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An Assessment of the Public Expenditure and Financial Accountability in Makueni County

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Introduction

The Public Expenditure and Financial Accountability (PEFA) assessment was carried out in the County of Makueni and five other counties, namely: Nakuru, Kajiado, Baringo, West Pokot and Kakamega. The exercise was undertaken by KIPPRA in conjunction with the World Bank (Kenya Office) in 2017. This was the first sub-national PEFA assessment in Kenya following devolved system of government. The rationale for the PEFA assessment is to provide a clear and deeper understanding about the functioning of the public finance management (PFM) system and the organizational aspects of existing institutions at county level. The main objectives of the assessment include: i) assess the state of financial management capacity in the county government; ii) identify gaps in capacities, systems, policies and processes in PFM; iii) provide a basis for PFM reforms; and iv) facilitate and develop a self-assessment capacity at the county level.

The users of PEFA include the private sector, civil society organizations, faith-based organizations and international development institutions. The PEFA scores and reports allow all users of the information to gain a quick overview on the strengths and weaknesses of the county's PFM systems. The importance of PEFA is to facilitate the attainment of fiscal discipline, strategic allocation of resources, and efficiency in service delivery.

The assessment covered a period of three (3) fiscal years 2013/14, 2014/15 and 2015/16. It focused on seven (7) key pillars of the PEFA framework, namely: (i) budget reliability; (ii) comprehensiveness and transparency; (iii) management of assets and liabilities; (iv) policy-based fiscal strategy and budgeting; (v) predictability and control in budget execution; (vi) accounting and reporting; and (vii) external scrutiny and audit.

County Administrative and Development Indicators	
Location	Eastern region
Area (km²)	8,0092 km²
No. of constituencies	6
No. of county assembly wards	30
Estimated total population (KNBS 2015)	961,738
Females	493,440
Males	468,298
Population density per km²	120.1
County contribution to national GDP	1.4%
Gross County Product (2017)	Ksh 100.9 billion
Poverty levels (2015/16)	35%

Key Findings of the PEFA Assessment

(a) Budget Reliability

Budget reliability refers to the extent to which a budget is realistic and implemented in accordance with the approved estimates. Although overall budget performance is relatively good in Makueni County, budget reliability is hampered by low rate of budget execution and high level of reallocation. The County prepares the budget in accordance with National Treasury guidelines which require budget proposals to be presented using administrative, economic and programme-based approach using Government Finance Statistics (GFS). Specifically, budget execution and reporting were made only on the basis of administrative and economic classification. Expenditure outside government financial reports represented less than 5% of total budgeted county government (BCG) expenditure.

The absorption rates of the approved budget improved but remained below 80% in the period under review. The low absorption in 2013/14 was because it was the first year of implementation of the devolved system of government in Kenya and counties were left with about 7 months to execute it. In addition, low absorption was attributed to the impact of litigation against the County Government which saw temporary suspension of administrative activities in the County.

Actual revenue collections were also far below target in the three years, but this did not lead to a budget deficit because of the low rate of budget execution.

The key challenge to financial discipline was deviations of actual expenditures from approved budget. This was heavily influenced by fluctuations in consumption of fixed capital and compensation of employees, the two largest items in the budget.

(b) Transparency of public finances

The key focus is on the comprehensiveness of budget, the fiscal risk oversights and accessibility by the public to fiscal and budget information. Generally, budget formulation, execution, and reporting were based on administrative and economic classification using GFS standards. Budget documentation that was transferred to the County Assembly contained forecast of the fiscal deficit/surplus, previous and revised budget in the same format as the budget proposal in the budget estimates and aggregated budget data for both revenue and expenditure. Expenditure outside government financial reports were also reported and they represented less than 5% of total expenditure.

The County Executive placed in its website various documents such as Annual Development Plan (ADP), County Fiscal Strategy Paper (CFSP), County Integrated Development Plan (CIDP), and County Budget and Review Outlook Paper (CBROP). The public was engaged during preparation and approval process of the annual budget through various forums (barazas and radio). Public participation was cascaded downward to the ward levels where ward administrators explain the budget and other public initiatives to the people. Besides, the County Assembly had a library where the documents could be accessed by the public.

All major investment projects were prioritized based on the established public participation framework. The County Government documented its public participation framework. Feasibility studies were carried out prior to implementation of major projects. However, economic analysis to assess the viabilities of the projects were not conducted. The process of monitoring and evaluation of such projects was not clear. In addition, there were no officially-approved contingency funds in the County. However, an emergency fund was created to cater for unforeseen circumstances.

(c) Management of assets and liabilities

Effective management of assets and liabilities is necessary to ensure public investments provide value for money. The County maintained a record of its holdings in all categories of financial assets, which were essentially cash at hand and its participation in one public enterprise. Rules for transfer or disposal of financial assets were also clearly defined and partial information on transfers and disposal was included in Annual Financial Statistics (AFS).

