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NATIONAL GOVERNMENT BUDGET MANUAL 2023

HARAMBEE

THE NATIONAL TREASURY
AND ECONOMIC PLANNING

NATIONAL GOVERNMENT BUDGET MANUAL

2023

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Foreword

Budgets are tools for implementing government programmes and policies. They are the means by which the strategic objectives of our country are realised. Through the national budget, the government translates strategic goals and objectives into programmes that meet the social, political and economic needs of the people. Budgeting is, therefore, one of the most important functions of the government, because it sets out quantitatively the plans and resources allocated to ministries, departments and agencies (MDAs) responsible for implementation.

The National Treasury and Economic Planning has developed this National Government Budget Manual. It sets out the legal provisions, rules, regulations, practices and procedures to guide MDAs on the budget process. The manual is intended for use by budget practitioners, public finance management officials, Members of Parliament and other stakeholders involved in the budget process. It will serve to improve national government budgeting and financial management.

Over the past two decades, the government has undertaken a series of public financial management reforms to improve the efficiency and effectiveness of public spending. These reforms included introducing medium-term budgeting, or what is popularly known as the Medium Term Expenditure Framework (MTEF) in 2000/01; integrating the internationally recognised Government Finance Statistics in the Standard Chart of Accounts (SCOA) and re-engineering the Integrated Financial Management Information System in 2008/09; adopting Programme Based Budgeting (PBB) with effect from 2012/13 in line with the Public Finance Management Act, 2012 (PFMA); and more recently, reforms in Public Investment Management (PIM). The adoption of the Constitution of Kenya, 2010 and enactment of the PFMA and accompanying regulations have made these reforms even more important, as we strive to link budgets with tangible results for the citizens of Kenya.

The main sections of this manual present key principles and concepts that should underpin the approach to budgeting. The annexes provide technical tools that will support practitioners in their daily work.

Budget formulation requires that choices between different priorities be informed by strong technical analysis – and the PFMA enjoins the government to reform the budget process in line with best practice. This demands capacity building among public financial management officials and other stakeholders. Publication of the National Government Budget Manual is an important contribution to building our public financial management capacity across the government.

A central tenet of effective budget preparation is the full participation of all stakeholders. I, therefore, call upon all Kenyans to actively participate in the annual budget process to ensure that the budget has wide ownership and that it addresses the most relevant priorities, which have maximum benefits to the citizenry.

NJUGUNA NDUNG'U, CBS
CABINET SECRETARY NATIONAL TREASURY AND ECONOMIC PLANNING

Acknowledgement

The preparation of this National Government Budget Manual was a collaborative effort across government. I wish to recognise and express my thanks to all those individuals and institutions that were in one way or another involved in this process. I also acknowledge the support received from the Public Financial Management Reform Secretariat, which facilitated meetings and workshops that brought together different stakeholders, MDAs and the National Treasury to draft the manual.

In particular, I wish to acknowledge the role played by the Director General - Budget, Fiscal and Economic Affairs Directorate, Mr. Albert Mwenda, HSC, for providing leadership in the process; Director of Budget, Mr. Francis Anyona, MBS, for providing technical guidance and coordinating the process; and the devoted efforts of the members of the Budget Policy Unit headed by Mr. Samuel Kiiru, Director of Planning/Budget. I also acknowledge the Sector Conveners and Co-conveners together with their technical teams in the secretariat for their contributions, which greatly enriched this manual. I want to recognize the valuable inputs from Macro Fiscal Affairs, Government Investment and Public Enterprises, Public Investment Management, Resource Mobilisation and Inter Governmental Fiscal Relations departments through their representatives who participated in the development of the manual. Special thanks to the officers from MDAs that worked with us in developing the manual. I wish to thank the administrative and support team of the National Treasury, which provided logistical and administrative services.

The National Treasury also acknowledges the technical assistance provided by the International Monetary Fund East African Technical Assistance Centre during the drafting of the manual – in particular the contributions received from Messrs. Imran Aziz, Gerhard Steger, Samuel Moon, Matthew Quillinan and Greg Rosenberg.

This manual will create awareness of the budget formulation process, budgeting methodology and our motivation to abide by international best practices – and in so doing, support efficient and effective public spending.

The manual will be reviewed and updated as and when need arises, especially when there are changes in laws, regulations, and guidelines.

DR. CHRIS K. KIPTOO, CBS PRINCIPAL SECRETARY NATIONAL TREASURY

Abbreviations

BPS	Budget Policy Statement
BROP	Budget Review and Outlook Paper
CARB	County Allocation of Revenue Bill
DORB	Division of Revenue Bill
FRP	Fiscal Responsibility Principle
FY	Financial Year
GDP	Gross Domestic Product
IMF	International Monetary Fund
KWh	Kilowatt Hour
MDAs	Ministries, Departments and Agencies
MTEF	Medium Term Expenditure Framework
MTFF	Medium Term Fiscal Framework
MTP	Medium Term Plan
MWG	Macro Working Group
PBB	Programme-Based Budgeting
PCN	Project Concept Note
PFMA	Public Finance Management Act, 2012
PFM	Public Financial Management
PIM	Public Investment Management
PPP	Public-Private Partnership
SCOA	Standard Chart of Accounts
SWG	Sector Working Group

CHAPTER ONE: PURPOSE AND STRUCTURE OF THE MANUAL

1.1 Purpose of the manual

1. The purpose of this Manual is to provide guidance on the national government's budget process. It provides key stakeholders, including budget practitioners, public finance management officials and Members of Parliament with a "one-stop-shop" reference document for all key stages in the national budget formulation process. A separate manual covers budget preparation at the county level.

1.2 Structure of the manual

2. The main sections of the manual cover principles and concepts that support sustainable budgeting. The annexes provide technical tools that will support practitioners in their daily work and will be issued through regular National Treasury circulars as part of the budget process. The manual is organised as follows:

Chapter 1 provides the purpose and structure of the Manual.

Chapter 2 sets out a broad overview of the legal and institutional framework that underpins the budget process.

Chapter 3 introduces key elements of sustainable budget preparation, centred on the development of the budget baseline. It further outlines fiscal rules, fiscal space and the use of expenditure ceilings, which are introduced in the context of fiscal responsibility principles.

Chapter 4 applies these principles to form guidelines for the national budget preparation calendar and the role of different stakeholders in the preparation of the budget. It further outlines the analysis and review to ensure that fiscal discipline is maintained and that spending is prioritised within stated expenditure limits.

Chapter 5 provides the rationale for a costing methodology for the recurrent and development budgets in three parts: it introduces different costing techniques, provides an overview of the costing tool and sets out guidance on how to conduct a budget baseline.

Chapter 6 introduces the concept of programme-based budgeting (PBB), and its application in budgeting, planning, monitoring and evaluation of government policies.

CHAPTER TWO: LEGAL, REGULATORY, INSTITUTIONAL AND STAKEHOLDER FRAMEWORK

3. This chapter sets out a broad overview of the legal and institutional framework that underpins the budget process. It Provides an overview of the legal and regulatory framework and sets out the institutional framework for expenditure prioritisation.

2.1 Legal and regulatory framework

4. Preparing the national budget involves several interrelated components. Budget preparation is a process through which MDAs plan, prepare, approve, implement and account for public resources. This process includes:

- The review of existing policies and the formulation of new ones
- Strategic and operational planning
- Budget formulation, adoption and approval
- Budget implementation or execution
- Accounting for resources and reporting
- Monitoring and evaluation
- Audit.

5. These processes are enshrined in various legal and regulatory frameworks, which include[1]:

- Constitution of Kenya, 2010 – in particular Chapter 12
- Public Finance Management Act, 2012
- Public Financial Management (National Government) Regulations, 2015
- Public Finance Management (Public Investment Management) Regulations, 2022— hereafter referred to as the PIM Regulations.
- Public Procurement and Asset Disposal Act, 2015
- Public Audit Act, 2015
- Public Procurement and Asset Disposal Regulations, 2020
- Other legal and regulatory frameworks.

2.2 Institutional framework

2.2.1 Sector classification

6. For purposes of budget preparation, MDAs are organized into sectors, which share goals across a range of closely related functions. Using the UN's Classification of the Functions of

1 *For the legislation and regulation listed below, the year reflects the year of promulgation, subsequent references in this manual will not include the year of promulgation, unless otherwise specified.*

Government, which allows for international comparability, national government functions are mapped into the following sectors:

- Agriculture, Rural and Urban Development
- Education
- Energy, Infrastructure and Information, Communication and Technology
- Environment Protection, Water and Natural Resources
- General Economic and Commercial Affairs
- Governance, Justice, Law and Order
- Health
- National Security
- Public Administration and International Relations
- Social Protection, Culture and Recreation.

2.2.2 Sector Working Group composition

7. In each of the 10 sectors, Sector Working Groups (SWGs) are responsible to prioritise and formulate sector budget proposals. The composition of SWGs is as follows:

- The Chairperson who is an Accounting Officer chosen by consensus from among the Accounting Officers in a respective sector.
- The Convener who is appointed by the National Treasury
- The Co-Convener is appointed by the department responsible for national economic planning.
- The Technical Working Group, which is appointed by the SWG.
- The Secretariat, consisting of technical officers appointed by respective Accounting Officers of MDAs in the sector to coordinate activities.
- Representatives from development partners that support MDAs in a given sector.
- Representatives from civil society.
- Representatives from the private sector.[2]

8. The SWG guides the Prioritisation process to ensure that the available resource envelope is aligned with identified competing priorities. Following the first estimate of the macrofiscal forecast, SWGs prioritise and formulate sector budget proposals. Sector Conveners and Co-Conveners from the National Treasury, together with representatives from MDAs rationalise and prioritise funding

2 *For example, representatives of the Kenya Private Sector Alliance and the manufacturing sector.*

proposals through a series of working sessions using agreed criteria, such as:

- Achieving the objectives of Medium-Term Plans (MTPs) and national development plans
- Furthering constitutional objectives
- Creating jobs and reducing poverty
- Achieving the core mandate of the MDAs
- Expected outputs and outcomes
- Cost effectiveness and sustainability of the programme.

2.2.3 Terms of reference for Sector Working Groups

9. SWGs are expected to ensure that proposed programmes and projects are in line with government's economic blueprint. The SWG process is based on the programme-based budgeting structure, where programmes are analysed and development spending proposals are assessed in the context of sector resource ceilings, based on the intended results of the expenditure.

10. The specific terms of reference for each SWG are to:

- Review sector goals, objectives and strategies and align them with the aspirations of the long-term government economic blueprint.
- Identify the programmes and necessary policy, legal and institutional reforms required in the sector.
- Approve the list of projects to be funded and propose the sources of funding.
- Analyse the medium-term cost implications of proposed programmes/projects.
- Prioritise programmes and allocate resources in accordance with agreed criteria.
- Identify programmes and projects that may require funding under public private partnerships (PPPs).
- Analyse baseline expenditures and remove any one-off expenditure for the previous years.
- Allocate resources to projects that have been fully processed and estimate requirements within the project cycle.[3]
- Introduce efficiency savings in sector budgets by reducing operating costs and non-core service delivery activities.

3 *A project being fully processed includes the completion of feasibility and design studies, land acquisition and project approvals.*

- Coordinate activities leading to the development of sector reports and indicative sector budget proposals.
- Identify critical stakeholders and engage them in programme prioritisation.
- Implement any other requirements that may be prescribed by the National Treasury from time to time.

2.2.4 Resource Allocation Panel

11. The SWGs present their proposals for resource allocation to the Resource Allocation Panel in the National Treasury, which reviews and makes recommendations. It consists of members from the following departments:

- The Budget Department, which chairs and provides the panel secretariat
- The Public Investment Management Department
- The Macro and Fiscal Affairs Department
- The Intergovernmental Fiscal Relations Department
- The panel may include any other officer appointed by the Principal Secretary.

12. The Resource Allocation Panel scrutinises the prioritised expenditure programmes for policy consistency. This includes reviewing:

- Prioritised projects in the pipeline
- Budget and project implementation documents for ongoing projects
- Absorption capacity for financed projects
- Ongoing project performance based on Public Investment Management Unit and other reports
- Proposed budget allocations for compliance with budget circulars
- The integrity of overall ceilings, including medium-term ceilings, as set out in the fiscal framework.

2.3 Role of stakeholders in the budget process

13. Stakeholders play key roles in the budget process and help to ensure adherence to legal and regulatory frameworks. Table 2-1 below outlines the main stakeholders and summarizes their primary responsibilities.

Table 2-1: Key stakeholders in the budget process

Stakeholder/Institution	Responsibility
Commission on Revenue Allocation	Makes recommendations to guide the basis of equitable sharing of revenue between national and county governments.
	Makes recommendations to guide financing and financial management of county governments, which give effect to the criteria of equitable share.
	Determines policy to identify marginalised areas.
	Submits recommendations on equitable sharing of revenue to Parliament.
Cabinet Secretary	Guides the budget process at the national level.
National Assembly	Determines allocation of revenue between national and county governments.
	Reviews and approves the national budget.
National Treasury	Guides the national budget preparation and execution process.
MDAs	Contribute to budget preparation and execution within their mandate.
	Provide technical support on planning, policy formulation, and implementation of policies, projects and programmes.
Senate	Reviews the Division of Revenue Bill as per the PFMA.
	key stakeholders in the budget process, the role of senate includes passing of the County Allocation of Revenue Act
Controller of Budget	Oversees budget implementation by authorising withdrawals from the Exchequer and other public funds.
	Prepares reports on budget implementation.
Auditor General	Audits the accounts of all government entities at national and county level.

Stakeholder/Institution	Responsibility
Macro Working Group (MWG)	Conducts macroeconomic forecasts that culminate in medium-term fiscal frameworks and expenditure ceilings.
Citizens	Contribute and give their input on planning and budgeting through public participation.
Development partners	Provide technical and financial assistance.

Source: National Treasury

2.3.1 Public participation

14. Consistent with the Constitution and the PFMA, the public have opportunities to provide input into the budget process. Article 201(a) and 232(d) of the Constitution and Section 35 (2) of the PFMA require the Cabinet Secretary to ensure public participation in the budget process.

15. Public participation in the budget process has three main objectives:

- Share information and create public awareness on policies, programmes and projects to be undertaken by the government on their behalf.
- Involve the public so that issues of concern are considered in the decision-making process.
- Enhance public understanding and collaboration in deciding on programmes and projects that best suit the interests of citizens. This objective is aimed at directly engaging the public to exchange information and cooperate with government.

16. Public hearings are conducted in line with the budget preparation calendar and are spearheaded by the SWGs. Such engagement includes holding public hearings, inviting submission of written memoranda, consulting stakeholders who are directly or indirectly affected by government policy decisions and soliciting the views of experts on technical issues.

CHAPTER THREE: PRINCIPLES AND CONCEPTS FOR SUSTAINABLE BUDGETING

3.1 Overview

17. This chapter introduces the key principles of sustainable budget preparation, which include budgeting in a medium-term context, analysis of fiscal space, compliance with fiscal rules and analysis of fiscal risks.

18. Budgets are policymaking tools. Through the national budget, government translates the country's strategic objectives into programmes and services that meet the social and economic needs of the people.

3.2 The concept of medium-term budgeting

19. Medium-term budgeting allows the government to prioritise programmes in the face of resource constraints. Programmes that have the greatest impact on economic and social development should be given priority. Programmes are continually reviewed for performance to ensure that they are operating efficiently, effectively and providing the best possible value for money to the citizens.

