REPUBLIC OF KENYA

Budget Speech

for the

Financial Year 1982/83
(1st July–30th June)

by

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Speech delivered to the National Assembly on 17th June, 1982, by the Hon. Arthur K. Magugu, Minister for Finance, Republic of Kenya, when presenting the Budget for the Financial Year 1982/83 (1st July to 30th June).

Mr. Speaker, Sir,

I beg to move that Mr. Speaker do now leave the Chair.

THE STATE OF THE ECONOMY

It is a tradition, Mr. Speaker, to begin the presentation of the Budget with a review of the economic circumstances facing the nation; and thereafter to dwell on the financial prospects for the following financial year during the course of which the main taxation proposals are revealed. But before I do that, I want to take this opportunity to pay tribute to His Excellency the President for his continued guidance of this country during rather difficult economic circumstances. Although the economy continues to be affected by adverse international forces, our institutions have, under His Excellency the President's leadership, weathered such global storms with resilience and the economic health of our nation remains robust in comparison with many other developing countries. Indeed, His Excellency the President's fortitude has been physically demonstrated to us through many acts and speeches. All of us should therefore resolve collectively and individually to support his efforts.

In addition, Mr. Speaker, I also wish to record my appreciation for the work carried out within the Ministry of Finance by my last two predecessors, the Hon. James Gichuru, Minister of State and the Hon. Mwai Kibaki, Vice-President and Minister for Home Affairs. I am sure Honourable Members will agree with me that these two distinguished Members of this House, have given unparalled service to economic management of this nation, and I would like that tribute, Mr. Speaker, to be duly recorded. It is the continuity provided by the linkage between the Harambee and Nyayo eras that gives me confidence to undertaken the fourth Nyayo Budget. As I do so, Mr. Speaker, I want to stress at the outset that my statement this afternoon will focus primarily on the Government's response to the growing domestic fiscal imbalance as well as the general problems of financial management in the public sector.

To put this theme into perspective, Mr. Speaker, it might be useful if I drew the attention of Honourable Members to the significance of today's proceedings. The occasion of the Budget Day, Mr. Speaker, affords the Minister for Finance an opportunity to inform the House about the Government's spending plans for the coming financial year. The annual Budget outlines the Government's spending priorities as well as the financing plans of such expenditures as may be approved by this Parliament. This plan emerges from the longer term five-year Plan which is further refined within the process of the Forward Budget exercise. This exercise takes place throughout the year; and the final plans in the form of the Printed Estimates of Recurrent and Development Estimates only emerge after serious review by Treasury and operating ministries. It is important therefore that Honourable Members keep this broader background in mind as I proceed to analyse what the Government's spending programme will be for the coming financial year.

The annual Budget also affords the Minister for Finance the opportunity of reviewing broad economic policies for the proper management of the economy in the short term. Such policies entail the translation of national goals as contained in the Development Plan into specific sectoral targets as well as general direction of Government action.

In outlining such policies, Mr. Speaker, my task is considerably eased by the comprehensive manner in which these policies have been treated in the recently issued Economic Survey for 1982. That document, Mr. Speaker, paints an international economic environment still deeply in recession with no clear signs of recovery in sight. High oil prices, interest rates and global inflation together with weak demand and low prices of our main agricultural exports have all conspired to frustrate the domestic forces of recovery. With the exception of the agricultural sector, the economy performed moderately during 1981. Throughout the year, we have lived through a weak balance of payments situation and our room for manoeuvre on the external account has been severely constrained. There was an acute imbalance between external receipts and payments, during much of 1981, and as a result our foreign reserves were drawn down heavily. Numerous factors contribute to this weakness in our balance of payments, but the most critical factors remain the high cost of petroleum imports, and the falling value of our principal exports. During 1981 export receipts amounted to only 75 per cent of import expenditures. It is this problem, more than any other, toward which the structural adjustment programme is directed. In the meantime, careful attention will be given to Kenya's external obligations to ensure proper adjustment in the balance of payments.

With regard to domestic financial conditions, during calendar year 1981 money supply increased by 13.3 per cent, somewhat below the rate of increase in GDP at current prices. Preliminary estimates indicate that growth of the money supply will be marginally higher over the fiscal year ending 30th June, at approximately 15 per cent and that private sector credit will increase slightly more than public sector credit during the final six months of this period. The resources of commercial banks continue to be strained, with virtually no real growth (i.e., after adjustment for inflation) occurring in the major categories of assets and liabilities. Non-bank financial institutions are continuing to expand their operations, and at present nearly a quarter of all credit is arranged through these institutions. While the vitality of financial institutions as well as insurance companies is certainly desirable, the Government is nevertheless concerned to maintain a healthy balance between traditional commercial banking activities and those of the non-bank financial institutions.

Management of the monetary and banking system during the last year was flexible. While numerous policy instruments are employed in carrying out these responsibilities, the most significant actions during the year have been adjustments in interest and exchange rates. Minimum deposit and maximum lending rates of commercial banks were raised twice during 1981—by a total of three percentage points. Likewise, the exchange rate was also adjusted twice during 1981. These measures have yet to show their full effect on the adjustment process; but we are confident that the present monetary and other policies being pursued by the Government will result in the appropriate adjustments.

Finally, although there are hopeful signs of recovery, largely due to better agricultural prospects, indications are that there will be no rapid growth in the medium term. Overall, we expect a growth rate of about 4.5 per cent, a slightly more rapid rate of inflation and a continuing current account deficit.

Notwithstanding these difficulties, Mr. Speaker, it is my view that the Government's attention must be focussed on the domestic causes and cures of our present economic condition. This, Mr. Speaker, will be the theme of my speech this afternoon.

