a number of donor-funded project accounts. While some of these accounts are held in the CBK, the bank accounts of district level units of line ministries, as well as a large number of project accounts and some public fund accounts are held in commercial banks. The Exchequer Account held in the CBK is also not functioning as a unitary account. Exchequer releases are held in a Treasury Funding Account with the CBK. From this account, cash is transferred to transitory zero-balanced sub-accounts of individual line ministries every day. At the end of the day the balance remaining in these accounts is returned to the Treasury Funding account. The Treasury Funding Account and the transitory cash balances lying in zero-balanced accounts are not considered a part of the Treasury Single Account. For local governments, cash balances of the General Rate Fund are held in commercial bank accounts, and local governments hold a number of accounts outside the General Rate Fund.

Box 7. Legal Provisions Enabling the Consolidated Fund and Government Banking Arrangements

- Consolidated Fund into which all monies raised or received pertaining to the central government are remitted.	Constitution Art. 99
- No monies can be withdrawn from the consolidated fund without authorization based on constitutional provisions or by an Act of Parliament.	Constitution Art. 99
- General Rate Fund into which all receipts of the local government are deposited and from which all liabilities are met.	Local Government Act Art. 261(1)
- Exchequer account in the CBK to hold the consolidated fund cash balances.	GFMA 2004 Art. 10
- No bank account for government purposes may be opened without the written authority of the treasury.	GFMA 2004 Art. 30

35. **Although part of the large stock of accumulated pending bills identified in 2003 has now been cleared, new pending bills continue to accumulate as controls remain inadequate.** *3.3.1*
The large stock of pending bills inherited by the new government in 2003 has been mostly audited and partly cleared. The stock of pending bills, which are reported in

[37] Constitution Article 99(2): Revenues or other monies received pertaining to the central government of Kenya may be paid into public funds, held outside the consolidated fund, which may be created by an act of parliament. No moneys can be withdrawn from such funds unless authorized by law.

Quarterly Budget Reviews (QBR), was reduced by almost a third by 2004/05.[38] However, new arrears are being created—the QBR reports an increase of Ksh 450 million in 2005/06 over 2004/05. The level of pending bills may be understated, however, since the main source for reporting pending bills in Kenya is the unpaid payment voucher. While pending bills on development spending have been brought under control, given the heightened scrutiny of Kenya's development partners, there is evidence of unpaid bills accumulating under recurrent expenditure, in particular utilities. With the weak internal audit function and the lack of adequate commitment control, the ability of Treasury to accurately establish the extent of unreported pending bills is limited.

36. **The cash flow planning system is functioning well**. *3.3.1, 2.1.4*

Cash flow planning was implemented at the beginning of the FY 2005/06. The system has stabilized now and is working well.[39] The cash flow planning process starts with the submission of annual cash plans by the ministries. During the year, ministries submit rolling three-monthly cash flow plans every month, indicating their cash flow requirements for the following three months. Weekly exchequer releases are based on the rolling cash flow plans submitted and approved by the Exchequer Committee,[40] which meets every two weeks to review the cash situation. The Committee is provided information on cash flows by the following agencies: (i) the Cash Management Unit (of the AGD) presents a summary of the exchequer position showing the funding for recurrent and development expenditures, public debt and pension and gratuities; (ii) the AGD also provides details of the cash and bank balances (separately for recurrent and development votes); (iii) the EAD provides reports on weekly revenue collections after reconciling the figures with the KRA; and (iv) the EAD and Budget Supply Department (BSD) provide budget outturn reports. Based on this information and the proposals of the Cash Management Unit, the Exchequer Committee makes recommendations on the amounts of exchequer releases to be made for the month. The CBK is not represented on the Exchequer Committee, although the CBK and the AGD are in daily contact. Direct inputs from the CBK into the decisions taken by the Exchequer Committee are essential to ensure that the exchequer releases and borrowing requirements are in tandem with the monetary operations and related borrowing of the CBK. The KRA is also not represented on the Exchequer Committee – revenue collection data and likely revenue inflows are provided by the EAD.

37. **Public debt is managed in a transparent manner with the participation of all the stakeholders**. *3.3.1, 2.1.4*

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[38] 2006 PEFA report indicates that pending bills were reduced from Kh 18 billion in 2002/03 to K Sh 12 billion in 2004/05. As a percentage of total expenditures, this represents a decline from 9 percent to 4 percent.

[39] Even though the government was entitled by law to use CBK overdraft facilities up to Ksh 13 billion by end-June 2006 the overdraft was only Ksh 41 million.

[40] The BSD, IAGD, DMD, EAD, ERD, and the DGIPE, as well as the Secretary to Pensions department are represented on the Exchequer Committee, which is chaired by the Finance Secretary.

As indicated in Box 2, government external borrowings are undertaken within the legal framework of the External Loans and Credit Act (1967) and government guarantees are issued under the provisions of the Guarantees (Loans) Act. Under the law, the MoF is responsible for contracting all external debt and for giving guarantees, subject to parliamentary approval. The Internal Loans Act governs the contracting of domestic debt. The Debt Management Department (DMD) is presently functioning as a back office for the settlement and recording of public debt. The DMD also records government guarantees. Front office functions are carried out by the ERD, CBK, and DGIPE. The External Resources Department's (ERD) main role is to service external concessional financing including loans and grants; the management of domestic debt is outsourced to the CBK; and DGIPE manages on-lending of donor funds to public enterprises. A formal debt management strategy has not yet been adopted. Nonetheless, the MoF ensures that the level and rate of growth of public debt is sustainable over time. Gross government domestic debt is published in the CBK's weekly report. The CBK also publishes total gross public external debt and guaranteed external public debt in its Monthly Economic Review (www.centralbank.go.ke). In addition the MoF reports debt data in the QBR, which provides reports on government guarantees and stock of government debt by debt instruments, and by debt holder. Annual reporting by the DMD on public debt management has recently been reintroduced, and the report includes statements on the currency and maturity structure of government debt, the stock of debt, and guarantees. Both these reports are available on the MoF website (www.treasury.go.ke). Domestic debt is only reported for central government, and does not include domestic debt from state-owned enterprises and local governments. Domestic debt arrears are not captured. The Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) is used for recording and reporting domestic and foreign debt transactions, and on-lending.

38. **Annual targets on domestic borrowing are set by the MoF through a consultative process between the MoF and the CBK**. *3.3.1, 2.1.4*

At the start of the fiscal year the CBK is advised by the MoF in writing about the government cash flow forecasts. Thereafter, the CBK draws up the annual program for the issuance of debt and clears it with the MoF. Main instruments of domestic debt are 91 and 182-day T-Bills and Treasury Bonds in maturities of 1 to 15 years. The success of the policy to change the mix of short term to long term T-Bills from 70:30 (in 2001) to 30:70 (in 2006) indicates renewed confidence of the market in Kenyan government securities. The issuance of debt for Treasury operations is managed separately from issuance for purposes of monetary policy, with the CBK bearing the interest costs for the latter. T-Bill auctions are administered by an auction committee chaired by the Governor of CBK and with representation from the MoF. The CBK convenes a market leaders forum every month to determine the perception and requirements of the market.

39. **The legal framework for the internal audit system of the government is weak and fragmented**. *3.3.3*
The Internal Auditor General's Department (IAGD) was established under the provisions of the GFMA 2004. [41] The scope and coverage of internal audit, and the duties and responsibilities of the Internal Auditor General have not yet been prescribed. Internal auditors in the ministries, departments and districts continue to operate under the provisions of outdated Treasury circulars.[42] The PS MoF issued a circular in October 2005[43] revising the mandate and guidelines of ministerial audit committees earlier prescribed in 2000. The PS MoF also issued an internal audit manual in November 2005, which was intended to be a handbook for use by internal auditors in the delivery of internal auditing services in government ministries, departments, and districts. The provisions in the current manual basically replicate international best practices in the area of internal audit. These laws and treasury circulars constitute the weak and fragmented legal basis for the internal audit function.

40. **Internal audit procedures are evolving and are not yet effective in practice.** *3.3.3*
Before the creation of the IAGD, internal audit was carried out within ministries by their own internal audit wings. The IAGD is in the process of consolidating the oversight of the internal audit function by merging internal audit units of individual ministries into a unified internal audit service centralized under the IAGD in the MoF. The IAGD has recently also been entrusted with the oversight of internal audit in local governments from the 1st of July 2007. Total staff component of the department is around 420—each district has two internal auditors and there are up to eight or nine internal auditors in the central government ministries and departments. While internal auditors in some government units continue to conduct pre-audit of each transaction, the internal auditors in most organizations are moving ahead with modern audit techniques such as risk-based audit. However, a study of the pilot implementation of risk-based audit in three ministries has brought out significant deficiencies in the planning and implementation of the reform.[44] Furthermore, internal audit lacks a strategic corporate plan for internal audit reform which would ensure that the reforms are carried out sequentially and in tandem with the capacity of the organization to absorb the reforms.

41. **Internal audit coverage is limited, follow up is weak, and there is little ownership by the management in line ministries and departments.** *3.3.3*
Due to the fact that the procedures are still evolving and the department is being consolidated, the coverage of internal audit is not yet comprehensive. Presently the audit of the IAGD extends to 70 percent of the central government units, while audit

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[41] Section 9(1)(c).

