



## Public Budget-2018-Mid-Year Report

September, 2018

## Executive Summary

This report casts light on the execution of the 2018 public budget during the first half of 2018 (H1 2018). It assesses how compliant the government has been with approved fiscal policies. The report comprises three sections: (1) government compliance with relevant regulations; (2) a presentation and analysis of revenues, expenditures, deficit, debts, grants, and aid; and (3) findings.

1. The report concludes that the civil society and citizens continue to be inadequately engaged in setting priorities. The principles of transparency and timely disclosure of information continue to be challenged.
2. The report finds out a perceived gap between publicly announced policies and the implementation of these policies. Public fiscal policies are also challenged by failure to set a clear timeframe and provide precise tools for implementation, undermining the achievement of these policies.
3. In spite of the improvement made, the report points out structural deficiencies in the budget distribution mechanism. The Ministry of Interior and public security continue to have the greatest share (21 percent) of the budget.
4. The report shows that the rationalisation of expenditures, as reported by public statements, did not involve operating or consumption expenditures, a major portion of which may to some extent be luxurious. The report shows that an integrated, transparent plan on austerity and expenditure reduction is not in place.
5. The report shows that the wage bill and salaries were reduced. However, the reduction was caused by pensioning off 24,000 civil servants in 2017 and 2018.
6. The report shows that the debt overhang is still an ongoing crisis (public debt is NIS 8.6 billion; Pension Fund NIS 7 billion; and arrears NIS 1.2 billion). This is a consequence of a chronic deficit and failure to seriously reduce net lending, indicating that progress has not been made towards reforming the health insurance and electricity distribution systems. Therefore, a transparent fiscal policy needs to be adopted in order to pay the Pension Fund debts. Private sector arrears should be paid on a regular basis. In addition to horizontal expansion, tax collection should be enhanced. Tax evasion should be eliminated and tobacco smuggling combatted.
7. As shown by revenues and clearance accounts, the report indicates that the budget execution does not reflect significant changes in the working relationship with the Israeli side.
8. The report shows that, in light of the aid and grants received from the donor community in H1 2018, the government's desire to restore the pre-2012 aid level is no longer workable. As a result, the financial crisis (deficit) is being handled in a spontaneous manner, causing damage to the interests of social sectors and public services.
9. As usual, the government has not been committed to the statutory deadlines set by the Budget Law in relation to budget formulation, submission, approval, enactment, dissemination, and monitoring.

10. Published data, including revenues, direct expenditures or transfers, do not reflect collections from or expenditures in the Gaza Strip, allowing parties to the conflict (i.e. the Palestinian Authority and Hamas) to use numbers without reference to published revenue and expenditure results.

## Introduction

This analytical paper seeks to review and analyze implementation of the 2018<sup>1</sup> Public Budget in the first half of the year based on the June 2018 financial report<sup>2</sup>.

### **This 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. It also examines the extent by which the MoF respects the known transparency principles of public budgets.
- **Section II:** this part of the paper presents an overview and analysis of what was implemented during the first half of the year compared with provisions of the 2018 public budget 2018.
- **Section III:** conclusions.

This paper is a commitment based data analysis report. The analysis is based on the assumption that the Budget reflects the fiscal policies declared in the 2018 Public Budget Law, aiming to intensify efforts to improve its financial performance through several focal points related to:

- 1- **Revenues policies:** continue the horizontal expansion of the tax commitment strategy; maximize revenues; improve the efficiency and effectiveness of tax performance; adopt a fair and homogeneous tax system; adjust the tax system and specifically amend the Income Tax Law; limit tax evasion and avoidance; persist in correcting the tobacco, fuel and fees trade system; intensify demand for Palestinian financial rights from the Israeli occupation.
- 2- **Expenditures policies:** continue to maintain the same level of employment in the public sector; focus on developmental projects funded by the budget; work towards addressing and reducing net lending; make austerity and bonuses adjustments; work towards health sector reform and nationalizing medical health services; continue with pre-payment permissions for the private sector and expedite payments due; reimburse due-payments of the Pension Fund.
- 3- **Improving relations with donor countries:** work towards restoring financial support by donor countries to the level it was in 2012 (i.e., 1 billion dollars annually; work with Arab countries to provide financial support; develop an action plan to urge donor countries to increase financial support provided.

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<sup>1</sup> Budget Law for the Financial Year 2018

<sup>2</sup> Financial Report, June 2018. Issued by the Ministry of Finance on 23/7/2018.

## **Section I**

### **Legal Aspects of the Draft Public Budget Law for the Fiscal Year 2018**

In reviewing the extent of the MoF commitment to financial legal references governing the public budget, the following observations were concluded:

- 1- The Budget was not prepared within the legal dates stated in the draft public budget law. In other words, the budget was not presented to the Palestinian Legislative Council (PLC) at the beginning of November 2017, as stipulated by provisions of article (a/3) of the budget regulation law, but was presented to few representatives of some parliamentary blocs in the PLC in February 2018.
- 2- The MoF did not provide an opportunity for representatives of civil society, and in particular members of the Civil Society Team for Enhancing the Public Budget (The Civil Society Team), who represent the majority of NGOs whose work is budget related. And despite commitments stated by the government in the National Policy Agenda 2017-2022, to enhance transparency, and allow access of information to all citizens, the government shows no intention of implementing these declared commitments. Only later, some businessmen and representatives from donor countries were briefed on the draft budget.
- 3- The 2017 Public Budget did not include a table showing amounts of debts and loans (short or long term) incurred by the Palestinian Authority (PA). Nor did it include a proposed plan for collection or payment of these debts. In addition, contributions and investments of the PA in local and non-local commissions and companies were not presented clearly, noting that such information is obligatory by law and is stipulated in article 21 of the Budget Planning and Financial Affairs Law.
- 4- The Citizen's Budget was issued, which is in line with the international transparency standards. It also concurs with the principle of citizen's right to access the public budget and to follow up on government expenditures and management of public funds. However, the budget's mid-year report was not issued, not to mention the absence of publishing the budget's final account reports for 2013, 2014, 2015, and 2016.

