**SPECIAL ISSUE**

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REPUBLIC OF KENYA

# *KENYA GAZETTE SUPPLEMENT*

## NATIONAL ASSEMBLY BILLS, 2022

**NAIROBI, 25th February, 2022**

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# THE DIVISION OF REVENUE BILL, 2022
## ARRANGEMENT OF CLAUSES

*Clause*

1—Short title.

2—Interpretation.

3—Object and purpose of the Act.

4—Allocations to National Government and County Government.

5—Variation in revenue.

**SCHEDULE**

**EQUITABLE SHARE OF REVENUE RAISED NATIONALLY BETWEEN THE NATIONAL AND COUNTY GOVERNMENTS FOR THE FINANCIAL YEAR 2022/23.**

**APPENDIX**

**EXPLANATORY MEMORANDUM TO THE DIVISION OF REVENUE BILL, 2022.**

**A Bill for**

**AN ACT of Parliament to provide for the equitable division of revenue raised nationally between the national and county governments in 2022/23 financial year, and for connected purposes.**

**ENACTED** by the Parliament of Kenya, as follows—

Short title.

**1.** This Act may be cited as the Division of Revenue Act, 2022.

Interpretation.

**2.** In this Act, unless the context otherwise requires—

No. 16 of 2011.

"revenue" has the meaning assigned to it under section 2 of the Commission on Revenue Allocation Act, 2011.

Object and purpose of the Act.

**3.** The object and purpose of this Act is to provide for the equitable division of revenue raised nationally between the national and county levels of government for the financial year 2022/23 in accordance with Article 203 (2) of the Constitution.

Allocations to national and county governments.

**4.** Revenue raised by the national government in respect of the financial year 2022/23 shall be divided among the national and county governments as set out in the Schedule to this Act.

Variation in revenue.

**5.** (1) If the actual revenue raised nationally in the financial year falls short of the expected revenue set out in the Schedule, the shortfall shall be borne by the national government.

(2) If the actual revenue raised nationally in the financial year exceeds the projected revenues set out in the Schedule, the excess revenue shall accrue to the national government, and may be used to reduce borrowing or pay debts.

## SCHEDULE (s.4)

## ALLOCATION OF REVENUE RAISED NATIONALLY BETWEEN THE NATIONAL AND COUNTY GOVERNMENTS FOR THE FINANCIAL YEAR 2022/23.

| Type/level of allocation | Amount in Ksh. | Percentage (%) of 2017/18 audited and approved Revenue i.e. Ksh. 1,413,694.84 Million |
|---|---|---|
| A. Total Sharable Revenue | 2,141,584,412,556 | |
| B. National Government | 1,764,099,760,466 | |
| C. Equalization Fund | 7,068,474,211 | 0.5% |
| D. County Equitable Share | 370,000,000,000 | 26.17% |

## MEMORANDUM OF OBJECTS AND REASON

The principal object of this Bill is to provide for the equitable division of revenue raised nationally among the national and county levels of government as required by Article 218 of the Constitution in order to facilitate the proper functioning of county governments and to ensure continuity of county services delivery to the citizens.

**Clauses 1 and 2** of the Bill provide for the short title of the Bill and the interpretation of terms used in the Bill.

**Clause 3** of the Bill contains the provisions on the objects and purpose of the Bill.

**Clause 4** of the Bill prescribes the allocations for the National Government and the county governments from the revenue raised nationally for the financial year 2022/23.

**Clause 5** of the Bill outlines the mechanisms for adjusting for variations in revenues emanating from revenue performance during the financial year in which this Bill relates to.

Dated the 25th February, 2022.

KANINI KEGA,
*Chairperson, Budget and Appropriations Committee.*

# APPENDIX

## EXPLANATORY MEMORANDUM TO THE DIVISION OF REVENUE BILL, 2022

**Background**

1. This memorandum has been prepared as an attachment to the Division of Revenue Bill (DORB), 2022 in fulfilment of the requirements of Article 218(2) of the Constitution and Section 191 of the Public Finance Management Act, 2012.