I begin first by outlining the nature of the economic difficulties facing the Nation. During the last decade, the capacity of the Government to provide essential services to wananchi has been increasingly and seriously strained by the growing gap between Government revenues and expenditures. In earlier years, Mr. Speaker, it was possible to sustain this gap through continued inflows of external resources in a context of a buoyant domestic economy. Management of the Budget deficit in those circumstances was less problematic, and on the whole, fiscal and monetary policies pursued by the Government acted to reinforce the momentum for economic growth in the private sector. However, as my distinguished predecessor, the Hon. Vice-President and Minister for Home Affairs observed in his last Budget Speech, the era of soft options is now behind us.

In spite of the slowing down in the rate of growth of the economy, the momentum of Government spending has continued unchecked. Between 1976 and 1981, gross domestic product at market prices increased by 66 per cent. During the same period, current revenue increased by 123 per cent—an exceptional effort in the circumstances. Commitments to the Consolidated Fund Services, from which Government makes its debt repayment increased by 210 per cent. Revenues available to ministries could therefore increase by only 110 per cent much less than the growth of current revenue. Expenditure by ministries, however, increased by 129 per cent. Hence more and more deficit financing was required although actual Government borrowing from the banking system was somewhat ameliorated by inflows of foreign grants. More recently, the terms of external borrowing have hardened and interest rates on Eurodollar loans are approaching 17 per cent. Government is therefore ultimately forced to rely on increased domestic borrowing. Such a situation, however, is clearly economically untenable and fiscally imprudent. In the first place, Mr. Speaker, high levels of Government expenditures and external debt service in conditions of scarce Government revenues tend to increase imports and capital outflows, thus further weakening the balance of payments. Secondly, Government requirements for revenue and domestic credit drain the private sector of funds needed to finance economic expansion. The inescapable conclusion, Mr. Speaker, is that because potential Government revenues are limited, and the Government's borrowing capacity is now severely constrained, the Budget deficit can now only be brought under firm control by curtailing Government expenditures.

Yet Mr. Speaker, Sir, we might pause and ask what are the prospects for curtailing Government expenditure? A review of the financial out-turn for the current financial year, convinces me, Mr. Speaker, that there are far too many people in Kenya who have as yet to appreciate the seriousness of the current financial problem facing the nation. Expenditure by ministries continues in many cases to outstrip available resources. Indeed as the recently issued Report of the Controller and Auditor-General for 1980/81 indicates this practice has become almost chronic. In addition to overspending, and despite the obvious nature of our financial problem, ministries continue to make unrealistic demands from the Treasury well in excess of the ceilings indicated. Sadly, one detects an apparent unwillingness of top managers in Government to appreciate the magnitude of the fiscal problem facing the nation. This, together with the general lack of financial discipline in many ministries is very disturbing; and I shall say more about it later. Suffice it to say at this juncture, that as His Excellency the President has said on many occasions, we must as a nation, learn to live within our means.

In doing that, we are convinced that the economic strategy which we have chosen for ourselves is the right one. When it has been necessary to make adjustments in the face of changing circumstances, we have not as a Government and a people hesitated to do so. Our faith in the principles of African Socialism as outlined in Sessional Paper No. 10 of 1965 and as practised by the ruling party KANU, remains unshaken. We cannot, therefore, Mr. Speaker, accept the uniformed and misguided arguments of those who would like us to change our course and follow some alien ideologies. As His Excellency the President has so often stressed, we must proceed from the known to the unknown. We shall therefore be guided by our own experience in determining how best to respond to the development needs of our people. The starting point of this task must be the restoration of the integrity and authority of the Budget as the central framework for the allocation of Government financial resources.

FINANCIAL OUT-TURN 1981/82

Mr. Speaker, Sir, I now turn to the review of the budget out-turn for the current financial year.

RECURRENT REVENUE

During the last Budget, it was estimated that ordinary recurrent revenue would amount to K£729 million, and Appropriations in Aid would be K£35.57 million, making a total of K£764.57 million. This recurrent revenue was to comprise of K£247.9 million from Customs and Excise, K£201 million from Income Tax, K£186.9 million from Sales Tax, and K£94.0 million from other taxes. I am glad to report, Mr. Speaker, that once again, Government efforts in raising revenue have been successful, and we expect that we shall exceed these targets by the close of the financial year on 30th June. Indeed, as of 30th May, Government revenues stood at a total of K£667.5 million. Significant improvements were registered in the collection of Income Tax, Sales Tax and other minor taxes, and I take this opportunity to congratulate the various revenue commissioners for their excellent work in this regard. Taken together with Appropriations in Aid, I expect that the Gross Revenue for 1981/82 will amount to K£833.45 million, compared to the forecast sum K£764.57 million.

RECURRENT EXPENDITURE

Turning now to expenditure, the 1981/82 Printed Estimates indicated gross recurrent expenditures of K£702.3 million, comprised of ministries gross expenditure of K£545.78 million and Consolidated Fund Services of K£156.55 million. Again, and in spite of the severe warnings on the need to adhere to the budgeted estimates issued by my distinguished predecessor, this figure has had to be adjusted, with the authority of Parliament last week, by a net sum of K£40 million thus bringing the gross recurrent expenditure of ministries to a total of K£628.1 million. Commitments to the Consolidated Fund Services also increased during the year by K£13.45 million arising from the adjustment in the exchange and interest rates in September 1981. All in all, issues from the recurrent expenditure during 1981/82 are estimated at K£826.4 million compared to the forecast of K£760.1 million.

Three factors account for this significant variation from last year's forecast levels of expenditure: namely, the increase in the provision for Consolidated Fund Services I have just noted; the significant carry-over of approximately K£20 million from previous financial years, and inevitable increases in costs of Government programmes due to inflation.

