Research Paper On

“Areas of Reducing Expenses & Increasing Revenues to Address the Current Financial Crisis”

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1. **General Framework**

1.1 **Introduction**

The Palestinian Authority (PA) has been suffering from a chronic financial crisis since its inception in 1994, with repercussions that affect Palestinians’ lives in the occupied territory (OPT). Many reports and research papers have been prepared concerning the financial crisis, its subjective and objective causes, as well as its effects on the Palestinian society as a whole. Therefore, this report will not cover the structural aspect of the financial crisis, but will address it (where necessary) in the context of the report in question.

The difference in the current financial crisis and the imperatives of addressing them is represented in the deepening of the crisis, fiscal deficit, and its longevity that coincides with the continuation of the occupation. Data indicates that most of the main sources of the PA treasury are drained. To begin with, the occupation government, for the fifth consecutive year, has deducted part of the clearing funds under the pretext that the PA government insists on paying salaries to martyrs and prisoners families amounting to nearly NIS 50 million per month; NIS 2 million were deducted, since the beginning of this year, under the pretext of compensating Israelis based on Israeli court decisions. Another $916 Million are deducted annually arguing that it goes to the Gaza Strip (GS). The latter excuse is part of the Israeli government’s policy to completely separate the West Bank (WB) from the GS, following the Israeli aggression on the GS in October, 2023.

However, as a natural response to Israeli measures, the PA refused accepting the clearing tax money since that date and for a long time, specifically after the last deduction for the GS. This caused a deeper deficit and hence the inability to pay public employees’ salaries; cover operational and development expenses that were approved and adopted within the public budget. It also weakened provision of basic services such as health and education. This was accompanied by a continuous spending from the treasury, in some areas and aspects that are (unnecessary); will be mentioned later in this report. To avoid continued spending without effectiveness and specifically under the circumstances concerning the financial crisis, that more than likely would not be resolved in the foreseeable future, a deep review required.

Despite the resumption of the PA receiving part of the clearance funds, the crisis persists. According to the Norwegian government, the PA received NIS 407 million ($114 million) On 29/2/2024. This was based on an earlier agreement, which took place earlier in the month, to prevent the collapse of the PA; ensure Palestinians’ access to basic services and pay teachers and health workers salaries.¹

And although the government adopted the Financial and Administrative Reform Agenda, presented during the Donors’ Conference in May 2022, it has been unable to implement the reforms intended, or fulfill the pledge it made, which is to rationalize spending in the 2023 budget, announced in April 2023. This plan included reform policies aiming to reduce salaries and wages by reviewing the administrative structures, reform the health system and reduce net lending.² Note that reasons for the failure to achieve this plan’s objectives do not differ from the previously developed programs and plans. This is because a decisive political will is questionable concerning the delivery of policies that provide possibilities to carry-out activities and measures and with capabilities to implement the plan and achieve its goals. Moreover, the Palestinian Council of Ministers (CoM) also took important decisions in November related to rationalization of government departments’ operational expenses and in particular, those linked to travel and transportation expenses and any other expenses that can be saved, to face the current financial crisis. In addition, the budget was considered an emergency budget, without specifying the emergency, or the areas it would cover.

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¹. https://www.aljazeera.net/ebusiness/.29/2/2024
². See: Bishara: Salaries exceeded net revenues and the financial situation is likely to worsen further. (al-ayyam.ps)
1.2 Paper Objective

AMAN worked, during the past years, to help the government adopt plans and measures related to rationalizing expenditures. It provided studies and reports such as the: Public Expenditure Rationalization Report; Gaps in Public Employment; Financial Leakage Report; Tax System Report; and the Financial relationship with the Israeli side Report. Consistent with AMAN’s work, this paper comes to identify areas for reducing public spending and methods of control it, due to the ongoing deepening financial crisis. It will also search for opportunities to increase revenues to reduce the deficit, face the financial crisis and existing challenges, and reduce the accumulated debts. It is worth noting that the targeted actions are linked to two main influencers: first: Legal dimension- represented by the consistency of the procedure with the law-cannot be violated- past contractual obligations of the Government, to protect government actions from any accountability, legal or administrative violations. As for the second dimension, it must consider the economic and social dimensions where the targeted procedures do not affect social benefits, especially for the marginalized and needy groups. Also, it must not increase the financial burdens on the various economic sectors. Accordingly, the paper aims to:

1. Identify areas where spending can be stopped and or postponed; control spending in other areas.
2. Identify areas and opportunities through which public revenues can be increased.
3. Submit specific proposals for mechanisms to address the financial crisis.

1.3 Methodology:

Preparation of this paper is based on the following steps:

1. Collect and analyze relevant information from various sources, including AMAN’s reports.
2. Conduct individual interviews with stakeholders and experts.
3. Prepare a first draft; present it in a stakeholders’ discussion workshop and modify it based on the results.

1.4 Focal Points

This paper includes the following focal points:

1. General framework: includes the objective and methodology of the Paper.
2. Description of the current financial crisis: features and causes.
3. Areas, on both the expense and revenue sides, that are possible to address.
4. Conclusion.
The current financial crisis is described as the deepest and most complex since the establishment of the PA; it is manifold, and negatively affects the various components of the Palestinian society. It is worth noting that the PA is facing a stifling financial crisis that didn’t emerge with the war on Gaza. Rather, its causes and repercussions have been around for the last three decades. In this regard, AMAN issued more than one report indicating that the policies of the Palestinian governments (especially the 18th) postponed addressing the: budget deficit crisis, accumulated debts; net lending, transferring the crisis to the following year instead of objectively addressing the problem. Similarly, periodic reports issued by the World Bank, the International Monetary Fund (IMF) warned of the up-coming difficult financial crisis, if not rectified. The recommendations issued by these institutions included calls to the PA to take the necessary measures that would reduce the fiscal deficit; and other calls to the international community to increase its funding to the public budget. The recommendations also called on Israel to ease restrictive policies and measures that choked the Palestinian economy. It is noteworthy that the World Bank’s assessment on implementing these recommendations reveals that the level of progress remains consistently minimal.³

The PA’s ability to manage the financial crisis is further exasperated due to the limited options available. In the past, the it resorted to three policy measures: Appeal to donors and Arab states for additional budget support; apply some austerity measures; increase internal borrowing and adopted pledges of financial increases for groups of workers, to be paid in the future. This time however, it has very limited margin for action on all three fronts. However, what deepens this crisis is its entrenched causes since three decades ago. most prominent of which are:

- The continued Israeli occupation and its oppressive practices and restriction on movement of the people and trade, by: installing hundreds of military check-posts; confiscating Palestinian land for building Israeli colonies and military posts; seizing Palestinian natural resources such as: the water resources in the (WB); monopolizing the sale of water, electricity and petroleum, to the Palestinian market; controlling natural gas, oil and minerals; and also, crossings and borders.

