NATIONAL ASSEMBLY

OFFICIAL REPORT

Thursday, 15th June, 2006

The House met at 2.40 p.m.

[Mr. Speaker in the Chair]

PRAYERS

ARRIVAL OF HIS EXCELLENCY
THE PRESIDENT

*(Mr. Speaker announced the arrival of
His Excellency the President,
the hon. Mwai Kibaki, MP)*

*(Hon. Members rose in their places while
His Excellency the President took
his seat in the Chair of State)*

COMMITTEE OF WAYS AND MEANS

MOTION

THAT MR. SPEAKER DO NOW
LEAVE THE CHAIR

The Minister for Finance (Mr. Kimunya): Mr. Speaker, Sir, I beg to move that Mr. Speaker do now leave the Chair.

Mr. Speaker, Sir, I feel greatly honoured to present my first Budget since becoming Minister for Finance. It is with utmost humility that I present the Budget proposals for the Financial Year 2006/2007 to this esteemed august House and to the people of Kenya, in the distinguished presence of His Excellency the President and several of my predecessors at the Treasury. Having experienced what they have all gone through during their time at the Treasury, allow me to pay my compliments to each one of them for their contribution to this economy.

(Applause)

Mr. Speaker, Sir, I would also like to record my appreciation for the support I have received from a very dedicated Budget team assembled through the Treasury over the last three months, as we analyzed and put together this Budget. I also wish to thank the many Kenyans who sent us proposals and even took time to discuss the same with us. This Budget is a collective product of all these people.

Mr. Speaker, Sir, as hon. Members are aware, our economy has steadily registered commendable growth rates over the last three years. This is a clear indication that our economy has now recovered. Indeed, in 2005, national income recorded a robust broad-based growth of 5.8 per cent and about 460,000 new jobs were created.

Mr. Speaker, Sir, for the first time---

(Loud consultations)

Mr. Speaker: Order, hon. Members! This is a very serious business. You will have your time to comment on the truth or otherwise of that statement.

(Applause)

The Minister for Finance (Mr. Kimunya): Mr. Speaker, Sir, for the first

time in two decades, we have been able to increase our per capita income over three successive years. This performance is not an accident. It reflects the policies that this Government has implemented since it came to power. It is a demonstration of our commitment to pursue the right economic policies to achieve rapid and sustainable economic growth. This is critical for ensuring increased employment for our youth, a sustainable reduction in poverty and generating the resources that can be used to reduce income; regional as well as gender inequalities. Mr. Speaker, Sir, despite this good economic performance, we recognise that more needs to be done to reduce poverty. Also the gap between the rich and the poor members of our society remain unacceptably high. This is why we need to dedicate ourselves to strive even harder to reach growth targets that will ensure that we win the war against poverty. In this context, therefore, the Government is committed to continue addressing poverty and unemployment challenges by implementing the reforms described in the Medium Term Budget Strategy Paper of 2006, which has already been circulated to hon. Members. In particular, we will continue to focus on implementing sound macro-economic policies which are key elements in creating an enabling environment for private sector-led growth, far-reaching structural and sectoral reforms aimed at enhancing efficiency of resource utilisation, and additional measures to strengthen governance and reduce waste and losses due to corruption.

Mr. Speaker, Sir, the Government's vision for the future is to build a strong, cohesive and prosperous democratic country for our youth and generations yet to come. This will require our continued hard work, patriotism and, above all, a shared development vision. In this regard, allow me to commend all Kenyans for their contribution to the significant progress we made towards larger political freedom and democracy since 2002. In the journey so far, we made our mistakes. We have also had our fair share of scandals. But more importantly, we have learnt vital lessons on the way forward.

Mr. Speaker, Sir, this year's Budget aims at consolidating the gains we have painfully achieved, while taking into account the lessons learnt over the last three years. It also aims at investing in programmes to achieve a prosperous new future; a new future with more wealth for our people, increased employment opportunities for our youth, more equitable distribution of the national resources and reduced poverty.

Mr. Speaker, Sir, having spent the last three years implementing key measures in our Economic Recovery Strategy, our economy has now reached a turning point. After years of stagnation, the economy is now poised for sustained economic growth and development. We must, therefore, develop and put in place frameworks in each of our priority areas that will take us to the prosperous future we all yearn for. The Budget for 2006/2007 is the first of those frameworks that seek secure solutions for our future challenges today. For this reason, the theme of this year's Budget is: "Frameworks for the Future Laying the Building Blocks."

Mr. Speaker, Sir, before I go into the main substance of my Budget proposals for 2006/2007, allow me to say a few words on the recent international and domestic economic developments. On the international front, the growth of the world economy in 2004/2005 demonstrated continued momentum and resilience despite higher international oil prices and natural disasters. The world output expanded by 5.3 per cent and 4.8 per cent in 2004 and 2005 respectively. In 2006, overall global economic growth is projected to remain strong at 4.9 per cent, aided by continued benign financial market conditions and the pursuit of appropriate macro-economic
policies across the world.

Mr. Speaker, Sir, the African region has also experienced strong growth with real Gross Domestic Product (GDP) expanding by 5.2 per cent in 2005. It is expected to grow further by 5.7 per cent in 2006.

Mr. Speaker, Sir, on the domestic economy, I will be very brief on my comments on recent developments in this sector. I, however, encourage hon. Members to read the Economic Survey of 2006 which has already been tabled to be circulated to them for more detailed information.

It is heartening to note that the bold measures we have painstakingly implemented over the last three years have begun to pay dividends. As I noted earlier, our economy is now enjoying a broad-based expansion that we have not witnessed in decades. The improved performance has been driven by strong growth in key sectors of the economy, such as agriculture, manufacturing, tourism, building and construction and transport and communications. As a result of this growth, 1.4 million new jobs have been created over the past three years.

Mr. Speaker, Sir, with regard to inflation, the combination of sound monetary and fiscal policies, better weather conditions starting in April this year, as well as a firm shilling exchange rate, have helped ease overall inflationary pressures. We have, in consequence, managed to bring down the annual inflation to about 13 per cent as of May, 2006.

Mr. Speaker, Sir, interest rates on Treasury Bills were stable throughout the first half of 2005/2006 with a 91-day Treasury Bill rate remaining within the range of 8 per cent to 8.5 per cent. However, reflecting continued fiscal discipline and a confidence by market participants that Government will contain its borrowing requirements, the 91-day Treasury Bill rate declined gradually in the second half of 2005/2006 to around 6.7 per cent by mid this month (June, 2006). Lending and deposit rates stabilised at around 13 and 4 per cent, respectively. This means that the interest rate, although it was narrowed, remained unacceptably high by international standards. We are considering putting in place corrective measures which will increase effective competition and, thereby, improve efficiency in financial intermediation.

Mr. Speaker, Sir, on the external front, our trade deficit widened during 2005 as strong growth in imports outstripped the increase in exports. The strong growth in inputs is attributable to higher oil prices and purchases of three aircraft by the Kenya Airways. However, on account of large in-flows of remittances and sizeable financial in-flow, our overall balance of payments remains comfortable. The result of this has been an appreciation of the Kenya Shilling exchange rate and a significant build-up of official foreign exchange reserves in the Central Bank to over US$2 billion, compared with just US$1 billion in December, 2002.

Mr. Speaker, Sir, we have noted the concerns raised by exporters regarding the strong shilling. We are, in this context, closely monitoring developments in this area to ensure that our goods and services remain competitive in the region and internationally.

Turning to the medium-term priorities and fiscal strategy, as I have already indicated, despite the strong growth performance in the last three years, poverty and unemployment challenges still remain. To substantially reduce poverty and further the income and regional inequalities and move decisively towards achieving the Millennium Development Goals, our economy must expand on a sustained basis by around 7 per cent per year. This is our medium-term objective which we believe is achievable.

Mr. Speaker, Sir, we believe that the strategy that we have adopted of sound macro-economic and structural policy, the shifting of resources towards social and economic sectors and fighting corruption will contribute towards achieving this objective.

Mr. Speaker, Sir, although rapid economic growth is central to reducing poverty and inequality, it must be accompanied by specific Government interventions to ensure that the poor also benefit. Accordingly, to ensure that the expected growth will be shared, the combined share of resources I am allocating to health, education, agriculture and rural development, and to infrastructure will rise from 60.7 per cent in 2005/2006 to 62.7 per cent in 2006/2007, and will rise further to 66.5 per cent in the next year, 2008/2009. This is a continuation of our policy to put our fiscal house in order by restructuring our expenditure towards priority areas that were spelt out in last year's Financial Statement.

