

## Action Fiche for West Bank and Gaza Strip

### 1. IDENTIFICATION

Title/Number	<b>PEGASE: Private Sector Reconstruction in Gaza (PSRG)</b>		
Total cost	€22 million		
Aid method / Method of implementation	Project approach – centralised		
DAC-code	32130 – SME development	Sector	Production sector

### 2. RATIONALE

#### 2.1. Sector context

Even before the Israeli military operation ("Cast Lead") in Gaza, the macroeconomic environment was very difficult. While Gaza experienced negative growth since the disengagement in June 2005, the living conditions since the 2006 military offensive and the Hamas takeover in June 2007 have further worsened due to continuous blockade, to relatively high inflation (10.3% in 2008) and resulting in rising unemployment reaching 41.9% and rising poverty 51.8% (official figures 2007). These data will certainly have worsened following Operation Cast Lead.

In 2005 Gaza had 3,900 industrial working establishments with 35,000 industrial employees. This had declined to 80 establishments with 860 employees in June 2008. In addition, the business associations estimated that another 70,000 workers have been laid off from other sectors. There are no reliable figures available for 2009, but given the effects of Operation Cast Lead and continued closures, living conditions have clearly worsened. In the aftermath of the war, preliminarily assessments indicated that more than 700 businesses in Gaza, of which 268 completely destroyed and 432 partially damaged, have suffered damage. Initial estimates suggested that the private sector suffered around USD 140 million in damages from Operation Cast Lead and not counting the losses due to the years of closure.

The industrial zone of Beit Hanoun in North of the Gaza Strip as well as other economic infrastructures across the Strip suffered massive damage during the 22 days of the Israeli military operation in Gaza. The damage to micro-enterprises, such as shops, workshops, agricultural smallholdings, etc. is very considerable. These enterprises play a vital role in immediately reducing Gazans' aid dependency and putting in place the very first steps towards the restoration of economic activity. Such enterprises are absolutely not in a position to take out loans in the form of micro-credits.

At the donors' conference at Sharm-El-Sheikh on 3 March 2009 which followed Operation Cast Lead, the European Commission proposed a range of new initiatives under the PEGASE mechanism and aimed at the recovery and reconstruction of Gaza. These initiatives responded to needs identified in the Palestinian Authority's Gaza Early Recovery Rapid Needs Assessment, to which the European Union

contributed actively. A subsequent EU "damage assessment and needs identifications in Gaza" report performed by EUNIDA further developed some of these initiatives.

The Palestinian Authority Gaza Early Recovery and Reconstruction Plan (GERRP), aims at enabling people in Gaza to emerge from aid dependency, and includes 7 important steps and a time horizon of several years:

- (1) Private Sector Reconstruction in Gaza (PSRG) (object of the project under consideration for EU funding)
- (2) Private sector revitalisation programme
- (3) Construction of Gaza local industrial estate
- (4) Support to businesses by providing guarantee systems to banking and micro finance institutions
- (5) Technical Assistance to private sector enterprises
- (6) Private sector job support and job creation
- (7) Enhancement of institutional capacity of private sector representing bodies

The EUNIDA assessment provided further elaboration of the main component of phase I of the more comprehensive plan, i.e. Private Sector Reconstruction in Gaza. (PSRG). With this initial contribution of €22 million from the European Union, the PSRG programme aims at stimulating economic activity in the Gaza Strip by enabling businesses affected by the Operation Cast Lead to resume economic activity, as well as by supporting businesses that were not directly damaged in the conflict but have suffered due to the prolonged closure and the deterioration of the overall situation in Gaza.

## **2.2. Lessons learnt**

The delivery mechanism for this programme will closely mirror the successful experience of the Temporary International Mechanism (TIM) (2006-2008) and PEGASE Direct Financial Support operations launched in February 2008, in particular the system used for paying arrears to the private sector. Activities will be carried out in full coordination with the relevant Palestinian stakeholders, in particular the Prime Minister's Office, the Ministry of Finance (MoF), Ministry of National Economy (MNE) and the Palestinian banks.

