ANALYSIS OF THE BUDGETARY PROCESS IN KENYA AND RECOMMENDATIONS FOR IMPROVEMENT

By

KIPKIRUI, Gilbert Cheruyot

THESIS

Submitted to

KDI School of Public Policy and Management

in partial fulfillment of the requirements

for the degree of

MASTER OF PUBLIC POLICY

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Committee in Charge:

Professor KIM, Taejong, Supervisor ....

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Abstract

Analysis of the Budgetary Process in Kenya and Recommendations for Improvement

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Budget reform is a continuous process for governments that seek better ways of allocating public resources. As government expenditure develops into the process of delivering services to the public, concerns about accountability, transparency and efficiency in budgeting process will certainly grow. This study reviews development of budget reforms in Kenya over past decades and the role of legislature in the budget process. In spite of past attempts, this study identifies that the budgeting process in Kenya is yet to be an accountable, effective and efficient tool for translating policies into tangible results. Poor synchronization between policy making, planning and budgeting has led to a disparity between what government promises in its policies and what the government can actually manage to pay for. Budgeting has become a struggle to keep things afloat, rather than allocating the little resources based on planned policies intended to achieve agreed objectives. This study recommends that policy making, planning and budgeting are three important processes that need to be linked. This study also illustrates that in Kenya, parliament's role of authorization, oversight and supervision of budget process is less effective. Limited capacity, high turnover of parliamentarians during elections, and little interest in the budget process by parliament have led to parliamentary budget committees failing to effectively examine the budget prior to its formal adoption. This paper recommends establishment of a dedicated parliament budget office to provide legislators with objective and nonpartisan analysis necessary for informed economic and budget decisions, among other comprehensive institutional reforms in the budget and budgeting process in Kenya.

With gratitude to God, this thesis is dedicated to Bridget, Gloria and Nancy.

Always there!

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Analyses, opinions and conclusions expressed or implied in this study are mine and do not necessarily represent views of above mentioned individuals and organizations.

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Acronyms

CEPR	Center for Economic Policy Research
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GoK	Government of Kenya
IEA	Institute of Economic Affairs
IMF	International Monetary Fund
IPAR	Institute for Policy Analysis & Research
KDI	Korea Development Institute
KIPPRA	Kenya Institute for Public Policy Research & Analysis
MTEF	Medium Term Expenditure Framework
NBER	National Bureau of Economic Research
OECD	Organization for Economic Cooperation & Development
PRFB	Program Review & Forward Budgeting
PIP	Public Investment Review
S.O	Standing Orders
UNSTATS	United Nations Statistics Division
ZBB	Zero-Based Budget

Chapter 1: Introduction

A government budget is a financial plan for the country. It outlines key sources of revenue to the government and how the revenues are to be spent in a given time, usually one year. This budget defines government policies, strategies and fiscal implications of public programs over the financial year while concurrently identifying resources required for implementing the programs. The budget is therefore a key indicator of a government's priorities on the diverse developmental needs of a country. Unless the budget is carefully prepared in substantial detail, inefficient and wasteful expenditure is more or less a certain outcome - a tragic loss in nations with limited resources such as Kenya.

Government budget is essential for achieving three significant policy objectives (Renzio 2004; Schick, 1999; World Bank, 1998):

a) Fiscal discipline: This involves decisions regarding total revenues, expenditures and financing arrangements to determine the size and form of government intervention in the economy. Aggregate expenditure ceilings should be set before any decisions on budget items to avoid obliging all spending demands, and should be sustainable over the medium-term.
b) Allocation efficiency: Expenditures ought to be done on the basis of government strategic priorities, and on considerations of effectiveness and equity. This requires a coherent linkage between policy, planning and budgeting both within and across sectors.
c) Operational efficiency: Spending agencies should utilize resources in order to maximize their outputs and outcomes. Predictable disbursements, building adequate capacity and correcting perverse institutional incentives can assist in this respect.

Though the concept of the budget as a gauge of performance is relatively new in many developing countries, Masya and Njiraini (2003) observe that it is steadily gaining ground with the dawning of more transparency and accountability in government.

1.1 Statement of the Problem

The budget process[1] is a process of deciding on the services to be provided by the government, ways to pay for and also how these services are to be provided. The central budgeting problem is: On what basis shall it be decided to allocate X funds to activity A instead of activity B? (Mikesell, 2007). Every government has some method for making these fiscal decisions. Budget is a result of budgeting process, the way which decisions about use and funding of public resources are made, from drafting of a budget law to its implementation.

Governments can operate with a haphazard budget process. However, a system designed with incentives to induce public officials to act in response to public needs is more likely to result in choices in the interest of the general public in the desired quality and quantity, at the desired times, locations and at the right cost. At minimum, the process must recognize competing claims on resources and should focus directly on alternatives and options.

Reforming systems of public finance management in Kenya has long been a priority for the Kenyan government. Improvements in planning, budgeting and budget execution, and oversight were acknowledged to be fundamental in achieving development objectives (Folscher, 2007). Program review and forward budget (1974 - 1986), budget rationalization program (1986 - 1990), public investment program (1990 - 2000), and medium term expenditure framework (2000 - present) are four notable initiatives. The primary objective in these reforms has been to entrench greater fiscal discipline on the government. In spite of these past attempts to reform the

[1] The process of creating a budget for government is known as budget process.

budgetary process, Masya and Njiraini (2003) found that the budget process in Kenya remains an unsatisfactory instrument of achieving public policy objectives.

Though the Kenyan government has carried out the reforms mentioned above, this study notes that these reforms are not sufficient. The budgetary process in Kenya is yet to be an accountable, effective and efficient tool for translating policies into tangible results. Poor synchronization between making policy, planning, and budgeting has led to a discrepancy between what government promises in its policies and what the government can actually afford.

Policy making, planning and budgeting are three important processes that need to be linked. The absence of this interrelation in Kenya has led to a great divergence in policies and budget. Budgeting has become an annual struggle to keep things afloat, rather than allocating the anticipated resources based on planned policies intended to achieve agreed objectives. This paper recommends comprehensive, rather than piecemeal, institutional reforms in the budget and budgeting process in Kenya.

1.2 Purpose of Study

Given the above concerns, the overall objective of this study is to examine various aspects of Kenya's budgeting process that should be reformed to improve budget accountability, efficiency and effectiveness, and thus achieve the fundamental policy objectives of a budget.

More specifically, the study sets out to:

i. Assess developments in budget practice

ii. Examine how the budgetary process is done in Kenya and changes in the budgetary process over the past

iii. Analyze international practices that Kenya can use to improve its budgetary process, especially on the roles of executive and legislature

iv. Make recommendations on any justifiable reforms for Kenya's budgetary process

1.3 Research Questions

This study is based on the following questions:

i. What are the significant developments in international budgeting practice?

ii. What are the past and present budgetary processes in Kenya?

iii. What weaknesses are prominent in Kenya's budgeting process?

iv. What lessons are available for Kenya from international best practices?

1.4 Limitations of the Study

Countries have different resource envelope sizes and thus priorities are not the same. While some countries can afford high costs of implementing budgets, some like Kenya cannot afford to have complex budget systems that take resources to monitor/audit. This study does not take into account the costs of implementing different reforms. This study however, is of the opinion that any reform that seeks greater efficiency and effectiveness is worth implementing despite the immediate costs since more resources will be saved in the long run. Further, the Kenyan public's demand for a government that does more with less will persist, so an important focus of budget reform efforts is to develop budget presentations that improve on efficiency and effectiveness. Budgeting system that seeks to hold managers accountable for what they achieved, not how they did it - results-based accountability, is therefore advocated.

This study expands budgeting scope to cover policy review, planning, resource allocation, budget implementation, activity monitoring and expenditure accounting, and evaluation and audit. This comes both as a strength and weakness of this study. The weakness is that comparisons may become a bit too generalized, and thus this study does not cover every aspect in complete detail.

1.5 Delimitations of the Study

As mentioned above, this study expands the budgeting scope to cover policy review, planning, resource allocation, budget implementation, activity monitoring and expenditure accounting, and evaluation and audit. Covering a wider range means that broader picture is analyzed. Reviewing a wider range of context recognizes the inter-linkages among different phases of budget process that would be essential for the process to meet objectives of public policy, and helps provide a good foundation for this study to make necessary recommendations to budget stakeholders in Kenya. Another strength is that it provides a better dimension for comparisons with international best practices for improved understanding of the weaknesses in the Kenyan budget process

Recommendations made in this study are based on what other countries have done. This means that each recommendation is tested and has known weaknesses and strengths. This gives a better platform for this study in making informed suggestions.

