COMMISSION ON REVENUE ALLOCATION

Promoting an Equitable Society

BRIEF ON THE CRA RECOMMENDATION ON THE BASIS CONCERNING EQUITABLE SHARING OF REVENUE AMONG THE COUNTY GOVERNMENTS

SENATE COMMITTEE ON FINANCE COMMERCE AND ECONOMIC AFFAIRS

NOVEMBER 19TH 2015
THE BASIS FOR EQUITABLE SHARING OF REVENUE AMONG COUNTY GOVERNMENTS

1. Introduction
In accordance with the provisions of Article 216 (1)(b), read together with Article 217 (2)(b) and Schedule 6 (16), the Commission on Revenue Allocation (CRA) recommends a basis for sharing revenue among county governments to the Senate for consideration. The recommendation is informed by the provisions of Article 216(3) (a). Table 1 shows a comparison of the first and second revenue sharing formulas.

Table 1: Summary on Parameters and Weights

<table>
<thead>
<tr>
<th>No.</th>
<th>Parameter</th>
<th>First Revenue Sharing Formula</th>
<th>First CRA Submission on the Second Revenue Sharing Formula</th>
<th>Second CRA Submission on the Second Revenue Sharing Formula</th>
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Annex 1 and Annex 2 presents allocations across counties simulated at Ksh 259,775 million and Ksh. 336,781 million


2. Parameters and Rationale for their Choice
The Commission recommends use of six parameters in the second revenue sharing formula. These are: Population, Basic Equal Share, Poverty, Land Area, Fiscal Responsibility, and Development Factor

The broad rationale for the choice of parameters is as summarised below:

i. **Constitutional and legislative stipulations:** as outlined in Article 203(1) of the Constitution, the parameters used give effect to the revenue sharing criteria.

ii. **Causal connection:** These parameters are measures of the factors that have the greatest impact on cost differentials between counties;

iii. **Measurability:** The data is either available at the Kenya National Bureau of Statistics (KNBS), or the relevant national ministries;

iv. **Susceptibility to data manipulation:** These parameters are generally less susceptible to distortionary gaming behavior that may seek to increase revenue allocation by altering data;

v. **International experiences:** These parameters have been used by various countries, which have implemented intergovernmental transfers, such as: South Africa, Nigeria, India, Philippines, and Ethiopia.

2.1. Population (45%)

1. Population is a good measure of the expenditure needs of a County.

2. It is a simple, objective and transparent measure that ensures predictability.
3. Article 203 (1) (j) provides for stable and predictable allocations of revenues to counties. The Population parameter guarantees this predictability and also ensures equal per capita transfers to all counties. Besides, use of population in the formula also ensures that counties are able to perform the functions allocated to them.
4. The data used for this parameter is based on the 2009 population census.

2.2. Basic Equal Share (26%)
1. Provision of a basic equal share in a transfer system in meant to guarantee a minimum funding for certain key functions, such as administrative costs of setting up and a running a government.
2. This is based on the assumption that a number of expenditures are, to some extent, similar for all county governments.

2.3. Poverty (18%)
1. A poverty index provides a measure of welfare of the citizens.
2. The Parameters uses the poverty gap index. This ensures that the poorest of the poor get the highest allocations
3. Poverty index is a good proxy of developmental needs and economic disparities among counties.
4. Use of this parameter in the formula guarantees allocations of revenue to disadvantaged areas which also happen to be the counties with the greatest need.
5. This is in line with Article 203 (1)(f)(g)(i).
6. The Data for this parameter is based on the 2009 data from the KNBS
2.4. Land Area (8%)
1. A county with a larger area has to incur additional administrative costs to deliver a comparable standard of service to its citizens.
2. The use of the size of a county (Land Area) as a parameter in the formula for sharing of revenues is compensates counties for additional costs incurred in providing services.
3. The parameter is based on the actual proportion of size of county relative to country.

2.5. Fiscal Responsibility (2%)
1. County governments receive transfers, collect and utilize public resources. Fiscal responsibility entails implementation of sound economic and budgetary practices to ensure citizens get value for money.
2. The fiscal responsibility parameter is meant to reward effort.
3. It is calculated from county annual revenue increase per capita.
4. In using this parameter, the Commission seeks to incentive counties to maximize on revenue collection and encourage fiscal prudence, in accordance with Article 216 (3) (c) and Section 107 of the PFM Act 2012.

