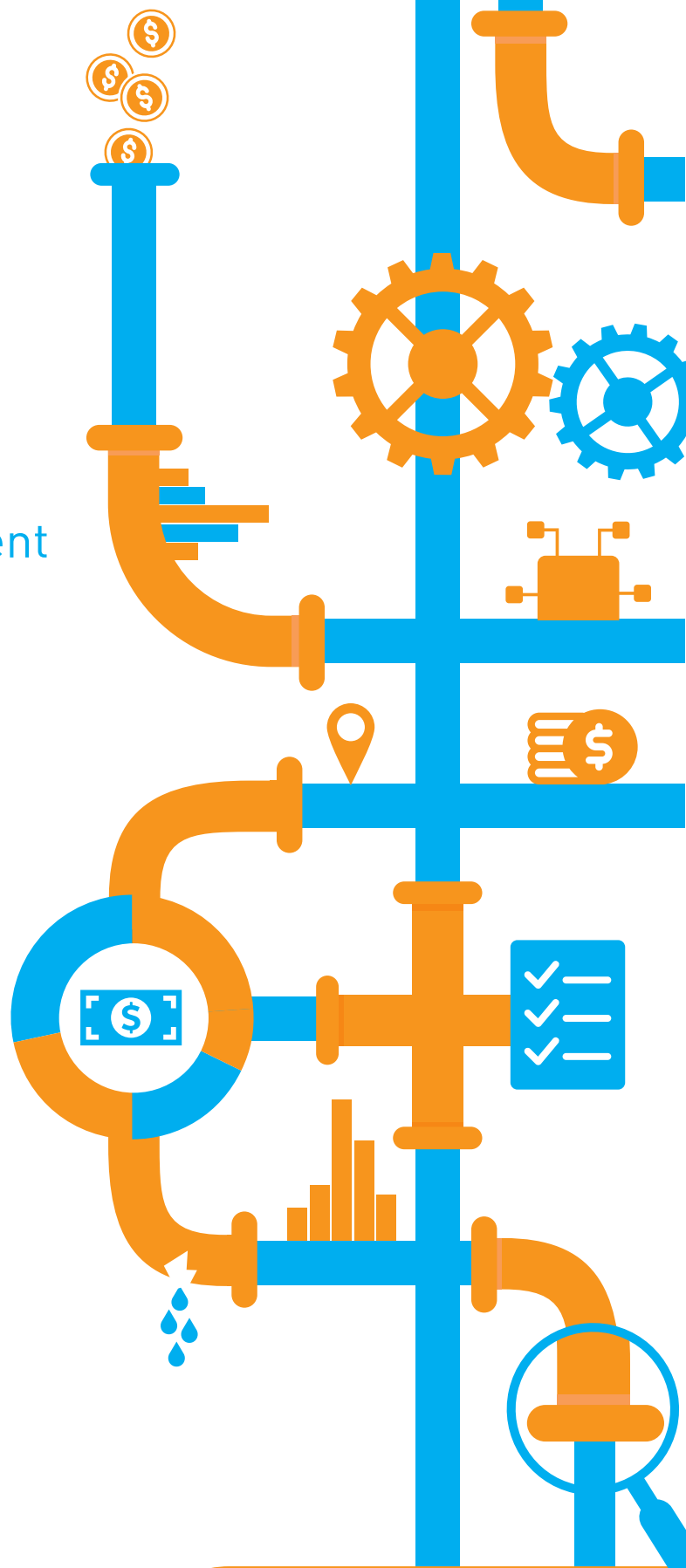


# PIPES, POLICY, AND PUBLIC MONEY

Integrity in Water Sector  
Public Financial Management  
in Kenyan Counties

July 2019

## SUMMARY



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## Foreword

Over the years, the Government of Kenya has formulated financial management frameworks for the public sector in order to improve performance, stewardship and accountability. The legislation ensures responsibility for efficient, effective and ethical use of financial resources within all ranks of Ministries, Departments and Agencies. Government ensures that organisations have a robust financial management framework that assist managers to use resources efficiently and effectively.

Constitution of Kenya 2010 under bill of rights and Kenya's Vision 2030 under the social pillar aims at achieving universal access to water and sanitation. Further, as its development agenda the Government intends to create jobs, achieve food security, spur industrialisation, affordable housing and universal health care for citizen as these are key contributors to economic transformation and development.

In Kenya, water is a finite resource with an annual water availability per capita of about 452 m3 per year with a decreasing trend due to increasing population, expanding economic activities and increasing degradation of catchment areas. In rural areas where service provision is not commercially viable, services are often unsustainable and not adequately monitored or regulated. This requires sector actors to invest more and in a sustainable manner.

National and County Governments recognize that transparent and accountable management of finances and preventing wastage and misuse by public institutions, government-owned corporations and companies, as well as other sector actors is crucial. This is necessary as it ensures investments achieve value for money and result in improvements of the lives of millions of Kenyans who are suffering from lack of access to adequate water and sanitation services. Further this provides confidence to investors that financial resource availed for provision of water and sanitation services are governed through robust legal and regulatory framework and this guarantees continue access to extra financial resources for funding to bridge the gap.

Since early 2000s, the water sector has undergone substantial reforms including decentralization; separation between policymaking, regulation, investment and service delivery. The Water Act, 2016 advanced these reforms under the new dispensation of devolution and is currently under review for harmonization. Guided by the Constitution of Kenya 2010, the Ministry of Water and Sanitation and the Council of Governors through the Inter-Governmental Water Sector Coordination Framework have agreed on the way forward in implementing the reforms. Both levels of Government are committed to strengthen sector coordination, monitoring and reporting, and establish strong government-owned corporations and companies that are able to fulfil their mandates, exercise good corporate governance, accountability and deliver value for money. In doing so, we embrace partnership and collaboration among government institutions and with partners from external support agencies, civil society and private sector.

