Beyond CDF

Making Kenya's Sub-Sovereign Finance Work for the Socially-Excluded

HEINRICH BÖLL FOUNDATION

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Edited by
Heinrich Böll Foundation

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Abbreviations and Acronyms

AG	Attorney General
AGOA	African Growth Opportunity Act
APO	Alternative Public offering
ASAL	Arid and Semi-Arid Lands
BIMAS	Business and Management Assistance Services
BPA	Beijing Platform for Action
CA	Capability Approach (to human well-being and development)
CBA	Community Benefit Agreements
CBC	Community Benefit Company
CBK	Central Bank of Kenya
CBS	Community Benefit Society
CBO	Community Benefit Organization
CBOs	Community-Based Organizations
CCGD	Collaborative Centre for Gender and Development
CDF	Constituency Development Fund
CDFIs	Community Development Finance Institutions
CDTF	Community Development Trust Fund
CDP	Community Development Programme
CIT	Charitable Incorporated Trust
CLARION	Centre for Law and Research International
CSR	Community Social Responsibility
C-YES	Constituency Youth Enterprise Scheme
CMA	Capital Markets Authority
DDCs	District Development Committees
DFIs	Development Finance Institutions
EAC	East African Community
EC	European Commission
ETI	Economically-Targeted Investments
ERS	Economic Recovery Strategy
GDP	Gross Domestic Product
HELB	Higher Education Loans Board
HFCK	Housing Finance Company of Kenya
ICDC	Industrial and Commercial Development Corporation
ICEG	International Centre for Economic Growth
ICT	Information Communication Technology
IDAs	Individual Development Accounts
IEA	Institute of Economic Affairs
IDB	Industrial Development Bank
IGAD	Inter-Governmental Authority on Development
IFC	International Finance Corporation
IPAR	Institute for Policy Research and Analysis
IPO	Initial Public Offering
KEEF	Kenya Entrepreneurs and Enterprises Foundation
KEPSA	Kenya Private Sector Alliance
KIE	Kenya Industrial Estate
KIPPRA	Kenya Institute for Public Policy Research and Analysis
KRA	Kenya Revenue Authority
KSB	Kenya Sugar Board

K-Rep	Kenya Rural Enterprise Programme
KTDC	Kenya Tourism Development Corporation
KWFT	Kenya Women Finance Trust
KUSCO	Kenya Union of Savings and Credit Cooperatives
LA	Local Authority
LPA	Limited Partnership Agreement
LASDAP	Local Authority Service Delivery Action Plan
LATF	Local Authority Transfer Fund
LECD	Local Economic and Community Development (Zone)
MDG	Millennium Development Goals
MFIs	Micro-Finance Institutions
MSE	Micro and Small Enterprise
NACC	National AIDS Control Council
NARC	National Rainbow Coalition
NCCK	National Council of Churches of Kenya
NGOs	Non-Governmental Organizations
NESC	National Economic and Social Council
NHC	National Housing Coorporation
NHIF	National Hospital Insurance Fund
NSIF	National Social Insurance Fund
PRSP	Poverty Reduction Strategy Paper
RDAs	Regional Development Authorities
REPLF	Rural Electrification Levy Fund
RMLF	Road Maintenance Levy Fund
SACCOs	Savings and Credit Cooperative Societies
SAGAs	Semi-Autonomous Government Agencies
SDF	Sugar Development Fund
TARDA	Tana and Athi River Development Authority
UNDP	United Nations Development Programme
WHO	World Health Organization

PREFACE

The debate about decentralization of public finance in Kenya, and about increased public participation in financial decision-making, is in full swing. Public interest and at times excitement have focused especially on the Constituency Development Fund (CDF), which allows for a certain percentage of public funds to be spent on public investments. While there are open questions as to the appropriate use and impact of the CDF, the principle behind it appears to have been widely accepted throughout Kenya today. Public finance decisions should be made not merely on the national level, but more directly in the interest of, and with greater participation by those who are affected by them most directly.

But there is much more to decentralized public finance than just the CDF. Over the years, successive governments of Kenya have created a range of other finance mechanisms that can be characterized as "sub-sovereign" or "devolved" in character. They have been established usually for purposes of developing particular sectors of the economy or infrastructure. This has not always been done in a systematic manner, and the outcomes are rather diverse. From all these experiences, a central question arises: How do these sub-sovereign financing mechanisms address the fundamental problems of contemporary Kenyan society? How can they be made to work better for the poor and the socially-excluded in this country?

Through this study, we want to invite readers to take a new and more systematic look at sub-sovereign finance in Kenya. We propose to view devolved funding schemes within the broader perspective of human capability/well-being and asset-building. Once put into such a framework, new ideas and avenues evolve for devolved funding to become more productive for the vast number of Kenyans who have largely been excluded from the economic growth in recent years. We argue that there is a vast, hitherto largely untapped potential for socially-inclusive development in Kenya, taking off from existing structures, organizations and institutions of the non-governmental sector, the social economy, and various governmental and semi-governmental agencies. This potential needs to be developed. In effect, we propose devolved funding to become part of a wider approach in building the social economy in Kenya by taking off from a holistic understanding of what human development is all about, and by suggesting a comprehensive and innovative institutional and legal framework for socially-inclusive local economic and community development.

This study has been commissioned by the Heinrich Böll Foundation (HBF), a political foundation pursuing civic educational activities. HBF is affiliated to the Green Party in Germany, operating its regional office for East Africa and the Horn of Africa in Nairobi since the year 2000. The idea for this study emerged from HBF's gender programme that is dedicated to the promotion of women's human

rights and to the strengthening of female participation in public and political life. The question "How can devolved funding be made to work in the interest of women?" stood at the beginning of the consultation process that led to this study. However, in the course of work, it became obvious that a wider conceptualization of the issues was both necessary and possible. Poverty and social marginalization always have a strong gender dimension—and this study makes a strong argument to that effect. However, many of the ideas and "recipes" developed to address gender inequity may as well be applied to other dimensions of social exclusion—and vice versa.

HBF presents this study to the Kenyan public as an invitation for a broader debate about development strategies. We believe that the approach taken is an innovative one, and we hope that this study will contribute to a productive discussion.

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Information on the possible role of the social economy as providers of public services has been gained from numerous interviews with stakeholders in the sector. Special thanks to Dr. Michael Cherugoy of the Ufadhili Trust, Ms. A. Were at Allavida East Africa Office, Mr. Hudson Shiverenje, previously with MS-Kenya, Mr. Peter Ostbrik and Mr. Gilbert O. Angienda—then at Osienala in Kisumu, and Mr. Ochwada at the National NGO Coordination Bureau.

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away poverty. Valuable support for the preparation of this study was also received from Ms. Mary Kimamo, then a student at the University of Nairobi.

Numerous critical appraisal and comment was received as the text took form. I am deeply grateful to Hon. Prof Anyang' Nyong'o, Member of Parliament for Kisumu Rural and the then Minister for Planning and National Development responsible for the development of the Economic Recovery Strategy for Wealth and Employment Creation, Mr. Duncan Okello, the Executive Director of Society for International Development Eastern Africa Office in Nairobi, Dr. Ludeki Chweya, Senior Lecturer in Political Science at the University of Nairobi, Mr. Duncan Hunda, Senior Economist with the Government of Kenya, Dr. Mary Kinyanjui, a Senior Lecturer at the Institute of Development Studies at the University of Nairobi, Ms. Betty Maina, the Regional Representative of the Parliamentary Network on the World Bank in Nairobi, Ms. Wanjiku Wakogi, the Programme Manager for Gender at the Heinrich Böll Foundation, Regional Office for East and Horn of Africa, and Dr. Axel Harneit-Sievers, Director of the Heinrich Böll Foundation, Nairobi Office. Finally, Mr. Felix Murithi worked hard to give the manuscript the panel beating necessary to make it an easy and presentable publication.

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The author is Director, Pathways Development. He has played key leadership roles in the formation of key platforms on gender, social exlusion and integrity. These include the Kenya Women's Political Caucus where he was the founding coordinator, the Women's Political Alliance-Kenya, the Ufungamano Initiative, the National Civil Education Programme, and the Gender and Governance Programme.

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Nairobi
October 2007

EXECUTIVE SUMMARY

Kenya is one of the poorest and most unequal societies. It is also one of the most socially exclusivist states globally. Poverty, inequality and social exclusion are deeply-rooted structural and historical phenomena in Kenya. Individually and in combination, poverty, inequality and social exclusion are grave threats to social cohesion and overall state viability. They threaten economic development, democratic consolidation, peace, security and sustainable development. Poverty, inequality and social exclusion matter for economic growth and development. It is difficult to achieve and sustain high levels of long term economic growth in conditions of extreme poverty, social exclusion and inequality.

Poverty, inequality and social exclusion also present real impediments to the realization of basic human rights for the majority of citizens and residents. Excluded and poor citizens are denied capabilities, assets and thus the opportunity they need to realize basic rights such as food, shelter, security and health. They thus constitute gross violations of the basic rights and entitlements of these citizens. As such, these conditions present a moral, ethical, legal and programmatic challenge that all of society, and especially its leadership, should rise up to.

Social, economic and political institutions of society have a duty to provide conditions conducive to the realization of the minimum material and psychological resources necessary for the realization of basic human rights for all. For majority of citizens, these resources are best secured through a strategic and long term process of capabilities and asset development obtained especially from quality education, healthy living, rewarding and competitive employment, a good business, long term savings, home ownership, etc. Citizens are also entitled to social protection in the event of social vulnerability, sickness, old age, and extreme youth. Within international human rights conventions, the duty of ensuring these conditions obtain rests with the state. Nationally, the challenge of securing these conditions will call for an imaginative and sound system of local economic and community development.

Historically, and more so over the last two decades, Kenya has embraced a variety of sub-sovereign financing schemes as key policy, administrative and technical financial instruments to provide solutions to the various manifestations of social exclusion, poverty and inequality. There is, in this context, a national Secondary School Bursary Fund, a Free Primary Education Fund, the Higher Education Loans Board (HELB), a HIV/AIDS Fund, a Local Authority Transfer Fund (LATF), a Youth Enterprise Development Fund and, soon to come, a Women's Enterprise Development Fund. These funds were preceded by other schemes, such as the establishment of Development Finance Institutions (DFIs),

many of which sought to address some of the purposes now taken up by the funds.

The rising importance of devolved and sub-sovereign finance schemes has provided socially-excluded persons and communities, gender and women's rights activists, as well as other actors working for a just society new hope, tools and avenues with which to critically evaluate the economic and state processes that work to promote social exclusion, gender injustices, inequality and poverty. Given the popularity and ubiquity of these financing schemes, what is the likelihood that they can be creatively employed to provide a competent system of sub-sovereign finance directed at helping local communities get to the bottom of the factors driving social exclusion, poverty and inequality? Put another way, how can sub-sovereign finance be used to supply the capabilities and asset development needs that are at the centre of many an individual's or community's vulnerability to social exclusion, extreme poverty and inequality?

It would be difficult to re-orientate or rethink the existing or emerging system of sub-sovereign finance to provide the basis for such capabilities and asset development without re-examining and capturing the primary notion of what constitutes wealth, prosperity, development and well-being at both individual and community levels. Wealth, for instance, is to be distinguished from income to an individual or community's total asset and capital holdings. Prosperity is to be distinguished from progress, and development from growth in its various expressions. A community's asset and capital holdings include the net of financial assets, physical, natural and institutional assets, human and social capital as well as the stock of cultural, legal and political assets. These assets and the capacity to utilize them creatively and sustainably constitute the basic building blocks for sustainable and socially-inclusive local economic and community regeneration. Capability and asset building at individual and community levels, thus, provides the real work—as we know it—for those who desire to overcome poverty, exclusion and inequality.

Capability and asset development is, unfortunately, a steeply gendered terrain tenured to a patriarchal and economic system undergirded by women's marginalization, subordination and oppression. A programme that seeks to creatively employ sub-sovereign or alternative community development financial intermediation to fight social exclusion, poverty and inequality must, therefore, recognize and be responsive to this gendered terrain. It must call for a new accountability and structuring of the system of local economic and community development so that it recognizes the prevailing gender relations and embrace women's own agency and potential to act in their long term interests.

Recognition of capability and asset building as the central building blocks for a local economic and community development programme to overcome social exclusion, poverty and extreme inequality also places certain demands on the

proffered sub-sovereign finance regime. Principally, the system of finance should be measured by its ability and propensity to aid the development and acquisition of these very capabilities and assets at community and individual levels, and particularly for those who have historically been left out and behind. Of necessity, such a system needs to be purpose or mission-driven. A generic and amorphous system of sub-sovereign finance will not suffice.

A re-orientation to a capability and asset building framework, in turn, places a higher premium on overall local and national state capabilities and requires a reordering of state social security policy away from social protection and welfare to one of a socially-investing state, investing primarily and with foresight in the capabilities and asset acquisition of all its citizens and their communities. Far from providing welfare-based relief and targeted social protection, this calls for serious rethinking and reordering of all economic, political, social and cultural institutions of society, and places the state as a key instrument of intervention in this regard.

Any meaningful and well-intentioned effort to employ sub-sovereign finance as a core ingredient of a comprehensive system of local economic and community development finance would face severe handicaps, including:

- The structural patterning of the current asset regime where very few people own and control nearly all productive assets.
- The patterning of existing institutional regimes in favour of elitist wealth formation and the accompanying circumscribed discourse on the subject.
- The gender patterning of social and economic relations.
- An unyielding and grotesque public administration.
- An extractionist and elitist private sector.
- A mis-directed and structurally weak social economy sector.
- A weak or non-existent system of local economic and community development.
- Deep-seated financial exclusion, marked especially by the paucity of financial intermediation institutions and capital that are directed to financing capital demands of the poor and socially-excluded.

Recommendations

In the face of these realities, and given the great demand for the type of institutions and capital to drive a socially-inclusive and gender-responsive process of capabilities and asset development, this study calls for:

1. As an *a-priori* condition:

- Recognition and entrenchment of a basic rights framework as an overarching element of state intervention in the economic, political and cultural life of society.
- Recognition and entrenchment of a sort of social contract rooted in the requirement to ensure that all citizens benefit from state processes and the necessity to structure economic, social, cultural and political institutions of society to secure this social contract within a regime of a socially-investing state.
- Recognition and entrenching of the capabilities and asset-building framework within core state legislation and policy.
- Creatively employing the state as an instrument and technology to reorder the gender patterning of society with a view to ensuring equitable relations between men and women in society.

2. This study also calls for building a competent system of socially-inclusive local economic and community development involving:

- A more central role for the social economy and its institutions. This would, however, entail significant restructuring in the face of structural, governance and institutional flaws currently obtaining in the sector. Specifically, there is need for a new legal framework and statutory description and delimitation of the not-for-profit sector grounded on social and community benefit; new legal forms and institutions to drive the social enterprise and community benefit functions in the sector; a new regulator; new standards and frameworks of accountability and auditing; and new standards of delivery and capacity building to the sector.
- New independent local economic and community development institutions and agencies, including: new zoning for local economic and community development comprising at least 26 new Regional Development Agencies, 70 local economic development zones, new non-state local economic development corporations and a new regulator for local economic and community development.
- New financial intermediation to supply to the needs identified and grounded on a system of not-for-profit Community Development Financial Institutions (CDFIs).

- A new national Social Accountability and Auditing Framework, and accompanying institutions and their regulation, with a view to ensuring that institutions in the sector, the various sub-sovereign finance schemes, and parties in the private and public sectors willing to partake service delivery and contracting via sub-sovereign finance schemes can be held to account for the social and environmental outcomes of their activities.

3. Within the specific context of the prevailing devolved funds' mechanisms, it will be necessary to:

- Introduce a progressively universal system of Independent Development Accounts and Individual Life Long Learning Accounts within the human capital funds such as HELB, the various bursary funds and others.
- Institute a regime of Community Benefit Agreement/Partnerships contracting within the various infrastructure funds, such as the Kenya Roads Board, Constituency Development Fund (CDF) and Local Authority Transfer Fund (LATF), with a view to making these funds more responsive to the demands for local economic and community regeneration.
- Adopt an overall framework of Community Development Accounts that seeks to capture the overall funds and financing available at community level to drive local economic and community regeneration.
- Rethink funds such as the CDF, LATF, Youth Enterprise Development and the anticipated Women's Enterprise Development Fund so as to:
    - Help leverage other resources or financing available from the broader economy, including donors and the private sector. This would entail using sub-sovereign finance to expand the sources of capital and financing available for local economic and community development.
    - Fortify their juridical and organizational complexity so that there is accountability and so that individual funds can go to the market and borrow in their own names, for instance. This would entail making the funds financially-competent and ensuring capable institutions that can issue, secure or securitize long term debt.
    - Re-model and remove any service provision functions from the core funds and invest these in qualifying social economy institutions—some aspects of this is already happening within the Youth Enterprise Development Fund. The core funds would concentrate on supplying patient and seed financing for investee portfolios held by these social economy institutions and seeking programme and overall accountability.

- Generally make sub-sovereign finance accessible principally through social economy institutions. Specifically, there is need to embrace the concept of CDFIs as the chief local mechanisms for fund disbursement and alternative community-specific financial intermediation.
- Engage the CDFIs, and use their facilities to drive long term and risk capital into their communities/jurisdictions.

4. Within the broader economy, it will be necessary to:

- Establish a social equity capital market to enable broader and deeper financing for local economy and community regeneration. This can be achieved through a new social equity trading floor on the Nairobi Stock Exchange or an entire self-regulating market subject to the oversight of the Capital Markets Authority. It would also entail constructing a raft of new security instruments and a debt market, such as social development bonds.
- Establish a new financing mechanism—the Social and Community Benefit Asset Endowment Scheme—run through an appropriate statutory authority—the Social and Community Benefit Asset Endowment Authority.

The principal statutory function of the scheme would be prefaced on the need to provide financing for a capability and asset development-led system of local economic and community regeneration. The Social and Community Benefit Asset Endowment Authority would be required to author a national index of social exclusion, poverty, and inequality. Thereafter, and every so often, the authority would authorize various schemes that would go to alleviate these conditions.

The scheme would be prefaced on an elaborate statement of basic human rights, a requirement that it seeks to secure this for individuals and communities through a capability and asset-development framework and a requirement that its work will be judged by how well it uses its resources to overcome them in the various regions and communities.

The financing of the scheme is grounded on:

- A well-structured Community Investment Tax Credit applicable to individuals and corporations
- A system of Community Development Venture Capital driven by dedicated sources of finance
- A well-structured and secure sub-sovereign debt market
- Strategic savings that can accrue from restructuring of the state's local and foreign debt

- Endowments and donations
- Own income
- Any other income

Financing from the scheme would be available exclusively through the envisaged system of Community Development Finance Institutions.

If taken up and well implemented, the scheme would provide the impetus to scale up socially-inclusive economic growth and wealth creation, promoting enterprise and innovation in the regions and socially-excluded communities, and deliver to and modernize the social economy as an asset class and key pillar in the national efforts to overcome gender-based and other exclusions, thus helping provide a sound framework for cultural, social political and economic development for Kenya.

The need for this study arose, in large part, from the conviction that in the face of endemic poverty, inequality and social exclusion and the demands for greater social justice and security that this places on society and its institutions, evolving and sustaining a strong moral and practical vision is essential if the economy and the politics are to be the instruments through which women and other sections of society overcome their exclusion and poverty.

Owing to the deep-seated nature of the conditions that produce inequality, poverty and exclusion, this study is also convinced that a programme to achieve basic social justice for all calls for strong vision, faith, hope and courage. It also calls for deep dialogue, experimentation and imagination. It calls for a new wealth, both material and spiritual, that would provide the common glue to our future in community.

The study was guided by these imperatives to propose a programme of action, grounded on a primal recognition of the basic and fundamental human rights of all citizens, operating within an asset, capability, and functioning framework to build individual and community capacity with potential to achieve genuine freedom and prosperity and supported by a far-reaching apex financing mechanism.

The overall programme is designed to rise to the challenge for experimentation and imagination and, hopefully, will form the substance of a deep national dialogue and ultimately restore the faith and hope of the poor and socially-excluded in society's capacity and resolution to heal its wounds. Hopefully, the programme will also inspire the vision and the courage of conviction for those who struggle for social justice as well as those called to leadership in society.

Structure

This study is divided into eight parts. Part I provides the background to the study and presents a case for action against run-away inequality, exclusion and poverty.

Part II provides a basis for assessing social policy and action, which ideally ought to be at the heart of new development planning and efforts in devolved and sub-sovereign finance.

Part III offers a theoretical and conceptual apparatus for re-imaging and re-engaging the state as an interventionist asset-building entity in favour of the poor and socially-vulnerable. It argues for re-articulation of what constitutes wealth and development; the mainstream role of socially-inclusive asset-building in local economic and community development; and the emancipatory potential of locating a social exclusion/inclusion perspective in state policy. The section provides a practical case by examining the connections between social exclusion, gender and asset development. The section argues for the need to reframe devolved finance as key cement for socially-inclusive asset-building for individuals and communities. The section also argues for the need to redirect state social policy and programming away from need-based welfare approaches to more proactive and holistic social investment frameworks rooted in aiding individuals and communities acquire the capability and asset base necessary for them to function above the basic rights threshold.

Part IV examines the prospects for achieving basic human development aspirations in the key areas of education and workforce development, health, hunger and nutrition, housing and enterprise development through micro-finance. It argues for new institutional frameworks that aid the realization of these for-poor and socially-vulnerable individuals through asset-based sub-sovereign finance-backed applications. Of particular interest is the possible application of Individual Development Accounts as institutional and structural infrastructure to aid poor and vulnerable individuals rise up the asset accumulation ladder. The section recognizes that to aid this process, the prevailing devolved finance mechanisms would have to undergo significant re-orientation to make them institutionally and organizationally autonomous, increase their capacities and efficacies, and convert them into viable financial backbone institutions.

Part V privileges the primacy of institutions in pushing or reducing individual and community vulnerability to social exclusion, poverty and inequality. It argues for a more central role for the social economy and its various actors as an institutional arena specifically tailored to respond to social vulnerability and help individuals and communities cope with negative events as well as build assets. The section argues that though Kenya has one of the most vibrant social economic institutional frameworks on the continent, there is much that is wrong with this

sector. Much needs to be done to ensure that the legal regime, the assets and regulation of this sector work to realize the social and community benefit purposes at the heart of this institutional model. There is also need to embrace new innovations, including social investing, social enterprise and new legal forms that are driving new competences in this sector in other jurisdictions.

Part VI presents the need to rethink the process or nature of local economic and community development that is often at the heart of asset building for individuals and communities. The section calls for a new regional and local economic and community development interface with appropriate development agencies that are independent and have the mandate and capacities to drive the process of socially-inclusive local economic and community development. The section also argues the need for new community development financial intermediation through a specific regime of social economy-based Community Development Finance Institutions tailored specifically to grow the asset development potential of individuals and local communities.

Part VII presents a framework for re-engaging sub-sovereign finance within the context of the new capability and asset-based local economic and community regeneration. The section recognizes the need to expand the scope of financing for local economic and community development at three levels: at an institutional level for local organizations engaged in community development; at the programme level targeting the actual delivery of assets/benefits to target individuals; and at the asset development demands of community infrastructure entities, including educational and health institutions.

The section argues for an expanded role of sub-sovereign finance to drive new forms of equity and debt financing of local economic and community regeneration efforts, including new money from the local financial and capital markets. These proposals recognize that in order to issue or manage debt, sub-sovereign finance entities, including the CDF and LATF, will need to assume institutional, organizational and statutory complexity that would make them competent actors within the evolving financial and capital markets. There is also need to re-model local financial and capital markets to recognize and reward the social economy and especially so that good quality debt and equity can flow to social economy-based actors at the heart of independent local economic and community regeneration. This section also argues for the need to creatively deploy the significant opportunity provided by public infrastructure contracting in order to maximize the potential of infrastructure financing to deliver high quality asset-building to local economies by grafting a new regime of community benefit partnerships and social auditing into the public procurement process.

Part VIII argues for the need for an independent, self-regulating and statutory apex finance mechanism that not only enables the flow of much needed new money in the local economic asset building process but also provides the

organizational mechanism to measure what is being achieved in the field. In particular, it calls for the establishment of a Social and Community Benefit Asset Endowment Scheme secured largely through a generous tax expenditure regime and run by a statutory authority.

BACKGROUND TO THE STUDY

Kenya has witnessed an increase in the rise of devolved and sub-sovereign finance schemes and implementation of community development projects away from centralized planning, implementation and control. Sub-sovereign and devolved funds are significant for many reasons. Perhaps the most obvious is that they represent a departure from past practice of centralized planning where the central government was the primary development agent, to a new regime where communities and stakeholders get to participate and determine their development priorities and allocate availed resources accordingly. Just as important is the rationale behind the new schemes, which has seen significant injection of 'new' money at community level and through a need-based criteria that emphasizes allocation based on the prevalent poverty levels. This has seen poor and otherwise marginal constituencies that, for instance, do not have a single formal banking institution receive significant amounts of money injected directly into the local economy.

Sub-sovereign and devolved funds are important to the poor and socially-excluded for other reasons. The emergence of devolved funding has provided, for instance, gender and women's rights activists as well as other actors working for a just society new hope, tools and avenues with which to critically look at the economic and state processes that work to promote gender injustices, inequality and poverty. Assuming an apriori position that asset poverty, in contradistinction with income poverty, is a better predictor of ones' social vulnerability to poverty, social exclusion and marginalization, it should be possible to theorize and operationalize a sub-sovereign finance regime that works in the strategic capability and asset-building interests of the poor and excluded individuals and communities.

Sub-sovereign finance schemes are also opportune as they present clear expenditure-based frameworks within which national finances are allocated to redress particular social conditions or problems. As such, they represent a critical resource that socially-excluded and poor individuals and communities, including socially-excluded and poor women, can appropriate and direct to finance their strategic capability and asset accumulation.

This study posed the critical question of the (potential) role of devolved and sub-sovereign finance in providing the much needed financing to solve historical, including gender-based, social exclusion, poverty and inequality. The consultation sought to raise the bar on providing solutions to the emerging devolved funding regime by examining a number of funding initiatives against a holistic theory and framework of local economic and community development. It also sought to break new ground by locating the unfolding devolved funding regime against

larger prior state commitments and obligations to providing redress to the core issues of gender justice, extreme poverty, social exclusion and inequality.

Within a capability and asset building framework, the proliferation of sub-sovereign financing schemes points to the potential for an integrated and deeper state-wide mechanism—a sort of fund of the funds—to direct resources to the capability and asset acquisition and accumulation needs of socially-excluded and poor individuals and communities. There is, therefore, an objective and strategic need to nurture a discourse on such an alternative and apex financing mechanism and whose resources would be directed solely to meeting the financing needs of asset-led development solutions to key problems and conditions, especially deeply-rooted causes of poverty, inequality and social exclusion. There is also an objective and strategic need to locate such a mechanism and the capability and asset development process within an overall framework of a gender-responsive socially-inclusive and participatory local economic and community development.

Recognizing, perhaps, that the rise of sub-sovereign finance mechanisms reflects a much deeper need to redress financial exclusion, there is also a strategic and objective need to push work aimed at ensuring that targeted financing and its intermediation are primed as a financial asset class for socially-excluded communities and individuals as well as poor men, women, boys and girls across the various communities and regions.

In preparation of this report, consultation was carried with the following objectives:

- Map out principal initiatives of devolved funding across government and the sectors.
- Provide a framework for evaluating devolved funding within the context of holistic and gender-responsive asset-based community and local economic development as well as key government commitments with respect to poverty, gender equality, overcoming exclusion and inequality.
- Appraise available literature on devolved funding from a vantage point of the emergent framework.
- Generate a comprehensive framework for embedding devolved and sub-sovereign finance to serve the strategic asset-building interests of the poor and socially-excluded individuals and communities with special reference to gender.
- Draw policy, administrative and legislative imperatives for carrying forward lessons from the study.

The consultation adopted a panoramic conceptual framework that combined the key elements of gender-aware analysis of women's strategic interests, social exclusion and women's positioning within a patriarchal state system, a new wealth

politics built on asset-based local economic regeneration and development, and the instrumentality of the social economy to provide a conceptual and practical map of how devolved and sub-sovereign finance can work to the asset and capability/capacity needs of the poor and socially-excluded citizens and communities.

Study Design and Methodology

The study sought out the case for a gender-responsive devolved funding regime dedicated to providing key financial and institutional drivers against poverty, social exclusion and inequality, principally by enabling community and local economic regeneration.

In order to meet the objectives of the study, a number of tasks were undertaken, including: an appropriate review of applicable literature and documentation; interrogating existing and past devolved funding initiatives from a variety of dimensions and attributes, principally their responsiveness to unmet asset-accumulation potential of the poor and socially-excluded citizens, etc. The study, therefore, consulted literature, individuals and organizations that have an interest in such an enterprise and the issues raised. It also sought to apply expert opinion on the process and in evaluation and recommendation of various options as they arose. The hallmark of the study process was documentation of various proposals and to which stakeholder participation and comment were invited. Responses to the document and expert comment and moderation form the final product of the process.

Methodology

The study was carried out through the following methods:

- Literature review/desk study of appropriate documentation;
- Mapping of the various institutions driving devolved funding;
- Panel and individual consultations with select stakeholders at community, institutional, policy makers, and other interest formations and actors engaged in the discourse and practice of devolved funding, including Constituency Development Committees, Members of Parliament, and key civil servants;
- Field and site visits to selected constituency development and other projects;
- Limited peer/expert review and analysis;

- Preparation of a final report inviting comment from select stakeholders/ participants; and
- Processing stakeholder feedback in a final validation workshop.

Desk Survey/ Literature Review

A desk survey was conducted using documents and facilities available at the following institutions: Kenya Leadership Institute, Institute for Economic Affairs (IEA), the Resource Centre at the Ministry of Planning and National Development, the Resource Centre at the Kenya National Bureau of Statistics, the Collaborative Centre for Gender and Development, Centre for Law and Research International (CLARION), Kenya Institute for Public Policy Research and Analysis (KIPPRA), Institute for Policy Analysis and Research (IPAR), Action Aid International-Kenya, and institutional libraries at Daystar University and the University of Nairobi. The study also benefited from ongoing work on community development finance, social exclusion and the social economy at the Pathways Development Institute. It also benefited from an extensive review of internet sources, made possible through the kind assistance of research librarians at Daystar University.

Individual Consultations with Select Stakeholders

The study sought the views of various individuals perceived as having a participant or expert opinion and experience in key areas under review. Informal interviews were conducted with key staff at the various institutions, especially the Central Bank of Kenya, IEA, Daystar University, the Collaborative Centre for Gender and Development, and the CDF National Office. The study also benefited immensely from previous and ongoing work with core line staff in the Ministry of Planning and National Development.

The study also benefited immensely by way of concept and operational validation of some key innovations and proposals from ongoing work to move a Social Enterprise Development Fund Bill in Parliament by Hon. Dr Julia Ojiambo, through a private members motion. The workshops that made this learning possible were kindly facilitated through the Collaborative Centre for Gender and Development and the mover of the Bill.

Field and Site Visits to Select Institutions

The consultation visited select institutions identified in the course of the literature and documentation. These institutions included the National CDF Office, the Central Bank of Kenya, the Institute for Economic Affairs, the Collaborative

Centre for Gender and Development, and Constituency Development Fund projects in Dagoretti and Makadara in Nairobi, Kikuyu, Mathira, Mwea and Nyeri constituencies in Central Province, and Meru Central in Eastern Province. The consultation also benefited from media reports of on-going CDF success stories from various constituencies.

Draft Consultation Report

The outcome of these processes was collated into a comprehensive draft report that sought to isolate emerging issues that need to be considered as part of any policy, legislative and administrative action aimed at making devolved funding more responsive to the asset-building demands and potential of poor and excluded citizens with special referencing to women. Once done, the report was subjected to, and was greatly enriched by, a review by acknowledged peers and experts in the field for their critique and feedback. Proposals to aid ongoing work in social development in the various fields and sectors were then made.

To aid the process of diffusion and uptake of key innovations, proposals and recommendations, the report was issued in unpublished format as the basis of an initial engagement with key target groups, including policy makers and stakeholders in the various sectors.

PART I

POVERTY, INEQUALITY AND SOCIAL EXCLUSION: BACKGROUND AND CONTEXT

> Even if he can vote to choose his rulers, a young man with AIDS who cannot read or write and lives on the brink of starvation is not truly free…Larger freedom implies that men and women everywhere have the right to be…free from want—so that the death sentences of extreme poverty and infectious disease are lifted from their lives—and free from fear—so that their lives and livelihoods are not ripped apart by violence…Indeed, all people have the right to security and to development.
>
> *Kofi Annan, March 2005*[1]

[1] See Annan Kofi, In “Larger freedom: Toward development, security and human rights”, available at http://www.un.org/largerfreedom/

THE CASE FOR ACCELERATED ACTION ON EXTREME POVERTY, INEQUALITY AND SOCIAL EXCLUSION

Extreme Poverty and Inequality

Kenya is one of the poorest countries in the world, ranking among the bottom twenty.[2] Poverty, however conceived and measured, is endemic and has been growing over much of the last two decades. About 46 percent of Kenya's population were living in poverty in 2006, an improvement from about 56 percent in 2001 and in contrast with about 45 percent in 1990.[3] The number of people living in poverty has grown phenomenally over the last two decades, owing largely to an increase in population and a contracting economy. Though a majority of Kenya's poor continue to reside in rural areas, the number of people living in poverty is rising faster in urban areas. About half of the population of Nairobi is estimated to live below the poverty line.[4] Over this period, also, Kenya's life expectancy has continued to decline from 58 years in 1988 to 44 years in 2003. Child and infant mortality has also risen owing to declining health standards.

Kenya is one of the most unequal societies on earth.[5] According to the UNDP Human Development Index report for 2006, over 40 percent of income in Kenya is controlled by 10 percent of the richest households, while the poorest 10 percent control barely 8 percent of income.[6] Great disparities persist between the regions. While the country, overall, can use more doctors and nurses, for instance, Central Province has 1 doctor for every 20,000 people compared with North Eastern Province, which has ratio of 1 doctor for every 120,000 people.

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[2] The dominant literature on poverty in Kenya, including the 2004 Economic Recovery Strategy (ERS), uses standard income poverty measurements and assumes a correlation between rise in population, GDP growth and poverty.

[3] Economic Recovery Strategy (ERS) 2004. The Poverty Reduction Strategy Paper (PRSP) used a 56 percent figure for population of Kenyan's living under the poverty line. This figure has since been disputed as it was computed from a survey done in an exceptionally difficult year—2001—characterized by a drought that carried over from year 2000. The figures are accordingly used with a little caution.

[4] Economic Recovery Strategy (ERS) (2004). A good number of the urban poor are actually immigrants from the rural areas. It is obvious, however, that urban areas are currently unable to cope with the demand for jobs, opportunity and basic social services. This would be a daunting task even if urban economies were well-planned and run.

[5] See Society for International Development (2004). The UNDP Human Development Report for 2006 places Kenya at position 42 of 177 countries polled on equality. The World Banks's World Development Report on Equity and Development places Kenya at position 13 in Africa and 31 globally on the basis of income and expenditure inequality. Inequality has been rising every year since 1990.

[6] The question of how to measure inequality along with other core concepts such as poverty and exclusion are prior to and crucial in a discussion on equality, social exclusion and poverty. While the UNDP and SID reports use the Gini Index to measure inequality, there are other, and some will say, better ways of doing this

Inequality and poverty are deep-rooted

While much of poverty and inequality has been blamed on the prevailing economic and political conditions, poverty and inequality is very much a structural issue. According to the UNDP Human Development Index report for 2006, the best places to live in are those endowed with agricultural potential, such as the Highland districts of Kericho, Nyeri, Mt Elgon, Tharaka Nithi and Muranga, as well as urban centres. Arid and semi-arid regions such as Turkana, Tana River, Ijara, Mandera, West Pokot, Makueni, Samburu and Kajiado perform poorly. Even among apparently well-off areas, conditions such as urban slums, squatting and landlessness occasion some pockets of deep poverty and inequality.

Most graphic representations of inequality, social exclusion and poverty have persisted in using indicators to draw regional comparisons, perhaps on the assumption that regional disparities must be attributable to systemic and structural causes. One other and perhaps more useful way to do this is to examine the situation of women. As a group, women, who make over 50 percent of the population, are over-represented among the extreme poor—those with the least incomes and assets, among those with the biggest burden of disease, among those with least political power, and among those with the least formal education and training.

In 1994, there were almost twice as many female-headed households living in absolute poverty as there were men. While female-headed households comprised one-third of all households in rural areas, 80 percent of these were classified as very poor. There are also more women living with HIV/AIDS than there are men. Within urban areas, the number of people in open unemployment and in informal and casual employment rose phenomenally over the last two decades. Even then women constitute an absolute majority of those who are unemployed, in casual work or under-employed in the informal sector. In 1999, one man for every three women were unemployed among the 20-24 age group.[7]

The relationship between the structure of Kenya's economy and the concentration of poverty and inequality is significant. Structural imbalances easily lead to and fortify existing inequalities and contribute in big measure to the prevailing social exclusion. In this respect, regions with the worst performance in poverty are also regions that have suffered structural or historical exclusion. The UNDP report cites urban slums and North Eastern Province, parts of Nyanza and Coast provinces as areas with populations in chronic poverty. At the individual level, socially-excluded persons such as single parents, children born to single parents, orphans, etc are more likely to sink into poverty. Similarly, the extreme vicissitudes visited upon women, coupled with an unyielding patriarchy, also expose women as a group to extreme gender-

[7] See Society for International Development (2004).

based oppression characterized by constant physical, psychological and material abuse, extreme want and culpable to manipulation and oppression.

Poverty, inequality and social exclusion: A threat to state stability

Exclusion, poverty and inequality are mutually interlinked conditions that threaten peace, security, democracy and sustainable development at state and various society levels. A state can clearly not be stable or viable if half of its population live in poverty. The existence of urban slums, comprising extremely poor people without access to basic services, is a threat to the social, economic and civic viability of urban centres such as Nairobi. It presents a very real challenge to urban security as well as health and educational systems and outcomes. Collapse of urban and rural economies also presents real prospects of systemic collapse as the state is unable to muster the resources and legitimacy necessary to turn around the situation of the poor.

Emotionally charged, historical identity grievances arising from inequality, poverty and social and economic exclusion constitute the greatest threat to democratic consolidation and sustained economic development in Kenya.[8] International and constitutional law places the contemporary state as a major interventionist agent in helping bring an end to conditions that cause poverty, inequality and social exclusion. The contemporary state is in this way a key determinant of whether citizens are excluded, poor or victims of inequality. It is instructive, therefore, to transform the character of the state in favour of inclusion, equality and the poor.

Poverty, inequality and social exclusion matters for economic growth and development

Contrary to popular thinking, it is very difficult to achieve high levels of long term economic growth in conditions of extreme poverty, social exclusion and inequality. The apparent inability of the current economic expansion to create jobs and lift significant absolute numbers of people out of poverty is a vivid example. Far from creating savings, jobs and other conditions such as a rapid domestic market necessary for sustained economic growth, economic expansion has led to higher consumption of foreign goods by the few with the purchasing power. It will be impossible to grow Kenya into a middle income economy by 2030 without growing the real purchasing power of the majority of poor Kenyans.

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[8] Note the reaction of the Minister of Finance, Hon. Amos Kimunya, to the *Daily Nation's* Wednesday 28 February first page headline *"Big divide: Kenya's richest and poorest",* of the UNDP Human Development Report. In *Daily Nation* Thursday 1 March 2007, Kimunya opines that such reporting and not objective conditions inequality amidst poverty and is dangerous.

This, in turn, cannot be achieved without addressing the structural forces that drive inequality and social exclusion.

As we have shown, very high levels of urban poverty, social exclusion and inequality present worrisome security and quality of living scenarios that any investor, local or foreign, would find difficult to wish away. Without significant investments in regional economies through a well structured system of local economic and community regeneration, the distribution of resources and opportunity will continue to be skewed in favour of large urban centres and create huge long term planning problems for these centres. Meanwhile, the blight that would have become of the rural, regional and other neglected and underserved areas will continue to demand increasingly higher social expenditures from the central government.

Poverty, inequality and social exclusion: A real impediment to realization of human rights

Social and economic exclusion inhibits the realization of the full human rights of the excluded, including rights to meaningful education, health, shelter, security, and food. Excluded and poor citizens need lifelong capacity establishment to enable them get a handle over the processes, ideologies, frameworks and institutions that work to keep them poor and excluded. Excluded and poor citizens and communities need capital resources and skills to negotiate with, and successfully make claims against state and global policies that promote their exclusion and poverty.

The Legal, Ethical and Moral Imperative

A question of rights—Basic rights

The notion of human rights presents an idea, a sort of conceptual and practical apparatus, that assigns priority to certain human attributes regarded as essential to the adequate functioning of the human being. As an apparatus, the notion of human rights is designed to provide some protective ring on these attributes and to invite deliberate action to ensure that they are secured, nurtured and protected. By dint of these attributes, human rights are imprescriptible—cannot be washed away with time; irreducible—cannot be whittled down to some sort of minimum; unassailable and inalienable. Human rights are foundational and exist prior to other general claims in society. Denial of human rights works against the basic tenets of life as is experienced by humans, and constitutes a threat to individual and community survival.

Even in the face of an apparently prospering economy, individuals, families, women and children, slum dwellers, pastoralists and other individuals from poor

and excluded categories are daily sinking into deeper and deeper poverty arising from economic, social and political activities they did not participate in and which they have been powerless to influence.

Unlike other creation, human beings depend for their survival, well-being and prosperity on a minimum of material conditions and comforts. Basic social justice calls for the establishment and attainment of certain material benchmarks on which each person can stand in welfare and community with others. Justice demands that social institutions be ordered in a way that guarantees all persons the ability to participate actively in the economic, political and cultural life of society.

The rights to life, food, clothing, shelter, rest, medical care, security and safety and education are integral to the protection of human dignity. In order to protect these rights, all persons have a right to earn a decent living, which for most will be through remunerative employment and enterprise. All persons also have a right to certain prerequisite competences and capabilities and to possess the asset base necessary for them to acquire and maintain a standard and level of living that enables one meet her basic needs. Similarly, all persons have a right to social security in the event of sickness, disability, extreme youth, old age and unemployment. Basic social justice also demands the establishment of minimum levels of participation in the life of human community for all persons.

Viewed this way the continued oppression and exclusion of women and other significant sectors of the Kenyan population, extreme asset and income poverty, disease and inequalities—all of which have come to assume a feminine face—constitute a crisis and present a moral, ethical and practical challenge calling for a clear moral and practical vision and programme that all of society and especially those in leadership in government, industry and civil society should uphold.[9]

Arising from these basic entitlements, economic, political and social institutions have a duty to ensure the availability of social and community conditions that make realization of these rights possible. There is need, therefore, to generate a new cultural consensus that the basic economic conditions of human welfare are essential to human dignity. This imperative calls forth a need to make cultural and economic institutions more supportive of the freedom, power, and security of individuals, and especially socially-excluded women and the poor, to realize a life of dignity due to them by right.

In light of the extreme poverty and inequality characterizing the Kenyan society, the imperative for providing basic social justice for all also means that

[9] That this is becoming a popular view can be gleaned from presentations such as that by the Kenya Private Sector Alliance delegation to State House where Dr Manu Chandaria called for committing as much as 25 percent of all gross government revenue specifically to fighting poverty (*Daily Nation*, Wednesday 21 February, 2006).

the poor and socially-excluded have the single-most urgent economic claim on the conscience of society and the nation. As individuals, corporate organizations and as a nation, there is need to make a fundamental commitment to the poor and socially-excluded.

Kenya's international commitments

One of the principal questions that confront proponents of a basic social justice regime tailored to assure all citizens of basic social and economic rights is that of the legal basis for such claims and their call for social mobilization. It has been the dominant view that Kenya needs a new constitutional dispensation that guarantees citizens these rights and freedoms and that would form the basis of claim-making by citizens.[10] The paradox of this view is that Kenya is signatory to several international human rights treaties and conventions that form the basic regime of international human rights law.[11] These treaties and conventions include the *Convention on Human, Social, Economic and Political Rights*, the *Convention on the Elimination of All Forms of Violence Against Women,* and the *Beijing Platform for Action*.[12]

The 1994 International Conference on Population and Development (ICPD) held in Cairo as well as the four successive World Conferences on Women, beginning in Nairobi 1975 and that culminated in the 1995 Beijing Conference provided the major global fora in which the commitment for women's empowerment and gender equality has repeatedly been reiterated. The most overarching expression of the commitment to promote women's empowerment and gender equality, however, is found in the *Beijing Platform for Action* (BPA), which was endorsed by 189 countries in 1995. The BPA mandated all governments and international institutions to integrate a gender perspective into all their policies and programmes, and also constituted the basis for "gender mainstreaming" the UN as an institution, along with all its policies and programmes. Subsequent five-year reviews (Beijing +5, Beijing +10) have revealed a lack of progress in the achievement of the goals set in BPA.

Beyond these major benchmarks, Kenya has been a signatory to numerous other international laws and declarations relating to the rights of children, persons living with disability and the right of all citizens to development. This international human rights regime and commitment, especially to women, children and socially-excluded

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[10] See Kindiki Kithure, in Kindiki Kithure & Ambani Osogo (2005).

[11] International treaties and conventions to which Kenya is signatory are sources of law to the extent that consent means that these principles and rules are applicable to the Kenya state. Such treaties are, in principle, binding on the parties and create binding legal obligations.

[12] A distinction is made between international treaties and the general resolutions of international conferences—in the absence of a 'final act' of such a conference. Treaties and so called 'final acts' are law-making while resolutions, while not binding, provide the basis for progressive development of law and the consolidation of customary rules.

groups provides a key legal, moral and practical imperative to advance a comprehensive programme to redress social exclusion, poverty and inequality.[13]

The millennium challenge

In addition, the *United Nations Millennium Declaration* in 2000, which committed nations to achieving key Millennium Development Goals (MDGs)[14] also included advancing basic capabilities and empowerment of the socially-excluded as key development goals. The MDGs represent perhaps the simplest and realistic yardstick to measure local progress with respect to achieving a host of other international obligations. Achieving goal number one, for instance, is important for women who constitute close to 70 percent of Kenya's extreme poor. Investing in food security invariably calls for recognition and significant investment in women, who constitute the majority of food producers and who are confronted daily with the challenge of 'putting food on the table'. Similarly, it will be impossible to eradicate child malnutrition and underweight children without bringing to a sharp focus the role of women in reproduction and child care.

While taking measures to meet these goals, such as improving food security and keeping various food forms accessible and affordable, will be critical to providing redress for women's practical gender needs, such measures must be taken with an eye on women's strategic gender needs as well. In the latter case, it is important that women are not burdened with more care work, or that technologies do not make it easier simply for women to farm without redress to the critical question of ownership of the production assets and technologies.

Achieving universal primary education, coupled with promoting gender equality through, for instance, increased access and completion by women to secondary and post-secondary education has a profound impact on women's strategic gender needs. In a similar vein, reducing maternal mortality is strategic for women of child-bearing age. It will be difficult to imagine reversing the spread of HIV/AIDS, Malaria and Tuberculosis without significant investment in women, who are now viewed as the new public face of these pandemics.

The Millennium Development Goals are a novelty for us in more ways than one. Owing to their very simple targets and goals, they bring to the fore some of the problems women and gender organizations have had to confront almost

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[13] For a comprehensive discussion on the nature of international law and obtaining obligations, see Brownlie Ian (1998).

[14] See http://www.un.org/millenium/goals/html. See also other related UNDP publications available online.

singly—the need to count all the people and offer gender-disaggregated information usable in a variety of settings. Patriarchal state and economic systems have historically and traditionally not taken to counting girls and women, and State data is often not useful for those interested in abstracting the differential impact and gains of State policy by men and women. Totalizing states have also not taken seriously the challenge gender-responsive local economic organizing that is so clearly required to meet the goals set out in the framework. States have also neglected the significant long term view of the impact of today's decisions on future generations of men and women. The Millennium Development Goals present for us good benchmarks and intentions via which to interrogate ongoing work in sub-sovereign and devolved finance. This report will attempt to integrate the need to deliver these goals, emerging government experience and the need to reshape or rethink community development and devolved/sub-sovereign finance.

To this benchmark and framework, this report adds four other crucial indices: local workforce development, local workspace development, women's financial exclusion, and mitigating women's vulnerability to exclusion-inducing events such as teenage pregnancy and women's personal security.

Enter Sub-Sovereign and Devolved Finance Schemes

The Kenyan government has historically responded to the emerging social and public problems through establishment of various decentralized and sub-sovereign financing mechanisms to redress the underlying causes of the problems. In the aftermath of independence, the government established schemes such as the Kenya Tourism Development Corporation, the Agricultural Finance Corporation, the Industrial and Commercial Development Corporation and the Industrial Development Bank to provide financing solutions to deep-seated problems and conditions in society.

Over the last two decades, and arising from a combination of factors and pressures, the government has increased the role of devolved funding and partial decentralization to initiate, implement, manage and finance community development projects. The last decade saw the rise of the Local Authority Transfer Fund (LATF), the Community Development Trust Fund (CDTF), the Rural Electrification Fund, the HIV/AIDS Fund and the Secondary School Bursary Fund, among others. Previously, through a combination of domestic and donor conditionality, the government established the Higher Education Loans Board (HELB) through which it channeled financing for access to university education. The last five years have seen the introduction of the Constituency Bursary Fund, Constituency Development Fund, the Youth Enterprise Development Fund, and the Women's Enterprise Development Fund, among others. The level and significance of devolved funding began to get critical attention in the media and

local development community especially with the establishment of two critical fund mechanisms—the Local Authority Transfer Fund and the Constituency Development Fund.

Devolved funds are significant for many reasons. Perhaps the most obvious is that they represent a departure from past practice of centralized planning, where the central government was the primary development agent, to a new regime where communities and stakeholders get to participate and determine their development priorities and allocate availed resources accordingly. In the view of the National Rainbow Coalition (NARC) administration, devolved funds "offer communities the possibility of addressing specific development needs" and "if well used…are a vital tool for combating poverty". For these and other reasons, they are "increasingly being viewed as a vital instrument for realizing faster and more sustainable development".[15]

Just as important is the rationale behind the new schemes such as the Local Authority Transfer Fund and the Constituency Development Fund, which have seen significant injection of 'new' money at community level and through need-based criteria that emphasizes allocation based on the prevalent poverty levels. This has seen poor and otherwise marginal constituencies that, for instance, do not have a single formal banking institution receive significant amounts of money injected directly into the local economy. There has been much praise for the new emphasis on devolved funding. There are many in government and Parliament who view this as the solution to much of the demand for community development finance at grassroots levels. There are many also at community level and civil society who see in it the potential for new financing to attack social problems that they deal with on a day by day basis.

While this new mantra of locating responsibility for planning and allocation of resources for community development at local level is encouraging, there are many critical questions and issues that need to be addressed for devolved funding to provide a unique, strategic and much needed solution to the social, economic, cultural, environmental and other factors at the root of present inequality, extreme poverty and social exclusion. There is a growing body of criticism from local civil society institutions that are seeking to raise some of these issues and questions. The Women's Political Alliance-Kenya, for example, have raised issues regarding the gendered nature of the Constituency Development Fund, including especially its composition and failure to gender-segregate its projects.[16] The Youth Agenda have questioned the constitutional and legal basis of the Constituency

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[15] Dr Edward Sambili, Permanent Secretary, Ministry of Planning and National Development. Speech to Hanns Seidel Foundation's Consultative Forum on Decentralized Funds. See also Wanjiru Gikonyo (2006).

[16] Discussion with Ms Beatrice Nzivo, Programme Officer, Women's Political Alliance-Kenya, Friday 25 August 2006.

Development Fund that entrusts Members of Parliament with huge sums of money to implement local development projects.[17] Action Aid International-Kenya recently issued a report on the Local Authority Service Delivery Action Plan (LASDAP) that was critical of the failure of the initiative to secure popular participation and its continued exclusion of critical constituencies, especially women, the youth and persons with disabilities.[18] There exists a real need to raise the questions and issues regarding devolved funding and the real impact and consequences to society, communities and the nation. There is also need to bring together a learning platform on the devolved funding by drawing critical lessons from evaluations already in place.

[17] In "CDF—The Constituency Fund: For development or campaigns?" The Youth Agenda and Fredrich Ebert Stiftung (FES), Nairobi, 2004.

[18] Local Government reforms in Kenya: A study on the Local Authority Service Delivery Action Plan (LASDAP) process in Kenya. Action Aid International, Kenya, Nairobi, July 2006.

PART II

SIGNPOSTS FOR A NEW SOCIAL POLICY

The regional differences in natural endowments and social and economic infrastructure have resulted in regional inequalities. My Government has, therefore, continued to channel substantial resources to the grassroots level through various devolved funds to finance development projects of the people's choice.

H.E. Hon Mwai Kibaki, President of the Republic of Kenya
Official Opening of the 6th Session of the 9th Parliament,
March 20th 2007

THE ECONOMIC RECOVERY STRATEGY: AN ELUSIVE DAWN FOR HOLISTIC SOCIAL DEVELOPMENT

The Basis of Social Action

It is tempting to read the prevailing conditions of extreme poverty, entrenched inequality and social exclusion as calling for a new radical social development policy. It is also tempting to view such efforts and goals as the MDGs, implementation of Universal Primary Education, and the now popular sub-sovereign finance schemes that are subject of this study as acknowledgement that such a policy is needed and overdue. These temptations and the new initiatives by the government beg answers to a prior but unstated question: what ought to be the aims or goals of social policy in the face of prevailing inequalities, poverty and exclusion?

Ironically, the answer to this latter question depends in part on how we answer another crucial question: how do we see or conceive social problems and what do we think are the duties or obligations of society and the state, if at all, in solving them? How we 'see' or 'view' social problems determines to a great extent what we do, and what type of policies, programmes or interventions we come up with in response to the problematic social phenomena.[19] One key concern that comes to mind is that of principles and values, namely what values and principles underlie basic institutions of society and the political community and how adequate they are in driving social policy and programmes. Are we, for instance, committed to achieving some social justice, to a certain prior notion of citizenship and minimal quality of life for each citizen? To what extent, if at all, can we tolerate inequality, deprivation and tracudation of basic human rights?

Even when they are unstated or not explicit, principles and values litter the political landscape and decision making process that informs social and economic policy. What are the values behind the massive investment in Universal Primary Education? What is the justification behind the ongoing expansion in tertiary education?[20] What is the rationale for new sub-sovereign programmes such as the Constituency Development Fund, the Youth Enterprise Development Fund

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[19] While this distinction may seem trivial, it is of foundational importance. The *Investment Programme for the Economic Recovery Strategy for Wealth and Employment Creation*, for instance, fails to identify explicit social goals and thus fails to deliver a development and investment strategy to pursue them. Subsequently, while the ERS provided for increased expenditures in health, education, and employment amongst young people and women, it has been criticized for failing to ameliorate basic social problems.

[20] The Government recently gazetted the establishment of six new university colleges located in areas that have not had such institutions before. As a result, government-sponsored university admissions have shot up from about 10,000 in 2004 to 16,000 in 2007.

or the Women's Enterprise Development Fund? Principles and values are important because they provide an objective and independent criteria against which to evaluate or judge stated goals and programmes vis-à-vis an acknowledged benchmark. Principles and values also provide us the space to argue and perfect some basic social good with which we can be identified.

We argued in the last section that a basic understanding and commitment to social justice, equality, freedom, basic rights and citizenship is foundational to the conceptualization of social and economic policy. Within the contexts of runaway inequality, poverty and social exclusion, social and economic policy ought to:

- be directed by a need to expand the scope of capabilities and freedoms available to the poor and vulnerable;
- achieve some basic equality between citizens, including an equality of opportunity;
- attain basic social justice grounded on a progressive conceptualization of a basic rights threshold and consequently a certain quality of life for each and every citizen;
- reflect a prior commitment to solidarity so that public policy and decisions are driven by the needs and concerns of those who are most vulnerable;
- reflect a prior commitment to empowerment so that each individual has a real chance and opportunity to realize the desired well-being.

Some clarification of these core assumptions regarding the values that should drive social policy may be conceptually and operationally helpful.

Expanding the Scope of Capabilities and Freedoms

We deal later with the concept of capabilities, freedoms and fuctionings and why these should be at the heart of evaluating and driving social policy. Suffice to say here that each individual must possess certain capacities to act in their own interests as well as the individual scope to initiate such action with a reasonable chance of success. Capabilities, freedom and functionings are central to the ability of individuals to face life, to recognize and take up opportunity and to pursue self-actualisation. It is also the case that in order for one to be free to do something, there may be need to be free from something else, such as being free from malnutrition in order to be healthy and take up other pursuits. Therefore, freedom is best measured from within the space of capability.

In policy terms, we may come to the view that what is needed is for us to pursue the ability and capacity of individuals to act to further their own well being, the

availability of resources and enabling to make real choices and to expurge the ability of institutions to curtail this foundational value.

Basic Equality Between Citizens

The constitution guarantees equality of citizens within the context of the state. Historical interpretations of this constitutional guarantee has, however, been limited to an equality of treatment and consideration—that all citizens are equal before the law and that state institutions shall treat all citizens equally without untoward discrimination. For the notion of equality to be helpful in how we conceptualise and provide redress to social problems, we need to go beyond this mere formalism to embrace a more instrumental and intrinsic equality.

Many talk of equality today as likely to comprise a division of the so-called national cake into 33 million-plus pieces spread equally and somehow magically between different regions, very much like one would share out a wedding cake among guests. In reality, no state or nation has ever succeeded in equalizing citizens, such as ensuring equal incomes and assets, but clearly there is need for a space within which all of us can be equal and stand equal especially in relation to our basic rights and membership to one political, economic and social community.

Assuming that freedom, and thus capability, is the basis for evaluating ones social state, and that the advancement of individual capability and freedom is a central pillar of social policy, then it may be the case that what we crave for is an equality of capability, an instrumental devise that guarantees and secures for each and every citizen the capabilities required to live up to and beyond a certain threshold quality of life. The aim of such a devise would be not so much to ensure equal outcomes—though outcomes may be equitable—but equality in the basic space from which we draw our membership to community so that we achieve some threshold functionings that work to enhance chances of individual flourishing.

Such conceptualisation of equality of capability may also point to another prior commitment to a related devise—an equality of opportunity and equal consideration. Key in this latter consideration is the banishment of advantage and privilege that is acquired socially and used to the detriment of others, the adequacy of opportunities open to all and an adequate response to requirements for expanding opportunity if such is the means of meeting the criteria for basic rights.

This conceptualisation also points to a commitment to reform institutions of society, including our markets, our domestic institutions, government religion and so on so that they reward equitably the prospects for conversion of capabilities into achieved functionings and real opportunity. In particular, institutions need

to stop discriminating or being privy to or aiding practices that discriminate against individual ability to acquire capability and convert it to ones advantage.

Within the realm of such conceptualisation, gross inequalities will be regarded as inherently problematic and undesirable. This would call for policies that, for instance, use fiscal measures and public expenditure to secure a requisite capability and functioning threshold for all citizens, to mitigate and eradicate advantage/ disadvantage by empowering the socially-vulnerable, etc. It would also call for a programme of institutional reform to turn around social, political and economic institutions that are beholden to accentuating advantage.

Basic Social Justice

The ability to provision for equality and capability is in part informed by our commitment to justice. To put it another way, our notions of social justice inform how much inequality we can tolerate. If we believe in pursing decisions and actions that promote the greatest possible good for all and that the aims of life lie in the pursuit of the greatest possible happiness for the individual, then we should be able to shape social policy goals that promote and enhance the greatest possible good for all, such as universal primary, secondary and tertiary education.

Should we believe that justice lies in the conduct of transactions and should not be concerned with the outcome of such transactions, then we should be concerned to ensure that fairness reigns in the conduct of transactional engagements and exchange; that individuals are provided absolute freedom to pursue self interest through voluntary and independent transacting and that choice and individual agency is paramount. Subsequently, we should be least bothered with the outcome of such transactions and exchanges and should have to be greatly tolerant of extreme inequalities.

Should we believe that justice has to be concerned with both the process and consequence of human action and interaction, that economic and social institutions should be ordered such that they confer the greatest benefit to the most vulnerable, and that outside this affirmative action criteria, all opportunity should be available to all without discrimination, then we would be able to advance a social policy that carefully weighs the consequences of various decisions and actions on different categories of citizens. We would also allocate resources and structure institutions in ways that most benefit the least advantaged. We would therefore not be concerned with the sanctity of individual voluntary transactions, but would be able to evaluate them for the inequalities they produce, considering who is benefiting, who is losing and with what consequences.

While there cannot be a prior basis for adopting one conceptualisation, our situational context of extreme poverty, social exclusion and inequality demand that we be visionally and bold in doing so. We will thus be drawn to a justice that

is concerned with the outcomes and processes of individual and institutional actions, that recognizes that the very nature of human beings dictates that individuals owe a debt to those who parented them as well as a duty of care to their own and future offspring, and that individuals live life in community with others. Importantly, any discussion on the basis or criteria for social justice assumes prior membership to a particular community or socio-political and economic entity. One of the cardinal precepts of a fair engagement by members of a particular community is to forestall a rigged outcome of deliberations and public actions. Another precept is the value placed on universal social inclusion, an equality of rights and treatment for each member and commitment to a basic equality of opportunity for each relative to another member and the whole. To put it another way, membership to a democratic state denotes certain prior conditions, including equality, equal opportunity and the right to self-advancement within the polity. These prior conditions of membership in turn call for policies that ensure universal social inclusion, the right to development for all members and that each member has the same potential opportunities and enabling.

Commitment to Solidarity

It would seem logical that when promoting well-being, priority should be given to those who are worst off in a particular economic or social setting. This would require that decisions are made on a criteria that not only lifts up the human rights of all but that also derives a clear picture of who is falling behind in the scheme of things, and whose ability to pursue the 'good' life as community understands it is compromised. Social and economic policy would stand in solidarity with these individuals and accord them the privilege of priority in processes of decision making.

Empowerment

We have argued for the imperative and necessity of equitable participation and deliberation in public life. We also argued for the imperative of enabling equal capabilities and opportunity. It may be argued that impaired social participation is a key agent of the inability to participate in public life—the lack of effective capabilities and individual failure to participate in public life. Indeed, one way of conceptualising social exclusion may be to view it as issuing from conditions and institutions that deny basic rights and freedoms. A restoration of the capacity to realize these and other rights and freedoms, therefore, constitutes an act of empowerment. Such restoration does not only appertain to the removal of obstacles in the way of ones freedom but is a conscious investment in the capabilities of those affected.

Government Intentions

Since coming to power in December 2002, the NARC administration has pegged Kenya's hope of transiting from extreme poverty, extreme inequality and meeting a core set of social economic rights on an *Economic Recovery Strategy for Wealth and Employment Creation* (ERSWEC) and accompanying public investment programme that lays stress on rapid economic development in excess of 7 percent of GDP, led especially by a rise in construction, tourism, manufacturing and agriculture. This level of growth, it has been argued, is necessary over a long period of time for Kenya to win the war against poverty. The ERS and its investment programme has also sought to supply resources to core social and anti-poverty expenditures, especially free primary education and health as well as provide fiscal incentives—primarily debt write offs—to smallholder agriculture and key large scale agro-processing sectors such as coffee and sugar.

Without doubt, the incoming NARC administration faced daunting economic and social challenges, not least constricting and dehumanizing poverty and extreme inequality made worse by a decade-long economic contraction. The administration faced a core challenge of fulfilling its generous electoral promises in an economic environment where the economy was actually in a free fall. Given that the economy was in decline, what opportunity was there to redistribute wealth? Between sealing holes in a sinking ship and sharing out ownership, lots amongst passengers already on board, what should be the priority action? It can be argued that the NARC administration chose to fix the ship and argue the merits of redistributive politics later. It has also been argued that the administration has been hugely successful in salvaging the ship, and quite to the dismay of majority of passengers, with potentially disastrous results.

