

Into the Breach

Salam Fayyad and Palestine



INNOVATIONS FOR SUCCESSFUL SOCIETIES

CONTROLLING SECURITY SPENDING AT THE PALESTINIAN AUTHORITY, 2002 – 2004

Tristan Dreisbach drafted this case study based on multiple conversations with Salam Fayyad in Princeton, New Jersey, during 2019, as well as other interviews conducted in Washington, D.C., Jerusalem, and the Palestinian cities of Ramallah, Nablus, and Jericho in June and July of the same year. The case is part of a series on state building in Palestine, 2002–05 and 2007–13. Case published March 2022.

SYNOPSIS

When Salam Fayyad became the Palestinian Authority's finance minister in June 2002, one of his biggest challenges was to improve financial management in the security sector. To pay police, emergency workers, and other security personnel, commanders handed out cash to subordinates—a practice that was demeaning and that created opportunities for corruption. Procurement of equipment and supplies was neither open nor competitive and took place outside scrutiny by the finance ministry, which had little or no way of knowing where the government's money ended up. To address the problems, Fayyad, a political outsider, had to take on a deep-rooted culture of secrecy, the reluctance of a powerful president, and resistance from some of the security officials. He began to tighten controls by working with a reform-minded legislature to incorporate procedural changes into the 2003 budget law. He then identified security service chiefs who were open to payroll reform, and he helped them become early adopters. After more than a year of private persuasion, backed by growing public discontent with corruption, Fayyad was able to implement reforms that reduced opportunities to divert funds and that increased security workers' take-home pay. He also put security forces' procurement activities under finance ministry oversight, thereby further limiting the risk of corruption.

INTRODUCTION

In June 2002, when Salam Fayyad became finance minister of the Palestinian Authority (PA) in strife-torn territories occupied by Israel, the government's security forces were a picture of financial mismanagement. The finance ministry transferred payroll money to the Security Financial Administration—a unit within a security services' division that was independent of any ministry—and in turn, officials disbursed individual wage payments in cash. Each month, senior officers drove away with roughly US\$20 million in large plastic bank bags.¹ “God knows what happened to it after that,” Fayyad recalled.

The security services were supposed to distribute the payroll to their 50,000-plus employees, but it was common knowledge in Palestine that at least some of the money did not reach the intended recipients. Because there was no way to monitor the expenditure, no one knew how much money leaked from the system or where it went.

According to Fayyad, the rumor on the street was that some lower-level security personnel were ghosts—people who did not show up to work and whose units did not expect them to. These people received payments equal to about half of the amount that corresponded to their ranks on the pay scale, with the remaining half retained to use for nonwage outlays without transparency or accountability.

“There is little doubt,” Fayyad said, “that this scheme served, for some, as an instrument of unlawful self-enrichment, which contributed to the scheme's becoming deeply entrenched.”

The Security Financial Administration also kept payroll money for itself by using one exchange rate to collect US-dollar-denominated allocations from the finance ministry, then applying a higher rate to determine individual salary payments (denominated in Israeli shekels), and pocketing the difference, Fayyad said.

The conflicts of interest embedded in the payroll system created pressure to hire more people than the services required. “The more people you hire, the more people who work for you, the more money you make,” Fayyad said. “That is bad for the treasury because it creates a bloated bureaucracy with more security people hired than needed.” Adding people to the payroll meant that the PA also would have to provide pensions and other benefits for many years to come. Those actions had long-term consequences for the budget—and for the balance between services like education and health on one hand and security on the other.

The security services' procurement practices were just as troubling. Each month, the finance ministry gave the Security Financial Administration a block transfer of about US\$11 million to buy essential goods for security personnel, who could purchase basic consumer products and food through a cooperative—sometimes called a *commisary*. (Weapons procurement was limited to handguns and rifles and highly restricted by agreements between Israel and the PA.) The

Security Financial Administration made all of its purchases through a single supplier called al-Sakhra (the Rock), a state-owned enterprise controlled by the head of the Security Financial Administration. The arrangement meant there was no market competition among suppliers for contracts, and prices were higher, as a result.

Fayyad and others believed some of the money given to the security services for procurement further enriched people both within and outside the security establishment. The Israelis claimed some money went toward smuggling weapons into the West Bank and the Gaza Strip or to armed groups that fought against Israeli troops. “For sure there was corruption,” Fayyad said. “There’s no reason for procurement to be done in that way. There was nothing legitimate about it.”