## **Section II**

### **Presentation and analysis: implementation of the 2018 Public Budget-Mid-Year**

This section of the paper provides the state of implementation of the 2018 public budget, six months into the fiscal year. It also provides analysis of the actual data achieved compared to the budget plan, and to data of the previous half year of 2017.

The analysis in this section is based on fiscal policies stated in the 2018 Public Budget Law, and on decisions taken during the first half of this year. Also in this section, the compatibility and deviation between the “planned” and “actual” is illustrated.

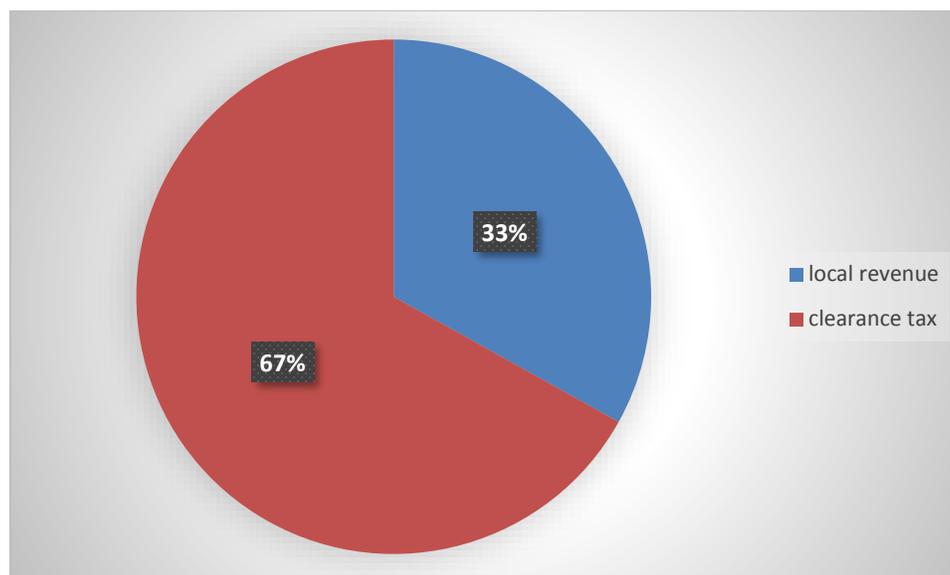
In addition, financial statements and data related to the public budget will be analyzed and presented in comparative tables and graphs, to include the following:

- Presentation and analysis of the **revenue** data during the first half of 2018, compared with the estimated.
  - Presentation and analysis of the expenditures data and related issues during the first half of 2018, compared with the estimated.
  - Presentation and analysis of net lending data during the first half of 2018, compared with the estimated.
  - Presentation and analysis of the deficit, grants, financial aid, arrears and bank loans data during the first half of 2018, compared with the estimated.
  - Presentation and analysis of public debt data during the first half of 2018, compared with the estimated.
  - Presentation and analysis of allocations for responsibility centers related to the social sector.
  - Presentation and analysis of special issues related to the public budget 2018.
1. Financial reserves
  2. Legislative Council budget
  3. Transferable expenditures

## First: Revenue Analysis

Figure (1)

### Revenue Ratios in the Estimated Budget 2018



Total estimated local revenues: Total revenues collected by the PA; 4.5 billion NIS

Total estimated clearance tax (Al-Maqasa) revenues: Revenues collected by the Israelis; 9.1 billion NIS

**Table (1): Total net revenues achieved compared with the estimated for the 1<sup>st</sup> half of 2018. Also, achieved local revenues, clearance tax, and tax returns compared with the estimated for the 1<sup>st</sup> half of 2018 (million NIS)**

	Achieved	estimated	Ratio within the budget (achieved)	2018 Budget
Total net revenues	<b>6552.9</b>	<b>6845.5</b>	<b>48%</b>	<b>13691</b>
Total local revenues	<b>2614.5</b>	<b>2266.5</b>	<b>58%</b>	<b>4533</b>
Total clearance tax (Maqasa) revenues	<b>3978.3</b>	<b>4579</b>	<b>43%</b>	<b>9158</b>
Tax returns	<b>39.9</b>	<b>93.5</b>	<b>21%</b>	<b>187</b>

As illustrated in the above table, the total revenues is close to the planned, where the total net revenues for first six months of 2018 amounts to 48% of the total net revenues for the whole of 2018. As for local revenues, the actual is higher than the estimated by approximately 400 million NIS, indicating an improvement in the government's revenue collection. One of the reasons is attributed to increase in the tax revenues paid by citizens and merchants at the beginning of the year in order to benefit from the tax incentives (discounts and offers). Thus, tax revenues are higher during the first three months of the year. As for the clearance tax, it accounted for 43% of the plan for the whole year.

**Table (2): Comparison of local tax revenues achieved during the first half of the year with the estimated for the same period (million NIS)**

	<b>Achieved; 1<sup>st</sup> half of (2018)</b>	<b>Achieved; 1<sup>st</sup> half of (2017)</b>
<b>Local tax revenues</b>	1569.2	1486.4
<b>Income tax</b>	499.5	501.5
<b>Value Added Tax (VAT)</b>	637.1	523.8
<b>Customs</b>	315.4	365.9
<b>Tax on Alcohol drinks</b>	2.1	2.2
<b>Cigarettes Tax</b>	104.6	82.1
<b>Property tax</b>	10.5	10.8

Analysis of the local tax revenue structure shows that the VAT, amounting to 637.1 million NIS in the first half of the year, constitutes the largest source of tax revenues. This accounts for 40% of the total tax revenues which amounts to 1,569 million NIS during the first half of the year. In addition, it rose by 113 million NIS from the achieved in 2017.