In addition, the Government will continue to implement core poverty programmes countrywide. In this regard, the non-wage components of core poverty programmes will be maintained at 4 per cent of GDP. Expenditures on this programme will, therefore, rise from Kshs78 billion in 2005/2006 to Kshs86 billion in 2006/2007, representing a 10.6 per cent increase.

Mr. Speaker, Sir, a stable macro-economic environment must be supported by structural reforms in order to more efficiently allocate our scarce resources. Therefore, to ensure effective public service delivery, including Budget implementation, the Government will deepen priority, structural reforms in the areas of Governance, public expenditure and financial management, revenue administration, public enterprises management, financial inter-mediation and private sector competitiveness. These reforms will improve the business environment to facilitate private sector growth and create employment for our youth.

Mr. Speaker, Sir, while the projected economic growth will provide us with the resources to advance our development objectives, sound fiscal policy management remains central in ensuring that we continue to do so in the future. We will, in this regard, continue to pursue fiscal policy management aimed at maintaining a strong revenue effort, restraining the growth of total expenditures while ensuring a shift in its composition from non-productive recurrent expenditures to operations and maintenance and capital expenditure, and to containing growth of domestic debt to a sustainable level.

Mr. Speaker, Sir, last year, my predecessor wisely excluded bilateral budgetary support from the 2005/2006 Budget. By so doing, we have managed to introduce predictability in our Budget process and line Ministries can now plan on the basis of more certain, albeit smaller, resources. This year, we are going a step further by also excluding all multi-lateral budgetary support.

(Applause)

Therefore, the Budget that I am presenting to you today does not contain any external budgetary support. However, we have factored in external financing which is tied to specific projects. Should external budgetary funding become available, I intend to use it to scale expenditures on education, health, agriculture and infrastructure and, if need be, reduce our domestic debt.

(Applause)

Mr. Speaker, Sir, even in the area of project financing, we are examining ways of deepening our bond market with a view to mobilising resources for our infrastructure. In this Budget, I will be making proposals to enhance the bond market so as to provide long-term funding for infrastructural projects. With the strengthening of the bond market, the Government and large infrastructural corporations will increasingly rely on the domestic but predictable sources of funding to achieve our medium-term development objectives. In the coming months, the Government will encourage parastatals to finance needs backed by good cash-flows to issue bonds as a further step to develop our bond market.

Mr. Speaker, Sir, consistent with our intention to maintain fiscal discipline, the Budget limits domestic borrowing to only Kshs29.5 billion. At this borrowing level, we expect interest rates to remain at affordable levels, which should serve as a catalyst for banks to increase credit to the private sector.

Mr. Speaker, Sir, allow me at this point to say a big thank you to all those Kenyan taxpayers for their great contribution to the realisation of our economic freedom.

(Applause)

Nonetheless, after we are through with the poverty reduction and growth facility programmes, we intend to continue our engagement with the World Bank and the IMF under the Policy Support Initiative so as to ensure our home-grown programmes meet internationally acceptable standards. In tandem, we are also expecting a country-rating mission from the world-renowned rating company, Standards and Poor's before the end of June, 2006. Such a rating will not only have a beneficial effect on foreign direct investments, it will also impact positively on the capacity of our private sector to access affordable financing from international markets.

Mr. Speaker, Sir, the 2006/2007 Budget framework is set against the background of medium-term macro-economic framework which I have already outlined. It aims to accelerate economic growth through continued sound fiscal and monetary policies, a strengthening of structural reforms and governance and enhanced investment in fiscal and human capital.

Let me start by providing a brief summary of the macro-economic assumption outlined in the proposed Budget. We anticipate the real GDP will increase by about 5.8 per cent in 2006/2007 provided the weather conditions remain normal and will be underpinned by continued strong growth in agriculture, manufacturing, construction, tourism, horticulture, transport and communications, as well as the financial and export sectors.

Mr. Speaker, Sir, the 12 months inflation rate is expected to decline to about 5 per cent by the end of 2006/2007 from the 13 per cent reported in May, 2006, mainly on account of benign weather conditions and continued implementation of a prudent monetary policy. Our gross international reserves of the Central Bank of Kenya are targeted to remain at well above three months of import cover to adequately cushion the country against any external shocks. Our proposed monetary framework targets an increase in money supply of about 10 per cent through June, 2007 and provides enough space for a significant non-inflationary expansion of credit to the private sector to support projected economic growth.

Mr. Speaker, Sir, the fiscal policy for 2006/2007 will continue to aim at containing the growth of non-core expenditure so as to create fiscal space to facilitate increased resources towards growth and poverty-reducing programmes. On revenue, as we aspire to become more self-sufficient in our development efforts, we will need to re-double our efforts in revenue collection. We are, therefore, targeting to collect revenues amounting to Kshs375.4 billion which is equivalent to 21.4 per cent of our GDP. This will be supported largely by the ongoing improvements in tax and Customs administration.

With increased independence comes increased responsibility. It is, therefore, imperative that each of us contributes to this effort of making Kenya less dependent on foreign resources. We expect the Kenya Revenue Authority to ensure that the rest of the set revenue targets are met while taxpayers will be expected to willingly pay their dues. On our part as a Government, we will make sure that the scarce resources are used effectively and in the most efficient manner.

Mr. Speaker, Sir, our overall expenditure in 2006/2007 will amount to Kshs461.2 billion. In relation to GDP, our expenditures will remain relatively unchanged from the previous year at around 26.4 per cent of the GDP, as our planned reduction in the Recurrent Expenditure is offset by increase in Development Expenditure. This is in line with our strategies of increasing the ratio of resources going to development programmes. Recurrent Expenditure is estimated to rise by 7.6 per cent to Kshs338.3 billion. However, in terms of GDP, these expenditures are expected to fall from 20.1 per cent of GDP in 2005/2006 to 19.3 per cent of GDP in 2006/2007. This is on account of moderately lower spending on foreign interest payment, pensions and other expenditures.

The Government's wage bill is expected to remain unchanged at about 7.4 per cent of GDP which translates to Kshs129.3 billion. This figure takes into account the wage awards for civil servants of Kshs2.1 billion and for teachers of Kshs4.9 billion. It is important to emphasise, however, that about two-thirds of the wage bill amounting to Kshs81.6 billion which is equivalent to 4.6 per cent goes to the education and health sectors, leaving only Kshs47.7 billion which is 2.7 per cent of GDP for the rest of the Civil Service.

Mr. Speaker, Sir, a core requirement of our economic recovery strategy is that, development expenditure should rise as a proportion of both the Budget and GDP. Development Expenditure is expected to rise from Kshs86.9 billion which was 5.6 per cent of GDP in 2005/2006 to Kshs120 billion, which is 6.8 per cent of GDP in 2006/2007. This represents an increase of 38 per cent from the previous year and compares favourably with a growth of 11 per cent of overall expenditures. Expenditures are, therefore, focused to be more development oriented and with a special focus on improving the road network, access to water, reliable and affordable energy and efficient telecommunication system.

Mr. Speaker, Sir, creating the fiscal space for priority social and development programmes requires sacrifices. Therefore, as part of the austerity measures to be implemented by the Government, starting in the new financial year on 1st July, 2006, a new transport policy in the public service aimed at reducing transport costs will on a pilot basis, be put in place. The re-organisation of transport and disposal of Government vehicles is expected to be completed by 30th September, 2006.

Mr. Speaker, Sir, as from 1st July, I expect the number of Government vehicles on the road to be reduced significantly and only a few will be retained for use by essential Government service providers and constitutional offices such as the Police Department, health, Judiciary, the Electoral Commission of Kenya and the Kenya National Audit Office.

Mr. Speaker, Sir, Ministers, Assistant Ministers and Permanent Secretaries will be allowed only one official car. To ensure equity, I have factored the savings arising from this measure into my Budget with a view to providing also transport allowance to all civil servants who will not be provided with transport any more.

Mr. Speaker, Sir, before 1st July, the Government will issue further guidelines on the implementation of this policy. Therefore, the Estimates I am laying before this august House have no provision for purchase of motor vehicles for most Ministries. In the case of essential service providers and constitutional offices, I am directing that approval shall be sought from the Treasury before any purchase is effected. This measure will apply to all public bodies and not just the Civil Service. Therefore, from 1st July, no public officials will be expected to use official vehicles to and from duty.

Mr. Speaker, Sir, accelerating structural reforms is critical to maintaining our external competitiveness.

(Loud consultations)

Mr. Speaker: Order! I am sure it has now sunk in. Proceed!

The Minister for Finance (Mr. Kimunya): Mr. Speaker, Sir, in order to use public resources more efficiently, we intend to accelerate the ongoing public expenditure and financial management reforms with a view to strengthening transparency and accountability. The intention is to seal loopholes in our expenditure management system that have been exploited by corrupt individuals. Following the enactment of the Public Procurement and Disposal Law, we shall establish shortly are independent procurement authority. We will also, in consultation with stakeholders, develop indicators for monitoring efficiency and transparency of procurement of the Central Government, including those related to security. The new procurement manual will also simplify procurement procedures.