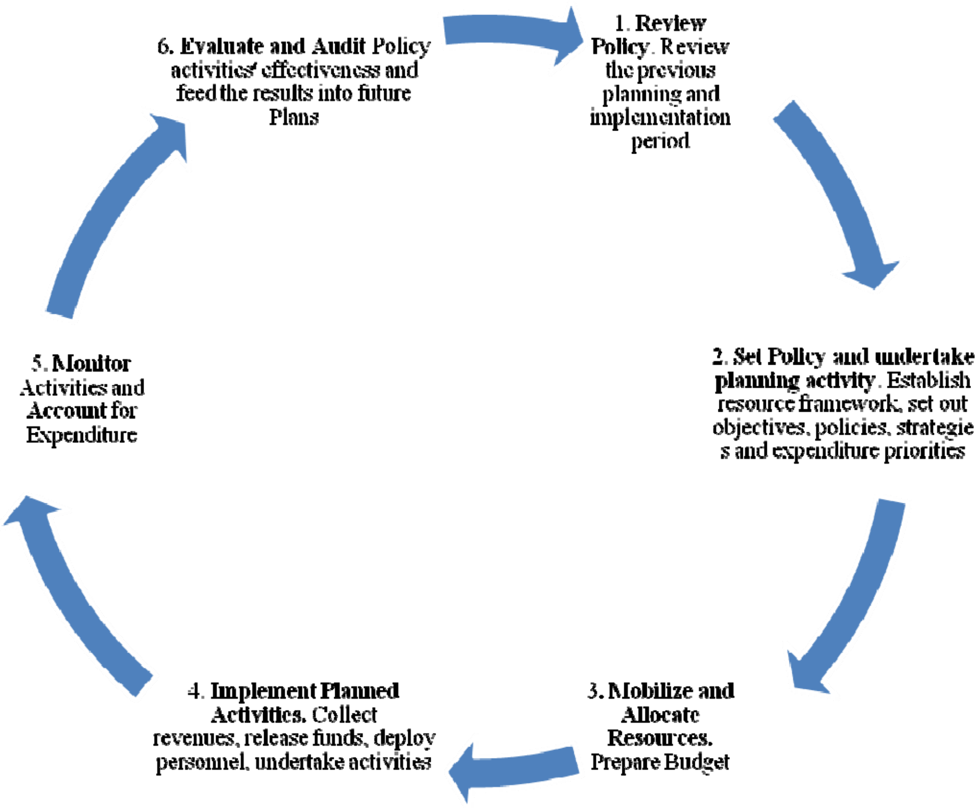
1.6 Significance of the Study

The government of Kenya has carried reforms on its budgeting process over the past. Several studies have been done on these reforms but these studies have been focused on budget preparations and execution at the very most. This study examines various aspects of Kenya's budgeting process in two fronts: the budget layout and the budgeting process, with a special focus on the role of the legislature. Results of this study should therefore be used by stakeholders to design and implement, in a broad sense, a more transparent, accountable and efficient budget.

Furthermore, this study considers budgeting reforms done in other countries that have succeeded in using budgeting as a policy tool to argue that more comprehensive reforms are vital to improve the budgeting process in Kenya. This study therefore, enriches the existing literature by providing a wider analysis of the budgeting process.

This study attempts to provide a broader view of budgeting as mentioned earlier. This view considers the budget cycle to include six phases: policy review, planning, resource allocation, budget implementation, activity monitoring and expenditure accounting, and evaluation and audit, as shown in Figure 1 below.

Figure 1: Linking policy, planning and budgeting in planning and resource management cycle (Adapted from: World Bank, 1998, p. 32)



1.7 Structure of the Study

The study is organized into five chapters. The first chapter covers introduction, problem statement, study objectives, research questions, limitation and delimitations of the study, and significance of the study. The second chapter gives an overview of budgeting by examining various literatures. Over the years, experts have emphasized the importance of budget as a policy tool. This study follows the development of literature from focusing on budget layout formats and systems to emphasizing institutions that are or should be involved in budgeting. The third chapter discusses research methods utilized in this study. The qualitative nature of research design is presented with a rationale for its usage. Research design, sources of data and information analysis procedures are discussed, followed by a discussion on validity and reliability of these methods. The fourth chapter presents findings on budget process in Kenya after providing an overview of changes in Kenya's budgetary process over the past. It also analyses the role of the legislature in budget process as stipulated in the Constitution of Kenya and other policy documents. The fifth chapter is conclusion and recommendations. This chapter interprets what the Kenyan process implies and provides recommendations based on the international models that can improve the budgeting process in Kenya.

Chapter 2: Literature Review

2.1 Introduction

This section starts with a snapshot of Kenya's economy to provide a broad picture of the economic situation in Kenya over the past years, drawing on the existing literature. The literature shows that Kenya has experienced fluctuating economic performance since independence. This section gives a reader an understanding why Kenya cannot afford to use its resources inefficiently. The budgeting process therefore must be made transparent and accountable to tax payers. The purpose of the next part of this chapter is twofold: abridge international budgeting discussions, and cite the international best practices which are worth emulated by countries such as Kenya. The purpose of these reviews is to show why accountable budgeting is crucial in Kenya, provide an understanding of previous studies, and place this research in a contemporary context.

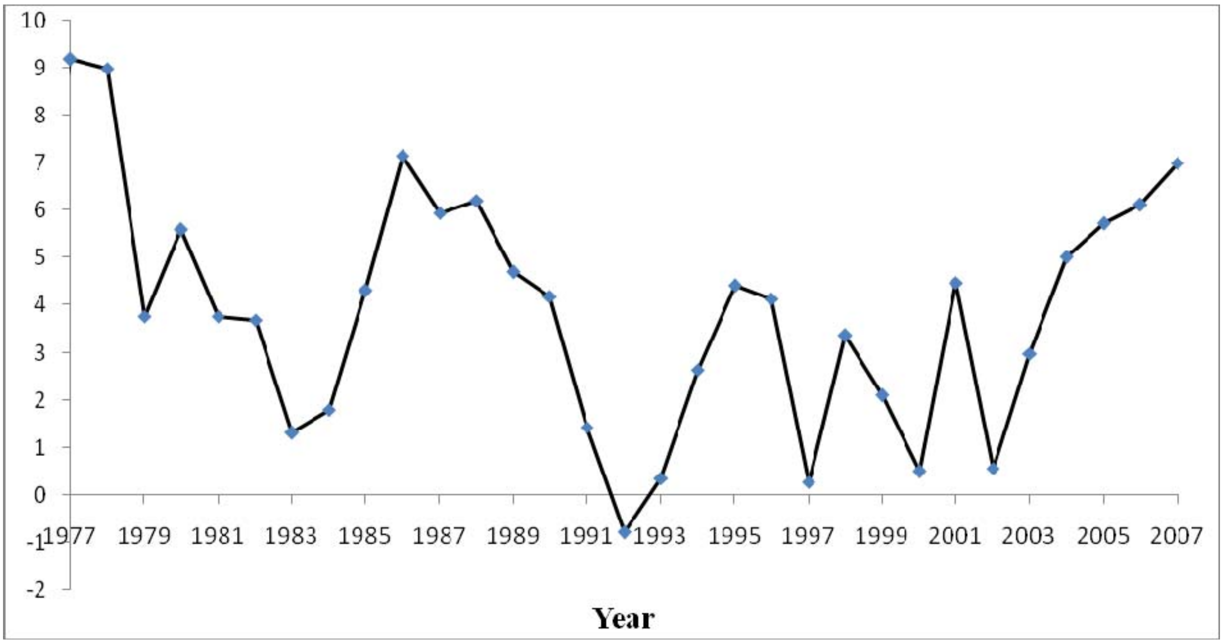
2.2 Kenya's Economy at a Glance

Kenya's growth performance has considerably varied over time. After gaining independence from Britain in 1963, Kenya encouraged economic growth through promotion of smallholder farming, public investment and provided incentives to private investors to invest in industries. In the first decade of independence, the economy performed relatively well, with an average growth rate (GDP growth) of about 6%. This was shadowed by oil shocks of 1973 and 1979 with impacts exacerbated by poor economic policies such as expensive borrowing to finance recurring budget deficits which eventually crowded out private investments. These led to balance of payments problems, with the average growth rate declining to an average of 5.2% in 1974 - 1979 (Mwenga and Ndung'u, 2002).

In their study, Mwenga and Ndung'u (2002) explain that balance of payment problems forced the country to seek conditionality aid from the Bretton Woods institutions (the IMF and the World Bank), and that consequently substantial donor-driven reforms were implemented in the 1980s and 1990s. Reforms covered almost all sectors of economy, including liberalization of foreign exchange market; opening up of domestic financial and capital markets; reforms in trade and payments system; and privatization and commercialization of public corporations. Despite these reforms, economic performance did not improve and Kenya experienced a meandering progress in GDP, with a general decline in economic performance between the 1980s and early 2000s.

Figure 2 below shows the growth rate of GDP in Kenya for the recent past 30 years as from 1977 to 2007 (UNSTATS, 2008).

Figure 2: GDP Growth of Kenya (1977 to 2007)



As shown in Figure 2, the worst economic performance in Kenya was experienced in the 1990s. In 1991, bilateral and multilateral donors suspended financial aid to Kenya because of concerns of slow economic reforms and weak measures to fight graft in government. This had been preceded by a general decline in growth attributed to unfavorable weather conditions, unstable markets for agricultural produce, dwindling foreign direct investment (FDI) flows due to loss of investor confidence and a shrinking private sector, among other reasons. Growth in GDP stagnated (to -0.7% in 1992), and agricultural production fell at the rate of 3.9 % annually. Subsequently, inflation soured to a peak of 100% in the last quarter of 1993. The government's budget deficit grew to more than 10% of GDP (GoK, 2007b).

