PRDP-TF: Quarterly Review
January - March 2010

In the first quarter of 2010 the PA continued to implement the reform program laid out in the PRDP. However, despite the reforms and recent economic growth, the PA's fiscal position remains difficult. The 2010 budget that was adopted during the first quarter of 2010 projects a recurrent budget deficit of $1.24 billion and the need for another $677 million in aid for development expenditures. In the first quarter of 2010, the PA was able to hold spending to less than projected by the budget and to raise domestic taxes by more than projected. However, external budget support was less than needed and consequently the PA continued to build up arrears and increase borrowing. During the first quarter the PA made significant steps on implementing reforms in the electricity sector while continuing its steady progress on reforming the public financial management system and social safety net. The PA continues to reduce the number of employees in Gaza while expanding the West Bank work force.

On a prorated basis the first quarter recurrent deficit of NIS 1.143 billion was more than 3% less than the budget target. Though total net revenues were more than 10% lower than the budget projections, total expenditures were about 7.5% less than projected. Thus, overall the recurrent budget deficit was less than a quarter of the annual target. However, development expenditures were NIS 210 million while only about NIS 8 million in development financing was received. Since, the budget calls for all development expenditures to be externally financed, this essentially increased the operating expenditures by NIS 200 million and raises the deficit nearly 13% above the budget target. Budget support in the first quarter was about $103 million less than targeted by the budget. Combined with the shortfall in domestic revenues and development finance, despite the under spending, this required the PA to accrue nearly $26 million in non wage arrears and resort to about $98 million in bank financing.

Tax revenues in the first quarter of 2010 were nearly 22% above budget targets and more than 50% higher than in the first quarter of 2009. This substantial jump in tax collections partly reflects the slowly growing economy but is mostly due to the PA's concerted effort to improve tax administration. Domestic taxes were up across the board: Income tax was 65% higher than in the first quarter of 2009, VAT receipts were 48% higher and property taxes were 53% more. Unfortunately, clearance revenues were nearly 10% less than budgeted, though still about 34% more than in the first quarter of 2009. Non tax revenues were almost 50% below their prorated quarterly target. But non-tax revenues are lumpy and they are expected to materialize later in the year.

Total expenditures and net lending were significantly less than budgeted in the first quarter of the year due to greatly reduced non-wage expenditures. Operational expenditures and transfers were 17% and 18% respectively less than 2010 budget projections. Overall nonwage expenditures were some 20% less than budgeted and more than 34% lower than the same quarter in 2009. It is not clear why operating expenditures were so much less than expected and lower than previous quarters. It is likely that spending has been suppressed, possibly due to uncertainty resulting from the delay in approving the 2010 budget, and will rebound dramatically in the following quarters. In February the PA made a onetime payment of nearly NIS 30 million as a hazard allowance for Ministry of Health staff. Despite this, the quarterly wage bill was within the budget target, though it was 7.5% more than the same quarter in 2009. In 2010, the PA no longer reports movable transport allowances as part of the wage bill and the MoF reports that this has the effect of lowering the wage bill by between $25 million and $40 million.[1] Net lending was more than 12% above its prorated quarterly target but still nearly 13% less than the first quarter of 2009. The PA reports that net lending is in line with their projections. They expect net lending to Gaza to decrease over the year as electricity collections there increase. Therefore net lending in the first half of the year is expected to be higher than in the second half and the PA believes it is on target to reach the 2010 budget target for net lending.

In the first quarter of 2010 the PA continued to increase the number of staff in the West Bank and reduce the number of staff in Gaza. Total employment in the first quarter of 2010 increased by 1,854; net employment in the West Bank rose by 2,158 and in Gaza fell by 306. Since December of 2008 total employment reported in the West Bank has risen by 7,467 while falling in Gaza by 837. The PRDP commits the PA to restricting net hiring to 3,000 a year, with the majority of going to health and education. However, in the first quarter the security sector continued to account for a large share of the new recruitment (Table 1). The 2010 budget provides a general 4% wage increase to existing staff, which is composed of a 1.25% time in service increase required by law for all existing staff and a 2.75% cost of living increase. This comes on the heels of a similar pay rise in 2009. The PRDP committed the PA to having no general pay rises during the three year life span of the Plan. However, the Prime Minister has backed off that pledge and has indicated that he considers small but steady pay rises every year the best policy. Despite the pay rises, if the PA is able to stay within its budget and projected growth rates are met, the PA could still achieve the PRDP goal of having the wage bill reduced to 22% of GDP. This goal is being helped by the introduction of a new system to ensure that all government agencies can only promote staff if there is room in the budget envelope.

Table 1: Net Change in Employment in Most Significant Sectors

	DEC 08- MAR 10	Q1 2010
Security Forces	2,665	436
Education	2,008	745
President's Office	672	45
Health Sector	422	471
Ministry of Social Affairs	368	40
Ministry of Interior	-536	-8

Source: PA Ministry of Finance Monthly Reports

In the first quarter of 2010, the PA continued its efforts to increase utility collections and reduce net lending. The PA maintained its programs to provide financial incentives to local governments that pay their bills in full and to withhold transfers from those that

[1] This allowance pays staff for work related travel costs.

don't. In addition, the PA continued to make withholdings from the salaries of PA employees with overdue utility bills. The PEA continues its efforts to distribute pre-paid electric meters and by the end of the March about 170,000 had been installed. The PA is now planning to provide meters for distribution in Gaza. The PA indicates that it has done about as much as it is able to reduce net lending in the West Bank, without collecting bills in the refugee camps and completing the transfer of electricity distribution from local governments to the newly created distribution companies. The PA's focus is now on increasing collections in Gaza by beginning to distribute prepaid meters and encouraging collections from large uses.

