Approved for tabling.
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9/10/19

THE NATIONAL ASSEMBLY
TWELFTH PARLIAMENT- THIRD SESSION (2019)

COMMITTEE ON DELEGATED LEGISLATION

REPORT ON THE CONSIDERATION OF THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNEMENT) (AMENDMENT) REGULATIONS, 2019 (LEGAL NOTICE 155 OF 2019)

OCTOBER 2019

Directorate of Committee Services
The National Assembly,
Parliament Buildings,
NAIROBI.

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ABBREVIATIONS

BPS	Budget Policy Statement
GDP	Gross Domestic Product
LN	Legal Notice
PFM	Public Finance Management
RMA	Regulatory Making Authority
SI	Statutory Instruments
SO	Standing Order

CHAIRPERSON'S FOREWORD

In exercise of the powers conferred by section 205 of the Public Finance Management Act, 2012, the Cabinet Secretary responsible for the National Treasury published the Public Finance Management (National Government) (Amendment) Regulations, 2019 on the 26th of September, 2019 vide Legal Notice No. 155 of 2019. The Regulations were submitted to the Clerk of the Assembly on 1st October, 2019 and tabled before the House on the same date. This was within the statutory timelines contemplated under section 11(1) of the Statutory Instruments Act.

The Regulations seek to amend Regulation 26(1)(c) of the Public Finance Management (National Government) Regulations, 2015 (Legal Notice No.34 of 2015) to provide a numerical limit to the total public debt of Kshs. 9 trillion in place of the current debt limit set at fifty per cent (50%) of GDP in net present value terms.

Pursuant to section 16 of the Statutory Instruments Act, 2013, the Committee invited the regulation making authority to a consultative meeting on 8th October, 2019 to consider the said statutory instrument.

Having scrutinized the Public Finance Management (National Government) (Amendment) Regulations, 2019 against the Constitution of Kenya, the Interpretations and General Provisions Act (*Cap 2*) Laws of Kenya, the Public Finance Management Act, 2012 and the Statutory Instruments Act, 2013, the Committee **approved it** for reasons advanced in this Report.

The Report is submitted to the House in accordance with section 205 (4) of the Public Finance Management Act, 2012 which requires that the Regulations made under this section of the Act be presented to Parliament for approval before they take effect.

I wish to most sincerely thank the Speaker and the Office of the Clerk of the National Assembly for the invaluable support accorded to the Committee in the discharge of its mandate.

On behalf of the Members of the Select Committee on Delegated Legislation and pursuant to Standing Order 210 (4) and section 67 of the Value Added Tax Act, 2013, it is my pleasure and duty to present to the House the Committee's Report on the Consideration of the Public Finance Management (National Government) (Amendment) Regulations, 2019.

HON. GLADYS BOSS SHOLLEI CBS MP

1.0 PREFACE

1.1. Establishment and Mandate of the Committee

The Select Committee on Delegated Legislation is established pursuant to ***Standing Order No. 210*** and is mandated to consider statutory instruments submitted to Parliament for consideration. The Committee is expected to consider in respect of any statutory instrument, whether it is in accordance with the provisions of the Constitution, the Act pursuant to which it is made or other relevant written laws.

The Committee is mandated to consider in respect of any statutory instrument, whether it:

a) is in accordance with the provisions of the Constitution, the Act pursuant to which it is made or other relevant written laws;
b) infringes on fundamental rights and freedoms of the public;
c) contains a matter which in the option of the Committee should more properly be dealt with in an Act of the Parliament;
d) contains imposition of taxation;
e) directly or indirectly bars the jurisdiction of the court;
f) gives retrospective effect to any of the provision in respect to which the Constitution does not expressly give any such power;
g) it involves expenditure from the consolidated fund or other public revenues;
h) is defective in its drafting or for any reason form or part of the statutory instrument calls for any elucidation;
i) appears to make some unusual or unexpected use of the power conferred by the Constitution or the Act pursuant to which it is made;
j) appears to have had unjustifiable delay in its publication or laying before Parliament;
k) makes rights, liberties or obligations unduly dependent upon non-renewable decisions;
l) makes rights, liberties or obligations unduly dependent insufficiently defined administrative powers;
m) inappropriately delegates legislative powers;
n) imposes a fine, imprisonment or other penalty without express authority having been provided for in the enabling legislation;
o) appears for any reason to infringe on the rule of law;
p) inadequately subjects the exercise of legislative power to Parliamentary scrutiny; and
q) accords to any other reason that the Committee considers fit to examine.

1.2 Committee Membership

Chairperson

Hon. Gladys Boss Shollei CBS MP
Uasin Gishu County Woman Representative
Jubilee Party

Vice- Chairperson

Hon. Fatuma Gedi, MP
Wajir County Woman Representative
Party for Development and Reforms

MEMBERS

Hon. Waihenya Ndirangu, MP
Roysambu Constituency
Jubilee Party

Hon. Alice Wahome, MP,
Kandara Constituency
Jubilee Party

Hon. Robert Mbui, MP
Kathiani Constituency,
Wiper Democratic Movement -Kenya

Hon. Daniel Maanzo, MP
Makueni Constituency
Wiper Democratic Movement -Kenya

Hon. Muriuki Njagagua, MP
Mbeere North Constituency
Jubilee Party

Hon. Timothy Wanyonyi, MP
Westlands Constituency
Orange Democratic Movement

Hon. George G. Murugara, MP
Tharaka Constituency
Jubilee Party

Hon. Ronald Tonui, MP
Bomet Central Constituency
Jubilee Party

Hon. William Kamoti, MP
Rabai Constituency
Orange Democratic Movement

Hon. Martha Wangari, MP
Gilgil Constituency
Jubilee Party

Hon. Gideon Mulyungi, MP
Mwingi Constituency
Wiper Democratic Movement – Kenya

Hon. William Kassait Kamket, MP
Tiaty Constituency
KANU

Hon. (Dr.) Wilberforce Oundo, MP
Funyula Constituency
Orange Democratic Movement

Hon. Jennifer Shamalla, MP
Nominated
Jubilee Party

Hon. Munene Wambugu, MP
Kirinyaga Central Constituency
Jubilee Party

Hon. Muturi Kigano, MP
Kangema Constituency
Jubilee Party

Hon. Patrick Kariuki Mariru, MP
Laikipia West Constituency
Jubilee Party

Hon. Sammy Seroney, MP
Nominated
Wiper Democratic Movement – Kenya

Hon. Tindi Mwale, MP
Butere Constituency
Amani National Congress

Hon. Alfred W. Sambu, MP
Webuye East
Amani National Congress

Hon. Abdi Koropu Tepo, MP
Isiolo South Constituency
Kenya Patriots Party

1.3 Committee Secretariat

Ms. Susan Maritim
Senior Clerk Assistant (Team Leader)

Mr. Jimale Mohamed
Second Clerk Assistant

Mr. Wilson Dima Dima
Principal Legal Counsel

Mr. Josphat Motonu
Fiscal Analyst I

Ms. Anne Njeri Kigoro
Research Officer III

Ms. Winnie Kiziah
Media Relations Officer II

Mr. Anthony Wamae
Serjeant at Arms

Mr. Charles Ayari
Superintendent of Electronics

Ms. Mary Otieno
Office Superintendent

2.0 CONSIDERATION OF THE REGULATIONS

2.1 Public Finance Management (National Government) (Amendment) Regulations, 2019

2.1.1 Introduction

1. The Public Finance Management (National Government) (Amendment) Regulations, 2019 were made by the Cabinet Secretary responsible for the National Treasury pursuant to section 205 of the Public Finance Management Act, 2012.

2. The Regulations were published in the Gazette as *Legal Notice No 155* of 2019 on the 26th of September, 2019 vide Legal Notice No. 164 of 2019. The Regulations were submitted to the Clerk of the Assembly on 1st October, 2019[1] and tabled before the House on the same date. This was within the statutory timelines contemplated under section 11(1) of the Statutory Instruments Act.

2.1.2 Purpose of the Regulations

3. The Regulations seek to –

   (i) to **provide clarity in terms of controls and timely oversight mechanism on the growth of public debt**. Monitoring public debt as a percentage of GDP makes it unclear and difficult to enforce compliance and undermine accountability as actual GDP number is a moving target;

   (ii) to provide a numerical limit to the total public debt of Kshs. 9 trillion in place of the current debt limit set at fifty per cent (50%) of GDP in net present value terms;

   (iii) to **provide adequate borrowing space to cater for potential guarantees for borrowing by County Governments & state-owned enterprises**; and

   (iv) **allow the government access to concessional funding sources** (multilateral financial institutions and bilateral sources) thereby facilitating government interventions in the public sector.

2.1.3 Policy Context & Rationale for the Amendments

4. The set debt limit as currently expressed on net present value terms as a percentage of GDP is unclear, difficult to verify compliance and thus undermines accountability.

5. In general terms, public debt limits are necessary in safeguarding an economy from shocks and risks such as exchange risks, interest rate risk and international financial instabilities and safeguarding public debt at sustainable levels as envisaged in the Constitution, the PFM Act and in accordance with international best practice.

6. The ceiling is proposed at Kshs. 9 trillion. As at end of June, 2019, public debt stood at 5.8 trillion and is expected to rise to Kshs. 6.3 trillion by the end of the current fiscal year

[1] Annexure 1: Paper Laid – Legal Notice No. 155/2019

based on the approved BPS by Parliament. The amendment will therefore enable implementation of the FY 2019/20 Budget as approved by Parliament.