In response, the government of Kenya, with assistance from the IMF and the World Bank, initiated further economic reforms and liberalization. The government abolished foreign exchange and price controls, and privatized a number of public corporations, reduced the size of civil service, and among other economic policy reforms. The real GDP growth rate averaged 4% per annum between 1994 and 1996, (Mwenga and Ndung’u, 2002).

However, the economy experienced a dent in growth in 1997, partly due to unfavorable weather conditions: El Niño rains which devastated infrastructure and subsequent La Nina drought which contracted agriculture and led to electricity rationing in 2000. GDP growth was negative in 2000. The Kenyan government with help from the IMF and the World Bank initiated further reforms, including establishment of an anti-corruption authority, further reduction in government payroll, and restructuring government procurement process. GDP growth slightly improved as weather returned closer to normal in 2001 (Mwenga and Ndung’u, 2002).

Under new political leadership in 2003, the government of Kenya embarked on further economic reforms and regained mutual association with the IMF and the World Bank. The government purposed to fight graft in public agencies, and enacted the Public Officers Ethics Act 2003and the Anti-Corruption and Economic Crimes Act. A key reform however was introduction of the Medium Term Expenditure Framework (MTEF) budgeting system. MTEF sought to create a macroeconomic environment that would attract private investment and to ensure that there is efficiency in utilization of public resources for wealth and employment creation (Kiringai and West, 2003). These reforms as well as reforms in government procurement and judiciary, led to restoration of aid by development partners and a renewed optimism on the economy.

The restoration of aid by development partners provided a shot in the arm to confidence by investors on the economy. For instance, between 2000 and 2003 net FDI was negative. Foreign investment trickled back in 2004, as demonstrated by rise in the number of operating firms in Export Processing Zones. There was an increase from 66 firms in 2003 to 74 firms in 2004. The total value of investments rose from US $247.3 million in 2005 to over US $278.3 million in 2006.

Generally, the economy started recovery path in 2002, with real GDP growth registering 0.6 % growth in 2002; 3.0 % in 2003; 5.0 % in 2004; 5.7 % in 2005; 6.1 % in 2006 and 7.1 % in 2007. Over the same period, real GDP per capita grew from -1.7% in 2002, 0.7% in 2003, 2.9% in 2004, 3.5% in 2005 and 3.9% in 2006 (GoK, 2007b).

Despite current significant improvement in GDP growth, Kenya still experiences a fiscal balance[2] deficit which stood at 1.5% of GDP in 2007. Central government revenue[3] in 2007 as

[2] Fiscal balance is revenues (including grants) minus expenses, minus net acquisition of nonfinancial assets.

percentage of GDP was 18.6%. Net aid in 2007 expressed as percentage of GDP was 4% and formed 23.9% of central government expenditure. Total external debt[4] also stood at 32.1% of GDP in the same year (World Bank, 2007). These statistics show that Kenya's economy is susceptible which implies that the country cannot afford improvident spending. Budget, as a tool for distributing funds, should ensure that taxpayers and donors are getting the best out of every cent spent.

A budget that is not transparent abets theft of public resources and ineffective service provision as it may lead to abuses of executive power. Improvement of budgeting therefore is part of wider fiscal management reforms that seek to improve management of public coffers. Also, reliance on external finance makes a country vulnerable to external political influences. It also creates macroeconomic instability since the flow of external resources is not guaranteed, and hence can destabilize markets.

A persistent budget deficit is a snag to the economy because a government budget deficit has to be financed. The level of government budget deficit is essential because by and large it affects the amount borrowing the government must get from the private sector to carter for the extra spending during the financial year. Any resources that the government borrows from the private sector are thus not available for investment by the private sector. When there is high deficit in the government budget, the government may have to offer interest rates higher than market rates to attract investors to buy government debt. This has significant consequences for interest rates, inflation, and hence performance of the economy in the long run. High borrowing by government

[3] Central government revenue is cash receipts from taxes, social contributions, and other revenues such as fines, fees, rent, and other income from property sales as a proportion of total gross domestic product (GDP). Grants, although also considered revenue, are excluded here.
[4] Total external debt is the ratio of total debt (sum of long-term debts in the form of official concessional, official non-concessional and private debt plus IMF credit and estimates of total short-term debt and interest in arrears on public and publicly guaranteed long-term loans) to GDP.

now may in future require a rise in taxes. This would again reduce household and private sector spending.

Over a period of time, continuous borrowing by government enlarges the national debt. The implication is that government has to pay more and more interest on debts each year. Opportunity cost of this is that interest payments could have been utilized in a more useful manner, for instance additional allocation to social services such as education. This also represents income transfer from private purses to those who purchased government debts which leads to income and wealth redistribution in the country. This implies that a prudent national budget is essential in Kenya to ensure that fiscal discipline, allocation efficiency, and operational efficiency are achieved.

2.3 Need for Fiscal Discipline

This study takes the perspective that a well laid budget with complementing economic reforms is necessary to achieve stable growth in economy. Several recent studies in Kenya (IEA, 2003, Masya and Njiraini, 2003, Kiringai and West, 2002) have shown that there is need to enforce greater fiscal discipline on government, notably by reforming budgetary process. As noted earlier in this study, budgeting is a set of procedures by which governments ration resources among claimants and control the amount and how each claimant spends. Within this context, budget can be used for three purposes. Firstly, as an instrument of economic policy, secondly, as a tool for economic management and thirdly, as an instrument for accountability.

The budget thus is viewed as an allocation mechanism that attempts to maximize contribution of public expenditure to national welfare. This can be achieved by ensuring that the budget process successfully allocates scarce resources so that each marginal unit of expenditure achieves the same marginal benefit across menus (or spending areas) (Kiringai and West, 2002). In determining resource allocations, a budget should reflect the development agenda of a country through which it influences attainment of national growth and investment targets.

Whereas Kenya has a strong, detailed and well-laid budgetary-legal framework based in the Constitution, and within which the executive branch raises and allocates revenue, weaknesses do exist, especially in relation to such issues as capacity of parliament in budgetary process, secrecy of budget information, management of extra-budgetary activities, violations of budget rules, and extra-budgetary expenditures (IEA, 2003, Masya and Njiraini, 2003). Therefore, there is a need to further refine Kenya's budgetary process, especially in terms of transparency and accountability.

For this reason, in the fiscal year 2008/2009 budget speech, Minister of Finance Hon. Amos Kimunya informed Kenyan Parliament that government will continue to strengthen public sector institutions in order to enhance efficient and effective service delivery. The Minister pointed out that this "will involve deepening budgetary and public financial management reforms, and in particular: (i) working with Honorable Members, develop an organic budget law to mainstream results oriented budgeting in our development strategy…" (GoK, 2008). This is a positive indication that Kenyan government yearns for further reforms in its budgetary process.

2.4 Synthesis of Related Studies

Over the years, experts have emphasized the importance of the budget as a policy tool. Existing literature indicates that budget experts have broadened from focusing on budget layout formats and systems to emphasis on institutions that are and/or should be involved in budgeting. One such institution is legislature. Several studies contain useful references that can be valuable for countries such as Kenya seeking to improve their budgetary process.

The practice of budgeting emerged in Europe during the 19th century as a means of dealing with growth in public expenditure (Schick, 1999). Other studies such as Rockoff (1985) however, argue that national budgeting as a concept started in the United States because executive budget offices were first established in US. These arguments are not essential for this study; what is important is the spirit – the drive to improve accountability and transparency of government operations.

As noted in the introduction, government budgets are intended for achieving three important policy objectives: control of public resources, management of public resources, and planning for the future allocation of the resources (Renzio, 2004; World Bank, 1998; Schick, 1966, 1999). These aims have not changed. What experts are debating is the optimal ways for budget to attain these three objectives. Discussions have centered mostly on budgeting format and the role of legislature in budget process.

Budgeting format is the way in which information in the budget is structured, the kind of information that is needed to substantiate financial requests, and the variety of questions asked during evaluation. The format of a public budgeting system is determined by the level at which governments to control and manage budgets. Budget formats therefore establishes benchmarks by which progress/achievements are evaluated over and above determining rules by which the budget decisions are made (Morgan and Robinson, 2002).

There has been a growing interest in recent years directed to government budget systems (Shah and Shen, 2007; Schick, 1999; World Bank, 1998; Campos and Pradhan, 1996). Several governments are focusing on deriving maximum benefits from scarce resources available and the budget is increasingly being recognized as a key tool for economic management. For example, Von Hagen (1992) illustrates that reforms in budgeting process in New Zealand greatly improved the fiscal condition of that country. The budget in New Zealand is used as a diagnostic and monitoring tool, while at the same time inherent problems such as leakages, shortfalls, delays, irregularities, and ineffectual utilization of resources have been minimized. Folscher (2007) and Sulamane (2006) assert that budget reform is one of critical avenues for developing countries, such as Kenya, to improve their financial management. Ha (2004) affirms that following the financial crisis of 1997, it was necessary to restructure budgetary and financial management systems in Korea for economic rebound.