[42] Treasury Circular No. 4 of March 1997 as amended in October 2003.

[43] Treasury circular No. 16/ 2005 of 4th October 2005.

[44] Risk-Based Audit Approach Report on a Pilot Follow-Up: Ministry of Health and Ministry of Planning and National Development October 2005, supported by GTZ.

committees have been set up in 95 per cent of the government organizations to monitor the functioning of internal audit and to follow up on their findings and recommendations. However, the committees are not meeting on a regular basis, minutes of meetings are not consistently recorded, and there is little ownership of the process within line ministries. Mid-year compliance audit reports of the budget execution process have alerted management of the ministries on the slow progress of expenditures and collection of AIAs. Special compliance audit reports have brought out deficiencies in the management of government assets such as stores and vehicles. Findings and reports are not made available to the public but there are moves to acquire software to enable the IAGD to warehouse reports in a single data base and make it accessible to the public through a website.

42. **The new public procurement law and regulations provide a sound basis for open and competitive procurement practices but implementation issues remain.** *3.3.2*
The Public Procurement and Disposal Act was enacted in 2005 followed by the promulgation of the Public Procurement and Disposal Regulations in 2006. The law and regulations apply to the general government sector. They prescribe open tendering process as the preferred procurement method; stringent rules for outsourcing, and disposal of government assets; and, procedures for constituting implementation committees and their functions. Penalties against interference in the procurement process are prescribed in the law. The law allows for the Director General of the Public Procurement Oversight Authority (PPOA) to inspect all procurement proceedings. The Public Procurement Administrative Review Board established by the law has been very successful in reviewing cases brought before it by aggrieved bidders. The prescribed review process is time bound with all stages of appeal and review scheduled to be completed within 104 days of the lodging of the complaint. The procedure also provides for appeal to the High Court which must dispose of the appeal within 30 days of the lodging of the complaint. The PPOA is negotiating MOUs with the CAG, IAG, and KACC to audit the implementation of procurement systems. An assessment of the efficiency of the new act through questionnaires indicates that the level of implementation is satisfactory in ministries and state corporations; however, local authorities still face challenges in the implementation.

43. **The Public Procurement Act is being implemented even though the Public Procurement Oversight Authority has not yet been established.** *3.3.2*
For the time being, while the Public Procurement Department (PPD) within the MoF is implementing the Public Procurement Act from 1st of January 2007, the formal establishment of the Public Procurement Oversight Authority is awaiting the confirmation of the interim Director-General of Public Procurement and the appointment of the members of the Board.[45] The law and procedures have been widely publicized and there is ownership and awareness at all levels of government. The PPD has supplemented the complaints mechanism prescribed by law with direct visits and reviews of minutes of the

[45] This has recently been ratified by Parliament.

meetings of tender committees. The Public Procurement Appeals Tribunal has also been established and there have been 42 cases of appeals under the law since January 2007. Certain provisions of the law have not yet been completely implemented due to lack of capacity. For instance, the annual procurement plans submitted by ministries are being prepared but not yet closely monitored. While all procuring entities are required to file returns on procurements exceeding Ksh 5 million, the PPD is currently not in a position to ensure the completeness of the data submitted by these entities. Data on the use of non-competitive procurements methods is also not fully available with the PPD. The capacity for monitoring and evaluating the implementation of the law is therefore still limited and there are still long lags in web posting of procurement contracts.

44. **Civil service employment procedures are clear and well-understood.** *3.3.2*
The public service, including the procedures for employment and termination, are overseen by the Public Service Commission (established under the Constitution of 1963 and provided for in the Service Commissions Act of 1963) which acts as the official employer for government. The new Public Service Commission Regulations of 2005, established under the Service Commissions Act, define clear and detailed procedures for recruitment, which have also tightened up on the qualification needed for each position to be filled. These regulations are widely available, including on the website of the Public Service Commission. Under the new rules, all positions being recruited for have to be advertised, even where internal promotions are being considered, with interviews and selection undertaken by a recruitment panel which includes a professional for the profession being recruited. Recruitment for upper grades is carried out by the Public Service Commission, while recruitment of lower grades is usually delegated to Accounting Officers. The new rules include an appeal mechanism, as well as an obligation to ensure regional balance in recruitment. The new regulations and procedures have significantly reduced the scope for discretion in decisions related to the management of personnel generally, and recruitment in particular. Remunerations are set by the pay scales, with discretion limited to some types of allowances,[46] which can be quite substantial. However, where discretionary allowances are to be offered for a particular post, the ministry concerned has to make a special case to the Ministry of State for Public Service and Permanent Remuneration Salary Review Board. Similar arrangements are in place for the Teachers, Judicial, and Defense Commissions.

Clarity of Internal Control and Independence of Tax Administration

45. **Tax administration has effective internal monitoring and control mechanisms**. *3.3.3*
Computerization at KRA is subject to on-going improvements, with most departments, routinely using computerized tax administration systems. Major investments to integrate tax administration systems are expected over the next few years. These systems will

[46] The DPM is in the process of rationalizing allowances (about 77 are on the books), but progress so far has been slow.

significantly improve capacity to perform internal monitor and control. There are both internal and external audit departments that ensure financial accountability of tax collection staff and systems. The internal audit department reports to the Board of Directors through a Board Audit Subcommittee. In addition, KRA has established an internal affairs department that handles matters of integrity and corruption among staff. On the question of advance tax liability rulings, there is room for requesting these on particular transactions but these are not legally binding. So far, the authorities have not been keen to introduce legislative amendments that would provide for binding advance rulings on particular transactions.

46. **The Kenya Revenue Authority is given legal protection from political interference**. *3.3.4*
The KRA was established by an Act of Parliament as an autonomous agency under the MoF, subject to the State Corporations Act. Its day-to-day administration is guided by a Board of Directors comprising of representatives from the private sector, the Attorney General, Inspector-General of State Corporations and the Permanent Secretary of the MoF. All public service representatives are ex-officio members with no voting rights.

Accounting and Reporting on Budget Execution

47. **The in-year accounting and reporting system, which is still evolving, remains inefficient and fragmented.** *3.3.1*
The basic recording and accounting framework for budgetary transaction was put in place with the implementation of the Electronic Vote Book system (Legacy) which captures the stages of the in-year budget execution process starting with the issue of monthly exchequer releases and culminating in the issue of checks to suppliers for delivery of goods or services. For in-year reporting purposes the data available through the Vote Book system is supplemented by the actual cash outflow data captured in the cash books of budget entities. This fragmented and limited system is now being replaced with a more comprehensive IFMIS system,[47] although in practice, the ministries are still using the Legacy system for accounting and budget control. In-year reports generated from the Legacy system are communicated through electronic or hard copy medium to the MoF as part of the monthly expenditure returns process. Within the MoF the BSD is responsible for preparing aggregate in-year budget execution reports for expenditure, to which EAD add revenue reports they have obtained from KRA, external flows reports from ERD, and debt reports from DMD, to complete the monthly fiscal tables. The EAD prepares quarterly tables for the QBR (published on the MoF website) from these and other sources. The aggregate cash position is prepared weekly by the AGD, compiled from: (i) returns on exchequer releases; (ii) expenditure returns received; (iii) revenue returns received; and (iv) returns on donor funded projects received from the ERD. There is a

[47] Kenya has chosen the Oracle Financials system for their IFMIS, under a project which started in 2002. Currently IFMIS has been rolled out to 24 line ministries (out of the 43 votes) which have started using the new system from July 2007 for their headquarter-based operations, and operational modules include the general ledger, accounts payable, and purchasing modules.

need to improve and coordinate data processing and sharing within the MoF in order to improve fiscal reporting, and broaden it to general government in due course. For the present, budgetary entities are submitting monthly expenditure returns separately to the AGD, BSD and EAD. The follow up process for monitoring the timely submission of returns is therefore fragmented among these three departments in the MoF. According to Treasury circulars, expenditure returns are to be submitted by the 15^{th} of the following month. Two to three weeks delay is not unusual and there are some cases of delays of up to two months.

48. **Fiscal reporting does not cover all of general government and there are gaps in the coverage of central government in in-year budget outturn reports.** *3.3.1, 2.1.1*
Reporting consolidated general government fiscal data remains elusive, with most reporting and analysis still focused on Central Government data with limited and less frequent reporting on sub-national governments, SAGAs, EBFs and FAs. Data collection arrangements exist, but remain fragmented and untapped for general government reporting purposes. A few local governments fail to comply with the quarterly reporting obligations prescribed under the Local Government Act, making consolidated quarterly reports incomplete.[48] In 2004, the DGIPE established an annual and quarterly data collection system for State Corporations, which includes the bulk of the SAGAs and EBFs. However, compliance with this reporting has been declining, as DGIPE has limited capacity for monitoring and analyzing the data, which is handled manually since DGIPE does not have a computerized recording system. Consolidation of these data, while not impossible, remain a serious challenge, as there is no overarching legal framework for implementing a uniform budget and accounting classification system across the whole of the government sector.[49] Furthermore, the basis of accounting in local governments and state corporations is accrual whereas that in the Central Government it is cash. Moreover, there has been no legal requirement so far for submission of consolidated general government accounts. Separately, there is also no standard format for donors to submit disbursement data but efforts are being made to come to an agreement with the donors on this and other accounting matters.

