PALESTINIAN PENSIONS

Whilst a longstanding and challenged pension scheme exists for public sector employees and security forces of the Palestinian Authority (PA) in the West Bank and Gaza (Palestine), there is no pension provision for the vast majority of private sector employees, who rely instead on highly-problematic and generally-insufficient end-of-service payments from employers. This briefing provides a full analysis of existing pension arrangements, including those of private sector workers who have been employed in Israel, and charts the efforts of the last decades to improve the situation. It summarises the existing issues that the current reform process needs to overcome in order to succeed.

Overview

Pensions exist within the wider set of social security, protective insurance and welfare systems that help ensure economic and societal stability, such as unemployment benefit and sickness payment provisions. Pensions, the focus of this briefing, entail specific personal financial arrangements that provide income during retirement or disability. They can be contributory, namely when one or both of the beneficiary and their employer make regular financial contributions, or non-contributory schemes, which are usually state-funded, offering a basic safety net.

Palestine

- ~3.3m Palestinians in the West Bank
- ~2.2m Palestinians in the Gaza Strip
- 37% of the population is under 15 years old
- 4% of the population is 65 and above

According to the Palestinian Central Bureau of Statistics (PCBS), the global Palestinian population is around 14.5m, of which some 5.5m reside in Palestine, evenly distributed by gender. An important measure for pensions is the old-age dependency ratio, meaning the percentage of over-65s relative to those of working age (15-64). In Palestine, as seen in Figure 1, this ratio has consistently risen, along with the overall population over 65. In 2022, the ratio was 6.12%, a 37% increase since 2000 and of 19% from 2010. Whilst low compared to many developed countries, it is comparable to Jordan (6%), a more relevant benchmark. This means that while the Palestinian population is quite young today, it is aging – making now the ideal time to set up a pension system.

Another relevant factor is unemployment, which is high, particularly among the young. This marks a significant challenge for any pension scheme, given that it limits the number of contributors. About two-thirds of waged private sector employees in Palestine lack a formal contract[2]. In 2022, about 40% received less than the statutory minimum wage, of 1,880 NIS (about $500) a month, although that figure was 89% in Gaza compared to 19% in the West Bank.[3] Only 26% have contributed to a pension fund or received end-of-service benefits, which is the main benefit foreseen by Palestinian law. Unemployment in 2022 was 24%, which comprises the Gaza Strip's 45% and the West Bank's 13%. The rate is higher among females, at 40%, compared to 20% for males, and running at a chronic 48.3% for female youth. An important group is the approximately 193,000 Palestinians who worked (before October 23) in Israel or the Israeli settlements, of which 58.6% had work permits.

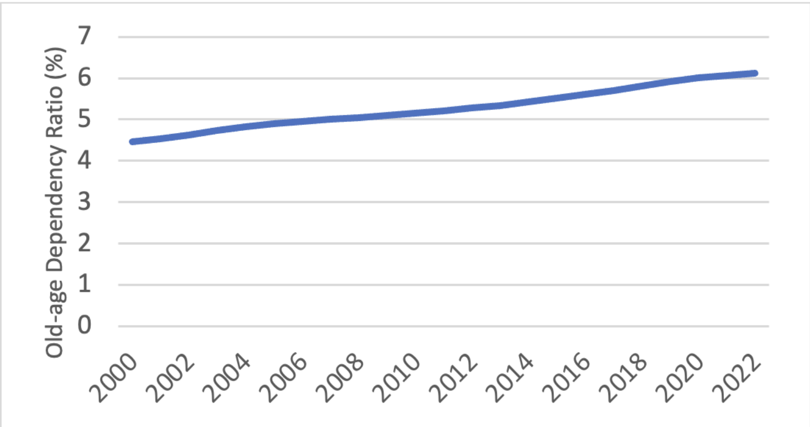

Figure 1: Old-age Dependency Ratio in West Bank and Gaza (%)
Source: World Bank

As in most countries, informal employment (Figure 2) is not covered by current pension plans. This was 53% of employment in 2023,[4] and three quarters of the employment increase in 2021.[5] 52% of waged employees are informal (53% in the West Bank and 48% in Gaza).[6] 49.5% of self-employed and business owners engage in informal activities (45% in West Bank, 65% Gaza).