As we look at income tax, it is evident that the achieved amount in the first half of this year is close to the achieved amount last year, for the same period. This means that no change has occurred on revenues from income tax on companies or individuals. Thus, the policies declared concerning tax amendment have not been carried out nor endorsed. Furthermore, the total tax revenue achieved during the first half of the year is also close to what was achieved last year for the same period, with an increase of 6% as a result of increased income from VAT.

However, taxes generated from cigarettes for the first half of the year amounted to 104 million NIS, which is close to the amount achieved during the same period of last year. The problem remains is that the government's declared intention to correct the tobacco, fuel and fees trade system, hence increase revenues from this sector was not tangible during the period mentioned, bearing in mind that the projected revenues for 2018 has not been declared for each type of tax. Thus, expected revenues from cigarettes' tax was not announced, as opposed to last year where cigarette taxes were expected to reach 830 million, although the achieved in 2017 did not exceed 25% of the estimated amount.

#### **Financial policies related to revenue increase**

The Budget Law of 2018 was prepared in the form of fiscal policies aimed at increasing revenues. However, in general, there was no apparent effect reflected in the implementation of the stated policies. For example, the Budget Law included a proposal for amending the Income Tax Law concerning companies and individuals. However, after a half a year this was not amended. Moreover, tax revenues showed no increase in income tax.

The Budget Law also stated a horizontal strategy, which means an increase in the taxpayer base. However, analysis of the income tax revenues did not reveal an increase despite the increase of VAT.

Fiscal policies also intended to limit the phenomenon of tax evasion and tax avoidance, but implementation of these policies has not been sufficient thus far. In that regard, the Civil Society Team noted that the volume of the budget's loss due to tax evasion and customs leakage can amount to 35% of the total revenues. This adds up to approximately 500 million dollars annually; equivalent to 1.8 billion NIS, which calls for immediate action to stop this waste of money in this regard. And although there was an increase in VAT during the first half of this year compared with the first half of last year of about 100 million NIS, which indicates an improvement in tax collection and procedures followed, it remains short of reflecting the desired result of the declared policies in combating the phenomenon of tax evasion and avoidance.

In addition, the government put forth policies that aimed at correcting the trade system governing tobacco, fuel and fees. However, no tangible improvement was revealed in this area as the achieved revenues from cigarette tax reached 104 million NIS in the first half of the year, which is the approximate amount achieved last year, during the same period. Thus, no clear implications for combating the phenomenon of tobacco smuggling were felt, and hence no increase in revenues for this sector were noticed.

Although a plan to regulate the tobacco sector, reduce smuggling, create a competitive product and increase revenues is at hand, figures do not reflect the implementation of this plan.

In regard to reforming the fee system, data analysis revealed that revenues from local fees did increase by about 111 million NIS compared to the achieved in the first half of 2017. This is indicative of the government's performance to increase revenues from fees and specifically fees derived from licenses to practice professions.

In 2017 and at the beginning of 2018, the President issued decisions concerning legislations related to tax exemptions and service fees in the southern governorates (the Gaza Strip). In this regard, a Decision by Law No. (10) Of 2017 was issued on April 20, 2017, based on the Presidential Decree that was issued on June 14, 2007, which exempts citizens of the southern governorates from taxes and fees, making exceptions in some cases. This means that the previous Decree of 2007 granted more exemptions than the Decision by Law of 2017. After eight months of issuing the Law, the President issued another Decision by Law cancelling the first Decision issued on December 27, 2017. Article (1) of the Decision by Law abolishes the legislation related to the

Decision by Law No. (10) of 2017 (i.e., the previous Decision), and the revocation of Decree No. 18 of 2017.

The above facts point to the government's confusion in decision-making, and especially in regard to the Gaza Strip. In addition, reports issued by the MoF do not refer to revenues from the Gaza Strip, which could contribute to tracking the impact of those Decisions. However, the existence of several contradictory Decisions within one year reflects confusion in decision-making and the potential for political machinations in financial policy decisions. This is inconsistent with any responsible government's identity as it should take financial decisions in isolation of political rivalries, not to mention that those decisions should be based on reliable studies and examination of the impact such policies on people's lives socially and economically.

The government also announced its intention to intensify efforts concerning pressuring the Israelis for their financial rights (i.e., Palestinian right to clearance the tax money). However, there are no signs indicating that the PA has indeed intensified its efforts in demanding this right. For example, no improvement was apparent in revenues generated by the clearing tax that might indicate that pressure was exerted on the Israeli side in congruence with the declared policies.

## Second: Expenditure Analysis

Table (3):

**Table (3): Total current expenditures and net lending in the 2018 public budget compared with the achieved (commitment based) in the 1<sup>st</sup> half of 2018 (million NIS)**

	Actual/achieved 1 <sup>st</sup> half 2018	Estimated; 1 <sup>st</sup> half 2018	Estimated; 2018	Ratio: Achieved from the total estimated for 2018
Total expenditures	7385.2	8089.5	16179	46%
Salaries & Wages	3268.9	3939	7878	41%
Social Contributions	292.4	382	764	38%
Use of Goods & Services	1046.2	1043	2086	50%
Transferable expenditures	2022.7	2466	4932	41%
Capital expenditures	17.1	39	78	22%
Interest	114.5	152.5	305	38%
Net Lending	444.3	450	900	49%
Customized payments	179.1			

\* Customized payments are those taxes and revenues of the Local Government Units (LGU), (90% property tax, and 50% transport and transportation taxes).

As illustrated in the table above, the total expenditures achieved during the first half of 2018 constitutes 46% of the planned for the entire year. This indicates a government performance that is committed to the estimated expenditure amount by not exceeding the planned. Upon examining the total expenditures item, it became clear that the salaries and wages item was less than the estimated for the first half of the year by 671 million NIS. This was attributed to the reduction of the number of employees by referring 24 thousand of them to early retirement.<sup>3</sup> By further examining the abovementioned item, it became clear that the reduction in the salary and wage bill, estimated for 2018, was less by 200 million NIS from estimated in 2017.<sup>4</sup> As for the salary and wage bill for the first half of this year, it is less than the estimated by 671 million NIS.

