PROJECT INFORMATION DOCUMENT (PID)  
APPRAISAL STAGE  

REPORT NO.: PIDA663  

I. Project Context  

Country Context  

The Palestinian Authority (PA) was established initially for a five-year interim period after the Oslo Accords (1993-95) with responsibility for the administration of the territory under its control. During this time of relative political stability, the economy grew rapidly and in 2000, immediately prior to the intifāda, growth was anticipated 5% in real terms and unemployment had reached a low of 9%. Subsequent to the end of the second Intifāda (in 2004), the PA embarked on a process of recovery and reform. This stability was disrupted after the Palestinian Legislative Council elections in 2006, which resulted in the suspension of much of the international aid and the transfer of clearance revenues from the Government of Israel (GoI) to the PA. Subsequent to the establishment of the Caretaker Government in 2007, fiscal stabilization resumed with a new influx of Donor aid and in the transfer of clearance revenues with the accrued interest from Israel. The PA issued its Palestinian Reform and Development Plan for 2008-10 (PRDP) with development partners pledging financial support. The Palestinian Authority (PA) has progressed in building its institutions and macroeconomic policy in accordance initially with the PRDP and, more recently, with the Palestinian National Development Plan, 2011-2013 (PNDP).  

The Palestinian Authority (PA) faces an increasingly difficult fiscal situation. Following robust GDP growth in recent years, economic activity in the Palestinian Territories significantly slowed in 2012. According to the Palestinian Central Bureau of Statistics (PCBS), real GDP growth for the
first three quarters of 2012 was 6.1 percent down from an average of 11 percent in 2010 and 2011. The declining trend was witnessed in both the West Bank and Gaza. For instance, Gaza’s economy was growing at an average rate of 15 percent between 2010 and 2011. However, growth dropped to 7.7 percent in the first three quarters of 2012. In the West Bank, real GDP growth averaged 9 percent between 2010 and 2011, but it declined to 5.5 percent during the first three quarters of 2012.

The current multi-layered system of physical, institutional and administrative restrictions that have fragmented the territory into small enclaves continues to stand in the way of increased economic growth and private sector investment. The fragmentation goes beyond a West Bank and Gaza divide, with the West Bank further fragmented into Areas A, B and C, each with its concomitant administrative and security arrangements. The Gaza Strip is further affected by periods of blockade, especially immediately after the December 2008 – January 2009 hostilities which affected all the border crossings, restricted imports and movement of cash to banks, led to suspension of exports and a general ban on the movement of people. The lifting of some restrictions in June 2010 and February 2011 has provided some relief. Nonetheless, growth of the economy continued to be constrained by restrictions on movement of goods, services and labor.

II. Sectoral and Institutional Context

The Palestinian population is largely urban with 74% living in 134 municipalities. Municipalities, which existed prior to the establishment of the Palestinian Authority, have a clear role as the lowest level of governance, representation and accountability for citizens. Municipal Councils are elected and the last election took place October 2012. However, municipal governments face profound challenges in meeting their responsibilities. Budgets have been shrinking due to the ongoing conflict, poor municipal management and a culture of nonpayment amongst users- thus eroding the coverage and quality of municipal services. Although municipalities can access seventeen revenue sources, collections are extremely volatile. For example, West Bank municipalities saw a 15% decline in revenues between 2010 and 2011 while Gaza municipalities saw a 43% increase in revenues during the same period. Although property tax collection has increased, its use as an intercept by the MoF to offset municipal water and electricity debt, coupled with a lack of transparency in the calculation and transfer of the intercept makes it almost impossible for municipalities to use it as a reliable source of income for planning purposes. Consequently, although the 134 municipalities are required to provide basic services within 27 functions mandated by law, only three functions (solid waste management, street maintenance and water supply) are consistently provided by the majority of municipalities. It is doubtful that municipalities could finance extensive service improvements in the current fiscal context. A recent study shows that most (75/98 who participated in the study) had a 2010 deficit.

