Action Fiche for West Bank and Gaza Strip

1. IDENTIFICATION

<table>
<thead>
<tr>
<th>Title/Number</th>
<th>PEGASE 2011: Additional support for recurrent expenditures of the Palestinian Authority (PA)</th>
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<tbody>
<tr>
<td>Total cost</td>
<td>EUR 85,000,000 - maximum EU contribution</td>
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<tr>
<td>Aid method / Method of implementation</td>
<td>Project approach – direct centralised management</td>
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<tr>
<th>DAC-code</th>
<th>Sector</th>
<th>Social/welfare services</th>
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<td>16010</td>
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2. RATIONALE

2.1. Sector context

Since its establishment in early 2008, the PEGASE Mechanism has provided direct financial support for the Palestinian Reform and Development Plan (PRDP). Through this support, PEGASE sustains the Palestinian Authority's (PA) efforts in the four PRDP key sectors of governance, social development, economic and private sector development and public infrastructure.

The PRDP, presented by the Palestinian Authority for a three-year term (2008-2010), received an unprecedented level of external support in 2008 that was maintained at a reduced but still high amount in 2009 and 2010. Its successor is due to be announced by the PA in the near future, but it is anticipated that the new "Palestinian National Plan" (2011-13) will build on, and not replace, PRDP. Despite continued sound budgetary management by Prime Minister (PM) Fayyad, which is gradually reducing the fiduciary deficit of the PA, the funds pledged by external donors for direct financial support are not sufficient to cover completely the PA’s financial gap foreseen for 2011. Moreover, in August 2009, PM Fayyad presented the PA’s "Programme of the Thirteenth Government", which is due to expire in August 2011 and the results of which will be evaluated shortly thereafter. Based on the PRDP, the plan aims at building strong governmental institutions which will serve as the basis for a future independent Palestinian State within a two-year time-frame. The plan focuses on the legal framework, organisational structures and processes, the use of technology in government, the management of financial resources and the management of human resources in civil and security sectors. The EU has expressed its support for PM Fayyad’s plan.

The EU funds provided in 2010 under PEGASE (EUR 209.4 million) from the European Commission budget for recurrent expenditures were complemented with just under EUR 73 million of funds from EU Member States: Spain contributed EUR 30 million for salaries and pensions for PA employees providing vital health and education services to the population; Germany paid EUR 20.3 million for the supply of fuel to the Gaza Power Plant; Italy EUR 7 million to cover social allowances to vulnerable Palestinian families (VPF); Sweden EUR 5.2 million to cover salaries; The Netherlands EUR 5.07 million for salaries to the civil police;
Ireland EUR 1.5 million for salaries/pensions and social allowances and Luxembourg EUR 0.5 million for salaries/pensions. Austria also made a contribution of EUR 1.5 million through assigned revenues for VPF payments. Switzerland contributed some EUR 1.9 million for the payment of social allowances. France made a contribution of USD 15.9 million to the PA, but not through PEGASE. Some Member States have contributed to the World Bank Trust Fund: however, the Ministry of Finance does not report on individual national contributions to the Fund. It is hoped that further contributions from Member States will be made during the budget year 2011.

Other donors are also providing support for direct financial assistance through non-PEGASE channels, including directly to the PA budget or via the World Bank Trust Fund. Further support was received in 2010 from Arab donors - Saudi Arabia (USD 143.7 million); United Arab Emirates (USD 43 million); Algeria (USD 26.3 million); Egypt (USD 8.1 million); Qatar (USD 9.8 million). The USA provided USD 222.9 million; India USD 9.9 million and the World Bank Trust Fund (USD 221.9 million). Further support is anticipated from Arab donors and from the USA in 2011, but not yet confirmed.

2.2. Lessons learnt

Actions under PEGASE build upon the successful experience of the Temporary International Mechanism in 2006 and 2007. PEGASE is implemented in full co-ordination with Palestinian partners and in co-operation and transparency with EU Member States, the European Parliament and other donors. It is particularly appreciated by the Palestinian Authority for its alignment with the PRDP and the strong sense of ownership on the part of Palestinians as well as for its flexibility and its catalytic nature in attracting funds from other donors without multiplying transaction costs.

The results of the mid-term review of the PEGASE Mechanism are being taken into account in the programme, and new Commission Decisions and Financing Agreements.