The main conclusion of the independent evaluation of TIM stated that the programme has been an innovative instrument capable in a very difficult and complicated environment to quickly mobilise resources and to target them efficiently to the most needy. The proposed Private Sector Reconstruction in Gaza (PSRG) programme will build on this.

In particular, TIM and the PEGASE mechanism have proved very successful means of operating in the highly problematic environment of the Gaza Strip and it is therefore both logical and important to assimilate as much as possible of this experience into the design of this new intervention.

## **2.3. Complementary actions**

This action is complementary to other projects of the European Union supporting the Palestinian Private Sector. Through PEGASE, the European Union has contributed €14 million to the EPCGF (European-Palestinian Credit Guarantee Fund), which guarantees loans to small and medium-sized enterprises (SMEs) through the

Palestinian banking system. The EPCGF is co-financed by the European Union and Kreditanstalt für Wiederaufbau (KfW). The EPCGF has signed partnership agreements with 6 partner banks and is expected to sign in the second semester 2009 a new partnership agreement with Bank of Palestine, which is the Bank with the highest number of branches in Palestine (including in Gaza). The current action aims at restoring private sector enterprises to a position that allows them to benefit from the EPCGF programme in the future.

The European Union supports the private sector institutional framework and the business environment through a number of interventions and is preparing several projects in these fields: reinforcement of the Palestinian Quality Framework, of the private and public sector capacities on trade in services, and of the Ministry of National Economy capacities to formulate PRDP programs. A project aiming at preparing Palestinian accession to observatory status to the World Trade Organisation (WTO) is also in preparation.

More broadly, PEGASE Direct Financial Support Operations provide a vital source of sustenance to the Gaza economy, through the provision of electricity, the part-payment of civil servants' and pensioners' salaries and pensions, and the provision of regular social allowances to the most vulnerable population.

In Gaza, the Palestinian Authority's Gaza Early Recovery and Reconstruction Plan (GERRP), provides a comprehensive strategy for economic, social and physical reconstruction, of which this action forms part. The European Union will contribute to other aspects of the GERRP, in particular if conditions permit, investment in infrastructure under a different action. And if access to the Gaza Strip improves in the remainder of this year, further contributions to the implementation of the GERRP would be envisaged in 2010.

In addition, a significant allocation of funds from the Instrument for Stability (IfS) was made in the immediate aftermath of the January military action in Gaza. Two contracts have now been signed: IFS-RRM/2009/215272 for €446,683 to deploy five explosives ordnance disposal (EOD) teams to support early recovery operations in Gaza, from the UN Mine Action Service (UNMAS); and IFS-RRM/2009/215028 for €13 million for a project entitled "UNRWA Emergency Job Creation Programme in the Gaza Strip – 2009". These contribute both to demining, and to immediate poverty alleviation through the placing of over 17,500 direct beneficiaries for 3-6 months, mostly unskilled workers, for temporary employment in damaged private business, local utilities, and in supporting delivery of UNRWA operations. This action will build on the immediate emergency contribution from the IfS.

Lastly, the European Union funds both the General Fund and project activities of UNRWA, addressing the needs of the refugee population which accounts for 80% of Gaza population. Other agencies like World Food Programme (WFP) and UNICEF have reinforced their programmes in the area and are being funded by the Commission's Directorate General for Humanitarian Aid and Civil Protection (ECHO).

#### **2.4. Donor coordination**

High level international donor coordination takes place at the level of the Ad Hoc Liaison Committee (AHLIC) which last met in Oslo on 8 June 2009. At the local level donor coordination takes place in various forums under the Local Development Forum (LDF) and its four "Strategy Groups" (governance, economy, social and

humanitarian affairs, infrastructure), each co-chaired by a different lead donor and PA Ministry. Beneath these a number of sector working groups (SWG) have been established, which are more operational forums for coordination and alignment of donor activities for the active stakeholders in each sector. More specifically, enhanced and targeted technical assistance will be coordinated with other donors through the Governance Strategy Group's Judiciary Sector Working Group, Elections Sector Working Group, and Public Administration and Civil Service Sector Working Group as well as the Fiscal Sector Working Group (which reports both to the Governance and Economic Strategy Groups) and the Health Sector Working Group (reporting to the Social Strategy Group).

