EUROPEAN
COMMISSION

Brussels, 14.7.2017
C(2017) 4856 final

COMMISSION IMPLEMENTING DECISION

of 14.7.2017

on modifying Decision C (2017) 1096 final on the Special Measure 2017 in favour of Palestine[1] to be financed from the general budget of the Union

[1] This designation shall not be construed as recognition of a State of Palestine and is without prejudice to individual positions of the Member States on this issue.

COMMISSION IMPLEMENTING DECISION

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on modifying Decision C (2017) 1096 final on the Special Measure 2017 in favour of Palestine[1] to be financed from the general budget of the Union

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 236/2014 of the European Parliament and of the Council of 11 March 2014 laying down common rules and procedures for the implementation of the Union's instruments for financing external action[2], and in particular Article 2 thereof,

Having regard to Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002[3], and in particular Article 84(2) thereof,

Whereas:

(1) Commission Decision C (2017) 1096 final adopted on 20 February 2017 approved the programme entitled "PEGASE Direct Financial Support to Recurrent Expenditures of the Palestinian Authority 2017. This Decision was financed under Regulation (EU) No 232/2014 of the European Parliament and of the Council of 11 March 2014 establishing a European Neighbourhood Instrument[4].

(2) The purpose of this modifying Decision is to authorise an additional EU contribution of EUR 20 million to Gaza under the Vulnerable Palestinian Families component of the PEGASE programme.

(3) The action provided for in this Decision is in accordance with the opinion of the European Neighbourhood Instrument (ENI) Committee set up by Article 15 of the financing instrument referred to in Recital 1.

HAS DECIDED AS FOLLOWS:

Article 1

Adoption of the measure

Annex 1 of Decision C (2017) 1096 final adopted on 20/02/2017 is replaced by the following:

Annex: PEGASE Direct Financial Support to Recurrent Expenditures of the Palestinian Authority 2017.

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1 This designation shall not be construed as recognition of a State of Palestine and is without prejudice to individual positions of the Member States on this issue.
2 OJ L 77, 15.3.2014, p. 95.
3 OJ L 298, 26.10.2012, p. 1.
4 OJ L 77, 15.3.2014, p. 27.

Article 2

Financial contribution

The maximum contribution of the European Union for the implementation of the PEGASE programme referred to in Article 1 is set at EUR 158,100 million and shall be financed from budget line 22 04 01 04 of the general budget of the Union for 2017.

The financial contribution provided for in the first paragraph may also cover interest due for late payment.

Done at Brussels, 14.7.2017

For the Commission
Johannes HAHN
Member of the Commission

This action is funded by the European Union

ANNEX 1

of the Commission Implementing Decision on modifying Decision C (2017) 1096 final adopted on 20/02/2017 on the Special Measure 2017 in favour of Palestine[1] to be financed from the general budget of the Union

Action Document for "PEGASE: Direct Financial Support to Recurrent Expenditures of the Palestinian Authority 2017"

1. Title/basic act/ CRIS number	"PEGASE: Direct Financial Support to Recurrent Expenditures of the Palestinian Authority 2017", CRIS number: ENI/2017/39376, financed under the European Neighbourhood Instrument	
2. Zone benefiting from the action/location	Palestine The action shall be carried out at the following location: Palestine	
3. Programming document	The next programming exercise for the period 2017-2020 is currently under preparation and is expected to be adopted in the second half of 2017. In the meantime, special measures are envisaged for 2017 to ensure continuity of support to the Palestinian Authority, thereby contributing to maintaining the viability of the two-state solution.	
4. Sector of concentration/ thematic area	PEGASE Direct Financial Support (PDFS) to the Palestinian Authority (PA)	DEV. Aid: YES[2]
5. Amounts concerned	Total estimated cost: **EUR 158,100,000** Total amount of European Union (EU) budget contribution: **EUR 158,100,000**	
6. Aid modality(ies) and implementation modality(ies)	Project Modality Direct management	
7 a) DAC code(s)	16010	

[1] This designation shall not be construed as recognition of a State of Palestine and is without prejudice to individual positions of the Member States on this issue.

[2] Official Development Aid is administered with the promotion of the economic development and welfare of developing countries as its main objective.

b) Main Delivery Channel	10000 - Public Sector Institutions 12000 - Recipient Government			
8. Markers (from CRIS DAC form)	**General policy objective**	**Not targeted**	**Significant objective**	**Main objective**
	Participation development/good governance	☐	☐	☒
	Aid to environment	☒	☐	☐
	Gender equality (including Women In Development)	☐	☒	☐
	Trade Development	☒	☐	☐
	Reproductive, Maternal, New born and child health	☒	☐	☐
	RIO Convention markers	**Not targeted**	**Significant objective**	**Main objective**
	Biological diversity	☒	☐	☐
	Combat desertification	☒	☐	☐
	Climate change mitigation	☒	☐	☐
	Climate change adaptation	☒	☐	☐
9. Global Public Goods and Challenges (GPGC) thematic flagships	N/A			
10. Sustainable development goals (SDGs)	Main SDG Goal: SDG 16, Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels. Secondary SDG Goals: SDG 1, End poverty in all its forms everywhere; SDG 3, Ensure healthy lives and promote well-being for all at all ages; SDG 4, Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all.			

