



THE WORLD BANK

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West Bank and Gaza

Institutional Capacity

July 2011

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I. INTRODUCTION

1. In August 2009 the Palestinian Authority (PA) presented a program entitled “Palestine: Ending the Occupation, Establishing the State.” Given its two-year time horizon and the high priority it accords to institution building, the second anniversary of the launching of this program is a useful occasion to assess West Bank and Gaza (WB&G) institutional capacity. Therefore, the objective of this paper is to gather the evidence and experience that collectively underpin the World Bank’s view of the functioning of WB&G public institutions, and their success in implementing reforms. No study could be comprehensive in examining all aspects of WB&G public institutions. As the PA itself has observed, there are several domains where new reform efforts are needed, or where reforms have only just begun. However, our analysis indicates that WB&G public institutions perform at least as well as a large number of World Bank client countries.

II. BACKGROUND/CONTEXT

2. Since the collapse of the power-sharing government in 2007, the authority of the PA has mainly been limited to the West Bank, while Hamas administration prevails in Gaza. Since May 2011, the two administrations have been discussing a unity cabinet composed of politically independent technocrats. Most of the studies cited below pertain to both West Bank and Gaza, although the institution-building agenda was mainly undertaken in the West Bank. Under the Israeli restrictions on the West Bank, a number of controls have been imposed limiting internal and external mobility. These controls include barriers at all international borders and numerous check points and barriers hindering internal transport of goods and people. The controls also block access to some 60 percent of land in the West Bank and most natural sources of water. The Government of Israel (GOI) prevents movement between Gaza and the West Bank and strictly controls the population registry. These controls and barriers have a major impact on cost of production and cost of living in WB&G, on economic growth and investment, and on employment, wages and poverty.¹ In addition, they greatly constrain the PA’s ability to develop its institutions.

III. COMPARISON TO INTERNATIONAL NORMS: THE OECD FRAMEWORK²

3. The remainder of this paper describes the institutional attainments of the Palestinian Authority as seen through the reforms and achievements in several domains. We ask how WB&G capacity to fulfill state functions compares to capacity in MENA and other countries, and show that it is often comparable and sometimes superior. In addition, we provide substantial evidence that the WB&G has considerable ability and willingness to improve its capacity, as significant recent reforms demonstrate. The relevant

¹ World Bank, “The Underpinnings of the Future Palestinian State: Sustainable Growth and Institutions,” September 2010; World Bank, “Coping with Conflict? Poverty and Inclusion in the West Bank and Gaza,” June 2011; Sharma and Vishwanath, “Mobility Restrictions and Labor Market Dynamics in Conflict Affected West Bank and Gaza,” World Bank, January 2011; Mandy Turner, ‘Challenges of Implementing the State-building Programme’ Presentation to the UN Seminar on Assistance to the Palestinian People, Helsinki, 28-29 April 2011.

² OECD, “Supporting State-building in Situations of Conflict and Fragility,” DAC Guidelines and Reference Series, 2011

domains were chosen according to an OECD framework defining key capabilities common to *effective* states: providing security and justice; raising, prioritizing and spending revenues effectively; facilitating economic development and employment; and delivering basic services. These capabilities are seconded in a framework defined by DFID.³ The OECD framework is defined as part of an agenda to support progress in statebuilding from conditions of post-conflict and fragility towards resilience. Thus the OECD framework is defined according to international norms of state functions, and not according to World Bank activities. Nevertheless, the Bank's extensive engagement in the region provides a window on PA capacity in each of these key domains.

A. Security and Justice

4. The Bank is not directly involved in the security and justice sectors, but both have been monitored and reported on as important factors in the investment climate. A variety of data has also been collected through perception surveys conducted among the beneficiaries of security and justice services.

Security

5. Security was one of four national goals espoused by the PRDP, considered a linchpin reform for improving the business environment. The PA has made major progress in bringing safety and security to the West Bank in recent years. "The PA deployed a large number of newly trained security forces throughout the major cities who have helped restore security and create a sense of normalcy. The improved security situation has led the GOI to reduce some of its internal security restrictions and is often cited by businesses as an important reason for the increasing economic activity."⁴ Public employment figures available to the Bank indicate a total number of 63,515 persons on the PA security forces payroll in early 2010, of which slightly more than half are assigned to Gaza. In addition, there is a further number, the magnitude of which is not known, of security employees hired directly by the Hamas Government and paid directly. Security personnel in the West Bank have been extensively trained by US and other Western government teams, and their capacity has been greatly strengthened. Several challenges lie ahead. The second is bringing the cost down of the security sector. Currently, the wage bill of PA's security personnel is running at over 13% of GDP. A third is ensuring that the PA's security forces continue to apply proper legal procedures in the arrest and detainment of citizens.⁵

6. According to the National Development Plan 2011-2013 (NDP), the Palestinian Center for Policy and Survey Research reported that as of the last quarter of 2009, 63 percent of Palestinians felt secure as opposed to 32 percent in March 2008, while two thirds of Palestinians rate the provision of security services as good. A survey by Fafo Institute for Applied International Studies also reports that nearly 60 percent of respondents felt that the PA had improved the security situation in the West Bank.⁶

7. A PCBS-sponsored survey of over 1500 Palestinians from both West Bank and Gaza, conducted in late 2010 by independent consultants, found that respondents had a strong degree of confidence in the police, security services, and the courts and judicial system. Security services and judicial and court

³ States in Development: Understanding State-building, by Alan Whaites, 2008. This framework proposes that after a political settlement: "the forging of a common understanding, usually among elites, that their interests or beliefs are served by a particular way of organizing political power," the key state functions include security, raising revenues and ruling through laws as well as progress in meeting social expectations.

⁴ Palestinian Reform and Development Plan Development Policy Grant III, Project Document, World Bank, August 2010.

⁵ 2010 Annual Report of the Independent Human Rights Commission.

⁶ Fafo Institute, "Palestinian Opinions about Governance, Institutions and Political Leaders: Synthesis of Results of Fafo's Opinion Polls in the West Bank and Gaza Strip, 2005-2011."

services rated 73 and 70 percent satisfaction rates, respectively. 83 percent of respondents reported a positive attitude toward the civil defense forces with 78 percent having a favorable view of the police.

Justice

8. The Palestinian justice sector has witnessed significant reforms during the last five to ten years. These reforms are backed by the Palestinian Authority, as well as generous support from the international community. Assistance from the donor community has been considerable over last decade, and was notably increased following 2007. The United States Agency for International Development (USAID), the European Union (EU), the Government of Netherlands, the Canadian International Development Agency (CIDA), the Government of Japan, the UNDP, the U.S. State Department and a handful of other EU states (such as France, Italy, and others) were among the main donors through multiple projects aimed at supporting the Ministry of Justice, the Supreme Judicial Council, the Public Prosecution, the Palestinian Bar Association, and civil society organizations active in the field.

9. Nevertheless, the leadership of the PA in the justice sector was quickly established and is apparent in a number of initiatives. The Supreme Judicial Council, the Ministry of Justice, and the Attorney General Office have been transformed from person-centered bodies into real institutions with clear mandates, modus operandi, and strategic visions. The Ministry of Justice has started conducting regular exercises on annual strategic planning. In an attempt to realize and expedite capacity building and institutional development, the Ministry of Justice has succeeded in obtaining funding for top notch experts and consultants to be housed at the ministry. In February 2011, the ministry organized a 3-day workshop in Jericho to discuss, brainstorm and obtain expertise on best practices on criminal law, as part of the ministry's endeavor to draft and pass a modern criminal code. This is part of a broader effort, highlighted in the 2009 Statehood strategy⁷, to modernize the legal framework which is being done in a consultative manner, involving civil society, the private sector and academic experts.