Mr. Speaker, Sir, in the financial sector, important reviews are under way to further strengthen the financial system. This includes a comprehensive review of the Banking Act; revisions to the Internal Loans Act to bring it to date with recent developments in the financial area; and developing of a comprehensive strategy for our development finance institutions aimed at addressing issues of mobilizing long-term financing for investment and access of credit by challenged sectors such as agriculture.

It is the Government's duty to ensure that Kenyans are not discriminated against in the provision of financial services. However, it has come to my attention that our Muslim colleagues cannot participate in the conventional banking system without violating deeply held principles of their faith. I, therefore, welcome the recent interest shown by some of the banks to fill this vacuum.

Mr. Speaker, Sir, in that spirit, and in order to deepen the financial system by bringing in those Kenyans who have been locked out, I will be proposing to amend the Banking Act to allow for a more differentiated and broader array of banking products and services. The resulting increased competition for funds in the financial sector will, no doubt, lower lending rates and, therefore, provide a further boost to our growth prospects.

Other measures to strengthen the efficiency of the financial sector and expand access to financial services by the poor will include the strengthening of the supervisory capacity of various financial sector regulators, including setting up an independent insurance regulatory authority and introducing legal and regulatory framework for micro-finance institutions.

Mr. Speaker, Sir, an acceleration of privatisation and restructuring of public enterprises is vital for efficient service delivery and strengthening of economic growth. In this regard, we intend to build on the recent highly successful partial divestiture of KENGEN, which has created unprecedented interest in the capital markets and provided an impetus for further divestitures. Specific actions slated for 2006/2007 Financial Year include the restructuring and subsequent privatisation of Telkom Kenya Limited, National Bank of Kenya; the sale of part of Government shares in Mumias Sugar Company and Kenya Reinsurance Company Limited, among others; the sale of a second fixed line licence for domestic telecom

operations, additional licences for international telecom gateways and enhanced private sector participation in port operations, including the container port operations in Mombasa.

Mr. Speaker, Sir, with respect to the framework for governance, while we have made progress in the fight against corruption, the challenge still remains. The Government is committed to upscaling the fight against this vice and in particular, the capacity of institutions like the Office the Attorney-General, the Judiciary and the Kenya Anti-Corruption Commission, which are in the front line of the war against corruption, will be further strengthened through a number of measures, which include the following: The hiring of lawyers and special prosecutors from the private sector as well as from outside the country; reviewing the terms and working conditions of legal staff in the Attorney-General's Chambers; increasing the number of judges and anti-corruption courts, and implementing various governance and anti-corruption strategies.

In this context, the National Anti-Corruption Plan, which has been developed through a process involving a wide cross-section of Kenyans, will be launched early next month. Based on this comprehensive plan, we are finalising our second annual anti-corruption plan that will have measurable indicators to facilitate monitoring of progress.

Mr. Speaker, Sir, the Government will also accelerate the investigation of prosecution of cases arising from the Goldenberg Commission, the Ndung'u Land Commission and the Anglo Leasing scam. Linked to this, the subject of security loan contracts has been of major public interest during the last two years. The contracts have been audited and investigated, and the reports prepared by the Controller and Auditor-General as well as the Public Accounts Committee (PAC) have been tabled in this House. The security loan contracts are also under investigation by the Kenya Anti-Corruption Commission.

As hon. Members are aware, the Controller and Auditor-General and the PAC reports have raised serious concerns of financial management weaknesses that require to be addressed. The Government has, in this context, given its commitment to addressing the issues. We are going to put in place a framework that will close the loopholes that have been exploited in the past to pilfer public funds. I wish to assure hon. Members that in the course of the next financial year, I will table a Debt Management Bill that will address the concerns that have been raised by the public and this House.

Mr. Speaker, Sir, an efficient and competitive private sector is essential for job creation. Therefore, to facilitate trade and expand investment opportunities in our country, I am directing the Kenya Ports Authority, the Kenya Revenue Authority, the Kenya Bureau of Standards, the Kenya Police and other stakeholders at the ports to ensure that services at our ports are provided around the clock, 24 hours a day.

(Applause)

Mr. Speaker, Sir, I have also received complaints about the multiplicity of charges at the port and wish to assure all stakeholders that the charges by the Kenya Ports Authority, the Kenya Revenue Authority and the Kenya Bureau of Standards will be rationalised to reduce costs to importers. I am also aware that the business community has been adversely affected by delays in VAT refunds and this has added to their costs of doing business. To address this issue, the 2006/2007 Budget has provided for the elimination of any outstanding refunds and increased the monthly refund allocations by 46 per cent to Kshs900 million. This amount should cater for all legitimate refunds. We nevertheless intend to come up with a more permanent solution in the course of the financial year so that the problem is resolved once and for all. Priority in processing refunds will be given to input claims that are Electronic Tax Register (ETR) compliant. May I also take this opportunity to warn those with wayward attitudes that we are also taking action in this Budget to curb fake claims by introducing severe penalties for fraudulent claims.

Mr. Speaker, Sir, the framework for sustaining our competitiveness requires that we reduce barriers to business investment and growth. As promised in last year's Budget, the Government has reviewed over 1,300 licences that directly affect trade and investments in Kenya. Hon. Members will recall that at the beginning of the financial year, we proposed to eliminate 37 licences and promised to eliminate a further more in the near future. Accordingly, I propose to eliminate an additional 118 licences which are unnecessary, burdensome, and hence no longer serve a useful purpose. Seven other licences will be simplified and an additional 700 licences will be simplified in the course of the financial year through harmonisation and reduction of fees and charges.

Mr. Speaker, Sir, with regard to local authorities, several licences, permits and other charges have been identified as requiring elimination, simplification and retention. In order to facilitate this process, the local authorities are required to re-submit by 30th September, 2006 to the Minister for Local Government for approval by 31st December, 2006, all their licences, fees, permits and other charges that they wish to retain. I must say at this point that whichever local authority will not have re-submitted the same by 30th September, 2006 for approval will be deemed to have been cancelled. We intend to put a hold to the mushrooming of licences and permits after the elimination process is completed.

Mr. Speaker, Sir, accordingly, I shall create a Business Regulatory Reform Unit in the Ministry of Finance to liaise with the regulators to ensure that all future regulations with respect to licensing conform to international best practices. The unit will develop and implement a medium-term regulatory reform strategy, including monitoring the quality of new licences. To facilitate private sector players, the Government will establish an electronic consolidated regulatory registry for all valid business licences. With regard to these reforms, I will, in the coming months, be introducing in Parliament a Bill on Business Regulation Reform.

Mr. Speaker, Sir, the streamlined business environment will reduce opportunities for rent seeking, lower the cost of doing business and encourage existing investments to expand. In addition, it will lead to initiation of new investment and new employment opportunities. These reforms are intended to transform Kenya into an ideal and competitive investment destination.

Mr. Speaker, Sir, let me now turn to the sectoral and Government development priorities. I will start with the education sector. Let me turn to the specific sectoral frameworks for our development strategy. As you are aware, the Government has continued to improve the quality of universal access to free primary education, by among other things, improving financial management and accountability in schools, rationalising deployment of teachers, targeting bursary to the poor and orphaned, expanding and improving educational facilities countrywide and providing adequate teaching and learning materials in all schools.

Government efforts in this area have resulted in significant achievement in the net enrolment rate; the transition rates from primary to secondary schools and increased enrolment in both public and private universities. However, some weaknesses in the sector remain including misappropriation of funds by some head teachers.

Mr. Speaker, Sir, strict monitoring and evaluation of the funds will henceforth be implemented for all schools to ensure that all resources earmarked for various aspects in support of the Free Primary Education Policy are not misused. In cases where abuses are detected, the Government will take stern corrective actions, including dismissal and taking those involved to court. On post-primary reforms, the Government will continue to provide incentives for the private sector to invest in the expansion of educational facilities. Towards this end, I will shortly announce some tax measures. On the university education, efforts will be made to harmonise regular and parallel programmes, including the rationalisation of tuition fee.

(Applause)

Mr. Speaker, Sir, to demonstrate the importance we attach to education, we have allocated to the sector the bulk of our resources amounting to Kshs99 billion, which is 27 per cent of our total expenditure. Out of this, Kshs71 billion is earmarked for teachers' salaries. We have continued to allocate much of the budgetary resources to this sector on the conviction that education is the most ideal instrument of empowering our youth.

In the health sector, the Government remains committed to providing low cost and accessible health care to all Kenyans. The Government will continue re-orienting policy towards preventive health care provision, including expanding immunisation coverage
while ensuring efficient and effective health care service delivery countrywide.