- Difficulty in utilizing and investing in Area (C), that is about 60% of the WB, due to: Restrictions and obstacles imposed by Israel on the Palestinian economic activities under the pretext of “security”.

- Restrictions of the Paris Economic Agreement have remained unchanged for 30 years: negatively affecting the Palestinian economy and its structure; the final outcome of the Paris Economic Agreement (PEA) is: concurrence of studies, reports and all statistical data indicating a sharp decline in the Palestinian economy during the last ten years, where an increase in its structural imbalances led to multiple overlapping economic distortions, and weakened its production capacity (The World Bank, IMF, UNCTAD and other various reports)⁴

- Weak fiscal policy: the PEA is the main reference for this policy, especially in relation to public revenues (taxes) in confronting external determinants and specifically the Israeli measures against the Palestinian people and their economy; and, the internal determinants, represented by international aid and basic characteristics of the Palestinian economy and its scarce resources.⁵

- Weakness in governance of the public sector: All indicators of governance in the Palestinian public sector are weak, with scores in the minus⁶ during the period 2000-2022.

3. Samhouri, Mohammed (2019), Israels Decision to Deduct Part of the Revenues It Collects on behalf of Palestinians accelerated a financial crisis that grips the Palestinian economy at a time where options available to overcome it are limited. https://carnegieendowment.org/sada/79060
5. Abd-Alraziq Omar, 2016. Evaluation of the fiscal policies of the PA. (MAS), Ramallah, Palestine
• Absence of accountability (dysfunction of the Palestinian Legislative Council- PLC) after 2007: until this date, as an authority with inherent competence to enact legislation in accordance with the legal system in Palestine, the PLC was completely suspended, leading to its dismissal at the end of 2018-endorsed by the Constitutional Court. This Led to the forcible transfer of legislative jurisdiction to the Palestinian president, under Article 43 of the Basic Law. Added to all this is the approval of the public budget away from discussions and participation of other sectors, particularly the private and civil sectors.

The above causes led to the continuation of the financial and economic crisis, and to lack of transparency of the announced fiscal reform policies. Thus, further increased dependence of the Palestinian economy on the Israeli economy, hence more difficult to disengage from it. It also increased its vulnerability to Israeli decisions and actions; created imbalance in both the economy and structure of the public budget; weakened and distorted investment, and increased poverty and unemployment. As a result, the current financial crisis worsened; its most prominent features can be summarized in two parts: the first is related to external influences, and the other is related to financial policy, or financial behavior and structure of the public budget, whether it relates to expenditures or revenues.

❖ External Influences on the Crisis:

Shrinking economy: decline in the GDP by 33%, where it declined sharply in the GS during the fourth quarter of 2023 by more than 80%. this was accompanied by an increase in unemployment reaching 74%, as a result of an almost complete collapse of all economic activities. The WB economy also declined by 22% with an increase in the unemployment rate by 29%. Moreover, the total of each: consumption, investment, imports and exports declined by one third compared to the same period of last year. In addition to that, there was a sharp rise in prices in the GS exceeding 30%, and an unprecedented rise in poverty levels in Palestine. Also, the consumer price index increased by 6% in 2023, in comparison with 2022, which negatively affected spending of the Palestinian households.7

The Private Sector Losses Due to the Israeli Aggression on the Gaza Strip:8 the aggression led to a decline in production in the majority of establishments; losses were estimated at nearly 2.3 Billion USD during a four-month period (October 2023- January 2024) as shown in table (1). This is equivalent to $19 million USD per day; excluding property and assets. The result was that production for about half of all businesses either stopped or declined.9 In the WB, it is estimated that 29% of its establishments’ production either declined or stopped, totaling 35 thousand facilities. In Gaza, however, the majority of businesses were shut down in addition to the majority of workers, estimated at 153 thousand laborers who became unemployed; excluding health and humanitarian relief workers. Moreover, the productive base also eroded, as the economic sectors in the WB lost 27% of their production during the first 4 months of the aggression; an estimated loss of approximately 1.5 billion USD. In contrast, the GS lost 86% of its production, equivalent to 810 million USD.

9. The number of establishments in Palestine in 2023 reached about 176 thousand establishments (56 thousand in the GS, and 120,000 in the (WB).
Table (1): Production losses of the Palestinian economic sectors caused by the occupation’s aggression on the GS during the 1st four months (10/2023-1/2024) * by region

<table>
<thead>
<tr>
<th>Sector</th>
<th>The value of normal production before the Israeli occupation aggression (four months)</th>
<th>The value of production during the Israeli occupation aggression (four months)</th>
<th>The value of losses during the 1st four months of the Israeli occupation aggression</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>WB</td>
<td>GS</td>
<td>Palestine</td>
</tr>
<tr>
<td>Industry</td>
<td>1,939,910</td>
<td>221,430</td>
<td>2,161,340</td>
</tr>
<tr>
<td>Business establish...s</td>
<td>74,267</td>
<td>11,135</td>
<td>85,2.4</td>
</tr>
<tr>
<td>Other Services &amp; Branches</td>
<td>3,511,860</td>
<td>711,691</td>
<td>4,223,551</td>
</tr>
<tr>
<td>Total</td>
<td>5,526,037</td>
<td>944,256</td>
<td>6,470,293</td>
</tr>
</tbody>
</table>

* The data does not include the Jerusalem governorate, which Israel annexed by force shortly after it occupied the WB&GS in 1967.