The principal fiscal policy objectives under the ERS have been to achieve fiscal "consolidation", to reduce domestic debt and fiscal restructuring, and to relocate resources to qualifying "high priority programmes". These "high priority programmes" included expenditures in core social sectors, especially education and health. Significantly, the fiscal policy or the entire ERS did not aim at directing resources to grow the economy while *simultaneously* ensuring strategic redistribution of wealth. Restructuring and redirecting resources to drive income and asset equity is not a strategic objective under the plan. The government, therefore, opened itself up to the charge of zealously driving economic revival and growth merely to put more wealth in the hands of those who already had it.

Under the plan, the government aimed at keeping money supply at 8.1 percent per year supported by net foreign assets and domestic money supply to the economy. The ERS aimed to drastically restructure the domestic credit supply with more money going to the private sector, and government reducing overall borrowing from both domestic and external resources. This measure has resulted in a large expansion of credit supply to the private sector that has stimulated consumption and investments.

The fiscal strategy was anchored on a revenue framework that sought to keep revenues to GDP at about 21 percent while making sure that government expenditure is met from local resources without recourse to domestic borrowing. Government has, therefore, had to double tax revenue. Under the fiscal strategy, the ERS aimed at reducing recurrent expenditure to GDP to create room for a rise in development expenditures, including devolved and sub-sovereign finance.

The ERS fiscal strategy also aimed at reducing the prevailing budget deficit from 4 percent of GDP to below 3 percent by 2007. Deficit financing was to be achieved through soft lending that focused on concessional external borrowing to enable reductions in the levels of domestic credit as well as maintain or lower prevailing present value of overall debt—NPV to GDP. In reality, external inflows have proved more elusive than predicted in the investment plan, forcing the government to shift to privatisation proceeds to realize its fiscal objectives.

The ERS forecast the economy to grow at 4.9 percent through 2007, with rise in investments providing the key drivers for this growth. Thus, investment levels were projected to rise to 24.3 percent of GDP from the 2003 base of 13.6 percent. Domestic savings would contribute to this rise of investments by increasing from 13.5 percent to 18.5 percent, still way below the minimum ideal of 25 percent of GDP to grow the economy from local resources. This low domestic savings situation meant that there would be need for significant infusion of foreign capital to meet the growth targets. The situation could also be reversed by seeking ways to accelerate domestic savings.

Efforts to scale up the levels of domestic savings have included amendments to the Retirement Benefits Act, making mandatory retirement savings accessible only at retirement or death and, most recently, the conversion of the public sector retirement plan into a contributory pension scheme that would fall under the regulation of the Retirement Benefits Authority. The government also undertook to reduce the statutory deposit required in operating commercial banks. Other measures have included adoption of a Micro-Finance Act, and a yet to be published Savings and Credit Cooperative Societies (SACCO) Bill that would make these alternative financial intermediaries competitive and secure avenues for savings and driving local investments. The overall net result is that there is now significantly more liquidity in the local financial markets that can be directed to the type of long term capital and asset financing necessary to grow the economy.

The ERS has already been declared a resounding success. Under the programme, the economy registered a 2.4 percent GDP growth in 2003 rising to 4.8 percent and 6.1 percent in year 2004-2007. Growth rate is projected to be higher than 6.5 percent in 2008 on the back of fairly good weather, higher earnings from tourism, improvements in industrial outputs and the realization of better than expected aid inflows, especially in infrastructure development. Under the ERS, the government has raised expenditure on education from nearly Ksh 30 billion in 2002 to Ksh 100 billion in 2006. Expenditure on health has risen from about Ksh 16 billion in 2002

to nearly Ksh 40 billion in 2006. The government has also made significant investments in agriculture, infrastructure and tourism.

Despite this obvious success, the government still faces near insurmountable challenges in seeking to deliver sustained rapid economic growth, arrest run away social inequality and exclusion and attending vices such as crime, supply to the expanded social programmes, all the while maintaining macroeconomic stability, reducing the size of the public service and propping up public and private savings and investments. This reality came to the fore with the NARC government's third budget, with expenditure rising from Ksh 240 billion in 2002/3 to Ksh 608 billion in 2007/8 and expenditure in education and health taking up one fifth of the expenditures. Even with good economic management, such a rise in expenditure present very real risks of spiraling budget deficits that may have to be financed through domestic and external borrowing. It is also unlikely that these kinds of expenditures are sustainable even in the mid-term without a significant infusion of foreign aid and a rapid expansion of government revenue and the tax base.

Failing Strategic Social Development Objectives

The ERS was designed and implemented during a season of high expectations issuing from nearly four decades of deteriorating social, economic and political conditions. The historic 2002 electoral mandate for the incoming NARC administration can, in many ways, be read as a demand for a new horizon in social development that takes with it holistic notions of basic social justice underpinned by an affirmation of the human rights of all citizens, equality between men and women, an equality of opportunity between all members of the national community, and a new citizenship grounded on, among others, basic equality, equitable participation and benefits in public life and freedom from want. Given the centrality of the ERS as the core government programme to deliver on these expectations, what values and principles lie at its base? How were these values and principles conceptualized? How, for instance, are the notions and concepts of justice, freedom, equality, human rights and welfare conceptualized under the ERS, if at all?

A key weakness of the ERS lies in its failure to locate a significant place for reorienting social policy. This weakness is obvious granted the obvious difficulties arising from the limitations imposed on public revenues and expenditures by the combination of a low economic base and above average taxation to GDP ratio. This failure is striking, granted that social development was perhaps the greatest casualty of the nearly two decades of structural adjustment and a shrinking economy.

One of the hallmarks of the new government's social development policy was the provision of universal and compulsory free primary education. Another significant development in social policy has been the gradual expansion of the health budget accompanied by significant reform in the public healthcare system, in particular

instilling greater efficiencies in service delivery and the waiver of user fees for needy patients. Significant achievements have also been made with regard to the provision of safe drinking water, rural electricity and rural infrastructure.

Significantly, however, these achievements and the accompanying increase in social expenditures have not happened against a shift in the overall social development policy framework. As noted, one of the obvious challenges in evolving a new social development framework would be how to harmonize the economic and social sectors in a way that ensures the benefits of economic development translate into real improvements in the standards of living all round. New economic and policy developments would also be expected to adopt the now universal basic rights framework in relation to overall social and economic development objectives. A concern for justice, for instance, would not only work to safeguard the quality and fairness of our interactions as citizens and thus reform the processes through which they are carried, but also the outcomes of these interactions so that all persons enjoy the same sort of freedoms and opportunities that issue from these interactions.[21] For citizens to exercise or enjoy the same sort of freedoms, for instance, it would be necessary to ensure that not only do they have the same level of opportunity open to them, but also that they enjoy a comparable level of capability and functionings to realise the opportunity. A situation where the scope of potential opportunity is different between each citizen easily leads to inequality, constitutes a social injustice, erodes the quality of citizenship and tiers the quality of freedoms available to each. A vastly different capability and functionings set has similar negative implications. A corrective programme genuinely interested in securing the fundamental freedoms of all citizens would be aware that individuals and communities bear different histories and backgrounds and that many will need intervening mechanisms to enable them partake of their freedoms equitably with others.

Significantly, however, the achievements and the accompanying increase in social expenditures within the ERS have not happened against a shift in the overall social development policy framework. Had the above been attempted, the ERS would have provided the critical turning point in Kenya's social and economic development. At the minimum, such a programme would be expected to: 1) institute structural change in such key institutions as landholding and tenure, the marital and household status of women, and the ability of economic institutions to gainfully and equitably compensate and reward labour; 2) reform key institutions (to be differentiated from sectors) of the economy to enable institutional regimes, structures, norms, processes and values that work to maintain social progress; 3) foster dialogue and compromise on key issues relating to governance and the overall generation, management, distribution and ownership of assets and resources in the economy; 4) establish the organizational and human resource capacity to plan and implement the resulting

[21] The terms freedom, equality and opportunity, are used broadly and capture usage described later and variously employed by Amartya Sen.

wide ranging social development policy, strategies and programmes across the various levels of state and community.

As we argue elsewhere, it has also now become fashionable to view social development, ultimately, as being about building the critical asset base of individuals and communities with a view to securing their ability to beneficially engage other economic agents in the state as well as survive changes in the social, economic, technological, political and physical environment with minimal erosion of their basic rights. In addition to undertaking much of the policies and strategies identified above, this strategy places a premium on the development of the assets and capabilities of individuals and communities. This latter includes investments in the core human capital assets of education, technical and workforce training, health and nutrition. It also involves securing basic housing and social infrastructure demands of all citizens, especially those who will not be served by skewed market forces.[22]

Understandably, within the prevailing circumstances of high expectations, the state sought to increase spending on high-impact select core social programmes while ensuring that this does not compromise the much needed economic growth. Unfortunately, a revenue-based approach means that the government must continue to collect even higher revenue to supply to the numerous unmet social goals. While the government has done a sterling job at collecting more revenue, the reality is that it cannot expect to collect a lot more revenue without achieving significant and long term improvements in the size of the GDP. The government can also not hope to raise more revenue by increasing the rate of taxation as this is already too high by both global and sub-Saharan Africa standards.[23] The stated policy options that have been pursued in the 2003-2007 budgets involve largely administrative measures—increasing tax revenue through modernization of tax administration and improving efficiencies in collection.[24] While this is helpful in the mid-term, it leaves serious challenges in the long term, especially viewed against rising demand for social spending to provide relief for the historic levels of poverty, social exclusion and inequality.

One significant consequence of this is that the government gets short of resources to direct to areas that are of strategic importance to especially vulnerable sections of the population.[25] This could see the government either resort to tokenism or simply

[22] For a useful and practical discussion of historical and contemporary developments of social development, see Beverly Sondra and Sherraden Michael (1995).

[23] See Mbui Wagacha, in Kimuyu Peter, Wagacha Mbui and Okwach Abagi (1999).

[24] State capacity to raise revenue is also severely constrained by the distortional effects of systemic corruption and rent seeking in the economy as well as the unyielding nature of the informal economy. These two systemic problems will take a lot more than reforming tax administration. They, however, present significant opportunity to raise higher revenue in the future.

[25] One outcome of this is that it may become more difficult in the future to justify increases in social assistance/support programmes were these to lead to greater taxation.

deny the validity of some of the claims made with respect to obtaining social problems. Another significant consequence is that the state risks *entrenching* personal dependency on the state and the emergence of personal entitlements irrespective and in the absence of initiative, drive and sustained efforts to prosper local communities. In the absence of a more fundamental recognition of the need to underwrite the ability of local and national conditions to secure local and individual capacities and competences necessary to achieve individual rights and freedoms, increases in social expenditure cannot be assured in the long term.

The weaknesses noted above are compounded by failure of the ERS to provide for a state interpretation and policy on the relative use of monetary and fiscal policy to aid national and local efforts to overcome extreme poverty, social exclusion and inequality. In the past, fiscal policy has been used largely as a macroeconomic stabilization vehicle to promote the rate of employment, growth and price stability while achieving the main objective of raising and allocating revenue to meeting the costs of public goods and services. This policy has been pursued without paying specific attention to underlying inequalities and social exclusion, the social and economic forces that drive them, and how fiscal policies can be used to achieve a desired distribution of wealth and income in society. In other words, fiscal and monetary policy needs to be used specifically to drive local economic and community regeneration and in securing the ability and capacity of local economies to provide sustainable livelihoods for their residents. Also, put another way, fiscal and monetary policy should be tied to an express regime that enables residents and other interested parties to build local economies and communities with a view to growing and prospering them. In reality, all government efforts to stem rising poverty, inequality and social exclusion without an explicit and radical shift in fiscal policy to capture these goals will fail.

Women's Strategic Gender Interests and the Economic Recovery Strategy

If the broad goal of the ERS was to grow the economy to generate wealth and employment, one would assume that care has been taken to define and differentiate 'economic recovery', and growing 'wealth' and 'employment' for various constituent groups and especially for differentially-located men and women. As we shall see later, women and men acquire 'employment' and 'wealth' differently. Women's employment, for example, is conditioned by a hostile labour market rooted in a sex-based division of labour as well as an unfettered patriarchy that prescribes and then fails to recognize and remunerate women's unpaid work in the care economy.

Growing employment cannot, therefore, be a gender-neutral project without at the same time fortifying the exclusion, marginalization and economic abuse of women. Similarly, wealth, equated with assets in this study for practical and strategic reasons, means different things depending on whether one is male or female. Growing

wealth, later referred to as asset development, especially at the individual and community levels will, therefore, call for strategies that respond to the differential locations and gender interests for men and women.

Unfortunately, the ERS and its accompanying public expenditure programme are silent on this key criterion that would have a fundamental bearing on the goals and strategies employed to recover the economy. When the strategy prioritizes growth in tourism for instance, males are likely to be the principal asset-holders in the sector —owning hotels, tour companies, and the entertainment industry that fuels it. Growing these two phenomena in ways that are in the strategic gender interests of women would entail adopting different strategies for women.

A key weakness of the ERS is that while it talks of growing employment and wealth, it is in reality based on a need to overcome income poverty. This key flaw is apparently a carry over from the Poverty Reduction Strategy Paper (PRSP), which it hastily replaced. The differences between asset and income poverty are manifold and the strategies required to overcome each different. The differences in strategy become especially manifest depending on whose wealth between men and women's one is attempting to grow and whether or not one intends to reduce prevailing social exclusion and inequalities in the process.

A key failure of the ERS and the Public Investment Programme, therefore, is its neglect to lay emphasis on growing the economy in areas and ways that will integrate poor, socially and historically-excluded communities into the new wealth and power brackets that accompany anticipated growth. Without factoring inclusion and systemic redress to social inequity, even within the context of a vibrant economic growth, the social, economic and political situation in Kenya would be greatly compromised, nay jeopardized. Arguably, prosperity without social equity and justice would defeat the very goals of such a strategy. A solution is begging that enables massive investments in the social sectors, in the productive capacity and basic life security of low income, poor and socially-excluded citizens and that can answer to the serious economic, social and political challenges, and that assists the government to cap its expenditure commitments.

Failing Basic Anti-poverty and Equality Goals

Partly as a consequence of these failures, and also arising from the relatively low human development index base that has bedeviled the country since independence, Kenya is unlikely to meet key international benchmarks and commitments relating to eradicating poverty, social inequality and exclusion. Key among these are international commitments to human rights, the empowerment of women, and elimination of all forms of violence against women, and the Millennium Development Goals.

The pessimism and a sense of panic that Kenya is not doing enough to permanently alter the economic decline witnessed in the 1990s as well as eliminate the gender, inequality and exclusion problem is creeping in even in official government literature. According to a report attributed to the Ministry of Planning and National Development, Kenya is likely to meet only one of the eight MDGs. According to a report by the Institute for Economic Affairs (IEA), Kenya has reached the apex of its chosen political and institutional models applied over the last three decades. "Based on the economic and institutional models that have dominated the past 30 years, (Kenya) has reached the furthest limits that could have been reached".[26] According to the report, "a successful and prosperous outcome for Kenya is still possible, though there is no quick fix. (Such an outcome) requires radical re-organization and great sacrifices by all Kenyans. Change will be costly and painful".

According to the report, there is not one but two "simultaneous crisis" unfolding in Kenya. One has to do with the political system, based largely on a patron-client structure that places a lot of demands and responsibility on political elites and the political structure, and which acts to compel them to misdirect political resources. This system is built on a weak legal and judicial infrastructure that is unable to check its excesses. Such a system cannot address itself to complex social problems and is unable to deliver equitable development. The problem has to do with a crisis of institutions, including, one supposes, the institutions of the market and their failure to nurture conditions necessary to overcome key social and economic problems. Institutions—to be differentiated from organizations—play a significant role within the overall context of social, political and economic development. According to the IEA report, institutions shadow our lives from the cradle to the grave. We are born into institutional life and we live and die within institutions. Institutions assign power and authority to individuals over resources. It would be futile to attempt to grow employment and wealth, overcome poverty and inequality, without seeking to reshape these institutions in terms of their structures and legitimating creeds. Such a project is necessary for women, if they were to use these institutions to achieve cherished strategic gender interests.

The question then arises regarding how to view government's commitment and strategy to overcoming poverty, inequality and social exclusion. The ERS has been hugely successful in investing especially in education and health. Under the ERS, spending on education has gone up and nearly all the children who ought to be in school are doing so. Within the health sector, a staggering 120,000 people have been put on life saving anti-retroviral treatment up from hardly 10,000 when the programme began. Essential medication for Malaria, Tuberculosis and major childhood diseases are available in government and

[26] See IEA and Society for International Development (2002).

mission hospitals at no cost. There has been massive investment in community level health infrastructure such as dispensaries and ambulances. Meanwhile, key livelihood sectors in agriculture, tourism, construction, and manufacturing have registered impressive growths. Clearly, things are looking up for many, especially when contrasted to the depths to which they had sunk years before.

All of these achievements have, however, happened without a policy commitment to restructure economic growth such that the economy can supply the resources needed to heal the rifts, social and public problems caused by structural poverty, inequality, and social exclusion. In this situation, the economy grows, social transfers grow at higher than anticipated rates, and a lot of people are happy. However, the absolutely poor sink deeper into poverty, the number of poor grows, inequality gets worse, and social exclusion remains a major cancer in society. Is economic growth a mirage, or is it, as some would say, a dry riverbed holding life sustaining resources during a drought, but hardly enough to bring prosperity to the lands through which it traverses except during those seasons when its banks burst their seams? It is not lost on many that Kenya has experienced such 'economic fortunes' before with the overall result that poverty and inequality are worse today than they were when the nation building project began.

This study adopts such view in its discussion of the prospects of interfacing gender interests and women's strategic gender interests as well as the universal desire to overcome extreme poverty, inequality and social exclusion.

THE DEVOLVED FUNDS AND SUB-SOVEREIGN FINANCE

Legal and Institutional Framework

One of the preliminary tasks of the study was to delineate the current practice of devolution/decentralization of funds with a view to adopting an acceptable working definition of the concept and its practice. Devolved, decongested, decentralized or other such terms refer largely to efforts to transfer responsibility for planning, management and local economic development from the central government to other units of government. Within this framework, it is possible to redistribute administrative responsibilities within central government (deconcentration), delegate functional authority and responsibility to semi-autonomous organizations (delegation) or transfer authority to autonomous and independent units of sub-sovereign governments (devolution).[27]

Decentralization has also been used to refer to the "transfer of legal, administrative and political authority to make decisions and manage public functions from the central government to field organizations of those agencies, subordinate units of government, semi-autonomous public corporations, area-wide development authorities, functional authorities, autonomous local governments or non-governmental organizations".[28]

Decentralization can be used to refer to either a territorial or area-based phenomena (such as the CDF and LATF) or functional phenomena (such as HELB, the HIV/AIDS Fund and the Bursary Fund). One involves the transfer of responsibility and authority for public functions to organizations with well defined sub-national, spatial or political boundaries such as a province, a region, a district or municipality. The other involves transfer of authority to perform specific tasks to specialized organizations that operate nationally or regionally. Authorities can be created to deal with infrastructure such as roads, power utilities, water, healthcare, etc.

In Kenya, decentralization is a much contested concept and there is no clear constitutional or other overarching legal or historical framework governing its practice. Much of the current efforts that use the district or constituency as a unit of decentralized activity rely on residual capacities and structures put up through the now abandoned "District Focus for Rural Development". Outside

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[27] This study uses the terms *decentralization* and *devolution* interchangeably to refer to the same concept.

[28] Kithure Kindiki & Osogo Ambani (eds) (2005).

the "Majimbo Constitution", the "District Focus" presented one of the most comprehensive administrative efforts to deconcentrate planning and execution of local economic development. Unfortunately, an apparently much desired but unstated purpose was to maintain and increase control by the executive of local level development initiative.[29] This study uses the terms decentralization and devolution interchangeably to refer to the same concept.

Decentralization is a popular concept because it is associated with implied greater efficiencies, increased local civic engagement and participation in state processes, greater accountability to grassroots and other stakeholders and communities, a reduced bureaucracy and red tape especially for local development projects, and increased flexibility on the initiation and implementation of development interventions. Decentralization can also be valuable in the mobilization of extra-budgetary resources and improving the links between market forces and local economies.

Politically, decentralization is popular for its promise to promote political stability, hold governments accountable to local communities and interest groups, mobilize local support for national development effort as well as nurture a spirit of local self-determination and reliance.

Decentralization has been practiced variously in Kenya since independence. Historically, Kenya gained independence as a quasi-federal state comprising seven units of political devolution. Each of these units had a distinct administrative structure with Nairobi forming an eight special administration district. This system was unpopular with majority of citizens and was repealed through successive constitutional amendments after independence. In the absence of an overarching statutory or constitutional framework, it is also not clear what constitutes a competent unit of decentralization or devolution.

Ideally, decentralization should be accompanied by well-structured measures of economic, fiscal and administrative functionality or territoriality. Devolved units of government should be able to raise or at any rate be assured of own resources, should be able to carry out their own planning and should be administratively autonomous of the larger polity.

Devolved or Sub-sovereign Finance

Devolved funding refers to the provision of structured finance within the context of devolved responsibility to key sectors and sections of society and the economy. Perhaps, as a reflection of the constitutional and legal ambiguity, the current practice of devolved funding does not distinguish between decentralization,

[29] See Chitere O. Preston and Onesmus N. Ireri (2004).

deconcentration, delegation or devolution. In the current practice, funding can be devolved to a sector through Semi-Autonomous Government Agencies (SAGAs), to a particular region or administrative unit such as district or constituency, to a statutory body charged with various delegated functional responsibilities and authority (for example, Regional Development Authorities, the Higher Education Loans Board, etc) or even to a specific institution such as a primary school (for example the Free Universal Primary Education Fund).

The practice of devolved or decentralized funding apparently began even before independence with the setting up of farmer organizations such as the Kenya Farmers Association and the Agricultural Finance Corporation through which the state channeled support to the sector.

This study uses the terms devolved or sub-sovereign finance interchangeably to refer to all those situations where fund mechanisms are set aside either through statute or executive decision and designated for particular functions and with discernible administrative structures.

The Devolved Funds

There seems to be broad agreement that the following are devolved funds or sector-finance mechanisms:

- Secondary Education Bursary Fund
- Road Maintenance Levy
- Rural Electrification Levy
- Local Authority Transfer Fund
- HIV/AIDS Fund
- Constituency Development Fund
- Free Primary Education Fund
- Kenya Housing Trust Fund
- Kenya Social Action Fund
- Kenya Community Development Trust Fund
- Higher Education Loans Board
- Youth Enterprise Development Fund

Devolved funds may also include sector-based development financing schemes such as:

- Kenya Tourist Development Corporation

- Agricultural Finance Corporation
- Industrial and Commercial Development Corporation
- Industrial Development Bank
- Kenya Industrial Estates

Semi-autonomous government agencies

Semi-Autonomous Government Agencies (SAGAs) include funds entrusted to statutory and executive agencies such as Regional Development Authorities, the Poverty Eradication Commission, the Community Development Trust Fund, the Tourism Development Trust Fund, the Industrial Training Levy, and the Catering Levy Trust Fund. Many of these are set up under respective Acts of Parliament often with a defined functional jurisdiction, a semi-independent governing structure and with complete legal personality. Some of these funds are described below.[30]

HIV/AIDS Fund: The Fund was established in 1999 through a Presidential executive order contained in Legal Notice No. 170 and targeting individuals infected and affected by HIV/AIDS. It is administered by the National Aids Control Council (NACC) and focuses on immediate and long term care and support. NACC receives budgetary allocations and channels them to independently organized AIDS control units within various sectors and ministries and Constituency Aids Control Committees for onward disbursement to NGO's/CBO's for implementation. The Fund received Ksh 14 billion in 2006/7 financial year, almost exclusively (over 80%) through donor funds.

Free Primary Education (FPE): The Fund aims to address financing and quality challenges in primary schools in the face of universal free primary education. It targets all Kenyan children attending formal and non-formal public schools but with an added emphasis to children from poor households. The fund allocates the equivalent of Ksh 1,020 per child per year. The monies are disbursed to the school depending on the number of pupils enrolled. The community is expected to participate in the management and implementation of the fund through school committees. The Fund received Ksh 7.8 billion in 2005/6 financial year.

Rural Electrification Levy Fund (REPLF): The Levy Fund was established in 1998 through sections 129 and 130 of the Electric Power Act (1997). It aims to finance electrification of rural and other underserved areas. The funds

[30] Information on these funds has been gleaned from various sources including Centre for Governance and Democracy (2005); KIPPRA (2006), also available online at the KIPPRA website; NCCK (2005: A manual on how to participate in the management and monitoring of decentralized funds".

are used for activities relating to the design, construction, equipping, operations and maintenance of rural electrification programmes identified by qualifying communities. The fund is administered by the Rural Electrification Fund in which the Ministry of Energy, the Kenya Power and Lighting Company, local District Development Committees, the Constituency Development Committees and project-specific local committees are represented.

Secondary Education Bursary Fund (SEBF): The Bursary Fund was established in 1993/1994 through a Presidential executive order. It aims to provide relief from poverty by cushioning poor and vulnerable groups against the high and increasing costs of secondary school education, thus reducing inequalities. The Fund also aims to increase enrollment and completion at secondary school by poor and otherwise deserving students. The Fund targets orphans, select girl-children as well as students from poor households and urban slums. The financial allocation depends on the Ministry of Education budget and will vary from year to year. Minimum annual allocation is per beneficiary by school category: day schools Ksh 5,000, boarding schools Ksh 10,000, and national schools Ksh 15,000. Since 2003, distribution of the SEBF has been coordinated by Constituency Bursary Committees. The Fund received Ksh 1.4 billion in 2005/6 financial year.

Road Maintenance Levy Fund (RMLF): This Fund was established in 1993 through the Road Maintenance Levy Fund Act to cater for the maintenance of public roads, including local authority unclassified roads. The Fund is made up from a fuel levy on petroleum products and collections from transit oil. It is presently administered through the Kenya Roads Board, established in 1999. Majority of the funds (60%) is taken up by international and national trunk and primary roads with the rest going to secondary (24%) and rural roads (16%). The fund received Ksh 14 billion in the 2006/7 financial year.

Local Authority Transfer Fund (LATF):[31] LATF was set up through the Local Authority Transfer Fund Act of 1998 as an inter-governmental fund transfer mechanism with the aim of improving financial management, debt resolution and effective service delivery by local authorities. The fund was established with the objective of enabling local authorities to improve local service delivery to citizens and improve local economic governance. The fund is part of a wider Local Authority Service Delivery Action Plan (LASDAP), which envisages a participatory and community-centered process in determining and prioritizing projects undertaken by LATF.

Annual allocations are set at 5 percent of the national tax income. Funds are allocated according to set criteria, including population size but allowing for a

[31] Odhiambo, M. Mitullah and Akivanga K. S. (2006); Ludeki Chweya (2006) at http://www.africaexecutie.com/modules/magazine/articles.php?article:720.

minimum allocation and assessment of relative poverty per local authority. Disbursement is pegged to certain benchmarks, including satisfactory performance on set standards, presentation of satisfactory estimates on time and the presentation of details on capital expenditure. The Fund is managed by a semi-autonomous advisory committee comprising of a chairman from the private sector, representatives from the ministries of Finance and Local Government, the private sector and co-opted experts.

Constituency Development Fund (CDF): The CDF was set up in 2003 through the Constituency Development Fund Act. The CDF was established with the express aim that "a specific portion of the national annual budget is devoted to the constituencies for purposes of development and in particular in the fight against poverty at the constituency level".[32]

The fund is financed principally through a subvention from the Consolidated Fund, equivalent to 5 percent of all ordinary government revenue collected every financial year. The Act sets up criteria for allocating the funds to respective constituencies in which 75 percent of the funds are shared equitably amongst all constituencies and the remaining 25 percent shared out depending on a constituency's ranking on the national poverty index.

The Act requires that projects implemented under the Fund be specific to constituency and of a community development nature. Communities are free to forward project proposals to the respective CDF provided these proposals meet the criteria set by the Act or subsidiary legislation.

The Act sets up various administrative structures for the fund, including a National Management Committee, a Constituencies Fund Committee, the Constituency Development Committee, and a District Projects Committee. This fund received Ksh 10 billion, or 3.5 percent of ordinary government revenue in 2006/7 financial year.

Higher Education Loans Board (HELB): This Fund was set up through the Higher Education Loans Board Act 1995 and came into effect on the 21st of July of the same year through a Kenya Gazzette Supplement (Cap 213A). The Act sets the criteria and conditions governing the granting of loans, including the rate of interest to be charged. Interest rates by the Board have been low and for a long time stood at 2 percent before rising to 4 percent in the last 4 years.

The Board is entitled to receive and consider all loan applications from eligible students who wish to pursue higher education in Kenya. The Board subsequently approves or rejects such applications in accordance with the provisions of the Act. The Board also has wide discretion to determine the maximum number of eligible persons to be granted such loans at any one particular time. Previously a

[32] CDF Act, available at the CDF website.

reserve of freshmen and women joining public universities, beneficiaries have in the recent past been expanded to include deserving cases in private universities. The Board is now also financing post-graduate Masters and Doctoral studies.

The Board is also charged with the task of recovering the loans granted, including those granted by previous schemes, which it replaced in 1995. The Act charges the Board with the responsibility of establishing a revolving fund, solicit for funds from sources other than government and seek assistance to promote its functions generally from other quarters other than government. The Board can and has in practice entered into contracts with financial institutions for the purpose of disbursement and recovery of loans it has disbursed. Under the Act, loanees are obligated to commence repayment of their loans one year after graduation and are not allowed to use prevailing market conditions such as lack of employment for default. Employers are also obligated to notify the Board immediately they employ a beneficiary of the Fund and to effect such statutory deductions as the Board may require for purposes of enabling the individual repay the loan.

The Board has historically received financial support almost exclusively from government. Annul allocations over the last three years have averaged Ksh 1 billion. The Board has also improved its loan recovery portfolio and is collecting over Ksh 60 million monthly from past beneficiaries.

Sugar Development Fund (SDF): This fund is financed from the Sugar Development Levy, which is levied on sugar consumers at the rate of 7 percent of the ex-factory price of locally-produced sugar and 7 percent of the cost of insurance and freight (CIF) value for imported sugar.[33] This levy was worth Ksh 1.6 billion in the 2005/6 financial year.

The fund supports a wide range of activities, including infrastructure development in the sugarcane belt, the Kenya Sugar Board, the Kenya Sugar Research Foundation, cane development, and assistance to out-grower schemes with land preparation, factory development and refurbishing. Out-grower institutions, millers, sugarcane growers and small scale transporters are also targeted beneficiaries. Factory rehabilitation and sugarcane development funds are disbursed in the form of loans. Roads development, Kenya Sugar Board administration, and research funds are given out as grants. The Sugar Development Fund is crucial to the financing of the massive reorganization and investments that are taking place in the sugar sector.

Poverty Alleviation Fund: The Fund was set up through the Ministry of Planning and National Development. Qualifying groups are given soft loans,

[33] There are proposals to reduce the rate to between 3 and 4 percent to enable millers to increase the price they pay for cane deliveries.

which they in turn provide to individual members to start income generating projects. This Fund is set up through Kenya Gazzette Notice No. 303 of 26th March 1996. The Fund is administered as a Semi-Autonomous Government Agency with trustees.

Community Development Trust Fund (CDTF): This Fund is set up through Kenya Gazzette Notice No. 303 of 26th March 1996. The Fund is administered as a Semi-Autonomous Government Agency (SAGA) with trustees appointed by the Ministry of Planning, and the European Union. The first phase of the Community Development Programme (CPD-1) run from 1996 to June 2001, closing officially on 15th January 2004. By December 2004, the Fund was implementing two key programmes: the Community Development Programme-II and the Biodiversity Conservation Programme.

The main aim of the Community Development Trust Fund is to "assist Kenya in achieving economic recovery and sustainable growth, increased employment creation, poverty alleviation and capacity building of local communities".[34] According to the project auditors, the programme seeks to "devolved poverty alleviation activities to local beneficiaries by providing capital investment funds for two categories of development interventions: 1) Poor District Project Investments, and 2) Less Poor District Project Investments".

By December 2004, the European Union had increased funds to the CDTF for CDP-II activities amounting to Ksh 445,520,076.

Typical projects under the CDP-II have included community health centres and dispensaries, boreholes, primary schools, youth polytechnics and vocational training institutes, water projects, and bridges.

Youth Enterprise Development Fund: The Fund was set up in December 2006 through a Gazette Notice by the Minister of Finance. The fund's objectives include:

- Provision of loans to existing micro-finance institutions (MFIs), registered non-governmental organizations (NGOs) involved in micro-financing, and savings and credit co-operative organizations (SACCOs) for on-lending to youth enterprises;
- Attracting and facilitating investment in micro, small and medium enterprises'-oriented commercial infrastructure such as business or industrial parks, markets or business incubators that will be beneficial to youth enterprises;

[34] From "External Financial Auditing Service Consultancy: Government of Kenya/EC Community Development Trust Fund/Community Development Programme Phase II (DP Financing Agreement NO 6316/KE Audit Report No 7: Financial Statement from the period 1st July 2004-31st December 2004. Prepared for the CDTF by Kigathi & Associates, Nairobi.

- Supporting youth-oriented micro, small and medium enterprises to develop linkages with large enterprises;
- Facilitating marketing of products and services of youth enterprises in both domestic and international markets; and
- Facilitating employment of youth in the international labour market.

Recognizing that targeted youth may be lacking in enterprise and workforce skills, the government proposes "intensive capacity building among the youth" to be achieved through skills training at "rehabilitated youth polytechnics and the National Youth Service alongside an elaborate district-based "sustainable and integrated training system" as well as "a national business plan competition and intensive training for qualifying participants".[35]

One half of the fund is distributed to all the districts equitably with the second half being divided as a factor of young persons in a particular district. About 30 percent of the initial Ksh 1 billion was disbursed through the Constituency Youth Enterprise Scheme (C-YES) chaired by a District Social Development Officer. Each constituency received Ksh 1 million with a ceiling of Ksh 50,000 per qualifying applicant. To qualify for this fund, one has to belong to a group legally registered and in existence for at least three months, be an entrepreneur, and the group must have a bank account and be in good standing in community. Loans are repayable in 15 months with a three-month grace period and are interest free, though an "administration fee" of 5 percent is charged. The group must submit a business proposal to the Divisional Social Development Officer who assesses it and forwards to the District Social Development Officer for approval.

The other half of the fund is administered through qualifying Micro-finance, SACCO, NGO, government agencies and statutory financial intermediaries of which the Kenya Rural Enterprise Programme (K-Rep), Kenya Women Finance Trust (KWFT), Kenya Industrial Estate (KIE), Kenya Union of Savings and Credit Cooperatives (KUSCO), Business Initiatives and Management Assistance Services (BIMAS), Nyamira Tea Farmers SACCO, Agricultural Finance Corporation (AFC), Werugha Financial Services Association, Taifa SACCO Society, Family Finance Building Society, Smallholder Irrigation Schemes Development Organization, Kenya Poverty Reduction Volunteers, Lokichogio Cooperative SACCO, and Kenya Entrepreneurs and Enterprises Foundation (KEEF) qualified for the first round of funds.

[35] Communication from Argwings O. Owiti (Public Relations Officer) and Samuel M. Wachenje, Personal Assistant to the Permanent Secretary, Ministry of State for Youth Affairs, Office of the Vice President.

These financial intermediaries would use their own criteria to reach out to the youth and would have a ceiling of Ksh 500,000 for any individual group and beyond, which they had to seek consent of the Ministry. 10 percent of the Fund grant was reserved for operations and to meet other strategic purposes set out in the establishment of the Fund, such as “promoting youth employment in foreign markets”.

Women's Enterprise Development Fund: The Fund is apparently inspired in part by the Youth Enterprise Development Fund and will most likely replicate the delivery structure set up for the former. Like the youth fund, the fund has been capitalized at an initial Ksh 1 billion.

Kenya Social Action Fund: This Fund has been proposed within the Ministry of Planning and National Development. It appears in the *Economic Recovery Strategy for Wealth and Employment Creation* but has not been realized.

According to the Investment Programme for the Economic Recovery Strategy, the Social Action Fund was to “support and finance the implementation of productive economic community-driven development projects” in the framework of “community project development, improved planning, and transparent selection and financing”.[36]

Housing Fund: The Fund was set up through the Housing Act of 1976 and as the financing instrument of the National Housing Corporation (NHC). It was set up through the same Act of Parliament. It has since become moribund and is one of the targeted government interventions under the new housing policy. Through the fund, the National Housing Corporation would construct houses, which local authorities and individual beneficiaries would repay over a period of as many as 40 years. The NHC has built about 40,000 housing units since inception. It has also facilitated acquisition of site and service schemes for many schemes. The NHC itself has been in decline and in 2005 only invested Ksh 50 million in new housing projects. Under the new housing policy, it is targeted for revival and is in the process of issuing a government-backed debt instrument worth Ksh 5 billion at the Nairobi Stock Exchange.

Social and Community Enterprise Capital Development Fund: This Fund is contained in independent member legislation moved by Hon. Dr Josphine Ojiambo, nominated Member of Parliament. The motion for the Bill was moved and passed in November 2006 and the draft Bill by the same title published in April 2007. The Bill sought to create institutional infrastructure for social

[36] Government of Kenya (2004: 59)

enterprise-based delivery of finance to deserving individuals and not, as the title suggests, finance the development of social enterprise.

Other Funds: Numerous other significant funds exist at various ministries. The Ministry of Agriculture has, among others, a Coffee Development Fund and a Cotton Development Fund. There is also talk of a National Sports Rotary under the Ministry of Gender, Sports and Social Services.

Sector-based development finance intermediation schemes

Sector-based development finance schemes include the Kenya Tourist Development Corporation, the Agricultural Finance Corporation, the Industrial and Commercial Development Corporation, the Industrial Development Bank, and the Kenya Industrial Estates. These Development Finance Institutions (DFIs) were established in the 1950s and 1960s to provide credit to Kenyans during a period characterized by extreme financial exclusion, a very limited capital market base and extremely conservative commercial banking institutions.[37]

At independence and after, the DFIs played a significant role in providing credit to various target groups and are largely responsible for the emergence of the new African industrial and commercial economic elite.[38] As a group, these institutions hold huge assets. There is an ongoing vicious debate about the need and future of these institutions, majority of which have suffered abuse and decline owing to the many factors that have bedeviled state enterprises over the last two and a half decades. There is need to expand this discussion to include the possibility of reforming these institutions to provide the much needed development finance for individuals and communities experiencing historical, area and gender-based financial exclusion.[39]

The Industrial Development Bank (IDB) was established to provide medium and small scale development credit. The Industrial and Commercial Development Corporation was expected to provide medium and large scale credit and equity investment for industrial development as well as small and micro enterprises (SMEs) while the Kenya Tourism Development Corporation (KTDC) was

[37] For a fairly objective rendition of the social purpose histories of these firms, see Rothschild Donald (1993).

[38] The Agricultural Finance Corporation, the then Land Bank, and the Agricultural Development Corporation all designed schemes that helped Africans purchase land in the highlands from former White owners.

[39] The significance of such a re-orientation can be gleaned from the historic role played by the Industrial and Commercial Development Corporation (ICDC) founded in 1954, first in working to expand and establish new industries in Kenya and after independence by ensuring Kenyan Africans held majority stakes in such industries. The ICDC and its venture capital spin-offs—ICDC Investment Company and ICDC Properties Ltd—are the most prolific investment companies in the history of Kenya's industrial and property development.

established to provide long term funding for tourism development, especially hotel infrastructure. The Kenya Industrial Estates was set up to advance small scale light industrial credit as well as set up workspace for light industry. The Agricultural Finance Corporation was set up to provide farmers with credit, especially to meet their financing requirements for production.

DFIs made a sterling contribution to the economy in the first two decades of independence, but began to decline in the late 1980s and through the 1990s. By December 2004, all the five DFIs had a total asset base of Ksh 9.5 billion, which was nearly half what they had a decade before. Their total loan value stood at Ksh 18.5 billion, a good part of which was unpaid interest on non-performing loans. This asset and loan portfolio compared poorly with mainstream commercial banks, which advanced loans totaling Ksh 286 billon, and SACCOs, which advanced Ksh 60 billion.[40]

Overall, the DFIs are viewed as a lost opportunity and badly in need of reform. Most of them reported losses up to 2004, and had a despicable lending record, some with no more than 1000 clients. Most losses have been incurred on account of provisioning for non-performing loans, with a good number of these clients simply refusing to pay.

The government has had a very difficult time justifying expending more resources on the DFIs. Most of the DFIs require massive restructuring and only those that lend to agriculture have received significant government support. There exists a genuine case for government involvement in restructuring the DFIs to supply financial intermediation to sectors and actors in the economy, such as women who have suffered from historical financial inclusion. It is conceivable that DFIs can be restructured to provide large scale secondary financial intermediation facilities to the fledgling micro-finance sector. Such restructuring should be made in a way that the new statutory purposes and working ethos are entrenched in law. The shareholding and management structure of these institutions should also be opened up to reflect this new constituency. A more comprehensive analysis of such purposes and the envisaged new financial intermediation is provided in later sections of this study.

General Critique of the Devolved Funds

It does not seem that the various sub-sovereign and devolved finance schemes have developed from a consistent application of some underlying principles of devolution. There is, however, increased consensus that devolved and sub-sovereign funds are a welcome departure from previous central government

[40] For an analysis of the current difficulties facing majority of these DFIs, see Murgatroyd Paul and Gachuba Peter (2004).

funding arrangements and offer a novel way of financing community development.

Unfortunately, though they are intended as economic instruments to drive particular social interventions, these funds have been designed and implemented outside a clear social development policy. This makes it difficult to locate some clear prior framework against which to evaluate their achievements. The funds have also been implemented without regard for a clearly spelt out policy and framework for decentralization. This denies them a coherent institutional framework, making it difficult to evaluate success or failures and make recommendations for their improvement. This has not been helped by the appearance of 'grafting' and 'afterthought' in the introduction of some of the schemes, including the now popular Constituency Development Fund, the Youth Enterprise Development Fund and now the Women's Enterprise Development Fund. Though they have become central pranks in government policy, these funds actually began their way into statute or government frameworks outside it. They are, therefore, difficult to pin as emblematic of a clear cut government fiscal regime with regard to management of public finances. Not unrelated to this, the funds seem to suffer a constituency stakeholder capture, with the most obvious one being the CDF, which is in many ways a fund for Members of Parliament.

Given the diversity and differential legal, administrative, juridical, functional, national reach and complexity of the various funds, it is not productive to treat the schemes as a single homogeneous entity. Given also that the various schemes are in different stages of maturity, it is also inappropriate and difficult to draw universal lessons and principles about their application. In reality, each of the schemes presents a unique approach and moment in attempting to offer financing solutions to various social problems when the fund was created.

The complexity, national, geographic and community spread of devolved and sub-sovereign finance points to the enormous and largely untapped potential to use these funds as one of the cornerstones of a vibrant, progressive and universal community development finance mechanism. The public nature of devolved and sub-sovereign finance makes the funds especially attractive for their potential to moderate and apply pressure to other financial regimes in the economy. Such financial regimes include customary and marital tenures that determine how families allocate resources to women, and the market-based institutions such as the banking and capital sectors.

The fund schemes are also strategically useful within a framework of strategic capability and asset development at both individual and community levels. A good number of the funds are designed to lead to immediate and long term asset accumulation, such as financing establishment of infrastructure holdings in tourism and establishing small and medium scale commercial and light industry.

Yet, other fund schemes are directed at crucial human capability-enabling capital sectors such as financing primary, secondary and post-secondary education. Other schemes are set up to provide long term regional development capital in ways that address particular expressions of social exclusion and poverty. Later sections of this study will seek to show how such funds can provide the genesis of a broader intervention to help raise the strategic capability and asset base of the poor and socially-excluded individuals and communities.

Joining Up

It will be clear, however, that some joining up will be necessary if one was to achieve the required synergies and pulling together necessary to make the fund schemes a compelling element of a well thought out gender-responsive national asset-based community development initiative.[41] In the absence of such joining up, the schemes, in the words of the Permanent Secretary, Ministry of Planning and National Development "can be quite problematic especially in the current context where they are characterized by different institutional structures and arrangements, which apply different approaches to service delivery leading to duplication of efforts and overlaps (and) resulting in opacity and wastage".[42] Such joining up will be attempted later in this study principally through a proposed comprehensive Social and Community Benefit Asset Endowment Scheme.

Subsidiarity social inclusion and community visioning

It is also evident that a clear and much needed correction is needed to bring the 'gender', 'participation' and 'community visioning' into a joined-up framework of devolved funding and socially-responsive local community development. As it were, the present variegated schemes were designed without much regard for inclusion, community visioning and gender mainstreaming. The result is that even where they seem to have worked in favour of women and inclusion, these outcomes were on the large part unintended.

It is also essential that an elaborate and participatory community visioning process is placed at the centre of the various devolved and sub-sovereign finance schemes.[43] This would entail coming up with an area-wide strategic plan that

[41] The need for such harmonization has also been identified by other critics. See for instance the report of the Hanns Seidel Foundation, July 2006 Conference "Making decentralized funds work: An expert forum on principles and standards of implementation", Nairobi: Hanns Seidel Foundation.

[42] Dr Edward Sambili, *op cit*; See also Mapesa Benson M. and Thomas N. Kibua (2006).

[43] The practical necessity for this type of local economic and community development regime is also noted by, among others, Chitere and Ireri (2004).

has emanated from a wide participatory process of identifying where community members want to go, how they want their community to 'look' like and authorizing a broad financing plan for the strategy.[44] Chitere and Ireri (2004) call for a re-orientation of development strategy "so that it starts at the local community level and cascades upwards to sub-district and regional levels", a measure that would confer "greater decision making and control to local communities".[45] This study picks up these suggestions later in its formulation for a new structure for local economic and community development.

It will also be essential to foster a local economic and community development regime that is capable of auditing the impacts and outcomes of such local development initiatives with a view to enhancing capacities for future planning and action and securing the information necessary to drive evaluation and accountability.

Accountability, juridical competency and autonomy

It will be difficult to deepen the scope of the funds and make them accountable to various diverse constituencies of society at both community and national level without addressing their juridical personality. To carry out their mandate effectively, including a revised mandate to drive gender and social inclusion, each of the schemes would need sufficient legal authority through substantive Acts of Parliament.

It is also desirable that a particular unit of a scheme, such as the Constituency Development Office, is conferred own and independent juridical personality as a corporate body that can initiate own independent actions. In this framework, it would be possible for locals to sue the particular unit in view of its performance of its statutory mandate, but also for other civil and criminal offences. The originating statute should be clear that officials, including Members of Parliament, can be removed through a court of law and should provide mechanisms for appointing new officials. The same can be achieved by requiring LATF to be run by independent juridical entities set up as Community Development Finance Institutions by local authorities. It may also be necessary to bring the schemes, or their social and community benefit purposes, under a single or consistent regulatory regime.

Accountability and juridical competency can also be better secured by engraining sufficient subsidiarity so that individual schemes and scheme units—

[44] For a description of Community Visioning, see National Civic League: The Community Visioning and Strategic Planning Handbook. Various variants of such a process exist. It would be necessary to capture some of the basic ingredients of a model process and procedure in statute (or through subsidiary legislation).

[45] Chitere and Ireri (2004).

such as the CDF broadly and a constituency unit—are enabled and empowered to make own decisions within the broader context of local community visioning. Each sub-sovereign fund unit, such as a unit of LATF or CDF as well as the entire fund scheme should also be a mandatory subject of a vigorous social and community benefit audit. A good performance on such an audit should be a prerequisite for further fund disbursement to a scheme unit. Entire fund schemes should be evaluated/audited ex-ante, mid and post-ante. In order to do this, it will be necessary that the schemes and their units adopt vigorous strategic plans that capture the goals they intend to pursue over a certain period, how long they wish to pursue them, and the means they will employ. These audits can be presented to institutional stakeholders, parliament, local authorities, etc.

Each scheme should also be chartered by an appropriate authority set up specifically for the purpose. The charter should confer the scheme with the juridical complexity and autonomy necessary to carry out its mandate. Each unit of a scheme should be similarly chartered. The chartering authority should be answerable to parliament through a standing committee with members appointed by the president.

It will also be necessary to ensure that each scheme and its constituent sub-parts have significant community presence. Regulation and the very set up of the schemes should ensure that they do not overlap in functions, are staffed by competent personnel, are accountable for their purposes to communities and to a given regulator, are transparent in decision making, and work within an overall framework that aims to build the asset base of local communities.

Community institutional asset class

It is imperative that the fund schemes are harmonized to recognize and work with other elements in the community development system, especially the voluntary and not-for-profit sector and the emerging social investment industry, to nurture a specific asset class primed for community development. Left to their present cause, majority of the programmes, especially those directed at the social sectors, help multiply government institutions such as primary schools and hospitals at community level. Available evidence suggests that communities are better empowered where such funds were used to help build community social projects, such as social enterprise-based water and irrigation projects, community producer utilities such as cattle dips and markets, etc.[46] Later sections of this

[46] Communication from Moses Ng'ang'a, CDF Dagoretti; K. Macharia, CDF Mathira; and "Draft report on CDF best practices, by the Collaborative Centre for Gender and Development (CCGD) made available courtesy of Eric Kimani at the CCGD.

publication will investigate a possible role for a strategic use of these financing schemes to prop up these and other institutions of the social economy.

Leveraging private sector finance for community investing

It will be obvious from even a casual analysis that careful thought has not been given to how the fund schemes can be used to leverage and pull in resources from the capital and banking sectors for the purposes of driving socially-inclusive local community development. To the contrary, the popular thinking so far seems to be that the public sector can always be relied on to provide all the financing needs of local community development. This is unrealistic and defeatist in the long term.

Community development financial intermediaries

It is also emerging that devolved funding, especially the Constituency Development Fund, but also potentially all others and in particular HELB, LATF, Community Development Trust Fund, the development finance intermediaries and the regional development authorities can play a central role in helping seed specialized financial intermediary institutions referred collectively in this study as Community Development Finance Institutions (or CDFIs). In turn, CDFIs such as Community Development Trust Fund and Community Development Business Loan Fund have proved particularly well suited in going to the root of the core problem of financial exclusion.

PART III

GETTING THE FOUNDATIONS RIGHT: CONCEPTUAL FRAMEWORK FOR NEW WEALTH AND PROSPERITY

> Development consists of the removal of the various types of unfreedoms that leave people with little choice and opportunity of exercising their reasoned agency.
>
> Amartya, Sen[47]

[47] Sen Amartya (1999). Amartya Sen is Professor of Economics and Philosophy at Lamont University, and winner of the Noble Prize in Economic Science in 1998.

RETHINKING WEALTH AND WELFARE

Capability Approach to Well-Being and Human Development

One of the key advances in development theory and practice over the last two decades has been the rise of the Capability Approach (CA) to well-being and development, also known as the human development theory and advanced originally by economist philosopher Amartya Sen. The Capability Approach offers a conceptual and practical framework for evaluation of individual well-being and social states and the design, implementation and evaluation of socio-economic policy and programmes.

The core attribute of the Capability Approach is its focus on what individuals are in effect able to be and do—their capabilities and potential or achieved functionings. According to the approach, the evaluative space in social arrangements and policy design should focus on what people are effectively able to do and be, on the quality of their life and on removing obstacles in their lives so that they have greater freedom to live the kind of life which, upon reflection, they find valuable. Thus, the basic proposition within the CA is that social states should be evaluated according to the extent of freedom members have to promote or achieve functionings they value. In this formulation, progress, development, poverty reduction or other desired social states happen when people have greater capability or freedoms to do and achieve what they value and desire to be. An individual's capability to achieve functionings that she values should, therefore, provide the criteria for evaluating various social arrangements.[48] In this formulation, other evaluative criteria such as consumption or income and commodities are inadequate to the task of measuring or determining well-being as they fail to adequately capture an individual's state of being. Such a state is best captured by an individual's functionings. Individual functionings can include, for instance, being well-educated, being well-sheltered, being healthy, being well-fed, etc.

Functionings and capabilities

The key ingredients of the Capability Approach are functionings and capabilities. Functionings represent "the various things that a person may value doing or being".[49] Being well-educated, enjoying excellent health, enjoying warm reciprocal relations are all things a person may find valuable. Subsequently, according to Amartya Sen, "In assessing the standard of living of a person, the objects of value

[48] Sen Amartya (1995:2).
[49] Sen Amartya (1999).

can sensibly be taken to be aspects of the life that he or she (has) succeed(ed) in living".[50]

Capability, to be distinguished from functionings and freedoms, represents "a person's capability to do valuable acts or reach valuable states of beings" and "represents the alternative combinations of things a person is able to do or be".[51] Capability represents "the various combinations of functionings…that the person can achieve…(a) set of vectors of functions, reflecting the persons freedom to lead one type of life or another…(or the persons freedom) to choose from (several) possible livings".[52]

The difference between functionings and capabilities is crucial to the development enterprise. Whereas a functioning represents an accomplishment, capability represents capacity to achieve. Capability relates to the freedom one has to achieve something, the real possibility that one has to live the life one has reason to choose. Even if a physically challenged person were in possession of a bicycle, she would lack the capability to use it and is thus lacking in freedom, in that respect, to achieve a core functioning of enhanced mobility.

Central to the Capability Approach is the key question—what should be the end of development? According to the this approach, well-being and development should be conceptualized in terms of an individual's ability to function or, to put it another way, the person's effective chance to undertake the actions and activities that she finds meaningful and to be what they desire or want to be. It is this ability to do something, or be somebody that makes life worthwhile. In this respect, what one can achieve and do with ones life is important and valuable, and equipping that individual to do so and to become what they desire is the work of doing development. The end of development is thus the human person, and doing development consists of raising and effecting the various capabilities that individuals need to achieve desired functionings.

It follows in this formulation that some functionings are basic and include being healthy, ability to work, being well-educated, living in a good house, living in a conducive environment, being secure, enjoying the sanctity of ones bodily integrity, being part of and able to live out life as a full member of a choice community, having fun, etc.

Capabilities are at the core of individual functionings and designate the freedom to achieve desired states. This approach to development, therefore, evaluates development policies according to their impact on people's capabilities and how this transits into enhanced or improved functionings. Do people have access to high quality education? Are they, therefore, better educated? Are people able to

[50] Sen Amartya (1987:2).
[51] Sen Amartya (1993).
[52] Sen Amartya, (1992:40).

effectively participate in public life? Are there institutions and cultures that enable participatory, deliberative and free democratic engagement? Are people thereby so engaged in public life? Are health facilities in a community functional and accessible to all? Are the resources necessary to ensure ones health such as hospitals, clean drinking water, protection from diseases and infections available? Are people healthier as a result?

Instinctive and instrumental value

A key analytical and functional distinction in the Capability Approach is that between the ends and means of well-being and development. In this distinction, only ends have intrinsic value. Means are instrumental in reaching the desired goal of well-being and, thus, have instrumental value. So is a goal intrinsically or instrumentally important?

What, then, according to the Capability Approach are the ends of well-being and development? Well-being and development should be conceptualized in terms of a people's capability to function, on their effective possibility to undertake the actions and activities that they value, to pursue that which they value and desire to be. It is the total of one's achieved functionings that makes life worthwhile and valuable. The goal of any development effort should, therefore, be to increase ones capability endowment. According to the approach, what is ultimately important is that individuals have the capabilities to lead the kind of lives they desire, to do what they desire and to become that which they long to be. Once they have this capability, it is up to them to do what they desire with it.

Following in the framework and mandate of human rights, which holds that certain rights are inherent and basic to the human condition, it follows that certain capabilities and functionings are mandatory. It also follows that social states can be evaluated on the basis of their ability to provide a certain requisite capability and functioning threshold.[53] To hold that certain functionings and, thus, capabilities are foundational to the human condition is to push the Capability Approach from being a critical proposition within philosophical liberalism to a practical development tool through which we can design and evaluate policy, programmes, development plans and interventions, and the entire actions of governments and states. Basic capabilities in this instance refer to the freedom one has to do some basic things that are necessary for survival and to avoid or escape poverty. This does not necessarily prescribe a certain minimum of capabilities but does appeal to a certain threshold of capabilities necessary to escape or overcome/avoid poverty or, in Sen's wording, "the ability to satisfy

[53] This is not an argument or position of the Capability Approach as advanced by Sen. Sen has been shy to endorse a certain set of capabilities or a certain functioning threshold as a basis for the Capability Approach.

certain crucially important functionings up to certain minimally acceptable levels".[54] This threshold will of necessity be dynamic and will depend on particular situations and social contexts.

As an evaluative framework, the Capability Approach rejects the assessment of individual well-being and social states based, for instance, on an income or utility measure such as a dollar a day. While income can be an important means to overcoming disadvantage, it can only serve as a rough proxy for capability; it does itself not constitute capability and cannot equate to a realized functioning. It may be neither intrinsically nor instrumentally important. It is possible for an income poor person to use a social pension to consume cheap liquor other than send a child to university.

The distinction between capabilities and functionings also provides some useful devise with which to arrest some previously problematic reality in development work, namely that of the relative inability of individuals possessing the same set of capabilities to convert these into achieved functionings. Within the approach, the ability to convert capabilities to functionings can depend on various factors at individual and institutional levels. Most importantly, individuals may be inhibited from achieving conversion owing to their social vulnerability arising from their positions in society. Women may be unable to acquire capabilities and achieve requisite functionings even where the capabilities are present, owing to prevailing gender relations and roles. Slum dwellers may achieve certain capabilities and fail to convert them into achieved functionings owing to prevailing power relations and the distribution of opportunity and resources in the economy.

By allowing a moment of indeterminacy, a Capability Approach to development is thus intuitively contrary to welfarist approaches to development, which rely almost exclusively on utility criteria to prescribe well-being. Power relation between the sexes, oppression and powerlessness and other drivers of social exclusion and inequality come to the fore in this new interface between capabilities and functionings. The approach is therefore not only useful for providing the informational basis of determining well-being and development, it is also useful for purposes of designing social policy interventions based on a prior conceptualization of equality, social justice, equal opportunity and a certain quality of citizenship.[55]

Freedom, agency and choice

Finally, one of the most progressive aspects of the CapabilityApproach is its accent on freedom, agency and choice. According to Sen, "The "good life" is partly a life

[54] Sen Amartya (1993: 41).

[55] The Capability Approach is itself not a theory of justice and does not prescribe a certain minimum quality of life standards for citizens.

of genuine choice, and not one in which the person is forced into a particular life —however rich it might be in other respects".[56] Freedom and individual agency, therefore, has an intrinsic value. The development enterprise can, therefore, not constitute a process of simply providing a higher standard of living for citizens without advance of democratic and participatory processes and freedoms that under-gird the citizen's own capability and opportunity to dictate what development is for them. Citizens are in this respect not passive recipients of social welfare policies, institutions and expenditures, but assume an active role in the determination and implementation of social and economic development policy and programmes.

In this latter view, an attempt to use the capability framework to drive social policy will not only be confronted with the question of which capabilities and functionings are relevant but also how to derive and deliver them. How do we arrive at a particular list for purposes of social policy? How do we avoid likely bias in determining what capabilities and functionings to pursue? One not so obvious solution to this lies not in deciding which capabilities or functionings to pursue but on an acceptable criteria and methodology for selecting them. This is especially the case since capabilities and functionings are not themselves static and evolve over time.

In determining such criteria and methodology, it is important that the role and place of agency, a people's ability to determine what is important and worthwhile for them, is paramount. It is also the case that the choice of capabilities and functionings will be context-dependent and, therefore, faithful to the realities of a particular geographical or other community expression. Again, given the plurality and open-ended nature of many capabilities that individuals have reason to value "there is a strong methodological case for emphasizing the need to assign explicitly evaluative weights to different components of quality of life (or of well-being) and then to place the chosen weights open for discussion and public scrutiny".[57] These prerequisites in turn call for deliberative democracy and participatory decision making in local economic and community development.

Sen has, however, been reluctant to move beyond requiring that public decisions be democratically agreed upon and have positive consequences for the expansion of the freedoms that people actually enjoy and that enable people to live the kind of lives they desire and value. Clearly, some clarity on how to bring about this kind of participation and consequentialism is called for. According to Ingrid Robeyns,[58] such criteria and methodology must include a requirement for explicit formulation where the list is made explicit, discussed and defended through public consultations and deliberations. The method for generating such

[56] Sen Amartya (1966:59).
[57] Sen Amartya (1999: 81:
[58] Robeyns Ingrid (2003: 61-92)

The Capability Approach and development theory and practice differentiates between democratic decision-making and participatory decision-making. In this differentiation, democratic decisions refer to decisions taken by freely elected governments—including local councils and sub-federal states. Participatory decisions are decisions taken directly by the people affected by that decision. While democratic decisions require the holding of free and fair elections with the resulting legislative and executive bodies making decisions on behalf of the electors, participatory decision making assumes a process of continuous consultation, participation and validation of decisions directly by members and through constituent groups. Participatory local economic and community development may require a blend of these two traditions.

In the Capability Approach, the capability to shape one's own future by participating in the life of community is not restricted to participation in public processes but also, fundamentally, the capability to participate in markets. "We have good reasons to buy and sell, to exchange, and to seek lives that can flourish on the basis of transactions. To deny that freedom in general would be in itself a major failing of society".[59] Accordingly, individuals should have the fundamental "right to interact economically with each other".[60] The freedom to participate in markets needs, however, to be matched with the freedom to participate in other non-market institutions of society. Since those who enjoy greater economic freedoms and command greater resources often trump the freedoms of others, social institutions, including those of the market, need to be arranged with respect to "a fair distribution of power"[61] in ways that secure the capabilities of the less powerful and vulnerable for claim making and self-assertion. This latter would entail a specific process of empowerment, rebuilding of institutions and capacity building.

It would seem, therefore, that decision-making within the Capability Approach requires a mechanism that would solve the tensions that arise from the exercise of the power of agency and the prevalence of privilege and advantage with a view to securing the process of determining and producing overall social good. In other words, decision making with the Capability Approach framework has to be faithful

[59] Sen Amartya (1999:26).
[60] Sen Amartya (1999:116).
[61] Dreze and Sen (2002:353).

to principles and values that allow the multi-dimensional character and nature of human well-being. We propose elsewhere a process and system of local economic and community development that would be faithful to such a dictum.

How might the Capability Approach alter "mainstream" thinking and practice regarding devolved and sub-sovereign finance? First, devolved and sub-sovereign funds have a clear "economic" rationale that is based on raising the basic incomes of the target groups or substituting for expected consumption of especially public services like secondary school education. Many of these funds are designed primarily using an investment criteria that precludes them from undertaking or financing certain types of activities. The Youth and Women's Enterprise Development Fund, or even the CDF, for instance, cannot fund a women's literacy project, for instance, even where such a project may have higher returns in terms of capabilities and functionings than advancing credit to them. A literacy programme can, for instance, help women 'see' that they are equal to men in terms of potential, that they are protected by law from violation of bodily integrity, that they can take better control of their reproductive health and functions and that they can eliminate 80 percent of the causes and incidence of infectious diseases in their families. Learning to read and write can also be an important prerequisite to acquisition of critical life skills, including filling out loan forms and better managing enterprises, accessing and participating in public office, etc. In this context, clearly a literacy project ought to be part of a credit programme for women who do not know how to read or write.

It is also imperative that consensus be arrived at regarding the ends and aims of the various funds relative to the ends of expanding human capabilities and freedoms; that the very design of the fund mechanisms and the their implementation accentuate the intrinsic value of human freedoms, agency and choice, and that these fund mechanisms and the funds themselves are availed to advance policy goals and programmes that are identified and implemented through processes and agencies that engender participatory and democratic decision making.

Re-membering Wealth and Prosperity

Decades of work to secure gender-responsive and socially-inclusive community and local economic growth, as well as increasing globalization and disparities in the economic fortunes of even citizens in ‘prospering’ economies, has led to the rise of new approaches and practices to grow local and national economies. It is now acknowledged that economic growth itself is not synonymous to development, though it may constitute an essential prerequisite.[62]

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[62] See for instance Thambo Mbeki’s 24th August 2003 weekly letter published on the ANC website www.anc.org.za/ancdocs/anctoday.