Public Sector Pensions

The existing pension scheme, which is for public sector employees, is run by the Palestinian Pensions Agency (PPA). The statutory retirement age is 60 with a minimum of 20 years service for males, and 55 with 15 years for females, or 50 with a minimum of 25 years service for males or 20 for females. The PPA administers four different schemes. Two are inherited from the Jordanian[7] and Egyptian West Bank and Gaza administrations, another for the civil service, and a fourth for the security sector. 2021 was the end of a 15-year transition period from this highly-fragmented setup to the unified pension scheme established by Law No. 7 of 2005, covering all civil servants and security forces born after 1 September 1961, as well as employees of the Palestine Liberation Organization (PLO) working abroad not participating in any other scheme. It is noteworthy that it has run a deficit from the start. It has three components, of which one is for welfare (a monthly payment of 700 NIS for former public sector workers and security forces who do not qualify for a pension). The second is a Defined Benefit (DB) component, and the third Defined Contribution (DC).[8]

The difference is crucial. In a DB scheme, an individual's retirement benefits are based on a formula using their salary and number of years working and contributing. Under the new scheme established in 2005, the PPA pays 2% of the average salary over the three years before retirement, multiplied by the number of eligible service years. This sum is paid as a monthly lifetime pension, so individuals know in advance how much they will receive. The contribution rate is 7% of wages for employees, and 9% for employers. Whilst in theory the DB scheme is fully-funded, meaning an employee's benefits should be financed through their accumulated contributions and the return on that investment, in reality, only a fraction of those contributions have historically been transferred from the PA to the PPA, resulting in the deficit and dire financial situation, dependent on the PA's general budget.

By contrast, in a DC system, which has become more prominent globally in recent decades, the level of benefits is not pre-defined, but instead depends on accumulated contributions and the proceeds generated from the invested pool of savings. Like the DB scheme, assets and contributions mainly accumulate on paper, but are not actually transferred to the PPA. Benefits are paid as a single lump-sum which is equal to total employer and employee contributions, without interest. The contribution rate for the DB scheme, for both employers and employees, is 3%. Employees can use 50% of their DC savings as collateral for bank loans.

The PPA manages a combined (DB and DC) investment portfolio of around \$303m,[9] invested in financial markets. Returns from the DC pool go to the DB asset pool. In 2021 around 67,000 individuals aged 65 or over received 1.8b NIS of benefits from the PPA (some 36% of the 65+ population), whilst just 147,000 (13% of the active labour force) contributed to it, which should have been 1.5b NIS for the DB. In 2022 the PA Ministry of Finance transferred just 5% of the contributions due to the PPA, increasing arrears and meaning most pensions were paid directly from the PA budget rather than PPA funds.

The sustainability of the public sector pension fund has been continually questioned. According to the Ministry of Finance,[10] arrears in the civil servants fund will reach an alarming \$3b in December 2024. No data is available for the security forces fund. This amounts to one third of the PA's entire public debt, equivalent to 22% of 2022 GDP. The issue became particularly acute in 2021, compelling the PPA to utilise its