2.6. Development Factor (1%)
1. This is one of the parameters suggested for inclusion by a large number of stakeholders during CRA’s extensive country-wide consultations on the formula.
2. This parameter considers Water, Electricity and roads, to capture economic disparities and developmental needs of Counties.
3. This parameter compliments the parameter on poverty to ensure that counties with the greatest developmental needs get additional resources to bring services to the level enjoyed in other
counties in accordance with the provisions of Article 203 (1) (f) and (g)

3. The Effect of the Change of the Basis on Revenue Sharing On Various Counties

1. Poverty Gap
   a. The highest change in allocations to various counties arises from the change on the data on poverty gap from 2005/06 used in the first formula to that of 2009 in the recommendation for the second formula.
   b. The reduction on the weight on the parameter on poverty gap from 20 per cent to 18 percent also affects allocations across counties.
   c. Overall, the changes in the poverty gap alters allocations substantially in several counties, some positively, some negatively.

2. Equal share
   a. The increase in the weight of the parameter from 25 per cent to 26 percent increases allocations to each county marginally.

3. Land Area
   a. The first formula used capped land (between 10% and 1%) to allocate 8% of the shareable revenue among counties
   b. The capping of land in the first formula recognized that besides size, terrain also has an impact of costs incurred by counties in service provision.
   c. Due to stakeholder demand, the current recommendation has uncapped the land parameter. The uncapping of the land reduces allocations to 25 counties marginally.
4. **Fiscal Responsibility**

a. The first formula allocated an equivalent of 2 percent of the shareable revenue to all counties equally.

b. The funds were meant to enable counties to put in place systems to enhance revenue collection and seal revenue leakages.

c. The current recommendation utilizes data on increase in county own sources revenues per capita for financial years 2013/14 and 2014/15 to allocate an equivalent of two percent of the shareable revenue to all counties.

d. Revenues collected by counties for Financial years 2013/14 and 2014/15 is presented in Annex 3.
### Annex 1: CRA second Submission on the Recommendation on Concerning the Basis for Revenue Sharing among County Governments

<table>
<thead>
<tr>
<th>No</th>
<th>County</th>
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<th>Population 45%, poverty 18%, Equal Share 26%, Land 8%, Fiscal Index 2%, Development index 1%</th>
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Annex 2: Simulations at Ksh 259,775 Million and 336,781 Million

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<th>First Formula: Population 45%, poverty (2005/06) - 20%, Equal Share 25%, Land 8%, Fiscal Index 2%, Ksh. 259775 Million</th>
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Annex 3: Own sources revenue for financial years 2013/14 and 2014/15 per county

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<th>Effort: Per Capita Increment (Ksh)</th>
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<td>Tana-River</td>
<td>240,075</td>
<td>32</td>
<td>33</td>
<td>1</td>
<td>6</td>
<td>0%</td>
<td>4</td>
</tr>
<tr>
<td>No.</td>
<td>County</td>
<td>Population</td>
<td>Revenue Collected 13/14</td>
<td>Revenue Collected 14/15</td>
<td>Increment</td>
<td>Effort: Per Capita Increment (Ksh)</td>
<td>Revenue Allocation Index (%)</td>
<td>Total Revenue Allocation</td>
</tr>
<tr>
<td>-----</td>
<td>-----------</td>
<td>------------</td>
<td>-------------------------</td>
<td>-------------------------</td>
<td>-----------</td>
<td>-----------------------------------</td>
<td>-------------------------------</td>
<td>---------------------------</td>
</tr>
<tr>
<td>43</td>
<td>Busia</td>
<td>743,946</td>
<td>329</td>
<td>315</td>
<td>-</td>
<td>0%</td>
<td>-</td>
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<tr>
<td>44</td>
<td>Mandera</td>
<td>1,025,756</td>
<td>90</td>
<td>88</td>
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<td>-</td>
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<tr>
<td>45</td>
<td>Samburu</td>
<td>223,947</td>
<td>201</td>
<td>196</td>
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<tr>
<td>46</td>
<td>Turkana</td>
<td>855,399</td>
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<td>127</td>
<td>-</td>
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<tr>
<td>47</td>
<td>Vihiga</td>
<td>554,622</td>
<td>123</td>
<td>116</td>
<td>-</td>
<td>0%</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Totals</td>
<td></td>
<td>38,610,097</td>
<td>26,296</td>
<td>33,849</td>
<td>7,588</td>
<td>7,824</td>
<td>100%</td>
<td>5,196</td>
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