10. The Supreme Judicial Council (SJC) has also taken impressive steps towards increased institutionalization, anchored in a series of reform strategies developed in a consultative manner. New departments were created and activated within the SJC with clear mandates and powers, such as the Court Administration Department, the IT Department, the Planning Department, the Inspection Department and the Technical Department. Appointment and promotion of judges and public prosecutors is reportedly being undertaken through more transparent and objective processes, including written and oral exams/competitions. Coordination with donors, as well as with other justice sector institutions has reportedly improved. Efforts to promote the independence of judiciary were undertaken, as well as efforts to address judicial bottlenecks and delays in resolution of disputes. The SJC had also taken steps to reduce conflicts of interest in the judiciary by rotating judges to different governorates.

11. As a result, services rendered by the justice sector have significantly improved, and perceptions of Palestinians towards the courts and the justice sector in general have significantly improved. The NDP reports that according to the High Judicial Council, Magistrate and First Instance courts handled 67 percent more cases in 2009 than in 2008. The number of judges on bench has almost tripled in the last ten years; specialized courts were established (such as the Anti-Corruption Court in 2010; the Customs Court in 2011); and specialized chambers within regular courts were also established (e.g. separate criminal and civil chambers; specialized labor cases chambers). Multiple new courthouses were constructed and refurbished (in Jenin, Nablus, Jericho), and efforts to construct other courthouses are underway. All courts are currently automated, and modern software (Mizan I and Mizan II) to manage cases are currently utilized. Manuals for case management and for other justice sector-related services (e.g.

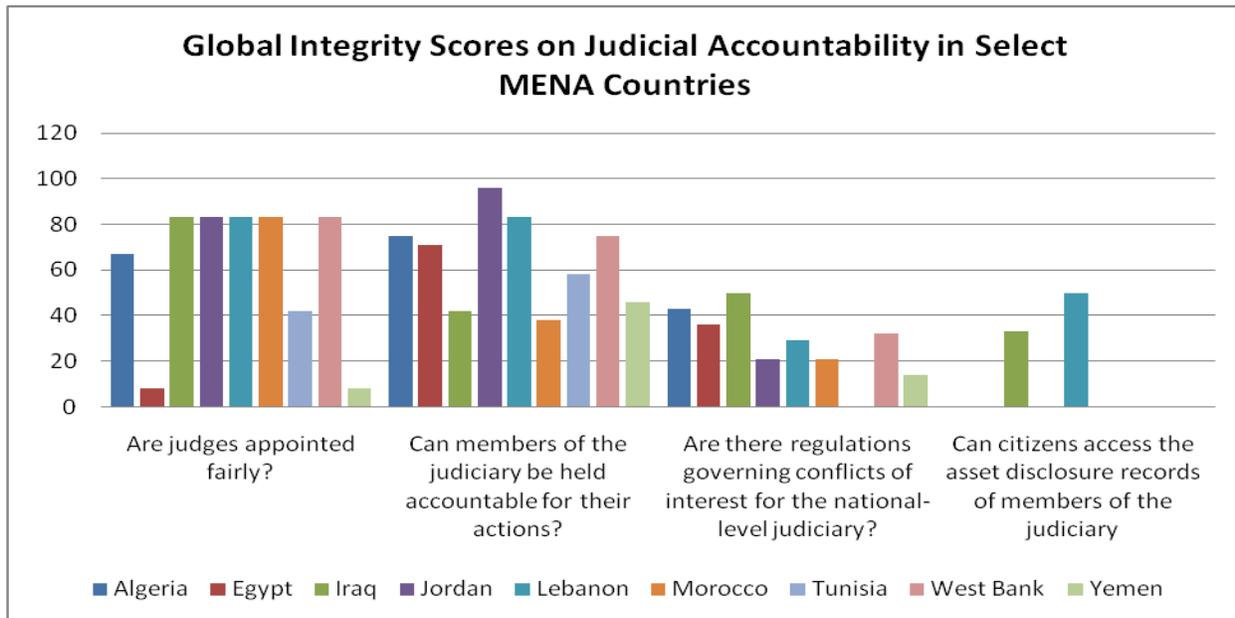
⁷ Palestinian Authority, August 2009, *Palestine: Ending the Occupation, Establishing the State*,

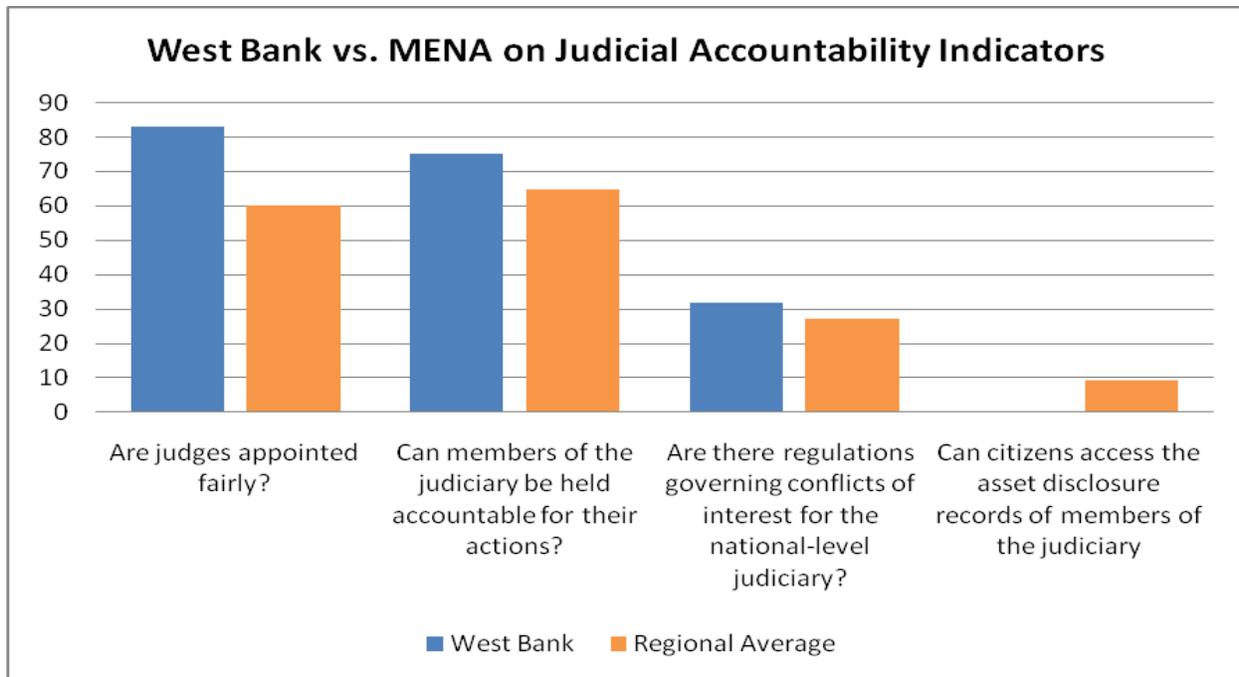
notarization; enforcement) have been written and are being used. And Notary Public offices in several districts have been refurbished, adequately staffed, and automated, and advanced archiving systems have been introduced as well. The Sharia Court system, which addresses personal status issues for Muslim Palestinians, has introduced an Alimony Fund to ensure alimony and child support payments are made on time.