In this 'new' conceptualization, the terms "growth", "development" and "prosperity" are used with some degree of caution. *Growth* is what happens when there is an increase in the quantities of particular phenomena such as jobs, population and income. Growth can also refer to changes in the quality of phenomena such as better and more secure jobs, better education, etc. *Development*, on the other hand, refers to structural changes in the community in question and can apply to such phenomena as changes in the distribution of income and assets, the functioning of a community's institutions and how resources are used in the community. Subsequently, it is conceivable that a community can experience negative growth following the increase in such phenomena as crime, unemployment, ill-health, etc. It is also conceivable that development can be positive or negative. *Prosperity* refers to an individual's or community's planned or conscious movement towards achieving certain desired outcomes relating to development. Progress, in contradistinction with prosperity, may refer to an individual's or community's planned movement towards achieving certain desired outcomes relating to growth, such as a salary rise. Prosperity will result from lasting progress resulting in an enduring change—recognizable as irreversible development in the community.

In these 'new' approaches, wealth is no longer described in monetary value but the different types of capital, capabilities and resources that, taken together, sustain and enable prosperity for individuals, a community or a region. To compute an individual's wealth, for instance, one would have to take into account the person's health and predisposition to illness, educational and skill levels, current income and net asset holdings. To understand a regions' economy, it is important to assess and track several types of assets, including: 1) human capital; 2) social capital; 3) cultural capital; 4) legal and political capital; 5) natural resource capital; 6) environmental capital, and 7) financial capital. Each of these forms of capital must be conserved and increased if the region is to grow, be prosperous, stable, and sustainable.

In the resulting framework, diminishment of any one asset will undermine the others. Neglect of human capital, such as a failure to provide first-rate education or the failure to supply these first-rate health or education benefits to all sectors of the population will lead to fewer opportunities for businesses and residents to multiply financial assets. Weak social capital, such as may issue from gross gender and historical inequalities, failure to reduce poverty amongst all sectors of a population, or failure to evolve dynamic local not-for-profit community institutions translates into a reduction in competitiveness for a region's other capital resources.

In this vein too, low financial capital, such as insufficient diversification and re-investment, leads to social instability, high unemployment, and vulnerability to economic decline cycles. Similarly, a deteriorating natural asset base, such as

disappearing rivers or diminished forest cover, reduces investment potential, drives away new businesses, and undermines the quality of life for current residents. Understanding, factoring and tracking all forms of capital is crucial to the economic growth, regional and national prosperity processes.

The Asset Building Paradigm

Assets, as used broadly in this study, refers to capacities and resources that, taken together, enable individuals, households and communities to have choice regarding what the good life is for them, to make those choices and to have a reasonable chance of realizing them.[63]

Asset building, or the processes and ways individual, community and national assets are nurtured and accumulated, is important because it focuses on policies, institutional processes and stratagem as well as the everyday individual and community actions that go into building a wealth portfolio. Asset-based development begins from the assumption that individuals and communities have particular asset acquisition potential and that it is possible to manipulate these to, in the first place, supply positive growth of certain desirables such as good education, employment, better and more secure income and to engineer real progress in the community. An individual's or community's asset base—that set of gifts, skills, capacities and other endowments, as well as the stock of institutions and corporations within the community—is vital to progress.[64]

Individual level assets include one's basic, tertiary, professional and technical education; one's cumulative workforce training, skills and experience; one's health; personal financial holdings, real estate and other immovable, movables such as jewelry and cars, etc. As we shall see later, individual asset-building is a steeply gendered terrain and presents itself differently for men and women.

Community level assets can be vast and include a region's or community's financial capital, natural resources, human capital, social capital and the set of institutions, legal and political capital.[65] These key components of a community's or region's asset and capital holdings are described below.

[63] This framing of assets is adopted using criteria advanced by Amartya Sen's formulations of "functioning and capability" as well "substantive freedoms" (see various works by Amartya Sen).

[64] See Tibaijuka Anna Kajumulo (2003). Address to the Building and Social Housing Foundation consultation, "Agents rather than patients: Realising the potential for asset-based community development.

[65] For a detailed presentation of community assets, see First Nations Development Institute: A research framework for understanding asset-based development in native communities. See also Linneker Brian and Sarah Brandshaw (2003).

- **Financial assets**: Usually the most liquid form of assets, including stocks, bonds, savings, trust funds, and other forms of monetized investments.
- **Physical assets**: Include utilities such as markets, water systems, electricity establishments, transport systems, communication systems, as well as the stock of plant and equipment available to and owned by individual and the community. They are critical for local economic activity and essential as a means of enhancing the productivity of other assets. Some physical assets, such as electricity, water, sewerage, waste and telephone utilities can generate own income if well run.
- **Natural assets**: Refers especially to the physical stock of land, forests, wildlife, and other naturally-occurring resources such as oil and gas. The ability to harness these resources responsibly and sustainably provides the base for local economic activity.
- **Institutional assets**: Refers to the range and complexity of institutions and organizations within a community. Institutions can attract resources into a community and help keep them there. Social and community development institutions include the entire range of civil society, CBOs, NGOs, and not-for-profit intermediaries in the various sectors. Local institutions include local enterprise organizations and their social and ethical practice.
- **Human capital**: Refers to the stock of skills, education, knowledge and experience available in a community. It also refers to the physical and mental health of members of a particular community and their predisposition to illness.
- **Cultural assets**: This includes customs, traditions and local knowledge systems. It also includes the range of languages, material art, music, dance, etc. Material expression of these assets and their performance can generate income and other assets for individuals and community.
- **Social capital**: Refers to the set of social relations within a community. Positive and supportive relations are vital to the productivity of other assets. Local community empowerment, civic engagement, democratic consolidation, volunteerism, gender mainstreaming, social justice and leadership development are essential mechanisms for generating social capital.
- **Legal and political assets**: Legal assets refer to the range and complexity of legal rights and claims available to individuals, groups and corporations in a community. Political assets refer to the sovereign status of local juridical institutions, ability to generate own revenue, tax status, etc. They are a near pre-requisite for creating and driving local economic growth and opportunity.

Increasingly, a nation's or region's economy and the entire set of institutional arrangements of society are being evaluated by the extent to which they enable progressive, universal and cumulative asset-building by their citizens and communities. Asset-building is actually the presumed goal of many households and communities in the economic development process. Through the voluntary exchanges of the market, individuals are assumed to get fair reward for their labour and expertise. These individuals in turn use these to generate savings, which are critical in the asset-accumulation process at individual and household levels. Many traditional asset-building strategies at individual level are, therefore, premised on the individual having quality education, training and experience, a stable income above one's basic consumption needs and available over long periods of time, and a personal aptitude to save and make 'wise' investment decisions. In reality, the majority of individuals hardly get this combination right. Moreover, 'market' conditions and institutions are such that they do not work the same way for everybody and at all times. Changing economic conditions, including the rise of an information and knowledge economy, have brought about new dynamics in the labour market, with jobs being more seasonal and requiring higher level skills than was necessary in typical industrial societies.

Moreover, and significantly in our case, these conditions and situations obtain and apply largely in industrial societies. In the case of Kenya, nearly 50 percent of the population are officially poor and do not boast much personal or household income. Many of these have little education and training and even those who do are unable to find gainful employment in the economy. For many of these, poverty is caused by their vulnerability to environmental risks. This vulnerability has grown over time as the individuals and their communities have been unable to cope with the demands of the colonial and post-colonial economy. Very rarely in the historical development of the Kenyan state have economic conditions been programmed to deliver real assets to individuals. Certainly, the Kenyan economy and its political expression negates even primitive/communal notions of asset building and sharing and is heavily inefficient and skewed in the way it distributes opportunities and rewards. In the recent past, owing largely to the management of the political economy, the Kenyan economy has been in a long recession that eroded the real assets of even previously 'well off' households and individuals. Individual vulnerability has also been exacerbated by rising incidents of physical catastrophe such as droughts. As we shall see later, the social economic status of many individuals in society, especially women, also predisposes them to social vulnerability.

The Kenyan state has historically not recognized 'the community' as an area of constructive asset-building. Many communities, therefore, lack basic assets and capabilities to meet the aspirations of their members. Where they exist, many of these resources, including educational institutions, hospitals, markets etc are not viewed as assets and are often plundered and abused. Owing to this historical

neglect to locate 'community' in development processes, Kenya also lacks a vibrant grassroots-based tradition of local economic and community development. This latter has worked to ensure that there is little institutional and organizational capacity to do asset-building work —to plan, grow and prosper local communities and their members.

Asset-building policies and programmes recognize the importance of assets and capabilities for individuals and communities and work to supply state interventions to make the acquisition of these possible. Unfortunately, for poor and socially-excluded individuals and communities, the state has often elected to perceive them as being bereft of any potential for meaningful asset accumulation and net consumers of social assistance and benefit. This orientation has virtually blinded the state about the potential and intrinsic value of asset accumulation for these individuals and communities. By way of contrast, the state has historically built into the fiscal, market and public institutional frameworks numerous structural incentives to build and protect the asset holding of those who already have investible income.[66] The whole property and investment regime is designed to secure the wealth of these individuals.

Community-Based Development Organizations as Civic Infrastructure for Asset Development

Crucially, the asset-based approach to local economic development assumes that many institutional and area-based obstacles to the development of a particular locality cannot be overcome through individual action alone but requires the activities of community-based organizations and institutions. Many of these institutions are required to overcome the collective action and economy of scale problems associated with local economic development. These institutions and those active in them are really the heart and soul of efforts at local economic development.

The health of a community is thus predicated not just on the availability of physical, human or financial assets, but just as much on the existence, quality and vibrancy of its institutional asset stock. Community-Based Organizations (CBOs) are in many ways the building blocks of continuing change in communities. They are the genesis of local voluntary, self-help capacity, build local leadership, build physical assets, design and run interventionist

[66] There are many illustrative examples of this point, including the setting up of stock markets, judicial systems, land tenure regimes, voluntary contracting, etc. In the Kenyan case, one of the most regressive examples was the policy granting civil servants leeway to establish businesses, which they promptly used to trade with the state. In many cases, a civil servant simply invoiced goods and services to himself. Often times, this involved supply of 'air'.

programmes, grow and support business formation, build and run health centres, and provide infrastructure for residents to enter and shape crucial development debate and agenda. Where community institutions are weak or absent, then the community's development will suffer. We revert to them in later chapters of this study.

Locating Asset-Building Within the Politics of Local Economic Development

Local economic development is usually a planned effort to build the asset base that increases the capacity of residents of a community or area to improve their quality of life.[67] Local economic development will also involve strategies that help individuals, households and the community to build and accumulate assets; ensure a local economic regime that increases the yield and benefits from these assets; minimizes the likelihood for local shocks and negative events; and reduces the impact of such negative environmental events on the quality of local asset holdings. Effective local economic and community development is achieved within holistic frameworks that place a premium on participatory and democratic bottom up planning that secures accountability and inspires hope and confidence in the future.

Our use of the term community assets in this report is very specific, and for good reason. Our usage assumes that there are resources in the area that are under-utilized or can be manipulated to achieve certain desired ends. It is conceivable that individuals in a community may have job skills or experiences that do not match what is presently in demand. It is also conceivable that a community may have educational and training institutions whose programmes do not quite match up to the required competency base in the market. Individuals and families in a community may have savings that they are investing outside that community. Communities may also have natural resources that could be of value as amenities for the development of economically-viable activities such as tourism.

Asset-based development is also attractive because typically, assets are embedded to individuals, places, regions or communities. Rather than, for instance, provide training for jobs that male workers must take elsewhere, which is important nonetheless, asset-based development also emphasizes training programmes that match jobs and opportunities that exist or can be created in a locality. Likewise, rather than aim simply to attract external resources or investments into a community, which is important, we also emphasize locating and capacitating local entrepreneurship and investment, including especially equity investment. We also emphasize the need to re-invest the wealth of a

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[67] This seems to be the spirit even in the Kenya Local Government Reform Programme through which LATF and LASDAP were initiated.

community in it, in addition to bringing in additional new financing for new projects and investments.

Asset-holding has many desired and positive effects on individuals, families, communities and regions. Acquiring a university degree is a valuable lifetime achievement for many people. Acquiring a marketable skill-based qualification such as medicine is a prized and much sought after opportunity by many students and their families. A community or region will gain immensely from the value of graduates and specialized labour available within its economy.

Assets easily capture the entire demographic and spatial character of a region or community. Demographically, it is easy to discern asset accumulation and capabilities in each demographic group such as pre-natal, newborns, under-fives, childhood and pre-teen, teenagers, young adults, mid-life all the way to old age senior citizens. Investment requirements in the asset acquisition of each of the demographic groups require different inputs and are clearly distinguishable. Investing in the health of pregnant women and new mothers is essential for the pre-natal, safe birth and post-natal life of new born children. Investing in the education system and ensuring that all children go to school will be essential inputs for a distinct demographic group. Investing in opportunities for life-long education is essential for demographic groups in mid-life. Nurturing conditions for life-long savings and converting these into investments is essential to provisioning for the asset requirements for old age.

An asset paradigm to growing wealth, social inclusion and reducing gender inequality is attractive for many reasons. The erroneous assumption that income is equivalent to wealth and an over-concentration on measuring income poverty has led to many poorly conceived development interventions. This simplistic assumption has led many to believe that simply growing the incomes of poor women and other socially-excluded individuals is the key to lifting them out of poverty and social exclusion. As we saw in the critique of the ERS, this assumption is at the root of the ERS and explains its key noted failure; its inability to grow wealth for the poor.

At individual level, assets are valued for many reasons. Assets such as a good education, a block of rental apartments or a business can be a reliable source of income for current consumption. One can also get income for owning the house in which they reside. Some types of assets can also be used as collateral for credit, a buffer during emergences and can be passed on to future generations. Accumulation of assets generates status and social advantages for current and future generations of the holders of such assets. Significant assets are a near prerequisite for a successful career in public office, for educating one's children in choice universities, and generally getting ahead in life.

Asset poverty is potentially a better indicator of poverty and inequality than income poverty. Assets easily describe the capability and potential functionings of both individuals and a particular community. Human beings and the communities that they form are assumed to be forever aspiring to higher personal and community "functionings" and achievements and use the freedom afforded by new and better capabilities to move up in complexity. Resources are important in helping drive up capabilities, which are an important descriptor of potential functionings, and which in turn describe the range of one's or a community's freedom to pursue and attain higher achievements.

Within an asset framework, poverty is viewed as lacking minimally adequate capabilities that, therefore, constrain potential functionings. Being poor is, in this sense, a capability and not an income handicap. Poverty reduction or elimination would, therefore, aim to fortify the capability of different persons and communities to achieve valuable functionings, including increasing their capacity and potential to pursue their respective strategic objectives. To quote from Amartya Sen, "the re-orientation from an income-centred to a capability centred view gives us a better understanding of what is involved in the challenge of poverty…(and) provides clearer guidance on the priorities of anti-poverty policy."[68] This re-orientation from income to assets and capabilities is a fundamental concession and prerequisite to advancing the broadest possible range of social, cultural and economic rights for individuals, as well as securing the prosperity of local economies and communities.

Within the equality discourse, assets easily help one of the core problematic of inequality debates —'equality of what'.[69] Assets give us a more useful 'evaluative space' within which to judge the existence and extent of inequality. How much capability does one have to negotiate around basic social conditions? How much more capacitating does one need to arrive at a level of functioning comparable to another? How much of this relative lack of capacity is attributable to some factor outside ones control, such as disability or socially-induced vulnerability? All these are questions that are better answered from an asset perspective.

Ultimately, assets should enable one to achieve the freedom they need to achieve; that which is in their best interests. In Sens' classic formulation, the freedom to achieve is to be differentiated from actual achievements. Actual achievements are what we manage to accomplish, freedom to achieve the real chance that we have, and what it takes to accomplish our strategic goals and desires. Equality or inequality should be evaluated at the level of the capabilities and not actual achievements or functionings. Different people will put the same capabilities to different effects. Some achievements will help one muster higher

[68] Sen Amartya (1992:151).

[69] Sen Amartya (1992) for a comprehensive discussion of the concept and its potential applications.

means and thus a higher propensity to achieve. The primary point in this latter phenomenon is to instill a motivation and desire to achieve while ensuring that personal and social conditions that reduce ones potential are eliminated.

Assets, unlike income, can also be a strong rallying point for a new politics of equality and social inclusion. Asset development connects individuals and communities with their core aspirations and values. Individuals desire to own a house, to have a good and well-paying job, to run a successful enterprise, to be in robust health and to hold a portfolio of financial holdings. Individuals also desire greater freedom and opportunity, social justice, fairness and the capacity to be of help when need arises. Asset development presents a positive claim to the future and is often told in success stories. While examining differences in income provides a snapshot of current inequalities, an analysis of the distribution of assets poverty provides a better way to comprehend how inequality builds up over time for individuals and communities and easily reveals the structural reasons for it.

Asset-building is also at once a deeply personal and social process. At the individual level it presents a process of self-investment and acting in ones best future interests. At the community and societal level, asset-building presents a challenge to build the right institutions and ensure social systems enable all to partake in them, including institutions in the market and public sectors through which we earn our livelihoods. Asset-building presents excellent strategies to improve personal, household and community stability, create an orientation towards working for an individual and shared future, increase civic engagement in the life and future of community, provides a framework for risk-taking and prioritization at individual and community levels, and enhances the well-being of present and future generations.

SOCIAL EXCLUSION, GENDER AND ASSET DEVELOPMENT

The Social Exclusion/Inclusion Framework

The notion and reality of social exclusion constitutes an important consideration in the theory and practice of asset-building and asset-based community development.[70] The social exclusion/inclusion framework is a particularly useful conceptual and operational tool in efforts to theorize and benchmark relations between citizens and the state. Social exclusion occurs when citizens and citizen groups experience or suffer a certain definable rapture of the social bond that undergirds their rights, privileges and responsibilities as citizens.[71] Such rapture can result from the failure of one or more of the institutions that are responsible for integrating the individual or community into the broader state framework.[72] Inherent in this thinking is the recognition that all citizens have certain rights and entitlements within a state system. States have a duty to help secure these rights for them and can do so either through direct provision of services or promoting conditions that make the realization of these rights within the reach of citizens.

Social exclusion is a consequence of other developments in the state within the various institutions of the household, market, public sectors, politics and culture. Official policy has often adopted a conservative view that it is the individuals' responsibility to respond and take advantage of changing conditions in these institutions. The devastating consequences of the now discredited Structural Adjustment Programmes have made it imperative to re-evaluate institutional environments and arrangements and how these impact on 'development' strategies, including those that privilege achieving high economic growth rates. This re-evaluation has seen social exclusion assume a useful explanatory and operational value that recognizes that social vulnerability is driven by social, economic, technological, and political factors working from various dimensions and at various levels.

Operationally, whereas various other concepts such as poverty, inequality and vulnerability do not impute or imply causality, social exclusion does.

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[70] See Poggi, A. (2003).

[71] In the context of social policy, *Social exclusion* has come to assume a shorthand term for what can happen when individuals or areas suffer from a combination of linked problems such as unemployment, poor skills, low incomes, inadequate housing, high crime, failing health, family breakdowns, etc. It is closely associated with poverty or economic exclusion and with particular groups of people: people with disabilities, people from ethnic minority communities, people with poor health, young people, the elderly, women, children in distress, etc. It is also associated with certain regions, cities and neighbourhoods.

[72] For a useful discussion of social exclusion/inclusion and how it relates to social deprivation, see de Haan A. (1999).

Accordingly, it is not enough to show that an individual, community or region is suffering social exclusion, but also one must show what persons, institutions, agencies, factors, phenomena, etc are causing the exclusion. In other words, who and what are doing the excluding? Ultimately, the state is held responsible for this and is often the supra-person doing the excluding.

In this operational framework, the state has a duty to undertake measures that restore individuals and communities to some social state or place in which they do not suffer social exclusion. The process of doing so has come to be referred to as social inclusion—the design of policies, strategies and programmes that work to overcome social vulnerabilities experienced by definable individuals, communities or places. Social inclusion policy and strategy will often reflect a positive choice by the state to deal with the consequences of social dislocation and is often underpinned by the creation and maximal utilization of opportunities for consequential participation of susceptible groups in economic, social and political exchange, and under conditions that enhance their well-being and individual capabilities.[73]

Since social exclusion obtains from social relations, the social exclusion/ inclusion problem is a dynamic one bound to keep changing over time depending on the changes in the various institutions at work in society. To address exclusion, one must of necessity address poverty and inequality and the factors that drive them. Inherent in the social exclusion/inclusion problem is an assumption that the key drivers of social vulnerability are structural and, thus, points to a continuing need to address the structural orientation of social, economic and political conditions.

Social exclusion/inclusion also points to the need to reframe policy and legal debate and solutions relating to vulnerability. In this reframing, the social vulnerability assumes a complex, multifaceted and deeply running character operating at individual, community and state levels and through various institutional actors in societies. An individual's or community's problems are, therefore, not rooted in individual or community failure, but in structural and institutional weaknesses within institutions in society. This does not deny that individuals and communities have a responsibility and duty to ensure that they rise to the challenge presented to them by social exclusion at personal and community levels. It does recognize, however, that many individuals and communities may be ill-equipped to deal with these environmental challenges.[74]

As a conceptual and practical apparatus, social exclusion/inclusion recognizes that various members of society are differentially placed and exposed to vulnerabilities

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[73] See Lombe Margaret and Sherraden Michael (2005).

[74] For a useful discussion of social exclusion, see Atkison, A. B. (1998).

that work to exclude them from the mainstream of the economic, political, cultural and social life of the state. The framework seeks to capture the factors and forces at work in aiding the social exclusion from a variety of perspectives, the most dominant being area/place-based and community of interest. The framework also interrogates macro and micro economic policies and their impact on social exclusion/inclusion.

Gender-Based Exclusion and Asset Accumulation

A gender analysis of asset development and accumulation reveals the relative asset poverty of women in comparison to males and, bearing the utility value of asset-holding, the severe handicap this places on women in their desires to get ahead in life. Gender gaps in the acquisition of key assets such as education, health, land and property also contribute significantly to constrained economic growth and reduce the capacity and potential for overall human achievement in much of sub-Sahara Africa.[75]

Unfortunately, such an analysis is itself beset with methodological difficulties at the outset. Traditional analysis of asset and wealth holding has been done at the household level, often during a national census or a household survey. Gender is hardly ever a key criterion in the survey except in the rare case of the so called “female-headed household”. Similarly, Kenya’s taxation is based largely on income, not assets or wealth. Income tax data does not reveal much and is a much preferred tax model than one based on assets.[76]

The typical household or census survey has tended to treat the household and individuals within such households as the same entity and enjoying equitable and similar rights and privileges. In reality, individual welfare within households are not the same.[77] Women often do not share the same rights with men in household settings. Not only would women, on average, be earning less than men in a typical household setting, they are also unlikely to have absolute control of whatever their income is. A woman’s income is often equated with a household resource and appropriated for purposes dictated by the household. Control and ownership of household assets, even acquired through a woman’s labour and income is almost always the exclusive province of the man. In many instances, women may not pawn even their personal assets such as jewelry without the consent of the male.

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[75] See Deere Carmen Diana and Cheryl Doss (2003); Blackden Mark, Sudharshan Canagarajah, Stephan Klasen and David Lawson (2006).

[76] Note the recent objection by Parliament of attempts to introduce tax on real estate holdings. Similarly, most local governments in Kenya long gave up hoping to get an up to date land and property asset register on which to base their annual statutory rates.

[77] For a more detailed discussion, see Deere Carmen Diana and Cheryl Doss (2003).

Moreover, women's ownership of marital property is often subject to judicial interpretation and confirmation even where there was a legal union between the two. As a result, and owing to the different sets of customary law and religions, it is indeed a very tenuous task to determine whether or not a certain woman really 'owns' property she thinks is hers for the taking on the demise of a spouse.[78]

Wealth data is also more difficult to acquire than income data. It is easy to determine how much income one makes from a cow than how much the cow is actually worth. With recent reform in the retirement benefits regime, pension data will soon become universally available, and this will be useful.

Women's ability to accumulate assets is conditioned by many factors working often simultaneously at the level of the state, the family, the community and the market. The state will usually define the parameters surrounding the accumulation, control, and transmission of property and assets through laws on property rights, the rights of children, marriage, the family, inheritance and others. The state will also play a crucial role in determining whether or not women get an education and technical and workforce development training. The state is also a major provider of frontline health services and infrastructure. As a major employer and significant actor in the economy, through its demand and supply of goods and services, the state has significant weight to leverage allocation of resources and assets in the economy in the mid and the long term.

The gender character of the state, including whether or not the state is available to push for women's strategic gender interests, is a primary consideration in determining whether or not women get to level out with men in asset accumulation. The truth of the state's ability to speak to male power in the asset accumulation process is evident, considering that it has immense powers to legislate on other institutions of society, including the family and the market. The state also has immense powers in judicial review and determination of "appropriate" legal regimes that apply to the asset-holding rights of women and men.

The family, especially under customary and religious law, has immense powers to allocate assets and often does this to the detriment of women.

Social and community institutions, excluding the family, have a modest bearing on women's asset-holding and life-outcomes. These institutions, however, have a significant moderating influence on the state, the market and the family through civic engagement and political advocacy. Economic institutions in this sector, working through not-for-profit and social enterprise organizations, are increasingly offering public and social merit goods and can be creatively engaged to advance women's strategic gender interests.

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[78] See, for instance, Jeremiah Nyegenye, in Kanyi Wambui and Maina Ngunjiri (eds) (2002).

Markets, especially under market economies or their variants, have significant scope to influence the allocation of assets in an economy. The labour market, for instance, determines who gets what employment income in the economy. Since employment income is crucial to accumulation of life-long savings for most people, then whoever gets the jobs and the highest income will tend to accumulate assets faster. This type of individual is also likely to out-perform others should the economy suffer shocks. Unfortunately, prevailing sexual division of labour has meant that the market is biased towards allocating resources and assets to male labour. The gender typology of care in the economy also means that more women stay out of productive employment and, thus, depend on the economy of affection to get their dues from the market.

On its own, the market has proved a very weak self-regulator and can hardly be expected to act in the women's longer term strategic interests. Women will typically earn less than men, are also likely to take time off work on account of conflicting gender roles, and are likely to have less skills and, therefore, be ineligible for high rewarding prospects. In weak economic arrangements characterized by a huge informal sector and an under-performing and underpaying formal sector, women are likely to be found in the informal sector and providing part time labour to industry. Capital and financial markets are unlikely to reward women with no other visible assets such as large enterprises, property, good quality jobs, etc. A powerful correction through state intervention is needed to get the market to recognize and reward women's strategic interests. In theory and objectively, women need to acquire and control more assets than males as they will need them longer, owing to their longer life expectancy.

There is also a strategic need to allocate more resources and assets to women to address prevailing and historical injustices. Unfortunately, not only does gender play an active role in asset acquisition, it does play an even greater role in asset depletion. In times of economic difficulty and hardship, women wear down and deplete their physical assets faster than men. This is partly because they are on the first line of provisioning for the daily requirements of their households, but also because a lot of the assets they tend to have are movables and have ready markets. Women will be the first to convert such assets as television and a car into cash to meet rising consumption needs.

Since women and men actually use their assets and wealth differently, such as simply selling a chicken to pay the pediatrician nurse's fee, and since this has consequences for households and the economy, not only is there a compelling case to ensure that women actually hold and accumulate assets in their own self, but that more attention is given to the gendered asset terrain within larger efforts to attain development. A lorry-full of grains amassed for replanting and, therefore, an investment can easily become a liquid asset to finance consumption in the event of a drought—securing the immediate livelihood of the household but

greatly compromising a woman's future economic security.[79] Moreover, to the extent that asset ownership and accumulation improves women's productivity and ability to earn a living, women's ownership of such assets will contribute to economic growth and development.

Asset holding has also been shown to have distinctive positive effects on the economic and psychological well-being of women in the event of marital disruption or other critical life events. Human, financial and physical asset accumulation is, therefore, a sensible protective strategy for women and children at risk of various forms of gender violence and deprivation.[80]

The question then begs how devolved funds and other functional sub-sovereign financing arrangements can be used to drive progressive universal asset accumulation at individual, community and regional levels. Recognizing the value that asset-building brings to efforts to overcome poverty and grow wealth, and the very gendered nature of asset-building and accumulation, how can sub-sovereign finance be used to eradicate inherent gender distortions in the asset-building and accumulation regime?

What can sub-sovereign and devolved finance do to help the ability of women to own, command and control the critical asset base necessary to ensure their basic capacities and competences in life? What can sub-sovereign and devolved finance do to aid women's effort to enter the economic mainstream, enjoy economic opportunity and gain economic security? Assuming that sub-sovereign and devolved finance are special apparatus of the state working at national and local levels to provide redress to social injustices, to what extent can they be employed and relied on to shape the other spheres of the market, the family, and community institutions?

[79] For a more detailed discussion, see Floro S. Maria and Antonopoulos Rania (2004).

[80] See Cho Esther Yin Mei (1999).

NEW DIRECTIONS IN SOCIAL SECURITY

> "Few people have ever spent their way out of poverty. Those who escape do so through saving and investing in long term goals"
>
> Michael Sherraden, 1991[81]

Up from Welfare: The Social Investment State

One of the central questions confronting any social security policy is what to do with individuals who are left out of economic opportunities in the mainstream. It is possible to view such individuals in either of two ways. In the first, such individuals may be viewed as being some sort of misfits, responsible for their own inability to take advantage of prevailing opportunities and not capable of making any claims against other members of the community. In the other view, individual social vulnerability issues from economic, social and political conditions obtaining in society. Vulnerability is, thus, a structural phenomenon to be addressed at the level of the community and institutions in society. In the first view, welfare is an aberration that amounts to taking away wealth from those who may have earned it justly and giving it to individuals who may be just lazy. In the second view, welfare is viewed as some sort of compensation for claims that issue from a certain disenfranchisement, such as poverty and social exclusion. In this latter view, social vulnerability does confer certain welfare rights to individuals *vis-a-vis* the state. This is particularly the case when social vulnerability leads to a denial of basic human rights for the individuals concerned. If vulnerable citizens can make these claims, then the state is obligated to institute a system of social insurance or to ensure conditions that work to redress the vulnerabilities and restore one's capacity to exercise their rights. Such a system would be deemed to confer certain prior rights to those who are likely to be socially-vulnerable. A right to welfare may also subsist as compensation for individuals and communities in situations where they have suffered entrenched injustices issuing from denial or violation of basic rights.

New thinking on social policy is progressively in favour of moving away from welfare income support and social protection goals—defined in terms of income and consumption support and focusing on a minimum standard of living, wide coverage and adequacy of basic social security insurance and minimum protections for the very poor and excluded[82]—to promoting the economic and social development of individuals, families, households and communities and the active and beneficial participation of all in the economic, social, cultural and political life of community and society.[83] This latter focuses on raising the capabilities and competences that define an individual's or community's capacity

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[81] See Sherraden Michael (1991).

[82] See, *Delivering Vision 2030,* July 2007, power point presentation.

[83] See, for instance, Connell, R. (2003); Midgley James and Sharraden Michael (eds) (1997)*;* Sen Amartya (1993).

and potential for higher level functionings through systematic and holistic asset-building.

We noted earlier that one of the core weaknesses of the ERS, and its accompanying public investment programme, is its failure to embrace new thinking in overcoming social exclusion, inequality and extreme poverty. The ERS is rooted in the traditional concept of a welfare state, with the government quietly and laboriously providing for its unfortunate part of the population, the private sector providing the real growth, jobs and opportunities in the economy and the state taxing this to meet expanding need for social services.[84]

The core assumption in this thinking is that if favourable macroeconomic conditions can be obtained and the private sector made to grow, and become progressively productive and competitive, it can provide the tax base and saving necessary to support increasing social services.[85] Where individuals are rung down the economic ladder and eke out a livelihood as casual workers, unemployed, or dutifully tending to family and community in the care economy, they have to simply wait their turn as the benefits of the economic expansion swell up and percolate or overflow to them.[86]

In the event that some individuals are far too removed from the mainstream of economic activity for factors that may be beyond their own making, then the state is considering pragmatic measures such as targeted cash transfers to mitigate their individual circumstances.[87] In this respect, the state is already experimenting with a limited cash transfer scheme for children orphaned by HIV/AIDS. There are also efforts to reform the National Social Security Fund (NSSF) into a National Social Insurance Fund (NSIF) to provide some measure of relief to those in extreme depravation.[88] The National Hospital Insurance Fund will also be graduated into a contributory universal and progressive National Social Health Insurance Scheme.[89] There is a lot to recommend in these efforts. Unfortunately,

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[84] See Nyong'o Anyang' (2007:3).

[85] Information on Vision 2030 is obtained variously from public presentations by the National Economic and Social Council (NESC) Vision 2030 Secretariat at Isiolo on 20th August and Embu on 22nd August 2007. Also, core presentation by Dr Gakuru Wahome at a Gender and Vision 2030 forum, on Friday 7th September 2007, Nairobi.

[86] See for instance Hon. Peter Kimunya, Minister for Finance, Kenya in "On the spot" television interview by *Nation Television* Thursday 1st March 2006. Challenged by the host, Jullie Gichuru to explain the apparently unacceptable situation of economic growth amidst rising poverty, the Minister opined that the benefits of growth are experienced on a pro-rata basis with the poor coming in last.

[87] See speech by the Permanent Secretary, Ministry of Gender, Sports and Social Services at an Action Aid International-Kenya workshop, "Towards a policy framework on social protection in Kenya", held on 21st February 2007, Nairobi.

[88] See Ogonda Job (2007).

[89] See African Union, Social protection: A transformative agenda —The Livingstone Call for Action.

this thinking, issuing from an inadequate analytical framework, is a little old-fashioned and inadequate for the task.

The need for 'new money' to provide for social expenditures is now widely acknowledged. This need, in part, explains the proliferation of sub-sovereign finance schemes. This can also explain the rationale to restructure national social security institutions such as the NSSF and NHIF to be more responsive to and take in more voluntary contributions, especially from the underserved informal sector. These efforts have been augmented by increases in social service spending particularly in the health and education sectors. Changing lifestyles that place a premium on small families and de-emphasize extended familial relations are manifestations of societal responses to increasing demands placed on the social system particularly in the economic and state contraction of the 1990s. Increasingly, people also want to stay longer in employment, as is evident in the current practice of retaining retiring specialized employees as independent contractors.

In the end, the state has to face up to the question about where 'new money' for its 'social programmes' will come from. Many hold that simply growing the economy high and fast enough will work to provide both the new money and reduce pent up demand for these services. In practice, little will be achieved without remodeling 'social spending thinking' to allow for investment in the capabilities and asset base of the socially-excluded and vulnerable individuals and communities in ways that improve their competence relative to the obtaining conditions in the economy and society. A socially-investing state is, in this respect, more than a conceptual shift from a welfare state; it implies a real shift in the character and orientation of the state. In this re-orientation, the state becomes an investor in the capabilities and assets of all its citizens and especially those who are vulnerable to changes in the environment.[90]

This re-orientation works well with the states' primary duty with respect to the basic rights of its residents. The state, as the duty bound guarantor of basic entitlements, has to model the public and private sector so that they can redress the factors that make these individual, groups and communities vulnerable. Promoting the economic and social development of vulnerable groups and their active participation in opportunities available in the economy may provide better social protection than subsidizing their income and consumptive needs. To put it another way, even while cash transfers and other income support is much

[90] For a useful, albeit administrative discussion of these new perspectives, see Moser C. (2005). See also Sherraden Michael (1996).

needed and will be valued by many,[91] in the long term this is only useful if it is done within a framework and context that builds the capacities and competences of recipients relative to obtaining social conditions.[92] Such support, while welcome, ought to be the first step of a larger and more holistic social investment programme.[93]

Capability and Vulnerability: Reshaping the Frontiers of Development in a Socially-Investing State

We have argued that an individual's capacity to acquire and accumulate assets depends more on environmental conditions than individual or community behaviour. In this vein, social exclusion and inequality as marked by the massive income and asset poverty and inequality are much a problem of structure and process and have little to do with individual behaviours. The institutional profiling at the heart of these processes includes one's family background, the immediate community, prevailing labour markets, prevailing capital markets, the quality and reach of public services, the ideological orientation of the state, etc. According to this view, structural inequality, for instance, is itself a major impediment to efforts to grow the income and asset base of low income women.[94] It has also been shown, even in prospering and widely diversified societies such as the US, that income and asset poverty are actually more a function of social-economic structure than the personal agency of the poor and excluded.[95] Accordingly, the problem of social exclusion or for that matter asset poverty is a structural one.

The economic expansion under the NARC administration exposes the more serious challenges confronting socially-inclusive local economic and community regeneration—the need to address the socio-economic and cultural patterning

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[91] The benefits of a well-targeted and effective cash transfer within the African context are becoming evident in schemes such as The Kalamo Social Cash Transfer Scheme in Zambia and in South Africa, where a massive transfer scheme is one of the interventions to mitigate extreme inequalities and poverty carried over from Apartheid.

[92] The South African social cash transfer system is increasingly being cited as illustrating the likely positive externality of cash transfers on economic growth and development (see, for instance, Ogonda Job (2007); Thomson Koy (2007). South African President, Thambo Mbeki, is on record warning South Africa against creating a culture of two perpetual economic realities in South Africa, with the so called "third world" economy relying on entitlements and rents from a prosperous "first world" economy. Thambo Mbeki, State Opening of Parliament 2004, also Thambo Mbeki "Letter from the President: Bold steps to end the two nations divide".

[93] For a useful comparison of social development approaches, see Midgley James (2004).

[94] This can be gleaned from the current expansion in credit supply by commercial banks, largely targeting persons with sufficiently high income. It can also explain why majority of subsidized funds advanced to commercial banks for on lending to the MSE sector end up drying up; the profits they make are invested to other more profitable ventures in the lending entity.

[95] See, for instance, Baverly S. G. and Sherraden, M. (1999); Baverly S. G. and Sherraden, M. (2001); and Deere Carmen Diana and Cheryl Doss (2003).

of the Kenyan society at the root of our inequalities and poverty. How do we explain a situation where the economy grows without visibly reducing the gaps between the rich and the poor, regional inequalities, inequalities between men and women, area-based social exclusions such as those responsible for urban slums? This patterning, driven by a regime of cultural rules and norms, often determines who can own property, and therefore who can sign a cheque, who gets counted in a census and for what reason, who gets to go to school and who does not, who gets that crucial qualification in engineering and, therefore, gets a leg into the future of government infrastructure procurement, etc. Structural patterning is what explains the deeply-rooted and persistent social exclusion and poverty, to be distinguished from occasional dips based on self-correcting phenomena. To put it another way, many individuals, households and communities suffer from such an acute shortage of capabilities and assets that they are unable to take advantage of positive changes realized in the economy. Moreover, many would still be unable to make any strategic use of arising opportunity even if temporary assistance was directed at them. Such individuals and communities are virtual prisoners in an enduring dynamic of structural poverty.

Much has been said about the role of broader societal factors in influencing and shaping personal behaviour. It is now accepted that the inferior and subordinate economic and social status of women, for instance, limits their ability to refuse unwanted or unprotected sexual intercourse irrespective of how much they know about HIV/AIDS and their desire to protect their health against it. One of the key insights from the American Dream Demonstration (ADD) Project was that societal, and not individual, conditioning is responsible for the inability of poor people to save; that 'savings is a structure, not a habit".[96] Recognition of social vulnerability, that reality that broad societal and collective factors such as gender relations and inequality work to constrain individual choice and enhance personal vulnerability, is gaining currency in ongoing demonstrations about the benefits of cash transfer programmes in places like Zambia.[97]

As we noted earlier, it is outside the scope of this study to delve into such issues as the cultural, legal and socio-economic status of poor and socially-excluded individuals and groups, how this relates to their capacities and asset accumulation and how new sub-sovereign finance can come to their aid. Such an evaluation is also an inevitable corollary to this consultation given the primacy of the human rights of the socially-excluded and the necessity to model social, cultural, political and economic institutions to promote these rights.

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[96] See Baverly S. G. and Sherraden, M. (2004) and also Sherraden, M., Schreiner, M. and Beverly S. (2002).

[97] See Commission for Africa Report.

In the emerging framework of a socially-investing state, capability, vulnerability and the asset-base of the poor and socially-excluded become key operational terms in defining and determining the new social security paradigm. In this paradigm, anti-poverty programmes are designed such that the poor build up the asset and capabilities that improve an individual's and community's capacity to cope and rise up to a crisis. To put it differently, one should not be required to live below a dollar a day to benefit from general or targeted anti-poverty expenditure. The assets and entitlements that an individual or community can command in the face of a crisis constitute that individual's or community's critical line of defence and resistance—the more and higher the assets, the less the vulnerability and the more the capacity to cope.[98] Helping maintain a community's asset base in the face of a natural disaster would be more crucial to their eventual recovery, while simply providing food after their assets have been depleted would not help stop their descent into poverty. Such an effort was nearly achieved with efforts to buy off cattle in the ASAL regions in the wake of the recent drought.[99] The enduring lessons from the failure of this effort point to a need for community-level financial and development institutions well suited to the conditions working in the strategic interests of these communities but competent to tap into national markets and resources.

Poor individuals, households and communities are actually adept and very sophisticated at managing assets—building them up in times of plenty and utilizing them effectively to cushion negative environmental events. Many times, however, these assets, including the knowledge base and institutional responses to cope, are systematically eroded by internal and external developments outside an individual's or community's immediate grasp. Rather than operating from the assumption that the poor actually have and own nothing, social policy should focus on helping individuals and communities build up their capabilities and assets with a view to converting these into resources they can draw on. It is such capabilities and assets that keep people and communities out of poverty in the long run. Anti-poverty expenditure on internal security and the police force, for instance, can be well used and progressively reduced by providing tax concessions to enterprises that help provide jobs and re-integration of ex-convicts, or women and girls perennially out of work. A similar effect can be realized by providing appropriate tax credit to social enterprises that provide shelter to abused women and girls.

In a similar vein, it will be necessary to model macroeconomic goals with social investment targets in mind. In this respect, economic growth is not of its

[98] See Moser C. (1998).

[99] For the asset-building potential of this particular response, see Lesorogol Caroline K. (2004). A comparable but more detailed description is available at Agobia Charles A. (1999).

own a panacea to poverty, but has to be pursued in tandem with other solutions that serve to redistribute income and assets—as the productive base and wealth. These latter, and not chiefly economic growth, are a necessary precondition for overcoming poverty and social exclusion. In this sense, the composition of growth, in contradistinction with the incidence of growth, is important to the overall effort.

In operational practice, it is therefore socially and politically strategic and vital to grow those areas of the economy that have a direct impact on the socially-excluded. Even accepting the minimalist but dominant neo-liberal view that economic growth and development will be driven by the accumulation of savings, investment capital, new technology and skills, the accumulation of these by the socially-excluded and the poor as well as their application in ways that empower them is vital to the very effort to grow the economy.

The implications of this thinking for macroeconomic policy are profound. As we have seen elsewhere, socially-excluded persons, especially poor women, have very limited resources to survive the effects of macroeconomic instability such as inflation and uncertainty. Poor women, for instance, will tend to keep their assets in the form of cash or tangibles that are easy to pawn, such as goats and sheep. They are also more likely to put out their valuables to the market in times of economic difficulty. With the demands placed on their income and assets on account of their gender roles within the household and community, women will also spend more and more of their assets and income in their efforts to rise to the cash demands of an inflationary and unstable economy. Measures to grow the economy, such as controlling inflation or keeping domestic interest rates low, are not only good for the stability of the local financial sector but are also important because of the cushioning they provide to the savings of such socially-excluded persons and low income households. These measures are also important in securing conditions that make it 'profitable' for these people to enter the formal financial market even where this happens through special financial intermediation.

It follows that even in this limited view, economic governance and management arrangements should be judged by the extent to which they go to secure the beneficial engagement and involvement of these excluded persons and groups in the economic regime. This can in most cases be achieved through universal and progressive policy and programmes entailing capability asset-building at individual and community levels. Disregard for social inclusion and accompanying prerequisites, such as the empowerment of women will, in the mid and long term nurture conditions for macro-instability even where other economic fundamentals are sound. Failure to invest in the post-primary and tertiary education of women, for instance, will mean courting higher taxes in the future as it becomes necessary to provide social expenditures to arrest the effects

of unplanned teenage pregnancies, large families and their inability to participate in the economy on account of lack of skills. To argue that such costs can be provided by males owing to their association in households is to not only subordinate the basic rights of women to males, but to misdirect the argument as these males would still be meeting the cost of failure to invest in the women in the first instance.

As we have argued elsewhere, the distinction between growth and development points to a much needed correction that economic growth alone or in combination with other measures such as increased social spending on health and education is the panacea to overcoming poverty, inequality and social exclusion. Such growth and expenditures are useful only if viewed within a larger effort to realize the basic social, economic and other rights of all individuals. Within an assets, capabilities and functionings framework, economic growth and social spending needs to be subordinated to an overall effort to grow the assets, capabilities and potential functionings of especially those who are poor, socially-excluded and vulnerable.

While the ERS sought to provide opportunity, referred to as 'job and wealth creation', it did not explicitly seek to create conditions that enable equitable opportunity and wealth. In reality, it is necessary not only to grow the jobs but to pursue equalization with equal zeal. "Opportunity" must, therefore, be targeted at redressing gender, historical, area-based, ethnic and other exclusions and disparities. Expenditure and tax measures directed at growing the economy and overcoming poverty, including sub-sovereign and devolved finance, must aim to effect shifts in the historical distribution of income, asserts, opportunities and benefits in favour of women and other socially-excluded persons. This kind of investment is likely to be more long lasting and devoid of cyclic growth patterns that has characterized the overall Kenyan development effort since independence. This type of growth will also yield more stable societies and communities, thereby creating conditions for further growth.

It is also strategically important to remove structural distortions that impede the participation of particular groups of citizens in the economy. Such distortions include but are not limited to, for instance, the unpaid and unrecognized work of women in various sectors of the economy such as agriculture, the unpaid reproductive work of women and the unpaid and unrecognized work of women in the care economy. This unpaid work is, in practice, a subsidy to the various sectors of the 'formal' and 'informal' economy, including the public sector. As such, its effect is to distort the real cost of goods and services in these economies. It makes achieving other broad goals such as driving efficiencies and competitiveness difficult to accomplish.

It is also important to remove structural subsidies in core areas of the domestic economy. Of special importance to women farmers is the subsidy of under-costed

produce by rural farmers, the majority of whom are women, to urban populations. It is also necessary to remove the rent-seeking expensive and grossly inefficient food distribution network that works to the disadvantage of both rural producers and urban consumers. Within urban centres and overall industrialization policies, it is strategically important to eradicate the subsidy of urban workers to capital and industry through perennial underpaid casual and domestic employment.

Capability and asset-building framework at individual and community level is a useful and strategic point from which to interrogate and align prevailing social policy to supply to the human rights and 'developmental' demands of citizens and communities. The capability asset-building framework stands at an important cross-road between the need for more secure livelihoods; improved local governance involving substantial decentralization of power, resources and responsibility; the imperative to reform institutions to deliver to the demands of social inclusion; and to ensure genuine prosperity and progress all round.

There is no reason why sub-sovereign and devolved finance cannot be creatively engaged to address these problems. Devolved funding can be structured to help poor people better respond to certain shocks in the economy, such as by establishing Individual Development Accounts that can be drawn down in such circumstances. Devolved funding can also be structured to feed into and leverage life-long Individual Learning Accounts, which ensures qualifying individuals of resources to help them acquire the critical education and training they need to overcome social exclusion and poverty. Devolved funding can also be used to help structure special derivatives of the IDAs, including a Universal Savings Account for Children, special retirement accounts for the poor and unemployed, and special interest savings accounts for vulnerable groups in society, such as orphans, battered women and deserving single parent households.

Devolved funds can also be useful as part of an overall strategy of Community Development Accounts, directed specifically to aid asset-building of communities and community development institutions. Devolved finance can also be structured to establish a market for CDFIs such as community development trust funds, community development credit unions, community development enterprise loan funds and community development banks that work to deliver financial and technical intermediation to bring investment capital to socially-excluded and poor individuals and communities. To do these things effectively, new legal, governmental and community-based instruments are needed to bring investment, entrepreneurship and opportunity to socially-excluded groups and communities. Ultimately, it will be necessary to rework the legal systems that redefine asset and capital holding in ways that are in harmony with the longer term and strategic interests of the socially-excluded. Such a task is outside the purview of this study.

PART IV

PROSPECTS FOR ASSET-BUILDING THROUGH INVESTMENT IN HUMAN DEVELOPMENT

> Human development is a process of enlarging people's choices. The most critical of these wide-ranging choices are to live a long and healthy life, to be educated and to have access to resources needed for a decent standard of living. Additional choices include political freedom, guaranteed human rights and personal self respect…The process of development should at least create a conducive environment for people, individually and collectively, to develop their full potential and to have a reasonable chance of leading productive and creative lives in accord with their needs and interests
>
> (UNDP, 1990, p1).

INVESTING IN HUMAN DEVELOPMENT: PROSPECTS FOR UNIVERSAL ASSET-BUILDING WITHIN THE HUMAN CAPITAL FUNDS

Human Development?

At the end of the day, the question must be asked, what should be the end result of the various sub-sovereign finance schemes? Clearly, sub-sovereign finance—devolved funds for many—is a vehicle and not an end in itself, what is the clearest and simplest notion of what it should be seeking to achieve? A cursory look at the various devolved funding mechanisms brings one simple and clear answer to mind—enabling asset-building for purposes of driving local human development. Human development presents an ideal reference point, some sort of beacons that tell us that we are moving in the desired direction relative to our goals.

Yet, for its apparent simplicity, human development presents a complex underbelly. In the approach we have taken with regard to the primacy of capability and asset-building, human development presents the ultimate goal of economic and social development. In this framework, under-developed communities and their residents do not simply lack income or commodities; they lack assets and capabilities that lead to a full productive and satisfying existence. Economic and social policy must be directed at ensuring that the broad goals of human development are realized for each individual in each generation. It will not be enough to simply grow the economy, however challenging that task is. It will not be enough to provide 'social services', 'social security' and 'social sector expenditures' if this simple goal remains outside the reach of citizens who even though they participate in these processes ought to be the ultimate beneficiaries.[100]

Within the capability framework, human development refers to investing in people's capabilities to enable them achieve desired functions relative to basic rights such as nutrition and freedom from from hunger, physical and mental health, basic housing, education, technical and workforce training, personal security and a life lived in fruitful community with others. Phenomena such as skewed distribution of wealth and income, absolute poverty, inadequate housing, failing health, social exclusion and other erosion in the quality of life is a manifestation of failed human development.

Investing in the basic capabilities of a community's members has intrinsic value, but it also has substantial social and economic returns and is a prerequisite for advances in the various fields of society, measured by economic growth and

[100] See UNDP (1990).

development. Enhancement of the *functionings* of individuals also ensures immediate and long term social returns to individuals, households, communities and the state. This multifaceted nature of investments in human rights makes this type of investment the most efficient and productive way to use scarce 'development' resources. It also makes this most secure safety net and underwriter for current and future prosperity. Accordingly, we make proposals, here and elsewhere in the study, for an appropriate and strategic linkage between institutional arrangements in society and the capacity of society to provide resources for these investments. We opine that well-structured sub-sovereign finance schemes can play a crucial role in moderating the prevailing institutional arrangements to increase the levels of investment going into human development; that this is best achieved through an asset and capability framework, and that institutional actors other than the state and market are required to make these investments a reality.

Adopting this normative and programmatic view, we interrogate the possibilities of creatively engaging sub-sovereign finance to build on the health, educational, nutrition, basic housing outcomes of poor and excluded individuals within an overall framework of asset-based local economic and community development. In later parts of this report, we make proposals regarding institutional and organizational regimes that may work to address programme and systemic vulnerability—the ability of the local economic and community development system to deliver products, services and solutions within a capability and assets development framework. Taken together with other proposals, these should serve as useful starting points for a larger discussion.

Education and Workforce Development

> Education is a key determinant of earnings and therefore an important exit route from poverty. Education improves people's ability to take advantage of the opportunities that can improve their well-being as individuals and be able to participate more effectively in the community and markets. Higher educational attainment for a household head significantly reduces the likelihood of a household being poor.
>
> Economic Recovery Strategy for Wealth and Employment Creation 2003-2007, p39

Education and health are key determinants of the capacities and vulnerabilities of the poor and socially-excluded to long term income and asset poverty. In a market and industrial economy, one's education and training and one's health pretty much determine the range of opportunities. Education, for instance, is perhaps the single most important determinant of ones' employability and capacity to negotiate life's chances—the higher up the educational and skills ladder, the more the likelihood that one can access and amass other assets necessary to move up and ahead in life.

The relationship between inequality, poverty, education and ones health can be telling. Poverty is endemic amongst certain socio-economic groups in society, including especially casual workers, small-scale farmers, persons living with and those affected by HIV/AIDS such as orphaned children, pastoralists, etc. These groups are, however, also described by their relative lack of education.[101] Regions with significant natural resource endowments but rank low in education are also the poorest. Similarly, the majority of the poor are pastoralists, work in agriculture and the informal economy.

The possibility of re-engineering the agricultural and informal sectors, for instance, is impinged partly by the educational and skill-holding capacity of those in the sector. High earning agricultural activity, with significant value addition and specialization (such as horticulture) demands significant knowledge and skills. Improving jua kali enterprises to be regionally and globally competitive will also involve significant investment in new knowledge, skills and technology, all of which command relatively high educational attainment. Even in the obtaining situation, the most prosperous SME firms are those where the owners have significant levels of educational attainment.[102] The instructive national Micro and Small Enterprise Baseline Survey analyzed the relationship between the level of education, business revenues and membership to business associations. The survey found that 'the highest proportion of entrepreneurs with the highest levels of revenue was found in the postgraduate group while the highest proportion of those with lowest revenues was found among those with no education".[103] Alternatively, the most successful SME products are those that combine vigorous training and mentoring with actual lending to compensate for the relatively low educational, technical and skills attainment for programme participants.

It is strategically important that the health, educational and skills attainment of socially-excluded individuals and communities are assured for their own sake but also in order to fortify the high road to social, economic and political development.

The necessity to invest in education at all levels cannot be gainsaid. As the statement above demonstrates, the government is conscious of the role education is expected to play in eradicating poverty and transiting the Kenyan society from a poor third world economy into a medium income one.[104]More significantly, for

[101] See Society for International Development (2004).

[102]For useful data and analysis in this regard, see the Central Bureau of Statistics, International Center for Economic Growth (ICEG) and K-Rep Holdings Ltd (1999).

[103] See Central Bureau of Statistics and others. This finding also serves to reinforce our claim about the role of structure in asset accumulation, poverty and social exclusion.

[104] Proposals for Vision 2030, for instance, identify education as a key platform to achieving its aims. Education has also received the largest share of resources under the new NARC administration.

our purposes, as demonstrated by the statement, the ERS categorically frames education as an asset, the acquisition of which is crucial to other life outcomes of the holder in terms of increased capabilities and functioning. The higher one goes the educational ladder the better the asset and the higher one's capabilities, functioning and potential achievements.

Unfortunately, the operational and programmed intervention to make education, and presumably critical skills and workforce development, possible for the poor and socially-excluded fail to capture the true importance that a capability and asset-based perspective brings to education. An intervention on education as a critical life asset must ensure that educational attainment is universal, progressive and lifelong. Such a strategy must also secure the integrity of the curriculum and skills offering within the education and training system—given that these constitute what is valuable in this asset. The ERS and its subsequent implementation provide a critical starting point by seeking to supply universal primary school education. While there are many unresolved issues with regard to the curriculum and the quality of the public school system, the pragmatic decision to open up public primary schools to all children has been one of the most lauded and popular decisions of the NARC administration. Many questions, however, still remain, including the need for a universal and compulsory pre-school component, the need to align the curriculum with current and future demands on education, and the need to ensure quality by hiring more teachers and putting up more infrastructure.

Ultimately, the value of education as an asset and strategic investment is realized at the secondary and post-secondary level. Not surprisingly, the issues and politics of access to secondary school education for all is increasingly becoming a public problem. As we noted earlier, the demand that the government opens up its secondary schools in the same fashion that it did with the primary schools is already bringing to the fore a critical debate about how to pay for this. What is the state to do with regard to the still unresolved issue regarding the much criticized curriculum offering within the secondary school cycle? Can the government afford to provide universal free secondary education? In the likely event that this is not possible, what other institutional and financial intermediation is desirable or possible to secure the possibility of removing the issue of access from this crucial asset building necessity? What is the potential role of sub-sovereign finance in this new financial intermediation? Questions, similar to those raised on secondary school education, can be raised with regard to post-secondary education and workforce development.

In our view, the challenges presented by the need to make educational attainment universally and progressively available for all needs more policy, programmatic and financing interventions than those presently in the public mainstream. To do this, it will be necessary to move beyond the key issues of cost/access and institutional efficiencies as identified in the ERS to the

institutional arrangements and forms available to the sector and their ability to embrace the poor and socially-excluded. Unfortunately, a situation has emerged within the secondary and post-secondary cycles in education where those who were privileged to access good quality high cost private education at primary school level take up nearly all the public places available at these other levels. Besides creating a direct state subsidy for parents who demonstrably can afford to pay for the education of their children at this level, this serves to compound the problem for those poor and excluded who miss out on an opportunity to acquire a critical and much valued asset.

We call, elsewhere, for embracing the social economy as a central institutional mechanism to deliver on the asset development potential of the poor and socially-excluded individuals and communities. In this new framework, the state would embrace a three-pronged strategy that entails public, private (for profit) and social economy-based (not-for-profit) enterprises to deliver key goods such as education and health. Embracing this within education would have immediate and lasting benefits as institutions such as the Starehe Boys Centre and now the Starehe Girls have demonstrated. These two institutions are a special asset class for poor boys and girls and have played a catalyst role in the career pathways and life outcomes of many previously destitute and excluded child, family and community.

Within this framework, it is conceivable that all the current national schools can be turned over to a similar model. It is also possible to have at least two such institutions per constituency by turning over existing institutional assets to this delivery framework. The converted assets would be required to account for their social purposes through regular social auditing and accountability to core constituents. This arrangement would at once achieve a much desired situation where needy students get public subsidy to enter these schools. Those who have demonstrated ability to pay through private primary education would be expected to continue doing so even as they enter these institutions. Assuming a situation where 50 percent of students in such institutions are need-based, and assuming 1,000 such schools nationally with each school having a population of 500 students, this would translate to 250,000 means-tested need-based students.

We propose below and elsewhere the exclusive use of community development entities and Community Development Finance Institutions to deliver key service and financing frameworks for local economic and community development. It is easy to see how an extensive system of Community Development Financial Institutions, backed by qualifying community development entities can be useful in the delivery of means-tested asset-building for the poor at this and other levels of education. More significantly, a well developed CDFI regime would also be valuable to parents/students who can demonstrate capacity to afford entry to such institutions but need alternative, effective and affordable financial

intermediation. CDFI products can also be modeled to stabilize the financing framework for the demand side of above average and high net worth prospects for such institutions.

Much more ambitiously, it is conceivable that significant benefits can be realized by grafting a junior secondary school section in each of the public primary schools and re-branding these schools as community development institutions. The chief benefit of this strategy would be to ensure automatic transition from primary to secondary school, at least Form one and two, for all pupils. An exit certification can be introduced for the junior school level, allowing students to either terminate basic schooling at this point or to proceed to senior secondary school at another institution. This development would also result in numerous new openings in secondary school institutions that would now offer only two years of education. Schools that convert to a social enterprise-based delivery framework can be allowed to retain Form one and two classes as an income generating activity. The most obvious cost for such an intervention is the massive investment in new infrastructure at the present primary school sites as well as the deployment and hiring of teachers to equip these new institutions. Though the initial costs are high, in the long-term the public would realize significant cost reduction as these institutions would be day schools and within easy reach of members of the community. The public would also benefit by significant future cost savings as teachers at this level can be diploma holders, who should cost less than degree holding ones. The community would also benefit as resources used in the construction and salaries used to pay the additional staff push up demand for labour and local produce.

What is the likelihood of crafting a sub-sovereign finance product to meet the infrastructural demands of this type of an intervention?

A sense of opportunity: Moving from the known to the unknown

Much of what we have presented with regard to education and workforce development constitute ambitious unknowns and could seem dangerous to weary bureaucrats. In reality, though, it may not be apparent, at first, that the state is actually devolving functional responsibility for helping individuals acquire key assets in education more and more to municipal and other sub-sovereign entities and seeking to guarantee them through devolved and sub-sovereign finance. The first of the funds in the education sector is perhaps the Higher Education Loans Board established in 1991 to provide low cost credit for qualifying university students in public universities. The fund also has a small bursary component to assist financially-challenged students. The Fund has, since its formation, disbursed over Ksh 6 billion to university students.

The second oldest fund in the education sector is the Secondary School Education Bursary Fund, designated to help poor students access secondary school education within the public system. There is now talk of a wider secondary education loan fund that may operate in a manner similar to the higher education loans scheme.

Recently, with the onset of University Free Primary Education, the government set up a fund mechanism to enable the initiative. The Free Primary Education Fund, set up to help finance free primary education, presents a series of policy innovations that are adaptable to the proposed Independent Development Accounts Scheme. First, for the first time in its independent history, the state has attempted to count all the children of primary school age and provided, at least those in school, with a minimum annual allocation of Ksh 1,002 per year. Secondly, all primary school pupils get the same monetary allocation from the fund regardless of their poverty status. Thirdly, each school is required to open an actual account where money from the fund is deposited. Lastly, the money can only be drawn from the account for gazetted purposes.

The allocation of funds to specific primary schools has been credited with contributing significantly to the success of public primary schools, which have progressively narrowed the gap between them and private schools. This allocation is also credited with ensuring parity between pupils within the public school system regardless of the geographic location of an individual or primary school.[105] In numerous places, the provisioning of primary education has been greatly aided by the use of the Constituency Development Fund to construct and complete physical facilities such as classrooms.

Recently, the government ordered the provincial administration to arrest and prosecute parents of children of primary school age still out of school, estimated at about 700,000. With some innovation and visionary leadership at all levels, it is not difficult to imagine a system that builds on these achievements to establish universal and progressively-matched children's savings accounts.

Prospects for individual lifelong learning accounts

Lifelong learning is a process of asset accumulation that, if properly structured, can contribute significantly to reduce inequality and improve the life outcomes of participants. Strategic learning and skill development is essential to an individual's effort to break the vicious cycle in which poverty and inequality is passed from one generation to another. Lifelong learning especially targets skills, capacities and competences that enable one to negotiate changing and evolving economic conditions.

[105] See Oxfam GB & ANCEFA (2006).

Individual Lifelong Learning Accounts were first introduced in the UK in 2000. Qualifying individuals, those determined to suffer certain social exclusions—especially grounded on poverty—would deposit UK pounds 25 into designated accounts. The government would supplement these with UK pounds 150 for the first 1 million accounts. Additionally, all account holders received tuition discounts of 80 percent for maths and information technology courses and 20 percent for others. The system was unfortunately susceptible to fraud and, consequently, much abused by individuals and institutions seeking for easy money. It was scaled down and is presently being replaced by a much better targeted one.

If well administered, the current HELB scheme, combined with the Secondary School Bursary Fund and the proposed secondary school loan scheme, make fertile building blocks for Individual Learning Accounts. Targeted individuals can be encouraged to open designated savings accounts in qualifying CDFIs, where local states and sub-sovereign finance institutions would deposit pre-determined matching finance. Such savings can be converted into Certificates of Deposit, allowing the CDFI to invest the money for the benefit of socially and gender-responsive local economic regeneration.

The Certificates of Deposit would earn a premium rate comparable to what can be obtained in the financial market and can be redeemed to finance the pre-designated purposes, such as paying for post-secondary and university education. Such securities can also form one of the elements of a larger Individual Development Account scheme that allows participants to redeem them for other purposes as discussed above.