SUMMARY

The overarching objective of the EU's support to Palestine is to contribute to maintaining the viability of the two-state solution. The multi-annual programming document for 2017-2020 is currently being prepared and is expected to be adopted in the second half of 2017. In the meantime, this special measure serves the purpose of ensuring continuity of the PEGASE[3] Direct Financial Support (DFS) to the Palestinian Authority, thereby sustaining the delivery of basic services to the entire Palestinian population.

Through PEGASE DFS, the EU has contributed substantially to the recurrent expenditure of the national budget (over EUR 2 billion since 2008), with systematic, predictable and unconditional

3 Mécanisme Palestino-Européen de Gestion de l'Aide Socio-Economique.

contributions to the payment of Palestinian Authority civil servants' salaries and pensions (PEGASE DFS "Civil Servants and Pensioners" (CSP) programme), of social allowances to the poorest and most vulnerable Palestinians families (PEGASE DFS "Vulnerable Palestinian Families" (VPF) programme), and, since 2013, of health referral bills through the PEGASE DFS "East Jerusalem hospitals" (EJH) programme. Through this programme, the EU provides crucial funding to avoid the collapse of those hospitals, which are amongst the few remaining Palestinian institutions in East Jerusalem and are providing key medical services to the Palestinian population. PEGASE DFS has contributed substantially to state building, as well as to the social cohesion, economic and security stabilisation of the Palestinian territories.

Coupled to PEGASE DFS, the EU has been supporting the Palestinian Authority to implement certain policy reforms aiming at enhancing its fiscal sustainability and improving the accountability, integrity, and transparency of its public finance system (public finance management, revenue mobilisation and fiscal reforms such as reduction of the net lending, health medical referrals), supporting its civil service reform, as well as improving service delivery (social protection).

In December 2013, the European Court of Auditors (ECA) published a report on PEGASE DFS[4] where it recognised that the European External Action Service and the Commission had succeeded in implementing direct financial support to the Palestinian Authority in difficult circumstances. The report also concluded that the control measures put in place are robust and that there is no sign of mismanagement or diversion of funds. It put forward a number of recommendations, most of which have already been addressed.

PEGASE DFS has undergone a shift towards a 'results-oriented approach' that aims to guide/formalise a more structured, coherent results-oriented policy dialogue, with stronger monitoring and evaluation of the Palestinian Authority's achievements in key areas, through a Results-Oriented Framework (ROF). Both the December 2013 ECA performance audit and the July 2014 external evaluation of the EU co-operation with Palestine confirmed the relevance and timeliness of this shift. The ROF was co-signed in March 2015 by the EU and the Palestinian Prime Minister and subsequently extended in June 2016 until the end of the year. It covers six sectors, falling within two pillars, aligned to EU PEGASE DFS specific objectives as set-up in the Single Support Framework (SSF) 2014-2016, namely Pillar I: Fiscal Consolidation and Policy Reforms covering (1) Macroeconomic Support; (2) Public Finance Management; and (3) Public Administration Reform; Pillar II: Service delivery covering (1) Education; (2) Health; and (3) Social protection.

The latest external evaluation in July 2016 reiterated that PEGASE DFS has contributed to build capacities of institutions critical to the underpinning of the two-state solution. It also found that the prospect of the programme's continuation, together with better targeted, reforms-oriented policy dialogue, is on the right track for pursuing that solution. Meanwhile, the EU and EU Member States steadily continue progressing towards an EU Joint Programming Approach to enhance programmes' consistency and avoid fragmentation. The Joint Strategy is currently being finalised and will be aligned on the national priorities, in particular as set in the upcoming National Policy Agenda, the overarching national document defining priorities, policies and interventions, which is expected to be completed by the end of 2016.

4 European Union Direct Financial Support to the PA - European Court of Auditors Special Report No 14 – 2013.

1 CONTEXT

1.1 Sector/Country/Regional context/Thematic area

Palestine has been marked by the disruption of nearly fifty years of Israeli occupation, during which the economic development path and the democratisation process have paralleled the political developments. After a period of sustained state-building progress and economic recovery between 2007 and 2011 (which was largely driven by government spending, in turn, funded by aid flows), the democratic path (no electoral process, limited institutional accountability) and the economy (slowing growth, high unemployment, large fiscal deficits) have significantly slowed down since 2012.

The general outlook has deteriorated over the last three years. During 2014, the Peace Process negotiations collapsed and the Gaza Strip suffered a major humanitarian crisis and massive destruction as a result of Israel's "Operation Protective Edge", while Israeli restrictions imposed on Palestinian people and their economy continued unabated. Starting at the end of 2015, violence and tension have alarmingly escalated in Jerusalem and the West Bank. More widespread violence is likely to return unless the root causes are addressed. A recent bilateral agreement regulating Palestinian debt payment to the Israel Electric Corporation signed in September 2016 does not seem destined to significantly alter the status quo.