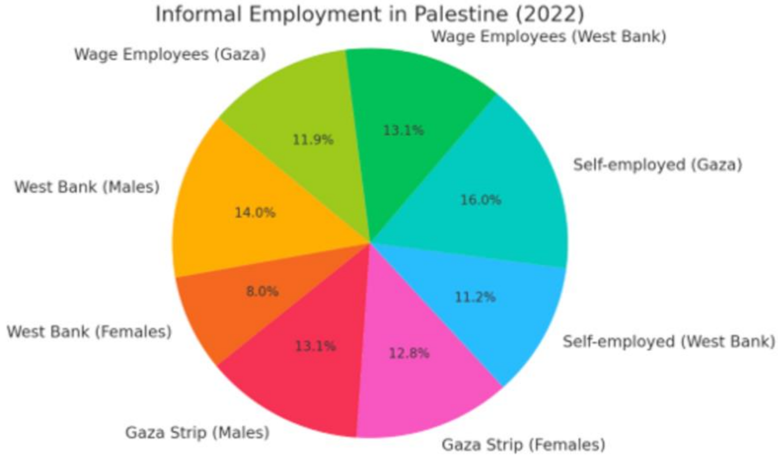

Figure 2: Informal Employment
Source: PCBS 2022

own resources to finance retirement benefits from January to September, some 500m NIS.[11] These large arrears from the PA to the PPA have made the scheme highly dependent on the PA's liquidity. Consequently, fluctuations in the PA budgetary situation directly impact the stability of the pension scheme. In 2021, the PA had a $940m deficit. It implemented salary caps and, in January 2022, pension benefits caps of 80%. This led to reduced payments to public sector employees and further increased arrears to the PPA. Despite reducing the deficit to $564m in 2022, the PA continues to cap pension payments, and the public pension scheme is expected to remain a significant burden to the economy, with costs representing 3% of GDP, illustrating that pensions paid from the DB scheme crucially depend on the PA's finances as the system's ultimate guarantor. The World Bank published a new report in September 2023 outlining several recommendations in response to this state of affairs.[12]

Private Sector Pensions

No widespread or national pension scheme exists for private sector employees. Some employers have established voluntary provident funds, which collect contributions from the employer and employees and provide each employee with an individual account. The fund's annual financial return is distributed to members' accounts according to size, and they pay out a lump sum at the end of employment.

The vast majority of private sector employees therefore have no pension, including those in civil society institutions. They do have some broader social security rights under Labour Law No. 7 of 2000, which mandates employers to directly fund annual paid leave, employment injury, paid maternity leave and paid sick leave, as well as an end-of-service severance payment. The amount of this depends on employment length, with those ending their employment after fewer than five years entitled to one third of their most recent monthly wage per year of employment, and those with between five and ten years entitled to two thirds of the same. Those with the same employer for at least ten years are entitled to one month's wage per year of employment. If the employment was involuntarily ended, workers are possibly entitled to up to three months' for each year of employment depending on circumstances.[13]

Thus today, Palestine loosely operates under this employer-liability model, so the financial and cashflow risks for these payments fall squarely on private employers. These indemnities are only available to waged workers. Excluding the public sector, this was 77% of all waged workers in 2022,[14] however, only 36% of workers with an employment history actually received this indemnity.[15] An additional 22% accepted an end-of-service payment below their entitlement due to the daunting prospect of long, costly litigation, often as a result of non-compliant employers potentially breaching the Labour Law.[16]

Working in Israel

A different situation exists for West Bank and Gaza Palestinians working in Israel and the settlements, some 193,000 prior to October 2023. Pensions, as well as other social security for Palestinian workers employed in Israel, is covered by the economic section of the Oslo Accords. Under the Paris Protocol, Israeli employers are required to deduct income tax and social security contributions from Palestinians' wages as per the Israeli laws covering pensions and benefits such as employment-related injuries, maternity leave and health insurance. Israel is mandated under the Protocol to transfer 100% of the deducted income tax for workers in settlements, and 75% for those in Israel, to the PA, as well as most of the health deductions, since those workers are ineligible for health services in Israel. However, in practice, this has been subject to repeated and growing political blocks, delays and deductions.

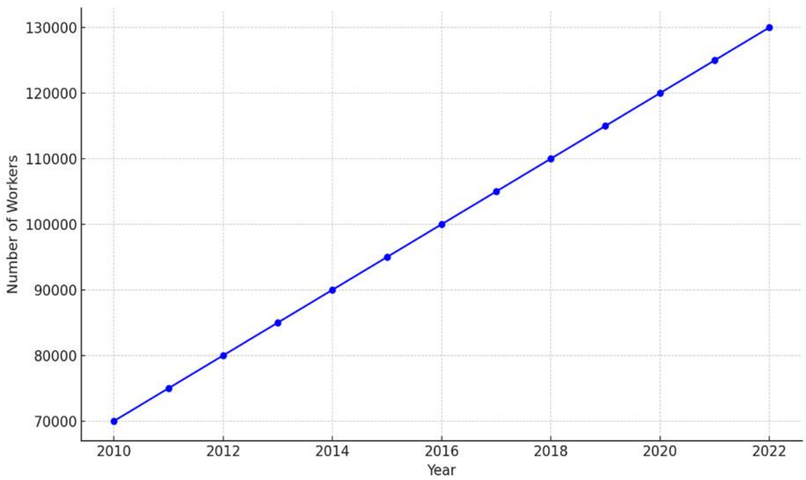

Figure 3: Number of Palestinian workers in Israel (excluding the settlements)
Source: PCBS 2022