7. To be able to re-profile existing high cost of debts through debt re-financing facilities guaranteed by multi-lateral financial institutions and bilateral sources to enable it pay-off expensive syndicated/commercial loans.

8. To be able to minimise domestic borrowing and allow local SMEs and private sector at large access affordable credit and avoid crowding out the private sector by confining multi-lateral and bilateral creditors which have lower interest rates and longer repayment terms.

2.1.4 Scrutiny of the Instrument

9. Pursuant to section 16 of the Act, the Committee held a meeting with the regulation making authority on 8th October, 2019 in Nairobi where Hon. (Amb.) Ukur Yattani, Cabinet Secretary responsible for the National Treasury made a presentation to the Committee on the proposed changes to the Regulations. The Committee was also guided by technical briefs from the Parliamentary Budget Office and the National Assembly Directorate of Legal Services.

10. The Committee considered the Regulations against the principal Regulations, i.e., the **Public Finance Management (National Government) Regulations, 2015 (Legal Notice No.34 of 2015),** the Constitution, the Interpretations and General Provisions Act (Cap 2) Laws of Kenya, the Public Finance Management Act, 2012 and the Statutory Instruments Act (No 23 of 2013).

2.2.1 Submission by the Parliamentary Budget Office[2]

The Parliamentary Budget Office informed the Committee as follows –

11. The current total public debt stood at Kshs. 5.81 Trillion[3] as of June, 2019 and this is equivalent to 61.8 **percent** of nominal GDP[4]. This indicates that the PV of debt to GDP is actually higher than the 50 percent **threshold** provided in the PFM regulation, as evidenced by the recent IMF Debt Sustainability Analysis for Kenya.

12. Parliament, as required in Article 211, has the power to legislate the terms on which the national government may borrow. In addition, Section 50 (2) of the PFM Act, 2012 provides that the National Government may borrow money in accordance with the PFM Act or any other legislation and shall not exceed a limit set by Parliament. Indeed, the proposal to amend the limit is in line with the National Assembly's resolution in the Report on the Budget Policy Statement 2019 on public debt which provided that "*at an appropriate time, the PFM Act should be amended to provide for a numerical debt ceiling as opposed to the current scenario where the debt is pegged on GDP projections.*" It was envisaged that the limit would be in line with the approved fiscal consolidation path.

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[2] Annexure 2
[3] As reported in the Quarterly Economic and Budgetary Review (QEBR), August 2019 Edition
[4] The nominal GDP for 2018/19 is estimated at Kshs. 9.51 Trillion

13. Earlier in 2014 before the PFM Regulations were in place, Parliament approved an increase in the ceiling for external debt from *USD* 14 Billion (Kshs 1.2 Trillion) to USD 28 Billion (Kshs 2.5 Trillion) through the Sessional Paper No. 14.

Legal Underpinning

14. The public debt limits have been provided for in several laws as follows-

(i) **EAC Treaty**: Kenya is a signatory to the EAC Monetary Union Protocol that provides that in the convergence criteria, member countries will endeavor to achieve a public debt ceiling of 50 percent of the Gross Domestic Product (GDP) in Net Present Value (NPV) terms by 2021.

(ii) **The Constitution:** Article 211 provides for borrowing by national government and gives power to Parliament to prescribe through legislation the terms on which the national government may borrow and also impose reporting requirements. In addition, Article 214 provides for the meaning of Public Debt, that it is all financial obligations attendant to loans raised or guaranteed and securities issued or guaranteed by the national government. Further, it provides that a public debt is a charge on the Consolidated Fund, but an Act of Parliament may provide for charging all or part of the public debt to other public funds.

(iii) **Repealed Internal Loans Act and the External Loans Act:** These Acts were in place and regulated the borrowing by the National Government before the PFM Act, 2012 came into place. In terms of providing borrowing limits, the Internal Loans Act did not provide a legal limit for domestic debt, however the External Loans Act provided that the limit for external debt was to be approved by Parliament.

(iv) **Public Finance Management Act (PFM Act), 2012:** Section 50(2) provides that the National Government may borrow money in accordance with the PFM Act or any other legislation and shall not exceed a limit set by Parliament.

(v) **Public Finance Management Act (PFM) Regulations), 2015:** Regulation 26(1) (c) provides that the national public debt shall not exceed 50 percent of Gross Domestic Product (GDP) in net present value terms.

Macroeconomic and Fiscal Implication of the Proposed Amendment

15. **Increasing the debt ceiling is likely to give more room for borrowing which will be inconsistent with the approved fiscal consolidation path FY 2019/20 and the medium term.** The government in its effort to achieve fiscal consolidation had projected the total public debt as a share of GDP to be 44 percent by FY 2022/23 which is Kshs. 7.21 Trillion, compared to the current level of 61.8 percent of GDP, as of June, 2019[5]. This implies that if the debt limit is set at Kshs. 9 Trillion, the country will be moving away from the fiscal consolidation path and the targets will be surpassed much earlier

[5] As reported in the Quarterly Economic and Budgetary Review (QEBR), August 2019 Edition

than expected. In addition, the fiscal deficit which has to be financed through borrowing is not consistent with the proposed fiscal consolidation path, where we have to borrow more and this affects the fiscal sustainability path. Therefore, before approving the amendment, there is need to consider the trends in the fiscal deficit, and the fiscal consolidation path.

Table 1: Total Debt for FY 2016/17 to FY 2022/23 (Kshs. Billion)

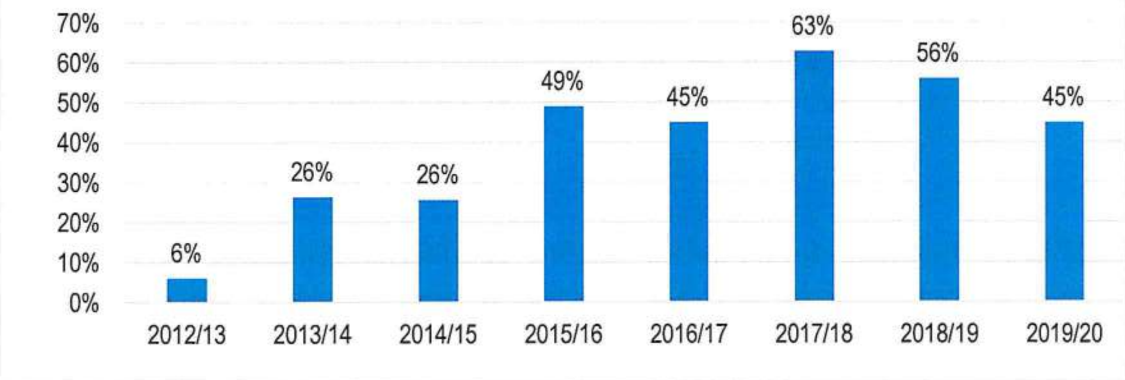
	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
	Actual	Preliminary Actual	Preliminary Actual	Estimate	Projection	Projection	Projection
Total Debt as a Share of GDP (%)	**51.9**	**51.5**	**61.8**	**50.6**	**48.8**	**46.4**	**44.0**
Fiscal Deficit (inclusive of grants) as a share of GDP (%)	**8.8**	**6.8**	**6.3**	**5.1**	**3.9**	**3.3**	**3.1**

Source: BPS, 2019

16. **Increasing the debt ceiling is likely to alter the approved borrowing framework for FY 2019/20 of 38% of external borrowing and 62% of domestic borrowing, to lean more towards external borrowing.** Additional room for borrowing will increase the chance of additional loans from external sources since domestic borrowing is not a viable option, at the moment. The current situation in the domestic market is that the government has crowded-out the private sector borrowers since lending to government is deemed to be risk-free with guaranteed returns. This reduces credit to the private sector which in turn adversely affects growth in investment, growth of SMEs and creation of job opportunities.

17. **Increasing the debt ceiling is likely to increase external borrowing and mainly from commercial sources which are more expensive.** The evolution of commercial debt since FY 2012/13 indicates that it has increasingly been a source of financing the budget deficit because it is easy to acquire with less demanding conditions when compared to concessional funding from multi-lateral and bi-lateral agencies. However, it is a high-risk option and also more expensive given that the interest rates are higher with a shorter pay-back period. If the country is not able to generate the targeted revenue in the shorter-term before the return on investment is realized, then it faces a refinancing risk and this forces the country to get into a debt roll-over (where it borrows to repay existing debt obligations that are due). If the debt ceiling is increased, then there should be a limit on external borrowing at commercial rates to contain external vulnerabilities.

Figure 1: Evolution of commercial debt as a share of budget deficit FY 2012/13 - 2019/20



Source: Budget Policy Statement

International Standards and Practice

18. The IMF provides for public debt sustainability benchmark thresholds that guide countries in different stages of development ranging from low-income to the advanced economies. This enables efficient tracking of the sustainability of debt given the prevailing macroeconomic environment in terms of the performance of GDP, revenue and exports.

19. **Currently, the country has surpassed some of the debt sustainability thresholds**, in particular the more distressing is the debt service to revenue ratio. This implies that the economy is not generating enough revenues to cover the debt servicing requirements. The risk is that the country will continue to borrow to repay the existing debts and not for development expenditure as contemplated in law. Table 2 provides the threshold for Kenya (which is currently a lower middle-income country), the performance since 2016 and the projections.