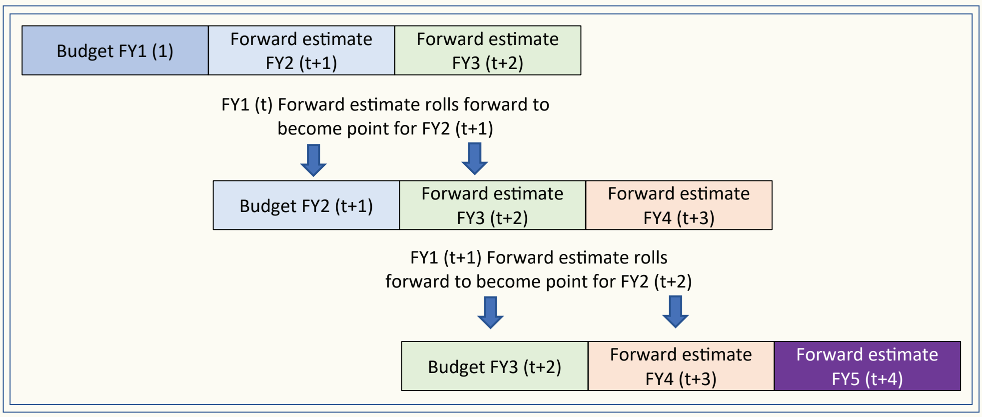
20. The MTEF sets out government's three-year spending plans. The MTEF is an annual, rolling budget and planning tool. That is, budgets for three financial years are prepared, but the projections are revised annually considering the previous year's performance and incorporating policy changes. The MTEF is underpinned by comprehensive technical analysis and aligned to the Medium-Term Fiscal Framework (MTFF), which establishes a firm expenditure ceiling over the three-year period. This fiscal constraint identifies the sustainable level of expenditure on government's development priorities.

21. Medium-term budgeting significantly enhances budget formulation, implementation and monitoring. First, it guards against annual incremental budgeting, by providing a comprehensive and realistic framework for the planning and management of public expenditure. Second, it increases the predictability of resources through more reliable revenue and expenditure estimates over a three-year period. Third, it better links resource allocation to policy and programme priorities and ensures these priorities are adequately funded.

3.3 A rolling medium-term expenditure framework

22. In a rolling medium-term budget plan, the first year forms the base for the following year's budget (Figure 3-1). Subsequent changes in policies (for example, new priority spending, approved policies/programmes and adjustments) are added or subtracted to the starting point to provide the updated budget estimates. Changes that have implications for successive years are also reflected in the updated forward estimates. Budget resources continue to be appropriated on an annual basis, but the budget planning process includes estimates of expenditure and revenue for the two years of forward estimates.

Figure 3-1: A rolling medium-term budget plan



Source: National Treasury

3.4 Macroeconomic projections

23. A macroeconomic forecast is the starting point for medium-term budgeting and is a precondition for conducting a budget baseline exercise. Factors such as gross domestic product (GDP), commodity prices and exchange, inflation and interest rates and commodity prices have significant consequences for revenue (e.g., taxes and customs duties) and expenditure (e.g. salary increases linked to inflation and the purchase of goods and services). A credible macroeconomic projection provides a sound foundation for budget preparation.

24. Macroeconomic assumptions are based on the most likely scenario and should err on the side of caution. Projections based on overly optimistic assumptions create fiscal distortions that adversely affect budget execution. Some of the methods used to avoid this bias towards optimistic macroeconomic projections are: comparing forecasts with other credible institutions, disclosing the accuracy of different projections and providing forecasts for different scenarios.

25. The macroeconomic projections used for budget preparation are updated prior to finalising the draft budget. Macroeconomic prospects can change significantly between the beginning and the end of the budget preparation process. An update shows whether the initial forecast remains valid or needs to be adjusted, with the necessary changes made to the draft budget.

3.5 Budget baseline

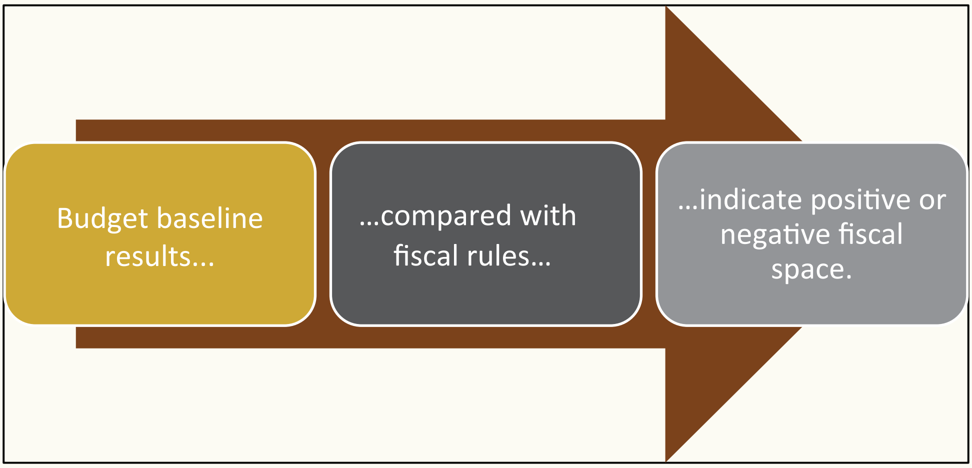
3.5.1 Rationale for the budget baseline

26. A budget baseline shows the budgetary consequences of existing policies for each financial year over the MTEF period. The baseline calculates the cost of current policies (including plans, programmes, projects and activities) in future financial years — in other words, today's policies costed at tomorrow's prices. This includes projections of expenditure, revenue and the budget balance. The expenditure and revenue forecast should be based on a costing methodology discussed in Chapter 5.

27. The results of the budget baseline should be compared to fiscal rules to determine available fiscal space. Fiscal rules are described in detail in section 3.6. They are yardsticks for fiscal sustainability and show whether the government is increasing, decreasing or maintaining fiscal space. Fiscal space is the room in a government´s budget that allows it to provide resources for a desired purpose without jeopardizing the sustainability of its financial position or the stability of the economy.

28. The comparison of budget baseline results and fiscal rules therefore reveals whether existing policies will be affordable in the future. Figure 3-2 depicts this process.

Figure 3-2: How to use a budget baseline



Source: National Treasury

29. The government then sets expenditure ceilings to comply with available fiscal space. Spending ceilings are the maximum amount that the government allocates in the budget in a given year to a target sector or expenditure category.

3.5.2 Scope and timeline of the budget baseline

30. The baseline covers all existing policies. Existing policies refer to plans, programmes and projects financed through the various budget votes and expenditure categories.

31. The costing of existing policies is not constrained by expenditure ceilings. The purpose of a budget baseline is to show the budgetary implications of existing policies and compare the results with affordable spending levels as expressed in fiscal rules. The overall magnitude of expenditure on existing policies needs to be revealed at this stage to ensure a realistic estimation of their spending impact.

32. The baseline calculation indicates whether required spending for existing policies complies with indicative expenditure ceilings. Baseline results that breach indicative ceilings set in compliance with fiscal rules indicate negative fiscal space and require Prioritisation of expenditure to comply with the fiscal rules.

33. Existing or ongoing policies are defined as those currently being implemented and include new policies formally approved by the Cabinet or National Assembly.[4] Proposals that await government approval are not part of the existing policies and are not included in the baseline.

34. Spending dynamics of existing policies are included. If the design of a policy automatically leads to increased expenditure from one financial year to the next (for instance, where beneficiaries of a government transfer increase over time in response to demographic shifts), this is included in the baseline.[5] However, if a sector proposes to enlarge an existing programme by increasing transfers per beneficiary, but the Cabinet has not yet decided on the proposed increase, it should not be included.

35. Planned efficiency gains should only be factored into the baseline if they are based on approved measures and there is certainty that the efficiency gains will materialize. Efficiency gains are measures aimed at reducing expenditure or increasing revenue.[6] For these gains to be factored into the baseline calculation as existing policy, they must first be approved by the responsible authority (Cabinet or National Assembly) based on realistic costings.

36. To fulfil its purpose, a budget baseline must be comprehensive. The more complete the budget forecast, the more useful it is for credible budget preparation. Table 3-1 indicates what should — and what should not — be included in the baseline.

Table 3-1: Calculating the baseline

Included	Not included
All policies currently being implemented and new policies formally approved by Cabinet or National Assembly	Proposals that await government approval
Automatic adjustments as defined by policy design	Unapproved proposals for design changes to policies

4 *For example, measures from a stimulus package in response to the COVID-19 pandemic.*

5 *Examples could include the publicly funded Linda Mama maternity healthcare programme, which aims to ensure that pregnant women and infants have access to quality and affordable health services. The number of births per year is a variable that drives the transfer to the National Health Insurance Fund.*

6 *Examples of expenditure measures include more efficient administrative structures, steps to combat fraud or waste, or cancelling ineffective programmes. Revenue measures could include improving tax collection efficiency.*

Included	Not included
Approved and realistic efficiency gain estimates	Unrealistic expenditure or revenue estimates
Verified pending bills (expenditure arrears)	Unverified pending bills
Multiannual contractual commitments	
Extrabudgetary funds	
Major fiscal risks with a high likelihood of materializing	

Source: National Treasury

37. A budget baseline needs to be realistic. Revenue and expenditure forecasts should be based on the most likely scenario. Overestimating revenues or underestimating expenditure distorts the purpose of the exercise, which is to depict the most realistic budgetary impact of existing policies (Box 3-1).

Box 3-1: Examples of overestimating revenues and underestimating expenditure

Overestimating revenue: Overly optimistic revenue estimations are conducted to simulate room for a certain level of expenditure required to cover high-priority programmes. During budget execution, revenue inflow is substantially less than planned, leading to in-year expenditure cuts (particularly for capital expenditure) that hamper planning certainty for MDAs, or higher deficits — or both.

Underestimating expenditure: The expenditure dynamic for important categories (such as salaries or transfer schemes) is underestimated to simulate fiscal space allowing for additional prioritised expenditure in other policy areas. During budget execution, expenditure in the under budgeted areas substantially exceeds budgeted amounts, creating the need for in-year budget cuts, or leading to higher deficits—or both.

Source: National Treasury

38. The calculation of the baseline occurs at the beginning of the budget process in July and comprises the three years of the MTEF. Each MDA is required to prepare and submit a budget baseline to the National Treasury. The baseline is informed by practical experience and updated information, and is consistent with the budget planning horizon. A detailed schedule of the main stages of conducting the budget baseline exercise is provided in Table 3-2.

Table 3-2: Stages of the budget baseline process

Steps	Activity and deliverable	Responsibility	Rationale
1	The budget baseline for each year of the MTEF is calculated using the costing tool and National Treasury guidelines and submitted to National Treasury.	Sectors and their MDAs	Important analytical prerequisites can be done earlier in the year.
2	National Treasury assesses the baseline calculations for validity and requests improvements where necessary.	National Treasury	This ensures credibility of baseline calculations.
3	Requested improvements to baseline calculations are submitted. National Treasury conducts a further check and either confirms the estimates or requests additional changes. This process of iterative improvement continues until National Treasury is satisfied with the validity of the baseline calculations.	Sectors and their MDAs, National Treasury	If required, meetings are conducted between National Treasury and sectors and their MDAs to discuss the required improvements.
4	The budget baseline results of each sector, together with the contribution of other National Treasury units, are integrated into one comprehensive national budget baseline projection, which is factored into key fiscal aggregates	National Treasury	This avoids double counting of expenditure and revenue and explicitly outlines which major fiscal risks have been included in the baseline

Steps	Activity and deliverable	Responsibility	Rationale
4	to allow a comparison with national Fiscal Responsibility Principles (FRPs).		projection —and their precise impacts.

Source: National Treasury

3.5.3 Fiscal risks

39. Fiscal risks are factors that can cause fiscal outcomes to deviate from expectations (as contained in the budget or other forecasts). Major areas of potential risk include macroeconomic shocks and specific fiscal risks associated with expenditure overruns, debt and government guarantees, state-owned enterprises, the financial sector, health emergencies and natural disasters.

40. Fiscal risk management is an essential part of the budget process. Decision makers need to be aware of the existence, magnitude and likelihood of major fiscal risks when preparing the budget. Fiscal risk management includes identifying, quantifying and, where possible, mitigating the impact of such risks.

41. Fiscal risk analysis supports comprehensive budget planning and sustainable public finances. Where the magnitude of fiscal risks is significant, the government may be justified in taking a more conservative approach to budget decisions to avoid unexpected revenue shortfalls or expenditure overruns impacting on budget sustainability and execution. The government may also wish to manage certain fiscal risks by specifically budgeting for them.

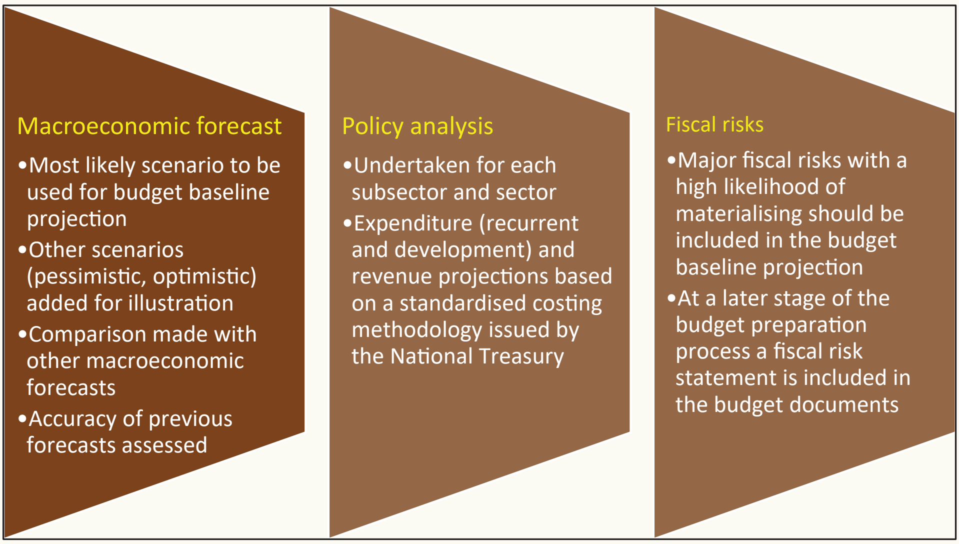
42. The government's Fiscal Risk Statement identifies and quantifies key fiscal risks and sets out mitigation measures. It is published as part of the Budget Policy Statement (BPS). This is important both to provide a comprehensive view of public finances and for budget transparency.

43. MDAs play a significant role in managing fiscal risks through the budget process. This includes:

- **Identification and notification of fiscal risks to the National Treasury**. MDAs should provide information to the National Treasury that supports their analysis of fiscal risks and identify any fiscal risks whose realisation is imminent (e.g. default on guarantees, additional expenditure on natural disasters and so on).

- **Incorporation of high probability fiscal risks in the baseline.** Budget baseline projections should factor in major fiscal risks that are likely to occur. Not all fiscal risks should be included in the baseline because it would lead to an unreasonable projection. MDAs can assess the likelihood of risk materialisation through analysis of previously occurring risks, modelling and obtaining additional information. Including significant and likely fiscal risks in the baseline can be done in two ways. Where risks have repeatedly materialised (e.g. persistent expenditure underestimates or infrastructure overruns), costing estimates should be improved. Where periodic risks are expected to occur but remain uncertain (e.g. natural disasters), the government may wish to specifically provide for them in the baseline. The National Treasury can provide assistance in the determination of fiscal risks and their budget treatment. Figure 3-3 shows the main elements of a budget baseline forecast for each financial year of the MTEF cycle.

Figure 3-3: Main elements of a budget baseline projection



Source: National Treasury

3.6 Fiscal rules

3.6.1 Rationale for fiscal rules

44. Fiscal rules are commitments to constrain fiscal policy to ensure sustainable public finances. Setting limits on and targets

for key indicators—such as the debt-to-GDP ratio—enables the government to contain spending pressures and maintain debt sustainability.

