



Analytical Working Paper

## **The Palestinian Public Budget: Estimated vs. Actual**

**First Half of 2016**

**September 2016**

## Introduction

**This analytical paper consists of three sections:**

- **Section I:** this section addresses and discusses the extent by which the Ministry of Finance (MoF) complies with the legal references governing the Palestinian Public Budget: provisions in the Palestinian Basic Law; the Budget Planning and Financial Affairs Law No. 7 of 1998, as well as other related legislations. It also examines the extent by which the MoF respects transparency principles of the Public Budget.
- **Section II:** this part of the paper presents an overview of items illustrated in the 2016 Budget through a comprehensive analysis by comparing the estimated numbers with what was achieved in the first half of 2016 budget (i.e., actual).
- **Section III:** this section will present the conclusions and recommendations of the paper.

This analytical paper seeks to review the 2016 Public Budget adopted by President Mahmoud Abass on January 8, 2016<sup>1</sup>, and to compare it with what has been achieved in the first half of year as well as with what was achieved in the same period of 2015, as needed.

It is worth noting that the analysis of this paper is a commitment based analysis of revenues and expenditures illustrated in the 2016 budget. The paper perceives the Public Budget as the key financial tool and budget schedule of the Palestinian National Authority (PNA), which details all expenses and revenues of the various activities included in a given fiscal year to accomplish financial, political, economic, social, and developmental goals and policies. The Budget also reflects future government's trends, programs, and policies regarding the various economic, financial, social and development fields.

This paper was prepared based on MoF data updated on August 21, 2016<sup>2</sup>. The information was accumulated by the researcher directly from the ministry's official website<sup>3</sup> and other pertinent documents, including the cumulative financial report for December 2015<sup>4</sup>, and the Decision by Law No.(1) for 2016, on the Public Budget for the fiscal year 2016, issued on January 8, 2016.

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<sup>1</sup> Decision by Law No.(1) for 2016 on the Public Budget for the 2016 fiscal year, issued on January 8, 2016.

<sup>2</sup> Mid-year Financial report, June 2016 report, issued by the Ministry of Finance and Planning on July 7, 2016.

<sup>3</sup> [http://www.pmof.ps/documents/10180/813287/merged\\_2016+june+laaast+final+arab.pdf](http://www.pmof.ps/documents/10180/813287/merged_2016+june+laaast+final+arab.pdf)

<sup>4</sup> Cumulative financial report-December 2015, issued by the Ministry of Finance and Planning on January 17, 2016.

## Section I

### Legal Dimensions of the Public Budget Bill for the fiscal year 2016

In this section we will review and discuss the extent of the MoF commitment to the legal references governing the Budget. This includes related provisions of the Palestinian Basic Law, the Budget Planning and Financial Affairs Law No. (7) of 1998, and other related legislations. We also will examine the extent by which the MoF respects transparency principles in management of the Public Budget.

By reviewing related data issued by the MoF on the 2016 Public Budget and comparing it with the Budget Planning and Financial Affairs Law No. (7) of 1998<sup>5</sup>, and related legislations, it is possible to note the following:

1. The legal deadlines for the preparation and approval of the 2016 Public Budget Bill were not met. As it was, the Bill was not submitted to the Palestinian Legislation Council (PLC) at the beginning of November 2015 in accordance with provisions of article (a/3) of the regulating Budget Law<sup>6</sup>. (Dysfunction of the PLC does not exempt the government from its obligation to present the Budget Bill on time (i.e., at the beginning of November 2015).
2. The 2016 Budget Bill did not include the economic and social objectives that the PNA intends to accomplish, partially or entirely, during the Budget Bill's year. It also did not mention the rationale behind the amount and priorities of spending; noting that this was published in the "book of the Public Budget" which was issued by the MoF on June 22, 2016 hence did not coincide with time of approval of the Decision by Law.
3. The President adopted the draft Public Budget Bill through a Decision by Law within the specified timeframe as stipulated in the legal provisions governing the budget, which is the end of the previous budget year<sup>7</sup> (i.e., December 31, 2015). The budget was formally adopted on January 8, 2016 by a Decision by Law as mentioned. This does not mean that the Budget was discussed and approved by the PLC in accordance with article 3 of the Public Budget Bill. The budget did not take into consideration the right of Civil Society Organizations (CSOs) and citizens (the biggest source of the Public Budget's revenues) to review and comment on the draft before approval. Moreover, the participatory approach, declared by the government time and time again was lost in the process.
4. The government issued the citizen's budget on June 16, 2016, only in English<sup>8</sup>. This defeats the purpose as this document was founded on the basis of addressing the Palestinian citizens and to be written in simple language (i.e., Arabic). This raises the question of whether the budget was issued only to appease donors by indicating that the MoF is committed to preparing and publishing it?

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<sup>5</sup> Budget Planning and Financial Affairs Law No. (7) of 1998.

<sup>6</sup> Budget Planning and Financial Affairs Law No. (7) of 1998, article No (3/a).

<sup>7</sup> Budget Planning and Financial Affairs Law No. (7) of 1998, article No ( 3/g)

<sup>8</sup> Official Website for the MoF and Planning-Citizen's Budget 2016.

5. The 2016 Budget Bill did not include schedules defined in Article 21 of the Budget Planning and Financial Affairs Law<sup>9</sup>, including:
  - a. An illustrative chart for the financial and cash status of the public treasury account.
  - b. An illustrative chart for the PNA stating long and short term debts or loans, as well as payment or collection plans.
  - c. An illustrative chart of the PNA's shares and investments in national and international companies and commissions.

The Budget Bill only included key data without any disclosures, or detailed information or figures. The Draft Budget Bill was published six months after approval by the President.

6. Proper accountability for expenditures has been completely paralyzed due to the absence of final accounts for the years: 2011, 2012, 2013, 2014 and 2015. Furthermore, this absence makes it difficult to assess compliance with enacted public budgets, since these final accounts were never audited by the State Audit and Administrative Control Bureau (SAACB). This indicates serious problems in the accountability system of the budget due to the time laps of five years, if we are talking about the 2011 final account for example, or may be more if it continues.

**Conclusion I:**

There are serious problems in applying principles of transparency in relation to disclosure of the Public Budget with all its details, according to the Budget Planning and Financial Affairs No.7 of 1998. Problems also exist in applying the law in regard to submission of the draft budget to the PLC, two months before the end of the year, as stipulated in article 61 of the Amended Basic Law of 2003<sup>10</sup>, and relevant provisions in the Budget Planning and Financial Affairs No.7 of 1998. And finally, there is a problem in the transparency and partnership approach applied in drafting the Budget, as well as in provisions of final accounts data and audited reports for the past years.

**Structure of the Budget**

Although the PNA has adopted the Budget program schedule, structure of the Public Budget remained in the form of items, especially financial reports issued by the MoF and Planning. This is presented in the form of grouped-items and is divided into: salaries and wages, social contributions, use of goods and services, transferable expenditures, capital expenditures, and developmental expenditures. These items show only sum-lump figures with no details or link to the program or extent of achievement desired, which leads to the absence of transparency and accountability. There is an urgent need for financial reports to include details related to the budget program and activities **for the purpose of greater transparency hence enabling the rationalization of expenditures and implementing the austerity plan more effectively.**

<sup>9</sup> Budget Planning and Financial Affairs Law No. (7) of 1998., article No. (21)

<sup>10</sup> Amended Basic Law, 2003, article (61).

## Section II

### Mid-Year Review and Analysis of the 2016 Public Budget Bill

This section presents a detailed explanation and analysis of the 2016 Public Budget items, comparing the estimated with the actual after six months of the Budget's approval. Analysis in this section relied on information contained in the MoF mid-year financial report posted on the Ministry's official website.<sup>11</sup>

Also in this section, data and analysis of the 2016 Budget will be presented in charts and graphs and will cover the following:

- Presentation and analysis of revenue estimates for 2016.
- Presentation and analysis of aid and grants estimates for 2016.
- Presentation and analysis for public expenditures and related issues estimates for 2016.
- Presentation and analysis of net lending estimates for 2016.
- Presentation and analysis of the financial deficit, arrears, and bank financing estimates for 2016.
- Presentation and analysis of the public debt for 2016.
- Presentation and analysis of allocations of responsibility centers related to the social sector.
- Presentation and analysis of special topics pertinent to the 2016 Public Budget:
  1. Financial reserves.
  2. PLC budget.
  3. Allocations for centers of responsibility.
  4. Transformational expenditures

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<sup>11</sup> Mid-year financial report, June 2016 monthly report, issued by the MoF and Planning on July 21, 2016.  
[http://www.pmof.ps/documents/10180/813287/merged\\_2016+june+laaast+final+arab.pdf](http://www.pmof.ps/documents/10180/813287/merged_2016+june+laaast+final+arab.pdf)