12. Of course, there is still room for improvement, and the situation is not ideal. Continued conflict with Israel and the obstacles often imposed by the Israeli authorities on freedom of movement and access for Palestinians, as well as on the liberty of security forces to mobilize and operate in West Bank areas under Israeli control (namely Area C), still hinder the delivery of justice. And the jurisdictions and powers among main justice sector institutions—namely the Ministry of Justice and the Supreme Judicial Council have not yet been clearly delineated in law. Coordination among justice sector institutions could also be improved and enhanced.

13. Litigants are now witnessing much more speedy trials; and, unlike the case seven to eight years ago, court decisions are being more regularly enforced and honored. As a result, the public’s confidence in the justice sector has increased, as evident by the increasing numbers of cases filed before courts nowadays, compared to a few years ago. Disputants are now less likely to resort to parallel means for resolving disputes.

14. The tables below show that West Bank compares favorably to other countries in the MENA region on judicial accountability indicators, with the exception of asset disclosure. The PA has an asset declaration regime de jure but not yet in practice. The regime will be the responsibility of the new Anti Corruption Commission which is currently working on an asset disclosure process.





Source: Global Integrity Report: Judicial Accountability, 2008

B. Revenues and Expenditures

15. At the end of the 1990s, the condition of Public Financial Management (PFM) in WB&G was very weak. Despite the continuing Israeli restrictions, things started to change for the better when a reform program was initiated following the appointment of a new finance minister in 2002. Since then, the PA has implemented a remarkably strong program of PFM reform, with a clear emphasis on “getting the basics” right, beginning with budget execution with the establishment of central control of revenues and spending. This has proceeded in two stages, beginning in 2002, with interruption and partial reversal between 2006-07, followed by restoration of systems and processes in 2008, and their further development to the present. The IMF has said, “IMF staff considers that the PA has successfully implemented core institution-building and public finance reforms set out in its Palestinian Reform and Development Plan (PRDP) for 2008-10.”⁸

16. Progress on tax administration reform has moved slowly until recently. It should be remembered that the PA operates under a number of constraints in the tax domain. For example, the PA is constrained in its control of customs revenues by lack of access to border control points, lack of information on imports from the Israeli customs service, and restrictions on imports to Gaza which also limit customs revenues. GOI has declined to provide needed information on WB&G imports passing through Israel, and meetings of the joint PA/Israeli revenue committee have been suspended due to a GOI decision to withdraw its cooperation. Nevertheless, the PA has designed and launched a three-year plan aimed at broadening the tax base and raising compliance, with a priority in 2011 on strengthening supervision of border crossings. This agenda, requiring restored cooperation with GOI, will allow a greater collection of clearance revenues from VAT and a better assessment of potential VAT revenues through comprehensive data compiled by GOI on imports from Israel.

⁸ IMF, “Macroeconomic and Fiscal Framework for the West Bank and Gaza: Sixth Review of Progress,” September 2010.

17. The PA has made important progress in reducing net lending to municipalities by taking steps to place electricity distribution on a commercial basis. It has also taken steps to manage property taxes, and improve local revenues. The PA has also created the Municipal Development and Lending Fund (MDLF) to further address municipal finance and capacity building. Through the MDLF, funds for capital expenditures are transferred to municipalities using a formula based on population, need and performance. The transfer is financed by seven donors and the PA and has improved transparency in the municipal allocation process. And this year the PA has provided guidelines to the newly amalgamated municipalities on how to raise revenues to ensure financing for amalgamated services.

18. During the last year, the authorities have launched the unification of VAT and income tax administrations for large taxpayers. In 2010, the PA increased domestic revenues to cover 63 percent of spending, up from 50 percent in 2009, while reducing donor budget support to 15.5 percent of GDP, down from 22 percent in 2009. Currently the PA mobilizes domestic revenue equal to nearly 27 percent of GDP, a rate higher than most countries in the region.

Public financial management

19. On the expenditure side, at the beginning of the reform period budget controls were ineffective, resulting in indiscriminate spending by line ministries. These had multiple bank accounts, significant off-budget revenues and spending, and incurred payment arrears leading to large overall deficits. Financial accounts were not produced, there was no internal audit, and external audit was not effective. Most importantly, the Ministry of Finance lacked both the tools and the political authority to manage public finances well, in an environment where formal rules were frequently overridden.

20. Things changed markedly for the better with the reform dynamics launched in 2002. In the Bank's view, reforms in the West Bank are a best practice example of what can be done to establish good PFM in a post-conflict setting. Indeed, these PFM reforms have been the foundation for building the confidence of external donors, bringing aid on budget, increasingly as general support, and greatly expanding it. Domestic revenues have strengthened, and, in turn, the reforms have underpinned a rapid expansion of the WB economy.

21. The first stage, launched at a time of acute fiscal crisis in 2002, was aimed at asserting central control over revenues and spending. This was done through closing a range of revenue bank accounts and the establishment of a treasury single account (TSA) enabling the central management of cash. All salary payments were brought under the Ministry of Finance, thereby curbing unauthorized hiring. Extra budgetary revenues and spending were brought into the budget, making the budget more transparent and comprehensive. Expenditures were largely centralized at the Ministry of Finance and this was supplemented by having financial controllers reporting to the Ministry of Finance were installed in each ministry. An internal audit unit was also established at the Ministry of Finance. Monthly reports of revenues and spending were published on the Ministry of Finance's website. These steps provided the tools for the Ministry of Finance to increase its control of spending, increase revenues, reduce arrears and begin to check the growth of fiscal deficits. Although a PEFA exercise carried out in 2006 still rated performance critically, there is no doubt that the foundations of a well performing PFM system were laid down in this first period.

22. The elections in 2006 and the formation of a Hamas government precipitated a fiscal crisis, as donors stopped direct financial support, and the Israeli authorities withheld clearance payments. The TSA was undermined as alternative financing arrangements were established by donors including supporting civil servants through direct payments. Increased hiring both before and after the election without regard to proper procedures increased the payroll by about 35,000. Public finances collapsed and arrears to suppliers and employees ballooned.

23. With the advent of the Caretaker Government, the PFM measures of the earlier period were reinstated, and reforms accelerated. The first requirement was to create a new central accounting capacity in Ramallah, since the Accountant-General's Department had been located in Gaza, now under Hamas control. A new integrated financial management system accounting system was established that consolidated the accounting and expenditure control functions. The system was gradually rolled out to line ministries as some of the earlier centralization of expenditure was unwound. In 2010 the system was further developed with the inclusion of a procurement module to support commitment control. With the benefit of the new system, for the first time, the public accounts for 2008 were completed on time and submitted to the newly created state audit agency, SAACB, for external audit. The accounts met international accounting standards⁹ in most respects and the Ministry of Finance expects to fully comply with the international standards with the 2010 accounts. The quality of monthly revenue and expenditure reports has also advanced over the earlier period. To make annual budgeting more strategic, the Government announced the introduction of program based budgeting, and the 2009 budget was the first presented in this way, bringing together recurrent and development budgets. Since 2008 a Medium Term Financial Framework has been presented annually in the budget speech and a medium term fiscal strategy was incorporated into the National Development Plan, 2011-2013. As part of the NDP process a strategic plan was also drawn up to guide the further development of PFM.