THE CHALLENGE

Fayyad was a political outsider, an economist educated at the University of Texas at Austin who had returned to Palestine in the mid 1990s as the International Monetary Fund’s resident representative and who then worked briefly with a private bank. He lacked the long history of comradeship that PA President Yasser Arafat and others in the security services shared.

When Arafat appointed Fayyad finance minister as part of a new, reform-oriented cabinet, Fayyad’s job was to institute strong financial management throughout the government. Fayyad had to deliver the PA from a dire financial crisis and gain the trust of international donors so that badly needed external funding would flow into the PA. Changing the payroll and procurement practices of the security services was one of the most challenging items on Fayyad’s agenda. Those services, which carried out such functions as crowd control, traffic regulation, border management, intelligence, and emergency response, had become a bastion of jobs and power—all of it under Arafat’s personal control.²

Fayyad had to carry out his reforms in what amounted to a wartime environment that he described as “totally chaotic.” In 2000, deadly skirmishes in the West Bank and Gaza between Palestinian civilians and gunmen on the one hand and the Israeli armed forces on the other escalated, which fueled the second intifada—an uprising of Palestinians against the Israeli occupation that had cost thousands of Palestinian and Israeli lives. (The first intifada was an uprising that erupted in late 1987 and continued into the early 1990s.) “It was bad,” Fayyad recalled. “There were buses exploding and casualties on both sides, and there were even air raids on targets in both Gaza and the West Bank.”³

The Israelis claimed some of the security services were complicit in the violence. In March 2002—just a few months before Fayyad’s appointment to the finance ministry—the Israeli military reentered Palestinian cities, destroyed Palestinian security installations, ransacked PA government facilities, and detained and disarmed PA security personnel.⁴ The Israeli attacks devastated the police and other commands, causing more than US\$70 million in damage to their facilities and equipment.⁵ When the Israelis left the Palestinian cities, they

set up a system of permits that restricted the movement of all Palestinians—including those formerly responsible for maintaining law and order—and banned the police and other units from wearing uniforms. The resulting vacuum led local armed groups to take control in Palestinian communities.

Although those events weakened the capacity of the security services, they left intact an unaccountable, personalist system of authority, over which Arafat and the security chiefs wielded power. The chiefs had earned their status in the Palestinian movement through decades of service to the Palestine Liberation Organization (PLO), which long predated the PA. Arafat had led the PLO since 1969, and the Fatah political movement, which had dominated the PA's politics, since 1959. He was a towering figure in Palestine and reluctant to cede any of the power he had accumulated. Arafat exercised tight control over all aspects of the PA's security forces and kept a close eye on the security chiefs—whom he had handpicked.

The PA's opaque financial system supported that status quo. The president and other PA leaders used the security payroll to hire unemployed people or dole out patronage to former freedom fighters. Commanding officers also acquired extra money by underpaying service personnel and exploiting other weaknesses in the cash-based system, Fayyad said, adding that the security forces also directly funded Arafat's Fatah coalition—the leading political movement in the Palestinian territories—by deducting a monthly flat fee of ILS50 (around US\$12 at the time) for the organization's coffers.

Israel alleged that the PA used the flawed procurement system to funnel money toward illegal weapons purchases, citing as evidence a high-profile smuggling incident in January 2002 that resulted in the Israeli arrest and prosecution of the head of the Security Financial Administration.⁶ The incident reportedly angered US President George W. Bush and in part motivated his public call—in June 2004, shortly after Fayyad joined the government—for the PA to enact governance reforms. (The speech in which Bush made that call was also the first in which a sitting US president publicly called for two states living side by side in peace and security as a way to resolve the persistent conflict between Israel and Palestine.)

As finance minister, Fayyad oversaw all aspects of public financial management, but cleaning up the mess surrounding security payroll and procurement presented a major challenge. He had to open up the practices of the Security Financial Administration to scrutiny by the finance ministry and by other institutions responsible for oversight, such as the Palestinian Legislative Council. Security chiefs would likely resist, and if they objected, Arafat, though he had given his formal assent to reform, might not back change either.

Improving transparency had also become an urgent matter that was important to development partners, on which the PA depended for assistance—especially because the second intifada and Israel's response had caused the economy to contract and revenues to dwindle. Since its establishment in 1994, the PA had received international and Arab donor support for economic development, as well as assistance that financed equipment, technical aid, and

training.⁷ By 2002, however, those partners had become wary about continuing to give their assistance without assurances that the government was handling finances in a responsible manner.