Table 2: Public Sector Debt Sustainability Ratios

Indicator	Threshold	2016	2017	2018	2019	*2020*	*2021*	*2022*
		Actual		Estimate		Projections		
PV of Public Sector Debt to GDP	IMF - 74%	50.6	55.4	60.6	59.9	*56.9*	*54.3*	*53.1*
PV of public Sector Debt to Revenue	300	275.9	285	299.6	292.9	*282.1*	*269.7*	*261.5*
Debt Service to Revenue Ratio	30%	36.3	42.7	44.8	49.4	*49.3*	*48.9*	*37.6*

Source: IMF, 2018

20. The country may be experiencing the tragedy of commons which implies that we presume that what we borrow is for productive expenditure, however, the trend indicates that borrowing has been used for recurrent expenditure as it is not fully financed by the ordinary revenue collected (*See Table 3*). To reduce the risk of external and domestic loans being used for recurrent expenditure instead of development projects and programmes as provided for in the law, it would be prudent to set rules on pre-approval of debt-financed projects/ programmes. In addition, the auditor general should undertake a forensic audit on the current stock of public sector debt.

Table 3: Distribution to ordinary revenue to key expenditure categories, FY 2014/15 to 2019/20

Details		Distribution (%)					
		2014/15	2015/16	2016/17	2017/18	2018/19	2019/20*
Total Ordinary Revenue		100%	100%	100%	100%	100%	100%
o/w	Interest payments	17%	19%	21%	24%	23%	23%
o/w	Pensions	4%	5%	5%	5%	5%	6%
Total Net Recurrent		63%	65%	58%	63%	56%	54%
County Allocation		22%	22%	21%	22%	18%	17%
Available Resources for Development		-6%	-10%	-6%	-14%	-4%	1%

Source: The National Treasury; Derivations: PBO

Policy Options

21. The following are the viable policy options-

	Policy Options	Implication
1.	Accept the amendment as proposed by the National Treasury	(i) The country will no longer comply with the EAC convergence criteria which it is a signatory to. (ii) Reduce the flexibility in the budget as debt repayment, which are a first charge to the consolidated fund, will increase. (iii) It will undermine credibility of the budget, in particular the medium-term projections which are part of the Medium-Term Expenditure Framework (MTEF).
2.	Reject the proposed amendment	(i) Status quo remains (ii) Allow the National Treasury to reconsider the limits to be within the fiscal consolidation path.

3.0 COMMITTEE OBSERVATIONS

The Committee observed THAT –

22. **Statutory Timelines:** The Regulations were submitted to the National Assembly within the statutory timeline provided for in section 11(1) of the Statutory Instruments Act, 2013.

23. **Consultations / Public participation**: Articles 10 and 118 of the Constitution, section 5, 5A and the Schedule to the Act and Standing Order 210 require the regulation making authority to conduct public participation and sufficient consultation with the stakeholders and persons likely to be affected by the regulations. The outcomes of such consultations are to be indicated within the explanatory memorandum in detail.

    The **Committee is in receipt of the explanatory memorandum demonstrating that sufficient public consultation was conducted as required under Articles 10 and 118 of the Constitution and sections 5, 5A and the schedule of the Statutory Instruments Act**.

24. **Regulatory Impact Statement:** Sections 6, 7, and 8 of the Act requires the regulatory making authority to carry out a Regulatory Impact Assessment and submit to Parliament a Regulatory Impact Statement if the proposed regulation has significant cost or impact to the community or a sect of the community. The Public Finance Management (National Government) (Amendment) Regulations, 2019 do impose significant costs on the community and hence need for the Regulation making authority to prepare a Regulatory Impact Statement.

    The **Committee is in receipt of the Regulatory Impact Statement that demonstrates that the regulation making authority conducted a regulatory impact assessment as required Sections 6, 7, and 8 of the Statutory Instruments Act, 2013**.

25. Pursuant to section 13 (q) of the Statutory Instruments Act, the Committee observed with concern that the fight against corruption ought to be stepped up to stem the increased in pilferage of public resources.

4.0 COMMITTEE RECOMMENDATION

26. Pursuant to Standing Order 210 (4) and having examined the Public Finance Management (National Government) (Amendment) Regulations, 2019 (*Legal Notice No. 155 of 2019*) against the Constitution of Kenya, the Interpretations and General Provisions Act (*Cap 2*) Laws of Kenya, the Public Finance Management Act, 2012 and the Statutory Instruments Act, 2013, the Committee **recommends that the House approves the said statutory instrument.**

Signed............ GBossShollei   **Date**........ 9th Oct. 2019

HON. GLADYS BOSS SHOLLEI CBS MP

(CHAIRPERSON)

ANNEXURES

COMMITTEE ON DELEGATED LEGISLATION

ADOPTION LIST

Report on the Consideration of the Public Finance Management (National Government) (Amendment) Regulations, 2019 (Legal Notice No. 155 of 2019)

We, the undersigned, hereby affix our signatures to this Report to affirm our approval:

DATE: 9 October 2019

	HON. MEMBER	SIGNATURE
1.	Hon. Gladys Boss-Shollei CBS MP (Chairperson)	
2.	Hon. Fatuma Ali Gedi, MP (Vice Chairperson)	
3.	Hon. Isaac Waihenya Ndirangu, MP	
4.	Hon. Robert Mbui, MP	
5.	Hon. Alice Wahome, MP	
6.	Hon. Daniel Maanzo, MP	
7.	Hon. Muriuki Njagagua, MP	
8.	Hon. Martha Wangari, MP	
9.	Hon. Timothy Wanyonyi, MP	
10.	Hon. William Kamoti Mwamkale, MP	
11.	Hon. Patrick Kariuki Mariru, MP	
12.	Hon. Ronald Kiprotich Tonui, MP	
13.	Hon. William Kassait Kamket, MP	
14.	Hon. Munene Wambugu, MP	
15.	Hon. George Gitonga Murugara, MP	
16.	Hon. Jennifer Shamalla, MP	
17.	Hon. Muturi Kigano, MP	
18.	Hon. (Dr.) Wilberforce Oundo, MP	
19.	Hon. Sammy Seroney, MP	
20.	Hon. Tindi Mwale, MP	
21.	Hon. Gideon Mulyungi, MP	
22.	Hon. Abdi Tepo, MP	
23.	Hon. Alfred Sambu, MP	

Annex 1

MINUTES OF THE 54TH SITTING OF THE COMMITTEE ON DELEGATED LEGISLATION HELD ON TUESDAY, 8TH OCTOBER, 2019 AT 3.30 P.M. COMMITTEE ROOM 7, MAIN PARLIAMEN BUILDINGS

PRESENT

1. **The Hon. Gladys Boss Shollei CBS MP - Chairperson**
2. **The Hon. Fatuma Gedi, MP - Vice Chairperson**
3. The Hon. Timothy Wanyonyi, MP
4. The Hon. Alice Wahome, MP
5. The Hon. Robert Mbui, MP
6. The Hon. (Dr.) Wilberforce Oundo, MP
7. The Hon. Jennifer Shamalla, MP
8. The Hon. Muturi Kigano, MP
9. The Hon. Kamoti Mwamkale, MP
10. The Hon. Muriuki Njagagua, MP
11. The Hon. Ronald Tonui, MP
12. The Hon. Martha Wangari, MP
13. The Hon. Kassait Kamket, MP
14. The Hon. Sammy Seroney, MP
15. The Hon. Abdi Koropu Tepo, MP

ABSENT WITH APOLOGY

1. The Hon. Waihenya Ndirangu, MP
2. The Hon. Daniel Maanzo, MP
3. The Hon. George Murugara, MP
4. The Hon. Patrick Mariru, MP
5. The Hon. Gideon Mulyungi, MP
6. The Hon. Munene Wambugu, MP
7. The Hon. Tindi Mwale, MP

ABSENT

1. The Hon. Alfred Sambu, MP

IN-ATTENDANCE

National Assembly Secretariat

1. Ms. Susan Maritim - Senior Clerk Assistant
2. Mr. Jimale Mohamed - Second Clerk Assistant
3. Mr Sydney Lugaga - Legal Counsel I
4. Ms. Ann Kigoro - Research and Policy Analyst
5. Mr. Charles Ayari - Superintendent of Electronics (Audio)
6. Ms. Mary Otieno - Office Superintendent
7. Mr. Anthony Wamae - Serjeant at Arms
8. Mr. Brian Wechabe - Legal Intern

MIN.NO. NA/CDL/2019/307 PRAYER AND RELIMINARIES

The session resumed with prayers at 3.35 p.m.

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MIN.NO. /NA/CDL/2019/308 **CONSIDERATION OF PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, 2019**

The Committee was briefed as follows, THAT;

1. The Public Finance Management (National Government) (Amendment) Regulations, 2019 are made by the Cabinet Secretary responsible for the National Treasury pursuant to section 205 of the Public Finance Management Act, 2019.
2. The Regulations were published in the Gazette as Legal Notice No. 155 of 2019 on the 26th of September, 2019, received by the Clerk of National Assembly on the 1st October, 2019 and tabled before the House on Wednesday 2nd October, 2019 within the statutory timelines contemplated under section 11(1) of the Statutory Instruments Act.
3. **The Regulations** are intended to **amend regulation 26(1)(c) of the Public Finance Management (National Government) Regulations to provide that the national public debt shall *not exceed nine trillion shillings* as opposed to exceeding *50 percent of Gross Domestic Product (GDP) in net present value terms.***

Committee Observations

The Committee made the following observations: - THAT;

a) Statutory timelines

the Regulations were submitted to the National Assembly were published on the **27th September, 2019,** received by the Clerk of National Assembly on the on **1st October, 2019** and tabled on **Wednesday 2nd October, 2019**. Pursuant to section 11(1) of the Statutory Instruments Act the Regulations were submitted within the statutory timeline (hereinafter referred to as the Act). Section 11(1) of the Statutory Instruments Act provides that "*Every Cabinet Secretary responsible for a regulation-making authority shall within seven (7) sitting days after the publication of a statutory instrument, ensure that a copy of the statutory instrument is transmitted to the responsible Clerk for tabling before the relevant House of Parliament.*"

b) Consultation / Public participation

Articles 10 and 118 of the Constitution, section 5, 5A and the Schedule to the Act and Standing Order 210 require the regulation –making authority to conduct public participation and sufficient consultation with the stakeholders and persons likely to be affected by the regulations. The outcomes of such consultations are to be indicated within the explanatory memorandum in detail. The explanatory memorandum from the Cabinet Secretary, National Treasury addresses and indicates their consultation with relevant stakeholders.