Taking the revised revenue collections estimated at K£833.45 million, I expect to transfer a sum of K£7.02 million to Development Exchequer.

DEVELOPMENT EXPENDITURE

The 1981/82 Printed Development Estimates projected a net expenditure of K£253.5 million and Appropriations in Aid of K£28.3 million, making a gross total development expenditure of K£281.8 million. The net approved development estimate of K£253.5 million was also adjusted by a sum of K£32.5 million during last week's Supplementary Appropriations Bill thus bringing the net total development expenditure to K£286 million. The Appropriations in Aid in Development Exchequer were also adjusted by a sum of K£10 million, making a total of K£38.3 million. All in all, gross development expenditure during the 1981/82 financial year is expected to be K£324.4 million compared to the original estimate of K£281.8 million.

In spite of this upward revision of proposed development expenditures, it is unlikely that ministries will spend the entire voted amount by the end of the financial year. The conjunction of underspending by certain ministries and requests for Supplementaries by other ministries, must, Mr. Speaker, appear paradoxical to Honourable Members. But as explained during last year's Budget Speech, it is never possible, Mr. Speaker, to anticipate the entire expenditure programme of the Government at the beginning of the financial year. Unexpected expenditure requirements may arise in the course of the financial year; and in certain cases, the priorities attached to some projects may be altered just as unforeseen bottlenecks in project implementation may also arise. The capacity of various ministries to undertake certain development projects also differs, and it is possible that certain projects could be completed ahead of schedule. For these reasons, it may become necessary for the Minister for Finance to seek the authority of this House to make the necessary adjustments to the Government's annual financial programme.

But understandable as these reasons may be, Mr. Speaker, the institutionalization of annual Supplementary Estimates and departures from the Printed Estimates are symptoms of a much deeper disease in our financial control systems. Mr. Speaker, Sir, I have already remarked on the deterioration in financial descipline within ministries. But even more disturbing Mr. Speaker, is the desultory and perfunctory manner in which ministries as a whole treat the budgetary process as well as planning and implementation of development projects. As I have already indicated in the beginning of my speech, the Budget is not merely the accounting framework of Government financial operations. The annual Budget is also the means of translating the Government's economic plans into concrete programmes of action. Development expenditures are therefore expected to have a direct impact on national development. But to do so, such expenditures must be carefully planned and co-ordinated with recurrent expenditures such that there are no unnecessary delays and large escalation in costs in project implementation.

Thus, accounting officers must be concerned with the broader aspects of project management as well as financial control. This means that before embarking on a certain project, spending units must ensure that funds for project financing are available and properly voted for. This commonsense approach will ensure that certain facilities are not physically completed and left idle for lack of appropriate personnel and other inputs. In any case, Mr. Speaker, we should have no instances where projects are started before they are approved by the Treasury through the normal budgetary process.

In establishing their requests for funds from the Treasury, ministries must also endeavour to accurately and realistically assess their requirements. The practice of under-budgeting in order to artificially stay within indicated ceilings is to be equally condemned as the practice of inflating requirements for funds. Mr. Speaker, all I am pleading for is an injection of professionalism in budgeting within ministries. The traditional adversary relationship between Treasury and spending ministries must be replaced with a common analytical approach to financial programming. In this connection, it is important to ensure proper control over commitments as well as expenditure. In addition I wish to appeal emphatically to all leaders to refrain from making promises for expenditure without first ascertaining that funds have been properly voted for.

I would also appeal to public officers to take a responsible attitude towards public funds. Many officers Mr. Speaker, approach the expenditure of public funds with a careless attitude. Such attitudes are well summed up by the Swahili phrase—— "Hii ni mali ya Serikali"; meaning that since Government resources are apparently inexhaustible; one can afford to be extravagant in the expenditure of such public funds. This attitude manifests itself in costly procurement practices, deliberate contract variations, and general dishonesty in accounting for funds. This general lack of commitment Mr. Speaker, is in my view, very damaging. It leads to expenditure of funds without relating such expenditure to the specific development objectives in the belief that spending of money is evidence of accomplishment, even when such expenditure is on trivial items. Clearly, Honourable Members will agree with me that if funds intended for the construction of say 20 classrooms are used for the construction of only 10 such units; then something has gone seriously wrong.

I might, therefore, be excused, Mr. Speaker, if at this juncture I issue a stern warning to all spending units that I expect absolute compliance with Treasury instructions on expenditure control and other aspects of financial management. Since the last Budget Speech, Treasury has issued detailed instructions on expenditure control; but although certain ministries are doing their best to adhere to these instructions, certain spending units continue to blithely ignore such instructions. Whereas Treasury is doing its best to improve financial control and monitoring procedures, I would like to reiterate to the House, that the budgetary process shall remain the sole framework for resources allocation and management of public funds.

In this connection, Honourable Members may recall that during last year's Budget Speech, my Honourable predecessor promised the House that an Economic Commission would be established to look into specific ways of improving financial management in Government and curtailing public expenditure. It is my pleasure, Mr. Speaker, to inform the House that His Excellency the President did appoint such a Working Party in January this year; and that Working Party on Government Expenditure has just presented its report to His Excellency the President. That report, Mr. Speaker, contains many useful specific suggestions for restoring financial discipline and diligence in the public sector, and no doubt, Hon. Members will have an opportunity to discuss these measures at the appropriate time. For the moment, it is the intention of the Treasury to pursue even more vigorously the fiscal adjustment programme on which we embarked last year.