And although the referral of the abovementioned number of employees was executed in 2017, the estimated salary and wage bill for 2018 was higher than the actual. This stems from the MoF's priorities where providing salaries takes first place and hence it's a way to ensure salaries. This explains the reduction in the salary and wage bill for the first half of the year.

Furthermore, it is also evident that the achieved transferable expenditures for the first half of the year was less than the estimated for that period by 444 million NIS, noting that the estimated amount was high from the start. While the operational expenditures (use of goods and services) amounted to 50% of the estimated amount for that purpose for the whole year (i.e., did not

<sup>3</sup> The referral of employees to retirement affects the acquired rights of these employees. It also violates pension legislations that regulate and define procedures and mechanisms for pension entitlement for public employees.

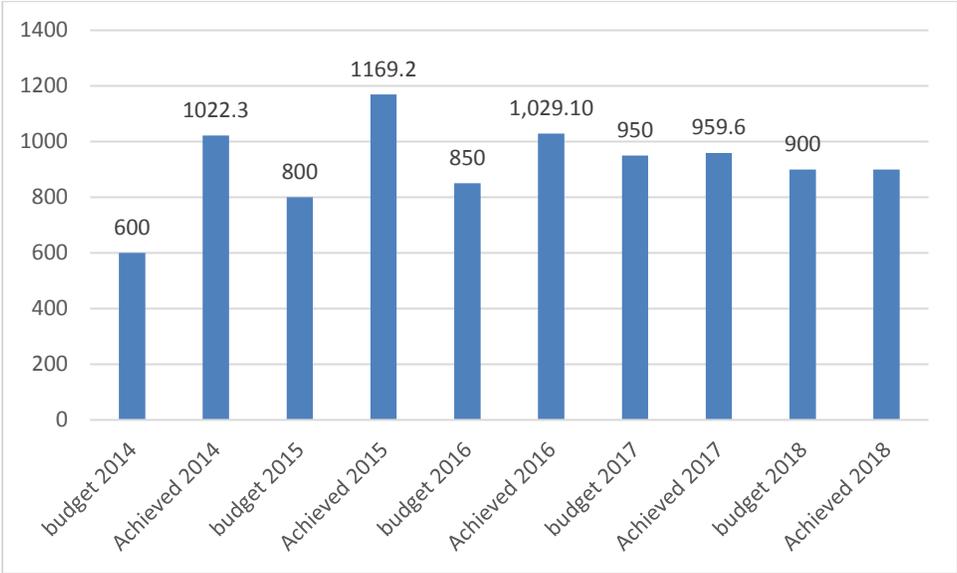
<sup>4</sup> The estimated salary and wage bill for 2017 was 8,093 million NIS, while the achieved bill for 2017 amounted to 7,631 million NIS.

decline), although there was intentions to rationalize expenditures in general including operational expenditures. The operational expenditures for 2018 were estimated at 2,086 million NIS; a slight increase of the amount of 2,035 million NIS estimated for 2017. While data shows that the operational expenditures over the past four year has been higher than the estimated. This was despite the government’s intentions to reduce these expenses, which indicates that the achieved operational expenditures have exceeded the estimated amount.

**Third: Net Lending**

**Figure (2)**

**Net Lending: comparison of the estimated and achieved, 2014-2018**



**Table (4): Net Lending in the 1<sup>st</sup> half of 2018: estimated versus achieved, commitment based) million NIS**

Net Lending	2018 Allocations	Half year allocations	Achieved in the 1 <sup>st</sup> half of 2018
	900	450	444.3

As illustrated in the table above, the amount achieved during the first half of 2018 is close to the estimated amount. This a good indicator of the government’s commitment to the estimated budget. However, information and details concerning net lending are not available as required

by the 2018 Public Budget Law. Similarly, there is no information or details concerning this item within the monthly report, which might shed light on how money is spent, although it amounts to 444.3 million NIS. This is particularly important for transparency of the budget. In addition, there is a need to inform citizens of the settlements that take place between the government and the LGU in that regard.

#### Fourth: Development Expenditures

The estimated amount for development expenditures in 2018 was set at 1,909 million NIS, which is more than the estimated amount for 2017 by 300 million NIS. 355 million NIS were allocated for this year for this purpose, which amounts to 165 million dollars more than allocations for 2017; an equivalent of 1,278 million NIS, accounting for 66% of the development expenditures.

Table (5): Estimated and actual operational expenditures for 2018-(Thousand NIS)

	<b>2018 Estimated development expenditures (does not include budget support)</b>	<b>Actual development expenditures in the 1<sup>st</sup> half of 2018 (includes development budge support)</b>
Total development expenditures	1278760	577000
President's Office	50571	8220
Interior Ministry & national security	58000	68505
Ministry of Finance and Planning	257605	8737
Ministry of Public Works & Housing	80000	15876
Ministry of Local Government	70381	64406
Ministry of Agriculture	66300	590
Ministry of Education	272000	115231
Ministry of Health	22200	28481
Labor Ministry	37360	1236
Palestinian Central Bureau of Statistics	8250	26454
Water Authority	26000	106803

Development expenditures of (1,278) million NIS were distributed on centers of responsibility. The table above illustrates names of the centers that consumed 74% of the development expenditures. For example, the MoF spent an estimated amount of 25 million NIS accounting for 20% of the total development expenditures that is financed by the public budget. Also the

Ministry of Education (MoE) spent an estimated amount of 27 million NIS accounting for 21% of the total development expenditures.

As for the Ministry of Health (MoH), which is supposed to acquire a higher share of the expenditures, in order to move forward in improving health services and nationalize medical services in order to reduce its needs of referring patients abroad for treatment, received a share of only 1.7% of the total development expenditures.