The Committee noted that the RMA conducted public participation by writing to various institutions including Parliament and that the stakeholders responded which informed the policy changes effecting amendment to the PFM (National Government) (Amendment) Regulations, 2019.

c) Regulatory Impact Statement

Sections 6, 7, and 8 of the Act requires the regulatory making authority to carry out a Regulatory Impact Assessment and submit to Parliament a Regulatory Impact Statement if the proposed regulation has significant cost or impact to the community or a sect of the community. The Public Finance Management (National Government Amendment) Regulations 2019 do impose significant costs on the community and hence need for the Regulation making authority to prepare a Regulatory Impact Statement. The Committee is in receipt of documentations that demonstrates that the regulation making authority conducted a Regulatory Impact Assessment.

Committee Resolution

The Committee deferred decision making on the Regulations to the next meeting.

MIN.NO. /NA/CDL/2019/309 ADJOURNMENT AND DATE OF NEXT MEETING

The meeting was adjourned at 7.15 p.m. until the following day Wednesday, 9th October, 2019 at 9.00 a.m

Signed: GBossSholei .... **Date:** 9th Oct. 2019 ....

HON. GLADYS BOSS SHOLLEI CBS MP

(CHAIRPERSON)

MINUTES OF THE 52ND SITTING OF THE COMMITTEE ON DELEGATED LEGISLATION HELD ON TUESDAY, 8TH OCTOBER, 2019 AT 7.30 A.M. IN INTERCONTINETAL HOTEL

PRESENT

1. **The Hon. Gladys Boss Shollei CBS MP - Chairperson**
2. **The Hon. Fatuma Gedi, MP - Vice Chairperson**
3. The Hon. Timothy Wanyonyi, MP
4. The Hon. Alice Wahome, MP
5. The Hon. Robert Mbui, MP
6. The Hon. (Dr.) Wilberforce Oundo, MP
7. The Hon. Jennifer Shamalla, MP
8. The Hon. Muturi Kigano, MP
9. The Hon. Kamoti Mwamkale, MP
10. The Hon. Muriuki Njagagua, MP
11. The Hon. Ronald Tonui, MP
12. The Hon. Martha Wangari, MP
13. The Hon. Kassait Kamket, MP
14. The Hon. Sammy Seroney, MP
15. The Hon. Abdi Koropu Tepo, MP

ABSENT WITH APOLOGY

1. The Hon. Waihenya Ndirangu, MP
2. The Hon. Daniel Maanzo, MP
3. The Hon. George Murugara, MP
4. The Hon. Patrick Mariru, MP
5. The Hon. Gideon Mulyungi, MP
6. The Hon. Munene Wambugu, MP
7. The Hon. Tindi Mwale, MP

ABSENT

1. The Hon. Alfred Sambu, MP

IN-ATTENDANCE

National Assembly Secretariat

1. Ms. Susan Maritim - Senior Clerk Assistant
2. Mr. Jimale Mohamed - Second Clerk Assistant
3. Mr Sydney Lugaga - Legal Counsel I
4. Ms. Ann Kigoro - Research and Policy Analyst
5. Mr. Charles Ayari - Superintendent of Electronics (Audio)
6. Ms. Mary Otieno - Office Superintendent
7. Mr. Anthony Wamae - Serjeant at Arms
8. Mr. Brian Wechabe - Legal Intern

THE NATIONAL TREASURY & PLANNING

1. Hon. Amb.Ukur Yattani, EGH - Cabinet secretary
2. Daniel Ndolo - Director / Dept policy strategy

3. Mr. Livigstone Bumbe - Deputy Director DPS&RM
4. Dr. Haron Lesirima - Director General, PDMO
5. Mr. Ainest Mwenda - DG-BFEA
6. Mr. Bernard Ndungu - DG/ASA QA
7. CPA Isabella Kogei - Parliamentary Liaison
8. Ms. Zahra Haji - Personal Assistant to the Cabinet Secretary
9. Mr Moses K. Kanagi - Deputy Director and Head Europe 1 Division, Resource Mobilization Department.

MIN.NO. NA/CDL/2019/298 PRAYER AND RELIMINARIES

The session resumed with prayers at 8.15 am.

MIN.NO. /NA/CDL/2019/299 CONSIDERATION OF PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, 2019

Submissions on the Regulations

Brief by the Parliamentary Budget Office

The Parliamentary Budget Office briefed as follows-

1) The PFM (National Government) (Amendment) Regulations, 2019 which seeks to amend the that the National public debt shall not exceed 50 per cent of Gross Domestic Product (GDP) in net present value terms and replace it with a provision of a Kenya Shilling 9 Trillion national public debt ceiling.
2) The Regulation is intended to amend the principal Regulation which proposes the deletion of the provision of net present value of total public debt and substituting it with the set limit.
3) The current total public debt stands 5.81 Trillion of as of June, 2019 which represents 61.8% of the nominal GDP.
4) This indicates that the Present value of debt to GDP is higher than the 50% threshold provided in the PFM Act, 2012.
5) Parliament as required in Article 211 has the power to legislate the terms on which the national government may borrow.
6) Section 50 of the PFM Act, 2012 provides that the national government may borrow money in accordance with the Act or any other legislation and shall not exceed a limit set by Parliament.
7) The proposal to amend the limit is in line with the National Assembly's Resolution in report on the Budget Policy Statement 2019 on public debt.
8) The PFM Act to be amended to provide for a numerical debt ceiling because currently the debt is pegged on GDP projections.
9) The fiscal analyst further stated the legal laws underpinning the public debt like the EAC Treaty where Kenya is a signatory to the Monitory Union Protocol. The Constitution of Kenya, Article 211 and Article 214 which provides for the Public debt, the PFM Act, 2012 and the PFM (National Regulations) 2015; which is Regulation 26(1) (c)

The brief by PBO further guides the macroeconomic and fiscal implication of the amendment that by increasing the debt ceiling-

1. Give more room for borrowing which will be inconsistent with the approved fiscal consolidation path 2019/2020 and the medium term. The government had projected the total public debt as a share of GDP to be 44 percent FY 2022/2023.
   The fiscal consolidation path and the targets will be surpassed much earlier than expected hence there's need to consider the trends in the fiscal deficit and fiscal consolidation path.
2. Alter the approved borrowing framework for FY 2019/2020 of 38% of external borrowing and 62% of domestic borrowing to lean towards external borrowing.
3. Also lead to increase external borrowing and from commercial sources which are considered to be more expensive.

The fiscal analyst further guided Members through the international standards and practice: -

(i) IMF provides member countries for public debt sustainability benchmark thresholds that guide countries in different stages of development ranging from law-income to the advance economies,

(ii) The country as surpassed the threshold the sustainability threshold in debt servicing to revenue ratio. The economy is not generating enough revenue to cover for the debt servicing requirement.

PBO informed that the Committee has two policy options-

a) Either accept the amendment as proposed, or;
b) Reject to remain status quo to allow the National Treasury to reconsider the limits to be within the Fiscal Consolidation Path.

MIN.NO. /NA/CDL/2019/300 **MEETING WITH THE NATIONAL TREASURY TO CONSIDER THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, 2019 – LEGAL NOTICE NO. 155**

Submission by the Cabinet Secretary - The National Treasury & Planning

Purpose of the proposed amendment

a) To provide clarity in terms of control and timely oversite mechanism and the growth of the public debts;
b) To provide a numerical limit to the total public debt of 9 trillion in net present value terms.
c) To provide adequate borrowing space
d) Allow the government access to multilateral institutions there by facilitating government investment in the public sector.

Policy context and rational for the amendment

1. The set debt limit on net present value terms is unclear and difficult to verify compliance

2. The ceiling is proposed at 9 trillion as at June 2019 therefore the public debt stood at ksh5.8 trillion and is expected to rise to ksh6.3 trillion.
3. Enables implementation of 2019/2020 budget approved by parliament.

Legislative context

The proposed amendment to the regulation is anchored to the PFM Act section 2205 and regulation 6 of the PFM (National government) (Amendment) Regulations 2019.

Public participation

The national treasury has undertaken public participation by inviting comments from stakeholders and general public on proposed amendments relating to PFM regulations. the outcome from the stakeholders and the general public consultation undertaken was incorporated into the final document and this is considered as part of the process of the amendments.