2. Article 218 (2) of the Constitution requires that the Bill be submitted to Parliament every year together with a memorandum explaining:

a) the proposed revenue allocation set out in the Bill;

b) the extent to which the Bill has taken into account the provisions of Article 203 (1) of the Constitution; and

c) any significant deviations from the recommendations of the Commission on Revenue Allocation (CRA).

3. Section 191 of the Public Finance Management Act, 2012 requires that the bill be accompanied by a memorandum which explains:

a) the extent, if any, of deviation from the recommendations of the Intergovernmental Budget and Economic Council; and

b) any assumptions and formulae used in arriving at the respective allocations proposed in the Bill.

**Explanation of the Allocations to the National and County Governments as Proposed in the Bill**

***County Governments' Equitable Share***

4. The Bill proposes to allocate County Governments **Ksh. 370 billion** for the financial year 2022/23 as equitable share of revenue raised nationally. This follows an approval of the Third Basis covering the years 2020/21 to 2024/25 for allocation of the share of national revenue among the County Governments. The equitable share allocation has been maintained at Kshs. 370 billion in the FY 2022/23. The retention in county governments' equitable revenue share is informed by the following prevailing circumstances:

a) The budget for FY 2022/23 is formulated at a time of Covid 19 which has affected revenue mobilization and brought with it significant uncertainty in revenue projection. Considering the uncertainty in resource mobilization it is therefore difficult to increase the county equitable share allocation;

b) The Government is implementing a fiscal consolidation plan, which is expected to be shared between the two levels of government, so as to lower the fiscal deficit and slow down debt accumulation. To reflect this fiscal tightening, the National Government recurrent ceiling has been restricted and;

c) The Consolidated Fund Services (CFS) budget for FY 2022/23 has been revised upwards by Ksh. 46.9 billion and therefore in order to retain the deficit at the 2021 BPS level, the National Government ceiling has already been revised downwards by Ksh. 15.0 billion while maintaining the county equitable share at the same level.

5. In addition, the fact that the approved Third Basis for allocation of the share of national revenue among the County Governments is now effectively linked to devolved functions (specifically with weighted parameters for health, roads and agriculture) means that it is now possible to achieve policy objectives of some conditional grants directly through the equitable share. For example, in health and agriculture, the new parameters to be used in distributing the equitable revenue share among Counties closely resemble those currently being used to distribute sectoral conditional allocations. Further, the approved revenue distribution criteria contain a parameter, 'population' with a weight of 18% which is specifically designed to reflect costs of 'other County Services' including village polytechnics.

6. The proposed Equitable Share for FY 2022/23 of Ksh 370 billion is equivalent to 26.17 percent of the last audited accounts (Ksh, 1,413,694.84 million for FY 2017/18) and as approved by Parliament. The proposed allocation meets the requirement of Article 203(2) of the Constitution that equitable share allocation to counties should not be less than fifteen (15) per cent of the last audited revenue raised nationally, as approved by the National Assembly.

**Evaluation of the Bill against Article 203 (1) of the Constitution**

7. Article 218(2) of the Constitution requires division of revenue between the two levels of government and across County Governments to take into account the criteria set out in Article 203(1) of the Constitution. The criteria include factors such as: national interest, public debt and other national obligations and needs of the disadvantaged groups and areas, among others.

Table 1 provides an assessment of the extent to which the requirements of Article 203 (1) have been incorporated in estimating the division of revenue between the national and county levels of Government in the financial year 2022/23.