To achieve this objective, key reforms will be implemented in 2006/2007, which includes improving heath care procurement procedures and accountability systems, as well as strengthening supervision capacity of medical supplies in rural health facilities. We expect this to result in improved access to drugs and medical supplies by our district and divisional health centres.

In order to reach out to disadvantaged groups, the Government, in collaboration with non-state actors, will set up mobile medical programmes targeting vulnerable groups such as people with disabilities and people living a nomadic life. In line with the Government's commitment to achieve the millennium development goals, the share of total resources going to the health sector will increase from Kshs30 billion, which was 8.6 per cent of the total expenditure in 2005/2006, to Kshs43 billion, which is 9.4 per cent of the total spending in 2008/2009. These resources will be used to fund HIV/AIDS interventions, health care infrastructure, affordable drugs and to train the medical staff as part of the initial implementation phase of the National Social Health Insurance Scheme.

Mr. Speaker, Sir, the agricultural sector is a major contributor to our development goals through the creation of employment opportunities in the rural areas where the majority of our people live. Therefore, over the past three years, the Government has implemented a number of structural reforms aimed at improving efficiency and productivity in the coffee, pyrethrum, sugar and the co-operative sub-sectors. I encourage the hon. Members to refer to the Budget Strategy Paper for more details on the reforms we are taking in this important sector.

Reflecting the need to address low agricultural productivity, and to reduce poverty and unemployment in the rural areas, the share of resources allocated to the agricultural sector is projected to increase sharply from Kshs18.6 billion, which was 5.3 per cent of the total resources in 2005/2006, to Kshs33.5 billion, which translates to 7.3 per cent of the total resources in 2008/2009. To enhance support for the sector, we will continue with our efforts to strengthen land management and tenure system, support fisheries, forestry and mining, and protect the environment and natural resources. We are also going to provide additional incentives for the sector which I will be announcing later.

Mr. Speaker, Sir, on the infrastructural development, as hon. Members are aware, the development and maintenance of physical infrastructure is a prerequisite for rapid and sustained economic growth and poverty reduction. Rehabilitating and maintaining our infrastructure is a necessary condition for reducing the cost of doing business and improving competitiveness of our products in the region and in the international markets. To this end, our framework for improving infrastructure calls for a dramatic increase in domestically financed capital expenditure by about 42 per cent in 2006/2007 or from Kshs41 billion to Kshs58.5 billion.

Over the Medium-Term, the share of resources going to the physical infrastructure will rise from Kshs81.7 billion in total, which is 19.2 per cent of the total expenditure in 2005/2006 to about Kshs126 billion, representing 21 per cent of our total resources by the year 2008/2009. We will continue to give priority to expanding and improving maintenance of the road network, providing easy access to water resources and accessing affordable energy. There are notable structural bottlenecks in the implementation of road projects and these delays continue to hold back our economy from achieving its potential. Our people would like to see actual roads and water projects on the ground and not figures in our books.

To this end, and to improve accountability in the Budget implementation, the Budget Monitoring Unit will be revamped and will be charged with the responsibility of co-ordinating development of sector specific benchmarks and monitoring Budget implementation, initially paying particular attention to roads and water programmes. This Unit will be required to prepare comprehensive quarterly reports on Budget implementation for dissemination to the public. The Economic Management Committee of the Cabinet will also enhance its monitoring of the implementation of the infrastructural programme.

Turning to the road transport sub-sector, the Government fully recognises that an efficient road network facilitates development by allowing easier movement of goods, services and people, and by creating linkages between products and markets to promote economic efficiency. To reduce road transport costs, we shall accelerate road repairs and construction by addressing all structural constraints including governance related challenges holding the sector back. To achieve this, I have set aside Kshs15 billion for road programmes.

In addition, private sector participation, including the maintenance of specific urban roads, will be encouraged beginning 2006/2007. To this end, I will propose measures under the income tax to allow private sector players to contribute towards the infrastructure improvement in our country. We are also planning to set up a Highway Roads Authority, a Rural Roads Authority and an Urban Roads Authority.

Mr. Speaker, Sir, it is common knowledge that road contractors take too long to complete new roads and many of our roads are in a state of disrepair mainly due to poor workmanship. This practice in unacceptable. From now on, strict rules and benchmarks will be developed to ensure that contractors deliver their services within the stipulated time and standards. Those who fail to do so, will be blacklisted and will not be allowed to participate in Government procurement.

While contractors have failed us in the delivery of quality roads, we know that this has been done in connivance with our engineers. We have ample evidence of this through the review of the pending bills. Let our engineers who are not ready to reform know that the Government is ready to dispense with them and, if need be, hire expatriate engineers. We cannot continue to tax Kenyans without giving them value for their money.

(A cellphone a rang)

Mr. Speaker: What is that? Can you put off that cellphone, please?

I am sorry, Mr. Minister; proceed!

The Minister for Finance (Mr. Kimunya): Thank you, Mr. Speaker, Sir. Under the transport sub-sector, we expect the concessioning of Kenya Railways services to improve railway transport and facilitate faster movement of cargo through the port of Mombasa. Similarly, we will continue with our efforts to modernize the Mombasa port including introducing private sector participation in the port container terminal operations. Furthermore, to improve the competitiveness of our port, we will initiate work on dredging the channel in order to accommodate large modern vessels. We welcome development partners who want to partner with us on this initiative. Plans to set up a free port in Mombasa will be hastened with arrangments to offer tax incentives to facilitate its establishment.

Mr. Speaker, Sir, on air transport, current efforts to modernize Jomo Kenyatta International Airport (JKIA) will continue and further upgrading and modernization of most airstrips in the country will be undertaken to improve air safety.

Mr. Speaker, Sir, on Information Communication and Technology (ICT), our country needs to do a lot more to reap the full benefits of ICT advancement. These benefits include reduced costs increased productivity and increased employment of our people. In this regard, our framework for improving ICT involves continuing to create an enabling environment for private sector participation, including through further liberalisation of the sector and by investing heavily in E-Government initiative mainly to boost the current strong growth in the sector.

Mr. Speaker, Sir, the Government will in particular facilitate training, ICT research and development and promote value addition services including incubators, tele-centres among others. To encourage rapid growth and create employment opportunity for our youth through sourcing back-office jobs abroad, I will be proposing further tax incentives targeted at strengthening Kenya's position as the regional leader in ICT.

Mr. Speaker, Sir, on the vulnerable marginalised groups and the Arid and Semi-Arid Lands (ASAL) areas, the recent drought has highlighted the need for a stronger response to the vulnerability of our people who live in the marginal areas. The Government is now taking steps to reduce such vulnerabilities on a sustained basis. Although we have a credible early drought warning system, its linkage to an early rapid response has been impaired by lack of funds. Accordingly, the Government in collaboration with development partners, has established a National Drought Contingency Fund to facilitate flexible, appropriate and quick responses to drought emergencies.

(Applause)

Mr. Speaker, Sir, as a sign of its commitment, the Government has allocated Kshs500,000 million as seed money to this fund. In addition, to ongoing drought mitigation initiatives and development programmes, the Government will adopt a comprehensive policy for the sustainable development of the ASAL areas. Towards this end, I am allocating a further Kshs1.5 billion for water programmes in the ASAL areas.

(Applause)

Mr. Speaker, Sir, a large number of Kenyans have in the past been rendered landless by tribal clashes and relocation from water catchment areas. To alleviate their suffering, in addition to the measures being taken by the Government, I am allocating Kshs400 million which in addition to the resources already held by the Settlement Fund Trustees which amount to over Kshs400 million, will be used to purchase extra land for resettling these people.

(Applause)

Mr. Speaker, Sir, the livestock sub-sector is estimated to account for 7 per cent of the Gross Domestic Product (GDP) in addition to contributing to food security. Within the ASAL areas, it accounts for nearly 90 per cent of family incomes. This sector was severely affected by the recent drought. In order to promote the growth of the sector, the Government will continue with aggressive marketing particularly in the external markets. In addition, as hon. Members are aware, the receivership of the Kenya Meat Commission (KMC) has been lifted and the rehabilitation of the factory facility is almost complete. I have, therefore, allocated a further Kshs200 million to make KMC fully operational.

(Applause)

This will create a market for livestock from ASAL areas which besides creating jobs, will begin to address the issue of regional inequality.