24. In the Bank's view, the most impressive part of the financial management reforms has been the establishment of the authority of the Ministry of Finance to supervise public finances, and the building of systems and staff capacities to do so. This has translated into greater trust in the way public finances are managed, and this has helped improve service delivery. Challenges remain. Attention to budget execution rightly was given priority over budget preparation. Now the task is to make annual budgeting less incremental and more strategic, focusing programs on the core functions of government. The new accounting system also provides an opportunity to further extend the transparency of budget reporting. The PA will also have to continue the winding down of exceptionally large fiscal deficits, which have been running at over 20% of GDP in recent years. This should come through the careful management of the relative reduction of international aid flows, tight control of recurrent and capital spending and increased focus on strategic priorities, and enabling domestic revenues to rise through the impact of economic growth on the tax base. And if the private sector is to grow rapidly, there will be need to continue the relative shift in public expenditures from spending on wages and transfers (85 percent of the recurrent budget) to greater emphasis on capital spending through development projects, all the while keeping deficits on a downward trend to GDP. These changes are outlined in aggregate terms in the NDP, and in turn are highly dependent on rapid growth broadening the tax base, and for the medium term, donors maintaining aid flows, both as general budget support and supporting public investment projects.

25. External assistance plays a very large role in the sustainability of WB&G institutions. To a great extent, however, this assistance compensates for the severe economic constraints under which WB&G operates. The need for such assistance could be expected to decline if the external constraints on private sector development were removed. However, even with the significant growth dividend that peace would bring, and the associated growth in the size of the tax base, it is highly unlikely that the WB&G could maintain current security and civil service commitments without substantial continued external assistance. The PA recognizes this and is taking steps to reduce donor dependency while creating institutions and conditions that will allow it to become more independent and fiscally stable if a sustainable political solution is found.

⁹ The International Public Sector Accounting Standard on a cash basis.

Civil service

26. The public civil service has followed much the same trajectory as public finances. From the formation of the PA after the Oslo Accords in 1993 until 2002, government payrolls expanded rapidly, with largely uncontrolled hiring and with insufficient attention paid to merit. Although a civil service law was passed in 1998 which defined the parameters by which the public service should be run, implementing regulations were not passed until 2004, and hiring by line ministries regularly was approved without regard either to justified need or budget funding. There are many highly skilled individuals in the PA, enabling the administration to perform quite well. At the same time, there are others occupying positions for which they are unqualified, and are largely ignored by ministers and senior management seeking to get things done.

27. From 2002, the payroll was brought under progressively tighter control through financial reforms. Nonetheless, by 2006 total public service employment, including teachers, health workers, security services and general civil servants, totaled around 150,000 – including 17,000 who had been hired in late 2005 without following the proper procedures. This was a large number for a population of around 3.5 million, particularly in the security area. Underlying this was a widespread view that, in the light of reduced Palestinian employment in Israel and Occupation constrained job opportunities in WB&G, it was the responsibility of the PA to provide jobs directly.

28. Between 2006 and 2007 PA employment expanded again, through the recruitment of almost 20,000 staff by Hamas, resulting in a total public service by the time the caretaker government was established of about 170,000. Numbers were quickly reduced through dismissal of the additional hires, deemed illegal. Since then, the public service has grown slowly, within an annual cap of 3,000 additional positions, mostly teachers and health workers, not all of whom are recruited within the year (partly because of security clearance delays). Payroll data for the beginning of 2010 show a total of 149,827 staff, with 84,580 in West Bank and 63,515 in Gaza. Within this total are 63,474 security staff (34,208 in Gaza, 29,266 in WB), 40,907 teachers (30,626 in WB, 10,281 in Gaza) and 12,210 health workers (5354 in WB, 6856 in Gaza). Outside the PA payroll are a number of staff hired directly by Hamas since 2007, of all categories.

29. Public service grades and pay scales, including allowance categories, are, like in some other governments in the Region, prescribed in the Civil Service Law, imparting inflexibility to pay adjustments, which have mostly come in the form of changes to allowances. Present pay levels are mostly in line relative to per capita income, but considered low alongside the cost of living for many staff, and scales are fairly compressed. To compensate for what is seen to be inadequate pay, grading of positions has been inflated. (There are more officers in the security forces than other ranks, and director-general positions are often created to enable professional staff to be employed, rather than matched to departmental responsibilities).

30. Currently, the PA, led by the General Personnel Council (GPC) has embarked on a job classification exercise, based upon job descriptions for each post and the development of approved staffing structures for all ministries, departments and agencies. A technical committee is revising the 1998 Civil Service Law, with a mandate to address inconsistencies between the law and the regulations, fill gaps and define processes better. There are plans afoot to create a public administration college. At the same time, the government has begun looking at the mandates and structures of ministries and agencies, with a view to streamlining (though at this point, there are no plans for downsizing). Reviewing the organizational structure of the government is one of the core institutional development objectives of the Salam Fayyad Plan. The aim is to eliminate duplication, clarify roles and responsibilities, and improve the machinery of government for efficient service delivery. Finally, under the leadership of the GPC, the government is looking at how existing recruitment and promotion processes could be made more merit based, supported by improved staff performance management and a greater emphasis on

training. This is work in progress, but critical to greater efficiency and effectiveness of the civil service, and fully in line with the strategy of 2009 which commits the government to “implement professional, merit-based systems and processes that will ensure equal opportunity and fairness in recruitment and promotion decisions”.

31. , There are many challenges ahead. Gains from undertaking a job classification exercise are limited if the newly classified jobs are to be fitted into the existing pay and grading structure, and not a new one. But to introduce a new pay scale, which provides for wider differentials and integrates most allowances into base pay, could have fiscal implications for the wage bill and the government’s nominally funded but in practice cash based pension scheme. There is a need to move from incremental staff budgeting (which the 3,000 hiring cap promotes), to one in which line ministries are challenged to meet needs by redeploying existing staff or modifying policies and programs. To keep a viable age structure for the public service, and equitably retire unqualified staff, there may be a need for some sort of early retirement scheme, if funding can be found. Updating of the civil service law could be an opportunity to spell out in clear terms the principles that will underpin the civil service of a sovereign state, and clarify the roles and responsibilities of the main institutional players, and the essential features of a modern human resource management system.

32. By far the most pressing challenge is the size of the public service wage bill, which is very high by global standards at around 22% of GDP. This is a challenge for both the PA and for donors, who effectively are funding the wage bill through general budget support. In many respects the large wage bill share of GDP is a reflection of the exceptional circumstances of WB&G, its tradition of using the public sector as an instrument of social policy, and the geographically truncated and occupation-constrained nature of the WB&G economy, which can be expected to grow rapidly in the short run if there is a peace agreement. At the same time, the public sector wage bill will need exceptionally careful management, to ensure the number of posts remains under control and, increasingly, line ministries are challenged to ensure existing staff are used effectively. And if some staff are to be retired early, the separation costs and pension plan implications will have to be monitored closely.

C. Economic Development

33. In recent years economic growth has revived along with donor support and greater freedom of movement, but the PA has actively nurtured this growth in a number of ways. The PA has exercised sound economic management by formulating realistic budgets and managing aggregate spending to stay within the macroeconomic plan. The improvement in security, noted above, has demonstratively bolstered the confidence of the private sector. The PA has also worked to develop and put in place regulations and mechanisms to promote private sector growth. In addition, the Palestinian Monetary Authority has instituted a solid regime of supervision and regulation of the financial sector. Moreover, the PA has designed and begun implementing comprehensive plans in infrastructure, including regulatory and legal structures. Real GDP growth reached 5.4 percent in 2007, 6.8 percent in 2009 and 9 percent in 2010, with GDP per capita recovering to 1999 levels. Poverty rates have fallen by 4 percent to 22 percent from 2004 to 2009.

