

Towards Strengthening Public Financial Management in County Governments in Kenya

Introduction

The Kenya Institute for Public Policy Research and Analysis (KIPPRRA) in collaboration with the World Bank undertook the first sub-national Public Expenditure and Financial Accountability (PEFA) assessment in six selected County governments in Kenya, namely: Nakuru, Kajiado, Baringo, Makueni, West Pokot and Kakamega. The PEFA assessment framework is based on seven (7) pillars, namely: (i) budget reliability; (ii) comprehensiveness and transparency; (iii) management of assets and liabilities; (iv) policy-based fiscal strategy and budgeting; (v) predictability and control in budget execution; (vi) accounting and reporting; and (vii) external scrutiny and audit. The assessment was carried out for three fiscal years; that is, 2013/14, 2014/15 and 2015/16 financial years.

The objective was to assess the Public Expenditure Management (PFM) systems rather than to evaluate and score the performance of specific County governments or individuals. The findings of the study provide a baseline of the current state of PFM within the counties and for the entire system, and indicates areas that require improvement. The assessment may also be used to determine whether the reforms and action plans in the County governments need to be adjusted in facilitating fair distribution of resources to enhance economic development and poverty reduction across the entire country as envisioned in Kenya Vision 2030 and the Constitution.

The results provide an entry point in strengthening the PFM systems at county level. Effective PFM systems foster fiscal discipline, strategic resource allocation, and efficient use of resources for service delivery.

Key Findings of the PEFA Assessment

Reliability of budgets

Whereas county governments implemented the budgets in accordance with the approved estimates, expenditure performances were lower than budgeted

for most counties, especially during the first year of implementation of devolution. Expenditure deviations were largely attributed to delays in disbursement of funds by The National Treasury, long procurement processes, unrealistic estimates due to human capacity constraints, and structural weaknesses in the financial and accounting systems.

The main sources of revenue for the County governments are equitable share, conditional grants and own source revenues. The equitable share constitutes about 84% of total County government revenues compared to 9.8% and 6.2% for conditional grants, and own source revenues, respectively. Thus, County government operations are heavily reliant on transfers from the National Government resources, with very limited own-source revenues.

Own-source revenues performed poorly mainly because of delays in automation of revenue collection, cases of delays in passage of finance bills in some counties, over-projection of non-specified revenues, lack of valuation rolls to determine appropriate property rates, low compliance rates, and pilferage due to weak revenue collection systems.

To expand the tax revenue base, counties are preparing valuation rolls, upgrading infrastructure to improve tourism revenues, and strengthening management and regulation of parking charges. To improve on compliance, there are ongoing efforts to automate revenue collection, training and improving the terms of service for revenue collectors, and sensitizing the public and private sector on County governments revenue generation programmes. Further, to enhance capacity, some counties have entered into agreements with the Kenya Revenue Authority (KRA) to collect revenues on their behalf.

Comprehensiveness and transparency of public finances

The key focus is on comprehensiveness of budget and fiscal risk oversights, and accessibility by the public to the fiscal and budget information. Generally, County governments have adopted the GFS/COFOG standard of budget reporting

which allows transactions to be tracked through the budget's formulation, execution and reporting cycle according to administrative unit, economic category, function, or programme. They also engage public participation during budget preparation and approval processes of the annual budget in various forms, albeit with shortcomings.

Implementation of the Integrated Financial Management Information System (IFMIS) and its integration with other IT-related PFM packages has been slow, and has affected timely preparation of budget implementation review reports, and oversight on implementation. Budget documentation is hardly sufficient to provide a complete picture of the County government fiscal forecasts, budget proposals, and outturn of the current fiscal years. The County governments generally use programme-based budgeting (PBB) that shows performance plans for service delivery. However, many do not articulate indicators for outputs and outcomes, and the allocation of resources to specific programmes is not guided by clear economic analysis on investment projects and other activities before financial resources are deployed. Counties also lack Monitoring and Evaluation Units but rather rely on Evaluation Committees or hire independent agencies to carry out performance evaluation.

Management of assets and liabilities

Effective management of assets and liabilities is necessary to ensure public investments provide value for money. Most counties do not identify nor monitor fiscal risks associated with adverse macroeconomic situations, financial positions of public corporations, and contingent liabilities. In addition, County governments are yet to develop effective tools for economic analysis of projects, standard procedures and rules for project implementation and establish Monitoring and Evaluation Units/Departments. Some counties have, however, devised alternative methods of offering car loans and mortgages to Members of County Assembly (MCAs) and other county officials. Of the six (6) counties assessed, only West Pokot has established the M&E Unit in 2016/17. Management of non-financial assets is also a major challenge in many counties, and those counties that have records have not undertaken age and value analysis. Effective management of assets and liabilities is further undermined by delays in transferring assets and liabilities from the defunct local authorities to the counties.