Source: pcbs.gov.ps_pcbs_2012/PressAr.aspx

According to the Palestinian Ministry of National Economy (MoNE)\(^{10}\), at the level of Palestine, the estimated daily losses resulting from the Israeli war on the Palestinian people amounts to nearly 24 million USD per day. The most affected sector is the tourism sector, in which more than 40,000 citizens work directly and indirectly. Also, 85% of the economic establishments suffered a decline in their performance, stressing that small and micro enterprises suffered the most. All of which is caused by citizens inability to move between governorates due to: Israeli check-posts, colonizers aggressions, and decline in the purchasing power. Moreover, company registrations decreased by 75%, compared to October 2023 and 2022. In addition, the industry sector also declined by 90%, and 41% of the economic establishments in the WB witnessed a decline in the average number of employees, accounting for 54% of the total number, due to the economic deterioration in the various economic sectors. Furthermore, 77% of businesses have difficulty moving and distributing goods between cities due to the repeated incursions and closures imposed by the occupation, in addition to the decline in monthly sales of about 97%, especially within the commercial sectors such as: food retail sales; furniture, clothing, shoes, and electrical tools and appliances.

Decline in the number of Palestinian employees working in Israel: All data indicate that the cessation of employment in Israel may extend for a long period of time, since Israel announced the closure of all crossings until further notice. This led to an increase in the unemployment rate at the level of Palestine, reaching 42.4% and 52.7%, with a rise in the WB to 22.8% to 38.4%. This affects public finances as follows:\(^{11}\)

1. Decline in income tax on workers’ wages, in Israel, from about 1.69% of the clearance revenues (194 million NIS) in 2022 to NIS 46 Million on to end of 3/2024.
2. Decline in total imports of goods by about 10% to 20%, reducing the PA’s revenues by about 7% to 14% on average.
3. The local value added tax (VAT): A 10-15% decline in the final consumption expenditure of households’ expenses will reduce the PA’s total net revenue collections by 0.9% to 1.3%.

\(^{10}\) https://pnn.ps/news/683511.
\(^{11}\) Habib Hin, Habib (2023) Economic Summary on the War on Gaza Issue 2023/11/15 – 5: preliminary conclusions of the impact of employment stoppage in Israel on Palestinian macroeconomic indicators. MAS. Ramallah, Palestine
In an effort to reduce the profound effects of the cessation of work inside the occupied territories (OPT), the government, represented by the Ministry of Labor (MoL) facilitated bank loans for about 220 small projects. It also provided an amount of NIS 700 allowance for Gazan workers stranded in the WB, in addition to in-kind assistance.

Decline in grants and foreign aid: clearly there is a decline in grants and foreign aid to both parts of the public budget: (treasury & development projects funding). Since the inception of the PA, foreign aid and grants flooded to promote building of state institutions, amounting to $530 million in 1998, about 40% of the total budget. While in 2008, it amounted to $1,953 million or about 56% of the total budget. This was followed by a relative decline in aid funds, reaching approximately 650 million USD in 2018, a mere 13.5% of the total budget, and in 2022, it amounted to 335 million USD, about 7% of the total budget. This is in addition to receiving conditional external funds that are based on the agendas of donors. Similarly, Arab funding also remained limited and volatile and hence cannot be considered a “safety net” for the support of the public budget. This decline in external support has directly affected social services and the various social sector projects, especially since development programs depend mainly on external funding. All of this casts a dark shadow on the future of external support.

The above-mentioned data reflects negatively on the data of public funds in Palestine. And despite the Ministry of Finance’s (MoF) publishing of monthly budget reports since 2008, its last published report was in September 2023. Also, neither the State Audit and Administrative Control Bureau (SAACB) nor the Monitory Fund (MF) have published their reports since October 2023. However, some data was provided by the Finance Minister during a press conference; he said “the amount Israel deducts, under various pretexts, from Palestinian money amounts to two-thirds of the amount collected per month”. He added: the total amount deducted by the occupation during 2023 alone amounted to 4.8 billion NIS (1.4 billion dollars), NIS 407 million were released in 2/2024 which deepens the financial crisis.

The total amount of clearing funds ranges between NIS 2700-3000 million per quarter, But it decreased in the fourth quarter to NIS 1970. Million, however, this amount declined in recent months due to the hostile economic policy pursued by the Israeli government towards the PA, Israel deducts 275 million NIS monthly under the pretext that this is Gaza’s share. It also claims that it keeps 52 million NIS due to the PA’s supporting prisoners and martyrs’ families; 60 million NIS with the excuse that these are electricity debts for the Jerusalem governorate. These financial cuts are added to a long list of cuts over the years; allegedly for electric, health, and sanitation services, reaching nearly $6 billion over the past ten years.

Furthermore, one prominent consequence of the war is that the total arrears of employees’ salaries, by the end of last year, towards the salary bill for two months on average; and by January, they amounted to NIS 3.2 billion. Moreover, the MoF expects the decline in trade to be between 40-50%, which will lead to a further decrease in the amounts collected as the clearing funds and to a sharp decline in revenues collected by the government. If the situation remains as is, without external funding, we will have to live with an income that covers 20-30% of expenditures, in the coming months, if the government continues to apply its traditional management policy concerning expenditures and revenue collection.

Despite the significance of publishing financial statements, especially, in these difficult times for ordinary citizens, public sector employees, and establishments of all kinds, the MoF has adopted a policy of not publishing any. Although it used to publish monthly budget reports since 2008, its last published report was in September 2023. Also, neither the (SAACB) nor the (MF) have published reports on new developments since October 2023. This poses many questions as to why all the absence of transparency at such a critical time.

12. Interview with Dr. Mohammed Al-Araj, Director General of Employment Services at the Ministry of Labor, on 2024/4/7.
15. Affaneh, Muayad (2020), previous source.
Depending on the baseline scenario, or the continuation of the current situation as predicted by the SAACB,\textsuperscript{16} the economy is expected to witness a sharp decline by 5% in 2024. This is due to the on-going Israeli aggression and hence its repercussions, not only on the GS, where the majority of its building and infrastructure have been destroyed, but also extends to the WB affecting most of its sectors and economic activities. Also projected:

1. Decline in consumption, investment and export spending; and in the value added of economic activities. These declines will be accompanied by a sharp rise in unemployment rates (35.1%) in 2024, compared to 30.7% in 2023.