It is also conceivable that such schemes can be used to draw in resources not previously available to the community, such as corporate giving and social investments. The beauty of such schemes is that sub-sovereign finance is used to actually help structure an asset structure for participating individuals while locking the resulting financial asset to grow the local economy. Such schemes are easy to target to vulnerable sectors of the community, including poor single parent households, children in difficult circumstances such as orphans, etc.[106]

The Higher Education Loans Board can also be strategically useful to targeting socially-ordered groups including poor/low income working women who wish to use their savings to pursue higher education. It is conceivable that a revamped loan fund can be used to leverage credit requirements by such women through measures such providing interest subsidies, and partial guarantees on loan performance. Interest subsidies, for instance, can work to keep the interest rates accruing to the individual low, thus providing direct incentives to target

[106] The need and potential role of the Higher Education Loans Board for this kind of targeting is noted in, for instance, IPAR's policy recommendations for the sector. See Institute of Policy Analysis and Research (2003).

individuals to take up such loans. This would in turn be helpful in expanding the total amount of money available to finance higher education.[107]

The HELB scheme can also be restructured to enable perennially unemployed graduates to seek other skills that would help them better fit into obtaining market conditions. This would include designing comprehensive packages that include appropriate write-offs or derogation of payment, working with CDFIs providing services such as micro-finance, and qualifying training institutions to subsidize the training element of a new start-up loan in micro-enterprise, for instance.[108]

Building Community-Based Institutional Assets in the Human Capital and Workforce Development Areas

We discuss later the prospects and promise of delivering especially secondary and higher education through social enterprise institutions. This would entail acknowledging that existing public secondary schools, polytechnics and universities are actually social enterprise institutions working with heavy government subsidies. The schemes we have proposed above would go a long way in securing the enterprising footing and viability of these institutions.

It is also conceivable that municipal and sub-sovereign finance can be used not only to help start and mature such institutions, but that they can work to keep their costs low by investing in their infrastructure. Such institutions can also be required to build endowment for their social purposes, thus increasing the financing available to meet local social investment goals. Much of this discussion has been carried in previous chapters.

The same argument we have made for HELB and other funds with regard to legal and institutional autonomy can be made for majority of these institutions. It will be necessary to ensure that universities, polytechnics and technical training institutions of various types are legally and institutionally independent to run their affairs and budgets relative to an appropriate regulatory regime. The same can be made of various schools, especially at the county, regional and provincial levels. This would entail creating Regional Development Agencies/Corporations through a special charter by a respective statutory authority, and vesting the

[107] The need to restructure the entire financing regime of tertiary education in Kenya and sub-Sahara Africa continues to be dire. The just released Education Strategic Plan for the next 10 years factors no immediate and longer term increases in state financing of tertiary education and calls, instead, for more experimentation with own revenue generation by the universities. The schemes we have proposed here make it possible for successful universities and other tertiary institutions to draw on financial resources available from the rest of the economy. They also ensure that student financing and the entire public education sector is primed to deliver ascertained social and community benefits as the primary rationale for embracing the enterprise framework.

[108] For a current discussion of African efforts to seek financing for education outside public funds, see Johnstone Bruce D. (2003).

management and ownership of these schools into them. Each particular school would itself be run on a social enterprise framework. The government would direct financial and other support to a respective school, with each school sourcing own requirements from the district. A school district can creatively engage any number and variety of schemes, including community development corporations, local economic and community development venture capital corporations, etc to run and supply resources to institutions under its jurisdiction. These institutions should also have the juridical and organizational complexity to enable them to boldly and creatively embrace their mandates within a social enterprise framework. This calls for effective devolution of management and governance of these institutions to constituencies that would be defined within their legal charters. The law can also empower the Ministry of Education to periodically negotiate performance and other benchmarks with each of the institutions in return for its continuing financial and technical support. Other sub-sovereign finance schemes and local governments can also negotiate service contracts with these institutions in return for their support.[109]

The law should be clear that the government is obligated to provide such support and should set an arbitration mechanism, such as through independent presidential or statutory commissions where there are disputes between the ministries and the universities. Setting up and the recommendations of these commissions would provide critical events in the life of these institutions.

The impact of these measures for local human capital development in education would be profound. Current government thinking and planning for education and training points to the need for relatively new and alternative thinking around the core challenges faced by the education sector. In the wording of a core government document, "the current heavy investment that is borne, to a very large extent, by government alone calls for a review to ensure collaboration and partnership with other stakeholders. The challenge is, therefore, to establish partnerships between the government, households and local communities, development partners, private sector providers of educational services including sector employers, religious organizations and civil society such as NGOs and foundations." [110]

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[109] The proposals made here would greatly aid the Government of Kenya's overall development and investment aims with regard to the education sector. See Ministry of Education, Science and Technology, "Kenya Education Sector Support Programme 2005-2010: Delivering quality education and training to all Kenyans". The proposals are, however, informed by an ongoing and historical public debate about the need for a new education system and would work well with an education system as that proposed by the 1999 Presidential Commission of Inquiry, headed by Davis Koech, see Government of Kenya (2000), "Report of the Commission of Inquiry into the Education System of Kenya". The Ministry of Education then argued against the adoption of the report, citing structural, financial and other difficulties.

[110] Government of Kenya (2005).

The measures proposed in this section, coupled with others elsewhere in this study, provide the basic framework for a new and imaginative partnership. With these in place, residents, local communities as well educational institutions would plan for their future confident that they have the resources needed to see them through the education and training cycle.

Health Capital

> The achievement of good health is critical in enhancing human development. Improving health conditions reduces production losses caused by worker illness, increases the enrollment of children in school and increases learning ability. Thus, the human capital of the poor is improved by increasing their access to basic healthcare and nutrition.
>
> Economic Recovery Strategy for Wealth and Employment Creation 2003-2007, p39

One's health is even prior to education in determining one's ability to accumulate assets and well-being. As a personal asset, good health is often a prerequisite to acquiring other assets, including education, a well paying job, a fulfilling marital relationship, a successful business, etc. At a community level, the health of a community's member impinges directly on the community's productive capacity and resourcefulness. Ill health has direct costs as community members spend money, time and labour caring for the sick. Yet, being or remaining healthy presents a different personal, institutional and social challenge than say acquiring education. Providing healthcare is often expensive and requires large outlays of capital at individual and community levels. Owing to this, three approaches are popular and standard in provisioning for healthcare: first, keep the likelihood of ill-health low through healthy public policy and individual behaviour; second, insure as much of future health risks as is possible and; three, invest in the institutional capacity to provide affordable quality healthcare services to all who need them. As a corollary to these three, since health is both a private and quasi-public good, then a good deal of the prevention, institutional development, provision and financing regime has to be in the public domain.

The ERS opines that the chief problem with heathcare is affordability, which can be a measure of costs or the income poverty of the majority, making them unable to access even subsidized services offered at a fee. The solution, according to the ERS, lies in a universal National Health Insurance Fund that covers both out-patient and in-patient costs and that distributes the cost between the government, employees, employers, the informal sector "and other productive

segments of society".[111] The government could set up a national endowment fund to capitalize its commitment within the broader scheme.

It is significant that the proposed scheme is a financing strategy and does not address the institutional aspects of healthcare delivery in Kenya. There are currently three models of healthcare delivery in the country: public, private for profit, and social economy-based not for profit charity and social enterprises. Significant reforms have been effected in the delivery of healthcare since the 1980's when the country was faced by an acute fiscal and budgetary crisis. These reforms included the full liberalization of the sector, the gestalt introduction of user fees for public health utilities, greater reliance on pooled insurance funds through the NHIF, and a virtual freeze on further publicly-funded infrastructure development.[112] The outcome of these reform measures was to make access to even public healthcare more inequitable.

The reforms taken in the 1980s were based on certain assumptions and imposed certain health outcomes for the majority of the population, which a policy such as the ERS was expected to deal with. Unfortunately, by neglecting to do this, the ERS made the task of achieving a sound, well-resourced, progressive and universal national health insurance scheme nearly impossible. Moreover, decades of neglect of a functional and decentralized public health system, coupled with unheralded unplanned development and an urban population that increasingly inhabits informal and slum settlements, meant greater demand for curative services than were necessary or feasible. This situation was going to be compounded by the fact that the ERS was coming into effect at a time when the full effects of the HIV/AIDS, Malaria and Tuberculosis epidemics were coming to bear on both private and public resources.

Like in education, we propose that one of the key demands of the current health problem is to fashion the institutional arrangements at work in the provision and financing of healthcare with a view to making them more amenable to implementing a universal and progressive health insurance system that does not provide a conduit for rent seeking and excessive profit taking. Such a system must be based on the integrity and quality equivalence of the health service regardless of who the service provider is—whether public, private or social enterprise-based. Such a system must, however, recognize and reward the public and social economy based delivery frameworks to enable their social purpsose nature as well as the superior positive externalities of their organizing form.

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[111] Economic Recovery Strategy for Wealth and Employment Creation, 2003-2007, p41.

[112] See, for instance, Dahlgren Goran (1994).

It is noteworthy that the current sub-sovereign finance regime, and in particular the CDF, has resulted in massive new infrastructure investments in public healthcare financing at community level. While this is laudable, it will be clear that redress of the institutional arrangements within the public provisioning of healthcare is crucial to the ability of poor and excluded residents to access quality healthcare. Such institutional arrangement would, as matter of priority, provide redress for gender issues in the healthcare regime. Even where these issues are redressed satisfactorily, there would still remain the bigger question of whether increasing public sector provision of healthcare presents the most strategic use of scarce public resources. As it were, the government is finding it difficult to take up majority of the infrastructure coming up through the CDF. Quite evidently, the government has also not dealt with the significant problem of wastage and low productivity of its existing and local government health services. These latter require significant new levels of staffing, equipment and budgeting for essential supplies than is currently in place.[113]

It is also important that the health system can find sufficient resources to put into the public health side of the healthcare system. Without denting the prevalence of major public epidemics, including HIV/AIDS, Malaria and Tuberculosis the demands on the entire health system will continue to be stretched beyond capacity, demanding more resources than would otherwise be necessary. Moreover, a good number of initiatives in the public health arena, such as providing safe drinking water, community sanitation, especially for small urban centres, and safe and environmentally sound urban waste management services can be provided for within a robust municipal and sub-sovereign finance system. Other significant infrastructure-based public health demands such as social housing to eradicate urban slum situations can also be provided for using a creative combination of sub-sovereign finance, new socially-inclusive property rights regimes and better all-inclusive urban planning. Other issues that can be tackled through a creative combination of an effective asset-based community development system with sub-sovereign finance include gender-based violence, crime and joblessness. Working to systematically eliminate social vulnerability of the poor and excluded would have immense benefit to the overall healthcare delivery system in ways that dent demand and allow optimal utilization of available resources.[114]

[113] For a useful discussion on healthcare planning and financing within the contexts of a developing economy such as Kenya's, see Green Andrew (1994). There are numerous other resources available for this purposes, many of which were pushed by the Breton Woods institutions at the height of structural adjustments and thus need to be read with due care.

[114] Effective asset-based local economic and community development coupled with advances in individual rights and freedoms can have significant public health outcomes. It is now acknowledged that the health outcomes of girls and women depend in large part on their economic and personal autonomy from having to acquiescence to male power and sexual demands. This is true in all areas of health but more so in reproductive health, HIV/AIDS and maternal mortality.

The proposals we have made for a more central role for the social economy in the overall social development policy would have significant applications to enabling effective community and public asset-building in the healthcare sector. We have also made proposals with regard to the need for an effective system of local economic and community development that is rooted in the empowerment of local residents and communities through participatory planning and implementation of development interventions and the need for asset development and accumulation at this level.[115] These proposals would have significant effects on the health outcomes of local residents, improving their productivity and ability to rise to future health shocks.

We make proposals elsewhere regarding the necessity to institute an elaborate system of alternative community development finance intermediation within the context of local economic and community development. Community Development Finance Institutions would offer near unparalleled advantage in the delivery of any envisaged National Social Health Insurance Scheme. As community level financial institutions, CDFIs would be crucial in rolling out savings infrastructure for community members, mounting financial literacy, providing micro credit to residents and increasingly providing micro-insurance to community members and institutions against environmental hazards. Such hazards would especially include healthcare-based risks.[116] Taken together with other proposals such as universal and progressive Individual Development Accounts, CDFIs can provide the next frontier in provisioning for means-tested social health insurance and ensuring that local and regional health institutions, especially those that are public and social economy-based get the much needed alternative financing they need to effectively mount quality services and products.

Again, the sub-sovereign finance regime can play a critical role in attracting money to the social economy providers and to the CDFI micro health insurance schemes to meet the costs of inclusion of the poor and vulnerable. Sub-sovereign finance can also help to leverage private sector resources to these institutions by underwriting the risks inherent in their operations. This latter can be crucial should these social enterprises and the CDFIs want to raise money in the conventional debt and capital markets.

[115] The system we propose is consistent with the demands of the District Health System advocated by the WHO and now partially in place in Kenya. A well-functioning health district can indeed be a veritable area-based asset building mechanism for communities and residents. For a discussion on the district health system, see Tarimo E. (1991); Cassels Andrew and Janovsky Katja (1991); Gilson Lucy, Bafour Thuthula and Goosen Balfour Vossie (1997).

[116] It is instructive that social enterprise-based micro-finance are increasingly facing the challenge of HIV/AIDS by incorporating group-based micro-insurance schemes for members. Many HIV/AIDS care interventions have also discovered the power and potential of small and micro-enterprise, savings, and social solidarity, typical institutional products and features of micro-finance.

Elsewhere, we call for the conversion of established national and regional referral hospitals into social enterprise institutions. It is also possible to create a new range of sub-regional health institutions covering several county councils by converting a good number of existing district hospitals into social enterprise institutions. Supply institutions such as the national health management and supplies agencies, health training institutions such as the Kenya Medical Training College and university-based training programmes are also prime candidates for such conversion. The assumption with these conversions is that in a well coordinated national health insurance system, nothing is actually lost in social enterprise-based provision of these tertiary level services, yet providing them institutional autonomy would provide them with the freedom they need to grow into competent and competitive health institutions. In the long-term, the government resources would be concentrated more into meeting the health financing costs of district, sub-district and community institutions. Using this formula, a lot more money would be diverted from the public and private sector-based financing to help build the infrastructure costs of the social economy-based social enterprise establishments.

Towards the end of this report, we make proposals for a new apex finance mechanism financed through a combination of sources, including an elaborate Community Investment Tax Credit, Dedicated Special Finance Vehicles, special purpose tax measures built specifically to finance set purposes, donor income and other resources. It is conceivable that a dedicated finance facility for financing infrastructure development in healthcare can be made via a charge on motor vehicle insurance. This apex mechanism would provide much of the needed matching funds to make such initiatives as Independent Development Accounts feasible. Devolved and sub-sovereign funds can also provide funds to match those from the apex finance mechanism in capitalizing the needs of social enterprise-based local healthcare provision.

Hunger and Nutrition

Freedom from hunger and good nutrition are essential for human health and have numerous social and economic returns. Investments to meet the food and nutritional requirements have the potential to aid overall productivity, increase economic growth and reduce the income and asset inequalities prevalent in society. Unfortunately, not much regard is given to food security within the ERS, outside an admission that "a significant number of people, particularly children, still live under continuous threat of hunger and starvation".[117] Surprisingly, not a single devolved fund is dedicated to securing food security.[118] With the exception

[117] Economic Recovery Strategy for Wealth and Employment Creation, 2003-2007, p44.

[118] In 2005, Oxfam called for a special finance mechanism to buffer famine and drought in North Eastern Province and other drought-prone regions.

of the Arid and Semi-Arid Lands (ASALs) where development of water pans, drilling of boreholes and small scale irrigation projects have been in vogue, not much of the existing funds have been utilized to enhance food security. That this is so is surprising since Kenya experienced a severe drought as recently as 2004 when the CDF and LATF were already in full bloom. A significant amount of CDF resources designated as emergency funds was allocated to meet the contingency needs that emerged with the 2004 drought.

Historically, at least since independence, the predominant strategy of the state towards food security has assumed a triune strategy: first, to improve the productivity and yields of high and low potential agricultural areas by developing and adopting high-yielding and robust crop and animal varieties resistant to hazards such as pest infestation, drought, etc while providing extension services; second, build up strategic cereal reserves to meet national emergences in the event of drought; and third, provide emergency food relief, especially to communities in the ASALs in the event of a catastrophic famine.[119] This strategy that has to work simultaneously and systematically at several levels of the state has placed considerable demands on state resources. These demands include the establishment of national research capacities in the various agricultural sectors, capacity for national outreach and extension, capacity to monitor the likelihood of drought and famine long before they occur, and the capacity to roll out social assistance interventions rapidly in response to unfolding famines and other natural calamities.[120]

While the Kenyan state has acquainted itself well in the recent past, it has been obvious that better results could be achieved with a better designed asset-building strategy in the sector. The need for an asset-building strategy is critical, considering that state assistance will often kick in when communities have depleted their food stocks. This is exemplified, for instance, through official use of a food security economy model as an approach to food security assessment. This model seeks to measure the impact of a negative event, such as drought, on food security at household level. The model is based on a quantifiable analysis of how households in a community acquire food and income in a 'base-line year' and how that is changing at the time in which the analysis is done. Government response based on emergency relief kicks in once a critical threshold of insecurity has been reached. In contrast, community coping and management of these shocks have tended to emphasize building up household assets such as livestock, increasing the range of income sources, including establishing small businesses that hawk firewood, for instance, and selling one's labour mostly as casual

[119] See Kinyua, Joseph (2004).

[120] According to Joseph Kinyua, Permanent Secretary in the Ministry of Agriculture, between 2000-2002, with the assistance of the international community, the government used over Ksh 27 billion to provide emergency relief largely to ASALs. 20 percent of this was used on transport.

workers. Communities close to rivers have also increasingly taken to irrigation to meet their food needs and extra for sale even in places like Mandera.[121]

Unfortunately, even within the relief strategy, the state does not always provide assistance that is culturally appropriate to communities, is often lethargic in initiating meaningful response, and does not always have the amounts of strategic food and cash reserves required. This has often forced it to make international appeals for food that are time consuming and expensive to organize. In the face of institutional state failure with regard to its response to food vulnerability, the international not-for-profit and donor community has come to play a critical role in the overall response to famine-induced emergences.[122] These agencies have also come to play a more central role than the state in helping local communities revert to historical capacities and competences after a drought. This latter often involves painstaking work, long after the incidence of drought.

Tragically, much of the policy with regard to food security has concentrated on rural and ASAL populations at the neglect of urban communities.[123] In a situation where 60 percent of city residents in Nairobi live in slums and informal settlements, and where nearly 30 percent of the urban population lives below the official poverty line, the need to ensure food security in urban centres can not possibly be overstated.[124] The dynamics of ensuring food and nutritional security for urban populations are clearly different from those at work in rural communities.[125] In the latter, factors such as the purchasing power of vulnerable groups and individuals based to a large extent on their incomes, savings and assets come into play. In this context, income and asset-poor households and individuals are likely to have higher food insecurity than those who are relatively well endowed.[126] Just as important is the efficiency and cost of the system of

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[121] See ALRMP (2004). This analysis is insightful regarding how pastoralists cope and manage drought as a negative environmental event and especially how households and communities with high and divergent asset-holdings are able to cope better than others. It also points to potential for an asset-building strategy intervention in drought management.

[122] See Lesorogol Caroline K. (2004). See also SPHERE (2007).

[123] See, for instance, Kinyua Joseph (2004). Joseph Kinyua was the then Permanent Secretary, Ministry of Agriculture.

[124] An analysis of food security based on a household or individual's capacity to access food locally available is in keeping with current definitions and dynamics of food security, which stress capacity to acquire and not necessarily produce food. This capacity is not only conditioned by ones income and assets but also larger demand and supply issues outside the control of an individual or household. For an exhaustive discussion, see Nyariki Dickson M. and Wiggins Steve (1997).

[125] These dynamics would, however, hold for high agricultural areas whose main economic activity is cash crop farming and which have huge net food production deficits.

[126] As we noted, such individuals and households find themselves in a poverty culdesac where they have to spend all their income and earnings on basic essentials, never having anything through which to accumulate savings and assets. Given the opportunity, they would build up an asset base like any other person or household.

food distribution, including milling and processing, the availability and efficiencies of wholesale and retail food commodity outlets,[127] etc. As the experience with HIV/AIDS care has shown, urban emergency situations also depend critically on the availability of an effective non-state community development system with organizational capacity to reach to vulnerable individuals and households.

The proposals we make elsewhere in this report with regard to, for instance, Individual and Community Development Accounts have very real prospects for alleviating the food security situation in both urban and rural environments. Like other areas of human capital development, the real process of doing so would take painstaking and long drawn out efforts that are possible only in contexts of the significant institutional and organizational capacities called in the social-based economy intervention and new regional and community development organization interface. In a similar vein, potential exists within the proposed apex finance mechanism than is imaginable in the prevailing conditions. A strategic institutional nexus involving the proposed apex-financing mechanism, Community Development Finance Institutions, existing devolved fund mechanisms—not for profit actors in the social economy—and the existing public sector institutions supplying solutions to the sector has historically unmatched potential to deliver real assets and permanently turn around the nutrition and food security situation.

Within the urban contexts, potential exists for the creative use of sub-sovereign finance to scale up the construction of a range of producer and consumer markets on a social enterprise framework, including municipal enterprise. Sophisticated and well distributed producer and consumer markets are essential in the establishment of a viable, efficient and cost effective distribution and market infrastructure in agricultural commodities. These developments would have significant impact on the availability of essential foodstuffs in urban centres at affordable levels, while at the same time ensuring massive generation of revenues to rural suppliers. Producer and retail markets have significant potential to develop physical infrastructure such as warehouses as well as the financial instruments necessary for the establishment of a thriving commodities market in agricultural produce. As we shall see later, social enterprise-based delivery of infrastructure services, such as warehousing, cooling facilities and other infrastructure have the potential to form the bulwark of a secondary market in these commodities, thus providing the much needed price stability for urban consumers and rural producers.

[127] The availability of small scale grain milling, for instance, in informal urban settlements and rural medium income grain deficit areas has played a great role in reducing the cost of grain foods in the cereals post-liberalization era. For a useful analysis, see Nyoro J. K. and Nguyo Wilson (1999).

Once established, such marketing, distribution and financial infrastructure in the sector would provide the basis for long term asset-building necessary to secure adequate production of needed food items. It would be feasible, for instance, to build a social economy-based extension services in the context of secure produce markets and incomes. The potential for this is evident in especially the dairy and tea sectors where comparable infrastructure and institutions are in place. Specialized food production and conservation knowledge and technologies are also easy to generate and perpetuate in such a stable environment.

Housing and Shelter

> …improvement in housing stock is a strategically important social and economic investment…well-planned housing and infrastructure of acceptable standards and affordable cost when combined with essential services affords dignity, security and privacy to the individual, the family and the community as a whole. Adequate shelter also prevents social unrest occasioned by depravity and frustrations of people living in slums and informal settlements. …housing is also an investment good contributing both directly and indirectly towards poverty reduction by employment generation, raising of incomes, improved health and increased productivity of the labourforce
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> Government of Kenya, National Housing Policy *Sessional Paper No 3. of 2004*

Housing and shelter are traditionally not one of the human capital assets. Their centrality to individual and household well-being, however, is such that they occupy a central place in social development literature. The right to housing is also a central feature of the international human rights regime, which recognizes everyone's right to an adequate standard of living, including housing.[128] The quality, tenure and ownership of the house one occupies has significant impact on the life outcomes of the occupants. The Economic Recovery Strategy recognizes that "shelter is a social as well an economic good" and that "shelter and housing are basic needs for human survival and are important for the advancement of well-being".[129]

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[128] Kenya has been a party to the *International Covenant on Economic, Social and Cultural Rights* (ICESCR) since May 1972. The UN Committee on Economic, Social and Cultural Rights has defined this right as including the right to live at some physical address in security, peace and dignity and in an environment that guarantees security of tenure, basic physical infrastructure and social facilities and adequate social services. The housing should also be habitable, accessible, appropriately-located, culturally-acceptable and affordable. The right to housing is also inherent and contained in many other international law instruments to which Kenya is a party, including the *Convention on the Elimination of All Forms of Discrimination Against Women*, the *Convention on the Rights of the Child, as well as the African Charter on Human and Peoples' Rights*.

[129] Economic Recovery Strategy for Wealth and Employment Creation 2003-2007. This is further stated in the new housing policy spelt out in *Sessional Paper No. 3 of 2004*.

Kenya is in the throes of a deep housing crisis in its urban areas, arising from a combination of factors working together. According to the ERS, the chief problem has to do with the "high cost of decent housing, which the majority of Kenyans cannot afford".[130] This cost is attributable to the high cost of essential inputs into housing—land, construction, building materials and their financing—often through expensive bank loans and mortgages.

Nearly 80 percent of all households in urban areas live in rental housing. By contrast, nearly 80 percent of households in rural areas own their own houses. This situation was historically wished away on the assumption that most urban residents ultimately wished to settle in their native areas and are thus reluctant to invest in owning their houses in the urban centres. With rising and permanent urban populations, majority of whom are middle, lower income or poor, the need for a holistic and progressive urban housing strategy had risen to national importance. Historically, the public sector, through the National Housing Corporation, municipal councils, the central government and parastatals have provided the bulk of low and middle income housing in Kenya. Public infrastructure for providing low cost quality housing collapsed in the wake of liberalization, public sector reforms and downscaling, poor governance and corruption in the 1980s/1990s. Many of public housing units put up between the 1950s and 1980s have been irregularly allocated to private citizens in the name of public sector reform.

Private sector initiative in housing has historically been active. Surprisingly, even with one of the most developed financial and capital systems in sub-Sahara Africa, very little private sector financing is actually available for the housing sector. Recent estimates put the total bank credit to the sector at about 7 percent of overall bank lending to the private sector. The predominance of commercial banks in Kenya's financial sector has led to a prevalence of shallow short tenure credit products in the market. Very few banks have mortgage products. These have traditionally concentrated on the high income market segment and will routinely require a detailed and stable employment or income history, annual net incomes often not less than Ksh 1.2 million for the lowest products, and a considerable down payment on the mortgage.

Before 2003, majority of the private mortgage providers typically charged an interest of 30 percent on their mortgage, further curtailing the appeal of their products to even aspiring middle income households. Since 2003, there have been numerous changes in the government's fiscal regime that emphasise low budget deficits and depressed public borrowing from the financial markets. This has left banking institutions awash with excess liquidity. These conditions,

[130] This might actually be a misrepresentation, since alternative building technology, financing and delivery systems exist. These have been amply demonstrated by, among others, ITDG and the Jamii Bora Trust.

coupled with the relative macroeconomic stability characterized by low and stable inflation and improving business environments, have led to an increase of private sector lending to the housing sector at reduced and stable interest rates averaging 15-20 percent. But even this, and the continued emphasis of high income stability, has meant that many middle income households have not benefited from the resulting 'boom'. As before, the prospects for low income and poor households entering this formal housing regime remain bleak.

Outside a dedicated state intervention, prospects for low cost affordable housing in Kenya look bleak even with ongoing economic expansion. Recent and ongoing developments in the financial sector, for instance, have seen the conversion of three of the pre-eminent building societies into formal banking institutions, where they have easily taken up significant market presence. There has also been persistent talk of the Housing Finance Corporation of Kenya also converting to a commercial bank.[131] This leaves very few financial institutions dedicated solely to housing.

Beyond financing, many factors stand in the way of the poor achieving their right to housing. One key problem remains the availability of affordable land in urban places. In Nairobi, for instance, about 20 percent of households occupy 80 percent of available residential land. Nearly 1.5 million residents live in informal settlements, occupying barely 1000 acres. Little land is available for new housing developments, leading to a situation where much of the developments in housing are taking place in previously high income neighbourhoods. Land tenure and the legal structure for holding land and property is a complex regime, leaving majority of urban residents, including many who charge rent in informal settlements, to squat on the land.

Ironically, besides having a reasonably sophisticated banking system by regional standards, Kenya has one of the best-developed capital markets on the continent. Despite the huge potential for affordable long term finance from this market, housing finance is predominantly sourced from commercial banks. Majority of rental units are actually not put up using conventional mortgage but through shorter term asset finance products. There is virtually no housing development bond market, with the few long term state actors in the sector, including the HFCK and the National Housing Corporation relying primarily on

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[131] Equity Bank, by far the most successful of these former building societies, has effected a market correction of sorts by seizing institutional control of the Housing Finance Company of Kenya (HFCK). With a historic injection of Ksh 11 billion of new venture capital shareholding, the bank is reported to have set aside Ksh 7 billion as new financing capital outlay for the HFCK. The bank had earlier secured Ksh 7.5 billion credit line from international financial markets to lend for mortgage and housing construction. These developments are likely to make HFCK a dominant player in housing finance. It is not clear whether HFCK will target the low income market served by Equity Bank.

Barclays Bank of Kenya has also successfully issued a Ksh 5 billion long term bond to grow its mortgage portfolio (see Daily Nation October 17 2007 and 15 November 2007).

government subventions.[132] Other long term financing sources such as the National Social Security Fund have preferred to go directly into the housing market and put up middle and upper income housing.[133] Other institutional actors who could provide a veritable debt issuing regime for long-term low cost housing have serious systemic financial and management weaknesses that make them unlikely candidates, at least in the mid-term. The dearth of social economy-based low cost housing developers has also meant that the physical infrastructure for low cost housing development is actually absent.

The new housing policy commits the state to enabling Kenyan's to progressively realize the right to housing. Among the many strategies contained in the new strategy include:

- Reviewing and amending the banking sector legislation to promote the peculiar needs of housing finance;
- In conjunction with other partners, to promote new financial products and institutions that intermediate between the financial sector and the housing market;
- Recognizing, promoting and mainstreaming the informal and innovative financing mechanisms that are emerging through alternative financial intermediation, such as social enterprise-based micro-finance;
- Reviewing and modifying foreclosure laws and practices to enhance the security of tenure enjoyed on housing loans;
- Establishing a housing levy modeled on the National Social Security Fund to drive the construction of low-income housing;
- Developing the legal and institutional mechanisms for the establishment of a secondary mortgage market to raise long term finance through appropriate securitization; and
- Restructuring the retirement pension regime to allow schemes such as the NSSF to assign life insurance and benefits to members. This would at once enable over 300,000 members to use these accounts to access housing finance. This restructuring would also be done with a view to enabling investment in the arising housing finance market.

[132] The National Housing Corporation has been mulling prospects for issuing a Ksh 5 billion bond on the Nairobi Stock Exchange. This would be the first housing bond instrument on the market. It would also be a considerable investment seeing that the NHC total lending to the sector between 1963 and 2002 was Ksh 40 billion, contrasted with the Ksh 49.9 million that it invested in 2005.

[133] There exists vast potential to utilize the pension funds industry to invest in housing. Fiduciary requirements, however, would greatly constrain the ability of the funds to drive social housing. A combination of financing from a reformed sub-sovereign finance regime, a social equity capital market and a raft of privileges offered through the proposed apex finance mechanism has potential to establish a much needed market for economically-targeted investments specific to social housing.

These measures, if implemented, would significantly dent the current demand for 150,000 housing units against an annual supply of barely 30,000. The new policy, however, recognizes that these measures will be unlikely to spur the market to provide housing for lower income and poor urban households. Consequently, the policy commits the government to providing direct and appropriately-targeted subsidies for the development of social housing for low income and urban poor households. Support can be targeted at several levels, including local government infrastructure provision, tax exemptions for building materials going into social housing, and changes to the income tax regime to enable higher investments in social housing.

The new housing policy also recognizes the need for reform of local government authorities to prepare them to participate effectively in issuing and managing sub-sovereign debt to finance affordable housing. Other measures directed at these authorities would help them prepare physical development plans and provide land for low cost housing development.

The policy development also seems to recognize the need for new institutional and organizational arrangements in the land and housing tenure and delivery system for low income and poor urban households, and is working to pilot and disseminate emerging best practices in this regard. This would include the use of new cheaper technologies, new building codes, new legal title holding, new alternative financial intermediation, strategic community partnerships, among others. Pilot programmes are already ongoing in Nairobi, Mombasa, Kisumu and Mavoko through the Urban Slum Upgrading Project.

There is much to recommend in this new government thinking and strategy with regard to housing. Kenya needs complex and ambitious solutions to solve the urban housing crisis. Clearly, if implemented, the policy would go a long way in alleviating housing demand in urban areas. Within an asset-building and capability framework, however, the policy can be significantly improved in several respects. Some examples of these include:

- Conferring prior recognition and privilege to the right to own the house one is occupying. Within the context of the new policy framework, this would involve directing legislation, municipal planning, financing and other resource allocation to enabling all urban residents to own the houses they occupy.
- Investing more resources, including legislative efforts, to redressing historical public and market failure in providing housing to low income and poor residents. This is imperative given the extent of the problem, historically, which has led to nearly half of Nairobi's residents to live in slums.

- Scaling up already proven institutional, technological, tenuring and delivery interventions, such as the Jamii Bora Trust, ITGD, use of new soil compacting technologies, etc that are outside of the current government experimentation framework.
- Placing a premium on new urban re-zoning to enable inclusionally planning and settlement as well as the demands of a new environmentalism that we become better custodians of our environmental assets.
- Locating a concise and innovative core financing strategy to drive the process of housing asset accumulation for low income and poor urban residents, given the need for new money.
- Locating a clear and appropriate community-based social economy delivery strategy that focuses specifically on these residents, given the need for new delivery systems especially in the context of manoeuvering the complex terrain of providing low cost quality and affordable housing for low income and poor residents.
- Placing universal and progressive asset-building itself at the heart of the new housing policy.

The proposals can have a significant bearing on the policy outcomes of the new housing regime:

- Recognizing and mainstreaming the social economy and social economy institutions can aid greatly in the institutional design and delivery of social housing. Already, social economy-based organizations such as Jamii Bora Trust, ITDG, the Kenya National Association of Co-operative Housing Unions, and K-Rep Bank have demonstrated the potential of this sector to innovate around the problem of affordable low cost housing.[134]
- The new legal forms we propose, including the Community Development Land Trust, have potential to take out key assets such as land and financing from speculative hoarding and trading;
- Proposals for restructuring existing sub-sovereign finance institutions such as the CDF, the Housing Trust and LATF have significant potential to attract much needed new money to social housing.

[134] Like many other micro-finance institutions, K-Rep Bank started as a not-for-profit NGO but has since acquired a shareholding structure; ITDG, Jamii Bora Trust, NACHU and Faulu Kenya are not-for-profit non-governmental organizations. Jamii Bora Trust is perhaps the trail brazer with 2000 housing units in Kajiado built from a combination of low cost technologies by its members. When complete, each two bedroom housing unit will cost Ksh 325,000. Financing has been arranged at an interest rate of between 8.5-10 percent with each occupant paying Ksh 3,000 per month over 15 years. Each occupant will also pay Ksh 500 monthly to maintain facilities and the house.

- Proposals relating to the development of a social equity capital market have great potential to create a primary market for social enterprise-based housing delivery and for a secondary social equity market for social housing.
- Given the complexity of the social housing demands, the proposed new local economic and community development system can prove immensely helpful to area-based asset building efforts in social housing.
- Individual Development Accounts can prove particularly hardy institutional mechanisms to help low income and poor urban residents come into the social housing regime in the first instance.
- Community Development Finance Institutions and other community benefit entities can be especially innovative in delivering financing and programming products to social housing. Of special significance in this area is the provision and bringing to scale of social housing micro-finance targeting the legions of urban workers and entrepreneurs in the informal sector.
- Finally, the proposed apex finance mechanism can prove especially hardy in any efforts to create national, regional and area-based social housing trusts by supplying dedicated finance vehicles as well as Individual Development Accounts and community investment tax credits and other privileges to social investors in the sector.

Micro-Finance as Human Development Strategy

Micro-finance is perhaps the newest and fastest spreading strategy for asset-building among poor and low-income citizens. Micro-finance typically involves the supply of financial literacy, business planning and management skills, savings, loans and increasingly micro-insurance through social economy institutions and frameworks to poor and low income individuals with a view to lifting them out of poverty. Micro-finance has been offered through a combination of relief and livelihoods strategies that aim to first respond to the income needs of the poor and systematically reduce one's vulnerability by building an entrepreneurial asset base.

Micro-finance builds the individual asset base of participants through forced savings and well-managed debt, through financial and business education and by enhancing social solidarity and capital that issues from group lending. Creative micro-finance has increasingly taken to building individual assets through micro-housing products and micro-insurance, especially to cover health and environmental emergencies. The forced group savings have also provided an institutional framework to initiate community responses to negative events. By

basing their collateral on the group and, in particular, future group borrowing, micro-finance ensures that community members acquire assets, become more responsible over the management of individual assets and take an interest in the financial conduct of other members. Since most micro-finance entities are social enterprises, the institutions themselves work to capture the value added by group lending to build a stronger community and institutional complexity that increases and adjusts its asset value proposition to members of the community. By growing businesses, houses and reducing environmental hazards, micro-finance institutions bring immense value to the communities in which they are found.[135] All these instruments help nurture an alternative financial intermediation that has been embraced world-wide.

The government apparently recognizes the potential of micro-finance, especially to deliver micro-enterprise. Much of the reasoning driving the establishment of first the Youth Enterprise Fund and now the Women's Enterprise Development Fund is based on the assumed economic and social benefits of micro-enterprise and the prominence of micro-finance in enabling it. It is important to note that the ingenuity of micro-finance as an asset-building strategy lies in the unique nature of the product, including financial education, forced savings and micro-insurance. Micro-finance institutions, for instance, intuitively recognize that many business ventures will succeed once they can accumulate savings and graduate from need for micro-credit products.[136] Indeed, the primary motivator to use social networks as collateral in lending is precisely to provide an alternative to deposit savings for non-income people. Even when they provide loans, micro-finance supports these businesses by helping these entrepreneurs establish social networks that are beneficial long after their last loan repayment. Because of the relative risk associated with the product as well the social purpose motivation of its origins, micro-finance has been offered principally through not-for-profit financial intermediation.

Unfortunately, the institutional and asset-building framework of micro-finance strategy were, apparently, not the key motivations for the new enterprise funds. An asset-building strategy beyond merely providing loans can be key to maximizing the value of public subsidies for micro-enterprise development. Such an approach will be useful in measuring the quality of the opportunity created by the micro-loan to the individual and community; in how they help generate savings and new lending that was previously unavailable at community level; and in establishing new business competences through the financing and the

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[135] For a useful discussion of the asset -building potential of micro-finance, see Schreiner Mark (2004).

[136] Many participants soon discover that living off savings is a better strategy than doing so from loans. Individuals within social networks begin to jealously guard their new found freedom by pressurizing members to build their asset -holdings as a cushion to future consumption and collateral requirements.

value of new social capital generated in the process. An asset-building framework can also be key to significantly increasing the social return of investments in micro-finance. The proposals we make regarding a more central role for the social economy, limiting the delivery/project implementation aspects of existing sub-sovereign/devolved funds in favour of delivery by actors in the social economy, such as CDFIs, and the very call for the entrenchment of Community Development Finance Institutions as an alternative institutional arrangement to redress financial exclusion will go along way to rectify apparent policy confusion. Fortunately, much of this money has been channeled through institutional infrastructure of the micro-finance institutions such as Faulu Kenya and the Kenya Women's Finance Trust.

Other proposals such as the Individual Development Accounts, the new Local Economic and Community Development system as well as the apex financing mechanism for social economy-based delivery of public goods will privilege growing community development finance intermediation, including micro-financing, as the preferred institutional vehicle to deliver finance for community development.

Prospects for Individual Development Accounts

We variously identified the need and prospect for the establishment of lifelong individual development accounts as a cornerstone asset-building strategy for the poor and socially-excluded individuals and their communities. Individual Development Accounts provide matched savings for particular or certain statutory purposes, including education, healthcare financing, credit etc.[137] IDAs operate from the premise that socially-excluded and poor people have capacities and desires to plan for and invest in their own futures through institutional mechanisms that enable savings and the strategic use of this saving to accumulate alternative assets.

Individual Development Accounts are modeled on four simple but not always apparent truths: first, that the poor can save and accumulate assets often better than anyone else; secondly, that asset-holding has transformational potential on the lives of those who hold them, their families and communities; thirdly, that the inability of the poor to acquire and accumulate assets is a structural issue pertaining to prevalent institutional arrangements in society and less to do with individual competences and; lastly, that assets are a better guarantor and predictor of well-being than competing measures such as income.

[137] Individual Development Accounts were proposed in the 1980s by Michael Sherraden of the Centre for Social Development at the University of Washington at St Louis. Federal experimentation on IDAs commenced during the Clinton Presidency and is now an established national programme in the US. There are now numerous IDA-type schemes in the US and around the world, notably in the UK, Canada, China, South Korea, South Africa and Uganda.

Individual Development Accounts present new operational tools in social policy development within the institutional parameters of a socially-investing state. In this new policy framework, individual and community asset-building provides the first new frontier to systematically reduce and eliminate risks that are traditionally covered by social security and assistance, including poor health, unemployment, and the lack of an income. Individual Development Accounts are far from being merely accounts held by individuals. Usually implemented with the assistance of non-state actors such as community development not-for-profits and involving alternative community development finance institutions, IDAs present wholescale community efforts aimed at availing opportunity to grow assets and opportunities for a community's most deprived members.

While non-income poor initially need basic support to help them get some initial capital, such as through support with getting employment or starting a small business, once a source of regular income is established, these individuals are capable of making continuing deposits into qualifying financial intermediaries, which seek to raise matching funds for the accounts. Where appropriate, these accounts are converted into financial assets with guaranteed income for the life of the asset.

In a typical Individual Development Account model, individuals are eligible to participate in the scheme if they meet certain criteria. An individual remains eligible for matches only on making regular agreed deposits into their IDA savings accounts. CDFIs then work, with the assistance of philanthropy, municipal or sub-sovereign financial arrangements, to match the accounts on a scale of one to one, one to two or one to three. The match money is often kept in a separate account and can only be accessed for purposes approved by the particular scheme, such as tertiary and technical education, small business development, workforce development training, qualifying family health emergencies, etc.[138]

An expanded, universal progressive scheme can target all citizens beginning with children, say under 15 years old. The state, through appropriate sub-sovereign or devolved finance mechanism would deposit, say Ksh 20,000 into IDAs held at qualifying CDFIs. From that point forward, finances would be matched to local individual and community savings with the matching criteria varied to allow for progressive investments in the extremely poor and marginalized. Invested funds would become available to the individual on the occurrence of specified trigger events that can be tailored to meet an individual's critical asset acquisition requirements.

It is conceivable that the local Community Development Finance Institutions can be mandated and subsidized to operate and run such accounts for children

[138] See Boshara Ray *et al.* (2005).

within their respective jurisdiction. Parents and other local juridical institutions such as municipal and local authorities, Constituency Development Committees or qualifying Community Benefit Corporations can be mandated to sub-vent finance to such IDAs. Such funds can be available for use by the particular children and their parents to accumulate savings for their secondary school and tertiary education. Parents may be required to co-invest with the local authorities and national authorities by committing permanent savings to the CDFI-held IDA schemes. The CDFI would be mandated to invest these funds very much like one would retirement pension schemes.

While the government commitment to meeting the costs of the free primary education would be irrevocable, putting incentives for savings towards the secondary and tertiary education by attaching a permanent matching funds targeted at qualifying beneficiaries would be one way of actually investing in these children. Savings held by the CDFI would be crucial to driving local economic regeneration.

On entry to secondary school, the subsidy element of the local savings would be taken up by the secondary school bursary fund, which can be phased into a soft mid-term security against the income assets of local sub-sovereign financing schemes, including the CDF and LATF.

Qualifying CDFIs can also be used as the *de facto* financial intermediation institutions for the Higher Education Loans Board. Students and parents would be rewarded by the Board for holding accounts with the CDFIs. CDFIs would also make returns from the Higher Education Loans Board within their jurisdiction. A fund similar to the Higher Education Loans Board can be established to provide concessional financing for post-secondary education. The fund could be compelled to work through qualifying Community Development Finance Institutions.

Community, municipal, and area-based sub-sovereign finance institutions such as the Constituency Development Fund, the Local Authority Transfer Fund and possibly individual schemes specific to socially-excluded women, youths and children can act as mobilizing agencies for further local financing of education and workforce development. Schemes such as municipal or sub-sovereign bond on the capital markets are discussed later in this book. Such bonds would be available to meet the financial needs of competent CDFIs. Municipal and sub-sovereign authorities can also help to securitize successful credit-based financing programmes, making more money available to local CDFIs for similar purposes.

STATUTORY AND INSTITUTIONAL AUTONOMY FOR THE VARIOUS FUNDS

We noted earlier the need for a more rigorous juridical regime for various sub-sovereign finance schemes. The potential for the various funds to play an anchorage role within the system of financing asset development within the human capital industry would be severely constrained in their current legal and institutional form. Some of these funds enjoy very limited institutionalized mechanisms, have no statutory mandates and are dependent for their working on day to day interpretation of their mandates by numerous public servants and politicians. In order for them to take up this central role, it will be necessary for each of the funds to assume full autonomy, anchored through a specific statute and with a full complement of trustees, directors, budget and the independence to source funds. They should be allowed to set their own loan/grant-making and recovery conditions, etc.

These funds would also work with the proposed apex finance mechanism to deepen availability of affordable financing for the various schemes within their jurisdiction. This would create the possibility of using the resources available from the apex finance mechanism to attract private sector financing to qualifying social enterprise-based financing and provider institutions in the community. We anticipate that the proposed CDFI regime would go to work immediately to structure financing schemes and drive uptake of targeted asset accumulation within their jurisdictions.

The apex financing mechanism could certainly be persuaded to set up special purpose financing vehicles in various fields and sectors of technical and higher education. Local sub-sovereign funds such as the CDF can provide key securities to market-based CDFI vehicles, such as local economic and community development education bonds or Loans by establishing fund loss reserves—a pool of locally-held funds or investments designed to shield investors in these instruments. This latter facility would help leverage risks, making CDFI-held instruments attractive in traditional financial markets.

The proposed reforms imply that CDFIs, and not HELB or the other funds, would be the principal institutions through which services and products are offered, with access to the fund pools and resources available to HELB. The Board itself would have to transition to an institutional regime focusing on enlarging and investing the overall fund pool and policing the various CDFIs active on its portfolio.

PART V

RISING TO THE INSTITUTIONAL CHALLENGE OF ASSET-BUILDING[139]

…we cannot save and build for the future if we do not re-build our institutions. Institutions…are the very foundation of opportunities.

H.E. Hon Mwai Kibaki, President of the Republic of Kenya during the official launch of the Economic Recovery Strategy for Wealth and Employment Creation, 11th June 2003.

The re-construction of Kenya is a joint effort. …we must bear this in mind. The problem…can only be adequately addressed through the concerted efforts of the Government, local authorities, local communities, the private sector and Non-Governmental Organizations. This partnership-based approach is ideal…for the overall development of the nation.

H. E. Hon. Mwai Kibaki, President of the Republic of Kenya, 9th June 2003

[139] Much of the material in this section has been inspired by efforts such as *Beacons of Hope,* a Social Enterprise Company set up by Jane Wathome to offer employment and crucial income support to women living with HIV/AIDS. For the inspirational story, see "Beacons of Hope", *Parents Magazine*, November 2006 issue.

A MORE CENTRAL ROLE FOR THE SOCIAL ECONOMY? THE SOCIAL ECONOMY AS AN INSTITUTIONAL MECHANISM FOR ASSET-BASED LOCAL ECONOMIC AND COMMUNITY DEVELOPMENT

Ultimately, the process of social development requires institutional and structural regimes appropriate to the delivery demands for attaining basic human rights and freedoms. Capability and asset-building has to take place within a specific institutional framework and has to be carried out or conducted by various local and community institutions. In the current framework, the institutions charged with core asset-building responsibilities are located within the public sector —government schools, hospitals, local markets, slaughter houses, bus parks, game parks and game reserves, recreational parks, universities, etc. Significant and increasing provisioning of these goods and services is also carried out by the private sector, which has a nearly competing and wide array of institutions. A third and much ignored sector, which we call the social economy below, has also been struggling to provide a near similar range of services.

In much of the Third world as well as the industrial nations of the west, the social economy has picked the pieces where the market and public sector have failed to deliver on key social development outcomes. The social economy presents alternative institutional arrangements than those contained in either sector and has been key to effecting seismic shifts in such major 'revolutions' as the 'green revolution' that helped push up food security in much of Southern and Eastern Asia and now alternative financial intermediation, such as micro-finance, which is causing serious re-think about poverty alleviation, asset-building and human development for poor and low income individuals.

There is much in government policy, as evidenced in the new housing and HIV/ AIDS policy, which shows that the government recognizes the limitations of both the public and private sector in the delivery of key public goods—in this case housing and community-based health interventions. In agriculture, the state relies extensively on social economy institutions such as cooperative societies to deliver services and products in the sector. Social economy institutions have also proved invaluable in healthcare delivery and financing. They have infinitely higher appeal and potential for asset-based local economic development owing to their localism, democratic ownership and accountability, their focus on social purposes and their institutional independence from state and private sectors. Unfortunately, the government has yet to fully appreciate the potential of this sector and seek to supply solutions that can make it a key engine in the supply of social goods.

The Social What?

Social economy describes an area of economic activity existing between the private sector and the public sector and not accounted for and separate from either.[140] The social economy has been defined as "a group of private companies created to meet their members' needs through the market by providing goods and providing services, insurance and finance, where profit distribution and decision making are not directly linked to the capital contributed by each member, each of whom has one vote. The social economy also includes not-for-profit organizations that are private non-market producers not controlled by general government, produce not for sale services for specific groups of households, and whose main revenues are from voluntary contributions by households as consumers, payments from the government and income from property".[141]

The social economy thrives at an intersection of both private and public sectors, often working to correct public policy and market failure. This intersection is populated by the activities of not-for-profits, cooperatives, mutuals, professional and voluntary associations, foundations, and others. It includes not only social enterprises but also voluntary and community organizations, development trusts, trade unions, religious bodies and housing associations, charitable organizations, mutual societies, cooperatives, and other social firms. These organizations are defined largely by their social equity and democratic values and their function in standing in to deliversocial and public goods in areas such as healthcare, housing, employment, infrastructure, sports and leisure and the environment through socially-motivated business practice.

Not-for-profit, non-profit, voluntary organizations, charitable organizations are all terms that are used to define and refer to actors within the social economy. Owing in part to historical reasons, some terms have come to be associated with different meanings and brands. The terms NGO, and increasingly Civil Society Organizations, have acquired a particular identity that mostly connects them with policy and legislative advocacy as well as work in governance. They also have serious image problems with their governance styles, accountability and management. Similarly, Community-Based Organizations have come to acquire distinctive brand characteristics.[142]

[140] The term social economy has been in popular usage in Europe since the early 1990s. For descriptions and discussion of the social economy and actors within it, see for instance Julia Juan F. and Server Ricardo J. (2003). See also Department of Trade and Industry-UK (2002).

[141] Chaves R. and Monson J.M. (2000), quoted in Julia Juan F. and Server Ricardo J. (2003).

[142] For a useful discussion of the not-for-profit sector in Kenya, see Chelogoy Michael, Anyango Hellen and Odembo Elkana (2004).

We use the term not-for-profit non-governmental organizations to refer to all actors who, by definition, are founded for largely social, community or public benefit purposes, are self-governing private entities independent of government control, are not founded for private gain and, therefore, amongst other things, do not declare profits or distribute dividend. Most entities presently referred to as NGOs, charitable trusts, charitable companies, not-for-profit societies—including professional associations and a host of others would fit this description —including especially community-based organizations, self help groups, some type of cooperative societies, not-for-profit companies, as well as clubs and societies founded in the public benefit.

Social Enterprise as an Organizing Framework Within the Social Economy

Enterprise is now recognized as one of the key drivers of the economy, in a new paradigm that places enterprise—and one would presume the pursuit of private benefit—at the centre of the social, economic and political life of the nation. There has, for instance, been a lot of official talk about creating policies to mainstream private enterprise and reduce government engagement in enterprise activities.[143]

A key element of the social economy, social enterprise and community enterprise or social business refers to enterprise or businesses established for social objectives and to deliver specific social benefits.[144] The enterprise would usually be seeking to solve certain social or community problems such as providing skills and work experience for chronically unemployed persons. Profits or surpluses made through the business are principally re-invested in the business or in the community, offering the possibility of an effective and sustainable operation and leading to wider social and community benefits. Community enterprise is a major subset of social enterprise and shares the same combination of entrepreneurial skills and strong social purpose. Community enterprise is distinguished, however, by its focus on a community of place or interest and delivers local services to locals—often involving the employment of area residents.[145]

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[143] This reasoning permeates current government thinking about job creation and is one of the central motivators of, for instance, the Youth Enterprise Development Fund, which aims to build the entrepreneurial capital of young Kenyans. There are currently demands for a similar fund for women.

[144] For definitions and discussions of social enterprise elsewhere, especially in the UK, see IFF Research Ltd: A survey of social enterprises across the UK. The research report was prepared for the Small Business Service, Department of Trade and Industry, UK. See also "Social What? The what, how and why of social enterprise", in The Social Enterprise Coalition (2003): *There's more to business than you think: A guide to social enterprise*; Orlitky Marc, Schmidt Frank L. and Rynes Sara L. (2004).

[145] The Kenya Women's Finance Trust is a good example of a community enterprise—in this case focused on a community of interest. Many mission hospitals are in essence community enterprises. Social enterprises tend to be national or regional in scope and can even be international. The micro-finance company Faulu Kenya and Kick Start—formerly Approtech—can be cited as social enterprises.

Social enterprises are defined by a strong drive for institutional, functional and financial autonomy, a flexible non-bureaucratic way of working, a willingness to take risks and adapt to changing needs, a close understanding of and commitment to client groups, a commitment to staff development, re-investing profits in the social aims of the business or community; and the ability to deliver on social objectives while delivering products and services.[146] In contrast, private firms and businesses exist principally for profit and other income returns to their owners.

Both forms of enterprise will also deliver jobs and, through their production processes, products and services that add value to other services and goods and the lives of residents. The level of enterprise sophistication, including the amount of value addition, technological sophistication and organizational complexity, combined with other local assets such as a competent workforce and physical infrastructure all determine the net value that residents and the community can derive from the local business stock.

The social economy, through social and mutual benefit enterprises and the broader not-for-profit sector, has great potential to deliver on many of the key challenges confronting socially-excluded communities. A well-designed and successful social and community enterprise regime can be invaluable in meeting the Millennium Development Goals (MDGs), in delivering significantly on the Beijing and Cairo Platforms in pushing GDP growth in excess of 10 percent points, which is necessary to overcome absolute poverty and contribute immensely to socially-inclusive wealth and employment creation. Social enterprises can also provide individuals and communities of place and interest with the tools to build the financial, physical, human and environmental asset base necessary to regenerate and build themselves and their communities out of poverty and exclusion.

Successful social and community benefit enterprises are also well-placed to complement government in the provision of essential public goods and services in key sectors, and in provision of essential infrastructure such as producer and consumer markets, workspace as well as aid significantly in driving social capital and civil and community safety. The social exclusion framework and social and community enterprise model offer unique and unrivalled opportunity for mainstreaming the participation, benefits and ownership of women in economic activities and the growth agenda. A well-designed and successful social and community benefit enterprise strategy is key to evolving a socially-inclusive and prosperous society, thus helping secure the social and political stability of the Kenyan state in the mid and long term.

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[146] See also Bode Ingo, Gardin Laurent Laville Jean-Louis, Lhuillier Vincent and Petrella Francesca (2003).

The social economy, and in particular social enterprises and social investments, have great potential to deliver targeted services and growth to socially-excluded and poor communities. Social enterprise as business form offers a unique way of using traditional business methods to deliver much needed public goods and services that are often at the heart of economic and social exclusion, and which are responsible for spiralling poverty. Social investments and socially-responsive investment is emerging as a highly effective method of mobilizing development finance to drive the much needed financial, skill and physical capital to solve social problems while providing a fair return on investment.

Social and Community Investing

Social investment refers to the act of making investment decisions to achieve social as well as financial return.[147] An increasingly important element of the evolving social economy sector, social or ethical investment means different things to different people and the literature is still consolidating on a universal application of the term.[148] At the barest minimum, social investment entails making financial investments with assured positive social impact. Social investors will often consider the social and environmental impact of investments, both positive and negative, within the context of a rigorous financial analysis. Using a variety of social and environmental criteria—often called screens—they will identify investments that meet certain social and environmental standards and single them out for investing.

There are presently three recognized fields or strategies in social investment: social guideline investing or screening, shareholder activism and community-development investing.[149] Social guideline investing refers to the practice of including-excluding and evaluating publicly quoted securities from investment portfolios or mutual funds based on social and environmental criteria. Shareholder activism describes the many actions socially-aware investors take in their role as owners of for-profit corporations. These actions, which include forcing dialogue on issues of concern, filing or co-sponsoring and voting on proxy resolution, are aimed at influencing corporate behaviour to adopt a more responsible level of citizenship and pushing management towards actions that best advance the social bottom line of the company. Community investing refers to the act of putting capital in communities that suffer financial exclusion and under-investment. Investors provide equity, credit, capital, development and conventional banking products that the communities need to

[147] See the Social Investment Forum Foundation and Cooperatives, "Investing in communities".

[148] See Bauer Rob, Koediijk Kees and Otten Roger "International evidence on ethical-mutual fund performance and investment style".

[149] For a useful and comprehensive description and historical information, see The Social Investment Forum (2003), Report on socially-responsible investing trends in the United States; Stone Bernell K., Guerard John B. Jnr, Gultekin Mustafa N. and Adams Greg (2001).

overcome their financial exclusion and under-investment. Community investment makes it possible for not-for-profit corporations and organizations to provide much needed financial services to low and non-income earning individuals as well as supply capital for underserved local businesses and service organizations in health, education, workforce development, child care, workspace development, affordable housing, and environmental conservation.

Social investment promises attractive new possibilities for accessing much needed finance and investment capital to redress social exclusion, poverty and inequality, including women's income and asset poverty and inequality. A social investor, who is presented with the possibility of making investments in a municipal market or municipal water utility, can be moved to consider additional criteria such as the differential impact of the proposed investment on women and men and what has been done in its design to provide redress for women's practical and strategic gender needs.

Similarly, local capital markets, which will increasingly become the key financiers of local infrastructure development, can be moved to require legal assurances and guarantees that projects financed through their instruments work to prove redress for gender and other social exclusion.[150] Devolved or sub-sovereign finance can play an important role in pushing these markets and investors to include such 'non-core' criteria in their financing instruments. Some prospects for this strategic collaboration between devolved finance schemes, such as roads levy and capital markets are considered later in this study.

Social Enterprises and Investing: Significant Untapped Potential

Kenya has some phenomenally successful social enterprises in nearly all areas of the economy. Some of the better known social enterprises include the Agha Khan Health Service, the Nairobi Hospital, the Guru Nanak, MP Shah and Mater hospitals. The Catholic, Presbyterian and African Inland Church run the largest health service outside the government and often serving remote and marginal communities on a social enterprise basis.

In education, majority of successful private establishments in university and tertiary education, such as Daystar University, Catholic University of Eastern Africa, the African Nazarene University and a host of technical training and business colleges are essentially social enterprise institutions.

In the financial sector, there were, by 2005, over 100 not-for-profit non-governmental organizations engaging in provision of micro-finance nationally.[151] By

[150] For a detailed example of a model of an interventionist social investment-led state reconstruction, see Bernier Luc, Bouchard Marie and Levesque Benoit (2003).

[151] See Central Bank of Kenya (2005).

2003, the social economy-based micro-finance institutions such us companies limited by guarantee, NGO-MFIs and SACCOs provided over 80 percent of the Ksh 71 billion loan advances to the MSE sector.[152] Leading and emerging micro finance institutions such as K-Rep Bank, Jitegemee Trust, the Kenya Women's Finance Trust, Jamii Bora Trust, KADET Services, BIMA and Faulu Kenya are essentially social enterprise institutions. Some of these institutions—the Jitegemee Trust, Kenya Gatsby Charitable Trust, Micro-Finance Enterprise Support Trust and the Oiko Credit are infrastructure institutions in the industry, mobilizing and raising finance for concessional low interest lending and grant-making in the sector—classified by the Central Bank of Kenya as "wholesale microfinance institutions".

Social enterprises have also ventured into social housing and workspace provision, among others. One of Kenya's most infamous slum upgrading programmes—the Mathare 4A Slum Upgrading Project—was conceived as a social enterprise through the agency of the local catholic church.

It may be difficult for many to view the activities of organizations euphemistically referred to as civil society as constituting a distinct area of economic activity that bears great potential for helping society overcome its many economic problems. In truth, this area of our economy and the organizing ethos of the not-for-profit is as crucial as the public and private sectors to helping our society meet the challenges of the day, and these go far beyond those captured by such well-intentioned formulations as the MDGs.

There is an emerging body of evidence that solutions from within the social economy are better-placed than government and private sector initiatives to meet the needs of society in a wide range of fields, including healthcare, education, workforce development, social housing, regeneration, childcare, environmental management, culture and sports, etc.[153] The work of organizations within the social economy is often focused on asset development and service delivery to those groups, or in those places where social exclusion is deemed to be high. The sector has immense untapped potential to deliver asset-based growth, incomes, jobs and skills in socially-excluded poor rural and urban communities.

Social enterprises, voluntary not for-profits and other actors in the social economy are an excellent institutional asset class working in the immediate and long term capital and asset interests of socially-excluded individuals and communities. The question about how to make devolved and sub-sovereign finance work in the long

[152] See Aleke Dondo (2003).

[153] See Department of Trade and Industry-UK (2002). Data for the size, role and contribution of social economy actors in Kenya is almost non-existent, but much can be gleaned from the government's reliance on community-based organizations and NGOs to deliver key public health strategies related to HIV-AIDS, Malaria, micro-finance, healthcare facilities and others. The success of high end actors such as the Agha Khan Health Services, missionary health services and private universities also point to the potential of the sector to deliver services.

term strategic gender interests of women and other socially-excluded groups cannot be answered adequately without examining its nexus with these institutional actors within the economy and society.

As public sector institutions, sub-sovereign finance schemes have tended to take on perhaps the worst face of the sector. Many studies have found them to be grossly inefficient, wasteful, corrupt, misdirected in terms of mission, lacking in complexity and form relative to their statutory purposes, and serving the patron-client relationship that exists between ruling elite politicians and their dependents in the rest of the economy.[154] Since they are premised on a flawed episteme of what ails society, it would be too much to ask that such schemes be gender-aware, gender-responsive or socially-inclusive.

There is also need to rethink the notion that all public goods must be provided by the government. This is not to be confused with a call for privatization, where the private sector provides the goods and owns the means of production. As we have shown through the social enterprise framework, public ownership and production models exist that are competent in producing such goods and services. Much of the analysis of the various sub-sovereign finance schemes have concentrated on their public sector character and the much stated need to seek and allow solutions from the private sector. While the private sector has immense capacity to supply solutions to many of the nation's social problems, the empowerment of socially-excluded and marginal groups and working in their strategic interests cannot be counted among such problems. To the contrary, the combination of private capital holdings and the interests of patriarchy in the private sector make such a possibility remote and serve to make the private sector itself the target of much correction by state interests.

There is, however, much need and scope for interrogating the possibilities of creatively employing sub-sovereign finance to shape and aid the capacity of state and private sector actors to come to the aid of women's strategic gender interests as well as the longer term social inclusion of historically marginalized communities. These possibilities form the subject of our considerations later. Of equal strategic but much ignored prospect is the possibility and promise of interfacing devolved and sub-sovereign financial intermediation with a sector that is a priori dedicated to fight social exclusion and injustice, and that has proven more responsive and accommodating to supplying solutions to women's strategic gender interest—the social economy. The social economy is, therefore, handy to the debate and project that has pre-occupied the larger part of this costudy—how to grow the economy while simultaneously seeking to provide redress for gender inequality and social exclusion by growing the strategic asset base of women generally but more so socially-excluded women as well as marginal groups, communities and regions.

[154] See for instance Kimenyi S. M. (2005). See also Mwalulu, J. & Irungu, D. (eds) (2004).

The social economy is unique and unparalleled in providing solutions to grow the productive capacities and asset base of socially-excluded individuals and communities by creatively and continuously investing in their educational, health, workforce, workspace, financing and technological capacity. A strategic coupling of devolved and sub-sovereign financial intermediation and the social economy and its actors, therefore, holds great potential for building capabilities and assets as well as securing a minimal functionings threshold for socially-excluded citizens.

Social and community benefit assets exist in nearly all the economic and social sectors. Investing in assets that feed into human capital can include such investment as primary and secondary school education, post-secondary school training institutions at community and regional levels, technical and tertiary education and other specialized educational institutions.

Investments in health institutions can include the entire range of health institutions beginning with community, sub-district and district hospitals, provincial hospitals and national referral hospitals. It is also conceivable to have a new range of hospitals located between the provincial and district hospitals, which we refer to as regional hospitals.