Plenary discussions

1) With regard to date ceiling, the committee raised the following concern; -
    a) transparency in debt levels and borrowing,
    b) weakness in revenue collection
    c) need for equity in donor funded project,
    d) wastage of public funds,
    e) commitment to fiscal austerity measure
    f) appetite for commercial borrowing,
    g) sustainability of public debt,
    h) institutional arrangement of public debt arrangement office and the need to reset the ceiling to a lower level of ksh7.5 trillion
2) On public participation, the CS noted that the National Treasury has conducted public participation as required by Section, 5, 5A, 13 (a) (m) of the Statutory Instruments Act which require that the regulation-making authority conducts public participation and that sufficient consultation with key stakeholders
3) The Cabinet Secretary committed to a sound economic and financial policies, prudent management debt and borrowing.
4) The proposed amendments to the regulation is firmly anchored to the PFM Act and is consistent with the provision of the constitution and take into consideration, the current and the future generations.
5) On media campaign and awareness to the general public; the CS assured the Committee that media will be involved to thoroughly make the public understand the debt ceiling and its implications to the country,

Way forward

The Committee further directed the CS and his team to submit additional documentation which indicates that consultations with relevant stakeholders were adequately undertaken.

The Committee deferred decision making on the Regulations to the next meeting.

the proposed regulation has significant cost or impact to the community or a sect of the community. The Public Finance Management (National Government Amendment) Regulations 2019 do impose significant costs on the community and hence need for the Regulation making authority to prepare a Regulatory Impact Statement. The Committee is in receipt of documentations that demonstrates that the regulation making authority conducted a Regulatory Impact Assessment.

Committee Resolution

The Committee deferred decision making on the Regulations to the next meeting.

MIN.NO. /NA/CDL/2019/309 ADJOURNMENT AND DATE OF NEXT MEETING

The meeting was adjourned at 7.15 p.m. until the following day Wednesday, 9th October, 2019 at 9.00 a.m

Signed: .... **Date:** 19th Oct. 2019

HON. GLADYS BOSS SHOLLEI CBS MP

(CHAIRPERSON)

(2) Mr. Kampati
Please deal urgently.
01/10/19

Annex 2

REPUBLIC OF KENYA
THE NATIONAL TREASURY AND PLANNING

Telegraphic Address: 22921
Finance – Nairobi
FAX NO. 310833
Telephone: 2252299
When Replying Please Quote

SECRET

THE NATIONAL TREASURY
P O BOX 30007- 00100
NAIROBI

Ref: DMD 4/85/N/(13)

Date: September 27, 2019

Mr. Michael Sialai, EBS
Clerk of the National Assembly
Parliament Buildings
NAIROBI

(1) DC. Sarah Kioko
For tabling in the House after being entered in the Register.
1/10/19

Dear Clerk,

RE: THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) REGULATIONS, 2019

The National Treasury is proposing amendment to the Public Finance Management (National Government) Regulations, 2015 Section 26(1) (c) through the Kenya Gazette Supplement No. 164 dated 26th September 2019. The purpose of the amendment is to set limit on total public debt as required under the Public Finance Management Act, 2012. The proposed amendment is subject to approval by Parliament.

The purpose of this letter is to submit herewith the Kenya Gazette Supplement No. 164 dated 26th September 2019 the request for the proposed amendment of Public Finance Management Regulations to be laid before the National Assembly for consideration and approval.

HON (AMB.) UKUR YATANI
Ag. CABINET SECRETARY/NATIONAL TREASURY & PLANNING

Attachment

Copy to:

Dr. Joseph K. Kinyua, EGH
Head of the Public Service
Executive Office of the President
Harambee House
NAIROBI

Justice (Rtd) P. Kihara Kariuki, CBS
Attorney General
Office of the Attorney General &
Department of Justice
State Law Office
NAIROBI

SECRET

SPECIAL ISSUE

Kenya Gazette Supplement No. 164 *26th September, 2019*

(Legislative Supplement No. 56)

LEGAL NOTICE NO. 155

THE PUBLIC FINANCE MANAGMENT ACT

(No. 18 of 2012)

IN EXERCISE of the powers conferred by section 205 of the Public Finance Management Act, 2012, the Cabinet Secretary for the National Treasury and Planning makes the following Regulations—

THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT)(AMENDMENT) REGULATIONS, 2019

1. These Regulations may be cited as the Public Finance Management (National Government)(Amendment) Regulations, 2019.

2. The Public Finance Management (National Government) Regulations, 2015, (in these Regulations referred to as the "principal Regulations") are amended in regulation 26(1) subparagraph (c) by deleting the words "50 percent of Gross Domestic Product (GDP) in net present value terms" and substituting therefor the words "nine trillion shillings". Sub. Leg.

3. Regulation 196 of the principal Regulations is amended in paragraph (1) by deleting the words "net present value of the total public debt that is" and substituting therefor the words "set limit".

Made on the 25th September, 2019.

UKUR YATANI,
Ag. Cabinet Secretary
for the National Treasury & Planning.

PRINTED AND PUBLISHED BY THE GOVERNMENT PRINTER, NAIROBI

Annex 3

REGULATORY IMPACT STATEMENT

THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) (AMENDMENT) 2019

1. Introduction

The Regulatory Impact Statement for the proposed the proposed amendment to The Public Finance Management (National Government) (Amendment) 2019 was prepared in accordance with the provisions of the Statutory Instruments Act, 2013 (No.23 of 2013).

2. A Statement of the Objectives and Reasons for the Regulations

i. Provide an effective oversight mechanism and accountability on sustainable level of public debt. It is difficult to monitor debt limit set as a percentage of GDP under a short time span due to a lag in publication of GDP figures. Furthermore, GDP figures may distort debt to GDP ratios due to periodic revisions;

ii. Provide a numerical limit to the total public debt of Kenya Shillings nine trillion in place of the current public debt limit set at 50 per cent of GDP in net present value terms;

iii. Allow the Government access to concessional funding sources (multilateral and bilateral agencies) facilitating public sector investment supportive of inclusive economic growth and development ;

iv. Provide adequate borrowing space to cater for potential guarantees for borrowing by County Governments and State Owned Enterprises.

3. Statement on the Effects of the proposed Regulations

i. The regulation seeks to strengthen the effectiveness of the PFM Regulation (National Government) 2015, specifically making the debt ceiling more transparent and facilitates more accountability and clear fiscal reporting in line with the principles of public finance specified under the Constitution of Kenya.

ii. It enables the economy to respond effectively to shocks, provides a solid foundation for the country to have increased access to foreign capital, more resources for private and public investments, improve business confidence, and a stronger safety net for Kenyans.

iii. Allows implementation of the FY 2019/20 National Budget and subsequent years.

iv. Enables re-profiling of existing high cost and risky debts in the portfolio through debt structuring techniques like re-financing with guaranteed multilateral financial institutions and bilateral agencies debt facilities;

v. Minimize government domestic borrowing and avoid '*crowding-out*' private sector, particularly Micro and Small Enterprises from accessing credit;

4. Statement of other practical means of achieving those Objectives

The substitute for borrowing is mobilization of domestic resources through revenue to finance expenditures. It's not feasible to raise adequate resources to finance the country's development needs solely through taxation. Raising tax rates to realize the amount equivalent to current and projected fiscal deficit will have undesirable effects to welfare of Kenyans.

5. Assessment of Costs and Benefits of the proposed Legislation

i. The cost of adjusting the debt ceiling is equivalent to Kshs 3 trillion being the amount of additional debt to be incurred over the medium-term. It is expected that the additional debt will be contracted on highly concessional terms with real interest costs below inflation rates. Interest cost will be minimal.

ii. The benefit from the additional borrowing is estimated to be more than Kshs 3 trillion in form of direct and indirect benefits associated new public investment.

6. The reasons why other means are not appropriate

i. Maintaining current debt ceiling limits the ability of the Government to fully implement the FY2019/20 National Budget and subsequent years;

ii. There is no scope to raise taxes to close the fiscal deficit without negative effects on the entire economy;

7. The proposed statutory regulation

i. The Public Finance Management (National Government) (Amendment) 2019

HON. (AMB) UKUR YATANI,
ACTING CABINET SECRETARY, THE NATIONAL TREASURY & PLANNING

DATE....27th September, 2019....

Annex 4

REPUBLIC OF KENYA
OFFICE OF THE DEPUTY PRESIDENT

EXTRACT RESOLUTION OF THE EXTRA-ORDINARY SESSION OF THE INTERGOVERNMENTAL BUDGET AND ECONOMIC COUNCIL (IBEC) HELD AT THE OFFICE OF THE DEPUTY PRESIDENT, KAREN OFFICE ON 7TH OCTOBER, 2019.

Following deliberations as per attached justification, the Council at its extra-ordinary session held on 7th October, 2019 considered and approved proposed amendments to the Public Finance Management (National Government) Regulations 2015 by having the debt ceiling set at an absolute numerical of **nine trillion shillings** rather than **a percentage of gross domestic product in net present value terms.**

Arising from the above, the Council directs the Cabinet Secretary, the National Treasury and Planning to transmit the recommended amendments to Parliament for consideration.

Dr. Patrick Omutia, CBS
Special Secretary IBEC

JUSTIFICATION FOR PROPOSED AMENDMENTS TO THE PUBLIC FINANCE MANAGEMENT (NATIONAL GOVERNMENT) REGULATIONS 2015, 26(1)(c) AND 196(1)

1. An absolute numerical rather than a percentage numerical rather than a percentage of gross domestic product (GDP) in net present value terms would provide better clarity in terms of controls and timely oversight mechanism on the grown of public debt.
2. The percentage of GDP in net present value term gives a moving target which poses difficulty in enforcing compliance and it undermine accountability.
3. The target absolute figure of nine trillion Shilling shall:
   (a) Provide adequate borrowing space to allow the Government to implement the financial year 2019/2020 budget which has a deficit of Kshs. 635 billion for development financing through borrowing;
   (b) Provide adequate borrowing space to allow the Government to access concession funding sources to facilitate Government investment for which such funding to the tune of Kshs 421 billion which have been concluded awaiting signature;
   (c) Provide adequate borrowing space to cater for potential guarantees for borrowing by County Governments and Parastatals;
   (d) In the medium term enable the Government implant its debt consolidation plan aimed both reducing deficit financing from 6.3% in 2018/19 to 3% of GDP in 2023/24 and reduce debt service levels thereby releasing additional shareable resources to both levels of Government.
4. To buttress the consolidation strategy Government shall deepen expenditure rationalization in the medium term and implement revenue enhancement measures.
5. As a safeguard, new debt over the consolidation period shall be monitored and managed through annual parliamentary budget approvals.
6. The proposed shift in methodology does not breach Kenya's debt sustainability threshold of 70% debt to GDP ratio in present value terms as set by the IMF World Bank.

