

**An-Najah National University
Faculty of Graduate Studies**

**Municipal Bonds as a Tool for
Financing Capital Investment in
Local Government Units, Palestine**

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Municipal Bonds as a Tool for Financing Capital Investment in Local Government Units, Palestine

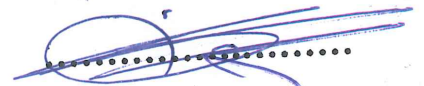
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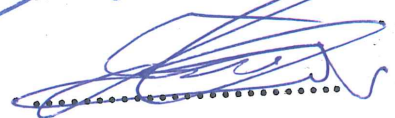
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Dedication

This dissertation is dedicated to my family and my parents for their endless love. I deeply appreciate their boundless support, particularly through the darkest times. I am sincerely proud of my lovely mother, whose love and passion have lifted me up when I were down. I am greatly indebted to my great father, Dr. Abdallah Hamdan Awad, who has always been a constant source of encouragement and inspiration. Gratitude is also extended to my sisters and to my brother Zaid for the help they had given me without waiting for any return.

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الاقرار

أنا الموقع أدناه مقدم الرسالة التي تحمل عنوان:

السندات البلدية كأداة للتمويل
الرأسمالي في الهيئات المحلية الفلسطينية

**Municipal Bonds as a Tool for
Financing Capital Investment in
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Abbreviations

Avg	Average
IFMIS	Integrated Financial Management System
IPSAS	International Public Sector Accounting Standards
KPIs	Key Performance Indicators
LGPA	Local Government Performance Assessment by the World Bank
LGUs	Local Government Units
MDLF	Municipal Development and Lending Fund
MoFP	Ministry of Finance and Planning
MoLG	Ministry of Local Governments
MSRB	Municipal Securities Rulemaking Board
PCBS	Palestinian Central Bureau of Statistics
PCMA	Palestinian Capital Market Authority
Pex	Palestinian Exchange
PIPA	Palestinian Investment Promotion Agency
PNA	Palestinian National Authority
PMA	Palestinian Monetary Authority
ROA	Return on Assets
SDIP	Strategic Development and Investment Plan
SEC	Securities and Exchange Commission
VAT	Value Added Tax
WSRC	Water Sector Regulatory Council

**Municipal Bonds as a Tool for
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Abstract

Municipalities are the public institutions that are responsible for providing services to citizens. Capital development projects are on the top priorities of municipalities. Such a priority is very demanding and critical due to the investment required, this is in addition to the scarcity of revenue sources in conjunction with the increased population. In Palestine, the trend of revenue per capita is decreasing in 73% of the sample municipalities. Thus, employing new ways of financing can be the solution. The percentage of employing debts at the Palestinian local authorities is very few. Accordingly, there is a room for using debts in certain circumstances as a new financial instrument with a debt limit according to the legislations and regulations. Municipal bonds have been used worldwide to finance capital investments at the local government units. This research concentrates on the determinants of municipal bond issuance, types of bonds, bond sale methods, debt maturity, par value, and risk-return relationship.

The purpose of this research is to develop and to find methods for assessing creditworthiness that are suitable and applicable to local government units in Palestine. The sample was composed of 11 municipalities in the West Bank.

Various variables such as macroeconomic and municipal status variables are identified to measure the effect of issuing municipal bonds on financing capital investment projects for the local government units in Palestine.

The study of the Palestinian economy has taken into consideration the following factors: historical interest rates, international financial position, external debt and general budget structure. Moreover, macroeconomic variables have been measured by revenues and expenditures per capita, cost of labour and unemployment rate. Municipal status variables have the following subgroup variables: municipality size, financial reporting quality, outstanding debt, and financial distress. Various financial ratios are used. Furthermore, comparative and cross-sectional analysis has been conducted besides horizontal and vertical analysis; the analysis for these ratios has been carried out to determine the municipal status variables.

The research concludes that macroeconomic variables and municipality status affect the issuance of "municipal revenue bonds." Based on testing the methodology, three municipalities are recommended to issue revenue municipal bonds.

Keywords: Municipal bonds, Issuance, Palestine, Municipalities, Revenues, Transfers, Grants, Debt, Budget, Deficit, Financial status, Creditworthiness, IPSAS, Disclosure, Strategic plans.

Chapter One

General Framework of the Study

1.1 Introduction

Municipalities are the main Local Government Units (LGUs) in Palestine. The abundance of financial resources affects the sustainable development of the local units; therefore, attention should be given to supporting the municipal development projects. Budget deficit that results from the lack of financing is the primary obstacle that hinders the implementation of Strategic Development and Investment Plans (SDIP), and the improvements of local government units and municipalities.

Revenues of municipalities are classified into three resources: operating activities, government transfers and grants or loans. Operating activities are assigned to municipalities by law. Whereas, central government transfers include transportation fees, property, and occupational license taxes. While the third resource comes from grants or loans.

The municipal revenue sources come from external sources except for self-financing sources that come from the internal activities of municipalities. The internal sources of revenues are generated from taxes, licensing fees of buildings, water tariff, connection fees, rent of owned properties, electricity, and other special fees from libraries, parks, zoos, and cultural centres.

Municipalities budgets vary from one to another since some of the Palestinian municipalities own and operate electric and water services, while others do not. Water and electricity provide cash to the municipalities and exaggerate their budgets.

One of the reasons for the recent economic decline is that LGUs cannot depend on the availability of assets grants and borrowing to finance their infrastructure needs (Vazquez, 2015). Thus, reform of the local government finance system is a precondition for the success of municipalities in Palestine (The World Bank, 2017). The Lack of the financial securities in Palestine threatens most of the LGUs. Financial securities are the most effective methods for funding development projects and improving the quality of the municipal services. Among the various types of securities are municipal bonds which contribute significantly to optimize revenues of municipalities (Ramazanov & Grigorian, 2015). Municipal bonds are issued by LGUs to fund activities that aim to fulfill civic duties and public goods.

According to the Palestinian Capital Market Authority (PCMA), corporate bonds have been issued four times before the year 2018; these issuances are to be explained in details. Also, bonds are included in the law of financial securities. According to the instructions for issuing securities, municipalities are authorized as the issuers of securities (PCMA, 2008). Moreover, bond issuers are delegated to issue bonds based on these

instructions. However, municipal bonds are not mentioned in the financial regulation system for the local government units in Palestine.

Although bonds, in general, are not realized as a common culture for both issuers and investors, the researcher is looking forward to achieving a Palestinian bond market since the increased financing to local government units by issuing bonds would be beneficial regarding portfolio diversification and financial market revival (Bajo & Primorac, 2010). Municipal bond markets are considered as an essential source for financing the operating lease, maintenance, construction of capital investments, and providing cash flow for services of pivotal public projects (Adelino, Cunha & Ferreira, 2017).

According to Horizon for Sustainable Development, a recommendation has been given to investigate the viability of issuing municipal bonds for capital investment projects in Palestine (Horizon, 2009). Using municipal bonds requires analysing the conditions before their issuance, this is in addition to analysing their effects on future investments for the LGUs in Palestine. This study concentrates on the specific requirements and procedures that have to be taken into consideration when issuing municipal bonds. By conducting financial analysis, the researcher examines employing municipal bonds as a tool for economic development projects of LGUs in Palestine.

1.2 Statement of the Problem

Municipality's development projects are diminishing due to the lack of revenue sources. For instance, operating activities lead mostly to cash deficits. Also, central government transfers account for 15% of the total revenues (ARIJ, 2009). The problem of government fund transfers is consistency, for example, in 2015 the percentage was 15.5% of total revenues and reached to 17% for the years 2016 and 2017. Loans can be used under many conditions; they are usually used for the short-term borrowing. On the other hand, revenues from grants are stable, but the population is increasing and so their needs. The average of grants for the years 2015, 2016 and 2017 was 5% of total revenues and 4% of total expenditures (MDLF, 2017). According to Sawafta (2011), revenues for municipal projects should progress by the passage of time.

Borrowing from commercial banks or issuing bonds might be better options for local governments. Bonds are beneficial because local governments receive the required funds directly instead of the gradual and the usual disbursement procedure of banks. Furthermore, financing by bonds is better in terms of time and interest by the average of two or three percentage points (Farvacque-Vitkovic & Kopanyi, 2014). Thus, the researcher suggests using municipal bonds as a way of financing since they can finance long-term capital projects which are chosen through feasibility studies. Municipalities are the suppliers of bonds, but individuals and financial institutions (investment funds, insurance companies, social

security funds, and commercial banks) purchase those bonds depending on supply and demand.

According to Bajo and Primorac (2010), the issuance of municipal bonds is the easiest way to avoid taking loans from banks, and thus to attract a large group of investors. By issuing bonds, LGUs get an immediate access to the private capital market. Among the conditions for issuing municipal bonds is the analysis of the project's financial sustainability (Farvacque-Vitkovic & Kopanyi, 2014). Sustainability of the project is the revenue generating ability. This ability depends on municipal sustainability plan which intends to maintain the same infrastructure service levels without any impact on tax rates or the service itself (BMA, 2017). The goal of the public entities is to provide adequate economic services for inhabitants (Kablana, 2013). Palestinian people live under Israeli occupation; Palestinian National Authority (PNA) has full civil and security control over 18 percent of the West Bank (Area A), whereas areas B and C have other restrictions for development (The World Bank, 2017).

The legal framework of the Palestinian economy is still under development. The research sheds the light on the determinants of the Palestinian municipality's bond issuing since bonds are needed to achieve a strategic growth in the coming decades. Thus, this study questions the creditworthiness of municipalities and it sheds the light on the applicable measures in Palestinian local government units.

1.3 Objectives

Much research has been done on Municipal bonds issuance. The topic has been tackled generally and broadly. Thus, this research concentrates on features of issuing municipal bonds based on key performance indicators (KPIs) of LGUs, particularly in Palestine. Furthermore, it reviews the municipal bond tactics so as to determine the suitable characteristics of bond issuance for the Palestinian capital market. Municipal bonds are introduced by using the most relevant variables and their ratio level of measurement to achieve the main goal of financing capital investments for municipalities. Thus, this research encourages spreading the culture of municipal bonds based on the financial analysis and scientific methods. Also, it emphasizes the additional requirements of the legal framework.

1.4 Research Questions

Municipal bonds have diverse elements. Accordingly, this study makes a connection between local governments investment needs and municipal bonds issuances. The researcher raises the following key questions:

- ❖ Can municipal bonds solve the financing obstacle for development projects of the local government units in Palestine?
- ❖ What are the most suitable characteristics of bonds for the Palestinian environment?

- ❖ Do macroeconomic variables affect the issuance of municipal bonds that are measured by revenues, expenditures per capita and the cost of labor, and unemployment?
- ❖ Do municipal status variables affect the issuance of municipal bonds which have subgroup variables as municipality size, financial reporting quality, outstanding debt, and financial distress?

1.5 Hypothesis

Neither macroeconomic variables nor municipality status affect the issuance of "municipal revenue bonds" which are targeted to finance capital investments of local government units in Palestine.

1.6 Legal Framework

Defining the determinants of municipal bonds issuance in Palestine is not an easy task; it requires a study that should be conducted to examine the legal environment that includes all related laws and instructions. The results of this study show that there are no special instructions for municipal bonds. However, municipal bonds are considered as financial securities, their issuance can be guided by the instructions of issuing financial securities. Policymakers may make special instructions and debt controls for municipal bonds issuance. It is the Ministry of Local Governments' (MoLG) responsibility to define the ways of permissible finance for LGUs; a designated instruction for the issuance of municipal

bonds can be publicized from the MoLG. New instructions may be coming after the year 2018.

Following is a summary of the laws in Palestine that are related to the topic of the research:

1. Law of LGUs in 1997: This law manages and determines municipalities' functions. It allows loans as it is stated in article (21): "LGUs can borrow funds from any financial institution after getting the approval of the minister of LGUs. If the loan requires the custody of the Palestinian National Authority, the approval of the board of ministers is required" (LGUs' Law, 1997).
2. Elections for local Authorities, 1996 Law: This law manages the elections of mayors and council members; LGUs mayors should be elected every four years. Accordingly, the mayor can be nominated for two elected periods. In other words, the maximum legal elected period will reach up to eight years.
3. Financial Law of LGUs: Since 1999, this law has organized the financial system of managing the Palestinian local government (Jaber & Sabri, 2007). Municipal bonds are not mentioned in the previous editions. This financial system has a new draft that is edited in 2017 and it has not been publicized yet.
4. Companies law in 1964: It defines bonds in general as it is stated in chapter 6, and in article (88); it also clarifies the certain approvals

needed for the issuance of bonds. Moreover, the forming of bondholders' committee which aims to defend the rights of the bondholder with the issuer is explained in article (96).

5. Palestinian Monetary Authority (PMA) Law in 1997 No. (2). According to article (6) of this law, PMA has the responsibility of bonds issuance and management. In article (7), PMA can buy or sell bonds to banks, individuals or to other entities in order to achieve the desired monetary policy. In article (35), PMA works for PNA as a financial agent in marketing, managing and transferring bonds and debt securities issued by the PNA and the public institutions.
6. The Securities Law No. (12) in 2004: it defines bonds as the securities issued either by a public shareholding company or by government agencies or public enterprises.

Article (71) of this law discusses bonds guaranteed or secured by a movable or an immovable property. If the bonds are secured by either the movable or the immovable property, or by other in-kind property, or by others types of collateral, guarantees or mortgages, that property and funds shall be placed as a security for the bonds, properly documented prior to the completion of subscription and prior to the deposit of the subscription proceeds pursuant to applicable legislation.

In Article (32), the law explains the conditions of the private placement.

7. Securities Issuance Instructions: issued in 2008 by the Palestinian Capital Market Authority (PCMA), and it was done pursuant to the Securities Law No. (12) in 2004 which has been explained before. In 2008 instructions, article (2) stated that government institutions and municipalities were authorized as issuers of securities (PCMA, 2008).

Article (31) explains some steps that the issuer of securities should follow to obtain private issuance. Article (32) listed the private issuance attachments required with the prospectus. The prospectus is the written document approved by the PCMA.

The prospectus is kept with PCMA. It includes complete disclosure of the information that allows the investor to make investment decisions (PCMA, 2008). The issuer should have details on investing issuance returns according to the strategic plans. Furthermore, projects could be evaluated by capital budgeting methods such as: internal rate of return, net present value and payback period.

Securities Issuance Instructions and other laws define the related functions terminology as follows:

"Issuance Agent: Any person licensed by PCMA to sell securities on behalf of the issuer.

The Custodian: The legal person who provides custody services in securities.

Underwriter: Any juridical person licensed by PCMA to purchase the issuer's securities for the purpose of reselling them.

Issuance Manager: Any juridical person licensed by PCMA to practise functions of securities issuance management and marketing on behalf of the issuer.

The Trustee: The body corporate licensed by PCMA, and it is responsible for the proper preservation of securities.

The Public Institutions: The public enterprises that the government owns in whole or in part or it exercises control over them.

After defining the related parties, this research proposes that the licensed companies in 2018 to conduct financial activities in Palestine; they could help significantly in issuing municipal bonds, each with its special purpose license (PCMA, 2018):

Table 1.1: Palestinian Licensed Companies in 2018

#	Company name	License
1	Lotus Financial Investment Co.	Issuing Agent
2	Al Wasata Securities Co.	Issuance Trustee Issuance Manager
3	Al Arabi Investment Group Co.	Issuance Trustee Issuance Manager
4	Sahem Trading & Investments Co.	Issuance Manager
5	Abu –Ghazaleh Consulting	Issuance Manager
6	Ithmar Invest	Issuance Manager
7	Bank of Jordan	Custodian
8	Arab Bank	Custodian
9	Bank of Palestine	Custodian
10	National Bank	Custodian
11	Cairo Amman Bank	Custodian Issuance Trusteeship

Source: PCMA, 2018, [https://www.pcma.ps/portal/english/Securities/ Licensees_sec/comp_2018_sec_eng.pdf](https://www.pcma.ps/portal/english/Securities/Licensees_sec/comp_2018_sec_eng.pdf)

Chapter Two

Theoretical Framework

Strengthening municipalities is vital. Thus, various policy choices that take into consideration the local needs and preferences can be very effective when they are taken at a local level (ARIJ, 2009).

The implementation of service delivery is left to the local level authorities because they have more experience in this aspect. LGUs consist of municipalities, village councils, and joint service councils. The primary purpose of LGUs is the provision of services, while the purpose of companies in the private sector is profit maximization (Kablana, 2013). Municipalities' major concern is not achieving profits, thus; the percentage of profits cannot be used as a "criterion for determining the success of a public government's management" (Eren, 2009, p. 3). What matters is to ensure that revenues and expenditures are used in the most effective way. The effective use can guarantee the healthy functioning of the budget, proper accounting, and efficient financial control system (Kablana, 2013). Consequently, the management of expenditures efficiently leads to the elimination of any unproductive expenditures and to a better understanding of managing the scarcity of public resources (The World Bank, 2017).

2.1 Municipal Bonds

Municipal bonds are debt obligations issued by LGUs (Maverick, 2015). A municipal bond is an obligation of a local government unit to

repay the specified debt on a specific maturity date including the stated or the formula-based interest rate (Dirie, 2005). In a municipal bond, the investor loans money to the bond's issuer in return for an agreed number of interest payments over the period that may take years (SEC Bulletin, 2012). The end of this debt period is the bond's maturity date in which the issuer of the bond repays the principal. Municipalities occupy an expensive function which is the capital infrastructure projects. The outcomes of municipal bonds lead to a fair distribution of costs over the project useful life due to use of the installment method in repaying the debt (Vazquez, 2015).

Debt ratios measure the efficiency and the size of the short and long-term debts. According to the level of service provided, the explanation of the results of the analysis differ. For instance, a municipality is in a good financial position when it has a low debt service ratio. In other words, a municipality can finance most of its projects internally. However, there is a controversial catastrophic reason of the low debt ratio is that the municipality delays the development of its capital projects and infrastructure.

Bonds are divided according to maturity dates into the following: short, medium and long-term bonds. Short-term bonds take one to three years to mature. While long-term bonds need ten years for maturity and the medium term bonds from four to seven years. Some countries consider one

to five year period as short-term bonds, and the ones which take more than ten years as long term bonds.

The interest on municipal bonds is exempt from the income tax as a general feature (Maverick, 2015). In Palestine, the tax exemption will be disposed of the first issue of municipal bonds. According to the tax benefits, the interest rate for municipal bonds is usually lower than the interest for taxable fixed-income securities of the corporate bonds. Reducing the cost of the interest requires applying the aggressive repayment strategies (BMA, 2007). There are cases in which the interest is paid in advance; it is subtracted from the loan occasionally so that the issuer receives fewer funds than the demand (Gitman, 2004).

According to the Securities and Exchange Commission, municipal bonds are classified to the following types:

- ❖ General obligation bonds are backed by the government's taxing power. The government has the authority to tax residents in order to pay bondholders, that is; the issuer's "full faith and credit" (SEC, 2010). A municipality's response to its economic environment is more important in assessing the riskiness of its general obligation bonds than the independent consideration of the accounting ratios (Wescott, 1984).
- ❖ Revenue bonds are supported by revenues from capital investments such as rental or lease payments, user charges or toll fees (SEC,

2010). Bonds are repaid by revenues that come from projects upon completion. Revenue bonds are designed to finance specific, designated public projects that generate discrete streams of income, such as toll roads, bridges, tunnels, airports, parks, ports, water, and sewer systems (Joel, Ronald & Larry, 2010). In Palestine, the most applicable projects are the ones that take advantage of the existing land. Municipalities assets possess the lands available for parking lots, museums, highways, water and sewer systems, parks including playgrounds, cycling tracks, in addition to parks of new modern types such as aqua parks, zoos, and flower parks.