49. **The legislature receives in-year reports on budget outturn and does undertake a mid-year review which reconciles budget with actuals.** *3.4.1*
As required under the GFMA the Treasury prepares two reports on budget execution,[50] the first report covering the first half of the financial year and the second covering the entire fiscal year. The report sets out the actual expenditures and revenue for the period and compares them with the expenditures and revenues budgeted for the period. Under the GFMA, the Minister of Finance is required to lay out these reports on budgetary

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[48] There is limited follow up of the submission of quarterly reports, which is not tied to transfer of funds under LATF, although the Act provides for the imposition of fines for late submission.

[49] Article 228(4) of the Local Government Act authorizes the Minister of Local Government to prescribe rules for the keeping of Local Government Accounts.

[50] GFMA 2004 Article 29.

performance before the Parliament. The Act does not prescribe any time frame for submission of these reports. However, the mid-year report is the basis for the supplementary budget.

50. **The audited final accounts are not available within the prescribed period of six months of the end of the fiscal year.** *3.4.2*

The legal requirement for submission of audited final accounts to Parliament is within six months of the end of the fiscal year. However, as mentioned in paragraph 65, there was a backlog of submissions of the annual audit reports for FY 2001/02 to 2003/04, which has now been eliminated. The audit report for 2005/06 was submitted to the Minister of Finance in May 2007, a delay of five months. The submissions of audit reports of state corporations and donor-funded projects is current. However, there are long delays in the submission of audit reports of local government authorities.

Results-Oriented Budgeting and Reporting

51. **The objectives and expected results from government activities are defined in broad terms in sector working group papers, but not formalized in the budget.** *3.2.2, 3.4.2*

Budget objectives are defined in the Sector Reports which compare actual performance and achievements with performance indicators developed to evaluate sector outputs. However, these performance indicators are not yet integrated into the budgetary process. The authorities have indicated their intention to moving in the direction of program/performance budgeting over the medium term.[51]

C. Public Availability of Information

52. **Fiscal information is fairly comprehensive and readily available to the public but with a time lag**.

During the formulation and finalization of the budget, published budgetary documents include the BOPA, Sector Reports which in detail discuss performance and achievements, medium-term resource requirements, cross-sector linkages, and emerging issues and challenges, the BSP, and the budget speech read out in parliament. The government does not publish a simplified layman's guide to the budget which could enhance the transparency of the budget and make it more amenable to analysis. However, local authorities have, since the last budget, started organizing public budget hearings on their budgets to improve local community involvement. Reporting on revenue, expenditure, and financing is on a gross and net basis, and transactions are classified by economic and administrative categories, but not by function. The economic classification adopted is compatible with GFS 2001. For the execution of the budget, fiscal information on government operations is published by the EAD in the QBRs. It covers recent economic

[51] The August 2006 FAD TA mission reviewed current practices and laid out a strategy and action plan for the Budget Department to start implementing a program budgeting approach over the next few years.

developments including economic growth, inflation, balance of payments, foreign exchange reserves, exchange rate, money and credit, interest rates, and capital markets; fiscal developments including fiscal outturn, revenue, expenditure, pending bills, guaranteed loans, and, external and domestic financing of the budget; public debt including the overall debt position, domestic debt, external debt; and outlays on core poverty programs. However, comprehensive budget outturn information for SAGAs State Corporations and Local Governments is not included. QBRs are published on the MoF website, but are usually available with a two-or-three month time lag: the QBR for the second quarter 2006/07 was published in March and the QBR for the third quarter 2006/07 was published in May 2007.

The Coverage and Quality of Budget Documents

53. **The budget documents cover central government fiscal activities comprehensively but provide no data on general government.** *2.1.1*
The following budget documents were laid before Parliament in June 2007: (i) the BSP; (ii) the Revenue Estimates Books, which details the tax and non-tax receipts to be collected in the budget year; and (iii) the two sets of Estimates Books, two books each for recurrent and development, in which the details of each vote in the Budget are provided by administrative (sub-vote, head and sub-head) and economic (item level) classification for the next three years. The BSP lays out the key macro-economic indicators, and macro-fiscal framework, key policy initiatives and government priorities, and three-year aggregate forecasts of resources and spending, as well as highlights of important initiatives in each sector and accompanying summary tables. The Estimates Books provide data only, although Ministries do provide explanations of their budgets during the budget hearings. The BSP, the Budget Speech, and a number of other documents containing fiscal data are published on the MoF website. The Estimates Books can be bought from the government printer.

54. **Defense expenditures are included in the budget, but only in aggregate.** *2.1.1*
The Defense and National Security Intelligence Service budget is included in the annual estimates, although the bulk of the spending is shown as a one-line item. Not included in the budget or under any reporting under the State Corporations Act, however, are state-owned defense industries. They are, nevertheless, subject to external audit by the Controller and Auditor General, as is the Ministry of State for Defense itself. Receipts collected by the Ministry of State for Defense are shown as AIAs, the bulk of these relating to peace-keeping operations.

Past and Forecast Fiscal Data in the Budget

55. **The detailed budget only provides data on the budget year and two years beyond the budget year, although actual data is included in aggregate presentations.** *2.1.2*

The Estimates Books provide current year approved budget, current year revised estimates, proposed budget, and two outer years' projections. It does not include past year's actuals or current year's estimated outturn. The accompanying BSP presents summarized provisional actual data for the previous year, as well as initial and revised budget for the current year and likely outturn, proposed budget and projections for two outer years along key economic items such as wages, interest payments, pensions, defense, development, and financing. In addition, the BSP presents summary analysis tables by sector and vote, as well as a table identifying poverty-reducing expenditures.

Budget Treatment of Off-Budget Fiscal Activity

56. **Government guaranteed debt is reported, but other statements on contingent liabilities are not included in budget documents**. *2.1.3*

Contingent liabilities, with the exception of guaranteed debts, which are disclosed in the government's financial accounts as audited by the Controller and Auditor General and in reports by the Central Bank and the Ministry of Finance (see paragraph 36 and 57), are not well reported nor quantified, but are potentially very significant, especially in the area of pensions and also in state-owned enterprises. Total publicly guaranteed debt as of end-June 2005 was Ksh 18 billion.[52] However, past problems of debt management, especially those related to the so-called Anglo-Leasing contracts, may increase this number. In the area of pensions, the central government, which currently operates a pay-as-you-go pension scheme for its civil servants, has accumulated claims in the order of Ksh 271 billion (25 percent of 2004/05 GDP), according to an August 2005 actuarial study. In parastatals, defined benefit pension schemes had an accumulated deficit of Ksh 28.6 billion. In addition, the National Social Security Fund (NSSF), which pays out lump sum contributions at retirement age of non-civil service workers in the formal sector, had an accumulated deficit of Ksh 16.7 billion at end-June 2006. Other contingent liabilities in state-owned corporations are difficult to assess due to the fact that the monitoring of their financial position is currently done manually, making early detection of fiscal risks difficult. However, the recent and ongoing restructuring of the National Bank of Kenya and Kenya Telkom provide examples where contingent liabilities surface to significant amounts. The DGIPE is conducting a study on contingent liabilities in 24 state-owned enterprises and in the NSSF. Overall, contingent liabilities could be close to 20 percent of GDP. Once it implements its PPP policy, the government will also face the challenge of assessing and reporting contingent liabilities that may arise from PPPs.

57. **Statements on tax expenditures are not included in the budget documents**. *2.1.3*

There is currently no comprehensive assessment of tax expenditures, although according to the KRA, the amounts are significant. Commissioners make assessments of foregone

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[52] The latest published audited accounts for the government are those for FY2004/05. However, a recently completed survey of all public and publicly guaranteed debt in parastatals suggests that outstanding debt at end-June 2006 amounted to Ksh 43.5 billion, which includes Ksh 18.4 billion on account of the National Bank of Kenya (NBK), and Ksh 6.5 billion on account of Kenya Telkom. In May 2007, the government has taken over the guaranteed debt to the NBK through issuance of a Ksh 20 billion special purpose bond, mostly related to parastatals that defaulted on their loans to the NBK. The government is also in the process of restructuring Kenya Telkom and will, in the process, take over some Ksh 11 billion of its contingent liabilities, apart from other restructuring costs.

taxes on a continuous basis, but these are not consolidated nor reported, and also not included in the budget documents.

Publication of Data on Debt and Financial Assets

58. **Information on gross government debt and financial assets is published regularly**. *2.1.4*

Gross government debt is published both by the CBK and the MoF in weekly, monthly and quarterly reports, as discussed in paragraph 37. Information on government financial assets is published by the MoF as a part of the annual Appropriation Accounts. In addition to information about central government cash balances with the CBK and cash balances in special fund accounts, there is information on investment by the government in local companies, and participation in quasi-government organizations and other statutory organizations. Information on on-lending is also available in the Appropriation Accounts. Similar information is required to be published by local governments in their annual accounts.