However, the additional deductions, many of which derive from industry-specific arrangements such as in construction and agriculture, where most Palestinians worked, are not transferred. These deductions include 2.5% for sick pay, 4% for annual leave, and 1.3% for disability pensions in construction. These funds are generally transferred to the Israeli Ministry of Finance, and in 2010 the Israeli comptroller estimated their accumulated total in 2019 to be around NIS 500m (some $150m).[17]

Israel also retains the deductions made for pension contributions, which are held by the Israel National Insurance Agency (INSA). Under the Paris Protocol, Israel agreed to transfer these funds to the PA upon establishment of a pension insurance institution to manage the transferred funds. This was a primary driver behind the PA's various legislative efforts, set out below. However, to date, this vehicle has not been established. Accumulated funds at the INSA are estimated to be approximately $1.5b as of 2017. As a result, many Palestinian workers have not received benefits. In August 2020, responsibility for these savings was handed over to a private Israeli pension fund called Amitim, which was tasked with managing $0.89b of savings. This marked a change from treating the funds as capital savings to retirement savings.[18]

PA Reform Efforts

There have been various efforts over the last twenty years to set up a formal, contribution-based private sector pension scheme in Palestine. The first version of the social security law was in 2003, set for launch in 2007. This was suspended due to World Bank concerns over sustainable funding and high enforcement costs,[19] as well as strong private sector opposition primarily due to the requirement for employers to make pension contributions to the social security fund beyond the end-of-service provisions of the 2000 Labour Law.

A second attempt, Social Security Law No. 19 of 2016, was even more controversial. Despite being drafted with the International Labour Organisation (ILO), it faced criticism for lack of transparency and insufficient stakeholder involvement, and encountered substantial resistance from both employers and employees,[20] ultimately leading to a decisive halt to implementation when the law was suspended in June 2019.

The most significant effort to revive the reform project since then was in March 2021, with the First National Conference for Social Dialogue, which sought to recognise the need for a more transparent and inclusive approach to such pivotal laws. The conference initiated a comprehensive dialogue on social security involving the PA and representatives of private sector employers and workers. Progress since has been slow, with a new public consultation in 2023.

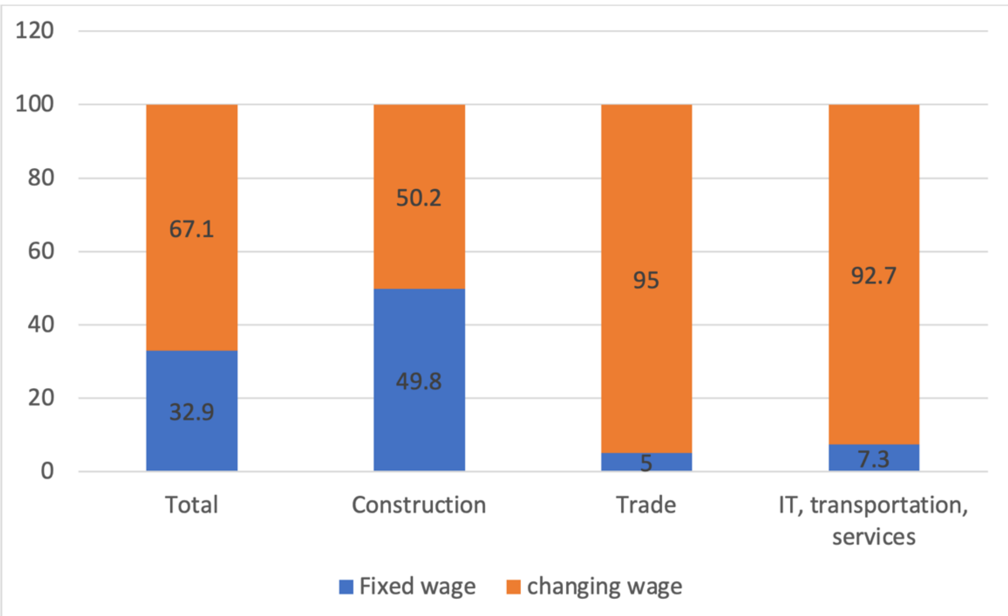

Figure 4: Distribution of Informal Sector Workers in Palestine by Economic Sector
Source: PCBS 2022

Why Was the 2016 Law Abandoned ?