This study has produced commendable findings and conclusions on how integrity risks are currently undermining effective financial and operational performance in the sector as well as good practices that can be improved. Most importantly, it provides practical recommendations on how to address the challenges and ensure that water sector finances are used effectively and for the intended purposes. The Ministry of Water and Sanitation welcomes these recommendations and in line with its mandate will provide leadership for advancing their implementation.

**Hon. Simon Chelugui EGH,**  
Cabinet Secretary,  
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Chairman, Tourism and Natural Resource Management  
Committee, Council of Governors.



## Preface

Since the early 2000s, the water sector has undergone substantial reforms including decentralization, separation between policymaking, regulation, investment and service delivery mandates. The Water Act, No. 43 of 2016 (Water Act) commenced application on 21st April, 2017 to align the sector with the new dispensation of devolution. These changes have resulted in important improvements in the lives of many Kenyans as coverage of water and sanitation services has increased and service levels improved. However, progress is not yet in line with the envisioned targets due to some challenges still predominant in the sector. The Annual Water Sector Review 2014/15 and 2015/16 in particular called for the Ministry and sector partners to address challenges around sector financing, economic viability of water service providers and governance.

This report contributes to implementing the Ministry performance contracting targets on good governance, prevention of public fund misuse and wastage. It also highlights commendable findings and conclusions on how integrity risks are currently undermining effective financial and operational performance in the sector as well as good practices that can be built on. With respect to devolved mandates, this report forms the basis upon which County Governments will prepare strategies to effectively and efficiently discharge their respective mandate on water and sanitation service delivery. Most importantly, it provides practical recommendations on how to address the challenges and ensure that water sector finances are used effectively, for the intended purposes and provide value for money.

Recommendations address priorities on strengthening sector coordination, monitoring and reporting, and establishing strong government-owned corporations and companies that are able to fulfil their mandates, exercising good corporate governance and accountability and delivering value for money.

The Ministry of Water and Sanitation welcomes these recommendations and in line with its mandate will provide leadership for advancing their implementation. WIN and KEWASNET will continue partnering with the Ministry and other National and County Government Institutions, external support agencies and private sector in supporting this process in order to enhance water and sanitation coverage.

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## Acknowledgements

This report assesses the water sector institutional framework and public finance systems in terms of integrity and governance, identifies risk areas and provides recommendations for addressing them. In recognizing the outstanding role of County Governments in water and sanitation services provision it focuses on the County level and the relations between National and County level institutions.

Above all, it would have not been possible to collect data and information for these findings without the continuous cooperation and facilitation from key partner institutions. We commend the Council of Governors' Water, Forestry and Mining CECs Caucus, Eng. F. K. Kyengo (Deputy Director for Water Services Development Programme, MWS), Eng. Robert Gakubia (CEO, WASREB) and Mr. Ismail Fahmy Shaiye (CEO, WSTF) for providing necessary coordination, guidance and feedback to facilitate the study. Our thanks also go to Mr Edwin Korir (Chief Manager, Internal Audit and Risk Management, WSTF) and Richard Cheruiyot (Inspectorate Services Manager, WASREB) with whom substantive technical discussions took place at the national level. We also thank Mr. Umrbek Allakulov of WIN for his keen review and useful comments.

We deeply appreciate the cooperation offered by the County Governments of Garissa, Kwale, Makueni and Nakuru, including departments and institutions responsible for water and sanitation services, finance, planning, budgeting and public service; and the selected WSPs, WRUAs, CBOs and WSBs in receiving the study team, organising meetings and discussions, field visits and providing information and documentation to the extent possible. Other partners like CESPAD are equally acknowledged for their coordination contribution during some of the case studies.

The report was prepared by a multi-disciplinary study team. We thank WIN and KEWASNET for providing the required financial and technical support to produce this report. In particular, we commend this process as a fruitful collaboration between government and civil society, whereby the study was closely coordinated and validated with both levels of government, while the independence of findings and recommendations was secured.

Lastly, we register gratitude for the professional input and personal commitment of the members of the study team particularly, Mr. Samson Shivaji, CEO, KEWASNET and Mrs. Lotte Feuerstein, Programme Manager WIN for continuous guidance to this study in terms of coordination and content.

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# 1 Introduction

Kenya recognizes the human rights to safe water and sanitation in its constitution and the government has made a commitment to achieve the SDGs and ensure universal access to water and sanitation services by the year 2030. Today however, access to water and sewerage services in areas covered by regulated water service providers have only marginally increased since 2014/2015 and are now reported at 57 per cent and 16 per cent respectively<sup>1</sup>. Public expenditure levels in the water sector are estimated to be only 10 per cent of the expenditure required to meet the targets.<sup>2</sup>

While it is important to increase financing to the sector, it is even more vital to ensure that existing resources are used efficiently and with integrity. This study examines how integrity in public financial management can be strengthened to reduce integrity losses and increase efficiency and WASH sector accountability towards citizens.

The study identifies key integrity risks in public financial management (PFM) systems and practices in the water services sector at county level, and recommends measures which stakeholders can take to mitigate risks and strengthen integrity. The assessment considers to what extent the sector's rules, institutions, and processes for decision-making on the allocation and management of resources are transparent, accountable, participatory, followed, and contain safeguards to prevent and sanction corruption.

The research for this report was undertaken by a multi-disciplinary team, supported by the Water Integrity Network (WIN) and the Kenya Water and Sanitation Network (KEWASNET). The inception phase comprised a desk review of the legal framework and existing reports and national-level interviews to identify key integrity risks for further investigation at county level. The resulting query framework guided further collection of primary national and county documentation and informed case studies of water services in five counties (Garissa, Kwale, Makueni, Migori and Nakuru). The findings and recommendations were validated with water sector actors.