During the last Budget Speech, my predecessor announced certain measures designed to boost savings; namely, the Save-as-You-Earn Scheme operated by the Post Office Savings Bank and the Housing Development Bonds which were to be issued by the Housing Finance Company of Kenya Ltd.; and the Savings and Loan Ltd. Hon. Members will recall that deposits under these schemes were to be tax-free for amounts up to K.Sh. 250.000 and K.Sh. 500.000 respectively. The Save-as-You-Earn Scheme, Mr. Speaker, was launched last October, and I am now informed that the scheme has 50,000 thousand contributors making savings of about Sh. 5 million per month, over and above the Savings Bank's other 1.1 million depositors. This is indeed a very commendable effort.

Housing Development Bonds have only been recently launched and I would urge the larger savers to make use of this scheme. During the coming financial year, the Treasury will examine the domestic financial market with a view to introducing other financial instruments in the effort of mobilizing domestic savings.

Work towards introduction of a comprehensive Insurance Bill promised last year, is also very advanced, and it is my intention to table before this House the new Insurance Bill before the end of this calendar year. The Bill has been extensively discussed between Treasury and the insurance industry and I take this opportunity to thank the industry for their positive comments on various drafts of the Bill.

Mr. Speaker, those Members with a longer memory will recall that the Hon. Mwai Kibaki had promised the House that an Agricultural Development Bank would be created soon. The necessary policy preparation for the establishment of this vital institution is also fairly advanced, and it is my hope that the creation of an Agricultural Development Bank could be announced during the course of 1982/83 financial year.

In the area of External Debt management, a great deal has also been achieved. We now have in place within the Treasury a proper debt management and reporting system which should enable the Government to keep track of its various external borrowing arrangements. Mr. Speaker, I shall be outlining other management systems for better financial control within Government later on in my speech. I would now like to turn to a review of the financial prospects for the coming fiscal year.

PROSPECTS FOR FINANCIAL YEAR 1982/83

During the next financial year, we intend that the financial programme of the Government will entail a reduction in the size of the Budget deficit from the anticipated level of 7.5 per cent of gross domestic product at the end of this financial year, to 6.5 per cent of the gross domestic product at the end of June next year. Such a reduction in the size of the deficit can only come about through cuts in expenditures since the scope of increasing Government revenues and further taxation are limited.

MANAGEMENT OF REVENUES

The assessment and collection of tax revenues is the major way in which national resources are directed to Government use. In capturing such resources for itself, the Government reduces the resources available to other sectors. Tax and non-tax revenue now amount to about 25 per cent of the gross domestic product at market prices. In our view, this figure is already too high and should be gradually brought down to a lower level.

I know hon. Members will agree with me that Government's efforts in raising revenue should shift to spreading the tax burden to all those who do not currently contribute their fair share of taxation rather than to increased levels of taxation. Revenue collection efforts will therefore be aimed at closing loopholes, eliminating tax arrears and bringing new tax-payers into the tax system. Similarly, means of eliminating evasion of sales tax and customs duty will be enhanced and I shall be saying more on this later on in my speech. Revenue collections from the tourist trade, multinational corporations and locally-based companies at present do not reflect the realistic potential of revenue yields from these sources; and all efforts will be made to recover as much revenue from these sectors.

MANAGEMENT OF THE DEFICIT

I have already remarked that borrowing by the Government from the banking system on recent scales has deprived the private sector of the credit it requires for economic expansion. Such borrowing, Mr. Speaker, has also contributed to the current high levels of debt service payments and weakened our balance of payments. The overriding consideration of Government's monetary and credit policies in the immediate future will therefore be to increase the access of private agriculture, commerce and industry to domestic credit from commercial banks and financial institutions. To this end, credit to the Government from the banking system in the next financial year will be reduced and Government borrowing from the banking system will not be allowed to grow at such high rates as we have experienced in the last few years.

The size and composition of Government expenditures also influences the pace of economic activity. At present, Government expenditures amount to nearly 35 per cent of the gross domestic product, a figure substantially higher than Government contribution to gross domestic product. Thus, the Government takes away more resources from the economy than its productivity justifies. It is necessary therefore that the level of Government expenditure is reduced, and the productivity of such Government activities improved.

Making such cuts, Mr. Speaker, could be quite easily done through arbitrary cuts across the board. The fiscal problem could then be said to be "solved"; but the momentum of development would be lost, and the pattern of development severely distorted. However, the challenge which faces the Government in the management of the economy in the medium- and long-term demands that the momentum of development is sustained despite restrictions on Government expenditures. That strategy calls for a review of the composition and level of Government revenues and expenditures by consciously emphasizing efficiency in resource allocation and utilization. This is so, Mr. Speaker, because even if fiscal balance is attained and productivity of Government expenditure remains low, the development impact of such expenditures will be lost.

To this end, accounting officers are urged to scrupulously following Treasury instructions, particularly Circular No. 1 of February, 1982 which forbids the issuing of cheques without certifying that there is money in the ministry's cash book. In addition, the Government is in the process of changing the format of its Local Purchase Order so that those who commit Government to any expenditures can explicitly certify to the members of the public that funds to pay for such services or goods exist. We shall be making other innovations in financial control in the course of the year and I do not want to bore the House with what are really housekeeping matters in the Treasury.

However, I now want to turn my attention to a sector on which so much has been said recently, namely management of the parastatal sector.

MANAGEMENT OF GOVERNMENT INVESTMENTS

Mr. Speaker, as hon. Members are aware, His Excellency the President has on many occasions called for improved financial performance in the parastatal sector. Yet performance in this sector as a whole remains disappointing. Since independence, Government has made investments, including guarantees to parastatals of about K£900 million. During the same period, Government has received only K£23.5 million in form of dividends. Furthermore, loan repayment by many parastatals remains erratic and in certain cases parastatals regard such loans from the Government as handouts. Treasury has, however, recently issued new guidelines in this area, and the response has so far been encouraging.