These bonds are paid solely from the income generated by the particular capital project (Joel, et al, 2010). This income generally covers the cost of the bond which consists of the principal and the interest. Revenue bonds often have protective covenants written in indentures. These usually demand establishing sinking funds, in other words; bondholders have recourse to the physical assets negotiations in case of default. Accordingly, revenues are treated as mandatory payments that must be made to 'sinking funds' or pools of money set aside from taxes or other revenue sources to repay debt obligations. Debt management strikes a balance between the sinking fund at maturity to equal full principle and the last payment of interest. Some revenue bonds are “non-recourse.” In other words, if the revenue ends, the bondholders do not have a claim on the underlying revenue source.

Revenue bonds are all about recovering funds from the executed projects. Such projects will not be approved without conducting feasibility studies that demonstrate the viability of the projects. The flow of funds is of a critical importance; when assessing revenue bonds, pledged revenue could be on gross revenue or net revenue, and after expenses, which is a promise that net revenues will be used for payment of debt service.

In revenue bonds, investors often require special covenants and pledges. For example, when bonds are issued to finance a series of projects undertaken by the same revenue stream, current revenues should be adequate to cover a specified percentage of both current debt service and future maximum annual service for both the outstanding bonds and the new bonds. These are preconditioned terms; none of these sorts of revenue covenants may be modified or abandoned by the bond issuer (Joel, et al, 2010). The following shows other examples of covenants that are included in revenue bonds:

- A rate covenant could specify user charges.
- An insurance covenant helps to determine how both the physical asset and its cash flows are to be repaid.
- A maintenance covenant helps to conclude that an asset should be kept in state of good repair.
- A non-discrimination covenant helps to specify that all users of the facility must pay user fees except in times of emergency.

Other security features of revenue bonds include requirements for financial reports, outside audits and restrictions on the issuance of additional bonds like project completion to protect the rights of the current bondholders.

Issuing bonds is a complex procedure; it requires preparing good data, disclosing the issuer's financial and economic information, and having information about the market to certify that the issue is placed at favorable terms (Farvacque-Vitkovic & Kopanyi, 2014). Many parties could take the responsibility of issuing municipal bonds; the assignment of responsibility between the various parties requires a decision by the municipality. Thus, financial managers, internal auditors and the manager of projects at the municipality are all responsible for the issuance of revenue bonds. To conclude, the elected municipal council does not interfere in the issuance of revenue bonds due to the fact that the elected members may be changed before repaying the debt, so it is not preferred to delegate them the responsibility of issuing the municipal bonds. For instance, if the municipal council issued revenue bonds for ten years, and the council won twice, it would leave the municipality before the maturity of these bonds, then the principal and interest might be lost without any control. It is probably favourable to start with conservative restrictions and reduce them by the time (Vazquez, 2015). This study concentrates on the most conservative ways to initiate issuing municipal bonds in Palestine, taking into consideration the prior experience and the best practices employed around the world to prevent defaults.

The main borrowing criterion for LGUs is that the operating revenue should not exceed the operating expenditure (Bajo & Primorac, 2010). Accordingly, issuing municipal bonds has become a popular method for financing the deficit of local budgets. The issuance of bonds has not been targeted to generate revenues but to replenish the local budget (Ramazanov & Grigorian, 2015). As a preventive factor, bonds should be issued to initiate an investment project (Samonikov, Veselinova, Fotov & Gruevski, 2016).

Ramazanov and Grigorian (2015) state that the use of market instruments for municipalities should be associated with the decision made on issues related to the local value of the fund raised, construction, apartments' purchase, housing for the poor, municipal service vehicles, and infrastructure utilities. Objectives included in SDIP should be linked with the budget preparation to ensure that the prioritized projects are not just as a shopping list, but they are realistic like the availability of the financial resources, time frame, institutional qualifications, and legal and human capabilities (Horizon, 2009).

For investors, municipal bonds remain one of the most and the least-risky investment. Bonds do not tend to offer extraordinarily high returns, so a bond's purchaser usually seeks a fixed stream of income payments in comparison to stock investors. Municipal bonds help investors to do diversification in portfolio management which aims to reduce the risk.

Even in tough times, municipal bonds have a low rate of default. When the default occurs, it usually results from bonds that fund hospitals or housing projects. Municipalities in Palestine are more concerned with infrastructures such as streets, tunnels, sewer networks, solid waste disposal, slaughterhouse, water supplies, transportation, fruits, vegetable markets, and parking taxi complex rather than housing projects (Rubenstein, Willoughby & Lipar, 1999).

The assessment of risk is based on the economic and financial conditions of the local government, past fiscal indicators, structure of debt, pending payments and future factors that may affect the creditworthiness of the local governments (Farvacque-Vitkovic & Kopanyi, 2014).

Investors of municipal bonds face some risks. Litvack and Rizzo (1999), demonstrate that unique characteristics of municipal assets and unpredictable political processes have made municipal bonds never risk-free. Borrowing at the local level can be risky since local managers can overspend and attempt to shift the repayment of debts to future governments and taxpayers (Vazquez, 2015). However, municipalities are required to use their resources in the most efficient way (Kablana, 2013). SEC (2012), explained the risks of municipal bonds as the following:

- ❖ Interest rate risk: The bond's market price has an inverse relationship with the interest rates, while one moves down, the other rises. So that the market value of the bond may be more or less than the par value. Investors who hold a low fixed-rate municipal bond and want to sell

it earlier than maturity could lose money due to the lower market value of the bond.

- ❖ Call risk: refers to the possibility of an issuer to repay a bond before its maturity date. The issuer may take such a decision if the interest rates decline. Bond calls are less likely when interest rates are stable or moving higher.
- ❖ Liquidity risk: the risk in the municipal bonds occurs when there is no much trading in the secondary market. The liquidity risk is represented in the difficulty in selling the bond (Afshar, 2013). Thus, investors will not find an active market for the municipal bonds (SEC, 2012). There is a probability to prevent investors from trading bonds when they want a particular price for them because secondary bond's markets are thinner than stocks'.
- ❖ Credit risk: this refers to the risk that the bond issuers may face financial difficulties that make it impossible for them to pay interest and principal in full (the failure to pay interest or principal is referred to as "default"). The reason for municipalities' financial distress may be the financial commitments of citizens who do not pay periodically and consistently.
- ❖ Inflation risk: refers to the upward movement in prices. Inflation reduces the purchasing power. Such a thing constitutes a risk for investors who receive a fixed rate of interest over the long run.

However, it can also lead to higher interest rates and, in turn, lower market value for existing bonds (Lioudis, 2018).

- ❖ Political risk: Palestine is under occupation, and thus any political change is beyond control. The political risk could be managed and reduced by particular agencies that offer political risk insurance for long-term debts and equity investments such as Overseas Private Investment Corporation, and Multilateral Investment Guarantee Agency (PIPA, 2016).

2.2 Methods of the Sale of Municipal Bonds

In order to issue municipal bonds, the concerned party chooses between a competitive or a negotiated offering (Schultz, 2012). In a competitive sale, possible underwriters submit sealed bids of the bond offering with identified characteristics. If the offering is small, individual underwriters may handle the entire issues on their own. Syndicates of the underwriters will bid for more substantial offerings that promise to issue the bonds at the highest price or the lowest yield. Usually, LGUs sell their debts using the method of sale that achieves the lowest cost of borrowing (Johansen, 2014).

In a negotiated offering, the costs and characteristics of the bond will be agreed upon by the negotiation of the municipality with the underwriters or a group of them (Schultz, 2012). Underwriters can raise the interest rate on the bond. However, they do not act as fiduciaries which minimize risk.

Bond sale method takes into consideration various factors, including but not limited to rating, security and structure. The following are factors indicating a competitive sale (Johansen, 2014):

- Rating of the proposed bonds is expected to be in the better category.
- Municipal bonds come in two varieties: general obligation and revenue bonds. General obligation bonds are backed by the full faith and credit. Whereas, revenue obligation bonds are secured by a reliable, known, and long-standing revenue stream (e.g., water, sewer, and electricity).
- The bond structure is not expected to include “exotic” products that require extensive explanation to the market.

The majority of municipalities enjoy the characteristics listed above. Yet, about 80% of the bonds are still sold through negotiation (Johansen, 2014). The following are factors indicating a negotiated sale:

- Rating of the proposed bonds is expected to be in the lower category.
- Bond insurance or other credit enhancement is not available or it is not cost-effective.
- The bond structure has features such as pooled borrowers, variable rate debt, deferred interest bonds. Thus, bonds require an extensive communication with the market.

- The issuer desires to target specific participants such as disadvantaged business enterprises, retail investors or local firms.

Marlowe (2009) points out that a negotiated sale allows the underwriter to develop more intimate knowledge of the bonds in question, and to use this knowledge to advertise the bonds to the potential investors. He uses data on several million municipal bond transactions to test whether that negotiated sales are advantageous or not. The results suggest that under certain circumstances, negotiated sales are an effective tactic to reduce the information asymmetry. However, the reduced asymmetry does not necessarily indicate lower actual borrowing costs for most issuers.

If municipal bonds were issued for the general public benefit, many social goals would be achieved in accordance with citizen's satisfaction. In other words, there will be participation in decision making concerning which project to finance by the designated municipal bonds. LGUs are sensitive institutions in the public sector because they touch people needs directly. People are very close to the LGUs and participate in setting SDIP and the budgets.

2.3 Corporate versus Municipal Bonds, Financial Markets, Borrowing, Grants, and Ranking

Several features differentiate the municipal bond market from the corporate bond market. First, asymmetry of information is likely to be greater in the municipal market (Marquette & Wilson, 1992). Individual

investors constitute the greater part of the municipal market (Daniels & Vijayakumar, 2007). The individual investor's ability to analyse security is not as well developed as those of institutional investors. But among all financial markets, the municipal securities market has the greatest requirements of information (Feldstein & Fabozzi, 2008). Second, all trading in the secondary market occurs over the counter market. There are no organized exchanges for municipal securities as it is the case for corporate securities (Daniels & Vijayakumar, 2007). Unlike the corporate securities market, the underwriting process for the municipal bond market is regionally segmented. In some regions, regional firms still dominate the municipal market (Lamb & Rappaport, 1987).

The municipal bond market is considered less risky than corporate securities market (Marquette & Wilson, 1992). However, the default risk in the municipal bond market has been increased. For example, Detroit bankruptcy represents the most significant default in the municipal bond markets since the Great Depression (Schwert, 2015) . Based on these considerations, the poor condition of the local government balance sheets is the primary motivation for studying default risk in the municipal bond market. However, historically speaking, municipalities issued by traditional tax-supported governments have opted for low-risk investments (Garner & Paul, 2014).

In Palestine, PADICO's Holing has had two issuances of commercial bonds. PADICO's issuances are the biggest in amount. For example, in

2016 it issued commercial bonds with total value of (USD 120 million) (PADICO, 2016). These proceeds were used to repay its previous bonds issuance (USD 85 million), pay short-term loans to banks (USD 35 million), and to finance many other investments. These investments are considered long-term projects which take time before making any cash returns such as Jericho Gate, Power Generation, and Nakheel Project. Comparison between various companies in Palestine regarding the corporate bonds has been carried out and explained in details in Table 2.3.1:

Table 2.3.1: Corporate bonds in Palestine

	Name of the company	Year of issuance	Maturity	The amount in USD	Par value in USD	Guarantee percentage of assets or stocks	Interest
1	PADICO	2011	five years	85,000,000	10,000	125%	first 30 months= fixed interest of 5% annually 30 months lasted= LIBOR+ 2,5% semi-annually with a floor not less than 5% annually
2	APIC	2012	five years	20,000,000	10,000	125%	first 30 months= fixed interest of 5,5% annually 30 months lasted= LIBOR+ 2,5% semi-annually with a floor not less than 5,5% annually
3	PADICO	2016	five years	120,000,000	500,000	130%	first 36 months= fixed interest of 5% annually 24 months lasted= LIBOR+3% semi-annually with a floor not less than 5% annually
4	APIC	2017	five years	35,000,000	10,000	110%	first 30 months= fixed interest of 5% annually 30 months lasted= LIBOR+ 2,5% semi-annually with a floor not less than 5% annually

Source: (PADICO, 2012) (PADICO, 2016) (PADICO's Holding website).

One of the financial securities that is worth mentioning is Sakk, or Sukuk (the plural form of Sakk). Sakk is referred to as 'Islamic bond' (Afshar, 2013). It is used as a way of funding, and raising capital in the Islamic capital market (Alam, Hassan & Haque, 2013). Moreover, it contributes approximately to 14.3% of the global Islamic finance assets. Attention has now turned towards applying Islamic principles in equity markets (Naughton & Naughton, 2000). Thus, Sukuk are verified to have a positive effect on the Islamic capital market.

The major concern of a financing system is to find reasonable solutions for the existing problems (Afshar, 2013). There are great religious differences between Sukuk and bonds, but there are no financial differences. Under Islamic Law, *riba* or interest is not allowed in the financial system (Naughton & Naughton, 2000). One of Islamic principles is profit sharing and considering money not as an asset. Money is regarded merely as a medium of exchange, and it is viewed as a measuring unit of value (Afshar, 2013). Holders of Sukuks own part of the principal assets (Alam, et al, 2013). The nature of the conventional bonds does not allow such type of ownership since the instruments are considered as debt obligations. Bonds are based on debt security while the Sakk is based on the equity method (Afshar, 2013).

There are many benefits of municipal bonds over borrowing from a commercial bank. Comparison of bonds and bank lending have been indicated by the following:

- Most commercial banks concentrate on short-term borrowing, which is appropriate for incremental financing but not for long-term financing (Peterson, 2003). Generally, a bond is meant to finance long-term investments, whereas a bank loan is more suitable for short-term needs.
- Local banks satisfy liquidity needs and provide a set of banking services on a daily basis. Bank's loans are available for most municipalities. Regarding the market accessibility, the bond market is very expensive for the aspiring local governments.
- LGUs usually lack creditworthiness. In other words, they do not have enough financial abilities to repay the obligations to banks over time, and they lack technical capacities to manage the debts. Therefore, LGUs' borrowing capacity declines (Vazquez, 2015). In brief, creditworthiness of LGUs can be improved through more transparent budgeting and accounting, this is in addition to the development of self-sufficient sources of the local government revenues. A municipal bond market relies on the public disclosure of the financial information in addition to other types of information by the municipalities. Bond markets rely on credit rating agencies which employ extensive methodologies to assess the creditworthiness of issuers (Asher & Sheikh, 2012). Loan departments at banks are required to possess proprietary information, and to develop techniques to ascertain the creditworthiness.

- Banks must establish a ‘relationship banking’ scenario; however, purchasers of bonds are not obligated to have a long-term relationship with the issuer (Asher & Sheikh, 2012). Eventually, banks engage in a long association with municipalities whenever the need for capital arises. This relationship between the bank and the local government provides flexibility regarding loan conditions. Borrowers can pay off the loan partly or totally, at any time, with little or no warning. One of the shortcomings is that lenders can change the terms of the deal; however, borrowers can theoretically move their accounts elsewhere, assuming that another lender is available. In any case, banks are entitled to manipulate the lending terms.
- Flexibility and information encourage most local governments to use a bank credit. Standardization strengthens the ability to reach a wider range of investors, and it helps to reduce search costs. In addition, it is acknowledged that liquidity, and bond proceeds are immediately available to the borrower without any conditions and regardless of the timeline of project implementation.
- LGUs need to build up their reputation. Thus, the issuance of bonds protects them from the unilateral change in conditions since bonds issuance involves standardized terms and conditions; it depends on the terms from which the capital is borrowed.

Grant and debt financing mechanisms are essential for LGUs to support development. Debt financing has advantages over grants; debt

financing imposes an obligation of repayment (Asher & Sheikh, 2012). The revenue project is designed and executed to repay the obligation. Moreover, it is based on obtaining adequate revenues, minimizing operation and maintenance costs, and generating a surplus over these costs, which is considered the motivation over the lifetime to the asset created (GoI, 2011). On the other hand, grants tend to soften budget constraints, and they lead to wasteful expenditures. Moreover, the consistency problem dominates the donor funds.

Grants for the Palestinian municipalities come mainly from the Municipal Development and Lending Fund (MDLF) to support the implementation of all strategies for the local government sector. MDLF is the primary source of development-linked assistance to municipalities since it has been established in 2005. MDLF has implemented hundreds of projects with a value that has exceeded USD 400 Million (MDLF, 2017). The lending function is not yet fully developed at MDLF (Appendix 1, Interview 4). Moreover, it has not implemented an overarching policy strategy on municipal lending, including the identification of a sustainable revenue source for this funding (Horizon, 2009).

The grant allocation mechanism is the most important element of grants (MDLF, 2015). The performance-based formula determines the amount of the infrastructure grants to each municipality in Palestine. The allocation formula is 50% on performance, 20% for needs and 30% for the population. The Scale Ladder consists of 10 levels from bottom-up: (D, C, C+, C++, B, B+, B++, A, A+, A++). Within each ranking level, KPIs were

recognized to reflect the municipal performance in the target areas including financial management, planning, social accountability, and municipal services provision. The allocation of funds depends usually on ranks. In other words, municipalities with a good ranking deserve better funding than those with a poor ranking. A major benefit from the MDLF ranking could be used to extract municipalities' creditworthiness of bond issuance. Accordingly, MDLF might be considered as a bond trustee or custodian in the process of issuing bonds.

MDLF helps LGUs to improve their performance indicators; however, till the end of 2017, no municipality had reached A++ which is the highest ranking. In order to reach this highest rank, municipalities should achieve all 23 of KPIs -explained in Table 2.3.2. There has been a significant improvement since 2014 ranking, when no municipality had passed the B rank; all municipalities missed at least one performance indicator of the B rank. This incompleteness in the rank has led to a certain emphasis on not choosing the general obligation bonds since the foreseeable credit rating for municipalities will be lower than MDLF performance rank; if a municipality achieved the highest ranking of MDLF, it could be tested to assess the creditworthiness of the general obligation bond. Generally speaking, there are conditions on municipalities to be financed via municipal bonds. They should have the highest rank of MDLF performance; their ranking should be level A and above (Salfeet, Al- Bireh and Ramallah), this is in addition to the further examination of creditworthiness that shall be tested.

Table 2.3.2: MDLF KPIs

Ranking	KPIs
A Rank	1. A plan for roads and public construction in a place according to a computerized system. 2. Salaries and wages expenses are less than 45% of total operational and capital expenses. 3. The existence of a cost accounting system to provide tariffs. 4. Using an Integrated Financial Management System (IFMIS), and providing reports accordingly. 5. Substantial operation and enterprise account surplus (More than 15%). 6. Offering public green spaces and parks more than .5 m2 per capita. 7. Effective complaint systems working under the instructions of MoLG.
B Rank	1. Actual maintenance of expenditures not less than 10% taken from the operational expenditures. 2. Surplus in operational budget of 2016 (without enterprises budget). 3. Keep the net lending without any increase (water and electricity debts). 4. Unqualified external auditor opinion of 2016. 5. Performing 70% of the operational budgeting, actual operation revenues $\geq$ 70% of the budgeted operational revenues, actual operational expenditure $\leq$ budgeted operational expenditure. 6. Public disclosure of the external audit report of 2016.
C Rank	1. Increase in the collection of revenues from operations or revenues per capita above 50 shekels from revenue from services and licenses revenues. 2. Separate accounting for municipalities' business enterprises, revenues and expenses including bank reconciliation. 3. The actual statements of operations and sending them to the MoLG. 4. Fixed assets are registered and updated annually. 5. Public disclosure of municipal budget execution and strategic development execution. 6. Announcing a complaint system for the public.
D Rank	1. A separate bank account of water and electricity service. 2. Financial accounting policies and procedures. 3. Public disclosure of budgets, SDIP, and ranking.

Source: MDLF ranking, 2017

In 2016 ranking, all 11 sample municipalities reached B rank and above, so they achieved the low ranks implicitly in order to get the B rank. Disclosure of the financial statements is a must to get the B rank. Thus, several municipalities started disclosing publicly their financial statements.

