

The GLOCEPS

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Research Focus: Development and Innovation

Kenya's public debt crisis: a call for reforms

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DEBT

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Executive Summary

Kenya's public debt situation has evolved into a significant challenge, marked by an accelerating debt burden and questions about the legitimacy and transparency of the country's public debt register. Although public debt can catalyze economic growth, when maintained at manageable levels, Kenya's excessive borrowing has led to economic uncertainty and distress. Equally, private businesses are increasingly crowded out, while the citizenry is subjected to annual tax increases. Dissecting Kenya's debt crisis illustrates that external debt accounts for over half of the debt portfolio. This debt situation is driven by persistent budget deficits, unproductive expenditures, public sector corruption

and wastages, and overpriced and politically driven construction projects that yield delayed returns. The implications of the ensuing debt servicing burden are profound with over 70% of government revenue dedicated to debt servicing. The country's debt situation has equally raised concerns that the country's current generation is mortgaging the economic viability of future generations. The paper recognizes that despite robust legal frameworks designed to ensure accountability and sustainability in public debt management, gaps in implementation, lack of political goodwill, prevalent political interference, refusal to comply with court orders on the release of public debt contracts, and lack of



transparency hinder effective oversight. Equally, establishing a presidential taskforce in 2024 to audit public debt has sparked controversy, as it complicates the governance landscape of public debt. To address these challenges, the country requires parliament to take its oversight responsibilities seriously. This includes enacting the required legislation for parliament to approve public debt. The office of the Auditor-General should be empowered to issue subpoenas regarding its often ignored request for complete documentation needed for the audit of public debt. Equally, linking future borrowing to specific projects is imperative. Collectively, these policy actions will address concerns of odious debt and restore fiscal responsibility and public trust.

Key issues

This section highlights significant issues, including Kenya's public debt management framework, gaps in implementation, political interference, and ingrained lack of transparency. The section offers critiques around the redundancy and constitutional concerns of the Presidential Taskforce on the audit of public debt and explores the complexities and implications of the potential classification of Kenya's debt as odious.



Public Debt Management Legal Framework

Kenya has a comprehensive constitutional and legal framework governing the administration of public debt, with requisite functions assigned to

the National Assembly, Treasury, and the Office of the Auditor General (OAG). The legal architecture includes documentation like the Constitution of 2010, the Public Finance Management (Amendment) Act (PFMA) of 2023, and the National Tax Policy. Collectively, the framework is designed to ensure transparency, accountability, and sustainability in public debt management. However, the effectiveness of its interpretation and implementation remains skewed and inconsistent.

The Constitution and the PFMA provide the foundational legal structure for managing public debt, including borrowing. In this regard, Parliament is mandated to play a pivotal role as outlined in Article 211 of the Constitution. Parliament is expected to legislate on borrowing, including setting terms and imposition of reporting requirements. This constitutional provision underscores the central role of Parliament in debt management, including the provision of legislative oversight in reinforcing debt transparency and accountability. Furtherance of this role is Section 32 of the PFMA, which places a legal requirement on the Treasury to report to Parliament annually the total number of loans guaranteed while providing details of parties involved, interest rates, and repayment terms.

Equally important, is the OAG which is tasked with the annual auditing of public debt. The Constitution under Article 222 (4) mandates the Auditor-General to complete the annual audit within six months after the end of each financial year, reinforcing accountability. These forensic audits are crucial in understanding the full extent of borrowing, outstanding amounts, and annual repayment schedules. To undertake this role, the Office of Public Debt Management, under the leadership of a Director-General at the Treasury, is mandated to furnish the OAG with detailed public debt information for forensic audit.



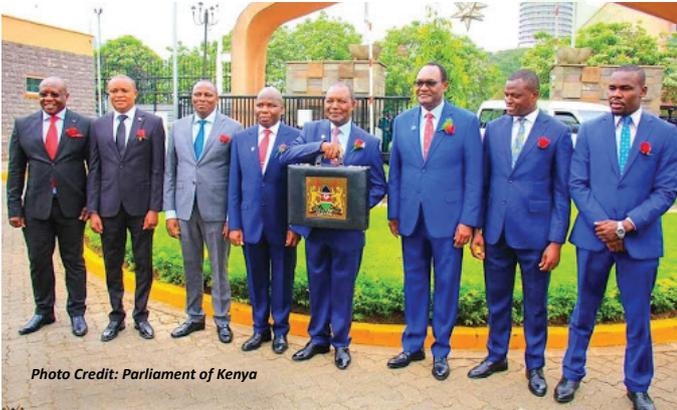


Photo Credit: Parliament of Kenya

Additionally, the Cabinet Secretary of the National Treasury is mandated to present detailed information of any loan or guarantee within seven days upon a resolution by either House of Parliament. This requirement is meant to ensure that Parliament remains informed and can exercise its oversight functions effectively.