45. Fiscal rules should meet several criteria to effectively guide budget decision-making. Compliance with the rules promotes long-term fiscal sustainability (especially debt) and stability through decreasing economic volatility. Well-defined fiscal rules can be translated into clear operational guidance through budget instructions. They should be simple to understand and stable over time. Compliance with the rules should be easily verifiable.

3.6.2 Fiscal rules and the Fiscal Responsibility Principles

46. Kenya's fiscal rules are set out as FRPs. According to the PFMA and the Public Finance Management Regulations (PFM Regulations), 2015, the National Treasury shall enforce the following principles:[7]

- Over the medium term, a minimum of 30 percent of the national government budget shall be allocated to development expenditure — the creation or renewal of assets that provide long-term public goods and services, such as roads and hospitals. The 30 percent minimum refers to national government MDAs compared against the total budget (recurrent and development) allocated to MDAs, excluding equitable transfers to county governments and consolidated fund services.
- National government's expenditure on wages and benefits for its public officers shall not exceed 35 percent of national government revenue (excluding revenues from oil and coal resources and the share raised by county governments), as prescribed by current regulations.[8] Wages and benefits refer to the total sum of national wages, rather than the individual MDAs' wages and benefits.
- Over the medium term, national government borrowing shall be used only for the purpose of financing development expenditure and not for recurrent expenditure.
- Public debt and obligations shall be maintained at a sustainable level, measured against the limits set in the PFM Regulations.[9]
- Fiscal risks shall be managed prudently.
- A reasonable degree of predictability with respect to the level of tax rates and tax bases shall be maintained, taking into account

7 *PFMA, section 15.*
8 *PFM Regulations, section 26 (1) a and 26 (1) c.*
9 *PFM Regulations, section 26 (1) a and 26 (1) c.*

any tax reforms that may be made in the future.

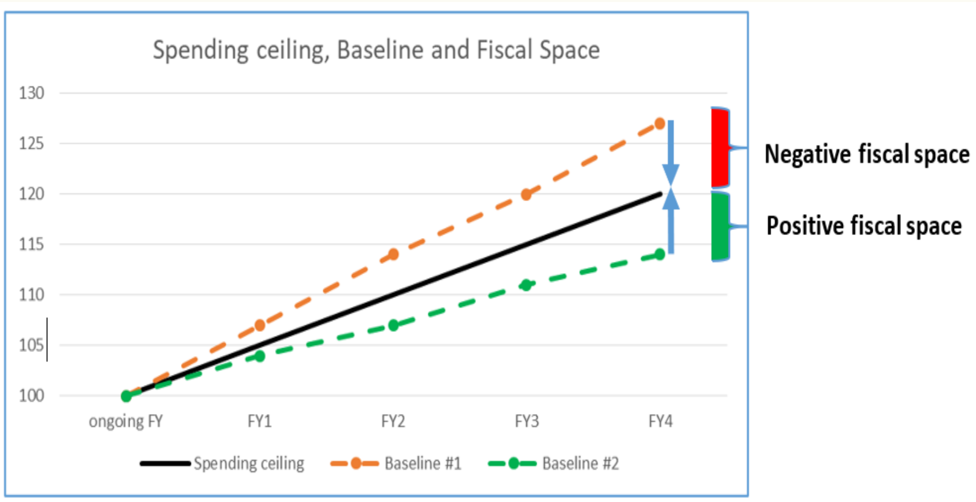
- The PFMA also stipulates that short-term borrowing shall be restricted to managing cash flows and, in case of a bank overdraft facility, it shall not exceed 5 percent of the most recent audited national government revenue.

47. The government reports on the implementation of the FRPs on an annual basis. This is done through the BROP and the BPS, which discuss each of the principles and provide data on their implementation.

3.6.3 How to use fiscal rules for budgetary decision making

48. The annual budget and the MTEF are prepared and executed in line with the fiscal rules. This requires a clear assessment as part of the budget preparation process. For example, a certain debt-to-GDP ratio can be translated into an affordable amount of expenditure for each financial year covered by the upcoming MTEF, based on the budget baseline and the stock of debt over the spending period. Fiscal rules and affordable spending levels can be effectively supported by expenditure ceilings covering the entire budget and the various individual sectors. Fiscal rules enable the government to gauge the results of the budget baseline projection, creating an important indicator of affordability.

Figure 3-4: The concept of fiscal space



3.7 Fiscal space

3.7.1 The concept of fiscal space

49. Fiscal space is the degree to which the government may provide resources for a desired purpose without jeopardizing the sustainability of its financial position or the stability of the economy. It is calculated as the difference between the budget baseline and expenditure levels in line with the fiscal rules. Where fiscal space is positive (revenue available is above the baseline), there is room for additional sustainable spending, but where it is negative, savings need to be made or revenue raised to restore the budget to sustainability. Fiscal space can be adjusted either through raising revenue or reducing expenditure in line with fiscal rules. Figure 3-4 outlines the concept of fiscal space.

3.7.2 How to use fiscal space for budgetary decision-making

50. Awareness of fiscal space is a precondition for good budgetary decision-making. Without knowing the available fiscal space, the budget easily runs into execution challenges because budget policy decisions have not been aligned with fiscal sustainability requirements (Figure 3-5).

Figure 3-5: Problems when fiscal space is not calculated properly

51. Fiscal space needs to be disclosed to influence decision-making. Making the comparison of fiscal rules and budget baseline results available informs sound, evidence-based decisions and public debate on the national budget.

52. In case of negative fiscal space, existing policies need to be modified to comply with the fiscal rules. This means that there is no room for new policies prior to modifying existing policies to eliminate negative fiscal space. This can be done either by taking action to increase revenue or to cut existing expenditure, or both.

53. Where positive fiscal space is identified, additional policies can be implemented. In such a case, the government could budget

additional expenditure for new or enlarged programmes, narrow the budget deficit (or increase the surplus) to reduce debt and debt-service costs or cut taxes.

3.8 Expenditure ceilings

3.8.1 Rationale for expenditure ceilings

54. Expenditure ceilings limit spending to levels compliant with fiscal sustainability. The total ceiling sets a limit on the government's overall spending for a specific financial year. Sector ceilings set these limits at the individual sector level. Expenditure ceilings are set for each financial year within the MTEF period.

55. Medium-term expenditure ceilings must be reliable. The National Treasury sets expenditure ceilings and ensures they are adhered to. Frequent changes to expenditure ceilings undermine budget and policy planning. Changing the ceiling for a specific financial year should be the rare exception, not the rule, undertaken in response to significant unforeseen shocks (such as the COVID-19 pandemic).

3.8.2 Setting expenditure ceilings

56. The overall expenditure ceiling reflects the affordable level of total government expenditure compliant with fiscal rules. The National Treasury performs this calculation, which is reliant on credible revenue estimates. Overly optimistic revenue forecasts would produce an unrealistically high level of expenditure that is not sustainable.

57. The total of sector expenditure ceilings complies with the overall expenditure ceiling. The sum of all individual sector expenditure ceilings (including those for debt repayments, contingency funds etc.) must not exceed the total.

58. The expenditure ceilings need to be credible and underpinned by accurate costing. For ceilings to be effective in guiding the budget, they should be underpinned by proper costing by MDAs. This ensures that the National Treasury can effectively review MDA budget submissions and ensure ceilings are adhered to.

CHAPTER FOUR: PREPARING THE NATIONAL BUDGET

4.1 Overview

59. This chapter describes the key features of the national budget preparation process. It explains the annual preparation of the MTEF step by step. The chapter starts with a summary of the budget preparation calendar and subsequently reviews each step in more detail. Annex 1 provides the full calendar.

4.2 Budget cycle and calendar

60. The budget process begins in July and consists of three broad phases (Figure 4-1). Following the issuance of the MTEF circular, the first phase from July to November is characterised by MDAs calculating their budget baseline and the derivation of affordable expenditure levels consistent with fiscal objectives communicated in the Budget Review and Outlook Paper (BROP). The second phase, which occurs between November and February, involves sector-based consultations to align and prioritise sector policies within expenditure ceilings, which are communicated through the BPS. The third phase consists of detailed budget preparation and the submission and approval of final budget documents.

Figure 4-1: Key Phases of the budget preparation calendar

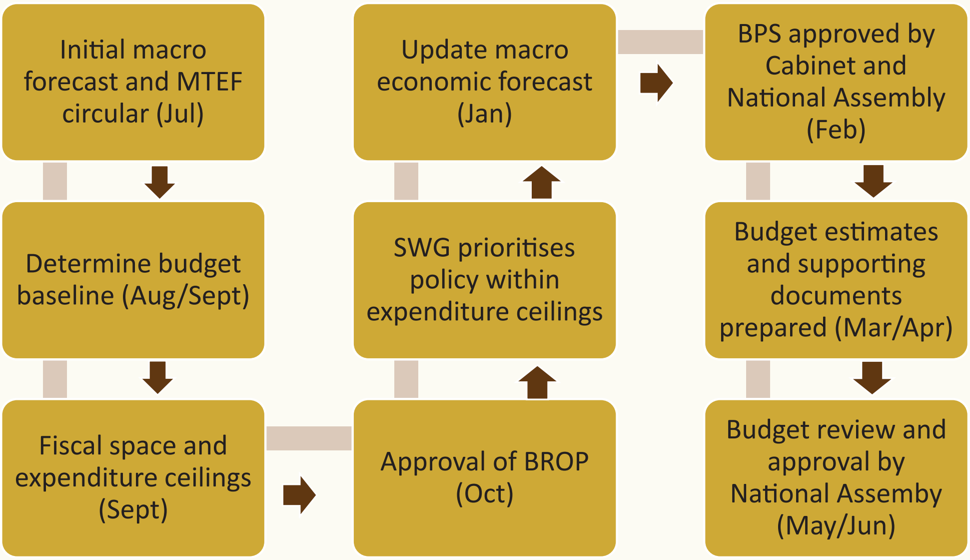
Baseline and set expenditure limits (July - Nov)	Prioritisation and policy choices (Nov - Feb)	Budget Finalisation and approval (Mar-Jun)
• MTEF circular issued • Baseline determined • BROP issued	• Prioritise sector policies within expenditure ceilings (SWG) • BPS communicates policy choices	• Detailed budget finalised • Submitted to National Assembly and approved

Source: National Treasury

61. The National Treasury issues a budget calendar to guide the budgeting cycle in line with requirements set out in the Constitution and the PFMA. The calendar is implemented through decision points that are in line with the constitutional requirement. The decision points, shown in Figure 4-2, are based on macroeconomic and fiscal analysis, a series of budget hearings and approvals by the executive and legislature through budget

documentation, which include the BROP, BPS and detailed budget estimates.

Figure 4-2: National budget calendar



Source: National Treasury

4.3 Purpose and timing of the macroeconomic projections

62. The budget process begins with the National Treasury preparing macroeconomic forecasts that consider all macroeconomic parameters that affect the budget outlook. This task is conducted using a model that covers relevant factors such as GDP and its components, inflation, interest and exchange rates, imports and exports, consumption and commodity prices. Development of certain revenue and expenditure items is substantially affected by the economic outlook. A clear and credible economic forecast is a precondition for a realistic budget baseline projection.

63. The macroeconomic forecasts used for the budget baseline should be available by mid July. These are reflected in the MTEF Circular issued at the end of July and the outlook needs to be factored into the budget baseline. The three-year forecast covers each year of the forthcoming MTEF period.

64. The macroeconomic forecast is updated by mid January to account for changes. By law, the National Treasury must submit the BPS to Parliament by 15th February. To ensure that the legislature

receives a BPS based on the most up-to-date information, the National Treasury updates its macroeconomic projection should be by the end of January. This allows time for the National Treasury to manage the impact of the updated forecast on the budget in consultation with sectors.

65. The results of the macroeconomic projections are used by different departments of the National Treasury and other stakeholders. For instance, the department responsible for macroeconomic and fiscal affairs at the National Treasury calculates the impact for the different revenue sources for each of the financial years covered by the MTEF and submits the results to the department responsible for budget.

4.4 Setting the framework for budget preparation

4.4.1 MTEF circular

66. The MTEF Circular contains guidelines for the preparation of the MTEF. It guides MDAs on how to contribute to the budget preparation process for the upcoming MTEF. This includes the preparation of the upcoming annual budget which is covered by the timeline of the MTEF. Key legal requirements for the content of the initial MTEF Circular are stipulated in the PFMA.[10] These include a budget preparation calendar, procedures for the review and projections of revenues and expenditure, key policy considerations, procedures for public participation, formats for budget submissions and any other information that may assist the budget preparation process.

67. The MTEF Circular sets out specific guidance on several processes that this manual discusses in a general manner These are: how to conduct the budget baseline; costing methodology; identification and quantification of fiscal space; assumptions guiding expenditure ceilings and costing sector-specific action plans to foster compliance with set expenditure ceilings.

68. The MTEF Circular is issued at the end of July in line with PFMA provisions.[11] This ensures sufficient time for the budget preparation process, particularly the calculation of the budget baseline projections.

10 *PFMA, section 36.*

11 *The PFMA states that the MTEF circular is issued by the end of August, however the baseline calculation should start before this date.*

69. MDAs must follow the guidelines of the MTEF Circular. They participate in the budget preparation process and submit their contributions as outlined in the MTEF Circular. Where MDAs identify compliance concerns, they seek clarification and, if possible, support from the National Treasury.

4.5 The process of conducting the budget baseline

70. The purpose of the budget baseline process is to calculate the budgetary impact of existing policies for the MTEF period. This allows gauging whether existing policies are affordable in the medium-term.

71. The budget baseline process starts at the beginning of August and ends in the second week of September, based on guidance provided in the MTEF Circular. The compilation of the budget baseline for each sector, and its review and aggregation by the relevant departments in the National Treasury, should be finalised by the second week of September. The MTEF Circular includes a detailed calendar for conducting the budget baseline exercise to properly guide sectors and their MDAs to deliver the required calculations.

72. The National Treasury guides and coordinates the budget baseline process. All MDAs within sectors are required to conduct standardised costing. The National Treasury also collects contributions to the budget baseline projection from other stakeholders, and where required, reviews them for the purpose of quality assurance. In scrutinising baseline calculations, the National Treasury conducts a review of budget submissions (Box 4-1), following which the results are aggregated into a comprehensive budget baseline projection for the national government.

Box 4-1: The budget review process of the National Treasury
The National Treasury is the custodian of the budget. It is responsible for coordinating the preparation of the budget compliant with fiscal rules, ensuring that the draft budget presented to the Cabinet and subsequently to the National Assembly is comprehensive, and that the budget numbers are in line with the most likely forecast. In this capacity, the National Treasury: • Ensures the expenditure ceilings set for each sector are adhered to and requires sectors to prioritise their budget requests consistent with these ceilings. • Scrutinises sector budget requests to determine whether they correctly apply the costing methodology and, if not, requires them to re-cost their budget requests. • Ensures that the budget baseline is anchored on agreed country priorities as outlined in the MTPs and the respective sector plans.

Source: National Treasury

73. Other departments within the National Treasury contribute to budget baseline projections. In particular, these are the departments responsible for:

- Macroeconomic and fiscal projections
- Debt management, which provides a forecast for interest payments and government debt developments
- Resource mobilisation for funds from development partners
- Public investment management
- Fiscal relations between the national and county governments.

74. Some important prerequisites for calculating the budget baseline can be undertaken prior to the beginning of August. In particular, sectors and their MDAs can:

- Analyse budget data to identify key revenue and expenditure drivers.
- Identify the budget line items that are directly affected by macroeconomic variables and, therefore, by macroeconomic forecasts.