### First: Revenue analysis

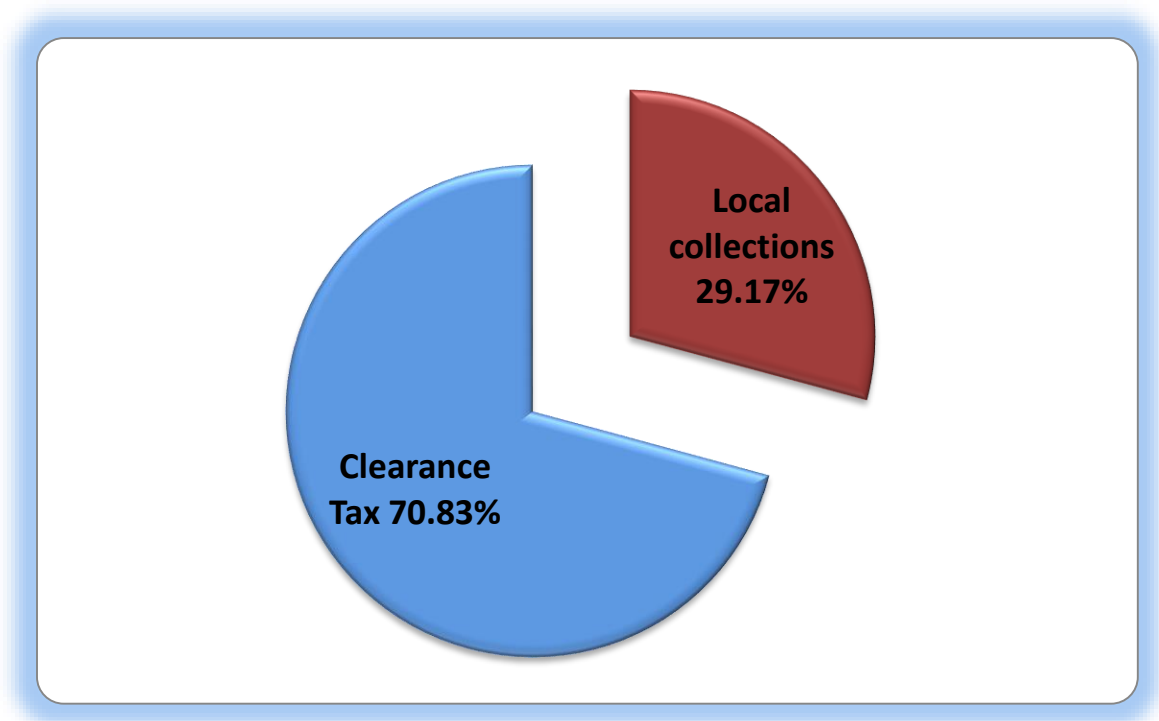
Approximately 11,630<sup>12</sup> million Israeli Shekels (NIS) was estimated for the 2016 public revenues; an increase by 5.17% from the planned in 2015 Budget, which was estimated at 11,058<sup>13</sup> Million NIS. Local revenues fall within two key items:

- Local tax collection, which was estimated in the 2016 Public Budget at 3,393 million NIS.
- Clearance revenues, which was estimated in the 2016 Public Budget at 8,237 million NIS.

Furthermore, tax refunds amounted to 441 million NIS.

Therefore, the total net revenues in the 2016 estimated budget amounted to 11,189 million NIS, while in the 2015 it was estimated at 10,658 million NIS (approximately 5%)

**Figure I: 2016 Public Budget revenue estimates in %**



- **Local Revenues:**

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<sup>12</sup> Decision by Law No.1, for 2016, on the Public Budget for the financial year 2016, issued on January 8, 2016.

<sup>13</sup> Decision by Law No.9, for 2015, on the Public Budget for the financial year 2015, issued on June 6, 2015.

Local revenues are divided into two parts: **the first part** constitutes revenues collected directly by the Palestinian government; these are: tax revenues, non-tax revenues, and revenues from PNA investment profits. **The second part** comes from indirect sources such as the clearance tax collected by Israel and is transferred to the PNA. Clearance tax falls into six key items: customs; VAT (added tax), purchase tax, hydrocarbon tax, income tax, and other taxes.

**Figure 2: Net revenues: estimated vs. actual in the first six months of the 2016 Budget (million NIS)<sup>14</sup>**

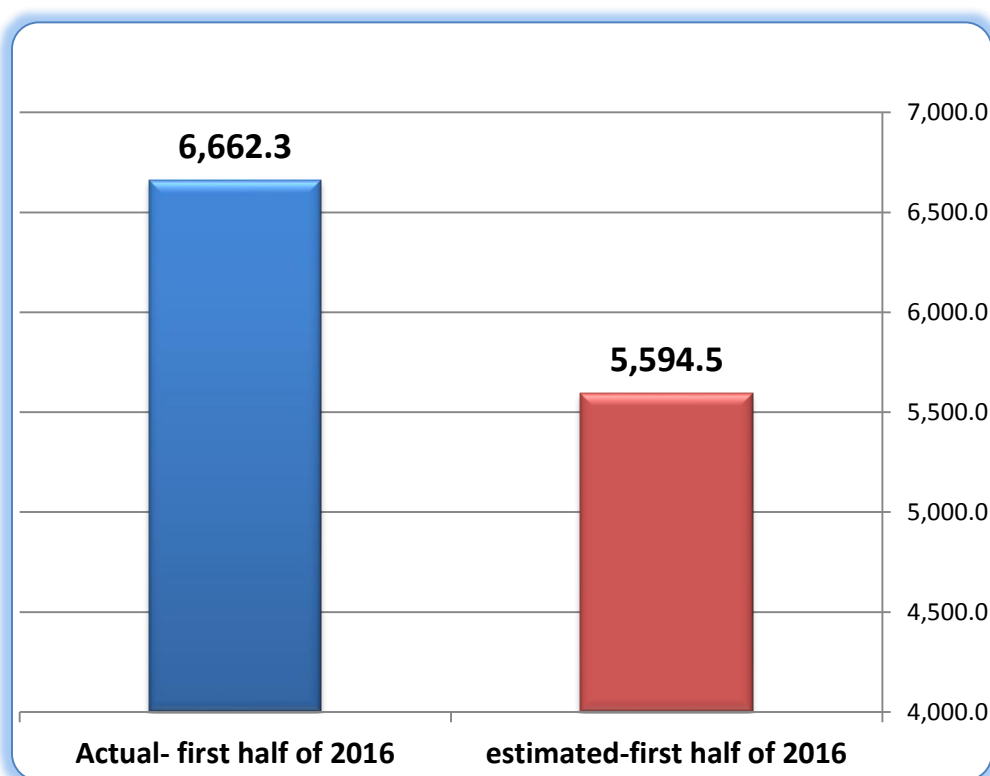


Figure no. 2 above shows that the total net revenues of the budget for the first half of 2016 are higher than the estimated amount reaching 6,662.3 million NIS. While the estimated amount for the same period was 5,594.5 million NIS. This means that 60% of the total net revenues of the whole 2016 Budget were achieved during the first six months of the year; an increase of 19.01% from the estimated amount for half of the year.

By analyzing the structure of the revenues, we notice that the actual local and clearance revenues are higher than the estimated. This is due to several reasons:

- Improvement in tax collection; whether at the level of local taxes or as a result of improvement of clearance procedures with the Israelis.

<sup>14</sup> Mid-Year Financial report, June 2016, monthly report. Table No. 1, issued by the MoF on June 21, 2016.

- Tunnels closures between Egypt and Gaza, which led to stopping the flow of goods and merchandise through these tunnels. This meant that goods can only enter via Israel, hence taxes are paid and are included in the clearance revenues.
- Citizens and merchants paid their taxes during the first half of the year in order to benefit from special offers available. Therefore, tax revenues were higher during the first three months of 2016.

Table 1 below illustrates clearance revenues during the first six months of 2016<sup>15</sup> in comparison with the same period in 2015<sup>16</sup>, and the estimated budget for clearance revenues during the first half of 2016.<sup>17</sup>

**Table No.1:**

**Comparative data: estimated clearance revenues-1<sup>st</sup> half of 2016; actual in 1<sup>st</sup> half of 2016; actual in 1<sup>st</sup> half of 2015 (million NIS)<sup>18</sup>**

| Item               | Estimated budget: 1 <sup>st</sup> half of 2016 | Actual:1 <sup>st</sup> half of 2016 | Actual:1 <sup>st</sup> half of 2015 |
|--------------------|------------------------------------------------|-------------------------------------|-------------------------------------|
| Clearance revenues | 4,118.5                                        | 4,641.2                             | 3,883.7                             |

<sup>15</sup> Mid-Year Financial report, June 2016, monthly report. issued by the MoF on July 21, 2016.