Section 50 (1) of the PFMA emphasizes that the overall public debt must be sustainable and within the national debt limits set by Parliament under Section 15 (2) (d) of the PFMA. However, this principle has been consistently upgraded to a Ksh 10 trillion debt ceiling before transitioning to the current 55% percentage of Kenya's Gross Domestic Product (GDP). As of 2023, Kenya's debt level stood at 70.10% of GDP.

Despite the robust legal framework, there exist notable gaps in its implementation. Parliament remains a key impediment to the effective management of the public debt burden. The National Assembly is centrally complicit in allowing the Treasury to flaunt set guidelines as evidenced by the excessive debt-to-GDP ratio. This has resulted in the Executive arm of government exceeding the public debt ceiling. Moreover, public participation in debt management, as legally required, is often neglected.

Moreover, the legal framework fails to allocate responsibility on which arm of government is

responsible for ratifying public debt. Treasury therefore exploits this loophole to unilaterally procure and ratify loan contracts. It is equally evidenced that the Cabinet Secretary often fails to comply with parliamentary requests for public debt information and clarifications. In instances where they are provided, they are often incomplete. The effective administration and oversight by Parliament is compromised as most parliamentarians have capacity challenges to interpret and understand information that they are presented with. They equally fall captive to their political allegiances, thus hindering discussion and weakening their legislative oversight role on public debt issues.

It is imperative to appreciate that while Kenya's legal framework is fairly well-structured and intentioned, implementation is weak. This necessitates the need for significant improvement of the legislative gaps and improved capacity of the various stakeholders in the public debt administration. Equally important, is the recommendation of penalties, including personal liabilities, in the management of public debt.



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Presidential Taskforce on the Audit of Public Debt

On June 5th, 2024, a Presidential Taskforce was appointed to audit Kenya's public debt and deliver a report within three months. However, this move has since sparked significant debate regarding the legality of the establishment of the task force and a lack of clarity in its terms of references. Citizens and



stakeholders in the public administration sector argue that the taskforce's mandate usurps those of constitutional bodies, particularly Parliament and the Office of the Auditor General (OAG). Equally, concerns have been raised about the taskforce not representing value for money as it duplicates the efforts of the requisite constitutionally mandated entities.

This fallout has led key stakeholders like the Law Society of Kenya to decline the invitation to join the taskforce. Emphasize has been placed that this is the role of the OAG, which can easily be undertaken when the Office of Public Management in the Treasury provides requisite debt documents for a forensic audit to be undertaken.

Moreover, the judicial pronouncement by the High Court waters down the legality of the Presidential taskforces. The court affirmed the centrality of the Auditor General in public audit matters. In a case involving the creation of a similar type taskforce by the county government of Trans Nzoia to audit county government debts, the court nullified the taskforce. The court asserted that the County Governor should request the OAG to conduct the forensic audit, as this is constitutionally under their purview.

A review of the public debt ecosystem posits that the ability of the Presidential taskforce to unearth and resolve the public debt conundrum is equally



Photo Credit: President William Ruto

compromised from the start. The taskforce will entirely rely on the government's full cooperation. Following historical, legal, and provisional consideration, taskforces can only request and receive relevant information or documents. However, they don't possess the powers to compel the State agencies to provide the required documentation. Thus, compliance with such requests has been historically problematic with the government often failing to provide complete information even when compelled by courts of law.

In light of the aforementioned issues, the formation of the presidential taskforce appears redundant and constitutionally questionable. The extant legal framework already designates the OAG as the appropriate entity for conducting public audits. Consequently, efforts should be directed to empowering and ensuring the Auditor General's office can perform its constitutional duties effectively, rather than creating parallel structures that may waste public resources and undermine established constitutional functions. This approach would mainstream and enhance transparency, accountability, and prudent management of Kenya's public debt, while concurrently aligning with both legal mandates and best practices of public finance management.

Odious debt

Kenya's escalating public debt conundrum, coupled with limited transparency and political goodwill has prompted discussion about the possibility of this debt being classified as odious. The concept of odious debt is tied to the legality, legitimacy, and sustainability of public debt. This is equally tied to whether citizens are unjustly burdened by debt that did not benefit them or was accrued under unfair, unclear, or illegitimate conditions.

The Constitution of 2010 and Section 15 (2)(c) of the PFMA stipulate that national debt should only be





procured for development purposes, not recurrent expenditures or consumption. It is however noted that the government disregards linking borrowed funds to specific development projects. This raises the argument that such debts could be declared odious. Equally, reports by the OAG gave noted that parliamentary approval had not been sought for much of the domestic debt, suggesting a plausible pattern of illegal borrowing for purposes other than development.