However, a number of studies have also recognized that a country can have a sound budget and financial system and still fail to achieve its intended targets. According to Schick (1999), this suggests that rules of the game by which the budget is formulated and implemented are equally important and that they do influence outcomes. This acknowledgment has led to a series of budget reforms.

Why does budgeting change? Over time, formats of budget and budgeting processes advance, as new ideas are taken on board, modified, and integrated in response to differences in amounts of resources and existing conventions. Xavier (1996) aptly notes that reforming budgets is an unending process for governments that seek to improve the manner in which resources are allocated.

2.5 Budget formats

A number of budget formats are extant in the literature. Budgeting has been modified from simple traditional budgets to modern formats which are quite complex and technical. Kiringai and West (2002) argue that these changes in budget formats were necessitated by growth in the complexity of government roles and continuous demands for transparency and accountability in government. Most authors focus on four formats: line item budgeting, performance budgeting (PB), program-based budgeting (program budgeting) (PBB), and zero-based budgeting (ZBB) (Mikesell, 2007; Schick, 1966, 1973, 1978, 1999; and World Bank, 1998). The following sub-section discusses these different budget formats with a view of recommending an optimal format for Kenya. This is important since as mentioned earlier, budget formats establish rules by which budgeting game is played and create criteria by which achievements are evaluated (Morgan and Robinson, 2002).

Line item budgets were common when governments had ineffective executive, weak influence by the central government and processes were thus idiosyncratic. It was natural then that financial systems were designed to achieve control over inputs in a simple manner. In a line item system, expenditures are listed as inputs to be purchased, or “line items.” These inputs are often detailed, with specifics of how much cash a specific spending agency will be allowed to expend on salaries, allowances, benefits, equipment and others (World Bank, 1998). The advantage of this structure rests in its relative simplicity, certainty, and for monitoring expenditures through simple comparison with previous periods and through detailed specification of items to be purchased.

This approach however, does not match well with greater demands that come with expansion of government. Line item budgets give information neither about why the allocations are necessary nor on the efficiency of the allocations. Under the line item budgets, Mikesell (2007) observes that efficiency is defined in terms of economizing on inputs rather than optimizing outputs. Spending agents do not have incentives to economize and are not encouraged to relate their activities to the outputs they are intended to deliver but instead, they learn ways of avoiding controls (Kiringai and West, 2002).

Performance budgeting developed due to a continuous pursuit for government efficiency and attempts to incorporate information about outcomes of government actions into the budget process so that financial decisions can be done on the basis of the link between government activity and the cost attached (World Bank, 1998; Schick, 1966). This allows managers to illustrate their workload and respective unit cost. Performance budgeting links expected results to budgets. Emphasis is placed on targets and measured outputs and accomplishment, while information is evaluated against targets and standards.

On the other hand, performance budgets hinge on quality of its performance measure. Some performance measures may be misleading or irrelevant, even though they can be measured and reported. Defining the quality standards of some activities may not be easy. Furthermore, a performance budget does not necessarily ask whether the performance being measured is a service that the public actually wants. This budget structure considers whether an activity is being done at a low cost; it does not consider whether the activity is worth doing.

The program based budget format categorizes proposed expenditures according to organization aims and contribution(s) to the general government objectives. It involves identification of programs, their operational objectives, costs and resources availed. Programs are therefore structured on the basis of their contributions to the strategic objectives devoid of administrative confines of the organizations responsible for delivery of the specific service. Program budgeting represents a significant change from line item budgeting because the classification system focuses on outputs (what government does with resources) rather than on inputs (what government buys with the resources) (Mikesell, 2007; Schick, 1973).

Critics of program budgeting argue that it fails because it attempts to create programs independent of organizational lines, which is probably opposed by civil servants, in light of importance of responsibility and ownership of faults and successes. Program budgeting has impacts where programs are agency- or, at most, sector-specific. The World Bank (1998) adds that since there is no universal index of worth for public programs, it is hardly possible to evaluate programs based on sheer efficiency.

ZBB is not incremental as are the budgets discussed above. Under ZBB, all allocations in the budget are evaluated each year, not merely changes at the margin. For every item in the budget, a question is asked: “suppose we didn’t have this item?” Each agency requesting for budget allocation must justify every cent that it requests (Mikesell, 2007).

Although the ZBB approach would, in principle, facilitate discontinuation of programs that are no longer required, Folscher (2007) argues that it is close to impossible to practically implement. First, like the performance budget approach, it generates masses of paperwork for which there is neither time nor human capacity to the process in budgeting systems. Second, it is not necessarily true that lower-priority programs should receive less funding or be discontinued: the approach fails to take into account the political realities that drive budgets. Third, some public policy areas - for example, those that are driven by legislation - do not lend themselves to dismantling and re-evaluation. In reality, most programs are not amenable to annual evaluation, because even if they are not required by legislation, they involve multiyear contractual relationships with service providers, not to mention public officials. And fourth, it is not self-evident what is maximized if ZBB is adopted in its classical form. In this form, it is an inwardly focused process that puts emphasis on the priorities of managers. Insufficient attention is paid to mapping decisions to preferences and priorities of beneficiaries.

The four formats discussed focused on different stages of expenditure-delivery system, from resources purchased (line item) through activities performed (performance) to services delivered (program). Line-item and performance budgets maintain traditional department structures in the organization of expenditure plans; program budgets classify government outputs (or services provided) without regard for administrative divisions.

Line item budgets have as their foremost concern expenditure control and accountability. Performance budgets seek to improve internal management and operation costs. Program budgets emphasize on improving decision capacity for rational choice. ZBB analyses worthiness of each and every expenditure in the budget. Table 2.1 below provides basic features and foci of line item, performance, program and ZBB formats, as discussed above.

Table 2.1: Alternative budget formats and associated features

Format	Characteristics	Organization Feature	Orientation
Line item	▪ Expenditure by commodity or resources purchased	Resources purchased	Control and accountability
Performance	▪ Expenditure by workload or activity ▪ Presentation of unit cost by activity	Tasks, activities, or direct output performed	Management & operation costs
Program	▪ Expenditure by activities serving common public purpose ▪ Not limited to an organization	Achievements, final product, outcome, or consumer output	Planning
ZBB	▪ Expenditure by output ▪ Not incremental	Cost per output	Prioritization Efficiency

Source: Adapted from Mikesell (2007)

Research conducted by the World Bank (1998) observed that none of these budget formats have been implemented independently at the national budget level. This is because each format has its own respective weaknesses; either too focused and/or too complex. One major reason also cited by other studies such as Schick (1990); Wildavsky and Caiden (1997) is that governments usually aim to achieve several objectives in their policies. For instance, efficiency is an inadequate criterion for allocation in public budgeting even though is an important goal in budgeting (World Bank, 1998). Governments always aspire to have control and accountability, effectiveness and prioritization in a budget in addition to efficiency which all cannot be met effectively under one format of budget.

Though countries such as New Zealand have institutionalized performance budgeting (Shah and Shen, 2007; Campos and Pradhan, 1996), some items in New Zealand's budget are in traditional (line item) format. Though line item budgeting is regarded as weak (Mikesell, 2007; Masya and Njiraini, 2003; Kiringai and West, 2002; World Bank, 1998), authors such as Wildavsky (1978) argue it lasts long and cannot be eliminated "simply because of its weaknesses."

Xavier (1996), while making a review of Malaysian budget reforms, notes that none of reforms experimented with in the US can be universally declared a success. However, most of these performance-oriented tools have failed in one way or another in implementation and not in concept. Premchad (1994) explains that all budget formats are "good and bad". Schick (1969) declares that one budget system cannot 'ignore' the other.

The World Bank (1998) puts it that budget systems include a broad range of supporting services, such as forecasting, estimation, examination, accounting, monitoring, and evaluation. Any budget system is not likely to perform effectively if these supporting services are inadequate. Poor performance also arises when budgets are based on unrealistic assumptions, revised frequently during the implementation period, contain deliberate opportunities for corruption, or are simply unrealistic. In such circumstances, detailed analysis of funds release, expenditure and accounting are necessary. It is also important to consider restructuring the organizations, create better institutions and revise objectives and procedures. Shortcomings will more often than not lie with the environment in which budgets operate and not with the budget systems per se.

2.6 Institutional and legal frameworks

This study takes the perspective that existing institutional/legal frameworks determine the degree of success (or failure) of any budget format. This stance is echoed by Schick (1998), when he argued that New Zealand model should not be emulated entirely by developing countries despite the significant efficiency it suggests. He comments that developing economies are no potential candidates for the New Zealand style because these economies are dominated by informal markets. This study opines that essential changes to strengthen governance should be undertaken first to that pave way for healthy markets, an attitude echoed by World Bank (1998).

