

## Module 3 Session 2: A New Formula and County Division of Revenue

### KEY TAKEAWAYS

- ❖ **EQUITABLE DISTRIBUTION IS IMPORTANT NOT ONLY ACROSS COUNTIES BUT ALSO WITHIN COUNTIES(AT THE WARD/SUB-COUNTY LEVEL)**
- ❖ **DISTRIBUTION ACROSS THE COUNTY SHOULD ENSURE THAT THOSE VILLAGES, WARDS AND SUB-COUNTIES THAT HAVE HIGHER NEEDS ARE ALLOCATED MORE FUNDS**
- ❖ **SOME COUNTIES HAVE TAKEN A STEP TOWARD FORMALIZING DISTRIBUTION OF RESOURCES USING LEGALLY BINDING FORMULA THAT INCORPORATE PRINCIPLES OF EQUITY TO VARYING DEGREES**

### TASK 3.2 ■ IMPROVING HOW WE DISTRIBUTE REVENUES AT THE NATIONAL AND COUNTY LEVEL

**1 HOUR 30 MINUTES**

### TASK OBJECTIVES

- ❖ **REFLECTING ON THE CURRENT CRA FORMULA AND HOW BEST TO SHARE RESOURCES THROUGH A FORMULA**
  - ❖ **REFLECTING ON HOW BEST TO SHARE REVENUE WITHIN COUNTIES**

### RESOURCES NEEDED

- ✓ Spreadsheet on County X, Y and Z
- ✓ Elgeyo Marakwet Equitable Development Act, 2015 (Excerpts on formula)
- ✓ Baringo, Meru, Kisumu and Nakuru Ward Development Fund Acts/Bills

### HOW TO RUN THE TASK

This session has two parts:

#### **Part one: Towards a New Formula (1hour)**

1. For this part, hand out the spreadsheet containing data on county X, Y and Z.
2. Divide participants into groups of three and ask them to look at some data on 3 hypothetical counties, County X, County Y and County Z (see information on County X Y and Z in the Annex of Key Documents).
3. Make sure that participants understand that they have data on three counties, and that the data relates to concepts from Module 3 Session 1. However, do not tell them what each type of data is meant to relate to at the level of principles. That is for them to discuss.
4. Then tell participants they have Ksh. 10 billion to split between the 3, and ask them how they would do it and why. Participants do not need to come up with a formula per se, but they do need

to be precise about how they would split the 10 billion (e.g., County X should receive 2 billion, County Y, 5 billion, etc.).

5. Return to plenary to have people report back and justify their decisions, emphasizing principles and their interpretations of the data.
6. Then discuss what this means for revising the CRA formula in future and for other revenue sharing initiatives in Kenya.

**Note:**

- (a) **This exercise can and has been modified to look at wards within a county, and requires only a few minor modifications. We have also included a version of the exercise for wards in the Annex of Key Documents.**
- (b) **One thing that needs to be repeated severally to participants is that they are not simply to apply the CRA formula, but to come up with their own approach to a fair distribution. There is usually someone in each group that tries to simply mechanically apply the CRA approach.**

**Part two : Ward/ sub-county distribution (30 minutes)**

1. Have a short discussion on distribution of resources within the county. Begin by asking the discussion question: ‘Should the same issues from Part One be taken into account within the county in distributing revenues to villages, ward and sub-counties?’
2. Discuss the EMC distribution formula together with the WDF formulas for Baringo and Meru (all in the Participant Manual) and how other counties have attempted to distribute resources across wards.
3. Ask participants in groups of three to make recommendations that they may present to their county government on what the county should take into consideration in distributing funds across the county. Let them look at the three formulas and think of how they would change them to suit their counties and the rationale behind the suggested changes (PM, p. 116).

**Note: if the participants are from different counties let them pick one county that is fairly familiar to them (such as Baringo using data from Module One)**

4. In plenary, let each group present their recommendations.
5. Ensure you advise them to apply the principles of fairness from this module.