Policy-based fiscal strategy and budgeting

Although counties prepare their budget documents including the CFSP, CBROP and budget estimates in line with the Public Financial Management Act 2012, they neither carry out independent macroeconomic forecasting nor undertake macro-fiscal sensitivity analysis due to technical capacity gaps and lack

of baseline data. The revenue and expenditure forecasts are largely unrealistic, though in line with MTEF requirements. In a few cases, budget preparation does have sufficient information in advance, including budget ceilings. Besides, not all County governments align their strategic plans to the medium-term budgets and to Kenya Vision 2030 framework.

Predictability and control in budget execution

Revenue raising measures relating to county taxes, licenses, fees and charges and provisions for the general administration of raising revenue are in force. Most counties have automated or are in the process of expanding automation of revenue collection streams to increase coverage and minimize revenue pilferage and make monthly or bi-monthly reconciliations after the bank statements are received.

However, the County governments do not have a formalized redress handling mechanism, and individual complaints are mainly channelled to the Chief Officers in person or through common interest groups. In addition, there is no documented risk management system for revenue collection across all the counties, including a comprehensive, structured and systematic approach for assessing and prioritizing compliance risks.

The counties prepare stocks of expenditure arrears by composition on a monthly, quarterly and annual basis. However, the expenditure arrears are not categorized by age and composition. Regarding personnel, county governments use the Integrated Personnel Payment Database (IPPD) management system to generate monthly payroll and staff payslips. But none of the counties has an approved staff establishment and hire new employees on need basis. They also use existing staff levels and projected hires as a basis for the annual budget. On procurement, most counties kept records about items procured, value of procurement and procurement method. However, the accuracy and completeness of the data cannot be ascertained. Different procurement methods are used, including open tendering, request for quotations, direct procurement and restricted tendering as provided in the Public Procurement and Asset Disposal Act, 2015.

Accounting and reporting

Most counties generally adhere to the stipulated timelines where bank reconciliations for all active County government accounts take place monthly. But some counties continued to operate bank accounts of the defunct local authorities in contravention of the provisions of the County Government Public Finance Management Transition Act 2013. The counties apply International Public-Sector Accounting Standards (IPSAS) cash which

include a summary statement of appropriation, the original budget and the adjustments in line with the laws of Kenya. Meanwhile, the Public Accounting Standards Board in Kenya is designing a framework for all County governments to move to accrual-basis IPSAS. Overall, poor IFMIS connectivity affects timely preparation of budget implementation review reports and oversight on budget implementation.

External scrutiny and audit

The external audit and scrutiny by the legislature do not hold the County Governments accountable for their fiscal and expenditure policies and their implementation as currently undertaken. The public finances are independently reviewed by the OAG but the external follow-up on the implementation of recommendations for improvement by the executive is not efficient with long delays in issuance and scrutiny of audit reports. The delays are quite often occasioned by low staff levels at the OAG as well as the back and forth between the OAG and the counties in correction of errors identified in the submitted financial statements. The scrutiny by the county assemblies, the Senate and National Assembly seldom result in corrective actions by the executive, nor is their work transparent to the public. Thus, the external audit is not effective to enable adjustments and corrections in the PFM system.

Major Constraints and Challenges

Expenditure and revenue deviations

Expenditure deviations in the counties are mainly attributed to: (i) delay in the disbursement of funds from the National government; (ii) procurement delays related to capital projects; (iii) low collection of own source revenue; (iv) technical and human capacity constraints in relation to budget preparations and execution; (v) procurement delays that create a mismatch between the procurement plan and the implementation; and (vi) poor IFMIS connectivity. On the revenue side, discrepancies were largely attributed to: (i) inaccurate forecasts for own revenues as evident by low collection of own source revenues; (ii) disconnects between donor agreements and the budgets; (iii) poor revenue collection systems; and (iv) inadequate sensitization of revenue payers.

Poor management of assets and liabilities

Some counties have not yet established asset registers showing an inventory of all assets by market rate value and age. Besides, there has been a slow pace of transfer of assets and liabilities from the defunct local authorities to the County governments. Incomplete transfer of assets and liabilities has made it difficult to clearly establish the amount of debts

and pending bills inherited from the defunct local authorities.