A primary reason was the financial burden on employers, both mandatory contributions to the social security fund, and the payment of a minimum wage.[21] The latter was a significant concern given that around 19% of the West Bank labour force were then earning less than the minimum wage.[22] On end of service payments, the law, as validated by the Palestinian Supreme Constitutional Court in 2019, stipulated employers must pay all staff members a full month's wage for each year of employment, regardless of the duration of their tenure.[23] This posed a threat to the stability of many businesses, particularly smaller ones.

Another crucial obstacle was a pervasive lack of trust in Palestinian institutions, such that employees were deeply sceptical as to whom they could reliably entrust their retirement savings. A survey by Palestine Economic Policy Research Institute (MAS) showed that only 34% of employers and 19% of employees believed the law should have been implemented, citing lack of trust in the administration of the fund as a key reason.[24]

The PA's deteriorating fiscal position compounds these challenges. In 2021 it faced a severe fiscal crisis, which has worsened since, with budgetary pressures on basic operational continuity requiring it to borrow heavily from all available sources, leaving employees fearing that their savings might see a similar fate.

A further reason was the limited representation of workers in reform discussions, and only partial familiarity with the law. While labour unions were actively involved before and after the law's enactment in 2016,[25] most salaried workers had no affiliation, with union membership rates a mere 13% inside the workplace.[26] A survey by MAS showed a correlation between familiarity with and support for the law, with 44% of workers unfamiliar with the law at the time of its suspension, and only 21% familiar.[27] This absence of adequate worker representation contributed to widespread street demonstrations.[28]

The Current Proposal for the New Law

The new proposed Social Security Law is based on the outcomes of the 2021 Conference and was put out to a widespread public consultation in 2023. Its ambitions, as with the 2016 law, were wide, including national insurance for work injuries, maternity, unemployment, health and sick leave. It sought to address previous concerns, eg by lowering the contribution age, enhancing the system's financial sustainability, raising public awareness and prolonging the transition period for businesses. As a result, a new transition period was introduced[29] An entirely new institution, independent of the PA, was proposed to oversee all these new provisions: the Social Security Corporation (SSC).

The below further analyses the specific provisions for the main, mandatory DB pension scheme, including disability, and the supplemental, voluntary DC pension scheme. Coverage is proposed for all waged workers in Palestine not already covered by the public sector scheme, with further discussions taking place to consider others, such as those working fewer than 15 days per month (who under this law are not considered waged); but it is not proposed for those informally employed. In addition, Palestinians working abroad, outside of Palestine and Israel, will have the option to participate by making full contributions equivalent to those of the employer and employee.

The baseline age for drawing a pension under the new law is set at 60. Individuals aged under 21 when it comes into effect will become eligible at 63, and that age increases by one year every 15 years. To be eligible for the full pension, an individual must also have contributed for at least 180 months. Early retirement is possible from the age of 55 (or 58 for individuals under 21 at the time the law comes into effect), provided men have contributed for at least 300 months, and women 240. Workers in high-risk professions (to be defined by the Council of Ministers in the future) can retire at 50 if they have contributed at least 240 months. Individuals with disabilities can retire after accumulating 120 months of contributions.

The Main DB Scheme

Contributions are 6.2% of an individual's wage for the employee and 9.8% from the employer, who is responsible for providing the necessary data and SSC registration and the transfer to it of monthly contributions. Contributions are exempt from income tax and there is a cap of ten times the minimum wage. Non-compliant employers will be fined, with proceeds going to the DB fund.

