

Is the Palestinian Authority Ready for Statehood?

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Brief Analysis

At the April 13 meeting of the West Bank/Gaza donors group known as the Ad Hoc Liaison Committee, the International Monetary Fund (IMF) and World Bank presented reports arguing that the Palestinians are ready for statehood. Yet that judgment requires three important caveats. First, it depends on future Israel-Palestinian cooperation; second, it is contingent on Gaza's return to Palestinian Authority (PA) control; and third, it does not take into account the PA's broader political readiness for statehood, which continues to lag.

Cooperation with Israel

The IMF report correctly emphasizes that Israel will play a central role in the PA's economic future: "To maintain the growth momentum, rebalance the composition of output, reduce regional disparities [i.e., Gaza compared to the West Bank], and accelerate the state-building process, it is essential for [Israel] to phase out all restrictions as soon as possible." This implies that a unilateral statehood declaration would not be the culmination of PA state-building efforts, but rather their undoing, since Israeli cooperation could not be counted on in such a scenario.

Consider the dramatic increase in PA tax revenue, which has reduced the Palestinians' past overreliance on foreign aid. Digging into the tables accompanying the IMF report, one finds that two-thirds of current PA receipts are "clearance revenues," that is, taxes collected on the Palestinians' behalf by Israel and passed on to the PA. These include taxes on goods shipped from Israel to the West Bank and Gaza, such as customs duties and heavy tariffs on petroleum products. In 2010, the PA received \$1.26 billion in clearance revenues, compared to the \$750 million in domestic revenue it collected on its own. In other words, the PA is able to pay its bills only because of the money transferred by Israel. If bilateral cooperation ceased, the PA would be in no position to pay salaries or meet its other commitments.

The Gaza situation highlights Israel's centrality to the PA economy. As the IMF and World Bank reports document, once Israel allowed more goods to be shipped into Gaza despite Hamas control there, the economy recovered nicely.

The IMF report also praises one surprising example of Israeli cooperation in Gaza, namely, the manner in which Israeli commercial banks have worked with Palestinian banks to facilitate "timely and regular" cash transfers into the territory, overcoming Israeli concerns about the "legal implications" of conducting business with the terrorist organization Hamas.

Sharp Contrast with Gaza

A ccording to the IMF report, "The PA is now able to conduct the sound economic policies expected of a future well-functioning Palestinian state, given its solid track record in reforms and institution-building in the public finance and financial areas." The report then goes on to list a series of activities the PA has undertaken in recent years, the absence of which the IMF severely criticized during Yasser Arafat's presidency. In particular, the PA has been able to "enhance transparency," "prepare and execute annual budgets," "prepare annual financial statements," and "tightly control and prioritize its expenditures" -- all significant accomplishments.

Unfortunately, this progress applies only to the PA, not to the Hamas authorities who control Gaza. The latter's methods of taxation and expenditure are exactly the opposite of what the IMF recommends: they are not transparent, not conducted in line with a budget, not accompanied by financial statements, and not tightly controlled or prioritized. The IMF report praises the continued strengthening of the PA's public financial management system, but it fails to mention how Hamas controls substantial sums that are completely outside this system and beyond PA control.

The World Bank report does note some serious problems in Gaza, such as judges not applying commercial law. But it is silent regarding the territory's lack of transparency, accountability, and sound public financial management. Both the IMF and World Bank should have noted that the progress seen in the West Bank is not matched in Gaza, making the establishment of a unified Palestinian state incorporating both territories difficult to envisage without Gaza's return to full PA control.

A State Is More than an Economy

T he World Bank report makes the far-reaching claim that if the PA "maintains its performance in institution-building and delivery of public services, it is well-positioned for the establishment of a state at any point in the near future." That claim goes beyond the World Bank's expertise, however, since statehood involves many other issues beyond the economic sphere.

On the surface, the bank's report seems to address some of these issues: "While no recipe for building a state exists, the Organization for Economic Co-operation and Development (OECD) has identified certain key functions as strategically important. Thus, in its 2011 policy guidance 'Supporting Statebuilding in Situations of Conflict and Fragility,' the OECD describes these key functions as security and justice; revenue and expenditure management; economic development, especially job creation; and service delivery." The bank then concludes that it "has documented some of the PA's achievements in the key state functions posited by the OECD."

Yet the World Bank assessment of the PA is in fact limited in comparison to the OECD criteria. The report does not -- nor should it, given the bank's mandate and expertise -- consider questions of "security and justice" beyond narrow discussion of contract enforcement and commercial law. To be sure, PA prime minister Salam Fayad has made great strides in building the capabilities of a future state, and law and order have been largely restored in many cities. More progress is needed on other aspects of "security and justice," however, including the observance of human rights standards, freedom from political violence, and the prevention of terrorism, particularly in Gaza.

More broadly, the bank's listed criteria comprise just one of the three dimensions of state building described in the OECD policy guidance: "state capability and responsiveness." The PA has made relatively little progress on the other

two dimensions -- "political settlement and processes" and "social expectations" of the state-society relationship, both of which are at the heart of the uprisings currently sweeping the Arab world. Efforts on these fronts have been stymied by stubborn resistance from Fatah and the other political parties that dominate the PA, which are reluctant to reform themselves or abandon the corruption and cronyism that propelled Hamas to its 2006 electoral victories.

The World Bank and IMF are correct to praise the PA, and particularly Fayad, for their hard-won progress in building the economic aspects of a future state. Fayad's accomplishments came against long odds and will be vital to the success and sustainability of any Israeli-Palestinian peace agreement. But they have been put at risk by the stagnation of peace negotiations and the looming prospect of a unilateral Palestinian declaration of statehood. Moreover, they are insufficient without greater attention to the political aspects of state building. The PA and its Quartet partners -- the UN, EU, United States, and Russia -- would be wise to put the same sort of steady and determined work into these areas that Fayad has put into the Palestinian economy.

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