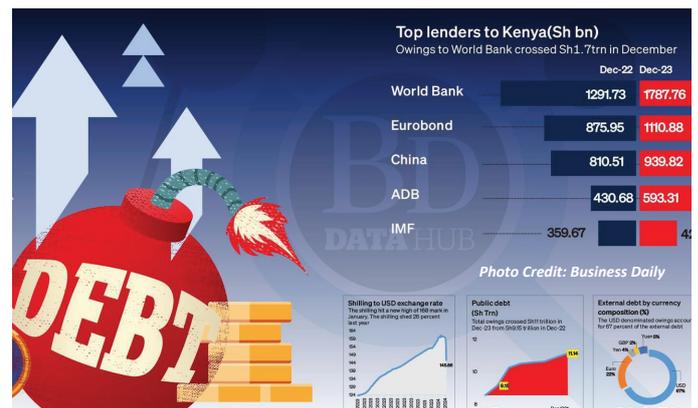
Policy discourses on odious debt in Kenya have been undertaken regarding both external and domestic borrowing. Loans from institutions like the International Monetary Fund (IMF) are often examined under this lens as they often come with stringent conditions and policy prescriptions. These conditions often include retrenchment, reduction in public and social sector expenditures, indiscriminate tax hikes, and economic policies that often violate national ethos, laws, human rights standards, and social justice principles. Most of these debts becomes unsustainable as they impede the government's ability to meet its obligation to the citizenry like the provision of essential services like healthcare, education, water, sanitation, and housing.

Equally, the issue of odious debt has gained traction since the release of the 2019 Auditor General's report on Kenya's \$2 billion Eurobond issues in 2014.

The report revealed that although the proceeds from the Eurobond were deposited in the National Exchequer accounts, they could not be traced to specific development projects. The National Treasury countered that the funds were fungible, as some expenditures occurred outside the government's Integrated Financial Management Information System (IFMIS). This raised concerns over the lack of transparency and accountability. Moreover, it suggests that the government's borrowing did not meet constitutional and legal requirements, which mandated borrowing solely for development expenditure.

In addition to discourses on the legitimacy of Kenya's debt, evaluating the implications of declaring the public debt odious is profound. Domestically, creditors of national debt include commercial banks, insurance companies, pension funds, public universities, and state-owned enterprises. The potential of disavowing government debt, if and when declared odious, will severely impact these institutional lenders and individuals who invest in the instruments. This includes the potential loss of deposits, premiums, contributions, and taxes. This scenario underscores the need for a nuanced approach to addressing Kenya's debt conundrum.

Mitigation measures around these issues are imperative and should be prioritized. For instance, future borrowings must be earmarked and identifiable to specific development projects.



Transparency and accountability should be reinforced through rigorous parliamentary oversight and adherence to constitutional provisions. Moreover, strengthening the OAG to ensure compliance with PFMA remains crucial in restoring fiscal responsibility and public trust. Addressing the root causes related to the ensuing discussion of odious debt requires political commitment and goodwill coupled with ethical borrowing practices, sustainable debt management, and a transparent governance framework that prioritizes Kenya's well-being.

Conclusion

Kenya's public debt audit highlights a well-intentioned but inconsistently implemented legal framework of the country's national debt. While management of public debt is guided by the Constitution, the PFMA, and the National Tax policy, with clearly assigned roles to Parliament, Treasury, and the OAG, to ensure transparency, accountability, and sustainability, implementation is rigorously challenged. Parliament's oversight and legislative duties as outlined in Article 211 of the Constitution and Section 32 of the PFMA, are compromised by the prioritization of political allegiances and capacity

challenges, which collectively allow the Executive to violate borrowing limits. The OAG mandate to annually audit public debt, coupled with Treasury reporting obligations, is frequently undermined by incomplete or non-compliant submissions. Moreover, the formation of the presidential taskforce to audit public debt has further complicated matters. Questions on its legality and effectiveness given its redundancy alongside the OAG's constitutional role abound. Addressing these impediments requires the strengthening of existing legal frameworks, mainstreaming rigorous parliamentary oversight, and enhancing the capacity and independence of the OAG to uphold fiscal responsibility and public trust.



Photo Credit: Office of the Auditor-General

Recommendations

1. Parliament should prioritize its oversight role and enhance the capacity of legislators to effectively interpret and evaluate public debt reports to ensure compliance with legal borrowing parameters
2. Parliament should empower the OAG with increased authority to subpoena public documents necessary to undertake thorough and timely audits of public debt
3. Parliament to amend the PFMA to mandate all public debt contracts are availed to the National Assembly for scrutiny, debate, and approval before they are adopted
4. Parliament to amend the PFMA to mandate the Treasury to undertake mandatory full disclosure and public participation on all external debt issues to enhance transparency and public trust in debt management





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