## 2 Context: the Kenyan water sector

### Legal and institutional framework of the water sector: separated functions and decentralized decision-making and fiscal management

The Water Policy (1999) and the Water Act (2002) laid out a progressive approach to developing the water sector, separating policymaking, regulation, service delivery, and resource management functions and establishing accountability lines between them.

The 2010 Constitution of Kenya included water and sanitation services as well as water conservation in the devolved functions of County Governments.

The Water Act 2016 upholds the basic tenets of the Water Act 2002 and realigns the sector to comply with devolution, delegating service provision and development of county assets to county-owned, regulated Water Service Providers (WSPs) for commercially viable areas. At national level, the Act introduces the licensing of WSPs by the Water Services Regulatory Board (WASREB) and the transformation of Water Services Boards (WSBs) into Water Works Development Agencies (WWDAs) responsible for the development, maintenance, and management of national public water works within their area of jurisdiction.

The division of responsibilities, assets, and liabilities, has generated significant debate. In 2019, institutions were still transitioning to the new sector structure. As the WWDAs were only established

<sup>1</sup> WASREB Impact 2017/2018

<sup>2</sup> Kenya Ministry of Water and Irrigation. 2017. Annual Water Sector Review 2014/15 - 2015/16.

operationally after conducting the case studies, evidence from the case studies still refers to the role of WSBs and not the WWDAs.

### New constitution and legislation is increasing transparency and accountability requirements for sector institutions

Key legislation establishing transparency and accountability requirements and creating spaces for public participation in how all public entities (including national and County ministries, departments, and agencies) allocate and manage public money include the Public Financial Management Act (PFMA, 2012), the Public Procurement Asset Disposal Act (2015) and the County Governments Act (CGA, 2012). By law, counties prepare three-year medium-term fiscal frameworks and detailed budgets. These budgets are linked to County Integrated Development Plans, and structured according to the national programme structure, the county administrative structure, and the economic classification structure of the Standard Chart of Accounts (SCOA). There are strict requirements for disclosure of county budgets and for participation in their development. County budget implementation is managed through an Integrated Financial Management Information System (IFMIS). The Controller of Budget reviews quarterly reports of all national and county ministries and departments, and compiles a Controller of Budget Report. The Controller has powers to stop disbursements. The Auditor General checks whether public accounts are compliant with regulation.

**State corporations** exercising key mandates at national level like WASREB, the WWDAs, and the Water Sector Trust Fund are subject to transparency and accountability requirements as per the revised State Corporations Act (2016) and the Mwongozo Code of Governance. The board of the corporation is accountable for the proper management of its affairs, including its financial affairs. State corporations have to submit annual expenditure estimates to the relevant minister and the finance minister for approval, and are subject to the Public Audit Act.

WASREB recommends that **WSPs** be set up as public limited liability companies. As such they must comply with the revised Companies Act (2015) and WASREB regulations. The Companies Act provides a framework for the relationship between WSPs and counties that is framed in corporate governance terms and not public financial governance terms. It nonetheless includes key aspects of financial transparency, the right to information, and the right and duty of counties as the shareholders in the company to hold the directors of a company to account. As public limited liability companies, WSPs do not have financial privacy. Because their shares can be traded, their financial accounts, statements, and directors' reports must be filed with the Registrar of Companies *and* published. They must hold annual general meetings of company shareholders. The WASREB Corporate Governance Guidelines for WSPs sets out that the shares of county WSPs must be held *ex officio* by the county secretary, and county ministers of finance, and water and sanitation. A separate class of shares with more restricted rights should be held by stakeholders from public and private registered institutions in the area covered by the WSP.

In practice, however, many WSPs were established as private limited companies and their articles of incorporation specify their shares are held by WSBs. Not all of these WSPs have made the transition to public limited liability companies with shares held by counties. Private limited companies have more financial privacy. However, they are still required to file financial statements and directors' reports with the registrar, but these do not need to be published. Both public and private limited companies must be audited by a qualified auditor.

### Water sector expenditure and financing

The main source of financing for the overall water sector, and also for the water services sub-sector, is nationally collected revenue, followed by tariffs/user fees. The financing flows are complex and fragmented. They are more difficult to track than in many other sectors, as separate water departments as such do not exist, and expenditure usually is fragmented between two or more county ministries.

Water sector budgets have increased significantly since 2013, but these increases are in large part due to increased allocations for the drainage and irrigation sub-sector. A national government assessment of sector financial resources has found that projected allocations are insufficient to meet requirements and



increasingly so.<sup>3</sup> Still, across counties, actual expenditure is much lower than budgeted expenditure due to a combination of lower disbursement from the treasuries and low absorption capacity.

In 2015/16, nearly 90 per cent of public expenditure in the water services sector went to capital projects; only 8 per cent was used for recurrent purposes. A large proportion of the recurrent cost of water service delivery is financed through water tariffs, highlighting the importance of WSPs having functional revenue collection systems. For this study, more than 60 per cent of the reporting WSPs were either not able to cover their operation and maintenance costs through their revenue or did not have credible data. WSPs reported a turnover of about KSh20.67 billion (approximately USD 200 million) to WASREB for the 2016/17 fiscal year.

### 3 Main findings: integrity risks and emerging accountability reinforcements

The water sector in Kenya is exposed to multiple, coinciding integrity risks. While lack of resources is often blamed for large numbers of people not having access to basic levels of water and sanitation, slow and variable progress against SDG6 is also seen to be the result of weak governance, management, and coordination of resources, leading to efficiency losses and integrity risks.