We make proposals elsewhere for the establishment of 26 regional economic development areas, each with distinct local economic and community development zones. Each of these zones, which would ideally comprise 3 or so counties and would have regional-wide infrastructure supporting key capability and functionings areas present excellent opportunities to locate viable social economy-based institutions. Each county would continue to have, say, a district hospital now renamed a county hospital with several sub-county hospitals. Each sub-county hospital would be flanked by several ward-based or community health centres. The prospects for interfacing sub-sovereign and social investment-based private sector finance to supply investment financing for these social enterprise-based community development infrastructure institutions can be overstated. It is also conceivable that each of the 21 regions can support, for instance, a regional polytechnic, or a regional hospital.

For these assets to prosper and deliver their full benefit to these individuals and communities, it will be necessary to overcome the many and considerable obstacles that stand in their way. Some of the key obstacles include:

- Lack of government recognition
- Failure by state to embrace the capability/asset-based development/ vulnerability and social exclusion framework
- Failure by state to acknowledge the existence and potential of the social economy and its various actors, including social enterprises and social investors

- Capture by more familiar for-profit organizing forms and the dominant civil society NGO form
- Disproportionate and weak regulation
- Inadequacy of legal forms available to the sector
- Lack of appropriate infrastructure to aid local economic development
- Lack of appropriate financial intermediation
- Lack of a structured social investment market
- A structural misfit in development facilitation and administration
- Irresponsive capital markets

The subsequent chapters of this section attempt to describe and propose solutions to some of these obstacles.

RETHINKING THE LEGAL FRAMEWORK FOR THE SOCIAL SECTOR

Despite the proliferation of social enterprise and a flourishing social economy, there has been little legislative and policy recognition of the key motivator behind this apparent flowering of the so-called civil society—that they are driven largely by a desire to help individuals and communities overcome social exclusion. There is no candid legal acknowledgement of the purposes and work ethos that motivate not-for-profit organizations. There is also no candid effort to provide legal, policy and fiscal innovations to actors in the sector to recognize their work and make it easier and rewarding to engage in it as well as make it difficult for fraudsters to use the purposes and methods of not-for-profit organizations for private gain. Subsequently, the social economy is riddled with many obstacles that hinder effective application of its philosophy and methods, including social enterprise, and investing to deliver real opportunities and assets to socially-excluded and poor communities and making it a weak candidate for long term strategic investing via sub-sovereign and devolved funds.

Unfortunately, it cannot be taken as a given that actors in the social economy will always live up to their social purposes. Providing systemic redress for social exclusion, including women's exclusion and subordination, may not constitute an entrenched social purpose for many of these actors. It would be necessary not only to make sure that the sector is obligated to deliver on its social purposes, but also that these purposes embrace women's and other peoples' social exclusion and discrimination.[155]

The first part of this review of the legal framework looks at regime issues—the overarching legal regime that governs not-for-profit and charitable non-governmental activity. It is our view that the current difficulties in the sector—from its financing, lack of independence, governance and accountability, failing purposes and its apparent failure to deliver real benefits to society, especially those to whom it owes its legitimacy—severely handicap its usefulness for any other project. It may also be the case that the roots of these structural weaknesses can be traced in good measure to the lack of an enabling legal framework. Given the strategic role of the sector in our conceptualization of what it would take for devolved and sub-sovereign finance to come to the aid of the empowerment/capability functionings/well-being and asset development interests, we make an attempt to provide solutions to these vexing problems.

[155] There are many factors that may contribute to a sub-optimal performance and mission drift in social economy organizations. For discussion, see for instance Spear Roger (2004).

Inadequate Legal Foundations

There is currently no overall centerpiece legislation or law defining charitable or not-for-profit purposes and activities in Kenya. In all the various frameworks in existence—the NGO Act, the Societies Act, the Building Societies Act, the Cooperative Act, Trustees Perpetual Succession Act, the Registration of Documents Act, the Companies Act or the Business Names Act—there is no elaborate attempt to define the statutory or legal purposes of not-for-profit or charitable activities. The limited recognition of such activity issues from the unlikely place of laws relating to taxation.

The predominant notion of not-for-profit and charitable purposes in taxation laws and in the NGO Coordination Act apparently borrows almost exclusively from the UK charity law in which charitable status is framed in the 1601 Statute of Elizabeth and cumulative decisions of the charity commission and case law. This statute and tradition recognizes the relief of poverty, advancement of religion, advancement of education and other purposes beneficial to the community. The 'other purposes beneficial to community' clause has been used by successful charity commissioners and case law to admit many diverse activities as charitable in purpose. While there exists a vibrant statutory interpretation and evolution of charitable purposes in the UK, the same cannot be said of Kenya.

There are many vexing issues that arise from a discussion of whether such a tradition is necessary. It would be clear that the current position where no single authority outside the NGO Board or the Kenya Revenue Authority can determine the purposes and activities of the actors in the sector is not tenable. It is also clear that the purposes recognized by this statute are clearly not adequate to our circumstances. Kenya, for instance, is one of the most unequal societies on earth. The country is one of the world's poorest and lacks a vibrant tradition of pursuit of a comprehensive range of basic human rights for all its citizens. The country also boasts rich and diverse cultural traditions, which would no doubt come into play in a debate about what giving, social support, community development and regeneration really means. Clearly, the extended family support structures and many other uniquely African social institutions would be difficult to trace in definitions of charitable or not-for-profit organizing or the conceptualization of what is private and public as may be framed in mainstream UK traditions, for instance.

Maintenance of privilege a dominant organizing motif for charities and NGOs

Owing in part to the colonial origins of the many successful not-for-profits and charitable organizations, and owing to the aspirations of patriarchal privilege and exclusion of the post-independence economic and political elite, many organizations working on a not-for-profit basis and receiving/enjoying public

goodwill and gifting are not required to demonstrate public, social or community benefit. This situation has been worsened by the absence or lack of any direction by the office of the Attorney General in the absence of a statutory charities' authority. Many organizations in the charitable and not-for-profit sector are indeed exclusivist clubs and societies and service the financial and political elite in areas such as healthcare provision, amateur sport, etc. They are distinguished, for instance, by the high cost of access for the services they offer and institutional cultures that look down on the poor and less fortunate, who might need their offices.

Official apathy towards a genuinely not-for-profit sector

There has over time developed considerable official apathy towards a genuinely not-for-profit and charitable sector working in the larger public, social or community benefit. The question, therefore, arises regarding what actually is the organizing ethos of institutions in the sector and why they should be given any privileged tax or other state treatment. Why, for instance, should a health facility frequented and accessed only by the financial crème of society enjoy tax privileges? Should the requirement to operate in the public benefit and actually deliver on it not be a core criterion for according privilege to the sector?

Benefit of community/public society

The lack of appropriate legal framework and regulation has combined to remove the sheen or veneer of public/community or social benefit from majority of actors in the sector. It is often assumed that not-for-profit activities or organizations are established essentially for the benefit of the public. Unfortunately, there is no law in Kenya that requires not-for-profits to operate in social, community or other public benefit and that prescribes an appropriate duty of care for the members, directors and key officials of such organizations to ensure that their activities are in line with this broad objective. There is also no law in Kenya that seeks to explicitly provide for what range of activities and objectives may be deemed as being in pursuit of such benefit. There is, however, a presumption of such benefit in both the NGO Coordination Act and within the tax regime. Similarly, the Registrar of Societies will often scrutinize the objectives of societies to eliminate the prospects of private returns accruing to the members of registering societies.

This has allowed the evolution of a situation where many not-for-profits do not feel compelled to deliver even a modicum of public or community benefit. This is so even where the majority of these organizations have been established with participation by the state through gifting of land and from the contributions of private individuals and charities. These organizations are also exempt from

taxation even where they charge for services. Many are the times, for instance, when critically ill patients will be turned away from supposedly not-for-profit healthcare establishments on account of their inability to secure admission via an unusually high access fee or security.[156] The assumption of public, community or social benefit is usually crucial to conferring privileged status to not-for-profit and charitable activity. It is important that this situation is corrected by requiring all those who aspire to the status of a not-for-profit public entity to show in their purposes that they indeed propose to offer such benefit, and through ongoing regulation to produce social and ethical accounts of such benefits.

Emerging Legal Framework

New and expanded definition of causes and purposes considered legitimate for charitable and not-for-profit activity

It will be necessary to adopt a new and expanded definition of causes and purposes considered charitable for purposes of not-for-profit activity. In formulating such purposes, it will be instructive to consider those factors that have been responsible for driving extreme poverty, inequality and social exclusion and factor them into such purposes. Purposes provided for by international agreements, such as the Universal Declaration of Human Rights, the Beijing Platform for Action, the Convention on the Elimination of all Forms of Violence Against Women, the Convention on the Rights of the Child, the Convention on Social and Economic Rights, and others relating to the environment form part of the recognized purposes for charitable and not-for-profit organizing. When complete, such purposes should include the advancement of health, human rights, equality, conflict processing/resolution and reconciliation, prevention, relief and mitigation of poverty, the advancement of culture, the arts and heritage, amateur sport and recreation, advancement of education, social and community advancement, promoting active citizenship, advancement of environmental protection and sustainability, advancement of civil and community safety, and other purposes beneficial to society and community.

Requirement to work in and demonstrate public benefit

We also propose to entrench in the determination of these purposes a clear requirement that they work in public benefit and demonstrate so in their institutional and other cultures. We expect that organizations in the sector will exist to deliver actual benefits to the public as a whole or to significant parts of it,

[156] It will, for example, be remembered that it took over one hour, and the intervention of the then Minister for Health, for the Nairobi Hospital to admit the late Dr Omondi Mbai who had been rushed to the hospital in a very critical condition. The Nairobi Hospital is a not-for-profit institution run by a social economy entity—The Kenya Hospital Association.

and that beneficiaries in the sector will not be defined or identifiable in terms of personal or contractual relationships to those offering the benefits. The beneficiaries should not be identified as secondary others; membership and services should be available to all those who fall within the class of beneficiaries. Any private benefit arising directly out of the pursuit of the organizations objects is legitimately incidental and the amount of private benefit should be reasonable. Charges should be reasonable and should not exclude a substantial portion of the beneficiary class. The service provided should not cater only for the financially well-off but should, in principal, be open to all potential beneficiaries.

It is also necessary that the sector be enabled to flourish and grow in order to secure its financial good health and to be able to pay for services such as contracting its workforce at rates that are competitive in the market. Often, actors in the sector, especially in healthcare, will require a huge outlay of capital to replace and maintain equipment, buildings, etc. For these and other reasons, we do not propose that the fees in the sector be fixed or pegged to particular benchmarks. It will, however, be clear that organizations in the sector will have to aspire to and demonstrate public benefit to society, and that their conduct in this regard should be measurable and ascertainable. It will also be clear that organizations in the sector that do not pass or meet a benchmark criteria of public, social or community benefit will not attract the benefits that come with the status of not-for-profit and charitable organizations in the sector, including exemption from paying corporation tax.

The legislation would also require that the proposed apex authority in the sector periodically carries out public consultations on what purposes and activities constitute public benefit and that following the requisite regulatory oversight hearing by Parliament, it can publish rules certifying such purposes as it may deem so as qualifying for purposes of the law. The legislation would require all applicants and actors in the sector to apply to the authority for determination and certification that their purposes and activities are charitable and not-for-profit. We do not propose that any of the purposes currently recognized as charitable and not-for-profit be excluded. We do propose, however, a recognition that conditions that drive not-for-profit and charitable work change and that assets previously aligned to service purposes that may not be considered charitable presently be re-aligned to other emergent purposes.

Test of public benefit

In order to ensure transparency, objective and fair criteria, the law should prescribe criteria for determining whether proposed activities and purposes are in public, social or community benefit and whether the continuing conduct of an organization meets criteria for public benefit. The principle means of establishing this would be through a test of public, social or community benefit

(test of public benefit). The test of public benefit would be simple and not obstructive for actors in the sector. It may be applied in large measure by using a lay or street person's perception of public benefit.

The test of public benefit would also require that aspiring organizations commit to practices that maximize public good out of the operation of the organization, including a commitment to social and gender equity in institutional cultures, work and outcomes, to fair work practices, and to submitting to social, ethical and environmental reporting.

The law should also be explicit that all the purposes for which organizations in the sector are established are in trust. The assets of such organizations, how they conduct themselves and carry their businesses in pursuance of these purposes and objects are, therefore, subject to a regime of duty of care. While not all assets in an organization may be held in trust, the purposes for which these assets are held are and, therefore, there will be a corresponding duty to ensure that the assets of an organization are appropriate and maximize value to these purposes. The law should give the proposed apex regulator power to take over the assets of organizations previously registered and incorporated as not-for-profits and charitable, and which have enjoyed the privilege of this status, where such organizations fail to comply with the new statutory regime for the sector. Such assets would be transferred to entities established for similar purposes and with an appropriate lock on their assets securing them for public benefit in perpetuity. The law should also require the authority to establish exhaustive mechanisms to ensure and secure this public character of organizations in the sector.

Permanent lock on assets

One of the key determinants of the difference between not-for-profit and charitable organizations from other modes of organizing is the application or conversion of an organizations asset for private gain. The underlying assumption in not-for-profit organizations is that assets and the income of not-for-profits are applied for the purposes for which the organization was established. There is no requirement in law, however, to ensure that this is indeed the case.[157]

[157] A recent case of such obvious conflict was the transfer of the Mt Elgon Hospital, which is a trust hospital, to a private status—an action recently reversed though a High Court decision. There is also an on going dispute pitting the Uasin Gishu Memorial Hospital, also a trust hospital, and the Moi Referral Hospital at Eldoret. Less conspicuous but which should have drawn the attention of policy makers and legal experts was the transfer of the Kabarak High School and the Sunshine Secondary School, previously considered 'public' schools and established through considerable government and public good will into 'private' schools. The decision for this was apparently effected through a request by the former Head of State that the government withdraws all teachers and other support attached to the schools in recognition of their private status. This was apparently in total disregard of the fact that these schools, though resting on private land, were indeed established through the use of public resources. At the time of the 'conversion', students in the schools were indeed government-sponsored.

All the assets of all not-for-profits, charitable non-governmental organizations and entities should be locked from being distributed for private gain and require that they be used for purposes that are clearly for the benefit of the public. Being statutory requirement, such an asset lock would be irrevocable to the extent that such assets cannot be transferred for use in purposes that are not charitable and not-for-profit. To achieve this, the law would declare an asset lock on the properties and other assets of not-for-profit and charitable organizations and that all organizations in the sector be required to have in their constitutions or statutes declarations that their assets are held for public benefit purposes and, save for certain purposes, such as statutory disposal to pay debts etc, would not fall into private use. The law would require the approval of the proposed apex regulator for a change of purposes or transfer of assets even when such assets are being moved to service other purposes considered not-for-profit and charitable. Asset protection in this way would bring this regulatory regime and actors in the sector closer to the regimes existing in other international jurisdictions.

Social enterprise not-for-profits

Many charitable and not-for-profit organizations either run enterprises or are run as enterprises. Many others charge a fee for services they offer even though they would not ordinarily view themselves as enterprise-based organizations or would not want to be perceived as such. Majority of these organizations will argue that the fee is essential in order for them to meet the cost of their services and that any surplus they generate in the process is re-invested in the organization, thus enabling it to better pursue its purposes.

Ideally, charging fees for services should not affect the public character of a not-for-profit organization. Indeed, some of our core recommendations for the sector include modernization of laws to allow social purpose organizations to employ the entire gamut of methods available in the economy to seek resources to finance and drive their purposes. In reality, however, many charitable organizations in Kenya charge fees that place majority of the population out of their potential service reach, achieving a perhaps undesired effect of promoting social exclusion. The test of public benefit should be set and administered such that organizations generally do not charge fees that have the effect of locking out potential beneficiaries. Where an organization in the sector has to charge high fees, and we expect there will be many instances, it should be clear that this is so that it can either subsidize the cost and access fee of some of its other services or so that it can generate certain conditions necessary for it to provide other public benefit purpose services. A university hospital, for instance, which charges high access fees for patients so that it can continue to offer low cost or free medical degree or diploma qualifications should pass a test of public benefit generally

for these purposes. In the same vein, a not-for-profit organization established for the purpose of providing specialized skill, experience and income opportunities to ex-convicts and specializing in the manufacture of high cost furniture should pass the test easily on account that its beneficiaries are really the prisoners and not the consumers of its furniture.

The apex authority would set up a clear system of determining the threshold and character of public benefit and apply it to all organizations with limitations on access to their service on a continuing basis. The authority would set up a complaints mechanism that will allow potential members and/or beneficiaries who feel offended by limitations on access to facilities or services of organizations in the sector to vent their frustrations. The authority would be obliged to notify the organization of the complaints and their nature and to require that the organization files a response with the authority. Depending on the nature and potential truth value of the complaints, the authority could order or conduct a full scale investigation of the organization with a view to recommending or taking action as may be appropriate. Where limitations on access are considered prohibitive and organizations fail the test of public benefit, the law and authority should allow affected organizations to grow/realign/reengineer their provisioning for public benefit in lieu of maintaining their not-for-profit status. Ultimately, failure to meet the compliance standards for the test of public benefit should lead to organizations losing their not-for-profit status and the authority moving in to secure assets and purposes of the organization.

Recognizing social and community enterprise

Enterprise is now recognized as one of the key drivers of the economy. There has been a lot of talk and policy to mainstream private enterprise, remove the government from engaging in enterprise activities and promote, especially, small and medium enterprises. However, there are individuals and organizations who will engage in enterprise activity principally and exclusively for public, social or community benefit. There are others who will contract enterprise activities with a view to helping them deliver on their social purposes. There are yet others who will incorporate as charitable and not-for-profit entities specifically for purpose of driving enterprise solutions. Not-for-profits are also increasingly turning to enterprise solutions to ensure that they are sustainable and that they deliver on their social and public benefit purposes.

Admittedly, however, there continues to exist a cultural and institutional predisposition against enterprise orientation and activity in the sector. The practice and law on trading by not-for-profits currently limits trading to activities directly connected or related to furthering their objects or purposes. A not-for-profit entity wishing to engage in substantial trading for the purpose of generating

income is required to set up a separate trading entity to do so. This separate trading entity may not enjoy the benefits of the status enjoyed by its parent entity.

It has been argued that this practice is helpful in making the liability of not-for-profits in taxation transparent and preventing the not-for-profit from abusing its charitable status in law. While this argument is certainly correct and persuasive, it must be weighed against other realities in the sector and the advantage and benefits that the sector delivers to society. There is no doubt, for instance, that not-for-profit health institutions such as mission hospitals cannot run without assuming an enterprise orientation. There is also no doubting the fact that mission-run health establishments have continued in many places to be the only healthcare institutions within miles and, even where other private and public ones exist, to be the ones that set the standards of care in the region. Yet, many social entrepreneurs who wish to establish health establishments often have to register as a trust, association or other entity, then incorporate the hospital as a limited liability company. Should they choose to incorporate the entity as a company limited by shares, it will lose its tax status and be liable to pay corporation tax. Yet, the ability of the organization to offer limited shareholding in the entity to other prospective social investors may be crucial to attracting much needed capital.

We make key proposals for a new company form that would release social entrepreneurs from these limitations. We propose below that measures be taken to recognize social benefit enterprise as a legitimate charitable and not-for-profit motivation and objective. Not-for-profit enterprise activities in the interest of the public or community should be recognized as legitimate charitable and not-for-profit purposes and activities. In this framework, laws relating to incorporation in the sector should be firmed up to enable organizations in the sector to engage in enterprise activity without the hindrance that can come with a deficient legal form and unlimited liability.

Statutory duty of care

A sufficient statutory duty of care should be placed on directors of all not-for-profit organizations that either choose the enterprise format or to contract enterprise activity to deliver on their social purposes, to account for their choice, to report to their constituency and the authority on their impacts, and to secure the organization against mission drift—where the social mission of the organization is lost to its enterprise orientation or character. The duty of care regime, in this case would include demonstration of specific training and capacities at the level of trustees, directors and membership for not-for-profits engaged in enterprise.

Governance/Trust public confidence

To grow the sector and to eliminate the current crisis of confidence especially suffered by the NGO form, and also in view of the numerous responsibilities, financing and privileges we propose for the sector, it is crucial that the sector enjoys and commands the utmost confidence from the public. To achieve this, it is imperative that the governance arrangements and outcomes, financial arrangements, accountability standards and practice and other institutional arrangements are tailored to secure this public confidence. Through appropriate subsidiary legislation, the authority should publish rules that:

- Entrench stakeholder participation in the governance of the sector, including especially stakeholder participation in the life of individual entities
- Require effective participation and representation of women in all aspects and life of the organization
- Entrench social auditing reporting and practice
- Provide legal protection for whistle blowing financial and social auditors
- Require exhaustive and material information on the activities of the entities as may be required
- Require that any not-for-profit entity with a turnover above a given threshold, say Ksh 2 million, to audit their books and have them signed or issued by a professional auditor
- Require organizations to establish three and five year strategic plans and two year operational plans
- Require organizations to make information on their activities available to the public
- Enable the authority to make information available to the public
- Require organizations to report any material impropriety to the authority, together with what actions have been taken to correct the situation (this would be confidential)
- Empower the authority to propose actions and recommendations
- Empower the authority to author/license or issue a rating and branding scheme on the quality of reporting, service and institutional soundness especially for large or any desiring organizations to inspire confidence of the public in the sector

A good and dynamic brand

One other key issue that relates to the legal form has to do with branding the entire sector and brand differentiation within the sector. A good and dynamic brand is a powerful asset in many respects. Appropriate branding provides a powerful resource mobilization tool for a sector and actors within the sector. On the face of it, and from the engrained attitudes of operators within the sector and society generally, not much thought is given to the place and need for an appropriate brand to drive the entire sector, its sub-sectors and individual actors.

Many observers will be forgiven if they assumed that the most dominant brand in the sector is the NGO. While there is no research or reliable data to go by, even a cursory inquiry into the sector quickly reveals that nothing is further from the truth. The most successful organizations in the sector are neither registered nor incorporated with the NGO Coordination Board. Such organizations include flagship institutions as the Nairobi Hospital, the Agha Khan Health Service and Hospitals, Catholic Health Services, PCEA Health Services, and many others.

In education, flagship organizations in this sector include universities such as Daystar, Catholic University of Eastern Africa, Baraton, Nazarene University, the Agha Khan University, and Strathmore University. In community development financial intermediation, organizations such as the Kenya Community Development Foundation, the Kenya Women's Finance Trust, Jitegemee Trust and many others are not registered NGOs. Indeed, many trading not-for-profits and other organizations that may desire the NGO status find the legal and regulatory regime currently in place for NGOs to be detrimental to their purposes and thus move to use other legal forms to incorporate.

One result of this unfortunate situation is that the sector suffers from lack of sufficient scope for branding. It is difficult, for instance, for the state to supply incentives to the various sub-parts or the sector as a whole with a level of certainty about the impact of these policies. While some sub-sectors have been clearly opposed to embracing the state, others must do this in order to better provide their services.

THE CHALLENGE OF LEGAL FORMS AVAILABLE TO THE SECTOR

To Incorporate or Register

Quite apart from the epistemic foundations of the sector, and partly as a result of it, the other major legal challenge to the sector is the legal forms available to it. There exists many routes through which organizations in the sector can register. These include registration as:

- Charitable trust under the Registration of Documents Act
- CBO with the provincial administration—district or provincial development officer
- Child welfare organization/home/informal educational institution with the Ministry of Education and the Ministry of Culture and Social Services
- Society with the Registrar of Societies
- Cooperative with the Commissioner for Cooperatives at the Ministry of Cooperative Development and Marketing
- Building society under the Building Societies Act
- NGO with the NGO Coordination Bureau
- Company limited by guarantee with the Registrar of Companies, or
- Business under the Registrar of Business Names Act

The existence of many routes through which actors in the sector can register is both a boon and disadvantage to the sector. One of the many positives of this scenario is that it has enabled the sector to become multi-faceted and dynamic and, therefore, defeating simplistic and misdirected attempts to capture and it. This situation has also enabled the sector to grow organically without the hindrance of a cumbersome regulator. Among the negatives is that the sector lacks sufficient differentiation and has commanded little official or state recognition. While the private sector is universally recognized, and hailed as the engine of capitalistic development, this sector has suffered from poor recognition and branding. Its value to society is often also much taken for granted as a non-economic community service. While this wide choice of registration forms may seem to indicate diversity and complexity, without an underlying legal framework of what charitable and not-for-profit purposes are, it can actually be quite chaotic.

Partly as a result of the lack of legal definition, there has not been clear differentiation between incorporating in the not-for-profit sector and registration. While many organizations are, for instance, registered as NGOs, it is not clear to what extent this actually confers to them the status of incorporation. Majority of

the registration forms actually do not confer incorporation. Unfortunately, not many people setting up establishments in the not-for-profit sector bother to differentiate registration and incorporation. Many so-called community-based organizations owe their legal status to a letter of recognition from the Ministry of Gender, Culture and Sports. Such existence has many shortcomings as members and officials soon come to discover. An organization will want to incorporate for any number of reasons, with the more familiar ones being the need to limit liability of members and officers as the organization becomes more complex to better manage its assets, to better mobilize resources, to engender more structured accountability to members and other institutional constituencies and to better the legal and public recognition. Lack of incorporation has serious drawbacks in terms of the legal and organic complexity of actors in the sector, their ability to acquire and hold assets, their ability to acquire equity or debt finance, the continuity and survival of the organization, etc.

While the lack of incorporation has many drawbacks, inappropriate incorporation is just as detrimental to the health of the sector. Many organizations in the sector find that they are registered under one legal regime and incorporated in another. An organization may be registered as a trust, for instance, but incorporated as a company limited by guarantee. Similarly, an organization may start life as an NGO or society before becoming a company limited by guarantee. Many not-for-profit SACCOs and emerging CDFIs are registered as cooperative societies but incorporated as companies limited by guarantee. While there is not much research or data to show the effect of this situation on the health of the sector, clearly there are many risks that attend to it, including the risk of double regulation, risks to membership and organizations purposes as the organization can be one or the other legal person at any one time, and the failure to secure the assets of the organization for the purposes for which it was started, which is essential for not-for-profits. It would be of interest to learn, for instance, what the impact of the social purposes of organizations such as K-Rep, which began life as an NGO and later branched into several different organizations such as K-Rep Bank, K-Rep Holding and K-Rep Advisory Services, has on the initial and continuing purposes of the organization. What legal issues arise, for instance, when an NGO converts into a company limited by shares and with dividend-driven equity?

There is clearly a need to differentiate between status and incorporation, with registration denoting more the status of the organization and incorporation the type and legal person of the organization. There is also a need to make both the process of registration and incorporation easy, predictable and assured in the sector. In Kenya, organizations are not assured of either even after meeting all the requirements. In majority of instances, not-for-profits have been frowned upon by government and state officials, who are in law central to their registration. In the past, this was the case with registration as an NGO with the NGO Board. A

new regime has made this relatively straight forward, albeit costly procedure for aspirants to this status. On the other hand, the Ministry of Lands, whose consent is required for the incorporation of trustees under the Trustees Perpetual Succession Act, has often been reluctant to grant such incorporation to aspiring Trustees. Partly as a result, there are many small trusts and charities whose trustees are not incorporated and who, therefore, shoulder a heavy risk and burden of liability with regard to their activities as trustees. This official reluctance has driven many to seek alternative incorporation either as a company limited by guarantee, as cooperatives or as NGOs with the attending legal ambiguity.[158]

There are also many other problems that come with the inadequacy of legal forms. Key among these are the insufficient provisions for protection of assets from demutualization and private use, registration and incorporation taking too long and the unavailability of any inbuilt form of legal and other organizational aid to the sector.

Modernizing the Legal Regime in the Social Economy Sector

It will be necessary to modernize the legal regime of the social economy sector by establishing the following new key legal reforms.[159]

- Community Benefit Company (CBC)
- Community Benefit Society (CBS)
- Charitable Incorporated Trust (CIT)
- Community Benefit Organization (CBO)
- Community Benefit Limited Partnership (CBLP)

Community Benefit Company

The company form has for long been a popular vehicle for incorporating not-for-profits. Many current leaders in their fields are all incorporated under this form as companies limited by guarantee. The company form is a good and universally accepted brand and holds the pride of place at the community of legal forms.

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[158] The difficulties that this kind of situation can bring was partly captured by the attempt in 1994 by the Attorney General to revoke the registration of the Mwangaza Trust on the grounds that one Act does not confer the requisite legal status to carry activities without incorporation while knowing fully well that this would be denied by the respective Minister once the incorporation was sought.

[159] The re-engineering of legal forms as proposed here has been attempted with commendable success in key jurisdictions such as the UK and Central Europe.

The companies form is, however, easy to manipulate and prone to abuse. Kenya has not evolved a rigorous tradition of accountability, such that while the private sector is hailed as the key mover in the economy, the Registrar of Companies can hardly monitor or account for the activities of companies. The registrar also clearly lacks the appropriate institutional framework to ensure that companies meet their minimum statutory requirements. Public trust in the not-for-profit sector is built on the assumption that actors in the sector are able to account for their actions and how they use their resources.

While there are numerous examples of not-for-profits incorporated under this form who are industry leaders in their specialty, there is little data on those that have failed and why, including whether incorporation and the burden that comes with regulation was a factor. The limited by guarantee incorporation route, however, has several inbuilt disadvantages, among them:

- It does not expressly prohibit profit-taking by members
- It does not provide for a permanent lock on the assets of the company for the purposes for which the company was formed
- It does not allow for equity participation in the sector
- It does not allow for exclusive branding of the not-for-profit public benefit nature of the entity and enterprise activity

We do not intend that not-for-profits incorporated as companies limited by guarantee change their legal form. However, all those incorporated as charitable not-for-profit companies should be brought under the regulatory regime of the proposed authority. An office of registrar of not-for-profit companies should be factored into the proposed structure and functions of the new authority. The new authority should, in consultation with actors in the sector, publish rules that will guide the incorporation and continuing status of not-for-profits incorporated as companies limited by guarantee. Such statutory requirements, as proposed elsewhere and including the lock on assets, should not be subject of subsidiary legislation.

In recognizing the need to provide the wider advantages of the company form to the sector, a completely new company form—the Community Benefit Company—available exclusively to the sector should be established. The key features and attractions of the new company form would include:

a) Incorporation as either limited by guarantee or limited by shares form.

b) Protection of the integrity of the not-for-profit nature of the company's operations. The shares issued by companies incorporating under the limited by shares form should assume the character of preference shares or such other entitlements with a limitation to the rate of return that the company can declare on the shares. This rate may be benchmarked to an

industry standard, such a few percentage points above long term government debt paper or a prevailing interest rate. Companies incorporating using this form would be barred by statute from issuing dividend but encouraged to offer a return on these shares that would be sufficient to attract investors. Investors would also benefit from relief on capital gains and income tax. It may also be feasible to cap the dividend policy of trading not-for-profits that choose the incorporation by shares mode. The particular policy can be issued as subsidiary legislation by the proposed apex regulator in the sector.

c) Protection of the not-for-profit purposes of entities that choose this route. A statutory cap on the number of shares that can be held by individuals in such companies to no more that 35 percent would be necessary.

d) No management responsibility for holders of equity in these forms, unless it is being exercised by a manager through the proposed Community Benefit Limited Liability Partnership form. These and other measures would be crucial for purposes of limiting the amount and extent of profit-taking that may be achievable in this company form.

e) Explicit duty of care and transparency requirements suitable to its public benefit trading status.

f) Explicit social and ethical accountability requirements suitable to its public benefit status.

g) Full compliance with modernized company law regime

We have made proposals elsewhere for a superior debt instrument registered or recognized by the Capital Markets Authority. Among other features of this instrument is its ability to enable the holder of the instrument to participate in the management and running of the company, without compromising its purposes and membership rights. This instrument has privileges more or less similar to preference shares. Companies incorporating under either the limited by shares or limited by guarantee should be able to issue these kinds of debt instruments to attract investment capital and key management and enterprise skills. Shares open up this company form to sources of finance in the market that are not currently available to actors in the sector. This company can issue preference shares with a fixed nominal return or based on a market benchmark. Shares can be perpetual or redeemable. Preference shares may or may not have voting rights as set out in the terms of the issue.

The CBC will be expected to file social accounts with the regulating authority, benchmarked to the complexity and size of the enterprise. Organizations choosing this form will have to contend with a strict regime for the test of public benefit than may apply to the other forms. Directors of such companies will be under

legal duty to ensure that the organization manifestly meets benchmarked criteria for public benefit.

A Community Benefit Company (CBC) will enjoy tax exempt status similar to other not-for-profits in the sector. The tax exempt status is a major attraction to social entrepreneurs and needs to be preserved in lieu of the extreme risks social enterprise companies assume to deliver to their social/public benefit purposes. Where there are clear and proven doubts about the not-for-profit and public benefit nature of a CBC, then such issues should be handled by the apex regulator and should not infringe on the status of the CBC in question. The authority will have sufficient powers to demand disclosures and reform with the CBC to bring it in line with the expectations of primary legislation relating to charitable and not-for-profit purposes. Other features of the company regime will apply to the form.

The primary advantage of incorporating in this new form is the ability to attract investments to the not-for-profit sector without suffering undue damage to the purposes and organizing motif of the sector. Shareholding, however restricted or limited, brings new types of accountability than those that are current in the sector. It is already clear that those social enterprises that are able to do well, such as the Kenya Women's Finance Trust, Jamii Bora or Faulu Kenya, are those that have accountability regimes that have a strong shareholder element even when such shareholding is held by other NGOs.

The requirement to return surpluses, some of which can be passed on to investors as returns on risks they have taken in investing in social enterprise ventures, will also reinforce expectations and enterprise cultures traditionally associated with for-profit corporations. Again, it has been proven that some of the most successful trading not-for-profits such as those in micro-credit, in tertiary education and in healthcare are those that have engrained enterprise cultures that are similar with those found in the for-profit sector.

The caps on profit-taking, on the size of shareholding and the new overall legal regime that places a cap on the assets of not-for-profits as well as requiring that not-for-profits work manifestly in social/community or public benefit will safeguard against the possible erosion of the core purpose of actors using this new company form.

Community Benefit Limited Partnership Agreement

We have proposed a new incorporated legal form—the Community Benefit Limited Partnership Agreement—to be achieved through amendments to Cap 65 (Limited Partnership Agreements) of the laws of Kenya. The limited partnership form has proven very effective and popular as a vehicle for channeling

venture capital investment especially in UK.[160] Reform of the current Limited Partnership Agreement legal form to make explicit amendments to recognize social economy-based and not-for profit Limited Partnership Agreement can, therefore, be strategic for asset-building and financing in the sector.

A discussion of venture capital may look strange in a presentation on the social economy. In reality, most trading not-for-profits need the kind of long term capital and enterprise and management support typical of venture capital investments. Local and global trends are also emerging where institutions with significant financial capital have adopted typical venture capital attributes of availing long term capital to not-for-profits on condition that they are involved in management decisions and that such capital assumes the status of so called 'programme-related investment', a long term loan with very low interest. Such arrangements are, however, not straightforward and depend on the good will of the receiving institution. Where the institution has serious governance problems, funds already disbursed are lost, with the donor withholding further disbursements.

The Community Benefit Limited Partnership Agreement form may also work well for not-for-profits that wish to graduate micro-enterprise offerings into longer term structures with typical debt-for-equity features associated with venture capital. This would offer them more legal and organizational complexity to offer larger, longer and more risky patient finance to emerging micro-finance portfolios as well as to small and medium scale enterprises.

While the proposals relating to the Community Benefit Company (CBC) form may offer some respite for some funding institutions, it is essential that the law makes provisions for investors who desire to enter relationships with actors in the not-for-profit sector akin to the venture capital model.

Evidently, there are also many for-profit corporations who wish to structure some of their activities for the benefit of community, as witnessed by the emerging Corporate Social Responsibility (CSR) activities, and who may wish for a convenient legal form.[161] This new legal form will enable them get into partnerships with not-for-profit entities to establish and finance activities in the sector while getting the tax and other benefits for these investments.

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[160] The UK has the second largest venture capital industry in the world behind the United States of America. Venture capital and reforms within the UK capital market is responsible for majority of the fastest growing companies in the UK and Europe.

[161] Notable corporations include Safaricom with the Safaricom Foundation and East African Breweries with the East African Breweries Foundation. Other companies with significant CSR activity include the Nation Media Group, Backlays Bank Kenya and Kenya Commercial Bank. CSR, often designed to massage the ego of the corporation is, however, to be differentiated from social investing.

This new legal form also offers considerable benefits to firms that have traditionally factored support for amateur and philanthropic activity within their business model. It is conceivable that corporations presently engaged in amateur sport, in conservation work and others will be attracted to the ease and transparency of this new form.

The Community Benefit Limited Partnership Agreement form is an improvisation on the Limited Partnership Agreement (LPA) form and will apply the provisions of the LPA form with the exception that investments and assets and purposes of the Community Benefit LPA are exclusively charitable and not-for-profit. Where it is set up for investment purposes, the Community Benefit LPA would also be required to invest only in companies established under the sector or to CDFI portfolio companies. The Community Benefit LPA form would be used for purposes of apportioning tax credit to private corporations and high net-worth individuals where applicable. Changes to the law would also entail establishing a Registrar-General for the new legal form.

Community Benefit Organization

Kenya has one of the most active grassroots community organizing sectors in African. Much of this sector has grown against the grain of, first the colonizing power and second, the post-independent centralist and closed government systems. Under the prevailing conditions, community-based organizations need the blessings of the provincial administration for their registration and continued operations in an area. Their registration does not confer incorporation and are often regarded as formalized groupings of people.

The transient and weak formalization belie the importance these organizations have assumed in delivering key public benefits, including resolving the key social and public problems. Community Benefit Organizations have attempted to solve some of the most intricate and complex problems facing community life, including halting the spread of disease, caring for the sick, overcoming illiteracy, generating investments and employment, generating and harnessing community savings, environmental protection, etc. Community-based institutions have started secondary schools, technical training institutions, hospitals, credit and savings societies, markets, etc.

The registration and the very institutional form open to community-based organizations, akin to a cooperative society, also severely limits the scope of their operations and their capacity to innovate and grow institutionally. There is clearly a need to ensure a legal form that guarantees institutional independence and vitality to pursue their community benefit purposes to the full, to ensure that they can attract human, financial and other resources and to secure the capacity of the organization to evolve in complexity as they grow. It is, however, also

necessary to ensure that such organizations remain faithful to their calling to community development, especially their ability to serve specified communities and to pursue well-articulated purposes that go to solve ascertainable problems in a community.

It will be necessary to change the law to enable a new incorporated legal form, the Community Benefit Organization (CBO), for not-for-profit civil society actors at community level, including broad communities of interest, and to be achieved through amendments to the Trustees Perpetual Succession Act. This status should be available to organizations incorporated as not-for-profits through other laws. It can also be used for purposes of incorporating entities under trust law. This can be achieved by changing the Trustees Perpetual Succession Act to allow the incorporation of the purposes for which they exist as trusts serving a particular stated community of place or interest with specific objectives, and for their registration as non-governmental organizations with the proposed apex regulator in the sector.

The amendments to this Act would also involve establishing a Registrar-General and accompanying staff for not-for-profit and charitable organizations. The registrar would also be responsible for the registration and incorporation of the proposed Charitable Incorporated Trust proposed below. The functions of the registrar would have to be available at least in each of the 30 zonal local economic and community development administrations referred to elsewhere in this study.

The proposed amendments can be modeled largely on existing requirements in the Societies or Companies Act, taking care to conform to traditional expectations of trust organizations.

Community Benefit Society

A Community Benefit Society can be achieved through amendments to the Industrial and Provident Societies Act, the Cooperative Societies Act, the proposed SACCOs Act, the Building Societies Act and the Societies Act. Kenya has witnessed the demutualizing of key building societies such as Equity, Family and East African Building Societies into fully-fledged commercial banks apparently as part of strengthening the financial services sector. While these developments have wide appeal, the new institutions seem likely to suffer from irreversible mission drifts from their institutional location as alternative financial intermediation organizations, targeting asset-building for sectors of the population that are underserved by the conventional commercial banks. The institutional form of societies is appealing for purposes of asset development for low-income and poor people. Many micro-finance institutions rely on this form to garner group

guarantees and eliminate the requirement for collateral that is a central feature in commercial bank lending.

The proposed new form provides for incorporation of societies dedicated to the benefit of community with the requisite provisions against private benefit by members, except where this is incidental to the delivery of the service or where members constitute a category recognizable as putative beneficiaries under charity law. Such members would, for instance, include low income, poor, ex-convicts, orphans, etc. Societies such as building societies for low income persons, societies of orphans or people living with HIV/AIDS or other chronic and long term illnesses, etc are also envisaged, as well as societies of beneficiaries of certain charitable organizations who set out to aid the organization, such as an alumni organization, an organization of rehabilitated ex-street children or ex-convicts or survivors of gender-based violence. Organizations under this regime should have typical features that protect assets and purposes of the society from conversion for any other use.

Amendments to the Cooperative Society Act, for example, would be needed to enable a cooperative society to qualify as a society for the benefit of community. This would bar dividend taking by members would bar conversion of equity or assets to exclusively private use, would allow for conversion into a normal cooperative or other status providing that the assets of the organization are secured and transferred to another asset lock-based organization serving similar purposes, and providing a sufficiently high threshold for the conversion, such as 75 percent of all members in favour. Legislation in the Societies Act should also enable cooperatives to permanently lock their assets and purposes by entrenching them in their constitutions. Amendment to the law should enable the establishment of a Registrar-General for Community Benefit Societies, whose consent would be called for before respective registration and incorporation by the parent statute. The law should also specify a liability regime, preferably one similar to the Limited by Guarantee Company form.

Community Benefit Land Trusts

Community Benefit Land Trusts could be achieved through amendments to the Trustees Succession Act. We make proposals elsewhere for the enactment of a comprehensive apex financing mechanism—Social and Community Benefit Asset Endowment Scheme—run by an authority established within the legislation setting up the scheme. We have also proposed that the apex regulator for actors in the social economy—the not-for-profits authority—would have powers to establish schemes that enable the conversion and transfer of various public properties into social enterprise-based sub-regional facilities.

It will be essential that these authorities have sufficient recourse in law not only to require that such properties be conserved for the purposes for which the conversion was granted, but to impose other requirements by way of charter that imposes conditions that they deem appropriate for the transfer of the property. Such conditions would include environmental conservation, such as protection of certain fauna, bird life or other naturally occurring features in the property, the preservation or establishment of certain historically important features, the provision of certain services to community/society, etc. Under this kind of scheme, for example, it is conceivable that Kamiti Maximum Security Prison, which is the acknowledged burial site of the late freedom fighter Dedan Kimathi, can be converted into a historical museum or a public park. The prison would be moved to another location without historical relevance, perhaps in the Nairobi Metropolitan region.

It is also conceivable that the communities, local government authorities, the central government and private corporations may desire to use the law to vest such title to properties. Cooperators in a particular urban housing development may, for instance, desire to conserve certain open spaces and fauna for posterity and their communal use. The proposed amendments should enable such purposes. The proposed Community Land Trust should enable such broad conservation. In the US, Community Land Trusts have become instruments of choice in conservation, low cost housing and other public and community benefit projects where land is a principal asset.

Charitable Incorporated Trust

Charitable Incorporated Trusts could be achieved through amendments to the Trustees Perpetual Succession Act. Present practice and law has limited opportunity for incorporation of charitable trusts, forcing many registered trusts to seek incorporation as companies limited by liability or to choose the NGO form. While there is provision for incorporation of trustees under the current law, this is rather restricted and it is not clear whether the trust body has the same benefit. The law also places those desiring such incorporation at the mercy of the minister, in this case Minister for Lands, who may or may not accept an application for incorporation altogether, or apply conditions to the certificate.

For those who choose either the NGO form or the Company Limited by Guarantee, it is not clear how well these different regulatory regimes fit their purposes as trust bodies. Board members of a charitable organization, for instance, are also charity trustees and have, therefore, to wear different regulatory hats depending on which regulator they are relating to. While the duties imposed by both laws are clearly not uniform, it is not clear which takes precedence. What, for instance, would be the impact on the Kenya Women's Finance Trust if it was

deregistered as a company or as a trust? Yet, it is clear that many trust bodies operating without the benefit of incorporation or the restricted incorporation of the Trustees Perpetual Succession Act carry too many risks and that the form is not suited for many of the activities they engage in to meet their purposes.

The new form will have the following features:

- Limited liability by members and trustees
- Foundation or membership formats
- Incorporated legal form
- Model constitutions by the regulating authority
- Key features of the not-for-profit charitable status as may be set out in statute and by rules made by the authority
- The amendment will allow for the establishment of a Registrar of Charities, separate from the Registrar of Titles/Documents or the Commissioner of Lands. This office will vest in the proposed apex regulatory authority in the sector
- Amendment will also allow existing charities, NGOs and not-for-profit limited liability companies to transit to this form should they so wish either by majority decision or unanimous resolution.

Municipal Enterprise Companies

Significant progress has been made in the establishment of municipal enterprises, particularly in the water sectors where municipal water companies are now the norm. Municipal enterprises are conceivably utility-providing institutions supplying essential services such as electricity, waste management, ICT broadband, producer and retail markets, local colleges and high schools, etc. Independent municipal enterprises, with boards that are statutorily differentiated and demarcated from the parent local government authority, can be key to providing key institutional assets to a local economy. They can also be important in redressing entrenched social and gender-based exclusion. Where they work well, local authorities often provide a regulatory and evaluative function to municipal enterprises, often anchored on a municipal enterprise law that sets the regulatory regime.

Municipal enterprises can be key to driving local economic diversification and competitiveness. Such key assets as wildlife parks and local forests can actually be run as municipal enterprises. Institutionally, the municipal enterprise form is invaluable to protecting and growing the infrastructure backbone of many social services. Social services such as provision of clean piped water, quality rail

and road networks, appropriate sanitation and drainage, health and education are all premised on the availability and quality of base physical infrastructure. The integrity of this infrastructure is, therefore, key to the quality and efficiency of the services provided. Many local authorities have, however, perceived service provision to commence once infrastructure has been developed, often by an external actor such as the central government. Many proceed to run the service without regard to safeguarding the structural integrity of the infrastructure, often reducing the design life of the structures, increasing the cost of maintenance and necessitating re-construction.[162]

Local authorities also lack the budgetary and management complexity to finance or attract financing for the set up, management and maintenance costs of built up infrastructure. Local authorities also often lack the institutional complexity to deliver services, even when these infrastructures are in place, leading to monumental wastage and dereliction.[163] These and other factors have led to a situation where the central government has historically assumed responsibility for the provision of core basic social services away from local authorities. In its turn, not only has this worked to produce a heavy central government bureaucracy, it has resulted in the central government supplanting local government as the key driver of local economic and community development. This has led to the emergence of structurally irresponsible and near irrelevant local authorities, while local populations have blamed their dissatisfaction with the service provision situation on the central government. An institutionally autonomous municipal enterprise regime can remove much of the structural weaknesses identified above.

Proposals we make elsewhere regarding the establishment of a new social equity market, a new debt market for social economy organizations, and a new asset-based system of local economic and community development would particularly reward service delivery through independent municipal enterprises.

The legislation on the new enterprise form would require local authorities to ou-source key social service delivery to these enterprises, with the local authority assuming the role of a regulator, public watchdog and custodian of the public interest in the service and facilities. The law should also require local authorities to align their resources in ways that support the public, community and social benefit mandate of these enterprises and specifically to match the capital and

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[162] The effect of this can be felt through the recent breakdown and reconstruction cost of such key infrastructure such as the Sasumua Dam, supplying about 30 percent of Nairobi's water requirements.

[163] The need to correct this situation was apparently one of the motivations for the Local Authority Service Delivery Action Plan and its financing instrument—the Local Authority Transfer Fund. Newer efforts to get around this problem have involved the establishment of semi-autonomous municipal enterprises such as the Nairobi Water and Sewerage Company, and the Sports Stadia Management Board. The jury is still out on the outcomes of both initiatives.

expenditure requirements of these enterprises on a framework determined by the dynamism of social enterprise delivery. Key infrastructure and the funding for it can be vested in an infrastructure trust company within the municipal enterprise with the local authority, the central government and the enterprise entity contributing funds. The trust company would be responsible for ensuring the structural integrity of the infrastructure, ensure localized knowledge of infrastructure management, including knowledge of actual assets, asset utilization and depreciation, asset operation and maintenance, asset accounting, and provisioning for improvement, disposal and new asset creation, etc. Major social enterprise organizations with significant state mandates, such as universities, should also be permitted to establish and run municipal enterprises, including university hospitals, industrial parks, etc.

Establishment through Public Charter

We propose elsewhere that various units of the devolved or decentralized schemes, such as the Constituency Development Committees, be juridically competent organizations and thus capable of setting up organizations with express mandates for various aspects of local economic and community regeneration, such as health, housing, environmental regeneration, etc. That the government has been one of the primary drivers of the establishment of many of the actors in the social economy is often an overlooked fact. The historical development of the not-for profit, non-governmental sector in Kenya points to many instances when government action was the key motivator in the formation of organizations in the sector. The presidential *harambees* for women and youth groups held in the late 1990s were responsible for the establishment of many community-based organizations, majority of which simply shared the proceeds of the *harambee* and wound up. Political involvement with the Maendeleo ya Wanawake since independence, especially from 1970 to 1990, was responsible for the establishment of many district-based affiliates of the organizations.

The question, therefore, arises as to whether the government or its agencies, including local authorities and parliament can legally establish non-governmental not-for-profit organizations. If the answer to this question is in the affirmative, then it begs other questions, including under what circumstances those entities can be established and their independence of the operations of government.

The answer to the question whether or not government can establish non-governmental organizations is in the affirmative. Indeed, we anticipate that were the government to give due recognition to the sector, then it would come to the conclusion that it is advantageous to itself and is duty bound to originate such organizations. What really is the issue is how to ensure the independence of such

organizations and under what terms the proposed authority would decline to give ascent to the registration of such organizations.

For government-formed non-governmental organizations to be registered and incorporated, they would have to satisfy several core criteria:

- Their legal and operational existence is independent of the government
- They should meet one or more of the purposes recognized in the sector
- They are established principally for the benefit of the public
- They fall within the regulatory jurisdiction of the proposed authority
- Once set up, they are self motivating and not dependent for their continuity and life on political or governmental decisions or action, including financing

It is important that 'independence' in the sector should not be misconstrued as control. Independence refers principally to the ability of an entity to pursue its purposes without undue influence or reliance on other entities. Organizations chartered by parliament, such as public universities or hospitals, or by local authorities, such as polytechnics and other educational institutions, health institutions or bodies for the advancement of such purposes are, therefore, eligible for incorporation and registration within the sector. This would entail reworking their statutory instruments to reflect this new status.

Incorporation through a Scheme of the Authority

It will be necessary for the proposed regulatory authority to propose and initiate incorporation of a non-governmental organization on its own leave. There will be instances where, for instance, an existing organization is being wound up, or the purposes for which it was established has been exhausted and fulfilled, yet the organization has significant assets and liabilities. The organization may also have been a recipient of public benefits, including tax advantages and donations on account of its apparent state as a public benefit.

The law would empower the authority to advise or order the affected organization regarding the regularization of its status. Such action would include, but not be limited to, the power to appoint or second directors or officials to the organization. Where the authority in its own wisdom finds that the organizations purposes or assets are best applied to the formation of a new organization, then the authority would have power through its own scheme to organize and charter such an organization, provided that, subsequently, this organization would be independent of the control of the authority.

SECURING OPEN, INDEPENDENT AND PROGRESSIVE REGULATION FOR THE SECTOR

The regulatory environment for the not-for-profit and voluntary sector has been in a state of flux for some time now. The key regulatory agencies for the sector have been the Registrar of Societies, the Registrar of Companies, the NGO Coordination Board, the NGO Council, the Commissioner for Cooperatives, the Provincial Administration and many other less visible agencies. Ongoing proposals to establish a regulator for the SACCOs and micro-finance institutions will also bring another regulatory regime to actors in this sub-sector.

There are many reasons for regulating the sector, including:

- The need to ensure that there is sufficient information to stakeholders and the general public on their activities, health and contribution to society
- The need to ensure that they keep their books and are generally accountable and transparent
- The need to ensure that they actually work in pursuit of stated purposes and objectives
- The need to ensure that there are sufficient governance benchmarks and standards in the sector
- To entrench and protect the interests of stakeholders, including donors and prospective beneficiaries
- The need to prevent beneficiary or institutional capture where not-for-profits that enjoy public resources and goodwill do not exist for the benefit of their founders or are not taken captive by particular classes of beneficiaries/stakeholders
- To prevent corruption
- To promote ethical accountability
- To protect donors' and public funds
- To promote public and stakeholder confidence

While all these are good and genuine reasons for regulation, in truth there is either very little regulation or whatever is there is actually misdirected, such that regulation achieves a policing function. Many actors in the sector fear that regulation will actually mean state harassment and misdirected interference with the sector's independence. That this has happened many times in the past has provided fodder to such fears. Often times, the government gets the objectives of regulation wrong. The expressed interests in regulating the SACCO and MFI sector is not to ensure the vibrancy, efficiencies and prosperity of the sector but

to secure depositors, which can easily be achieved if the financial health of the sector itself is assured.

Similarly, the cooperative movement has recently come under a heavy regulatory regime on account of past practices but which, at the same time, fails to ensure that there are investments and other resources going to the sector. On the other extreme, the Minister of Lands has given the lack of regulatory capacity at his ministry as the key reason for suspending the issuance of certificates of incorporation to trustees.

Regulation presents numerous issues and challenges. How much regulation is desirable? How does one ensure that regulation does not translate into interference with the independence of a sector?

The current approach to a light touch regulatory environment for the sector clearly does not sit well with the enormous challenges of governance and relevance within the sector, neither does it conform to the need to establish a requisite level of trust and confidence in the sector. We propose elsewhere that the state and government makes specific provision to ensure that sufficient domestic resources are directed towards the sector to secure its financial and institutional viability. We also propose that the role and potential of the sector to deliver key public goods such as healthcare, education, leisure, amateur sports, research and technology transfer, financial intermediary and investment in financially-excluded communities, care for the old and terminally ill, regeneration, environmental sustainability, etc be recognized and provisioned for in the governments' dealing with the sector. In the light of these, it is crucial that the current regulatory regime be brought to conform with these raised expectations and responsibilities.

National Not-for-Profit Non-Governmental Organizations Authority

It will be necessary to pass legislation to enable a more robust and dynamic regulatory environment for the sector. This can be achieved through amendments in the principal NGO Coordination Act and various other laws to establish a single regulatory authority for the public benefit not-for-profit sector, perhaps through a National Not-for-Profit Non-Governmental Organizations Authority.

The policy and strategic objectives of these amendments, to be set out in statute, should be made with a view to:

- Increasing public confidence in the sector, and enhancing broad accountabilities in the sector,
- Ensuring compliance with applicable tenets and ethos of not-for-profit non-governmental organizations,

- Establishing an appeals tribunal for actors in the sector, and
- Promoting the not-for-profit sector to achieve and maximize its economic potential, i.e. to drive the social economy.

The amendments are also designed to:

- Ensure the emergence of not-for-profit organizations as a special asset class working honestly and altruistically in the public benefit,
- Promote a regulatory environment that positions this asset class as a safe destination of choice for tax relief and investment and donor finance,
- Promote the qualifying sub-sectors of this asset class, such as social enterprises and provident societies as safe and secure destinations for public benefit spirited investments,
- Secure independent, predictable and open regulation for the sector,
- Maximize accountability of the sector to the public, to beneficiaries, stakeholders, donors, etc and
- Ensure an excellent brand for all the sub-categories in the sector.

New Registrars for Not-for-Profits

It will be necessary to amend other relevant laws, such as the Trustees and Perpetual Succession Act, the Societies Act, the Companies Act, and other statute as may be appropriate with a view to easing incorporation in the sector. This study proposes establishment of registrar/regulator for:

- Trusts/charities, to be brought under the oversight of the Attorney Generals Office and with sufficient scope and authority to ensure the good health of charities
- The proposed Community Benefit Company under the Registrar of Companies
- The Community Benefit Organization and the Charitable Incorporated Organization under the Trustees Act
- Community Benefit Societies under the Societies Act
- Community Land Trusts under the proposed Community Benefit Asset Endowment Authority

All these registrars would share reporting and duty of care responsibility with the proposed apex regulatory authority in the not-for-profits non-governmental sector.

Without seeking to duplicate resources and functions, the not-for-profit authority should have powers to summon witness and evidence in relation to the work of these regulatory authorities, assist with ensuring that sufficient information is available on the overall health of the sector and various sub-sectors, and carry out and prepare reviews to the sectors. All the registrars and the proposed authority should be independent from day to day political interference and should have organizational status that enables them statutory independence with sufficient stakeholder participation. The functions of these offices should be widely available, at least in each local economic and community development zone.

The proposed authority will need sufficient powers and appropriate functions. This study proposes that the proposed authority:

- Have overall responsibility for registration of organizations in the sector
- Preclude very small and un-incorporated organizations in monitoring the affairs or organizations in the sector
- Be provided with technical assistance on legal, administrative, governance, etc to help the sector run better
- Be given investigate powers for corruption, misconduct, etc
- Be the sole custodian of the register of public benefit not-for-profit organizations, regardless of their form of incorporation and registration. Only organizations appearing under this register should be entitled to privileged tax and other state treatment on account of this status
- Be given powers of certification, and that certification be sufficient proof of the registration and legal status of the organization as a not-for-profit working in the public benefit
- Publishes on electronic format and through annual year books and other periodicals information on the sector
- Be a veritable knowledge and data clearing house on the sector. Such knowledge and data bank should be such that it provides the public, government, stakeholders, etc with sufficient up to date information on the economic, social, cultural, political, environmental contribution, activities and impact of the sector on society. The authority should also be able to provide stakeholders with a sufficiently detailed view of the size and scope of the sector within a particular jurisdiction.

Service performance contract

To safeguard operational efficiency of the regulator, this study proposes the entrenchment in statute that the Minister in charge designs a Service Delivery Contract with the authority, which should be the subject of public oversight hearing by an appropriate parliamentary committee. Upon passage by Parliament, this contract should become binding on the authority with respect to its conduct of affairs for the subsequent specified period.

This contract should set performance targets, which should be helpful in establishing indicators of performance for the authority. In setting the targets, the Minister and the respective parliamentary committee should carry out extensive consultations with the commissioners to the authority and stakeholders in the sector. The commissioners can invite own independent review of the draft performance targets and present the outcome of the review to the committee before it makes its decisions. The commissioners' review should also be provided to members of parliament for informed debate when the matter comes before parliament. The regulatory authority, in consultation with stakeholders, can also raise the minimum thresholds set in the performance schedule should it establish that this is called for.

Accountability

The regulator should be accountable to parliament through the respective government minister. It should publish an annual report, which the minister should lay before parliament with independent comment. Parliament can decide to call the authority to respond to queries or issues raised by the minister with regard to its performance and the state of the sector.

The respective parliamentary committee should also conduct periodic inspection and oversight hearings at which the constituents of the authority can place petitions, evidence and pleadings. The authority's accounts should be subject to the authority of the Controller and Auditor General. The authority should also carry out an independent evaluation of its efficiencies and systems for presentation to the parliamentary committee.

Without compromise to its budget and work, the authority should also facilitate, including providing financial assistance, to parallel independent stakeholder reports on its work to accompany its official annual reports.

Independence

The proposed authority should be a corporate body able to set up its own corporate, operational and administrative procedures, strategic plans, etc. To

secure the independence of the regulator, and by extension actors in the social economy:

- The authority should be independent of political interference and that of the sector itself
- The decision of the authority's appeals tribunal can be overturned only by a competent court—the High Court
- No politician should have the power to direct or change any of the authority's decisions
- Commissioners to the authority, once appointed by parliament, should have security of tenure for five years and should only be removed following an independent judicial inquiry called at the request of the president
- The authority should be an effective voice on the status of the sector, and should be available to the sector in promoting issues within it to both parliament and government. Its voice should, however, be independent of the sector, be balanced and objective
- The authority should be able to conduct hearings on the sector regarding proposed legislation, policy, programming, financing, etc including that as may be contained in independent parliamentary action, government budgets and proposals, fiscal and other economic policies and plans, etc
- The authority should have the power to request for a parliamentary oversight hearing on an issue or issues it deems to be important to the sector

Openness and transparency

The authority has to be able to generate and command high esteem and confidence in the public and the sector, especially given that the ability of the sector to take up its role in the economy and society is pegged, to a great extent, on the quality of the regulator.

In the past, the decision making process of the various regulators has been mirred with official secrecy, have been inconsistent, and sometimes contradictory. To ensure openness and transparency:

- The authority's decisions should be public record, available on electronic format for all to read
- Its decisions should have the power of precedence and can be reviewed only by the tribunal and the courts
- The authority should publish guidance on all matters that are likely to come before it

- The authority should conduct internal reviews of its decisions whenever the decisions are challenged and these reviews and their outcomes should be conducted in public
- The authority's board meetings should be open, very much like a parliamentary committee would, to members of the public except where board business is reserved, such as when dealing with personnel, strategic plans, etc of the organization
- These board meetings should include a question and answer session with the public

Public profiling

In its conduct of business, the authority should seek to address the entire spectrum of its putative constituency and the general public. It would be an error to assume that only those intimately involved in the sector need information or services from the authority. A good measure of the future economic out-turns and the ability of Kenyan society to achieve key national goals will depend on the performance of the sector. Achieving confidence in the sector will require that the public is kept informed on its performance and potential.

To secure effective public profiling:

- The authority should carry out authoritative and independent reviews on key aspects of the sector, including but not limited to governance, financing and capitalization, workforce and skill development, technological adaptation, regulation, etc.
- The authority should also be able to offer authoritative information about actors in the sector, including NGOs, CBCs, CBOs, charities, etc. All organizations in the sector should be required to file any material changes in their operations, such as elections of new boards, change of chief officers, change of official seat, etc to the authority. Similarly, organizations that seek to change their purposes and objects and receive the authority to do so from their regulators, or where this is not necessary proceed to effect changes in their objects should notify the authority of such changes. The authority should have the power to call for and receive evidence on the change of purposes if, in its opinion, this constitutes grounds for an infringement on the status of the organization.
- The authority should also be able to carry out compliance reviews and have powers to recommend and enforce remedial measures it deems appropriate. Such measures can include appointing key officials to the organization, appointment of directors, suspension of directors, freezing of an organization's bank accounts, applying a caveat on the sale or transfer

of an organizations assets and, in extreme circumstances, recommending and enforcing the winding up of an organization.

Gate keeping role of the authority

The authority will be required to register any organization as a non-governmental not-for-profit. In the past, a lot of questions have been raised on the 'gate keeping' function of the NGO Coordination Board, the Registrar of Societies, the Provincial Administration and the Minister of Lands regarding registration of not-for-profit non-governmental organizations. The NGO Board, for instance, requires that all applicants be vetted by the national security agency before they can be registered by the Board. The Minister of Lands has on various occasions recently refused to recognize the right of trustees to various non-governmental charities to incorporation.

Even in the absence of such obvious policing, registration has often required that organizations provide a range of information about their intended purposes and activities before registration, including a one year budget forecast for NGOs. This procedure invites several shortcomings, including the fact that:

- It mars the right of non-governmental organizations to registration and incorporation regardless of their obvious prospects
- The registrar unfairly applies criteria that is clearly biased against start up organizations in the sector
- The registrar confers upon itself a security role for which it was not intended in law

The authority is clearly entitled to a gate-keeping function. One of its functions and strategic objectives will be to ensure and secure the good health of the sector. This cannot be achieved without clearly benchmarking basic standards of conduct, governance, financial management, etc for the sector. As the final authority outside the courts on the not-for-profit non-governmental status of an organization, the authority has a duty of care or due diligence role and should legally be entitled to ascertain that a prospective organization qualifies for that status. It can not do this without an effective gate-keeping function.

Elsewhere in this study, we make proposals to the effect that certain types of prospective or aspiring organizations will be required to meet or pass a test of public benefit, social or community benefit to be eligible for registration and recognition for purposes of benefits accruing to the status. Again, this cannot be done without requiring information about an organizations intended or continuing activities beforehand.