Although the County maintains a register of its holdings of fixed assets and updates records upon acquisition of new assets, the reports about their usage and age were not available. Besides, there was no debt management strategy and reports about the debt inherited from the defunct local authority.

(d) Policy-based fiscal strategy

Budgets and fiscal strategies should be prepared with due regard to government policies, strategic plans, and adequate macroeconomic and fiscal projections. The County's budget preparation was based on a clear annual budget calendar and based on a comprehensive and clear budget circular provided by the National Treasury. Budget ceilings were established during the CFSP preparations but fixed only after the budget calendar is issued. Besides, the County prepared revenue and expenditure forecasts for the current year and the two following years in the CBROP and revenue forecasts in the CFSP, albeit with no clear underlying assumption. However, macroeconomic forecasts were never done, neither was sensitivity analysis on various fiscal scenarios carried out.

The County Executive prepared the CBROP that reviews the previous year's performance in the CFSP, but reasons for the deviations from the objectives were not clearly exposed in the CBROP.

Legislature's review of strategic resource allocation and other elements of the budget proposal were based on organizational arrangements, including specialized review committees, technical support, negotiation procedures and public consultation.

The annual budget presented an estimate of expenditure for the budget year and the two subsequent fiscal years, but these estimates were not supported by macroeconomic forecasts. Besides, strategic plans were not aligned to medium-term budgets to each other and to previous year's estimates.

(e) Predictability and control in budget execution

This focuses on whether the budget is implemented within a system of effective standards, processes, and internal controls, ensuring that resources are obtained and used as intended.

The Directorate of Revenue obtained weekly data from all entities collecting all revenues, which was consolidated into a weekly report and transferred to the Treasury account. However, no audits of revenue from any of the sources were undertaken and payers did not have sufficient access to information on their rights and obligations. Further, there were no systematic approaches for assessing and prioritizing compliance risks for revenue streams.

Reconciliation of the payroll with personnel records took place at least every six months through a payroll audit. Required changes to the personnel records and payroll were updated in time and retroactive adjustments are rare, but there was no evidence that staff hiring was controlled by a list of approved staff positions. Payroll audits were periodically conducted.

The County Government used both the IPPD and manual payroll systems. Generally, the authority and basis for changes to personnel records and the payroll were clear and adequate to ensure integrity of the payroll data. However, this was not the case with respect to the manual payroll.

Moreover, appropriate segregation of duties was clearly laid down and comprehensive expenditure commitment controls are in place. Budgetary units were provided with reliable information on commitment ceilings quarterly in advance and limit commitments to projected cash availability and approved budget allocations.

Regarding public procurement, legal and regulatory frameworks, bidding opportunities and data on resolution of procurement complaints were available to the public. However, no database was maintained to provide information for contracts, value of procurement or who has been awarded contracts. The County relied mostly on Direct Procurement and Request for Quotation, which accounted for more than 60% of total procurement, while open tendering was used for less than 40% of total procurement. The procurement complaint system was nevertheless compliant with good practices, except for charging fees that may prohibit access by concerned parties.

The revenues collected were deposited on a weekly basis to the county collection accounts, which was then transferred to the Treasury account. When revenue was collected by cash, the deposit was made to the Treasury account within one week.

(f) Accounting and reporting

Accounting and reporting look at whether accurate and reliable records are maintained, and information is produced and disseminated at appropriate times to aid decision-making, management and reporting.

The County prepared monthly bank reconciliations for all the key bank accounts. Reconciliations were done as per the County Financial and Procedure Manual every 5th day of the following month.

Annual Financial Statistics (AFS) were generally completed and available for audit, respectively, three and four months after the end of the year. They contained information on revenue, expenditure, financial assets, financial liabilities, guarantees, but not on long-term obligations.

Although internal audits were focused on evaluation of the adequacy and effectiveness of internal controls, no quality assurance process had been put in place to show adherence to professional standards. However, internal audit remained focused on financial compliance, with an indication that most payments were compliant with regular payment procedures.

(g) External scrutiny and audit

These include assessment of external audit and legislative scrutiny of audit reports, specifically the arrangements for scrutiny of public finances and follow-up on implementation of recommendations by the executive. External audits for the County are performed at the national level by the Office of the Auditor General (OAG). Material weaknesses were highlighted in the management letters that are issued to the County. For 2013/14, which was the first year of operation, the OAG stated that the County Executive and County Assembly had challenges in adhering to the existing PFM Regulation and Procedures, the Public Procurement and Asset Disposal Act 2015 and Regulations 2016 and to general human resources management policies and procedures.

Like in several other counties, the scrutiny by the County Assembly, Senate and Parliament did not lead to actions being taken up by the Executive, nor were they transparent to the public. Thus, the external audit was not necessarily effective to enable adjustments and corrections in the PFM system.

(h) Risk assessment

The County did not have a risk management policy and risk register. Consequently, executive and administrative decisions made did not appear to be driven by risk assessment and management activities. Given the absence of a risk profile, risks were not evaluated hence the likelihood of occurring almost at all budget processes.