Capacity gaps in implementation of the PFM system

The key gaps include lack of and/or weaknesses in macroeconomic forecasting, macro fiscal sensitivity analysis, and assessment of impact of fiscal policies, with clear underlying assumptions; lack of consistency of MTEF budgets; low absorption of development expenditures, which is largely hampered by inadequate technical capacities to prepare bill of quantities (BQs) and supervising projects; weak capacities to carry out economic analysis of investment projects to identify the costs and benefits of every investment proposal; and weak internal audit systems because of low staffing levels and skills. In addition, the focus of the internal audit is mainly on compliance and regulatory issues and is not yet developed to provide full oversight (of all budget users) of the effectiveness of the internal control system.

Revenue and expenditure arrears

Most county governments do not keep proper records of revenue arrears, except for land rents and house rents, making it difficult to ascertain the value, age and composition of revenue arrears. Besides, the revenue arrears were quite significant, hence affecting operations of various departments and effective implementation of some budget functions. Counties are not able to monitor revenue arrears for most revenue streams mainly because of lack of up-to-date databases on revenue payers, especially the lack of up-to-date business registers and valuation rolls.

Weak link between policy making, planning and budgeting

The link between policy, planning and budgeting is weak, especially the extent to which approved expenditure policy proposals are aligned to costed ministerial strategic plans or sector strategies as identified in County Integrated Development Plans (CIDPs). There also exist inadequate mechanisms to monitor budget implementation and performance for service delivery.

Low levels of transparency in the PFM

Public access to information is limited, especially access to budget documents within set timelines, for example publishing of budget statements (including citizen's budget), budget execution reports, audit reports, macroeconomic assumptions, etc. The performance indicators for measuring the outputs or outcomes of the different ministries are not in place. Consequently, no information related to performance achieved for service delivery is provided to the public.

Conclusions and Recommendations

There has been considerable effort made towards establishing the foundations of a sound PFM system within the devolved system of government in Kenya. However, implementation of the PFM systems in the counties is still in the initial phases. There is still much work to be done to achieve the level of performance to ensure that PFM systems impact significantly on the achievement of outcomes of aggregate fiscal discipline, strategic allocation of resources and efficient service delivery at local, regional and national levels. Other than addressing institutional and human capacity issues, the internal and external audit systems require strengthening to provide full oversight of the effectiveness of the internal control system. Identified weaknesses undermine their efficiency and effectiveness in identifying irregularities and errors in the PFM.

Considering the findings of the assessment, the following recommendations are suggested herein:

- Improvement of disbursement of revenue by the National Treasury and timely submission and approval of audited reports to enhance budget credibility and predictability in the county governments.
- Automation of revenue collection systems and sensitization of revenue payers on existing levies, charges and fees and their importance in service delivery.
- Capacity building in macroeconomic forecasting (revenue and expenditure forecasting), MTEF budgeting, macro fiscal sensitivity analysis, fiscal impact analysis, and economic analysis of investment projects.
- Strengthening the link between planning and budgeting and ensuring that priorities within CIDPs are in line with Vision 2030 framework.
- Enhancing transparency in public finances by availing all budget documents to the public (posted on official websites) in a timely and user-friendly means of communication (e.g. radio, notice boards, loudspeakers, public barazas and civic education), packaging budgets in a user-friendly manner, and giving adequate notices.
- Identifying, evaluating and keeping record of all non-financial assets, especially land, machinery and equipment, is important. In addition, the cooperation between the Inter-Governmental Relations Technical Committee (IGRTC) and the counties is also critical in ensuring that the transfer of assets and liabilities to the counties is complete.
- Establish systems to monitor revenue arrears especially through automation of revenue systems and updating of business registers and valuation rolls.
- The Inter-Governmental Relations Technical Committee needs to work with the counties to resolve the issue of transfer of assets and liabilities from the former local authorities so that the countries address effectively the issue of assets, liabilities and inherited debts.
- Maintain comprehensive records of revenue arrears including the value, age and composition of revenue arrears.
- The legislative oversight role and scrutiny should be strengthened to ensure all audit recommendations are implemented by the county governments accordingly for accountability and improvement of service delivery.
- Establish and/or strengthen monitoring and evaluation units to ensure effective implementation of various activities and programmes and increase the value for money across various counties.

About KIPPRA Policy Briefs

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