The aforementioned conflict and humanitarian tragedy in Gaza has made an already struggling Palestinian economy worse and put further stress on the Palestinian Authority, both in terms of legitimacy and on its fiscal situation – the Palestinian Authority's total deficit amounted to EUR 1.1 billion for 2015. Due to the lack of reconciliation process between Hamas[5] - the *de facto* authority in Gaza – and Fatah, diminished funding from the Gulf countries and Israel's sporadic withholding of clearance revenues, the Palestinian Authority ongoing fiscal crisis and difficult governance have been further exacerbated. Difficulties of the Palestinian Authority in paying salaries and bills are recurrent, putting the institutional functioning and the delivery of basic services to the Palestinian population at risk. This is particularly exacerbated in the Gaza Strip where the process to create a "National Consensus Government" (NCG) is stalled and civil servants recruited after 2007 are receiving irregular, partial payments of salaries.

Despite revenues having become the main source to cover expenses, with coverage ratio for revenues growing from 50% in 2009 to 70% in 2015, the Palestinian Authority continues to accumulate considerable debts to the banking sector and arrears to the private sector. The Palestinian Authority debt as of 31 December 2015 amounted to 43% of Gross Domestic product (GDP). Arrears to private sector stood at over EUR 500 million, while arrears to the Pension Fund amounted to over EUR 2 billion. Domestic banks are highly exposed to the Palestinian Authority as their share of loans given is 42%. In this context, social services have been greatly affected. As a result of the Palestinian Authority's accumulated unpaid arrears, hospitals in East Jerusalem have recurrent difficulties in paying salaries and are highly indebted to medical suppliers.

The decreasing political prospects for a viable two-state solution and the lack of intra-Palestinian reconciliation progress further increases donors' fatigue, including on the side of Arab Gulf countries. For instance, Saudi Arabia has withheld a pledge of USD 20 million monthly support

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5 Following Hamas' victory in the Palestinian legislative elections in 2006, the West Bank has been governed by Mahmoud Abbas and Fatah and Gaza by Hamas, which is regarded as a terrorist group in many countries.

to the Palestinian Authority budget, and although approximately USD 5 billion was pledged at the Cairo Conference on 12 October 2014 (over two thirds of which to be dedicated for the reconstruction of Gaza), there has been significant lack of progress in the actual volume and speed of the contributions[6]. According to the Ad-Hoc Liaison Committee (AHLC), "the Palestinian Authority has made good progress in fiscal and budgetary matters, but the sharp decline in budget support by certain donors risks to put achieved fiscal consolidation into question and could lead to unforeseeable consequences". In the absence of successful peace negotiations, the Palestinian economy will continue to be unsustainable and excessively dependent on donor aid.

Poverty and unemployment levels remain of serious concern. A quarter of the Palestinian labour force is still unemployed. The latest available data from the Palestinian Central Bureau of Statistics (PCBS) indicate that, in 2011, poverty rates reached 18% in the West Bank and 39% in Gaza, with 70% of the population in Gaza being aid dependent. These figures have increased due to the 2014 hostilities in the Strip, which pushed many Gaza families into (deeper) poverty. According to the World Bank report to the AHLC of September 2016, poverty in Palestine reached 27% in 2016, with levels in Gaza at 42%.

1.1.1 Public Policy Assessment and EU Policy Framework

Taking stock of previous planning exercises, the Palestinian Authority has engaged in developing a new National Policy Agenda (NPA) covering national priorities, policies and interventions. The NPA is expected to be adopted towards the end of 2016 and will be valid for the period 2017-2022. Main national priorities will comprise the achievement of independence, government reform and sustainable development. The latter revolves around: 1) economic independence, 2) social justice and rule of law, 3) inclusive, quality education 4) health for all, and 5) resilient communities. Twenty one sectoral strategies are being reviewed and should also be finalised by the end of 2016. The NPA will be the basis for a European Joint Strategy for Palestine from 2017 onwards. Building on the current Results-Oriented Framework, efforts will be targeted towards further improving alignment, enhancing monitoring and evaluation, and continuing strengthening the policy dialogue.

The Palestinian Authority released its "National Early Recovery and Reconstruction Plan for Gaza 2014-2017" in 2014 in the aftermath of the devastating conflict of July/August 2014. The implementation of this plan, in particular with the current level of Israeli's restrictions, remains challenging. Furthermore, prospects for reconciliation between the Palestinian faction governing Gaza – Hamas – and the Fatah-administered West Bank have so far come to naught.

In October 2015, the Palestinian Council of Ministers approved the merging of the Ministry of Planning with the Ministry of Finance, thus creating the Ministry of Finance and Planning and improving the outlook for more effective policy monitoring and evaluation.