These prerequisites should be finalised by the end of July to facilitate the finalisation of budget baseline exercise by the second week of September.

75. Budget expenditure and revenue are estimated separately for each year of the MTEF period. This estimation applies for the entire sector budget and all existing policies. Expenditure estimates are derived by sectors and revenue projected by the National

Treasury. To this end, the expenditure and revenue drivers for each of the policies of each sector are identified and their movement quantified using the standardised costing methodology.

76. The sectors calculate medium-term baseline projections for their policies and the results are reviewed. The calculations are done as part of the sector strategic reviews conducted in August by SWGs, which bring together MDAs within the sector.[12] Based on the approved costing methodology, each individual SWG costs all of its programmes, compares the result with the expenditure ceiling set for the sector and submits them to the National Treasury. [13]

77. The sectors' budget baseline results are integrated into one comprehensive national government budget baseline projection. This requires quality assurance measures, such as checking the proper application of the standardised costing tool, avoiding double counting of expenditure and revenue positions and identifying major fiscal risks (and their estimated costs) that have been included or excluded from baseline projections.

78. The budget baseline results are factored into key fiscal aggregates. This allows for a comparison between the budget baseline results (baseline for expenditure, revenue, budget deficit/ surplus and debt) and the FRPs. Key fiscal aggregates include the debt-to-GDP ratio, the overall level of the wage bill and development expenditure.

79. As required by the PFMA, the budget baseline results are published in the BROP. The National Treasury submits the draft BROP to Cabinet by 30th September for approval and subsequently submits it to the National Assembly (not for approval, but for information purposes) by the third week of October. The paper must be published and publicised not later than 15 days after laying the paper before Parliament.[14]

4.6 Comparing baseline results with Fiscal Responsibility Principles

80. A comparison of the budget baseline results and the FRPs allows for identifying and quantifying the fiscal space. The results

12 *Annex 2 of the MTEF Circular lists which MDA is included in which SWG.*

13 *The projected ceilings communicated in the most recently published MTEF serve as a guide for the costing exercise. The outer year (FY+2) will not have been estimated in the previous MTEF; for the purposes of the costing exercise MDAs are advised to use the outer year (FY+1) as the provisional ceiling for the outer year (FY+2).*

14 *PFMA, section 26.*

of the budget baseline should be compared with the FRPs over the MTEF period.

81. Identified and quantified fiscal space is published in the BROP. Thus, the comparison must be ready in time to inform the draft BROP before it is submitted to Cabinet as set out above.

82. The BROP must disclose where fiscal space is diverging from the intent of the FRPs. Because the FRPs address different aspects of fiscal sustainability, it is likely that the comparison between the budget baseline projection and individual FRPs will result in diverging numbers for fiscal space. For instance, negative fiscal space arising due to non-compliance with the debt level as approved by Parliament would suggest the need to cut expenditure or increase revenue, whereas non-compliance with the requirement to spend at least 30 percent of the budget for development would suggest a need to increase development spending, or decrease recurrent expenditure.[15] Such transparency supports informed decision-making and oversight regarding fiscal policy trade-offs.

83. Given that there are multiple FRPs, it is important that the one with the largest deviation of overall expenditure to the baseline results is addressed. This would automatically eliminate the gap between the other FRPs with a smaller deviation to the baseline. Additionally, the composition of expenditure needs to be addressed properly as shown in the example in Box 4-2.

Box 4-2: Variation of fiscal space

Seven FRPs apply to the national government(see Section 3.6.2). The hypothetical examples below demonstrate the requirement for the National Treasury to calculate fiscal space for each FRP and ensure overall compliance.

- **Example 1:** Over the medium term, national government borrowing shall be used only for the purpose of financing development expenditure and not for recurrent expenditure. Assume that the baseline recurrent expenditure will require borrowing of Ksh. 6 billion.
- **Example 2:** National government's expenditure on wages and benefits for its public officers shall not exceed 35 percent of national government revenue. Assume the baseline shows that this threshold will be breached by Ksh. 3 billion.

15 *PFMA, section 15 (2d).*

Box 4-2: Variation of fiscal space
• **Example 3:** Over the medium term, a minimum of 30 percent of the national government budget shall be allocated to the development expenditure. Assume that the baseline shows this limit will be breached by Ksh. 2 billion. In the situation outlined above, the largest gap between an FRP and the baseline is equivalent to Ksh. 6 billion (Example 1). Therefore, corrective measures totalling Ksh. 6 billion are required, either by reducing expenditure or increasing revenue. Closing this Ksh. 6 billion gap could also eliminate the gaps in Example 2. However, it would still be necessary to close the gap shown in Example 3, because this concerns the composit*ion* of expenditure with a specific minimum percentage level.

Source: National Treasury

4.7 Setting medium-term expenditure ceilings

84. By law, expenditure ceilings must take the fiscal rules into consideration.[16] The ceilings define limits for expenditure compliant with the FRPs. Overall sector recurrent and development ceilings should be consistent with expenditure ceilings for the national government.[17] In addition, a contingency fund is appropriated within the total government expenditure ceiling.

85. Expenditure ceilings are set in the BROP and approved by the National Assembly in the BPS. The ceilings set in the BROP guide sectors to prioritise their policies and expenditure accordingly. The ceilings in the BPS, as proposed by the Cabinet, should be adopted in the National Assembly by end of February.[18] They should be consistent with the ones set in the BROP, provided those macroeconomic projections do not deviate from the initial forecasts. Where the outlook has changed significantly with an impact on fiscal space, expenditure ceilings in the BPS may be adjusted to be consistent with the FRPs. Box 4-2 shows how an updated macroeconomic forecast could affect expenditure ceilings.

16 *PFM Regulations, 2015, section 34(c).*
17 *PFM Regulations, section 34(d).*
18 *PFMA, section 25.*

Box 4-3: How updated macroeconomic forecasts can affect spending ceilings
Example 1: The updated macroeconomic projection is more favourable than the initial one. A higher amount of available budget revenue can be assumed, which allows for improving the budget deficit/surplus, lowering taxes or other government revenue sources or additional expenditure. In the latter case, expenditure ceilings set in the BROP at the end of September might be increased according to political decisions, provided that they comply with the FRPs. **Example 2:** The updated forecast is less favourable than the original projection. This is expected to reduce budget revenue. As a result, expenditure must be reduced to comply with the FRPs. This would require lowering expenditure ceilings in the BPS compared to those set in the BROP.

Source: National Treasury

86. The expenditure ceilings set in the BPS are binding. PFM Regulations state that the development expenditure and personnel spending of the national government budget shall be approved by Parliament and be binding for the next two budget years.[19]

87. For each sector, policies are prioritised in line with the set expenditure ceilings. This happens immediately after the approval of the BROP. During the SWG meetings, sectors prioritise their policies and projects to comply with the expenditure ceilings, and the National Treasury reviews them for compliance.

88. Expenditure ceilings are underpinned by measures to ensure their credibility. If the National Treasury has concerns as to whether a sector can comply with set expenditure ceilings based on its existing policies (as calculated in the budget baseline projection), it will require a sector-specific action plan which will be presented and discussed at the SWG. Here, sectors will be required to submit prioritised policies with costs (based on the standardised costing methodology), corrective measures to reduce the budget requirement and expected cost savings. Such measures may include terminating/scaling back; or merging programmes; harmonising existing structures; or conducting spending reviews (see Box 4-4). Annex 2 includes templates for a sector-specific action plan.

19 *PFM Regulations, section 27(5).*

Box 4-4: Options for reducing a budget requirement

Terminating/scaling back programmes

Some programmes or sub-programmes may fall substantially short of delivering the intended results identified through the evaluation process, or persistently require more budget funds than initially planned. Such programmes may therefore not deliver sufficient value for money.

Merging of programmes

Programmes with very similar objectives might exist within one MDA or among two or more MDAs. This could result in duplication and ineffective use of resources.

Harmonisation of administrative structures

Two or even more administrative units within one MDA or among several of them might be tasked with very similar duties. This could result in duplication, which is inefficient and unnecessarily expensive.

Conducting spending reviews

Spending reviews are critical reassessments of existing expenditures, and of the policies they are based upon, viewed through the lenses of efficiency, effectiveness, economy, sustainability and/or affordability to identify potential savings in selected policy areas.

Source: National Treasury

89. Expenditure ceilings are approved at the political decision-making level. Limiting expenditure sets hard budget constraints for the entire national government, cascaded to each sector. Given their political and fiscal impact, such decisions need to be taken first by Cabinet, and then by Parliament.

90. The National Treasury provides technical level guidance to support decision-makers. This includes: presenting options for allocating the overall affordable expenditure ceilings to sectors; taking into account the validated results of the budget baseline projections; presenting costed savings options that enable compliance with expenditure ceilings; clarifying the concept of fiscal space and the budgetary impact of FRPs for decision-makers and; scrutinising sector-specific action plans to ensure compliance with expenditure ceilings.

91. Sectors are required to prioritise their programmes to adhere strictly to the expenditure ceilings set in the BROP. The National Treasury reviews sector priorities for compliance and, where necessary, recommends amendments. This process yields sector budget proposals.

4.8 Final budget preparation and budget approval

92. Budget documents are submitted to Parliament for final approval of the budget based on the adopted BPS. Details of the budget documents are shown in Box 4-5.

Box 4-5: Budget documents for submission to Parliament as per the PFMA

Estimates of expenditure and revenue

The estimates include a list of all entities that are appropriated from the budget; estimates and explanations of revenue and expenditures flows from and to the Consolidated Fund; all revenue allocations to county governments from the national government's share; all estimated revenue by broad economic classification; all estimated expenditure, by vote and by programme, clearly identifying both recurrent and development expenditure; an estimate of any budget deficit or surplus for each financial year over the MTEF—and the proposed sources of financing.

Budget summary

The summary outlines budget policies on revenue, expenditure, debt and deficit financing; explains how the budget relates to the FRPs and discusses how the resolutions adopted by the National Assembly on the BPS have been taken into account.

Specific information

Specific information includes loans and guarantees made to and by the national government; payments to be made and liabilities to be incurred by the national government for which an appropriation is not required and measures to implement recommendations of the National Assembly.

Appropriation Bill

Upon approval of the budget estimates by the National Assembly, the Cabinet Secretary shall prepare and submit an Appropriation Bill of the approved estimates to the National Assembly.

Box 4-5: Budget documents for submission to Parliament as per the PFMA

Finance Bill

The Finance Bill sets out the revenue-raising measures for the national government and is approved with or without amendments by the National Assembly.

Division of Revenue and County Allocation of Revenue Bills

These bills are approved by Parliament with or without amendments not later than 30 days after they have been introduced.

Budget Highlights (Mwananchi Guide)

The Budget highlights cover key elements of budget policy and revenue-raising measures in plain language for the public.

Statistical Annex to the Budget Statement

Background statistics to the budget, containing historical data series on key macroeconomic indicators, national budgets and the public debt.

Source: PFMA, sections 37-42.

93. Following approval by Cabinet, the budget documents are submitted to the National Assembly by 30th April. The submission comprises documentation supporting the budget estimates and any other bills required to implement the budget.[20] The documents are prepared by the National Treasury and the Cabinet Secretary is responsible for submitting the budget documents to the National Assembly for review. However, this package excludes budget estimates for Parliament and Judiciary, which are submitted to the National Assembly by the accounting officer for the Parliamentary Services Commission and the Chief Registrar of the Judiciary respectively. The National Treasury is provided with copies of these estimates and may comment on them by 15th May.

94. The National Assembly approves the budget estimates with or without amendments by 30th June for publication.[21] Before the National Assembly considers the estimates of revenue and expenditure, the relevant committee of the house reviews the estimates and makes recommendations to the National Assembly, considering the views of the Cabinet Secretary and the public on the proposed recommendations.[22] Budget amendments by

20 *PFMA, section 37.*
21 *PFMA, section 39.*
22 *These include departmental committees and the budget and appropriation committee*

the National Assembly have vested conditions: an increase in expenditure in a proposed appropriation must be matched by a reduction in expenditure elsewhere.

95. The National Treasury consolidates, publishes and publicises the approved budget. This must take place within 21 days of National Assembly approval. [23]

96. During implementation of the approved budget, MDAs may ask the National Treasury for authority to reallocate funds within and across programmes, or for additional funding to cater for emerging priorities. The National Treasury may grant such approvals under Article 223 of the Constitution. This presents a variation from the original budget and therefore, the National Assembly approves the revised budget estimates through a Supplementary Budget.

97. Section 43 of the PFMA gives power to accounting officers of national government entities to reallocate funds between programmes, or between Sub-Votes, in the budget for a financial year, in the following circumstances:

- Where provisions made in the budget of a programme or Sub-Vote are available and are unlikely to be used.
- Where a request has been made to the National Treasury explaining the reasons for the proposed reallocation and the National Treasury has approved it.
- If the total of all reallocations to or from a programme or Sub-Vote does not exceed 10 percent of the total expenditure approved for that programme or Sub-Vote for that year.

However, such powers are limited to the extent that the accounting officer shall not authorise the transfer of an amount that is appropriated:

- For transfer to another government entity or person
- For capital expenditure except to defray other capital expenditure
- For wage to non-wage expenditures
- If the transfer may result in contravention of FRPs.

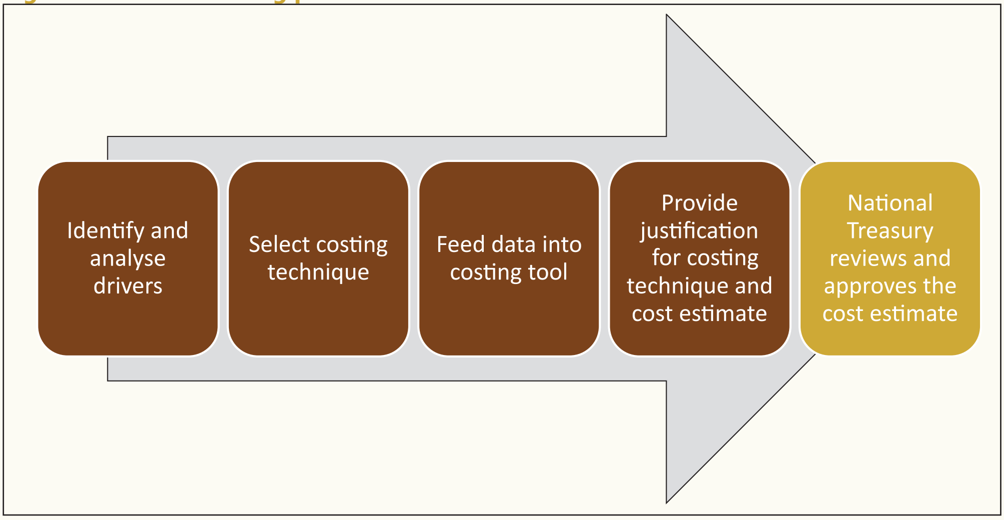
23 *PFMA, section 39.*

CHAPTER FIVE: COSTING THE NATIONAL BUDGET

5.1 Overview

98. This chapter sets out the rationale for costing the national budget. It introduces the costing process and sets out the rationale for a costing methodology and describes different costing techniques. It then provides an overview of the costing tool and guidance on how to conduct a budget baseline exercise for the recurrent and development budgets. The main stages of the costing process are shown in Figure 5-1.

Figure 5-1: The costing process



Source: National Treasury

5.2 Rationale for a costing methodology

99. A standardised costing methodology is a precondition for calculating a budget baseline. It sets cross-cutting standards for costing policies of all sectors, thereby supporting data reliability and comparability. The benefits of costing policies in a standardised manner include reviewing estimates in a comparable way; fostering comparability of calculation results; facilitating a process of challenging the calculation results to verify data; providing verified data allow for matching policy priorities with an expenditure ceiling and measuring value for money performance.