## **BACKGROUND INFORMATION**

### **Part two: Ward and sub-county distribution of resources**

The Constitution and national legislation do not explicitly indicate the criteria counties should use in spatial distribution of revenues within counties (to wards, for example). The underlying constitutional principle however is that public finance expenditure should promote **equitable development** and **marginalized groups should have specialised provision**. These two specifications apply to both the national and county governments.

Most counties have begun discussions about distribution of development funds to county sub-units (ward and sub-counties). Some counties have resorted to distributing revenues equally to each ward (for example Nakuru gives 25M to each ward). Other counties have devised formulas for distribution of revenue across the county by enacting county legislation to distribute part of their revenues to wards using formulas. One exceptional county, Elgeyo Marakwet, has devised a more sophisticated formula for distributing its development funds. Below is a table showing the formula adopted by Elgeyo Marakwet County.

**Table 1: Elgeyo Marakwet County Approved Revenue Sharing Formula**

County	Policy Instrument	Relevant Proportion of County Revenue	Formula
Elgeyo Marakwet	Equitable Development Act, 2015	All development expenditure (which should be at least 40 % of the county's total annual expenditure )	60% distributed equally to each ward 40% distributed equitably to each ward using the following parameters <ul style="list-style-type: none"> <li>• 38% in accordance with the ward's population</li> <li>• 22% according to poverty index in the wards</li> <li>• 8% in accordance with the ward's land area</li> <li>• 23% in accordance with county flagship projects (not distributed to wards)</li> <li>• 5% be allocated for emergencies</li> <li>• 2% in accordance with the fiscal responsibility</li> <li>• 2% be allocated to arid and semi-arid Lands (ASAL) (See next section)</li> </ul>

A large number of counties have enacted or are in the process of enacting Ward Development Fund legislation, which also provide for sharing of a portion of their revenues across the county. Meru and Baringo are good example of counties with enacted WDF acts, and Kisumu and Nakuru have bills tabled in parliament. The formulas adopted in these acts are more or less the same, with some contradictions. Below is a table indicating the distribution of these ward development funds in these four counties.

**Table 2: Meru, Baringo, Kisumu and Nakuru Revenue Sharing Formula (Approved and Pending)**

County	Policy Instrument	County Revenue Shared by Formula/Criteria	Mode of Distribution to wards	Distribution within wards (if specified)
Meru	Ward Development Fund Act, 2015	At least 22.5% of the equitable share transfer and any other monies donated/lent or	85 % of ordinary revenue distributed equally to all wards 15% of ordinary revenue to be distributed in	At the discretion of WDF Committees (which may allocate funds to a minimum of 3 projects and maximum of 10 projects in every ward). In addition, there are additional guidelines on the use of the funds:

		received by the fund	accordance with <b>population size, poverty index, and infrastructural differences.</b>	Exactly 15% for bursary fund* Exactly 5% (of the total allocation for each project))for administration expenses* A maximum of 3% for monitoring and evaluation and capacity building.*
Baringo	Ward Development Fund Act, 2014	At least 10% of the approved development budget and any other monies donated/lent or received by the fund	There are two different formulas in the law and it is not clear when each should be applied. 1. As per the CRA formula 2. 85 % of ordinary revenue distributed equally to all wards and 15% of ordinary revenue to be distributed in accordance with <b>the ward share of the total county population.</b>	At the discretion of WDF Committee (which may allocate funds to a minimum of 5 projects and maximum of 25 projects in every ward). In addition, there are guidelines on how the funds can be used:  Exactly 3% (of the total allocation for each project) for administration* Exactly 5% for an emergency reserve* Exactly 15% for education bursary and school fees etc.** A maximum of 3% for ward expenses, for example: rent, salaries ** Exactly 2% for sporting activities** Exactly 2% environmental activities** A maximum of 3% in purchasing, running and maintenance of vehicles and equipment*
Kisumu <sup>1</sup> / Nakuru	Ward Development Bills (yet to be passed )	At least 5% of ordinary revenue and donor funds; any other monies donated/lent or	85 % of ordinary revenue distributed equally to all wards 15% of ordinary revenue to be distributed in	At the discretion of WDF Committees (minimum of 5 projects and max of 25 projects in every ward)