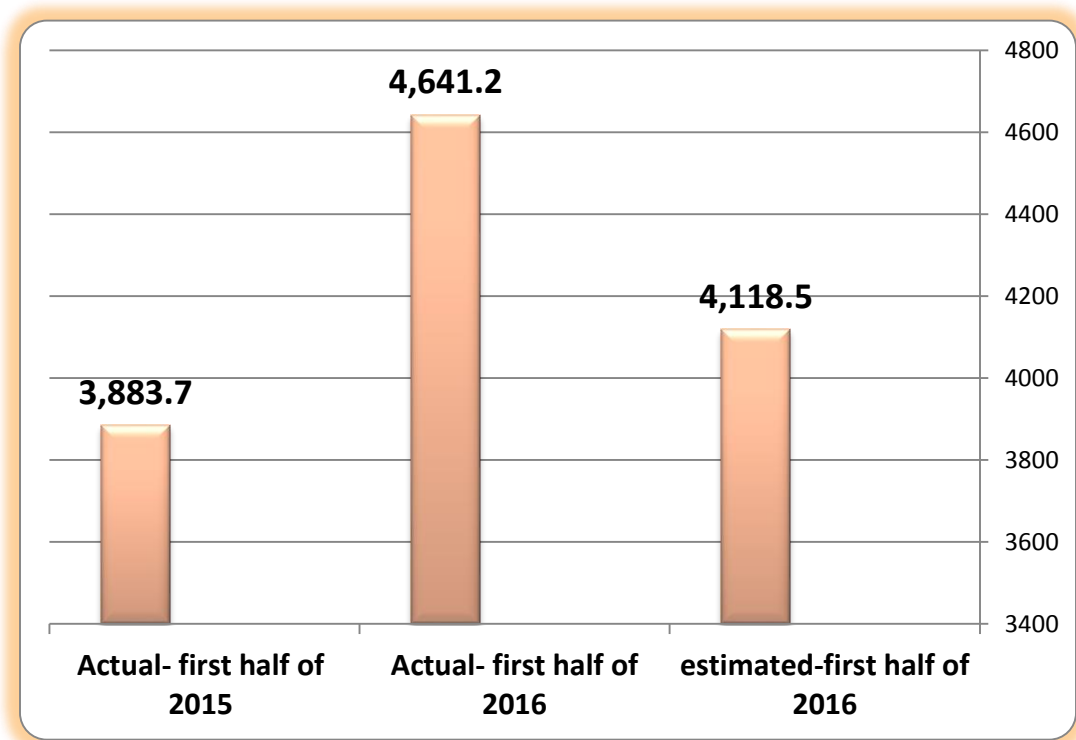
<sup>16</sup> Mid-Year Financial report, June 2015, monthly report. issued by the MoF on July 28, 2015.

<sup>17</sup> Decision by Law No.1 for 2016, on the financial year 2016, issued on January 8, 2016.

<sup>18</sup> Mid-Year Financial report, June 2016, monthly report. issued by the MoF on July 21, 2016.

**Figure No. 3**

**Comparative data: estimated clearance revenues-1<sup>st</sup> half of 2016; actual-1<sup>st</sup> half of 2016; actual-1<sup>st</sup> half of 2015 (million NIS)**



**Conclusion 2:** the figure above shows that the actual net for public revenues was higher than the estimated amount. It is also higher than the actual amount accomplished in the 2015 budget. These are good indications if sustained until the end of the year, although it is too soon to evaluate without tying it to the economic context.

## Second: External Aid and Grants

Aid and grants or external support continues to constitute a major and important source of revenue for the PNA. And due to the difficult political circumstances the Palestinian occupied territories are under, these grants are given twice a year. Therefore, any delay or withholding of these aids, which occurred in 2015 and in other previous years, will inevitably cause a deficit in the Public Budget, and consequently have significant adverse effect on implementation of the budget, financially and economically.

Table 2 below compares the 2016 estimated external aid and grants for either Budgetary support or Development Expenditure with the actual funding received during the first half of 2016 (million NIS).

**Table No. 2**

Comparing the estimated 2016 external funding for either budget or development expenditure with the actual funding, in the first half of 2016<sup>19 20</sup>

| Item                               | Estimated 2016 Budget | Actual amount achieved during the 1 <sup>st</sup> half of 2016 | Actual percentage during the 1 <sup>st</sup> half of 2016 |
|------------------------------------|-----------------------|----------------------------------------------------------------|-----------------------------------------------------------|
| Funds for Budget support           | 2,925                 | 1,015.4                                                        | 34.71%                                                    |
| Funds for development expenditures | 956                   | 190                                                            | 19.87%                                                    |

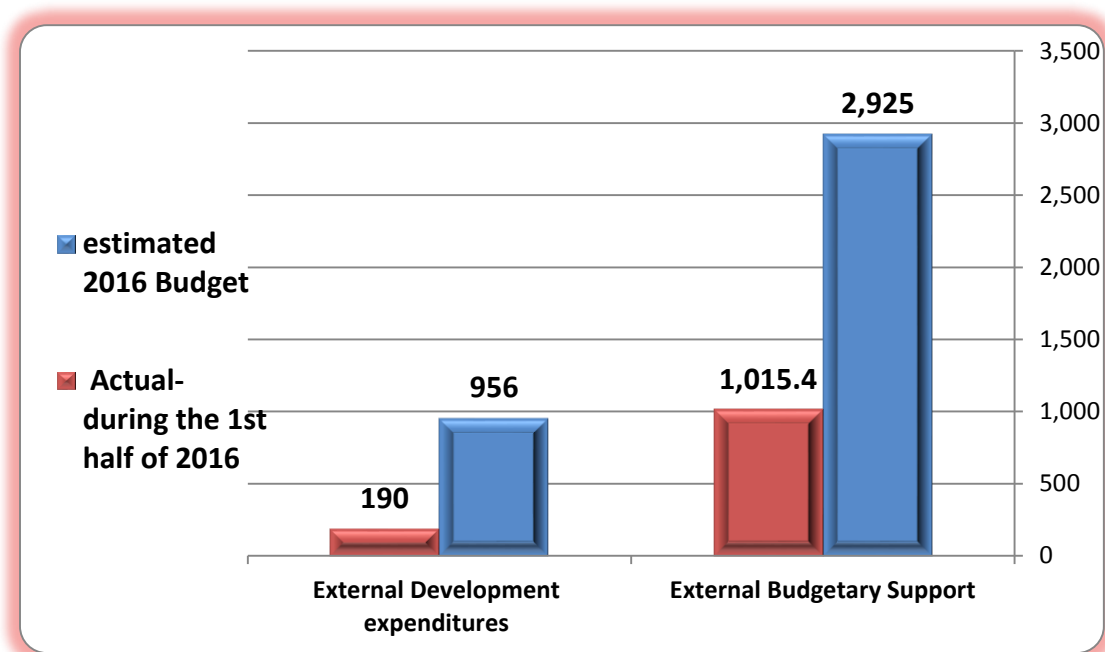
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<sup>19</sup> Decision by Law No.1 for 2016, on the Public Budget 2016 financial year. Issued on January 1, 2016.

<sup>20</sup> Mid-year Financial Report, June 2016 monthly report, table 1. Issued by the MoF on July 21, 2016.

**Figure No. 4**

**Comparative figures: External support and development expenditure in the 1<sup>st</sup> half of 2016- the estimated vs. the actual (million NIS)**



It is evident from table 2 and figure 2 above that the budgetary support for the Budget and development expenditure, as in previous years, did not reach the expected level.

The data above reveals the 34.37% of the external budgetary support for 2016 was accomplished in the first half of 2016. It also reveals that what actualized for development expenditures did not exceed 20% of the planned during the first half of 2016.

**Conclusion 3:** it is clearly evident that despite low estimates expected for external funding, the amount received is far less than the estimated, which creates an increase in the budget deficit, and causes a serious problem in the implementations of plans and activities that depend on this funding.

### Third: Expenditure Analysis

The total expenditure and net lending estimated in the 2016 Public Budget accounted for (15,212)<sup>21</sup> million NIS, marking a slight increase from the 2015 estimated Budget, which was (15,085)<sup>22</sup> million NIS. Table 3 below illustrates the estimated expenditures:

**Table No. 3**

#### **Total Expenditure and Net Lending: Estimated Vs. Actual (million NIS)<sup>23</sup>**

| Item                      | Actual: 1 <sup>st</sup> half of 2016 | 2016 Budget      Estimated | Actual ratio:1 <sup>st</sup> half of 2016 |
|---------------------------|--------------------------------------|----------------------------|-------------------------------------------|
|                           | Million NIS                          | Million NIS                | %                                         |
| Total Expenditures        | <b>7,976.4</b>                       | <b>15,212.0</b>            | 52.43%                                    |
| Wages and Salaries        | Deci3,856.3                          | 7,662.0                    | 50.33%                                    |
| Social Contributions      | 371.2                                | 723.0                      | 51.34%                                    |
| Goods and Services        | 1,080.8                              | 2,056.0                    | 52.57%                                    |
| Transferable Expenditures | 1,812.0                              | 3,599.0                    | 50.35%                                    |
| Capital Expenditures      | 13.4                                 | 54.0                       | 24.81%                                    |
| Interests                 | 80.2                                 | 269.0                      | 29.81%                                    |
| Net Lending               | 521.9                                | 850.0                      | 61.40%                                    |
| Embarked Payments         | 240.6                                |                            |                                           |

\* Embarked payments are taxes and revenues pertaining to Local Government Units (LGU); 90% of property tax, and 50% from transportation taxes.