34. The PA has exercised sound economic management by maintaining a tight fiscal stance, controlling the wage bill and reducing dependence on donor financing. Over the last few years the recurrent budget deficit has been reduced from 21 to 15 percent of GDP and is programmed to drop to 4 percent of GDP in the 2011 to 2013 NDP, a goal that was judged by the IMF to be ambitious but achievable given the PA’s ability to conduct sound economic policies and its strong track record in implementing the equally challenging PRDP 2008-2010. At the same time, structural reforms implemented by the PA have worked to keep the wage bill in check and improve revenue collection. Further, net lending to localities has also been reduced through improvements in energy bill collections and support to raising local government revenues. Finally, the PA has instituted steady reforms in PFM

systems, applying rigorous budget preparation and execution practices, and establishing fiscal transparency and accountability in line with international standards. The IMF also notes the major improvements in the quality, transparency and timeliness of economic and financial statistics, meeting Special Data Dissemination Standards and comparing favorably with other countries maintaining high data management and dissemination standards, an assessment that the World Bank shares.¹⁰ However, the results of these reforms could be put at risk by GOI decisions such as the recent (temporary) withholding of customs clearance revenues belonging to WB&G.

Investment climate

35. The improvement of the investment climate in West Bank and Gaza has been heavily restricted by the closures imposed by the Israeli government on both the West Bank and Gaza. These restrict the movement of goods and people both within and across borders, thereby increasing labor and transportation costs and strongly discouraging private and foreign direct investment. This has created a fragmented private sector which is driven by low cost, labor intensive products such as garments, furniture and shoes for the heavily protected domestic and Israeli markets. In the past 40 years, Palestinian firms have had to adapt themselves to the environment imposed on them by the government of Israel. Therefore the Palestinian private sector remains dominated by small, family owned businesses that serve their local community, town, or city. Despite the negative impact of closures on private economic activity, unemployment fell from 18 to 17 percent in the West Bank over the last year and from 39 to 37 percent in the more heavily restricted Gaza.¹¹ However, underemployment and youth unemployment remains high even though labor force participation rates are low.

36. The investment climate in WB&G benefits from low corruption, low taxes and good investor protection mechanisms. According to the Global Corruption Barometer 2010¹² 59% of those surveyed in WB&G say corruption has declined in the last 3 years, and only 22% say it increased. This compares to Lebanon, where only 6% say it declined, and 82% say it increased. Thus while many countries in the region suffer from high corruption, it does not seem to be a significant problem in doing business in the West Bank and Gaza. “The PA and private sector associations backing anti-corruption reforms should be given due credit, particularly in light of the fact that many governments far more sophisticated than the PA continue to struggle to develop effective governance arrangements vis-à-vis the relationship between the public and private sector.”¹³ In fact, the 2011 Doing Business report ranked WB&G ahead of its neighbors Jordan, Egypt, Lebanon and Syria in 4 out of its 9 core indicators (figure 1), including taxes and investor protection. In contrast, its rankings in starting and closing a business were near the bottom. As the Doing Business report makes clear, the PA has made good progress, but there is much left to do.

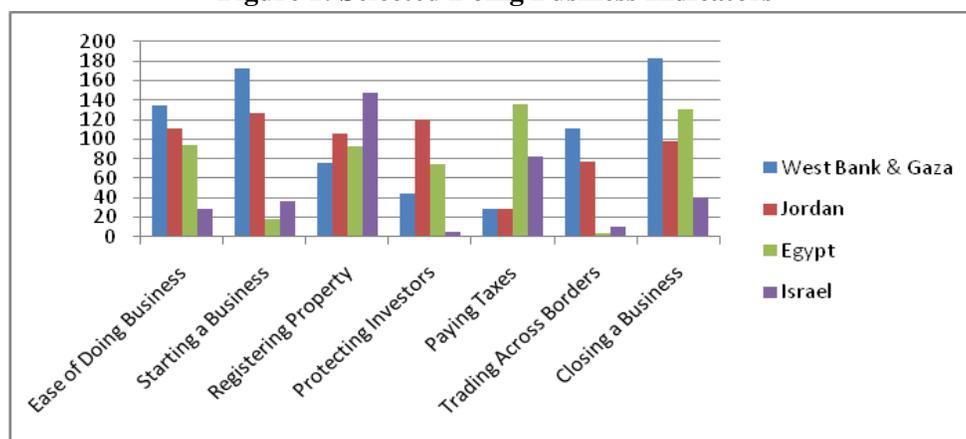
¹⁰ IMF, “Macroeconomic and Fiscal Framework for the West Bank and Gaza: Seventh Review of Progress,” April 2011.

¹¹ The impact of closures on employment and wages are examined in, “Mobility Restrictions and Labor Market Dynamics in Conflict Affected West Bank and Gaza,” World Bank, 2011.

¹² see on-line tables at http://www.transparency.org/policy_research/surveys_indices/gcb/2010/results

¹³ “West Bank and Gaza: Improving Governance and Reducing Corruption,” World Bank, 2011

Figure 1: Selected Doing Business Indicators



Source: “Forward-looking Priorities for Investment Climate Reform in the West Bank & Gaza”, 2011

37. Most recently, authorities have been issuing as well as amending laws in order to improve the regulatory framework of the private sector. The laws below, assuming final approval, will facilitate the Palestinian private sector in the transition to the manufacture of higher value goods as well as in search for potential new markets:

- **Investment Law:** An amendment to the original 1998 law was signed into law in January 2011 by Presidential decree. The new law is viewed favorably by the private sector and is meant to provide incentives for both smaller businesses and the service sector in particular. This law has raised the tax break minimum from \$100,000 to \$250,000 in new investment, but also created new tax breaks for investments that are lower than \$250,000 but higher than \$100,000. This law also allows Cabinet to create new incentives for projects that will provide high job creation or export potential without having to change the law itself. Thereby, granting the government with an additional tool in providing investment incentives.
- **Companies Law:** This law is still in draft form and would remove minimum capital requirements, as well as permit sole proprietorship under certain limited conditions, and limit the role of the government.
- **Competition Law:** This law, still in draft, would establish an independent agency to regulate competitive behavior¹⁴.

38. While Palestinian firms are facing many constraints due to restrictions that are imposed, the PA is working to facilitate a sound regulatory framework for firms to face these challenges.

¹⁴ World Bank, “Forward-looking Priorities for Investment Climate Reform in the West Bank & Gaza”, 2011

Banking and finance

39. The Palestinian Monetary Authority (PMA) was established in 1994 by presidential decree, and the Legislative Council PMA law Number (2) in 1997 outlined the full authority and autonomy of the PMA. Despite not being able to regulate monetary policy, as it cannot create a currency, it has quickly developed the capacity needed to become a central bank. As the IMF has documented, the PMA has developed in a just a dozen years into an institution providing rigorous supervision and regulation of the financial sector, consistent with international practice. It looks to become a full-fledged Central Bank and is building the institutional capacity in order to be ready for the new challenges that a more prominent role in monetary policy would bring. Strengthening of regulatory framework as well as supervision are top priorities for the PMA where it has improved the supervision and operational climate of the banking sector in both West Bank and Gaza. This was further consolidated by the Strategic Transformation Plan which was developed by the PMA in 2006 in order to fulfill its mandate of ensuring “the soundness of banking operations, maintaining monetary stability and encouraging economic growth in Palestine, in accordance with the general policy of the National Authority”¹⁵. The PMA continues to institute regulation and supervision of the financial sector in WB&G. These regulations are applied to all Gaza and West Bank banks through regular on-site and off-site supervision of the banking sector. In 2010, a law ensuring the independence of the PMA was under review by the Cabinet and is pending Presidential approval.