<sup>1</sup> In 2015/16 the WDF was distributed equally to all 35 wards in Kisumu at 8million per ward

		received by the fund	accordance with <b>ward share of total county population(s.26)</b> Note: subject to WDF Committee approval. wards may pool resources for joint projects	Exactly 5% (of the total allocation for each project) for administration* Exactly 5% for emergency reserve* Exactly 15% for education bursary and school fees etc.** Exactly 3% ward expenses, for example rent salaries** Exactly 2% sporting activities** Exactly 2% environmental activities A maximum 3% in purchasing, running and maintenance of vehicles and equipment.*
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\*this is mandatory (the words 'shall' and 'must' are used)

\*\*this is optional (the word 'may' is used) but insinuates a maximum limit.

### TASK 3.2

#### (QUESTIONS AND ANSWERS)

##### Part One: Towards A New Formula

**Question: How would you split 10 billion between County X, County Y and County Z?**

**Answer: There is no one right answer to this question. However below are some notes to guide you in facilitating the discussion:**

By design, this is not meant to be simple. But we are looking for participants to bring up a number of issues using the different sets of data.

##### Health data

- Looking at the health data, we might say that County Y has the highest need for health money because it has the largest number of people visiting facilities. People may end up being confused when they see that more people use facilities in County Y, but this is only 27% of the population, less than other counties. How should we think about that? Basically, assuming a similar unit cost, the important thing is not the visits/population, but the visits in County Y as a share of all visits for the three counties. County Y has 43% of all visits for the 3 counties combined. County Y therefore has highest need by this measure.
- On the other hand, when we look at disease incidence, the story is more complex. While County Y has the most HIV cases, it has fewer cases of TB and malaria than County Z. This could mean that County Z has a sicker population on average, but they don't always visit the health facilities. The data suggest that County Z has fewer facilities, so this might be one reason why this happens. On the other hand, County Z has fewer people per facility than County X or Y, meaning it is relatively better off in terms

of facility access. So maybe people just don't like to visit facilities in County Z. Giving them more money might not help. But we also lack other data that might explain this. For example, County Z could have more facilities per capita, but fewer doctors or nurses. We might need more information. This is another key point to raise.

- Ultimately taking the health data together, there is a clear argument for giving more to Y to manage its higher absolute number of people visiting facilities, but participants may also feel it is necessary to look at the particular scourge of malaria in Z and do something about it. This should allow for an interesting discussion of need and help to clarify the issue of percentage versus absolute needs. If we assume that there is a particular unit cost for every health visit, then a county with a higher absolute number of visits needs more to cover the cost of those visits than a county that is "sicker" but has fewer people overall (and therefore fewer absolute numbers attending facilities). It may be that a special grant is also needed to deal with a particular crisis, such as the malaria crisis in Z, but this has to be balanced against services for all.

### **Agriculture Data**

- Agriculture/crop-farming data is a measure of need though many people see it as a measure of capacity to produce and generate revenues. Some see it as a measure of need, but in the reverse sense from what was intended, meaning that for them areas with more crop-farmers should get less because they need less support (are more productive already). These approaches are okay but tend to assume that those not engaged in crop-farming are destitute, rather than engaged in other activities. The agriculture data can be interpreted in various ways including:
  - The need for extension services. Extension services are a key county function in the agriculture sector. If counties are deciding how to distribute funds for extension, they might look at need based on the number of farmers that are actually going to use these services in different counties. This would argue for giving more to County Y than the other counties. One could, however, also ask whether X needs some additional support to help its heavily rural population become more effectively engaged in farming, as they seem not to have a substantial farming population.
  - An alternative interpretation is related to economic productivity. Some would argue that what the data show is that there is more productive activity in County Y than in County X, for example. This is because the share of the rural population that is actively engaged in farming is much higher in Y. It is not clear what is happening in County X. There could be high unemployment or high dependence on remittances or other factors. On the other hand, County Z has a much smaller rural population. This might indicate that the economy is more tilted toward urban businesses than rural farming. It is not possible to tell this from the farming data, but one clue is in the revenue data, which shows that County Z has very low per capita revenues from land rates and business permits. This might indicate an urban but depressed economy in County Z. Taken together, one could then interpret this data as related to need (which economies need more uplifting), effort (which counties are engaging in more productive economic activity) or capacity (which counties are generating or capable of generating more resources per capita).