In large part, criticism and the crisis of confidence obtaining in the sector has been as a result of poor governance, corruption, embezzlement, ghost and briefcase organizations and unmatched inefficiencies. These cannot be eliminated if the authority cannot require demonstration of adherence to standards in the sector. If this cannot be done, public faith in the sector would wane and the sector and its potential contribution to society and the economy would continue to suffer.

To insure against abuse of the gate-keeping function of the authority, this study proposes that:

- The authority be given responsibility for registering not-for-profit non-governmental organizations.
- Having decided to recognize an organization as a not-for-profit non-governmental organization, the authority should also be within its rights to make enquiries about its viability or the quality of its governance, financial management, etc. This should be the case even where the organization is incorporated under law that specifies such governance or management arrangements. The authority should be able to pursue these concerns with a view to helping the suspect organization move up the benchmark standards.
- To ensure proportionate considerations and application of procedure, provision should be made for organizations to seek a certificate of exemption from the authority. The effect of this certificate should not be to put the organization beyond the regulatory authority of the authority. The certificate of exemption should be issued with conditions, subject to periodic review, and can be recalled by the authority in which case the authority would recommend the measures it deems necessary to safeguard the purposes, assets and liabilities of the organization. Such certificates may be issued to extremely small organizations, which may need some time to rise above certain benchmark standards or to organizations incorporated under laws that confer a burden of regulation similar to the authority's.
- The authority and all subordinated registrars should be purged off security and other extraneous policing functions or behaviour.
- The authority must also separate the capacity building/confidence-building function from the right of organizations to incorporate and register with the sector so that, regardless of any provision to the contrary, any organization that seeks registration gets it in lieu of other considerations.

Financial Accounting and Auditing in the Sector

In the past, the auditing function of regulators in the sector has been limited, in most cases, to annual returns to the respective registrar. There, however, has been little effort to effectively audit the sector, or even verify the truth or veracity of the returns.

Auditing is important for many reasons. With the growth of the sector, the risk of harm to society and the economy generally and to specific stakeholders and beneficiaries is great if proper financial standards are not set and followed. It is also difficult to determine the scope, nature and size and contribution of the sector to society and the economy if the veracity of its records cannot be ascertained.

To secure adequate financial accounting and auditing in the sector, this study proposes that:

- The authority has a statutory power to require financial, social environmental and other reporting audits of all organizations in the sector. Where such reporting is not required by other law, such as the Companies Act, the statute should require that the organizations carry out and file equivalent or authority-benchmarked audits to the regulator.
- The authority sets audit thresholds in the sector depending on the size of the organization, based on income, for instance. Returns based on a certain minimum threshold should be made by filing of returns by the officials. Any returns above this threshold should be issued by a legally and professionally qualified person.
- As far as is possible, all legislation relating to incorporation in the sector, such as the Companies Act, should make it mandatory for organizations to professionally audit their financial returns.
- It should become a criminal offence for officials or directors to file returns that are false regardless of whether they knew them to be so. This should make it the duty of the professional auditor to assent to such accounts.
- The authority, in consultation with stakeholders and professional associations, should set and publish respective auditing standards.
- The authority may accept at face value the audits by professionals but can also carry out own inquiry following certain trigger events or circumstance.
- The authority can bar professional audit firms or individuals from carrying out work in the sector if investigations identify culpability or professional negligence.

Advisory and Support

The authority should have a clear advisory and support function to be distinguished from its regulatory function, to assist the sector with legal, accountability, governance, administrative and other issues. Activities under this function can be delegated or licensed to other actors, including professional bodies, tertiary institutions or other commission-authored or sanctioned schemes with a view to continuously modernizing and updating good practice in the sector. The authority should, however, be required by legislation to maintain plain and rigid boundaries between the two functions, with the advisory function being contracted as suggested and with much of the cost being met by other actors in the sector.

Enforcement

Presently and in the past, regulatory authorities have had very little scope to enforce their decisions and standards on the sector. Where 'enforcement' has occurred, this has been at the behest of political and other interests and has often meant the most drastic action—deregistration. Enforcement is, therefore, met with a lot of apprehension and suspicion in the sector.

The justification for the authority to have enforcement powers can be made on many grounds. Perhaps the most compelling includes the enormity of public funds entrusted to the sector, the enormous expectations on the sector in terms of helping society meet its goals and aspirations, the necessity to ensure that the sector grows in tandem with demands placed on it by society and, quite basically, the need to enforce applicable law.

We propose that the authority will:

- Have statutory power to enforce its decisions in carrying out its mandate
- Have an embedded independent tribunal within its operations to arbitrate on matters in the sector and with authority to review and overturn a decision of the authority. Unless presented to the tribunal, the authority's decision can only be challenged at the High Court. The authority is also at liberty to challenge a decision of the tribunal at the High Court.
- Seek to interrogate and investigate any existing or prospective organization aspiring for registration or active as an entity in the sector.
- Seek to protect the assets and purposes of not-for-profit and non-governmental organizations from abuse, so that assets are actually used for the purposes intended and in public/community/social benefit.

- Protect assets of not-for-profits, especially at the risk of misappropriation, dissolution etc.
- Be empowered to take appropriate action, including recommending and instituting prosecution for those responsible for mismanaging not-for-profit organizations where this can be shown to have been deliberate and fraudulent.

Persons responsible for fraudulent or other misdemeanor with respect to the assets of such organizations should, by law, be held personally liable. The law should borrow, as appropriate, from that of the Capital Markets Authority with regard to types of offences and deterrent actions.

Value Adding to the Sector

One of the strategic objectives of the authority relates to helping the sector realize its economic, social, cultural, and scientific and other benefits to society. Nothing in the current practice or remit of regulation equates to this role. There is also no available data or evidence of the actual impact of the sector on society and national life.

The authority should be required in law to audit the performance of the sector in terms of its variegated contribution to communities, society and national life. The reports issued should be helpful to the general public and to the various interest communities in the sector. The purpose of the reports, unless this is the remit of an official inquiry by the authority, should not be or lead it to interfere in the operations of a specific organization or sector or to actively motivate the specific development of a particular sub-sector. The reports anticipated here should be aimed at enhancing knowledge of the sector, and be helpful to actors and the public to engage in informed debate and decisions. Nothing in this proposal should be read to mean that the authority can not carry out extensive studies and make recommendations on the health of particular sub-sectors or the social economy as a whole.

Financing the Authority

The current practice in financing respective regulators in the sector is that they are publicly funded. The government, however, seeks to recover the cost of the regulation by charging various fees to those seeking these services. This has its merits and limitations. One of the key limitations is that regulators in the sector have no dedicated sources or assurance of finance. They cannot draw programmes, cannot draw up budgets, etc. There is also failure to recognize the sector as needing specialized expertise. No effort has been made to ensure that such expertise is developed and available in the sector. Some of the fees charged

in the sector are also too high and designed to prohibit financially-weak startup organizations from seeking registration.

It will be necessary to secure and ensure independent sources of finance for the regulator. To achieve this, and given the primary role of the sector in society, the authority, and through it the various registrars in the sector, should secure finance through a direct charge to the Consolidated Fund fixed at 0.5 percent of the revenue collected by the Kenya Revenue Authority the preceding year. We also propose that only 50 percent of this money can be used for recurrent, administrative and management costs at the authority, with the rest going to fortify activities in its core functions and to capacity building programmes in the sector.

The authority and regulators should be at liberty to set and levy fees for their advisory and other services, including levying administrative fees to organizations in the sector relative to the cost of the service. The authority should also be required to set up, with income from other activities, an own purposes endowment scheme seeking to match resource from the Consolidated Fund. The targets and uses can be set periodically through public hearings and regulatory oversight with parliament.

Authority to draw plans and report

The authority should be required to draw five year strategic and three year operational plans, which should be subjected to public consultations and a parliamentary oversight hearing. The authority to spend resources should then be subject to these plans, which should be approved by the parliamentary oversight committee.

The authority should also be required by law to offer programme-related grants and investments to infrastructure organizations—discussed in subsequent proposals—in the sector for purposes of capacity building.

The authority should also account to parliament for its expenditures and resources through an annual report. The financial report should be an independent component of its annual report. The respective Minister should be required to draw up a response to its report for consideration by respective stakeholders and presentation to the respective oversight committee. The authority should respond to the reports of the Minister, stakeholders and the committee.

Composition and Structure of the Authority

It will be necessary to set up an appropriate institutional structure for the authority. The following may be considered:

- A board of between 7-9 commissioners
- Composition of the commissioners to comprise a mix of social scientists, philanthropists, clergy, legal minds, and academics
- Commissioners should have demonstrable interest and competence in the sector and demonstrate expertise in key areas relating to development
- Commissioners to reflect gender and other diversity
- Commissioners to be proposed by industry and forwarded to the parliamentary committee by the respective minister
- No government functionally or civil servant should sit on the authority
- Specific registrars should join the board in ex-official capacity
- Directors of key divisions such as finance, information technology, communications, resource mobilization, and human resource should join the board in ex-official capacity if and when required
- The executive director should be an ex-official board member, and head of secretariat
- Commission to recruit the executive director and send nominees for parliamentary oversight vetting
- Commissioners to hire other directors and registrars in the sector
- Authority to have grassroots offices in the proposed regional development structures

Right of Independent Appeal Against the Decision of Commissioners

Presently, regulation in the sector lacks a systemic and credible complaint and review system. There is, therefore, no avenue for individuals and organizations dissatisfied with the decisions of respective regulators to lodge formal complaints against them outside the court process. Owing to many reasons, not least the lack of faith in the court process and the long and tedious nature of litigation, very few people or organizations actually seek recourse to the courts for a hearing relating to their dealings with the regulators.

Without any appropriate checks on the commissioners, considerable bureaucratic ineptitude, an engrained political patronage system and the force of habit, regulators operate without any regard to the due care, fairness and justice

that must accompany their decisions. Cases of outright arbitrary action by regulators without sufficient recourse to independent review are legion. As a result of this, many organizations seek to operate along the lines of least resistance in matters relating to regulation.

The objective need for an independent appeal mechanism exists on several other grounds. Granted the increased powers and autonomy proposed for the authority, there may be need for an independent review of the decisions made by the authority. There will also be instances when individuals and beneficiaries likely to be affected by the decisions of the authority will want to challenge it. It is also conceivable that entire sub-sectors, categories or associated organizations may be affected by a decision of the authority. It is also necessary that the decisions of the authority assume the power of precedence for the sector and that it works to develop and evolve a tradition of case work from which the sector can master the resources for predictable self-regulation and practice.

In the light of these arguments, it will be necessary that:

- The law creates an independent appeal tribunal to hear complaints against the decisions of the authority's commissioners. Persons affected or likely to be affected by such decisions have a right of review, first with the commissioners for pre-emptive review, and with the tribunal for decisions made, or to require that the commissioners conduct a pre-emptive review.
- Appeals against the decision of the tribunal should go straight to the High Court.
- The tribunal board should comprise sufficient legal and technical experts and a few lay persons.
- Members of the tribunal are institutionally-ranked at the level of the commissioners.
- The tribunal be accorded a small secretariat and commensurate resources headed by a principal or clerk within the main establishment of the authority.
- The clerk the tribunal be appointed by the tribunal members on the nomination of the commissioners.
- The rank for the clerk be institutionally equivalent to deputy director of the authority.
- Members of the tribunal be short-listed by the Attorney General for presentation to the president, but whose decision to appoint them will be subject to a regulatory oversight hearing by parliament.
- The appeals tribunal be made up of between three and five members appointed by the president with the recommendation of parliament and

who should be qualified to be appointed judges of the High Court. With the exception of the clerk, the others members should not be permanent employees of the authority but should draw allowances and pay depending on the schedule of work.

Regulators of other entities such as private universities and hospitals and public institutions vested with a not-for-profit non-governmental status should be required by law to impose regulatory oversight of the authority on these institutions and to audit compliance of these organizations with authority rules even where such institutions have been exempted from registration with the authority. This, in essence, means that the entire not-for-profit non-governmental sector falls under one apex regulatory regime in accounting for their status as not-for-profits and non-governmental organizations. A university or tertiary health institution established as a not-for-profit non-governmental organization will, therefore, apply the standards of public benefit and social accountability as established by the statute and the rules of the authority. The authority can also exercise other supervisory functions set up in statute and its rules.

SECTORAL INFRASTRUCTURE

Active Institutional and Infrastrcutural Support

There is no denying that the not-for-profit non-governmental sector, which we have referred to as the social economy, has played a key part in Kenya's political, economic, social and other life. It is inconceivable today, for instance, to imagine that we can overcome the challenges brought by HIV/AIDS without the much derided Community-Based Organizations. It is also true, however, that this sector has survived and grown without the active institutional and infrastructural support by either the government or by the state. It is unlikely that the sector can achieve its full potential and take up its rightful place in aiding development without such support. Yet, given the high level of independence proposed for the sector, it is instructive that such support should not compromise the envisaged sector-wide and institutional autonomy.

Industry voices and bodies are desirable and important for many reasons. They are essential for pushing standards in the sector, voluntary compliance and self regulation in relation to applicable law, driving new thinking and innovation and ensuring rapid diffusion of such new thinking and innovation. They also provide the much needed advocacy avenues and platforms for the sector and are instrumental in nurturing leadership and talent.

Perhaps the most obvious is that numerous actors in the sector need very active support to help them meet their objectives. Many institutions in the sector are started by individuals who have limited skill, knowledge and experience of what it will take to grow the organization to successfully address its core purposes. Many of these organizations are founded with limited financial and other resources and majority fold up within the first year of their existence. Ironically, Kenya has continued to produce highly trained human resources. Quite apart from the sectors' many other benefits to society, with adequate workforce development strategies for the sector, there exists great potential to turn this into a reliable employment avenue.

In order to make the vision of a vibrant and growing social economy possible, investment in sector-wide infrastructure organizations providing high quality and sustainable support at community, regional and national levels is necessary. The diversity and geographical spread of the sector also demands support infrastructure to meet both the generalist and specialty development needs of actors in the sector at the various levels. Such support should also be integrated with public and private institutions, especially the universities and other tertiary training institutions. Different infrastructure organizations will, therefore, be needed and at different levels. At the outset, infrastructure organizations should

help institutions in the social sector meet the following strategic needs and objectives:

- Providing capacity building support, including resource mobilization, at organizational level
- Providing a voice in policy making and public discourse for various sub-sectors in the social economy
- Enabling joining up of objects, programmes, energies and other resources across the various sub-sectors in the social economy
- Providing physical infrastructure for local, regional and national platform formations
- Providing generic support for entities within a particular geographical community
- Providing specialist support for entities serving specific communities of interest

All these and other functions not described here are essential for the good health, viability and growth of the sector. Almost all not-for-profit non-governmental organizations, regardless of their size or specialization, need advice and assistance to nurture and sustain their range of activities, services and purposes. Many of them require effective mechanisms through which they can enter into dialogue with other sectors of society without straining their limited and fragile resource base. Many people who venture in the sector, whom we have called social entrepreneurs, are overwhelmed by the levels of professionalism, the legal complexity, accountability and paucity of resources and goodwill they face in their efforts.

Operators in the sector need continuing capacity building to guarantee that they have the skill and knowledge base and the organizational structures and resources necessary to live out their desired potential. Many of the support services we have come to expect of small and micro enterprises are actually much needed by not-for-profits at all levels. The special character of the sector, the very fact that it is not-for-profit, however, imposes distinctive characteristics that command specialty support infrastructure. This is evident, for instance, by the lack of distinction within the Association of Micro-Finance Institutions between not-for-profit micro-finance institutions and those that are driven to lend to micro enterprises by the desire for profit.[164] Consequently, the sector has evolved a law that confers similar legal status to these very different types of

[164] The Bill now enacted into law was apparently blind to this fundamental distinction and imposes 'mainstream' and exclusively private sector criteria in regulating the sector.

organizations. Beyond this, organizations in the sector need the kind of support that helps them conserve their energies and direct it to core purposes. The following kind of capacity building support is discernible in the sector:

- Start-up, expansion, re-visioning, etc
- Networking and building linkages to drive partnerships with other actors in a particular sector in the social economy as well as with other actors in the public and private sectors
- Representation to present a coherent and accountable vehicle for actors in a particular sub-sector or region
- Information, advice and technical assistance, especially related to best practices, new/unfolding developments in a sector, resource raising opportunity, institutional development and management, communication technologies, personnel, volunteer and board recruitment, etc
- Policy research—collecting the evidence needed to push issues relating to the sector as well as the purposes served by the sector in the public arena
- Advocacy around core purposes and proposed or desired public policy
- Driving social and ethical accountability in the sector

The consolidation and maturation of the sector has also seen the emergence of specialist infrastructure organizations bringing together actors in a particular sub-sector, such as juvenile justice, women's rights, youth, persons with disability, etc. Granted the skewed development of the sector, which has been driven not only by objective conditions but also donor conditionality, majority of these organizations are in the so called civil society sector. There is need to ensure that infrastructure organizations are available for actors in the entire sector.

Specialist organizations will be important in setting and reinforcing standards and promoting evidence-based best practice. Specialist infrastructure organizations would also be expected to secure the financial, resource and organizational gifting of a particular sub-sector.

In this latter framework, specialist infrastructure organizations are needed in many areas, including resource mobilization for specific actors in a sub- sector, resource mobilization for sector-wide actors in a particular geographical location or community of interest, organizations to drive application of ICTs across the entire sector and sub-sectors, drive volunteerism, secure the start up and viability of diverse purpose organizations in underserved communities, secure the growth and vibrancy of specialized sub-sectors such as social enterprise, social investing, social and ethical accounting and auditing, socially-responsive local economic and community development or regeneration, etc.

Infrastructure Delivery Levels

We have proposed elsewhere in this study that various aspects of laws relating to regional development be amended to allow for the establishment of genuine and independent infrastructure to drive socially-inclusive local economic and community regeneration. Specifically, we have proposed the establishment of about 21 Regional Development Agencies and 60 Local Economic and Community Development Zones, each comprising several counties. We have also called for an apex authority responsible for monitoring and driving the performance of the proposed Regional Development Agencies.

Following these proposals, it will be necessary to ensure that infrastructure organizations serving actors in the social economy mirror the various proposed structures in the new local economic and community development regime. In this formulation, there will be national infrastructure institutions, regional infrastructure institutions, zonal/sub-regional infrastructure institutions and infrastructure institutions active at county and community levels. Some of these organizations will emerge through the envisaged Local Community Benefit Development Organizations, the Community Development Finance Institutions, and others. Others will be set up with specific purposes, such as driving volunteerism in a particular region, or driving accountability in the sector for a particular region. National organizations such as the National Council of NGOs will continue to be in vogue.

Infrastructure organizations can also be sectoral, with apex organizations as is currently the case with the Association for Micro-Finance Institutions.

Pushing Forward Infrastructure Organizations and Governance in the Sector

Since the onset of regulation in the NGO sector, the law has expected the National Council of NGOs to drive key developments in the sector, including governance and accountability. Granted the strategic role of this organization, one would expect it to be exemplary in good governance, and promoting values and practices that are central to the good heath of the sector.

Recently and historically, however, the industry has been plagued with deep-rooted governance and accountability problems, which have resulted from the very legal structure of the sector and, in part, owing to rent-seeking behaviour in the sector. At its best, the NGO Council also served to secure the regulatory capture of the sector by the NGOs themselves, such that the development of regulation in the sector has indeed stalled and is counter-productive. It is also clearly the case that the NGO Council is actually not representative of all the sub-sectors in the social economy. Conceived essentially as a vanguard against the possible tyranny of the state-directed NGO Coordination Board, with

increased democratic space and prospects of a new constitutional dispensation that guarantees fundamental rights and freedoms, it may be the case that the very idea of the Council needs a serious rethink.

We propose that the law requires the authority to set up objective benchmarks, minimum standards of performance and best practice applicable specifically to infrastructure organizations and which should be enshrined in their proposed charter. The requirement for comprehensive performance management will require adherence to performance indicators and long term capacity development as part of the regulatory review of infrastructure organizations. These benchmarks and standards will be subject to thorough public review and consultation before they can be published and become effective. The point here is to subject infrastructure organizations to a rigorous accountability and performance regime that best secures their ability to serve the interests of the sector as a whole.

Financing Infrastructure Development

This study makes elaborate proposals for financing the social sector and connecting devolved or sub-sovereign finance schemes and financial capital to aid socially-responsive local economic development. Most of the proposals with regard to financing will apply for infrastructure organizations. In view of the specialized role of infrastructure organizations, however, it is instructive that dedicated financing for their core purposes be established from some secure source.

The study has proposed that the apex regulatory authority for the sector be financed by a direct charge to the Consolidated Fund set in statute at 0.5 percent of the total Kenya Revenue Authority collection for the year, and that no more than 40 percent of the funds realized be actually utilized for the purposes of meeting the costs of the authority. The remainder 60 percent should be set aside in statute to aid the strategic development of the sector, including financing the core costs of chartered infrastructure institutions.

In a scenario where the Kenya Revenue Authority collected Ksh 300 billion in a particular year, the total charge to the Consolidated Fund would be Ksh 3 billion of which Ksh 1.2 billion would be available to the proposed authority and Ksh 1.8 billion for qualifying strategic development in the sector. Since the authority would have a physical presence at the national, regional and zonal levels, this would require an administrative bureaucracy in at least 40 sites. It is, therefore, conceivable that such a distribution of income would be adequate for the authority's purposes. The authority should be responsible for generating the strategic budget for the sector, which should be done through adequate open consultations with the sector and be subject to parliamentary oversight.

Not-for-Profit Authority to Charter/Accredit Industry Bodies/Voices

Presently, the law has only established one industry voice, the National Council of NGOs, for the sector. While the NGO Board may have escaped constituency capture by NGOs, the same cannot be said of the Council. The NGO Coordination Board is potentially at risk of such capture by NGOs should the Council be a strong and coherent institutional vehicle.

The proposed authority should be empowered by law to charter, license or accredit various stakeholder and industry bodies or associations that provide infrastructure to either the whole sector or sub-sectors. This will ensure that the industry assumes robust self-regulation; that there is a mechanism for providing infrastructure support to the sector, including education and workforce development; and that the sector is competitive and lives to the aspirations of being among the best anywhere. We have in mind such likely institutes, bodies or associations such as an Association for Grant Makers, Association for Chief Executives of Social Enterprise Companies, Association of Chief Executives of Community Development Finance Institutions, Institute for Development Executives, Institute for Fundraisers, Institute for Community Development Finance, etc.

While actors and members in the sector would naturally be expected to drive the membership bodies especially in terms of financing, the proposed law would acknowledge a duty of the authority to provide grant and other financing to these bodies, provided that this does not compromise their independence from it and does not generate dependency.

An Institute for Small and Voluntary Not-for-Profit Organizations

At present, voluntary not-for-profit activity at community level is taken up largely by community-based organizations, qualifying cooperative societies, welfare societies, etc. We have made proposals elsewhere for the mainstreaming and modernization of the legal forms for these organizations. It is, however, essential to ensure the mainstreaming of these organizations within the dominant discourse in the sector. The question also arises of the wisdom and merits of regulating the small operators and how to ensure that regulation is also beneficial, other than burdensome, to them.

Recognition and regulation will be vital and mandatory if actors at all levels are to benefit from state resources. It will also be vital for the actors own fundraising and enterprise efforts, including possible contracting by local governments, community development corporations and the community development finance sector. Moreover, recognition and the high profile branding

that will come with the new regulator will be essential for grassroots organizations who desire to operate independently of possible actions by local governments.

It is also clear that the aims of the legislation—to prosper communities—will not succeed without the growth and vibrancy of grassroot community organizations. These organizations and the values they represent at community level are essential to the success of social inclusion. The authority should charter, by its own initiative and after sufficient regulatory impact assessment, an institute or academy for small voluntary and not-for-profit organizations to ensure that there is sufficient infrastructure to provide support to small and start-up organizations within the sector. The authority will also be required by law to audit its own impact on communities and the sector with appropriate and adequate input from grassroots community organizations.

An Institute for Development Education

Development education is a key prerequisite for development. Unfortunately, this is one of the most ignored aspects of Kenya's development effort. While, for instance, the government has produced five year development plans without fail since independence, there has never been any meaningful debate on what development really means for our purposes. Not surprisingly, there has never really been any systematic effort to evaluate the outcome of the development plans, whether others are needed and what direction they should take. The central role of government in issuing those plans also meant that development planning was effectively perceived as the domain of and left to government.

Until recently, with the historic consultative process leading to the Poverty Reduction Strategy Paper in 2001, the government never bothered to incorporate the views and priorities of any other sector or citizens in development planning. In the 1970s, almost by historical accident, the Catholic Church through its diocesan development programme began the pioneer development education programme in Kenya. The programme adopted a pedagogy based on the Paul Frere and Latin American Conscietization Movement. Soon, Catholic lay faithful began to question the acts of their clergy and their position in the church hierarchy. The programme also came to the attention of the provincial education, with the government considering it as verging on the subversive. A series of actions were initiated to effectively kill the programme, with its chief architects, including especially Anne Hope and Sally Timmel, being forced out of the country.

While there will always be argument on the aims, contents and methods of development education, it is not the intention of this study or intended legislation to define what this actually is, merely to say that it is important and must be recognized as one of the instruments that will ensure that citizens are equipped

and competent to enter discourses on the future of the country and the direction of national and local policy and plans.

Local economic and community regeneration cannot happen in a vacuum and, for it to work, it needs to be locally owned and driven. In a democratic society, such ownership must be as broad-based as possible. Given the central role of public opinion and those who shape and purvey it, including leadership across the breadth of society and the media, a certain minimum of development education will be crucial to ensuring that we approach the debate with the level of sophistication that guarantees that society is richer for it. Our own history since independence points to the continuing need for a kind of education for development relevant to our own circumstances, and that speaks to our realities, experiences and aspirations as a people. There is clearly a need to ensure that citizens are fully aware of the place of the environment in our activities, the human rights conditions of all our people, the need to engrain awareness about peace and mutual understanding as prerequisites for a national community, the foundations and health of our democratic processes, the real and lasting consequences of state policies and plans, including a genuine concern for social justice, cultural and other diversity, globalization and our place in the regional, African and global community.

We propose that the authority charters, by its own initiative, an Institute for Development Education whose work will be to conduct research, draw up a body of knowledge, curriculum, materials etc in the entire spectrum of development education, and to accredit training programmes and trainers in development education.

An Institute for Gender, Social Inclusion and Development

Gender awareness, analysis and mainstreaming as well as social exclusion and local economic re-engineering have become dominant perspectives in planning and implementing development interventions and organizational competences. While there has been a lot of work to ensure that these perspectives are understood, there has not been a mainstream or state effort to ensure that these efforts are coordinated or can be sustained. Given the primacy of the concepts in the entire development interventions proposed in this study, and the centrality of the gender and social exclusion problematic in Kenya's development experience, the authority should, in addition to an Institute for Development Education, charter by its own initiative an Institute for Gender, Social Exclusion and Development. This institute would carry out capacity building work, conduct research, draw up a body of knowledge, curriculum, materials etc in the entire spectrum of its core fields. It would also accredit training programmes and training providers in gender, social exclusion and development. The Institute

would work in concert with others to ensure that their curriculum meets minimum requirements in its core fields.

Institutes for the Promotion of the Social Economy

The Institute for the Promotion of the Social Economy would be instrumental in moving innovation and change in the various areas and fields of the social economy through research, capacity building, policy and legislation and advocacy. Likely areas of focus could include governance, the enterprise model, delivering on mission and purposes, membership, targeting, product and service delivery, etc.

Prohibition Against Competition with Base Membership

It is important that infrastructure organizations be barred from competing with their membership, usually those primary organizations offering 'front-line' services in a particular sub-sector, such as a community hospital. Conversion of infrastructure organizations to offer 'front line' services will defeat the very aim of establishing them and cause considerable friction and duplication. To avoid this, it is important that these organizations are enabled to meet their overhead costs, secure stable and predictable sources of finance, and nurture capacities that enable them to plan and operate from the longer term.

Securing Trust and Accountability

To secure the new brands and enable an enduring, respected, vibrant and socially-relevant sector, the statute should set up a new social accounting and auditing standard/framework for state enterprises, social and community enterprise and the private and public sector and a national mechanism, chartered by parliament, to promote and regulate social accounting and auditing.

RISING TO THE ORGANIZATIONAL CHALLENGE OF LOCAL ECONOMIC AND COMMUNITY DEVELOPMENT SYSTEMS

THE CALL FOR NEW REGIONAL DEVELOPMENT AGENCIES

We argued earlier that the ability to participate in life in community, and to take part in decisions in matters affecting one's own life and the life of fellow citizens is at base "one of the elementary freedoms that people have reason to value,…even among people who lead very deprived lives in material terms".[165] We also argued that the combination of reasoned agency, democratic and particpatory decision making and the imperative to reconcile tensions between powerful elites and the socially-vulnerable in decision making processes and their outcomes calls for us to rethink the processes through which we do local economic and community development.

At any rate, a revamped effort to deliver a socially-inclusive capability and asset-led local economic and community regeneration will be confronted by very practical logistical and organizational problems. What, for instance, is the physical and institutional infrastructure via which to pursue and achieve such ends? Much of the criticism of the centralized state, and the accompanying clamour for devolution, can actually be attributed to the lack of independent and citizen-centred physical and institutional infrastructure to pursue and deliver local economic and community development.

Strong local communities are vital for the realization of development objectives as set out in such key policy and strategy papers as the anticipated Vision 2030. Without an appropriate structure to drive local economic and community development planning, it is unlikely that communities will realize the benefits that can come with economic growth and development. Similarly, without a well articulated independent participatory, inclusive and resident-led local economic and community development system, it unlikely that current efforts in devolved and sub-sovereign finance will yield little more that a shopping list of projects at the behest of local and national elites. A well structured local economic development regime is central to the success of the proposals espoused elsewhere in this study.

The study argued earlier for a central place for local citizen-owned and driven social economy organizations, especially not-for-profit social and community benefit organizations and enterprises, as a key institutional asset class in driving a new local wealth and asset development process. In this section, we review institutional infrastructure at state level and call for reform of existing infrastructure to deliver local economic and community development. We also call for state support of independent not-for-profit actors capable of undertaking

[165] Dreze and Sen (1995:106).

and promoting asset-building strategies for local economic and community development.

Through these and other formulations elsewhere in this study, we aim to carefully circumvent and side step the emotive issue of political devolution and decentralization and its possible application to local economic and community development. We do this in the conviction that neither political devolution nor decentralization, as variously proposed, are based on the objective need to locate local economic and community development in the personal and collective agency of residents and those who have suffered historic or social exclusion. By working to build the individual and collective capability asset-base of the socially-excluded and their communities, we lay the ground for a more engaging process of devolution or decentralization where the viability and sustainability of local states, however expressed, are assured.

Inadequate Community Development System

Kenya has an acute dearth of appropriate local community development planning infrastructure. An inheritance from colonial state infrastructure, the work of economic and development planning has been arrogated to the central government chiefly through the Office of the President, the Ministry of Planning and National Development, and in smaller measure the Ministry of Local Government, and the Ministry of Regional Development Authorities. While districts have had development plans since independence, the function of planning has been largely a central government authority with some administrative delegation at the provincial level.

With the onset of the District Focus for Rural Development in the early 1980s, many districts acquired some capacity for economic planning through the posting of economists and the establishment of District Development Committees (DDCs). The district focus strategy, however, only succeeded in increasing the control that the central government had on local planning and development as the DDCs were essentially command and control structures.

Regional Development Authorities country-wide have been used by politicians to entrench political patronage. They have also been a principal site of corruption, including engagement in dubious investments and heavy borrowing that goes to fuel the political patronage regime. Ironically, Regional Development Authorities ought to fare better than the provincial planning as they are established through statute and have extensive development and asset-holding mandates. Many also cover more than one province, making it feasible to achieve significant economies of scale in their operations.

Perhaps the most central component of the local economic and community development system is the local authority, existing variously at County, Town, Municipal or City Council. Local authorities and their governments have, however, by and large failed to evolve as viable sites for planning for local economic and community development. Local governments have been faced by a myriad of problems including corruption, inappropriate legal structures, mediocrity, low skill, and low revenue basis that have effectively made them a drain on assets.[166]

The capacity for strategic engagement, planning and monitoring at community level is critical to ensuring that growth and anti-poverty interventions, even in the unfortunate case where they may be driven by forces outside the local community, are tailored to local conditions, are effective and long lasting. It is also important that local communities learn how to organize and plan their own processes, how to access global, national and regional government resources, and hold their governments and global structures to account.

The Question of Process in Local Economic Development

It is difficult to imagine or achieve an improvement in the quality of life of individuals within a locality without a well-articulated process of local economic and community development. Members of a particular community soon resign themselves to apathy when they are not able to point to successful outcomes in their community that they can attribute to their own efforts and planning. It is also difficult to bring community and para-state institutions active at community level to account without an effective locally-engineered and local-led development process. Such institutions include primary and secondary schools, technical training and workforce development institutions, healthcare institutions and health boards, all of which are key to delivering desired national and local growth and developmental outcomes. It is also true that past approaches to local economic development that have left community development processes to local or central government agencies have failed to inspire genuine development at this level. Much of the current apathy and cynicism regarding public life can be blamed on the failure to deliver effective local economic development.

Past approaches to local development have concentrated on providing incentives for uptake of local productive resources and the provision of essential services through large scale centrally-planned and controlled social service agencies in areas such as health and education. There has not always been adequate recognition of the place of local or community-based organizing, asset development and investments in the solution of run- away under-development.

[166] See Amaya J. A. and Gitau S. (2003) and Mitullah, Odhiambo, Akivaga.

The mushrooming of, for instance, locally-controlled and initiated community wildlife trusts in Laikipia and Samburu districts, which are now rivaling the Maasai Mara as key high-end tourist attractions, points to the need for a critical rethink of centralist planning for local economic development. While there is clearly an acute need to reverse the spiral of under-investment, negative social capital and under-capitalization in rural and urban poor communities, it must be recognized that in terms of planning, this is best done from the bottom up and by promoting strong local social and private sector enterprise cultures.

While there has been much debate about the empowerment of women and the need to bridge the gap between the rich and the poor nationally and within regions, it is also unlikely that much can be realized in this effort without significant reform of economic development planning to enable effective capacities and self-motivating efforts at local levels. From ongoing debate on the draft constitution, one can already see the danger of this becoming a national agenda without sufficient correlates and facing much resistance and hostility at local and community levels. Yet, it is practically impossible to regenerate social capital or build strong communities without taking stock to account for the place, participation and consequence of women in these efforts.

In the final analysis, and in the wake of a market and private sector-led economy, dynamic and effective local communities must develop strong organizing, entrepreneurial, management and leadership capacities to ensure long-term economic sustainability. It will be difficult to acquire such capacities without bringing a significant economic planning function to this level.

There is clearly a need to embrace a pro-active local economic development strategy grounded on the imperative to:

- Respond to the legitimate, self-defined needs of local populations;
- Entrench community engagement and participation in the economic growth process;
- Entrench community organizing, voluntary action, enterprise, asset development and capital accumulation as the organizing framework for local economic and community development;
- Entrench the role of local savings and investments in regenerating communities and securing local economic development;
- Grow local social capital and inclusion as a prerequisite to sustainable local economic development;
- Provide local economic, social and political drivers to overcome poverty, inequality and social exclusion.

New Regional Economic and Community Development Agencies

In view of these arguments, we propose a completely new face, structure and process of delivering local economic and community development comprising of the following:

New regional economic development agencies

A completely new regional community development administration should be established. It should be anchored on 26 new Regional Development Agencies (RDAs)—statutory but independent—with each RDA bringing together several counties in one economic development area. Ideally, the territorial scope of each RDA will reflect the current provincial set up, with each province being split into two to make 16 RDAs. In addition, Rift Valley Province and Eastern Province should each get an additional RDA for some counties in the North comprising perhaps of Isiolo, Turkana, Samburu, Marsabit, Moyale and Wajir. An additional RDA for Greater Nairobi should be created to comprise the metropolitan/adjacent urban areas of Mavoko, Ngong', Kikuyu, Kiambu, Ruiru, Juja and Thika. A special status RDA comprising of the major municipalities/urban centres of Mombasa, Kisumu, Nakuru, Eldoret, Nyeri, Meru, Kakamega, etc should also be created.

Local economic and community development zones

The establishment of about 70 new Local Economic and Community Development Zones set up within the jurisdiction of respective Regional Development Authorities will be necessary. A Local Economic and Community Development Zone would bring together several counties into one Local Economic and Community Development Zone. Each RDA can yield about three LECD zones making for 70-75 of such.

With own resources and chartered cities, metropolitan areas and qualifying municipalities can also charter stand alone Local Economic and Community Development Zones or Regional Development Authorities with respective Community Development Zones. The law would be clear regarding the regulation and functions of such local authority chartered bodies, including their independence from the authority issuing the charter. The proposed apex regulator should have power to moderate the contents of a charter.

Regional or Local Economic and Community Development Zones could be chartered for specific purposes or in specific fields such as health, housing, workforce development, industry, etc. They would consequently have functional jurisdiction over those purposes and fields. The law could require consultation between various agencies and authorities with a view to pushing integrated development efforts and strategies.

Community development zones

Establishing stand-alone Community Development Zones comprising a single county and falling within one of the 70 Local Economic and Community Development Zones for purposes of local economic and community development planning will also be essential.

RDAs and the Local Economic and Community Development Agencies are themselves not executing agencies and require the existence of other bodies, including the central government, local authorities, community development corporations, local business corporations, community benefit organizations, and companies and local community development finance institutions to execute various plans and strategies.

Regional Development Agencies (RDAs) are, however, lead agencies in the process of local community visioning, strategic planning and attracting investments and financial inflows for local economic and community development. Accordingly, they will coordinate the process of community visioning and lead in the design, implementation and evaluation of strategic development plans and partnerships. RDAs will be the accounting unit and custodian of the Community Development Account and will authenticate the validity of strategic plans and investment programme to effect desired local economic and community development.

Apex Regulator for Local Economic Development—Local Economic and Community Development Commission

This study proposes setting up of an apex authority—the Local Economic and Community Development Commission—responsible for regulating the work of the new regional and local economic and community development agencies. This would call for a re-visioning of the Ministry of Regional Development Authorities to reflect the new developments.

Government development office

A Government Development Office styled as a chancellery for local economic and community development (development chancellery) at existing provincial level and headed by a Development Chancellor and comprising such directorates and expertise in the key sectors of local economies such as health, education, and industry may be necessary. The Chancellor and the directorates would be responsible for joining up key line ministries and government policy with local economic and community development aspirations.

Regional Community Development Venture Capital Corporations

It will be necessary to restructure the current Regional Development Authorities so that they take up the task of providers of long term regional development finance along the lines suggested later in this study, largely as long term venture type development capital used to back up the long term financing needs of the strategic plans approved by the new Regional Development Agencies. The amendments to the statute should vest in them their current assets in their respective jurisdictions, with a statutory requirement that 25 percent of the income made from these assets revert to them as a permanent charge.

The Regional Community Development Venture Capital Corporations would be assured of significant transfers through a mechanism similar to that employed by LATF but with specific proviso prohibiting the use of resources from this transfer for administrative or recurrent purposes. These new Regional Community Development Venture Capital Corporations would also be mandated to issue development bonds and raise capital from the local and foreign debt market to finance their work. This should, however, be done on the basis of private debt and without government guarantee. As we propose later, these corporations should be at liberty to use the security of their transfers to secure such debt.

Individual Regional Development Authorities could charter their own Regional Community Development Venture Capital Corporations. Again the corporations can be set up in specific sectors such as health, education, manufacturing, tourism, etc. The proposed apex regulator would have regulatory jurisdiction over the work of the venture capital corporations.

Securing the Development 'Process'

The study proposes that the statute captures minimum requirements for the local economic and community development process. In particular, the statute should require:

- Elaborate and participatory community visioning and planning
- Responsiveness to historical and other social exclusion
- Gender aware and responsive processes and outcomes
- Respect and nurturing of community-based development organizations
- Participatory and systematic evaluation and monitoring of development efforts
- Continuing and independent resource mobilization, i.e. not just dependent on transfers from the exchequer.

The statute must also secure local economic and community development processes from excessive interference by politicians and the central government.

Key Characteristics of New Regional Development Agencies

This study proposes 26 new Regional Development Agencies to spearhead economic and social-cultural development and investments in their respective jurisdictions. In our view, the authorities can be achieved through amendment to the various statutes establishing current Regional Development Authorities. We outline here the key characteristics of the new development organizations as proposed, their motivation and relationship to the existing development authorities, their institutional form and autonomy, as well as how they sit *vis-à-vis* local authorities and the central government. We also outline changes we propose in the functioning of central government, especially through the scaling up of the Ministry of Regional Development Authorities to provide for greater prominence of regional economic planning and development.

Statutory functions

- Coordinating bodies charged with leading local economic development in their regions
- Promoting economic development and community regeneration in their jurisdiction
- Promoting enterprise development, business efficiency, investment and competitiveness in their jurisdiction
- Promoting human resource development
- Promoting workforce development and employment
- Ensuring that the region is not left behind in social, cultural and economic development

Strategic/Statutory activities

- Preparing economic planning strategies and operational plans for the region
- Identifying opportunities and coordinating feasibility assessments
- Collecting and distributing information
- Building local capacity for economic development planning
- Promoting investments into the region
- Marketing the region for purposes of tourism, sports, etc

- Providing operational assistance to not-for-profits, social enterprises and industry bodies representative of the region
- Providing operational assistance to other bodies, including local authorities
- Providing financial, operational and technical assistance and oversight to the Local Economic and Community Development Zone Agencies in their region
- Providing financial, operational and technical assistance to independent area/community development corporations incorporated by residents or that desires to be active in local economic and community development
- Providing financial, operational and technical assistance to regional economic development agencies headquartered or with significance presence in the region

Structure

- Governing Board made up of six representatives of the Council plus three government representatives from the Development Chancellery. The Board would be chaired by the vice-chair of the Council, who should not be a government or local government functionary
- Directorates and centers responsible for, for example, social enterprise development
- Appointment of Chief Executive Officer of the Regional Development Agency by sending three nominees from whom the responsible Minister picks one or rejects all.
- Directors and other staff appointed by the Chief Executive Officer in consultation with the Governing Board.

Governing Council

The chief function of the Governing Council is to:

- Approve local economic and community development strategic plans brought before it by the Governing Board of the respective RDA
- Approve work plans of the RDA
- Approve investment plans made by the RDA
- Provide a forum for oversight over the executive function of the RDA
- Advise the Governing Board, nominated by a combination of actors, including local councils, local civil society, business and trade organizations, etc

Municipal and local government representatives should not be more than a third and should comprise of political representatives, such as mayor. The Council

should be chaired by the Development Chancellor. It should be mandated to carry out investigations, and call and receive evidence on matters placed on its agenda by the Governing Board. The Council should also be able to initiate its own agenda.

The Development Chancellery will advise the Council. However, representatives of the local authorities, representatives of civil society, representatives of social enterprise and community benefit not-for-profits, representatives of local business and trade councils, representatives of local professional associations, etc can also veto the decisions of the Council. Each body should elect a principle with the power to exercise veto vote. Each membership constituency should have an institutional forum that meets at least once per year. The law should provide a reasonable measure of administrative autonomy of these agencies.

Involvement of local councils

Local councils should be involved in the decision-making process of the new local economic development administration by nominating persons to sit on the advisory boards of respective agencies. They should also be entitled to participation on the governing boards of a Regional Development Authority, a Local Economic Development Agency and a Community Development Agency. Participation, however, should not equate to control, and measures should be established in law to secure the independence of the authorities and agencies from such control by either the central or local government authorities.

The issues of structure are vexing but should secure:

- The need to ensure participation by local communities
- The need to place requisite economic development and regional planning expertise at the disposal of regional and local communities and organizations
- The need to secure long term planning and execution capacities for regional and local communities
- The need to ensure that communities attract the resource mix necessary for sustained and environmentally healthy growth

Statutory Functions of Local Economic and Community Development Commission

The Local Economic and Community Development Commission will bring together the chief executive officers of each RDA, several independent council

members from each region, several appointed or elected representatives from each RDA, nominees from the minister, nominees from civil society in each region, nominees from national civil society, nominees from local social enterprise organizations, etc.

The Commission should be chaired by a presidential appointee with approval of parliament. The Commission should also have a non-executive board of directors with a Chief Executive Officer nominated by the Board and approved by the minister.

Some of the statutory functions of the Commission would include:

- Providing independent oversight of the proposed RDAs, including monitoring the work of the agencies relative to their mandates
- Proposing and gazetting subsidiary legislation relating to the conduct of RDAs, LEDA, CDA, etc
- Making rules entrenching emerging best practices in local economic development
- Evaluating development outcomes in each of the RDAs
- Advising the minister on matters relating to local economic and community development
- Reporting to the president and parliament through the minister

Though the Commission may not have power to cancel proposed regional economic development plans, it should be required to audit them, subject them to independent critic and public hearings and make recommendations for amendment and embargo to individual RDAs, the minister and parliament.

Each regional development plan should receive a letter of no objection or conditional or unqualified opinion from the Commission. In case of an objection, the RDA can present a petition to the minister, stating its reasons for adopting the plan. Following this action, the minister should appoint an advisor to the RDA seeking to help it negotiate new grounds with the Commission. If within three months of setting up the advisor the Commission maintains its objection, the advisor will prepare a report to the minister, who should then refer the matter to the Head of State. The Head of State will appoint a committee of between three and five qualified persons who will then subject the matter, including the proposed plan, the objections of the Commission and the recommendations of the advisor to thorough scrutiny and a public hearing. The committee will make recommendations, which once assented to by the Head of State will be binding on the Commission and the authority.

Proposed New Independent Institutions in Local Economic and Community Development

Current efforts in devolution and sub-sovereign finance have involved public type bodies and juridical institutions. The recommendations of this study have focused on these public sector development agencies. It is unlikely, however, that the structural problems bedeviling local economic development can be addressed without significant engagement and legitimating of independent, social economy-based infrastructure organizations. These local economic and community development corporations can be vital in driving inclusion, new strategic accountability, attracting new independent finance, skills and ideas to a region or locality and in serving the strategic needs of historically-excluded groups and communities in a sector or locality.

Through the legislation establishing the new local economic and community development structure, we propose that the apex commission be provided authority to charter or authorize such chartering by local authorities or RDAs the following types of institutions:

- **Regional Development Corporation**: Incorporated through one of the legal forms available to the sector but preferably through not-for-profit company law, and specific to a region or sub-region
- **Area Development Corporation**: Incorporated through one of the legal forms available to the sector but preferably through not-for-profit company law, and specific to a local economic development zone or a county and responding to select issues such as health, housing, workspace development, and amateur sport
- **Community Development Corporation**: Incorporated through one of the legal forms available to the sector but preferably through not-for-profit company law, and specific to a county, ward or other defined communities of interest

Community Development Accounts

We made proposals elsewhere for the adoption and implementation of Individual Development Accounts as a key instrument for driving capabilities and assets progressively for all individuals but starting especially with the most vulnerable and socially-excluded persons in society.

We propose to extend this model to specific communities though the adoption of the Community Development Account framework. Community Development Accounts, to be held by individual community and area development zones and through these the Regional Development Agencies, will differ significantly from individual development accounts. While Individual Development Accounts are

real accounts held by individuals within various Community Development Finance Institutions, Community Development Accounts will principally be planning and budget instruments used by local economic and community development agencies to compute the total financing pool available to a particular community or region. This tool will form the basis of financing the local and regional strategic development plans. It will also form the basis of tracking local expenditures relating to local economic and community regeneration. Community Development Accounts are, therefore, strictly speaking not monies held by these development agencies but the total annual and long term financing available to a community and tracked by the Regional Development Agency.

The Community Development Account will provide the basis for pursuing and implementing equilization expenditures under the proposed apex finance mechanism—Social and Community Benefit Asset Endowment Scheme. This mechanism will derive a set of statutory indices, including a National Social Exclusion and Vulnerability Index and a National Index on Quality of Life, well-being and freedom to allocate resources to various communities with a view to boosting their capability, assets and functionings thresholds beyond a given level. Defined communities would get significant resource allocations pegged to their performance on these indices and subject to real strategic investment plans articulated by development institutions and agencies in these communities.

We anticipate that these independent development agencies will provide healthy competition and alternatives to the public/statutory ones and will also provide for independent development organizing in a region or community even in the face of state/government/public failure.

RETHINKING FINANCIAL INTERMEDIATION FOR LOCAL ECONOMIC AND COMMUNITY DEVELOPMENT

> "Access to financial markets is important for poor people. Like all economic agents, low-income households and micro-enterprises can benefit from credit, savings, and insurance services...
>
> But financial markets, because of their special features, often serve poor people badly...Since poor people often have insufficient traditional forms of collateral (such as physical assets) to offer, they are often excluded from traditional financial markets... transaction costs are often high relative to the small loans typically demanded by poor people. And in areas where population density is low, physical access to banking services can be very difficult..."
>
> *Source: World Bank, World Development Report 2000-2001*

The success and popularity of the Constituency Development Fund as a decentralized institution may be found not so much in the success of the types of projects financed through it but principally as a financial intermediary for local community development working to overcome long term financial exclusion suffered by these communities. Members of Parliament and the public have expressed awe that indeed such money can be directly available at the constituency levels.[167]

On the whole, however, sub-sovereign finance intermediation has had a disastrous record locally and nationally.[168] Most of the institutions established to drive development finances in the various sectors have been tottering on the brink of collapse owing largely to mismanagement and political interference. Sub-sovereign development finance institutions, including the CDF, have also provided the financial architecture through which male political elites have accessed state resources.

The apparent popularity of the various sub-sovereign finance schemes such as the CDF and the Youth Enterprise Development Fund may also actually be a pointer to a much greater unmet demand for well-structured community development finance and infrastructure, to be differentiated from typical commercial and micro and small enterprise credit.

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[167] Samuel Moroto, MP for Kapenguria.

[168] See, for instance, Murgatroyd Paul and Gachuba Peter (2004); also, Yaron Jacob and Mithika Michael (2004).

It will be necessary to rethink financial intermediation, and especially the supply of financial institutions that are appropriately tailored to deliver socially-inclusive financial intermediation for local economic development. Fortunately, we do not have to search very far for the prospect of such institutions as is evidenced by the numerous not-for-profit micro finance institutions, which have proven to be effective and hardy instruments in marshalling financial resources to communities and socially-excluded individuals.

Social enterprise-based micro-finance institutions, for instance, have done better than development finance institutions and local banks in reaching rural and socially-excluded populations for many reasons. Perhaps the most obvious will be their social benefit purposes to work to help overcome financial exclusion and extreme poverty. Less obvious is their combination of products that offer not only credit to individuals and groups but also community-based savings schemes, business support, advice and training. Social enterprise-based providers also supply a mix of other psychosocial products such as inbuilt support for persons living with HIV/AIDS, those supporting orphans and the sick. Micro-Finance Institutions, such as the Kenya Women's Finance Trust, are also proving adept at getting to the root of key social-exclusion phenomena such as the empowerment of women through targeted enterprise development finance.

The success of these MFIs forces a distinction between formal banking organizations tailoring their products to the MSE sector, which certainly needs to be encouraged, and social enterprise and not-for-profit-based interventions to address core social problems and the conditions that drive them. If well nurtured, this mode of delivering to financial exclusion and enterprise development has potential to help society get to the roots of many other afflictions in the economy such as low productivity, a non-diversified export base, lack of development finance and enterprise support to mature the informal sector, low savings per capita and low and erratic income basis for majority of the nations workers and the poor.

As we have shown elsewhere, the type of financial intermediation provided by Community Development Finance Institutions is crucial to the success of the various devolved and sub-sovereign finance schemes currently in operation. Some of these schemes, such as the Kabete CDF, have even resorted to establishing their own revolving fund schemes in the face of the institutional failure by formal banks and the inadequacy of available MFI institutions.[169] There is obviously a much needed intervention to supply solutions to grow and prosper this sector.

[169] See, The Standard, *How revolving fund changed the lives of women in Kabete,* The Standard Monday 20th November 2006, p18.

Unfortunately, the Micro-Finance Bill seems to confuse this sector for its various cousins, including MFI establishments set up solely on a for-profit basis.

Community Development Finance Institutions are a range of independent financial intermediaries, financed from a variety of sources including individuals, banks, charitable organizations, social investors and government. CDFIs use a variety of methods to achieve their social and financial goals. In other jurisdictions where they are accepted as part of the available financial intermediation, CDFIs include micro-finance funds, community development venture capital funds, social and community banks, community loan funds, community development credit unions and mutual guarantee societies.

Kenya has the basic institutional framework for nurturing and prospering a CDFI regime. There are, for instance, a well established stock of not-for-profit micro-finance institutions, SACCOs, community loan schemes such as ROSCAS and merry-go-arounds. These offer a ripe platform from which to grow and nurture a well-defined and appropriately regulated CDFI regime. It is significant to note that even in economies like the US and UK, CDFIs are valued institutions for their ability to provide much needed alternative financial intermediation to individuals and communities, who would otherwise go without any. According to Andrew Robinson, Chairman of the UK Social Investment Forum and Head of the Community Development Banking at NatWest/Royal Bank of Scotland:

> "There are real and perceived barriers that prevent marginal small businesses accessing finance from the banking sector. CDFIs are finding ways to support enterprise in communities, but it's more than just risk mitigation and reducing high transaction costs. It's a whole new way of working, underpinned by a commitment to social justice. This isn't about responding to demand. It's about stimulating enterprise in no-go areas, and providing the necessary backing." [170]

These barriers are even more real in our own context and have spawned an entire industry concentrating, for instance, on micro-finance. It is worth noting that financial exclusion is not limited to MSEs sector and individuals in excluded communities. There is considerable demand for financing to develop infrastructure and large scale enterprises in otherwise deprived and rural areas, or among excluded groups such as women. Such financing can be used by local communities to grow slaughterhouses, markets, grain silos, etc. CDFI intermediation will therefore apply even to medium scale and large enterprises.

We capture below the description of a set of CDFI type institutions, which we believe need to be accorded formal and legal recognition in an effort to deepen

[170] See UK Social Investment Forum Press Release, "The UK Social Investment Forum joins forces with the Treasury and banks to support a range of new financial products for the socially responsible investor", 21st February 2002.

available financial intermediation.[171] These institutions, individually and as a group, constitute an excellent asset class providing financial intermediation solely for the purpose of redressing financial exclusion to deserving clients and communities. Despite their obvious promise and potential, there has not been a clear policy and legislative framework to encourage their development and prosperity.[172]

Community Finance Development Institutions (CDFIs) present a completely new tier of banking and finance institutions and infrastructure that is to be differentiated from the conventional banking sector and the SACCO. Following proposals to regulate SACCOs and capture them as a second tier banking sector, the proposed CDFI would, therefore, qualify as a third tier dedicated exclusively to providing community development finance and driving investments and financial inclusion in underserved and poor regions. To bring this about, we propose the enactment of a Community Development Finance Institutions Bill[173] that seeks to learn from, recognize and reduce the key character of these institutions into an enabling legal and regulatory framework.

Character of Community Development Finance Institutions

Community Development Finance Institutions adopt various institutional and legal structures. Some of the more common include:

Community Development Bank

Banks are essential institutions in any community, and the establishment of a bank is often a prerequisite for the investment process. The creation of banks in communities lacking such institutions is, therefore, important to the welfare of these communities. Community development banks do not require government subsidy. After start-up costs, the banks are expected to be profitable.

We see the proposed bank as a membership institution that has used some of the advanced incorporation forms available to actors in the social economy to offer services to members and other target groups. While members may get loan and other banking services from the organization, they would not be entitled to dividend. The surpluses from the institution are directed to its social purposes.

[171] Community Development Finance Institutions are firmly established especially in the US, where they are an integral component of the Community Development System. The descriptions provided here are closely aligned to CDFIs in the US.

[172] For ongoing and relatively recent work to recognize CDFIs and make them work to alleviate financial exclusion, see for instance the UK Social Investment Forum (UKSIF), *"Community Development Finance Institutions: A new financial instrument for social, economic and physical renewal".*

[173] For comparative legislation in other jurisdictions, see the USA's CDFI Act.

The statutory purpose of a Community Development Bank would be to advance capital formation and increase the productive capacity and wealth producing ability of a definable community, especially socially-excluded and financially underserved communities; provide capital for community assets development and regeneration; and to build low income communities and regions through targeted lending and investment. We envisage that these will usually need large start-up capital considerations and to comply with a moderated schedule of regulatory requirements under the Banking Act.

Community Development Banks would be regulated by a Directorate of Community Development Finance at the Central Bank of Kenya. The licensing regime would impose on the banks a statutory requirement to:

- Check against possible mission and purpose drift
- Have a community or geographical area of focus
- Secure community and stakeholder participation at the board level, advisory level and an entrenched institutional forum

We envisage that Community Development Banks can take one of the company and other legal forms available to the not-for-profit sector, including especially the proposed Community Benefit Company and Community Benefit Society forms, to enable it tap into equity resources available from the mushrooming social investment market. The legal form should require particular membership.

A Community Development Bank should be a deposit-taking institution and can offer consumer financial services without a personal loan portfolio. A Community Development Bank can actually encourage beneficial shareholding through schemes where individuals own special shares akin to long term superior debt or preference shares.

Community Development Banks should only issue loans through group saving schemes initiated by the bank through special shareholding and through other CDFI-type institutions and SACCOs. Community Development Bank borrowers should be principally members of group savings schemes, qualifying not-for-profits, portfolio-based (fund) investments in small and medium size enterprises in target communities, low cost social enterprise-based and not-for-profit housing and workspace developers, other social enterprises and CDFIs. The bank should also be able to offer grouped workspace development loans, grouped mortgage and home improvement, and security-backed debt and equity finance to large for profits that meet benchmarked criteria and located or locating business in the target communities.

Other product ranges can include securitized student and workforce development loans to students and workers in the target sector. They should

also be able to access other schemes that may be launched by the proposed Social and Community Benefit Asset Endowment Authority, government-backed schemes, etc and should be enabled to raise long term development finance from the capital market and other sources. The Community Development Bank can be capitalized from a combination of members' equity, grant, debt and deposit finance.

Community Development Credit Union[174]

The statutory purpose or mission of a Community Development Credit Union would be to provide community ownership of assets and savings, provide route—through contracting with Community Development Banks—to affordable credit and retail financial services to lower income people and other target communities, through appropriate contracting with community development banks—and take deposits and make loans to members. The Union would have to comply with subsidiary legislation setting regulations and rules requiring contracting or instrumentalizaton of some services with community development banks or with mainstream banks under the Community Benefit LPA form.

The credit union could be incorporated using other forms available to the not-for profit sector, most likely a community benefit society, a company limited by guarantee or CBC and registered as a CDFI with the Central Bank of Kenya. To access benefits, one would have to be a member and qualify as for purposes of the charity and not-for-profit purposes.

Capitalization of the credit union could come from a range of sources and schemes, including member deposits, grants, targeted investment instruments from other actors in the sector, government, structured social investment deposits by high net worth individuals and for-profit corporations, etc. The union would essentially exist to provide largely a savings scheme function for the poor and socially-excluded and for financially-excluded regions. The range of services would include contracted consumer banking services and securitized MSE-contracted limited mortgage and home improvement finance. Technical assistance within the scope of their range of services would be required.

Community Development Loan Fund

The statutory purpose of the Community Development Loan Fund would be to aggregate capital from individuals and institutional social investors and re-lend this money principally to not-for-profit housing and workspace developers, CDFI-enterprise portfolios, social enterprises and qualifying not-for-profits in target regions and communities.

[174] Information of Community Development Credit Unions in the US can be obtained at the National Federation of Community Development Credit Unions website http://www.natfed.org.

The fund could be structured and incorporated in any of the forms available to the sector, including an LPA, if the issuers are all not-for-profits, a community benefit—LPA, any of the company forms as may be appropriate or any other available form. It should be registered with the social and community benefit asset endowment cooperation as a Community Development Loan Fund. The Fund will usually have designated purposes, which can be in any of the recognized purposes for the sector, and could be accessed by actors in the sector as well as qualifying MSE portfolio investments held by Community Development Banks or Community Development Venture Capital Trusts.

Capitalization of the fund could come from a wide range of sources, including foundations, private sector, banks, charities, programme-related investment by religious organizations, government, the proposed Social and Community Benefit Asset Endowment Corporation, insurance companies, pension schemes and individuals. Products and services should be targeted to enterprise-based operators in the region helping drive solutions for qualifying purposes for not-for-profits, and could be used for construction, business start up and expansion loans for qualifying portfolio investments, etc.

The fund manager should be required to take a position of the boards and project teams of funded projects. The manager should offer extensive guidance to beneficiaries before, during and after the transaction. The loan funds should acquire the character of the proposed superior debt instrument that enables fund managers to take over management and running of defaulting investee portfolios.

Community Development Venture Capital Fund

The statutory purpose of the Community Development Venture Capital Fund would essentially be to provide equity and debt with patient capital equity features for medium-sized businesses with manifest potential and capacity to create more jobs, entrepreneurial capacity and wealth that benefits low income and socially-excluded people and targeted communities and regions. These will require large investment capital outlays.

The venture capital fund could be structured most appropriately as an LPA or Community Benefit LPA depending on the issuers and participating entities. Issuers would be registered or incorporated in any of the legal forms available to the sector but with the intention of generating sufficient surpluses and minimum guarantee to investors. Investment instruments—specific funds—should be registered and authorized by the Capital Markets Authority. Once issued, the funds would be available to any takers in the market but should be of significant interest to government, institutional investors, targeted investment communities in the case of the Social and Community Benefit Asset Endowment Corporation-backed funds, etc. The aim would be to exclusively offer long term equity investments and loans to qualifying enterprises in qualifying regions or

communities. The funds should be required to offer extensive technical assistance to investee companies, including taking up management and board of director positions on the companies.

Community Benefit Micro-enterprise Development Loan Fund

The statutory aim of the fund will be to foster social and business development through loans and technical assistance to low income people involved in very small businesses, farmers, the self-employed and those unable to access conventional credit in targeted communities and regions. The fund will be instrumental in enabling take up of some key aspects of asset building, including business education, micro-insurance, social housing and business and personal saving cultures. It can use any of the forms in the sector to incorporate but should preferably be structured as an LPA or Community Benefit LPA.

The fund should be regulated chiefly by the conditions built into the fund instrument and any other statutory conditions that may apply, and registered with the Social and Community Benefit Asset Endowment Corporation. It should be available to qualifying businesses, workspace developers, and individuals through fund managers by issuing CDFIs, commercial banks, area and community development corporations, etc. All must include significant participation of borrowers in the entire loan allocation process and lend only through registered peer/group lending schemes, with the borrowers being involved in loan decisions.

The fund could be capitalized from a variety of sources, including actors in the social economy, commercial banks, private sector SRI activities, government, SACCOs and the regulatory instrumentality of the Social and Community Benefit Asset Endowment Corporation. It should be required by law to provide extensive technical assistance and training in enterprise and development to target beneficiaries and participants. Fund managers can securitize and graduate loan schemes to other formats in the CDFI regime to enable more participation and control to prevent or stop abuse or default.

Community Development Corporation

The aim of a Community Development Corporation is to renew and revitalize regions, neighborhoods and communities by sponsoring industry, producing affordable housing, creating jobs, and providing social services to low income and socially-excluded communities and targeted regions. They can take any of the legal forms available in the sector but should register with the Social and Community Benefit Asset Endowment Corporation.

Community Development Corporations could be capitalized from a wide range of sources available in the sector, the private sector and government. They should provide a wide range of services, including equity investments, mortgage lending,

debt financing, PRI investments and grant investments, linked deposits (with a license from commercial banks or CDFI banks), and individual development accounts, again with appropriate linkages. They should be required by law to offer extensive education and technical assistance to targeted and beneficiary individuals, communities and entities.

Social Development Banks

These are social enterprise-based banking institutions whose mission is to provide banking services to social economy institutions.

Community Re-investment Trusts

Community Re-investment Trusts are legal instruments using social economy legal forms established by for profit firms to direct their community and social investment portfolio. In return for these investments, such firms would qualify for a range of benefits from the proposed apex finance mechanism. Later in this study, we make proposals for an apex finance mechanism to drive new investment and resources in socially-inclusive local economic and community development regime. The proposed CDFIs form a central community-based institutional infrastructure for this scheme.