In the light of this dismal record, hon. Members will agree with me that there is need for change in Government's investment policies in the parastatal sector. Consequently, the Government has decided that it will gradually withdraw from active direct participation in commercial enterprises. This is so, Mr. Speaker, because in our view many parastatals have exceeded their original mandates and have made investments in industrial and commercial activities in areas which strictly speaking are outside the proper domain of Government activities. The affairs of the Government have also suffered because of the inordinate time senior officers spend in trying to rescue ailing projects; not to mention the heavy burden such salvaging operations place on the Exchequer. Time has therefore come, Mr. Speaker, for the Government to reconsider its approach in this area. In the meantime, the general supervision and direction of parastatals by Treasury as well as the Parastatals Advisory Committee will be strengthened.

More specifically, the financial planning and control of parastatals will be fully integrated into the Government's annual Budget. Consequently, no new investments by parastatals will be allowed unless they have been included in their parent ministry's budget and approved by Treasury in the normal budgetary process. Furthermore, in future Treasury will expect prompt and adequate contribution by the parastatal sector towards the financing of the Government's long- and short-term domestic borrowing requirements.

Mr. Speaker, Sir, I now want to touch on another related issue in the utilization of public funds. Honourable Members are aware that the Government has gone out of its way to assist farmers and traders with loans for crop production and other commercial activities. The repayment record of many of these loans is, to say the least, very disappointing. On a current year basis, only about one-third of farmers are repaying their seasonal credit loans. Yet it is clear that crop failures do not occur every season. By not repaying their loans, these farmers and traders, Mr. Speaker, deprive others of access to credit and eventually force the Government to borrow even more money from the banking system in order to finance the needs of others. During the next financial year, we shall launch a special task force to recover all loan arrears both within the agricultural sector and the industrial and commercial sphere as well.

Mr. Speaker, Sir, I have dwelt on the need to improve management and use of resources in the public sector because as I have already indicated, the solution to our problems lies within our hands. As we approach the next financial year, we are determined to resolve the perpetual problem of imbalance between Government expenditures and revenues while at the same time laying the foundations of better financial and economic management in the future.

Mr. Speaker, I now want to turn to the forecast of expenditures and revenues for the coming financial year.

PROJECTED OUT-TURN 1982/83

EXPENDITURE 1982/83

As honourable Members will no doubt have seen from their copies of the Printed Estimates, gross recurrent expenditure of ministries is estimated at K£953.4 million; comprising of net expenditure of K£868.2 million; and Appropriations in Aid of K£85.3 million. In addition to this, there is a carry-over of Excess Votes of K£32.2 million for 1979/80 financial year. Thus estimated issues from the Recurrent Exchequer are expected to be K£985.6 million. Considering the rate of domestic inflation, the proposed recurrent expenditures are in real terms less than for the current financial year which is consistent with our policy of gradually reducing the share of Government expenditures in the gross domestic product from its current high level to more manageable proportions. Once again, Mr. Speaker, I call upon all ministries to ensure that they live within these estimates so that we may once and for all get rid of the recurring problem of Excess Votes.

Honourable Members will note that once again, expenditure on Consolidated Fund Services will go up from K£139 million in 1981/82 to K£264 million during the next financial year. This as I have already indicated is due to the rising burden of debt repayments which we must honour as a country.

Development Estimates for 1982/83 call for an expenditure of K£370.1 million, including Appropriations in Aid of K£86.6 million and Excess Votes for 1979/80 of K£13.4 million.

I do not intend to analyse further the details of either recurrent or development expenditure for now. Suffice it to say that I expect to finance a total expenditure of K£1,355.7 million. The rest of my speech will outline how I intend to do this.

EXTERNAL REVENUE 1982/83

In view of the limitations on the growth of Government revenue I have mentioned earlier on, we shall continue to rely to some extent on the assistance of our international friends. I am confident, Mr. Speaker, that I speak for the whole House in paying tribute to His Excellency the President's tireless efforts in this area. Not only has he journeyed to many parts of the world to win us new friends and strengthen long standing friendships between Kenya and many foreign countries; but he has brought to bear his diplomatic skills on the need to increase humanitarian aid to the continent of Africa as a whole. The response to His Excellency the President's efforts in this area has always been positive and for this assistance I would like to thank all our external friends.

I would, however, like to call upon such donors to consider increasing their level of programme assistance in addition to their traditional financing of projects. From our point of view, programme assistance is preferable because it assures speedy disbursement of funds. In addition, since the funds are not tied to specific projects, it enables the Government to finance projects in a comprehensive manner within the priority framework of the Budget.

Mr. Speaker, I have already noted that the terms of external borrowing are hardening; and it is my hope that more donors will soften their lending terms by increasing the share of grants and concessionary loans in their aid programmes. Several donors are already doing this and I appeal to others to do the same. In addition, I would urge more donors to adopt the practice of payments of project aid in advance so that the Government does not have to strain the Exchequer in spending its own resources before receipt of reimbursements from donors

We on our part, Mr Speaker, will make all efforts to ensure that the cycle of claims and reimbursements will be shortened so that the momentum of project implementation can be enhanced

In the next financial year, I estimate that we shall draw some K£253.6 million from external sources in the form of grants concessionary loans and other external assistance from bilateral and multilateral sources. Thus I expect to finance 19 per cent of the total expenditure of K£1.355.7 million from external sources. The main burden on financing Government expenditures will, however, remain on the shoulders of Kenyans and I now turn to how I intend to raise the balance of K£1.102.1 million from local sources.

INTERNAL REVENUE 1982/83

I estimate that ordinary revenue, including local Appropriations in Aid should provide some K£933.5 million at current rates of taxation. Government stock issues should provide another K£85 million from the non-bank sector, making a total of K£1.018.5 million. I therefore have a gap of K£83.6 million to finance. The rest of my speech will outline how I intend to do this.