2.3. Complementary actions

In 2010, EUR 445 million was committed by the Commission for the benefit of the Palestinian population: EUR 394 million from European Neighbourhood and Partnership Instrument (ENPI) allocations, out of which approximately EUR 211 million for PEGASE support to recurrent expenditure (including Austria's contribution of EUR 1.5 million through assigned revenues) and EUR 103 million for United Nations Relief and Works Agency (UNRWA, responsible for providing basic health, education and social services to Palestine refugees and which included a contribution of EUR 86 million to their Regular Budget). EUR 69 million was allocated for projects aimed at social and economic development and institution-building in support of the Palestine Plan for Reform and Development and the PA's Two Year Plan for Statehood. A further EUR 58 million has been committed as humanitarian assistance to the Palestinian population in the Occupied Palestinian Territory and to Palestine refugees in Lebanon. EUR 2.2 million was mobilised from the Food Security budget line to support innovative actions. Support for civil society is being provided from the European Instrument for Human Rights and Democracy
Local donor co-ordination has been streamlined in accordance with the conclusions of the Ad-Hoc Liaison Committee (AHLC) meeting held 14 December 2005 in London following a proposal by the Commission, the World Bank and Norway to reform the Aid Management Structures. The Commission continues to play a leading role in these structures at all levels, as well as in local EU Member State co-ordination. Complementarity and co-ordination with other EU actions are assured through regular co-ordination meetings at Headquarters and daily contacts between the Commission's Directorate General for Humanitarian Aid and Civil Protection, and the European External Action Service and the Commission's Directorate General for Development and Cooperation staff working in the European Union Technical Assistance Office (EUTAO) in East Jerusalem. The PA made known to potential donors at the Sharm-el-Sheik Conference in March 2009 that PEGASE was amongst its preferred delivery mechanisms for channelling funds.

A first decision for the use of 2011 funds, allocating EUR 60 million to the PA to meet salary costs for the first three months of the year, and EUR 40 million to UNRWA's General Budget was taken by the Commission in December 2010. This assistance was "front-loaded" at the request of PM Fayyad, taking into account that other donors are not usually able to mobilise funds so early in the year.

3. **DESCRIPTION**

3.1. **Objectives**

The objective of this action to be implemented through PEGASE is to support the Palestinian Reform and Development Agenda by helping the PA to:

- reduce its budget deficit and implement its reform agenda;
- meet its obligations towards civil employees, pensioners and vulnerable sectors of Palestinian society;
- maintain the functioning of the administration and the provision of essential public services to the population; and,
- reduce the net lending (essentially advances for energy generation and distribution).

3.2. **Expected results and main activities**

Under this action it is intended to provide direct financial support to PEGASE. Three components are foreseen:

*Component 1: Supporting Palestinian administration and services (Indicative allocation EUR 45 million)*

PEGASE will make available an additional contribution to the payment of salaries and pensions to the PA civil servants in the West Bank and the Gaza Strip, notably in
the health and education sectors. The objective of this activity is to help the PA meet its financial obligations towards civil employees and pensioners. The regular contribution to the funding of the wages expenditure for civil servants reinforces the PA’s public finance management and public finance reform implementation. At the same time, it allows the administration to function and thereby to provide services to the Palestinians in the West Bank and Gaza Strip.

Component 2: Supporting the Palestinian social protection system (Indicative allocation EUR 40 million)

PEGASE will make available at regular intervals an additional contribution to the payment of social allowances to vulnerable Palestinian families in the West Bank and the Gaza Strip. The objective of this activity is to ensure the continued assistance to the poorest and most vulnerable Palestinian families dependent on financial aid from the PA. This activity reinforces the reform of the social protection system and improves PA public finances by reducing pressure on the budget by reducing expenditure through the coverage of allowances due to the beneficiaries of the Ministry of Social Affairs’ cash support programme.

Component 3: Private Sector Arrears

The PA seeks to develop a market economy led by the private sector. PEGASE supports the creation of a proper environment for Palestinian businesses to flourish by providing a facility for the payment of debts which the PA has built up towards private sector businesses for the purchase of goods and services. These contributions have resulted in a rapid injection of funds into the economy, providing relief to Palestinian businesses and raising their purchasing power. They further secured the employment of thousands of Palestinian workers and consequently, ensured that the provision of services to the administration could continue.

Component 4: Supporting the provision of essential public services

The objective of this activity is to help the Palestinian Authority ensure the continued provision of essential public services for the benefit of ordinary Palestinians. While it is not intended to finance fuel deliveries to the Gaza Power Generating Company, it is possible that some Member States and other donors will wish to continue doing so. PEGASE will therefore maintain the facility in place, notably for audit and verification of fuel deliveries to the power plant and support the PA’s fuel database.

3.3. Risks and assumptions

It is expected that contributions from Member States and other donors will be made available during the implementation period to complement the proposed funds. Fluctuations in the exchange rate may have an impact on funding needs.

Full co-operation with the Palestinian Authority is essential. This co-operation needs to be maintained, in particular for the identification of eligible beneficiaries and timing of payments and for the identification of eligible expenditure.

All actions under this special measure require that no additional restrictions are imposed by the Israeli Government, for example on financial transactions, including transfer of funds between the West Bank and Gaza Strip.
3.4. Cross-cutting Issues

Good governance principles are applied to the implementation mechanism and ownership on the part of the PA is assured. The actions proposed provide services vital to the social and economic rights of the Palestinian population.