Commitment to Timely Publication of Fiscal Data

59. **Formal commitments for more regular publication of fiscal data have not been made and advance release calendars are not announced**. *2.2.1, 2.2.2*

It is not currently a legal requirement to publish fiscal data. However, the MoF publishes a number of key budget documents and QBRs on its website, as earlier discussed in paragraph 52. While there are quality questions remaining, and advance release calendars are not available, Kenya meets or exceeds the GDDS recommendations for serviceability and timeliness of all disseminated data.[53]

D. Assurances of Integrity

Integrity of Data Processes

60. **Budget data are still not reliable and the variance between budgeted and actual outturn of main fiscal aggregates is published but with a time lag**. *4.1.1*

The accuracy of revenue estimates has improved significantly in the last two years. The reliability of expenditures, on the other hand, is mixed, with reasonable accuracy in aggregate recurrent spending but significant variance in aggregate development spending. Variance between budgeted and actual recurrent spending at sector and vote level however is slightly more significant. Variance in spending is shown in Table 2. Actual budgeted versus outturn data is available in the 4th Quarter Budget Review, with a lag. This outturn data is however based on expenditure returns, which includes a significant component of unreconciled accountable advances to districts, and may differ significantly from the final accounts submitted to the CAG, which usually occurs after the QBR for the

[53] Kenya Data ROSC – IMF, October 2005.

fourth quarter has already been published. Final accounts are not made available until the CAG has completed the audit and reports are printed and tabled in Parliament, which has been more than one year after year end in recent years. However, provisional data from the final accounts submitted to the CAG is used internally in the MoF, and is included at aggregate level along key fiscal aggregates such as wages, interest, pensions, defense, other recurrent, and development spending in documents such as the BOPA which is generally issued mid-year.

Table 2: Variance Between Budgeted and Actual Outturns—2002–06[54]
(In percent)

CG Budget excluding CFS	2002-03		2003-04		2004-05		2005-06	
	Aggr.	Comp.	Aggr.	Comp.	Aggr.	Comp.	Aggr.	Comp.
Total	1.51	14.87	3.13	13.33	16.34	0.38	3.54	4.34
Recurrent	*4.68*	*5.08*	*1.35*	*14.21*	*5.98*	*5.67*	*6.95*	*7.01*
Development	*24.85*	*16.53*	*20.24*	*12.73*	*42.70*	*0.00*	*30.73*	*13.89*

*(1) Composite **sector** variance calculated using prescribed PEFA methodology for Indicator 2.*

Analysis of differences is included in the annual ministerial budget review undertaken at the start of the budget cycle, and feeds into the sector working groups as budget preparation progresses. These working group reports are made available on MoF website, though the impact in Parliament is limited as the Parliamentary Accounts Committee still has a two-year backlog in looking at audited accounts. Supplementary budgets are submitted to Parliament every year to reflect the not insignificant changes that are made during the year.

61. **Statements on accounting policy are not included in the budget and final accounts documents**. *4.1.2*
The GFMA 2004[55]authorizes the Treasury "to establish accounting procedures and system for the government to properly account for government money and property". However, there are no provisions in the GFMA or any other law or regulation that prescribe the authority competent to set public sector accounting standards. In practice, central government accounts are maintained on a cash basis while accounts of other entities of the general government such as state corporations and local authorities are maintained on an accrual basis. The procedures for recording transactions on a cash basis are prescribed in the Government Financial Rules and Procedures of 1989. These procedures are not being uniformly applied as is evident from the accounting and recording deficiencies pointed out by the Auditor General (paragraph 33 above).

[54] These calculations, which are based on original budget versus actuals, differ from the 2006 PEFA report, which used revised budget data instead of original budget.

[55] Article 4 (b).

62. **The process of accounts reconciliation with bank accounts is effective but there are delays in clearance of suspense balances booked in accounts**. *4.1.3*
The reconciliation between budget appropriations and accounts in the budget entities is carried out automatically through the application software (both the Legacy and the new IFMIS). In the Legacy system the reconciliation with bank accounts is done regularly with reference to transactions recorded in the cash book but this process is manual. IFMIS provides an automated facility to carry out this reconciliation. While a majority of ministries submit their reconciled accounts within a month there are instances of delays due to late receipt of bank statements by the budget entities. The reconciliations are not shown explicitly in accounts. At the aggregate level, the AGD reconciles the transactions on the Exchequer Account reported by the CBK, with the exchequer releases and the actual revenue inflows recorded in accounts. The reconciliation and clearance of suspense accounts should be completed by the end of the year. However, the CAG's findings[56] indicate that there are substantial balances, at the end of the year, in suspense accounts pertaining to outstanding imprest balances with the ministries and departments.[57] Instances of discrepancies between the Appropriation accounts and the Statement of Assets and Liabilities submitted by the Vote Holders have also been documented. Debt and deficit data are reconciled in the DMD.

Independent Oversight

63. **Kenyan National Audit Office (KENAO) is independent of the executive and the legislature**. *4.2.1*
The KENAO draws its authority from the Constitution, which establishes the office and defines its responsibilities. It also provides for the independence of the office and mandates its powers. The CAG is appointed by the President. The CAG may be removed from office only under specific circumstances defined in the Constitution and only by the President on the recommendation of a tribunal. The emoluments of the CAG are also determined under an Act of Parliament. The Public Audit Act of 2003 established the Kenya National Audit Commission (KENAC) which approves the budget of KENAO and determines the remuneration and other terms of appointment of staff of KENAO. For issues related to human resources management the KENAO functions under the authority delegated by the Public Service Commission. The Public Audit Act of 2003 (PAA) makes it mandatory upon the government of Kenya to ensure that the KNAO has the staff the CAG believes necessary to properly carry out the prescribed audit functions.[58] The KENAO has not yet adopted the performance contract mechanism. However, ways of implementing a performance contract system without affecting the independence of the KENAO are being examined.

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[56] The Report of the Controller and Auditor General on The Appropriation Accounts and Accounts of the Funds for the year 2004/05.

[57] Ksh. 419,770,823 at the end of 2004/05.

[58] Public Audit Act, Section 35.

64. **KENAO's statutory mandate extends across all components of finances of the general government sector**. *4.2.1*
Under the PAA, KENAO is mandated to audit all central government ministries and departments, local authorities, semi autonomous government agencies, special funds, extra budgetary funds and state corporations. The mandate covers all entities for which the holdings of government and other public corporations is more than half the total equity. KENAO is independent of any other authority in carrying out its prescribed functions. [59] The PAA provides wide ranging powers to the KENAO to enable it to access documents and property, and the right to demand explanations.[60] The PAA also authorizes the CAG to conduct performance audits. However, not many such audits have been undertaken.

65. **The timeliness of submission of audit reports has improved but challenges pertaining to delays in legislative scrutiny are still being addressed**. *4.2.1*
The CAG is required to submit audit reports to the Minister of Finance. The Minister of Finance is required to table audit reports in the National Assembly not later than seven days after the Assembly meets after receiving the report from the CAG. The law provides for direct submission of the audit reports to the National Assembly in the event of delays by the Minister of Finance in tabling reports.[61] The PAA requires the CAG to submit the audit report within six months after the end of the financial year. The Law also permits the National Assembly to extend the due date. There was a backlog of submissions of the annual audit reports for FY 2001/02 to 2003/04, which has now been eliminated. The audit report for 2005-06 was submitted to the Minister of Finance in May 2007—a delay of five months. The submissions of audit reports of state corporations and donor funded projects is current. However, there are inordinate delays in the submission of audit reports pertaining to local government authorities. Delays are due to limited resources available with the CAG and the poor quality or non-existence of accounting and financial statements of local governments. Delays also persist in the examination of government accounts by the Public Accounts Committee (PAC) and Public Investment Committee (PIC). There are proposals to amend the Standing Orders of Business of the national Assembly so that more than one annual audit report can be discussed at the same time. There are also proposals to enable the parliamentary committees to discuss the most recent report before dealing with the backlog.

66. **The requirement for state-owned corporations and local governments to pay a fee for the conduct of statutory audit may create a conflict of interests**. *4.2.1*
The PAA requires state owned corporations and local governments to pay audit fees as determined by the CAG.[62] The Act prescribes that the fee shall be decided by the CAG.

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[59] Public Audit Act, Section 46.

[60] Public Audit Act, Section 37.

[61] Public Audit Act, Section 11(3).

[62] Public Audit Act, Sections 19 and 28.

The payment of audit fees for the conduct of statutory audit may create a conflict of interests as no authority other than the CAG is empowered to conduct a statutory audit. The international best practice in such cases is to clearly state the various components of the fee structure and to provide for a process of arbitration in case the client does not agree with the fee proposed. These should be included in the PAA.

67. **Audit capacity is currently not fully adequate for the KENAO to address its functions adequately**. *4.2.1*
The number of Financial Statements to be audited including statements of Assets and Liabilities of the Ministries are: (a) Central Government entities 237; (b) Local Authorities 175; (c) State Corporations and SAGAs 167, and (d) Donor funded project accounts and Special Fund Accounts 116. The audit work is to be completed within three months to meet the prescribed deadline for the submission of the Annual Audit Report by 31st December. In addition to financial audits the KNAO is mandated to conduct value for money audits and special purpose audits such as investigative audits, procurement audits and audit of internal control systems. Presently KENAO has a staff of 915 (722 Auditors and Examiners and 193 Administrative and Support Staff) as against an authorization of 1300. KENAO's ability to exercise its functions efficiently is hampered by capacity weaknesses, however, particularly in the areas of computerized and performance audit.

68. **The legislature discusses external audit reports but there are delays in the follow up on audit findings**. *4.2.1*
The PAC and the PIC review the audit reports. All audit reports are publicly available. There are inordinate delays in the submission of audit reports and the review of reports by the legislature as described in paragraph 64 above which have reduced the effectiveness of this oversight function.