The researcher has conducted a lot of search to find out the municipalities that have shown full disclosure on their websites. Unfortunately, the researcher has found that not all the municipalities have disclosed their information publicly. The strategic plans have not been disclosed even, despite the fact that this action is the minimum requirement to get the low ranking of D. It has been noticed that most of the municipalities publicly published their financial statements of 2013 and 2016 in order to conform with the minimum requirements of the MDLF ranking. But they did not publish the financial statements for the years in between since their goal was to answer the questionnaire by the surveyed municipalities. Disclosing financial information to the public yearly is a matter of the credibility and integrity. Among the sampled municipalities, only Bethlehem municipality has disclosed all the financial statements, in addition to its budget for the last five years on its website. Other municipalities disclosed their financial statements without the notes. The statements of the years required by MDLF ranking have been 2014 and 2017. Thus, if MDLF required the years in between 2016 and 2013, this would give positive results to the users of financial statements. Thanks to MDLF ranking that pushed 3 out of 23 performance indicators, KPIs that

were concerned about publishing and disclosures to the public are demonstrated in Table 2.3.2 with the rest of MDLF ranking indicators.

Rankings are considered as financial incentives that indicate a better performance. MDLF ranking asked for a complaint system to help municipalities get a better ranking. In Palestine, the overall satisfaction rate about the responsiveness of LGUs is low; it is less than one-third of the households agree that LGUs are very responsive to citizen concerns and complaints (The World Bank, 2017). For example, in Tubas, only 1 in 10 households agrees that their LGUs is very responsive. Whereas, in Tulkarm and Qalqilya almost half of the families agreed that their LGUs are very responsive (The World Bank, 2017). Local Government Performance Assessment by the World Bank (LGPA) suggests one shortcut for LGUs to collect more revenues from user fees, to increase responsiveness to citizens' needs. Per capita revenues are strongly associated with higher LGU performance. This statement affected one macroeconomic variable of revenue per capita.

The percentage of the disclosed financial items of the LGUs is approximately 56% for financial data and budgets, and 60% of LGUs disclose their performance rank (*This Week in Palestine*, 2011). Financial audits from external auditors increase the confidence in LGUS and their financial management. The auditor's reports and opinions afford a high level of accountability and credibility (Farvacque-Vitkovic & Kopanyi, 2014). Management attitude and corruption can be measured by applying

municipal administration financial expense ratios that result from transportation, travels, telephone calls, and hospitality expenses. These unproductive expenses should be decreased to the minimum. Thus, employing performance indicators in the public sector helps in evaluating the efficient performance which minimizes input for the given output.

Public sector entities are accountable to those who provide them with resources, and to those who depend on them to use those resources to deliver services during the reporting period and over the longer term (IPSASB, 2016a; Woldehawariat, 2017). In addition to financial and disclosure indicators, transparency and governance took place in the KPIs.

Transparency of a government is defined as the extent to which its information is available to the public. Transparency is essential to improve public confidence. Transparency quality of the reporting made by public entities is very crucial for public accountability. Disclosure ensures accountability of the public officials to report on the use of public resources and obligations, and thus to meet the performance targets which have been set (Bovens, 2007; Adi et al., 2016). Transparency affects the credibility of LGUs. Credibility supports the trust levels of financial securities among investors. Robbins and Austin (1986) point out that there is a significant relationship between the levels of financial independence and the disclosure of information.

The usual financial statements that are provided under the accrual basis of accounting include: financial position, financial performance,

statement of changes in net assets/equity, cash flows and notes to the financial statements, or annex (IPSAS 1). Whereas, for cash basis accounting the primary financial statements that are provided are: cash receipts and payments (IPSASB, 2016a; Woldehawariat, 2017).

Municipalities control significant resources. IPSASB encourages the disclosure of information about assets and liabilities to enhance accountability (IPSASB, 2017b). Noncash assets and liabilities will not be reported on the face of the statement of cash receipts and payments under the cash basis of accounting. However, municipalities maintain records, monitor their debt, and manage their liabilities, and assets. IPSAS for cash basis mentioned disclosure about restrictions on cash balances with their nature and amount. Available and restricted cash balances can affect entities access to borrowing.

According to Jaber & Sabri (2007), the percentage of employing cash-based accounting by municipalities is approximately 85%. Cash basis financial statements lack comprehensive information about LGUs. Furthermore, they do not demand allowance for doubtful accounts which gives the reason for municipalities not to chase their debts. The scope of the cash basis accounting system is narrow (Kablana, 2013). It does not show the underground and ground investments that are the critical function of the municipality. The fact is that the increase in fixed assets is higher than the increase in current assets which is considered to be normal for the public sector. Municipalities are part of the economic developments.

Therefore, they cannot be held far from the performance, customer satisfaction, cost, quality, efficiency and productivity criteria in the private sector.

IPSASB encourages governments to achieve a progress in the accrual basis of accounting (IPSASB, 2017 b). IPSASB has promoted for this type of accounting to be employed by local governments by publishing studies and articles.

The public has access to different types of media, one of them is websites which are used to provide public financial information. One of the advantages of using websites is flexibility of time as the public can access a website anywhere, so it supports the interaction between the public and LGUs (Sprecher, 2000). Several studies have been conducted about the use of websites for the disclosure of financial information (Laswad, Fisher, & Oyelere, 2005; Adi et al., 2016). Some researchers analysed the level of disclosure over the websites. Adi et al (2016) researched the quality of the content published on the websites to citizens. As a result, the variable of financial reporting quality has been developed to measure the disclosure of financial statements on websites.

The World Bank measured the performance of municipalities with many KPIs (The World Bank, 2017). The analysis focused on the drivers of local service delivery performance, starting from the size of LGUs (economies of scale), the level of income (GDP per capita), fiscal strength (revenues per capita, total revenues, expenditure per capita and total

expenditure), institutional capacity (planning and financial management, etc.), governance arrangements (transparency, accountability, and participation), and modes of service delivery with the enabling environment and institutional framework such as revenue and expenditure assignments, sector policy and strategies, and service standards. The emphasis was on the core services, (a) piped water supply, (b) wastewater management, (c) solid waste collection and (d) local roads (The World Bank, 2017).

In addition to the employment of fiscal strength to measure municipalities' performance the role of fiscal sustainability, proxied by indicators for satisfactory collection efficiency, and a necessary surplus in both operational and enterprise budgets, by holding both population size and geographical attributes fixed. On average, municipalities with satisfactory collection efficiency and own revenue sources, have a 5.6 higher performance score. On the other hand, municipalities with a surplus in operational and enterprise budgets achieve 5.4 points higher. According to data analysis from 2011 to 2014, total revenues per capita of municipalities that provide electricity services are four times higher than others who do not offer such services (The World Bank, 2017). Where a 1 percent increase in per capita revenues is associated with an on average 6.5-point higher performance score. Some municipalities justify the reason for this higher ranking to electricity providing service. As Salfet municipality serve the small population and still keep the cash revenues from electricity. Salfet municipality kept additional reserves while using

fund accounting. Fair comparison between LGUs is to divide the sector to cost centers according to service provision. In the year 2017, 55% out of Salfet Municipality revenues are from electricity. It is not fair to compare total municipality revenues while they are not providing the same services. In 2012, per capita operating revenues were NIS165 for municipalities

Highly populated municipalities are recognized to have a declining cost of infrastructure than others, a one percent increase in population density resulted in 3 points higher performance score (The World Bank, 2017). Global evidence suggests that there is a strong correlation between increased density and expenditure efficiency, which has been confirmed by LGPA (ibid, 2017). Per capita cost of service delivery increases with declining density, given that the 2 of households served is much lower in less densely populated areas. This has a direct impact on the capital and operating cost of infrastructure networks and service provisions, such as the water and sewage pipe meters, and operating hours for solid waste collection trucks that have to cover a large service area with few users.

Many ratings have been conducted on Palestinian municipalities. MoLG ranking depends on population; all sample municipalities are ranked in the first category by MoLG. Nablus and Hebron are considered highly populated municipalities; they are minimum two times higher than any other municipality from the sample. More will be explained about the sample in the research methodology. An analysis of the ranking for the center sample municipalities has been conducted in Table 2.3.3:

Table 2.3.3: Comparison of previous sample rankings

#	Municipality	MoLG Ranking	MDLF Ranking 2014	MDLF Ranking 2017	2017 KPIs out of 21	world bank performance score 2017	world bank performance Rank out of 380
1	Ramallah	A	B+	A+	19	80	6
2	Nablus	A+	B+	B+	13	73	18
3	Hebron	A+	B+	B++	15	72	23
4	Jericho	A	B+	B++	15	68	44
5	Jenin	A	B+	C++	9	45	41
6	Tulkarm	A	B+	B+	13	76	12
7	Qalqilia	A	B+	B+	13	79	8
8	Al- Bireh	A	B+	A+	19	80	7
9	Salfeet	A	B+	A	17	89	1
10	Tubas	A	B+	B++	15	55	144
11	Bethlehem	A	B+	B+	13	70	30

Source: (The World Bank, 2017), (MDLF website)

2.4 Municipality Financial Status in Palestine

Municipal budgets in Palestine have significantly declined over the last decade primarily due to the Israeli occupation. The contraction of the economy, high unemployment rate, poor municipal management, and a growing culture of non-payment; especially since the second Intifada (This Week in Palestine, 2011). The Palestinian financial municipal situation is very critical as many municipalities are unable to provide its staff with their salaries regularly (ARIJ, 2009). The decline in budget has resulted in budget deficits.

There is a difference between explicit and implicit budget deficits. Loans can cover the explicit deficit or by cutting some expenses. This would affect the quality of local services because this cut will be from the

operating and maintenance costs although it should be from the administrative and salaries expenses. However, the main concern is the implicit budget deficit, which forces municipalities to cut investments and projects and to decrease their improvements implicitly.

Palestine has 3% increase in population every year (PCBS, 2017), grants were considered stable in amount for the previous years by MDLF, so there is no matching between the increase in population and the need for municipal financing. The deterioration of municipal finances has led to a subsequent decline of service coverage and quality, ultimately negatively impacting the quality of life of most Palestinians (This Week in Palestine, 2011). Various achievements have improved the quality of services provided by municipalities. The water and wastewater services have been enhanced and developed in the last ten years. Many improvements are still in need; new water infrastructure is a top priority to reduce leakage to an acceptable level. Palestinians currently face a 90 MCM shortage in water, and estimation of meeting a 450 MCM gap by 2020 (PIPA, 2016). Projects like Rainwater dams and technologies for conserving agricultural water may be placed but need financing (PIPA, 2016). Wastewater is in a high need for infrastructure, in Jericho, nearly the half (54%) of roads have wastewater infrastructure by the year 2018 (Jericho SDIP, 2018).

Municipalities are forced to limit service provisions to the basic minimum due to the economic crises. The following are some facts on service needs in Palestine (This Week in Palestine, 2011):

- 26% of water supply network need maintenance;
- Municipalities have 82% of classrooms needed;
- Municipalities have only 46% of the required equipment;
- 52% of municipal roads are unpaved and require maintenance. 2 out of 3 households have access to paved roads (The World Bank, 2017)

Israeli occupation has led to many restrictions; PNA has full civil and security control over only 18 percent of the West Bank (Area A) and manages public affairs in around 21 percent of the West Bank (Area B), with security under Israeli control (The World Bank, 2017). The remaining 61 percent of the West Bank is Area C under full Israeli military administration. Population in Area C reached 279,000 (The World Bank, 2017). LGUs in areas classified as B and C face additional challenges, obtaining permissions for development as to Oslo Agreement is a hurdle to development needs. Construction and maintenance in area C require a permit and approval from Israeli occupation; this permit is extremely hard to obtain and may take years. They have less access to services and poorer quality for those available. They rely on outdated, deteriorated infrastructure, and when granted the limited number of additions and upgrades are wholly insufficient to address Palestinian's needs (The World Bank, 2017).

There is another major issue facing municipalities is the increasing of the total debt due to citizens (Horizon, 2009). According to BMA (2007),

on a yearly basis, a certain percentage of the citizens on a yearly basis is not able to pay municipal taxes which has caused debts. The increase of this percentage over time shall weaken the municipality's financial health. Moreover, as the uncollected taxes rise, liquidity decreases. Bad debt financial indicator calculates the allowance for uncollected taxes divided by the total operating revenues, this ratio purpose is to measure how much revenue is lost to the bad debt every year. If the allowance account exists, the ratio can be used. However, the allowance account does not exist in municipalities that use the cash basis, and so they can not determine the size of bad debt. Consequently, the use of the growth analysis is justified to reach the ratio for the collection rate of accounts receivables.

Ramallah municipality periodically evaluates the collectability of receivables owed to the municipality from citizens according to a specific policy set by the management. It takes the necessary provisions to address the risks of not collecting accounts receivable aging and to expense them as bad debts. The following table demonstrates the percentages of the outstanding debt payment in 2016 (Ramallah municipality audited financial report of 2016):

Table 2.4.1: Percent of accounts receivables allowance

Accounts receivables	Percent
> than one year and < than two years	20
> than two years and < than three years	40
> than three years and < than four years	60
> than four years and < than five years	80
> than five years	100

Source: Ramallah municipality audited financial report of 2016.

The debt that results from citizens who do not pay their taxes has grown to more than 100% of the annual budgets. This applies to the majority of the leading municipalities like Nablus, Hebron, and Gaza. Municipalities that have the highest collection rate would exceed 100%; 100% from years arrears and another 100% for the same years' taxes and charges. These two collection rates are mixed in municipalities and have to be separated in the future. Debt analysis indicates the component of water and electricity debts due to camps which should be transferred from the government. The collection rate goal for municipalities could be debts minus the camps charges, the amount resulted is the highest targeted collection rate, until the central government committed to pay for camps charges regularly. Horizon explained the low debt in some municipalities is due to the fact that its revenues include only taxes and fees but not charges for services because the municipalities do not supply them.

Citizens who do not pay periodically and consistently will not have clearance for their financial commitments unless they make complete payment of cash or checks, that is a considerable effort done by municipalities to reduce citizens debts (Swafta, 2011). The culture of non-payment in Palestine is prevalent (Appendix 1, MDLF interview), not only for citizens who do not pay their fees and taxes, but also for municipalities who do not pay their obligations of water and electricity bills, reaching to the higher level of central government which does not pay their rent expenses and the collection of property tax and transportation fees periodically.

The municipal financial data indicate that some municipalities which operate water and electricity services impose profits on the condition that they collect fees of the services from citizens. However, in other municipalities utility service provision is not cost-effective, and some utility services do not even cover their variable costs. Most Palestinian municipalities do not provide the electricity service, as it is delegated to distributing companies after providing assets and staff from municipalities. However, municipalities still have control over electricity in different forms; municipalities are now shareholders in those companies, continuing to receive cash dividends from electricity (The World Bank, 2017). The philosophy of the electricity income tax is to be argued. If the municipality is still producing electricity service, then the income generated is free from income tax, in contrast when municipalities transfer electricity to the distribution companies, the income is taxed before paying cash dividends to municipalities. These decreased revenues of municipalities and the increased expenses are for the benefit of the Palestinian National Tax Department. Additionally, electricity bills for municipalities include the Value Added Tax (VAT), at least electricity bills of municipalities should have zero VAT.

LGUs do not have effective instruments to encourage or nudge unwilling citizens to pay. Very few LGUs apply pro-poor payment modalities through payment plans or allow vulnerable citizens to pay reduced amounts. The lack of support from local councils to increase the willingness of citizens to pay, hinders efforts to increase citizen

commitments to pay for services (e.g., support enforcement or courts). Notably, not only individual users but also governmental institutions, do not pay for the services they receive from LGUs (The World Bank, 2017) .

The Qunaiby study reached to a positive conclusion: Palestinian municipalities who have high adherence to the municipal rules, laws, and regulations (Qunaiby, 2009). Most municipalities actually disclose their budgets to MoLG. The ministry applies a unified chart of accounts for revenues and expenditures since 2014 and it is obliged by the municipality to approve the municipalities budgets. According to our research, 82% of our sample approved their 2017 budget. Almost 64% of municipalities adopted the chart of accounts in their accounting systems for both actual and budgeted amounts (Jaber & Sabri, 2007). The next step is to use a unified chart of accounts and coding system for all accounts by all municipalities, for both budgeting and accounting systems.

Furthermore, most municipalities have applied new unified payroll system for the municipal employees. This unified payroll includes some financial commitments and unified organizational chart to stop the staff who works without a clear description of their job titles. Although amendments to this law were made, further work is highly needed to achieve justice. It is not clear why the municipal employees do not follow the same payroll system for the MoLG and the rest for the government. Application of the system is a precondition for approving the budget from MoLG. Some municipalities, especially with high numbers of staff, have

had problems in the application due to the difficulty in reducing premium allocated to the salary of the employees, in addition to the amendments to the instructions of the calculation. This new system was issued in 2009 with modifications across years. Such a thing has made it difficult for municipalities to commit; modifications have given some jobs premiums according to the nature of work and to the field specialty like engineering, in contrast, a reduction in existing premiums according to the scientific qualification like accounting. From our sample, Nablus and Hebron did not approve their budget of 2017, and Tulkarm did not send financial data.

According to the World Bank (2017), the collected local taxes and fees are supposed to be the main source of revenues for municipalities. It was estimated to be only 22% of the local government revenues for the period from 1995 to 2004 (Rubin, 1997). This led to a growing reliance on alternative revenue sources, such as user charges. User fees may be more reasonable to taxpayers since their costs are directly related to benefits received. In most cases, citizens can avoid the charges by choosing not to receive specific services. The main sources of revenue for LGUs are locally collected revenues that are comprised of: (a) user fees, such as payments for electricity, water, solid waste collection, and fees for public markets and slaughterhouses; (b) local fees, such as building permits and fees for signs; and (c) taxes (The World Bank, 2017).

LGUs depend heavily on user fees to finance operating expenditures, not to mention critical capital investments. On average, charges and service

fees account for 50–70% of total revenues, mostly from public utility services such as electricity and water, but also from charges for building permits, solid waste collection, signboards, and cemetery fees.

The property tax is the leading local tax, which forms about 18% of the total regular revenues of the Palestinian municipalities (Jabr & Sabri, 2007), in 2009 ARIJ result about the property tax was as an assertion by consisting 15% of total revenues. The property tax provides a distinct advantage as a revenue source by its stability in economic downturns and exportability through taxation of non-residential property (Monk, 1990; Bland, 1989). Gaza municipalities collect property taxes and professions license directly keeping 90% of their revenue and transfer the remaining 10% to the national government as expenses. In West Bank, the proportions of revenue distribution are the same, but the central government collects property taxes instead of the municipalities and later transfer their 90% that may stick a couple of years with MoFP (ARIJ, 2009; Swafta, 2011).

The sources of shared revenues which is centrally collected and then split between LGUs include property tax, occupational license tax, and the transportation fee (Swafta, 2011). The Ministry of Transportation collects the transportation fee, MoLG have control on 50 percent of the total revenue collected and then allocate to the LGUs on per capita basis. However, in practice, the Ministry of Finance and Planning (MoFP) intercepts the majority of the 50 percent share to compensate for the arrears, these arrears are usually related to electricity or less often to water

charges and referred to as “net lending,”. The net lending, includes “transfers to local government to cover clearances revenue deductions by Israel for water, electricity, and health and Ministry of Agriculture services” (Ministry of Finance, 2007). Net lending formed about 11% of the total current expenditures for 2000-2012 (Rizeq, 2015).

Property tax has traditionally been collected only in around 30 municipalities, although this number has been expanding more recently and has now reached 70 municipalities in total. Revenue-sharing mechanism of the transportation fee is underway to make it more transparent, predictable, and regular. In parallel, MoFP has improved transparency in reporting the annual amounts of property tax transferred to local governments, but further communication is still in need.