## Table 1: Evaluation of the Bill against Article 203 (1) of the Constitution

| | ITEM DESCRIPTION *(Kshs. Millions)* | FY2018/19 | FY2019/20 | FY2020/21 | FY2021/22 | FY2022/23 |
|---|---|---|---|---|---|---|
| | **ORDINARY REVENUE (EXCLUDING AIA)** | **1,499,757** | **1,573,418** | **1,574,009** | **1,775,624** | **2,141,584** |
| A | **National Interest** [Article 203 (1)(a)] | **84,186** | **94,168** | **86,753** | **83,197** | **90,727** |
| | *Enhancement of security operations (police vehicles, helicopters, defence etc.)* | 27,800 | 27,974 | 24,816 | 22,261 | 25,967 |
| | *National irrigation & fertilizer clearance* | 11,775 | 11,103 | 11,375 | 11,199 | 14,676 |
| | *Youth empowerment* | 7,442 | 16,226 | 16,127 | 14,548 | 14,364 |
| | *National social safety net - (for older persons, OVC, child welfare, presidential bursary, severe disability)* | 26,812 | 26,362 | 28,832 | 29,286 | 29,817 |
| | *Primary school digital literacy program* | 6,333 | 8,400 | 1,500 | 1,800 | 1,380 |
| | *School examination fees (KSCE & KCPE& Grade 6(CBC Examination)* | 4,024 | 4,103 | 4,103 | 4,103 | 4,523 |
| B | **Public debt (Art. 203 [1][b])** | **641,514** | **538,802** | **829,906** | **1,174,013** | **930,354** |
| C | **Other National obligations** (Art. 203 [1][b]) | **391,878** | **442,627** | **477,045** | **514,018** | **560,592** |
| | *Pensions, constitutional salaries & other* | 90,573 | 109,526 | 124,451 | 136,978 | 145,951 |
| | *Constitutional commissions (Art. 248(2)) i.e., CRA, SRC, NLC, NPSC, IEBC, TSC* | 233,619 | 261,387 | 281,099 | 299,333 | 321,968 |
| | *Independent offices (Art. 248(3)) - i.e., AG & CoB* | 6,412 | 6,336 | 6,295 | 6,499 | 6,981 |
| | *Parliament* | 34,490 | 36,240 | 36,222 | 37,883 | 50,220 |
| | *Other constitutional institutions-State Law Office and DPP* | 7,602 | 8,765 | 8,154 | 8,371 | 8,713 |
| | *Other statutory bodies (e.g., EACC, RPP, WPA, CAJ, IPOA, NGEC)* | 5,724 | 5,937 | 6,674 | 7,036 | 8,462 |
| | *Judiciary* | 13,458 | 14,437 | 14,150 | 17,918 | 18,297 |
| D | **Emergencies** [Art. 203 (1)(k)] | **6,419** | **6,418** | **5,000** | **5,000** | **5,000** |
| | *Contingencies* | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 |
| | *Strategic grain reserve* | 1,419 | 1,418 | 0 | - | - |
| | **Equalization Fund** [Art. 203 (1) (g) and (h)] | **4,700** | **5,765** | **6,532** | **6,825** | **7,068** |
| E | **BALANCE TO BE SHARED BY THE 2 LEVELS OF GOVERNMENT** | **371,060** | **485,638** | **168,773** | **-7,429** | **547,843** |

| | ITEM DESCRIPTION *(Kshs. Millions)* | FY2018/19 | FY2019/20 | FY2020/21 | FY2021/22 | FY2022/23 |
|---|---|---|---|---|---|---|
| F | **County Government allocation from revenue raised nationally of which; -** | **322,193** | **324,160** | **330,231** | **377,537** | **375,654** |
| | *a) Equitable Share of Revenue* | 304,962 | 310,000 | 316,500 | 370,000 | 370,000 |
| | *b) Additional conditional allocations financed from revenues raised nationally* | 17,231 | 14,160 | 13,731 | 7,537 | 5,654 |
| G | **Balance left for the National Government** | **48,867** | **161,478** | **-161,458** | **-384,966** | **172,189** |

8. **National Interests:** These are expenditures which relate to projects and programmes that:

- are critical to the achievement of country's economic development objectives;
- potentially will have significant impact on social well-being of citizens;
- are anchored in the Vision 2030 and the Medium-Term Plan III (2017 – 2022);
- have significant resource investment requirements; and
- have been specified in the 2022 Budget Policy Statement.

These national interests include; activities aimed at enhancing security operations; national irrigation and fertilizer subsidy initiatives; Youth Empowerment; provision of national social safety net for vulnerable groups and primary school digital literacy program, and school examination fees subsidy. Revenue allocation for these programs is expected to increase slightly from Ksh. 83.2 billion in 2021/22 to Ksh. 90.7 billion in 2022/23.