In 2016, the EU budget contributed a total of EUR 168 million, through PEGASE DFS, to help the Palestinian Authority with the payments of Palestinian Authority salaries/pensions (EUR 115 million), of allowances for poor Palestinian families (EUR 40 million) and of arrears for medical referrals to East Jerusalem Hospitals (EUR 13 million). These funds were complemented in 2016 by the following contributions from EU Members States: EUR 1 million from Ireland (EUR 0.30 million for salaries/pensions and EUR 0.70 million for social allowances) and EUR 4 million

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[6] According to the WB report to AHLC meeting in September 2016, 46% of pledges to Gaza were disbursed.

from the Netherlands for salaries/pensions, earmarked to the justice sector; EUR 1.5 million from Austria for social allowances and EUR 25,000 from Portugal also for social allowances.

In 2016, other donors (including EU Member States) have also provided additional support to the Palestinian Authority budget either directly or via the World Bank-managed Palestinian Reform Development Plan (PRDP) Trust Fund. The Arab countries direct financial assistance support to the Palestinian Authority in the first eight months of 2016 amounted to NIS 576 million (EUR 136 million), mainly from Saudi Arabia (NIS 461 million - EUR 109 million), Algeria (NIS 103 million - EUR 24 million) and Egypt (NIS 12 million - EUR 3 million). The PRDP Trust Fund's total disbursements in the first 8 months of 2016 amounted to NIS 281 million (EUR 66 million)[7].

1.1.2 Stakeholder analysis

The final beneficiary of the action will be the Palestinian population as a whole, estimated at 4,8 million[8]. Eligible beneficiaries and expenses are identified through a system based on strict and objective criteria set by the EU and based upon requests and information provided by the Palestinian Authority.

The Civil Servants and Pensioners component targets some 47,000 civil servants and pensioners in the West Bank, of which a significant majority works in the education and health sectors.

The Ministry of Social Development (MoSD) manages the Palestinian Authority's Cash Transfer Programme (CPT). For 2017 NIS 520 million (EUR 123.4 million) have already been allocated by Ministerial Council decision to the CPT[9]. With an annual average family allowance amounting to NIS 4,640 (EUR 1,100), the CPT is expected to target 112,000 vulnerable families in the West Bank and the Gaza Strip, i.e. around 670,000 persons, based on an average family size of six.

The Ministry of Health (MoH) and the East Jerusalem Hospital Network, composed of 6 East Jerusalem Hospitals (EJH), are the main counterpart for the EJH component. Since 2012, the EU and MS have covered the referral costs for patients referred for treatment in EJH by the MoH.

Overall, key partners include the Palestinian Authority institutions: Ministry of Finance and Planning, the technical Ministries and other relevant Departments and Agencies of the Palestinian Authority.

All donors contributing to the PEGASE DFS mechanism are considered key stakeholders.

1.1.3 Priority areas for support/problem analysis

Volatile context, worsening macroeconomic outlook and continuing donors' dependency

In its last report to the AHLC in September 2016, the World Bank (WB) considered the economic outlook for Palestine to be very challenging and subject to considerable risks. The WB summarised the situation as follows: "Political instability and the long lasting restrictions on movement, access and trade are the main impediments to economic growth in Palestine". These restrictions have significantly limited private sector activity and resulted in the

7 EUR amounts based on August 2016 InfoEuro rate: 1 EUR is equal to 4.2383 ILS.

8 The latest census was carried out in 2007; the figure is an estimate by the Palestinian Central Bureau of Statistics: http://www.pcbs.gov.ps/Portals/_Rainbow/Documents/gover_e.htm

9 This amount is meant to encompass already prospective donor contributions to the PA budget.

“deindustrialisation” of the Palestinian economy - with the share of manufacturing in GDP dropping from 18% in 1995 to around 10% in 2015. The share of agriculture in the economy has also decreased to 50% of what it was in 1995.

The World Bank also stated that whilst the Palestinian economy will not be able to reach its potential until a permanent peace agreement is established there is much that can be done. One of the key constraints to economic growth continues to be Israeli restrictions on Palestinian access to Area C. A 2013[10] World Bank study suggested that unrestricted Palestinian economic activity in Area C, including the exploitation of its natural resources, could increase GDP by as much as 35%". WB and IMF project medium-term growth in real GDP at 3.5%, which is insufficient to reduce unemployment below its current level of more than a quarter of the Palestinian labour force and raise per capita income given the projected population growth.

Moreover, it is to be noted that, in the past, the Government of Israel froze the transfer of clearance of revenues on several occasions as a response to political decisions made by the Palestinian Authority. This is considered a potential significant recurrent risk. In addition, as mentioned above, donor support has significantly declined in recent years (budget support in particular has decreased by around 40% since 2011) and become less predictable, with stalled commitments from several countries. Against this background the Palestinian Authority was forced to increase its debt to domestic banks, thereby exposing them further to the public sector and almost exhausting their legal borrowing capacities.