40. The PMA has been able to operate in a difficult environment that uses multiple currencies, and authorities have been able to establish a financial sector that offers most services, such as banking, a securities market and insurance. The banking sector has 18 banks, seven of which are listed on the stock exchange. These banks are licensed and supervised by the PMA; ten of the banks are branches of foreign banks, with Jordanian Banks dominating the sector, and with no state owned banks. The 8 other banks are locally owned, two of which are Islamic Banks. The WB&G financial sector operates through 198 branches, with total assets that amounted to \$8 billion in 2010, and with deposits of over \$ 7 billion and loans of over \$2 billion. In contrast to most developing countries, the role of banks in financing the WB&G economy remains low; this is mostly due to the political instability as well as the depressed economic activity. The PMA can be credited with maintaining bank operations in Gaza intact as well as fully integrated with the West Bank. The banking sector is the only institution with such limited impact from the West Bank/Gaza separation. The PMA monitors the sector with a broad range of prudential instruments which have been working towards bringing in line with international standards. These tools include: (i) required reserves ratios, (ii) minimum capital requirements, (iii) minimum liquidity ratios, and (iv) limits on credit concentration and currency exposure.

41. In addition to these monitoring tools, the PMA has been monitoring banks’ compliance with a corporate governance code in line with Basel II standards since 2008. Most recently, in 2010, the PMA issued Basel II compliant regulations governing the disclosure of information by financial institutions. In addition to enacting regulations, the PMA has enforced Basel standards and procedures when liquidating two banks in 2010 (one insolvent bank and one OFAC-listed bank). In order to strengthen the banking sector’s capital base it has continued to pass measures to do so. The most recent in December 2010 which include: (i) an increase in the minimum capital requirement to \$50 million (from \$35 million); and (ii) new “counter-cyclical” reserve requirements according to which banks should add 15 percent of their net

¹⁵ World Bank, “Project Appraisal Document Palestinian liberation organization for the Capacity Building for Palestinian Economic and Regulatory Institutions Project”, May 27, 2010

(after tax) income to their Tier I capital as an additional “bad times” buffer. These measures strive to bring the banking sector in line with international standards.¹⁶

42. The PMA has made noticeable strides with many regulations concerning the financial sector and its ability to regulate its banks as well as credit worthiness as well as lending operations. Notwithstanding the difficult operational environment the PMA has been able to enact and enforce:

- The Anti-Money Laundering (AML) law has been in force in line with international standards since October 2007, with technical assistance from the IMF and USAID;
- The establishment of a modern credit scoring system which became operational in July 2010. This system is part of the online-based credit registry, further enhancing the quality of information on borrowers’ creditworthiness and facilitating bank’s lending to new customers. This has been the most successful initiative in MENA and has enabled the registry to be elevated as a regional benchmark;
- A significant decline (25%) of bounced checks in the first half of 2010 has been made possible by a check-tracking system made operational at the end of 2009¹⁷.

43. The PMA is also conscious of instating and implementing codes that meet international standards. They have based their code of good governance on the OECD’s 2004 Corporate Governance Principles. This code, which was recently enacted, outlines both requirements and sanctions for non-compliance for the guidelines that the PMA monitors and enforces. These guidelines includes good governance practices concerning composition, structure, and the role of board of directors; compliance, internal and external audit; disclosure and transparency; and risk management. In addition, the PMA’s monitoring of the banking sector as well as its openness with data has been impressive.

Infrastructure

44. In the infrastructure sector, the forward agenda is extensive, but the PA has made important progress.

45. The Palestinian Water Authority (PWA) is the central agency in the water sector in WB&G. The “Water Sector” includes water resource management (WRM) and water supply and sanitation (WSS) activities. In a context of overall inefficient institutional capacity and governance, PWA copes with ad-hoc strategy, planning, regulation and infrastructure program implementation agendas and with donor coordination challenges. A new chairman, in place since March 2008, has engaged PWA in a series of reform initiatives such as i) a critical review of projects and operations, *An Audit of the Operations and Projects in the Water Sector in Palestine: The Strategic Refocusing of Water Sector Infrastructure in Palestine*, Final Report, 18 November 2008., ii) an in-house governance clean-up, and iii) a campaign to negotiate a more equitable distribution of water resources. PWA has also initiated the spin-off of its West Bank Water Department, to create an autonomous bulk water utility. Two years into the changes, PWA initiatives are making moderate progress, and the agency has yet to fully recover from the initial loss of morale and capacity felt in its ranks as a result of the 2008 management shake-up. Nonetheless, PWA is impressively pushing ahead with a solid PWA-drafted *Action Plan for Reform* to define and implement an institutional and legislative reform program in the water sector. The action plan has been endorsed by the PA Cabinet of Ministers and there is considerable political pressure on the PWA to follow through.

¹⁶ IMF, “Macroeconomic and Fiscal Framework for the West Bank and Gaza: Seventh Review of Progress Staff Report for the Meeting of the Ad Hoc Liaison Committee”, April 13, 2011

¹⁷ IMF, “Macroeconomic and Fiscal Framework for the West Bank and Gaza: Sixth Review of Progress Staff Report for the Meeting of the Ad Hoc Liaison Committee”, September 21, 2010

46. Looking at the institutional framework for the water sector in WB&G from a comparative perspective, it fares well in comparison with other developing countries. The fact that water is the critical, limiting resource in the area has played an important role in establishing relatively strong (though still fundamentally weak) institutional arrangements for the water sector. Other countries with more extensive institutional structures, such as Indonesia, show much less cohesion and policy consistency in the water sector than there is in WB&G.

47. In energy, the PA has implemented much of its medium-term power development strategy set out in the 1997 policy statement through the Palestine Energy Authority (PEA)¹⁸ and embarked on policies to reduce net lending on electricity. It has created three electricity distribution companies: the Northern Electric Distribution Company (NEDCO) that was established in the northern region of the West Bank on January 14, 2008, and started operating the electricity services in Nablus and Jenin in 2010; and the Hebron Electric Power Company (HEPCO) and Southern Electric Power Company (SELCO) that were created around 2003-2004 in the southern region of the West Bank.

48. NEDCO and SELCO are taking over the electricity operating assets and staff of the municipalities and village councils in their areas. This process has been slow and would take another two more years to complete. These utilities and HEPCO join the long-established utility serving the central area around Jerusalem - the Jerusalem District Electricity Company (JDECO). The Gaza Electricity Distribution Company (GEDCO) is responsible for electricity transmission and distribution in Gaza.

49. In addition, the Electricity Law was approved and enacted in May 2009, and in February 2010 the President approved the establishment of the Palestinian Electricity Regulatory Commission (PERC) which has since made significant progress in its operations. It has issued licensing to two of the electricity utilities, and completed a tariff methodology (cost-based methodology) for a unified tariff structure -- recently issued -- for the electricity utilities.