### **Revenue data**

- When we look at revenues, County X has the highest revenues per capita. But when we look at effort, which we measure as the change in per capita collections over time, we see that County X has performed poorly, while County Z has excelled. County Y has also performed relatively poorly.

### **Housing data**

- This data is intended to capture need. Since housing is a county function, improving the quality of housing qualifies as a need which may be used to allocate resources. The data follow a familiar pattern with County Y having a higher number of absolute households with earth floors, though County Z has the highest percentage of the population living in this manner. People living in such housing conditions might also be a proxy for other types of need.

### Education data

- The data on population under one and ECD is related to need for preprimary education. It captures first the population that is likely to need ECD services in the next few years. County Y has again a large share: 57% of all under 1 year olds live in the county. The facility data again suggests that County Y is somewhat worse off, with the fewest facilities per person. One issue that might be raised is about teachers. Some counties might have good physical access to facilities but few teachers. The data does not clarify this issue. The same question could be asked of health facilities.

### Population data

- One thing that the data show, and which is quite realistic, is that on average, County Y has more needs than the other counties for population-related services because it has a much bigger population overall. When we look at infrastructure, though, it is County Z that has the greatest “need.” Need here is measured as the land area per km of paved road, and population per km of paved road. Basically, if a county has a larger land area or higher population per paved road, it means that for a given area or population, there is less access to paved roads. So County Z is worst off, while County X is best off.

### Part two : Ward/ sub-county distribution

**Question: How would you alter the Elgeyo Marakwet, Baringo and Meru formulas for use in your county?**

**(Refer to ‘Background Information’ above for the formulas used in Baringo, Meru and Elgeyo Marakwet.)**

**Answer: There are many ways to improve on these formulas, here are a few suggestions:**

The changes may be of three types:

- i. Changes in weights of the parameters in the formula
- ii. New parameters to be included in the formula
- iii. Parameters to be removed from the formula

### Improving the Elgeyo Marakwet formula

1. No need for an extra emergency fund because the counties already have an emergency fund as prescribed under the PFM Act, 2012; why should it be incorporated here as well? In any case an emergency fund is arguably a pooled risk fund and should be at a higher level than the ward.
2. There is need for the county to appreciate infrastructural gaps/deficits over and above the land area parameter.

3. Fiscal responsibility not a good place to start because wards do not have fiscal autonomy from counties; good to ask if there is any sense in which wards can exercise fiscal effort? One possibility is for communities to put their own resources into projects in exchange for a matching grant from the county to that ward.

### **Improving Baringo formula**

1. Eliminate the contradiction in the law about the two ways of distributing the funds. The CRA formula also changes over time. It is not clear whether the formula will correspondingly keep changing. In any case, the CRA formulas (2012 and 2016) do not necessarily meet the objectives of the county's fund, which is for development and fighting against poverty at the ward level. Additionally, wards are not financially autonomous units and as such we can't ascribe fiscal responsibilities to them.
2. The second formula applies to 10 % of the budget. How will the rest of the revenue be shared?
3. A huge percentage (85%) is distributed equally not addressing the disparities in the wards.
4. Need more parameters over and above poverty to address the issue of historical injustices in sharing of resources and access to capital assets.
5. Distribution should be on a need basis and not in relation to the population as a whole. For example, how many people in a particular ward do not have access to water or any other services as a share of the numbers in the county as a whole?

### **Improving the Meru formula**

1. The formula applies to 22.5% of the equitable share and donor funds. This is a significant amount and there is need for some coordination with the rest of the budget. For example, if the budget has already allocated a considerable amount of funds to certain wards, how much more can they get from the WDF?
2. A huge percentage (85%) is distributed equally, failing to address the disparities in the wards.
3. Distribution should be on a need basis and not in relation to the population as a whole. For example, how many people in a particular ward do not have access to water or any other services as compared to the numbers in the county as a whole?
4. We cannot tell how the other parameters are measured, so open to discussion how to do so in the best way.