FRAMING A RESPONSE

When Fayyad joined the 2002 PA government, he worked with legislative council members, ministers, and international donors to create a 100-day plan that won adoption shortly after his arrival in the finance ministry. One of the plan's priorities was to pay security personnel through direct deposit to their bank accounts—a measure that would substantially reduce the scope for corruption and nontransparent use of funds that resulted from diverting payroll money away from its stated purpose. The plan became official government policy, enabling Fayyad to portray the payroll issue not only as a top priority but also as one that had broad support. In other words, he would not be acting alone. (Other financial management items in the 100-day plan were the creation of a single treasury account and consolidation of the PA's commercial and investment operations. For more, see companion case studies on remaking the ministry, managing revenue, and managing spending.)

Fayyad also had a general idea of how to tackle the procurement issue, although he and his colleagues had not included that proposal in the 100-day plan. He wanted to put security forces procurement under finance ministry oversight and move the Security Financial Administration toward competitive bidding for specific items and away from the practice of buying from a single supplier under bulk contracts.

Fayyad said he planned to use every opportunity to push his agenda. In late September 2002, he was in a routine meeting with Arafat in the presidential compound in Ramallah, when the Israeli military laid siege. The Israelis, whose target was Arafat, offered Fayyad and other officials who did not work at the compound the chance to leave. Fayyad chose to stay, remaining holed up with the president and a small group of PA personnel for 11 days while Israeli forces demolished most of the surrounding buildings and the vehicles that were inside the compound.⁸

Taking advantage of his extended and close audience with the president, Fayyad broached the issue of the security services' financial management. "If you're really going to fix the salaries, then issue a directive and get this thing done once and for all," he recalled telling Arafat.

The president responded with an amused look. "This guy's crazy, I'm sure he was thinking," Fayyad said. "Do you think this is really the time to talk about something like this?" He remembered resorting to humor himself: "Well, in the unlikely event we survive, we'll have something to work with!"

Fayyad hoped that continued pressure and compelling arguments would eventually change the president's perspective. In addition to promoting his reform agenda during personal meetings, he planned to take his case to the Palestinian public.

Fayyad had three tactics in mind. The first was to characterize reforms as a tailored solution to a local problem. He would emphasize the benefits of efficient financial management for the cash-strapped Palestinian Authority and the Palestinian people while downplaying the roles of international institutions and donor countries that were pressuring the PA for change.

The second was to build coalitions. Fayyad planned to keep a sharp eye out for possible allies, including members of the security forces who were more open to change or members of the legislative council who could make the case to other leaders. Fayyad planned to use social occasions and chance encounters to develop relationships that could strengthen momentum for reform. It was common to run into PA officials, including security chiefs, around town—especially in the small and densely packed Gaza Strip.

The third tactic was to turn to the law. Although the reforms constituted part of the 100-day plan, which was adopted soon after he became finance minister, Fayyad knew that achieving lasting change required strong legal backing. He was aware that PA officials had disregarded laws in the past, but he still believed that an appeal to the law carried weight with the public—and would help persuade Arafat and the security chiefs to go along. “I looked for ways to make undesirable behavior unlawful, even when I knew I had no enforcement powers,” he said.

Persuading Arafat and the security chiefs was a long-term proposition; it would take time for any of the tactics to work. “At the beginning, Arafat resisted Salam Fayyad’s approach,” said Yasser Abed Rabbo, a longtime PLO leader who had worked closely with Arafat and served in the cabinet with Fayyad. “He wanted to remain the real chief of the security services. Fayyad was patient to explain that the reforms had nothing to do with weakening that control, but simply introduced some order. Arafat knew that this was his only option if he wanted to keep Fayyad with him, and he wanted that.”

GETTING DOWN TO WORK

To reform the security services’ financial management, Fayyad took several steps. He knew he must (1) have a law that would back him up, (2) identify cooperative security chiefs through whom he could seek some early wins, (3) ratchet up pressure on the other chiefs to accept direct deposit of salaries, and (4) implement measures to fix the procurement system.

Codifying reforms in a law

Fayyad’s initial priority was to secure legal backing for his proposed reforms. This step was relatively easy because most members of the Palestinian Legislative Council supported financial management reforms and had pressured Arafat—though largely unsuccessfully—to increase the transparency of the security forces’ financial dealings. Moreover, the annual budget process provided an appropriate vehicle.