Mr. Speaker, Sir, turning on to women-related activities, the Kenya Government is also conscious of the important role our women play in the development of our country. We commit to take further efforts to provide an enabling environment to ensure more effective participation of our women in national development. In this regard, and recognising that women are more likely to be unemployed than men, special attention will be paid to those measures that increase opportunity for employment or access to productive resources for women including access to credit, health care, safe water and education. Priority will be given to provision of portable and clean water within reasonable walking distance in order to reduce the water-related illnesses and time spent by women and girls fetching for water. In addition, we expect the proposed increase in expenditure on health and education to also increase the opportunities for employment among our womenfolk.

Mr. Speaker, Sir, let me also mention that as part of our efforts to enable women to improve themselves and take advantage of the opportunities in the job market, various skills and entrepreneur training programmes will be developed and implemented. Given that the majority of our women live in the rural areas and are mainly involved in agriculture, the Agricultural Entrepreneurship Development Programme will be developed and implemented in the Financial Year 2006/2007.

Mr. Speaker, Sir, turning to our youth, as you are aware, they constitute a large percentage of the Kenyan population and yet they are generally marginalised. Today, young Kenyans are confronted with daunting challenges including unemployment, lack of skills and training, crime and drugs and health problems such as HIV/AIDS. Our "Framework for Youth Empowerment" begins with a commitment in the Financial Year 2006/2007 Budget of substantial resources to youth-related programmes and activities in order to provide them with meaningful economic opportunities.

(Applause)

It is evident that the youth lack skills and access to capital for investment in various productive activities available in the country. Therefore, the Government will establish a Youth Enterprise Fund to enable young people access credit to start or scale up small and medium-scale enterprises and to develop their entrepreneurial skills and create job opportunities. To make this Fund operational, I have allocated an initial Kshs1 billion in the year 2006/2007 Budget.

(Applause)

I wish to encourage Kenyans to assist us in building a brighter future for our youth by making further contributions to this Fund.

Mr. Speaker, Sir, key priority areas of our immediate attention include: rehabilitation and development of youth polytechnics, skill development, including through expanded admissions to the National Youth Service (NYS) and vocational training centres; and youth empowerment and participation especially through career fairs and leadership training, among others. Towards this end, I will be allocating a further Kshs105 million towards the rehabilitation and operations of at least one youth polytechnic in every constituency which will provide a start-up kit including working tools that will be accessible to all youth graduating from those village polytechnics.

(Applause)

In addition, I have allocated a further Kshs50 million for various innovative youth projects across the country. In this regard, I wish to urge our young people living around those institutions to take advantage of this opportunity and acquire the necessary skills for securing a lifetime source of livelihood. I wish also to urge the management of these village polytechnics and vocational training centres to consider organising youth groups under their training and where possible, tender for some of the construction works being implemented under the Constituencies Development Fund (CDF) and I believe hon. Members will give them their full support.

(Applause)

This will create employment opportunities for the youth in the rural areas, reduce the rural-urban migration and level of crime in urban centres.

Mr. Speaker, Sir, as part of the Government commitment to democracy and freedom, I have allocated a further Kshs100 million towards the establishment of the proposed Kenya Youth Council (KYC) which will create a forum for the youth countrywide to discuss matters that affect their socio-economic and political welfare. I have also allocated a further Kshs250 million towards the operations of the National Youth Service (NYS) to upscale their operations, and a further Kshs100 million to scale up the food rations required because of the extra intakes.

Mr. Speaker, Sir, special measures will be taken in promoting the growth of music and the theatre industry alongside expansion of technical and vocational centres. I will refer to some fiscal incentives I am putting in place to encourage music, drama and such entertainment services which are dominated by our youth.

Mr. Speaker, Sir, in line with the Government's commitment to mainstream gender in development, the Government will endeavour to earmark 50 per cent of the proposed funds for the Youth Enterprise Fund (YEF) to support entrepreneurial initiatives by young women. In addition, the Government is currently working on modalities to develop special credit products and incentives to be extended to financial institutions that set aside funds specifically to support enterprising women.

Mr. Speaker, Sir, turning on to frameworks for improving the management of devolved funds, this Government is fully committed to improving the delivery of services at the local level as a way of alleviating poverty, providing increased employment opportunities and reducing regional imbalances. The Government has continued to increase the level of devolved funds for poverty alleviation and local development mainly through the Constituencies Development Fund (CDF), the Local Authorities Transfer Fund (LATF) and the Roads Maintenance Fund (RMF), among other funds.

In the Financial Year 2006/2007, the funds that have been earmarked for the CDF will increase by 40 per cent from Kshs7.2 billion to Kshs10 billion. This is equivalent to increasing the statutory requirement from 2.5 per cent to an upwards of 3 per cent. The resources for LATF will also increase---

(Loud consultations)

Mr. Speaker: Order, hon. Members! Order! The Budget does not end with the CDF! Proceed, Mr. Minister!

(Laughter)

The Minister for Finance (Mr. Kimunya): Mr. Speaker, Sir, the resources for the LATF which is also targeting the same grassroots areas will increase from Kshs5.6 billion in the Financial

Year 2005/2006 to Kshs7.5 billion in the Financial Year 2006/2007. This includes Kshs1 billion from accumulated deposits while those for the overall Road Maintenance Levy (RML) will also increase from Kshs9 billion to Kshs14 billion, to be disbursed partly through the constituencies.

Mr. Speaker, Sir, as hon. Members can see from the Printed Estimates, the resources we have earmarked for each constituency in the form of the CDF have increased by 43 per cent in the Financial Year 2006/2007. On average, it will increase from Kshs30 million to anything between Kshs40 million to Kshs50 million in every constituency.

Mr. Speaker, Sir, of the Kshs14 billion earmarked for road maintenance, Kshs4.2 billion will be allocated for district and constituency roads, with each constituency directly receiving Kshs11 million for roadworks.

(Applause)

I expect that hon. Members will ensure efficient and effective deployment of these funds in order to significantly improve the economic conditions of our people in the rural areas.

Further, to avoid duplication and waste of scarce resources, the provision of the bursary funds and construction of some police posts and health clinics has been shifted from their respective line Ministries to the CDF. I am confident that hon. Members, in close collaboration with the line Ministries and the local CDF committees, will be able to disburse these funds equitably and transparently to fund priority programmes at the local level.

In addition, given the sharp increase in the RML, I have proposed under miscellaneous amendments to reduce the statutory allocation to the Kenya Roads Board (KRB) from 3 per cent to 2 per cent and allocate the savings of the 1 per cent to road improvement and maintenance within the city of Nairobi from where we collect about 80 per cent of our taxes. This proposal will in no way reduce the absolute resources available to the KRB.

Mr. Speaker, Sir, while these funds have improved the lives our people in some constituencies, in others, their managements have come under sharp scrutiny by the public, including some allegations of abuse, mis-allocation and corruption. As part of efforts to ensure efficiency, transparency and accountability in the use of these funds, the Government, in collaboration with the hon. Members, will develop and enforce stringent auditable systems and cases of abuse will be dealt with promptly.

(Applause)

In the meantime, I need not remind hon. Members that we will all be going back to the electorate next year and our management of these resources will be a major criteria by which we will be judged.

Mr. Speaker, Sir, let me now to the financial outturn for the Financial Year 2005/2006. Allow me to briefly update hon. Members on the Budget outturn for the year just about to end. Our total revenues, including LATF were originally estimated at Kshs326 billion comprising Kshs296 billion in ordinary revenue and Kshs29.9 billion in Appropriations-in-Aid (A-in-A). Due to administrative challenges relating to the new customs automation management system and the strengthening of the Kenya Shilling against the major hard currencies, our total revenues are now estimated at Kshs325.6 billion, out of which Kshs291 billion is ordinary revenue and Kshs34.5 billion is A-in-A.

Mr. Speaker, Sir, on the Recurrent Expenditure, hon. Members will recall that the Supplementary Estimates for the Fiscal Year 2005/2006 that were recently approved by this House had Gross Recurrent Expenditures of Kshs400 billion. This included Kshs30.5 billion financed through A-in-A and payments financed directly from the Consolidated Fund Services amounting to Kshs132.5 billion leaving Kshs237.5 billion for discretionary expenditure. The Consolidated Fund Services for the financial year comprised of Kshs28.6 billion for domestic interest; Kshs4.7 billion for foreign interest and Kshs23.3 billion for pensions, gratuities and others. The Supplementary Estimates indicated that Kshs11.5 billion would finance external redemptions while domestic redemptions totalled Kshs64.3 billion.

Mr. Speaker, Sir, on our Development Expenditures, the Supplementary Estimates for the Financial Year 2005/2006 also had Gross Development Expenditures of Kshs92.1 billion including Kshs29.9 billion to be financed through A-in-A. Therefore, Kshs62.2 billion was to be financed from the Exchequer.