NEW TAXATION PROPOSALS

In my review of the current state of Government Budget, I have warned of the great difficulties that we shall experience in financing public expenditure and the need for public officers to be cost conscious. In this connection, I have enumerated some of the measures to be taken to contain public expenditure.

Mr. Speaker, the remaining part of my speech will therefore be concerned with how I propose to close the gap of K£83.6 million in Government spending while at the same time observing the policy guidelines I have already outlined. The Finance Bill published today contains amendments aimed at streamlining several existing fiscal measures and removing existing anomalies, as well as increasing the level of revenue. I would, therefore, ask that the rest of my speech be regarded as being Notice of a Motion to be moved before the Committee of Ways and Means.

CUSTOMS AND EXCISE

I begin with measures under the Customs and Excise Act. Many of the changes proposed in the Finance Bill deal with Customs and Excise. Before drawing the attention of the House to the most important of these changes, let me first deal with a few technical and procedural matters. The Finance Bill includes amendments to the Customs and Excise Act intended to rectify previous typographical errors and omissions. It also includes amendments to streamline and harmonize Tariff and Statistical Codes in accordance with the recommendations of the International Customs Co-operation Council.

Mr. Speaker, the Customs and Excise Act has no provision giving the commissioner powers to appoint an agent to collect duty on his behalf as is the case with the Income Tax Act. Lack of this provision has created a problem where some manufacturers of excisable goods have sold the goods and refused to remit the duty to the commissioner even where the commissioner could have easily requested the buyer to remit duty direct to the Customs Department. It is, therefore, proposed to provide the commissioner with powers to appoint agents for collection of any payable duty.

Currently, the distress levied in the event of an excise licensee failing to pay duty does not include buildings, land or plot owned by such licensee. The distress can only be levied on machinery. In some cases, the machinery may be so old that substantial duty owed cannot be realized from the sale of such machinery. It is, therefore, proposed to broaden the coverage of such distress to include buildings and land. This will ensure that excise licensees pay duty when due and payable.

As hon. Members may know, the East African Customs and Transfer Tax Management Act and the East African Excise Management Act ceased to have the force of law in Kenya following the enactment of the Customs and Excise Act in 1978. However, there is no provision under the latter Act linking administrative or legal obligations which arose under the former to allow continuity of the department's operations. The effect of this omission renders some types of operations illegal and since, in practice, the continuity was inevitable, it is necessary that Parliament provides legal backing to such operations. There are, for example:

First, bond securities which were executed or given in favour of the then commissioner-general for revenue protection which are still operating; second, cases where duties which were due prior to the commencement of this Act were demanded and collected under this Act; third, cases pending in Kenya law courts filed under the East African Community Acts but which continued to be heard for or against the commissioner under the new Act; and fourth, goods which were seized under the East African Community Acts but for which investigations had not been completed so that the respective cases had to be completed after commencement of this Act.

The Finance Bill contains a new section to provide a legal link between East African Community Acts and this Act.

Mr. Speaker, there are several cases where non-payment of duty may occur due to incorrect tariff classification, such that lower rates of duty or duty-free admission of goods may be permitted. Changes are proposed in the Finance Bill to eliminate this situation. In addition, there are a number of cases where owners of transit goods fail to export them by the due date or do not account for the goods in accordance with the law. In all such cases the Customs Department demands the duty payable in addition to fines where applicable. Almost invariably, owners deliberately delay the payment of duties and taxes due, thereby depriving the Government of revenue. As in the case of the Income Tax Act, I propose to amend the law to provide that an interest of 10 per cent shall be chargeable where such delays occur.

Mr. Speaker, section 158 of the Act limits the period for demand for duty short levied or erroneously refunded to 12 months only. This period is obviously short in view of the large number of documents which have to be audited to establish the correct duty that is chargeable or refundable. A lot of revenue has been lost as a result of this restriction and I, therefore, propose to extend the period to 5 years to be in line with the average period of storage of customs documents.

There are also a number of other technical amendments in the Finance Bill intended to close loopholes in revenue loss and with which I shall not bore hon. Members. These will be elaborated upon while the House is debating the Bill. I would now like to turn to the amendments which have direct revenue implications.

Hon. Members will recall that I increased the price of beers and cigarettes in April this year in order to avoid pre-budget hoarding which has characterized these products in recent years. To effect that increase, I amended the rates of sales tax and excise duty on locally produced beers and spirits respectively. In order to put the price of imported spirits at par with those of locally produced spirits, I propose to increase the rate of duty on imported whisky, brandy, gin, vodka, rum and other spirits from Sh. 75 per proof litre to Sh. 100 per proof litre. This increase will be effective from mid-night tonight. No additional increases will be effected in the price of beer in this Budget.

Mr. Speaker, during the last two years, the Government has been pursuing an import policy aimed at replacing quantitative restrictions and other industrial protection measures with equivalent tariffs. Since 1980, a lot of effort has gone into this reform; and members of the public now have access to a comprehensive Import Schedule which lists all our imports according to national priorities. This year, further rationalization of this process is envisaged by shifting some 317 items from Schedule II to Schedule I. Consequently, tariffs on some of these items may have to be raised to afford local manufacturers adequate protection. In addition, I also propose to correct tariff anomalies which have been brought to our attention by local manufacturers during the course of the year.

Accordingly, duty on imported plastic jars, bottles and paper containers will be raised from 50 per cent to 60 per cent. Duty on ceramic tiles and tableware will be raised from 40 per cent and 50 per cent respectively to 80 per cent. Similarly, duty on imported iron, copper and aluminium articles will be raised by an additional 10 per cent.