Benefits upon retirement will be calculated with an accrual rate of 2% of the average wage over all contribution periods for each year of contribution, adjusted for inflation. Early retirement results in a penalty of 6% of the monthly amount for every year prior to the statutory retirement age. Apart from early retirement or disability, a minimum benefit level is guaranteed of 75% of the minimum wage or the poverty line threshold, whichever is higher, for individuals who have contributed 15 years. Each additional year of contribution increases the minimum 1 percentage point a year, to a maximum of 85%. Those reaching 60 who do not qualify due to a short contribution period are entitled to a lump sum payment equal to total contributions (both employer and employee), adjusted for inflation. Benefit adjustments will occur yearly, based on decisions by the SSC Board of Directors. The adjustment will not exceed the rate of inflation or wages, whichever is lower. In case of death, heirs become eligible, provided the beneficiary was drawing their pension, had contributed for at least 12 months, or at the time of death had contributed for at least 60 months. Any remaining funds go to the DB fund.

The Supplementary DC Scheme

The voluntary DC scheme is open to anyone living in Palestine, employed or not, as well as to Palestinians abroad. It involves individual accounts, and those not employed in Palestine can set their own individual contribution rates. Investment returns are credited to the individual member's account and contributions, benefits and investment returns are all tax-exempt. On retirement, contributors choose between a lump sum payment of contributions plus investment return, a lifelong annuity, or scheduled payments for a fixed period. If the contributor dies before retirement, their estate is entitled to the full amount in the personal account, plus a funeral grant equivalent to three times the statutory minimum wage.

Also, employers must contribute monthly the end-of-service benefit provision into the DC fund, rather than, as is currently the case, setting it aside internally. Employees earning above ten times the minimum wage can contribute the excess part of their wage to the DC scheme, and employers are required to contribute 9.8% of the excess wage if the employee contributes 6.2%.

The SSC

The SSC will be responsible for implementing the Law's provisions and those related to social security under the Paris Protocol, and so manage both the DB and DC schemes. It will operate as a separate legal entity independent of the PA with two branches: operations and investment.

The SSC's Board of Directors, which will be responsible for drafting laws related to social security, will be chaired by the Minister of Labour and is made up of representatives from the Ministries of Social Development, Finance, National Economy and Labour (in addition to the Chair), seven workers' representatives nominated by trade unions and other federations, five representatives of the Federation of Palestinian Chambers of Commerce, Industry and Agriculture (nominated in consultation with other organisations), and one independent financial expert nominated by the Council of Ministers. Board member appointments will be limited to four years and require approval by the Council of Ministers. The Board elects two Vice-Chairs from the representatives of the employers and employees, also four-year terms, once-renewable. Board members will be required to declare any conflicts of interest.

The Board will establish an external technical committee consisting of subject matter experts to provide input on matters such as investment management, governance structure and financial reviews, as well as a General Manager (GM) and a Director of the Investment Department. It will issue investment instructions, including strategic allocation. There will be internal committees for audit, risk management, investment and governance, appointed to four-year terms. It will provide quarterly reports to the Council of Ministers and Legislative Council, detailing investment performance and other relevant factors.

The Board will also establish an Investment Committee (IC), which will be responsible for proposing an investment strategy and policy to the Board, to be reviewed annually. The IC will consist of one representative from each of the PA, employers and employees, who will themselves select one of the three as Chair. It will also include the GM and three non-SSC financial experts, nominated by the Board. The Investment Department will handle investment-related activities and manage the portfolios of all SSC funds. The selection of external asset managers will be conducted through open and legally-compliant tendering processes. Initially, there will be limited investment allowed in foreign markets. An international actuary will review the financial positions of all SSC funds at least every three years. If that indicates estimated contributions and investment returns for the next ten years are less than ten times the estimated expenditure for that period, the Council of Ministers is required to take steps for legislative amendments, such as adjustments to contribution rate, retirement age or benefit level. If assets fall short of estimated liabilities, the PA must provide loans to cover the SSC's shortfall.

The PA's New Revised Proposals

Following the 2023 consultation, the PA issued a draft law with revised proposals, ongoing in 2024. These included wider social security measures, such as a new unemployment benefit, not covered here, although as they flow through the SSC, they are relevant, especially for sustainability and governance questions. On pensions, it seeks to address employer concerns and amend the transition period, rates, governance and other issues.