Mr. Speaker, Sir, turning now to the financial projections for the coming year, the total revenue target for the Financial Year 2006/2007 is Kshs375.4 billion which represents 21.4 per cent of our GDP. This comprises Kshs336.4 billion of ordinary revenue and Kshs38.9 billion of A-in-A. The targeted revenue is predicated on the on-going reforms in tax and customs administration. We have overcome the teething problems associated with the implementation of the customs modernization reforms and the difficulties with the new Simba 2005. In addition, efforts are also on the way to improve the efficiency of the large taxpayer office.

Mr. Speaker, Sir, as hon. Members have noted from their copies of the Printed Estimates, Gross Recurrent Expenditure for the Financial Year 2006/2007 is estimated at Kshs412.5 billion. This includes Kshs31.1 billion to be financed through A-in-A and payments financed directly from the Consolidated Fund services amounting to Kshs129.1 billion leaving Kshs252.3 billion for discretionary expenditure. The Consolidated Fund services comprise Kshs32.3 billion for domestic interest, Kshs5.3 billion for foreign interest, Kshs22 billion for pensions, gratuities and others, and Kshs133 million for subscriptions to international organisations. In addition, I expect to finance external redemptions amounting to Kshs16.5 billion while domestic redemptions will amount to Kshs52.9 billion.

Mr. Speaker, the Gross Development Expenditures for 2006/2007 are estimated at Kshs137.6 billion. Out of this, Kshs46.1 billion will be financed through

Appropriations-in-Aid (A-in-A) composed of direct project financing of Kshs19.8 billion in loans; Kshs18.7 billion in grants and Kshs7.5 billion in local A-in-A. Consequently, I expect to finance net development expenditures of Kshs91.5 billion from the Exchequer comprising Kshs9.7 billion in grants, Kshs10.4 billion in loans and Kshs71.4 billion from the Government of Kenya.

On External Grants, I have received commitments amounting to Kshs28.4 billion to finance projects. Details of all the donors and projects financed are included in the Development Estimates. I would, therefore, like to sincerely thank all those donors.

Mr. Speaker, Sir, the overall fiscal deficit after the grants will amount to Kshs57 billion. After taking into account the net foreign financing of projects amounting to Kshs9.7 billion and projected privatisation receipts amounting to Khs18.2 billion, this will leave me with a financing requirement of Kshs29.5 billion which will be financed through domestic borrowing. This means that the Fiscal Framework for 2006/2007 is fully financed and there are no financing gaps.

(Applause)

The rest of my Speech outlines the tax measures I intend to take to further remove administrative and legal barriers in order to create an enabling environment for private sector growth. The proposed measures are also intended to address inequality while creating opportunities for the youth to actively participate in economic development. These measures will result in additional revenue of about Kshs1 billion. I, therefore, request that the remainder of my Speech be regarded as a Notice of Motion to be moved before the Committee of the Ways and Means.

Mr. Speaker, Sir, my presentation of tax proposals today groups together the various proposals based on the intended objectives rather than grouping them by the type of tax. I will start by measures aimed at reducing poverty and addressing inequality in our society.

The broad objective of the following set of tax proposals is to reduce poverty and address inequality. First, hon. Members will recall that last year, the Government zero-rated basic commodities such as maize flour, milk, liquified petroleum gas (LPG) and kerosene making them affordable to Kenyans. However, wheat flour was left out. I now, therefore, propose to also zero-rate wheat flour.

(Applause)

I expect the wheat millers to reduce the prices of wheat flour and make it affordable to the consumer so that we can all have our daily bread.

Secondly, Mr. Speaker, Sir, young parents incur a significant proportion of their income on child care and upbringing expenses. To ease the family burden of raising children, I propose to zero-rate baby diapers, napkins and feeding bottles. I am sure that hon. Members in this House will welcome this proposal.

(Loud consultations)

Mr Speaker: Order, hon. Members! Proceed, Mr. Minister!

The Minister for Finance (Mr. Kimunya): Mr. Speaker, Sir, I expect the traders to translate this relief into reduced prices and enable our mothers to access these products for child care.

Thirdly, in order to allow for input tax deduction, reduce the cost of treatment and supply of natural water; and encourage supply of clean water to every home in Kenya, I am proposing to zero-rate the supply and treatment of natural water by all local authorities and public water supplies. **[The Minister for Finance]**

Bottled water, unfortunately, will, however, remain taxable.

Fourthly, increasingly bicycles are becoming a major mode of transport among our people both in the rural and urban areas. In order to create incentives for the assembly and to make bicycles affordable, I propose to remove duty on completely knocked-down kits for bicycles imported by local assemblies.

(Applause)

Mr. Speaker, Sir, fifth, I also propose to reduce the duty on un-assembled kits for motor cycles imported by approved local assemblers from 25 per cent to 10 per cent. This will be for both bicycles and motorcycles.

Sixth, electrical energy costs have continued to adversely affect household budgets. To promote energy efficiency and reduce energy costs on consumers, I propose to remove the duty on energy saving bulbs.

Seventh, to create employment through the promotion of youth talents in sports, music and drama; and to tap our potential that we have in our youth so that they can expose themselves to a wider audience than they currently do, I propose to exempt from Value Added Tax (VAT) entertainment services supplied by our local Kenyan artists.

Eighth, Mr. Speaker, Sir, while the property sector has grown tremendously in the recent past, its share of income tax contribution has not grown as much. To ensure the equity between those who have and those who do not have in our tax system and to ensure that those who derive their income from capital gains that they contribute to the financing our development programmes, I propose to lift the suspension and re-introduce the taxation of capital gains on transfer of property other than road vehicles and marketable securities.

Ninth, as we reduce dependency on donor support, it will be important for all Kenyans to contribute to development of this country. In this regard, I am proposing that in addition to taxing the salaries of constitutional office holders, the housing and entertainment allowances payable to these office holders be taxed like is currently the case for all other Kenyans.

(Applause)

Lastly, I recognise that hon. Members take pride in contributing towards the development of our country. I, therefore, wish to humbly appeal to hon. Members to quickly appoint an independent Committee to repeal the current legal barriers under the National Remuneration Act which denies them this opportunity to make their due contribution through payment of taxes on their house and entertainment allowance.

(Loud consultations)

Mr. Speaker: Order, hon. Members! Proceed, Mr. Minister!

The Minister for Finance: This will allow hon. Members to proudly participate in the development of their country as proud taxpayers like all the other Kenyans.

(Applause)

Mr. Speaker, Sir, I now wish to turn to measures to promote agricultural productivity and reduce poverty. Allow me to now move to incentives intended to promote productivity in the agricultural sector and thereby lead to reduction of poverty. Towards this end, I propose to zero-rate tyres for agricultural tractors and semi-trailers for agricultural tractors. These measures will reduce cost to commercial farmers and boost productivity for their welfare.

Secondly, the cost of transporting unprocessed agricultural produce has been of a major concern to farmers, agro-based industrial players and exporters. I am, therefore, proposing to zero-rate transportation of unprocessed agricultural and agro-forest produce.

Thirdly, in addition to the above measures under the VAT, I am proposing several measures under the Income Tax to support the growth of the agricultural sector as follows. I propose to increase farm-work allowance from 33.3 per cent to 50 per cent. To make our horticultural produce more competitive, I propose to exempt commission payable to non-resident agents for purposes of auctioning horticultural produce abroad from withholding tax.

Fourthly, to encourage the growing of avocados and mangos, I propose to declare them permanent and semi-permanent crops so as to enjoy tax advantage as is available to declared crops.

Mr. Speaker, Sir, on housing, I propose to offer incentives to many Kenyans to build and own homes through mobilisation of personal savings. Currently, the deposits made into a home ownership savings plan, popularly known as "HOSP", by an individual are tax exempt only up to a maximum of Kshs4,000 per month or Kshs48,000 per annum, and for a maximum period of 10 years. I propose to exempt from Income Tax the interest that will be earned on deposits of up to Kshs 3 million by a depositor, who uses these deposits as part of that plan as a first time buyer of a house.

Mr. Speaker, Sir, on education, I wish to reiterate that education is of vital importance to our country. To encourage expansion of learning facilities, and improve the transition rate from primary to secondary schools, I propose to exempt from stamp duty all land that is purchased for expansion and development of schools.

(Applause)

Secondly, to encourage the construction of hostels, especially for our college-going girls, and ensure their safety and to encourage construction of school buildings, I propose to give an industrial building allowance to both hostels and buildings used for educational purposes at an enhanced rate of 10 per cent.

Mr. Speaker, Sir, let me turn to measures to encourage philanthropy and social development. The recent overwhelming response by Kenyans to help those affected by drought shows just how charitable we are, as a nation. There is need, therefore, to encourage philanthropy and offer incentives for private and public participation in social development. First, in furtherance to private-public-sector partnership, I propose to make the cost construction of a public school, a hospital, a road, or any similar kind of social infrastructure to be Income Tax deductible when tax expenditure is incurred with the prior approval of the Minister for Finance.