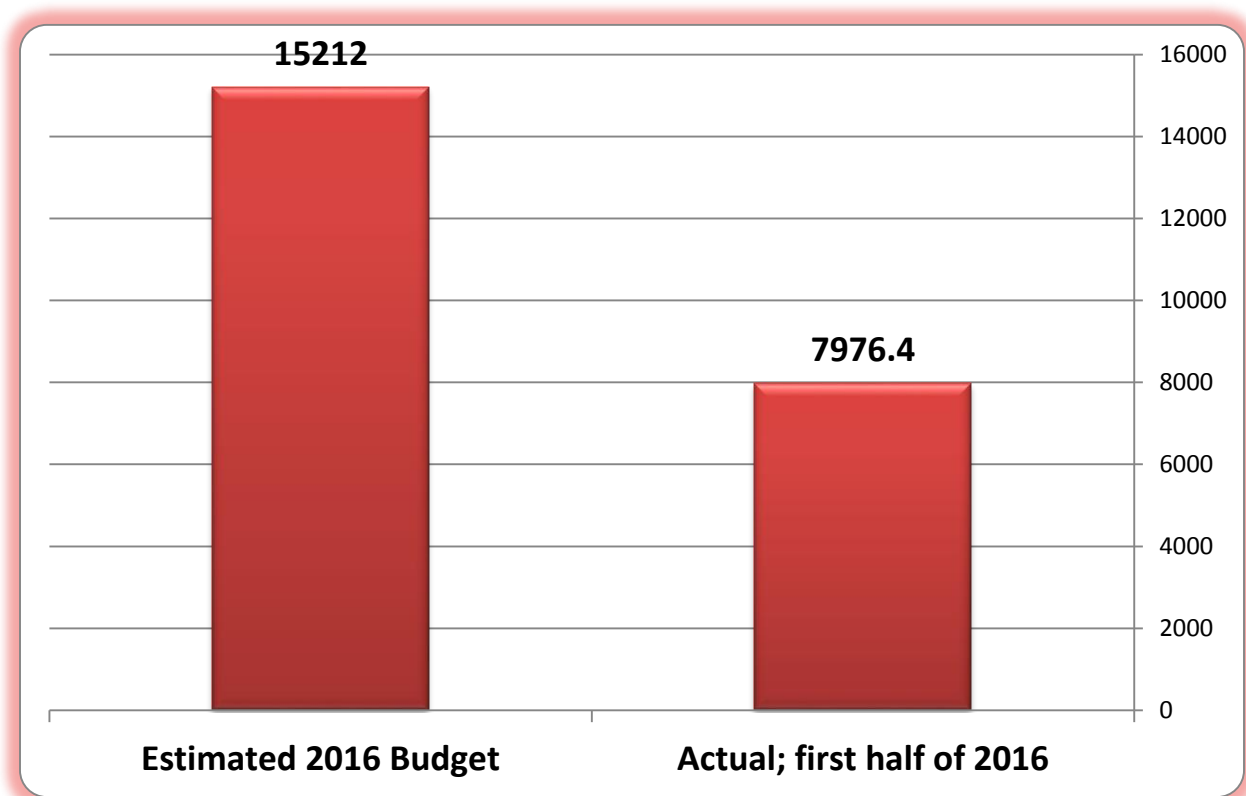
<sup>21</sup> Decision by Law No.1 for 2016, on the Public Budget 2016 financial year. Issued on January 8, 2016.

<sup>22</sup> Decision by Law No.9 for 2015, on the 2015Public Budget. Issued on June 30, 2015.

<sup>23</sup> Mid-year financial report 2016, June monthly report, table 1. Issued by the MoF on July 21, 2016.

**Figure No. 5**

Total Expenditure: Estimated vs. Actual (million NIS)



**Table 3 and Figure 5 illustrate the following:**

- An apparent increase is noticed in the actual total expenditures for the first half of 2016 reaching 52.43% of the planned for the whole year; where actual expenditures amounted to 7,976.4 million NIS from a total of 15,212 NIS estimated for the whole of 2016. The significant increase mentioned comes in light of the government's launching of its austerity and rationalization plan and the existence of a funding gap in the 2016 budget.
- In the first half of 2016, expenditures for goods and services increased, accounting for 52.57% of the amount allocated for this item for the period mentioned, despite that this item is targeted in the government's austerity and rationalization plan.
- Net lending, during the first six months of the year accounted for 61.40% of the total allocated finances for 2016; reaching the amount of 521.90 million NIS.
- A decrease from the estimated amount was noticed in capital expenditures. However, it did not affect the total expenditures given that the amount allocated for that item is only 54 million NIS.

**Conclusion 4:**

Despite the rationalization measures trumpeted by the government to reduce operational expenditures including those related to “goods and services”, this item not only was not reduced, but has increased by 50% in the first half of 2016. This is despite the existence of a budget deficit and funding gap the government spoke of over-bridging. In this regard, the Civil Society Team, in the past had repeatedly recommended that the operational expenditures be controlled in addition to developing an austerity and rationalization plan.

Therefore, in order to avoid repetition of the state of affairs of 2014, and 2015, the Civil Team recommended the adoption of its austerity and rationalization plan.

#### Fourth: Net Lending

In the 2016 Public Budget, net lending was estimated at 850<sup>24</sup> million NIS, while in the 2015 Budget the estimated amount was 800<sup>25</sup> million NIS; while in the 2014 Budget, it was estimated at 600<sup>26</sup> million NIS, indicating a steady rise.

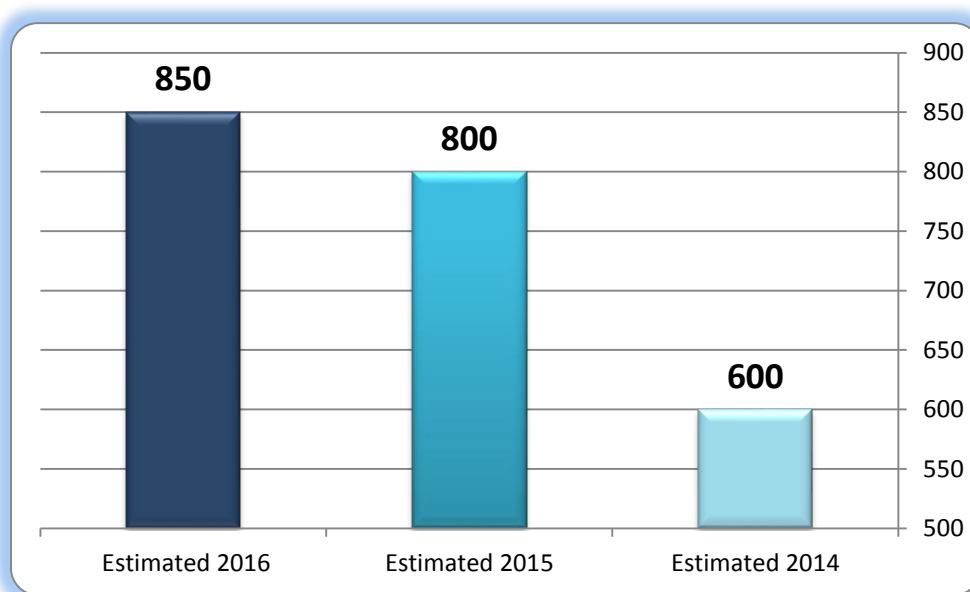
**Table No.4**

**The Estimated Net Lending item: years 2014-2016 (million NIS)**

| Item        | 2014 Budget | 2015 Budget | 2016 Budget |
|-------------|-------------|-------------|-------------|
| Net Lending | 600.00      | 800.00      | 850.00      |

**Figure No. 6**

**Estimated Net Lending Item: Years 2014-2016 (million NIS)**



<sup>24</sup> Decision by Law No.1 for 2016, on the Public Budget 2016 financial year. Issued on January 8, 2016.