D. Service Delivery

50. WB&G has been called a “stellar” performer with regards to various achievements it has made in human development outcomes.¹⁹ WB&G’s progress to date can be seen across all human development sectors including health, education, social protection, pension reform, and local development. As a result of the challenging political circumstances, there has been some decline in the provision and quality of services in certain sectors. This has required the PA to provide additional support to these sectors which would, in the long-term, be unsustainable. However, as indicated in the NDP 2011-2013, the PA remains committed to addressing current challenges and further strengthening its achievements in human development, as indicated by human development outcomes, equity and access to services.

51. WB&G’s health indicators are strong relative to other World Health Organization (WHO)/Eastern Mediterranean Region (EMRO) countries. Mortality rates, including maternal mortality rates, are lower than other countries in the region, life expectancy is considered high for a country with the same income level, while high immunization rates and relatively strong childhood nutrition indicators also prevail.²⁰ Current education indicators are also favorable, reflecting the PA’s systemic emphasis on

¹⁸ “Palestine National Authority, the Palestine Energy Authority, the Power Sector, Letter of Sector Policy”, August 7, 1997.

¹⁹ World Bank, “Coping with Conflict? Poverty and Inclusion in the West Bank and Gaza,” June 2011, p. xiii.

²⁰ World Bank (2011). Building the Palestinian State: Sustaining growth, institutions and service delivery. Economic Monitoring Report to the Ad Hoc Liaison Committee, April 13, 2011; Pederson, Randall & Khawaja (eds). Growing fast: The Palestinian population in the West Bank and Gaza Strip.

human capital development as essential to future economic growth. Indeed, the development of the education system has been considered comparable to that found in middle-income countries. The enrollment rate has been high overall in the last several years (on average approximately 90%) with notable growth in student numbers since 1994.²¹ The secondary gross enrollment rate is also high – being approximately 20 percentage points higher than the rate found in average middle-income countries and 15 percentage points higher than that found in other countries in the Middle East and North Africa (MENA) Region. School attendance rates are also high. WB&G also has one of the highest literacy rate of any country in the MENA region (and the highest female literacy rate (over 90%) while very low repetition rates are also observed.²²

52. The PA has demonstrated its commitment and capacity to assist the poorest and most vulnerable while achieving economic growth and human development gains. The PA with the support of donors and other organizations has provided assistance to a large number of poor and vulnerable households. As part of the cash transfer program (CTP), currently more than 63,000 households receive cash benefits on a quarterly basis. This number is expected to increase significantly while thousands of others are receiving food aid and other kinds of assistance. The PA also provides needed health insurance and other types of support to thousands, including targeted assistance to various vulnerable groups. In order to ensure the population's well-being secured in the future, major reforms of the existing pension scheme have been agreed and set in motion to address key issues which jeopardize the program's sustainability (overly generous pensions, high level of fragmentation). Further, to strengthen local government capacity, community participation and government responsiveness, the PA has focused on and achieved significant progress in the area of local development.

Health

53. The PA has been highly engaged to ensure services are accessible and of high quality, and to promote the equitable distribution of human development gains. Today, within the health sector a wide range of services are provided, and there has been a positive trend in terms of public's level of satisfaction with health services.²³ Though access to health services appears to be equitable, the closure and political situation has negatively impacted health in a number of ways – and in some places more than others. The closures have contributed to an increase in the prevalence of specific health issues (e.g. mental health disorders), while also exacerbating basic health needs.²⁴ Together, these have contributed to an overall increase in the demand for health services. Yet these issues -- the limited supply of material and human resources in WB&G and movement restrictions -- have reduced access to services for many and the level and quality of services for those in need, particularly during periods of conflict.

²¹ World Bank, "Coping with Conflict? Poverty and Inclusion in the West Bank and Gaza," June 2011; World Bank, *Building the Palestinian State: Sustaining growth, institutions and service delivery*. Economic Monitoring Report to the Ad Hoc Liaison Committee. April 13, 2011.

²² World Bank (2006). *Impressive achievements under harsh conditions and the way forward to consolidate a quality education system*. West Bank and Gaza: Education Sector Analysis.

²³ Tiltnes et al. (2011). *Palestinian Opinions about Public Services: Synthesis of Results of Fafo's Opinion Polls in the West Bank and Gaza Strip, 2005-2011*. Fafo Paper 2011:08. Fafo Institute for Applied International Studies.

²⁴ Espie et al. (2009). *Trauma-related psychological disorders among Palestinian children and adults in Gaza and West Bank, 2005-2008*. *International Journal of Mental Health Systems*, 3(21),

WHO (2008). *Health conditions in the Occupied Palestinian territory, including east Jerusalem, and in the occupied Syrian Golan*. A61/18 Rev. 1.

Giacaman et al. (2009). *Health status and health services in the occupied Palestinian territory*. *Lancet*, 373, 837-849.

54. In the face of such challenges, the PA has worked to provide equitable services in primary, secondary and tertiary care. To cope with current demands, as well as the epidemiological transition whereby the burden of disease shifts from primarily infectious diseases to non-communicable and/or chronic diseases expected in countries experiencing economic growth and transition, the PA is focused on strengthening capacity to meet current and future population health needs. Specifically, the PA is in the process of undertaking a construction and maintenance plan for all levels of health care infrastructure and has committed to continuing investment in preventive health care measures including immunizations, screening efforts and public education campaigns, promoting human resource development and specializations (particularly in tertiary care); encouraging increased private sector participation in the health sector to secure the quality and sustainability of services; and continuing outreach of basic services to all population groups, particularly among the most vulnerable.

Education

55. In education, achievements have remained steady at high levels, with 30% of young adults enrolled in higher education (more than half of whom are women). This figure is high in comparison to middle-income countries. The PA's efforts to promote equitable access to education and to improve education quality throughout WB&G are highly visible on the ground. Since 1998, it has put in place a national curriculum, accompanied by editing and distributing of textbooks and in-service teacher training; achieved high enrollment rates and diversified education options (e.g., increasing number of areas that can be studied, further developing technical and vocational education); and has focused on quality and outreach including promoting early childhood care and education. Efforts to strengthen the education sector have also been observed at the community level, where, for example, additional teacher training has been provided. In addition to an increasing level of private sector investment in education, the PA, through the Ministry of Education and Higher Education (MOEHE), has also provided US\$23 million as loans and grants to needy students and has invested significantly in quality improvement to promote and secure development of skills relevant to labor market needs among Palestinian students. To date, US\$11 million has supported the first round of the Quality Improvement Fund (QIF) which focused on initiatives to further strengthen the quality, relevance and international competitiveness of tertiary institutions.

56. To further promote human capital investment through the education sector, and in the context of the Teacher Education Strategy and the MOEHE Five Year Development and Strategic Plan, the PA has emphasized the importance of pre-service, in-service and general teacher training and of improvements in the quality and relevance of education. These issues have also been at the forefront of various projects including the tertiary education project (TEP) and the Teacher Education Improvement Project (TEIP)). To strengthen administrative capacity within the education system, nearly 5,000 individuals from the administration were provided with training in several areas including leadership, planning and computer skills. The PA continues its commitment to modernize the approach and type of education, improve standards, and encourage increased enrolment in specific areas. To ensure these changes, particularly those in tertiary education, are institutionalized throughout WB&G, a higher education council and a quality assurance commission have been established and are fully functional. Still, education quality requires continued attention.