9. **Public Debt:** The Bill has fully provided for all public debt related costs. These comprise of the annual debt redemption cost as well as the interest payment for both domestic and external debt. In financial year 2022/23, the revenue allocation for payment of public debt related costs is expected to decrease from Ksh.1,174 billion allocated in financial year 2021/22 to Ksh. 930.4 billion.

10. **Other National Obligations**: as provided for under Article 203(1) (b) of the Constitution, the Bill has also taken into account the cost of other national obligations, such as, mandatory pension contributions and/or payments, financing for constitutional offices, including Parliament as well as expenses relating to other statutory bodies. These are estimated

to cost Ksh. 560.59 billion in financial year 2022/23 up from Ksh.514 billion in financial year 2021/22.

11. **Fiscal Capacity and Efficiency of County Governments:** The Third Basis for sharing revenue raised nationally among county governments has two components namely: i) Allocation Ratio which relates to application of ratios used in FY 2019/20 to one-half of the equitable share allocated to county governments in FY 2019/20; and ii) the Formula which relates to application of the difference between the determined equitable share and the amount allocated using the Allocation Ratio to the parameters approved in the basis.

12. **County governments' ability to perform the functions assigned to them and meet other developmental needs of the county governments:** County governments are allocated equitable share of revenue which is an unconditional allocation to enable counties have autotomy to plan, budget and implement development projects based on county priorities and account for the same. In addition, Article 209 of the Constitution has assigned counties revenue raising powers and as such counties are expected to improve and maintain sustained collection of their own source revenues.

13. It should also be noted that, in order to balance between priority development and performance of the assigned functions, the Third Basis formula is premised on eight parameters which relate to devolved functions assigned to county governments in Part II of the Fourth Schedule of the Constitution. Accordingly, counties will have to allocate a prescribed minimum to specific functions contained in the Third Basis.

14. Thus, the proposed vertical division of revenue proposed in the Division of Revenue Bill, 2022 therefore takes into account the cost of County Governments' developmental needs and it is expected that county governments will have the ability to perform the functions assigned and transferred to them as contemplated under Article 203(1) (f).

15. **Economic Disparities within and among counties and the need to remedy them:** Allocation of the sharable revenue (i.e., equitable share of Ksh.370 billion) among counties is based on the Third-generation formula approved by Parliament in September, 2020 pursuant to provisions of Article 217 and Section 16 of the Sixth Schedule of the Constitution. The Third Basis formula which should be applicable from FY 2020/21 to FY 2024/25 has taken into account the following parameters; (i) Population (18%); (ii) Health Index (17%); (iii) Agriculture Index (10%); (iii) Urban Index (5%); (iv) Poverty Index (14%); (v) Land Area Index (8%); (vi) Roads Index (8%), and; (vii) Basic Share index (20%). The horizontal distribution of County Governments'

equitable revenue share allocation of Ksh.370 billion for FY 2022/23 shall be based on the Third Basis Formula. Accordingly, in FY 2022/23, the Counties will share an estimated Ksh. 370 billion. It should be noted that the Third Basis formula, which will be applied in FY 2022/23, takes into account disparities among counties and aims at equitable distribution of resources across counties.

16. Further, it should be noted that Ksh. 7 billion has also been set aside for the Equalization Fund in 2022/23 which translates to 0.5 per cent of the last audited revenue accounts of governments, as approved by the National Assembly. This Fund is used to finance development programmes that aim at reducing regional disparities among beneficiary counties.

17. **Need for Economic Optimization of Each County:** Allocation of resources to County Governments was guided by the historical costing of expenditures for functions assigned to the County Governments. The equitable share of revenue allocated to County Governments in the financial year 2022/23 is Ksh.370 billion, an allocation which remains unchanged from the FY 2021/22. This is an unconditional allocation which means that the County Governments can plan, budget and spend the funds independently. With the resources, therefore, County Governments are in a position to prioritize projects and consequently allocate resources thus optimizing their potential for economic development.

18. **Stable and Predictable Allocations of County Governments' Vertical Share of Revenue:** The county governments' equitable share of revenue raised nationally has been protected from cuts that may be occasioned by shortfall in revenue raised nationally, more so in the advent of the effects of Covid-19 Pandemic. According to clause 5 of the DoRB 2022, any shortfall in revenue raised nationally is to be borne by the National Government, to the extent of the threshold prescribed in Regulations by the Cabinet Secretary.