2 RISKS AND ASSUMPTIONS

Risks	Risk level (H/M/L)	Mitigating measures
Substantially worsening political and fiscal context with continued occupation, notably the potential freezing of the transfer of Clearance Revenues by Israel, which may lead to increased instability, volatility and of a return to violence in the medium-term growing	H	Enhanced EU dialogue with Israel, including linking EU co-operation effectiveness in Palestine directly to Israeli actions – in line with the ECA recommendation that 'the EEAS and Commission in conjunction with the broader donor community, should further engage with Israel, within the framework of broader EU-Israeli co-operation, in order to determine what steps Israel needs to take to ensure PEGASE DFS is more effective'.
Lack of progress of in the reconciliation process and continued regression in democratic and social accountability, with decreased legitimacy of the	H	EU support for the NCG to take leadership both at the technical and political level, as well as policy dialogue and monitoring of progress in reforms

10 World Bank Report No. AUS2922 -Area C and the Future of the Palestinian Economy

Palestinian Authority among the Palestinian population		Increased support for civilian oversight
Deterioration of the status quo in Gaza with expected increased level of poverty	M/H	Enhanced EU dialogue with Israel and the NCG
Fluctuations in the exchange rate may have an impact on funding needs	M/H	Continuous monitoring

Assumptions

- The two-State solution is still the political aim supported by the EU; and the EU continues supporting the Palestinian Authority in view of a peaceful solution;
- The PA continues to be committed to its statehood agenda and the reconciliation process;
- The Government of Israel respects its Oslo/Paris agreements' commitments, notably in terms of transfer of clearance revenues, and does not impose further restrictions under the occupation;
- Contributions from EU Member States and other donors will be made available during the implementation period to complement the proposed funds;
- Full co-operation with the Palestinian Authority is essential. This co-operation needs to be maintained, in particular for the identification of eligible beneficiaries and timing of payments and for the identification of eligible expenditure.

3 LESSONS LEARNT, COMPLEMENTARITY AND CROSS-CUTTING ISSUES

3.1 Lessons learnt

The PEGASE DFS mechanism builds upon the successful experience of the Temporary International Mechanism (2006-2007) and is implemented in full co-ordination with the Palestinian Authority and in close co-operation and transparency with EU Member States, the European Parliament and other donors. It is particularly appreciated by the Palestinian Authority for its flexibility and its catalytic nature in attracting funds from other donors without multiplying transaction costs.

The mid-term review of PEGASE conducted in 2009 highlighted the flexibility in planning and implementation, the highly competent and professional staff and the use of well-proven management systems while continuously innovating, which contributed to the success of this mechanism. Final evaluations covering the periods 2008-2015 have confirmed these findings. In particular, the latest evaluation covering the period 2014-2015 found that PEGASE DFS mechanism has contributed to provide "predictable, reliable and unconditional contributions to the Palestinian Authority. It has enabled the Palestinian Authority to maintain and manage its administration and build capacity despite the very critical political situation imposed by the occupation and the restrictions from Israel. The Palestinian Authority/PMO appreciates this support and call for its continuation in the same spirit". At the same time, "there are some elements within PEGASE DFS that would be better addressed through policy dialogue, such as the progression of the wage bill and the political issue of the reintegration of civil servants and pensioners in Gaza."

In December 2013, the ECA published a report on PEGASE DFS providing a number of recommendations. Most of these have already been addressed (e.g. using competitive tendering for technical assistance; review of the mechanism aiming at its simplification and applying the relevant simplification measures; establishment of a results-oriented approach – details under section 5.7).

3.2 Complementarity, synergy and donor coordination

Following the Single Support Framework for 2014-2016, the next programming exercise will cover the period 2017-2020, as part of a well-advanced Joint Programming process with MS, and in line with the Palestinian National Policy Agenda starting in 2017 and covering a 6 years period. The first European Joint Strategy currently being developed with European development partners has identified the following 5 pillars of support aligning with the next planning document of the Palestinian Authority: 1) Governance Reform, Fiscal Consolidation and Policy (Macroeconomic and Public Finance Management, Public Administration and Local Governance); 2) Rule of Law, Justice, Citizen Safety and Human Rights (Justice, Safety and Human Rights legislation); 3) Sustainable Service Delivery (Education, Health and Social Protection); 4) Access to Self-Sufficient Water and Energy Services (Infrastructure focus); 5. Sustainable Economic Development (Agriculture and Private Sector). The Strategy is due to be finalised in the last quarter of 2016 on the ground and be approved in the second quarter of 2017.

The EUREP has already provided complementary capacity building activities in line with the ongoing Results-Oriented Framework pilot sectors (macro-economic support, public finance management, public administration reform, education, health, and social protection), in terms of: (1) Policy Reform: a) strengthening of the accountability, integrity, and transparency of the public finance system, by supporting 'checks and balances' aspects (tackling both the supply and the demand-side), b) domestic revenue mobilisation - through a support to the Palestinian Authority's Taxpayer Awareness Programme; c) support to the Palestinian Authority's efforts in reducing the burden of net lending (ended in July 2014 – additional support could be envisaged in co-ordination with other donors); d) civil service reform; and, e) strengthening statistics capacities. (2) Service Delivery: through support to the Ministry of Social Development. Other EU Member States provide complementary capacity building support in relation to policy reforms and service delivery (in the fields of education and health).