Secondly, to encourage and deepen philanthropy, I propose to make cash donations in form of cheques to charitable organisations, whose income is exempt from Income Tax, or to projects that are approved by the Minister for Finance, Income Tax deductible.

Lastly, in this category, while our country now enjoys political freedom, we must make deliberate efforts to strengthen political parties, or party politics, by encouraging democratic participation in our political parties. To encourage wider participation in registered parties and promote transparency in political funding, I propose to make Income Tax deductible any contribution by an individual or enterprise of up to Kshs1 million per annum, provided that a contribution is made through guaranteed cheques drawn in the name of a political party.

(Applause)

Mr. Speaker, Sir, turning to the infrastructural development and the capital market, there is need to deepen our bonds market so as to mobilise private sector resources to improve our infrastructure. First, in order to encourager private sector participation in the rehabilitation and maintenance of our infrastructure, I propose to exempt from Income Tax income earned by investors who buy listed bonds as asset-backed security for purposes of developing infrastructure.

Secondly, on the development of the capital market, hon. Members may recall that in 1995, the Government made the legal cost and other incidental costs related to initial public offer of shares Income Tax deductible. I am proposing to extend this incentive to companies which list on the securities exchange without raising additional capital in order to deepen the growth of the stock market. Thirdly, to help deepen the bond market and provide an avenue to mobilise resources for the development of our infrastructure, I propose to exempt from Income Tax interest income accruing from all listed bonds used to raise funds for infrastructure and social services, provided that the bonds shall have a maturity of at least three years.

Fourth, ownership of enterprise, or business, jointly between employers and employees not only improves corporate governance, but also creates incentives for productivity among employees. In order to, therefore, to encourage employers to establish Employee Share Ownership Plans (ESOPs), I propose to introduce legal provisions to determine how the benefits accruing to employees, by exercising the option to own shares, shall be brought to charge.

Lastly, our motorists spend a lot of money and time complying with requirements for road licenses under the Traffic Act. We have calculated that on average, a motorist spends about Kshs300 per day, or approximately four litres, on fuel, which excludes the cost of wear and tear arising from the poor conditions of our roads. In a year, this translates to about Kshs100,000, or Kshs1500 litres of fuel. In addition, we all know that the motorist will spend anything between Kshs5,000 and Kshs10,000 depending on the vehicle on road licenses, which is annual, and more on compliance cost, including waiting and queuing at the Kenya Revenue Authority (KRA) offices, and all other costs associated with enforcement. To reduce the compliance cost incurred by motorists under the Traffic Act, I propose to remove, with immediate effect, requirements for road licences on our vehicles.

Mr. Speaker, Sir, as you have quickly calculated, based on the consumption of an average of 1,500 litres and a licence costing about Kshs5,000, I intend to recover this amount by charging it to be collected under the Road Maintenance Levy at Kshs3.20 per litre with effect from midnight tonight.

(Loud consultations)

Mr. Speaker: Order, Members! Order!

The Minister for Finance (Mr. Kimunya): Mr. Speaker, Sir, while this may appear, on the face of it, to increase the cost of fuel, it works out to exactly what the motorists are spending, but when coupled with other measures within the insurance industry which I will be proposing, the elimination of the road licence and improved roads if calculated, the net result is a huge gain for motorists. I, therefore, do not expect any public transport operators to raise fare on account of this.

This measure will also raise an additional Kshs5 billion in revenue of which Kshs3 billion will be earmarked for roads maintenance thus bringing the total allocation from the current Kshs9 billion to Kshs12 billion. The remaining Kshs2 billion will be used for rehabilitation and construction of new roads. Improvement of our road network should ultimately reduce the cost of private sector and lead to happy motoring for all of us.

Mr. Speaker, Sir, I will now turn to industrial growth and making imported commodities affordable. In order to facilitate faster growth of Information and Communication Technology, create employment opportunities for our youth and make our country a regional leader in ICT, I propose, in keeping the promise and pledge made by His Excellency the President to remove the VAT on computer equipment, computer parts and accessories.

In consultation with the Ministers for Finance for Uganda and Tanzania, we have also agreed on a number of measures designed to improve the welfare of our people, reduce the cost of production and offer some protection to our infant industries. There is a whole list of all those and they are contained within the Finance Bill that will be available. However, some of this include removal of import duties on the following:

(i) Solar equipment and accessories, including the deep cycle and sealed batteries specifically for solar power in order to promote alternative sources of energy and save our forests.

(ii) Filter paper, which is an essential input used in the production of oil, fuel and air filters which are used in the motor vehicle industry. This, further, brings down the cost of motoring.

(iii) Wire of stainless steel and nickel bars, rods, profiles and wire, which are essential inputs for the manufacture of arc welding electrodes used widely in metal fabrication. That should bring down the overall cost of construction.

Mr. Speaker, Sir we have also agreed to reduce the import duties on unprinted aluminium foil from 25 per cent to 10 per cent to give an incentive to local manufacturers. We agreed to increase the import duty on floor coverings and mats from 10 per cent to 25 per cent. In order to reduce the increased dumping of matches in our country and killing of our local industries we propose to increase the duty on matches from 35 per cent to 50 per cent.

Mr. Speaker, Sir, I now turn to the popular subject of excise taxation. The measures that I am proposing under excise duty are intended to address equity concerns and to improve excise tax administration.

First, the current excise tax payable to the Exchequer is only Kshs42 per litre or Kshs21 per 500 ml bottle of malt beer. I propose to increase the excise tax on malt beer from Kshs42 per litre to Kshs48 per litre. This modest increase of Kshs3 per bottle will allow those loyal malt beer drinkers to contribute more towards financing our development priorities as they enjoy their drink.

(Laughter)

Secondly, many Kenyans continue to drink illicit and dangerous alcohol, thereby becoming not only unproductive, but also imposing higher costs on our health care facilities. We have all seen the unfortunate incidents caused by this. Therefore, to make beer products affordable to the poor so that they can avoid the dangerous drink, I propose to remove the excise tax on non-malt beer sold in keg. I expect the industry to reduce the price of these beers by at least Kshs5 per 300 millilitres. I also expect them to expand their production and distribution network so that more Kenyans can have access to good quality beer at the same prices as sodas.

Mr. Speaker, Sir, for your information, the current keg is sold at Kshs20 per measure and we propose to bring that down to less than Kshs15 per measure so that people can enjoy a good quality beer at the same cost as sodas. That way, people will avoid illicit drinks.

(Laughter)

Thirdly, Mr. Speaker, Sir, to simplify and enhance compliance with taxation of wine products, I propose to increase the excise tax on wines from 45 per cent to a hybrid rate of Kshs54 per litre or 65 per cent, whichever is higher. This measure will harmonize all wine products including fortified wines.

Similarly, to improve compliance with excise tax laws under the spirit industry and to ensure equity in our tax system, I propose to increase the tax on portable spirits from the current rate of Kshs100 per proof litre or 65 per cent to Kshs120 per proof litre or 65 per cent, whichever is higher. This measure is expected to create a level playing ground for the alcoholic beverage industry.

Mr. Speaker, Sir, to improve compliance with tax laws and drawing from the successful experience in the cigarette industry, I propose to introduce excise stamps on wine and spirits whether locally produced or imported.

In order to address inequity among cigarette smokers and to raise more resources, I propose to increase the excise tax on category "B" and "D" by 10 per cent to Kshs780 per mille and Kshs1,690 per mille respectively. These excise measures are effective from midnight, today.

Mr. Speaker, Sir, on measures to encourage growth of the financial sector, a strong, vibrant and efficient financial sector is essential for economic development and needs to be encouraged.

First, in the insurance sector, the income received by Policy Holder's Compensation Fund is not exempted from Income Tax. I propose to exempt the Fund from paying Income Tax in line with Investor Compensation Fund and the Deposit Protection Fund, which have similar objectives.

Secondly, the current unlimited level of compensation for Third Party body injuries claims by the insurance companies has made insuring motor vehicles not only costly to motorists, but it has also made business unviable to insurers. To encourage the growth of this sector and to create employment opportunities for our young persons, I propose to limit up to Kshs3 million, any compensation payable by the insurance companies on the third party injury claims arising out of any one claim by any one person. I consider this as a stop-gap measure, while we await for the enactment of a Structured Accident Compensation Bill or a long-term solution to the existing problem.