100. A costing methodology is used for budget impact assessment of proposed new policies. MDAs are required to develop a rapid assessment of the affordability of policy proposals in the budget

preparation process. A standardised costing methodology facilitates a sound and objective determination. This will ensure that MDAs produce more realistic budgets as opposed to wish lists.

101. Costing requires documentation to allow traceability and support validation of the estimates by National Treasury. Sectoral budget baseline calculations are documented according to costing methodology instructions provided in the MTEF Circular. The documentation is submitted to National Treasury with the calculation results, which are used to assess their validity.

102. Identifying and analysing the primary revenue and expenditure drivers of existing policies is a key element of costing. The medium-term factors influencing revenue and expenditure of each policy are identified and their associated developments analysed, as shown in Box 5-1.

Box 5-1: Examples of key expenditure and revenue drivers

Each driver has a quantitative component (such as the number of teachers or doctors) and a price component (such as the average salary per teacher or doctor).

Key expenditure drivers for education: Pupils, teachers, schools.

Key expenditure drivers for health: Patients, nurses, doctors, other health staff, hospitals and medicine.

Examples of revenue drivers: Consumption for value-added tax, personal income for personal income tax and users of public services for user fees.

Analysis reveals which drivers are relevant for which policy area and the forecasts for these drivers over the MTEF. This requires good databases that should be updated regularly.

Source: National Treasury

5.3 Costing techniques

103. The National Treasury's costing methodology incorporates four techniques and covers both the recurrent and development budget. These are: (i) quantity x price; (ii) trend; (iii) lump sum, and; (iv) ad hoc. The methodology is applied by all national government entities during the budget baseline process, with specific costing guidelines communicated by the National Treasury to MDAs in the MTEF Circular. An additional initial classification of projects

is required for development expenditure to help identify which projects are selected for the budget.

104. The application of the costing techniques is applicable over the MTEF period. The projected ceilings communicated in the most recently published MTEF serve as a guide for the costing exercise. The outer year (FY+2) will not have been estimated in the previous MTEF; for the purposes of the costing exercise. MDAs are advised to use the outer year (FY+1) as the provisional ceiling for the outer year (FY+2).

5.3.1 Costing technique: *quantity x price*

105. The preferred costing technique is quantity x price. For each budget sub-item, the technique that provides the most plausible result should be identified and used for calculation. Where possible, quantity x price should be prioritised as the most transparent of the recommended techniques. For MDAs to properly cost existing policies, they should have full knowledge of the cost drivers for their different interventions.

106. When applying quantity x price, users identify the "cost drivers" for expenditure defined by the total quantity of units and price per unit. This method requires identifying the units of measurement, the quantities of each unit involved and the different prices associated with the sub-items. Quantities are the result of the number of units multiplied by the frequency within a financial year. Examples are outlined in Table 5-1. The standardised calculation template includes columns for quantity (number of units multiplied by frequency) and price. MDAs are required to use this calculation method and any deviations from this approach must be justified.

Table 5-1: Examples of applying quantity x price

Expenditure	Quantity (number of units x annual frequency)	Price
Basic salary	Number of employed staff per grade x 12	Average monthly salary per grade
Subsidy	Number of beneficiaries x 1	Average amount per beneficiary
Utilities	Number of kWH (energy) or cubic meters (water) x 1	Price per kWH or cubic meter

Expenditure	Quantity (number of units x annual frequency)	Price
Road construction	Number of kilometres of a specific road category x 1	Price per kilometre

Source: National Treasury

107. When applying quantity x price a number of factors will be considered:

- **Variations by financial year:** Quantities and prices might differ from one financial year to the next; these numbers need to be disclosed.
- **Inflation:** The National Treasury will guide whether inflation shall be considered when calculating the prices and, if so, which inflation rate should be applied for which financial year within the medium-term timeframe.
- **Exchange rate:** For some sub-items (such as imported goods), exchange rates might apply. The National Treasury will guide which exchange rate should be applied for which foreign currency.
- **Standard commodities:** Some commodities (such as oil) might be important cost drivers for more than one MDA. To support comparability and plausibility of calculations the National Treasury will guide MDAs on which price to use for which of these commodities and for which financial year.

5.3.2 Costing technique: trend

108. This approach extrapolates past trends based on the expenditure pattern of the sub-item over a period of three or more years. This technique might be applied if quantity x price is not applicable (e.g. due to inadequate data for quantities and prices involved, or where calculations are too complex) or where there is no indication available that future developments might substantially deviate from the past. An example could include small stationery items.

5.3.3 Costing technique: lump sum

109. A lump sum is a fixed amount that is kept nominally constant for each of the three upcoming financial years. As a single figure, it does not require any additional calculation and analysis of cost drivers (quantity, price). Using a lump sum for estimating future expenditure is plausible when the expenditure amount on the sub-

item level is below a certain threshold[24] and there is no indication of a substantial change in the future. In this case, the lump sum calculation simplifies the baseline procedure without hampering credibility. An example could include payments for subscriptions to international organizations.

5.3.4 Costing technique: ad hoc

110. An expenditure is ad hoc if it is not regular and will only be relevant for one or two of the years of the MTEF. It could refer to expenditure expiring in the first or second upcoming financial year; new, approved expenditure starting in the second or third year of the MTEF; or one-off expenditure that only happens in one upcoming financial year. One-offs might require application of quantity x price technique for the relevant financial years as the amount might be driven by a certain quantity of units and unit prices, while in other cases one-offs might just be a lump sum as a fixed amount of expenditure might apply. Box 5-2 outlines some examples of ad hoc spending.

Box 5-2: Examples of ad hoc spending

Large events that do not occur annually. For instance, a conference organised by the government will usually incur expenditure in the financial year in which it is held. The previous and subsequent financial year will not be affected. Therefore, the expenditure required for the conference will be one-off and should only be calculated for that one particular financial year.

A court award that the government is expected to pay in one instalment.

Source: National Treasury

5.4 Application of the costing tool

111. Costing is conducted using a customised tool provided by the National Treasury. This system uses the Standard Chart of Accounts (SCOA) definitions used by MDAs to prepare the budget baseline at sub-programme, sub-head, sub-item and geographic location.

112. The tool enables costing to be undertaken at the sub-item level and has four components that MDAs use to conduct the costing exercise. MDAs are required to identify programme objectives and responsibility, cost recurrent expenditure, update the status of development projects and cost development expenditure. The entire MDA budget baseline will be consolidated within the costing tool.

24 *As determined by the National Treasury*

113. Each department head is responsible and accountable for costing their departmental activities and respective projects. The costing tool adopts the same structure as part of the standard budget preparation process. The officers responsible for finance should request cost centre managers to prepare costing individually, submitting these for review, consolidation and submission to the National Treasury by the accounting officer.

114. Costing is undertaken at the sub-item level, with the unit description, identification of costing technique and funding source required to be entered. With the spending sub-item identified with the SCOA, the tool then requires the MDA to provide a description of the unit, including the costing technique used and the source of funds for the sub-item. The interface of the recurrent and development forms varies slightly: recurrent requires the identification of the policy as either new or ongoing, while development draws information on the status of the project and consequent implications for funding.

115. Costing is undertaken over the medium term and as such costing fields must be completed for each financial year in which there is an anticipated cost for the sub-item. The chosen costing technique has implications for the data required for costing and the tool provides fields for entering number of units, frequency, and price if the quantity x price technique is selected. If another methodology is selected then the amount is entered as “other”.

116. Any verified pending bills must be included as per reporting date and legal requirements. Verified pending bills will generate expenditure and need to be considered when calculating the budget baseline.

117. The costing tool checks consistency with the latest expenditure ceiling. The tool automatically calculates total sub-item cost per financial year, including the verified pending bills, and then sums all sub-items of a vote to the calculated baseline expenditure of the vote for each financial year (for recurrent and development expenditure). The tool compares the baseline amount with the expenditure ceiling (recurrent or development) and calculates and illustrates any gap. This allows identification of negative or positive fiscal space for the given financial year at a glance.

118. Justification is required for costing, which is the entry point for budget scrutiny. Evidence here will be used within the MDA by officers responsible for finance to review the estimates made by cost centre managers, within SWGs during Resource Allocation Panels, and by the National Treasury to review estimates delivered by MDAs. The justification fields follow the same logic as the costing data: if the quantity x price technique is selected, the MDA is expected to justify first the quantity and frequency, then the price; if any other technique is selected, this choice and the cost itself is justified.

5.5 Conducting a budget baseline forecast for the recurrent budget

119. This section guides users on how to calculate a budget baseline for recurrent expenditure. The costing tool covers the different categories of recurrent expenditure.

5.5.1 Wages, salaries, allowances and pensions

120. The budget baseline projection will precisely quantify numbers of staff in each sector. Given that wages and salaries represent a significant share of government expenditure, forecasting them as accurately as possible is necessary for a credible budget projection and requires thorough analysis.

121. Staff numbers usually differ between approved and filled positions. The budget baseline projection aims to identify the most likely result of staff numbers for each grade over the MTEF. This requires sound and informed judgement on whether all vacant positions will be filled. This view can be based on experiences in previous financial years, as well as a clear assessment of the likelihood of a change in staffing levels based on the approvals provided by the Public Service Commission and the National Treasury.

122. The budget baseline projection multiplies staff numbers with their wages and salaries. The different amounts applicable to staff grades and allowances are factored into this calculation. Given that decisions about the distribution of non-payroll allowances might only be made during budget execution, baseline projections can use averages based on the experience of previous years. If there are strong arguments for doing so, projections can consider additional circumstances that may apply in the upcoming financial years.

123. Salary increases can influence the wage bill substantially. Contributing factors include collective bargaining agreements, creation of new offices, revision of schemes of service and promotions. MDAs require approval from the Public Service Commission, the Salaries and Remuneration Commission and the National Treasury before including adjustments in the baseline. Box 5-3 shows options on how to address salary and wage increases in the baseline forecast.

Box 5-3: Factoring salary and wage increases into the budget baseline calculation

There are several options to factor salary and wage increases into the budget baseline.

Assume a salary increase aligned with the projected inflation rate: While this seems to be an obvious option, it may conflict with the requirements for budget cuts and/or wage bill negotiations. When the government assumes inflation-linked compensation into the budget, trade unions may use this as an argument that the government has already accepted inflation compensation and insist on additional salary and wage increases. This can be avoided by using the next option.

Calculate a certain amount for salary and wage increases in the budget reserve: Usually, the budget reserve is not specified by outlay, so it could be used to budget for salary and wage increases without revealing the respective magnitude. Although this approach might support the government's position in wage negotiations, it lacks transparency.

Require sectors to cover salary increases within their expenditure ceilings: In this approach the amount of any salary and wage increases is not budgeted for individually across MDAs, which are required to manage the increase within their expenditure ceilings. MDAs should be aware of this requirement in advance, so that they can reserve some space for covering the still unknown salary increase when projecting different line items.

Clarify the salary increase in time to factor the result into the draft budget: From the standpoint of reliable planning, this is the preferred option. However, such an early agreement on salary and wage increases might not be realistic given negotiation schedules.

Wage increases are determined by a given wage drift. The National Treasury computes the average wage drift. This is determined by the annual increments and considers any possible promotions, especially for common cadre officers.

Source: National Treasury

124. The budget baseline calculation for the wage bill should be comprehensive and realistic. This is necessary to avoid excessive supplementary budgets to fully cover an underestimated wage bill, and/or in-year budget cuts of other expenditure categories to compensate for a higher-than-budgeted wage bill. Either outcome would undermine the credibility of the budget and create budget execution challenges.

125. Calculating pensions for public officers requires consideration of different factors. Pension payments are driven by the number of pensioners and the average pension per category. These factors should be well known and allow for reliable baseline forecasts by the National Treasury. The number of pensioners is influenced by the age cohorts of staff reaching retirement age, incorporating the estimated number of deaths of pensioners per year, based on average mortality rates.

126. Government's contribution to the Public Service Superannuation Scheme is calculated based on a set percentage. This annual contribution will be calculated as total contributing employees multiplied by a proportion of basic monthly salary, multiplied by 12 months.

5.5.2 Goods and services

127. Calculating a budget baseline for goods and services may require various costing approaches. While some goods or services are suited for using quantity x price (such as cost of trainings, workshops, computers, utilities), others (such as stationery) comprise many small items where it may be practical to avoid a cumbersome detailed calculation. In this case, assumptions based on trend analysis (such as expenditure for stationery in previous financial years) may offer a pragmatic alternative.

5.5.3 Transfers and subsidies

128. Transfers and subsidies will in most cases be calculated by using quantity x price. For most transfers and subsidies, the number of beneficiaries and the (average) amount per beneficiary are known for recent financial years. Policy analysis should allow the sectors to assess how any of those parameters will presumably develop in each year of the upcoming MTEF.

129. Estimating transfers and subsidies requires databases that are updated regularly. The responsible sector should document

the number of beneficiaries per policy and the (average) amount per beneficiary in a database. Sectors should keep the databases current to provide a reliable foundation for policy analysis and should ensure that the National Treasury has this data available to scrutinise assumptions.

130. Transfers undertaken in the development budget should adopt the principles set out above. In most cases the calculations will use quantity x price. For most transfers the number of beneficiaries and the (average) amount per beneficiary should be known. Conditional grants that include donor financing will be included as development budget items and should include the quantity x price costing based on the grant agreements.

131. All semi-autonomous government agencies are bound to the budget preparation calendar, the MTEF circular and costing techniques outlined in this manual. Parent MDAs are responsible for delivering the required budget information for semi-autonomous government agencies under their responsibility to the National Treasury, and the costing techniques outlined in this manual will be applied to these agencies.

5.5.4 Interest payments

132. Calculating interest payments for domestic and foreign debt requires specialized knowledge and is performed by the debt management directorate within the National Treasury. Interest payments are driven by the size and structure of the loan, and the implications of the forward path of interest rates (for variable rate loans) and exchange rates (for those denominated in foreign currency). Debt projections factor in the debt stock and forecast additional debt that may arise from the projected deficit for upcoming years.

5.6 Conducting a budget baseline forecast for the development budget

133. This section guides users on how to prepare the budget baseline for development expenditure. It covers the requirements of the PIM Regulations, 2022, and implications of these requirements for budget costing, including for existing projects and proposed projects, and project selection for inclusion in the baseline.

5.6.1 Defining project status

134. The PIM Regulations define existing projects as either ongoing or stalled, and proposed projects as either pipeline or new. See Table 5-2. The regulations describe the actions required to achieve pipeline status.

Table 5-2: Project status definitions

Status	PIM Regulations definition
Existing projects	
Completed	A project that has been fully implemented, with expected output delivered as per the project implementation plan.
Ongoing	Implementation is under way, with works having commenced or contractual commitments entered into.
Stalled	Project implementation has halted, or the project has received minimal budget allocations over the medium term that cannot facilitate meaningful progress.
Proposed projects	
New	A pipeline project that has been prioritised and financed, but work is yet to begin.
Pipeline	A project that has been appraised and granted the necessary approvals.

Source: National Treasury

5.6.2 Costing of existing projects

135. Existing projects must be included in the baseline and fully costed for all existing commitments in accordance with the PIM Regulations. Existing projects include certain completed and all ongoing and stalled projects. The starting point for deriving the development budget baseline is project commitments. These include verified pending bills, contractual obligations, and other obligations related to externally financed projects. These commitments, defined in Box 5-4, should be used to estimate the development baseline.

Box 5-4: Defining multi-year commitments

Commitments are agreements or contracts made by MDA accounting officers to make payment(s) to another party in exchange for that party supplying goods and services or fulfilling other agreed conditions. Commitments can be for specific works, goods or services and arise when a formal action is taken by an MDA, such as issuance of a purchase order or signing of a contract.