Varied integrity risks have been identified through this study. Many of these integrity risks in the water services sector at county level, including those associated with the companies or other institutions involved in water services provision, arise from two main sources: the implementation of and compliance with the 2016 Water Act, and weaknesses in the governance capacities of water services providers. These two factors also affect the ability of county governments to oversee WSPs properly.

#### Public disclosure and public participation

County governments are not consistently publishing and posting online all the key planning, budgeting, and reporting documentation required by law though they have created websites and published a number of documents. Information on request is not easily obtainable. Nonetheless, over the course of the study, positive developments were observed as audit reports that had been delayed by more than a year were brought up to date and made available. The water sector is neither performing particularly weakly nor strongly in that regard, as these challenges apply to all sectors.

County governments are making efforts to improve public participation approaches especially during planning, and there is some evidence of meaningful links between public participation and operational and budget decisions. There is also evidence of high demand for water projects from citizens. However, in some cases where water services infrastructure was not handed over and instead managed by WSBs, participation processes were non-existent or weak, as the same requirements for public participation do not apply to these bodies as they do to counties.

In two of the county case studies, technical departments manage public participation processes enabling the link to budget decisions quite effectively. When participation processes are run by non-sector personnel, such as the planning bureaus of the counties, without proper technical guidance, their effectiveness for the quality, efficiency, distribution, and sustainability of water services can be undermined. For example, the technologies selected for projects on community insistence were in some cases inappropriate or sub-optimal in terms of wider county infrastructure processes and economies of scale. In other cases, feedback from county officials on community concerns and proposals was weak.

Legislative processes can also affect the results and quality of participation and increase accountability risks. For example, citizen preferences that were articulated during budget preparation and taken up in budgets, might be overturned when the budget is debated in the County Assembly, on account of

<sup>3</sup> Ibid.



narrow-interest lobbying by parties or pro rata distribution of available capital budgets. While there was no explicit evidence of instances in the water sector where these issues occurred, they are seen as a risk for overall county expenditure. A second issue noted by respondents is that some County Assemblies run participation exercises of their own which are not well coordinated.

All the factors mentioned above mean that at times communities are unclear why they are participating, when, with what ends, and for which decision-making processes – creating a high risk for community fatigue. On the other hand, the capacity of citizens for meaningful participation is still weak, as knowledge of the budget process is low, which often results in participation being limited to the planning stage.

## Roles and rules

Most interview respondents noted that the shift in sector roles combined with devolution of expenditure responsibilities have resulted in poor understanding and operationalization of water resource management, water service delivery, and oversight roles and responsibilities in practice. This lack of clarity and understanding is the main issue affecting integrity in the sector as it has not allowed solid new practices to develop in a changed context. This is partially due to murky distinctions in the laws themselves, and also to conflicting interpretations of the laws, driven by competing interests in terms of mandates and control over resources.

The study found examples where water services infrastructure was not handed over and instead managed by WSBs. Furthermore, in all counties studied, WSBs solicit funds to establish water works despite being detached from their consumers and with only limited involvement of WSPs or county governments in the latter stages. Relationships between counties and WSBs can be fraught, as WSBs hold onto water service provision roles. The management of donor financed projects has not clarified the situation. Cases were found where donors still opted to channel funding for county water services infrastructure through the WSBs rather than WSPs.

The issues are primarily about the availability and use of resources and accountability for assets and liabilities. The process for transferring existing (pre-Water Act 2016) assets and liabilities from the WSBs to the WSPs and/or WWDAs is not clear. National government interests differ from those of the county government and WSPs in these matters. National government expects the county governments/ WSPs to accept all liabilities attached to transferred county water works. County governments argue that they cannot accept this because a) the WSPs are unable to repay the loans and b) the assets may not be worth the liabilities attached to them as there may have been mismanagement by the WSBs in their development. Lack of registers of these assets further complicates the situation. The study found instances where WSPs had to lease assets in addition to buying bulk water from WSBs or were expected to take on debt before assets were complete, contributing to their cost coverage challenges.

Counties also distrust WSPs (which in some cases still see themselves as WSB-linked bodies) and therefore are less willing to provide full support. Apart from offering ad hoc subsidies to WSPs, counties hold on to water infrastructure development projects and the resources associated with them, further muddying the waters as to who is responsible for services in the eyes of users and citizens. Weak coordination between counties and WSPs on infrastructure and service delivery mean that WSPs run into solvency and cash-flow problems, putting pressure on counties to provide emergency bail-outs. The regulatory framework for asset development by WSPs and for direct financial support from counties is not clear, resulting in ad-hoc measures that do not address underlying problems.

The fact that asset management systems are weak complicates the picture. The asset management systems are still manual. One system is managed by the finance ministry and the other by the spending agency. WSPs are responsible for water services asset management, and county governments are required to form cross-sectoral asset management committees, but these rarely exist. In the case study counties, neither water departments nor WSBs maintained good asset registries for the sector. Such registries would be critical for tracking the transfer of assets from WSBs to WSPs and their management in WSPs.

In remote areas and in areas beyond the service provision areas of WSPs, many schemes are managed by bottom-up community-driven organizations that are registered as self-help groups and not as proper

associations. These groups often operate in isolation, are not aware of regulatory requirements, and very rarely have any formalized arrangements with county governments or WSPs, let alone WASREB. This means they operate in regulatory limbo, informally and with weak accountability arrangements. The situation poses a significant challenge to the ongoing operation of the community groups and their integrity.