One of the finance minister’s main tasks was to guide preparation of the PA’s annual budget law, which established rules that specified the ways the

government could collect and spend money and stipulated how much government funding went to individual PA institutions. Fayyad planned to include in the draft 2003 annual budget law new rules related to the security services' payroll and procurement. Almost as soon as he took office in June 2002, he began work on a draft, which he would submit to the legislative council in the form of a bill. If approved, as was likely given the council's support for reform, the bill would authorize the measures Fayyad wanted to implement.

Fayyad did not want to call out the security forces specifically in this law because that step that might be construed as confrontational and might create unnecessary tension with Arafat and the security chiefs. Instead, the language he crafted applied the reforms to the entire government, even though other PA institutions had already adopted many of them, such as direct deposit and competitive bidding under finance ministry oversight.

Fayyad's draft budget law, which he presented to the legislative council in December 2002, included a provision that banned all PA agencies from executing any payment operations in cash. It also required that all government purchasing take place through a competitive-bidding process under the control of the finance ministry's procurement department. (A procurement unit had existed since the beginning of the PA, but a 2003 cabinet decision elevated it to a department in the finance ministry, Fayyad said.) Although the draft law did not single out the security services, Fayyad clearly communicated his intentions in his December 2002 budget speech to the legislative council. In addition to stating that *all* ministries and *all* agencies had to comply with the provisions of the procurement law, he specifically mentioned the Security Financial Administration's exclusive relationship with the state-owned enterprise al-Sakhra, a noncompetitive arrangement that he said, "represents a clear violation of the law, and it, therefore, should not, and will not, be allowed to continue."⁹

The council members responded with applause, and the speech caught the attention of outside observers.¹⁰ An unidentified Western diplomat told the *New York Times* that Fayyad "had thrown down a gauntlet in front of the security services."¹¹

The council, which had pushed for such reforms, approved the budget law, with 44 of the 50 council members who attended the session (out of a total of 88 members) voting in favor. Arafat signed the 2003 budget law without complaint, but Fayyad knew this was only the beginning. The security branches were likely to ignore the new rules.

"I had no illusion that the law would be automatically implemented," he said. Still, the law marked an important step that provided credibility and boosted visibility for the steps he would take next.

Making inroads with security chiefs

Expecting no support from Arafat, Fayyad began what he called the "long, drawn-out business of persuading the chiefs" to adopt the payroll reform included in the budget law. "There's no way [Arafat] was going to centrally

command them” to change, he said. “So it was a war of attrition. It took a very long time.”

The security chiefs raised numerous objections, Fayyad recalled, “This does not work for security because the names of our officers will become known to Israel,” said some, and “this will not be good for discipline because people will receive their pay directly,” said others. None of their counterarguments had any validity, however, and they knew that, Fayyad surmised. Patiently and courteously, that same conversation took place over and over. “They knew what I was up to and why and that there was no way I was going to change my mind,” he recalled, “but they acted as if they did not presume any of that; likewise, I acted as if I took their objections and reservations seriously. *I was looking for an opening, and they were playing for time.*”

Fayyad’s personal touch helped pave the way forward. Through informal meetings at cafés and restaurants in the Gaza Strip, Fayyad had developed a friendly relationship with Amin al-Hindi, chief of Gaza-based general intelligence and a longtime Arafat ally. Al-Hindi was a PLO veteran who had been a leader of Black September, a Palestinian militant organization suspected of involvement in attacks such as the 1972 killings of members of the Israeli Olympic team in Munich.¹²

After passage of the budget law in 2003, Fayyad recalled al-Hindi’s telling him his units did not engage in corruption. “One day, out of the blue, he surprised me,” Fayyad said. “He says, ‘You know there’s nothing I know more than how desperate you are to get this done.’” Al-Hindi added that he had nothing to lose and would cooperate in switching to direct-deposit payments for his personnel, Fayyad recalled. Fayyad asked him to provide the finance ministry a list of people in his Gaza-based units and to instruct them all to open bank accounts. (In practice, al-Hindi had authority only over units in Gaza, although under law his authority was broader.) Al-Hindi soon complied, and the finance ministry began paying his people with bank transfers—as was the norm for PA civil servants—instead of cash.