Annex 5

REPUBLIC OF KENYA
PARLIAMENTARY SERVICE COMMISSION
PARLIAMENTARY BUDGET OFFICE

Analysis of the Public Finance Management (National Government) (Amendment) Regulations, 2019

October, 2019

Annex 7

Disclaimer

Parliamentary Budget Office (PBO) is a non-partisan professional office of Parliament of the Republic of Kenya. The primary function of the Office is to provide professional non-partisan advice in respect of budget, finance and economic information to committees of Parliament.

Parliamentary Budget Office, 2019
For more information, contact:
The Director,
Parliamentary Budget Office
Parliament of the Republic of Kenya
Protection House, 10th Floor
P.O. Box 41842 – 00100 GPO
NAIROBI, KENYA
Tel : +254-20-284-8810
Email: pbo@parliament.go.ke.

I. OVERVIEW

1) The Public Finance Management (National Government) (Amendment) Regulations, 2019 seeks to amend regulation 26 (1) (c) which provides that the national public debt shall not exceed 50 percent of Gross Domestic Product (GDP) in net present value terms and replace it with a provision of a Ksh. 9 Trillion national public debt ceiling. Subsequently, Regulation 196 (1) is amended to delete the provision of net present value of total public debt and substituting it with *the set limit.*

2) The current total public debt stands at Ksh. 5.81 Trillion[1] as of June, 2019 and this is equivalent to 61.8 percent of nominal GDP[2]. This indicates that the PV of debt to GDP is actually higher than the 50 percent threshold provided in the PFM regulation, as evidenced by the recent IMF Debt Sustainability Analysis for Kenya.

3) Parliament,as required in Article 211, has the power to legislate the terms on which the national government may borrow.In addition, Section 50 (2) of the PFM Act, 2012provides that the National Government may borrow money in accordance with the PFM Act or any other legislation and shall not exceed a limit set by Parliament.Indeed,the proposal to amend the limit is in line with the National Assembly's resolution in report on the Budget Policy Statement 2019 on public debt which was as follows-*that at an appropriate time, the PFM Act should be amended to provide for a numerical debt ceiling as opposed to the current scenario where the debt is pegged on GDP projections.*It was envisaged that the limit would be in line with the approved fiscal consolidation path.

4) Earlier in 2014 before the PFM Regulations were in place, Parliament approved an increase in the ceiling for external debt from USD 14 Billion (Kshs 1.2 Trillion) to USD 28 Billion (Kshs 2.5 Trillion) through the Sessional Paper No. 14.

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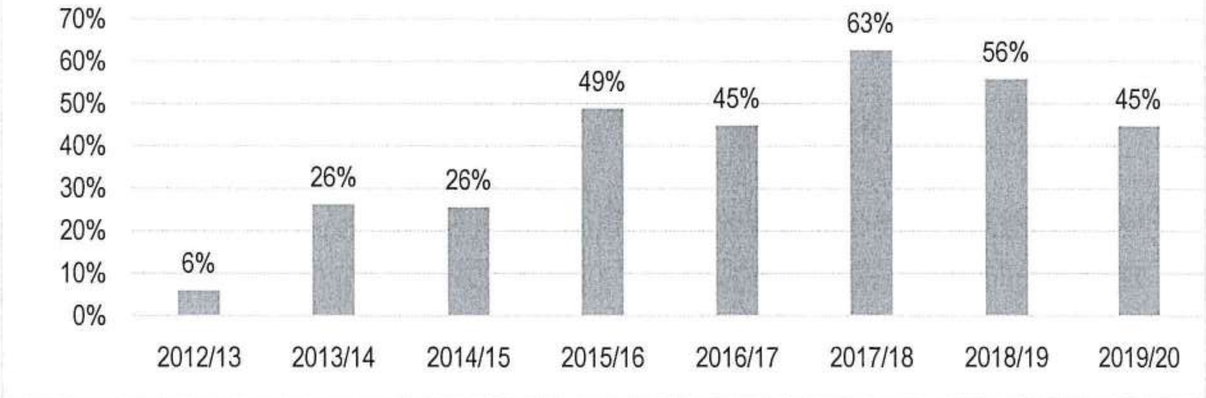
[1]As reported in the Quarterly Economic and Budgetary Review (QEBR), August 2019 Edition

[2] The nominal GDP for 2018/19 is estimated at Ksh. 9.51 Trillion

towards external borrowing. Additional room for borrowing will increase the chance of additional loans from external sources since domestic borrowing is not a viable option, at the moment. The current situation in the domestic market is that the government has crowded-out the private sector borrowers since lending to government is deemed to be risk-free with guaranteed returns. This reduces credit to the private sector which in turn adversely affectsgrowth in investment, growth of SMEs and creation of job opportunities.y.

8) **Increasing the debt ceiling is likely to increase external borrowing and mainly from commercial sources which are more expensive.**The evolution of commercial debt since FY 2012/13 indicates that it has increasingly been a source of financing the budget deficit because it is easy to acquire with less demanding conditions when compared to concessional funding from multi-lateral and bi-lateral agencies. However, it is a high risk option and also more expensive given that the interest rates are higher with a shorter pay-back period. If the country is not able to generate the targeted revenue in the shorter-term before the return on investment is realized, then it faces a refinancing risk and this forces the country to get into a debt roll-over (where it borrows to repay existing debt obligations that are due). If the debt ceiling is increased, then there should be a limit on external borrowing at commercial rates to contain external vulnerabilities.

Figure 1: Evolution of commercial debt as a share of budget deficit FY 2012/13 - 2019/20



Source: Budget Policy Statement

IV. INTERNATIONAL STANDARDS AND PRACTICE

9) The IMF provides for public debt sustainability benchmark thresholds that guide countries in different stages of development ranging from low-income to the advanced economies. This enables efficient tracking of the sustainability of debt given the prevailing macroeconomic environment in terms of the performance of GDP, revenue and exports.

10) **Currently, the country has surpassed some of the debt sustainability thresholds, in particular the more distressing is the debt service to revenue ratio.** This implies that the economy is not generating enough revenues to cover the debt servicing requirements. The risk is that the country will continue to borrow to repay the existing debts and not for development expenditure as contemplated in law. Table 2 provides the threshold for Kenya (which is currently a lower middle-income country), the performance since 2016 and the projections.

Table 2: Public Sector Debt Sustainability Ratios

Indicator	Threshold	2016	2017	2018	2019	*2020*	*2021*	*2022*
		Actual		Estimate		Projections		
PV of Public Sector Debt to GDP	IMF - 74%	50.6	55.4	60.6	59.9	*56.9*	*54.3*	*53.1*
PV of public Sector Debt to Revenue	300	275.9	285	299.6	292.9	*282.1*	*269.7*	*261.5*
Debt Service to Revenue Ratio	30%	36.3	42.7	44.8	49.4	*49.3*	*48.9*	*37.6*

Source: IMF, 2018

The country may be experiencing the tragedy of commons which implies that we presume that what we borrow is for productive expenditure, however, the trend indicates that borrowing has been used for recurrent expenditure as it is not fully financed by the ordinary revenue collected (See Table 3).To reduce the risk of external and domestic loans being used for recurrent expenditure instead of development projects and programmes as provided for in the law, it would be prudent to set rules on pre-approval of debt-financed projects/ programmes. In addition, the auditor general should undertake a forensic audit on the current stock of public sector debt.

Table 3: Distribution to ordinary revenue to key expenditure categories, FY 2014/15 to 2019/20

Details		Distribution (%)					
		2014/15	2015/16	2016/17	2017/18	2018/19	2019/20*
Total Ordinary Revenue		100%	100%	100%	100%	100%	100%
o/w	Interest payments	17%	19%	21%	24%	23%	23%
o/w	Pensions	4%	5%	5%	5%	5%	6%
Total Net Recurrent		63%	65%	58%	63%	56%	54%
County Allocation		22%	22%	21%	22%	18%	17%
Available Resources for Development		-6%	-10%	-6%	-14%	-4%	1%

Source: The National Treasury; Derivations: PBO

V. POLICY OPTIONS

11) The following are the viable policy options-

	Policy Options	Implication
1.	Accept the amendment as proposed by the National Treasury	(i) The country will no longer comply with the EAC convergence criteria which it is a signatory to. (ii) Reduce the flexibility in the budget as debt repayment, which are a first charge to the consolidated fund, will increase. (iii) It will undermine credibility of the budget, in particular the medium term projections which are part of the Medium Term Expenditure Framework (MTEF).

2.	Reject the proposed amendment	(i) Status Quo remains (ii) Allow the National Treasury to reconsider the limits to be within the Fiscal Consolidation path.

