

OFFICE OF THE SPECIAL ENVOY FOR DISENGAGEMENT

**Periodic Report
April 2006**

Role of the Office of the Special Envoy

The Office of the Special Envoy for Disengagement will close on 30 April, one year after the Quartet principals agreed on the Envoy's mandate. Quartet Special Envoy Wolfensohn and his team would like to thank all for their cooperation and support. Since its establishment on 1 June 2005, the QSE Office has been able to play a key role in the unfolding developments and can point to four primary accomplishments: (1) to demonstrate the operational functionality of the Quartet and its co-operation with the international community, (2) to act as a trusted partner in negotiations between the parties, (3) to facilitate Israeli-Palestinian co-ordination on main issues related to the Israeli withdrawal from the Gaza Strip, and (4) to advance co-ordination and co-operation between the Palestinian Authority (PA) and the international donor community.

Update on the 6+3 Agenda

While success was achieved at Rafah, and for a time at the Karni crossing, the overall implementation of the 15 November Agreement on Movement and Access (AMA) has been disappointing. Each side bears responsibility for this situation, which has ultimately meant that the benefits we had hoped would accrue to the Palestinian economy – and ultimately to the security of both peoples – have not materialized. Although the results of the Palestinian elections altered the parties' expectations, it is regrettable that the parties did not work harder to conclude some of the issues immediately after the signing of the AMA. The AMA remains on the agenda of the Quartet with expectations of its full implementation.

Responsibility for the biweekly monitoring reports on the implementation of the AMA will be transferred from the QSE office upon its closing to the United Nations.

The Six Bilateral Issues

(1) *Border Crossings and Trade Corridors*: The prolonged and repetitive closure of Karni, attributed to IDF warnings of security threats, has been extremely damaging. Since the beginning of the year, Karni has been closed on 50% of the days it was scheduled to operate. Export volumes during this period averaged just 23 truckloads per day, compared to the target level of 150 truckloads per day by 31 December as set out by the AMA (not including agricultural exports).

By 17 March, the flour mills in Gaza had run out of wheat and on 18 March, UNRWA had run out of petrol. To help alleviate the humanitarian crisis building as a result of the closing of Karni the Government of Israel (GoI) opened Kerem Shalom for the import of essential food commodities from Egypt on 23 March. Since the opening of Kerem Shalom, more than 300 truckloads of flour, sugar and rice were

imported from Egypt into Gaza using the back-to-back system. No goods have been exported through Kerem Shalom.

Erez crossing was closed on 12 March because of the Purim holiday and has been closed since. In the 6-week period leading up to this closure of Erez, 2800 Palestinian workers and businesspeople were entering Israel through the crossing each day. This represented a significant increase compared to the average of 1841 persons daily during the eighteen months prior to Israel's disengagement from Gaza.

(2) *Connecting Gaza with the West Bank*: Neither bus nor truck convoys began by their respective deadlines of 15 December 2005 and 15 January 2006 and discussions on a permanent territorial link ceased after violence erupted in the Gaza Strip at the end of 2005 and beginning of the New Year.

(3) *Movement in the West Bank*: The AMA called for a plan to be agreed by 31 December to reduce the number of obstacles to movement in the West Bank. A plan has not been agreed and since the beginning of the year, the number of obstacles counted by OCHA increased from 411 to more than 500.

(4) *Airport, Sea Port, and Rafah*: Since 26 November, Rafah has operated more or less continuously under the supervision of the EU Border Assistance Mission (EU BAM). Standard operating hours were recently increased and the crossing is now open daily from 8 a.m. to 7 p.m. Since its opening, nearly 200,000 border crossings have taken place at Rafah. In recent weeks, an understanding was reached between the Egyptians and Palestinians on the export of goods through Rafah. It is hoped that in the near future agricultural product will exit through Rafah for export to the Gulf using the Al Arish airport in Egypt. To date, exports through Rafah have occurred only twice once in December 2005 (one truckload of furniture) and once when, on 14 March, four truckloads of furniture and handicrafts bound for exhibition were exported using the back-to-back system under the supervision of the EU BAM.