The lack of intergovernmental transfers characterizes the current architecture in Palestine. No regular fiscal transfer exists to supplement the shortage in own-source revenues (The World Bank, 2017). No predictable intergovernmental fiscal transfer exists to fund essential capital investments. The benefits of decentralization depend on the intergovernmental system to be equitable and efficient regarding the mechanism of horizontal transfers. Otherwise decentralization will fail to materialize (Bhujbal, 2010). Establishing a fiscal transfer mechanism requires the highest attention from both MoLG and MoFP. Political factors are crucial in defining the intergovernmental transfers allocation, which was indicated in an empirical study (Bhujbal, 2010). Establishing a fiscal

transfer mechanism that effectively addresses imbalances is long overdue. Transfers from central government need equalization to reduce the existing inequalities between transfers to LGUs. Addressing vertical and horizontal fiscal imbalances is critical to improve local service delivery performance (The World Bank, 2017). LGUs are supposed to receive revenue from property taxes, occupational license taxes, and transportation fees, but the revenue base varies dramatically across LGUs, leading to significant horizontal imbalances. Local revenues are insufficient to cover the operational expenditure required of LGUs, leading to a vertical imbalance which is the gap between generating sufficient revenues to match the expenditure needs.

Palestinian local government unit's system is part and extension of the central government (Horizon, 2009). The Local Government Act assigns 27 functional responsibilities to LGUs (Appendix 3), in Article (15) (ARIJ, 2009; Swafta, 2011; The World Bank, 2017). But those functional assignments are not matched with appropriate revenue sources. Although the act assigns 16 revenue sources to municipalities, the Local Government Act of 1997 does not distinguish between delegated responsibilities and own responsibilities. In the case of delegated responsibilities, the PNA would ultimately be responsible for the regulation and financing of those functions, but LGUs would implement them. However, for own responsibilities, LGUs would generally be responsible for the services, including the raising of sufficient revenues (The World Bank, 2017).

However, the current revenue assignments are not even enough to deliver on core services.

As a critical step, the Ministry of Local Government must review and revise LGU revenue and expenditure assignments. These are significant shortcomings that need to be considered by the Ministry of Finance and Planning (MoFP). Although Palestinian municipalities and village councils are responsible for providing critical public services, they have not been assigned sufficient revenue sources. Changing the financial incentive structure for service provision will need to be at the core of the reform agenda. Due to chronic underfunding, LGUs have developed a practice of diverting revenues from service fees to meet their expenditures needs (The World Bank, 2017).

Roads on the one hand are the responsibility of LGUs, they have full authority over local roads, development, planning, and maintenance of the network. On the other hand, the Ministry of Public Works and Housing is responsible for regional roads outside the municipal master plans. Fewer than 2 in 3 Palestinian households have access to paved roads (The World Bank, 2017). Because LGUs have no direct income source to cover road rehabilitation and maintenance cost. Postponing the tackle of these needs shall negatively impact the cost to a multiple expense. It can take three to four times as expensive to repair a road with late examining than one that is inspected more often. Given the limited resources that are available from transfers and shared taxes, LGUs have to rely mostly on own-source

revenues which have significant variations across LGUs (The World Bank, 2017).

PNA needs to introduce a system of conditional grants beyond the donor-funded Municipal Development Program to fund delegated responsibilities and provide an incentive for LGUs to complement and implement PNA's sectoral objectives at the local level. These conditional grants are to be allocated by the MoLG as it is the monitor on the LGUs, that receives and requires data on all municipalities in Palestine.

Due to the delay in remitting the municipal transfers and the acute need of the funds collected, rose the idea of municipalities collect the tax themselves, at least to ensure the daily cash liquidity at the right time (Sawafta, 2011). As to conduct its business properly, to characterize the relationship between the ministry and local entities to transparency and clarity and to achieve greater financial decentralization which is the lifeblood of the municipalities. 90% of municipalities surveyed had the ability to collect property tax, and they refuse the current collection method due to the low collection rate of the tax and delay of transferring collected taxes, 81% requested the transition of property tax to their offices instead of the tax department.

Intergovernmental transfers are analyzed in Table 2.4.2, with the variance percent between the actual and the budgeted intergovernmental revenues. Al- Bireh and Ramallah municipalities have the highest percent of intergovernmental revenues percent to total revenues in Table 2.4.3.

Table 2.4.2: Analysis of intergovernmental revenues in an amount

Municipality	Year	Property Tax	Transportation Fees	Occupational License Tax	Intergovernmental Revenues	Variance Percent
Tubas	2015	843,100	454,677	-	1,297,777	76%
	2016	376,287	-	-	376,287	18%
	2017	1,332,999	554,548	-	1,887,547	69%
Jericho	2015	3,238,756	451,824	247,007	3,937,587	105%
	2016	4,391,832	551,141	399,348	5,342,321	108%
	2017	4,584,561	560,370	311,335	5,456,266	N/A
Al- Bireh	2015	22,545,080	948,793	935,434	24,429,307	130%
	2016	12,758,491	1,452,195	845,838	15,056,524	79%
	2017	16,053,339	1,157,959	250,014	17,461,312	97%
Hebron	2015	11,736,131	-	1,746,518	13,482,649	43%
Jenin	2015	3,500,000	1,161,058	-	4,661,058	31%
	2016	-	500,000	-	500,000	11%
Bethlehem	2016	2,589,141	755,634	933,522	4,278,297	63%
	2017	3,766,553	754,605	551,337	5,072,495	81%
Ramallah	2016	21,304,493	831,946	1,358,868	23,495,307	85%
	2017	18,910,240	1,081,530	1,262,452	21,254,222	78%
Salfeet	2015	655,396	-	81,509	736,905	78%
	2016	1,211,553	-	141,481	1,353,034	138%
	2017	937,935	-	91,393	1,029,328	80%
Qalqilia	2015	1,740,725	4,453,928	249,621	6,444,274	162%
	2016	2,188,422	-	328,658	2,517,080	N/A
	2017	2,368,573	1,112,678	320,924	3,802,175	96%
Nablus	2015	-	5,000,000	4,259,333	9,259,333	18%
	2016	7,369,157	8,235,516	1,881,898	17,486,571	N/A
	2017	22,034,678	3,091,881	1,265,877	26,392,436	N/A
Total/ NIS		166,437,442	33,110,283	17,462,367	217,010,092	

Table 2.4.3: Analysis of intergovernmental revenues in percent

Municipality	Year	Total Revenues	Percent of Intergovernmental Revenues from Total Revenues	Property Tax	Transportation Fees	occupational License Tax
Tubas	2015	6,142,069	21.1%	14%	7%	0%
	2016	5,103,837	7.4%	7%	0%	0%
	2017	6,956,008	27.1%	19%	8%	0%
Tulkarm	2015	73,288,131	0.0%	0%	0%	0%
	2016	69,833,428	0.0%	0%	0%	0%
	2017	82,368,002	0.0%	0%	0%	0%
Jericho	2015	27,671,104	14.2%	12%	2%	1%
	2016	20,689,282	25.8%	21%	3%	2%
	2017	21,932,086	24.9%	21%	3%	1%
Al- Bireh	2015	45,979,268	53.1%	49%	2%	2%
	2016	39,107,291	38.5%	33%	4%	2%
	2017	33,989,618	51.4%	47%	3%	1%
Hebron	2015	77,075,813	17.5%	15%	0%	2%
	2016	74,252,031	0.0%	0%	0%	0%
Jenin	2015	21,175,905	22.0%	17%	5%	0%
	2016	17,783,973	2.8%	0%	3%	0%
Bethlehem	2016	17,048,242	25.1%	15%	4%	5%
	2017	20,721,097	24.5%	18%	4%	3%
Ramallah	2016	61,245,669	38.4%	35%	1%	2%
	2017	72,554,235	29.3%	26%	1%	2%
Salfeet	2015	15,672,065	4.7%	4%	0%	1%
	2016	17,102,780	7.9%	7%	0%	1%
	2017	19,367,249	5.3%	5%	0%	0%
Qalqilia	2015	68,378,617	9.4%	3%	7%	0%
	2016	68,636,455	3.7%	3%	0%	0%
	2017	79,923,548	4.8%	3%	1%	0%

Municipality	Year	Total Revenues	Percent of Intergovernmental Revenues from Total Revenues	Property Tax	Transportation Fees	Occupational License Tax
Nablus	2015	128,031,661	7.2%	0%	4%	3%
	2016	98,750,417	17.7%	7%	8%	2%
	2017	108,101,417	24.4%	20%	3%	1%
Total/ NIS		1,398,881,298	15.5%	12%	2%	1%

2.5 Municipal Bonds around the world

Municipal bonds would help many commercially minded LGUs spread their wings and be less reliant on central government, this has been concluded by the United Kingdom Municipal Bonds Agency (UKMBA, 2015). Local governments in North America depend mostly on municipal bonds, specific purpose revenue bonds primarily financed municipal investment in North America which also called project financing (Farvacque-Vitkovic & Kopanyi, 2014).

Issuance of municipal bonds as a way to fund civic services was applied in some Indian municipalities (Asher & Sheikh, 2012). Many other countries adopted the issuance of municipal bonds. Swedish and Danish municipal bonds agencies both have a very successful record in issuing municipal bonds (UKMBA, 2015).

The size of municipal bonds market in the United States and Canada is larger than the market for corporate bonds (Farvacque-Vitkovic & Kopanyi, 2014). USA has certain rules are issued by Municipal Securities Rulemaking Board (MSRB), these rules explain procedures of municipal bonds in details. The US Federal Reserve data from municipal bonds website indicates that the total outstanding municipal debt went from USD 1.60 trillion in 2001 to the peak amount of USD 3.74 trillion in 2011; a 133.8% increase. Therefore, how big the municipal bond market around the world is out of the question because it is large. The U.S. Municipal bond market grew with the average maturity increasing from 7.14 to 9.45 years.

In contrast, some researchers debated that "local government borrowing is too low" compared to their expenditure responsibilities for infrastructure and by the cause of "the low levels and high needs for capital infrastructure" (Vazquez, 2015, p.26). Thus, in some countries, there is a need to study how to operate a "subnational credit market." The necessary levels of subnational borrowing may not take place because of market failure on the supply side.

Bonds are very common in Jordan; the neighbor country of Palestine. Different types of financial instruments are issued including corporate bonds, treasury bonds, treasury bills, and Islamic Sukuk. Bonds for water authority are marked in Amman Securities Exchange. In 2017, there was new issues of a total value of 250 million Jordanian Dinars (SDC, 2017). In 2016, the total value registered of treasury bonds for the whole Jordanian government is JD 5701 million. From our interviews, Khraim explained that the Jordanian government-initiated bonds by private placement to the financial institution contending higher interest rates and complicated terms, later bonds were targeted to the public (Appendix 1, PEX Interview).

Jordan Securities Commission plays a role in supervising and regulating the issuance besides dealing in securities. Also, Securities Depository Center has been created by the private sector in Jordan to ensure safe custody of ownership of securities, registering and transferring

ownership of securities traded on Amman Securities Exchange, and settling the prices of securities among brokers.

PMA was able to take the first step to improve Palestine's socioeconomic status. PMA tried to encourage lending and borrowing by suspending credit rating to make financial instruments more accessible for people (Awartani, 2016). Thus, the PMA has launched a financial inclusion strategy "that bodes well for efforts to enhance access to credit on more affordable terms to a wider share of the population, including all Palestinians sectors" (Awartani, 2016).

In Croatia, LGUs used all possible debt instruments, including municipal bonds, loans and even getting into debt with contractors (for works) from 1997 to 2009 (Bajo & Primorac, 2010). South Africa is the only African country that issues municipal bonds (Farvacque-Vitkovic & Kopanyi, 2014). In 2004 the city of Johannesburg issued USD 53 million, 11.9 percent bond, mature in 12 years, and purchased a partial bond guarantee about 40% of the bond's proceeds. Even though in Western Europe municipal banks have been formed to support local governments, Western Europe leveraged the historical preferential access to long-term saving deposits and government contributions to create municipal banks and financial institutions. Examples of some countries having municipal banks include Netherlands, Belgium, France, and Spain (Farvacque-Vitkovic & Kopanyi, 2014). Some countries prohibit municipal borrowing such as Pakistan, China, and Chile (Farvacque-Vitkovic & Kopanyi, 2014).

In Brazil, borrowing is forbidden from the central bank and upper levels of government.

To borrow means cost money. The strong financial position is aimed. Ongoing monitoring of borrowed funds should be completed frequently or annually which depends on the risk and basic analysis. Ongoing monitoring and expanded analysis should be documented.

Credit ratings and creditworthiness analysis are treasured methods to prove that the municipality has the capacity to repay a loan or bond on time. Credit rating system can detect omissions in managing municipal operations, and detect failures (Bajo & Primorac, 2010). Better credit rating allows borrowing at lower interest rates; this theory corresponds with a history of positive credit rating implications on debt repayment. Emerging economies that have local government ratings include Romania, Ukraine, Morocco, Brazil, India, Poland, South Africa, Argentina, Kazakhstan, Turkey, Mexico, Bulgaria, the Russian Federation, and Malaysia. Mexico has been particularly active in promoting the preparation of credit ratings for local governments as a base for both bank credit and bond issue. Ratings are mandatory for local governments in India when the maturity of the issue is more than 18 months (Farvacque-Vitkovic & Kopanyi, 2014). Rating agencies use mathematical ratios to compare an issuer with others. Different agencies use methodologies to determine their rating opinions and different quantitative and qualitative criteria (MSRB, 2008). However,

a rating is not a scientific evaluation. But the subjective judgment plays a fundamental role in the rating assigned .

Bond issuing is expensive. LGUs (issuers) need to pay fees to the rating agency, fees to the bank that sells the bonds to the public (underwriter), fees for the operations in the capital market, and the cost of marketing and publicity (Farvacque-Vitkovic & Kopanyi, 2014). The bond rating process is a complex one (Palumbo, Shick & Zaporowski, 2006). For instance, Fitch Rating's payment can reach up to USD 750,000 per issue (Farvacque-Vitkovic & Kopanyi, 2014). The cost depends on the time and effort it takes to evaluate the bond issuer. Given the lack of data on small municipalities, the rating can be expensive. Small or medium municipalities can rarely issue bonds because of the high cost and because potential investors are not very interested in minor issues. According to this research, the sample consists of the largest municipalities in Palestine.

Rating agencies appeared in 1909, and ever since they have played an important role in emerging and established markets (Farvacque-Vitkovic & Kopanyi, 2014). Rating agencies play a crucial role in providing the market with information on the capacity of a given local government to issue debt and pay it on time. A bond rating performs the function of a credit risk evaluation. It does not constitute a recommendation to invest in a bond and does not take into consideration the risk preference of the investor (ibid, 2014). Although municipalities are rated on their merits, the country rating is considered a ceiling for subnational entities. Thus, the

rating of a city cannot be better than that of the host country. Three major rating agencies for municipal bonds account for 95 percent of all international ratings around the world:

- Moody's Investors Service
- Standard & Poor's
- Fitch Ratings.

Different instruments have been used internationally, here are some municipal debt controls (Farvacque-Vitkovic & Kopanyi, 2014).

- In Czech Republic and Poland, debt service must be less than 15 percent of revenues. Five-year debt service projections are required.
- In Spain, total municipal debt may not exceed 110 percent of annual revenues.
- In Italy, municipalities must have balanced accounts. Debt service payments may not exceed 25 percent of current revenues. Loans must have terms of at least ten years. The State Treasury sets the maximum legal interest rate
- In France, operational surpluses from prior years must exceed debt service payments.
- In Germany, each local government has borrowing limits, and explicit approval is needed from the state.
- In Ireland, The Ministry of Finance must approve each municipal borrowing.

- In Norway, municipal borrowing is allowed for investment only.
- In The United Kingdom, the government gives credit approval ceilings each year to each local government.

Chapter Three

Application of Methodology

3.1 Sample Population and Participants

The methodology of this study emphasizes the added value, and the creditworthiness rating of the Palestinian municipalities. Consequently, it has targeted all the municipalities in Palestine which have reached to 128 municipalities according to the Palestinian Central Bureau of Statistics (PCBS). Gaza strip is not included here because of the difficulty of contacting the municipalities and obtaining their data. This is in addition to the deteriorating political situation and the instable economy that Gaza suffers from due to the Israeli occupation blockade. The sample of the research consists of 11 municipalities which have been regarded and rated as the largest West Bank municipalities by the MoLG. Large municipalities are more capable of making strategic capital projects that are funded by the municipal bonds.

Data sampling has been taken from the largest governorates in the West Bank which represent 85% of the West Bank's population (PCBS, 2016). For each governorate, the central municipality has been chosen as a sampling unit. The municipalities are Nablus municipality, Hebron municipality, Jericho municipality, Jenin municipality, Tulkarm municipality, Qalqilia municipality, Salfeet municipality, Tubas

municipality, Bethlehem Municipality, Ramallah municipality and Al-Bireh municipality. Ramallah municipality and Al-Bireh municipality are in the same governorate. It is worth mentioning that Al-Bireh and Ramallah were considered as two separate municipalities by MoLG and rated as A.

3.2 Data collection

This section presents the municipalities' financial data for the last five years (from 2013 till 2017) and budgets from the start of the budget gate (from 2015) making up the secondary data. The primary focus of the study will be the statement of revenues and expenditures, and the statement of the financial position. Financial position statement analysis has been carried out by the researcher to find the size of debts and loans for each municipality. Furthermore, attention is paid to the size of the budget deficit, in addition to the deficit in the operating budget on one side and profitable ones on the other side.

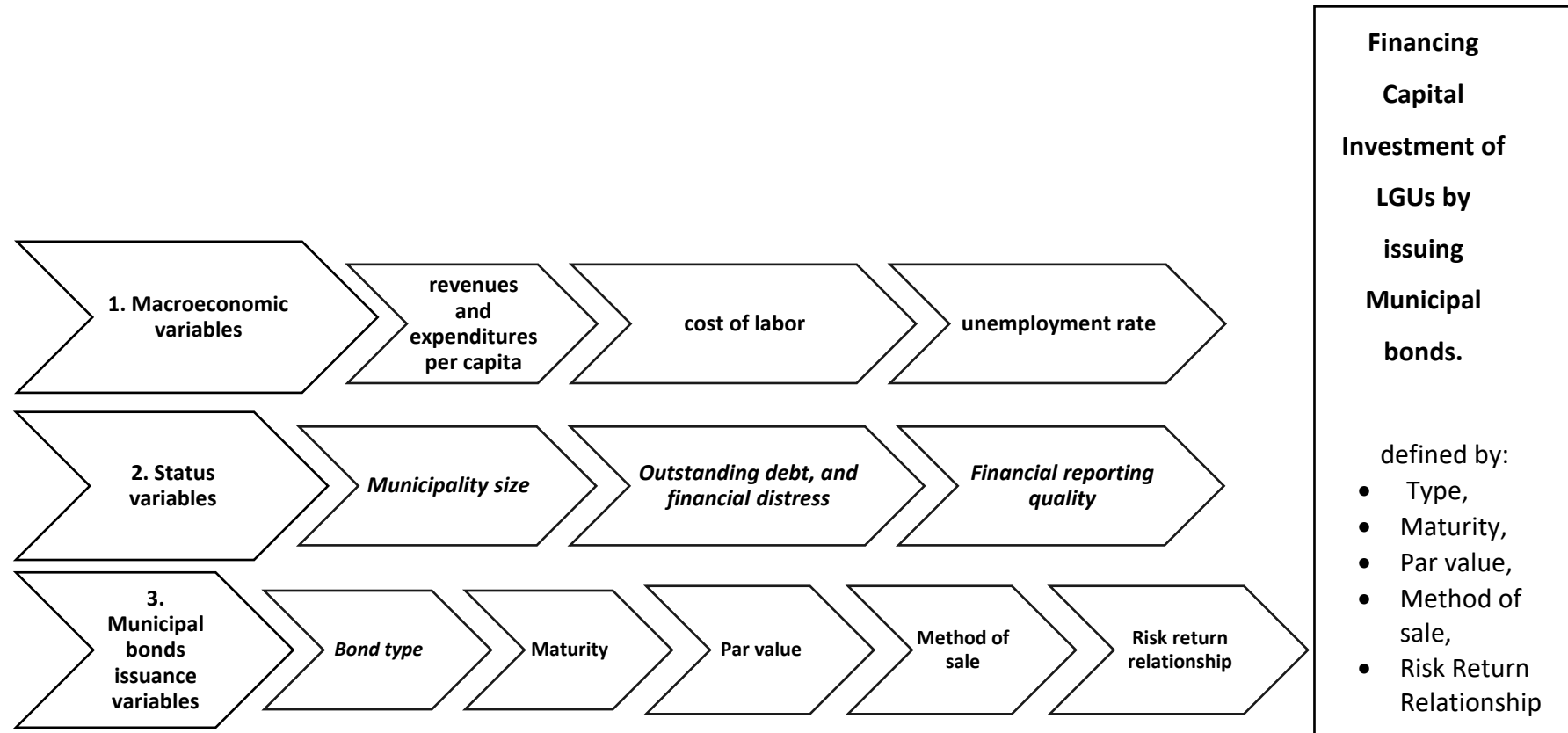
Analysis of financial reports according to the research variables has also been carried out to test their quality and disclosure through trend and comparative analysis of the financial ratios. However, the financial data has not been published for all the municipalities. So, the researcher has resorted to search for the obligatory disclosure variable so as to check the financial reporting quality. With the help of the comparative statements' analysis method, it is possible to compare the financial statements of LGUs for the years respectively, this in addition to the employment of the percentage analysis method which determines the magnitude of the items in a financial

statement, and it helps in comparing between the enterprises of different sizes (Kablana, 2013). The performance measure is virtually valueless without the comparison with the relevant baseline data (Farvacque-Vitkovic & Kopanyi, 2014). A proxy on the key performance indicators as an average of the benchmark can be obtained from these sample municipalities to make future comparisons with other municipalities results. MoLG should institutionalize performance benchmarking and make it as an integral instrument for evidence-based policy making (The World Bank, 2017).