A multiyear commitment arises if the stream of payments arising from a commitment extends over multiple years.

Verified pending bills and agreed government contributions to externally financed projects should be recognised as commitments.

Source: National Treasury

136. Existing project costs will use quantity x price for most items identified in project design documents. Costing of construction and fittings, plant and equipment, human resources and other administrative costs must all be quantified using the same units as described in the technical specifications, bill of quantities and other project documents. It is neither useful nor practical to cost very small items or detailed components of a larger item, so costing may be conducted at an aggregate level. In some cases, this may require the use of a lump sum approach.

137. As with the recurrent budget, certain cost drivers are considered. Accurate updates to the baseline are required for project implementation, indicating any cost changes as a result of phasing, frontloading, or re-scoping. Other common factors related to cost overruns include delays to schedule, penalty charges or increased interest payments, particularly for projects that have stalled due to the lack of adequate budget resources.

138. MDAs should support the costing justification of ongoing projects by submitting standard schedules of costs such as bill of quantity documents. The documents should be uploaded to the costing tool attached to the costing item. Costs provided in the costing tool and/or in bills of quantities should be consistent with those submitted in the e-Procurement system and the Market Price Index regularly published by the Public Procurement Regulatory Authority.

139. MDAs must review and update the maintenance and lifecycle costs for ongoing projects provided in the project concept note (PCN). The PCN provides information on the estimated lifecycle costs of a project. While the project is under way, these estimated costs must be reviewed, updated and incorporated into the budget baseline. Where an existing project does not have a PCN, the MDA should prepare the information for part 9(D) of the PCN as prescribed in the PIM Regulations for inclusion in the costing tool. The PIM Regulations require MDAs to carry out routine and periodic maintenance (Box 5-5) to ensure the sustainability of completed projects.[25] Costing should differentiate between routine and periodic maintenance. Maintenance for regular operation of the asset should be costed under the recurrent budget as an ongoing cost. Significant rehabilitation or extension works should be costed as new capital expenditure projects.

Box 5-5: Routine and periodic maintenance

Routine maintenance is typically cosmetic and preventive maintenance that is performed regularly to keep an asset operating according to its design. Funding needs are usually calculated using the age and number of assets in an asset class, not project by project. In other words, budgeting for routine maintenance can be estimated with a formula, rather than based on asset-by-asset inspection. Maintenance funded through the recurrent budget is usually routine maintenance.

Periodic or capital maintenance is often necessary to enable an asset to reach its planned life. Without periodic rehabilitation, for instance every 10 or 20 years, the asset may have to be phased out earlier than planned. Capital maintenance also includes activities to enable an asset to extend its life and to increase its capacity. This is often referred to as reconstruction. Rehabilitation and reconstruction activities typically are funded through the capital budget, and for convenience, are collectively referred to as capital maintenance.

Source: National Treasury

140. Stalled projects may still incur costs associated with existing commitments and these costs must be included in the project baseline. Commitments including verified pending bills for stalled projects may include ongoing maintenance fees, legal fees, compensation or other associated costs. These are costed in the same manner as with ongoing projects.

25 *The National Treasury will develop methodologies to identify funding needs for routine and capital maintenance.*

141. Termination/cancellation costs are heterogeneous, depend on multiple factors, and are calculated on a case-by-case basis. Various factors need to be considered when assessing the financial consequences of termination or cancellation. These include the costs associated with closure of site offices, the sale or disposal of assets, ongoing maintenance fees, legal fees, and compensation or other associated costs. These are included in the budget baseline if this decision is made for a particular project (Box 5-6).

Box 5-6: Factors to be considered in potential project termination

Several factors should be considered in a potential project termination:

Are the relevant contract terms available for a judgment to be made? If not, they should be requested early to avoid delays and/or gaming by MDAs. This request could be strengthened by informing that a "no response" would result in an assumption that there are no financial consequences.

Would termination incur explicit costs? These would include contractual penalties, interest and other charges as well as the payment of any arrears.

Would termination incur contingent costs? Might additional costs be incurred if the termination lasts beyond a certain timeframe? Would termination lead to costs being incurred to make an unoccupied site safe and secure? Would it result in unintended environmental costs? What would be the start-up costs if and when financing resumes?

What are the legal consequences? Will the termination result in:

The government breaking any laws?

The violation of any international treaties?

Material breaches of agreements with development partners?

Material contractual breaches with private companies?

Source: National Treasury

5.6.3 Costing of proposed projects

142. The costing process for pipeline and new projects is well documented in the PIM Regulations and related schedules. To be included in the pipeline, a project must be independently appraised and approved by the National Treasury having met the relevant requirements of the PIM Regulations including a completed PCN and, where applicable, a pre-feasibility and/or feasibility study.

143. The PCN requires standard information regarding project costs and costs associated with future operation of the completed facility where relevant. The PCN requires an annualised breakdown of the estimated cost of the project. The information should clearly separate the costs of prerequisites and actual implementation by financial year. This information must be consistent with what is entered into the costing tool when costing the project. Further, PCN requires information on the estimated annual operation and maintenance costs. To reflect lifecycle costs properly, this information should clearly state annual costs estimated for routine maintenance and operation (under recurrent expenditure) as well as for capital maintenance (under capital expenditure). The costing tables in the PCN must clearly show when operation or maintenance costs are expected to be incurred following project completion. These costs must be included in the budget baseline under the programme responsible for the facility, if scheduled in the medium term.

144. Pre-feasibility and feasibility studies shall be undertaken with existing capacity or sourced from other government institutions. Activities shall be undertaken using internal capacity of the MDA or from another government institution. However, external expertise may be sought as provided in PIM Regulations. Such additional resources should be costed within the department providing the capacity or, if capacity from another government institution is used, any allocation for facilitation of the work must be costed by the MDA and included in the budget baseline. The cost of a feasibility study shall not exceed 5 percent of the estimated total cost of a project and the total budget of all feasibility studies should not exceed 5 percent of the MDA's annual development budget.

145. Pipeline projects that require funds to complete conditions precedent and other prerequisites of the PIM Regulations require a consistent costing approach. Table 5-3 maps the major cost drivers for these prerequisites and their costing considerations. Wherever possible, MDAs should use the same units as identified in the appraisal documents, including technical design documents and the environmental and social impact analysis.

Table 5-3: Costing considerations for project prerequisites

Prerequisites in PIM Regulations	Costing considerations
Ensure all conditions precedent have been fulfilled, including **land acquisition, compensation**, stakeholder management and other development partners' requirements have been met.	Land acquisition and any compensation costs should use the *quantity x price* costing technique as a priority. The price per square kilometre or compensation costs per person or other entity are extremely important to compare with standards, regulations and other similar projects and assess value. Legal fees related to project prerequisites may require the use of the lump sum costing technique.
Ensure detailed **designs** have been completed.	Design costs are likely to be costed using the lump sum technique.
Ensure that the project has received necessary **regulatory approvals.**	Regulatory approvals are likely to be lump sum.
Ensure that detailed resource requirements are planned for, including source of funding and **personnel** to operationalise the project.	Personnel requirements can be costed using *quantity x price*.

Source: National Treasury

5.6.4 Project selection and costing implications

146. The PIM Regulations outline structured criteria for project selection for budgeting. Existing projects must be funded first; then, where fiscal space allows, new projects may be considered. Clear decisions must be made for a pipeline project to be selected for budget resources to cover prerequisites or, if those are met, a separate decision must be made to include the project in the budget for full implementation.[26]

26 For example, the PIM Guidelines indicate that where the project prerequisites have not been met, the accounting officer shall only request for budgetary resources to meet these prerequisites in that financial year.

147. Before projects are prioritised for resource allocation, a review of the status of all existing and new projects will be required to support the costing of the development baseline. The status of a project will change as it progresses through the project cycle. A review at the start of the baseline costing exercise ensures that the list of existing projects and project pipeline is complete, and the status of each project is verified. The status has implications for the costing of that project and whether it will be included in the budget baseline. All pipeline projects should be costed to ensure they are ready for entry into the budget baseline if they are selected for funding. Specific decisions around costing must be identified and made for projects of each status to enable clear cost estimates.

148. Costs projected to be incurred in the medium term should be included in the baseline. This may include security, idle capacity and litigation costs among others. Ongoing and stalled projects are prioritised for allocations to allow progress towards completion or, where the project is no longer viable, cancellation/termination. Each of these have cost implications that must be factored into the baseline. Table 5-4 outlines the related implications. The National Treasury must approve new and pipeline projects before they can be included in the budget baseline. This will ensure that all new and pipeline projects meet the requirements of the PIM Regulations and the MTEF Circular.

Table 5-4: Costing/baseline implications on the project status

Status	Costing Implication
Existing Projects	
Completed	For projects that result in capital assets, ongoing operation and maintenance costs become the responsibility of the department managing the facility once handed over. MTEF allocations could include unpaid closure costs and those related to the defects and liabilities period.
Ongoing	The medium-term requirements shall be costed and be covered in the MTEF period.
Stalled	Cost projected to be incurred in the medium term should be incurred in the baseline. This may include security, idle capacity and litigation cost among others.

Status	Costing Implication
Proposed projects	
New	All conceptualisation and preparation costs planned for the upcoming three fiscal years shall inform the baseline. The medium-term requirements shall be costed and be covered in the MTEF period.
Pipeline	All conceptualisation and preparation costs planned for the upcoming three FYs shall inform the baseline. The medium-term requirements shall be costed and be covered in the respective MTEF period.

Source: National Treasury

CHAPTER SIX: BUDGETING AND MONITORING FOR RESULTS

6.1 Overview

149. This chapter explains the purpose of programme-based budgeting (PBB).[27] It provides a step-by-step process for MDAs to apply PBB effectively as part of the budget process. The chapter:

- Defines programme classification and how it is aligned to the structure of government.
- Explains core principles required for designing effective results chains to guide medium-term planning.
- Outlines how monitoring, reporting and evaluation of programmes supports budgetary decision-making.

150. PBB is a means of linking the government budget to public policy objectives. PBB covers both financial and non-financial information and the results in terms of outcomes and outputs, which are used in the budget preparation process. Discussions on the allocation of financial resources and on the proposed or previously delivered policy results should be linked. The budget preparation calendar (Annex 1) identifies key junctures for this in September and November during the SWG process, where sectors are required to prioritise programmes within expenditure ceilings and produce a report on the choices made.

151. PBB results inform the setting of expenditure ceilings. Expenditure ceilings do not merely perpetuate past budget allocations but consider programme performance. Performance monitoring reports required by the PFM Regulations are, therefore, provided in due time prior to setting expenditure ceilings. [28]

6.2 Using PBB for budgetary decision-making

152. PBB supports policy prioritisation as part of the SWG process. The intended policy deliverables expressed in result chains of programmes, and the financial resources requested for them, should provide decision-makers with good arguments to prioritise scarce budget resources both among and within sectors.

153. PBB monitoring and evaluation results can be used to rank programmes to facilitate prioritisation within budget ceilings.

27 *This part of the manual focuses predominantly on how PBB informs the planning and budgeting process outlined in previous chapters and should be read in the context of the more detailed PBB manual.*

28 *PFM Regulations, section 136(4).*

Furthermore, non-financial performance information might reveal overlap among budget programmes, which would offer opportunities to make budget cuts without impacting intended policy results.

154. Underperforming programmes should be subject to scrutiny. Options include improving service delivery by enhancing effectiveness and efficiency, scaling down budget allocations or discontinuing these programmes. Programmes with a low value for money record would indicate opportunities for reducing expenditure or redeploying resources to other programmes with a better performance, or to promising new initiatives. This requires using the monitoring and evaluation results for upcoming budget decisions.

6.3 Programme classification

155. Government policy and strategic planning are divided into 10 "policy areas", known as sectors, each of which has specific objectives.[29] These form the starting point and highest level of classification in the PBB structure.

156. Sectors are designed to allow stakeholders in the budget process to see which programmes are being implemented by the government. This includes relevant public services and budget appropriations allocated to each sector at programme and sub-programme level. Programmes are groupings of activities aimed at achieving outcomes and outputs within the general objectives of a policy area.

157. Within the PBB architecture, budgets are costed, presented, and justified in terms of programmes with supporting performance information.[30] A programme classification structures the budget to support effective and efficient planning and use of resources. Public services and activities with a common outcome in a given policy area are grouped together to form a programme.

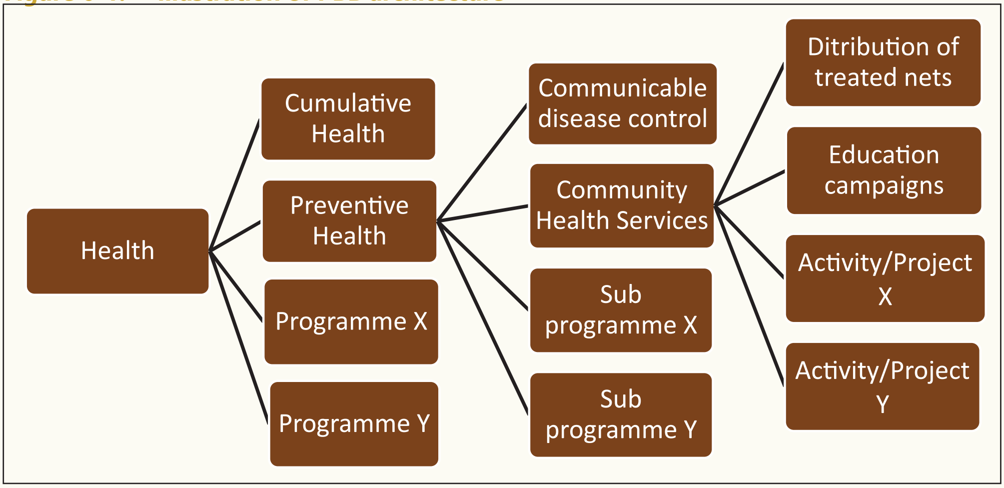
158. PBB therefore structures the budget according to sectors, programmes and sub-programmes that implement specified general policy objectives. PBB requires multi-year programmes, definition and measurement of outcomes and outputs to assess

29 Refer to section 2.2.

30 Presentation of the budget in programme format is a legal requirement under Section 38 (1)(b)(v) of the PFMA, 2012.

achievement of general policy objectives. Figure 6-1 provides an illustration of the PBB architecture.

Figure 6-1: Illustration of PBB architecture



Source: National Treasury

6.4 Alignment of organisational structures and programmes

159. Programmes are aligned to specific lead implementing MDAs. Effective and efficient management of public resources require a clear alignment of the administrative structure with programmes.

160. There should be clear organisational accountability for programmes. Each programme is assigned to one MDA and delivery unit responsible for its successful implementation, even if several units contribute. In such a case, one unit is responsible for leading the programme for accountability purposes and coordinating all contributions to ensure that the intended results are achieved. Box 6-1 outlines typical tasks that a leading and a contributing organisational unit is responsible for. Programme management structures should be kept as simple as possible to avoid accumulation of administrative costs.

Box 6-1: Tasks for lead and contributing delivery units

Lead delivery unit:

- After consultation with the contributing delivery units, design and approve a programme results chain.
- Conduct policy analysis on the requirements for successful programme implementation.
- Work with contributing delivery units to define their specific programme contributions.
- Proactively monitor and evaluate the performance of the programme.
- Report on the financial and non-financial performance of the programme.
- In case of performance gaps, undertake corrective action.
- After discussions with contributing units define requirements (particularly undertake capacity building and data improvement) to successfully implement a programme.