On-Going Reforms

The County had initiated several reforms to facilitate strengthening of the PFM systems.

In terms of improving budget reliability, the county invested more resources towards timely execution of budgets, recruitment of competent staff, and staff capacity building. Besides, the County was putting in place measures to enhance revenue mobilization by reducing leakages, enhancing efficiency and identifying new revenue sources. It was also in the process of bringing all the extra-budgetary units into the mainstream budget, as demonstrated by the inclusion of sand cess in the budget under the section on other revenues. In addition, guidelines had been developed and a unit established to operationalize the revenue automation system and improve the mapping of all available revenue streams. Guidelines had also been established for reducing payment delays.

On strengthening management of public assets and liabilities, all staff in the County were subject to performance contracts through performance appraisals and monitored by the Performance Management Coordinator and the Officers' Forum. Ad-hoc committees had been constituted to facilitate negotiation before signing of performance contracts and an evaluation committee oversaw the evaluation process and the ranking at the end of the financial year. Further, a County Debt Framework was being developed by the National Treasury in consultation with Intergovernmental Budget and Economic Council (IBEC) to improve debt management.

On enhancing predictability and control in budget execution, the process of rolling out a Government Human Resource Information system (GHRIS) which is an online system that addresses all HR-related needs of the government had been initiated. This system was expected to interface with other existing systems such as IFMIS, G-PAY and IPPD.

About strengthening accounting and reporting, an audit committee was established at the beginning of 2017 to support the management of risk control and governance and provide associated assurance. Finally, the County had developed an in-house financial reporting manual, which was constantly being updated with best practice. However, the business intelligence system was yet to be put in place to improve budget and financial reporting.

Conclusion and Policy Recommendations

The County Government of Makueni has made considerable efforts to establish a strong and effective PFM system. Notable achievements include the establishment of various PFM structures, and timely preparation of budget documents as per the PFM Act 2012 guidelines and timelines. Besides, the County has a strong public participation framework upon which all major investment projects are identified and prioritized.

However, there is room to improve the PFM systems to achieve the outcomes of aggregate fiscal discipline, strategic allocation of resources and efficient service delivery. Other than addressing institutional and human capacity issues, the internal and external audit systems require strengthening to provide full oversight of the effectiveness of the internal control system.

In view of the findings of the assessment, the following recommendations are suggested:

1) **Strengthening budget preparation and reliability:** There is need to reduce expenditures and enhance own revenue sources to improve expenditure – revenue deviations. This can be done through mapping of potential revenue sources to expand revenue streams and cut down on non-essential recurrent expenditures. Besides, there is need to automate revenue collection systems and sensitize revenue payers on existing levies, charges and fees and their importance in service delivery to enhance revenue collections.

2) **Enhancing transparency of public finances**: There is need to undertake fiscal risk impacts to clearly identify contingent liabilities. Besides, identifying, evaluating and keeping records of all non-financial assets, especially land, machinery and equipment is necessary. The information would help in development of a debt stock and a debt management strategy.

3) **Effective management of assets and liabilities:** There is need to develop an accurate and complete record of fixed assets such as land purchased by the County. Besides, clear rules and regulations for transfer and/or disposal of assets should be developed. The county should finalize and implement the debt management strategy and establish a debt management unit to strengthen management of public assets.

4) **Policy-based fiscal strategy:** There is need to conduct macroeconomic fiscal sensitivity analysis with clear underlying assumptions and potential impacts on revenue, expenditures and debt accumulation. Besides, the County should continue aligning budgets with departmental plans, CIDP and the Vision 2030 framework. The aforementioned require targeted capacity building of relevant technical staff in macroeconomic forecasting (revenue and expenditure forecasting). The other technical skills required include revenue sensitivity analysis, fiscal impact analysis, and economic analysis of investment projects.

5) **Predictability and control in budget execution:** There is need to establish systems to monitor revenue arrears especially through automation of revenue systems and updating of business registers and valuation rolls. On procurement, a database to provide information for contracts, value of procurement or who has been awarded contracts should be maintained. Besides, there is need to maintain comprehensive records of revenue arrears, including the value, age and composition of revenue arrears.

6) **Accounting and reporting:** There is need to put in place a quality assurance process in adherence to professional standards. Efforts should also be made to expand the scope of audit beyond financial compliance. Besides, there is need to establish and/or strengthen monitoring and evaluation units to ensure effective implementation of various activities and programmes and increase the value for money.

7) **External scrutiny and audit:** The recommendations arising from audit scrutiny by the County Assembly, the Senate and Parliament should be implemented by various responsibility holders. This would enable adjustments and corrections in the PFM system.

About KIPPRA Policy Briefs

KIPPRA Policy Briefs are aimed at a wide dissemination of the Institute's policy research findings. The findings are expected to stimulate discussion and also build capacity in the public policy making process in Kenya.

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