The Budget Law also stated that the government will cover approximately 66% of the development budget. And by looking into the achieved total development spending during the first half of the year, which is 577 million NIS, 379 million NIS of that are from the public budget and 197 million NIS are from external funding; a total of 33% of the estimated 1909 million NIS estimated for that purpose. According to the data given, therefore, the government did not commit to contributing its estimated amount for the first half of the year, which is 639 million NIS. Rather the amount spent was as mentioned, 379 million NIS accounting for 60% of the estimated amount for the first half of the year (i.e., 29% of the planned for the whole year).

### **Fifth: Deficit and Arrears**

The total deficit for 2018 was estimated at 4,584 million NIS with expectation that part of this deficit be paid through grants and financial assistance, which was estimated at 2.790 million NIS. While the total deficit for the first half of the year reached 572.8 million NIS, it is less than the estimated<sup>5</sup> for that period despite the lower projected external financing, with the achieved funding not exceeding 30% of the estimated amount for the whole year.

The decrease in the total deficit is due to lower expenditures and achieving the expected revenues. However, as noted earlier, the reduction in expenditures was the result of the referral of 24 thousand employees to early retirement.

**Table (6): The Budget deficit between the estimated and the actual for the 1<sup>st</sup> half of 2018 (million NIS)**

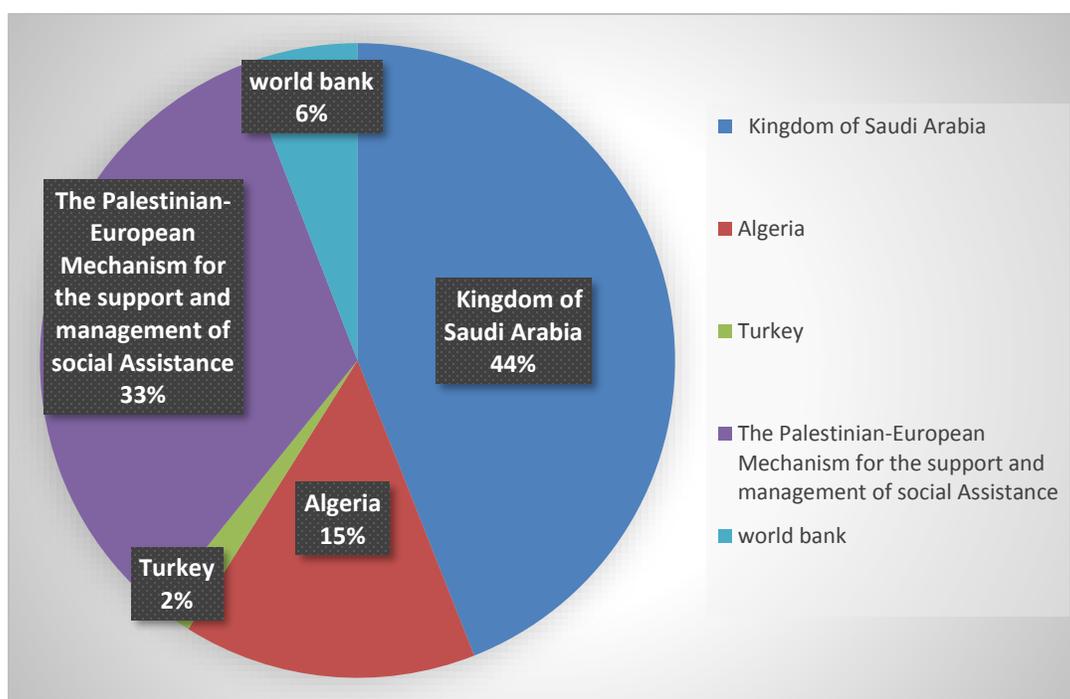
	Public Budget 2018	Estimated for the 1 <sup>st</sup> half 2018	Realized in the 1 <sup>st</sup> half 2018
Deficit	1794	897	572.8

**Table (7): Grants and financial assistance between the estimated and actual for 2018**

<sup>5</sup> Excluding payment of net arrears.

	Public Budget 2018	Realized in the 1 <sup>st</sup> half 2018	Achieved ratio from the estimated, 2018
Total funding	2790	836.8	30%
External budget support	2160	639	30%
Development financing	630	197.8	31%

**Figure (3): External support sources for the 2018 Public Budget**



The figure above reveals that the grants and various financial assistance for the first half of the year did not exceed 30%. In addition, no assistance from the United States of America (USA) was received due to the political situation and Palestinian stance from “Deal of the Century”. Also as illustrated, most of the aid is from Saudi Arabia, followed by the Palestinian-European Mechanism for the support and management of social Assistance

**Table (8): External Assistance between the estimated and actual for the 1<sup>st</sup> half of the year (million NIS)**

<b>Total external support (budget and development support)</b>			
Year	Amount in million NIS	Value of decline	Percentage change
2013	4915		
2014	4402	-513	-10%
2015	3104	-1298	-29%
2016	2905	-199	-6%
2017	2597	-308	-11%

It is worth noting that the total external support has been declining steadily for the past five years; reaching close to 5 billion NIS in 2013, while not exceeding 2.6 billion NIS in 2017. This indicates that decline of external funding is not new.

### **Sixth: Public Debt**

The amount of public debt in 2018 reached 8,849.7 million NIS. Data provided by the MoF at the end of June 2018 indicate a decline in public debt, where it amounted to 8,637.6 million NIS. However, this decline is small amounting to 212.1 and cannot be considered in isolation of the arrears expenditures, which is 1,210.6 million NIS, and the accumulated Pension Fund's debt. Noting that the amount of arrears declared does not necessarily reflect the actual figure and is expected to be higher due to lack of agreement concerning calculations of the number arrears. It is also due to the multiplicity of procedures used in the internal audit and accounting process of arrears invoices.