In parallel, the Palestinian Reform Development Plan-Trust Fund (PRDP-TF) is managed by the World Bank, and its main donors include the UK, France, Norway, Australia and Kuwait. The release of funds is untargeted, but conditional on the implementation of key reforms for: a) improving the Palestinian Authority’s fiscal sustainability; and, b) improving public financial management and accountability. Synergies between PEGASE DFS and PRDP-TF are fostered to the largest extent possible.

Local donor co-ordination has also been streamlined in accordance with the conclusions of the AHLC meeting held in December 2005, following a proposal by the European Commission, the World Bank and Norway to reform Aid Management Structures. The EU continues to play a leading role in these structures at all levels. Relevant platforms include: (i) the Fiscal Working Group (co-chaired by the Ministry of Finance and Planning and the International Monetary Fund); (ii) the Public Administration and Civil Service Sector Working Group (co-chaired by the Ministry of Finance and Planning and the UK/Department for International Development (DfID)); (iii) the Social Protection Sector Working Group (co-chaired by the Ministry of Social

Development and the EU); and (iv) the sub-group on Health Referrals under the Health Sector Working Group.

Finally, the EU plays a leading role in local EU Member States co-ordination. Under the framework of the EU Heads of Co-operation meetings, an EU Informal Group on PEGASE DFS was set-up in early 2013 and has become the main forum to jointly monitor progress on the pilot sectors covered by the aforementioned ROF. Since 2013, increased co-ordination with other direct financial assistance donors (mainly the World Bank and the contributors to the PRDP-TF) has taken place.

3.3 Cross-cutting issues

Good governance principles are applied to the implementation mechanism and ownership on the part of the Palestinian Authority is assured. The EU also supports complementary capacity building activities focusing notably on the strengthening the public finance system, including 'checks and balances' aspects.

The actions proposed provide services vital to the social and economic rights of the Palestinian population.

As for gender equality, the upholding of key social services such as education and health will be critical to cater to women's –as well as men's – basic needs. Of the funds disbursed so far in 2016 within the CSP component, 42.3% of beneficiaries were women.

4 DESCRIPTION OF THE ACTION

4.1 Objectives/results

The overall objective of this special measure is to maintain the viability of the two-state solution by avoiding the fiscal collapse of the Palestinian Authority and sustaining basic living conditions of the whole Palestinian population.

The specific objective is to support the Palestinian national development agenda and in particular:

(1) to support the Palestinian Authority to deliver to the Palestinian population essential basic services by maintaining the functioning of the administration;

(2) to improve the economic opportunities of poor, vulnerable and isolated population; and

(3) to support the Palestinian Authority in reducing its budget deficit and implementing its reform agenda while increasing the Palestinian Authority's transparency and accountability.

This programme is relevant for the Agenda 2030. It contributes primarily to the progressive achievement of SDG Goal 16, Peace, Justice and Strong Institutions; but also promotes progress towards Goal 1, No Poverty; Goal 3, Good Health and Well-being; Goal 4, Quality Education. This does not imply a commitment by the Palestinian Authority benefiting from this programme.

4.2 Main activities

Three categories of public expenditure are eligible for support under this action for a total amount of EUR 158.1 million, which follows previous actions committed every year since 2008 for funds disbursed through the PEGASE DFS mechanism:

Component 1: Supporting Palestinian administration and services (indicative allocation: EUR 85 million)

The EU will contribute to the payment of salaries and pensions to the Palestinian Authority civil servants in Palestine (West Bank). The objective of this activity is to support the Palestinian Authority to maintain the functioning of the administration effectively under its control and thus deliver to the Palestinian population essential basic services in the West Bank. The regular contribution to the funding of the wages expenditure for civil servants also reinforces the Palestinian Authority's public finance management and public finance reform implementation.

Component 2: Supporting the Palestinian social protection system (indicative allocation: EUR 60 million)

The EU will contribute to the quarterly payment of social allowances to poor and vulnerable Palestinian families through the Palestinian Authority's national cash transfer programme (CTP) that functions in the West Bank and the Gaza Strip. The objective of this activity is to ensure the continued assistance to Palestinian families living in extreme poverty, who are dependent on financial aid from the Palestinian Authority. This activity also reinforces the reform of the social protection system and the social cohesion among Palestinians. Without prejudice to the overall level of budgetary allocation for the CTP, determined by the PA, and the individual level of funding for vulnerable families, determined using proxy means testing on equal basis for the beneficiaries in the West Bank and Gaza, EUR 20 million out of the overall amount under Component 2 will be used to increase the EU's contribution to social allowances specifically in Gaza.

Component 3: Support to East Jerusalem Hospitals (indicative allocation: EUR 13 million)

The six Palestinian hospitals in East Jerusalem form an integral part of the network of health provision for Palestinians. In addition to the importance to the health network, these hospitals are also a symbol of continued Palestinian presence in East Jerusalem. The financial difficulties of the Palestinian Authority have resulted in a situation where many of the hospital bills underwritten by the Ministry of Health, and validated by the Ministry of Finance, remain unpaid. The hospitals are therefore, and to differing degrees, themselves immediately affected by the Palestinian Authority's financial crisis.