Nonetheless, the PA and municipalities have demonstrated significant progress in municipal and local development. In 2005, the PA established the Municipal Development and Lending Fund (MDLF) to address financing and capacity building of municipalities. Established by a Ministerial Decree, the MDLF has the legal mandate to provide development assistance to municipalities through transparent, rules-based and efficient financing. The MDLF is also the PA’s preferred mechanism for channeling development assistance to municipalities. The PA, through the MDLF, with the support of Donors, and have implemented several municipal reforms with the support of Donor financed projects (including the Local Government Capacity Building Project, Emergency Municipal Services Rehabilitation Project 1&II). In 2009, the PA developed the Municipal Development Program which was supported by seven Donors (including the World Bank through the Municipal Development Project 1) to operationalize the local government goals of the PRDP
which is to strengthen local government through greater fiscal and administrative autonomy. The Municipal Development Program is a multi-phase PA program which provides municipalities with a combination of technical assistance and performance based grants for sub-projects. The formula for performance grants is designed to create incentives for municipal performance improvements. The initial project, MDP 1, was designed to test tools for performance improvements, particularly in municipal finance and municipal planning, through the provision of a performance based grant and capacity building packages to municipalities through four Parts or Components. MDP 1 is meeting its Key Performance Indicator targets and is, in some cases, exceeding these. Eighty-six percent of municipalities have graduated to a higher performance category thus far, thus exceeding the target of fifteen percent for this performance indicator. Sixty-eight percent of municipalities disclosed information in at least two of the following three areas at project mid-term review: (i) financial data and municipal budgets; (ii) municipal ranking; and (iii) projects and achievements. This exceeds the PDO indicator target of thirty percent for 2011.

The MDP 2 will consolidate the MDLF’s experience in performance based grant programs. Practical achievements of the PA have included the development of a unified chart of accounts and standard budget guidelines. All municipalities now report their budgets yearly to the Ministry of Local Government. Fixed Assets Registration guidelines have been issued and implemented in at least 47 municipalities, a Financial Policies and Procedures Manual has been developed and is in use in at least 89 municipalities; and at least 84 municipalities have prepared Strategic Development and Investment Plans (SDIPs) in an effort to prioritize investments over the medium term. Furthermore, an IFMIS has been piloted in 33 municipalities. Finally, since 2008, the MoF supported by JICA and Danida has been rolling out a program to improve property tax collection. The collection has increased from USD 10m in 2006 to USD 30m in 2010. These improvements have resulted in the graduation of approximately 112 municipalities to a higher performance category in the national municipal performance ranking system developed as part of the PA’s MDP.

III. Project Development Objectives
The objective of the project is to improve municipal management practices for better service delivery and municipal transparency.

IV. Project Description

Component Name
Municipal Grants for Capital Investments
Support to Municipal Innovation
Technical Assistance for Municipalities and the MDLF
Project Implementation Support and Management Costs

V. Financing (in USD Million)

<table>
<thead>
<tr>
<th>Borrower</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>BELGIUM MOFA-Directorate-General for Int. Coop.(D)</td>
<td>6.80</td>
</tr>
<tr>
<td>DENMARK Danish Intl. Dev. Assistance (DANIDA)</td>
<td>1.20</td>
</tr>
<tr>
<td>EC European Commission</td>
<td>20.00</td>
</tr>
<tr>
<td>FRANCE French Agency for Development</td>
<td>6.30</td>
</tr>
<tr>
<td></td>
<td>2.50</td>
</tr>
</tbody>
</table>
VI. Implementation

Project Implementation: The MDLF will be responsible for project implementation including all payments to contractors and suppliers on behalf of municipalities.

The MDLF is managed by a Board of Directors (the Board) which is the policy and strategy-setting authority responsible for monitoring the direction and performance of the Fund. The Board Chairman is the Minister of Local Government and its 11 members consist of representatives of Public Sector entities (State Ministry for Planning, Ministry of Finance, Ministry of Public Works and Housing, and Ministry of National Economy), civil society (Engineers Association, Banking Association, Association of Palestinian Local Authorities, women’s association) and two mayors.

The MDLF has successfully demonstrated its capacity to effectively administer donor funded projects since its establishment in 2005 including the multi-donor financed MDP 1. (Note that this project, MDP 2 is essentially a repeater of MDP 1), the World Bank financed Emergency Municipal Services Rehabilitation Project (EMSRP), the multi-donor EMSRP 2, and the Local Government Capacity Building Project (financed by Denmark and administered by the World Bank), in addition to projects financed by Germany, France, Sweden and the Netherlands. MDP 2. The MDLF is currently fully staffed for all key positions required for project implementation.

Flow of Funds & Legal Relationships. The Recipient of the grant is the Palestinian Liberation Organization (PLO) for the benefit of the PA as with nearly all cases of assistance provided to the Palestinian people under the TFGWB. The PLO will make the proceeds of the Grant available to the PA through a Subsidiary Agreement. An On-Granting Agreement between the PA and the MDLF will further make the proceeds of the Grant available to the MDLF as the implementing agency. The Bank and the MDLF will also sign a Project Agreement. The MDLF would implement the project in accordance with the legal agreements and the Operations Manual. The Ministry of Finance (MoF) would open the Designated Account on behalf of the MDLF, under the Single Treasury Account. The MDLF would be responsible for managing the account but the Ministry of Finance is responsible for requesting replenishments from the World Bank. Other Financing Partners may have different arrangements for withdrawal applications.