3.5. Stakeholders

The direct beneficiary of the action is the Palestinian population.

Eligible beneficiaries and expenses are identified through a system based on strict and objective criteria set by the Commission and based upon requests and information provided by the Palestinian Authority.

PEGASE will be implemented in close co-operation and full partnership with the Ministry of Finance the Prime Minister's Office, and the technical Ministries and other Departments and Agencies of the PA and UNRWA.

PEGASE will be co-ordinated locally with the EU Member States, other international donors and International Organisations. In order to do so, full use will be made of the existing local co-ordination groups already in place such as the Local Development Forum, the AHLC structures, the co-ordination meeting between Member States and the EU Delegation.

All donors supporting the mechanism will also be key stakeholders.

4. IMPLEMENTATION ISSUES

4.1. Method of implementation

This project will be financed under a Financing Agreement signed with the Palestinian Authority Direct centralised management will be applied for all components.

PEGASE will be implemented by the Commission through the EUTAO in East Jerusalem, in close co-ordination with Member States officials and with the Palestinian Authority.

Disbursements will be made by the Commission either directly to the benefit of Palestinian Authority suppliers or to the Palestinian Authority following eligibility checks and verification and control procedures by external experts and international audit firms. These modalities have already been implemented through the earlier Temporary International Mechanism (TIM) mechanism.

4.2. Procurement and grant award procedures

All contracts implementing the action must be awarded and implemented in accordance with the procedures and standard documents laid down and published by the Commission for the implementation of external operations, in force at the time of the launch of the procedure in question.
Participation in the award of contracts for the present action shall be open to all natural and legal persons covered by the ENPI Regulation 1638/2006. The West Bank and Gaza Strip is facing a crisis, as defined in Article 168(2) of the Implementing Rules of the Financial Regulation. As a result negotiated contracting procedures or direct award for grant contracts may be used in accordance with applicable provisions for so long as this situation persists.

**Budget and calendar**

The maximum contribution to PEGASE – Additional Support to Recurrent Expenditures of the PA under this decision is EUR 85 million. The contribution will be used for:

- **Supporting Palestinian administration and services (indicative allocation EUR 45 million)**
- **Supporting the Palestinian social protection system (indicative allocation EUR 40 million)**
- **Private Sector arrears (no indicative allocation)**
- **Supporting the provision of essential public services (no indicative allocation)**

It is anticipated that, as in earlier years, other donors will make considerable contributions.

PEGASE ran for a three-year period in line with the PRDP, covering the financial years of 2008, 2009 and 2010. The mechanism will be extended to accompany the successor PA strategy to PRDP, due to be announced in the coming weeks. The period of operational implementation of the current action is 24 months. The funds under this decision are expected to be totally disbursed in 2011 for Component 1 (PA salaries/pensions) and mid 2012 for Component 2 (social allowances).

Funds for the necessary technical assistance, evaluation, audit and visibility actions have already been made available under previous Commission Decisions.

4.3. **Performance monitoring**

PEGASE will continue to implement a comprehensive monitoring, verification and control system to provide reassurance over the use of their funds, and the efficient and effective provision of support to the Palestinian administration and population while fully protecting donor interests.

Monitoring arrangements also include reviews to take stock of other donor contributions, reviews by the World Bank on reform progress, reviews by the International Monetary Fund on budget execution as well as other relevant political developments.

Payments will be executed in accordance with Commission regulations. A sophisticated and uniform financial reporting system is in place and will continue to be implemented, giving detailed information on all operations processed. Individual
beneficiaries as well as businesses will be uniformly checked against international sanctions lists.

4.4. Evaluation and audit

Financial experts and qualified auditors will work for PEGASE which will be complemented by Commission and Member States specialists and international or local experts.

Advanced monitoring, control and audit systems are set up for all of PEGASE’s activities. All donors participating in PEGASE have full access to the corresponding monitoring and audit reports on the basis of which their contributions are disbursed.

As well as audits of eligible expenditures to identify and validate payments, the PEGASE team will organise a general annual audit of the programme in accordance with international standards with a view to providing the maximum level of assurance. Donors will be invited to participate. In addition, contributing donors may carry out ex-post audits of expenditures covered by their payments.

In addition, a mid-term evaluation of PEGASE was undertaken and the results of this evaluation are being taken into account in new funding proposals. A comprehensive evaluation covering the first three years of the PEGASE mechanism aligned on the 3-year PRDP will be launched shortly.

Communication and visibility

The action will follow the visibility guidelines of the Commission.

Progress of PEGASE implementation will be communicated regularly to all stakeholders, including through a weekly bulletin. Information meetings are held with Member States in Brussels as well as locally.