Al-Hindi’s branch accounted for only a small percentage of the PA’s security forces: a few hundred people out of 56,640.¹³ But for Fayyad, al-Hindi’s cooperation represented a modest but crucial initial victory in his quest to ensure that the PA’s money was going where it was supposed to go. In subsequent conversations with other security chiefs, Fayyad said, he argued that if the intelligence chief was not worried about the identity of his personnel being known, no other chief should be.

Another win soon followed. Al-Hindi had a prominent colleague in Gaza who led the preventive security branch there and whom Fayyad also met with frequently. “This guy must have felt some peer pressure,” Fayyad suspected, and he did not want to look bad in comparison to al-Hindi. Soon he told Fayyad he would also comply, thereby adding a few thousand personnel to the direct-deposit system.¹⁴ “All of a sudden, I have these two agencies in Gaza doing it,” Fayyad said.

For Fayyad, the cooperation of the two chiefs signaled much more than individual steps in a slow march toward implementation of his payroll reform. To him, the willingness of both officers to adopt new procedures that Arafat had opposed was an indication that the president's influence was waning. The fact that both of the agencies in question were in Gaza whereas the president was in Ramallah may have helped, Fayyad recalled thinking at the time. But that did not appear to have similarly influenced the disposition of other Gaza-based security chiefs, who had substantially more personnel than the general intelligence and the preventive security branches combined.

"There's no way this would have happened when [Arafat] was at his peak, because the chiefs feared him," Fayyad said. "There's no way, I thought, the head of intelligence would act, but much to his credit, he did, and I was grateful."

The changes in payroll procedures apparently also went over well with these two security forces' rank-and-file members among whom, in 2003, lower-ranking personnel received about US\$200 a month. That year, a *New York Times* reporter interviewed a sergeant in the Gaza preventive security branch who said he was happy to receive his pay by direct deposit rather than having to wait for a superior to hand him cash. "You feel you're respected," he told the reporter. "It's civilized. And it will make it much easier for me to get a loan."¹⁵ Fayyad repeatedly stressed that point in his public messaging on the importance of security payroll reform. "This is about personal dignity for our security personnel," he recalled saying.

In addition, when payments first started going through banks, Fayyad stopped the practice of automatically deducting the flat Fatah fee of NIS50 per month (about US\$12), leaving it up to the officers themselves to decide whether they wished to make that donation.

Building pressure for change

Fayyad moved ahead on his end goal: to expand the payroll reforms to other branches of the security services. In a group meeting with security chiefs, he tried to persuade the majority, who had not yet adopted the reform, that the new payroll system had advantages. He asserted that requiring personnel to stand in line for cash handouts was humiliating and undignified. But they resisted, claiming that sending soldiers to the bank took them out of the barracks, where they belonged. "This doesn't work in the army," one of the chiefs told *The New York Times*. "It doesn't make any sense for a soldier with a gun to go to the bank."¹⁶

Fayyad decided to appeal to the legislative council for support to help push the reforms through. During his regular meetings with the finance committee, he made a point of telling its members which of the security chiefs were cooperating with him and which were holding out. "The intention was to shame them," Fayyad said, creating public pressure, including through media coverage of the legislative council hearings. He emphasized that direct deposit benefited

security sector workers by ensuring they were paid on time and by enabling them to qualify for bank loans.

Fayyad also made clear that if the security services adopted stronger financial management, everyone would benefit from the money saved. In a statement directed at all PA employees, he said that across-the-board salary reductions that had been implemented in response to the government's financial crisis could be rolled back if all of the security services implemented payroll reforms.¹⁷ The salary reductions, which the legislature viewed as illegal, were sometimes referred to as the *intifada tax*, and they were deeply unpopular.¹⁸

Momentum grew as Fayyad cultivated support. Allies within Arafat's Fatah movement took up the cause by distributing leaflets to the public stating: "Why do some commanders of the security forces still refuse to transfer their personnel's salaries to the personnel's bank accounts? Our people should ask this question."¹⁹

International pressure helped accelerate the push for change. The April 2003 road map for peace—a plan for resolving the Israel–Palestine conflict—proposed by the United States, the European Union, Russia, and the United Nations, called for security-related reforms, including consolidation of the PA's security organizations into three branches reporting to an empowered interior minister.