2. Israel will continue to deduct part of the clearing tax funds at the same rate that was before the Israeli aggression on the Gaza Strip in 2023, which will negatively affect the government’s ability to meet its obligations towards the government sector and private sectors’ suppliers.

3. Decline in income tax revenues and value-added (local and clearing) as a result of an economic recession.

4. The level of foreign aid supporting the PA’s budget will remain as it was in 2023; minimum.

5. Development projects will come to an almost complete halt.

\begin{itemize}
\item Fiscal policy influencers or financial behavior; public budget’s structure of the financial crisis:
\item Expenditures: A haphazard spending policy, without transparent controls or rules, has exacerbated the crisis from time to time. The most prominent proofs resulting from this policy can be summarized as follows:\textsuperscript{17}
\begin{itemize}
\item Increase in expenditures for the majority of the past years at a faster pace than revenues. For example, the increase went from $2.8 billion USD in 2010 to about $5.22 billion USD in 2023. Most of it was under the salary and wage item; and operating expenses other than salaries, specifically transfer expenses.
\item No significant change occurred concerning the overhead structure. These expenditures remained mostly the same (ranging between 88%-95%) of the total expenditures and inflexible in its distribution.
\item Continuous overrun of the actual and cash-incurred expenditures on the planned expenses, which has become an ongoing condition in the history of Palestinian budgets. It is also considered poor planning stemming from uncertainty of the revenue amount that can be collected. This reflects the extent of difficulties facing the government in fulfilling its obligations, especially since the growth pace of expenditures is greater than the revenues.\textsuperscript{18}
\item Continuous rise in net lending, which began at approximately 173 million $ in 2003, only to exceed 1.34 billion NIS in 2023. The net lending item is huge in volume with a twofold problem: the first is about transparency, where only numbers are provided with no details despite the importance and sensitivity of this item. The second is related to the large deviation from the plan by about 30%. And although efforts have been exerted to reduce the size of net lending, especially in terms of local governmental units (LGU) inability to pay the full electricity and water bills, this decline caused by lack of payment of LGUs (about 40%) contributed to not achieving the desired goal of reducing net lending spending.\textsuperscript{19}
\end{itemize}
\end{itemize}

\textsuperscript{17} Abd-Alkarim, Nasr (2021), An updated report on the Financial Crisis of the PA «Reality and Difficult Options to Reduce it» AMAN, Ramallah – Palestine.
\textsuperscript{19} Interview with Mr. Raed Sharbati, person in charge of managing the net lending file at the Ministry of Local Government on 2024/4/7
The sectoral distribution of expenditures has not varied much over the years; as the share of the economic sector, for example, still ranges between 3%-5%, where most of it is current expenditures, not development. The agricultural sector, however, received about 1%, compared to the governance sector and in particular the security sector whose share is 21%, and the social sector of 43%.

Although the zero rule was followed in appointments, the salary bill continued to rise year after year; from about $1.4 billion in 2005 and ranged from $1.7-2.2 billion during the period of 2015-2021.

Applying an expansive operating spending policy, as: rental fees, travel expense and job privileges, that is disproportionate to the possibilities and resources available, contributed to the exacerbation of the deficit year after year...reaching NIS 1.5 billion in 2015 and increased to NIS 2.7 billion in 2022.

The development budget became significantly less in recent years (6-8%) of the public budget; while the actual disbursement rate of this budget remained between 60% and 70%, due to its full dependence on international aid.

Continuous rise in medical referrals and cost on the PA treasury. In 2022, the number reached 110.8 cases, with a cost of approximately one billion NIS. It is masked with major difficulties that contribute to the continuation of a negative phenomenon and weakens the foundations of integrity, transparency and accountability in the management of medical referrals. Most notable: Absence of a comprehensive an inclusive health system; continued intervention of parties and institutions (other than the MoH) in medical referrals; weak internal and external control tools. According to some analysis, the increase in the number and cost of referrals will be three times as much as it is now; where by 2028, it is expected to reach 308,000, at a cost of 2.7 billion NIS.

Revenues: There is an increase in public revenues, but not sufficient enough to significantly reduce the current budget deficit; it only covers about 70% of total current expenditures. Moreover, revenues growth depends on the clearing tax fuds, a factor that limits financial independence. On the other hand, the relatively high tax and customs revenues indicate an improvement in collection, in addition to the increasing contributions by the Palestinian citizens to public expenditures - despite an improvement in tax collection. Tax policy, however, still suffers from some shortcomings, perhaps the most important of which are: Failure to satisfactorily expand the tax base, as there are still large sectors and segments without tax files. Also, failure to reduce the phenomena of tax evasion and leakage, estimated by the MoF to be about $500-600 million USD annually. In addition, the General Director of Income Tax at the MoF said that it is very difficult, in the current period, to increase local tax revenues due to the decline in economic activities (tax base).

The growth of tax and customs revenues indicates an improvement in collection, also Palestinian citizens increasingly contributing in covering public expenditures. This, however, must be accompanied by a participatory policy, a transparent public budget, citizens’ right to hold their government accountable for public policy and to participate in its making. Although the MoF has committed to publishing the citizen’s budget in 2022 and 2023, the current difficult circumstances require the publication of this budget (quarterly or monthly) to clarify the financial situation. It is also beneficial to hold press conferences and televised interviews that illustrate the reality of the state of public funds. Such actions would reassure the citizen on how and where fees and taxes he pays are spent, hence confidence in the government is gained.

22. Interview with Mr. Emad Abu Subha, General Director of Income Tax at MoF.
Financial leakage: The size of the financial leakage and losses incurred by the PA in its relationship with the Israeli occupation is about $ 509 million USD annually, distributed as follows: 30 Million USD in indirect import, through the leakage of customs, purchases, levies and duty tax; 40 Million USD differences in administrative commissions; 152 million USD as a result of customs evasion; $22 million as a result of not transferring departure tax; 223 million USD as a result of non-transfer of income tax concerning laborers working in Israel and not transferring the equivalency tax of all workers; and $20 million as a result of not transferring income, value-added, property and other taxes concerning Israelis in Area C.  