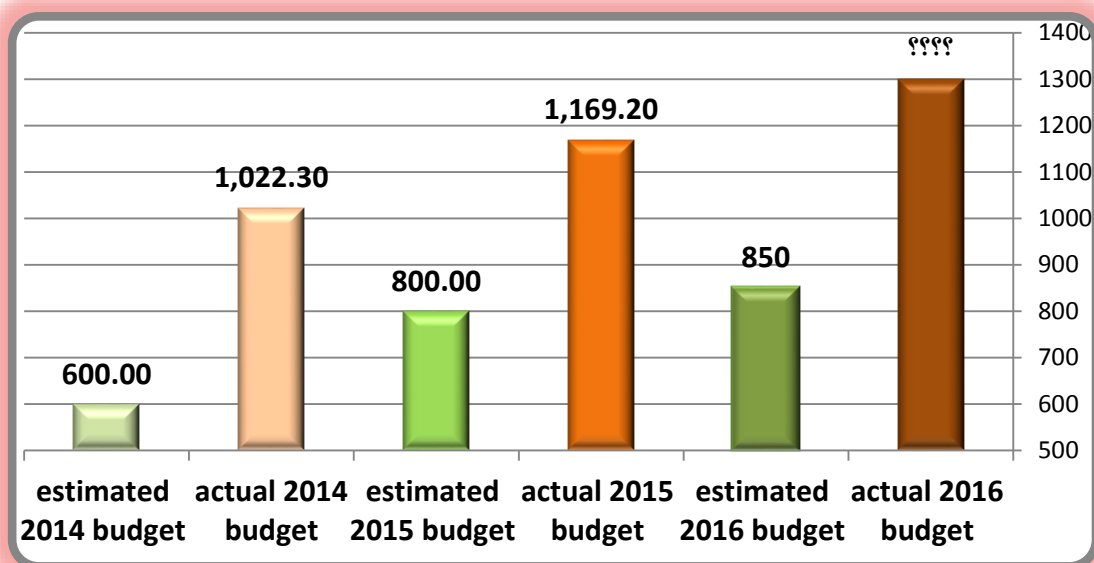
<sup>25</sup> Decision by Law No.9 for 2015, on the Public Budget 2015. Issued on June 30, 2015.

<sup>26</sup> The 2016 Budget Bill, MoF.

Despite the large sums allocated for the net lending item in budgets of past years mentioned above, it has been significantly exceeding the estimated by far as illustrated in the figure below:

**Figure No. 7**

**Net Lending Item: The Estimated 2016<sup>27</sup> VS. Actual 2015<sup>28</sup> and Estimated 2015<sup>29</sup> and Actual 2014<sup>30</sup> and estimated budget 2014<sup>31</sup> (million NIS)**



**Table No. 5**

Net Lending: estimated 2016 whole and Mid-year budgets vs. actual for Mid-year on commitment basis (million NIS)<sup>32</sup>

| Item        | Estimated 2016 | Estimated Mid-year-2016 | Actual After 6 months-2016 | Deviation from the Budget | Deviation Percentage |
|-------------|----------------|-------------------------|----------------------------|---------------------------|----------------------|
|             | Million NIS    | Million NIS             | Million NIS                | Million NIS               | %                    |
| Net Lending | 850            | 425                     | 521.9                      | 96.9                      | 22.80%               |

<sup>27</sup> Decision by Law No.1 for 2016, on the Public Budget 2016 financial year. Issued on January 8, 2016.

<sup>28</sup> Annual Financial Report, Dec. 2015; issued by the MoF and Planning on January 17, 2016.

<sup>29</sup> Decision by Law No.9 for 2015, on the Public Budget 2015. Issued on June 30, 2015.

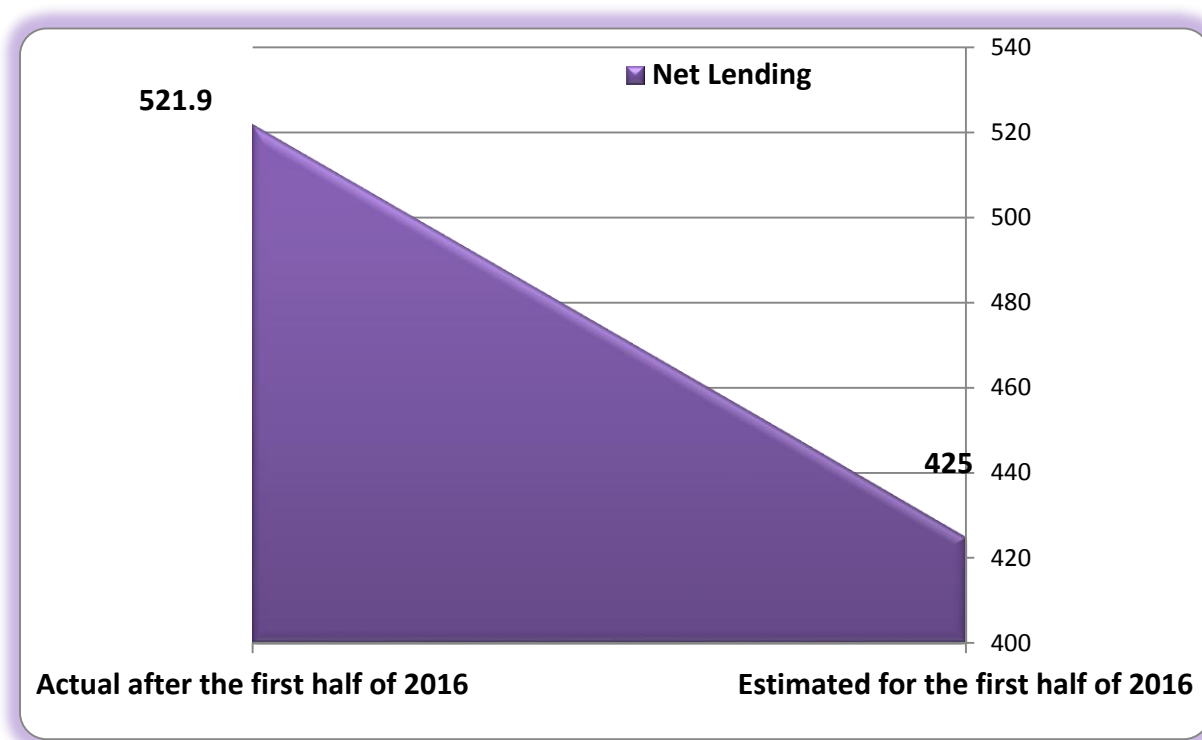
<sup>30</sup> Annual Financial Report, Dec. 2014; issued by the MoF and Planning on January 20, 2015.

<sup>31</sup> Public Budget Bill 2014. MoF.

<sup>32</sup> Mid-year Financial Report, June 2016 monthly report issued by the MoF on July 21, 2016.

**Figure No.8**

**Net Lending: Estimated Vs. Actual- Mid-Year 2016 Budget (million NIS)<sup>33</sup>**



**Table 5 and figure 8 show that:**

- The problem of net lending is on-going with and increasing pace year after year, exemplified in the amount spent during the first six months of 2016, which accounted for 61.4% of the total estimated budget for the whole year, amounting to 96.9 million NIS (i.e., a deviation of 22.4% from the planned for the first six months).
- No details or sufficient information is provided for the items of net lending indicated above, which amounted to 521.9 million NIS. These items on which loans were spent should be clear to ensure transparency of the budget. Moreover, citizens should be informed of the nature of accuittances between the government and municipalities.

<sup>33</sup> Mid-year Financial Report, June 2016 monthly report issued by the MoF on July 21, 2016.

**Conclusion 5:**

Net lending has a considerable impact on the Public Budget. For the past few years, it has been increasing steadily in a cryptic manner. It is also a major source of depletion for the Public Budget as each year the actual amount significantly exceeds that of the estimated. Therefore, it is vital to know where and how these millions are spent, since for example, in 2014 and 2015, the amount exceeded 2 billion NIS, with no sign of being addressed properly, until it reached the amount of 521.9 million NIS by June 30, 2016. Hence, actual spending for this item is expected to exceed one billion NIS by the end of the fiscal year 2016. For this reason, rationalization of this item is of great importance in order to wipe out the Public Budget deficit.

**Recommendation:**

Due to its substantial negative impact and constant depletion of the budget, the net lending Item should be given utmost attention by the government to ensure that this item no longer exists on the Public Budget. This calls for the government to reveal the underlying reasons for its inability to reduce it despite its significance; a vow often made by the government and the MoF. It is also necessary to hold the Finance and Local Government Ministries accountable for this item. Furthermore, more transparency is needed in net lending (i.e., items on which net lending were spent should be declared along with the criteria upon which the spending was based). Accuittances with municipalities, LGUs, electricity distribution companies and others should be made public. Finally, this item needs to be dealt with seriously due to the substantial impact it has on the government's austerity and rationalization plan.