That same year, Arafat finally signed a long-awaited constitutional reform that created the post of prime minister, thereby reducing the president's authority over the security forces.²⁰ The new prime minister, Mahmoud Abbas, also took the post of interior minister, which had purview over the police force, the civil defense, and the preventive security branches of the security services, including the Gaza branch of preventive security that had already adopted direct deposit. At the same time, the basic law, as amended, specifically stipulated that general intelligence and the national security force, which was the largest security agency, would continue to report directly to the president.

By July 2003, the two other branches under interior ministry control, including the civil police, had agreed to the direct-deposit system. It meant that a total of more than 20,000 security personnel already received their salaries directly in their bank accounts. But Arafat still refused to go along with the reform when it came to the roughly 30,000 members of the branches of the security services that he directly controlled.²¹

In his December 2003 budget speech, Fayyad, using harsher language than he had when introducing the budget the previous year, sharply criticized the continued payment of cash to many security workers. "The failure to fully apply this reform clause is a direct violation of the current general budget and cannot be ignored," Fayyad told the legislative council. "The persistence of delay in this field, without any acceptable justification, will inflict plenty of damage on the reform efforts' credibility in general. This is unfair to the sincerity and depth of these efforts and it weakens our ability to obtain the aid we need to fund the budget."²²

The speech helped fuel internal political pressure on Arafat. In February 2004, more than 350 members of Arafat's Fatah movement resigned, citing lack of political reform, corruption, and the leadership's failure to challenge the Israeli occupation.²³ Meanwhile, other ministers joined Fayyad in trying to persuade the security chiefs and the president of the legitimacy and logic of the payroll reforms. "There have been discussions between the cabinet and some of the security forces about these payments," labor minister Ghassan Khatib said in February 2004. "We are doing our best to proceed with reforms in general: first because it helps us secure foreign aid, and second, because we need it for our own purposes."²⁴

The World Bank and other donors upped the pressure further. In 2004, they established a trust fund for budget support and set preconditions for releasing tranches of money, including full compliance with the budget law's requirement that all security personnel be paid via direct deposit.²⁵ Nigel Roberts, head of the World Bank's West Bank and Gaza office at the time, told Voice of America that the issue was a high priority. "There are definite areas where transparency has to be improved," he said. "The whole donor community feels very strongly about . . . this payment of all salaries through . . . the direct-deposit scheme."²⁶

As Arafat's authority continued to fade in light of the changing situation in Palestine, Fayyad, his reform allies, and the donor community found it easier to advance reforms. "The president became weak in the context of the second intifada," Fayyad said. "There was a lot of international pressure. The PA was underperforming. There were all kinds of rumors about it not doing the right thing with money and the security chiefs' doing all kinds of things that were not considered right."

In February 2004, after more than a year of pressure, Arafat authorized the payment of all security forces' salaries by direct deposit. "When the time came to do this, he was a very pragmatic person and knew when to let go," Fayyad said, adding "there were countless tense moments along the way, but especially in hindsight, it felt like the president was less annoyed than amused by my obsession with the matter, not to mention my antics. He certainly could have blocked it." By the end of the following month, all branches were using the new system.

This reform was Fayyad's second success in improving management of the security sector payroll. Fayyad had included in the 2003 budget law a provision that required that the shekel be used as the reference unit of account for the purposes of both budget preparation and budget execution instead of using US dollars for one and shekels for the other. With the stroke of a pen, that step eliminated the authority to set exchange rates in ways that enabled administrators to capture some of the money rightfully due to personnel. The Security Financial Administration could no longer use that tactic to divert payroll money into nonpayroll uses, including unlawful personal enrichment.

Reforming procurement

The next step was to introduce competitive bidding. Fayyad had included in the 2003 budget law a provision to extend the PA's existing procurement legislation—which required competitive bidding—to cover the security services. The legislature had laid the groundwork for that move in 1998, when it enacted a law creating a directorate for procurement located in the finance ministry.

Pointing to that authority, Fayyad insisted the finance ministry control the security services' purchasing, and the procurement department at the finance ministry began overseeing the security services' purchasing operations and publicly advertising tenders.²⁷ In order to buy anything, the Security Financial Administration had to inform the central procurement committee, which included representatives from other ministries. The committee would then publish an advertisement announcing the tender.

Introducing competitive bidding struck against al-Sakhra, the state-owned enterprise that had been the security services' sole supplier and was under the personal control of the head of the Security Financial Administration. Al-Sakhra received bulk procurement contracts, usually including more than one item, from the Security Financial Administration without other vendors' having the opportunity to compete.