It seems that the Palestinian tax system in its current form is a fertile environment for continued financial leakage, considering that, until now, the PA does not have the capabilities to control or deter the bulk of this leakage. However, the internal legal environment relating to the issue of financial leakage is found to be inadequate to address its causes, since many of its aspects are shrouded in ambiguity and complexity. It is also powerless to respond to changes and emergency developments in regard to tax and customs evasion. Moreover, the work environment in the regulatory and security institutions, in charge of law enforcement, seems inappropriate and limited in the effectiveness of combating financial leakage due to the weakness of material, human and logistical capabilities necessary to confront this phenomenon.

Establishing new institutions in light of the financial crisis: approving decisions to establish new bodies and institutions in light of the financial crisis, such as: Decision of the Council of Ministers on 2/11/2020 to establish the “Palestine Water Company”, to be a governmental company; Council of Ministers on 6/9/2021 AD to establish the Palestine Natural Gas Company; State Public Company; Decision of the Council of Ministers on 3/7/2023 to establish the Unified Emergency Response Center (911) No. (79) of 2023 which is a public institution that enjoys financial and administrative independence, and the establishment of the Olive Oil and Olive Museum “Palestinian Countryside”, where a presidential decree was issued on 5/7/2023 to form an establishing committee; Presidential Decree No. (1) of 2024 concerning the National Institute for Documenting the History and Memory Preservation of Palestine, a public institution that enjoys financial and administrative independence; and the decision of the Council of Ministers on 5/2/2024 to establish the “Supervisory Authority for Trust Service Providers” which would increase the financial burden. **The establishment of new institutions is incompatible with the financial crisis since it affects the government’s ability to meet its basic obligations.

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24. The previous source.
27. https://maqam.najah.edu/media/uploads/10/2023/legislations/%D8%A7%D9%84%9D%8B%7D%88%9D%8A%7D%8B1%D8%A6.pdf
3. **Addressing Possible Areas of Expenditures and Revenues**

The Palestinian government’s attempts to reduce the budget’s deficit thus far were always based on a reaction to Israel’s withholding of the clearance tax money or to decline in foreign aid. Only then does it quickly decide to announce its intentions to austerity spending or improving tax collection. However, these efforts did not yield tangible results in reducing the budget deficit in a sustainable manner for various reasons; most notably: failure to substantially reduce spending, either due to the absence of a well-thought-out vision and plan, or due to the weak impact the targeted expenditures have on the structure of current expenditures.\(^{30}\)

On the other hand, it must be recognized that fiscal sustainability is difficult to achieve without stimulating economic growth, which is subject to the lifting of restrictions imposed on the Palestinian economic activities, confirmed by the World Bank.\(^{31}\) The World Bank showed that raising the economic growth by 7% will reduce the salary bill by 5% compared to GDP. Moreover, it indicated that there are chronic problems in the PA budget such as: its failure to expand the tax base, inability to reduce the salary bill, inability to solve the problem of public expenditures on health, and inability to deal properly with net lending.\(^{32}\)

Furthermore, other reports\(^ {33}\) confirms that the PA’s ability to cope with the repercussions of this crisis is very limited, since it lacks the resources and financial capacity. Also, carrying out its administrative responsibilities has become hostage to the occupation’s decisions and donor countries in providing support, at a time when the stricken GS needs all available resources and more. Moreover, the uncertainty of clearance revenues adds insult to injury, i.e. Israel’s unwillingness to transfer these funds. However even if when it is transferred, the analysis indicates a decline in clearing and local revenues, due to the shrinkage of demand under the current conditions, and hence the decline in the PA’s financial capacity. Despite all that, the increase in government consumer spending, especially social transfers to poor and marginalized families, is essential to reduce the depletion of GDP and help those most affected by the crisis.

> **Therefore, the government must reconsider its work methodology and adopt policies and decisions based on the principle of partnership with other sectors. And since the greatest impact of this crisis is its humanitarian repercussions, represented by the increase in the number of families who are unable to meet the basic necessities of life, the whole population in the GS, and a sharp decline in economic performance in the WB, it is necessary for efforts of all sectors be joined together to overcome this crisis.**

### 3.1 Expenditures:

The following are areas in which spending can be controlled and reduced:

- **Short Term**
  1. Freeze cabinet decisions and all presidential decrees on establishing new institutions.
  2. Start cleaning up the salary bill and reducing waste of financial resources, whether by stopping employment through private contracts and consulting or addressing the phenomenon of ghost employees, by ending payments to those who are not actually employed.

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\(^{30}\) Abd-Alkarim, Nasr (2021), previous source.
\(^{31}\) World Bank (2015), State Building through better public expenditures – a reform agenda for the PA. Ad Hoc liaison
\(^{32}\) IMF (2018). Regional Economic Outlook, Fiscal Policy in Support of Growth- Middle East and Central Asia Department.
\(^{33}\) Habib, Habib (2023). Previous source
3. Freeze spending on non-essential items, such as: travel allowances, external missions, and capital expenditures, such as: government vehicles, and unnecessary equipment; also freeze some development projects.

4. Provide qualified employees and accounting systems required to audit and follow up on medical bills sent by Israeli hospitals, which will contribute to preventing manipulation of treatment costs, and also to rationalizing spending.

5. Immediately activate internal and external control tools and procedures on the performance of the competent departments in charge of medical referrals.

6. Publish the citizen’s budget retro-actively from the start of war on the GS; provide full details of the PA’s financial situation; organize for press conferences and TV interviews to clarify the financial situation of public funds. This is to reassure citizens of where and how the taxes they pay are spent, and increase confidence in the government.

7. Move forward in applying e-government due to its positive impact on reducing expenditures; facilitating access and enhancing the quality of services, which is consistent with the sustainable development plans and goals.

8. “Exceptional “medical referrals must be stopped immediately. Only those that are in accordance with the regulations issued by the CoM must be passed.

9. The PA should protect social services from any funding risks as much as possible due to their significant impact on the poor and marginalized groups.

Medium Term:

1. Provide support for the industrial and agricultural sectors by promoting investment in these two sectors. This requires first, amending the Investment Promotion Law. Also, provide incentives to projects in the two sectors, especially small ones; amend the Income Tax Law in order to mitigate the tax burden on these sectors.

2. Rectify the current situation regarding the 2009 financial regulations of ministries and public institutions, in terms of re-discussing and publishing them in the Official newspaper.