In all case studies, the study found instances where Water Resource User Associations (WRUAs) were also taking up water service delivery responsibilities without realizing that this was outside their mandate. WRUAs are recognized in the Water Act 2016 as having a mandate for collaboratively managing water resources at sub-catchment level, but not for service delivery. Not all WRUAs were able to provide the paperwork on their licensing and some were even unaware of licensing requirements. Generally, the division of roles between community water supply organizations and WRUAs is not clear to communities or the WRUAs, which further weakens accountability and contravenes the separation of water resource management and service delivery functions established by law.

### Accountability lines

There is confusion around whether WSPs are seen or see themselves as accountable to county governments, WSBs, or WASREB. The 2016 Water Act makes WASREB the regulatory authority for WSPs. The County Governments Act 2012 makes supervision of service delivery a function of the county executive. Actually, the status of WSPs as (public) companies means that WSPs' management is accountable to their boards, and that directors are accountable to shareholders, which should be - but in practice often are not - county governments. There was however evidence that the separation of management and oversight duties between the WSP and its board is not always clear. Some boards for example sign off on checks. In all case studies, county treasuries and water departments are at least represented in the WSP board of directors, giving them a direct pathway to exercise oversight. However not all county governments use this channel effectively.

Counties are also unclear on WSP accountability. County officials who were interviewed were not certain to who WSPs should report, how they should budget and report, how to sanction any breaches, and whether they could impose standards and implement systems via seconded staff. As a result, counties were not aware of the full extent of WSPs' funding. The lack of continuous access of counties to WSPs' financial information raises the risk that funds will be misused, particularly as transparency to the public on WSP finances is also poor.

The public tends to hold county governments responsible for water services, accountability for WSPs is generally weak. Furthermore, weak links between county planning and WSPs investment plan processes lead to WSPs' projects not being made transparent to rights' holders (customers/citizens) via counties. As WSPs themselves are much less transparent with regards to their resources and their use than counties, and have not invested much to develop participative planning and budgeting mechanisms, the result is lack of social accountability.

Combined these issues create pressure on counties to bail out WSPs facing financial difficulties or intervene in WSP affairs in other ways, such as dismissing executives and board members, setting the pace for 'cleaning out' bloated WSPs, and drafting legislation for sector governance. While such interventions in many cases take place for good reason, sanctions were exercised by direct intervention of the governor, instead of county governments following due processes. Where legislation has been drafted, concerns are that the county is overstepping its mandate in some cases.

There are emerging examples of sanctions for integrity breaches through statutory accountability bodies such as the Ethics and Anti-Corruption Commission (EACC), via counties that have intervened with WSPs to strengthen governance and management, and via county assemblies that have raised queries, investigated misappropriations, and summoned officials to account. Even so, informal systems, local culture, and the local political economy can result in sanctions not being applied.

### Systems and capacities of Water Service Providers

A key research question was whether the setup, proceedings, and practices of WSPs and providers of water services outside of WSP areas, are in line with the provisions of the various acts to safeguard

integrity. The study found weak WSP revenue management, budgeting, reporting, and oversight systems and weak WSP capacity, which translate into material risk of misuse of funds and/or power. There are two major areas of risk: weak technical systems and weak capacity.

The technical systems of WSPs to collect and manage revenue, control expenditure, and control procurement are weak. In many cases, these systems are still manual with clear integrity risks. Billing systems, for example, are often not automated, with a commensurate effect on the effectiveness of these systems but also on their transparency and the accountability of revenue. Issues with vandalising meters and unmetered water usage are common. There are however also good examples of the use of modern technology (including M-Pesa and electronic meter readings) to improve revenue collection and management systems and reduce the risk of inefficiencies and corrupt behaviours.

There was little evidence of WSPs getting sufficient guidance and support from counties to boost their financial management capacities. Indeed, counties typically lack the necessary skills themselves. Nevertheless, there are instances whereby counties have attached/seconded staff to the WSPs. Some WSPs interviewed were staffed in alignment with the WASREB norms. Others were under- or over-staffed. Attracting and retaining sufficient skilled and experienced staff is a common challenge.

Donor funded projects can boost the systems and capacities of WSPs, as they often come with investment in financial and project management systems. These are however often only used for managing donor funds, losing the opportunity to also build the underlying WSP systems.

### **Systems and capacities of counties for public financial management**

The county case studies confirmed desk review findings that internal control, accounting, procurement, and record-keeping at county level were still weak and posed integrity risks. Many counties face a dual problem of overloaded wage bills and lack of key skills experienced staff for specific functions such as planning, budgeting and monitoring, internal auditing, and procurement. There is significant evidence that weak technical capacity at county level prevents full implementation of integrity system requirements under the law.

The implementation of programme budgeting is generally weak at county level. Counties typically submit and approve manually-prepared programme budgets, which may not exactly match the programmes coded in the Integrated Financial Management Information System (IFMIS). Variations in the use of the prescribed programme structure over time within and across counties limit ability to compare. That these variations are not fully updated in SCOA furthermore means that even within a fiscal year, budget structures will differ from actual expenditure structures, limiting analysis, and the ability to hold counties to account in-year. This undermines coherence between policy and implementation, the reliability of reported information, and the ability to hold departments and office holders to account.

In relation to procurement, issues noted are that interpretation and understanding of the procurement law are limited; procurement processes are weak with poorly managed and controlled selection of vendors, low use of price benchmarking, and weak management and record keeping of deliveries and stock. The interviews for the study also raised issues of collusion between vendors, of the expectation of interference and kickbacks deterring credible bidders, and of delays in payment having the same effect.

Internal auditing is another key area of risk. While the study found evidence of internal audit taking place in counties, capacity and incomplete roll-out were a problem. In some cases, the deployment of internal auditors to departments and other entities was incomplete. Operational internal audit systems are not complete or harmonized, as county level audit committees are not necessarily formed and neither post-audit nor pre-audit practice is followed. None of the counties visited by the study had formed audit committees.