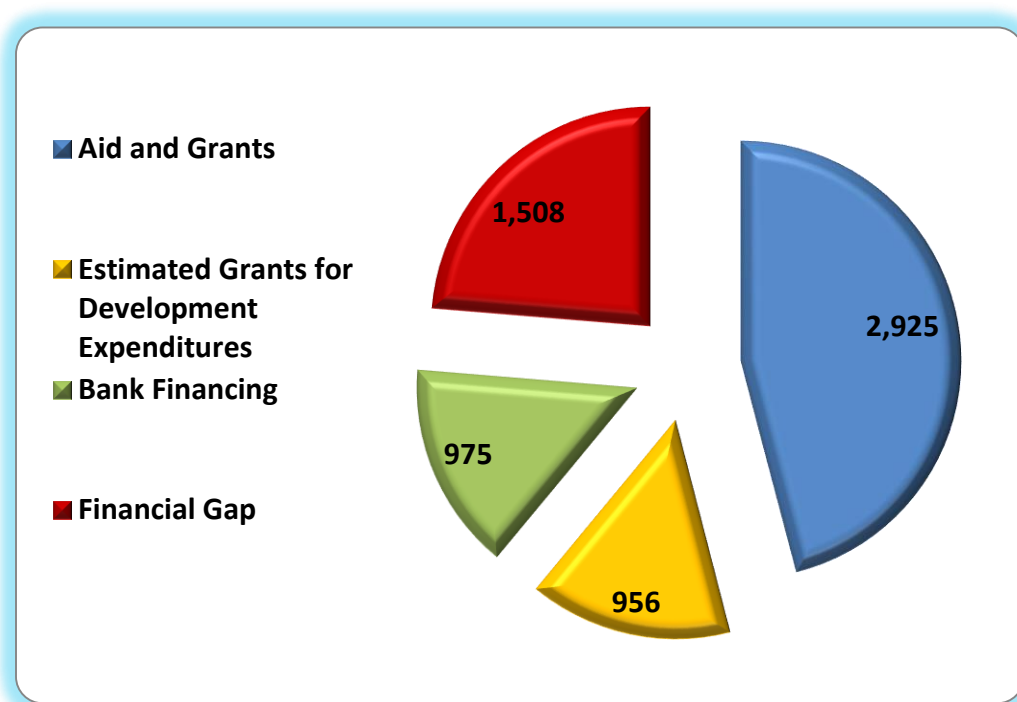
## Fifth: Deficit and Arrears Analysis

The total deficit, prior to funding, for the 2016 Public Budget was estimated at 5,388 million NIS distributed as follows: the current deficit accounted for 4,023 million NIS; budget development expenditures 409.5 million NIS; and 955.5 million NIS for funding development<sup>34</sup>.

The 2016 Budget data indicated that the total bank financing, estimated at 975 million NIS will wipe out the total arrears. However, there remains 1,508 million NIS, which form a financial gap in the 2016 Budget. This, the government vowed to abridge by reducing its monthly operational expenditures with amounts proportional to the gap<sup>35</sup>. Needless to say that the 2015 Public Budget suffered from the same financial gap, which the government promised to take austere measures to reduce it, but did not follow up on the issue, according to the MoF monthly report for Dec 2015<sup>36</sup>. Figure 9 below illustrates the estimated deficit and suggested solutions to bring an end to the Budget's deficit.

**Figure 9**

**Components of the 2016 Budget deficit and alternative payment solutions (million NIS)**



<sup>34</sup> Decision by Law No.1 for 2016, on the Public Budget 2016 financial year. Issued on January 8, 2016.

<sup>35</sup> Council of Ministers session No.82 held on Dec.2, 2015.

<sup>36</sup> Annual Financial Report, Dec. 2015 Report; issued by the Financial and Planning ministries on January 17, 2016.

Data the 2016 Public Budget shows that the arrears amounted to 819.8 million NIS six months after approval of the budget.

**Conclusion 6 and recommendation:**

The 2016 Public Budget entailed a multilayered deficit. This was due to the existence of a relatively large financial gap, and failure of the government to abridge the gap through its austerity and rationalization plan which was declared in the 2015 budget. Therefore, the Civil Team recommends the adoption of a scientifically based austerity and rationalization plan in participation with all related parties, including the Civil Team. This will better ensure a sound plan that will address this issue among others, hence wiping out the financial gap in the 2016 Public Budget.

**Bank financing (Loans):**

The 2016 Public Budget included an estimate of 975 million NIS to be borrowed from the banking system. This item was listed as is with no details. In addition, mechanisms for borrowing, conditions for payments, loan interests, etc were not clarified, which is a violation of the principle of transparency.

In reviewing decisions issued by the Council of Ministers during the first half of 2016 regarding this subject, it was noted that borrowing money from banks was carried out more than once from the Arab Bank. This was noted repeatedly in several of the Council's decisions, namely, Decision No. (m,r,/h,w/17/108/01)<sup>37</sup> issued on June 21, 2016. This decision mentions renewal of present agreement regarding current debt accounts and interests owed by the Finance and Planning Ministries in the amount of 248 million NIS, at an interest of 6.9%. This means that the interest paid to the Arab bank amounts to 14.26 million NIS a month<sup>38</sup>.

Also decision No. (h.r/w.m/17/109/3)<sup>39</sup> issued on June 28, 2016, which illustrates details of a "bridging loan" from the Arab Bank in the amount of 30 million U.S. dollars with an interest rate of 3.5%; and decision No. (h.r/w.m/17/109/01)<sup>40</sup> issued on June 28, 2016, approving a financial loan through a checking account with the Bank of Palestine in the amount of 60 million NIC, with an interest of 5%.

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<sup>37</sup> [http://www.palestinecabinet.gov.ps/WebSite/Upload/Decree/GOV\\_17/29062016110113.pdf](http://www.palestinecabinet.gov.ps/WebSite/Upload/Decree/GOV_17/29062016110113.pdf).

<sup>38</sup> 248 million NIS X 6.9 % / divided by 12 months

<sup>39</sup> [http://www.palestinecabinet.gov.ps/WebSite/Upload/Decree/GOV\\_17/11072016111152.pdf](http://www.palestinecabinet.gov.ps/WebSite/Upload/Decree/GOV_17/11072016111152.pdf).

<sup>40</sup> [http://www.palestinecabinet.gov.ps/WebSite/Upload/Decree/GOV\\_17/11072016110654.pdf](http://www.palestinecabinet.gov.ps/WebSite/Upload/Decree/GOV_17/11072016110654.pdf).

**Conclusion 7:**

It is evident that bank loans have become a fixed item in the Public Budget. Therefore, it is vital that the government illustrate more transparency regarding bank loans. I.e., it needs to publish full information regarding amounts borrowed, interests paid, government's foresight for payments, names of banks, conditions and criteria, etc. This is important information that needs to be provided by the government, especially in light of the many agreements signed with banks during 2016 concerning the large sums borrowed and the various interest rates paid to banks.

**Conclusion 8:**

The financial gap in the 2016 Public Budget amounted to 1,508 million NIS. This translates into a 125.66 million NIS a month. It would be interesting to know what steps and mechanisms the government plans to take to wipe out this gap, especially since the total expenditures was higher than the estimated for the first half of 2016. Therefore, a solution must be found in order not to exasperate the deficit problem further.

## Sixth: Public Debt Analysis

The public debt saw a decrease at the end of June 2016 according to data provided by the MoF. As it stood, public debt in December of 2015, amounted to 9,908.1<sup>41</sup> million NIS, while in June 2016, it was 9,739.1<sup>42</sup> million NIS. Table 6 below shows available comparative data for public debt:

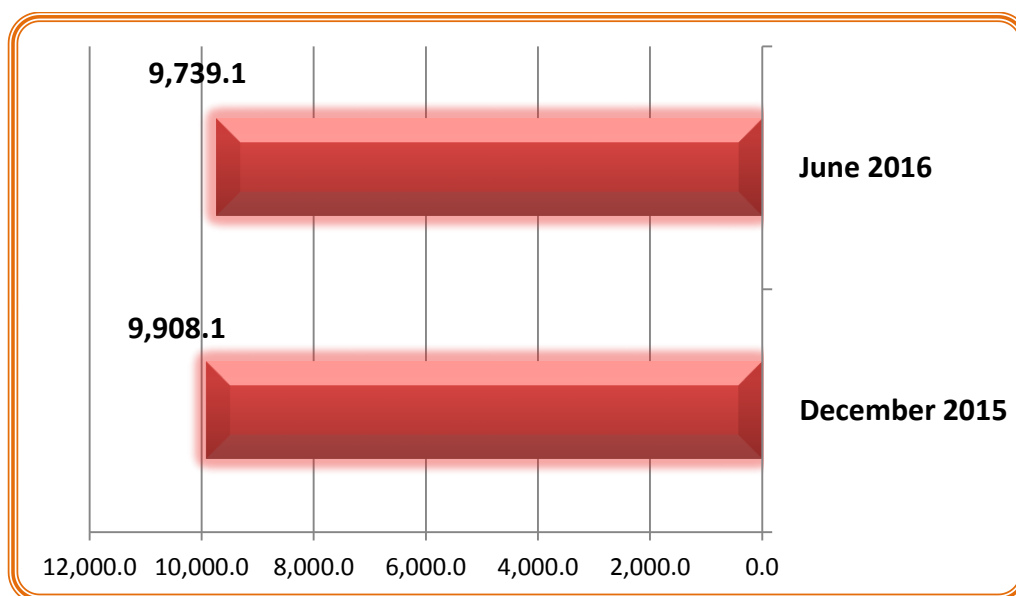
**Table 6**

**Comparative data for public debt: Dec. 2015-June 2016 (Million NIS)<sup>43</sup>**

| Item        | Dec.2015 | June 2016 | Deviation % |
|-------------|----------|-----------|-------------|
| Public Debt | 9,908.1  | 9,739.1   | -1.71%      |

**Figure 9**

**Comparative data: Dec. 2015-June 2016 (million NIS)**



### **Conclusion 9:**

Although reduction of the public debt was one of the government's objectives, it remains to be a persisting problem. As shown above, it accounted for a mere (1.71%) for the first half of 2016.