3. Restructure the institutions and agencies entrusted with law enforcement, and reduce financial leakage. Among the most prominent of these institutions: Taxes General Departments at the MoF; Customs Enforcement Service and Palestine Standard Institution. Restructuring means that they must have clear systems and regulations, and must be supported and provided with the human cadres as well as the financial and logistical needs necessary to carry out their tasks.

4. Approve the package of local laws that stimulate direct imports, local production and exporting; impose well-thought-out technical restrictions on imports from Israel; establish and apply legal and technical restrictions on imports through Israeli merchants.

5. The MoF must adopt a flexible planning methodology for the public budget that takes-into-account systematic and irregular risks surrounding the Palestinian reality. To also bridge the gap in the estimated budgets and actual spending, especially development expenditures that are externally funded.

6. The expenditures’ structure data shows that the problem of spending inflation can be deduced to three main items in the budget: payroll, medical transfer, net lending and security expenses. To solve this issue, studies\textsuperscript{34} suggest that:

\textsuperscript{34} MAS. 2023. Previous source
First: actual and practical implementation of the reform plan, announced by the MoF, that addresses the salary bill; by:

- Regulate government positions; establish regulations on early retirement for public sector employees.
- Restructure government agencies and employees, in this era of the digital economy.
- Adopt and apply the principle of excellence of performance in the various government jobs.
- Adopt the principle of efficiency and quality of spending; raise productivity of public spending based on results, performance and practical, and scientific evaluation of employees’ work.
- Review the Civil Service Law for some salaries, that are considered a formality in terms of performance, might be beneficial (e.g. salaries of the hitherto ineffective PLC). To also review the Retirement Law on Ministers, Governors and PLC Members.
- Cleanout the payroll bill by finalizing the issue of the non-working employees, by either placing them on the structures of vital responsibility centers, refer some to early retirement, and/or terminate services of the rest of them, after carefully considering their files.
- Adopt a systematic staff turnover policy; i.e., the transfer of some employees to other centers of responsibility based on need of the center qualifications and experience of the employee.
- Discontinue the policy of hiring employees on temporary employment contracts or as consultants through exceptions. Such hiring must be based on the provision of financial allocations in the budget for this purpose.
- Take measures to ensure adherence of the responsibility centers to implementing government decisions relating to job privileges such as raises, allowances, travel and other compensations... This means cancelling the margin of exception granted to the concerned minister.

Second: Eliminate or limit net lending, which is extraneous to the budget and contributes to the inflation of expenditures; therefore, it is essential to:

- Setting strict laws and standards for LGUs; collect electricity and water bills by technological methods.
- Apply in practice the set of interventions stated in the government’s plan, which aim at addressing the net lending item; audit medical referrals to Israel; most importantly, establish a specialized and joint unit between the Ministry of Local Government (MoLG) and the MoH to address and follow up on all net lending issues.
- Concerning costs of medical referrals: review and raise health services and health insurance fees to an acceptable limit; especially for the less affected groups (i.e. divide the beneficiaries into three categories, with specific fees for each) and ensure application. This is to raise the level of coverage or to increase revenues of the MoH; pass a law that adopts a comprehensive, efficient, effective and balanced health insurance system, in terms of resources and coverage.

7. Security Services Expenditures:

- Reconsider the number of security agencies and institutions, and the size of each of them; all security agencies, with the exception of the police and customs officers, should be rationalized.
- Reduce the number of employees in each agency separately, in accordance with the tasks entrusted to it. It is advisable to transfer a large number of them to the police or customs police after training them.
- Cancel the 2010 Exceptional Financial Regulations for the Security Services; urgently issue a financial system for security expenditures that considers integrity, transparency and accountability (ITA).
- It is essential that officials tasked with the security services expenditures abide by the provisions of the Procurement, Tenders and General Supplies Law.
- Activate internal and external control; prepare a detailed budget for each security agency separately, then include it in a unified budget, according to its administrative subordination.

**Long Term**

To promote disengagement from the Israeli economy; switch to direct import; strengthen self-capacity of the Palestinian economy and replace with local alternatives to imports from Israel; main suggestions:

It is essential to provide the requirements and conditions for the establishment of a social security fund in order to transfer to it the entitlements of Palestinian workers in Israel.

Activate the understandings reached between the Palestinian and Israeli sides, in 2012 on: the clearing tax mechanism; adopt the actual trade volume not the clearing invoices possessed by each party.

Launch an organized evidence based international campaign against Israel to expose its repeated violations of political and economic agreements with the Palestinians.

The proposed cuts can be divided into two parts: the first is linked to the government’s will, and its capabilities. The second is somewhat linked to variables and factors beyond the capabilities of the government. This figure should be approached with great caution, since it is partially based on estimated data and assumptions, hence subject to increase or decrease, and requires detailed data that is difficult to obtain due to lack of budget transparency.

**Table (1): Estimate- size of the decrease in expenditures according to the financial statements and recommendations proposed in the study**

<table>
<thead>
<tr>
<th>Realization Odds</th>
<th>Expenditures Item</th>
<th>Estimated Decrease Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>High, subject to government will; within its capabilities</td>
<td>Development Expenditures</td>
<td>Postpone (freeze) non-urgent projects (20% of the total development expenditures financed by the treasury)</td>
</tr>
<tr>
<td></td>
<td>Operational Developments</td>
<td>Decrease 5% from operational expenditures.</td>
</tr>
<tr>
<td></td>
<td>Auditing medical transfers</td>
<td>Audit actual and documented expenses= NIS 436 million</td>
</tr>
<tr>
<td>Medium &amp; subject to variables outside the will &amp; capabilities of the government</td>
<td>Salaries &amp; Wages</td>
<td>Implement the 2022 Reform Plan</td>
</tr>
<tr>
<td></td>
<td>Net Lending</td>
<td>Political will, good planning, coordination among stakeholders, &amp; seriousness in implementation reduces 30%</td>
</tr>
</tbody>
</table>
3.2 Possible Solutions-Revenues

Proposals concerning revenues can be summarized as follows:

1. Defer benefits (taxes, customs exemptions & exceptions) for investment projects under the Investment Promotion Law for the coming period. According to the Investment Promotion Authority & Industrial Estates website, the number of projects benefitting from exemptions and privileges reached 412 in various fields. Now, assuming that the average capital of the project is $5 million (about two billion dollars for all projects); and the annual profit rate is 10% ($200 million), exempt from income tax of 15%, the estimated revenue that can be collected from such projects, is about ($30 million annually).