Von Hagen (1992) defines budgeting institutions as a collection of formal and informal rules and principles governing budgeting process within executive and legislature. Budgeting institutions divide budgeting process into a number of phases, determine roles of different players, and ensure that required information is shared among various actors. In doing so, such institutions distribute influences, make or break prospects of collusion and hold individual agents accountable for their actions. The constitutional role of budgeting process is to provide a framework in which all competing claims on public funds are manifested and reconciled with each other.

Political will was one reason for the success of performance based budgeting in New Zealand. Across the literature, several studies remark that strong political will, training (guidance), gradual establishment of the desired systems accompanied by corresponding reforms to support performance are indispensable for these tools to achieve reform intentions. Political will is necessary, but this study asserts that political will alone is not equivalent to having legal systems and institutions in place.

Wilks (1995) attributes the failure of program budgeting in Sweden to an absence of mechanisms to control costs and a lack of political commitment to the system. This implies that political will and legal frameworks are independent and thus neither can political will replace the need for legal and institutional frameworks nor vice versa. Kiringai and West (2002) conclude that past reforms as well as current MTEF faced greater obstacles of poor political commitment. This paper takes the position that legislature should have a role in policy review, planning, resource allocation, budget implementation, activity monitoring and expenditure accounting, and evaluation and auditing. New studies championed by the IMF, the World Bank and OECD among other international institutions emphasize the need for the legislative role to be strengthened in the budgeting process (World Bank, 1998; Schick, 1999, 2002b). This is a position informed by history.

Since early 1990s, responsibilities of executive and legislature have been discussed in analyses on institutional limits that play a role in controlling deficits and debt in government budget (Schick, 1990; Von Hagen, 1992, 1994). Studies on the powers of legislatures in budget process have been conducted in several countries, mostly in the US (Schick, 2002a; Shuman, 1992), Japan (Meyer and Naka, 1998) and also in Germany (Wehner, 2001). Salumane (2006) studied role of parliament in Mozambique. In Kenya, IEA made a comprehensive survey (IEA, 2001) on how to strengthen the role of parliament in budgetary process.

Schick (2002b) focused on whether legislature is capable of regaining some of its powers in budgeting. He observes that two advancements are sustaining the work of legislature in budgeting. Firstly is the drive to control fiscal aggregates in order to regulate public finances; secondly is the effort to expand the role of legislature in policies regarding revenue and expenditure. The role of legislature in future will be determined by the outcome of these trends as either harmonizing or conflicting. This study opines that the ability to budget will not change politicians into managers; rather it allows the politicians to exercise their political authority with discipline.

One salient conclusion of these studies is that having a robust budget agency in the executive and an empowered legislature helps in enforcing discipline in the budget. Some studies nevertheless, have argued that fiscal discipline may be weakened by an active legislature (von Hagen, 1992) or the legislative activism could witness a rise in pork-barrel[5] allocations However, a national budgetary process can have clear separation of powers between the legislature and the executive as it is in the US (Blöndal, Kraan and Ruffner, 2003).

Legislature should be supported by impartial budget analysts for it to play a meaningful role in budgeting. Examples of nonpartisan budget analysts for legislature are present in the US (i.e. Congressional Budget Office), Korea (the Parliament Budget Office) and in a number of other countries which do provide independent and objective analyses on the budget (and perhaps large-scale economic) information without polarizing relations between executive and legislative branches. This access by the legislature to technical expertise on the budget is not limited to developed countries only but also there in developing nations such as neighboring Uganda (the Budget Office of Uganda) among others. It is important to note that parliament cannot effectively carry out its budgetary oversight function without proper guidance and knowledge of the budget and the budget making process bearing in mind that the executive is assisted in the budget process by pool of qualified and well versed technocrats. In Kenya, the executive comprehends much about public finance while the parliament knows very little beyond what the

[5] The term "pork barrel politics" is used often to refer to spending that is intended to benefit constituents of a politician in return for their support, either in the form of campaign contributions or votes.

executive intends it to know. The legislature is placed at a substantial disadvantage by this information asymmetry.

2.7 Conclusion

Explaining growth performance in Kenya and understanding the role of the budget in ascertaining answerability of government has been the main objective of this chapter. This chapter covered GDP growth pattern which shows that Kenya is susceptible, implying that the country cannot afford improvident spending. Budgeting, as a tool for distributing funds, should ensure that taxpayers are getting the best out of every cent spent. This chapter progressed to show how government budgets have developed from a simple process to a potential management yardstick. Budgeting has increasingly become a key tool for economic management. This study noted the importance of institutional/legal frameworks in determining success (or failure) of any budget reforms. The impression from the literature is that several patterns are available for countries that seek to reform their budgets. It is envisaged practices in other countries assembled from literature as best practices paints a good picture of reforms needed in Kenya. This will thus form a solid basis for making recommendations on the Kenyan budgetary process.

Chapter 3: Methodology

3.1 Introduction

This chapter discusses the research methods utilized in this study. The qualitative nature of research design will be presented along with a rationale for its usage. This chapter shows how the study mapped out significant developments in international budgeting practice, analyzed budgetary process in Kenya and its weaknesses, and found lessons available for Kenya from international practices. Research design, sources of data and information analysis procedures are also presented, followed by a discussion of validity and reliability of these methods.

3.2 Research Design

This study uses an exploratory, inductive qualitative approach. There are no regression models as the study is not quantitative. In their studies, Bouma (2001) and Neuman (2003) explain that qualitative research is ideal when one investigates the *why* and *how* of policies, not just *what*, *where*, and *when*. Qualitative research is of essence in policy research (such as this study), where understanding *why* and *how* certain outcomes were accomplished is as important as establishing *what* those outcomes were.

Qualitative researches provide useful insights about policies by answering three key questions: Were expectations realistic? Did processes function as expected? Were key players able to perform their roles? The issues of developments in international budgeting practice, Kenya's budgetary process and its weaknesses, and lessons available from international best practices that this study seeks to answer are best answered through qualitative research.

This study is conducted as analytical and descriptive; designed to generate basic knowledge on budgeting, clarify relevant policy issues, unearth problems associated with budgeting in Kenya, and also drafted to provide justified recommendations to make the process transparent, efficient and accountable.

3.3 Sources of Information

This study gathered information by carrying out interviews with key informants to gather up-to-date information, and analyzing relevant documents and materials. The advantage with the interviews is that the respondents can freely discuss issues in their own words more candidly. It also allows the researcher to probe further and ensure that respondents are interpreting questions as intended, and also a chance to explore interesting or unexpected ideas or themes raised by respondents, which is then triangulated with information from government of Kenya (GoK) official documents. These documents include publications of department of Budgetary Supplies, Ministry of Finance, and Ministry of State for Planning. Publications such as national budget, budget articles, national economic development plans, Public Expenditure Reviews, the Constitution, seminar reports, speeches, and Treasury circulars are utilized.

Resources from think-tank and research institutions such as KIPPRA, IPAR, IEA and universities also provide alternative observations on budgeting process in Kenya. Publications from international bodies such as the IMF, the World Bank and OECD are used to review experiences on budgeting from other countries.

Information is also collected from internet websites (e.g. Ministry of Finance website) and through a literature review of related textbooks and documents published. This study also uses information from reputable international journals (e.g. Journal of Public Economics). The following e-databases were used to gather relevant sources: Cambridge journals, CEPR discussion papers, JSTOR, NBER Working papers, Oxford Journals, source OECD and the

World Bank e-library. This synthesis of literature aims to understand theories of budgeting, its importance as a policy tool, and why having it right is important.

3.4 Information Analysis

To analyze the history of budgeting, this study examined literature on budget formats and budget processes that have developed over time, as new ideas are taken on board, modified, and integrated in response to differences in amounts of resources and existing conventions. Characteristics, main organizational features and orientation of these formats are discussed as presented. Weaknesses of each format are discussed and thus sequence of adoption since each format sought to improve on failures of the preceding. This design of describing budget formats to discuss development of budgeting is used by several renowned authors (e.g. Schick, 1999, World Bank, 1998).

This study states repercussions of each procedure finding. Results of status quo are made and lessons that can be drawn from other countries are used as policy lessons for Kenya. This study focuses only on budget processes (or part of processes) that have implications on the overall quality, transparency and accountability of budgeting in Kenya.

3.5 Validity and Reliability

This study uses official policy documents to establish conditions prevailing in Kenya. These government documents guide the budgeting process and thus reflect the true policy stance of the government of Kenya. This study also uses research studies done by think-tank organizations such as KIPPRA, IPAR, IEA and academic institutions to assemble the implications of the guidelines and the overall legal framework. This improves the credibility of this study as the current prevailing situation is weighed vis-à-vis standpoint of other independent observers.

To understand international practice standards, this study utilizes multiple studies conducted by the IMF, the World Bank and OECD. These are international organizations with a vast body of reputable research works. These organizations also provide technical (and perhaps financial) support to countries desiring to improve budgeting process and thus are taken in this study as reliable.