<sup>41</sup> Annual Financial Report, Dec. 2015 Report; issued by the Financial and Planning ministries on January 17, 2016.

<sup>42</sup> Mid-year Financial report, June 2016 (table 7a); issued by the MoF on July, 2016.

<sup>43</sup> Mid-year Financial report, June 2016 (table 7a); issued by the MoF on July, 2016.

### **Public Debt and the Pension Fund**

The commitment base review showed that: Actual social contribution, by the end of the first half of 2016, was 371.2<sup>44</sup> million NIS which was as planned. However, in reviewing the cash based files, it was discovered that the amount was only 130.0 million NIS<sup>45</sup> (i.e., 35% of the amount quoted on commitment basis). This raises questions about the government's transparency concerning the pension fund, public debt, and arrears.

### **Conclusion and recommendation:**

The 2016 Public Budget did not include details on the pension fund and salaries. Neither did it provide details on the amount of money borrowed from the fund. Therefore, enhancing transparency in the fund is greatly needed, as well as publication of its annual reports. This is vital; especially since the September 2016 World Bank report indicated that the Palestinian government had borrowed the amount of 1.6 billion U.S. dollars.<sup>46</sup>

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<sup>44</sup> Mid-year Financial report, June 2016 (table 1); issued by the MoF on July, 2016.

<sup>45</sup> Mid-year Financial report, June 2016 (table 2); issued by the MoF on July, 2016.

<sup>46</sup> The World Bank report on the economic situation in the West Bank and Gaza-Sept. 19, 2016.

## Seventh: Ministerial Social Allocation Analysis

This section will provide a comparison between public ministerial expenditures for ministries of social responsibility centers (i.e., the Ministry of Education and Higher Education (MoEHE), Health (MoH) and Ministry of Social Development (MoSD) versus expenditures of the Ministry of Interior and National Security (MoI&NS) during the first half of 2016, as illustrated below.

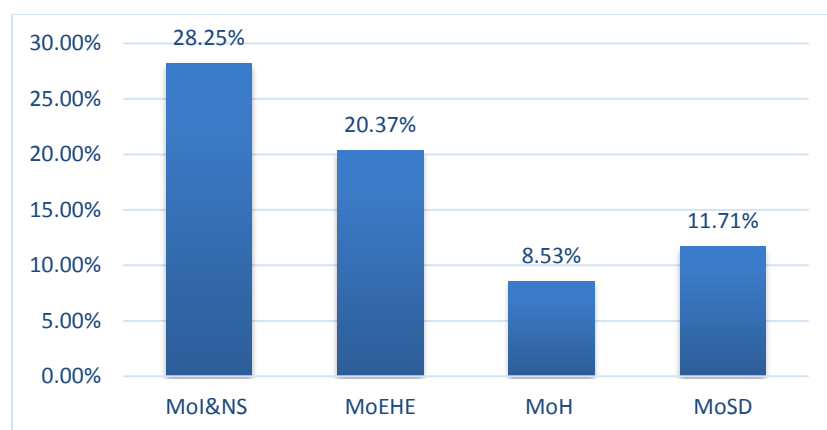
**Table 7**

**Ministerial Expenditure as per Responsibility Centers (commitment based) during the first half of 2016 (thousand NIS)<sup>47</sup>**

| Item                                       | Total Expenditure Allocations | Wage and Salary Allocations | Percentage of Expenditure from Total Expenditures |
|--------------------------------------------|-------------------------------|-----------------------------|---------------------------------------------------|
|                                            | Thousand NIS                  | Thousand NIS                | %                                                 |
| Ministry of Interior and National Security | 1,954,746                     | 1,635,333                   | %28.25                                            |
| Ministry of Education and Higher Education | 1,409,718                     | 1,121,950                   | %20.37                                            |
| Ministry of Health                         | 590,595                       | 378,313                     | %8.53                                             |
| Ministry of Social Development             | 810,044                       | 29,765                      | %11.71                                            |

**Figure 10**

**The Actual Ministerial Expenditure as per Responsibility Center (Commitment based) during the first half of 2016 (thousand NIS)**



<sup>47</sup> Mid-year Financial report, June 2016 (table 5b); issued by the MoF on July, 7, 2016.

**Table 7 and figure 10 illustrate the following:**

- The Mol&NS accounted for 28.25% of the total public expenditure; out of which 83.65% went for salaries and wages.
- The MoEHE received 8.53% of the total public expenditure.
- The MoH received 8.53% of the total public expenditure.
- The MoD received 11.71 of the total expenditure.
- The Mol&NS received an allocation that nearly exceeded allocations for both, MoEHE and MoH.

**Conclusion 10:**

Allocations for security continue to devour the lion's share of the Public Budget. In the first half of 2016, it was given an allocation that approached allocations for the MoEHE and the MoH combined. In addition, the salary and wage item still consumes the major part of the security budget and exceeds "total budgets" of the MoEHE and MoH put together.

Furthermore, no details for the Mol&NS are provided in the budget; only general items.

**Eighth: Presentations and Analysis of the Public Budget-Special Issues**

**- Financial reserves:**

The 2016 Public Budget included a financial reserve estimate that amounted to 55 million NIS. During the first half of 2016, 5,790<sup>48</sup> million NIS were spent under the item "Transferable expenditures".

**Recommendation:**

There is a grave need to enhance transparency and disclosure of data related to the financial reserve expenditures, especially since it is lumped under a "loose" item called Transferable expenditures. Details of amounts spent need to be disclosed regardless of size.

**The Palestinian Legislative Council (PLC):**

The PLC budget for 2016 amounted to 59.507<sup>49</sup> million NIS, 16.193 million NIS of which went to operational expenditures. This is in spite of the fact that the PLC has been dysfunctional for the

<sup>48</sup> Mid-year Financial report, June 2016 (table 5b); issued by the MoF on July, 7, 2016.

<sup>49</sup> Decision by Law No.1 for 2016 – fiscal year 2016. Issued on January 8, 2016.

past 10 years; deficit in the Public Budget, and the unemployment and poverty that are on the rise.

Actual expenditures for the PLC in the first half of 2016 amounted to 23.62<sup>50</sup> million NIS listed under the PLC item in the Budget. Operational expenses consumed 4.48 million NIS, and transferable expenditures accounted to 8.88 million NIS.

**Questions for thought:** does the government's austerity and rationalization plan give priority to these expenditures? Under which items in the budget are these expenditures listed given the dysfunctional status of the PLC? 9 million NIS were spent in six months under the "**vague**" item transferable expenditures...clarifications are needed as to how and where are they spent?

#### - **Transferable Expenditures:**

The MoF defined transferable expenditures to be "expenditures that are allocated in the Public Budget for the benefit of a third party". Examples include assistance provided by the Ministry of Social Affairs for needy families (i.e., welfare) as well as provisions for families of martyrs', wounded or imprisoned individuals.<sup>51</sup> Upon analysis of public expenditures for the first half of 2016, it was noted that the actual transferable expenditures accounted for 1,812<sup>52</sup> million NIS, which is 25.12% of the total current expenditures.

In conclusion, transferable expenditures constitute the second largest expenditure item in the Public Budget; the first being the salary and wage item. Moreover, this item is virtually found in every cost center of the budget, and not only in cost centers of the social sector. For instance, it amounted to 21 million NIS in the PLC budget; 55 million NIS in the Energy Authority's budget; and more than 623 million in the PLO's budget.<sup>53</sup> According to the 2016 budget, the transferable expenditure item is found in 15 out of a total of 50 centers of responsibility.

It is plainly evident that the transferable expenditure item is in need of more transparency. The item on which these expenditures are spent should be declared in detail along with criteria by which the spending is carried out, which at the end will facilitate rationalization of expenditures. Finally, it should be placed under one responsibility center for accountability purposes.

#### - **Allocations for centers of responsibility**

During the past few years, the Public Budget included allocations under centers of responsibility that are not of their jurisdictions. The budget also had no details regarding these expenses hence transparency is clouded making it difficult to hold these centers

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<sup>50</sup> Mid-year Financial report, June 2016 (table 5b); issued by the MoF on July, 7, 2016.

<sup>51</sup> Citizen's budget 2013.

<sup>52</sup> Mid-year Financial report, June 2016; issued by the MoF on July, 7, 2016.

<sup>53</sup> Illustrative tables in the 2016 Public Budget Bill-General Administration of the Public Budget- Finance and Planning Ministries.

accountable. For example, according to data provided by the MoF, the MoSA is still baring responsibility for expenses that are not of its specialty (i.e., to activities unrelated to its work) such as regular financial compensations to the appointments of 2005. These compensations exhausted the 2013 budget consuming 213.219,384 NIS<sup>54</sup>. The abovementioned allocations remained listed under the MoSA subsequent budgets until today.

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<sup>54</sup> Citizen Budget 2013.