2. Intensify coordination between the MoF and MoNE concerning basic (food) commodities subject to the Commodity Quota System that are imported duty-free, and ensure consumers benefit from these exemptions through reduced prices. Otherwise, stop tariff exemptions that benefit importers if they don’t comply with price reductions.

3. Oblige senior taxpayers to pay early (prompt) tax on their expected profits for the current year, hence providing instant cash.

4. Urge companies to intensify social responsibility, directing them to provide relief and health care, and reduce their taxes.

5. The government, with international support, must introduce a comprehensive and unconditional “emergency basic income” plan, as an integral part of a coherent “recovery” program. The suggestion is to establish a donation fund to help raise several million dollars needed to fund a small basic income pilot project in one selected region examining best methods to introduce and implement an emergency basic income for ordinary residents.

6. Exhaust efforts to urge the international community to increase financial and humanitarian support primarily to Gaza, and the WB.

7. Motivate taxpayers to comply/tax incentives such as: tax processes of losses carried from previous years; using the accelerated depreciation method for calculations; permanent and temporary exemptions; discriminatory tax rates; export and import incentives; incentives related to the collection mechanism and payment times.

8. Urge banks to take a more active role by postponing loan installments, whether to the government or to public sector employees. Note that, the PMA issued instructions to banks regarding the postponement of installments for employees in March 2024; this could be applied to government loans as well.

Medium Term

1. Enact a modern Palestinian law to deal with property tax in parallel with the completion of the land settlement project.

2. Amend the Income Tax Law Decree, to become 4 tax brackets on individuals, ranging from 5%-20%, and impose a three tax brackets on companies, ranging from 15-25%. This may increase revenues by 3.37%. (in 2022, the revenues generated amount was NIS 16.2 billion multiplied by 3.37%), i.e., an increase of 546 million NIS.

3. Propose strategies for the development of the income tax system in Palestine that addresses the development of: tax legislation on income tax; income tax payments; area of funders/taxpayers of income tax; tax accounting; and the investment activity environment.

4. Coordinate with Arab countries to absorb the largest number of workers who usually work in Israel, according to specific criteria and time periods until the current crisis is overcome. While in the mean-time, thinking of other temporary and strategic solutions to integrate these workers in the local economy, or try to mitigate the social repercussions that accompany unemployment.

5. Mobilize financial resources (local, foreign, public and private investment and foreign grants) to invest in development projects that contribute to disengage from the Israeli economy, and increase the national product. Suggested projects: cement plant, iron and steel products factory, oil refinery, renewable energy, electricity generation, animal feed factory, Water & Wells projects. Finally, invest in advanced health institutions that include all specialties and qualified human resources, which will decrease medical transfers and treatment.

6. Benefit from the current situation concerning the clearance funds being in the spotlight of international attention who’s concerned with the Palestinian issue and its serious repercussions on the ground. Within this context, the Palestinian decision-maker must take advantage of the current circumstance to include the issue of financial leakage and take steps to correct the clearing tax mechanism to stop it and to formulate a contractual relationship in the interest of Palestinians.

7. Benefit from the powers conferred by the Paris Protocol (Article 10/a); importing oil derivatives from neighboring countries other than Israel. Also, increasing electricity interconnection projects from Jordan and Egypt. This should reduce the import invoice from Israel and limit financial leakage.

8. Reforming the Income Tax System: Policies to Follow

   8.1 The possibility of expanding and enhancing an ascending tax -bracket system through registered or unregistered taxpayers, or by adding new taxpayers to the income tax system. This requires consensus of all components of the Palestinian society including: academic institutions, unions, professional federations, chambers of commerce and CSOs must all be involved in setting objectives.

   8.2 Improve tax efficiency and combat tax evasion by criminalizing tax evasion and providing an effective executive team for tax follow-up and prosecutions; reinforce the judiciary to enable it to address tax evasion cases.

   8.3 The government is expecting\(^38\) a 10% rise in 2024 in revenues from local VAT due to the approval of the Value Added Tax Law Decree (That’s about NIS 621 million). However, this item is linked to the approval of the proposed mentioned law awaiting signature by the PA President.\(^39\)

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39. Interview with Mr. Emad Abu Subha, General Director of Income Tax at the MoF. Interview was conducted on 2024/4/7.
Long Term:

1. Activate the fiscal policy: by changing the philosophy on which Palestinian fiscal policy is based (Financial reform programs), to become a tool in achieving economic and social goals.

2. Raise the issue of Palestinian control over crossings internationally, especially with regard to trade relations with the world.

3. Since the Paris Protocol can only be legally amended with the consent of both parties, the only choice left is to demand the implementation of its provisions, and request for the Joint Economic Committee and its Technical Committees to meet.\(^\text{40}\)

4. Other practical alternatives include Palestine’s accession to the World Trade Organization.\(^\text{41}\)

5. The Trade Facilitation Agreement must be enforced in the OPT regardless of whether Palestine is a member of the WTO Agreement or not. It is essential that this agreement is applied in order to remove restrictions imposed by Israel on Palestinian trade.\(^\text{42}\)

6. Ensuring Israel’s compliance with the Trade Facilitation Agreement in terms of applying it to Palestinian external trade requires a series of measures; to free it of the exclusive unilateral Israeli domination and transfer it to the binary and multiple dimensions required.\(^\text{43}\) Requirements include: building a “trade partnership” with friendly countries (e.g. Turkey, Jordan, Egypt, Morocco, Saudi Arabia), as members of the WTO, which can serve as an entry point for raising controversial issues. Moreover, Israel’s legal obligations under the 2013 Trade Facilitation Agreement, is to treat Palestinian foreign trade as it does to its own, while its numerous and repeated violations damage its trade with a number of friendly countries.\(^\text{44}\)

Table (2) below illustrates the possible increase in revenues, the rest of the proposals require more accurate data. The targeted increase can be divided into two parts: first: subject to the government will and capabilities. Second: linked to variables outside capabilities of the government.