ANNEX: Key Fiscal Indicators

No.	Indicators		2018/19	2019/20	2020/21	2021/22	2022/23
1	Total Debt		Kshs. 5.8 Trillion	Kshs. 6.44 Trillion	Kshs. 7.03 Trillion	Kshs. 7.61 Trillion	Kshs. 8.19 Trillion
2	Debt / GDP ratio	Draft BROP 2019	61.8%	55.2%	53.6%	51.8%	49.2%
		Budget Estimates 2019		49.9%	48.8%	46.4%	44.0%
		BPS 2019		50.6%	48.8%	46.4%	44.0%
3	Real GDP growth	Draft BROP 2019		6.1%	6.3%	6.5%	6.8%
		BPS 2019		6.2%	6.4%	6.7%	7.0%
4	Budget deficit (Excl. Grants)	Draft BROP 2019		7.1%	5.1%	4.6%	4.0%
		BPS 2019		6.0%	4.3%	3.7%	3.4%
5	Ordinary Revenue as a share of GDP	Draft BROP 2019		17.0%	15.3%	15.3%	15.2%
		BPS 2019		17.4%	16.7%	17.0%	17.1%
6	Recurrent expenditure as a share of GDP	Draft BROP 2019		16.1%	14.9%	14.4%	13.9%
		BPS 2019		16.2%	14.2%	14.1%	13.9%
7	Development & Net lending expenditure as a share of GDP	Draft BROP 2019		6.6%	4.5%	4.5%	4.5%
		BPS 2019		5.9%	5.7%	5.7%	5.8%

Source: BPS 2019, Draft Budget Review &Outlook Paper, 2019

SUMMARY OF STATUS OF LOAN AGREEMENTS PENDING APPROVAL OR UNDER NEGOTIATION BETWEEN THE GOVERNMENT OF KENYA AND DEVELOPMENT PARTNERS AS AT 30TH SEPTEMBER 2019

TABLE 1: LENDER AND LOAN AMOUNTS

NO	DEVELOPMENT PARTNER	AMOUNT IN KENYA SHILLINGS
1	Africa Development Bank	94,155,038,000
2	China	86,950,000,000
3	Japan	83,313,300,000
4	World Bank	51,300,000,000
5	Agence De Francaise Development	30,552,000,000
6	South Korea	15,900,000,000
7	Germany KfW	15,276,000,000
8	IFAD	12,380,000,000
9	Middle East	9,700,000,000
10	French Embassy	5,989,560,000
11	Spain	4,233,868,686
12	European Investment Bank	3,990,000,000
13	Italy	3,066,072,522
14	Belgium	2,838,000,000
15	Finland	2,280,000,000
	TOTAL	**421, 923, 839, 208**

TABLE 2: SECTOR AND LOAN AMOUNTS

NO.	SECTOR	NO. OF AGREEMENTS	AMOUNT IN KENYA SHILLINGS
1	Infrastructure	10	149,193,468,686
2	Water & Irrigation	14	126,897,298,000
3	Energy	7	50,451,700,000
4	Trade & Manufacturing	1	35,977,300,000
5	Housing	2	35,260,000,000
6	TIVET	4	13,148,000,000
7	Higher Education	1	3,420,000,000
8	Health	2	3,009,072,522
9	Environment	1	2,255,000,000
10	Basic Education	1	1,400,000,000
11	Urban Development	1	912,000,000
	TOTAL	**44**	**421, 923, 839, 208**

STATUS OF LOAN AGREEMENTS PENDING APPROVAL OR UNDER NEGOTIATION BETWEEN THE GOVERNMENT OF KENYA AND DEVELOPMENT PARTNERS AS AT 30TH SEPTEMBER 2019

NO.	MINISTRY/MDA	SECTOR	PROJECT TITLE	DEVT PARTNER	TYPE OF FUNDING	CURRENCY: FOREIGN CURRENCY	CURRENCY: KENYA SHILLINGS	CURRENCY: INTEREST RATE	STATUS OF THE FINANCING AGREEMENT
1	Ministry of Water, Sanitation & Irrigation	Water	Thwake Multi-purpose water Development Program	ADB	Loan	EUR 43.19 M	4,923,660,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium = 0% -0.14%+0.8%+0.2% =0.86% Per Annum	The loan agreement was signed. Legal opinion is required for the loan to be effective. We are waiting for feedback from the Attorney Generals Office
2	Ministry of Water,Sanitation & Irrigation	Water	Thwake Multi-purpose water Development Program	ADB	Loan	EUR 192.56M	21,951,840,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium = 0% -0.14%+0.8%+0.2% =0.86% Per Annum	The loan agreement was signed. Legal opinion is required for the loan to be effective. We are waiting for feedback from the Attorney Generals Office
3	Ministry of Energy/ KETRACO	Energy	Supplementary Financing for the Ethiopia-Kenya Electricity Highway Project	Africa Development Bank	Loan	Euros 26,510,000.	3,022,140,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium = 0% -0.14%+0.8%+0.2% =0.86% Per Annum	The loan agreement was signed. Legal opinion is required for the loan to be effective
4	Ministry of Water and Sanitation	Water	Nairobi Rivers Basin Rehabilitation and Restoration Program: Sewerage Improvement Project Phase II	Africa Development Bank	Loan	EUR 59,407,000	6,772,398,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium = 0% -0.14%+0.8%+0.2% =0.86% Per Annum	The loan agreement was signed. Legal opinion is required for the loan to be effective
5	Ministry of Water and Sanitation	Water	Nairobi Rivers Basin Rehabilitation and Restoration Program: Sewerage Improvement Project Phase II	Africa Development Bank	Loan	UA 2, 910,000	410,000,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium = 0% -0.14%+0.8%+0.2% =0.86% Per Annum	The loan agreement was signed. Legal opinion is required for the loan to be effective
6	The National Treasury	Housing	Kenya mortgage Refinance Company Project	Africa Development Bank	Loan	EUR 90 Million	10,260,000,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium = 0% -0.14%+0.8%+0.2%	The bank has submitted two copies of the loan agreement for signature by the Cabinet Secretary of the National Treasury
7	State Department of Transport and Infrastructure/ KENHA	Infrastructure	Kenol- Sagana- Marua Road Upgrading Project	ADB and GoK	Loan	UA 233.7 M	33,015,000,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium (To be confirmed)	Negotiations between the Governmnet of Kenya and the African Development Bank to held
8	State Department of Vocational Training	TIVET	Technical Vocational Education Training and Entrepreneurship Project	ADF	Loan	UA 26.9 M	3,800,000,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium (To be confirmed)	Negotiations between the Governmnet of Kenya and the African Development Bank to held
9	Ministry of Energy/ KPLC	Energy	Last Mile Connectivity Phase III	ADB	Loan	USD 100M	10,000,000,000	Base Rate (Euribor) +Funding Cost Margin+ Lending Margin + Maturity Premium (To be confirmed)	Negotiations between the Governmnet of Kenya and the African Development Bank to held

NO.	MINISTRY/MDA	SECTOR	PROJECT TITLE	DEVT PARTNER	TYPE OF FUNDING	CURRENCY			STATUS OF THE FINANCING AGREEMENT
						FOREIGN CURRENCY	KENYA SHILLINGS	INTEREST RATE	
10	State Department of Infrastructure (KENHA)	Infrastructure	Steel Bridges Project Phase II (T-Mall Flyover at Langata Road and Five Footbridges on Mombasa and Langata Road)	Government	Concessional Loan From ICO and Commercial Loan from BBVA	Euro 23,250,000 from ICO and Euro13,889,199.28 from BBVA	4,233,868,686	0.2 for Concessional Loan and 2% for BBVA	The Draft Financing Agreements has been agreed and negotiated by both Parties.
11	Education	TIVET	Youth Employment and Vocational Training in Kenya	KfW	Concessional loan	Euro. 20M	2,280,000,000	1.3 % Per Annum	The Agreements have been cleared by the Attorney General for signature subject to resolution of land ownership issue of the Kiambu Institute of Science & Technology
12	Education	TIVET	Promotion of Youth Employment and Vocational Training Project	KfW	Concessional loan	Euro. 12M	1,368,000,000	1.3 % Per Annum	Negotiation on the project are expected to take place before December 2019
13	Water , Sanitation & Irrigation	Water	Development of the Water and Sanitation Sector -Water Sector Trust Fund, Phase IV	KfW	Concessional loan	Euro. 11 M	1,254,000,000	1.3 % Per Annum	Negotiation on the were carried out in June 2019. The KfW has forwarded the revised version which is under review and will be forwarded to the AG for clerance thereafter.
14	Water , Sanitation & Irrigation	Water	Lake Nakuru Biodiversity Conservation Project	KfW	Concessional loan	Euro. 29 M	3,306,000,000	1.3 % Per Annum	Negotiation on the were carried out in June 2019. The KfW has forwarded the revised version which is under review and will be forwarded to the AG for clerance thereafter.
15	Water , Sanitation & Irrigation	Water	Lake Nakuru Biodiversity Conservation Project	KfW	Concessional loan	Euro. 14 M	1,596,000,000	1.3 % Per Annum	It entails shifting of 14 Mio. € loan IDA terms from project "Small Hydro Lake Victoria" in benefit of the project "Lake Nakuru Biodiversity Conservation Project" (IDA terms remain unchanged).
16	Water , Sanitation & Irrigation	Water	Coastal Water Security and Climate Resilience Project	World Bank	IBRD loan	120,000,000 USD	12,000,000,000	0.75 % Per Annum	US D 80 million cancelled. Financing Agreement amended to reflect this.Forwarded to CS for consideration and signature
17	National Treasury & Planning	Housing	Affordable Housing Fina	World Bank	IBRD loan	250,000,000 USD	25,000,000,000	EURIBOR plus Fixed spread	The Project documents were cleared by Attorney General for signature.Already submitted to CS's office for consideration
18	Water , Sanitation & Irrigation	Water	Water Security and Climate Resilience Project	World Bank	IBRD loan	143,000,000 USD	14,300,000,000	0.75 % Per Annum	US D 70 million cancelled. Financing Agreement amended to reflect this. Forwarded to CS for consideration and signature
19	Water , Sanitation & Irrigation	Water	Lake Victoria Water and Sanitation (LVWATSAN) Project	1. AFD 2. EIB	Consessional Loan	1. 20,000,000 Euro 2. 35,000,000 Euro	6,270,000,000	1.26 % Per Annum	The has been several rounds of exchange of letters. There are several outstanding Cluases and the teams are planning a round table negotiation in September 2019.
	MINISTRY/MDA	SECTOR	PROJECT TITLE	DEVT PARTNER	TYPE OF FUNDING	CURRENCY			