In addition to the secondary data, interviews and questionnaires have been conducted to help with the data collection. The interviewees include the LGUs, Ministry of Local Governments (MoLG), Municipal Development and Lending Fund (MDLF), Palestinian Capital Market Authority (PCMA), and Palestinian exchange (PEX). Financial analysis of the questionnaire will be done to determine the need and ability for municipalities to use bonds as a source of finance. Interviews are needed to draw the future of the issuance with the main players based on their opinions.

The researcher has combined between the quantitative and the descriptive analysis of the current financial situation by figuring out the underlying assumptions of bond issuance situation. Then, the researcher has shed the light on the financing investing problems of municipalities by assessing the different effect of each financial ratio on municipal bonds characteristics.

3.3 Research Model



3.4 Research Variables

The variables of the research are related to the bonds and the municipalities in the Palestinian context. The research has tackled significant variables that may affect issuing municipal bonds and the capital investment problems. In brief, the variables are: macroeconomic variables, status variables and municipal bonds issuance variables.

3.4.1 Macroeconomic variables

Increasing debt-financing for government spending has economic effects that can improve economic conditions during recessions (Adelino, et al, 2017). The willingness of the municipalities in the developing countries to issue municipal bonds depends greatly on the public confidence in such instruments (Samonikov et al., 2016).

Capital investments have a high potential of success in Palestine. This is due to many economic facts (PIPA, 2016):

1. 1 million skilled labour.
2. 95% literacy rate (higher than MENA region, China, India, and Turkey).
3. Competitive labour costs (average wage 77% lower than Israel, also more economical than Turkey and Jordan).

4. Competitive cost of utilities: average utility costs of 0.57 NIS (USD 0.17) per kWh electricity and 3.17 NIS (USD 0.93) per m³ water.
5. Well-developed import and export infrastructure via Israel and Jordan.
6. Major growth sectors include agriculture- agribusiness, construction, tourism, IT, and light manufacturing.
7. World religious and historic sites (Ancient, Roman, Byzantine, and Holy Land) have huge tourism potential (PIPA, 2016).

In the past five years, the Consumer Price Index (CPI) has varied between 2– 4% (PIPA, 2016). Palestine has been importing its inflation from Israel since the Paris Protocol (Awartani, 2016). This continued Israeli occupation impact on Palestine has led to further concessions on the ability of the Palestinian Monetary Authority to implement inflation targeting policies.

Macroeconomic variables measure the economy and marketability. Before launching municipal bonds, the currency fluctuation and interest rates across years are assessed. For the Palestinian national economy, the macroeconomic variables are needed for the analysis of the general budget, the international investment position and the external debt. For the Palestinian local economy, the following measures are very significant: revenues per capita, expenditures per capita, cost of labor and

unemployment rate. They help to assess the future investment capacity and needs of each municipality.

For most of the Palestinian municipalities, the cost of labor is increasing because the municipalities are considered as national vehicles to absorb the increasing unemployment (Horizon, 2009). One way suggested to absorb unemployment is that municipalities may stop the overtime expense of the existing employees and instead bring new workers. Unemployment drives governmental units to have more workers under disguised unemployment with low productivity. The weakness in the labor force is associated with higher interest rates. According to Palumbo et al. (2006), unemployment rate was used on the regional level. In Palestine, unemployment rate is measured across governorates. Table 3.4.1 demonstrates unemployment rate in Palestine.

Table 3.4.1: Unemployment in Palestine by Governorate

Unemployment in Palestine by Governorate			
Governorate	2015	2017	Growth rate
Jenin	16.1	17.3	7%
Tubas and Northern Valleys	18.1	20.7	14%
Tulkarm	17.8	14.3	-20%
Nablus	17	18.5	9%
Qalqilia	13.2	10.1	-23%
Salfeet	15.4	15.2	-1%
Ramallah & Al- Bireh	19.7	15.9	-19%
Jericho & AL Aghwar	14.5	14.7	1%
Bethlehem	13.7	19.9	45%
Hebron	19.6	21.7	11%
West Bank	17.3	17.9	3%
Total	25.9	27.7	7%

Source: Palestinian Central Bureau of Statistics, <http://www.pcbs.ps>.

According to Table 3.4.1, the highest unemployment rate in 2017 is represented in Hebron governorate which has 21.7 unemployment, while Bethlehem has the highest increase of unemployment rate from the year 2015 to 2017. Higher unemployment rates may indicate weakness in the economic base and lower credit quality (Palumbo, et al, 2006).

Some socio-economic indicators are more important than others. Among these are the state of the economy and population level (BMA, 2007). Municipal analysts have given a lot of attention to the population variable (Palumbo, et al, 2006). Increasing per capita expenditures reflect changes in expenditures relative to changes in population (BMA, 2007). Increasing per capita expenditures may indicate that the cost of providing services is outstripping the community's ability to pay .

As population increases, it might be expected that revenues and the need for services would increase proportionately (BMA, 2007). The level per capita revenues would remain at least constant in real terms. However, this is not always the case as the cost of providing services is not directly related to population. If per capita revenues decrease, the municipality may be unable to maintain the existing service levels unless it finds new revenue sources or ways to reduce costs.

The international investment position is defined as an accounting sheet record the stock investing for the residents in Palestine- individuals, institutions and government- that has been invested abroad under the name of (assets), in contrast to the stock investing owned by residents outside

Palestine that has been invested in Palestine under the name of (liabilities) (PCBS, 2012). In 2017, stocks of Palestinian assets invested abroad were about USD 6,455 million, while stocks of foreign liabilities on the Palestinian economy were approximately USD 5,082 million (PCBS, 2017).

According to PCBS (2016) results of the Palestinian International Investment have showed that there was a continuous increase in investing outside Palestine. For example, investing in 2012 rose from USD 532 million to USD 1,173 million in 2016, and reached USD 1,373 million by the end 2017 as in Table 3.4.2 (PCBS, 2017). These consists of external assets minus foreign liabilities; meaning that the Palestinian economy had invested outside Palestine more than the investment amount in Palestine. Growth rate of 2017 is 158% as 2012 a base year (duplicated 2.5 times). Thus, there is a priority and a necessity to attract Palestinians to invest inside Palestine so as to strengthen the economy by using new ways like bonds.

In 2017, the Palestinian economy analysis of other investments revealed that cash deposits of local banks in foreign banks and foreign exchanges are the main contributors in the external assets value of USD 4538 million, creating 70% of external assets. Foreign direct investment abroad reached 7%, while portfolio investments overseas had contributed to 18% of the total value of external assets. The total stocks of foreign liabilities in Palestine had amounted to USD 5,082 million. The foreign direct investment contributed to 54% of the total investments. Whereas,

portfolio investments constituted about 13% of the total investments. In contrast, loans and deposits from abroad amounted to 33%. The component analysis showed that the investments by the Palestinian enterprises outside Palestine are higher than the foreign investments in the Palestinian enterprises.

Table 3.4.2: International investment position in Palestine

Ratios	Amount in million USD	Ratios	Amount in million USD	Ratios	Amount in million USD	Ratios
Investment	Total 2017		Total 2016		Total 2012	
International Investment Position (net)	1,373	100%	1,173	100%	532	100%
Total External Assets	6,455	100%	6,101	100%	5,262	100%
Foreign Direct Investment Abroad	232	4%	400	7%	420	7%
Portfolio Investments Abroad	1,031	20%	1,112	16%	1,052	18%
Other Investments Abroad	3,336	63%	4,276	70%	4,538	70%
Reserve Assets	663	13%	313	7%	445	5%
Total Foreign Liabilities	4,730	100%	4,928	100%	5,082	100%
Foreign Direct Investment in Palestine	2,337	49%	2,660	53%	2,704	54%
Foreign Portfolio Investments in Palestine	809	17%	658	13%	666	13%
Other Foreign Investments in Palestine	1,585	34%	1,610	34%	1,720	33%

Source: Palestinian Central Bureau of Statistics (PCBS)

The external debt is defined as an accounting sheet record of the debt stocks on the Palestinian economy sectors due to non-resident debts, which include (loans from nonresidents, the nonresidents' deposits in the Palestinian banks, the Palestinian bonds purchased by the non-residents, debt transactions between the non-resident enterprises and fellow enterprises in Palestine, in addition to any other liabilities on the Palestinian economy. The data of external debt have been extracted from the liabilities side in the international investment position matrix (debt items from other foreign investments) (PMA 2012).

The total gross external debt on the Palestinian economy sectors had amounted to USD 1,601 million in 2012 (PMA, 2012), and to USD 1,720 million by the end of 2017 (PMA, 2017). The debt on the governmental sector represented 60.5%, while debts on the banks sector reached to 35.1%, and debt on other sectors (nonbanking financial companies, non-financial corporations, NGOs and household sector) amounted to 4.1%. Moreover, the lending between affiliated companies reached 0.3%.

In 2016, external debts were USD 1,615 million consisted of USD 1,269 million with a total percentage of 79%; long-term debt had been 70% in 2015 (PMA, 2016). PMA force banks to invest at least 55% of their deposits in Palestine (Appendix 1, Pex Interview).

In 2016, the Palestinian national budget resulted in a deficit of USD 1.09 billion, and amounted to 8 percent of GDP (The World Bank, 2017).

Thus, the PNA is under severe fiscal stress, experiencing a significant downturn in the budget since the support from donors has dropped from 32% of GDP in 2008 to 5% in 2016 (The World Bank, 2017) .

Table 3.4.3: Comparison of Palestinian national budget (MoFP, 2017)

Item	2018		2017	
General PNA Budget in thousands		16,559,061		16,290,604
Infrastructure sector	4%	583,484	4%	600,948
Among infrastructure: MoLG	0.9%	139,176	1.3%	219,825
Ministry of Health	11.0%	1,787,683	10.6%	1,724,572
Ministry of Higher Education	20.6%	3,350,781	19.1%	3,117,930

Source: Ministry of Finance and Planning (2017), Palestinian Budget Law.

The Palestinian Budget Law for 2017 put a goal to enhance LGUs revenues by initiating profitable projects and new businesses, in addition to subsidizing LGUs in order to implement these projects (MoFP, 2017). MoLG is the central party that is accountable for monitoring the functions of LGUs (Sawafta, 2011). However, the share of MoLG decreased from 1.3% to 0.9%. Despite the fact that its share was 3% in 2013 with voices requesting to increase this percentage, the share of LGUs needs clarity, and fair distribution of the governments share funds (Sawafta, 2011). This share is considered very low in comparison with the developed or the developing countries. In contrast, the total local government expenditure in Kenya is less than 4% compared with 60% in Japan (Bhujbal, 2010).

In Palestine, credit facilities are welcome especially overdraft facilities (Sabri, 2003). This is due to the lack of profitable projects and

higher interest rates compared to the expected return on investments and the increase of non-performing loans.

In Palestine, 92% of loans are short-term, and less than 1% is considered as long-term financing. The value of deposits was USD 3.5 billion in 2001 (Sabri, 2003). The annual change percentage of total deposits was 8.1 in 2015, with a rise later in 2016 to 9.8 percent. The private sector deposits percent was 10.4 for 2015 and 2016 (PMA, 2016). The Palestinian private sector may invest in bonds, as this money is available as deposits in banks without investment. Thus, the use of local deposits of the Palestinian economy increased to approximately USD 11 billion by the end of 2017.

Palestine shares the same currency with Israel which is the Shekel. The Shekel has had almost a stable rate for over ten years (PIPA, 2016). Interest rates vary according to the required currency of the loan. Palestine has a three- currency system with constant fluctuations among their values; this pushes banks to charge higher interest rates to compensate for the risk of lending or holding deposits (Awartani, 2016). The interest rate is lower on USD currency that indicates that municipal bonds are better to be issued in dollar currency. According to Sabri (2003), the acceptable interest rate in Palestine is from 7% to 11% for long-term loans of the industrial sector. Ratios which include: return on investment, profit margin, inventory turnover and debt ratio are considered the base assessment for having long-term loans in the industrial sector.

The PMA has also encouraged the reduction of interest rates and facilitating the attached conditions of structured loans granted to small enterprises (Awartani, 2016). The PMA encourages lending by exempting commercial banks from the 2% risk reserve requirement to any loanable funds or financial services provided for small enterprises.

Table 3.4.3 represents the interest rates in Palestine for the periods from 2013 to 2017 (PMA, 2016). For the last five years the average interest rate on loans taken in different currencies was 7. The highest interest rate on loans was 9.35 in 2013 by NIS currency, and the lowest was 5.87 in 2016 by USD.

Table 3.4.4: Historical interest rates in Palestine

Interest rates on loans and deposits (%)						
Period	JD		USD		NIS	
	Deposits	Loans	Deposits	Loans	Deposits	Loans
2013	7.48	2.08	6.44	0.62	9.35	1.32
2014	7.20	2.15	6.05	0.83	9.09	1.46
2015	6.94	2.20	5.92	0.94	7.80	1.56
2016	6.34	2.28	5.87	1.01	6.94	1.49
2017	6.61	2.19	5.79	1.39	7.09	1.43

Source: Palestinian Monetary Authority, 2016.

3.4.2: Status variables

Credit ratings are expensive; they require evaluation and benchmarking of the local government (Farvacque-Vitkovic & Kopanyi, 2014). In reality, municipalities assess the bond rated gains versus the cost. By assigning a rating for municipal bonds, the following factors are assessed by rating agencies:

- Financial condition
- Demographic factors
- Management practices of the local government and the legal framework.

This study has shed the light on the demographic factors which have been included under the macroeconomic variables, in addition to the status variables which measure financial condition, fiscal health and sustainability of the municipality. Status variables are related to many subgroup variables as the various following subtitles show:

a. Municipality size

Three indicators define municipality size: population, the owned assets and operating activities which are affected by the ability to generate revenues. The large municipalities should issue bonds because they have the financial ability and they are capitals of the economy with the highest population density. The population is a common measure for the size of a municipality. The population of the sample Palestinian municipalities was taken into consideration for this study. Assets are studied through the vertical analysis of the financial position statement and by the ratio of a land rate. Moreover, operating activities are analysed by different types of budgets for businesses and general ones which resulted in the mandatory surplus from the operating budgets.

LGUs own and control large asset portfolios, including physical assets such as lands, buildings, infrastructure, vehicles, equipment and financial assets such as investments, ownership in enterprises, and bank deposits (Farvacque-Vitkovic & Kopanyi, 2014). LGUs could evaluate their properties and exploit them in productive projects.

In 2014, financial statements of Tubas municipality showed details of land owned by the municipality, which is worth an estimated 1,528,096 NIS; that is, about 4.5% of the total land are available for projects, sale or for other uses like guarantee for issuing municipal bonds.

Net debt refers to either assessed valuation or estimated valuation of real estate. To be more conservative, only land available for sale is considered as the guarantee of municipal bonds in the first issuing. Estimated valuation represents the actual values which are better if the market values exist.

To measure the municipality size variable, the current and fixed assets have been analyzed vertically to get percentages for the total assets of the available sample municipalities. Results are in appendix 2. The financial analysis has depended on financial numbers available in the financial statements; better analysis will result from better represented financial statements.

An analysis of the operating activities has been conducted to examine the mandatory surplus for the operating budgets. Analysing

profitable budgets facilitates understanding the structure of revenues and expenditures of the Palestinian municipalities.

Among municipal activities, water is the most profitable budget for municipalities; water is the vital lifeline service for citizens. From the performance of water and wastewater service providers in Palestine in 2016, Water Sector Regulatory Council (WSRC) has developed two important ratios: the first one is the working ratio, or the efficiency ratio for water service which is calculated by operation and maintenance (O&M), in addition to the administrative costs (excluding depreciation) / operating revenues from water service. The second ratio is the collection efficiency for water service which is calculated by water fees during the year, in addition to the collection of the total annual water, and wastewater billed sales (NIS) $\times 100\%$. As we explained before, this collection ratio may exceed 100% for some municipalities because they have the collection from arrears and new year's bills without separation.

As table 3.4.5 shows, most of the sample municipalities are water service providers; different bodies are the water service utilities which provide four out of the eleven municipalities. Al- Bireh and Ramallah are supplied by the same body which is Jerusalem Water Undertaking. Such a body provides water for municipalities citizens instead of the municipalities themselves.

Table 3.4.5: Sample results of (WSRC) ratios

#	Municipality name	Working ratio 2016	Collection Efficiency - water service			Served Population	Utility water provider
			2016	2015	2014		
1	Nablus	0.89	71%	71%	71%	215,435	Nablus Municipality
2	Tulkarm	0.81	46%	50%	51%	85,000	Tulkarm Municipality
3	Qalqilia	0.78	68%	55%	53%	53,722	Qalqilia Municipality
4	Salfeet	0.87	88%	100%	82%	15,900	Salfeet Municipality
5	Jenin	1.08	54%	102%	52%	54,000	Jenin Municipality
6	Jericho	0.96	73%	71%	50%	35,000	Jericho Municipality
7	Hebron	1.1	55%	74%	66%	238,985	Hebron Municipality
8	Tubas	0.75	58%	67%	65%	48,958	Tubas Joint Service Council
9	Ramallah	0.9	92%	108%	98%	340,000	Jerusalem Water Undertaking
10	Al- Bireh						
11	Bethlehem	0.91	85%	74%	69%	96,195	Water Supply & Sewerage Authority of Bethlehem, Beit Jala, and Beit Sahour

Source: Water Sector Regulatory Council, (2016).

b. Outstanding debt, and financial distress

Outstanding debt variable is very important because debt of the local governments is usually regulated by legislation; it is generally followed by a particular regulation on local debt. "which regulates at least three issues: (a) debt authorization for each type of local government; (b) types of legal instruments (short- term, long term, loans, and bonds); and (c) establishment of a debt limit" (Farvacque-Vitkovic, Kopanyi, 2014, p. 347).

Some countries have their regulations and conditions for the local government borrowing (Farvacque-Vitkovic & Kopanyi, 2014). It is probably desirable to start with conservative limits and reduce them over time (Vazquez, 2015). The regulations on local government borrowing are typically focused on some rules, some of these rules are implemented as an international practice to limit borrowing at the local governments level:

- The golden rule states that borrowed funds cannot be used to finance current expenditures but for capital expenditures (Vazquez, 2015). There are controls imposed on the use of the loan proceeds; only main types of expenditures can be financed with these proceeds, and they should be used to finance long-term investment projects but not for the current expenditures (Farvacque-Vitkovic & Kopanyi, 2014). Controls are imposed on revenues in order to secure debts.
- The debt limit or ceiling means the maximum amount of money that local governments can borrow. The total debt outstanding is generally defined as the percentage of revenues. Controls imposed on debt service (payment of interest and amortization) should be limited to a portion of annual revenues. In Brazil, debt stock cannot be greater than 60 percent of the operating revenues; debt service should be lower than 25% of the current revenues (Farvacque-Vitkovic & Kopanyi, 2014). For each issue one at a time, municipalities cannot issue new bonds unless the previous bond's principal and interest are paid in full.