Many of the internal control and accounting weaknesses are associated with systemic weaknesses in the transversal IT systems used in PFM processes. While the study found positive examples where the national transversal systems have enhanced counties' capabilities for internal control, accounting and reporting, the study overall found that significant challenges remain within the design and implementation of the systems. The systems are not tailored to county needs, resulting in high risk

practices for accountability. For example, the standardized national coding for revenue sources and expenditure is not adequate for county needs, forcing off-system working which is then not captured well, resulting in inaccurate or incompatible reporting when inconsistencies then occur between budget documentation and IFMIS. Project definitions are not clear, so that some expenditure that should be planned and reviewed as projects is not. Generally, this creates an environment in which expenditures can be left out of reports and review processes (such as of the Controller of Budget) arbitrarily.

The weaknesses are partly confirmed by the Auditor General reports for all five counties for 2015/16. In these reports, the Auditor General expressed a disclaimer of opinion, meaning that the auditors were unable to obtain sufficient appropriate audit evidence to support a finding on the financial statements. The audit findings that directly relate to the water sector signal a breach of internal controls and due process, particularly in the procurement process. Reports from EACC and national level interviews strongly indicate that these weaknesses are symptomatic beyond the case study counties.

In summary, public financial management and public accountability weaknesses are mutually reinforced at county level, and strongly affect the governance of water services.

WSPs emphasize that they have insufficient clarity on where to account for their activities and finances, a situation caused at least in part by incomplete transitions from previous accountability lines to new accountability lines. County governments are unclear on their rights relative to WSPs: some counties intervene heavily (but do so without a clear regulatory framework), others keep WSPs very much at arms-length. Capacities are limited, and full understanding of governance duties of county level water suppliers is lacking. The financial management systems of WSP and community water suppliers for receiving tariffs, managing expenditure on services and safeguarding assets are weak. All-in-all the system in practice is plagued by weak systems, weak capacities, and in weak oversight of WSPs by counties, with accompanying integrity risks.

On average, citizens have either no, poor, or late information on water sector budgets and expenditure by counties due to weaknesses in public financial management systems, and are not well capacitated to demand better information, creating incentives for better management of resources. Within counties, weaknesses in upstream and downstream management of county resources for the sector create integrity risks for investment in and the management of water services assets. Factors include human resource shortfalls, mismatches between nationally designed transversal systems, and county-specific needs. While this does affect integrity in the sector, it also has significant implications for the efficiency of financial resource use, with commensurate impact on access to water services.

## 4 Recommendations

In selecting recommendations, the team favoured interventions that are most urgent or most likely to have an earlier impact, shifting the integrity and service delivery outcomes in the water services sector.

**Recommendation 1: National government agencies should issue national, cross-county guidance on public investments, financial management, and reporting in the water sector, including for WSPs.**

- **Clear written guidance and training from national agencies** is essential for clarifying to counties how they should instruct WSPs to budget and report, with clear templates for each. The MWS together with WASREB should take the lead in developing these sector-specific guidelines and training packages, with the National Treasury ensuring alignment with PFM legal frameworks, regulations, and formats. Where there are conflicting formats or non-aligned accounting practices, the Public Sector Accounting Standards Board needs to clarify this in collaboration with Government Investment and Public Enterprises (GIPE) department of the Treasury.
- **The National Treasury, through the Budget Department and Public Investment Management Unit, must provide clear systems, guidance, and training to enable counties to comprehensively budget, monitor, and report on individual projects within the IFMIS system** and in line with the PFMA and (draft) Public Investment Management guidelines. The systems should enable county governments to provide information on the implementation of individual projects in clear and accessible formats

- to stakeholders and citizens, including projects financed by development partners.
- **The National Treasury and WASREB should provide guidance on procedures and conditions/sanctions on bailouts and emergency financing of WSPs.** Counties should be responsible for implementing the guidelines, and for issuing county-level guidance to govern the process for bailouts and to regain some control for the county. WASREB and relevant National Treasury departments (including Budget, GIPE, and PIM) should contribute guidance for these procedures.
- **Similarly, there should be guidance on when WSPs' operations and maintenance (O&M) costs may be subsidized.** WSPs' subsidies for O&M should be based on a strict programme with time frame and guidance from WASREB, geared towards sustainability while ensuring equitable access to water and sanitation services. Financing to WSPs should be primarily for investment in infrastructure, so that they expand their service delivery base.

**Recommendation 2: The Ministry of Water and Sanitation and the Council of Governors should agree on a clear division of roles and responsibilities in the development and management of water and sanitation infrastructure, including a timeline, process, and support mechanisms for transfer of responsibilities, assets, and, liabilities from WSBs to counties/WSPs and WWDAs.**

- In line with the provisions of the 2016 Water Act, MWS should consult stakeholders, most importantly the county governments (through the Council of Governors) and the WSPs (e.g. through WASPA), on the roles and responsibilities of the newly gazetted WWDAs and their relations and coordination mechanisms with county governments and WSPs in terms of asset management and development, including establishing and agreeing on clear definitions on what constitutes national and county public water works.
- MWS, Treasury, and CoG must agree on appropriate criteria and process for transferring ownership of existing assets and attached liabilities from WSBs to counties/WSPs and WWDAs (including criteria for determining which assets will become county assets held and managed by WSPs and which assets will be national assets managed by WWDAs; the process for registering, valuing, and legally transferring assets and liabilities to these entities; and potential financial support mechanisms for WSPs to serve liabilities for assets transferred to them).
- MWS, Treasury, CoG, and donors must agree on appropriate arrangements and coordination mechanisms for transferring loans and grants from ongoing external support programmes from WSBs to counties/WSPs and WWDAs, as well as for future external support programmes.
- MWS, WASREB, and WSTF in collaboration with CoG and development partners need to set up capacity development programmes to support WSPs in operationalizing their new role in management and development of county water supply and sewerage assets (including a review of needed capacities and possible hiring/secondment of additional staff).
- **Donors, WSTF, MWS, and counties must not provide funding for infrastructure development without ensuring engagement of the actors which will be responsible for managing related services.**
- **Counties should respect the clear separation of responsibilities between government (both national and county) and the management of water services and development of county assets for water and sewerage services by the WSPs, in line with capacity strengthening undertaken by the MWS, WASREB, and the WSTF. This means they should allocate budgets to WSPs to support the development of infrastructure, rather than developing infrastructure as county projects.**