Discussions on the airport and seaport have not taken place. A draft letter regarding Israeli guarantees concerning the sea port was passed via US intermediaries to GoI in December 2005, and is still pending.

(5) *The Houses in the former Settlements*: The GoI and the United Nations Development Programme (UNDP) signed an agreement on 20 December whereby the GoI would pay the UNDP to clear, sort, shred and store the rubble remaining from the dismantled settlement buildings. Work on the first site will begin in May and the UNDP estimates that the rubble from all the evacuated settlements (around 1.2 million tons) will be cleared by the end of 2006 and that hundreds of thousands of working days will be created as a result. In addition, some of the recycled rubble will be used in the development and construction of roads throughout the Gaza Strip. There has been no progress regarding the final destination of rubble that cannot be recycled.

(6) *The Greenhouses in the former Settlements*: Closure at Karni has been devastating for the agricultural sector in Gaza. No exception has been made for the settlement greenhouses generously purchased by philanthropists and transferred to the Palestine Economic Development Company (PEDCO), the government-owned, commercially-run company now responsible for their operation. USAID contractors estimated that the daily revenue losses to the former settlement greenhouses resulting from the closure of Karni during the peak harvest season was more than \$150,000 per day. Revenue losses to the agricultural sector as a whole in Gaza were estimated at around

\$450,000 per day during the peak season. Since the beginning of the year, the sector has lost more than \$18 million in foregone revenues due to the closures at Karni.

In accordance with original intentions, PEDCO is now looking into options for divestiture. With the repetitive closure of Karni, PEDCO can no longer financially support the operation of the greenhouses (having already invested an additional \$15-20 million upon receiving them). Divestiture will be carried out with certain goals in mind, such as ensuring the continued operation of the facilities and preserving employment for some 4,000 Palestinians. One possible model is to transfer management and leasing rights to a union of co-operatives that would in turn auction them off in smaller lots to Gazan farmers.

The Three Palestinian Issues

(1) *The Fiscal Crisis:* The fiscal situation of the PA has gone from bad to worse. Prior to the establishment of the new government, the PA faced a monthly budget deficit of roughly \$70 million. Israel's withholding of \$50-60 million in monthly revenue collected on behalf of the PA has almost doubled the monthly deficit and the PA must now identify nearly \$130 million in financing each month to maintain current operations.

The QSE visited President Putin and a number of Gulf and European States in February and again at the beginning of March to consult and determine the various states' positions on funding the interim government. After the visits in February, funds were forthcoming from the Qataris, the UAE, the Saudis, the Russians and the European Commission released funds from the World Bank Trust Fund and provided additional monies for the payment of utilities. However, failing adherence to the Quartet's three conditions set out in its 30 January 2006 statement (see under "Challenges Ahead", below), external budget support to the Hamas-led PA will not be forthcoming from most Western donors.

PA salaries for the month of March have not been paid and are now a month overdue. It remains unclear how funding to pay these salaries, as well as some \$20 million in outstanding payments for operations in the month of February, will be secured. Recently, a few Arab nations have come forward with pledges of assistance to the Palestinian people and in some cases have transferred funds to the Arab League for the purpose of providing budget support to the PA. Given the scale of the problem, however, such assistance if forthcoming provides only temporary relief. Actions to reduce the deficit are simply unavoidable and the drastic financial shortfall will undoubtedly force more aggressive action by the PA in the near future.

The PA's problems are further exacerbated by the fact that banks presently are not willing to do business with the Hamas-led government for fear of sanctions and litigation in the United States. Thus, even if the funds were available, it is as yet unclear how the financial transactions involved in the transfer of funds and distribution of salary payments would be carried out.

(2) *The Three-Year Plan for Palestinian Development:* In February, the Local Aid Coordination Secretariat (LACS) led an effort to coordinate donor consultations on the PA's draft Medium Term Development Plan (MTDP). Comprehensive feedback was provided to the Ministry of Planning in early March. The MTDP has not yet been approved by the Cabinet.