**Table (9): Public debt from Dec. 2017-June 2018 (million NIS)**

Item	Dec. 2017	June 2018	Decline %
Public Debt	8849.7	8637.6	-2%

### **The Pension Fund and Public Debt**

The actual amount of social contribution realized six months into the 2018 public budget was 292.4 million NIS, which is less than the planned amount of 382 million NIS. And in reviewing the cash-base, we discover that the social contributions amounted only to 101.8 million NIS, accounting for 26% of the estimated amount. In addition, the government did not fulfill its commitment towards the Pension Fund of paying it 25 million NIS, as it declared. This means that

debts to the Fund will continue to rise hence jeopardizing sustainability of the Fund. This raises the question once more of transparency concerning the tense issues of the Pension Fund, Public Debt and Arrears.

In general, the total public debt owed by the government can be calculated by taking the amounts declared and adding debts owed to the Pension Fund and arrears, which may reach to more than 15 billion NIS. This issue requires the development of practical plans that are well-thought out in order to repay debts and limit its accumulation.

### **Policies on Rationalization of Expenditures**

In its 2018 Public Budget Law, the government introduced several policies that aimed at rationalizing expenditures and reducing the budget deficit. This was exemplified through maintaining the level of employment in the public sector. And by scrutinizing expenditures concerning the salary and wage item, considering that it reflects employment best, decline in the salary bill was clearly noticeable, as shown by the data. As mentioned earlier, this was the result of referring a large number of employees to early retirement. In this regard, the Civil Society Team, supports the government's move towards maintaining a Zero employment policy, where the number of new employees equals the number the retired. At the same time, however, the Team condemns the transfer of employees to early retirement.

Regarding development expenditures and projects financed by the public budget, the collected data shows that the government spending on these projects during the first half of the year did not exceed 30% of the estimated amount for the whole year. This raises questions on the possibility of implementing these development projects and the implementation of the declared policy.

And as we examine the declared policies in regard to addressing and reducing net lending, we see that the amount realized is 444 million NIS, which is close to the amount estimated for that period. However, and in accordance with repeated recommendations made by the Civil Society Team, this issue needs to be addressed seriously, as such a slight reduction does not reflect a serious will to achieving a solution to this problem.

The Budget Law of 2018, in addition to the National Policy Agenda, and the National Health Strategy all included work that aimed at reforming the health sector and nationalizing medical services, which require the allocation of sufficient budgets in order to achieve the desired goal. And although the budget of the MoH was increased by 2%, a small increase indeed, this increase was spent on salaries, which is estimated at 812 million NIS, a 30 million NIS more than that of 2017. In the meantime, the Civil Society Team has been demanding an increase in the operational expenditures and in particular those related to government health services and medicine provision. This was not reflected in the public Budget Law of 2018. Although there is an increase in the health sector's development expenditures, which is a positive trend, the allocated budgets remain short of fulfilling this sector's needs. To emphasize the point...if we take the amount of

money allocated for development expenditures within the MoH budget and compare it with the total allocations for development expenditures, it would not exceed 1.7%.

The government also declared its intention towards scheduling of arrears, by continuing to issue prepaid permissions, as a way of dealing with it. However, during the first half of the year, prepaid permits did not exceed 30% of the value of arrears, which led to the accumulation of more arrears. The amount paid during the first half of the year amounted to 456 million NIS accounting for 32% of the amount planned, noting that the arrears expenditures had reached 1,210 million NIS. This raises questions of the extent to which the government is committed to implement its own policies in this area, and in paying the private sectors' dues.

And although the government took bank loans amounting to 1.4 billion NIS in order to pay its arrears, it did not include it in its monthly reports, not to mention that its way of addressing the issue added "insult to injury" (i.e., more debts by taking bank loans).

On another issue, the government declared its intention to pay the retirement debts owed to the Pension Fund, where it claimed to have transferred 25 million NIS to the Fund. However, upon examining the cash basis, the government did not come through. In this regard, the Civil Society Team prepared a report on this issue where it pointed out that in order to prevent accumulation of further debts the amount required to be transferred to the Fund monthly amounts to 115 million NIS. Moreover, it is worth noting that presently the debt of the Fund has exceeded 7 billion NIS.

## Seventh: Allocations of Ministries related to Social Issues

In this case study, public expenditure of ministries and centers of responsibility for social services (MoE, MoH, MoSD), is compared with the expenditures of the Ministry of Interior and Public Security (Mol & PS), during the first half of 2018.

**Table (10): Comparison of expenditure according to Centers of Responsibility (Commitment Basis) during the 1<sup>st</sup> half of 2018**

	Total planned expenditure for 2018	Total expenditure for half the year 2018	Percentage achieved from the planned	Salaries and wages for 2018	Salaries and wages realized for half the year 2018	Percentage of total achieved expenditure from total expenditures achieved for the 1 <sup>st</sup> half of 2018
Mol & PS	3,546,653,000	1,503,141,000	42%	2,965,618,000	1,198,140,000	21%
MoE	3,077,481,000	1,400,582,000	46%	2,500,000,000	1,063,072,000	19%

MoH	1,754,483,000	862,210,000	49%	812,080,000	319,682,000	12%
MoSD	<b>1,484,689,000</b>	<b>664,927,000</b>	45%	<b>63,259,000</b>	<b>23,965,000</b>	9%
MoD	788,786,000			57,000,000		
Foundation for the Care of Martyrs Families	695,903,000			6,259,000		

\*Note: Budgets for the Centers of Responsibility do not include development expenditures

\*Note: MoSD includes the Ministry and the Foundation for the Care of Martyrs' families

**Figure (5): Comparison of actual total expenditures according to Centers of Responsibility (Commitment Basis) during the 1<sup>st</sup> half of 2018 (Thousand NIS)**