**Recommendation 3: National and county governments must operationalize and align national sector oversight, monitoring, reporting, and coordination mechanisms.**

- MWS and CoG urgently need to operationalize the Intergovernmental Water Sector Coordination Framework and clarify how it will relate to existing multi-stakeholder sector monitoring, reporting, and coordination mechanisms such as the Annual Water Sector Conference and the Annual Water Sector Review. In consultation with the Ministry of Health, the framework should also integrate issues of management and governance of sewerage, onsite sanitation services, and faecal sludge management to prevent further fragmentation of the sector. Such sector reporting and coordination mechanisms should take into account the budget cycle for timing, and seek to actively involve public finance actors.
- MWS and MoH need to agree on integration of existing sanitation sector monitoring, reporting, and coordination mechanisms into such a framework, so as to prevent further fragmentation of the sector and ensure integrated management and governance of sewerage, onsite sanitation services, and faecal sludge management.



- MWS and WASREB need to ensure better data on water and sanitation investments and delivery of services in areas which are not served by the professional WSPs in national sector reports.
- **National state departments, regulators, and other state corporations responsible for water supply and sanitation and water resources management must work with the county governments to provide comprehensive guidance on the interlinked roles of WRUAs, water users associations (WUAs), service providers** (bulk water providers, county WSPs, community-based organizations, and private operators), and communities. They must ensure access to full guidance and training materials for these actors to support the understanding and establishment of the full necessary system of institutions required for communities to have functional and sustainable water management and provision.

**Recommendation 4: County governments, WASREB, and other actors must operationalize and strengthen oversight, monitoring, reporting, and coordination mechanisms of water and sanitation service provision at county level.**

- **WASREB and counties should establish a formal line of communication with established focal points for each county and dedicated staff in WASREB to rapidly respond and engage counties on regulatory issues.** This line of communication is seen as essential to pre-empt and avoid regulatory misunderstandings or misapplications.
- **WASREB and county governments should agree on, implement, and institutionalize mechanisms to coordinate regulation and oversight of the WSPs.** This would entail a dedicated approach from WASREB to systematically and consistently engage with county governments to enhance the oversight capacity of county officials (such as following due process when terminating senior WSP officers or clustering WSPs).
- **County governments with guidance and support from WASREB should put in place accountability arrangements and monitoring systems for actors with delegated water service delivery functions in areas where such services are not commercially viable.**
- **County water departments should convene coordination meetings with other water sector actors at county level.** These meetings should systematically coordinate the development and operation of water and sanitation facilities throughout the planning, design, implementation, commissioning, and handing over of projects among the concerned institutions (e.g. county water departments, MWS, WASREB, WSB/WWDAs, WSTF, development partners, and CSOs) on one hand, and with the operators (such as WSPs, CBOs, and CSOs) on the other.

**Recommendation 5: Water sector actors must ensure quality and consistency in public participation and improve institutional coordination in mobilizing communities on water and sanitation issues and decision-making.**

- **Building on a coordination platform at county level, national institutions like WSTF could also make use of county and WSP public participation mechanisms in the planning of their infrastructure projects to lower the burden on communities and institutions.** WSPs, WWDAAs, WSTF, and other water sector actors should liaise more strongly with county planning departments to ensure the quality and alignment of their public participation processes.
- Public participation processes need to be combined with citizen education and guided by technical expertise to ensure they result in technically feasible and financially sustainable infrastructure and services. Communities should set priorities in terms of services they want and be consulted on technical designs, while technical departments should lead the decisions on technical options. CSOs should support these processes and engage with WSPs and county governments to sensitize and mobilize communities on water and budget issues.
- **WASREB and county governments can also provide guidance to WSPs on how to align and harmonize WSP public participation interventions,** mainly on tariff setting, with county budgeting and investment processes to ensure investments are responsive to O&M and consumer needs, as well as quality considerations.
- **CSOs specialized in water and in public finance should work with CBOs, communities, accountability institutions, and media to activate public oversight in budget execution and reporting, and maintain its quality and consistency.** Donors should support such processes. CSOs in water and in public finance need to:
  - Coordinate the CSO voice, demanding full disclosure of budget and financial documents.

Coordination with actors outside of the water sector may strengthen the advocacy as many of the county documents are not water specific.

- Demystify and analyse budgets, break down issues, and interpret the data for community leaders and other actors.
- Use their analysis to engage citizen organizations, communities, the media, and other non-state accountability actors in the scrutiny of financing and service delivery, engaging state and service delivery actors and demanding feedback, further disclosures, or changes in policies.