NO.						FOREIGN CURRENCY	KENYA SHILLINGS	INTEREST RATE	STATUS OF THE FINANCING AGREEMENT
20	Water , Sanitation & Irrigation	Water	Nairobi Water and Sanitation Project	AFD	Consessional Loan	100,000,000 Euro.	11,400,000,000	1.4 % Per Annum	The Agreement has been cleared by the AG for signing subject to confirmation of compliance with provisions of Treasury Circular No. 12/2018.
21	Transport, Infrastructure, Urban Development &	Infrastructure	Arid and Semi-Arid Lands Rural Roads	AFD	Consessional Loan & Grant	60,000,000 Euro	6,840,000,000	1.36 % Per Annum	The Agreement is under review by the National Treasury & the Ministry. The Ministry has also been requested to confirm compliance with the provisions of
22	Education	TIVET	Support to the Technical and Vocational Education and Training (TVET)	AFD	Consessional Loan & Grant	50, 000,000 Euro	5,700,000,000	1.4 % Per Annum	An initial request has been received from the Ministry. The Ministry has been requested to confirm compliance with the provisions of Treasury Circular No. 12/2018
23	Education	Higher Education	Construction of an engineering and science complex at the University of Nairobi	AFD	Consessional Loan	30, 000,000 Euro	3,420,000,000	1.4 % Per Annum	A Statement of Intent was signed in March 2019. The AFD is carrying out a feasibility study at the University of Nairobi
24	Transport, Infrastructure, Urban Development & Housing & Public Works	Urban Development	Additional Funding for Kisumu Urban Project (KUP) to Finance the Construction of Jubilee Market	AFD	Consessional Loan	Euro 8,000,000	912,000,000	1.4 % Per Annum	A request has been made to the AFD for the support, The GoK is awaiting for the response.
25	Energy/KETRACO	Energy		China Exim Bank	Loan	114.7 M USD	11,470,000,000	LIBOR + 300 b.p	The Agreement has been cleared by the AG for signature
26	Energy/KETRACO	Energy	Lot 1: Turkwel-Lokichar-Lodwar 220KV Transmission Line and Associated Substations Facilities LOT 2: Myanga-Busia-Rangala-Bondo-Ndigwa 132KV Transmission Line and Associated Substations Facilities	China Exim Bank	Loan	96.1 M USD	9,610,000,000	LIBOR + 300 b.p	The Agreement has been cleared by the AG for signature
27	Energy/KETRACO	Energy	144KM 132KV Double Circuit Kitui-Mutomo-Kibwezi Transmission Line with Substation at Mutomo	China Exim Bank	Loan	58 M USD	5,800,000,000	LIBOR + 300 b.p	The Agreement has been cleared by the AG for signature
	MINISTRY/MDA	SECTOR	PROJECT TITLE	DEVT PARTNER	TYPE OF FUNDING	CURRENCY			
NO.						FOREIGN CURRENCY	KENYA SHILLINGS	INTEREST RATE	STATUS OF THE FINANCING AGREEMENT

28	Transport, Infrastructure, Urban Development & Housing & Public Works (Kenya National Highway Authority)	Infrastructure	Upgrading of Kitui - Mwingi-Kandwia Road : Lot 2	China Exim Bank	Loan	180.7 M USD	18,070,000,000	LIBOR + 300 b.p	The Agreement has been cleared by the AG for signature
29	Transport, Infrastructure, Urban Development & Housing & Public Works (Kenya National Highway Authority)	Infrastructure	Upgrading of Kandwia-Tseikuru-Usueni Road: Lot 3	China Exim Bank	Loan	126.6 M USD	12,660,000,000	LIBOR + 300 b.p	The Agreement has been cleared by the AG for signature
30	Water , Sanitation & Irrigation	Water	Mzima II Water Supply Project	China Exim	Loan	293.4 M USD	29,340,000,000	LIBOR + 300 b.p	The Agreement has been cleared by the AG for signature
31	Water , Sanitation & Irrigation	Water	Upper Tana Natural Resource Management Programme(UTaNRMP) Additional financing	International Fund for Agriculture Development (IFAD)	Loan	USD12.38 M	12,380,000,000	No interest rate but has a service charge of 0.75 %	Has been forwarded to the Cabinet Secretary for consideration
32	East Africa Community and Regional Development (Coast Development Authority)	Health Sector	Malindi Integrated Social and Health Development Programme - Phase II	Italy Agency for Development Cooperation	Concessional Loan	Euro 6,395,373	729,072, 522	0.3 % Per Annum	The Loan Agreement is under review by the National Treasury
33	Environment and Forestry	Environment Sector	Kajiado Integrated Waste Management Project	Italy Agency for Development Cooperation	Concessional Loan	Euro 20,500,000	2,337,000,000	1 % Per Annum	The Loan Agreement is under review by the National Treasury
34	Transport, Infrastructure, Urban Development &	Infrastructure	Samatar - Wajir road Project	Kuwait Fund, OPEC	Concessional Loan	USD 83 Million	8,300,000,000	1.75 % Per Annum. 1 % Service Charge	Development partners do not want to be enjoined as tax agents in the financing agreement as required by the National Treasury/BFEA; We are yet to get draft
35	Education	Basic Education	Development of Schools Infrastructure in Nyamira County project	Kuwait Fund and GOK	Concessional loans	USD 14 million	1,400,000,000	1.5 % Per Annum 1 % Service Charge	Development partners do not want to be enjoined as tax agents in the financing agreement as required by the National Treasury/BFEA; Cannot proceed due to
36	Transport, Infrastructure, Urban Development &	Infrastructure	Supply of Pedestrain Steel Bridges	Belgium	Loan	24.9 Million Euro	2,838,000,000	0 % Interest Rate. Insurance Premium - 12.64 %	Commercial contract signed. Loan Agreement pending clearance at the AG to be signed by CS, NT & Planning.
37	Health	Social	Upgrading Maternal and Newborn Care Units	Finland	Mixed Credi	Euro 20million	2,280,000,000	Nill	Negotiations yet to be started
	MINISTRY/MDA	**SECTOR**	**PROJECT TITLE**	**DEVT PARTNER**	**TYPE OF FUNDING**	**CURRENCY**			
NO.						**FOREIGN CURRENCY**	**KENYA SHILLINGS**	**INTEREST RATE**	**STATUS OF THE FINANCING AGREEMENT**

38	Trade, Industry & Cooperatives	Trade & Manufacturing	Mombasa Special Economic Zone	Japan	Consessional Loan	37.09 Billion Yen	35,977,300,000	Interest Rate 0.1 % P.A.	Exchange of notes signed and the negotiations on the financing agreement ongoing.
39	Transport, Infrastructure, Urban Development & Housing & Public Works	Infrastructure	Mombasa Gate Bridge	Japan	Consessional Loan	48.80 Billion Yen	47,336,000,000	Interest Rate 0.1 % P.A.	Exchange of notes signed and the negotiations on the financing agreement ongoing.
40	Transport, Infrastructure, Urban Development & Housing & Public Works	Infrastructure	ITS Phase II	South Korea	Consessional Loan	100 Million USD	10,000,000,000	Interest Rate 0.1 % P.A.	Negotiations on the financing agreement ongoing.
41	Transport, Infrastructure, Urban Development & Housing & Public	Infrastructure	BRT II	South Korea	Consessional Loan	59 Million USD	5,900,000,000	Interest Rate 0.1 % P.A.	Negotiations on the financing agreement ongoing.
42	Water , Sanitation & Irrigation	Irrigation	Drought Resilience Project in Northern Kenya	KFW	Consessional Loan	8 Million Euro	912,000,000	Interest Rate 0.75 % P.A. Commitment Fees 0.25 %	The Loan Agreement was signed on 24th December 2019. The Legal Opinion is the only Condition Precedent that is pending
43	Energy	Energy	Menengai -Rongai Transmission Line	French Treasury	Mixed Credit	52.54 Million Euro	5,989,560,000	Risk Premium -16.04 % Commitment Fees 0.5 % CIRR -0.95 %	The financial terms of the loan were reviewed by the National Treasury and it was established that the loan's consessionality is 27 % which is below the 35 %
44	Energy	Energy	Olkaria Upgrade	KFW	Consessional Loan	40 Million Euro	4,560,000,000	Variable interest rate based on the 6-month EURIBOR plus the Margin, calculated on an actual/360 basis. The variable interest rate, however, will be at least 0.00 % p. a. **Commitment Fee: 0.25 % p.a.** on the undisbursed Loan Amount. **Management Fee: 0.50 %** flat on the total Loan Amount;	The financial terms of the loan are under review by the National Treasury.
	TOTAL						**421,923,839,208**		