Fayyad required the ministry's procurement department to unbundle all purchase requests in order to create separate contracts for specific categories of items. "You could, in theory, be doing public bidding for procurement, but it would be a sham, because one bidder always wins," Fayyad said. Now, distinct categories of items—such as cheese, meat, or boots—were opened to separate bidding.

The change opened the door for smaller businesses to bid on the contracts, which reduced opportunities for corruption and put money into the pockets of a broader group of Palestinian suppliers. The effect was immediate. Once the bids were unbundled, al-Sakhra submitted bids but failed to win any contracts at all, Fayyad said, whereas businesses around the West Bank and Gaza gained new contracts with the security forces. "The barriers to entry disappeared," Fayyad said. "It was now possible for the corner bakery to actually bid on government business rather than sell to al-Sakhra, which would then have turned around and sold the same items to the security services at highly inflated prices." The total cost of procurement also dropped, confirming Fayyad's suspicions that al-Sakhra had charged above-market prices.

Some security chiefs complained to Arafat, claiming that the new system created shortages of equipment and supplies. But Fayyad rejected those complaints, asserting that the PA was buying all it could for the security forces given limited funds. "What you're hearing are complaints about things that either are not under my control or are related to [the chiefs'] not having the freedoms they did before," Fayyad remembered telling the president. "We simply don't have the resources they're looking for to fund all these things."

But Fayyad was not done with al-Sakhra. By June 2004, the onetime procurement monopoly's business had dried up and it was essentially out of

business. That month, Fayyad ordered a special-purpose audit of the once-powerful enterprise.²⁸ The audit report identified control weaknesses that included the signing of blank checks, lack of documents to support various financial transactions, and an unclear basis for payroll calculation and benefits. The report also detailed misuses of funds, including unjustified perks to the general manager and financial manager. Revenues recorded elsewhere as having been paid to al-Sakhra were not received by the company, instead going into other bank accounts, including, in one case, the general manager's personal account. The audit led the PA to shut down the company.²⁹

OVERCOMING OBSTACLES

By March 2004, Fayyad had achieved full implementation of the direct-deposit system for the security forces, but that did not mean that all resistance to it had been overcome. In his office in Ramallah, he received a phone call reporting a shooting inside the Arab Bank branch in Gaza City. Not long after that, he received a message from Arafat in the form of a fax sent from a security officer in Gaza with the report of the shooting, with Arafat's notes to Fayyad written in the margins: "Doctor Salam, didn't I tell you that paying through the banks does not work for security services?"

That day was a payday for security workers, and Fayyad was immediately skeptical of the report. "I calculated that it was contrived," he said. "This was something the security people had concocted in order to demonstrate that paying security services through the banks doesn't work."

Still, Fayyad was worried. He had received many notes from Arafat and said he could discern from the handwriting—in particular, the multiple question marks—that the president was furious. Fayyad was worried that officers who were angry about losing their ability to profit from the cash payments might push the president to change his mind. But the more he thought about Arafat's message, the more hopeful he became. The president had not instructed him to change anything but had merely expressed his displeasure.

Fayyad thought that if he stuck with his decision, he could weather the storm. He called one of the security chiefs whom he knew to be close to Arafat. He acknowledged the report but told him there would be no change in procedures—that the next month, all security personnel would still receive their money through direct deposit. The policy remained in place.

Another kind of resistance was more difficult to deal with, however. During the more than one and a half years it had taken to fully implement the payroll reform, some of the security chiefs had taken preemptive steps to exercise the discretionary decision-making power they would soon lose, adding about 3,400 personnel despite a hiring freeze mandated in the 2003 budget law.³⁰ Fayyad and others believed that the chiefs had replaced the fake names on their payrolls with the names of real people so they could continue to receive the same amount of payroll funding and obscure the fact that they had used fake names in the past. "We didn't know whether the names [provided were] real or not," Azmi Shuaibi, at the time a leading reformer in the legislative council, told the World Bank.

“We wanted to undertake an audit of all the names to make sure they were real, but the resistance we faced was too strong.”³¹

Fayyad said he was not surprised by the maneuver. “During this period, while we were working on the reform, there was a clearly determined effort to hire people who would not otherwise have been hired. I strongly expected it was going to happen.” Placing more people on the payroll helped disguise the magnitude of past misappropriation of personnel salaries.