- Sources of financing: in general, local governments are not allowed to borrow abroad because no foreign loans are permitted.
- In the case of default. Who pays if a default occurs, or what revenues can be intercepted to pay the debt, must be specified (Farvacque-Vitkovic & Kopanyi, 2014). As fiscal discipline routines set by the government, it is well established that the central government will not act as the guarantor of a subnational debt nor as a lender (Vazquez, 2015).
- Controls imposed on guarantees apply also to their issuance and to types of collateral a local government may offer to a lender (Farvacque-Vitkovic & Kopanyi, 2014). A Subnational debt cannot be guaranteed by the central government (Vazquez, 2015). Municipal guarantees are justifiable in the case of supporting essential service projects. However, they should not be used for supporting commercial or revenue-generating investments. If the local unit cannot repay the principal and the interest, the government is obliged to repay the debt. The Croatian Government gives guarantees to protect the investors in case a local unit cannot repay its debt (Bajo & Primorac, 2010). For this reason, before taking on a debt, the local units must receive the guarantee of the Government in Croatia (Bajo & Primorac, 2010).

- Controls on intermediaries are restrictions imposed on the types of lending institutions, including currency, interest rates, fees, and other pledges (Farvacque-Vitkovic & Kopanyi, 2014).

Only local governments with considerable investment projects, good ratings, and long-term financial needs will be able to issue municipal bonds (Farvacque-Vitkovic & Kopanyi, 2014). Local ratings are showed through the study, and MDLF good rating is used as a ceiling for municipal bonds issuance. Assessing borrowing capacity and adherence risk is a key action for LGUs (ibid., 2014).

Debt to assets ratio is one of the debt ratios that shows the extent to which a municipality is financed by debt. To avoid trouble in debt service and severe liquidity crises, local governments might need to build a debt service reserve fund to ensure their ability to repay debts in a timely manner (Farvacque-Vitkovic & Kopanyi, 2014). It is important to avoid using simple trends to project the debt service, and to analyze carefully the fluctuation of interest payments and debt amortization, or the principal repayment. Some studies employed a size variable which is a debt burden variable calculated by debt per capita that analyzes the ability of local citizens to pay the total existing debt burden through taxes (Wescott, 1984).

The outstanding debt and financial distress variables summarize the fundamental analysis and determine the credit rating suggestion by reviewing the following: 1) budgets to find if a surplus or a deficit occurs, 2) the variance between current and actual balances 3) the application of

liquidity and solvency ratios. This research methodology has a target to reach the best variables used for local rating of LGUs.

Financial accounting ratios that have been used in profit analysis are percentage change in total revenues, total expenditures per capita, percentage change in total expenditures, and net debt per capita (Wescott, 1984). In this research, return on assets (ROA) is the most suitable ratio to be used on Palestinian municipalities. ROA is the earnings divided by total assets. Moreover, total revenues to total expenditures ratio shows how many times income yielded by the municipality to cover its costs; if the ratio comes higher than 1, then the results of the municipality are positive. The fiscal condition was proxied by the ratio of tax revenues to expenditures (Palumbo, et al, 2006). Conducting cross-sectional analysis and benchmarking with relation to other firms help to recognize the better ones than the average.

A comparison of each municipality's overall financial position calculated as assets indicates that fewer liabilities performs the change in net assets. Net-debt or net asset is the difference between financial assets and financial liabilities (Bajo & Primorac, 2010). It is a very useful indicator of liquidity and the ability of local government to repay the interest and the principal of the existing debt. Another liquidity ratio is the current ratio which calculated current assets to current liabilities. Also, net working capital which is the difference between current assets and current liabilities.

Outstanding debt includes some financial ratios (Gitman, 2004). This Research analysed the outstanding debt subgroup variable by the following ratios:

- Avg change in net assets
- Current ratio
- Debt to assets
- Return on assets
- Net lending
- Net working capital
- Avg change of net income
- Avg total revenues and total expenditures
- Collection rate of accounts receivables

c. Financial reporting quality

What standards local government units follow, Governmental Accounting Standards (GAS) or International Public Sector Accounting Standards (IPSAS)? what are the effects on transparency? How to group municipalities according to their level of disclosure? These questions would be refined further during the analysis based on the data collection of the reporting quality variable.

In the United States, the Government Accounting Standards Board (GASB) sets standards for government accounting (Farvacque-Vitkovic & Kopanyi, 2014). At a global level, the International Public Sector Accounting Standard Board (IPSASB) is the independent international board that develops IPSAS. Its operations are facilitated by the International Federation of Accountants (IFAC) (IPSASB, 2016b).

Each standard determines obligatory and voluntary disclosure, the financial information should be available for the public. Investors in municipal securities use financial statements to assess the financial status of the LGUs that issue the securities. According to LGUs conditions, investors make informed decisions about whether to acquire, hold, or sell their investments (Garner & Paul, 2014).

IPSASB developed IPSASs applied to the accrual basis, and to the cash basis. IPSASs scope is applied to financial reporting under both bases (IPSASB, 2017). Accrual IPSASs are based on the IFRSs (International Financial Reporting Standards) that applies to the public sector entailing of other issues that are standing only in the public sector. IPSAS apply to entities that are responsible for redistributing of wealth, delivering services, and their primary objective is not making profits. Public sector finances their activities by taxes, transfers from central governments, debts or fees. Many public sector programs are long-term, so they have been described in the conceptual framework of IPSAS by longevity. Governments have the right to establish their accounting guidelines; IPSASB encourages the

adoption of IPSASs with harmonization of the country's financial reporting requirements. Diversity in the municipal financial reporting and degree of conformance with IPSAS affects the reliability of municipal financial data (Wescott, 1984).

IPSAS obliges full compliance. Financial statements shall not be described as complying with IPSASs unless they comply with all the requirements of all applicable IPSASs (IPSASB, 2017a). If all the elements are not met in full, entities cannot be considered as fully compliant with IPSAS (Woldehawariat, 2017). The overall consideration of the financial statements is the fair presentation and compliance with IPSASs. The presentation of financial statement standard ensures the comparability of financial statement with prior periods and with other entities. The presentation standard considers the structure and the minimum requirements for the content of the financial statements.

IPSAS 1: Presentation of the financial statements applies to all public sector entities except government business enterprises which follow IFRSs. Financial statements could be presented separately, or within the annual reports, a complete set of financial statements comprises the following IPSAS 1.20 (IPSASB, 2017):

1. Financial position statement.
2. Financial performance statement.
3. Changes in net assets and equity statement.

4. Cash flow statement.
5. When the entity makes publicly available, its approved budget, a comparison of a budget and actual amounts either as a separate statement or as a budget column in the financial statements.
6. Notes, accounting policies, and other explanatory notes.
7. Comparative information in respect of the proceeding period.

Financial statements should be described as complying with IPSASs only if they comply with all the requirements of cash applicable IPSAS. IPSAS reporting under the cash basis of accounting have mandatory components of financial statements in part 1 IPSAS 1.3.4, they are (IPSASB, 2017b):

1. A statement of cash receipts and payments which:
 - a. Recognizes all cash receipts, cash payments and cash balances controlled by the entity, and
 - b. Separately identifies payments made by third parties on behalf of the entity
2. Accounting policies and other explanatory notes
3. When the entity makes publicly available its approved budget, a comparison of budget and actual amounts either as a separate

financial statement or as a budget column in the statement of cash receipts and payments.

Municipalities are required to get the external auditor reports like corporations. While, corporations should complete them before the end of April of the next year. In Palestine, there is no deadline for municipalities to finish preparing their financial statements. Till the end of June of 2018 of writing this thesis, no one of the sample municipalities has disclosed its financial statements of 2017. The researcher has asked municipalities to send their reports to the researcher, such as Ramallah, Tubas, Hebron, and Nablus; those municipalities have replied that their reports have not been ready yet, only drafts are ready. So, the researcher recommends specifying the deadline before June which is the half of the next financial year. Instructions from MoLG need to be established and declared about the date of publishing the audited financial statements. The external auditor qualification affects the quality of the report. Donors determined the acceptable auditors for auditing MDLF. So, it is recommended that MoLG determine the auditors who are acceptable for LGUs and this will have a positive impact on issuing bonds.

3.4.3 Municipal bonds issuance variables

These represent descriptive variables that are proposed as the best practices and the most applicable ones in Palestine. With the method of coding implemented in this research to test the effect of each ratio on the following municipal bonds issuance variables:

1. Par value (from USD 1,000 to USD 10,000)

The bond face value is also referred to as the par value or the principal amount. When the bond's price is below the par value, the bond is sold "at a discount." Whereas, when the bond's price is above the par value, it is sold "at a premium."

2. Maturity of bonds (short- term bonds 1-3 years, or medium bonds 3-7 years, or long-term ones that take more than a decade).

Long-term financing of the infrastructure projects will support municipalities with liquidity and avoid the pressure of short-term maturities. Strategic plans demonstrate borrowing capacity for municipalities. The suggested projects of municipalities force them to resort either to short, medium or long-term borrowings. The required projects from municipalities' strategic plans are at Appendix 3.

Strategic plans for municipalities contain many projects that wait for financing; this financing depends mainly on grants, not borrowing nor financial instruments. Many of the delayed projects are long overdue. However, this may not exceed the reasonably expected economic life of the project being financed (Hemsley & Huffer, 2006). Providing a concrete value for how much LGUs can borrow while maintaining fiscal balance over the course of full repayment of the debt (Farvacque-Vitkovic & Kopanyi, 2014). In Palestine, most

of the strategic plans include projects that take 4-5 years to be completed. The maturity of the bonds is determined by the average projects lifetime which are delayed. As a result, medium municipal bonds are preferred. They help mainly in preventing overborrowing and reducing the possibility that LGUs will default on their debt.

3. Bond type

Revenue bond type is recommended and supported by certain investment projects which will generate revenues upon their completion. These revenues generally cover the cost of the bond which consists of the principal and the interest. These bonds encourage new projects and more investments. Accordingly, bonds should never be used to finance the usual operating activities or the covering budget deficits.

4. Method of sale

For the issuance of the bonds, negotiated sale or private placement decision should be made. These two options have been discussed with their pros and cons in the literature review. Despite that competitive underwriting which usually produces more efficient, transparent, and equitable outcomes, most municipal bonds are sold through negotiated underwriting and they are guaranteed in advance of the sale. A bank that sells the bonds to the public is the underwriter. Bonds repayment has two options for the principal and

the interest either once at maturity or by installments; interest could also be paid annually or semi-annually.

5. Risk-return relationship

The capacity of a local government to borrow depends on two factors:

the projected local revenues that can be used to pay or cover future debt service and the size besides structure of the existing debt, that is; the average maturity and interest rates, which together determine the debt service for the upcoming years (Farvacque-Vitkovic & Kopanyi, 2014). A definite proof that funds are successfully managed and associated with the revenue-generating project does not need rigidity (Samonikov et al., 2016).

Every financial instrument has a risk-return relationship. Valuation is the process that measures this relationship (Gitman, 2004). Many articles show modules that calculate bond prices and bond yields. In general, interest rate has a direct positive relationship with the bond maturity. For LGUs, the cost of borrowing is vital but there is a need to be calculated based on the existed interest rates. Since 2000, the interest rate average differs for various maturities, interest rates of LGUs' borrowing have decreased due to the increased competition among banks on the capital market (Bajo & Primorac, 2010). Since 2006, interest rates on local government units borrowing increased again, exceeding the level of 6% as in Croatia.

MSRB rule G-33 explained equations particular for each type of municipal bonds. As we mentioned earlier, municipal bonds risks include the following: interest rate risk, call risk, liquidity risk, credit risk, political risk, and inflation risk.

Auditor report recalls risks management for each municipality, some are parallelized with municipal bonds risks, like credit risk, interest rate risk and liquidity risk. Other financial risks are foreign currencies risk and operational risk that is inherent in municipal activities.

Chapter Four

Empirical Findings and Analysis

1. Macroeconomic variables

The population is reflected in the macroeconomic variables through per capita ratios. The population that is available for municipalities till the year 2016 only. New investments will generate opportunities that can reduce unemployment. From the research sample (Appendix 2, 2015-2016), we notice that 8 out of 11 municipalities have had a decreasing revenue per capita ratio, which illustrates the need of new ways of financing.

Ratios that measure the macroeconomic variable for each municipality are analysed in appendix 2. The results of each ratio will affect the issuance of municipal bonds in a different way; the analysis for the results of each ratio is included in the following tables: Avg expenditure per capita in Table 4.11, avg revenue per capita in Table 4.12, unemployment for the year 2017 in Table 4.13, and the cost of labour in Table 4.13.

On budgets gate, each of the salaries and administrative expenses have different sheets and modules to be filled; some municipalities have not filled the salaries and administrative expenses. Although they have filled other expenses and revenues total sheets. LGUs have complained about budgets gate, describing the process as very hard and time

consuming because it demands including the percentages of every department separately.

The researcher has faced a lot of difficulties in the collection of data. Ramallah municipality filled out 2016 modules but without including the percentages of salaries and the administrative expenses. Moreover, some municipalities do not have data of the budget because it is not approved from MoLG. For example, data of 2017 for Hebron municipality has not been included, data of Bethlehem and Ramallah Municipalities for 2015 has not been sent to the budget gate which is the MoLG database.

2. Status variables

Actual data from MoLG budget gate is obtained, most of the sample municipalities had the variance reports according to the MoLG unified chart of accounts, this report explains the variance between actual and budgeted data.

Ten municipalities out of 11 from our sample have information about their financial position. Not all municipalities have filled out the required data completely for the year 2017. For instance, Tulkarm municipality neither published the information nor answered the researcher's questions.

Net income from financial statements has been measured by the net income ratio. Net income has a different value than revenues minus expenses in the budget gate, which is measured by mandatory surplus

operating budget, total revenues and total expenditures. Each factor was taken into consideration with different ratios.

However, MoLG need to identify the differences between the surplus and the deficit results of the budget gate in Table 4.1, in addition to the financial statements of each municipality under the cash basis of cash receipts and payments statement, or the accrual basis of the financial performance statements concerning net income.

Different ratios and data analysis tools are employed to measure each subgroup variable of the status variables, through the analysis, the result of each ratio was used for the rating of the sample municipalities and these total coding formed the best issuers of municipal revenue bonds.

a. Municipality size

The population has expressed a size of measure. Regarding the owned assets, a vertical analysis of a land rate out of the total assets has been conducted (Appendix 2). Furthermore, the operating and the profitable activities of all of the local governments are analyzed.

Table 4.1: Revenues and expenditures analysis

Municipality	Year	Total Revenues	Revenues Growth Rate	Total expenditure	Expenditure Growth Rate	Surplus/ Deficit	Total Revenues /Total Expenditures
Tubas	2015	6,142,069		3,919,237		2,222,832	1.57
	2016	5,103,837	-17%	5,113,619	30%	(9,782)	1.00
	2017	6,956,008	36%	5,696,195	11%	1,259,813	1.22
Tulkarm	2015	73,288,131		74,616,187		(1,328,056)	0.98
	2016	69,833,428	-5%	69,216,774	-7%	616,654	1.01
	2017	82,368,002	18%	540,515,688	681%	(458,147,686)	0.15
Jericho	2015	27,671,104		21,770,801		5,900,303	1.27
	2016	20,689,282	-25%	22,762,574	5%	(2,073,292)	0.91
	2017	21,932,086	6%	1,367,254	-94%	20,564,832	16.04
Al- Bireh	2015	45,979,268		14,901,438		31,077,830	3.09
	2016	39,107,291	-15%	28,309,135	90%	10,798,156	1.38
	2017	33,989,618	-13%	27,279,191	-4%	6,710,427	1.25
Hebron	2015	77,075,813		62,020,238		15,055,575	1.24
	2016	74,252,031	-4%	49,032,573	-21%	25,219,458	1.51
	2017		-100%		-100%	-	N/A
Jenin	2015	21,175,905		7,708,127		13,467,778	2.75
	2016	17,783,973	-16%	11,713,729	52%	6,070,244	1.52
	2017		-100%	-	-100%	-	N/A

Bethlehem	2015			-		-	N/A
	2016	17,048,242	N/A	12,515,145	N/A	4,533,097	1.36
	2017	20,721,097	22%	8,574,389	-31%	12,146,708	2.42
Ramallah	2015			-		-	N/A
	2016	61,245,669	N/A	32,117,279	N/A	29,128,390	1.91
	2017	72,554,235	18%	46,745,729	46%	25,808,506	1.55
Salfeet	2015	15,672,065		13,069,780		2,602,285	1.20
	2016	17,102,780	9%	13,966,898	7%	3,135,882	1.22
	2017	19,367,249	13%	13,745,042	-2%	5,622,207	1.41
Qalqilia	2015	68,378,617		67,210,912		1,167,705	1.02
	2016	68,636,455	0%	75,138,181	12%	(6,501,726)	0.91
	2017	79,923,548	16%	50,133,226	-33%	29,790,322	1.59
Nablus	2015	128,031,661		110,920,779		17,110,882	1.15
	2016	98,750,417	-23%	124,653,319	12%	(25,902,902)	0.79
	2017	108,101,417	9%	127,538,056	2%	(19,436,639)	0.85
		1,398,881,298		1,642,271,493	1188%	(243,390,195)	0.85

b. Outstanding debt, and financial distress

Benchmarking which is a type of cross sectional analysis has been conducted in order to compare and recognize the firms which are better than the average. For the following ratios, sample municipalities formed the benchmark that can be used for LGUs in Palestine:

Table 4.2: Benchmark Ratios of LGUs in Palestine

Ratio	Result
Change in net assets	21%
Current ratio	2.49
Debt to assets	21%
Return on Assets	0.03%

Six of the sample municipalities participated in this benchmark. As noticed, extreme ratio results are associated with some of the most populated municipalities. Further details of other cross-sectional ratios are demonstrated in Table 4.3:

Table 4.3: Highest ratios and lowest values

Ratio	Benchmark	Highest value	Municipality	Year	Lowest value	Municipality	Year
Change in net assets	21%	596%	Salfeet	2015	-86%	Hebron	2016
Current ratio	2.49	9.27	Al- Bireh	2014	0.40	Hebron	2015
Debt to assets	21%	92%	Hebron	2017	1%	Al- Bireh	2014
Return on Assets	0.03%	8%	Ramallah	2015	-5%	Hebron	2015

Many financial ratios are used in the study and analysed based on the average of the previous years or the growth average; each ratio affects the issuance of municipal bonds in a different way:

- Avg collection rate of accounts receivable
- Avg change in net assets
- Current ratio
- Debt to assets
- Return on assets
- Net lending
- Net working capital
- Avg change of net income
- Avg Total Revenues and total expenditures

If a current ratio is low (below 1) and current liabilities exceed current assets, the entity may have problems meeting its short-term obligations. A current ratio that is below 1 indicates that the entity does not have enough liquid assets to cover its current liabilities. The best current ratio is between 1.2 to 2.

Some municipalities considered investment in distribution companies as an additional category for assets in the financial statements.

For example, Nablus municipality considered such investments as current assets and the rest of the sample municipalities treated them as fixed assets. However, this affected the benchmark ratio of the sample municipalities and resulted in a high current ratio of 2.49. Other liquidity ratio was affected by this divergence treatment and resulted in the following:

Net working capital in shekels		Municipality	Year
Highest value	452,070,122	Nablus	2014
Lowest value	308,424,517-	Hebron	2017

The return on assets (ROA) shows that the municipality's assets are profitable in generating revenue. ROA is over 5%; it is generally considered good. The higher the ROA percentage, the better is the case since such a thing demonstrates that an entity earns more money on less investment

The debt to total assets ratio is an indicator of financial leverage; it shows the percentage of total assets that were financed by creditors, liabilities and debts. The debt to total assets ratio is calculated by dividing a municipality's total liabilities by its total assets. From a pure risk perspective, lower ratios (0.4 or lower) are considered better debt ratios since it demonstrates that a municipality uses less leverage.