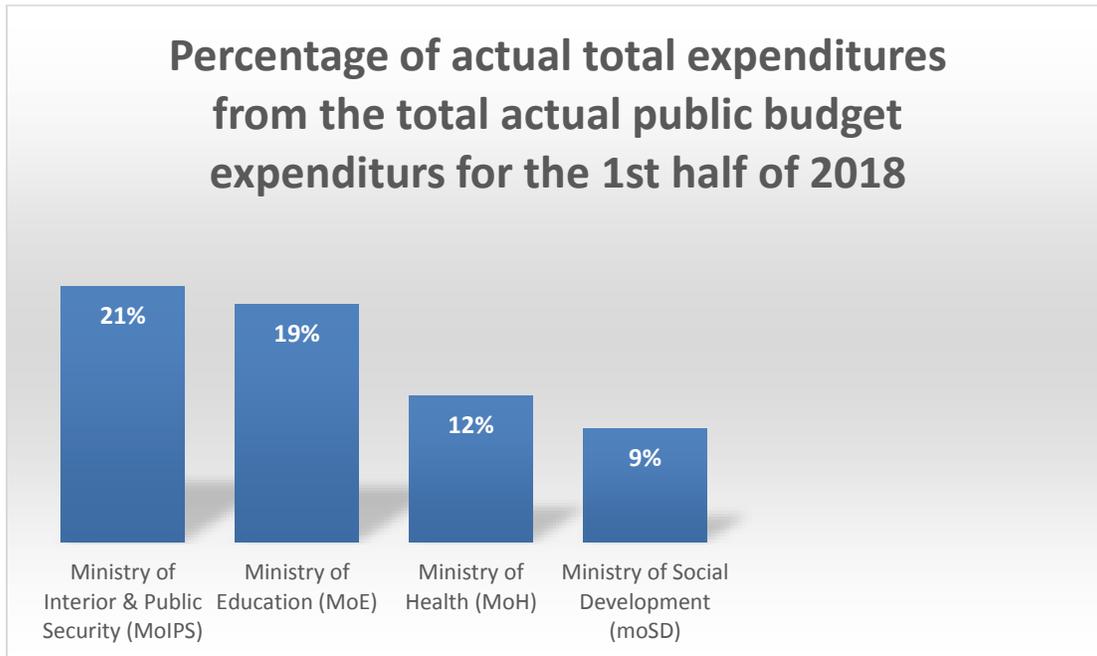


Table and figure above illustrate the following:

- The Ministry of Interior and Public Security consume 21% of the total public expenditures. Moreover, 83% of its budget goes to salaries and wages despite all repeated recommendations of the Civil Society Team to reduce these expenses. As it stands, the security institution allocations continue to account for the largest share of the budget, most of which goes to salaries and wages within the institution, all in the absence of transparency concerning this institution.
- The MoE received 19% of the total public expenditures. In scrutinizing details through the working paper prepared by the TEAM on priorities of the Ministry and budget item allocated to the Ministry, it was clear that the Ministry's share is not excessive. However, problems lie in the structure of the budget, where salaries and wages consume the largest share, and the budget's lack of compatibility with the strategic plans of the education sector.
- The MoH received 12% of the total public expenditures. According to the working paper prepared by the Civil Society Team, this budget is not sufficient to meet the needs of the Ministry. Furthermore, the need for national insurance remains valid, which can be a source of income to the Ministry as well as to the development of health services.

Moreover, it is important to put forth a development plan that aims at improving specialized medical treatment services within the MoH institutions in order to reduce dependence on medical referrals to centers outside the Ministry and or outsourcing certain medical treatment services. The plan should have clear indicators of progress over the next five years where the Ministry can work on: capacity building training for staff, provide medical supplies related to high-cost diseases such as cancer, blood diseases, heart surgery, neurosurgery, etc., in order to achieve the desired goal of reducing expenditures of this item.

- The MoSD and Foundation for the Care of Martyrs Families, jointly, received 9% of the total public expenditures. The total budget of the Ministry amounted to 788 million NIS accounting for 5% of the public Budget. Upon analysis of the budget structure of the Ministry, it was noticed that there are costs and compensations charged to transferable expenditures within the Ministry's budget. The Ministry has no information or knowledge about these charges and certainly are not part of its projects. According to data provided by the MoF, however, the MoF uses that money to pay compensation to employees that have been laid-off in 2005 (as a result of the political internal division). The number of these employees is 11,850 where each employee receives a compensation of 1,500 NIS monthly, which amounts to 213,300,000 NIS annually. This huge sum is listed and dispersed under the MoSD's budget without first consulting with the ministry. The Ministry has reservation concerning this action by the MoF, to say the least. Based on that, it is fair to say that the actual share of expenditures allocated for the MoSD accounts for only 4% of the total public expenditures, where transferable expenditures take up 92% of that, and 8% are used for salaries and wages and operational projects seeking development.

However, developments have occurred to the budget's structure and distribution in 2018, where allocations for development have risen from one million NIS in 2016 and 2017 to about 52 million NIS in the 2018 budget. Of that, 42 million NIS were allocated for the Economic Empowerment Program. On the downside, it is noticed that a decline has occurred in the allocation for transferable expenditures (the Cash Assistance Program) by approximately 40 million NIS (i.e., the increase in the development budget was at the expense of the transferable expenditures).

## **Seventh: Presentation and Analysis of Special Issues related to the Budget**

### **Financial Reserves:**

The budget includes an item called financial reserves. The amount allocated for 2018 is the same as the previous years of 2015, 2016 and 2017, which is 55 million NIS. During the first half of this year, 12 million NIS were spent in the form of transferable expenditures. While in 2017, the amount was 11 million NIS accounting only for 20% of the planned. However, there is dire need for disclosure of data and more transparency in regard to distribution of money allocated for this item, especially since it is spent under such a “loose” item which is transferable expenditures.

### **The Palestinian Legislative Council:**

Budget for the PLC for 2018 was estimated at 57 million NIS, noting that the PLC has been dysfunctional for the past 12 years. Operation expenditures of the PLC for 2018 were estimated at 14.9 million NIS, accounting for 26% of the estimated budget. 17 million NIS were spent in the first half of 2018 of which 1.8 million NIS were spent on operational expenses and 6 million on transferable expenditures (salaries of PLC members), while 8 million NIS went for salaries and wages of employees of the dysfunctional PLC.