69. **The KENAO and Parliament are taking measures to improve public availability of information on audit procedures and audit reports.** *4.2.1*
KENAO has recently created a website (www.kenao.go.ke) for posting the audit reports pertaining to the central government, state corporations, local authorities and specialized audits. The website is still being developed and the content is presently limited to general information about KENAO. The Parliament has recently passed a resolution to open the proceedings of the PAC to the public, in line with a regional parliamentary initiative.

70. **External scrutiny of macroeconomic assumptions is encouraged**. *4.2.2*
During the budget process,[63] as part of public hearings on key sectors organized by the government, a discussion of the macroeconomic framework also takes place. Since the 2006/07 budget, outside experts have been invited to chair the discussion or serve as discussants on the macroeconomic framework hearing. The formulation and estimation of the KIPPRA-Treasury Macro Model, which is used as an input into the final formulation

[63] Sector hearings take place after finalization of the BOPA, but before the preparations of the BSP. Sector hearings took place in March during the formulation of the 2007/08 budget.

of the macroeconomic framework, is described in several KIPPRA publications which can be requested through the KIPPRA website (www.kippra.org),[64] and the underlying database to conduct simulations is available upon request. In addition, the BOPA and BSP are presented to development partners, even though delays in their formulation may limit the potential for meaningful feedback.

71. **The national statistics office is given legislative assurance of autonomy**. *4.2.3*
Under the Statistics Act (2006) the Central Bureau of Statistics was replaced in July 2007 by the Kenya National Bureau of Statistics (KNBS), established as a SAGA under the Ministry of Planning and National Development. The new KNBS is overseen by a board of directors. In collecting, compiling and publishing economic and financial data, the KNBS is guided by explicit provisions under the Act for public access and dissemination of information.

II. IMF Staff Commentary

72. **Kenya meets some of the requirements of the fiscal transparency code**. Kenya has made significant progress since 2003 in improving fiscal transparency and accountability. The introduction of key legislation, including the Public Officer Ethics Act, the Anti-Corruption and Economics Crimes Act which sets up the KACC, the Public Audit Act, the Government Financial Management Act, the Public Procurement and Disposal Act, the Privatization Act, and the Statistics Act, establish important building blocks for the construction of a sound fiscal management system. These and other initiatives and practices have helped Kenya comply with some of the requirements of the fiscal transparency code. However, a great deal more is needed to establish a sound PFM system and conform with best international practices.

Clarity of Roles and Responsibilities

- The fiscal roles of the executive, legislature, and judiciary are clear and enshrined in the Constitution, and relations between the Central Government and local government are well defined in law and in practice. However, most government-owned NPIs (including SAGAs and EBFs) have traditionally been classified together with state-owned enterprises under the State Corporations Act, creating a lack of clarity between government and the rest of the public sector. This lack of clarity also extends into areas of information collection, making it difficult to accurately establish the full extent of extra-budgetary spending or to clearly define general government consistent with GFS principles. Furthermore, the steady growth in the number of SAGAs and EBFs is a matter of concern. There is, therefore, a pressing need to clarify the status of SAGAs and EBFs.

[64] KIPPRA Discussion Papers No. 11 and 16, and KIPPRA Working Paper No. 5.

- Relationships between central government and public nonfinancial and financial corporations are generally clearly defined. Regarding quasi fiscal activities (QFAs), while public corporations are generally compensated for carrying out QFAs and these are, for the most part, reflected in their budgets, the total value of subsidies is difficult to determine from available information in the central Government's budget, raising concerns of transparency and parliamentary accountability.

- The legal framework for management of public funds is neither clear nor comprehensive. The Government Financial Management Act (GFMA) 2004 is the only general PFM act at this time but it has very limited coverage of key areas of government financial management and does not take into account important reforms implemented in recent years (e.g., MTEF, new budget classification, new approaches to internal and external audits, and the introduction of finance officers). Moreover, the PS Treasury is not assigned any significant PFM duties and responsibilities. As a result of these, the MoF has had difficulties in ensuring adherence to financial regulations and other instructions. The FAD PFM mission of August 2006[65] noted that the legal framework for PFM in Kenya requires significant revision to bring it in line with international best practice and to incorporate recent reforms. This view is also reflected in the authorities' own PFM reform strategy adopted in the second half of 2006. The recent work on updating the GFMA[66] has included broad consultations with a wide range of stakeholders outside the Ministry of Finance, although so far these consultations have not included the Parliament. The authorities face the pressure to conclude the current drafting, however, as a legislative proposal (the Fiscal Management Bill) by a member of Parliament is currently awaiting final reading in Parliament. There is an urgent need to initiate a dialogue between the government and the Parliamentary Committees on the legislative framework for PFM management in order to arrive at a comprehensive and operationally clear bill.

- The legal and administrative framework for tax policy and administration is generally sound. The legislative basis for taxation is clear and comprehensive and tax administration is clearly defined and well coordinated with overall fiscal policy. The tax administration is functionally based and is generally in line with best practices, with the exception of the domestic tax department, which is headed by two commissioners (large and other taxpayers), which created two accountability centers for the same taxes, and therefore the potential for conflicting rulings. While the current dual system appears to be functioning efficiently, consideration should be given to a structure based on best practices over the medium term. Each tax law has its own tax procedures code and there is a need to unify them. There is, however, a wide range of tax exemptions under the law and tax expenditures are not quantified

[65] Kenya – Strengthening the Budget and Fiscal Reporting System: a Reform Agenda. Khemani, Ramachandran, Ljungman and Shall, January 2007.

[66] FAD through AFRITAC East has been providing technical assistance in upgrading the GFMA and financial regulations since October 2006.

nor reported. Tax officials have very limited discretionary authority over exemptions but tax commissioners have an overall discretion in granting waivers on penalties and interest. Taxpayers' legal rights are well defined and they have recourse to administrative reviews and tribunals.

- The Public Officer Ethics Act establishes a clear legal framework for the ethical conduct of public servants, including a requirement for senior public officials to prepare a declaration of assets, which is supported by the Anti-Corruption and Economic Crimes Act and the KACC, which also verifies wealth declarations of ministers and publishes a quarterly report on its activities on its website.

Open Budget Preparation, Execution and Reporting.

- The annual budget process is generally open and the budget documentation is partly consistent with international standards. The annual budget cycle, which has been improved in recent years under the MTEF reforms, is well defined and structured, communicated to budgetary entities, and generally adhered to, even though there are delays in the preparation process. Coordination between the planning and budgeting functions, which are split between two ministries in Kenya, seems to be working well. However, the cycle does not allow Parliament to adopt the budget before the start of the fiscal year. Budgetary and accounting classifications include administrative and economic classifications, but do not include functional or program-based classifications.

- Budget forecasts and underlying macroeconomic assumptions are clearly presented within a medium-term framework and have been generally realistic over the last two years. An area where further improvement is needed, however, is in the budget forecasting of development expenditures, both domestically and foreign financed. The government's medium-term fiscal objectives are clearly stated in budget documents but analysis of fiscal risk is lacking. There is a need to perform sensitivity analysis and discuss contingent liabilities, including in particular, those related to government pension schemes. Going forward, there is also an urgent need to develop proper accounting and risk analysis capability for PPP arrangements, as initiatives are already underway in this area.[67]

- Basic accounting and internal control are not underpinned by a set of consistent and legally enforceable financial regulations. The legal framework for a consolidated fund and banking arrangements are in place. There are, however, many bank accounts outside of the control of the Treasury, with significant balances. At the same time, the cash-flow planning and the debt-management systems have been efficiently managed thus contributing to a more effective budget execution. However, assurance of the transparency and openness of the budget execution process through a rigorous internal

[67] A World Bank Policy Framework consultant's report on PPPs has recently been issued and is being studied by the authorities.

audit system is not yet fully enabled. The legal framework for the internal audit system of the government is weak and disjointed. Internal audit procedures and mandates are still evolving from the earlier mandate for pre-audit to more modern concepts such as risk-based audit and performance audits. As a result, the coverage of internal audit is limited; follow up is weak with very little overall effectiveness. There is a need for a strategic corporate plan to address the capacity, skills and ownership issues related to the implementation of modern internal audit techniques, in a systematic and sustained manner.

- The public procurement law and regulations provide a sound basis for open and competitive procurement practices. Outreach activity has been effective and there is awareness at all levels of government of the new modalities. Also, the Public Procurement Administrative Review Board established by the law has been successful in reviewing cases of aggrieved bidders. However, the implementation of certain key provisions, including the establishment of the Public Procurement Oversight Authority, has been slow thus impeding the full operationalization of the new system.[68]

- Civil service employment procedures are clear and well understood. The new Public Service Commission Regulations of 2005 defined under the Service Commission Act, define clear and detailed procedures of recruitment and these are widely available. The new regulations have significantly reduced the scope for discretion in decisions related to personnel management.

- The tax administration has effective internal monitoring and control mechanisms and the KRA is given legal protection from political interference.

- The accounting and reporting system is still evolving. Fragmented legacy systems are slowly being replaced by a modern IFMIS. At the same time, coordination and data sharing between MoF departments is still lacking. Regular fiscal reporting is also essentially limited to central government, and audited annual accounts are not available within the prescribed period. Audit reports for local governments are substantially in arrears.