Contributing delivery units:

- Comment on proposed results chain of the programme.
- Conduct policy analysis on the requirements for successful contribution to implementation.
- Deliver the agreed results/contribution of the unit to the programme.
- Proactively monitor and evaluate the performance of the contribution to the programme.
- Report on the financial and non-financial performance of the sub-programme to the lead delivery unit.
- In case of performance gaps, undertake corrective action.

Source: National Treasury

161. The programme structure is approved by the National Treasury to ensure the building blocks are sufficiently in place in accordance with the PFM regulations 2015. The PFM Regulations reinforce the point under section 136 (1) in terms of design of the results chain structure and 136 (2) for a robust IT system that can collect, exchange, and store non-financial information (Box 6-2). The non- financial information includes outcomes, outputs, indicators and targets.

Box 6-2: Governance arrangements for linking programme and organisational structures

The Cabinet Secretary prescribes a framework for monitoring and reporting on non-financial performance for use by accounting officers in evaluation of programmes and projects by measuring:

- Financial indicators that capture expenditure on implementation

Box 6-2: Governance arrangements for linking programme and organisational structures

- Output indicators that measure what is directly supplied through implementation
- Outcome or results indicators that capture the expected effects on intended beneficiaries.

The Cabinet Secretary also establishes a system to facilitate efficient and effective data collection, storage and exchange to monitor and report on non-financial performance of the national government entity's individual programmes and projects.

Source: PFMA Regulations, sections 136 (1) and (2)

162. MDAs are required to seek approval from the National Treasury if any changes are to be made to the programme structure. Given that programmes are reflected in the SCOA and require budget allocations, issues around the creation and alignment of new programmes and consistency with the SCOA require strict controls through an automated IT system.

6.5 Design of effective results chains

163. A results chain is a consistent sequence of elements for a policy or programmatic intervention to produce a defined result. MDAs are required to develop results chains under programmes and projects as part of the multi-year budget process, and will report against these as part of in-year and annual reporting.

164. The design of a results chain should be easily implementable across MDAs and as lean as possible to avoid information overload. Standardised templates are issued by National Treasury (see Annexes 3-6). These are communicated as part of in-year instructions.

165. MDAs are required to provide a full narrative of results in the annual and multi-year budget submissions. This includes:

- What the MDA accomplished in the previous three years and at what cost.
- Major challenges encountered during implementation of the previous medium-term budget and how to address the challenges in the forthcoming budget.
- Which outcomes and outputs (with which performance indicators and targets, respectively) the MDA plans to accomplish over the medium term.
- What it will cost to realise the MDA's outcomes and outputs in the forthcoming budget and over the medium term.

166. A precondition for formulating proper result chains is a diagnosis of policy challenges. Implementing government or sector strategies via PBB requires MDAs to clarify obstacles to achieving intended results. This provides the basis to properly formulate result chains, which should focus on overcoming these obstacles. Figure 6-2 outlines a methodology that can be used in that respect.

Figure 6-2: Conducting policy diagnosis: the challenge tree

Policy diagnosis requires one to identify the root causes of an identified challenge. This is due to the fact that what is observed could be the consequences of a given root cause.

Based on the results of the diagnosis, identify data required to quantify the challenge, its roots, and consequences. Make the data available and analyse it to identify the proper outcomes, outputs, indicators and targets for the programme in question. This exercise needs to be conducted for each challenge identified for implementing a policy priority.

Three steps to discuss the challenge for implementing policy priorities:

Step 1: Discuss and agree on the challenge – which becomes the trunk of the tree (the focal challenge).

Step 2: Identify the causes of the focal challenge – these become the roots of the tree

Step 3: Identify the consequences of the focal challenge – these become the branches of the tree.

Source: National Treasury

167. The following elements should be considered when forming a results chain based on the policy diagnosis:

- **Outcomes** describe the expected result for intended beneficiaries of the programme within available resources.[31] The outcome should be derived from the policy priority objective (s) outlined in a government or sector strategy. For instance, a programme to tackle malaria could have an outcome termed "Reduced prevalence of malaria cases by 20XX".
- **Outputs** are specified policy results (such as goods, products,

31 See PFM Regulations, section 136(1).

services) contributing to achieving a programme outcome. For the above mentioned outcome an output could be,. "Mosquito nets provided to households"

- **Indicators** measure the achievement of an outcome or of an output. One indicator alone usually cannot capture all the information related to the achievement of an outcome or of an output. The most appropriate indicators should be chosen to avoid complexity. This will involve limiting the number of indicators by outcome or output to ensure they are strategic and focused. For instance, an indicator for the above mentioned output could be "number of households provided with mosquito nets".
- **Targets** measure whether an indicator has been achieved and thus, specify a value or milestone that the indicator should reach by a specific date in the future. For instance, "100,000 households provided with mosquito nets by the year 20XX".

168. Result chains should highlight strategic policy issues and can be guided by best practice principles. The performance information in budget documents should focus on the strategic policy results particularly on outcomes, their indicators and targets. The S.M.A.R.T and C.R.E.A.M methodologies are stated in Annex 4 to provide guidance in these areas.[32]

6.6 In-year and end-year reporting on outcomes and outputs

169. A monitoring and evaluation (M&E) framework is an integral part of the budget process. Monitoring and evaluation are separate but mutually reinforcing components of the budget process. Monitoring focuses on whether plans are being implemented and the intended results are being achieved, while evaluation focuses on assessing the efficiency, effectiveness, impact, relevance, coherence and sustainability of programmes.

170. In-year and end-year reporting on outcomes and outputs is relevant in all stages of the budget process. The starting point is to have outcomes, outputs, performance indicators and targets monitored throughout the budget cycle developed and incorporated to form the basis of PBB. This process can benefit from automation to support standardisation (for example through the SCOA) and reduce the administrative burden associated with manual processes.

32 *S.M.A.R.T refers to outcomes and outputs that are Specific, Measurable, Achievable, Relevant, and Time-bound. C.R.E.A.M indicators are Clear, Relevant, Economic, Adequate, and Monitorable.*

171. M&E and reporting should focus on targets that were agreed on during the budget preparation stages and approved by Parliament. Each programme has one outcome, which is tracked through clearly defined performance indicators and targets. Sub-programme outputs are tracked through clearly defined performance indicators and targets.

172. Monitoring, evaluation and reporting should be based on a standardised framework guided by the Cabinet Secretary responsible for economic planning. The National Integrated Monitoring and Evaluation System as prescribed in the Kenya National M&E Policy provides a framework for monitoring, evaluation and reporting as required by PFMA Regulations section 136 (1) and (2). This facilitates a systematic and comparable conduct of monitoring, reporting and evaluation and thereby, supports the proper use of its results for decision-making.

173. The Central Planning and Project Monitoring Department coordinates development of outcomes, outputs, indicators and targets for the programmes in their respective MDAs. During programme implementation, progress is tracked by collecting data to assess achievement of the targets based on the performance indicators. This information is used by MDAs to report quarterly (for outputs) and annually (for outcomes) to the National Treasury.

174. Outcomes are monitored and reported at the end of each financial year. End-year monitoring, reporting and evaluation assesses whether intended programme results have been achieved and lessons learned for upcoming financial years to avoid performance shortfalls. The actual performance should be compared to the respective annual target set for each outcome indicator. The end-year reporting formats for programme outcomes are outlined in Annex 5 and are communicated through in-year Treasury circulars.

175. Although monitoring should be undertaken for all programmes, evaluation should focus on critical strategic programmes. Evaluations require substantial technical and administrative effort, which is not realistic on an annual basis for a given programme.

176. Outputs are monitored and reported quarterly. The purpose of the monitoring for the first three quarters of the year is to track in-year implementation progress of the annual output indicator

target and trigger corrective action to comply with the target where required. The report for the fourth quarter assesses whether intended programme results have been achieved for the full year. The in-year and end-year reporting formats for sub-programme outputs are outlined in Annex 6 and are communicated through in-year Treasury circulars.

Glossary

Terms	Definition
Activity	An action taken to achieve a policy priority; generally the smallest building block within a programme that has a definable purpose and specific allocated costs.
Budget	A statement of the government's proposed expenditures, revenues, borrowing and other financial transactions.
Budget baseline	The budget baseline quantifies the projected cost of existing policies on a "no-policy change" basis. This includes the costs of the current level of activity, which is the costs of ongoing programmes adjusted in light of the macroeconomic forecast, demographics, legally mandated requirements, one-time expenditures and the impact on a full year basis of decisions made in the current year.
Budget costing	An estimate of the fiscal cost of an existing or new policy over the MTEF period based on an understanding of the impact of key expenditure and revenue drivers.
Budget Policy Statement	A document that sets out the broad strategic priorities and policy goals that will guide national and county governments in preparing their budgets for the financial year and over the medium term. The BPS sets out historical budget performance, budget projections, policy decisions and priorities and binding expenditure ceilings.
Budget Review and Outlook Paper	The BROP elaborates the medium-term fiscal framework that determines the overall resource envelope and provides the background and parameters which form the basis for the detailed budget. The BROP includes expenditure ceilings to guide sectors to prioritise their policies and expenditure.
Cabinet Secretary	Cabinet Secretary responsible for matters relating to finance.
Development expenditure	Expenditure for the creation or renewal of assets that provide long-term public goods and services, such as roads and hospitals.
Fiscal risks	Factors that can cause fiscal outcomes to deviate from expectations as contained in the budget or other forecasts.
Fiscal rules	Commitments to constrain fiscal policy in the future by setting limits on and targets for key fiscal aggregates.
Fiscal space	The room in a government´s budget that allows it to provide resources for a desired purpose without jeopardising the sustainability of its financial position or the stability of the economy.
Medium-term Expenditure Framework Circular	A written instruction issued by the Cabinet Secretary providing broad guidelines on the budget process of the national government. This is issued in accordance with section 36 of the Public Financial Management Act, 2012.

Terms	Definition
Medium-term Expenditure Framework	An annual, three-year rolling budget and planning process. Budgets for three years are prepared, with projections revised annually considering the previous year budget performance and incorporating policy changes.
Medium-Term Fiscal Framework	The top-down specification of the aggregate resource envelope and the allocation of resources across spending agencies.
Medium-Term Plan	A five-year implementation plan of the longer-term national development plan.
Ministries, departments and agencies	MDAs are responsible for delivery of national government operations and include independent offices, the Judiciary, Parliament and constitutional commissions.
Outcome	The expected result of a programme on intended beneficiaries within available resources.
Outputs	A specified policy result (such as goods, products, services) contributing to achieving a programme outcome.
Performance indicators	A yardstick to measure the achievement of an outcome or of an output.
Programme	A grouping of related activities contributing to a key outcome, based on the main functions performed or services delivered by an MDA.
Programme-based budgeting	A means of linking the budget and other resources to public policy objectives. A PBB is structured according to programmes that are designed to achieve a specified policy objective through a budget appropriation.
Recurrent budget	National government expenditure on goods and services, excluding development expenditure.
Standard Chart of Accounts	A framework for classifying, recording and reporting information on financial plans, transactions and events in a systematic and consistent way, using a standard structure of codes.

Annex 1: Budget calendar

Activity	Responsibility	Timelines
Develop initial macroeconomic forecast	National Treasury/MWG	By mid July
Develop and issue Circular on MTEF Budget Process	National Treasury	By 31st July
Launch of Sector Working Groups	National Treasury	By 7th August
Review programme performance	National Treasury SWG	1st August to 5th September
Develop/update the budget baseline	National Treasury and MDAs	1st August to 5th September
Assess fiscal space and derive expenditure ceilings for the draft BROP; policy priorities and PBB results are considered for allocating the overall expenditure ceiling to individual sectors.	National Treasury	By 15th September
Compile the draft BROP	National Treasury and MWG	By 15th September
Circulate the draft BROP to stakeholders for input	National Treasury	By 15th September
Incorporate stakeholder inputs	National Treasury	By 21st September
Submit draft BROP to Cabinet for approval	National Treasury	By 30th September
Submit approved BROP to National Assembly	National Treasury	By 21st October
Publish and publicise BROP	National Treasury	By 21st October
Prioritise and align sector policies to set expenditure ceilings (drafting of sector budget proposals)	Sectors and the National Treasury within the conduct of SWGs	By 15th November
Public hearings on sector budget proposals	National Treasury	By 30th November
Submit Sector Report to National Treasury	SWGs	By 5th December

Activity	Responsibility	Timelines
Develop and issue Guidelines for the Preparation of Annual Budget Estimates for State Corporations	National Treasury	By 15th November
Submit State Corporations Revenue and Expenditure Estimates to National Treasury	State Corporations	By 31st January
Draft Budget Policy Statement (BPS), Division of Revenue Bill (DoRB) and County Allocation Revenue Bill (CARB)	National Treasury	By 15th January
Circulate BPS, DoRB andCARB to stakeholders	National Treasury	By 15th January
Incorporate comments from the stakeholders	National Treasury	By 22nd January
Submit draft BPS to Cabinet for approval	National Treasury	By 5th February
Submit the BPS, DoRB and CARB to Parliament for approval	National Treasury	By 15th February
Approval of BPS by Parliament	Parliament	By 28th February
Publish and publicize BPS	National Treasury	By 1st of March
Develop and issue Circular on the Finalisation of the Budget Estimates	National Treasury	By 5th March
Prepare and review of the Budget Estimates	MDAs and National Treasury	By 10th April
Submit the Budget Estimates and other budget documents to Cabinet	National Treasury	By 15th April
Submit the draft Budget Estimates, Finance Bill and other documents to National Assembly	National Treasury	By 30th April
Review of Budget Estimates by the National Assembly	National Assembly	1st–30th May
Presentation of Budget Statement (the Budget Speech) to National Assembly	National Treasury	By Mid June
Approval of the Budget Estimates	National Assembly	By 30th June

Activity	Responsibility	Timelines
Approval of Appropriation Bill	National Assembly	By 30th June
Approval of Finance Bill	National Assembly	By 30th June

Annex 2: Sector-specific action plan template

This template compares baseline results and expenditure ceilings for each vote per fiscal year for total expenditure, economic classification and programmes.

The template is populated with the results of the expenditure prioritisation to ensure alignment of sector policies with set expenditure ceilings (conducted mid-November). Moreover, it discloses which corrective measures the sector plans to close the gap between baseline results and expenditure ceilings—in case the baseline is higher than the respective ceiling—and which savings each corrective measure is expected to contribute in which fiscal year.

As each programme is assigned to a specific MDA, the template tracks how much each MDA is expected to contribute to the savings.