(3) *A Package of Quick-Impact Economic Programs*: Political developments have forced most donors to review their programs of assistance to the Palestinians. In his visits to the region in February and March 2006, the QSE held consultations with key donors and recommended to the Quartet that a donor meeting be held to determine a coordinated and effective way forward. On 27 April, the Canadians held a donor meeting in London to shape and stimulate the discussion. A number of donors, while scaling back assistance to the PA, have indicated they will maintain or increase provision of humanitarian assistance to the Palestinian people through the United Nations agencies or international and Palestinian NGOs. Such activity will continue to play out and shape up in the coming weeks.

The Russian Government for example has agreed to provide \$10 million in budget support although it will be not be directed to the PA but instead specifically earmarked for identified institutions and projects, including Avian Influenza prevention and compensation to farmers, the Red Crescent Society, six hospitals and health centres, pharmaceutical supplies and to the *Tawjihi* (high school diploma) examination.

In an effort to assess donor activity on the ground leading up to and in the wake of disengagement, the QSE office, together with the LACS, compiled a database of estimated donor disbursements in 2005. This information was released to the donor community on 6 April. The LACS will continue to work with the Ministry of Planning to use this information to their benefit. Furthermore, the LACS will work with donors and the Ministry of Planning on an improved system to report and track donor activity efficiently, frequently and accurately.

Challenges Ahead

On 30 January the Quartet set out the three conditions to be met by the Palestinian Authority: nonviolence, recognition of Israel and acceptance of previous agreements and obligations, including the Roadmap. In its statement of 30 March, the Quartet members repeated its call for the new Palestinian government to commit to these principles and noted that any future assistance to any new government would be reviewed by donors against that government's commitment to those principles.

In a scenario where Israel continues to withhold the transfer of clearance revenues to the PA, trade and labour restrictions continue and aid flows are reduced – all three of which seem plausible in the near future – the World Bank estimates that the real GDP per capita will decline by 27% in 2006. The absence of the spending power of up to 150,000 PA employees is already felt. Business is reduced, tax revenues are decreasing and banks are calling in outstanding private loans. By 2008 in this scenario, unemployment would reach 47% and poverty 74%. Most donors have accordingly come to the conclusion that they will increase or maintain levels of humanitarian assistance to the Palestinian people and are looking to the United Nations Agencies and NGOs to do so.

However, the PA provides over 60% of all health and education services, public sector employment accounts for about 25% of total employment in the West Bank and Gaza, and PA expenditures accounted for roughly 45% of GDP in 2005. It is not possible to immediately replace these existing PA functions – neither the UN nor the NGOs many of the donors are looking towards have the capacity to fulfill these roles. As such, donors are looking at ways to continue to support PA provision of health and education services in particular within the parameters of domestic legislation and

policies. Some, for example, are exploring the creation of a financing mechanism that satisfies technical requirements, including an independent and credible verification of the payment function, and at the same time functions in a manner consistent with overarching policy objectives and legal constraints.

At the same time we are searching for ways to address these needs, we must ask ourselves if humanitarian assistance alone will suffice and bring us to the ultimate goal of a two state solution, as laid down in the Roadmap, and a successful conclusion of the peace process. Over the past few years, the international community has spent about \$1 billion annually on assistance to the Palestinians, much of it directed at ensuring that credible and well functioning Palestinian institutions are built – a critical ingredient in the mix to meet our goal – and dedicated to the revitalization of the Palestinian economy – both essential foundations of a viable Palestinian State. Will we now simply abandon those goals? Or can we find a way by which we can work within our own laws and policies while continuing to support building a democratic, responsible government which can work to bring the Palestinian and Israeli people to their dream of living side by side in peace and security? For their sake but also for the sake of international peace and security, and the credibility of the international community to solve conflicts – even as protracted and complicated as the Israeli-Palestinian issue - every effort must be made to find this way forward.

Finally, we are deeply concerned that an uncontrolled resolution of all these issues between the Palestinians and the Israelis will have regional repercussions of a very serious nature involving a greater role for some other ME states and political organizations. This issue is a subject for a separate discussion but it is a critical and challenging element to the leaders of the International Community to consider and address with urgency.