Public Availability of Information

- Fiscal information on central government is fairly comprehensive and readily available to the public but with some delay. There is no simplified “citizens’ guide” to the budget. Local authorities have begun with the 2007/08 budget to have live presentations of their respective budgets to their inhabitants, which has enhanced public awareness of budgetary programs and should help to enhance accountability. As noted earlier, no consolidated data on general government are available.

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[68] Before closing its 2007 session, the Parliament had approved the Advisory Board of the Public Procurement Oversight Authority.

- Information on gross government debt and financial assets is published regularly. Government guaranteed debt is reported but other statements on contingent liabilities are not included in the budget documents nor are statements on tax expenditures included in budget documents.

Assurances of Integrity

- Budget data are still not reliable. The accuracy of revenue forecasts has improved significantly in the past few years but reliability of expenditure data remains mixed; there is reasonable accuracy in aggregate recurrent spending but a significant variance in aggregate development spending. Statements on accounting policy are not included in the budget and final accounts documents. In practice, central government accounts are maintained on a cash basis while local government accounts, as well as those of SAGAs and state-owned enterprises are on an accrual basis.

- The KENAO is independent of the executive, and its statutory authority extends across all components of the general government sector. The timeliness of the submission of audit reports has improved but significant backlogs persists in reports pertaining to local governments. Reviews of audited accounts by the Parliamentary committees are conducted with delays of three–four years, which dilutes the effectiveness of the independent audit function. Audit capacity is currently not adequate for the KENAO to fully address its functions adequately including the performance of value-for-money audits.

73. **The main areas where further improvements are required include**:

High priority

74. **Kenya needs to put in place the building blocks for PFM reform**. The authorities, with support from development partners, issued a PFM reform strategy and action plan in 2006 (Box 8). The following recommendations, some of which have been treated in greater detail in the August 2006 FAD mission TA report, support this reform strategy.

75. **The legal framework for public finance management should be revised and made more comprehensive than in the GFMA adopted in 2004**. Unlike the current GFMA, the revised GFMA, or Organic Budget Law, should ideally cover all areas of PFM, and apply to all parts of government (Central Government, Local Government, SAGAs, EBFs, and FAs). In principle, the new law should aim to strengthen the technical management of PFM, and in doing so, vest primary responsibility for oversight of PFM in Kenya in the PS Treasury. Ideally, it should also incorporate the elements of the Fiscal Management Bill, within its general guiding principles, and in the government's reporting obligations to Parliament. It should be noted that while the elements of the Fiscal Management Bill are indeed important, they are not sufficient in themselves to create the new standards of PFM needed at this time in Kenya, and in particular, expected by Parliamentarians.

Box 8. Kenya's new PFM Reform Strategy

The MoF, in collaboration with Kenya's development partners, prepared in 2006 a comprehensive PFM reform strategy and action plan. Funding for this plan has been agreed at US$114 million over a five year period, a coordinator has been appointed and responsibilities assigned for each component. In broad terms, the PFM reform plan stresses the need to clarify PFM roles within government, professionalize staff involved in PFM, and strengthen the legal framework for PFM, in order to underpin the government's overall vision of sustained economic growth and poverty reduction, improved service delivery and good governance.

The components and their key objectives are list below.

Component	Manager	Objectives
Macro-fiscal policy & Planning	*Economic Affairs Department*	To develop a macroeconomic model and refine the macro framework for the budget, improve revenue estimation and capability to analyse effects on poverty.
Budget Preparation and Formulation	*Budget Supply Office*	Develop budget document which is comprehensive and from which the government's priorities and policy changes are explained and possible to identify, and which is developed within a multi-year framework. The document shall be built upon the provisions from the district level and from which the government's priorities and policy changes are explained and possible to identify.
External Resources	*External Resources Department*	Enhancing coordination of external finance with the budgetary process through establishment of reporting procedures, databases and forum for dialogue, ensure exhaustiveness of resources accounting for better predictability and budget statistics.
Debt and Guarantee Management	*Debt Management Unit*	Develop and implement a debt management strategy and debt database. Deepen the domestic market for government securities.
Taxes, Customs and Excise	*Kenya Revenue Authority*	Improvement of customs administration and risk management, improvement in effectiveness of domestic tax administration, and improved taxpayer education
Budget Execution	*Accountant General's Dept., Exchequer unit*	Develop and implement improvements in the cash based release system to obtain better predictability for spending units, improved commitment control and increased efficiency throughout the public sector.
Accounting and Reporting	*Accountant General's Department*	Review of the legal and regulatory framework, accounting and reporting system, development of a professional cadre, institutional arrangements for reporting, records management and filing, monthly reporting and bank reconciliations
Payroll and Pensions	*Dept. of Personnel Management, Pensions Dept.*	Develop and implement personnel databases, payroll and pension systems integrated with the financial management system.
Procurement	*Public Procurement Directorate*	Develop and implement new legal and regulatory framework, create professional cadre, establish workable institutional arrangements, support internal control and commitment control and provide expertise to the MDAs to implement their plans and budgets through procurement for better cash management
Parliamentary Oversight	*Public Accounts Committee*	To develop the capacity of the Parliament to play its oversight role in public resources management. Legislative scrutiny of the annual appropriations bill and review of external audit reports
External Audit	*Controller and Auditor General's Office*	Review and amend legal framework, Develop regulations and manuals, establish policies, expand scope of professional cadre and train, review institutional arrangements, develop mechanisms for upgrading methodologies.
Internal Audit	*Internal Auditor General's Office*	Develop regulations and manuals, establish policies, develop and train, review institutional arrangements for greater independence, support management in implementing reforms
Electronic Services Delivery (IFMIS, IPPD)	*Accountant General's Department*	To improve public expenditure management through an on-line integrated financial management system in order to improve accuracy and timeliness of financial reporting and to enhance both transparency and accountability
Consistent Legal Framework for PFM	*Ministry of Finance*	To review and harmonise existing legislation on PFM and in the broader context of Public Sector Reform. To build capacity to undertake legislative reforms relating to PFM
Capacity Building and Service Conditions	*Min. of Finance HRD unit, Inst. of Public Accountants Kenya, Inst. of Internal Audit, Universities*	Review the Kenyan Accountancy Regulations, develop training curriculum, develop and promote public finance specialisation, Promote international standards, Revised Conditions of service for PFM staff

The PFM reform Plan has been operational since late 2006, although progress to date has been slow, with the exception of activities which had started before the adopted of the Plan.

76. **Budget execution, accounting and internal audit need to be given a firmer legal and institutional basis**. The new GFMA will allow the replacement of outdated government financial regulations and procedures with a new framework aimed at

strengthening and enhancing the relationship between MoF staff and their counterparts in line ministries and elsewhere in government. In particular, the new financial regulations should clearly define the following, among others: (i) the duties and responsibilities of the Accountant General in all matters related to accounting and reporting of government financial transactions; (ii) the various stages of budget execution controls and the assignment of responsibilities for exercising these controls; and (iii) the duties and responsibilities of the Internal Auditor General and internal auditors, as well as the audit committees. The regulations will need to be supplemented with manuals in the various areas, giving detailed guidelines and procedures in each area, which can be used as source materials to train staff in the new legal environment. To be effective, the new legal framework will need to be backed up by credible and enforceable sanctions and penalties. The internal audit area would also benefit at this stage from the preparation of a strategic corporate plan to guide its effective introduction throughout government.

77. **Steps should be taken to consolidate the Exchequer Account to function as a TSA of the government.** The authorities should address the buildup of significant cash resources being held outside the control of the Treasury,[69] by introducing a TSA approach in which all cash is consolidated and managed efficiently by a professional cash managers in the Treasury, all the while delivering cash to users on a just-in-time principle using the latest banking techniques, in particular electronic funds transfers. This work should start with a full survey of all government bank accounts, including donor-funded project accounts, and the establishment of a time bound program to progressively incorporate the operations of each account under the TSA before closing it. The TSA should be underpinned by an effective treasury general ledger system which will manage user sub-accounts under the TSA in a transparent and efficient manner, building on the software that is planned to be implemented by the CBK.

78. **The concept of general government should be clarified and embodied in the law**. The authorities should make the clear distinction between state corporations which perform a non-profit government service delivery or regulatory function, and those that are essentially commercial in nature. Under GFS, the former belongs to general government while the latter belongs to the rest of the public sector. The next steps will be to formalize this distinction by: (i) including the appropriate definitions of general government and public sector in relevant laws, in particular the new GFMA; and (ii) establishing different treatment for each, with respect to PFM, regulatory oversight, banking statistics, and government finance statistics. Once this is completed, and effective and appropriate reporting is established, the authorities should consider routine inclusion of general government fiscal reports in the QBR, and the preparation of consolidated general government annual accounts.

[69] The latest figures published in the March 2007 QBR indicate that government deposits in the banking system exceed Ksh 73 billion, or around 3.5% of GDP.