57. Despite the restrictions which negatively impact school attendance rates and children's access to schools, the PA has made notable progress in education. It has articulated a long-term vision of education sector development and aims to restore WB&G as a center for excellence in higher education and academic research. The population has indicated a high level of satisfaction with the education system and the services it provides. The comprehensive strategy for the education system is characterized by significant coordination and is articulated in the recently issued Education Sector Strategy 2011-2013. The PA continues to facilitate the capacity of tertiary education institutions to access financing from private sector and overseas while aiming to strengthen local capacity and gain visibility by establishing a

national fund for scientific research, supporting tertiary education institutions in building international networks, and by continuing to provide student lending to those with limited financial means.

Social protection

58. To protect the more vulnerable households, social protection support mechanisms are increasingly sophisticated, well-targeted and far-reaching. In fact, it has been noted that the PA is currently poised to have one of the most advanced cash assistance mechanisms which can be easily scaled up in crisis situations to help extremely poor and vulnerable households. The recent merger of the EU-funded and Bank-funded cash assistance mechanisms into a unified Cash Transfer Program (CTP) became a reality in June 2010 when almost 63,000 households in WB&G were provided cash assistance applying the same benefit level and using the same payment modality. The Ministry of Social Affairs (MOSA), responsible for the CTP, in the past several years has strengthened its capacity to manage and implement this large and complex cash transfer program using proxy means test-based targeting. By demonstrating its ability to manage and implement this program using a poverty-targeting database, collaboration with other partners has increased as they increase their reliance on this database and mechanism. It has placed MOSA at the forefront of critical reforms in the area of social protection. The PA is now aiming, in the context of the CTP, to reach out to all poor households and increase the number of CTP beneficiaries to approximately 95,000 in the coming months. Apart from the CTP, the PA also provides assistance to various other groups including assistance to families of prisoners, wounded individuals, orphans and foster children, and victims of domestic and community violence. The PA has also acknowledged diversity of need by providing, often in cooperation with others, various types of support (monetary/insurance, economic empowerment through income generation activities, and psychosocial assistance). In its recently issued paper on the Social Protection Sector Strategy, the PA further articulated its long-term commitment to this sector by strengthening the CTP mechanism and in the MOSA Business Strategy Paper the importance of honing its capacity to assist some of the most vulnerable, including persons with disabilities and the elderly was underscored.

59. Pension reform is another area with an extensive agenda and significant challenges. Currently, pension schemes exist for public sector and security force employees which is administered by MOF with some Palestinians contributing to Israeli social insurance programs. Additionally, employees of some large companies and international organizations are covered by company social schemes. There are, however, no mandatory insurance programs and the existing pension scheme is in the process of being reformed to address high levels of fragmentation and overly generous pensions which threaten its sustainability. In 2005, the Unified Pension Law was enacted which set the stage for major pension reform to ensure that the pension system would be financially viable and sustainable in the longer-term. The Pension Reform Action Plan was approved last year by the Cabinet to reduce pension liabilities and establish a unified pensions scheme which is sustainable in the long term. The PA has committed itself to achieving a number of milestones by end 2011 including extensive reform of existing pension law.

Local development

60. WB&G has made significant progress in strengthening local development with capacity-building efforts targeted towards the local level. The PA's program of community-based projects has made major contribution to upgrading of services in previously neglected areas. While municipalities are supposed to be key providers in meeting basic needs through the 27 functions they are legally required to provide, serious deficits remain. With assistance from the PA, municipalities are taking steps to improve their internal management. Several, with the help of community participation, are undertaking Strategic Development and Investment Plans to help identify priorities and align their investments with them. Municipalities have also undertaken several steps to improve their public financial management. These improvements have allowed municipalities to more easily disclose their financial data. An estimated 56 percent publicly disclose their financial data and budgets, and 60 percent disclosed their performance

ranks (in accordance with the MDLF ranking system). Finally, municipalities are increasing the focus on their citizens as customers. Through establishing citizen services centres, municipalities are trying to serve their citizens using a private-sector approach, treating citizens as customers who should receive efficient and transparent services.

61. The establishment of the MDLF has proved to be an effective mechanism for financing local development. One of the greatest initiatives supported through the MDLF has been the development of an Integrated Financial Management System to ensure standardization of management, accounting and operating procedures across WB&G municipalities when it is completed. This has been complemented by development of unified procedures for policy and physical planning as well as the amalgamation of various local government units, to increase the visibility and accountability of local government and encourage community participation and input. This important task will promote community development and participation in the long-term in WB&G. These mark some of the most significant achievements in WB&G in the last several years.

62. A diversity of actors including donors and NGOs have been assisting and supporting the PA.²⁵ Even so, various institutions within the public human development sector have furthered their capacity to manage services more effectively and to meet basic needs of the population, even during the worst points of crisis across WB&G. Despite continued closures, violence, and political uncertainty, the PA has demonstrated its capacity and commitment to continue to providing relevant and needed services to a large portion of the population.

63. The PA's report entitled *Homestretch to Freedom: The Second Year of the 13th Government Program* (August 2010) described achievement in the first year of its program, including reforms of the CTP, and highlighted remaining challenges for the second year. The PA asserts that it "will continue to work in all sectors, to improve institutional performance, public service delivery, quality of life, and economic prosperity." In addition to ensuring access to services and their quality, as well as significant reforms of the social safety net, the PA has indicated its commitment to increase the level of financing for these areas within the national budget. While it still faces significant difficulties as a result of continued closures and periodic violence, WB&G as a result of the PA's efforts on institutional capacity-building and ensuring the provision of basic services, has been able to maintain and even improve some human development indicators. Operating with high standards of accountability and transparency, these gains have been even further solidified through the development of, and emphasis on, relevant policy and legislation.

IV. INSTITUTIONAL EFFECTS OF CONTESTED SOVEREIGNTY

64. This paper has surveyed the record of the caretaker government on building institutions in WB&G, examining the domains of public institutions where government effectiveness matters most, according to international norms. The record demonstrates that WB&G institutions are reasonably effective, both by any absolute standard one might have, and especially in comparison to other countries, in the region or elsewhere. While the PA faces a number of challenges in improving its administration of certain domains, WB&G institutions have improved rapidly in a short period of time. One factor that imposes a negative influence in every sector is the closures and restrictions imposed as instruments of the contested sovereignty that prevails in WB&G. The World Bank, in its recent World Development Report

²⁵ The role of NGOs and Civil Society Organizations in service delivery as well as in providing voice for civil society will be examined in an upcoming Bank study.

on conflict,²⁶ documents the high economic and social costs of contested sovereignty on grounds that it suppresses development.

65. This survey has demonstrated a number of ways that contested sovereignty suppresses institutional and economic development in WB&G. The withholding of clearance revenues and lack of cooperation on customs by GOI undermines revenue mobilization and budget execution in WB&G. The blockade of all international borders inhibits the import of raw materials and the export of finished products. The restrictions controlling the internal and international movement of goods and people discourage foreign investment vital to economic growth and job creation. The lack of access to land and local natural water sources has devastated the agriculture sector. Restrictions on movements of materials and people hinder the supply and distribution of health and education services, as well as the access of workers to their jobs. Thus the impressive achievements of WB&G institutions, comparatively with countries in the Middle East and other regions, come at the high cost of overcoming restrictions imposed in the context of conflict. Going forward, a continuation of these restrictions will further constrain the good functioning of WB&G's accomplished institutions.

²⁶ "Conflict, Security and Development," World Bank, 2011