19. **Need for Flexibility in Responding to Emergencies and Other Temporary Needs:** Included in the equitable share of revenue for the National Government is an allocation of Ksh.5 billion for the Contingencies Fund established pursuant to Article 208 of the Constitution. This Fund will be used to meet the demands arising from urgent and unforeseen needs in all Counties that suffer from calamities in the manner contemplated under Section 21 of the Public Finance Management Act, 2012. In addition, the Public Finance Management Act, 2012 and the PFM (County governments) Regulations, 2015 requires each county government to set up a County Emergency Fund. County

governments are expected to set aside at least 2 % of their budget as part of their allocation for this purpose.

20. It should be noted that after taking into account all the other factors contemplated under Article 203(1) of the Constitution, including the needs of county governments, there is minimal resources left to finance other National Government needs, such as, defense, roads, energy etc. In fact, this leaves a balance of Ksh. 172.19 billion. This balance includes the requirements of Ksh. 46.4 billion for *"Other statutory allocations/earmarked funds (e.g., NG-CDF, Affirmative Action)."*

**Response to the Recommendations of the Commission on Revenue Allocation (CRA)**

21. The Division of Revenue Bill, 2022 proposes to allocate county governments an equitable share of Ksh. 370 billion from the shareable revenue raised nationally. The CRA reiterates County Governments' equitable share of revenue of Ksh 370 billion as an unconditional allocation to be shared among county governments on the Third Basis of the formula for sharing revenue approved by Parliament. In this case, there is no difference in the amounts of proposed allocation of equitable share to county governments by both CRA and the Division of Revenue Bill. 2022. CRA's Recommendation is premised on the following seven criteria provided for in Article 203(1) of the Constitution;

i.) National interest,

ii.) Provisions in respect of the public debt and other national obligations;

iii.) The needs of the national government, determined by objective criteria;

iv.) The need to ensure that county governments are able to perform the functions allocated to them;

v.) The fiscal capacity and efficiency of county governments;

vi.) The desirability of stable and predictable allocations of revenue; and

vii.) The need for flexibility in responding to emergencies and other temporary needs, based on similar objective criteria.

22. **CRA Recommendation is based on the following:**

i) **Economic growth:** The Commission is cognizant of the need to stimulate the economy following the slump occasioned by the COVID-19 global pandemic. However, given the limited fiscal space the Commission recommends that each level of government restructures its expenditures to stimulate the economy.

ii) **Revenue performance:** The expected slow recovery of the economy and the 2022 general election are likely to affect revenue performance negatively in the financial year 2022/23. To contain the fiscal deficits within the recommended target there is need for equitable shares to be retained at the financial year 2021/22 levels.

iii) **Debt Sustainability:** Persistent underperformance of revenues has led to increased fiscal deficits occasioning the accumulation of more debt to finance government functions. This call for fiscal consolidation to contain the public debt.

iv) **The 2022 General Election:** The general election will be held in August 2022. It is important that the national government restructures its expenditures to finance the election as a matter of national interest.

23. Additionally, the DORB 2022 proposes additional Ksh.5.6 billion to be financed from the National Government share of revenue to the County government comprising of Kshs 5.2 billion for leasing of medical equipment and Kshs 454 million to supplement construction of County headquarters whereas CRA has not made any additional proposals to fund Counties.

**Conclusion**

24. The proposals contained in the Bill take into account the fiscal framework set out in the 2022 BPS and are intended to ensure fiscal sustainability specifically against the backdrop of escalating expenditure pressure on the fiscal framework occasioned by increase in Consolidated Fund Services (CFS) and the persistent under performance of the ordinary revenue.

25. The proposed equitable share allocated to county governments in the Division of Revenue Bill, 2022 has also taken into account the approved Third Basis for Revenue Allocation. The proposed Kshs 370 billion allocation among county governments pursuant to Article 217 of the Constitution is equivalent to 26.17 per cent of the FY 2017/18 revenue which is the most recent audited and approved revenue by the National Assembly. This is above the minimum threshold required under Article 203(2) of the Constitution.