79. **The growth of SAGAs and EBFs should be tracked and carefully managed and their spending control procedures and reporting strengthened**. The proliferation of these entities, which currently weaken the transparency, scrutiny and prioritization of government spending, should be subject to careful consideration by the authorities. The recent growth of these entities, which is unlikely to be sustainable in the long run, has: (i) increased the percentage of public resources that are not considered together with, and in the same policy framework as, the annual budget; and (ii) become a major disincentive for the rest of the public service to perform. For that reason, the government should carefully review whether: (i) the currently operating SAGAs can still be justified; (ii) agree on strict guidelines for the conditions under which new SAGAs can be created; (iii) clarify the division of responsibilities and establish procedures to improve coordination; (iv) engage SAGAs and EBFs more in the MTEF and budget formulation and execution processes, including of spending through CDF; and (v) strengthen the regular reporting from SAGAs and EBFs. Earmarked revenues assigned to SAGAs and EBFs should also be periodically reviewed to determine whether the level of resources they provide is appropriate. Regarding CDFs, coordination with government planning should be enhanced, recurrent costs ought to be taken into account in the project selection process, and oversight and audit functions of their activities should be reinforced.

80. **The coverage, reliability and relevance of in-year accounting and reporting needs to be improved**. The ongoing efforts to computerize budget execution and accounting (IFMIS) should be completed as a matter of urgency. The arrangements for collection of in-year information on budget execution should be improved so that once IFMIS becomes operational and its rollout is completed, the Accountant General's Department (AGD) should be made primarily responsible for the collection, consolidation and timely provision of in-year information on budget execution to all users within the MoF and beyond. In-year reporting provided by the AGD should also include the debt position and the wage bill of general government. The timely submission of monthly and quarterly reports related to accounts should be included in the performance contracts of the Vote Holders and heads of other institutions of the general government. The reports received in the AGD should be reviewed and a monthly assessment of the trends in budget execution presented by the AGD to the PS Treasury.

81. **The effectiveness of Parliamentary oversight needs to be enforced by ensuring that the follow up of audit findings by Parliamentary Accounts and Investment Committees are timely and sustained**. The backlog of accounts to be submitted to the CAG and the backlog of audits completed by the CAG should be cleared as fast as possible (in the case of Local Authorities, this may require some decisions on the question of opening balances). Present delays in the completion of audits are undermining the efficacy of external audit as an instrument of assurance of integrity. The present procedures for processing and printing reports for presentation to parliament and the timetable for discussion in parliament should be reviewed and bottlenecks identified and removed. The government should also be encouraged to cooperate with Parliament on a timetable to clear the backlog of accounts to be reviewed by PAC and PIC, to ensure that the work of these two essential committees become current as soon as possible. There

is a need to put in place rules and procedures which prevent the delays in processing and follow up of audit findings in future.

82. **Contingent liabilities need to be carefully quantified and taken into account in the context of government borrowing decisions, and policies to mitigate these implemented**. Significant macro-fiscal risks arise from the lack of a clear quantification and reporting on contingent liabilities. The BSP could usefully include a yearly estimate of contingent liabilities and updated fiscal sustainability analysis, and government borrowing decisions should be taken in that context. In the area of pensions, in view of the sharply rising liabilities of the current pension system for civil servants, alternative pension schemes need to be considered. A mechanism to continually assess contingent liabilities in state-owned enterprises as well as other fiscal risks needs to be established. A first step in this direction would be the compilation and sharing of data collected on a quarterly and annual basis from state corporations.

83. **Other urgent tasks include**: (i) establish the Privatization Commission; (ii) establish a legal and institutional framework for PPPs and develop appropriate capacities to assess risks in PPP arrangements; and (iii) implement all provisions of the Public Procurement Act; (iv) finalize and make public the report of the closing committee on pending bills; and (v) identify all quasi-fiscal activities and transparently report the compensation for them in the form of subsidies that are subject to normal budget procedures.

Other important areas, some of which may take time

84. **The budget should be adopted *before* the start of the fiscal year**. It would be helpful to review and agree with Parliament a set of actions that would enable them to adequately scrutinize and debate the budget within a timetable that would allow it to be voted before the start of the financial year. The proposals in the Fiscal Management Bill could be a starting point for discussion but these may need to be supplemented by other actions on the broader legal framework under the new GFMA. Also, a more timely release of the Budget Strategy Paper is needed to allow early discussion on the budget framework.

85. **Continue to improve the credibility of the budget**. The government should continue to undertake measures aimed at improving the quality of the budget, as well as its in-year monitoring, so that the budget can be executed as planned, thus limiting the need for supplementary budgets each year. In the short term, it should carefully review the share of donor commitments to be included in the development budget, and align this with expected disbursements and project implementation capacity. In the medium term, it should improve the allocative efficiency of the budget by adopting program and performance budgeting techniques.

86. **The composition of the Exchequer Committee should be reviewed with a view to broadening its membership to include CBK and KRA representatives.** The CBK is the banker to the government and also entrusted with the responsibility of recording and managing domestic debt requirements. The presence of a representative of the CBK on

the exchequer committee will ensure better coordination between the cash requirements of the government and the monetary operations of the CBK. Similarly, KRA representatives could usefully provide the Exchequer Committee with accurate information on developments at the revenue side.

87. **The information in Budget documents could usefully be enhanced and made user-friendly**. The following recommendations are made:

- add actuals, or even 'provisional' actuals, for last year in the detailed estimates, which would greatly enhance the analysis of trends in spending;

- include a statement of tax expenditures and subsidies as a Budget Annex (care should be taken not to misclassify subsidies in the Estimates Books);

- include a statement of outstanding debt, guarantees and contingent liabilities as a Budget Annex;

- include a summary of the operations of SAGAs, EBFs and FAs;

- identify all quasi-fiscal activities, and transparently report and explain these in the BSP;

- include a fuller discussion of fiscal risks in the BSP, preferably with some quantification of the major risks or a description of contingency measures to be taken;

- include summaries of employees by agency and grade, with total costs (consideration should also be given to discontinuing the current practice of including in the Estimates Books the detailed listing of employees under each Vote);

- expand the range of budget summary tables, e.g., add summaries by economic and functional classifications;

- prepare a "citizen's guide" to the budget.

88. **Some reforms underway in the area of revenue administration should be completed**. A unified tax procedures code should be adopted and disseminated to simplify and streamline tax procedures and give greater clarity on taxpayer's rights. Similarly, the work already underway to prepare clear procedures for granting waivers on tax arrears, with a view to limiting discretion, should be completed. The KRA would do well in ensuring that, over the medium term, the current arrangement in the Domestic Tax Department (DTD), which has two Commissioners, is replaced with best-practice recommendations to have only one accountable head of the DTD. VAT withholding arrangements need to be phased back in a gradual manner.

89. **The capacity to analyze information on public servant's wealth declarations need to be enhanced**. Periodic analysis of wealth declarations and their comparison with tax returns should be initiated. In addition, it would be in line with best-practice to make wealth declarations of ministers and senior officials public.

Other issues for the medium term

90. **Outer year forecasts need to be enhanced in the MTEF**. While the immediate focus should be improving the credibility of the budget year, work can also begin on improving the quality of outer year forecasts by: (i) improving the macro-fiscal projection models; and (ii) strengthening the strategic planning, as well as general planning, capacities in the MOF and within line ministries.

91. **Move towards performance audits**. The government has implemented MTEF and is considering moving towards the implementation of program/performance based budgeting. If these reforms are to be effective in the long run, the accounting and audit systems should also evolve to provide the monitoring, feedback and evaluation essential to output focused allocation of resources. Audits reports should include a report on the economy, efficiency and effectiveness of government expenditures which assesses and comments on the achievement of performance targets and indicators. This will require new training programs for auditors to include specialized audit techniques, such as value for money and performance audits. Such changes will need to be carefully planned and sequenced, to ensure maximum benefit is derived.

III. Summary Tables

Table 3. A Summary Assessment of Practices

Code Reference	Summary Assessment	Comment
Clarity of roles and responsibilities		
1.1	***The government sector should be distinguished from the rest of the public sector and from the rest of the economy, and policy and management roles within the public sector should be clear and publicly disclosed.***	**Largely not observed**
1.1.1	General government is not defined consistently with Government Finance Statistics (GFS) principles.	The concept of general government should be clarified and embodied in law.
1.1.2	The fiscal roles of the executive, legislative and judicial branches are clearly defined in the Law and the responsibilities of different levels of government are clearly defined.	
1.1.3	Mechanisms for the coordination and management of budgetary and extra-budgetary activities are not adequately defined.	Coordination is complicated by the large and growing number of Semi autonomous government agencies (SAGAs).
1.1.4	Relationships between central government and public nonfinancial and financial corporations are generally clearly defined, but include some quasi-fiscal activities (QFAs). The CBK has operational independence and a limited fiscal role, and profit transfers from the CBK are clearly regulated by the CBK Act.	
1.1.5	Arrangements regulating profit transfers from public financial and nonfinancial corporations to the budget are defined by their respective Boards.	
1.1.5	Privatization, which has until recently been guided by the Privatization Policy Paper of 1994, is now to be managed under clear principles set out in the Privatization Act of 2005.	The Privatization Commission needs to be established to operationalize the Act.
1.2	***There should be a clear legal and administrative framework for fiscal management.***	**Largely not observed**
1.2.1	The legal and administrative framework for public finance management is neither clear nor comprehensive.	A new organic budget law is needed to put in place building blocks of