Table 2a. Recurrent expenditure by economic classification (Ksh. million)

Sector Name	Economic Classification	Approved Budget 1	Baseline/requirements 2			Expenditure Ceilings 3			GAP 4		
		2022/23	2023/24	2024/25	2025/26	2023/24	2024/25	2025/26	2023/24	2024/25	2025/26
	Sector Total										
Vote Code and Details	**Economic Classification**										
	Gross										
	AIA										
	NET										
	Compensation of Employees										
	Transfers & Subscriptions										
	Other Recurrent										

Table 2b. Development expenditure by economic classification (Ksh. million)

Sector Name	Economic Classification	Approved Budget [1]	Baseline/requirements [2]			Expenditure Ceilings [3]			GAP [4]		
		2022/23	2023/24	2024/25	2025/26	2023/24	2024/25	2025/26	2023/24	2024/25	2025/26
	Sector Total										
Vote Code and Details	**Economic Classification**										
	Gross										
	Government of Kenya										
	Loans										
	Grants										
	Local AIA										

Table 2c. Programmes and sub-programmes by economic classification (Ksh. million)

Sector Name	Program/Sub Programme/ Economic Classification	Approved Budget [1]	Baseline/ Requirements [2]			Expenditure Ceilings [3]			GAP [4]			Corrective Measure[5]	Savings[6]		
		2022/23	2023/24	2024/25	2025/26	2023/24	2024/25	2025/26	2023/24	2024/25	2025/26		2023/24	2024/25	2025/26
	Sector Total														
Vote Code and Details	**Programme 1**														
	Current														
	Capital														
	Total for programme 1														
	Sub programme 1														
	Current														
	Capital														
	Sub-total for sub-programme 1														
	Sub programme 2														
	Current														
	Capital														
	Sub-total for sub-programme 2														

Explanatory notes to Table 2a to 2c

Component	Name	Description
1	Approved Budget	The appropriated budget plus any supplementary budgets that have been approved by the time the template is completed
2	Budget baseline/ requirements	The budget baseline quantifies the projected cost of existing policies on a 'no-policy change' basis. This includes the costs of the current level of activity, which is the costs of ongoing programmes adjusted for inflation services, demographics, legally mandated requirements, one-time expenditures, and the impact on a full year basis of decisions made in the current year.
3	Expenditure Ceilings	Expenditure ceilings communicated in the most recent published MTEF. These reflect the maximum amount that an institution is allowed to commit or spend.
4	Gap	The difference between baseline and expenditure ceiling
5	Corrective measure	Measures which the (sub) program will undertake to reconcile the gap indicated in (3). This should be a narrative description, which is quantified in columns of component 6.
6	Savings	The total amount of saving resulting from the corrective measures in (5)

Annex 3: Programme-based budgeting templates for planning and budgeting

A. Programme Template

<table>
<tr><td colspan="8">(1) State Department:</td></tr>
<tr><td colspan="8">(2) Budget Programme:</td></tr>
<tr><td colspan="8">(3) Outcome:</td></tr>
<tr><td colspan="8">(4) Implementation challenges and their causes in trying to achieve the outcome:</td></tr>
<tr><td rowspan="2">(5) Outcome indicator(s) Maximum 3</td><td rowspan="2">(6) Baseline (Year)</td><td colspan="3">(7) Target for the indicator</td><td colspan="3">(8) Total budget amount for programme in Mn. Ksh.</td></tr>
<tr><td>FY1</td><td>FY2</td><td>FY3</td><td>FY1</td><td>FY2</td><td>FY3</td></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td rowspan="3"></td><td rowspan="3"></td><td rowspan="3"></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
</table>

Notes to the template

This template should be populated by the responsible State Department and validated by National Treasury prior to inclusion in the budget document.

Component[33]	Explanation
1	The first element of the template identifies the State Department responsible for the budget programme in question. This aims at highlighting the organisational responsibility for successfully implementing the budget programme and supports accountability for results.
2	The second element denotes the name of the budget programme as included in the SCOA.
3	The third element defines the outcome of the budget programme which needs to be S.M.A.R.T and should be linked to strategic documents of the national government. The outcome is supposed to address the main policy result of the budget programme on a strategic policy level and in a wording that is simple and understandable. To reduce complexity of the PBB approach, only one outcome for a budget programme is accepted.

33 *Refers to the corresponding number in brackets within the template.*

Component[33]	Explanation
4	The fourth element very briefly (maximum of three lines) sums up the main challenges (and their causes) to implement the outcome. This should support readers of the document to understand the main difficulties to achieve policy progress and the magnitude of the challenges and their causes. To this end, the text needs to include the most important reference numbers for challenges and causes and the wording should be well understandable for non-experts.
5	An outcome indicator provides a yardstick to measure achievement of the outcome. To reduce complexity of the PBB approach a maximum of three indicators for a budget programme is accepted. The wording of the indicator should be compliant with the C.R.E.A.M approach and well understandable for non-experts.
6	The baseline of the target refers to the most recent year for which reliable data is available and allows readers to understand the magnitude of intended progress in each of the upcoming three FYs.
7	A target specifies a particular value or milestone that an indicator should reach by a specific date in the future. Thus, a target needs to be fully consistent with the respective indicator. The formulation of targets should be formulated according to C.R.E.A.M in an ambitious but also time realistic manner. This includes that the target should be implementable within the amounts allocated to the budget programme in question. To reduce complexity of the PBB approach only one target is accepted per indicator. It is specified for each of the three financial years covered by the medium-term budget planning timeline separately.
8	The budget amount reflects the allocation to the budget programme in each of the three financial years covered by the budget planning timeline separately. As it would be too complex to assign the budget amounts to each indicator, the amounts reflect the total annual budget allocation to the programme in question and are not disaggregated further.

B. Sub-programme template

<table>
<tr><th colspan="10">(1) State Department:</th></tr>
<tr><th colspan="10">(2) Budget Programme:</th></tr>
<tr><th colspan="10">(3) Outcome:</th></tr>
<tr><th colspan="10">(4) Sub-programme:</th></tr>
<tr><th colspan="10">(5) Leading delivery unit of the sub-programme:</th></tr>
<tr><th rowspan="2">(6) Output(s) of the sub-programme Maximum 2</th><th rowspan="2">(7) Output indicator(s) Maximum 4</th><th rowspan="2">(8) Baseline (Year)</th><th colspan="3">(9) Target for the indicator</th><th colspan="3">(10) Total Budget amount for sub programme in Mn. Ksh.</th></tr>
<tr><th>FY1</th><th>FY2</th><th>FY3</th><th>FY1</th><th>FY2</th><th>FY3</th></tr>
<tr><td rowspan="2"></td><td></td><td></td><td></td><td></td><td></td><td rowspan="4"></td><td rowspan="4"></td><td rowspan="4"></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td rowspan="2"></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
</table>

Notes to the template

This template should be populated by the responsible leading delivery unit of the sub-programme and validated by the responsible State Department and the National Treasury prior to publication.

Component[34]	Explanation
1-3	The first three elements – State Department, Budget Programme and Outcome are explained in Template A.
4	The fourth element denotes the name of the budget sub-programme as included in the SCOA.
5	The lead delivery unit of the sub-programme identifies the unit which is responsible for the sub-programme implementation and thereby, coordinating contributing units if any. This aims at highlighting the organisational responsibility for successfully implementing the budget sub-programme and supports accountability for results.
6	Outputs of the sub-programme contribute to achieving the outcome on the budget programme level and need to be S.M.A.R.T To reduce complexity of the PBB approach a maximum of two outputs for a budget sub-programme is accepted. The wording of the outputs should be easily understandable to non-experts.

34 *Refers to the corresponding number in brackets within the template.*

Component[34]	Explanation
7	An output indicator provides a yardstick to measure achievement of the output. To reduce complexity of the PBB approach a maximum of two indicators per output is accepted. The wording of the indicator should be compliant with the C.R.E.A.M approach and well understandable for non-experts.
8-9	The explanation for baseline and target is provided in Template A but applies to output baseline and targets.
10	The total budget amount reflects the allocation to the budget sub-programme in each of the three financial years covered by the budget planning timeline separately. As it would be too complex to assign the budget amounts to each indicator, the amounts reflect the total annual budget allocation to the sub-programme in question and are not disaggregated further.

Both standardised templates are populated by the responsible organizational unit but require approval of the National Treasury. As the templates combine financial and non-financial information, the State Departments responsible for guiding policy and budget planning respectively, need to confirm adequacy and accuracy of the provided information.

Annex 4: S.M.A.R.T and C.R.E.A.M methodology

Features of S.M.A.R.T	Explanation
Specific	Outcomes and outputs should be formulated in a way that, answers the questions "What is to be done?" "How will you know it is done?" and describes the result (end product) of the work to be done. The description is written in such a way that anyone reading the outcome or output will most likely interpret it the same way.
Measurable	Measurable answers the question, "How will you know that the implementation of the outcome or the output meets expectations?" Measurement is conducted via indicators and targets.
Achievable	Achievable answers the questions, "Can the institution responsible for an outcome or output can Do it?" "Does the institution have the experience, knowledge or capability of fulfilling the expectation?" It also answers the question "Can the outcome or output be successfully implemented given the timeframe and available resources?"
Relevant	Relevant answers the questions,"Should it be done?", "Why?" and "What will be the impact?" This particularly relates to the findings of a diagnosis of policy challenges. Is the outcome or output meant to tackle an important challenge or is it just dealing with a random topic which does not have much policy impact?
Time-bound	Answers the question, "When will it be done?" Outcomes and outputs should be achieved by an end point (deliverable at the end of the envisaged process which might easily take a couple of years). Within that time horizon annual check points should be envisaged (yearly targets for indicators addressing the intended implementation progress).

Source: Wayne State University; https://hr.wayne.edu/leads/phase1/smart-objectives

Features of C.R.E.A.M	Explanation	Example: Literacy among girls living in rural areas aged 10 shall reach XX percent by the year 20YY.
Clear	Precise and unambiguous. All readers should understand the same meaning of the indicators and targets to avoid misinterpretation.	The target is easy to understand and can barely be interpreted differently by different people.
Relevant	Dealing with important aspects of the outcome or output which the indicator and target are assigned to.	The target focuses on an important aspect of the output which in this case is: Improve literacy in rural areas.
Economic	Achievable at a reasonable cost and within the allocated amounts of the respective budget (sub) programme.	This requires a check if sufficient funds are available to achieve this based on efficient implementation.
Adequate	Provide a sufficient basis to assess performance of the outcome or output.	Allows to assess the performance of the output as it references to a key indicator for improving literacy in rural areas.
Monitorable	Amenable to independent validation both in-year and end-year.	The target is formulated sufficiently specific to allow for an independent validation.

Source: World Bank

Annex 5: Programme monitoring and evaluation template

State Department:						
Budget programme:						
Outcome:						
(1) Total Programme Expenditure (Mn. Kshs)						
	Reporting FY			**MTEF**		
Expenditure Category	**Budget**	**Actual**	**Variance**	**Current FY**	**Outer FY1**	**Outer FY2**
Recurrent						
Development						
Total						
Programme Performance						
	(3) Reporting FY			**(4) MTEF**		
(2) Outcome	**Budget**	**Actual**	**Variance**	**Current FY**	**Outer FY1**	**Outer FY2**
Indicator 1:						
Indicator 2:						
Indicator 3:						
Indicator 1:						
(5a) Analysis of variance						
Name of cause 1:						
Brief explanation of cause 1:						
Quantified estimate impact on variance:						
Name of cause 2:						
Brief explanation of cause 2:						
Quantified estimate impact on variance:						
(5b) Planned corrective measures within expenditure ceilings of MTEF						
Name of cause 1:						
Name of corrective measure 1.1:						
Brief explanation of corrective measure 1.1:						
Quantified estimation of contribution to close variance:						
Name of corrective measure 1.2:						
Brief explanation of corrective measure 1.2:						
Quantified estimation of contribution to close variance:						
Indicator 1:						

Notes for the monitoring and evaluation template for outcomes of budget programmes

Component[35]	Explanation
1	The total programme expenditure columns outline whether spending for the programme in the reporting financial year was in line with the respective expenditure ceiling for the programme and show the budget allocations for subsequent financial years to allow addressees to understand the planned expenditure development for the programme.
2	This states the name of the outcome indicator.
3	Comparing target and actual of the reporting financial year and calculating the variance allows to monitor, whether or to which extent the target has been achieved.
4	The target columns for the current and the two outer financial years are included in the template to make addressees understand which progress is required from the actual of the reporting to subsequent financial years. This is particularly important in case of performance shortfalls experienced in the reporting financial year and allows to gauge the magnitude of the required catch-up.
5a	The analysis of variance outlines the causes for performance gaps and estimates the quantified impact of each cause on the performance variance for a given outcome indicator. After having dealt with the first indicator for components 5a and 5b the other indicators need to be dealt with in the same systematic way and respective lines have to be added to the template. The quantification can be done either in percentages (total variance being 100 percent) or in nominal amounts. The template includes lines for the two most important causes per indicator which usually should be sufficient to explain the bulk of the variance. It is not recommended to try to explain 100 percent of the variance as this might result in a very cumbersome detailed analysis which may overburden the reporting unit. In case more than two causes are to be addressed to explain the performance gap in question, additional lines need to be included in the template.

35 *Refers to the corresponding number in brackets within the template.*

Component[35]	Explanation
5b	For each cause of variance outlined in the template, corrective measures should be identified to avoid repeating the performance shortfall in subsequent financial years. The corrective measures need to be implemented within the available budget allocations for the respective Department or lead delivery unit. The template includes lines for the two most important corrective measures per cause which usually should be sufficient to address the bulk of the variance generated by the respective cause. It is not recommended to try to address 100 percent of this variance as this might result in a very cumbersome detailed analysis which may overburden the reporting unit. In case more than two corrective measures are to be addressed to tackle the performance gap generated by the respective cause, additional lines need to be added to the template.

Source: National Treasury

Annex 6: Sub-programme monitoring and evaluation template

State Department:							
Budget programme:							
Outcome:							
Sub-programme:							
Leading delivery unit of the sub-programme:							
Total Sub-programme Expendiyure (Mn. Ksh)							
Expenditure Category	**(1) Previous Year Actual**	**(2) Approved Budget**	**(3) Quarter Expenditure**	**(4) End Year Estimate**	**(5) Variance to Budget**	**Cause of Variance**	
Recurrent							
Development							
Total							
Cumulative quartery Sub-programme Performance							
Output/Indicator	**(6) Previous Year Actual**	**(7) Current Year Target**	**(8) Required by Quarter**	**(9) Actual by Quarter**	**(10) Quarter Variance**	**(11) End Year Estimation**	**(12) End Year Variance**
Output 1:							
Indicator 1:							
Causes of variance and planned corrective measures							
Indicator 2:							
Causes of variance and planned corrective measures							
Output 2:							
Indicator 1:							
Causes of variance and planned corrective measures							
Indicator 2:							
Causes of variance and planned corrective measures							

Notes on monitoring and evaluation template for sub-programme outputs

Component[36]	Explanation
Total Sub-programme Expenditure	
1	**Previous year actual:** Actual expenditure incurred for the previous financial year.
2	**Approved budget:** The appropriated budget plus any supplementary budgets that have been approved by the time the template is completed.
3	**Quarter expenditure:** Cumulative expenditure for elapsed quarters in the financial year.
4	**End year estimate:** Estimated expenditure amount by the end of the financial year; applies for reports for the first three quarters of a financial year. To be left blank for the report for the fourth quarter.
5	**Variance to budget:** For the first three quarters: Variance of the estimated expenditure amount by end-year to the appropriated amount in the budget. For the fourth quarter: Variance of cumulative expenditure at the end of the fourth quarter the budget.
Cumulative quarterly sub-programme performance	
6	**Previous year actual:** The target achieved in the previous financial year.
7	**Current year target:** The planned target for the year as outlined in the budget document
8	**Required by quarter:** This benchmark indicates which status (based on cumulative amounts for elapsed quarters) is considered to be compliant with the in-year service delivery pattern required to delive the set target by end-year.
9	**Actual by quarter:** Cumulative performance for elapsed quarters.
10	**Quarter variance:** Difference between (8) requirement by quarter and (9) actual by quarter.

36 *Refers to the corresponding number in brackets within the template.*

Component[36]	Explanation
11	**End-year estimation:** This indicates the estimated result by the end of the year (based on cumulative performance for elapsed quarter plus the estimated performance for the remaining quarter (s) in the year. This applies for the first three quarters of the financial year and should be left blank for the fourth quarter.
12	**End-year variance:** Difference between (9) actual by quarter and (7) current year target. This column only applies in quarter 4.
In addition, the narrative fields after the indicator should be used to very briefly specify causes for performance shortfalls (if any) and corrective measures to tackle them. If more space is needed for that an additional document can be added to the template to provide more details.	

Source: National Treasury

NOTES

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NATIONAL GOVERNMENT BUDGET MANUAL 2023

THE NATIONAL TREASURY
AND ECONOMIC PLANNING

NATIONAL GOVERNMENT BUDGET MANUAL

2023