This study attained essential breadth and depth by mirroring Kenya's budgetary process with that of international best practices. Past trends are analyzed for the reader to understand budgeting process and appreciate how having it right is vital for any country. Lessons for Kenya are made using exemplary practices and thus any other similar study looking at the current prevailing situation would reach similar conclusions.

3.6 Conclusion

This study employs an exploratory, inductive qualitative approach which is recommended when one investigates the why and how of policies, not just what, where, and when. Qualitative research provides useful insights about budgeting process in Kenya by answering three key questions: Were expectations realistic? Did procedures function as expected? Were key players able to perform their roles? Issues of developments in international budgeting practice, Kenya's budgetary process and its weaknesses, and lessons available from international best practices that this study seeks to answer are best answered by analyzing policy documents and available literature. The next chapter presents results of these methods.

Chapter 4: Findings - Budget Process in Kenya

This chapter presents findings on policy regulation regarding budget process in Kenya. The chapter begins by describing four budget formats that Kenya has adopted over the past. These include program review and forward budget, budget rationalization program, public investment program and Medium Term Expenditure Framework (MTEF). The chapter then describes the budget process, in particular parliament's role as stipulated in the Constitution and parliamentary standing orders.

4.1 Budget Formats

The Kenyan budget system has changed severally since independence, mainly in response to problems at hand. Government has attempted to make the budgetary process more coherent, efficient, participatory and pro-poor. However, there is still room for improvement as new challenges emerge. Overviews of the main initiatives are discussed below.

4.1.1 Program Review and Forward Budgeting

In early 1970s, the government adopted Program Review and Forward Budgeting (PRFB) with the objective of designing and developing a comprehensive list of public sector projects and programs on a three year basis. It was first put into practice in the budget for fiscal year 1974/75 (Kiringai and West, 2002; Oyugi 2005). The aim of PRFB was to link the national budget with the national development plan. It gave spending agencies indicative three-year rolling ceilings. In return, agencies were allowed to identify priorities on which resources would be spent, but they were required to take the forward cost of their choices into account (Folscher, 2007).

Specific objectives included to (i) generate data that would facilitate the monitoring of project and program implementation by ministries (ii) facilitate identification of the funding agency or funds (iii) contribute to more prudent decision making and (iV0 create a database for design of a system database.

However, as Kiringai and West (2002) and Byaruhanga (2004) noted, the new system did not pay sufficient attention to the process through which allocations were made, with the result that instead of ensuring competition between spending proposals, the new system simply extended incremental budgeting over the medium term. Folscher (2007) argues that PRFB also failed in providing realistic resource frameworks, because resource estimations were not based on realistic forecasts. Spending ministries therefore operated under conditions of resource uncertainty during the spending year.

4.1.2 Budget Rationalization Program

In another attempt to prioritize expenditure, GoK introduced the Budget Rationalization Program in 1985 (Folscher, 2007). It aspired to increase efficiency of government expenditures by devoting sufficient funds to priority programs that would lead to faster economic growth. Resources were devoted to projects that contributed to increased production, created employment, generated income, helped the poor, conserved foreign exchange, and minimized the requirements for recurrent resources (Kiringai and West 2002). The objectives of the BRP were to (i) improve productivity of public expenditures (ii) strengthen planning and budgeting (ii) increase contribution to budgetary resources from user fees and other non-tax revenues i.e. cost sharing, and (iv) structure external assistance more rationally.

Unfortunately, the program did not achieve the transfer of funds from lesser to higher priority projects. Due to resource constraints, resources were reduced across the board without considerations for whether spending was on explicit priorities. At the same time, ongoing projects could not be reduced. Folscher (2007) notes that sectoral planning groups failed to ensure effective links between policy, project planning, and budgeting. Budget structure and classification system made their effective functioning practically impossible. Costs of projects were not assessed properly for project appraisal or budgeting processes (Kiringai and West, 2002; Masya and Njiraini, 2003).

4.1.3 Public Investment Program

As the development budget became gradually unmanageable and the increasing need for renewed investment in public infrastructure, Public Investment Program (PIP) was introduced in 1990. PIP sought to strengthen planning, selection and prioritization of public expenditures to improve quality of capital investments. PIP ranked projects in terms of 'core', 'high priority', and 'other'. The assumption was that a continuing public investment plan would help transform long-term development plans into annual investment activities ((Folscher, 2007; Kiringai and West 2002). PIP thus aimed to: (i) examine the project portfolio and rank them, then provide clear priorities, (ii) Link those priorities to both available domestic and external finances, and macro-economic strategies, and (ii) concentrate scarce resources on selected core priorities.

All the same, PIP faced similar problems as previous reform efforts. Although it was supposed to bring greater attention to priorities, it lacked an adequate review mechanism and had weak links to the rest of the budget process. Agencies used the public investment plan to introduce new projects without completing existing ones. At the same time, projects were not justified in the context of overall sector strategies. Linkages between the public investment plan and resource planning were also inadequate: not even all the core projects were financed (Folscher, 2007).

By the end of 1990s, in spite of the three major reform initiatives, fiscal management in Kenya faced a number of challenges. These challenges included exorbitant levels of spending, insufficient attention to stated policy priorities, and skewed composition of expenditures, with spending on wages and interest crowding out necessary complementary spending on operations and maintenance. A key deficiency remained with failure to establish realistic resource envelopes. Folscher (2007) observes that even though national development plans contained longer-term estimates, these estimates were not the results of rigorous forecasting and were at times unrealistic. In addition, these initiatives were still bound by weaknesses of budget classification system that focused on inputs without paying sufficient consideration to measuring performance against policy objectives.

The joint public expenditure review held in 1997 found that budgeting in Kenya was held back by economic mismanagement, low credibility of the budget process, and low productivity in the public sector (Kiringai and West 2002). Folscher (2007) concludes that although the reform initiatives were to some extent institutionalized, the budget preparation process was in practice still incremental line-item budgeting. Program reviews including evaluation of existing activities were largely ignored. Other weaknesses included poor forecasting ability, failure to cost future resource requirements properly, cash rationing and late release of funds to ministries, fragmentation of spending between budgets and revenue sources, political interference in budgeting especially project prioritization, a limited classification structure, weak expenditure controls, and weak accounting and reporting systems (Kiringai and West 2002; Oyugi, 2005).

4.1.4 Medium Term Expenditure Framework

It was against this background that MTEF was introduced in the budget of 2000/2001 financial year following recommendations of the 1997 Public Expenditure Review which noted that there was no link between budgeting and planning. MTEF process was introduced with two main objectives: (a) to create an economic environment that can appeal and retain investors, and (b) to ensure that public funds are utilized most productively to foster wealth and employment creation.

In implementing MTEF, government agents are obliged to concentrate on expected outcomes of their funded programs. The annual budget with the 3-year MTEF enables evaluation of outputs and outcomes and their contribution to national development. Public and other stakeholders are engaged in the budget process through sector hearings where sector agents discuss their past performance, their program priorities and budget requests.

MTEF planning and budgeting cycle allows for wider consultations to ensure that budget formulation, implementation and oversight benefits from the input of diverse economic actors and interest groups in the economy and output of both the national and district planning processes. Since its introduction, MTEF has changed a few times, necessitated by among other things, an early start of the budget process and need to make it more inclusive. The current budgeting process starts early and benefits from more stakeholder input and participation such as budget hearings and wider circulation of budget documents such as Budget Outlook Paper and Budget Strategy Paper.

These projections of government spending over the medium term are useful for a number of reasons. Firstly, they indicate general policy changes and direction. Without a medium term plan, a budget readjustment to reflect changing circumstances are inclined to be done in blanket, impromptu, and focuses generally on inputs and those items which can be cut easily down. These spending adjustments will not be sustained unless they are policy based. Through revelation of spending implications of current policy choices on future budgets, MTEF also enable evaluation of cost effectiveness and determination on whether the government is committing more than the economy can afford. Medium term spending projections also compels the government to tackle key managerial concerns, for instance, should an activity be done by central government, devolved to a lower level or contracted out to the private sector?

However, as Folscher (2007) opines, the MTEF approach has been less successful in increasing strategic allocations. Although spending on operations and maintenance increased in comparison with personnel spending in the early years of MTEF, the link between stated spending and actual spending priorities is still weak. A persistent weakness in expenditure control is partly to blame for this failure. Weak MTEF-budget institutions in spending ministries and weak links centrally between MTEF and annual budget phases of budget preparation mean that valuable analytical work undertaken during MTEF phase does not consistently translate into prioritized annual budget allocations.