Net income growth is not stable for municipalities; there is a huge move between each year's values. The highest average of net income growth is for Bethlehem municipality, and the lowest value is for Al- Bireh municipality.

Table 4.4: Net income of the financial statements

Growth rate analysis					
Municipality Name	2014	2015	2016	2017	Average change
Tubas	-2762%	-27%	-88%	1467%	-352%
Salfeet	-66%	15%	23%	7%	-5%
Qalqilia	-61%	-69%	78%	-219%	-68%
Nablus	-190%	-125%	-371%	-25%	-178%
Ramallah	-35%	-924%	4%		-318%
Hebron	8%	-62%	-53%		-36%
Bethlehem	40%	-9%	18%		16%
Al- Bireh	-53%	-2569%	45%		-859%
Jenin	62%	22%	-44%		13%
Jericho			-209%		-209%

As it was explained before, income is important but it is not the measure for public institutions. LGUs are divided to separate budgets for business enterprises other than the budget for general operating. For Nablus municipality, deficit was considered in 2016, it was 25 million, and it decreased to 19 million in 2017. This is an excellent growth indicator, but it is still alarming until reaching a zero deficit. Profitable business enterprises are supposed to have a surplus; theoretically, this surplus will cover the shortage in the operating budget. According to the previous results, some municipalities had an unacceptable deficit in profitable business enterprises. This deficit is due to low collection rates, unproductive expenses, weak financial management and hidden or disguised unemployment, or labour hoarding. Accordingly, further analysis to these reasons is required. For the purpose of testing, the separation between budgets is helpful and it was carried out in Table 4.5 and 4.6. Table 4.5 shows the analysis of 2016 budgets; it shows surplus and deficit that result from each of the profitable and the operating budgets:

Table 4.5: Results of 2016 Budgets

Profitable Budgets	Revenues	Expenses	Surplus/ deficit	Operating Budget	Revenues	Expenses	Surplus/ deficit	At the municipality level	Total Surplus/ deficit
Nablus	39,428,984	46,833,044	(7,404,060)		59,321,433	77,829,275	(18,498,842)	Nablus	(25,902,902)
Qalqilia	60,245,283	52,673,938	7,571,345		8,391,172	22,464,243	(14,073,071)	Qalqilia	(6,501,726)
Salfeet	13,092,611	10,247,508	2,845,103		4,010,169	3,719,390	290,779	Salfeet	3,135,882
Ramallah	-	-	-		61,245,669	32,117,279	29,128,390	Ramallah	29,128,390
Bethlehem	201,454	100,184	101,270		16,846,788	12,414,961	4,431,827	Bethlehem	4,533,097
Jenin	4,535,386	4,172,309	363,077		13,248,587	7,541,420	5,707,167	Jenin	6,070,244
Hebron	46,043,211	21,750,618	24,292,593		28,208,820	27,281,955	926,865	Hebron	25,219,458
Al- Bireh	4,984,971	3,686,803	1,298,168		34,122,320	24,622,332	9,499,988	Al- Bireh	10,798,156
Jericho	9,241,612	7,241,957	1,999,655		11,447,670	15,520,617	(4,072,947)	Jericho	(2,073,292)
Tulkarm	58,338,226	45,658,540	12,679,686		11,495,202	23,558,234	(12,063,032)	Tulkarm	616,654
Tubas	1,913,228	1,878,134	35,094		3,190,609	3,235,485	(44,876)	Tubas	(9,782)

Analysis of the year 2017 to separate surplus and deficit resulted from each of the profitable budgets and operating budget:

Table 4.6: Results of 2017 Budgets

Profitable Budgets	Revenues	Expenses	Surplus/ deficit	Operating Budget	Revenues	Expenses	Surplus/ deficit	At the municipality level	Total Surplus/ deficit
Tulkarm	69,323,362	533,790,174	(464,466,812)		13,044,640	6,725,514	6,319,126	Tulkarm	(458,147,686)
Jericho	12,201,007	539,257	11,661,750		9,731,079	827,997	8,903,082	Jericho	20,564,832
Bethlehem	227,942	48,072	179,870		20,493,155	8,526,317	11,966,838	Bethlehem	12,146,708
Ramallah	4,257,800	3,331,709	926,091		68,296,435	43,414,020	24,882,415	Ramallah	25,808,506
Al- Bireh	5,049,935	2,649,256	2,400,679		28,939,683	24,629,935	4,309,748	Al- Bireh	6,710,427
Tubas	1,602,611	1,575,252	27,359		5,353,397	4,120,943	1,232,454	Tubas	1,259,813
Jericho	12,201,007	539,257	11,661,750		9,731,079	827,997	8,903,082	Jericho	20,564,832
Salfeet	14,190,684	9,873,924	4,316,760		5,176,565	3,871,118	1,305,447	Salfeet	5,622,207
Qalqilia	62,822,351	42,847,209	19,975,142		17,101,197	7,286,017	9,815,180	Qalqilia	29,790,322
Nablus	43,900,097	57,317,638	(13,417,541)		64,201,320	70,220,418	(6,019,098)	Nablus	(19,436,639)

Analysis of the year 2017 profitable budgets, surplus and deficit results are:

Table 4.7: Analysis of profitable budgets results

Profitable Budgets Analysis	Nablus	Qalqilia	Salfeet	Tubas	Al- Bireh	Ramallah	Tulkarm	Jericho	Bethlehem
Water and Wastewater	(4,749,736)	3,569,397	773,558	12,857	2,345,377	926,091	6,416,815	8,779,160	-
Electricity	-	12,720,813	3,077,525	8,194	-	-	(471,836,264)	-	-
Dynamometer	-	265,351	465,676	6,308	-	-	-	-	-
Parking Complex	(41,928)	(56,603)	-	-	-	-	719,200	-	-
Slaughter houses	(370,490)	93,302	-	-	193,500	-	233,437	108,459	-
Parks and Museums	(5,473,855)	2,872,659	-	-	-	-	-	1,871,615	-
Fruits and Vegetables Markets	146,281	510,222	-	-	(138,199)	-	-	902,516	179,870
Treatment Plants	(2,927,813)	-	-	-	-	-	-	-	-
Total Surplus/ Deficit	(13,417,541)	19,975,142	4,316,760	27,359	2,400,679	926,091	(464,466,812)	11,661,750	179,870

c. Financial reporting quality

The researcher depended in her analysis on grouping the sample municipalities according to the level of disclosure of financial statements on their websites for the last five years, in addition to the statements required by IPSAS based on the accounting basis.

Results of the disclosure variable by grouping municipalities is listed, starting from the municipalities that did not disclose any financial statements for the years on research:

Group One	No disclosure of any financial statement
1	Al- Bireh municipality
2	Qalqilia municipality
3	Tulkarm municipality
4	Jenin municipality

Municipalities in Table 4.9 demonstrates the requirements of cash basis by IPSAS, which is the statement of cash receipts and payments:

Table 4.8: Disclosure of the cash receipts and payment statements

Group Two	Statement of cash receipts and payments	2013	2014	2015	2016	2017
5	Bethlehem municipality	Yes	yes	yes	yes	no
6	Jericho municipality	No	no	no	yes, without notes	no
7	Nablus municipality	No	no	yes, without notes	yes	no

Results and statements required based on the accrual basis by IPSAS are:

- a. A statement of the financial position.
- b. A statement of the financial performance.
- c. A statement of changes of net assets and equity.
- d. A cash flow statement.

Table 4.9: Disclosure of the financial statements

Group Three	Municipality	St.	2013	2014	2015	2016	2017
8	Ramallah municipality	a.	yes	yes without notes	yes without notes	yes without notes	no
		b.	yes	yes without notes	yes without notes	yes without notes	no
		c.	no	yes without notes	yes without notes	yes without notes	no
		d.	yes	yes without notes	yes without notes	yes without notes	no
9	Tubas municipality	a.	no	yes	yes	yes	no
		b.	no	yes	yes	yes	no
		c.	no	yes	yes	yes	no
		d.	no	yes	yes	yes	no
10	Salfeet municipality	a.	yes	yes without notes	no	no	no
		b.	yes	yes without notes	no	no	no
		c.	yes	yes without notes	no	no	no
		d.	yes	yes without notes	no	no	no
11	Hebron municipality	a.	no	no	no	yes draft	no
		b.	no	no	no	yes draft	no
		c.	no	no	no	yes draft	no
		d.	no	no	no	yes draft	no

The disclosure index from 2013 to 2017 on the municipalities' websites is in Table 4.8. The quality of disclosure for the last five years for LGUs is low; the average disclosure for the following sample municipalities is below 50%. This disclosure index has been calculated as an average for the sample municipalities; each municipality has its own disclosure percentage as shown in Table 4.10.

Table 4.10: Disclosure index of the sample municipalities

#	Municipality	Out of %100
1	Al- Bireh	0
2	Qalqilia	0
3	Tulkarm	0
4	Jenin	0
5	Hebron	20
6	Jericho	20
7	Nablus	40
8	Salfeet	40
9	Tubas	60
10	Ramallah	75
11	Bethlehem	80
	Average	31%

Issuance guidelines that are based on subgroup variables and financial analysis ratios are represented in various tables. For instance, ratios of macroeconomic variables are represented in tables 4.11-4.14. Status variable which shows the subgroup variable of municipality size is illustrated in tables 4.15-4.16, and financial reporting quality is represented in table 4.17. Whereas, the ratios of outstanding debt, and the financial distress variables are demonstrated in tables 4.18-4.25.

Ratio results of the macroeconomic variables helped in determining the issuance variables.

Table 4.11: Avg Revenue Per Capita

Municipality	Avg Revenue Per Capita	Methodology, issuance variables	
Ramallah	1	Bond type	Revenue bonds to finance capital investment projects.
Salfeet	2	Method of sale	Underwriter " Banks", negotiated or competitive sales.
Qalqilia	3	Maturity	The highest rate municipality (11, 10, ...) needs a short-term injection, so short-term revenue bonds are required. Whereas, the smallest rate municipality (1, 2) needs long-term investment; it seeks for capital appreciation
Tulkarm	4		
Jericho	5		
Al- Bireh	6	Par value	The highest rate municipality (11,10, ...) need bonds from financial institution up to (10,000 USD), so they need high trust investors. Whereas the smallest rate municipality (1, 2) which has respectable financial status, its individual bonds reach up to (1,000 USD)
Nablus	7		
Bethlehem	8		
Jenin	9	Risk-return relationship	The highest rate municipality (11,10, ...) indicates high risk, whereas the smallest rate (1, 2) faces a low risk investment.
Hebron	10		
Tubas	11		

Table 4.12: Avg expenditure Per Capita

Municipality	Avg expenditure Per Capita	Methodology, issuance variables	
Qalqilia	1	Bond type	Revenue bonds to finance capital investment projects.
Salfeet	2	Method of sale	Underwriter " Banks", negotiated or competitive sales.
Tulkarm	3	Maturity	The highest rate municipality (11, 10, ...) needs a short-term injection, so short-term revenue bonds are required. Whereas, the smallest rate municipality (1, 2) needs long-term investment; it seeks for capital appreciation
Jericho	4		
Ramallah	5		
Nablus	6	Par value	The highest rate municipality (11,10, ...) need bonds from financial institution up to (10,000 USD), so they need high trust investors. Whereas the smallest rate municipality (1, 2) which has respectable financial status, its individual bonds reach up to (1,000 USD)
Al- Bireh	7		
Bethlehem	8		
Hebron	9		
Tubas	10	Risk-return relationship	The highest rate municipality (11,10, ...) indicates high risk, whereas the smallest rate (1, 2) faces a low risk investment.
Jenin	11		

Table 4.13: Unemployment 2017

Municipality	Unemployment 2017	Methodology, issuance variables	
Hebron	1	Bond type	Revenue bonds to finance capital investment projects.
Tubas	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Bethlehem	3	Maturity	The lower rate (10, 9...) municipalities have the minimum unemployment rate. Thus, they need a short-term injection of revenue bonds. Whereas the upper rate (1, 2) municipalities need long-term investment; they seek capital appreciation.
Nablus	4		
Jenin	5		
Al- Bireh	6	Par value	The lower rate (10, 9...) municipalities have the minimum unemployment rate and they have a better economic situation. So, bonds can be issued to individuals up to (1,000 USD), while the upper rate municipalities of (1, 2) need to take bonds from financial institution up to (10,000 USD) to create new jobs and to absorb unemployment.
Ramallah	6		
Salfeet	7		
Jericho	8		
Tulkarm	9	Risk-return relationship	High risk acquires higher returns.
Qalqilia	10		

Table 4.14: Cost of labour percent from total revenues

Municipality	Cost of labour percent from total revenues	Methodology, issuance variables	
Tubas	1	Bond type	Revenue bonds to finance capital investment projects.
Al- Bireh	2	Method of sale	Underwriter " Banks," negotiated or competitive sale.
Jericho	3	Maturity	The lower rate (11,10, ...) municipalities have the minimum cost of labour percent from the total revenues, so they need short-term injection of revenue bonds. Whereas, the upper rate municipalities (1, 2), need a long-term investment in order to reduce the percent from the revenues.
Ramallah	4		
Salfeet	5		
Hebron	6	Par value	The lower rate municipalities (11,10, ...) can issue bonds to individuals with (1,000 USD), while the upper rate municipalities (1, 2) have the maximum cost of labour percentage from total revenues, so they need financial institution up to (10,000 USD).
Bethlehem	7		
Jenin	8		
Tulkarm	9		
Nablus	10	Risk-return relationship	The lower rate municipalities have a lower risk (11,10) as the cost of labour percent out of the total revenues is minimum. Whereas, the upper rate municipalities (1, 2), face high risks.
Qalqilia	11		

Ratio results from the status variables helped in determining the issuance variables, subgroup variable municipality size:

Table 4.15: Vertical analysis of land rate from total assets

Municipality	Vertical analysis of land rate from total assets	Methodology, issuance variables	
Tubas	1	Bond type	Revenue bonds to finance capital investment projects.
Al- Bireh	2	Method of sale	Underwriter " Banks," negotiated or competitive sale.
Jericho	3	Maturity	The highest rate municipalities (7,6,..) need a short-term injection of revenue bonds because they have fewer guarantees from lands. Whereas, the lowest rate ones (1, 2) can have long-term investments, and they can use the balance of the available land to guarantee bonds up to ten years.
Ramallah	4		
Salfeet	5		
Hebron	6	Par value	The highest rate (7,6, ...) municipalities need a short-term injection of revenue bonds; they need bonds up to (1,000 USD). Whereas, the smallest rate (1, 2) municipalities, can be financed by financial institution up to (10,000 USD).
Bethlehem	7		
Jenin	8		
		Risk-return relationship	The highest rate (7,6, ...) municipalities show high risks due to the lack of assets available to be guaranteed, whereas the lowest rate municipalities (1, 2) face a low risk investment

Table 4.16: Mandatory Avg Surplus of the Operating Budget

Municipality	Mandatory avg Surplus of Operating Budget		Methodology, issuance variables	
Ramallah	27,005,403	1	Bond type	Revenue bonds to finance capital investment projects.
Al- Bireh	6,904,868	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Jericho		3	Maturity	Municipalities with a minimum surplus that starts from (9,8, 7...) rating need a short-term injection of revenue bonds. Whereas, municipalities that have the smallest rate (1, 2) can be provided with strategic projects in the long run.
Jenin	5,707,167	4		
Bethlehem	4,431,827	5		
Jericho	2,415,067	6	Par value	Financial institutions give up to (10,000 USD) to municipalities with the ratings of (9,8, 7...), whereas the smallest (1, 2) rating ones which have respectable financial status, individual bond can reach up to (1,000 USD) The highest (11,10, ...) rate municipalities need to reach the minimum requirement of the operating budget surplus. Municipalities with the rates of (9,8, 7...) face higher risks. Whereas, the smallest (1, 2) rate municipalities, have a low risk investment.
Hebron	926,865	7		
Salfeet	798,113	8		
Tubas	593,789	9		
Qalqilia	2,128,945-	10	Risk-return relationship	
Tulkarm	12,063,032-	11		
Nablus	-12,258,970	12		

Table 4.17: Financial reporting quality

Municipality	Financial reporting quality	Methodology, issuance variables	
Bethlehem	1	Bond type	Revenues bonds to finance capital investment projects.
Ramallah	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Tubas	3	Maturity	Municipalities with the highest rate (6,5) need a short-term injection of revenue bonds. Whereas the smallest rate ones (1, 2), need long-term investments, and they seek for capital appreciation.
Salfeet	4		
Nablus	4		
Hebron	5	Par value	Based on the disclosure requirements, the highest rate municipalities (6,5), with the minimum disclosure, can take financing for bonds from financial institution up to (10,000 USD), Whereas, municipalities with rate of (1, 2) and they have respectable disclosure and better transparency, their individual bonds reach up to (1,000 USD).
Jericho	5		
Tulkarm	6		
Qalqilia	6		
Al- Bireh	6	Risk-return relationship	Municipalities with the highest rate (6,5) indicate high risk, whereas municipalities with the smallest rate (1, 2) have a less risk investment and they can have better interest terms.
Jenin	6		

Ratios for subgroup variable outstanding debt, and financial distress

Table 4.18: Avg change in net assets

Municipality	Avg change in net assets		Methodology, issuance variables	
Salfeet	151%	1	Bond type	Revenue bonds to finance capital investment projects.
Ramallah	0%	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Tubas	-1%	3	Maturity	Based on net assets change which measures the sustainability of municipalities, the highest rate (6,5) need a short-term injection of revenue bonds. Whereas the smallest rate (1, 2), needs a long-term investment.
Nablus	-2%	4		
Qalqilia	-2%	4		
Al- Bireh	-12%	5	Par value	The highest rate municipalities (6,5) need bonds from financial institution up to (10,000 USD). While, (1, 2) municipalities can target individual bonds up to (1,000 USD). Revenue bonds to finance capital investment projects.
Hebron	-30%	6		
			Risk-return relationship	Underwriter " Banks", negotiated or competitive sale.

Table 4.19: Debt to assets

Municipality	Debt to assets		Methodology, issuance variables	
Al- Bireh	0.02	1	Bond type	Revenue bonds to finance capital investment projects.
Tubas	0.05	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Ramallah	0.08	3	Maturity	Based on debt to assets, all the municipalities have a small amount of debt (less than 1) with lower debt ratios (1,2) indicating lower degrees of debt financing. So, they can ask for long-term investments. Whereas, municipalities at the highest rate (7, 6,5) need a short-term injection of revenue bonds.
Salfeet	0.23	4		
Qalqilia	0.24	5		
Nablus	0.25	6	Par value	The highest rate municipalities (7,6,5) need bonds from financial institution up to (10,000 USD). Whereas, (1, 2) rate municipalities can target individual bonds up to (1,000 USD).
Hebron	0.65	7		
			Risk-return relationship	Risk increases when ratio results for each 1 shekel asset a close amount of liability.

Table 4.20: Return on Assets

Municipality	Return on Assets		Methodology: issuance variables	
Tubas	4%	1	Bond type	Revenue bonds to finance capital investment projects.
Salfeet	4%	1	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Ramallah	3%	2	Maturity	Municipalities with the highest rate (6,5,4, ...) need a short-term injection of revenue bonds. Whereas, the smallest rate ones with (1, 2), can have a long-term investment because they are characterized with a better return on assets.
Al- Bireh	1%	3		
Nablus	0%	4		
Qalqilia	-1%	5	Par value	Municipalities with the highest rate (6,5, 4,) need a short-term injection of revenue bonds; they need bonds that reach up to (1,000 USD) from individuals, whereas the smallest rate (1, 2) municipalities can be financed by financial institution up to (10,000 USD).
Hebron	-3%	6		
			Risk-return relationship	Municipalities with the highest rate (6, 5,) have higher risks in investing. Whereas, municipalities with the smallest rate (1, 2) face a low risk investment.