Municipalities are responsible for sub-project implementation. The 134 local government units classified as municipalities by the MoLG – if they fulfill the eligibility criteria for the program – will be responsible for implementing sub-projects that they identify through a participatory public consultation process. Municipalities would be responsible for all contracting once the MDLF has approved the sub-projects. They will also submit invoices to the MDLF who will be responsible for making direct payments to contractors and suppliers, including for recurrent expenditures in Gaza. However, five pilot municipalities will manage grant funds as part of an effort to encourage greater
municipal responsibilities.

Results Monitoring and Evaluation: The project uses indicators aimed at fostering the principles of social accountability, sustainability, and transparency related to municipal service delivery. Data on outcome results including municipal performance rankings and MDLF Annual reports will be made public. Citizen feedback on service delivery improvements and systems’ transparency will also be sought and published periodically based on the results of Citizen and Client Beneficiary Satisfaction Surveys focusing on direct beneficiaries under Components 1 and 2a. Such feedback will be used to trigger management decisions on adjustments and for distilling lessons learned, to enable the PA to formulate and redesign its policies and procedures towards improving the lives of citizens. Outcome and intermediate indicators are presented in Annex 1.

Arrangements for Results Monitoring: The MDLF will be responsible for monitoring the achievements of the PDO, project outcomes, and physical, financial and procurement performance of the project. MDLF will continue to use a web-based Program Management Information System (PGMIS) as well as the Financial Management Information System (FMIS) to automate data aggregation, storage, and presentation as part of a results-based M&E system. In addition to data collection exercises carried out directly by MDLF for project reports, periodic independent evaluations and assessments (including an infrastructure survey, and Citizen and Client Beneficiary Satisfaction Surveys) will also be outsourced in order to measure achievement of the PDO (See Annex 3). The MDLF will produce Semi-Annual and Annual Progress Reports and Quarterly Interim Financial Management Reports, to report on the achievement of the PDO and implementation progress of the project activities. (See Annex 3).

Results-Based Outcome Monitoring at the MDLF: The MDLF uses a Results-Based M&E system, which attempts to measure the relevance effectiveness, efficiency, impact, and sustainability of initiatives implemented by the institution. The MDLF’s Results-Based Monitoring Manual (RBMM) has aligned the individual objectives of various projects and programs with the PA’s PNDP strategic objectives. The M&E arrangements proposed under the project, including the Results Framework (Annex 1) and data collection tools (including an infrastructure survey, Citizen and Client Beneficiary Satisfaction Surveys and Municipal Ranking Survey) are fully consistent with the RBMM and the MDLF’s M&E system. As such, no additional arrangements or staff is required for the M & E of this project.

Sustainability
The project supports municipalities in improving their performance through a combination of incentives (financing of capital expenditures) and Technical Assistance for capacity building. Municipalities will continue to improve their ability to undertake and implement plans, manage finances and generate revenues so that they can continue to provide quality service to their citizens and continue to expand their accountability to their citizens, thereby working towards sustainability.

VII. Safeguard Policies (including public consultation)

<table>
<thead>
<tr>
<th>Safeguard Policies Triggered by the Project</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environmental Assessment OP/BP 4.01</td>
<td>✗</td>
<td></td>
</tr>
<tr>
<td>Natural Habitats OP/BP 4.04</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Forests OP/BP 4.36</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Pest Management OP 4.09</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Physical Cultural Resources OP/BP 4.11</td>
<td>✗</td>
<td></td>
</tr>
<tr>
<td>Indigenous Peoples OP/BP 4.10</td>
<td>✗</td>
<td></td>
</tr>
<tr>
<td>Involuntary Resettlement OP/BP 4.12</td>
<td>✗</td>
<td></td>
</tr>
<tr>
<td>Safety of Dams OP/BP 4.37</td>
<td>✗</td>
<td></td>
</tr>
<tr>
<td>Projects on International Waterways OP/BP 7.50</td>
<td>✗</td>
<td></td>
</tr>
<tr>
<td>Projects in Disputed Areas OP/BP 7.60</td>
<td>✗</td>
<td></td>
</tr>
</tbody>
</table>

**VIII. Contact point**

**World Bank**

Contact: Soraya Goga  
Title: Senior Urban Development Specialist  
Tel: 5366+214/9  
Email: sgoga@worldbank.org

**Borrower/Client/Recipient**

Name: Palestine Liberation Organization  
Contact:  
Title:  
Tel: 2973382  
Email: lsbaih@yahoo.com

**Implementing Agencies**

Name: Municipal Development and Lending Fund  
Contact:  
Title:  
Tel: 02 296 6610  
Email: abednofal@mdlf.org.ps

**IX. For more information contact:**

The InfoShop  
The World Bank  
1818 H Street, NW  
Washington, D.C. 20433  
Telephone: (202) 458-4500  
Fax: (202) 522-1500  
Web: http://www.worldbank.org/infoshop