<table>
<thead>
<tr>
<th>Realization Odds</th>
<th>Revenue Item</th>
<th>Revenue Opportunities</th>
</tr>
</thead>
<tbody>
<tr>
<td>High and subject to the will of the government; within its capabilities</td>
<td>Investment Promotion Law Exemptions</td>
<td>Postponing exemptions for investors</td>
</tr>
<tr>
<td></td>
<td>Collecting part of the income tax in advance</td>
<td>Collecting annual income tax from large taxpayers in advance (Estimated at 10% of total income tax) 10% of 860</td>
</tr>
<tr>
<td>Medium &amp; subject to variables outside the will and capabilities of the government</td>
<td>Financial Leakage</td>
<td>20% reduction in financial leakage,</td>
</tr>
<tr>
<td></td>
<td>Tax Evasion</td>
<td>20% reduction in financial leakage,</td>
</tr>
<tr>
<td></td>
<td>Value Added Tax (VAT) income tax</td>
<td>Revenues increase by 2024.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Revenues increase, due to tax bracket adjustment</td>
</tr>
</tbody>
</table>

\(^{40}\) MAS, (2019). Previous source.
\(^{41}\) UN Conference on Trade and Development (UNCTAD), 2015, WTO Trade Facilitation Agreement 2013: Israel’s Commitments to Palestinian Trade. UN, Geneva
\(^{42}\) UN Conference on Trade and Development (UNCTAD), 2015. Previous source.
\(^{44}\) MAS, 2019, previous source.
4. Conclusion

This paper aimed to identify areas of controlling and reducing public spending, and increasing revenues to face the current deficit and financial crisis. It noted that the current financial crisis is the most profound and complex since the establishment of the PA, and not the result of the war on Gaza. In this regard, many reports warned of a severe financial crisis if urgent measures are not taken to rectify the situation. The persistence of the main causes of the crisis will reduce the chances of remedying the issue in the short term, these are: occupation measures, structural imbalances and absence of accountability.

More than once, the government announced its intentions to apply rationalization’s policy and procedures to face the financial crisis. However, these efforts did not bear real results towards reducing the budget deficit in a sustainable manner for many reasons, mainly: its failure to fundamentally reduce expenditures due to the absence of a well-thought-out vision and plan. Or due to the weak impact the targeted expenditures had on the current expenditures.

The PA’s ability to cope with repercussions of this crisis is very limited, since it lacks the resources and financial capacity. Also, carrying out its administrative responsibilities has become hostage to the occupation’s decisions and donor countries that provide support, at a time when the stricken GS needs all available resources and more. Moreover, the uncertainty of clearance revenues adds insult to injury, i.e. Israel’s unwillingness to transfer these funds. The paper provided many recommendations that are doable in the short, medium and long terms. However, since the current crisis is embedded with unprecedented economic and financial consequences, the government must rethink its work methodology where decisions and policies taken must be based on partnership with other sectors.

The budget’s expenditures can be sorted into two categories: first- contractual expenses, which cannot be annulled immediately since they are of legal status, and second, expenditures that are unlinked to contracts where it is possible to reduce spending in many areas such as: operating expenses linked to travel missions; petty cash; government purchases of capital goods; suspension of contracts and consultations employment; addressing the phenomenon of ghost employees; immediate freezing of a number of non-urgent development projects. Similarly, revenues are divided into two parts: first: revenues that can be collected before their due date, such as: income tax owed by dominant companies; banks; insurance companies and other top taxpayers. The second part of revenues also includes exemptions and benefits granted to investors under the Investment Promotion Law. However, this can be postponed or stopped for the time being.
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Civil Society Team for Enhancing Public Budget Transparency

AMAN has worked to establish a civil team to support the transparency of the public budget, representing a number of Palestinian sectoral civil organizations, namely: Aman Foundation, Miftah Foundation, Center for Democracy and Workers' Rights, Hydrology Society, Creator's Teacher Center Development work - together, the Union of Agricultural Work Committees, the Federation of Food Industries, the Federation of Pharmaceutical Industries, the Federation of Chambers of Commerce, Agriculture and Industry, the Palestinian Federation of Local Authorities, the Network of NGOs, the Economic Policy Research Institute (MAS), the Law Center Ah Civil Society Development, a forum of intellectuals Charity Association, Conscience Foundation, Al-Haq, the Institute of Development Studies) Birzeit (University, Jerusalem Center for Legal Aid and the Jerusalem Center for Social Rights and the Economic Commission national civil organizations Palestinian, as well as some economic experts.

AMAN performs secretarial work for CSTPBT, through providing logistical and technical support to it in light of insufficient and unstable financial capabilities. AMAN invites for CSTPBT meetings and prepares the agenda of meetings and minutes, in addition to any papers and documents related to the public budget, working as a bridge between the team and the official authorities, presided by the Ministry of Finance. With the vital support of AMAN, CSTPBT team participated in a number of training workshops to build their capacity in the public budget field.

The CSTPBT team believes in the urgent need of informing the citizens about the public budget to participate in its preparation, in order to be able to hold it accountable and follow up the management of government spending and public money. To achieve this goal and before approving the budget of 2011 specifically, the CSTPBT team submitted a proposal to the Ministry of Finance & Planning, requesting the adoption of the citizen’s budget, which is one of the basic elements that guarantee the transparency of the public budget. Indeed, the Ministry adopted the proposal and instructed to manage the public budget in cooperation with the CSTPBT team in this field. The citizen’s budget was issued for the first time in Palestine during the year 2011, and it was developed to become the citizen’s guide during the year 2013 where the national team will work to raise the awareness on it. Moreover, Aman succeeded recently in convincing the Council of Ministers of the need to involve civil society organizations to cooperate with the ministries in discussing annual budgets before submitting them to the Cabinet for approval.

Specialized sub-committees were formulated from the members of the CSTPBT, focusing on three main essential sectors (Health, Education, Social development). Each sub-committee has a leading organization that is in charge of it.

Aman will work in the future to establish the monitor unit, which will be specialized in following up on all issues related to the public budget, thus creating a reference for all interested citizens, researchers and various institutions.