Employers had important concerns about both the DB mandatory contribution rate's link to the minimum wage (given so many do not pay it), and also severance payments during the transition period. These have been partly addressed. The minimum wage requirement remains, but the revised draft law includes an extended five-year transition period, providing the private sector with additional time to adapt. Also, it no longer mandates private businesses to transfer accumulated end of-service funds to the SSC. The financial burden is further eased, particularly for smaller businesses, by extending the grace period. The contribution rates have also been adjusted. Employees would now contribute 6.2% (down from 7%) and employers 9.8% (up from 9%), which many small businesses see as a substantial financial burden.

There is also a revised DB calculation for payments on retirement, which was previously based on average wage over the employee's last three years of service, and could lead to disadvantage in the event of any sudden income drops in a contributor's final years. The new draft is based on the average wage over all the employee's contribution periods. Newer discussions are also considering a dual-method approach, with a view to using whichever yields the most for the worker.

Concerns about sustainability have also been partially addressed, as the PA will now act as a guarantor, covering any potential SSC bankruptcy or default on payments. However, as the PA's fiscal condition has worsened, the credibility of this guarantee remains highly questionable.

Addressing governance-related concerns, the new draft places the SSC and its funds under the supervision of the State Audit and Administrative Control Bureau, as well as the Anti-Corruption Commission. Also, IC membership is expanded from one to two independents, and a consultative committee, composed of five financial and investment experts, will be formed to advise the SSC Board on investment matters.

Efforts were also made to enhance worker awareness and representation, with a national four-month marketing and media campaign, supported by the ILO, rolled out in 2023 to raise employees and employers awareness, which held 203 meetings with workers and 113 round-table discussions with employers.[30]

On governance, there was pressure to reduce PA representation on the SSC Board, specifically from five seats to two, to be filled instead by subject matter experts, and to change the Chair from the Minister of Labour to an independent representative. This discussion remains unresolved and has raised significant concerns among workers, employers and other stakeholders. General uncertainty over the capacity in the PA to ensure adherence to laws, regulations, and the directives of oversight bodies, including the absence of an active parliamentary system and a robust, independent judicial system in the PA compound this. A particular concern given the fiscal crisis is that the PA may simply use a decree to bypass legislation that prohibits the fund from lending to it. The transparent reporting of investment results and accounting, especially concerning the individual DC accounts, is also an ongoing issue.

Ideally, the fund would be managed by an independent entity, free from political influence, responsible for safeguarding the contributions of workers and ensuring their investment and management in the best interest of beneficiaries, so reducing potential for conflicts of interest, promoting transparency and fostering trust. Keeping a Minister as Chair will be seen to compromise independent decision-making.

Conclusion

Significant progress has been made over the last three years to try and establish a new pension scheme for private sector workers. However, the PA's deep and ongoing fiscal crisis, and the pension scheme's institutional connection to it threaten to undermine trust and sustainability in any such expansion. Also, the plans do not cover the informal sector, where a majority of Palestinian workers are employed, and may not be the optimal organisational setting to absorb the long-term pension savings set aside in Israel for West Bank and Gaza Palestinians that worked there. The continued setting of private sector pensions within broader and ambitious social security reform may also be to the detriment of narrower pension reform. In the meantime, most private sector employees continue to rely on end-of-service benefit provision which is often not enforced. Unfortunately, the history of pension reform in Palestine has been marked by failure. Any design needs sustainability of funding, viable enforcement, transparency and sustained stakeholder engagement.

The new draft law addresses many of the concerns raised since 2016, and considerable strides have been made to make it more inclusive and participatory, reflecting the input directed from independent experts, as well as a nationwide campaign to raise awareness and understanding. While the problem of funds withheld from Palestinian workers in Israel remains unsolved, the PA has, in the face of persistent scepticism and opposition, shown commitment to establishing a comprehensive system.

Done well, establishing a sustainable, comprehensive pension system for private sector employees in Palestine would be one of the most beneficial long-term reforms the PA could make, not only for the wellbeing and long-term financial benefit of Palestinian workers and the elderly, but also for the Palestinian economy generally. A solid pension system would boost financial market development, help reduce budget deficits, encourage long-term saving and build, over time, a domestic capital stock for long-term infrastructure and other investments. This is an aspirational and realisable objective the international community should heavily support.

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For full referencing, please see the website version of this note, on the Portland Trust site, at https://portlandtrust.org/publications/

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[30] Private source involved with the campaign.