Thirdly, as a I have pointed above, the motor vehicle insurers have been experiencing a lot of difficulties, some emanating from insurance brokers holding premiums collected on their behalf for 60 days, and in some cases, for more, and in some cases, not even limiting it, while the insurer assumes the risk immediately the premium is paid to the broker, or the cover is issued. To address this and reduce the cost to the insurance industry, I propose, under the Insurance Act, to provide that in respect of motor vehicles and fire insurance business, the broker should remit the premium the same day he or she receives it. This "cash and carry" measure will improve the liquidity of the insurer as well as minimize the risks of the money not being remitted to the brokers, thereby exposing the insured.

Fourth, the current insurance law restricts insurance agents to act for a maximum of three insurers. This also reduces the choice to the insurers as to who they can appoint as their agents. To circumvent this, it has prompted the agents to use different names in order to look for more businesses in the insurance industry. To encourage our talented young school and college leavers to find jobs in the insurance industry, I propose to amend the Insurance Act to remove this restriction. This will enable the agents to act for as many insurers as can appoint them, consistent with a liberalized economy.

Finally, as I mentioned earlier, there is need to broaden the financial sector to allow for more differentiated banking products and services. I am, therefore, proposing to amend Section 53(1) of the Banking Act to allow for the introduction of new banking products, subject to approval by the Minister. These will include products such as Islamic banking, mortgages and asset leasing which are currently not covered by the law.

On measures to improving Tax Administration and Reducing Compliance Costs and to further simplify Value Added Tax (VAT) under the hotels and restaurants, I am proposing to harmonise the VAT rate applicable on all taxable services provided by hotels and restaurant owners at a general rate of 16 per cent.

Secondly, the current tax payers are allowed to recover the cost of their Electronic Tax Registers (ETRs) from the tax payable, but there is no time limit on this. I propose to provide for tax payers to recover the cost of the ETRs from the tax payable by 31st December, 2006. Tax payers who will purchase and instal ETRs after 31st December, 2006, will not be allowed to recover the cost of the ETRs from the VAT payable, but may recover that through investment reduction. They will have to pay out of their own resources.

Thirdly, I mentioned about the fraudulent claims being raised which are delaying the whole issue of assessment of VAT claims for payment. To penalise the tax payers who lodge refund claims that are not genuine, I propose that any registered person who submits a fraudulent refund claim will be liable to a penalty equivalent to twice the fraudulent claim lodged. Such a person will also be prosecuted and imprisoned for a term not exceeding three years or both. This penalty for fraudulent claims applies to all taxes; VAT, Income Tax and any applicable tax.

Fourth, the non-resident withholding tax rate of service providers in telecommunication sectors has been left to the discretion of the tax authority. To remove this uncertainty, I propose to impose a withholding tax at the rate of 5 per cent on the gross receipts by a non-resident service provider whose income accrues or is derived from Kenya.

Fifth, during the last Budget, the employee's contribution to the Retirements Scheme was locked in until the employee's retirement age. This has created some difficulties to some people, especially those who are leaving the country permanently. In view of this, I propose to allow those individuals leaving Kenya permanently to access all their benefits.

Sixth, business deals between foreign entities and related resident persons within a multinational group should be carried out as if there were two independent entities. Determination of "arms length" price has not been clear in the law. In order to bring certainty in the determination of "arms length" price, I propose to publish the Income Tax (Transfer pricing) Rules, together with the Finance Bill.

Seventh, since the introduction of Income Tax leasing rules in 2002, asset financing of equipment and machinery through leasing has increased. The potential for lease financing of saloon motor vehicles is high in Kenya. I, therefore, propose to remove the current restriction that limits tax advantage to asset financing for commercial vehicles. However, in order to safeguard revenue, I further propose that lease rentals will be subject to withholding tax at the rate of 15 per cent of gross sum payable.

Lastly, on this category, up to 75 per cent of the registered VAT payers file nil returns or do not file any returns at all annually, while the 40,000 VAT registrants who have a turnover of below Kshs5 million pay a total of less than Kshs300 million annually. We appreciate both the considerable costs borne by those taxpayers in complying with VAT regulations and the disproportionate costs incurred by the KRA in trying to enforce compliance. To reduce the burden to taxpayers, improve compliance and ensure taxation of small taxpayers conforms to best international practices, I propose to introduce a turnover tax, effective 1st January, 2007, under the Income Tax Act at a rate of Kshs150,000 per annum or 3 per cent of the declared turnover, to cater for this category of taxpayers which shall be a final tax. Consequently, the VAT threshold will be raised to Kshs5 million per annum. This means that any business not earning Kshs5 million per annum need not register for VAT.

Mr. Speaker, Sir, on measures to improve on governance, first, the current law provides that the Governor and Deputy Governor to be the Chairman and Deputy Chairman of the board of directors of the Central Bank of Kenya (CBK), respectively. This arrangement leads to conflict of interest. To enhance corporate governance in the management of the CBK, I propose to amend the CBK Act to provide for the Chairman to be an independent person. In this regard, the Governor will become the Chief Executive of the Bank and will be responsible for carrying out functions imposed on him by the CBK Act. The Governor will then be answerable to the Board of Directors.

Secondly, for a long time the Sugar Development Levy has been levied erroneously as a sugar tax on the consumers, contrary to the understanding of user charge. As a user charge, the Sugar Development Levy should correctly be levied on those who use or directly benefit from the Fund. In order to correct this situation, and to improve governance by ensuring that those who contribute this levy hold the Kenya Sugar Board accountable, I am proposing to amend the Sugar Levy Order to shift the base from the final consumer to the cane growers where it should have been in the first place. This measure will reduce the price of sugar to our consumers, while making sugar farmers vigilant on the utilisation of this Fund. This order will take effect from 1st January, 2007 to allow for the necessary adjustments and consultations with all those affected.

Mr. Speaker, Sir, lastly, a number of companies hold huge amounts of unclaimed dividends attributed to various reasons, including change of addresses of the beneficiaries, and closure of bank accounts, among others. To ensure that beneficiaries do not lose their benefits according to the Limitation of Actions Act after seven years, I propose to amend the Capital Markets Act to approve that dividends that remain unclaimed for more than seven years be paid to the Capital Markets Investor Compensation Fund where the beneficiary will be able to access or claim if he or she resurfaces.

In conclusion, as I noted earlier, the 2006/2007 Budget I have just presented contains the main framework for building a prosperous future for our country. This framework includes;

(i) The shifting of resources to key priority areas such as infrastructure, agriculture, health, education, youth and undeveloped or marginalised groups;

(ii) The deepening of the structural and governance reforms to reduce administrative and legal barriers to create a favourable environment for private sector investments.

(iii) Reducing the poverty and addressing income and regional inequalities through targeted intervention, including through increased spending in rural development and reducing taxes which fall disproportionately on the poor.

(iv) Empowering all Kenyans, and in particular, our youth, through skilled development, and by creating economic opportunities and business environment both in the rural and urban areas.

Mr. Speaker, Sir, the Budget proposals I have outlined this afternoon are intended to lock in the gains in development we have achieved over the last three years. But more importantly, these proposals are aimed at laying a firm foundation for accelerated growth as a means of wealth creation, poverty reduction and equitable social development.

Mr. Speaker, Sir, achieving our shared development vision for a prosperous and democratic Kenya with equitable social development will not be easy. It will require our continued commitment to excellence, persistence, hard work and above all, a strong sense of patriotism. It will also require renewed faith in ourselves, and a passionate conviction that with God's help, we can achieve our best dreams. In my humble opinion, we only need to engage less in politics and more in production, with our eyes firmly fixed on the goal.

(Applause)

As His Excellency the President has time and again reminded us, we should try to ensure that indeed, Kenya becomes a working nation. We should focus on creating opportunities and defining avenues for our people and our companies to assist in accelerating the pace of national development.

Finally, this great nation belongs to all of us. It has a great future. Let us walk together to achieve the Kenyan dream. Our differences should not obscure our collective vision as a nation, which is to strive to improve the well being of all Kenyans. I, therefore, urge each and every Kenyan to play their part in helping to build a truly prosperous Kenya; a Kenya that we shall all be proud to call home.

Mr. Speaker, Sir, I beg to move.

(Applause)

The Vice-President and Minister for Home Affairs (Mr. Awori) seconded.

(Question proposed)

Mr. Speaker: Hon. Members, just before His Excellency takes his leave, I would like to announce that the Minister for Finance has organised for a reception for all of us and the guests at the usual venue within Parliament precincts.

DEPARTURE OF HIS EXCELLENCY THE PRESIDENT

Mr. Speaker: Order! Hon. Members, it is now the pleasure of His Excellency the President to take his leave.

(Hon. Members rose in their places while His Excellency the President left the Chamber)

ADJOURNMENT

Mr. Speaker: Order, hon. Members! That concludes our business for today and the House is, therefore, adjourned until Tuesday, 20th June, 2006, at 2.30 p.m.

The House rose at 4.35 p.m.