PART VII

RE-IMAGING SUB-SOVEREIGN FINANCE AS A STRATEGIC ASSET IN FINANCIAL INTERMEDIATION

FINANCING FOR LOCAL ECONOMIC AND COMMUNITY DEVELOPMENT INSTITUTIONAL INFRASTRUCTURE

> …A sustainable community regeneration organization has to be able to continue in operation when external grants are withdrawn or wound down. …An agency has to have the capacity to build up a revenue earning asset base either through the development of projects or by the transfer of assets. The possession of tangible assets… or a dedicated income is the key to achieving the goals of self-sufficiency, independence and stability, which underpin the practice of community-based regeneration organizations.
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> *George Nicholson*[175]

It is imperative that local, regional and national sub-sovereign and devolved finance schemes provide the bedrock financial support and be compelled to provide financial and other support to independent community development institutions in their areas. The potential for this has been amply demonstrated by the HIV/AIDS Fund, which has worked primarily with national and community-based not-for-profit organizations to achieve remarkable results in beating back the HIV/AIDS pandemic. We call elsewhere for the establishment of a community and regeneration-specific financial intermediation regime anchored on Community Development Financial Institutions to make this kind of collaboration sustainable and efficient.

We have proposed earlier that the state should carry a basic obligation of enabling the core budget of the Regional Development Agencies proposed elsewhere. We also anticipate that qualifying local not-for-profits, including the Regional/Area/Local/Community Development Corporations will access significant resources from the proposed apex financing mechanism—the Social and Community Benefit Asset Endowment Scheme. It is anticipated that much of the financing available to the sector through the proposed mechanism will be for purposes of strategic development, such as establishing endowment income to service core functions of an organization, assisting in the start-up of a particular infrastructure organization, etc.

It is expected that organizations will go out of their way to develop own and independent sources of financing, including membership fees, income from services, independent contracting and grants. This requirement should not remove such an organization from providing support and services to organizations in a particular sub-sector, who may not afford to pay for their services, and whose cost should be met from endowment income. It is imperative that these organizations, and indeed all organizations in the sector, are able to

[175] Quoted in Development Trusts Association, "Asset base development for community-based regeneration organizations".

operate on a full cost recovery basis where the cost of their services are charged to multiple sources of income in ways that do not jeopardize their public benefit and not-for-profit status but also help secure the sustainability of the organization.

For the purpose of this study, and also to reflect realities in the sector, we separate financing for the local economic and community development institutional assets, which should be provided chiefly through non-state not-for-profit and non-governmental activity with actual financing of local economic and community development. It should be clear, however, that since not-for-profit and non-governmental organizations exist primarily to serve community, such a distinction can be potentially misleading. A separation is in order as often financing may be available for local economic and community development that specifically avoids the strategic needs of the community development organizations at the heart of a particular local economic development effort.

Non-state actors, not-for-profit non-governmental organizations traditionally access finance through a number of methods and approaches. These include membership contributions, donations, grants from government, grants from foundations and NGOs, and grants and increasingly programme-related investments from bilateral and multi-lateral sources. With the onset and popularity of Corporate Social Responsibility (CSR), some financing is now available from the private sector.

While there are no data available on the amount of equity and debt finance that go to the sector, it is clear, however, that majority of organizations in the social economy actually obtain much of their income from a combination of donor income, a charge for their skills and services, various product offerings and debt finance. Some trading not-for-profits are able to plough surplus income into the activities of the organization. The paucity of reliable data also limits discussion on whether or not not-for-profits actually enjoy financing that is adequate for their purposes. A cursory glance at the sector points to the conclusion that organizations in the social economy hardly receive financing adequate to their levels of immediate and strategic needs. Indeed, it seems the case that they have too little money and as such hardly operate at full potential or meet their strategic growth needs.

Donor and Grant Income

Grants are perhaps the single largest source of financing for organizations in the social economy, even for large and established entities. Grants are even more significant for organizations serving extremely underserved communities such as those found in the arid and semi-arid regions. Access to grant finance is usually crucial to the ability of even successful organizations to develop a new product

or service range, put up a new building or even continue giving services. This is the case regardless of the sector. The lack of grant-based donor finance, for instance, is being blamed for the collapse of crucial family planning support services since the 1990s. The shrinkage of these services is currently being cited as one of the factors explaining the increase in Kenya's fertility rate, even discounting for the increased use of other types of family planning, especially condoms and abstinence on account of the onset of HIV/AIDs. If this is correct, clearly donor-based grant financing plays a pivotal role in the sector.

Problems with grant finance

Over-reliance on external donor financing, that is reliance on multi-lateral, bilateral and NGO funding for core purposes and administrative expenses, has many negative side effects. Perhaps the most obvious of these is the project or programme nature of the funding, which often means that the goal and purposes of the grant are set from within the source organization, with the recipient entities competing for the funds against the criteria set by the source. Partly as a result of this and principally reflecting changing thinking and conditions in the source markets for the aid, foreign funding is also often prone to thematic shifts. As a result, many recipient organizations in the south find that they have to undergo periodic disruptions and often mission, purpose and target reorientation in order to continue to access funding from these markets. Often times, the recipient organization has to go for long periods without the funding, causing severe attrition of staff, services and capacities. The effects are compounded considering that much of this aid comes with a heavy bureaucratic establishment that often does not support core organizational development and administrative services and which has to be 'retrenched' in the wake of the seasonal and thematic shifts in funding. Moreover, grant aid often comes with many attending conditionality and accountability requirements to the source markets, which will often require bureaucratic and institutional complexities not available or sustainable for recipient organizations.

While many organizations find that life without this funding is untenable for their purposes, and indeed while the presence of a certain donor has been the catalyst for the formation of many NGOs, majority of these entities soon find that it is nearly impossible to grow a viable organization based on these financing markets. Yet, one can never really get all the funding that they require and often the need for finance is often much greater than whatever is available. There is clearly not only a need to grow the sources of this finance and harness it to the strategic needs of the sector, but more importantly to wean the sector to grow internal and alternative sources of funding to enable grant finance to take up a more appropriate supportive role in the sector.

Inefficient administration and allocation

Grant financing is helpful when it is allocated efficiently and with due consideration to the need for proportionality. Owing to many reasons, a situation has evolved where there are very little efficiencies in its allocation and where total disbursements to the sector may not be due to any well founded criteria designed to match objective conditions obtaining in the sector. As a result, a large part of the aid goes to the pockets of a rent-seeking economic elite sitting in and constituting the membership of local NGOs. A larger part is spent by the representative administrative and bureaucratic machinery of the source markets. Many are the professionals who make handsome incomes and an enviable lifestyle in developing countries as consultants to the representative organizations and advisors to the fledgling NGO sector in developing countries.

Grants are much sought after and advantaged in part because they are non-payable. They, however, carry a huge cost as they may be difficult to align with other programmes and priorities of the organization. Often, further frustrations lie in the way of successful grant recipients who have the technical capacity and independence to define and determine their own work priorities. Many find that they have to conform to funding conditionality that actually takes away their best human resources to service purposes and activities, which they would otherwise consider non-priority. They also find that it is highly unlikely that they can build up a reserve and asset base from which to ensure the continuity and future of the funded activity once the grant has been exhausted.

Grants are often made with an insistence on new thinking, and often only the most creative and adoptive get to access the grant. Moreover, donors will often command better skill, knowledge and information resources and, combined with their financing, have the muscle to easily commandeer entire sectors. The combination of the insistence on and the better endowment and muscle of the source markets often leads organizations in the south to suffer mission drifts as they seek to follow the direction of the 'new money'.

A very severe drawback, especially in the face of the flurry of activities and new capacities created by grant funding, is the relatively short term nature of project and programme grants. It, therefore, has the effect of leaving behind lots of idle and displaced capacities. Its programme nature is such that, as many established social enterprises discover, it is nearly impossible to find donors who will contribute to the establishment of a new university complex to train medical workers as opposed to say financing the recurrent needs of an understaffed hospital. Many will be happy to supply recurrent needs such as drugs and personnel from the source market rather that enable the production of the same in the local economy. Clearly, it is difficult to secure the viability and independence of the local not-for-profit sector without addressing the vexing issue of grant finance.

Local gifting

Donations from businesses and individuals are the life blood of the not-for-profit sector in economies such as the US and UK. The market for individual and corporate giving in Kenya is, however, undeveloped and untapped. Where such gifting exists, such as the Safaricom and East African Breweries foundations, the size of the giving, the mission orientation and the sophistication of the portfolio are limited to serving the corporate image of the organization.

Individual giving has historically been cultivated through *harambee*. Though *harambee* giving was the dominant and official policy for nearly four decades, there was no effort to offer specific policy, regulatory and legislative structures to it and it soon fell into abuse within the first decade of independence. The use of *harambee* to finance public programmes was discontinued in 2003 with the Kibaki administration. It can be argued that in discontinuing the use of *harambee*, the government lost a clear opportunity to provide enabling policy, regulatory and legislative infrastructure for well directed regime of private giving for public purposes. The government also, apparently, equated giving for public purposes with giving to or directly subsidizing government projects.

Debt and Equity Finance

Owing to the lack of data and casework, it is difficult to make comparisons or informed discussions about the relationship between debt, equity and grant financing in the sector. Lack of data or research also restricts our ability to draw conclusions whether there is a clear and unmet demand for debt and equity finance in the sector. By extrapolating from the growth of the not-for-profit social enterprise micro-finance institutions and their own need for finance, we assume that it is actually the case that there exists unmet potential to grow the sector through a vibrant combination of grants, equity and long-term debt. The most 'successful' MFIs, for instance, have been able to access considerable long term or patient debt and have had to explore ways of harnessing equity participation to generate money for their core business and improve their risk ratings. It is tempting to surmise from the growth of the NGO micro-finance sector, most of which began as grant-based projects before branching out to more complex financing mechanisms, that a diversified financing regime as we propose here is not only desirable but much needed in the sector.[176] It is also clearly the case that the most successful social enterprise-based institutions, such as private universities and hospitals need significant low cost long-term financial commitments to grow their product and service offerings.

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[176] The Kenya Women's Finance Trust owes its financial success in part to a significant project finance grant by the Ford Foundation. The Jitegemee Trust was engineered out of a successful bilaterally-funded micro-enterprise support programme.

Debt and equity can have considerable superiority over grant income. Debt and equity products can be long-term and have the potential for allowing the organization time to grow its financing strategy. Moreover, managing debt and equity finances imposes fiscal and other financial discipline on the organization that is normally lacking if the organization is not required to generate surpluses and make savings. Debt and equity finance also provides greater license or freedom on the use of money to develop the organization. Equity and debt finance also creates numerous accountabilities that is more disciplining for the organization.

Income from Trading Activities

Trading not-for-profits, such as the Nairobi Hospital, mission hospitals, etc have been able to earn significant income from charges for their services and product range. While there is no hard evidence for it, it can be safely assumed that not-for-profits that are able to charge for their services have survived and grown while those that rely on well-wishers, including donors and government have either stagnated or folded. There are many ethical and ontological issues that attend to allowing not-for-profits to trade and, as we saw earlier, most of these issues have not been adequately addressed in policy, regulation and law.

Rent Seeking and Institutional Capture

Professionals and other individuals working in the not-for-profit sector should be barred from rent seeking within not-for-profit organizations. There clearly exists a conflict of purposes and interests when trading and tax exempt not-for-profits are formed or controlled by professionals with the primary aim of developing a consulting practice from those institutions. It is the case now, for instance, that majority of the 'successful' health institutions, such as the Nairobi Hospital, have been taken captive by stakeholder communities such as health practitioners and elite users who are the largest beneficiaries of these institutions. We propose a statutory limitation on the ability of special interest formations to capture such institutions.

Tax Reform for Private Public-Spirited Giving

To encourage private giving and build a market for individual and corporate giving, we propose reform of the tax code to offer income tax relief to individuals and corporations who give to qualifying charities and not-for-profits. Specifically, we propose that individuals be provided tax relief up to 10 percentage points for money given to qualifying charities and purposes. We also propose that corporations be granted 7 percent relief for similar actions. It is our view that the

particular tax relief scheme should be administered by the Kenya Revenue Authority in combination with the proposed apex regulator for the sector. The regulator would issue guidelines and rules for not-for-profits willing to engage in the tax relief scheme. These rules would include meeting best practices in social auditing and accounting, financial accounting and governance. All not-for-profits, irrespective of charitable purposes, would qualify for the scheme. This scheme is different from the tax relief proposed to drive the social and community benefit asset endowment scheme discussed in later chapters.

Requirements to Establish Permanent Endowments and Asset Base

Much of the reform agenda we have outlined elsewhere and below should make the emergence of a thriving local finance sector for the not-for-profit non-governmental sector. To secure their independence and ensure a healthy relationship with this sector and external finance markets, it should be mandatory for actors in the sector to entrench a culture of endowments and asset-based investments with a view to ensuring that their core services can survive withholding and withdrawal of such financing. As the local finance market gets more complicated and senior, it is likely that money will be available largely to those establishments that are able to add value, or the grants themselves will seek to add value to the operations of the not-for profit entity.

We also propose that the envisaged Social and Community Benefit Asset Endowment Authority and applicable statute:

- Be required to conduct policy, regulatory and legislative review that would lead to opening up new spaces for local not-for-profits to engage other income generating activity, especially through social and community enterprise
- Works to establish an equity and long term debt market for social enterprise organizations in the regions and on the country's stock markets
- Works to establish patient and social finance markets for social enterprises
- Works to deepen the financing of social enterprises through establishment of community development finance institutions
- Works to establish a high level and mainstream funding mechanism—the Social and Community Benefit Asset Endowment Scheme—to finance long term development needs in the sector
- Establishes dedicated income vehicles for sub-sectors in the sector as part of the asset endowment scheme

- Takes regulatory and administrative measures to make the sector more accountable, transparent and financially prudent so that it can command greater confidence from its financing community and stakeholders

We also propose that the government takes concrete steps to direct more state business through government grant in aids and contracting to the sector. It will be crucial that organizations in the sector be able and encouraged to work on full cost recovery basis, including charging for services. Organizations in the sector should be enabled in law to trade in their core and related services without attracting tax on surpluses, provided the surpluses are re-invested in the strategic development of the organization and to further the organizations purposes.

The measures proposed earlier with regard to a single point of call regulatory authority to enhance efficiencies in the sector will also go a long way in securing adequate seed type and strategic finances for the sector.

Other Types of Financing

The proposals we have made, especially for new company forms, and the social and community benefit asset endowment scheme should open up other types of financing, especially leasing and hire purchase to the sector. It should be possible for social enterprise establishments to lease or hire out key assets needed in the sector.

Requirements for Establishing Permanent Endowments

Endowments are funds or investments where trustees or directors of a not-for-profit organization are authorized to spend an income from the investment to the exclusion of the principal or capital. Permanent endowments are crucial in ensuring a fixed income for the organization as well as promoting institutional savings and investments. Owing to their reliance on donor and member financing, many actors in the social economy have a systemic inclination to spend down their income. While many funding agencies will view this as institutional efficiency and an indicator of need, this practice has the effect of leaving them over-exposed and vulnerable to the funding market.

Endowment income can be the lifeblood of an organization's social purpose or mission. Harvard University, a social enterprise and one of the leading higher education institutions in the world, has creatively used an endowment system to cover 30 percent of its annual operating budget. The endowment income is key to the university's ability to offer tuition scholarship to qualifying students, thus securing its ability to attract the best students from all over the world. The endowment is run by the Harvard Management Company, which also runs the university's pension and trust funds. Less than 10 percent of the endowment

income is spent annually on the financing programmes at Harvard. In 2001, the endowment gifted US$ 615 million to the university, whose operating budget was about US$2 billion.

The Harvard University Endowment system actually consists of a multitude of gifts and their investments made over time and with very specific purposes. Endowments have to be run well and professionally to guarantee a steady and reliable source of financing for the social enterprise. In 2001, the Harvard Endowment was worth in excess of US$ 19 billion and had consistently yielded above average returns in the preceding five years.[177]

Unfortunately, the tradition and practice of endowment funding is not popular with the sector in Kenya. This partly explains the over-exposure of the sector to grant income. It also severely limits the very likelihood that grant income can be used for the purposes for which it is set as organizations rely on the grant for all their financing needs.

We propose a range of measures to drive organizations in the sector to adopt endowment investments. These measures include requiring that any organization that seeks to benefit from state businesses invests the income gained into permanent endowments. We also propose that the Social and Community Benefit Asset Endowment Authority, through its various schemes, enable endowment investment by non-enterprise organizations—that is to say that while the authority cannot make traditional donations and grants to these organizations, it can make recoverable or non-recoverable investment grants to enable them set up permanent investments.

The proposed apex regulatory authority as well as the apex financing mechanism—the Social and Community Benefit Asset Endowment Authority—should be barred by law from financing the operations of entities in the sector that are not committed to establishing endowment income for their core purposes and to embracing social enterprise ethos and other financing schemes that aid them to become self-sustaining. We also propose relaxing the income and corporation tax regime to reward individuals and organizations that donate to endowing the causes of not-for-profits.

Not-for-profits generally and especially those above a certain income threshold should be required by law to set up such endowments and to grow them relative to the size of their operations. The threshold or benchmark level should be such that an organization can meet at least 60 percent of its basic commitments without recourse to grant finance while ensuring that no more than 50 percent of endowment-based income is used to service salaries and administrative expenses.

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[177] Information adapted from Havard Gazette Archives: http://www.news.havard.edu/gazette/archives.html.

Once set up, the uses and administration of endowments should be entrenched in the constitution of the not-for-profit entity and protected in law from conversion to other purposes without the permission of the authority. The authority may make it a condition before such permission can be granted that the applying entity show that it has conducted thorough consultations with its stakeholders and membership, including targeted and past beneficiaries, on the proposed conversion. Further, the authority should be required to perform or cause to be performed by an independent entity a social audit relating to the proposed conversion. Nevertheless, the authority should be required to make case by case considerations for such applications in order to preempt a situation where the effect of its practice is to bar such conversion.

The authority can order mergers and other asset consolidation with other similar not-for-profit establishments if it is convinced that the purposes and objects of the distressed organization holding the endowment are best served by this measure. The endowments should not be used as bank collateral. Only the income from the investment and not the assets themselves can be used to secure bank credit. Even this measure will need the nod of either the asset endowment corporation if it was involved in setting up the endowment or the authority. Both will consider the likely impact of the proposed grant and its securitization against endowment income on the ability of the organization to offer the services financed by this income.

Generating Sub-sovereign Income Financing

Grant income is an important component of financing the social economy sector. Even with the presence of elaborate government licensed service contracting to the sector, there would still be need and justification for structured grant making by sub-sovereign governmental authorities to actors in the social economy. A lot of this is already happening in such areas as HIV/AIDS community interventions and increasingly the CDF. There is need, however, to view the prospects for a structured engagement that enables these entities to provide grants to independent institutions in the social economy that meet certain benchmarks in addressing core challenges, such as aiding acquisition of key capital assets by qualifying individuals and communities. Later sections of this study propose some ways through which this can be done, including CDFI-based Individual Development Accounts.

Increasing Earned Income from Devolved Finance

Devolved and sub-sovereign finance schemes are some of the largest local and national consumers of goods and services in the economy. We propose in later

sections measures to drive local economic and community development through increase in government procurement from local enterprises and economies. It is, however, important to emphasize procurement of services in ways that aid the strategic gender needs of women, fight social exclusion and ensure that goods and services supplied by the poor and competent actors in the social economy receive preference in the public procurement regime.

There also exists opportunity for government to exit service provision in some of the other key human capital sectors by converting its existing infrastructure, such as teacher training colleges, polytechnics, technical institutes and universities, to independent social enterprise organizations with compulsory public service obligations. In the same vein, there exists opportunity for government to consider 'buying' those services from independent actors in the social economy through a regime of specialized licensing and commissioning that enables them to provide those services at a cost to government. This would enable, say, a mission hospital to provide healthcare to the poor under license and charge this to the government or municipal authorities.

The benefits from such a regime shift in the provision of such public goods and services would be enormous. Constitutionally, and in theory and practice, the government is obligated to provide basic public goods and services to vulnerable groups in the population. In reality, government provisioning for these goods has been such that the poor and underserved get the brunt end through inferior and sub-standard public service institutions. Contracting social enterprise-based firms to provide the services and converting key tertiary government holdings in sectors such as health, education, technical training, research and extension, etc will have the effect of providing these organizations with the autonomy required to run vastly improved services.

Such a shift would also enable a clear distinction between the service provision and the public sector support for public goods and services. The resulting structure creates room for sophisticated financial intermediation to ensure that poor and socially-excluded groups and individuals get special targeting but also the best education, skills and health services. This new regime is vital in the actualization of such much needed interventions as progressive universal health insurance, progressive universal learning accounts, and progressive universal individual development accounts. Conceivably, a restructured sub-sovereign finance regime would be crucial to the delivery of the financial intermediation necessary to ensure widespread and progressive access to the resulting institutions.

Sub-sovereign Investing in Social Enterprise

The fact that genuine social enterprises have to continually take risks to deliver their public benefit often works against them. A genuine social enterprise-based women's hospital, for instance, not only charges a comparatively low fee to widen access, but may also not engage in such usual practices as requesting for securities as a pre-condition for admission. Similarly, a genuine, social enterprise-based private women's university would have to keep its fee structure low to enable access to as many as can afford it. It also has to build up an endowment or support base to enable genuine but needy students to access its services. As a result, it may take a long time for it to be in a financial position where it is assured of surpluses that it can invest to developing other programmes. Many such institutions are often considered not bankable and investor-worthy. Consequently, social enterprises have debilitating start-up problems, take too long to firm up and will usually have numerous financing difficulties in attracting investment for new products.

Social enterprises exist primarily to deliver social or community benefits. Many social entrepreneurs wish for a financial or fiscal regime that would recognize their social benefits and other positive externalities when making decisions about their financing. This is not to say, for instance, that they should not deliver excellent results as a business or that this should cease to be an important criteria in considering whether to invest in them, but rather that an acknowledgement should be made that they will incur costs and encounter risks that are attributable solely to their social purposes. There is, therefore, not only a need to eliminate this handicap, but to actually compensate social enterprises for the risks that they have to make. It is often the case that the risks that these organizations take will often translate into direct benefits to the public. Besides helping improve the productivity of the local workforce, a successful social enterprise that works with survivors of domestic abuse and trauma by offering skills and linked workforce development and employment opportunity saves the government and society money it would otherwise spend on civil and community safety. Likewise, an enterprise that provides apprenticeship opportunity for women ex-convicts who have acquired skills while in prison will have the effect of not only improving productivity and reducing unemployment but also actually saving government money it would spend policing crime and running its prison service. Such an enterprise also helps to ensure that money and time spent imparting skills to the convicts is rewarded.

Sub-sovereign financial institutions such as the CDF, HELB as well as restructured Development Finance Institutions can play a significant role by investing in the equity holdings of social enterprises. We have proposed earlier a possible raft of new legal forms that would make such equity-holding tenable. We also make subsequent proposals about local financial intermediation, in

particular the Independent Development Accounts and Community Development Finance Institutions that provide the institutional and practical tools to make and grow these investments.

It will be necessary to peg financial services available from these schemes, as well as the principal Community Benefit Asset Endowment Scheme and the CDFI framework, to the social returns of the social and community enterprises, MSEs companies and community organizations. Specifically, fund managers should be required to demonstrate that the beneficiaries of their investments are delivering demonstrable social returns. This requirement can be met by providing detailed gender and social audits (or gender responsive social audits) of the impact of the investments or carrying out such audits as a precondition to lending or investing in these organizations and businesses.

Conclusions

At the end of the day, investments and credit resources will materialize for the sector only when and if it can muster the trust of would be social investors and the larger investing and banking establishment. It is important, therefore, that sufficient safeguards be established in law to ensure that the sector can command the requisite trust through its performance and effective monitoring, auditing and reporting of that performance. We proposed earlier that the law establishing the various legal forms and regulator for the sector requires mandatory financial and social audits for all the actors in the sector. We have also proposed that the apex not-for-profit authority charters a statutory institute for practitioners in social auditing. We also propose that the Social and Community Benefit Asset Endowment Corporation, the apex not-for-profit authority, and the proposed CDFI Directorate at the Central Bank of Kenya consider taking up some of the cost of carrying out independent performance and social audits on the sector.

Proposals on a social accounting and auditing framework have called for a strong and mandatory connection between the ability of the proposed authorities and sub-sovereign finance to lend support to organizations in the sector. These organizations own performance on established social and ethical accounting standards. The issue here is whether there needs to be a linkage between an organizations' social returns and the kind of finances and support it can get from public sources and, by opportunity, created by virtue of the proposed legislation, without at the same time imposing a heavy financial and regulatory burden on the social enterprise or organization.

We propose that requirements be set up in law as a way of not only ensuring that financing available through public funds is protected against misappropriation, but also as a way of ensuring the sector's fidelity to its public benefit status. In recognition of the potential difficulty of spelling out such

requirements in law, we have proposed that the apex regulator be empowered in law to set up schemes and rules requiring compliance with such standards, to establish the standards and to charter infrastructure institutions in the industry to regulate and coordinate the practice of social auditing and reporting. We also propose that the practice of financial and social auditing and reporting be required in law for all actors in the sector, with provision for proportionate regulation based on a core criteria that can include the size of the organization.

FINANCING COMMUNITY DEVELOPMENT AND LOCAL ECONOMIC REGENERATION

A History of Neglect

Part of the new excitement with the visible devolved and sub-sovereign finance schemes is the sudden availability of new and easily accessible money to finance locally-determined community development projects. With schemes such as the CDF and the Youth Enterprise Development Fund, it seems that all of a sudden money is now available to help communities to what they have always struggled to do on their own—sink boreholes, build dams, expand schools, etc. That this new devolved financing wave has caught the popular imagination must point to existing and real need for such financing. This excitement also reveals one of the most serious flaws in Kenya's mainstream financial sector—the awful exclusion of large parts of the country and entire communities and groups off the financial mainstream of the economy. Yet, Kenya's financial and capital markets sector is one of the most sophisticated in sub-Saharan Africa.

Kenya is one of the poorest and most unequal countries on the continent and in the world. What may be the possible connection between past government failure to provide real money for local economic and community development, a relatively well established formal financial and capital market and the appalling levels of poverty and inequality? Why has the formal financial sector failed to provide redress for the financial exclusion experienced by the vast majority of citizens and communities, even while doing so is in the obvious strategic and long term interests of the sector? What can sub-sovereign and devolved finance do to help eradicate this financial exclusion?

Robust banking environment?

Kenya's banking sector accounts for over 10 percent of the gross domestic product. In 2005, Kenya had in excess of 40 commercial banks, over 10 non-bank financial institutions, over 50 higher purchase companies, over 39 insurance companies, over 20 investment banks and stock brokerages, a well entrenched stock exchange, several investment advisory firms, a nascent venture capital industry, a well entrenched cooperative savings and credit culture, several mortgage finance companies, one mainstream building society, several development finance institutions, a rejuvenated post office savings bank, numerous micro-finance institutions, etc. This sector had a loan and advances portfolio in excess of Ksh 400 billion, a total asset base of over Ksh 600 billion and total deposit base in excess of Ksh 400 billion. This sector has played a key role in mobilization of deposits and the provision of credit to the private and public sectors. One cannot,

however, possibly discuss financial exclusion, poverty and social inequality without bringing a sharp focus to the banking industry in Kenya. The sector has many shortcomings and, with the exception of the numerous SACCOs and MFIs, has been one of the leading contributors to inequality, social exclusion and poverty since independence.[178]

Kenyan banks have historically been very ineffective in mobilization of domestic savings, which are vital to locally-driven high economic growth. Banks typically offer below market interests on their deposits —often lower than any other available investment. Other than maximize revenue from deposits by converting them into long-term instruments for purposes of lending to the economy, banks have sought to make money from depositors by way of numerous and excessive service charges. Meanwhile, the banks still make money from the deposits by charging interests on loans that are way higher than what they offer the depositors.

The decade of the 1990s was notorious and perhaps the worst in terms of banking conduct. This decade saw the emergence of "politically-correct" banking institutions set up with the connivance of the ruling political elite to rip off the public sector. Banks also made huge profits, contributing to shrinkage in the economy by trading principally in government paper. Banks also chose to close majority of their up-country and low income clientele outlets. When they did lend, the banks specialized in supposedly high value often politically-correct clients. This, and in combination with other factors, led to a negative growth rate by the turn of the century. Evidence for the banking profligacy of this decade is available especially through the Goldenberg scandal, the high interest rates regime that peaked 70 percent in the early 1990s, the current huge domestic debt overhang, and the huge bad and doubtful debts advanced to politically-correct individuals and enterprises. Kenyan banks have also given a wide berth to the MSE sector despite its demonstrated potential and huge size, estimated at about 14 percent of GDP.

A role for the Central Bank of Kenya?

There has been little discussion of the role and enormity of the contribution of the Central Bank of Kenya and the banking sector generally to poverty, inequality and social exclusion. While current government policy attempts to fix the problems of the banking sector, it does not go far enough and is at risk of triggering a repeat of most of the problems. The government, for instance, has decreased its appetite for borrowing from the banking sector, instituted financial sector reform with a view to eliminating systemic risks that led to the huge political

[178] See Kimura Joseph (1999).

debt portfolio, and encouraged more lending by reducing capital reserve requirements and keeping the treasury bill interest low. These efforts may not yield significant dividend either to the enterprises, social economy or other actors at the heart of local economic and community regeneration. An examination of the Economic Recovery Strategy does not reveal an awareness of the great need to reform the sector with a view to containing and eliminating financial exclusion.

Unfortunately, the current extreme inequalities in Kenya work to effectively handicap the banking institutions from reaching out to the poor and socially-excluded. Kenya's extreme concentration of wealth and incomes in a tiny minority of the population effectively means that the vast majority of Kenyans have little power to consume or save and are effectively locked out of the formal banking market. Unfortunately, the extreme income and asset inequality has a very chilling effect on the ability to use the formal banking sector to drive local economic and community regeneration. Recent and ongoing economic expansion and growth in the supply of credit to the private sector by the banking establishment, for instance, has led to higher import bill.

While this study does not seek to prescribe reform of mainstream banking practices, which ideally should be the focus of wide ranging policy and legislation, it is informed by this background. Some of the recommendations we make should be attractive for commercial banks and development finance institutions willing to increase investments in the target sectors and could lead to significant reform of bank practices and attitudes. Other proposals will have wide ranging impact by growing previously excluded and underserved regions and providing a powerful motivation for commercial banks to invest in them. Yet, others will have the impact of compelling change in the sector owing to the emergence of social enterprise and community targeted CDFIs.

Elements of the New Financial Instruments

Debt and patient capital

Debt finance is a significant source of capital for the development of enterprise. Local economies and socially-excluded groups and communities cannot possibly prosper without sufficient access to good quality and low cost debt finance. Debt finance is usually issued against existing or future assets and income. It is also important that these assets can be easily converted to liquid assets. Where individuals or communities lack sufficient assets and incomes, they are considered unbankable. Similarly, where an individual or community holds assets that can not be easily converted to liquid assets, then they will be left out of the formal bank debt market. The significance of debt finance to growing individual and community assets cannot be overstated. Debt finance will usually constitute between 40-70 percent of the financing of typical medium and large scale projects.

In reality, this is the real new money flowing into a region's economy and is much sought after by individuals, companies and governments.

Besides the lack of assets and income, there will be many other factors contributing to low levels of good quality debt in a local economy. Many of these will be considered later.

Devolved and sub-sovereign finance holds the key to especially the challenge presented by low quality local assets, local liquidity and lack of income. Devolved funds may be the only source of new money coming into a community. CDF, for instance, presents a guaranteed flow of money into a region's or community's economy. The fund, therefore, presents a significant asset that, if well structured and utilized, can be a strategic source of security for sourcing concessional finance on the national and international debt market. The HELB, for instance, presents excellent opportunity to structure debt financing schemes targeted at a group of female students, a region or a community. Consideration, therefore, ought to be made of the possibility of using devolved finance schemes to leverage the strategic financing needs of local communities. It would also be necessary to recognize financial exclusion as one of the strategic purposes of all the sub-sovereign finance schemes.

There is also a need to establish mechanisms that would enable the peculiar assets of the actors in a local economy, especially those in the social economy, such as NGOs and charitable companies as well as the proposed new forms to provide opportunity for these organizations to access appropriately-structured debt and bank credit by leveraging locally and nationally-available sub-sovereign finance. Organizations that are able to sign up grant agreements with a range of donors should, similarly, be enabled to use these agreements and backing by sub-sovereign finance to access debt finance, especially from the capital markets.

A social enterprise organization working to provide secondary school or workforce to underserved youth, and that has stable donor financing to meet the recurrent costs of its service should be able, for instance, to access low cost mortgage finance to put up necessary facilities if it can devise some ways of generating a surplus that services the debt. This debt should be structured such that should the organization succeed in raising support to pay, it should do so without penalties.

Patient capital

Patient capital is especially important for long term asset development. Its long term nature, and often equity character, makes it especially suitable for startups and expanding enterprises, whether private or social enterprise-based. When it is structured as a debt, it can have capital and interest payment holidays to the

extent of differing all capital payments until the maturity of the loan, or alternatively it can be structured as an extremely low interest loan almost similar to a recoverable grant.

Schemes such as the Higher Education Loans Board (HELB) and the various development finance institutions are actually instances of the states' attempt to provide long term patient finance to meet the capital requirements of key sectors in the economy. Unfortunately, the differential strategic needs of women and men in long term patient financial capital are often ignored. Most of the interventions required to provide redress to asset poverty will require long term capital. It will be difficult, for instance, to grow the skill and knowledge of women without offering long term financing for it. It will also be difficult to ensure women's reproductive health without providing for the supply of sufficiently trained health personnel, health facilities and healthcare financing, all of which require long term financial intermediation.

Recoverable grants

Recoverable grants assume a variety of alternatives following the broad outline where grants offered are used primarily to finance endowment schemes for qualifying community benefit organizations. The assets of the scheme are held by the corporation or its appointed agents until the grant is recovered. The asset is then released to the grantee organization as a permanent endowment.

Superior debt

Many not-for-profits, even those that are enterprise-based, may not take the proposed Community Benefit Company route but would still desire to harness the power of the financial markets to secure reasonably-priced long term finance. Where such organizations are successful and sufficiently large, we expect that they would be able to get finance from the stock market by way of social development bonds. Many organizations, however, may not meet threshold requirements that may be set to be able to list bonds on the stock exchange. For such organizations, we propose the introduction of a completely new instrument—superior debt.

The superior debt would confer on the debtor organization obligations similar to those owed to holders of preference shares. Their income rights should be defined and will be entitled to a fixed return on the debt. The debt instrument may also be redeemable by a certain fixed date and at a fixed premium. The issuer of such a debt, where it is above a certain threshold, may acquire rights to participate at the board level of the company and may set as a condition that the organization restructures to allow an institutional or advisory forum. Such an

investor, however, shoulders the risk of default and may be constrained by other creditors from recovering his loan in the event of dissolution of the organization.

Senior debt

It may also be necessary to structure a senior debt instrument that would confer rights and privileges along the class of 'A' ordinary shares (also known as preferred ordinary shares, cumulative convertible participating preferred ordinary shares).

Economic considerations

It is important that debt and other forms of financial assistance to generate a local long time credit market should contribute rather than crowd out other available private capital involvement in providing the kind of redress sought in driving gender-responsive and socially-inclusive asset accumulation and local economic regeneration.

Assistance should also aim at achieving or aiding inclusion so that financial intermediation is carried to the point that allows beneficiaries to mature and independently participate in the broader capital and banking markets. Where appropriate products are lacking, or owing to strategic market failure in the sector, the new intermediary institutions should be aided to become part of the mainstream financial products markets. Financial assistance should ideally be directed at creating a market for social economy-based development finance capital. Such a market should be enabled to take up a life of its own, much like is the case with current experimentation in MFIs and SACCO regulation.

USING SUB-SOVEREIGN FINANCE TO EXPAND FINANCIAL INCLUSION BY FORMAL BANKING AND CAPITAL MARKETS

We have made assumptions and presentations elsewhere in this study that redressing the asset poverty of socially-excluded communities and individuals is actually at the heart of supplying drivers to eradicate historical social exclusion, poverty and inequality. We have also made the case that asset-building for this purpose works at individual, household and group or community level. We identified social and community benefit enterprise as core to the delivery of this asset development foundation; that indeed, organizations in the social economy constitute a special asset class built to deliver on other individual and public benefit assets. We subsequently made recommendations about the strategic legal, structural, institutional and financing needs of the sector with a view to firming up its appeal, demand fundamentals and credit prospects. It is imperative, however, that we also deal with the supply side—the institutional willingness, readiness and capacity of the mainstream capital markets to invest and offer services to the actors in the social economy as well as reach out to the yawning asset accumulation demand of the poor, and how devolved and sub-sovereign finance can be of help. In the process, it crucial that we interrogate devolved and sub-sovereign finance with a view to making it a key factor driving this process.

Key Issues in Sub-sovereign Leveraged Debt

Several key issues are central to the ability of sub-sovereign finance, including the devolved funds, to leverage community development financing. These issues, framed as questions here include:

- Should devolved funds or sub-sovereign finance be used to leverage or seek debt for local economic and community regeneration?
- Should there be limitations on what the debt should be used for?
- How can we guarantee that borrowed funds are used for public, social and community benefit purposes?
- Who should issue the debt?
- What type of debt is appropriate for purposes of long term capability and asset development finance?
- Are there sufficient credit remedies to secure against default and what would be the consequences of failure?
- Does there exist a rigorous and sufficient disclosure regime that enables creditors assess and take necessary risks?

- In the case of leveraged debt, i.e. debt to other local social enterprise entities leveraged against income to devolved or sub-sovereign entities, is there a predictable and adequate revenue regime to guarantee such intermediation?
- What really are the capacities of these funds to take the complex nature of anticipated financial intermediation?

Devolved funds as leverage for local economic and community regeneration

The practice of devolved or sub-sovereign finance in Kenya thus far has been that funds are simply accessed from the Consolidated Fund and expended on identified and qualifying projects within the fiscal year. Qualifying projects have to be included in the fiscal estimates and approved for the fiscal year. The issue of using devolved funds to secure debt finance for asset-based local economic regeneration from within the larger financial markets, therefore, presents a problematic proposal. Yet, nurturing and maturing such a local debt market is strategically useful for many reasons. From the analysis of the constraints facing the government in raising and actually allocating public revenue to 'social expenditures', it would strategically be useful if the sources of such finance can be found outside of mainstream public expenditure. Devolved and sub-sovereign finance schemes present the best hope for generating a primary and secondary debt market as a source for such finance.

Debt use limitations

We present elsewhere in this study the statutory purposes for social enterprise activity. It will be necessary that debt that is secured through public subsidy goes to provide absolutely necessary and strategic public, social and community benefit goods and services. We have classified not-for-profits and social enterprise purposes designed to help Kenya meet international commitments relating to human rights, women's empowerment and equality, elimination of violence against women, and working to meet the practical and strategic gender interests of socially-excluded and poor women as qualifying purposes.

The type of debt instruments we are proposing are especially useful in financing long term asset finance needs such as financing the capitalization of local small and medium scale enterprise fund portfolios, construction of produce or retail markets, targeted and low income housing, technology and light industry parks, etc. We propose later that borrowing—or the issue of deb—should only be allowed against firm five year—and longer—strategic development plans arrived at through wide, thorough and inclusive, gender-responsive public participation through a statutory community visioning process. Such plans should be the

bedrock planning efforts to drive socially-inclusive and gender-responsive local economic development. It may be necessary to expose such plans to voter or special constituent approval. This can be done through a local plebiscite or a special college system that ensures that all constituent groups are represented. A local electoral college system involving elected representatives of local preferential trade areas, business organizations, women's organizations, etc would be ideal on account of the logistics and costs of organizing a plebiscite. It would also guarantee the gender composition and representation of women.

Such referenda are necessary as borrowing essentially entails committing future income today. It is also important in the event that local councils or social enterprise organizations—such as a producer market—are required to raise charges to meet debt obligation. Involving the community in this way is helpful in biding local development committees even in the event of changes in elected officials.

Anticipated plans would include:

- An assessment of the current social, economic and environmental reality in the community or region
- A gender assessment of the prevailing situation
- Determination of the emergent needs
- An audit of the resources and assets available, including a gender differentiated skill and asset base
- Determination of long-term asset development requirements
- Prioritization of the arising needs in the order of urgency and strategic importance
- Identification of integrated frameworks and goals to meet these needs
- Formulation of strategy to achieve the goals within certain time and other constraints
- Identification of the resourcing needs and gaps
- Proposed implementation schedule and activities and an appropriate monitoring and evaluation regime

Once the plans are passed by the constituent groups' local executive, agencies can thereafter borrow against them without recourse to extensive consultation.

Even within these strategic plans, debt should only be issued to finance social enterprise-based community assets, including institutional assets working to enable strategic asset accumulation by individuals. In particular, debt should target local Community Development Finance Institutions, who should be able

to act as local financial intermediaries for various asset development purposes. These purposes can include helping excluded and poor women acquire critical skills and knowledge, business start up or expansion loan funds, hedge against loss in produce or enterprise, gender-responsive community health insurance schemes, etc. CDFIs can also be useful in channeling resources to local institutions such as markets, cattle dips, hospitals, secondary schools, polytechnics, universities, etc. Furthermore, borrowing should only be allowed to finance a statutory list of social and community benefit purposes. Loans can also be considered to help re-engineer local authorities and strategic social enterprise institutions.

It will be necessary to ensure that borrowed funds are used for public purposes. We made extensive proposals on how to reform the legal, regulatory and institutional regime of actors in the social economy with a view to safeguarding investments made into these institutions for public and social benefit. We propose elsewhere a statutory mechanism, the Social and Community Benefit Asset Endowment Scheme, which will be the central mechanism for issuing schemes that qualify for such purposes.

Issuing of the debt

Ideally, debt should be issued by the sub-sovereign entities such as municipal government and devolved finance mechanisms themselves, such as the constituency office of the CDF, qualifying social economy organizations—such as well established industrial parks or producer/retail markets—regional development agencies and community or area development corporations. The fact that there does not yet exist such a debt market and that these entities, where they exist, have not participated in issuing such debts raises several issues that would need redress.

The first is that these issuers should be market-capable; that is, they should have the institutional complexity to come to the market on their own and issue the debts. Being market-capable involves and requires expansive legal and institutional reform for many of these institutions. It will be necessary, for instance, that they be juridical persons capable of acting in their own legal personality, that they have enough qualified personnel, that they have sufficient income streams to convince market participants of their creditworthiness, etc. In large measure, these schemes should also be encouraged to issue debt in their own names.

It is also important that issuing authorities and funding schemes have capacity to repay the debt without recourse to additional support from the central government. This calls for these schemes to have adequate and reliable income of their own. With some modifications, such schemes as the CDF and LATF with

secure statutory government subventions may meet a rigorous income-based criteria of market readiness. Other schemes such as the HELB and the Community Development Trust Fund may also qualify with some modification. The proposed Regional Local Economic and Community Development Venture Capital Corporations with significant assets and income can also sponsor their own debt instruments. Municipal authorities such as the City Council of Nairobi, Mombassa, Kisumu, Nakuru, Eldoret, Thika, Nyeri and Mavoko, with sufficient fiscal discipline have a revenue base that would qualify them to issue mid and long term municipal debt. Other authorities such as Narok, Isiolo, Embu, Meru, Naivasha, Malindi with technical and fiduciary assistance have potential to graduate to similar status. It would be necessary to offer both general and targeted technical assistance to get all the schemes and authorities to participate in the debt market. Weak local authorities can also team up, incorporate joint schemes, and issue debt collectively. Successful social and community enterprises such as local hospitals, secondary schools and technical training institutions, slaughter houses, producer markets or technology parks can be assisted to pool their receivables into securities that can used to attract debt.[179]

Community Development Finance Institutions as well as the proposed regional, area, local or community development corporations would be excellently placed to pool such receivables into a single security. Given the public, social and community benefit nature of these institutions it would be necessary to enact specific law such as the Social and Community Enterprise Act and a Municipal Enterprise Act that would, among others, work to ensure that the assets and enterprise habit of these institutions are in conformity with their public, social and community benefit purposes and mission.

The conditions under which sub-sovereign finance schemes can issue debt may, however, need to be the subject of statutory legislation. It may be necessary to generate a regulatory regime that can classify the different issues, vouch for their credit rating and prescribe different borrowing powers depending on the credit rating. This would call for the enactment of a specific municipal and sub-sovereign borrowing legislation that would spell out more clearly some of the issues touched upon in this section.

Credit remedies against default

Owing to the fact that the market is non-existent, there are no credit remedies available now for those who may want to lend to Community Development

[179] Daystar University, for instance, recently took out a Ksh 57 million debt with an ecumenical financial intermediary partly to refinance a bank overdraft with Baclays Bank of Kenya. The potential for such debt issues by a social enterprise was also evident in the issue of a Ksh 250 million debt by the IFC to Strathmore University. Micro-finance institution, Faulu Kenya, recently floated a successful Ksh 500 million bond on the Nairobi Stock Exchange.

Finance Institutions through the leveraging of these schemes. It would be necessary that such remedies are available for the scheme to work. Existing and future schemes can be required to:

- Pledge future income or revenue but not exceeding a certain limit necessary to run basic services.
- Pledge the use of their statutory power to set taxes, interest rates and other revenue raising measures to offset debt.

Other devices that should be considered and can prove beneficial to a rigorous credit regime include:

- A well-defined and structured legal regime giving the creditor powers to take over running of affected schemes and social/municipal enterprises.
- Requiring all credit to be backed by ascertainable current or future credit flows.
- Establishment of legal instruments that can assign to their creditors all the interest in specific revenue streams locally or from the central government.

Since majority income for these schemes will issue from government revenue, and granted that these schemes must aid the government's overall fiscal and expenditure measures, there should not be an expectation that that the central government will guarantee their debt. Indeed, for efficiency and strategic reasons, the law should be unambiguous that the government will not guarantee any sub-sovereign debt.

A specific creditor remedy regime that includes some of the measures proposed here would ideally be part of the legislation on municipal and sub-sovereign borrowing. It is crucial, however, that such remedies are not counter-productive and lead to speculative borrowing or lending with the sole object of effecting private transfer of public goods. The creditor remedy regime should also not have the effect of stifling the emergence of purely market-based solutions to the elimination and mitigation of such risks and realities.

The tax credit regime proposed under the Social and Community Asset Endowment Scheme, which is based largely on social enterprise and special juridical financing, is designed in part to hedge against the likelihood of over-exposure to loss by debt-issuing authorities. It is also designed to direct tax credit to secure and well run social enterprise schemes. Under this scheme, tax credit is issued primarily to supply to the development finance requirements of local Community Development Finance Institutions, who would hold a portfolio of investment funds for local enterprises. Such financing would also be backed by mid- and long term strategic local economic development plans, which would

locate the necessity for the financing and work to mitigate and insulate against local and national economic shocks.

Disclosure regime

Increased sophistication in the local debt market and the need to maintain confidence in the operations of CDFIs and sub-sovereign finance institutions calls for sufficient disclosure of critical information by various actors in the debt market. The necessity for disclosure exists at three levels:

- At the debt issuing sub-sovereign finance scheme
- At the level of the sub-sovereign authority backing such a scheme, if at all
- At the level of individual CDFIs and social enterprises for which the debt is issued

Disclosure can be required by the market, by regulatory agencies, by the asset endowment authority, by local authorities and by constituent groups. Disclosure can also be required during such stages as the preparation of an organizational strategic plan, an area-wide or local authority strategic development plan, in lieu of a mandatory investment conference, etc. CDFI intermediaries can be required to make quarterly reports available widely, say, on a website. Disclosure should also be required for social accounts, profiling the social, community and public benefit nature of the proposed transaction and how it furthers stated area, community, statutory and constitutional obligations to further capability and well-being, individual and community asset development, equality, equity, the empowerment of women and socially-excluded groups and holistic inclusive local economic regeneration. Such social accounts should be issued or validated by registered social auditors.

The proposed Social and Community Benefit Asset Endowment Authority should be required and mandated in law to require disclosure and establishment of an authoritative central depository. The authority can also be mandated to sanction a limited number of privately-held depositories to form a systematic and comprehensive disclosure regime targeting all sectors. It can then issue rules and monitor effectiveness of available services.

It is also necessary to maintain a register of debt issues. Registration can be taken up by the Capital Markets Authority or, failing this, the Assets Benefit Authority. Registration should carry detailed and sufficient information about the nature and quality of debt and the conditions for its issue. Such conditions should include performance expectations, social and community benefit objectives, expected milestones and indicators of performance, etc. The Assets Benefits Authority should be empowered by law to audit progress and sanctity

of the social conditions. It can do this by authoring various social auditing regimes and licensing auditors qualifying under those regimes.

There should be a continuing statutory obligation to report on performance of debt issues to the standards stipulated in the issue. Failure to honour such requirements should be met with stiff penalties, including refusal to enter the market on other issues, and possible taking over of the management of the affected CDFI by authorized agents of the authority.

Revenue regime

An adequate revenue regime will be necessary for sub-sovereign finance schemes and the CDFI and social enterprise entities for which the debt is being secured. A revenue regime can comprise of any combination of assured income from the central government, operational cash flow from social CDFI and social enterprise entities and own income by local authorities and area-based devolved schemes. The quality of the revenue regime will be crucial in negotiating interest and income yields of the debt, especially as there are no central government guarantees.

A secure and well structured revenue regime will also be a prerequisite to enable secondary trading in the debt through securitization and derivatives. It may be necessary to place limitations on the use of debt. It would not be helpful for debt to be used to meet recurrent costs. It would also be ill-advised to commit all the anticipated income to secure the debt.

Capacities for financial intermediation

It will be obvious that many of the existing schemes do not have the legal, institutional and human resource capacity to carry out the tasks envisaged here. It is conceivable that with appropriate legislation and regulation, schemes such as HELB, the Development Finance Institutions and the Community Development Trust Fund are capable of generating own capacities and resources. Others, such as the CDF, may need significant investments of technical assistance to bring them up to speed with the new demands and environment.

It will also be necessary to design regional and national infrastructure institutions to help build capacity of the various relatively small devolved units that may want to enter the new development finance market. Such infrastructure institutions can provide core support functions, including bond and risk pooling, co-guarantee funds, debt securitizing agents, etc.

Leveraged Sub-sovereign-Backed Investment Finance

Local authorities at county levels as well as municipal, city and metropolitan councils would be some of the principal beneficiaries of community-benefit linked growth and regeneration. Such growth would lead to more viable local government, a larger tax base and vibrant and productive local economy. It would also lead to a reduced demand for public-funded social services and investments in health, education, workspace, etc. Local authorities have also the most to gain from an excellent human capital, physical and social infrastructure. Local authorities also have the dual role of not only providing or ensuring service provision in their respective jurisdictions, but they also have the responsibility of attracting investments, jobs, new skills and opportunity in these areas. It can be safely put that all local authorities have failed to realize both of these functions. In view of these and other anticipated benefits, there is a need to make local governments a major supplier of strategic asset development finance in their respective jurisdictions.

It will be necessary to ensure that local authority and area-based sub-sovereign finance schemes, such as the CDF, as well as the local authorities themselves take up a significant role in helping the formation of such capital assets as detailed in this study. There are many ways that local authority and area-based schemes help prosper long term capital accumulation for local residents and their communities. We consider the possible use of local authority and CDF-backed debt in the next sections. Later sections will consider other prospects.

Local government authorities should also be encouraged to seek other ways of assisting social and community benefit schemes in their jurisdictions. Such assistance can include guarantees for local citizen-based block grants co-invested in qualifying portfolios held by CDFIs. The Asset Benefit Corporation should vigorously pursue participation of local authorities as partners in local community development.

Social development bonds and commercial paper

The Social and Community Benefit Asset Endowment Authority, through its schemes and the various Regional Community Development Venture Capital Corporations, with the help of the various regional and local economic and community development authorities/agencies should also help local authorities, area-based and functional funds to design appropriate instruments to help them tap into the capital markets. Some of the instruments that these funds can use include the municipal development bond, a social development bond, and other specially designed local economic development bonds. We propose that the Social and Community Benefit Development Authority be authorized by law to design the structure of such bonds, again under its various schemes, where investors

would enjoy tax credits and other benefits in return for their investments in these bonds.

Sub-sovereign funds can either issue municipal, local economic or social development bonds singly, can guarantee such bonds issued in favour of local CDFIs, or can partner with the Social and Community Benefit Asset Endowment Corporation for investment in local enterprises and community development organizations. The conditions and pre-conditionality under which the financial schemes would be able to issue their own bonds should be worked out and issued by the Capital Markets Authority through wide consultation with the sector. The Capital Markets Authority should be expected to issue notice of intention to make rules setting such conditions and to provide sufficient time and resources for input by these and other stakeholders. The considerations for conditionality should include, but not be limited to, proven financial discipline by the sub-sovereign fund/financing scheme, a clear revenue base and target collection by the sub-sovereign fund/financing scheme, a clear and viable investment strategy detailing the income base to finance the proposed bond issue, acceptable economic and investment planning in the affected development zone, and requirements for the local authority and those promoting the bond to conduct exhaustive and all-inclusive public consultations on the need and viability of the bond, including exposing to public input the development and investment programme to be financed by the bond.

The measures here would aim to, among other things, prevent abuse of such bonds by sub-sovereign fund/financing schemes and regional development agencies as well as ensure maximal local economic and community benefit through the ensuing bond regime. The rules should also work to inhibit sub-sovereign fund/financing scheme and other institutions from acquiring debts that they may not service and putting affected residents into a debt spiral. In practice, it will be realized that such bonds can only work in situations where sub-sovereign fund/financing schemes are managed professionally, achieve best possible governance styles and outcomes, and work perpetually to attract utmost public confidence and trust in them.

It is our proposal that since these attributes are so crucial to the future of our urban development and local governance, a specific law should be put in place that provides for issuing of elaborate charters to urban and local councils, including a county council. The charter would spell out the conditions of the issue of a certain status. The law would also establish a statutory agency under the local government ministry to draw up the charter as well as monitor adherence to it by respective local authorities. Nothing in law, however, should bar or stop local authorities from participating in a bond authored by the Social and Community Benefit Asset Endowment Authority.

Sub-sovereign fund/financing schemes can also guarantee commercial paper issued by successful social enterprises wishing to expand their enterprises and with guaranteed income streams. The proposed bill, either through primary or subsidiary legislation, may make it a requirement that guarantee of commercial paper by sub-sovereign fund/financing schemes for social enterprises be done either through the participation of Community Development Banks or arrangements arrived at through other instruments available in the CDFI, such as community benefit LPAs, or through the agency of the Social and Community Benefit Asset Endowment corporation with a view to reducing and spreading the risks to the sub-sovereign fund/financing scheme.

It is also conceivable that various CDFIs may desire to raise capital on the stock exchange as commercial paper backed by the income and competences of various enterprise portfolios they have invested in. We propose that the law enables the Social and Community Benefit Asset Endowment Fund to come to the aid of such CDFIs by authoring schemes that extend facilities to investors in such commercial paper. This aid can include issuing basic guarantees of repurchase to minimize the risks attached to such paper.

Other proposals relating to debt and equity financing of local economic and community development are presented in subsequent sections.

Local economic and community development capital campaigns

The proposals made in this report for alternative Community Development Financial Institutions, once realized, will make possible alternative financial and investment vehicles located in the rural and fringe communities. Community Development Financial Institutions are financial intermediaries dedicated principally to local economic and community regeneration. They offer first class assets for re-investing financial resources in a particular community. CDFI capital appeals through secured certificate of deposits, for instance, can be excellent ways of attracting long term investments into a community.[180]

In addition, the very real institutional investments that are going on by way of rural agricultural savings and credit societies, coupled with the existing employee-based SACCOs, make very real the prospects for alternative financial intermediation in these areas. With some improvisation and under proper regulation, successful savings and credit societies should be encouraged to issue certificates of deposits to non-members, benchmarked on the assets of the SACCO and various member guarantees such as salary intercepts. Already, SACCO societies based on stable agricultural crops such as tea are taking risks with

[180] There already are products in the market, such as the Jitegemee Trust, established as sources of financing for on-lending to candidate CDFIs such as the Kenya Women's Finance Trust and Faulu Kenya.

borrowing from such institutions.[181] Major statutory developments in SACCO and MFI management, regulation and capitalization will make these financial intermediaries safe places to hold capital.

Current and ongoing developments in information and communication technology (ICT) make banking feasible in any geographical environment. With the availability and liberalization of technologies, such as Very Small Aperture Satellite Technology (VSat) and the ongoing investment in national and regional fibre optic network, the costs previously associated with establishing and maintaining a regional and rural banking infrastructure are expected to go down drastically. In the very near future, and increasingly in almost all the major urban settlements in Kenya, it will be possible for one to operate a bank account in a geographic region far removed from ones place of residence. One can, for instance, open a savings account in Kisumu but permanently access the account in Nairobi by use of bank and credit cards. One can also issue a cheque in Nairobi against a current account located in Marsabit. To put it another way, advances in technology make it possible for society today to overcome one of the most insidious distorting functions of money—the amount of money supply available in a particular location—and the ability of local financial intermediation to loan this out to the local population.

It is conceivable that high net-worth individuals can be encouraged to consider relocating at least 10 percent of their savings deposits to alternative financial institutions such as SACCOs and MFIs and CDFIs in fringe areas with the aim of achieving a geographical spread that covers the entire country and also along targeted lines, such as directing money to women lending micro-finance institutions such as the Kenya Women's Finance Trust (KWFT). This would have the effect of ensuring that money is actually available to those in the local economy who need it for their businesses and for every day needs.

Local, area-based and other sub-sovereign funds such as LATF, CDF and HELB would work to co-guarantee the safety of the funds by matching depositor investments in these institutions.[182] They can also provide the financing required to insure the investments financed through such deposits. This measure of using sub-sovereign finance to attract more money to local financial intermediaries alone would significantly reduce the level of financial exclusion suffered by local residents and that is witnessed across the regions without any noticeable economic or financial risk.

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[181] Personal communication from Programme Manager for East Africa- AACC Building, Westlands, Nairobi.

[182] The Family Finance Building Society recently realized over Ksh 900 million by encouraging account holders with the Society to convert savings into equity.

MARSHALLING EQUITY FINANCE TO AID LOCAL ECONOMIC AND COMMUNITY DEVELOPMENT

Ultimately, debt as an asset building or development strategy has its own limitations. Consideration ought to be made regarding whether and how the community development sector, especially those organizations at work in the social economy ought to be enabled to raise equity. If that question was answered affirmatively, then it raises further questions about the prospects for using existing capital markets to raise such equity and whether these entities raising such capital would require reform of the capital markets or raising an alternative capital market for the social economy. Depending on how one answers these questions, the issue then arises about the possible role of the devolved and sub-sovereign finance schemes in enabling such developments. Such considerations also assume that it is indeed necessary to structure such assets in ways that allow equity participation.

In seeking to answer these strategic and important questions, we confine the discussion to actors in the social economy, whom we have opined elsewhere are in reality a much under-valued and under-utilized asset class dedicated solely to efforts to overcome social exclusion, poverty and inequality. It may be necessary, once again, to offer examples of such actors who include well known institutions such as K-Rep Bank Holdings, Faulu Kenya, Kenya Women's Finance Trust, Jamii Bora, Kick-Start (formerly Approtech), and many others. It will be obvious from our proposals on reforming the legal forms available to the social economy that we consider equity participation good and in the greater interests of the purposes served by the sector.

Not-for-profits in Kenya are not structured to attract private or public equity participation and their legal forms usually do not allow or anticipate equity. The proposals made elsewhere on new legal forms, especially the Community Benefit Company, and the Community Benefit Limited Partnership Agreement, the new regulatory regime for actors in the social economy as well as the superior and senior debt proposals outlined above also contain far-reaching proposals on how to secure the not-for-profit and social purposes that govern the sector.

Elsewhere in this study, we also make far-reaching proposals on asset building within the human capital sector—health, education and local workforce development. In these proposals, we advance the view that human capital development should embrace individual development accounts, life long learning accounts and community development accounts that enable individuals and communities to be actively engaged in their own strategic asset development and accumulation. Our proposals on marshalling private equity to grow local economic and community development should be read together with these and other proposals.

Importance of Equity Finance

Equity finance, whether at individual or community level, is a key form of finance in asset-based development. Without equity participation, very little asset development and accumulation would be realized. Equity also serves to provide a basis for ownership and residency even for basic social infrastructure like a water project, school, polytechnic, market or local hospital. Equity is also important for other purposes. Investors in any security value liquidity and can be relied on to pay a premium for shares in assets that have sufficient liquidity. It would be difficult to achieve sufficient liquidity in the stock of social enterprises unless there is a sense of equity participation in them.[183]

Elsewhere, we propose a massive new apex finance mechanism—the Social and Community Benefit Asset Endowment Scheme—to grow community and individual assets and as the central cog in renewed efforts to local economic and community regeneration. Anticipated investment schemes, however, risk stunted growth and uptake without an enabling and thriving secondary market tailored to the sector. It would be difficult to establish a primary or secondary market for capital to drive local economic and community regeneration without significant equity participation by residents and community development corporations in local asset development and accumulation.

In the mid and long term, it will be impossible to avail and mature long term finance for local economic and community development without reforming the capital markets regime to enable participation by qualifying actors in the social economy, especially social and community benefit enterprise schemes and institutions and mutual organizations such as SACCOs. It would be necessary to develop such a secondary market for such shares of social enterprise organizations held by respective fund managers. It will also be necessary to establish market for securities held in the anticipated social development bonds and commercial paper and in the long term superior debt and other investments held by various investment schemes.

Clearly, those parts of the social economy that can legitimately apply equity financing for their growth without compromising their public benefit status should be enabled to do so. The Community Benefit Company and Community Benefit LPA forms enable direct participation of equity in return for investments into the sector. We also expect that the proposed Regional and Local Economic and Community Development Venture Capital Corporations will view a vibrant and appropriately-structured capital market as a prime avenue for realizing value earned in their investments in local enterprises. These corporations will also view

[183] The prospects for such an equities market exist as can be gleaned from committee work of the Nairobi Stock Exchange itself.

the capital market as a good place to raise new capital for their investments in local enterprises. We expect that these will be popular forms and will help the development of the basis for an equities market in the sector.[184]

We consider below the major proposals for how sub-sovereign and devolved funding can aid capital markets reform, including backing new instruments that would enable social enterprises and actors in the social economy to access the market.

Opening a New Social Investment Floor at the Stock Exchange

The Nairobi Stock Exchange presently has two trading floors. In order to open the market to the new institutional asset class envisaged in the social economy, it will be necessary to establish a third tier trading mechanism set up specifically for investors in social enterprise companies and related schema, including the proposed sub-sovereign finance-backed social development bonds.[185]

As MFIs such as the Kenya Women's Finance Trust and Faulu Kenya have shown, investments in socially-excluded and asset poor people have on average similar or higher returns than other investments. While we expect the proposed statutory limitations imposed on these various social enterprise legal forms and instruments to force a strong fiduciary regime in the sector, we nevertheless expect investments in their instruments to be attractively priced above a certain benchmark such as prevailing inter-bank lending rates or appropriate treasury instrument. We also expect returns from these investments to fair just as well as any other.[186] These measures are, however, unlikely to work in the mid and long term without unreserved and all embracing financial discipline from the government.[187] It will be necessary, for instance, for the government and Central Bank of Kenya to work to put a cap on the Treasury bill interest rate. It is

[184] These Venture Capital Corporations will take the shape of Venture Capital Trusts, established principally by government to help drive venture capital financing to back regional and local economic enterprise development. Local authorities or other juridically competent Community Development Corporations and Community Development Finance Institutions can also structure associated Regional Local Economic and Community Development Venture Capital Corporations. Their stocks should be quoted on the stock exchange.

[185] There has been discussion on how to use capital markets, especially the Nairobi Stock Exchange, for social development financing. Many of these, however, do not anticipate or call for significant reform of the capital markets themselves in favour of the mission/purpose nature of social entrepreneurs.