The European Union, as previously mentioned, as well as individual EU Member States play a leading role in these forums. In addition EU policy is coordinated through regular meetings of the EU Heads of Cooperation.

### **3. DESCRIPTION**

#### **3.1. Objectives**

The overall objective of this programme involving an EU contribution of €22 million is to provide immediate support to the private sector and thus take the first steps towards ensuring sustainable livelihoods in the Gaza Strip. The specific objective of this programme is to provide financial support to businesses affected by Operation Cast Lead in order that they may resume economic activity, as well as to businesses that were not directly damaged during Operation Cast Lead but have incurred economic losses due to the prolonged closure and the deterioration of the overall situation in Gaza. This programme will directly contribute towards sustaining and providing new employment and will help in ensuring a source of income for currently unemployed and vulnerable workers. Damaged factories will be more able to satisfy their primary needs and to cover the operational cost for guarding their assets.

#### **3.2. Expected results and main activities**

The main expected result of this programme is that businesses benefiting from the programme are able to resume and sustain their economic activities through reconstruction and replacement of damaged capital equipment, through repair of damaged buildings and equipment and/or through support to the businesses' operational needs. The Palestinian Authority has commissioned a comprehensive database of applicants for financial support (hereinafter referred to as the "2009 PA Database"). These applications have now been assessed or are in the process of being assessed in the field, and the technical eligibility of individual claims is being established. For technically eligible applications, the database pinpoints the eligibility of specific expenses according to stringent and rigorously applied criteria. The individual files, once technical work is complete, are screened by the Palestinian Authority for a decision on possible financial support.

The "2009 PA Database" comprises claims for financial support from businesses affected by Operation Cast Lead. Other databases will be developed to include claims for financial support from businesses that were not directly damaged during this Operation but have incurred economic losses due to the prolonged closure and to the deterioration of the overall situation in Gaza.

Moreover, in order to be eligible for financial support from the PEGASE programme, the Commission will determine its own, specific eligibility criteria. The Commission will:

- Verify, by an audit in the field, the quality of the PA's database and the correct application of the PA's technical eligibility criteria;
- Verify *ex-ante* and certify all applications submitted by the PA to the Commission and considered for support through the PEGASE programme;
- Authorise the payments of financial support of eligible applications subject to the specific agreed eligibility criteria of the PEGASE programme and to *ex-ante* systematic verifications;
- Perform *ex-post* audits of payments made, as well as intermediary verifications of the use of payments when claims are settled in tranches.

### **3.3. Risks and assumptions**

The above-mentioned operations are based on the full cooperation with the Palestinian Authority, in particular for the identification of beneficiaries, of eligible expenditure and timing of payments.

All actions under this special measure might be hampered by any additional restrictions imposed by the Israeli Government, for example, on the delivery of goods into the Gaza Strip or on financial transactions.

On the other hand, if the Agreement on Movement and Access is gradually implemented following negotiations post-Annapolis, this PEGASE specific programme could be a powerful instrument at the disposal of the PA, EU and other governments and the European Commission, to mobilise resources thereby contributing to the successful recovery of the Gaza economy and the construction of a Palestinian State based on peace and prosperity.

### **3.4. Crosscutting Issues**

Good governance principles are applied in the implementation mechanisms, in particular through the ownership of the programme by the PA. The specific attention given to control and audit helps to promote high standards of public financial management in the PA more generally. The clearance of rubble alongside any reconstruction will contribute to alleviate the environmental and health problems of Gaza.

### **3.5. Stakeholders**

The direct beneficiaries of this programme are businesses affected by Operation Cast Lead in order that they may resume economic activity, as well as businesses that were not directly damaged during this Operation but have incurred economic losses due to the prolonged closure and the deterioration of the overall situation in the Gaza Strip.

In addition the Gaza population will benefit from the private sector revitalisation in terms of employment opportunities and in terms of availability of services, food and non food products and other items alleviating the dependency on donations and humanitarian aid.

Eligible beneficiaries and expenses will be 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. Specific ex-ante audits will be performed for each request selected to benefit from PEGASE financing.

This PEGASE programme will be implemented in close cooperation and full partnership with the Prime Minister's Office, the Ministry of Finance, the Ministry of National Economy and the technical Ministries and other Departments and Agencies of the PA.