Component 4: Visibility of PEGASE DFS programmes (Indicative allocation: EUR 0.1 million)

Visibility and outreach activities related to the PEGASE DFS mechanism will be organised, notably with respect to the VPF programme.

4.3 Intervention logic

Through systematic and predictable contributions to the Palestinian Authority's recurrent expenditures made through the PEGASE DFS mechanism, the EU is making a key contribution to avoiding the financial collapse of the Palestinian Authority itself and of many Palestinian institutions and private sector actors that financially depend on it. In doing so, the EU significantly contributes to maintaining the viability of the two-state solution and the Palestinian Auhtority's state-building activities, notably in terms of service delivery. The funds channelled through the PEGASE DFS mechanism thus contribute to the social cohesion and the economic and security stabilisation of Palestine. The contributions made through any of the aforementioned three main components play a key role in supporting the PA to implement policy reforms aiming at enhancing its fiscal sustainability and improve the accountability, integrity, and transparency of its public finance system, as well as to improve service delivery.

5 IMPLEMENTATION

5.1 Financing agreement

In order to implement this action, it is foreseen to conclude a financing agreement with the partner country, referred to in Article 184(2)(b) of Regulation (EU, Euratom) No 966/2012.

5.2 Indicative implementation period

The indicative operational implementation period of this action, during which the activities described in section 4.1 will be carried out and the corresponding contracts and agreements implemented, is 24 months from the date of entry into force of the financing agreement. The funds under the three Components are, however, expected to be disbursed in total by the end of 2017.

Extensions of the implementation period may be agreed by the Commission's authorising officer responsible by amending this Decision and the relevant contracts and agreements; such amendments to this Decision constitute technical amendments in the sense of point (i) of Article 2(3)(c) of Regulation (EU) No 236/2014.

5.3 Implementation modalities

Direct management will be applied for all four components.

PEGASE DFS programmes will be implemented by the Commission through the Office of the European Union Representative to the West Bank and Gaza Strip, UNRWA (EUREP), located in East Jerusalem, in close co-ordination with the Palestinian Authority and EU Member States.

Subject in generic terms, if possible	**Type (e.g.: works, supplies, services)**	**Indicative number of contracts**	**Indicative trimester of launch of the procedure**
Support to the recurrent costs of the Palestinian Authority through PEGASE DFS programmes	Direct Financial Support (pro-forma contracts)	3	First quarter 2017
Visibility	Services	1	Second quarter 2017

For the aforesaid Components 1, 2 and 3, disbursements will be made by the Commission through specific sub-accounts of the Palestinian Authority's Single-Treasury Account to the eligible beneficiaries of the PEGASE DFS programmes detailed in Section 4.2 above, following eligibility checks and verification and control procedures by external experts and international audit firms.

5.4 Scope of geographical eligibility for procurement and grants

The geographical eligibility in terms of place of establishment for participating in procurement and grant award procedures and in terms of origin of supplies purchased as established in the basic act and set out in the relevant contractual documents shall apply, subject to the following provisions.

The Commission's authorising officer responsible may extend the geographical eligibility in accordance with Article 9(2)(b) of Regulation (EU) No 236/2014 on the basis of urgency or of unavailability of products and services in the markets of the countries concerned, or in other duly substantiated cases where the eligibility rules would make the realization of this action impossible or exceedingly difficult.

5.5 Indicative budget

	EU contribution (amount in EUR)	Indicative third party contribution, in currency identified
Component 1: Supporting Palestinian administration and services (CSP)	85,000,000	N/A
Component 2: Supporting the Palestinian social protection system (VPF)	60,000,000	N/A
Component 3: Support to East Jerusalem hospitals (EJH)	13,000,000	N/A
Component 4: Communication and visibility for PEGASE DFS programmes	100,000	N/A
Totals	158,100,000	N/A

The aforementioned allocations are indicative and may be changed depending on the needs expressed by the Palestinian Authority and the funds received from other donors for specific areas covered by PEGASE DFS programmes. It is anticipated that, as in earlier years, other donors will make contributions.

Other funds for the necessary technical assistance (aligned to the Results-Oriented Framework), evaluation, audit and visibility actions have been made available under separate Financing Decisions (notably Decision C(2016)1359 on "Direct Financial Support to Recurrent Expenditures of the Palestinian Authority 2016" - ENI/2016/38842).

5.6 Organisational set-up and responsibilities

On the Palestinian Authority side, the leading partners in the implementation of the PEGASE DFS programme will be the Ministry of Finance and Planning in the execution of the payments to final beneficiaries, the Ministry of Social Development (Component 2) and the Ministry of Health (Component 3).

All contracts and payments are made by the Commission on behalf of the Beneficiary.

EUREP will be in charge of the management and the implementation of the operation, in close co-ordination with other donors and international organisations, including for the following:

- liaise with the Ministry of Finance and Planning concerning eligible expenditures;
- organise and manage the process of validation, control, payment and audit; and,

- be responsible for paying contributions or for supporting payments to be made by individual donors.