Table 4.1 below gives a summary of these reforms (objectives adapted from Ministry of Finance, 2008)

Table 4.1: Different budget formats and (potential) causes of failure		
Budget Format	**Objectives**	**(Potential) Causes of Failure**
Program Review and Forward Budget (PRFP)	– Provide spending agencies with 3-year ceilings – Establish a method of reviewing priorities and linkage to available resources – Allow for identification of requirements in future that are results of current policies – Recommend a standard for assessing operations of present and planned programs – Provide a linkage between planning and budgeting	– Failure to adhere to budget ceilings – Failure to prioritize programs and activities – Laid more emphasis on item level allocation – Failed to link the budget to national development plan
Budget Rationalization Program (BRP)	– Improve productivity of scarce resources – Improve overall budgetary process especially planning – Increase contribution of non-tax revenues especially user fees to budget resources – Seek donor contributions to increase soft aid and streamline external assistance	– Complexity and lack of flexibility of the forward budget – Failure by development partners to honor their pledges leading to unmet forecasts – Over-emphasis on budget ceilings – Poor prioritization of projects
Public Investment Program (PIP)	– Strengthen project cycle – Instrument to monitor capital formation targets in public sector and ensure that strategies are translated into projects and programs – Assist in synchronizing government investment needs with donor financing – Supervise investment plans of public institutions that impinge on government finances directly or indirectly – Provide correct forecasting of future budget requirements	– Weak linkage between planning and budgeting – Inadequate technical capacity to carry out projects appraisal hence poor cost-benefit estimations – Donor and political influence in project selection and prioritization
Medium Term Expenditure Framework (MTEF)	– Link the annual budget to the long-term development policies, objectives and plans – Improve macroeconomic growth targets through consistent and realistic budget – Enhance resource allocations to inter and intra sectoral priorities – Create responsibility of spending agencies to increased predictability in resource allocations for future planning – Increase incentives for more effective and more efficient utilization of resources by providing agencies with predictable funding levels and increased autonomy	Weaknesses that can so far be identified on MTEF process include: – Failure to achieve aggregate fiscal discipline within government – Poor forecasting ability across spending agencies – Political interference on budget where unbudgeted items are introduced mid-budget execution – Weak link between planning process and budgeting since two separate ministries are responsible for each of these interdependent functions

4.2 Kenyan Budgeting Process

The budget process is a collective function that benefits from the contribution and input of a wide variety of economic players and actors. These include government ministries, the Treasury, Kenya Revenue Authority, Central Bank of Kenya, Parliament, interest groups and the citizens in general.

Estimates of budget requirements are compiled by government ministries or institutions (spending agencies) for consideration by Ministry of Finance. They are then analyzed, consolidated and submitted to parliament by the Minister of Finance in a formal speech to the parliament. Through the Budget Speech, the Minister examines the current and future condition of the country's economy, and makes proposals on how proposed expenditures will be funded (IEA, 2001). This speech to parliament is presented together with Appropriations Bill, Finance Bill, Fiscal Strategy Paper, Financial Statement and Statistical Annex to the budget. The Statistical Annex indicates, among other things, the government's indebtedness to both domestic and external lending institutions, while the Financial Statement gives a summary of proposed revenue and expenditure measures.

Section 99 of the Constitution of Kenya ascertains the protector of public coffers as the parliament. The legislative branch is therefore expected to act as a check or balance on the executive branch. Legally, once the budget is formulated, it must be presented before the national assembly not later than 20th June of each financial year (Constitution of Kenya, Section 100, National Assembly Standing Orders (S.O.), 133). This provides members of parliament an opportunity to scrutinize budget allocations and anticipated sources of funds. To enable the government to finance its operations during this stage, parliament votes to authorize by vote on account appropriations of funds required for purposes of enabling the government to carry out its plans. The S.O. specifies that debate on annual estimates shall be limited to 7 days immediately after the budget is presented before the House (by 26th June) (S.O., 137, 142).

The debate on each ministry's vote is then commenced. The parliament also has up to the 31st of October to pass all ministerial appropriation bills (votes). Since the law requires that the debate be concluded by the end of October, not all ministry votes can be deliberated in parliament. Any ministry vote that has not been deliberated by the twentieth day is passed using the guillotine method[6] (S.O., 142). During the 2008/2009 fiscal year, for example, the parliament approved KSh162 billion of the KSh670 billion (25%) budget for 34 government ministries and departments without subjecting the estimates to any scrutiny. By 29th of October MPs had only scrutinized estimates for only 8 out of the current 42 ministries (Namunane, 2008). This implies that the parliament is greatly constrained by the law in deliberating on the budget.

In essence, the relationship between the legislature and the executive is that the government proposes and the parliament only consents. Brazier (2007) draws an analogy where the executive determines the amount, to whom and the time it should be paid, and the legislature simply endorses. This is truly because on the 20th day, when billions of shillings are authorized with little inquiry, parliament is portrayed more or less a yielding spectator.

In addition, parliament in Kenya has two House Select Committees established by the S.O. meant to keep government accountable. These are the Public Accounts Committee (PAC) that examines appropriation of sum voted by the House to meet public expenditures, and the Public Investments Committee (PIC) that examines whether government investments are run in

[6] On the last day of budget discussion and voting on allocations, at the appointed time the Speaker puts every question necessary to dispose of all the outstanding matters in connection with the budget debate. This is known as the guillotine. The guillotine concludes discussions on the budget.

accordance under prudent commercial doctrines and discreet commercial practices (ibid 147, 148).

The implementation stage is the longest, lasting throughout the budget process. Permanent Secretaries of various ministries, as authorized by the Treasury, assume the role of accounting officers. They are held accountable for all finances allocated to their institutions. After Parliament has passed the Appropriation Act, Constitution (Section 105) provides that Controller and Auditor General (C&AG) is supposed to ensure that all withdrawals from the Consolidated Funds are legal (IEA, 2001, Masya and Njiraini, 2003).

A well designed budget can be undermined by poor implementation. Various problems are often encountered during the implementation stage: (a) amendment of budget after approval by parliament; (b) over-optimistic projections for donor assistance projections; (c) discrepancy between approved budgets and actual releases; (d) over-emphasis on monitoring cash movements at the expense of monitoring spending commitments (too much focus on cash audit rather than outcome analysis); (e) parliament lagging behind schedule in discussing Controller and Auditor General reports; and (f) over-reliance on donors to finance development projects (Oyugi, 2005; Masya and Njiraini, 2003; IEA, 2001, 2003; Kiringai and West, 2002)

Indeed, parliament’s role of authorization, oversight and supervision of budget process has not been effective. As noted above, the time allocated for the parliament to discuss budget is quite limited. The pattern of preparing line item budget results in budget documents that run into thousands of pages and the squeezed budgetary calendar leaves little time for parliament to scrutinize the budget (IEA, 2001, 2003). It is ironic that S.O. expects the parliament to make a constructive examination of the budget within 7 days. This is further worsened by lack of technical capacity for parliamentarians. This means that the parliament may not be usefully engaged in the budgeting process.

Limited capacity and little interest in the budget process by parliament have led to parliamentary budget committees failing to effectively examine the budget prior to its formal adoption. Parliament's engagement is further limited by substantial turnover of members of parliament (MPs) during elections. The past four general elections can be cited as examples. In a house of 222 members: during the 1992 general elections, less than half (only 49 percent) were reelected; in 1997, 43 percent of members were re-elected; in 2002, about 50 percent were reelected while during 2007 general elections only 30 percent were reelected (Oyugi, 2005). This high turnover of MPs erodes institutional memory. Since there can be no legislation governing the turnover, the point of view of this study is that performance of parliament can be improved by attaching staff to parliament (like Congressional Budget Office in the US) to provide legislators with nonpartisan budget and economic analysis necessary for informed decisions.

The executive branch in Kenya has immense control in the budgetary process. Ministries play important roles in planning, budget formulation and implementation. As discussed earlier, budget execution, audit and monitoring roles of the executive are performed ineffectively. This results in accumulation of pending bills; weak internal checks; and cash rationing which has led to poor performances. Even though the permanent secretaries (the accounting officers) are individually responsible for their ministries' allocations, Masya and Njiraini (2003) note that they are hardly ever penalized when they do not comply with set managerial controls. This has resulted in general non-compliance with financial regulations.

Despite these numerous problems, not all aspects of budgeting in Kenya are gloomy. Informal discussions with officers concerned with the budget process in the Ministries of Finance and Planning indicate that Kenya has been able to improve on experiences of the past programs and has achieved relative success in improving fiscal discipline through MTEF. Over the first few years of MTEF, public spending and deficit contracted as a percentage of GDP. Interest payments decreased as debt stock declined. Kenya has institutionalized public expenditure tracking surveys (PETSs). PETSs are useful instruments for tracking how funds are transferred and used right down to location of service delivery. Kenya also has other instruments such as ministerial public expenditure reviews (MPER) (which culminates to Public Expenditure Review), Budget Outlook Paper (BOPA), and Budget Strategy Paper. Kenya has also made considerable progress in introducing reforms to planning and budget preparation to improve allocation of resources to priorities. It also more recently initiated reforms in budget execution, accounting, reporting, and monitoring systems to ensure a better link between budget and implementation. However, increases in funding will not necessarily translate into improvements in the delivery of basic services, even if the funds are properly disbursed.