### **Section III**

#### **Conclusions and Recommendations**

**The following conclusions were drawn based on the above analysis:**

- In reviewing the 2016 Public Budget for the first half of the year, it became plainly clear that it was executed with a structural imbalance, as the actual expenditures far exceeded the estimated. This raises questions about the austerity and rationalization plan put forth by the government and the government's failure to abridge the financial gap. In this regard, and based on information provided by the MoF, analysis of this paper considers this to be a negative indication of the feasibility of the plan.
- Upon analysis of the various sources of revenues, a satisfactory increase was detected six months into the fiscal year. However, this increase was accompanied with an increase in expenditures; or, to say the least, expenditures were not decreased in order to abridge the financial gap.
- Application of transparency principles of the Public Budget disclosure faced a serious problem according to the relevant provisions of Law No. 7 of 1998 on Budget Planning and Financial Affairs. Similarly, legal problems exist as the budget was not submitted to the PLC in due time (i.e., two months prior to the end of the year), as stated in article 61 of the Amended Palestinian Basic Law for 2003. Other problems faced included a decline in applying community participation approach during preparation of the budget.
- The 2016 Public Budget continues to suffer from a structural imbalance embodied in the complex deficit resulting from: failure of the government to abridge the financial gap caused by the cumulative ascending expenditures year after year. Also the fact that foreign grants and aid did not actualize as estimated; and lack of effectiveness of the austerity and rationalization plan.
- The 2016 Public Budget entailed a multilayered deficit. This was due to the existence of a relatively large financial gap, and failure of the government to abridge the financial gap through its austerity and rationalization plan, which was declared in the 2015 budget with no tangible results. Therefore, it would be beneficial to adopt the austerity and rationalization plan developed by the Civil Society Team.
- Structure of the Public Budget clearly entails an imbalance exemplified in the following: inflated expenditures for some sectors at the expense of other sectors; a salary and wage item that consumes the lion's share of the budget; the social sector which includes the three major service providing ministries, MoEHE, MoH, and MoSD receives the smallest share of expenditures; and large allocations for transferable expenditures that are allocated for more than one sector, all of which create a state of overlapping and uncertainty in dealing with this item.
- The government did take a pragmatic step by reducing dependency on grants and foreign aid to support the Public Budget and development expenditures. However, when reviewing the budget for the first half of 2016, it was confirmed that the actual amounts received from these sources (external aid) were still less than planned. However, the question is what are the government's alternatives in the event that funding is not received, bearing in mind that expenditures for development rely heavily on funding.

- The wage and salary item continues to weigh heavily on the Public Budget and in need of more transparency and sorting out. (i.e., ensuring that individuals on the payroll are actual employees, and that privileges and raises are well deserved and are based on merit based on declared criteria etc.).
- The item, net lending, lacks transparency and details. Therefore, in order to ensure transparency, it is important that expenditures regarding this item be declared along with criteria by which the spending was based. This is vital due to the considerable impact it has on the Public Budget, especially since for the past few years it has been increasing steadily hence exhausting the Public Budget. Every year the actual net lending significantly exceeds the estimated, which is in contradiction of the austerity and rationalization plan.
- **Transparency in bank loans:** it is plainly evident that bank loans have become a fixed item in the PA's Public Budgets. Therefore, it is vital that the government publish details regarding bank loans such as: which banks? What are the amounts borrowed? How much are the interests charged for each loan? What is the government's foresight for payments? These are some of the important questions which need to be clarified by the government for more transparency of the Public Budget.
- **Public Debt- Arrears- Pension Fund debt and salaries:** there is a real problem in the budget's transparency regarding mechanisms in dealing with these issues due to the fact that the relationship is organic, interrelated, and has great impact on the ground as well as the future of the Palestinian economic landscape.
- **Security Allocations:** Allocations for security continue to receive the lion's share of the Public Budget. And by comparison, allocations for social affair ministries structurally deformed and ratio distribution of its items, especially in regard to development expenditures which devolves to zero as in the case of the MoSA and MoH. Moreover, the MoSA 's budget is misleadingly inflated due to its inclusion of transferable expenditures, which accounts for the main part of its budget, noting that the ministry does not have full control over these expenditures. One example where these expenditures go is salaries for the 2005 appointments (a complex situation resulting from the internal division, where an employee is not at his job but continues to receive his salary)
- **The Pension Fund and Salaries:** more transparency is needed for the financial reserve item, especially since millions are ambiguously spent under this item. The only term specified in this regard is that it is a transferable expenditure; and reinforcing of the austerity and rationalization plan approach.
- More transparency is needed in relation to the financial aspect of the Pension Fund and salaries as well as the size of the government debt. It is not feasible to continue deferring the problem year after year without complete transparency, especially when the past years did not include regular transfers of monthly payments and salaries to the Pension Fund. Furthermore, borrowing operations from the Fund should be revealed including providing a comprehensive data on all levels of borrowing and repayment mechanisms, in order to

guarantee sustainability of the Fund. In addition, the MoF should disclose reasons for liquidating assets of the Fund to repay the due retirement salaries, since these assets constitute the core investment of the Fund. The September 2016 World Bank indicated that the PNA's debt to the Fund and salaries amounted to 1.6 billion U.S. dollars.

- Although the PNA adopted the 2016 Public Budget's schedule, the structure of the budget remains an item based program, especially in terms of the financial reports issued by the "Ministry of Finance and Planning". It is virtually rounded-items divided into: salaries and wages, social contributions, goods and services, transferable expenditures, capital expenditures, and development expenditures. These items have sum-lump numbers with no details. Also they are not linked to the schedule or objectives, which leads to the absence of accountability and transparency.
- Despite the dysfunction of the PLC and its state of paralysis since 2007, it is still included in the Public Budget and consumes a relatively large sum of money, especially operational and transferable expenditure items.

## Recommendations

1. It is of the utmost importance that firm commitment and adherence to the Palestinian Basic Law and provisions of the Public Budget Law be applied by all relevant parties including the MoF throughout the various preparation stages of the Public Budget. In addition, the draft budget bill should be submitted to the PLC two months before the forthcoming fiscal year for review and approval.
2. It is vital that the government display respect to the participatory approach by providing an opportunity for community discussions of the draft budget before its approval. After all, it is the citizen who is the main source of income to the budget.
3. To provide opportunity for the Civil Society Team to review the draft Public Budget, therefore complying with the participatory approach espoused by the PNA, which will ensure participation of economists, academics, and relevant CSOs, hence benefiting from their accumulated expertise.
4. It is important to review the Public Budget structure and allocation distribution. The review should aim at the redistribution of budgets to match the program at hand, paying special attention to the social sector.
5. It is vital that the government adopt an austerity and rationalization plan developed according to a well thought-out scientific methodology and in participation with all related parties, which the Civil Team had previously called for.
6. Due to the significant weight it carries on the Public Budget items as well as its relevance to marginalized groups, the transferable expenditures item is in need of more transparency. Similarly, transparent details are needed regarding the financial reserve expenditures, since it is also listed under the vague item transferable expenditures.
7. The salary and wage item needs to be filtered (i.e., removal of all unnecessary services, which in turn reduces expenditures).
8. Although the government and the MoF have confirmed the need to reduce net lending due to its considerable impact on the Public Budget, the government has failed to do so, therefore, a clarification is in order. The Ministry of Local Governance and that of Finance need to be held accountable for this failure. The government is also called upon to have more transparency regarding this item, and to reveal details of the nature of settlements with municipalities, LGUs, and electricity distribution companies, among others.
9. It is important that the 2016 Public Budget's financial reports include details on mechanisms dealing with three interrelated issues: public debt, arrears, and transfers made to the Pension Fund and salaries.
10. It is important that the 2016 Public Budget's financial reports include an annex on the total revenues and expenditures for the Gaza Strip, as well as development expenditures. This will promote transparency of the budget and provide accurate official information of amount spent on the Gaza Strip.
11. It is important that the 2016 Public Budget's reports include details on the number, salaries and privileges of public sector's employees that are categorized as "special groups, experts, and or consultants". This is necessary since salaries for this group

are not subject to the Civil Service Law and annexes. Therefore, reconsidering salaries of senior officials, salary scale in the public sector, especially in the security sector, and narrowing the gap between employees may achieve social justice. It also should be integrated in the austerity and rationalization plan.

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## **Acronyms**

The Coalition for Integrity and Accountability-AMAN: (AMAN)

Palestinian National Authority (PNA)

The Palestinian Legislative Council (PLC)

Civil Society Organizations (CSO)

The Civil Society Team for Enhancing Public Budget Transparency (Civil Team)

State Audit and Administrative Control Bureau (SAACB)

New Israeli Shekels (NIS)

Local Government Units (LGU)

The Palestinian Ministry of Education and Higher Education (MoEHE)

The Palestinian Ministry of Health (MoH)

The Palestinian Ministry of Social Affairs (MoSA)

The Palestinian Ministry of Social Development (MoSD)

The Palestinian Ministry of Interior and National Security (MoI&NS)



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