According to a report prepared by the Civil Society Team on the state of operational expenditures which stated that a high operational budget is allocated to the Council despite the fact that it is dysfunctional, and that the actual amount spent is lower than is estimated. This could be to earn PLC members’ satisfaction when the MoF is consulting with them during the stage of approval of the Public Budget. Or possibly it could be to provide flexibility for the MoF to set the higher ceiling for the Council once its fully functioning.

### **Transferable Expenditures:**

The MoF defined transferable expenditures as “those expenditures that are allocated in the budget of a public institution and is benefitted by a third party, such as the assistance provided through the MoSD to poor families and families of martyrs and the wounded and prisoners’ allocations<sup>6</sup>.” Results of this analysis showed that the amount of the achieved transferable expenditures for the first half of 2018 amounted to 2 billion NIS, accounting for 27% of the total expenditures.

Transferable expenditures, therefore, are the second largest item of expenditures after salaries and wages. In practice, it is in 18 out of 54 centers of responsibility. For example, budgets that are spent in the form of transferable expenditures within the Energy Authority and Natural Resources reached 35 million NIS. In the meantime, the MoF’s expenditures was 43 million NIS. That being said, the need for more transparency concerning this item is of great importance.

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<sup>6</sup> Citizen’s Budget 2013.

Components of this item, methods of spending, allocations within the mentioned centers should all be clarified in order to find ways to direct and channel spending.

## Section III

### Conclusions

- **Transparency of the Public Budget:** there is clearly a problem in applying principles of transparency related to the disclosure of the Public Budget, as stated in the Budget Planning and Financial Affairs Law No. 7 of 1998. There is also a problem in application of the law in terms of presenting the Budget to the PLC two months before the end of the year, as stated by article 61 of the amended Palestinian Basic Law of 2003, and related legal provisions in the Law No 7 mentioned, in addition to publishing the Budget's detailed statement, which is considered part of the law. Lastly, accessing the full data and information directly and in a reasonable time remains to be problematic.
- **Participatory approach:** Although the Budget proposal was presented to representatives of some parliamentary blocs, private sector businessmen, employees from the MoF and Council of Ministers, and representatives of donor countries, the participatory approach in its holistic sense remains incomplete. The missing link is civil society. Therefore, it is important that the government involve civil society organizations and institutions in all stages of the budget preparation and to make available data and other related documents concerning the budget. That being said, it is worthy to note that the MoF did not provide an opportunity for civil society organizations, and in particular, the Civil Society Team, to review the budget.
- **Revenues:** revenues for the first part half of the year rose by an estimated amount of 400 million NIS. This indicates an improved government performance in revenue collection. As mentioned earlier, usually revenues tend to be higher in the first half of the year than the second half due to businesses and individuals paying taxes at the beginning of the year in order to take advantage of concessions and discounts.
- **External funding:** Despite the low estimates of external funding, the realized remains lower than the estimated. This creates two problems. The first is the increase in the budget's deficit, and the second is the fate of plans and programs, especially the development projects that depend on external funding.
- **Expenditures:** it is noticeable that the total actual expenditures is slightly lower than the estimated. This was due to the referral of 24 thousand employees to early retirement. It is also noticed that the operational expenses have not decreased despite the

government's repeated claim of rationalizing expenditures, and the existence of a financial gap that needs to be remedied through rationalization of expenditures. In that regard, it is worth noting the Civil Society Team has pointed out on several occasions the need to control these expenses and issued a rationalization and austerity plan in this regard.

- **Net Lending:** this item was decreased slightly. However, there remains a need to restrain it further taking into consideration the detailed recommendations presented by the Civil Society Team, which included practical measures and procedures. This is vital since the government failed to end this phenomenon for the past years.
- **Budget Deficit:** the PA's Public Budget continues to suffer from a chronic structural defect typified by the large deficit resulting from a large gap between expenditures and revenues. This gap continues to widen due to the following reasons: accumulation of increased expenditures year after year; regression in financial grants and foreign aid to the budget; the ineffectiveness of the government's austerity and rationalization plan.
- **Public Debt:** a slight improvement has occurred to this item, except it is impossible to evaluate the actual amount without examining the government's debt to the Pension Fund and arrears, because it is all debt.
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- **The Palestinian Pension Fund:** there are many problems related to transparency of the Fund, the amount of debt owed to it, and the government's mechanism for paying these debts. It is noted that there is a significant disparity between the government's contributions to the Fund (commitment basis and cash basis).
- **Security allocations:** security institutions continue to consume the larger portion of the public budget. In addition, salaries and wages continue to drain and consume the bulk of the security expenses, where it far exceeds the sum of expenditures of the MoH, MoSD, and the Foundation for the Care of Martyrs Families. Furthermore, there are no details available for the public on the MoI&PS other than the basic structure of its budget.
- **Distribution of the Public Budget allocations:** the Budget allocations are clearly distorted, as there is inflation of expenditures in some sectors at the expense of other sectors. In addition, the salary and wage item continues to consume the lion's share of the public budget. And development expenditures continue to suffer from great financial scarcity, especially those related to social development.

- **Budget of the Ministry of Social Development:** this budget has been suffering from an accumulative defect and imbalance for several years, which is basically due to the merging of the responsibility center of the Ministry with the responsibility center of the Foundation for the care of Families of Martyrs, and then classifying the two under the name of the MoSD. Thus, the allocated budget for the responsibility center “Social Development” is inflated, unclear and unreal. In addition, the allocations assigned for the MoSD do not meet demands and needs of the Ministry, as well as lack harmony with its strategic plans.
- And in all cases, the following are some problems and challenges that need to be overcome in order to ensure good governance of public funds; these are: the long delay by the MoF in submitting final accounts to the State Audit and Administrative Control Bureau (SAACB) and to the PLC; the inability of the SAACB to audit the accounts in a timely manner; the SAACB’s reservation to publish findings of its audits; and last but not least the paralysis of the PLC in accountability towards correcting any deviation in the budget before its approval.