Financial experts and qualified auditors will work for the project and will be complemented by other experts as required.

The Ministry of Finance and Planning will provide all necessary information and documentation to enable EUREP to implement the various components while ensuring the highest level of verification and control over the use of resources.

5.7 Performance monitoring and reporting

A comprehensive system of monitoring, control and audit will continue to be applied in the framework of the implementation of PEGASE DFS programmes, to provide assurance over the use of funds, and the efficient and effective provision of support to the Palestinian Authority and population while fully protecting donor interests.

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

As from early 2013, the EU started working towards a Results-Oriented Framework for PEGASE DFS covering both Policy Reforms and Service Delivery, under which EU donors would further co-ordinate the support (in terms of funding, technical assistance and policy dialogue). The ROF is anchored within the EU process towards EU Joint Programming expected to start in 2017. The basis has been the EU/MS Local Development Strategy (EU LDS), which defines rolling EU operational priorities and an EU/MS division of labour in Palestine. This includes 16 EU/MS Sector Strategy Fiches in line with the Palestinian National Development Plan 2014-2016 and related sectors strategies. The approach is thus a consolidated EU approach, and a step towards Joint Programming. The development of such framework has also been done in close collaboration with the Palestinian Authority and the other direct financial assistance donors.

The EU and the Palestinian Authority signed a Memorandum of Understanding on 25 March 2015, which includes the ROF and its performance monitoring and reporting set-up, for the period 1 April 2015 to 31 December 2015. A quarterly (internal) and yearly (shared with the Palestinian Authority) operational reporting system has been put in place, building notably on internal and external reviews such as reviews by the World Bank and by the International Monetary Fund (IMF) on macroeconomic issues. The pilot phase has been extended in June 2016 until the end of the year.

The pilot ROF covers six of the above 16 sectors, under the respective EU leaderships in accordance with the local EU Division of Labour:

(i) *Pillar I: "Fiscal consolidation and policy reforms"*: (1) Macroeconomic Support/Fiscal Outlook (sector led by the EU with the Ministry of Finance and Planning as counterpart); (2) Public Finance Management (sector led by the EU with the Ministry of Finance and Planning and the State Audit and administrative Central Bureau as counterparts); and, (3) Public Administration Reform (sector led by the UK with the Prime Minister's Office and the General Personnel Council as counterparts).

(ii) *Pillar II "Service delivery"*: (1) Education (sector led Belgium with the Ministry of Education and Higher Education as counterpart); (2) Health (sector led by Italy with the

Ministry of Health as counterpart); and, (3) Social Protection (sector led by the EU with the Ministry of Social Affairs as counterpart).

The next programming exercise covering the period 2017-2020, as part of a well-advanced Joint Programming process with MS, will further align with the Palestinian National Policy Agenda. Particular attention will be paid to enhancing monitoring and evaluation, and continuing strengthening the policy dialogue in terms of reforms.

5.8 Evaluation

An evaluation of the PEGASE DFS programmes for the period 2014-2015, including an evaluation of the pilot ROF, took place in the first semester of 2016. Earlier, a comprehensive evaluation report covering the first three years (2008-2011) of implementation was carried-out in 2012. Another evaluation covering the period 2011-2013 was completed in March 2015.

Follow-up evaluations are currently planned to take place every 18 months. They will be carried out for accountability and learning purposes, in particular with respect to the alignment with the priorities defined in the future NPA; the assurance that the Palestinian Authority leads the process of monitoring, evaluation and reporting of the ROF; and the increased impact of policy dialogue.

The evaluation reports shall be shared with the partner country and other key stakeholders, notably contributing donors. The implementing partner and the Commission shall analyse the conclusions and recommendations of the evaluations and, where appropriate, in agreement with the partner country, jointly decide on the follow-up actions to be taken and any adjustments necessary, including, if indicated, the reorientation of the project.

5.9 Audit

Financial experts and qualified auditors will be involved in the implementation of PEGASE DFS programmes, which will be complemented by Commission and EU Member States specialists and international or local experts.

Advanced monitoring, control and audit systems are set up for all of PEGASE DFS programmes. All donors contributing to PEGASE DFS programmes have full access to the corresponding monitoring and audit reports on the basis of which their contributions are disbursed.

In addition to the regular verifications and audits of eligible expenditures to identify and validate payments, annual ex-post audits of PEGASE DFS programmes will be undertaken in accordance with international standards, to provide the maximum level of assurance which will be partly contracted from other decisions related to the PEGASE DFS activities. Contributing donors will be invited to participate. Contributing donors may also carry out ex-post audits of expenditures covered by their payments.

5.10 Communication and visibility

Communication and visibility of the EU is a legal obligation for all external actions funded by the EU.

Progress of implementation will be communicated regularly to all stakeholders through mid-and end-year financial and operational reports. Regular meetings are held with EU Member States in Brussels as well as locally.

It is foreseen that one contract (through a relevant framework contract) will be signed for visibility and communication purposes during the second quarter 2017.

6 PRE-CONDITIONS

None.