[186] The Faulu Kenya Ksh 500 million bond was priced to compete with other bonds issued by leading private sector holdings, such as East African Breweries and Safaricom. The bond was, however, made attractive by significant underwriting by foreign capital holdings in Faulu Kenya.

[187] Much of the current expansion at the stock market and with private sector credit is attributable to a deliberate low budget deficit by government and a commitment to keep domestic and foreign debt at manageable levels (See the ERS and successive budget speeches).

important that the government works to offer the lowest interest rate in the market so that it is not in competition with other sectors seeking the market to finance their investment needs.

Within the context of larger economy-wide efforts to secure progressive and universal social advancement, it will be necessary to enact a comprehensive Fiscal Responsibility Act that would compel government to work in the long term financial and asset interests, especially of low income and asset poor citizens. A long-term view and commitment to fiscal responsibility is central to efforts to grow assets and capabilities today in ways that do not compromise the potential capabilities and asset holdings of future generations. It is also imperative that assets and capabilities are viewed from a generational perspective so that those born today have stronger and better assets and capabilities in the face of future uncertainties. Unfortunately, government behaviour since independence and especially in the 1980s and 1990s showed no respect for such considerations in design and pursuit of fiscal policy.

We are persuaded that the proposals we have set elsewhere on the use of sub-sovereign finance to leverage social economy debt as well as the Social and Community Benefit Asset Endowment Scheme and the dynamic investment regime backing it will yield sustained pressure on investible resources in the economy. This will in turn eliminate the structural weaknesses in the economy where high interest rates are sustained not by independent market activities but by the credit demands of government.

Equity Participation in Qualifying Social Enterprises

We have called elsewhere for the legal incorporation and substantive improvement of the juridical character of sub-sovereign and area-based finance schemes such as the CDF within a broad and well—defined regulatory regime. Should this be achieved, there is no compelling reason why such schemes should not incorporate trust funds and other investment schemes to enable them take up strategic equity in the proposed new Social and Community Benefit Enterprise Companies. There should not be much reason, for instance, why a sub-sovereign finance scheme run by the City Council of Nairobi should not take up equity holding in an entity such as the Nairobi Hospital, Faulu Kenya, or Kenya Women's Finance Trust, if such equity holdings were possible. There is also no reason why juridically competent Constituency Development Committees should not set up permanent trust funds to help start up and invest in the proposed Community Development Finance Institutions.

The proposed Social and Community Benefit Asset Endowment Authority, through its various schemes or through the agency of other intermediary CDFIs, should also be enabled to participate directly in long term equity investments

with provisions of exit structured especially for actors in the sector, such as an Alternative Public Offering (APO) or private treaty or stock market transfer to the CDFI and other qualifying social enterprises/investors.

Social Investment Angel Finance Matching Mechanisms

Duly incorporated sub-sovereign and devolved funding schemes and the various schemes of the proposed Social and Community Benefit Assets Authority should be required to establish investment matching facilities to enable social angel capital to find appropriate and suitable CDFI-based investments as well as spur a secondary market for trade in the shares of social enterprise organizations and CDFI-backed portfolios.

Programme-related investments

The asset endowment authority should enable a market, through appropriate CDFI instruments and institutions, for such projects by raising benchmarked investment funds and inviting the participation of Programme-Related Investments (PRI) fund schemes held by the sub-sovereign and devolved finance schemes, etc. Devolved funding schemes should also be encouraged to make recoverable Programme-Related Investments, again by way of block funds, in qualifying asset endowment and development schemes.

PRIs can also set up structures with appropriate CDFIs for purposes of participating in the various schemes set up by the proposed apex financing mechanism. This will be useful in helping the participating devolved fund schemes not to spend too much time and expertise as well as ensuring that the paper work and accounting is located within the CDFI. Devolved and sub-sovereign finance schemes should be encouraged to set up own CDFIs for this and other purposes and use the Community Benefit-LPA or the plain LPA form.

Venture capital trusts

We have proposed elsewhere the establishment of designated Venture Capital Trusts (VCTs) as quoted-fund vehicles designed specifically for investors in social enterprise companies and the MSE sector. Constituting part of the instruments and firms available under the Community Development Finance Institutions, they will offer private block investors tax incentives in return for a minimum three year investment commitment. VCT investee companies may face restrictions on what they can do and their future development in order to guarantee the minimum returns set in their issue prospectus and information memorandum.

Venture Capital Trusts will most likely adopt the LPA form either as a Community Benefit LPA if their limited partners are for profits or the more popular LPA for partners already incorporated as not-for-profits. The proposed apex financing mechanis—the Social and Community Benefit Asset Endowment Authority—may make it a requirement for firms to get listing before participating in its various fund schemes.

We have also called for legislative reform to improve the juridical complexity and competences of devolved finance mechanisms. Duly incorporated and self-motivating devolved and sub-sovereign finance schemes present excellent sources of the formation of such venture capital trusts, which can be formed directly by the scheme or preferably by local CDFIs through leveraged finance or assurances provided by a devolved fund scheme.

Alternative public offerings

Many Kenyans are now used to some terminology from the capital markets such as Initial Public Offerings (IPOs), floatation, going public or listing. These are some of the many terms used when a company obtains a quotation on a stock market. An Alternative Public Offerings (APOs) is essentially an "ethical" share issue providing social investors with an opportunity to invest in social enterprises or certified ethical stocks that may be listed on a specially-designed counter or in shares of venture capital firms investing in unquoted social enterprises. Social enterprise companies such as the Kenya Women's Finance Trust, Jitegemee Trust and others offer excellent prospects for the issue of such shares.

APOs would be regulated by the Capital Markets Authority. We propose exhaustive consultations with the CMA and actors in the social economy to establish a regulatory regime appropriate to the sector. It may be necessary to amend the Capital Markets Authority Act to make the establishment of a capital market for the social economy mandatory. Subsidiary legislation with the Capital Markets Authority will establish under what terms a social enterprise can embrace an APO. We expect that to qualify for an APO, investee social enterprises must reach a certain threshold level of growth and financial stability. Investee companies must be judged capable of paying the capped dividend to investors.

Regulations can also require that investee companies demonstrate certain characteristics, including wide memberships/ownership, democratic participation in decision making, superior returns to community, superior performance on other criteria such as environmental governance, etc.

An APO listing would enable investors to invest in a firm without assuming the levels of control that would be typically associated with venture capital and huge business angel finance.

It is conceivable that national universities and polytechnics, regional and national referral hospitals and even health and school districts can be fashioned to list as APOs. It is also possible that infrastructure agencies such the Kenya Medical Supplies Agency (KEMSA), the national drug procurement agency supplying public hospitals, can be structured in a similar way to supply mission ans social enterprise-based hospitals. It is also conceivable that other social enterprises such as sectoral development corporations may want to issue shares through this new social economy window at the Nairobi Stock Exchange.

In order to motivate uptake of APO shares and ensure liquidity in the investment window, devolved and sub-sovereign finance schemes should be encouraged to take up share holding in such entities, especially those that have a strategic value in their local settings.

The law should also require the Capital Markets Authority to facilitate establishment of key capital market infrastructure institutions such as brokerages, investment banks, investment advisors, social audit firms, etc necessary for a competent market in social investment securities. Such investment banks and venture capital firms should be required to draw up a matched investor index, which would match those willing to buy with those willing to sell, or some other arrangement every so many months. Such an issue may be backed or sponsored by interested development agencies/community corporations, etc.

Sub-sovereign finance agencies, regional and national development agencies and community corporations or such other entities should be encouraged to sponsor special rights issues once the APO is settled and the social firm doing well in the market. They can also establish special investment vehicles under any of the proposed forms and guarantee offer to buy shares not taken at prevailing or given rates. They may also offer to purchase such shares at a certain guaranteed rate some time in the future. Regulations can require APO firms to open up their constitutions to enable institutional forums and advisory bodies where investors in these firms can participate and through which they can get a place on the board of the firm.

Strategic Asset Building and Development Venture Capital

Venture capital finance has infinitely superior advantages to other forms of investment financing as it entails attracting significant low cost and long term, mostly equity-based finance to grow a regions wealth. The region is, therefore, less likely to suffer capital flight and to move from a spiral of under-investment. In the long run, directed asset building and development—the type necessary to bridge historical underinvestment—is a risky and tenuous community building strategy and Kenya is unlikely to mature a social economy-based asset development strategy without allowing for seed financing for various asset

development schemes. A good example of this is the Higher Education Loans Board (HELB). The loan scheme presents a possible excellent institutional asset class to finance tertiary education and workforce development. Over the last several years, the scheme has improved loan recovery to Ksh 50 million per month, or Ksh 600 million annually. The loan scheme is mandated in law to establish a revolving fund scheme for onward disbursement of these recoveries to new cases. In reality, the funds initially invested present some type of long term asset-building and development venture capital, the seed finance necessary to build up the fund base. It is noteworthy that the government continues to take up the financing of initial seed money to this scheme.

There exists a lot of room to improvise and modernize the Higher Education Loans Board within the context of community-based and community-specific financial intermediation. Much of this has been discussed elsewhere in this study. In the resulting scenario, the HELB would become a source of financing for education financing within the CDFI schemes. Qualifying CDFIs wishing to set up human capital and workforce development schemes in their jurisdictions would negotiate financing with HELB. Beneficiaries of the CDFI schemes would still be free to attend college or university in any institution that qualifies for a HELB scheme, and not necessarily within the source jurisdiction.

Local sub-sovereign schemes such as CDF, or a specific bursary fund, can help leverage some of the costs to the CDFI of such a loan, making the loans accessible to local participants. Local sub-sovereign schemes can also place Programme-Related Investments with CDFIs that target specific areas in local human capital development, such as women's uptake of health or engineering, thus directing more money into human capital development in these areas.

Sub-sovereign finance schemes such as the Youth Enterprise Development Fund, CDF, LATF and HELB can play a strategic seed financing role, similar to the HELB scheme, in capitalizing a local institutional asset class and structured through the proposed CDFI forms. Such local institutional assets stand to gain the most from the proposed Social and Community Benefit Asset Endowment Scheme.

In principle, all investments enabled and provided for through CDFI schemes and the Social and Community Benefit Asset Endowment Scheme should be recoverable, and should thus take the nature of local economic and community development venture capital. It is necessary to stress especially the principle financing mechanisms or methodology of recoverable grant investments, i.e. grants provided to not-for-profit and public benefit organizations for purposes of endowing their purposes and which grants are recovered from the investment before the endowment is fully ceded to the beneficiary organization, and the more familiar venture capital finance.

In recognition of these statutory limitations on the working of the proposed CDFI-based schemes, it is desirable that the government works to mature venture capital to work for community development. We have also envisaged CDFIs attracting finance and investing in their choice communities through principally venture capital-based arrangements. Through these arrangements, the CDFIs will be free to source investment finance outside the market created by the sub-sovereign finance and Social and Community Benefit Asset Endowment Scheme. This is desirable in part to ensure that sub-sovereign finance and the scheme are not the only active providers of long term community development finance.

Regional venture capital corporations

To help drive independent/alternative development venture type capital into various regions, it is our proposal that the existing Regional Development Authorities, such as the Tana and Athi River Development Authority, Lake Basin Development Authority and others be converted into Regional Local Economic and Community Development Venture Capital Corporations with the mandate to mobilize long term finance and invest it in viable and qualifying enterprises in communities within their respective jurisdictions. The revitalized corporations will, therefore, work to ensure that enterprises in their respective jurisdictions, regardless of the capital requirements, can get the finance needed for their growth. These corporations can also co-invest in successful establishments that began as investee portfolios of the proposed CDFIs but which now desire broader capital participation to grow beyond their original aims and scope. The Regional Local Economic and Community Development Venture Capital Corporations would participate in such establishments primarily with a view to maturing them for an IPO at the Nairobi Stock Exchange or other such appropriate exchange.

It is anticipated that part of the Regional Local Economic and Community Development Venture Capital Corporations core investments will be in enabling social enterprise-based infrastructure in core areas necessary to aid widespread growth of various sectors in a region's economy. Such infrastructure can include construction of processing industries for meat/fruit/vegetable, producer and retail markets and associated warehouses, specialized workspaces for various light industries, and appropriate low cost housing parks, etc. These venture capital corporations can and should be required to recover their investments through a combination of options, including APOs, IPOs and securitization of income from these investments.

Regional Local Economic and Community Development Venture Capital Corporations (and not Regional Development Authorities) should also be empowered in law to issue bonds on the stock and securities exchange backed by their own income and assets. These bonds should be issued to enable financing

of investments identified in broad consultation, and especially in line with the strategic plan developed by the Regional Development Authorities. The Community Development Venture Capital Investment Corporation should be expected to satisfy its own and other investment criteria to ensure that all investments are sound, including the amelioration of investment risks by other agencies and, where applicable, schemes of the asset endowment authority. In this respect, a Regional Community Development Venture Capital Corporation is not required to invest in enterprises identified by the regional development authorities unless they are convinced of the viability of these enterprises.

The above arrangement and prospects have the very significant contribution to the proposed CDFI fund schemes as it would guarantee investors in successful enterprises an exit strategy keyed to an IPO/APO. The proposal would also help secure the liquidity of the CDFI-based community investment market. It will also ensure that, eventually, the establishments generated through these CDFI fund schemes become available for wider public participation.

Derivatives, futures, options and community development

Ultimately, ensuring that no citizen, group, community or region is left behind by the prospects and benefits of a creative and genuinely gender-responsive and inclusive local economic growth and continuous regeneration calls for solutions that go beyond current structural limitations within the Kenyan financial markets (including the sub-sovereign funds). With the ongoing consolidation and sophistication of the local capital markets, Kenyan investors will soon be able to explore opportunities offered by options, futures and other derivate markets. The Capital Markets Authority, for instance, recently issued draft rules to enable the development of a securitization industry within the local capital markets. The Nairobi Stock Exchange is also discussing prospects for developing a Commodities Exchange in two years time.

Potential exists for the kind of contracting arrangements under a successful futures options and other derivative market regime to drive a gender-responsive asset development regime that would be the cornerstone of socially-inclusive local economic and community regeneration. To ease discussion and comprehension of this potential, an understanding of what options, futures and other derivative markets is essential.[188]

[188] Much of the literature for this section has been sourced from Bodie ZVI, Kane Alex and Marcus Alan J. (1999).

Options market

An *option* refers to a contract that gives its holder the right to purchase an asset for a specific price—called the exercise or strike price—on or before some specified expiration date. A 15th December call option with an exercise price of Ksh 300 on the recently issued KenGen shares entitles the holder to purchase KenGen shares for Ksh 300 at any time up to and including 15th December. The holder is, however, not obliged to exercise the option. It will only pay or make sense to exercise the call only if the market value of the asset is in excess of Ksh 300. When this happens, the holder can sell the option and realize a profit. If a call option is not exercised before the expiry date on the contract, the option simply expires.

Sellers of call options—referred to as call writers—receive premium income now as payment against the possibility they will be required at some later date to deliver the asset in return for the exercise price, which conceivably will be lower than the prevailing market prices. This premium represents the purchase price of the option and is the compensation the purchaser of the call must pay for the right to exercise the option if exercise becomes profitable. If the option is left to expire because the excise price remains unfavourable to the holder of the call option, then the writer of the call clears a profit equal to the premium derived from the sale of the option.

On the other end of the spectrum is a *put option,* which gives the holder the right to sell an asset for a specified excise or strike price on or before the expiry date. A 15th December *put option* on KenGen stock with a strike price of Ksh 300 entitles its owner to sell the stock at Ksh 300 any time before the 15th of December. It will only make sense to exercise this option if the asset sells for less than the exercise price. If the KenGen stock were trading at Ksh 200, the holder of a put option can sell the option to clear a Ksh 100 profit by purchasing it at Ksh 200 and delivering it to the put option writer at the exercise price of Ksh 300.

A *futures option* gives the holder the right to buy or sell a specified futures contract using, as a futures price, the exercise price of the option. In this scenario, supposing Wakulima Market is a social enterprise organization in which participating traders can purchase farm produce collectively through the market corporation, the market can offer a firm price for beef to a producer market in Marsabit. The contract would specify that Wakulima Market will buy specified quality and quantity of beef at Ksh 50 a kilo in December. This would help beef farmers in Marsabit predict how much their stock will be worth then.

Futures market

Futures and Forwards contracts are similar to options in that they specify purchase or sale of some underlying security at some future date. The key

difference is that the holder of an option to buy is not compelled to buy and will not do so if the trade is unprofitable. A futures and forward contract carries the obligation to go through with the agreed upon transaction. A forward contract is thus, essentially, a commitment today to transact in the future.

A futures contract calls for the delivery of a commodity at a specified delivery or maturity date for an agreed upon price, called the futures price, to be paid at contract maturity. The contract specifies precise requirements for the commodity. In the case of agricultural commodities, a commodities exchange sets the allowable grades (qualities and quantities) and specifies the place and means of delivery.

Delivery of agricultural commodities is made by transfer of warehouse receipts issued by approved warehouses. Thus, a producer market in Marsabit can deliver produce to an approved warehouse in Marsabit and electronically deliver the warehouse receipts to Wakulima Market in Nairobi. The warehouse at Marsabit may be linked or owned by a social enterprise-based abattoir, which may then process the produce for delivery to the market at Wakulima. In the case of financial futures, delivery may be made by wire transfer while delivery of an indexed future may be accompanied by some cash settlement procedure.

Because the futures exchange specifies all the terms of the contract, the traders need only bargain over the futures price. A trader taking a long position commits to purchasing the commodity on the delivery date. A trader taking a short position commits to delivering the commodity at contract maturity. The trader in the long position is said to buy a contract while one in the short position is said to sell a contract. In reality, however, there is no buying or selling as all parties enter a mutually-binding contract. Money only changes hands on the delivery of the commodities.

Futures trading can make significant contribution to agricultural and industrial development. Futures trading can also make significant contribution to the development of certain forms of social enterprise, such as trade in commodities made by social enterprise companies employing and meeting the needs of ex-convicts, persons living with chronic illness such as cancer and HIV/AIDS and persons who have suffered chronic social-exclusion.

A futures agreement can be traded at an exchange. A group of ranchers in Marsabit can trade their futures contract for cash following certain rules established by the commodities exchange. The ranchers can also approach a bank for credit on the strength of the contract. The bank would, therefore, acquire a charge on the contract. This kind of financing can be crucial to unlocking and deepening agricultural finance institutions such as the Agricultural Finance Corporation (AFC). CDFIs can also use the contracts and market that emerges in these instruments to develop viable investments into various communities.

It is also conceivable that once these institutions mature, with the development of an appropriate legal framework, they can be replicated across the wider Eastern and Horn of Africa region under the auspices of such regional organizations as the East African Community (EAC) and the Inter-Governmental Authority on Development (IGAD). Not only would this go a long way in securing trade and industry within the region, it would provide the legal and institutional framework to rise to challenges presented by drought and under-development in the region.

Potential also exists for this kind of contracting to be used to consolidate and grow service sectors such as tourism as well as the farming of especially export crops such as flowers, fruits, vegetables, as well as tea and coffee. It is conceivable, for instance, that women farmers working through a social enterprise organization or their own cooperative society can be contracted to supply certain types of flowers, fish, eggs or vegetables to a social enterprise company-owned warehouse, which then delivers the flowers to certain markets in Europe or to exporters in Nairobi. It is also conceivable that women weavers on the shores of Lake Turkana can contract with a textile firm to supply a particular product for export under AGOA at a future price. Once the contract is made, the women through a local CDFI can go to a securities exchange or a bank and liquidate the asset for cash to develop facilities they need today.

Futures trading clearing house

When an investor contacts a broker to establish a futures position, the brokerage firm wires the order to the firms trader on the floor of the exchange. The floor trader then seeks a dealer willing to accept the terms of the deal. Once a dealer is found, the trade is recorded and the investor is notified. At this point, the deal is brought before the clearing house—a legal corporation established perhaps in conformity with rules issued by the Capital Markets Authority, which executes the contract on the one hand with the investor and on the other with the producer. The clearing house is then obligated to deliver the commodity to the long position and to pay for delivery to the short position, effectively assuming the role of trading partner of each trader. In this arrangement, an investor based at Wakulima Market can contract a farmer's cooperative trading through Saku Market in Marsabit to provide commodities to the investor at a future price without having to go to Saku in Marsabit. To effect the agreement, the clearing house will require certain legally-binding irrevocable guarantees from the farmers' cooperative or Saku Market and the Wakulima Market as it has undertaken an irrevocable guarantee to deliver on both sides of the agreement.

Securitization

Securitization refers to the act of pooling loans for various purposes into standardized securities backed by those loans, which can then be traded like any other security at a stock exchange. Within the financial intermediation proposed in this study, it is conceivable that successful CDFIs would want to securitize their investment portfolios to achieve capital to make further investments. It is conceivable that the Kenya Women's Finance Trust can securitize various mid-term loans it may make to women groups. It then proceeds to sell this security at the stock exchange and uses the funds so realized to make other loans.

Sub-sovereign finance, acting together with the proposed Social and Community Benefit Asset Endowment Authority, can play powerful enabling roles in making such securitization possible. Sub-sovereign finance can, for instance, simply offer to buy such securities once offered, thus ensuring that a market exists for the instrument. Sub-sovereign finance can also offer to leverage the security by offering to discount it so that it is issued to the market at a discount.

It will also be necessary that the law empowers sub-sovereign finance schemes and the proposed Social and Community Benefit Asset Endowment Authority to expend resources to nurture the development of infrastructure organizations and physical infrastructure, such as producer markets and warehouses necessary for the take off of a futures, options and other derivatives market. Through its strategic plans, the sub-sovereign schemes and authority should commit to establishing and growing schemes that: 1) Finance the establishment of social enterprise-based markets, warehouses, industrial parks and workspaces, etc; 2) Finance the establishment of a social enterprise-based clearing house for trading in futures; 3) Establish schemes to finance investments by CDFIs in farmers and local enterprises holding futures type contracts, including local hotels, farmers groups, and social enterprise-based local utility companies in electricity, and information communication technology.

UNPACKING THE INFRASTRUCTURE FUNDS AND PUBLIC PROCUREMENT TO DRIVE SOCIALLY-INCLUSIVE LOCAL ECONOMIC AND COMMUNITY REGENERATION

Public Procurement, Social Exclusion and Women's Strategic Gender Interests

The public sector is by far the largest consumer of goods and services in the economy, with an annual procurement budget in excess of Ksh 150 billion. A large proportion of the money granted to devolved and sub-sovereign funds is indeed tied to procurement. The CDF Act requires that only 3 percent of the funds allocated be used for recurrent and administrative services. LATF are released against specific service delivery plans, which require 50 percent of the money to be used largely for capital projects. These requirements follow from the widely held view that development obtains from such capital investments. In this vein, much of the allocation to the CDF, for instance, has been used for infrastructure projects such as water projects, constructing health and education facilities, and rebuilding roads and bridges.

Normative policy approaches will view these expenditures as being socially-inclusive, non-discriminatory, gender-blind or gender-neutral, intended to benefit entire communities. It may actually be shown that socially-excluded groups and individuals will be the first line beneficiaries as expenditures related to key infrastructure projects such as water and health, for instance, go to redressing core gender-based activities, freeing up time and labour that would otherwise have been expended fetching water or trekking long distances to hospital. Improved medical facilities also significantly aid women's health by increasing safety during pregnancy and childbirth. Readily available and clean drinking water is a boon to infant health and greatly reduces women's work in the care economy.[189]

Such arguments, while true, serve to mask other equally significant and heavily gendered realities—that men are more likely than women to benefit from the procurement regime fuelled by the construction and attending activity occasioned by these projects. The immediate beneficiaries of public procurement are actually those who supply the goods and services. In a situation where about 20 percent of the population own and control 80 percent of the country's productive

[189] A recent study by the Society for International Development (see SID 2007) on gender budgeting and the CDF makes precisely such a claim.

capacity,[190] this means that a lot of the expenditure on procurement will go to these 20 percent. A good case for this arose with the implementation of the Universal Primary School Education, popularly referred to as Free Primary Education. Much of the resources in the scheme are used to procure books, stationery and other materials necessary to effectively mount the curriculum. In many places, the Free Primary Education has been augmented by the construction of much needed physical facilities through the local CDF.

Clearly, public procurement is one of the avenues that can be creatively employed to redress social exclusion, inequality and extreme poverty. At a practical level, procurement can deliver immediate short and long term employment and income to local residents and can be crucial to helping drive local economic and community regeneration. Within a capability and asset-building framework, creative and far-sighted procurement by public agencies can be key to nurturing and developing core local assets and capabilities. Is a municipal authority procuring engineering services for local road construction merely interested in an excellent road network, or can it bundle the procurement budget with other objectives so that through the same tender it procures increased participation of women in technical areas of local public works? In the latter case, the municipal authority would award the tender not only to a construction company with a solid reputation of doing the job, but also to one that has significant presence of local female residents in its technical staff, or at least one that makes an explicit commitment to hire such.[191]

The primary question in making procurement serve the immediate and longer term interests of socially-excluded communities and local economic regeneration is not how much money but what it does, who it pays and what for. There is clearly a need to view the procurement process under the sub-sovereign and devolved fund schemes, as well as the entire public sector, with a little more creativity from being a heavily regulated and mechanical process to one capable of delivering real money and wealth to local communities and groups. When we use devolved funds to build a police post or station we hope to improve local security, but can local security be obtained via other means, such as helping resettle/reintegrate ex-convicts?

There is clearly a need to rethink and situate the overall public procurement regime within the framework of solving the nations most urgent problems relating to social exclusion, poverty and inequality. A commitment, for instance, to procuring goods and services from providers working with or representing the most socially-excluded and deprived areas can result in significant transfers to

[190] UNDP Human Development Report 2006.

[191] The legal validity of such contracting has been confirmed in European jurisdictions by the European Court, which has ruled variously that local and municipal authorities are within their rights to impose such criteria as may provide them with the best economic value.

such communities per year. This is beside the obvious benefit of helping residents and communities acquire key skills and competences to come into the mainstream of the national economic process. Under the schemes we propose elsewhere, the government can, for instance, decide to award a major computer procurement programme to an industrial park where a local university is working with youth from a slum to assemble the computers.

The benefits of such a procurement regime cannot be gainsaid. Gender-responsive procurement, for example, will be crucial to delivering jobs and crucial skills to women. Gender-responsive procurement is beneficial to women even in simple cases such as the purchase and distribution of relief food, which can become a prominent activity in the face of a drought such as happened in 2005. In majority of the cases, the contract to supply will be won by male-owned or led enterprises, the distributing bureaucracy such as the provincial administration would be predominantly male and the male head of a particular household may have a dominant decision making role over what happens to the relief food once it gets to the house. On the other hand, the woman will bear the cost of accessing the food and preparing it.

At a more strategic level, women entrepreneurs can gain immensely from increased and equitable participation as independent contractors in the local, regional and national procurement process. Success in sourcing public procurement contracts will be crucial to growing women-owned enterprises, or enterprises that are run for social purposes such as providing skills and opportunities for single parents, ex-convicts, persons living with HIV/AIDS or persons suffering certain types of physical impairments.

Rethinking the procurement and public sector contracting within the context of socially-inclusive local economic regeneration may involve adopting a detailed pro-inclusion, pro-women and pro-poor public procurement regime that enshrines the rights of socially-excluded and poor groups to partake and benefit from the procurement process. It is, therefore, important not only to see a new hospital or road, but to demand that that the very process of procuring and delivering it brings added value to the community by acting to heal social inequalities by aiding strategic assets and capabilities acquisition by socially-excluded individuals.

Creatively re-thinking procurement provides a fine huddle over some of the challenges confronting area-based devolved and sub-sovereign funds, and how to use their facilities to supply employment and income support to deserving and neglected local groups. There is no reason why construction of a bridge should not provide a fine opportunity to equip local women engineering graduates with the skills and opportunity they need to start off in life. The construction and periodic maintenance of water pans and dams can provide local women groups and social enterprises with a much needed source of income and workforce

development opportunity. This in turn can lead to lower crime rates and a reduced cost for future public works as the skills developed remain available locally.

Community Benefit Agreements/Partnerships in Public Sector Contracting

Community Benefit Agreement (CBA)/Partnerships have been used elsewhere, especially in the US and Europe, to change the shape and face of public sector procurement especially for large infrastructure projects to ensure that the public procurement regime has defined and lasting benefits to a community and its members.[192] Community Benefit Agreements/Partnerships are legally enforceable contracts signed by community groups and a developer or contractor and setting forth a wide range of community benefits that the contractor agrees to provide as part of public sector contract/construction project or development. Within the contract, a contractor agrees to shape a project such that it provides certain benefits deemed essential by the community, such as recruiting labour from long time or previously unemployed residents. Such criteria can be factored into the call for a tender, which ensures competition even for the best methods to respond to the public/community interest aspect of the procurement. Alternatively, where this was not set as a condition in the call for tendering, a community can promise to lobby for and support the particular development/project with government and, in our case, executives and decision makers within sub-sovereign and devolved finance schemes.

The negotiation for a Community Benefit Agreement and the actual contract itself provides opportunity for the community and large capital holding institutions, such as construction companies, to come to the aid of a community's immediate and long term interests, other than those that may be served by the particular infrastructure project. It is conceivable that the base site for a road construction company can be done in such a way as to deliver basic infrastructure for a major health facility once the contractor moves out of site. A contractor can also be persuaded to help pull crucial infrastructure such as water and electricity to a key market as part of the road construction work. Contractors can bide to paying certain wages, providing equitable employment for men and women on the project, facilitating local banking by opening accounts with local financial intermediaries, and using local materials and labour, etc.

CBAs are also good evidence that national and regional governments as well as independent contactors value the local economy, the very reason for the infrastructure investment in the first instance, and are willing to use every

[192] See, for instance,Puttner G. (2003) .

opportunity to drive new money into it. By ensuring that significant income, physical and human capital assets are used in the local economy, Community Benefit Agreements provide key catalysts of jumpstarting local economic development.

CBAs provide opportunity to stretch debate and monitoring of public sector procurement and service provision by transforming local groups and communities into active participants and beneficiaries in the procurement process. Besides being beneficial for its own sake, this local stakeholder involvement has the added benefit of opening up the public procurement regime, making it more transparent and reducing the role of corruption in the award of tenders.

Where the physical infrastructure involves amenities such as sports complexes, shopping districts, housing units, etc the benefits can be considerably more— including the nature and gender composition of anticipated tenants, businesses, etc.

For CBAs to work, procurement entities, local communities as well as devolved and sub-sovereign funding agencies should be encouraged to call for them and include them in their evaluation criteria for awarding contracts. CBAs should be compulsory in situations where the government or public are subsidizing the construction of a particular facility. The same can be achieved for the larger public sector contracting. In this case, the CBA becomes enforceable by the agency that is awarding the contract. It will be necessary to set in place the civic community development infrastructure referred to earlier and that enables independent citizen groups to come into the local economic development process. It may also be worthwhile to create certification or accreditation for procurement agencies that would brand contractors and service providers as meeting minimum elements of socially-inclusive local economic regeneration, including a commitment to engage comprehensive community benefit partnerships and agreements, local value engineering in manufacturing, etc. The Roads Fund, with an annual kitty in excess of Ksh 15 billion, presents an excellent opportunity to try out community development partnerships in the road construction business.

Value Engraining through Social Accounting and Auditing

We have made proposals elsewhere for the establishment of a national social accounting and auditing framework, especially targeting social economy-based institutions. Social auditing and accountability brings new value to the practice of firms and institutions as they seek to reform their practices to deliver higher social and environmental benefits. Once national standards and institutional mechanisms are in place, there is not much reason why local communities and the central government should not require that the public procurement process

comes under increased scrutiny through consistent social auditing and accountability. Procurring entities can require reports of the measures contractors propose to make to maximize the social and environmental benefits of their works as well as measures they will take to safeguard existing standards achieved in industry. To be useful, these proposals should have the seal of authority of certified independent social auditors.

JOINING UP: TOWARDS AN APEX INSTITUTIONAL AND FINANCING MECHANISM

SOCIAL AND COMMUNITY BENEFIT ASSET ENDOWMENT SCHEME

One key prank of our recommendations is the necessity for joining up. It will be difficult to carry through the kind of capability asset-building we have envisioned here without significant joining up of efforts in this direction. Yet, it is also desirable and practical that such joining up does not take away the independence and own agency status of the various devolved and sub-sovereign finance schemes. It is also imperative that the joining up has the effect of enabling the realization of the various strategies needed to bring more finance to the project of helping socially-excluded citizens, groups and communities acquire the asset base necessary for them to get even and get ahead. Earlier, we identified the creation of an institutional mechanism called the Social and Community Benefit Endowment Scheme as ideal for the purposes of such joining up. The scheme will be established with the sole purpose of helping under-served and marginal individuals, groups and communities across all the regions overcome poverty, social exclusion and inequality by principally aiding their long term asset development and accumulation by investing in CDFI-based schemes in those communities.

As an institutional mechanism, social enterprise CDFIs have demonstrated that there is great potential to advance these purposes. The scheme will also provide grant-based investment income to non-enterprise-based not-for-profit organizations working for these purposes in these communities. We have established that one of the most enduring efforts to rid poverty, social exclusion and inequality is to drive high quality capability and asset-based investments and investment financing into poor and under-served communities, targeting especially historically-excluded individuals and groups in all the regions of the country.[193] These investments should be made solely with a view to helping these individuals, groups and communities to acquire a critical capability and asset mass necessary to secure their individual self and strategic development. Such capability and asset-building are in essence a primal pre-condition for personal and community growth in these regions. This type of asset development will spur other economic activity, enabling more and higher profile employment opportunities, consolidate future asset accumulation, enable an increase in local purchasing power and ultimately lead to a higher GDP and tax base across the board in the region.

[193] There is much old wisdom to recommend this ‘new’ thinking, including the experiment with Black Economic Empowerment Programmes in South Africa, a variety of venture capital funds and finance mechanisms in the UK targeted to deprived areas and the Community Re-investment Act in the US, the Solidarity Fund in Quebec Canada, the Grameen Bank in Bangladesh, among others.

The new wealth base will be crucial to the survival and prosperity of local government authorities, enabling them to offer sustainable and superior services and ultimately ease the burden of liability for such services from the central government. We consider that it is the duty and obligation of government to stimulate new private sector and social enterprise-based investments in these regions.

Within the context of decentralization or devolution, the Social and Community Benefit Endowment Scheme sets a framework for driving massive investments to all regions and communities in the country and thus secure the livelihoods of individuals and communities in these regions. The framework seeks to ensure that the country actually grows from its foundations, as opposed to growing from the center and a few other places, and rises to be a splendid community free of extreme poverty, inequality and social exclusion. The scheme, taken together with the other proposals, will ensure that Kenya grows at rates in excess of the fabled 10 percent GDP, in a sustainable (gender and socially-inclusive) manner and for the long periods necessary to lift the country to the status of a wealthy, economically and politically stable country. In the view of this study, the government and all of society must seize the initiative captured in the proposed scheme.

The scheme comprises a series of tiered funds and matching or corresponding financing mechanisms directed at the four principal asset-building strategies identified in the study:

- Building widespread progressive and universal individual development accounts, preferably commencing at birth
- Enabling the prosperity of an institutional asset class driving inclusive and gender-responsive asset-based local economic regeneration
- Modeling institutional arrangements within core public and private sectors to respond to the asset-building potential and requirements for poor and socially-excluded citizens and communities
- Enabling and driving a system of asset-based local economic and community development grounded on progressive and equitable application of Community Development Accounts.

Social and Community Benefit Asset Endowment Authority

The Social and Community Benefit Asset Endowment Scheme should be administered by a statutory authority with powers and structure designed with a view to securing its independence from the day to day running of government, political, business or other vested interests. The authority should be answerable to parliament, with a parliamentary committee calling for nominees and sending

them to the president for appointment. The authority should also have its own budget and be able to charge the consolidated vote directly for its expenditure. The authority should be led by competent commissioners, taking care to ensure gender parity—at least 40 percent representation of either gender and broad regional make up. The authority should be headed by Commissioners, but with an executive commissioner who takes the role of chief executive officer. Other senior officials, especially directors of various schemes and functions, should be appointed by commissioners following competitive recruitment.

To secure its independence, commissioners should enjoy security of tenure of not less than seven years, renewable once. The commissioners would be responsible for setting up various schemes, which would be sent to the appropriate minister and parliamentary committee for presentation to parliament. The authority should be subject to periodic social and ethical audits and should publish annual plans and reports as part of its accountability to the public.

Statutory Purposes of Authority

The statutory purposes of the Social and Community Benefit Asset Endowment Authority should be to:

- Develop and make operational a national index on well-being and human development based on the capability approach to human well-being and development
- Develop and make operational a national social exclusion, deprivation and vulnerability index based on a comprehensive mapping of freedoms, endowments and assets held at individual and community levels
- Identify from time to time key institutional and other constraints at the heart of driving social exclusion, inequality, poverty and other social vulnerability and identify key areas and programmes of reform necessary to enable these institutions work for the well-being and development of all members of the community
- Use resources at its disposal, and work through a gender-responsive asset based local economic and community development to supply the financial and economic drivers necessary to accentuate capabilities, functionings and well-being of all citizens with a view to securing an evolving minimal capability and functional threshold necessary for each citizen to realize their basic human rights and a quality of life befitting of citizenship
- Designate various local economic and community development regions and zones for its purposes

- Identify and work principally through independent social economy-based asset building for individuals, households and communities in under-served groups, regions and communities
- Build and enhance strategic national and local capacity for the capability and asset-based building frameworks for local economic and community development
- Build and enhance national and local capacities for participatory social accountability and auditing
- Build and enhance strategic national and local capacity for social and community investing

Through the scheme, the authority will reduce aspirations for basic economic and social rights into a basic capability set and functionings threshold and identify an investment and asset-based development framework and provide instruments for their realization through investments in qualifying actors in the social economy. These basic rights include:

- Right to attainable standard of physical and mental health as evidenced by access to quality and affordable medical services, sanitation, clean water, etc
- Freedom from hunger and access to safe and nutritious food
- Access and ownership or control of a safe, secure, habitable and affordable house
- Right to asset and income opportunity, including acquisition of strategic assets, wage employment, fair wages and a decent standard of living for self and family
- Freedom from unemployment
- Life long access to quality basic, technical and tertiary education
- Social security, a guarantee of the means to secure basic needs and services
- Personal security and a life free from abuse and violence
- Cultural life and community with others—opportunity to partake in the cultural life of community and to equality of participation and benefits in the making of community

The authority should be required to institute a comprehensive investment scheme allocating tax credit, tax waivers, and other resources to qualifying social economy-based formations, including CDFIs, community enterprises and other community benefit entities in designated local economic and community development zones. The authority should be authorized to work with other

development finance institutions, including devolved and sub-sovereign finance schemes, in promoting its purposes.

The authority should be subject of a parliamentary and stakeholder oversight hearing. The effect of the regulatory oversight hearing would be to audit the achievements of the scheme and not obstruct its investments. The authority should, therefore, present annual reports to an appropriate parliamentary committee, which should discuss and make recommendations to the scheme. If it so wishes, the committee should be enabled to raise substantive issues to be brought before parliament. Parliament should be restricted in law to order an official investigation into the matter for its own action.

Financing Mechanisms to be Incorporated under the Scheme

The principal instruments of the authority should be the design, institution, allocation and administration of a Community Investment Tax CreditScheme,[194] an Independent Development Account Tax Credit Scheme, and various Dedicated Special Purpose Finance vehicles and connected instruments. Every year, the authority would be required to present to the Minister of Finance an investment plan indicating proposals for the use of these instruments, potential improvements and design of new revenue raising measures, and propose specific amounts to qualify for the tax credit, tax exemptions and other instruments of the scheme for the year.

Individual development account tax credit

The authority should, through rule making and respective presentation to parliament, design and publish the following and other universal and progressive Independent Development Account Schemes:

- Universal Children's Savings Account
- Universal Life Long Learning Account
- Targeted, means-tested Kick-Start Independent Development Account
- Targeted, means-tested Retirement Benefit Accounts
- Targeted, means-tested Independent Accounts for vulnerable communities of interest

[194] Tax credits reduce the tax liabilities of individuals or corporations in exchange for their contribution to or participation in a designated activity. These credits have the effect of reducing state taxes owed by the taxpayer by the stated amount often capped per contributor.

The authority should make initial and continuing down-payments to specific individual development account schemes through funds realized from designated special purpose finance vehicles. Local sub-sovereign and devolved funds should be free to make targeted or generic contributions and grants to Individual Development Accounts (IDAs) schemes in their jurisdictions. CDFIs are also encouraged to make contributions to IDA fund accounts from their operating surpluses. The IDAs should be drawn down for purposes and in ways that are contained in the applicable statute and should relate specifically to the asset-building potential of identified individuals.

Qualifying individuals should operate accounts jointly with qualifying social development personnel from designated community benefit entities. Community Benefit Entity should get capacitating grants from the authority and other partners in the scheme.

The IDAs will be held as real accounts in qualifying Community Development Finance Institutions. CDFI entities should institute designated fund managers for Independent Development Accounts within their jurisdiction. The managers and CDFIs will be expected to take responsibility for the fiduciary decisions they take with respect to IDA-specific fund allocations. Fund managers and CDFIs should ensure that IDA funds are invested in instruments that deliver above average market returns. As far as is practicable, CDFIs should ensure that IDA funds investments are realized within local and regional communities. This latter requirement should not override the necessity to realize the best possible returns in the national market. IDA funds should be invested using economically-targeted and social investment criteria. CDFIs are expected to establish a trust fund and hold escrow accounts reflecting the particular details of each account holder.

The Individual Development Account Tax Credit will be enjoyed by corporations who make contributions to designate Individual Development Account schemes. The Individual Development Account Tax Credit is to be set using criteria that makes it broadly appealing to corporations. Specific criteria can include:

- Deferrable—can be portable within a range of, say, three years;
- Transferable—allow corporations to qualify by engaging in eligible activities but transfer the credit by selling them to non-participating entities that fit certain descriptions and need to reduce their tax liabilities.

We propose a 50 percent tax credit for IDAs capped at an appropriate figure, say Ksh 50 billion annually, and to an individual corporation contribution of say Ksh 100 million. This would generate an additional Ksh 50 billion of IDA savings annually.

Community investment tax credit

The proposed Social and Community Asset Endowment Act should establish a tax credit scheme that offers investors in qualifying authority endowment schemes up to 15 percent tax relief credit for Pay As You Earn (PAYE)-based investments and 10 percent credit for qualifying corporate investments. The law should require that PAYE-based investors take priority over those pegged to the corporation tax, with the effect that over 65 percent of all the investments are taken up by the former.

The minister should be required to allocate a special investment window — pegged at not less than Ksh 50 billion or 25 percent of the overall development vote, whichever is higher, every year, which should contain the upper ceiling of the tax credit allocation for the year. In considering the size of the special investment window, the minister will consult primarily the Social and Community Benefit Asset Endowment Authority, which should be required by law to establish a strategic framework for investments in the various regions and communities. To do this, the corporation should call for investment proposals from CDFIs and schemes in each of the various community development zones. CDFIs have, as part of their mandate, exhaustive local asset development and technical assistance to social and community enterprises and small and medium enterprises in their various jurisdictions. The authority should be required to organize investment conferences in each of the regions to establish an asset development and investment culture and market specific to the regions. Once it has pre-qualified various investment funds proposed or in force by existing CDFIs, the authority should then license fund managers in these schemes to raise investment finance against the allocated tax credit. Fund managers should have up to three years within which to draw down all the funds allocated through the tax credit.

Under the scheme, every Ksh 100 investment in qualifying funds would get a Ksh 15 or 15 percent tax credit for PAYE-based investments. A Ksh 50 billion tax window, being 15 percent, would therefore attract another Ksh 283 billion to tally approximately Ksh 333 billion. Assuming that our proposals for 26 community development zones are in place, the Asset Endowment Authority would be required by law to ensure that 50 percent of the realized funds are distributed equitably in all the 26 regions. This alone would give about Ksh 6.0 billion for investments in each of the 26 community development zones. The law would also require that 25 percent of the remaining 50 percent (Ksh 141 billion) be allocated to the bottom half community development zones, using affirmative action criteria pegged to incidence of asset poverty measured at county levels or lower. Assuming that these funds go to the bottom 13 of these communities, this would yield another Ksh 7 billion per community development zone for these bottom 13 most marginal and poor of the communities.

The law should also require that 25 percent of the remaining Ksh 70 billion be allocated equitably to the regions to finance community development projects that have regional and national significance and impact. Recall that we proposed 26 Regional Economic Development Authorities. What this means is that each region has about Ksh 800 million to channel to such investments. Particular community development investment zones in the regions can also be allowed to allocate not more that 25 percent of their allotted quota to these regional investments. The remaining 75 percent of Ksh 70 billion, about Ksh 53 billion, would be allocated to qualifying CDFI investment funds depending on an objective performance and superior return criteria that would reward the best performing fund proposals in a priori determined sectors. This criteria would be weighted to ensure that investment funds from all the regions have equal chance of benefiting.

The corporation would be authorized by law to charge not more than 2 percent of the total investments realized to meet its administrative, strategic and statutory obligations. This can be charged as fees to various CDFI and other institutions active in the scheme. The authority, however, does not have to do this and should revert to it especially to secure its strategic objectives, including establishing endowments in various areas of its work, endowing community development organizations that aid in its work, including the proposed regional development corporations, etc.

The law should require that investee CDFIs meet certain minimum criteria, including commitment to gender inclusion and responsiveness, ethical trade and work practices, including non-discrimination and inclusion. This would include their hiring basis—that they should reward diversity in their workforce policy, and that they promote gender-based equality, etc. Qualifying social enterprises, including the CDFI vehicles themselves, would have to meet all the regulatory requirements as set by the proposed not-for-profit authority.

To be valuable as community development finance, the law should require that investments assume essentially the character of venture capital, with its long term nature. Fund managers should be restricted from distributing dividend from their portfolio investments before the fourth year of the investment. When debt as opposed to equity finance is provided to investee enterprises, then these would assume the character of superior or senior debt. Fund managers would be required in law to supply more equity than debt finance, say in the ratio of 60 to 40, with a view to ensuring enterprises and by extension the communities they are located in actually receive equity-backed assets and are not riddled with debt.

To be useful as an instrument of mobilizing savings in the economy, and thus to secure the availability of investible funds, the law should require that investments into the various schemes be made solely by way of block savings, achievable through SACCOs and other savings schemes designed for this purpose

or through an appropriate Community Benefit LPA (Limited Partnership Agreement) instrument for corporate investors. This latter would in effect ensure that corporates actually establish a fund scheme to invest in the anticipated CDFI-based funds, which is helpful for its tax and other statutory transparency.

The scheme should also be available to other savings and investment vehicles in the social economy, such as Programme-Related Investment schemes set up by charitable and religious organizations, as well as qualifying institutional investors such as pension schemes, etc. The proposed tax incentives set at 15 and 10 percent for PAYE and corporate investing schemes, respectively, are set sufficiently high to attract the volumes necessary for investments in the sector.

Returns from CDFIs

We have proposed that investments be made through fund instruments held by qualifying CDFIs. Community Development Finance Institutions should take the responsibility of vouching for the economic viability and social and community benefit value of the businesses they wish to invest in. Usually, these social enterprises and MSE schemes should be aligned with the poverty and asset-building growth plans of the respective regional development authority. The scheme can consequently authorize CDFI fund managers to draw down bloc funds with any necessary conditionality. Staged and co-investment deals can also be considered.

CDFIs will be expected to guarantee the investor worthiness of the investee companies making their fund portfolios. For the credit scheme to work effectively and establish itself as a solid market for investment funds, CDFIs must also ensure that their portfolios deliver above market returns to the investors but in ways that do not compromise the primary purposes of setting up the funds in the first place. We thus foresee a situation where CDFIs guarantee a minimum return on investment, ranging between 7-10 percent net of all costs of the CDFI and structured such that CDFI costs constitute between 2-3 percent of a particular investment. Returns realized higher that the resulting 13 percent threshold should be retained as endowment capital by the appropriate CDFI.

We anticipate that CDFIs will set up investment vehicles using primarily the LPA or Community Benefit LPA route. The LPA is an established and popular form in setting up investment fund schemes and has numerous advantages for actors across the Board. The Social and Community Benefit Asset Endowment Authority, as the agency appraising the CDFIs running fund schemes as well as the fund schemes themselves, should be required to issue, through subsidiary legislation, objective criteria and rules for setting up the investment schemes. Such criteria should require proposed funds to have clear mission, goals and objects, to have a clear and qualifying investment portfolio located within the

target investment area—or at least 75 percent of target applicants being from the area. The CDFI must provide development services as well as technical support to enterprises and community development establishments in the region. It can do this through licensing/contracting providers or by establishing affiliate development support organizations.

The CDFI must maintain a healthy accountability relationship with communities in its target investment regions/communities, must be a non-governmental entity independent of any public body, must be not-for-profit, and established for the benefit of community. It should be able to vouch for the value of their investee stock, should be up to date with issuing social accounting reports, and should have impeccable financial reporting.

Generating and directing economically-targeted investments

Recent retirement benefit and pension reforms in the public and private sector have had the effect of increasing the pool of funds available for investments in the economy. The conversion of the public retirement benefit regime into a contributory pension scheme is alone expected to contribute in excess of Ksh 15 billion of investment savings annually. Most of these funds have found their way into the Nairobi Stock Exchange. With this pool of funds, debate is fast rising on how best the economy can utilize them to drive strategic investments in the economy.

One vehicle that is available to pension fund trustees and managers to creatively use their funds to achieve returns other than financial returns include Economically Targeted Investments (ETI). ETI refers to the practice of making risk-adjusted market rate investments that deliver social and economic benefits that assist in the development of a certain community, group or region. ETIs are, thus, driven as much by the need to achieve superior returns as well as the need to deliver certain economic and social collateral or externalities to a targeted community. ETIs, however, are not social investments and bear all the risk profiles of a conventional investment. Consequently, they must be structured to yield the best possible financial returns commensurate with the level of risk. Trustees are, therefore, under a legal duty of care to ensure that the investment portfolio has sound financial dynamics before considering any other benefits.

ETIs, unlike conventional investments, are made to provide money to under-served or under-financed sectors or regions in an economy. Within the language of local economic and asset development, ETIs provide a special financial asset class, dedicated principally to overcoming the effects of capital market failure. Though many will claim that capital markets are efficient, in reality even the best markets hardly 'discover' all possible investments in an economy. An economy is unlikely to meet its financial inclusion goals if it relied chiefly on free

flowing 'market forces'. ETIs can be useful and hardy tools in providing new jobs, businesses and infrastructure in a region. Investing in the corporate bonds and stocks of enterprises that deliver superior social and economic returns to a target group or community will facilitate in the creation of jobs and other assets in this community. Investment in social development bonds, such as that pioneered by Faulu Kenya, will ensure that small and medium scale enterprises have access to much needed start up and enterprise capital. Investment in the sub-sovereign and municipal financing bonds we have captured elsewhere will mean that local and target communities have the funds necessary to grow their asset base.

The proposed Social and Community Benefit Asset Development Authority would be authorized in law to use its resources to nurture and seek investment vehicles meeting core criteria of acceptable Economically-Targeted Investments. The authority, together with various sub-sovereign and devolved financing schemes, can help mature various investment portfolios for entry into an ETI market.

Tax-free local economic, community and social development bonds

We have made proposals that the Social and Community Benefit Asset Endowment Authority be authorized in law to author schemes that enable successful issuance of various local economic, community and social development bonds at the Nairobi Stock Exchange. There are many ways that the authority can come to the aid of successful bond issuance and the particulars of such a scheme should be left to the authority, and these need not always be tax free. The authority should, however, be legally competent to facilitate the issuance of tax free bonds. Such legal authority can, for instance, be exercised through secondary legislation issued in consultation with the Minister of Finance.

There are many other ways that the authority can assist to ensure a vibrant social and community development bond market. We discuss some possibilities here to demonstrate the potential of such schemes. Of necessity, the details are not exhaustive or even finely worked out. It would be expected that the authority would hold lengthy and exhaustive consultations on how best to enable such a market.

One of the ways that the authority can come to the aid of such schemes is through securitization of the income that various already successful bonds generate. Supposing several municipal authorities have successfully negotiated funds for infrastructure and low-cost housing development and are now realizing stable financial returns from the resulting investments. Securitization of such returns, where the municipal councils issue a bond against the income, would have the effect of freeing the municipal councils from the debt and, thus, enabling

them to structure and issue other bonds. To enable the municipal councils do this, the authority could author a corporation to purchase the rights and risks related to the various investments from the councils and in turn issue bonds backed by the income. To participate, municipal councils would have to meet set conditions, such as putting in place various governance and financial accountability systems, carrying out consultations with the public on the use of available income, etc which would be published and gazetted.

Assuming that the housing development loans or bonds had initially been taken to help housing cooperatives and local area and community development corporations to realize investments in low cost housing, these cooperatives and corporations would continue to service their loans with the new corporation set up with the aid of the authority. The income realized would then be used to service the bond issued by the corporation. To attract the uptake of such bonds, the Asset Development Authority would accredit investment returns on schemes run by the resulting corporation with a pass through status, with the taxes being paid by the investor and not the corporation. Investors in these schemes would enjoy various income tax advantages. The charter of the resulting corporation can also enable it to retain income and independently arrange to purchase other bonds in the sector, including those issued by successful CDFI fund portfolios.

The authority should, however, only aid such schemes against its own income, including income derived from its endowment funds and the various measures proposed in this section, such as income from dedicated financial vehicles discussed below where the impact of this would be to enable faster and better realization of the goals of particular programme regimes of the dedicated vehicles. A successful bond programme promises immense financial resources to aid local economic and community development. To prevent the abuse of such bonds, we propose that the law restricts participation by local authorities and the various local economic development agencies in bond issuing to subscription to an appropriate scheme of the Asset Endowment Authority.

Enhancing financing of social enterprise through lines of credit

Many successful social enterprises will face severe constraints to accessing affordable credit owing locally, in part due to its relative scarcity. The Asset Endowment Authority, through its various schemes, should be empowered in statute to negotiate and arrange lines of credit from international lenders, including the International Finance Corporation (IFC). The authority should, however, only secure such lines using its own resources, or in combination with guaranteed resources from other sources within the larger sub-sovereign and devolved financial pool. Such negotiating and aligning should be weighted so that the resources of the authority and through it those of sub-sovereign finance

schemes work as an insurance against the risks associated with lending to these enterprises. It will be essential for the enterprises to be capable and competent to meet their borrowing obligations.

Tax allowances on donations to charities and qualifying social enterprises

Kenya's tax regime does not recognize giving to charities and social purpose not-for-profits. This has unfortunately forced many charitable organizations to structure their investments in education, health and other areas as fully-fledged enterprises, working to defeat their social purposes. This also has the effect of preventing potentially huge investments in various social sectors such as health, education and workspace development. The Social and Community Benefit Asset Endowment Authority should be legally competent to issue tax allowances, including full tax remission to donors of qualifying charitable and not-for-profit activity. Again, the authority would be expected to publish schemes or rules through which charities and not-for-profits can access such facilities. Such schemes and rules would, as expected, work to reward and move charities and not-for-profits to the best possible practices in pursuit of their social purposes. This facility, alongside others such as the bond issuance scheme, should be instrumental in driving new money to endowment schemes, scholarship funds, Community Development Finance Institutions and qualifying social enterprises.

Dedicated Special Purpose Finance Vehicles

Many of the needs in targeted strategic asset building and development cannot be met principally through tax expenditures. It will be necessary to explore and establish other finance sources for the sector. We propose that the authority be mandated by statute to explore and pursue such other financing mechanisms. Such pursuit will include carrying out advocacy work with various actors in the political economy with a view to raising direct expenditures to drive implementation of desired schemes.[195] In this and other functions, the authorities' activities and decisions should be independent of any other authority. One way to achieve this is through Dedicated Special Purpose Finance Vehicles for social enterprise and not-for-profit establishments in healthcare, social/affordable housing, workspace development, knowledge funding, armature sport and leisure, MSE enterprise development, environmental protection, tertiary education, technical education, etc.

[195] Direct expenditures refer to public expenditures charged to the Consolidated Fund and subject to yearly government budgeting and parliamentary approval/accountability.

All schemes and their purposes would have to be presented to parliament and approved either by independent/stand alone legislation or through the Finance Bill. We see prospects for financing from such sectors in the economy as insurance, property transfers, airline fares, mobile airtime, etc.

Dedicated special purpose vehicle for healthcare financing

One of the proposed Dedicated Special Purpose Finance Vehicle is a charge on motor vehicle insurance pegged to the capacity of the engine or to any other mechanism, such as the annual road licence. This vehicle would be calculated to yield an average of Ksh 10,000 per vehicle. Assuming there are 600,000 active vehicles, this mechanism would yield Ksh 6 billion to the Dedicated Special Purpose Vehicle. This money would then be available for investments and grants to social enterprises and other not-for-profit community-based organizations active in the target purpose—in this case health. The corporation would be required in law to ensure equity and fairness in its allocation of the realized funds.

To illustrate the likely impact of such a facility, we propose an elaborate healthcare facility endowment scheme requiring Ksh 15 billion per year that would lead to the upgrading or establishment of four new national referral hospitals superior to the Kenyatta National Hospital, 10 new regional referral hospitals, 30 new regional general hospitals that would replace the existing provincial hospitals and about 80 district hospitals.

The first phase of this scheme, lasting up to 4 years, would entail the physical and human resource investment in these establishments. The second phase and which would be open to other qualifying social enterprises in healthcare provision would include helping these institutions establish permanent endowments to secure their not-for-profit status. This phase can last anywhere from 6-10 years but would result in a well endowed healthcare facility establishment, equal to the best of such facilities in developed economies and that is accessible to all who need it.

Dedicated special purpose finance vehicle for low income low cost housing and workspace development

An instrument such as a surcharge on property sales and transfers can yield significant resources for use in starting up low cost housing development and work space development. Other avenues for this kind of income include possible surcharge on land rates in high value zones in urban centres, a charge on community reserved land for such commercial amenities as shopping centres, petrol stations, etc.

Dedicated special purpose financing for technical workforce and tertiary education

This requires that all operators in the sector operate on a social enterprise framework with a view to ensuring access but also with generating surpluses. All graduates should pay for the services—effective at most two years after leaving school. It also would require these institutions to seek to internationalize their scope to attract students from the rest of the continent and elsewhere. Ideally, student fees could meet at least part of the fee, but this should be kept at levels that are affordable.

Other possible sources of dedicated finance can include:

- Reviewing the Industrial Training Levy to allow the various institutions to charge this levy for some of their services
- A tax on airline tax or other appropriate tax on aviation
- Reviewing the Catering Levy and Trustees, increase their collection, as well as increase the fee, and require all restaurants to pay for the fee
- Expanding the scope of the Catering Levy and Trustees and scope of similar funds to fund training courses at polytechnic and university level. The fund should also fund research in tourism, in food and food safety standards

Dedicated special purpose financing for cultural production

Social enterprise-based investments in community radio, television production, film, theatre, all genres of music with appropriate local inspiration, amateur and semi-professional sport, cultural and other museums, local language and cultural schools and centres, etc can be supported through:

- Special levy on advertising
- Special levy on television and radio licensing
- Special levy on hotel, gaming and other leisure facilities
- Special levy on foreign print, film, radio and television programming
- Beneficiary local authorities—those where the investments are to be made plus other community organizations to raise matching investments

Omnibus special purpose vehicles

There will be other purposes, including the above, that may not be set up in law but with great potential for social and community development. We propose

that the corporation be empowered in law to set up such schemes as the need arises.

Direct Surcharge on all Tax Collection Surplus

We anticipate that the measures we have proposed in this study will lead to year on year surplus tax collections by the Kenya Revenue Authority (KRA) on account of increases in productivity, greater commercial activity, rising base incomes, expansion of the tax payer base, etc. We also anticipate that owing to the improved social development environment, the core demand of publicly-funded social expenditures can actually decline with increased and sustained economic growth. The 'liberalization' of social service delivery largely through actors in the social economy can also lead to significant savings, resulting from a reduced public wage bill. Partly in recognition of these benefits as well as the direct contribution of the measures proposed to the fortunes of the KRA, but also in recognition of the social and community benefit purpose of the proposed funds, we propose a direct surcharge of 5 percent on all tax collection surpluses by the KRA. We also propose a surcharge of at least 25 percent of any money returned unused to the Consolidated Fund at the end of a financial year. Assuming that the KRA continually returns a surplus of Ksh 10 billion per year, this would yield an extra Ksh 500 million shillings.

Grant Income from Successful Social Enterprises

The law should empower successful social enterprises to make grants or investment directly to the authority, its various funding schemes or to organize other investment schemes in support of qualifying social enterprises and community benefit organizations.

Direct Surcharge on Revenue

Notwithstanding any proposals made here, the core costs of the corporation should be met by a direct surcharge of up to 0.2 percent of the total revenue collection by the KRA. This measure is important in securing the financial autonomy of the authority and is a reflection of the role of the social economy in delivering to larger social, economic and political development goals and aspirations.

Macroeconomic Restructuring

The measures we have proposed are informed by and would lead to a significant re-ordering of the economy at micro and meso levels. It is our view that significant benefits can be realized from substantive restructuring of the macro economy. There is great value, for instance, in restructuring Kenya's domestic debt with a view to externalizing at least 80 percent of it. At current debt serving rates, this would result in significant savings in excess of Ksh 35 billion per year, as servicing the local debt is several times more expensive to servicing a foreign one.

We propose that the corporation be empowered and required by law to investigate, make recommendations and actively pursue such structural reform agenda with a view to channeling a statutory allocation of at least 25 percent of the savings accruing from successful restructuring, with the remainder going to benchmarked pro-poor investments as may be prioritized by government.

Similarly, it is likely that a lot of benefits may be realized with the setting up of a corporation to purchase at discounted rates the bad and doubtful debt stock clogging the financial system. Granted, as we have argued elsewhere, that this huge debt portfolio originated from practices that are responsible for the current levels of financial exclusion, it is only logical that benefits from such restructuring be availed to investments in poor and underserved communities. We propose, therefore, that the corporation be allowed to set up a special purpose finance vehicle that would be financed from the sale of this debt stock. The corporation would purchase the debt stocks from the commercial banks at a discounted rate and proceed to recover the debts. The proceeds from this recovery would be invested in qualifying social enterprise-based investments, including in CDFIs lending to MFIs and MSEs.

Donors

Donors can fund the SCBAS directly, make equity or programme investments and grants to qualifying social and community benefit enterprises or choose to partner with development institutions.

The Social and Community Benefit Asset Endowment Authority should also be enjoined as a state actor/body with the framework of Kenya's multilateral and bilateral donor relations. This would mean that the authority engages independently and directly with donors for purposes of effecting its various schemes and investment strategies. Since these are linked with strategic and investment plans drawn up by RDAs and other local economic and community development agencies, and implemented independently through CDFI (and CDFI-type) institutions, this would have the desired benefit of accessing external resources directly for capability and asset-based local economic and community

regeneration. This would also siginificantly improve the absorptive capacity of foreign aid.

Enhancing Social Auditing and Accountability

We have placed much faith in the capability of institutions in the public, private and social economy sectors of society. It is unlikely, however, that these institutions can live up to the requirement to deliver much needed social returns and benefits without a comprehensive framework and measure of social reporting, auditing and accountability. Various proposals we have made with regard to placing statutory and practical requirements for numerous institutions across the board to be seen to deliver maximum social returns also necessitate an independent and rigorous social auditing regime on which various actors in the public, private and social sector can rely on to evaluate claims regarding delivery of such returns. It will be necessary, in this regard, to institute a national framework for social accountability and auditing. Key features of such a framework would include:

(i) Statutory requirement that the following broad categories and institutions submit to new social reporting and auditing regime:

- Social Sector not-for-profit trading and non-trading corporations
- All agencies, corporations and businesses desiring to and engaged in contracts with government and public bodies
- Public corporations and agencies

(ii) Statutory Authority on Standards and Industry Regulation with rule making powers and powers to require compliance.

(iii) Independent but statutory mechanisms to drive practice and enforce voluntary compliance with standards.

Enhancing Social and Community Investing

We have also placed a lot of faith in drawing social and community investment resources from within the financial and capital markets. The proposed authority will be expected to aid in the realization of such hopes by working to institutionalize mechanisms and incentives for social and community investing. These mechanisms and incentives need not be statutory and can be industry-based.

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