**Recommendation 6: County governments with support from WASREB must ensure that the boards of WSPs possess necessary expertise and knowledge, understand their role, and be appointed through due process.**

- **CECMs responsible for water and finance should appoint qualified staff from their respective departments into the boards as members**, to ensure expertise and the doctrine of separation of powers, as reports are presented to them and issues are raised, including on the performance of the BoDs, as per their supervisory/oversight role.
- **Other board members must apply through public advertisements**, to represent the other sector stakeholders in complementary technical areas (including social, legal, and business). In selecting board members, county governments have to ensure adherence to WASREB corporate governance guidelines for the WSPs.
- **WASREB and CoG with support from development partners need to set up capacity development programmes for boards that include induction on corporate governance, integrity, and risk management, and monitor their performance, including these aspects. Development partners should support this process and CSOs should seek to strengthen public oversight of the performance of state corporations and their boards.**
- **While this study focuses on the county level and WSPs, the recommendation applies to the boards of national state corporations under MWS (in which case MWS and SCAC would be in the lead).**

**Recommendation 7: County governments should pay immediate attention to improving transparency for more effective formal public and social accountability.**

- County governments should proactively improve and maintain transparency in budget preparation, approval, and reporting.
- They should seek to incrementally ensure that they meet legal transparency requirements and disclose budget documents and report on their website.
- Given the intensity of the preparation of budget formulation and implementation documents and the frequency of publication required, county governments should consider setting up a separate team (possibly with initial technical assistance support) to publish all required documentation in a continuous manner, rather than depending on the Finance and Planning Department teams who are always burdened by ministries' routines.
- County governments should sensitize county assemblies (CAs) through the committees in charge of budget and water, and where needed put in place a more strategic resistance to ensure pro rata assignment of development funds.
  - There are compelling arguments around delivery, which can be made in favour of a pro rata (i.e. in line with population density and need) and fair approach to 'equity', and the planning, budgeting, and finance department as well as sector departments need to be able to make these firmly, and explain the reasons through budget documentation and public participation processes.
  - CAs should not alter budget proposed by county executive committees (CECs) beyond more than 1 per cent (as per section 37 of the PFMA Regulations), so as not to influence the final selection and allocation of projects independent of technical considerations about population density and need. Should CAs adjust budgets outside of such considerations, they would compromise their oversight role on budget performance, as they would be actively engaged in budget making.

**Recommendation 8: Counties must ensure that budgets and reports are comprehensive and include information on donor contributions and the financial affairs of WSPs.**

- County budgets should identify all expenditures and revenues. On the revenue side, all transfers, own revenue flowing to the county revenue fund, donor funds flowing through county systems, and all



appropriations in aid (donor support managed by donors or third parties and the fees and charges collected by county departments but not transferred to the county revenue fund) must be identified and accounted for. On the expenditure side, expenditure against donor funding must be accounted for, as this is a growing source of financing in the sector.

- Counties must ensure that the county department responsible for water presents the budgets of the WSPs to both the CECs and the CAs alongside their departmental budget, as the WSPs are public sector institutions even if they are autonomous, and their financial affairs are still a public concern. Where WSPs have limited capacity to prepare budgets and provide respective reports, the county treasury and water department should devise and provide adequate training in connection with the guidance discussed in Recommendation 1 above.

**Recommendation 9: National and county public finance institutions must strengthen PFM systems and ensure that financial statements present a reliable picture of county finances.**

- **The National Treasury must adopt a proactive mechanism to continuously engage with treasuries in the counties**, in monitoring and enhancing their performance towards strengthening execution, accounting, and reporting (contracts, payments, and internal audit) at the county level, which could be achieved in the short-term through secondment of staff with special experiences, knowledge, and skills; and through recruitment of adequate required cadre in the medium-to-long term.
- **The National Treasury should address the systemic weaknesses in the IFMIS and SCOA to allow for comprehensive use of the system by county governments** to manage their full budgetary and financial affairs. Adequate and continuous training must be on offer to county government officials to use the system towards more robust budgeting, cash management, internal controls, accounting, and reporting.
- **Expenditure control/internal audit capacity must be put in place at each spending agency of the county government**; and counties must establish audit committees as per 2016 Audit Committee Guidelines for County Governments by issued by the National Treasury, Gazette No. 2690. However, to avoid accumulation of mistakes/errors, and in view of capacities at county level in performing internal audit functions, it is recommended that counties consider a continuation of pre-audit practices. Risk-based internal compliance audits and audits of transactions where it was not possible to provide pre-audit advice can complement this practice, and should only be implemented if adequate capacity is in place.
- **Clear sanctions should be imposed on county departments on account of inaccurate, invalid, non-auditable, or incomplete financial statements, or irregular and inappropriate procedures** that lead to Auditor-General disclaimers, adverse, or qualified opinions in audit reports, especially as a result of unsupported receipts and payments. These sanctions could include withholding portions of funds until issues are addressed (such as by the Controller of Budget who has the power to do so), withdrawal of authority to procure, or handing over of cases for prosecution. This would be an incentive in shaping accounting and reporting systems in the counties and in reducing fraudulent acts by county authorities

**Recommendation 10: Water sector actors should strengthen their collaboration among themselves as well as with anti-corruption and accountability actors to ensure full compliance with the existing framework for transparency, participation, and accountability in the management of resources for water service delivery.**

- Actors, such as KEWASNET and/or WASREB, will take the lead in bringing together other national and cross-county government and non-state water sector actors and accountability actors to discuss this report's findings, conclusions, and recommendations and decide on a way forwards in terms of specific recommendations.
- Actors such as the MWS, WASREB, or the Council of County Governors should run sensitization programmes on the importance of citizens fulfilling their obligations to pay for water while also demanding accountability for the use of such charges to deliver services.
- Accountability / anti-corruption actors (such as EACC or the Kenya Leadership and Integrity Forum) should work with water sector CSOs (such as WIN and KEWASNET), and public actors such as WASREB to refine and tailor interventions to prevent or discourage integrity breaches (such as complaint lines and anonymous whistle-blower channels) and follow up on and refer breaches that do occur / are reported for further investigation and prosecution.



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