Fayyad also concluded the chiefs possibly had another motive for the additional hiring, as they started to feel the inevitability of losing the battle to perpetuate the status quo. “They knew very well that the minute the payroll reform went into effect, they would no longer be able to hire or promote even one officer without prior finance ministry approval, and that was a big deal.”

In his December 2003 budget speech to the legislative council, Fayyad criticized the failure to abide by the budget law.³² He conceded that the suspected payroll juggling probably diminished the savings he had hoped the PA would realize as a result of the reform. However, he viewed the situation as a modest price to pay, in the short run, for the reform’s ultimate success. Plus, aware that any investigation was unlikely to do much good anyway, Fayyad decided to move on. He said that underpayment of actual security service employees was more common than fake names on the payroll, and his priorities were to ensure (1) that people received their full salaries, (2) that the full range of corrupt practices associated with administration of the payroll completely disappeared, and (3) that finance ministry control over security sector hiring was fully asserted and exercised.

ASSESSING RESULTS

Fayyad’s reforms helped usher the PA into an era of more-responsible, more-credible, and more-transparent government. Improved financial management of the security services saved money overall, reduced opportunities for corruption and misuse of funds, and increased donor confidence in the PA.

By 2004, Fayyad had achieved his two main goals in reforming financial management of the PA’s security services. All branches had joined the direct-deposit system, meaning that more than 50,000 security sector workers were receiving their salaries via electronic transfers to legitimate bank accounts rather than relying on their local commanders to pay them in cash. Fayyad’s reforms placed the security forces’ procurement operations under finance ministry control and required competitive bidding for specified amounts of supplies and equipment, which reduced costs and led to the shutdown of al-Sakhra, the state-owned enterprise that had held a lucrative monopoly. Doing that opened the door for businesses around the West Bank and Gaza to win PA contracts, which helped support small businesses, whose only way to deal with the Security Financial Administration had been through al-Sakhra.

International donors cheered the reforms and allowed financial assistance to continue flowing to the PA. Those external partners also became more

comfortable engaging with the PA when they trusted the PA's financial management and could follow how the government used the funds it received.

A World Bank team that tracked the PA's performance on financial management during 2003 and into early 2004 applauded the procurement reforms and the extension of payroll direct deposit to members of the security services.³³ However, the team also reported that control over security service recruitment was still a work in progress, citing limits on hiring that were less stringent in the security sector than for civilian employees—a likely reference to the formalization of roughly 3,400 additional personnel in early 2003, before the reforms were completely in place. The team also said that as of early 2004, there was still no comprehensive database of personnel that included all of the security services, including those under the president's purview. Fayyad said there *was* a database but that the information linking names to banking information still resided in the Security Financial Administration and not in the finance ministry.

After Fayyad's resignation in 2005, before the 2006 elections, there were further efforts to place more security personnel on the official payroll. Fayyad and others referred to these appointments as an effort to “unload” supporters onto the government payroll. The acting finance minister received requests to clear the additions and was under the impression that they had prior approval.

REFLECTIONS

Looking back on the reforms he implemented from 2002 to 2004, former Palestinian Authority finance minister Salam Fayyad was acutely conscious of the length of time it took to push them through. “Chip away, chip away, chip away,” Fayyad said. “Eventually it worked.” But the time he spent building pressure for change gave resistant security officers an opportunity to cover their tracks and hide the extent of their malfeasance prior to reform implementation. Fayyad could not always act directly. Instead, he found ways to apply increasing pressure on the president and the security chiefs to implement the reform agenda. It was an imperfect solution, but Fayyad thought it the best possible strategy for success at that time and under the circumstances.

Fayyad believed the reforms benefited the Palestinian cause. It was important to emphasize that the government would ultimately have more money if there was less corruption and that people on the ground would receive their full salaries instead of losing some of their money to their commanding officers. Fayyad also benefited from pressure exerted both by people in the streets—including protests against corruption in the PA—and by international donors. In the end, it was the combination of those factors that resulted in change.

For Fayyad, it also was important to appeal to human, personal needs. He said it was demeaning for hardworking people to have to line up to get their pay from a commanding officer and feel obliged to him personally as well. He found this a powerful argument when talking about the need for reforms in the payroll system.

“There's nothing that resonates better than issues related to human dignity,” he said. “It's a very delicate chord in the way we humans are configured.”

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