This PEGASE programme will be coordinated locally with the EU Member States, the EU Delegation, other international donors and International Organisations. In order to do so, full use will be made of the existing local coordination groups already in place in liaison with the PA administration and the Office of the Quartet Special Representative like the Local Development Forum, the AHLC structures, the coordination meeting between Member States and the EU Delegation etc.

#### **4. IMPLEMENTATION ISSUES**

##### **4.1. Method of implementation**

Direct centralised management will be applied for this programme. A Financing Agreement following the standard models in force will be signed with the Ministry of Finance of the Palestinian Authority. A database has been established ("2009 PA Database") and others will be established taking into account detailed eligibility criteria. As a first step, the Commission needs to ensure the quality and soundness of the database(s) with regard to the structure and methodology applied in setting it(them) up. Following the verification (and any necessary corrections) of the database(s), the Commission will proceed to deal with individual cases. This entails a check of eligibility criteria which will vary depending on the category of beneficiary:

Window 1: Claimants included in the 2009 PA Database. For those operating with business registration:

- registration by the legal entity allowing it to operate in accordance with the PA requirements;
- date of business registration prior to 26<sup>th</sup> December 2008;
- not appearing on international and ad hoc sanction lists.

For those claimants included in the 2009 PA Database that operated without business registration but existed prior to 26<sup>th</sup> December 2008:

- existence prior to 26<sup>th</sup> December 2008;
- not appearing on international and ad hoc sanction lists.

Window 2: Businesses not included in the 2009 PA Database:

- registration by the legal entity allowing it to operate in accordance with the PA requirements;
- not appearing on international and ad hoc sanction lists;
- any other criteria or condition that is established by the specific regulatory framework for eligibility for this Window.

After the Commission has identified its eligible beneficiaries and their corresponding entitlement, a transfer of funds will be made to the Central Treasury Account of the PA Ministry of Finance specifically opened for this programme. The MoF will then

transfer the payment entitlements to the eligible beneficiaries on receipt of an ex-ante authorisation letter from the Commission, prepared after case-by-case verification

All payments executed by the MoF to the eligible beneficiaries are subject to an ex-post audit to verify that the funds are disbursed with full transparency and accountability to the eligible beneficiaries. In the event that a beneficiary is found not to have complied in full with the requirements, (e.g. effectively re-starting the business) recovery will be obtained from the PA.

#### **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.

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 grant direct award may be used in accordance with applicable provisions.

#### **4.3. Indicative budget and calendar**

The maximum indicative contribution to the beneficiaries of this programme is €22 million.

The duration of this programme is estimated at 60 months after signature of the Financing Agreement, including an operational phase of 48 months and a closure phase of 12 months.

Funds for the necessary technical assistance, evaluation, audit and visibility actions should be made available under this decision.

Project Activities €21 million

Audit, Evaluation, Visibility and TA €1 million

#### **4.4. Performance monitoring**

PEGASE will implement comprehensive monitoring, verification control and audit (including ex-ante verifications) systems to provide assurance over the use of EU 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 (IMF) on budget execution as well as other relevant political developments.

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

For all types of project and programmes financed, taking into account the characteristics of the sector of activity concerned, the geographical location, the

payment system used and donors' requests, specific adapted ex-ante, real-time and ex-post monitoring control and audit procedures will be systematically put in place

#### **4.5. Evaluation and audit**

Financial experts and qualified auditors will work for PEGASE which will be complemented by the 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 ex-ante audits of eligible expenditures to identify and validate payments, the PEGASE team will organise a general ex-post 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.

A mid-term evaluation report of PEGASE will shortly begin and a comprehensive final evaluation report will be undertaken in accordance with the Commission Annual Management Plan.

#### **4.6. Communication and visibility**

The programme will follow the visibility guidelines of the Commission. It is intended to reinforce the Commission's efforts to gain recognition for its unprecedented efforts over the period 2006-2009 to highlight the evolution to PEGASE with the emphasis on moving from emergency to development assistance.

This will be done in close co-ordination with the EU Member States.

Progress of PEGASE implementation will be communicated regularly to all stakeholders, including through the weekly bulletin.