The Government has for some time now been aware of an anomaly in the pharmaceutical industry where drugs are imported duty-free while the raw materials used for the local manufacture of drugs are dutiable at varying rates. The effect of this situation is that local manufacturers of drugs have found it difficult to compete effectively with importers of finished drugs. In order to remove this anomaly, I propose to remit duty on raw materials used by genuine local drug manufacturers with effect from tomorrow. A Legal Notice to effect this measure is published today.

Export Taxes

Mr. Speaker, export duty on coffee and tea is currently charged at the rate of 15 per cent of the difference between the price realized per tonne and the threshold of K£1,000 per tonne. Costs of coffee and tea production have, however, risen since the days of the coffee boom, and in order to give a break to farmers I propose that export duty on coffee will in future be calculated on the basis of average price realized in the quota and non-quota markets. Furthermore, the rate of export duty on coffee and tea will be progressive such that where the price does not exceed K£1,500 per tonne, the rate of duty shall be 10 per cent of the difference between the realized price and K£1,000 per tonne. The rate of duty shall rise progressively such that should there be another coffee boom in the future so that prices exceed K£3,500 per tonne, the rate shall be 25 per cent.

The effect of the changes I have announced in export duty as hon. Members may have already guessed, is that farmers will now get more for their produce. I consider this relief to farmers fully justified.

Considered together, the measures I have announced on Customs Tariff, which will take effect from midnight tonight, will provide the Exchequer with additional revenue amounting to K£6.51 million.

Sales Tax

Mr. Speaker, I would now like to turn to sales tax. The Sales Tax Act requires manufacturers with a turnover of more than Sh. 200,000 to apply to the commissioner for registration for the purposes of the Act. Unfortunately, some eligible manufacturers have decided not to register themselves and are therefore not paying the tax even though their selling prices often include sales tax. These manufacturers are not only cheating the Government but also the public. I am therefore amending the law to provide the commissioner with powers to register these manufacturers and to assess tax due and payable retrospectively from the date that such manufacturers became eligible. This, Mr. Speaker, is one of the measures we intend to take to bring more manufacturers into the tax net.

As hon. Members are aware, fruit juices and sodas have become significant beverages. In order for the Exchequer to maintain its fair share of this rapidly growing trade, I propose to increase the rate of sales tax on fruit juices from 25 per cent to 30 per cent and that of sodas from 40 per cent to 50 per cent. This should result in an average increase in the price of sodas of 20 cents per bottle.

Mr. Speaker, hon. Members may recall the lively debates which have taken place in this Chamber on the subject of wigs. I am still convinced that our women's hair is superior to any artificial substitutes, and I therefore propose to raise the rate of sales tax on wigs by 35 per cent. Similarly, those who are rich enough to afford videos and thus can afford to watch films at home instead of patronizing local cinemas will pay an additional 20 per cent of sales tax on videos.

The measures I have just announced on sales tax will provide the Exchequer with an additional K£3.76 million.

INCOME TAX

Mr. Speaker, I shall now turn to income tax. As hon. Members are aware, there are still many tax loopholes which are exploited by tax-payers. Several amendments to close such loopholes are proposed in the Finance Bill.

First, section 3 (2) (*d*) makes alimony liable to tax if it is derived from Kenya while under section 15(3) (*c*) payment of alimony is deductible before computing tax liability. One of the problems with this arrangement is that where the recipient is non-resident, such payments could easily escape taxation particularly because there is no withholding tax on alimony. The second problem is that by exempting alimony from tax where the person making the payment is paying tax at a higher rate than the person receiving it, the Government subsidizes the couple to the extent of the difference between what tax would have been paid and what has actually been paid. Finally, while the total family relief is only K£84 per annum, there is no limit on the amount of alimony a person can claim to have paid and with collusion of the recipient, the amount can be inflated to evade tax. To close this loophole, alimony shall cease to be deductible for tax purposes and the same shall not be taxed on the recipient.

Secondly, lease-hire payments for non-commercial vehicles are not allowed as deduction for income tax purposes. In order to circumvent this prohibition some people have resorted to registering private cars as commercial vehicles so as to get lease-hire payments deducted for income tax purposes. In order to close this loophole, the Act will be amended to define the commercial vehicles which will be eligible for this deduction and also to eliminate further abuse of lease-hire arrangements.

Thirdly, section 12(1) (*b*) of the Act, encourages tax evasion by making lease-hire arrangements more attractive compared to purchase of assets. This is particularly so for commercial vehicles, and I intend to amend the law to restrict the capital sum which can be included for calculation of tax deductions.

Mr. Speaker, hon Members will recall that the rate of capital gains tax was reduced by half last year in order to enable sellers to put more houses, shares and stocks in the market. Judging by the current prices of houses and stocks in the market, the sellers do not seem to have responded to this incentive and I propose to reduce the rate of capital gains tax on companies and individuals further by half. This measure will cost the Exchequer some K£2 million in revenue.

TAX RESERVE CERTIFICATES

Finally, Mr. Speaker, Tax Reserve Certificates are issued by the Treasury to enable companies and individuals pay tax in advance. For this reason, the interest earned on Tax Reserve Certificates is free of tax. The interest currently paid on these certificates is 4 per cent per annum. In view of last year's general increase in the rates of interest, I propose to increase the rate of interest on Tax Reserve Certificates to 8 per cent per annum. I hope this measure will encourage tax-payers to buy more certificates.