The new electricity law passed in May 2009 calls for the transfer of all electricity distribution from local governments to licensed distributors, i.e. the distribution companies, by the end of May 2010. There have been a number of delays and this goal is not attainable. However, in the last quarter, the PA has begun to make significant progress towards this goal. The new regulatory commission was activated by presidential decree and has begun to operate. PEA contracted Jerusalem District Electricity Company (JDECO) to assist in the smooth startup of the Northern Distribution Company (NEDCO). With the assistance of JDECO, the PEA plans to start the first phase of NEDCO operation in June 2010. The first phase will consist of transferring the service and the assets from the Municipality of Nablus and possibly those of Jenin as well. The MoF, Ministry of Local Government, the PEA and local governments have been negotiating a program of financial aid to assist local governments transition from their reliance on electricity revenues to fund current operations. Coming to an agreement on a plan is a necessary step before local governments will be able to transfer their assets.

Public pensions remain one of the PA's largest liabilities and under the most recent Letter of Development policy, the PA has committed to developing a reform plan that will address the lack of funding and put the pension plan on a sustainable footing. The World Bank has provided a paper and other analytical work that suggests options and estimates the cost and benefits of some parametric reforms. In the first quarter of 2010, the PA developed a plan that is currently being discussed within the PA. The Prime Minister has indicated that he expects to present it to the donors and have it officially adopted before the end of the June 2010.

In February 2009 the Council of Ministers issued a decree to merge all on-going cash assistance programs using the poverty targeting database developed under the World Bank supported Social Safety Net Reform Program (SSNRP) as the main mechanism for targeting assistance. In the first quarter of 2010 the Ministry of Social Affairs (MoSA) began to implement a strategy do to this that was finalized in the fourth quarter of 2009. MoSA has merged the databases of the two largest cash transfer programs. Previously MOSA reviewed and updated its proxy means test (PMT) for determining eligibility for payments based on data from the 2007 household census and 2007 household expenditure and consumption survey (PECS). In 2010 MoSA will continue to visit households in the West Bank to update their data using the new system.[2] In the first quarter information for about 1,745 households was verified and added to the 36,000 households that had already been verified. MoSA plans to verify at least 24,000 households in 2010. After a household's data has been verified, if it is identified as a potential beneficiary, it is invited to complete a registration and submit any missing supporting documentation. This process started at the end of December 2009, and by the end of March 2010, 17,065 household have been identified as being in extreme poverty. Of these 9,560 families out of them are from the "Social Hardship Cases", 675 from SSNRP, and 6830 are new beneficiaries.[3]

The PA reports continued progress on implementing its ambitious program of public financial management reform. The 2010 budget was finally signed into law on March 31, 2010 a full quarter into the fiscal year. However, the outlines of the budget were known and the PA has been operating within its framework. The MoF reports that 60 ministries and institutions are now connected and fully implementing the Computerized Accounting System. In addition, the MoF reports that all non-zero balance bank accounts, except for those required by law, held by line ministries have been closed.

The Ministry of Finance issued the Final Financial Statement of 2008, Consolidated Statement of Cash Receipts and Payments and Comparison to 2008 Budget for the Year Ending 31 December 2008 and delivered it the external auditor (State Audit and Administrative Control Bureau, SAACB) on January 19, 2010. The SAACB formed four groups from their staff to perform the audit (Expenditures, Revenues, Salaries, Bank Settlements and Loans and Grants and Projects). The first two stages are nearly finalized, while the third stage of examination for all components related to Expenditures and Revenues will start soon. The internal audit department at MoF issued final audit reports on the Ministry of National Economy MoNE, Ministry of Social Affairs MoSA, Bureau of the Chief Justice, the Ministry of Education and Higher Education MoEHE and the Ministry of Interior (MoI) during. In addition, the internal audit department issued draft audit reports and is awaiting final comment from the Ministry of Agriculture, Palestinian Land Authority, Ministry of Transportation and Palestinian Broadcasting Corporation.

The PA continues to implement the PRDP and progress appears to have improved in the first quarter of 2010 compared to the last half of 2009. The new electricity regulator has become operational and the first transfer of electricity distribution to NEDCO is expected by June. The MoSA continues to implement its plan to merge the cash assistance plans. Spending has been contained well below budget, but this may be as a result of the uncertainty caused by the late passage of the 2010 budget. Non wage spending will almost certainly rise in the following quarters. While the PA has held the wage bill to the prorated quarterly budget target, hiring continues to be skewed toward

[2] The political situation prevents them from revisiting households in Gaza so payments are made based on the old system. However, MoSA is seeking a way to begin household visits in Gaza and hopes to begin doing so soon.

[3] Social Safety Net Reform Program (SSNRP) is the World Bank funded project and Social Hardship Cases are from the EU funded program. These are the two main assistance programs that are being merged.

the West bank and is not mostly in health and education. The lack of hiring in Gaza can be attributed to the fact that many of the services are being provided in Gaza by staff of the de factor authority. However, it is unclear why the new hiring in West Bank is at its current level if the original PRDP estimate of 3,000 new workers was meant to meet the needs of both Gaza and the West Bank. The faster its payroll expands the more difficult it will be for the PA to absorb the workers in Gaza who are not currently on the PA's payroll when there is a political solution to the separation of Gaza and the West Bank.