Code Reference	Summary Assessment	Comment
		PFM reform.
1.2.1	The overall role of the MoF in fiscal management assigned in both the GFMA and the Constitution is comparatively weak.	
1.2.2	The legislative basis for taxation is clear and comprehensive. Tax exemptions are generally not subject to discretion, but they are fairly extensive and tax expenditures are not reported. KRA maintains close working relations with the MoF during budget preparation and execution, to ensure effective monitoring of tax revenues. Taxpayers' legal rights are well defined.	
1.2.3	The Public Officer Ethics Act of 2003 establishes a clear legal framework for the ethical conduct of public servants.	Wealth declarations should be made public.
Public availability of information		
2.1	***The public should be provided with full information on the past, current, and projected fiscal activity of government.***	**Largely observed**
2.1.1	The budget documents cover central government fiscal activities comprehensively but provide no data on general government. Defense expenditures are included in the budget but only in aggregate. There are gaps in the coverage of central government in in-year budget outturn reports.	The growth of SAGAs and EBFs should be carefully managed and their reporting strengthened. In the medium-term, reporting on general government should be introduced.
2.1.1	Fiscal information is fairly comprehensive, but available with a time lag.	The timeliness of QBRs has improved in the last year.
2.1.2	The detailed budget only provides data on the budget year and two years beyond the budget year, although actual data are included in aggregate presentations.	
2.1.3	Government guaranteed debt is reported, but other statements on contingent liabilities are not included in budget documents.	Contingent liabilities need to be carefully quantified and taken into account when making government borrowing decisions.
2.1.3	Statements on tax expenditures are not included in the budget documents.	
2.1.4	Public debt is managed in a transparent manner with the participation of all stakeholders.	
2.1.4	Information on gross government debt and financial assets is published regularly.	
2.2	***A commitment should be made to the timely publication of fiscal information.***	**Largely not observed**
2.2.1	Formal commitments for more regular publication of fiscal data have not been made.	The timeliness of QBRs has

Code Reference	Summary Assessment	Comment
		improved in the last year.
2.2.2	Advance release calendars are not announced.	
Open budget preparation, execution, and reporting		
3.1	***The budget documentation should specify fiscal policy objectives, the macroeconomic framework, the policy basis for the budget, and identifiable major fiscal risks.***	**Largely observed**
3.1.1	A statement on medium-term fiscal policy objectives is included in the budget document, but fiscal sustainability analysis is not presented.	A debt sustainability analysis is under preparation.
3.1.2	Fiscal rules used in the budget process relate to borrowing. Annual targets on domestic borrowing are set by the MoF through a consultative process between the MoF and the CBK.	
3.1.3	Budget macroeconomic forecasts and underlying macroeconomic assumptions are clearly presented and are generally realistic.	
3.1.4	Estimates of new initiatives and ongoing costs of government policies are not presented in budget documents submitted to parliament, but are available through sector working group reports.	Program budgeting could be introduced in the medium term.
3.1.5	There is a limited discussion in the budget documents on the sensitivity of budget estimates to changes in economic variables and of fiscal risks.	
3.2	***Budget information should be presented in a way that facilitates policy analysis and promotes accountability.***	**Largely not observed**
3.2.1	The annual budget process is generally open, but the budget is not generally adopted until after the start of the fiscal year.	The budget should be adopted before the start of the fiscal year.
3.2.1	Coordination between development and recurrent budgets is managed through the MTEF process.	
3.2.1	Budget presentation is partly consistent with international standards. Spending through semi-autonomous government agencies, extra-budgetary funds, and fund accounts is not recorded in budget documentation.	Budget documentation should include a summary of the operations of SAGAs, EBFs amd FAs.
3.2.2	The objectives and expected results from government activities are defined in broad terms in sector working group papers, but not formalized in the budget.	
3.2.3	The net domestic financing position and the overall balance of central government are the main indicators of fiscal policy and are closely monitored.	

Code Reference	Summary Assessment	Comment
3.3	***Procedures for the execution and monitoring of approved expenditure and for collecting revenue should be clearly specified.***	**Largely not observed**
3.3.1	The in-year accounting and reporting system, which is still evolving, remains inefficient and fragmented.	IFMIS should be further introduced to the districts.
3.3.1	Basic accounting and internal control procedures are frequently modified and are not legally enforceable, and the application of the accounting methodology varies across ministries.	
3.3.1	The legal framework for a Consolidated Fund is in place but the principles of a Treasury Single Account are not being followed.	Steps should be taken to consolidate the Exchequer Account into a TSA.
3.3.1	New arrears continue to accumulate as controls remain inadequate.	
3.3.1	The cash flow planning system is functioning well.	
3.3.2	The new public procurement law and regulations provide a sound basis for open and competitive procurement practices but implementation issues remain and the Public Procurement Oversight Authority has not yet been established.	The Public Procurement Oversight Authority needs to be established.
3.3.2	Civil service employment procedures are clear and well-understood.	
3.3.3	The legal framework for the internal audit system of the government is weak and fragmented, and internal audit procedures are still evolving and are not yet effective in practice.	A firmer legal basis for internal audit is needed as a building block for PFM reform.
3.3.3	Internal audit coverage is limited, follow up is weak, and there is little ownership by the management in line ministries and departments.	
3.3.3	Tax administration has effective internal monitoring and control mechanisms.	
3.3.4	The Kenya Revenue Authority is given legal protection from political interference.	
3.4	***There should be regular fiscal reporting to the legislature and the public.***	**Largely observed**
3.4.1	The legislature receives in-year reports on budget outturn and does undertake a mid-year review which reconciles budget with actuals.	
3.4.2	The audited final accounts have been delayed beyond the prescribed period of six months of the end of the fiscal year.	The backlog of audits has been recently cleared.
Assurances of integrity		
4.1	***Fiscal data should meet accepted data quality standards.***	**Largely not observed**
4.1.1	Budget data are still not reliable and the variance between budgeted and actual outturn of main fiscal aggregates is published but with a time lag.	
4.1.2	Statements on accounting policy are not included in the budget and final accounts	

Code Reference	Summary Assessment	Comment
	documents.	
4.1.3	The process of accounts reconciliation with bank accounts is effective but there are delays in clearance of suspense balances booked in accounts.	
4.2	***Fiscal information should be subjected to independent scrutiny.***	**Largely observed**
4.2.1	External audit is independent of the executive and the legislature, with a mandate across all components of the general government sector, but audit capacity is not fully adequate.	
4.2.1	The timeliness of submission of audit reports has improved but challenges pertaining to delays in legislative scrutiny and in following up on audit findings remain. The KENAO and Parliament are taking measures to improve public availability of information on audit reports.	Accountability will be significantly enhanced with more timely discussion and follow up of audit findings.
4.2.2	External scrutiny of macroeconomic assumptions is encouraged.	
4.2.3	The national statistics office is given legislative assurance of autonomy.	

Table 4. Public Availability of Information—A Summary

	Budget and fiscal report element	Included in budget/report documents	Available to the public	Para. ref.	Code ref.
1.	Central government (CG) budget estimates	Yes	Yes, printed estimates can be bought from government printer; summary available on internet. http://www.treasury.go.ke	52, 53	2.1.1
2.	CG Defense Expenditures	Yes	Yes, as above.	54	2.1.1
3.	CG EBFs (including special development funds, social security funds, resource revenue funds)	No. Only CG transfers to EBFs are included in CG budget.	No.	14, 53	2.1.1
4.	CG Budget outturns	Yes. QBR and BSP has broad categories of revenues, expenditures and financing, available for past two years.	Yes, available on internet. http://www.treasury.go.ke	52, 59	2.1.2
5.	CG Budget forecasts	Yes. BSP has broad categories of revenue, expenditures and financing for 3-year forecast.	Yes, available on internet. http://www.treasury.go.ke	55	2.1.2
6.	CG Contingent liabilities	No.	No.	56	2.1.3
7.	CG Tax Expenditures	No.	No.	57	2.1.3
8.	CG QFAs	Partly. Compensation for QFAs is included in budget.	No.	4	2.1.3

	Budget and Fiscal report element	Included in budget/report documents	Available to the public	Para. ref.	Code ref.
9.	Macroeconomic assumptions	Yes, in BSP.	Yes, available on internet. http://www.treasury.go.ke	27	3.1.3
10.	Analysis of fiscal risks/sensitivity analysis	No.	No.	31	3.1.5
11.	CG Debt	Yes. QBR and budget documents include detailed composition.	Yes, available on internet. http://www.treasury.go.ke	37, 58	2.1.4
12.	CG Financial Assets	Yes, in annual appropriation accounts. Ministry of Finance is responsible.	Yes, available from government printer.	58, 60	2.1.4
13.	Sustainability Analysis	No.	No.	28	3.1.1
14.	General government budget estimates	No.	No.	48, 53	2.1.5
15.	CG Monthly/quarterly reports on fiscal outturn	Yes. QBR is available about 2 months after the end of the quarter.	Yes, available on internet. http://www.treasury.go.ke	52, 59	3.4.1

	Budget and Fiscal report element	Included in budget/report documents	Available to the public	Para. ref.	Code ref.
16.	General government Monthly/quarterly reports on fiscal outturn	No.	No.	48, 53	3.4.1
17.	CG Final Accounts	Yes. Annual appropriation accounts are submitted to parliament with audit report of Controller and Auditor General, but with delay.	Yes, available from government printer.	60	3.4.2
18.	Consolidated general government Final Accounts	No.	No.	48, 53	3.4.2