EXPORT COMPENSATION

As hon. Members are aware, Government accords high priority to the promotion of exports. It is mainly for this reason that export compensation scheme was introduced in 1974 and hon. Members may recall that the rate of export compensation was doubled from 10 per cent to 20 per cent in 1980. Furthermore, the Kenya External Trade Authority, K.E.T.A., has organized many promotional tours of various markets in the world; but in spite of these efforts, the rate of growth of our manufactured exports remains disappointing. It has become necessary therefore to take stock of our entire approach to export promotion and incentives. As part of this exercise, the Government has undertaken a study on the implementation of the Export Compensation Scheme, the results of which convince us that the scheme, as presently operated is an ineffective instrument of export promotion for the following reasons:

Firstly, the study reveals that compensation is going to products in which Kenya is already internationally price competitive and on which there is, therefore, no need for export incentives. Secondly, the bulk of the compensation payment are being received by four or five companies, which as I have already indicated have an edge over many other regional producers of such commodities. Thirdly, in practice, the test of domestic value added is hardly applied, and compensation is often paid for non-qualifying commodities. Indeed, the scheme has been exploited by some exporters to defraud the Government of large sums of revenue. Fourthly, the foreign exchange earned on products eligible for compensatory payments actually fell by 7.8 per cent between 1979/80 and 1980/81 notwithstanding the increase in the rate of compensation.

Finally, Mr. Speaker, I believe that the problems facing Kenyan exporters are more complex and require reforms in the manufacturing technologies themselves, management and improvements in labour productivity before the advantages of export subsidies such as the export compensation scheme could enhance international competitiveness of our exporters of manufactured goods. In the light of these revelations, it has been decided to suspend the Export Compensation Scheme with immediate effect. Consequently, no further payments under this scheme will be made from mid-night tonight.

In the meantime, Government is examining a comprehensive package of export incentives which will be unveiled during the course of the year. For the moment, exporters should take advantage of the recent adjustment in the rate of exchange of the Kenya Shilling to penetrate new export markets and increase the volume of their manufactured exports

The suspension of export compensation will benefit the Exchequer to the tune of K£13.5 million in foregone payments.

Hotel Accommodation Tax

Mr. Speaker, I would now like to close a couple of loopholes in Hotel Accommodation Tax.

First, the Hotel Accommodation Tax Act defines the word "hotel" as any premises, including those known as game "lodges", in which accommodation only or accommodation with food, is supplied or is available for supply to five or more adult persons at any time in exchange for money or other valuable consideration. This definition has been used by hoteliers to evade tax by—

either removing the beds during the day to make the number of beds appear less than five and returning them at night;

or contending that beach cottages, bungalows and bandas do not qualify as hotels even where these premises are hired for short and long period and at varying charges; and

or stating that they have converted their lodging rooms into residential rooms to collect rent on monthly basis.

In order to close this loophole, I propose to redefine the word "hotel" to include cottages, bungalows, apartments, bandas, and rented camps let on service tenances or on written lease for specified or unspecified period.

Second, section 3(2) (*b*) of the Act provides that tax payable "in any other case shall be equal to 10 per cent of the charge for hiring or occupation". This has provided a loophole for tax evasion in that contracts between hoteliers and tour operators include provision of food and accommodation. However, when hoteliers compute tax, they charge accommodation only. The result is under-payment of tax. I, therefore, propose to close this loophole by providing that the tax shall apply to both accommodation and food.

Third, some hotels do not keep registers or issue receipts. As a result, no tax is collected on such hotels as there are no records. It is, therefore, proposed to make it mandatory for hotels to keep records.

Fourth, as it stands now, the Act has no provision for tax collection where no records are kept by the hotelier. It is therefore easy to avoid tax by simply not keeping records. To close this loophole, I propose to provide a provision to enable the Controller of Inland Revenue to charge a presumptive tax on the basis of charges and the number of rooms

Finally, section 8 requires the defaulter to pay penalty equal to one-half of the amount of tax in respect of which he is in default. The amount owed by hoteliers to Government in form of tax is civil debt. Like all civil debts, courts take a long time to recover them and I therefore propose that the tax and penalty shall be recovered through the process of distraint as in other taxes. Another anomaly in the Act is that there is no legal provision empowering the courts to order recovery of tax due in the event of conviction. I propose to introduce such a provision.

These measures will provide the Exchequer with an additional K£700,000 in revenue.

Traffic and Transport Licences

Mr. Speaker, I would now like to turn to the motorists. As the hon. Members are aware, the cost of maintaining our roads has increased considerably in recent years and it is only fair that those who drive on these roads should pay more towards their maintenance. Accordingly, I propose to make the following changes in the level of fees charged under the Traffic Act regulations

First, drivers licence fees will be increased from Sh. 70 to Sh. 100.

Second, road licence fees on motor vehicles will be increased progressively such that for a car whose engine capacity does not exceed 1,000 c.c., the fee will be raised from Sh. 200 to Sh. 300. For those who enjoy driving bigger cars, the fees will be raised progressively to a maximum of Sh 7,500 for cars with engine rating exceeding 5,000 c.c. This increase is compatible with Government policy to reduce consumption of petrol.

Third, commercial and public service vehicles exceeding 5,500 kg. will have their road licence fees increased progressively such that those whose tare weight exceeds 5,500 kg. but does not exceed 6,000 kg. will pay an additional Sh. 1,000 while those with tare weight in excess of 6,000 kg. will be charged an additional Sh. 250 for every 500 kg. or part thereof.

These measures, plus minor increases in other fees paid to the Registrar of Motor Vehicles will provide the Exchequer with an additional K£3.05 million.

Firearms Act

Mr. Speaker, the security of one's life and property is guaranteed in our Constitution. It is for this reason that the Government provides adequate resources to the security forces to enable them perform their duties satisfactorily. In spite of these free services, however, some people still prefer to provide themselves with extra protection by owning guns. I guess these people do so in order to protect their properties and therefore are able to afford higher taxes. I therefore propose to increase licence fees on firearms from the present small charge of Sh. 40 for a pistol or revolver to Sh 1,000.