Other new changes have been the extension of the budget timetable to star in September rather than December which allows stakeholders more time to be engaged in planning. Also, in the recent past, Kenya's civil society has become gradually more involved in budgetary process (IEA 2003). IEA (2003) concludes that there is need to improve budget information for the public especially the civil society to participate constructively. It is important for the taxpayers to be empowered to actively, efficiently and effectively participate in governance processes such as national budgeting.

Civil society involvement will create awareness and build literacy among the public on the need to safeguard resources by making government accountable for every cent of taxes. The civil society contributions include simplifying the budget and deepening debate through collation, synthesis and dissemination of information. Through its analysis and dissemination activities, civil society organizations can assist in pursuit of government accountability. This occurs, for example, when groups monitor the follow up by the executive to audit reports and parliamentary resolutions. Together with the media, this puts pressure on the executive to take corrective actions.

Analysis of the budget by the civil society can supplement scrutiny by parliament, the media and even the executive. It could also provide specialized information and study on effect of the budget on special interest groups such as the poor and women. This analysis could be fourfold: budgeting process and institutions, sector and group incidences, general macroeconomics, and revenue analysis. Involvement of the civil society in Kenya therefore is a move to the right direction. At the time of writing, several reforms were underway including the revision of the parliamentary Standing Orders.

Chapter 5: Conclusion and Recommendations

This study aimed at examining the budgetary process in Kenya in an endeavor to provide recommendations for improvement. This study used an exploratory, inductive qualitative approach which is ideal when one investigates the *why* and *how* of policies, not just *what, where, and when*. This study examined Kenya's budgeting process on two fronts: the budget layout and the budgeting process, with a special focus on role of the legislature. This study reveals that despite several reforms in the past, key weaknesses persist in the budgetary process in Kenya.

The next section of this chapter highlights salient implications of some steps in the budgetary process. This section is followed by specific recommendations.

5.1 Conclusions

A key revelation from this study is that budgeting in Kenya is yet to be accountable, efficient and transparent. There is urgent need for a deliberate reform of the budget. In this study, the need to have comprehensive rather than piecemeal reforms is emphasized. Comprehensiveness is not about struggling to accomplish everything at the same time. Rather, it is taking an extensive attitude to identify weaknesses, understand existing inter-linkages and evaluating hurdles, and then identifying the most suitable way to introduce reforms in phases.

Although some argue that the comprehensive approach involves lengthy time span than the narrowly focused approaches, there are several reforms which failed when the initiative has not been comprehensive and the narrow approach addressed parts of the challenge. In instances where comprehensive reform efforts have failed, it has mostly been due to poor understanding of the underlying problem.

While the design of a comprehensive reform program that recognizes links between public finance management institutions represents important progress, one great challenge in Kenya is little political determination to make the reforms. This political will needs to be backed up by motivated implementers who can manage changes, demonstrate benefits, and pass on skills. A sequenced and prioritized comprehensive approach is needed to further Kenya’s budget reforms to secure progress and build on existing successes. There is need to focus on achieved outcomes, while making sure that lessons are understood and lapses not repeated, ensuring that lessons by individuals are translated into development of the institutions.

This study recognizes that improvements in planning, budgeting and budget execution, and oversight are fundamental in achieving key development objectives. Building capacity for public financial management and strengthening existing legal framework is crucial to the reform program. The reform program should include components to improve credibility of the budget, transparency, effectiveness, accountability and policy-based budgeting.

There is need for a shift away from a traditional system of line item expenditure controls to a system that focuses on delivery of specified outputs and outcomes. Budgetary allocations are more likely to be driven by input costs when budget management is tied up with budget structure and classification. This tends to force budgeting back to line-item incremental budgeting. A programmatic classification that enables better links between policy priorities, ministerial objectives, and funding programs would help bring the final stage of detailed budgeting in line with earlier sector and ministerial allocation processes. Fully reforming the classification system and linking the new budget classifications to budget controls and the chart of accounts for implementation and reporting should be a priority on the reform agenda. Translating the budget into programs and sub programs is useful in providing a basis for tracking and interrogating budgetary allocations and budget implementation by various government ministries and agencies. It will also buttress a firm foundation for systematically monitoring and evaluating progress towards the realization of development targets.

Reforming budgeting institutions is an important part of a policy seeking to achieve better fiscal outcomes. This does not mean that a change in legal and procedural rules mechanically produces better results. However, the outcomes of political decision-making processes are shaped by institutional environments within which these processes develop, and reforms of the budgeting process contribute significantly to achieving better fiscal outcomes. As noted earlier in this study, quite often, institutional reforms (such as Korea's) are usually the result of fiscal crises, of times when there is widespread awareness and a general gratitude of the need for change. Strong institutions help to make this attentiveness long lasting and thus serve as a commitment mechanism for good fiscal performance.

There are extensive differences internationally in the responsibilities of legislatures in budget processes. These roles are determined to some extent by constrains of country's constitution, as well as the political environment which the legislatures operate. The US Congress has the power to alter or discard budget proposals of the executive branch. The Congress also has authority within the constitution to design alternative budget. Though this paper does not recommend a full constitutional review in imitation of the US system, the system provides important lessons that Kenya (the Westminster system) can emulate.

This study has indicated that the existing system for budget interrogation in Kenya is not effective. Whereas the legislature is responsible to reaffirm and assert its position concerning fiscal analysis, the executive has a responsibility to relate constructively with parliament in budget process. The executive and the legislature should recognize that good scrutiny is good governance. At minimum, there should be more chances for parliament to deliberate and consider government's budget proposals and more opportunities to shape priorities. A case is also made for greater public discussions on alternatives and concerns faced by government.

5.2 Recommendations

Specific essential recommendations that can be deduced are as follows:

1. **Adopt new budget format:** The current classification of public expenditure in Kenya (line item budget) fails to indicate the purpose of expenditures. The classification focuses on financial inputs rather than outputs or expected outcome(s), discourages consideration of alternative options of reaching a desired objective or service level. In as long as core incentives for budget management are tied up with budget structure and classification - for example, if the budget is structured by administrative unit, allocations are more likely to be driven the by input cost of organizations than by outputs required to meet enumerated policy objectives - this situation would tend to force budgeting back to line-item incremental budgeting.

   A strong case is put in this study for a programmatic classification that enables better links between policy priorities, ministerial (agency) objectives, and funding programs. This would help bring the final stage of detailed budgeting in line with the allocation processes. Entire reforms on the classification system and linking new budget classifications to budget controls and the chart of accounts for implementation and reporting should be a priority on the budget reform agenda. The move towards performance based budgeting in Kenya is thus a shift in the right direction.

2. **Set up of a Resource Center for Parliament:** Budgeting is a specialized and highly technical field. A resource center which is effectively and efficiently run by multidisciplinary specialists would be critical as it would provide members and the public with neutral, non-partisan, high-quality research, which they would use to challenge ministers in their areas of operations and accountability. Availability of research materials will make the role of a member as an individual and Parliament as an institution, more effective and efficient. This study has cited the Congressional Budget Office of the US as an example of such an institution.

3. **Embed Budget consultative process in the Constitution**: In the MTEF strategy, consultation among key stakeholders is critical. Furthermore, as noted by this study, it is evident in other countries such as New Zealand that better results are achieved where where pre-budget consultations have been entrenched in the law that better results are achieved. To ensure the executive consults the legislature in the budget preparation to implementation processes, the consultative process should be entrenched in the constitution.

4. **Simplify and publicize budget:** A budget should provide unambiguous information on all aspects of government policy. The technical-jargon language used in the budget should be simplified to make it easy for the laypersons to read and comprehend the document. The budget should also be made accessible to the public through the media, internet, as this would demystify the budget.

5. **Reduce budget optimism:** As indicated in the literature, budgets that are over-optimistic tend to be non-transparent. Throughout its history, Kenya's Treasury has repeatedly

provided over-optimistic predictions of the economy. The executive can often blame external shocks, natural calamities and poor climatic conditions for its failure to achieve its macroeconomic targets. There is need to utilize macroeconomic modeling that accounts for these occurrences.

6. **Build Capacity on Budgeting:** Political commitment and enforcement by the management alone will not succeed if civil servants lack the capacity to implement the budget successfully. A performance budget, which this study recommends, will be seriously challenged by a lack of capacity. Without adequate training, managers and other implementers are unlikely to understand potential value of a results-oriented approach or be able to provide for effective implementation and use. Trainings can make a difference, not only by grooming competent executers of the budget but also by changing attitudes.

In conclusion, this study has shown that despite several reforms in the past, key weaknesses persist in the budgetary process in Kenya. The process is still plagued by a critical disconnect between the Medium Term Expenditure Framework and the yearly budget preparation and the underlying shortcomings of the budget structure and classification system. In addition, despite initial reforms on the budget execution side, budget implementation discipline is still very weak. These factors underpin difficulties in realizing political priorities in the budget. Poor synchronization between policy making, planning and budgeting has led to a discrepancy between what policies of government promise and what government can actually afford. The potential gains from effective parliamentary inquiry of government finances are significant, as legislature would be offering what the public wishes for: the most efficient use of taxes through effective government services. A comprehensive overhaul of budgeting process in Kenya is necessary.

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