Table 4.21: Current ratio

Municipality	Current ratio		Methodology: issuance variables	
Al- Bireh	7.8	1	Bond type	Revenue bonds to finance capital investment projects.
Nablus	3.3	2	Method of sale	Underwriter “Banks”, negotiated or competitive sale.
Salfeet	2.1	3	Maturity	Based on current ratios, municipalities at the highest rate (7, 6,5) need a short-term injection of revenue bonds to balance the liquidity situation quickly. Whereas, municipalities at the smallest rates (1, 2) need long-term investments because they maintain a good liquidity position.
Tubas	1.8	4		
Ramallah	1.1	5		
Qalqilia	0.6	6	Par value	The highest rate municipalities (7, 6, 5) need bonds from financial institution up to (10,000 USD), While (1, 2) rate municipalities can target individual bonds up to (1,000 USD).
Bethlehem	0.6	6		
Hebron	0.4	7		
			Risk-return relationship	The highest rates (7, 6,5) indicate high risk in terms of repayment, whereas the smallest rates (1, 2) indicate a low risk investment due to the liquidity available at municipalities.

Table 4.22: Net lending

Municipality	Net lending		Methodology: issuance variables	
Nablus	174,274,976	1	Bond type	Revenue bonds to finance capital investment projects.
Al- Bireh	35,635,545	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Ramallah	31,557,729	3	Maturity	Based on net lending, municipalities at the highest rate (7, 6,5) need a short-term injection of revenue bonds. Whereas, municipalities at the smallest rate (1, 2) need long-term investments because they can maintain a good liquidity position.
Salfeet	10,289,687	4		
Tubas	7,202,313	5		
Qalqilia	54,537,087-	6	Par value	The highest rate municipalities (7, 6, 5) need bonds from financial institution up to (10,000 USD). While, (1, 2) municipalities can target individual bond up to (1,000 USD).
Hebron	213,682,061-	7		
			Risk-return relationship	The highest rates (7, 6,5) indicate higher risks in terms of repayment. Whereas, the smallest rates (1, 2) indicate a less risk investment due to the liquidity available at municipalities.

Table 4.23: Net working capital

Municipality	Net working capital		Methodology: issuance variables	
			Bond type	Revenue bonds to finance capital investment projects.
Nablus	366,296,571	1	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Al- Bireh	74,949,736	2	Maturity	Based on net working, capital municipalities at the highest rates (8, 7, 6, ...) need a short-term injection of revenue bonds. Whereas, municipalities at the smallest rates (1, 2) need long-term investments because they maintain a good liquidity position.
Salfeet	14,630,387	3		
Tubas	6,081,666	4		
Ramallah	2,217,097	5	Par value	The highest rate municipalities (8, 7, 6...) need bonds from financial institution up to (10,000 USD). While, (1, 2) municipalities can target individual bonds up to (1,000 USD).
Bethlehem	2,242,809-	6		
Qalqilia	47,530,014-	7		
Hebron	272,275,328-	8	Risk-return relationship	The highest rates (8, 7, 6...) indicate higher risk in terms of repayment. Whereas, the smallest rates (1, 2) show a low risk investment due to the liquidity available at municipalities.

Table 4.24: Avg change of net income

Municipality	Avg change of net income		Methodology: issuance variables	
Bethlehem	16%	1	Bond type	Revenue bonds to finance capital investment projects.
Jenin	13%	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Salfeet	-5%	3	Maturity	Short-term bonds are needed for municipalities which are rated as (10, 9...). On the other hand, long-term bonds are acceptable for municipalities that have better net income analysis (1, 2).
Hebron	-36%	4		
Qalqilia	-68%	5		
Nablus	-178%	6	Par value	Based on the change of net income in municipalities with the highest ratings (10, 9), they can be financed from financial institutions up to (10,000 USD). While, (1, 2) municipalities can target individual bonds up to (1,000 USD).
Ramallah	-318%	8		
Jericho	-209%	7		
Tubas	-352%	9	Risk-return relationship	higher risk is associated with municipalities with the lowest ratings.
Al- Bireh	-859%	10		

Table 4.25: Avg Total Revenues /Total Expenditures

Municipality	Avg Total Revenues /Total Expenditures		Methodology: issuance variables	
Jericho	6.07	1	Bond type	Revenue bonds to finance capital investment projects.
Jenin	2.13	2	Method of sale	Underwriter " Banks", negotiated or competitive sale.
Al- Bireh	1.90	3	Maturity	Municipalities with the highest rate (11,10, ...) need a short-term injection of revenue bonds because their revenues are less than expenditures, so they need quick revenue generating. Whereas, municipalities with the smallest rates (1, 2) can work until long-term investment finish.
Bethlehem	1.89	4		
Ramallah	1.73	5		
Hebron	1.38	6	Par value	Municipalities with the highest rate (11,10) can be financed from financial institution up to (10,000 USD) since citizens need high investments to raise expenditure coverage from revenues. Whereas, municipalities with the smallest rates (1, 2), which have respectable financial status, they can target individual bonds up to (1,000 USD).
Salfeet	1.28	7		
Tubas	1.26	8		
Qalqilia	1.18	9	Risk-return relationship	The highest rate (11,10) indicate high risks. Whereas, companies with the smallest rates (1, 2), have a less risk investment because more than one means how much income yielded to the municipality.
Nablus	0.93	10		
Tulkarm	0.71	11		

Table 4.26: Hypothesis test

Final	1. Macroeconomic variables				2. Status variables												Result Rejected, R for the hypothesis	
Municipality	Avg revenue per capita	Avg expenditure per capita	Unemployment 2017	Cost of labour percent from total revenues	Vertical analysis of land rate from total assets	Mandatory avg surplus operating budget	Financial reporting quality	Avg collection rate of accounts receivables	Avg change in net assets	Current ratio	Debt to assets	Return on assets	Net lending	Net working capital	Avg change of net income	Avg total revenues /total expenditures	Standard deviation test	Hypothesis, if st above 1 then rejected
Hebron	10	9	1	6	4	7	5	7	6	7	7	6	7	8	4	6	2	R
Nablus	7	6	4	10	7	12	4	3	4	2	6	4	1	1	6	10	3	R
Tulkarm	4	3	9	9		11	6									11	3	R
Qalqilia	3	1	10	11	1	10	6	2	4	6	5	5	6	7	5	9	3	R
Al- Bireh	6	7	6	2	3	3	6	4	5	1	1	3	2	2	10	3	2	R
Jenin	9	11	5	8	10	4	6								2	2	3	R
Ramallah	1	5	6	4	2	1	2	7	2	5	3	2	3	5	8	5	2	R
Bethlehem	8	8	3	7	9	5	1	5		6				6	1	4	3	R
Jericho	5	4	8	3	8	6	5	8							7	1	2	R
Tubas	11	10	2	1	6	9	3	1	3	4	2	1	5	4	9	8	3	R
Salfeet	2	2	7	5	5	8	4	6	1	3	4	1	4	3	3	7	2	R

Final Result

The hypothesis of this study, which states that neither macroeconomic variables nor municipality status affect the issuance of "municipal revenue bonds," has been rejected.

According to the analysis conducted in this study, macroeconomic variables and municipality status affect the issuance of "municipal revenue bonds" which are targeted to finance capital investments of local government units in Palestine.

Macroeconomic variables that are measured by revenues and expenditures per capita, cost of labour, and unemployment affect the issuance of municipal bonds.

Municipal status variables affect the issuance of municipal bonds which have subgroup variables such as: municipality size, financial reporting quality, outstanding debt, and financial distress.

Palestinian municipal candidates for issuing bonds are rated by the highest total marks in Table 4.26. Using the coding for municipalities shows which ones have the best risk return relationship. Therefore, the most suitable Palestinian bond issuers are the municipalities in sequence: Hebron, Qalqilia, Nablus, Tubas, and Salfeet.

Qalqilia and Nablus municipalities are excluded; Qalqilia did not disclose its strategic plans and it did not achieve the mandatory condition

of the general operating budget in 2016. The case is the same for Nablus municipality; it is required to have a minimum surplus in the general operating budget so as to reach creditworthiness, as Nablus has a good potential for financing. Also, Nablus and Qalqilia got B+ at MDLF 2017 ranking, so they need to reach the A category because MDLF ranking is used as a ceiling for financing. Although Tubas and Hebron got the highest rates; they are one step away from category A and a slight improvement can take them to the highest ranking, their ranking of B++ is exceptional. However, Salfeet municipality got an A at MDLF ranking.

For each accepted municipality (Salfeet, Hebron and Tubas), the most suitable project was chosen from Appendix 3. For instance, Hebron is seeking financing of USD 5 million for the establishment of parking lots and complexes for Public vehicles (SDIP 2016-2019). Whereas, Salfeet is seeking financing of USD 5 million for the creation of a recreational city (SDIP 2013-2016). Tubas is seeking financing of USD 1 million for the drilling and equipping agricultural water well in the Tubas Plain area (SDIP 2014).

In Palestine, most of the strategic plans include projects that take 4-5 years to be completed. As a result, medium maturity for municipal revenue bonds is preferred. The decision concerning the best sale method is up to the municipality in order to get the lowest cost, which can be sold to financial institutions of USD 10,000 or to individuals of USD 1,000.

Chapter Five

Conclusions and Recommendations

5.1 Conclusion

Regarding the debate about the financing of municipal projects, there is a need to shift from grants dependence to a more proper discussion of the new financial instruments, particularly revenue bonds. If municipalities are considered bad service delivery, the new strategy should be implemented to prevent them from becoming worse. In Palestine, the trend of revenue per capita is decreasing in 73% of the sample. The international investment position shows that Palestinian investments outside Palestine are higher than the foreign investments in the Palestinian enterprises. Based on an analysis of the debt to assets ratio, all Palestinian municipalities have a small amount of debt (less than 1), so there is a room of getting benefit from some additional debts.

Revenue bonds are chosen because they finance specific, designated public projects that generate discrete streams of income (Joel, et al, 2010). In Palestine, the most applicable projects are the ones that take advantage of the existing assets that can be used in productive projects (Farvacque-Vitkovic & Kopanyi, 2014). The municipalities possess assets such as lands that are specified for parking lots, museums, highways, water and sewer systems, parks including playgrounds, cycling tracks, parks of new modern types, zoos, flower parks, and aqua parks.

The most critical task is the development of the legal framework for the issuance of municipal bonds. The Securities Law No. (12) of the year 2004 defined bonds as the securities issued either by a public shareholding company or government agencies or public enterprises (PNA, 2004). Securities Issuance Instructions, issued in 2008 by the Palestinian Capital Market Authority pursuant to the Securities Law No. (12) in article (2), stated that government institutions and municipalities were authorized as securities issuers, this article delegated these bond issuers to issue bonds (PCMA, 2008). In conclusion, there are no special instructions for municipal bonds. However, municipal bonds are considered as financial securities, so their issuance can be guided by the instructions of issuing financial securities.

LGUs mayors cannot be responsible for municipal bonds pay back specially the long- term bonds, because they should be elected every four years. The mayor can be nominated for two elections period. This would make the maximum legal elected period up to eight years. Municipal managers and financial officers should be responsible of issuing municipal bonds.

Municipal revenue bonds can solve the financing obstacle of the development projects of LGUs in Palestine. In Norway, municipal borrowing is allowed for the sake of investment only (Farvacque-Vitkovic & Kopanyi, 2014). Vazquez's golden rule demands the use of bonds proceeds for the new development investments, and not for current

expenditures. The results of this study are consistent with the previous studies, and they emphasize that no issuance is allowed until achieving mandatory surplus from the operating activities budget.

To issue municipal bonds LGUs creditworthiness should be significantly improved. This result is in line with the same result by Vazquez's findings in 2015. Creditworthiness must be achieved for the purpose of issuing municipal bonds. Creditworthiness can be improved through more transparent budgeting and accounting, this is in addition to the development of self-sufficient sources of revenues of the local governments. A municipal bond market relies on the public disclosure of the financial information by the municipalities. Financial information could be misleading if it is not provided adequately and based on the accounting standards. Municipalities could not get any financing without having a clear and a solid base of assets and operating revenues.

The characteristics of municipal bond issuance are determined according to the need of LGUs, the researcher concluded the most applicable measures to use as a rating model to test the creditworthiness of LGUs. Many financial ratios are used, each affects the issuance of municipal bonds in a different way. For example, macroeconomic variables are measured by revenues and expenditures per capita, cost of labour and unemployment rate.

Municipal status variables have subgroup variables of municipality size determined by population, assets owned and operating activities,

financial reporting quality has its own indicator. Financial distress and outstanding debt are measured by change in net assets, current ratio, debt to assets, return on assets, net lending, net working capita, change of net income, collection rate of accounts receivables, and total revenues to total expenditures.

Financial reporting quality variable resulted in the disclosure index of 31% as an average of sample municipalities in Palestine. Other ratios showed that the results of the benchmark for municipality industry were as the following: the percentage of change in net assets was 21%, debt to assets was 21%, current ratio was 2.49, return on assets was 0.03%, avg revenue per capita was 893 NIS, and avg expenditure per capita was 735 NIS.

5.2 Recommendations

According to the results of research, municipal bonds are highly recommended. The most suitable characteristics of bonds for the Palestinian environment are summarized by type, maturity, par value, method of sale, and risk return relationship. Each ratio affects these characteristics differently depending on the need for financing, municipal revenue bonds have different choices: negotiation or private placement, the short or medium or long-term maturity, investment by financial institution of USD 10,000 or by individuals up to USD 1,000, conditioned by the tradeoff of risk and return.

The MoLG role is beyond giving approvals to municipalities on loans, line credits, and other bank facilities. MoLG can establish equitable mechanism of intergovernmental fiscal transfer, or delegate the tax collection to municipalities themselves. Credit ratings are used to determine the creditworthiness, but they are expensive internationally, so it is recommended to do local credit ratings to evaluate the risks. PMA can help with determining LGUs solvency as they have financial balances database, and they can confirm the borrowing capacity for each LGU (Appendix 1, PEX Interview).

Instructions from MoLG need to be established and declared about the date of publishing the audited financial statements. It is recommended by this study to set a deadline that is before June of the next fiscal year since the researcher had waited for the end of June to get the audited financial statements published by LGUs.

MoLG should be the data center for all municipalities. One of the major obstacles that the researcher has faced during this study is that MoLG did not have the complete data for some municipalities. Budget gate needs improvement to provide better data for their owners. MoLG helps the goals of the best monitoring of LGUs. MoLG need to identify the differences between the surplus and deficit results, between the financial statements and the budget gate for each municipality. This is in addition to the differences in the financial results based on cash basis statement of cash receipts and payments, or net income from the statement of financial

performance based on the accrual basis. Regarding the further researches, the researcher advises conducting researches about the compliance of LGUs in Palestine with IPSAS.

A designated instruction for the issuance of municipal bonds can be publicized from the MoLG since it is the MoLG responsibility to define the ways of financing that are permissible for LGUs. New instructions might be after the year 2018. Also, the Palestinian Capital Market Authority can issue new regulations for the issuance of municipal bonds. The allowed debt limits as a portion of annual revenues need to be set, issuance restrictions like establishing sinking fund, or debt service reserve fund (Farvacque-Vitkovic & Kopanyi, 2014). Types of acceptable collateral and guarantees may be added to the legal framework.

The interest on municipal bonds is exempt from income tax as a general feature (Maverick, 2015). In Palestine, the tax exemption will be disposed of by the first issue of municipal bonds. Reducing interest costs require applying the aggressive approach to debt repayment (BMA, 2007). There are cases when the interest is paid in advance, it is subtracted from the loan occasionally so that the issuer receives fewer funds than demanded (Gitman, 2004).

To sum up, it is obvious that Palestinian municipalities need to employ new ways of financing that depend primarily on the issuance of municipal bonds. Which method of financing should be considered is a matter of choice. If they do not want to issue bonds, they should think

about different scenarios as suggested by MDLF (Appendix 1, MDLF Interview). Municipalities are in great need for investment projects, therefore they should find the solution to stop the falling down of capital investment.

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Appendix 1: Interviews summary

1. PEX, Mr. Muhammad Khraim

PEX welcomes new instruments and it is ready to work and cooperate with different issuers. Khraim has represented new issuances that will add value to the Palestinian financial market as it is the case of the exceptional diversification that has existed in Jordan (PEX interview). PEX has the same program for trading all types of financial securities. Thus, the same procedures that were used previously are going to be applied on municipal bonds issuances.

Khraim considers the issuance of municipal bonds as a great idea, and it is very applicable in Palestine. He argues that municipalities should collect the debts on their citizens. The credibility of the issuer plays a significant role in determining the risk of the issuer to repay the interest and principal in full.

Previous issuances for APIC and PADICO did not demand disclosing their prospectus as their bonds were sold privately.

The subject of international financial institutions and credit rating agencies were discussed. One of the shortcomings to adopt local credit rating is the political risk, in addition to the instability of the unmeasurable general conditions for foreign investors in Palestine. Long-term instruments are too risky with the presence of the Israeli occupation, that's why the previous bond issuances were up to five years (PEX interview). Khraim

pointed out that PMA has superiority in affording credit rating for municipalities because PMA has its own database of solvency and debts with access and supervision to all financial transactions. So, achieving a credit rating to satisfy local financing needs will strike a balance between the local level investments and the international investments. PMA forces banks to invest at least 55% of their deposits in Palestine. Also, a bank's interest rate is considered as the ground basis of the required interest of financial securities.

2. Palestinian capital market authority, Mr. Murad Jadbeh

PCMA's financial manager opinion is strange and shocking. Mr. Jadbeh highlights that municipal bonds deviate from the instructions of issuing municipal bonds due to the certain exceptions such as treasury bonds from PNA, and the issuance by the lending institutions or non-profit organizations. However, municipalities do not belong to any of these exceptions. The researcher argues that LGUs are not NGOs. Jadbeh states that treasury bonds are under the responsibility of the Palestinian National Authority and the Palestinian Monetary Authority.

Logically speaking, bonds were considered as part of the instructions as we explained in the legal framework. Thus, a legal advisor could make a decisive judgment. Accordingly, MoLG will have a monitoring role and it has approvals to issue municipal bonds. However, who is responsible for issuing municipal bonds if it is not PCMA ?

Why are they not issuing bonds occasionally? There are certain requirements according to Companies Law of 1964. For instance, liabilities should not exceed 100% of owner's equity. In other words, bonds should not exceed owner's equity in total. Moreover, owner's equity should have been paid in full before issuing bonds. In a private placement, (30) people shall be offered the securities.

The procedures to issue municipal bonds take three months to finish. In a private placement, (20) days or two weeks of subscription procedures are needed. According to the instructions, they must not take over two months from the meeting date of the general assembly.

The bondholder's committee meets at least once a year; this meeting could be held to discuss dividends and financial statements. After the subscription of bonds, the meeting of general assembly should be held to elect the Indenture Trustee. Funds which constitute the value of the bonds, the custodian bank is responsible for them. So, all funds should be registered by the custodian bank's name to guarantee the subscribers rights. Until the general assembly meeting is held, funds will be kept on the the name of the custodian.

Guarantees are juridical; they are pledged to the indenture trustee to serve the rights of the bondholders, so the issuer can neither use these guarantees nor sell them. After these guarantees are pledged, the indenture trustee orders the custodian to release the funds. Guarantees are based on the creditworthiness of the issuer and his\her credibility to determine the

interest rate. Collaterals provided in the prospectus may be the financial securities, lands, or real estates. These collaterals to be valued by a selective committee that consists of three evaluators. The committee chooses the average estimation between them. The custodian bank should guarantee that this evaluation should not decrease under a specified limit. Such a limit should be tested every three months if the trigger is on the issuer; s/he should propose other guarantees to reach the limit. Then, the guarantees should be moved from the name of the custodian to the name of the indenture trustee. Any change in property ownership enables the indenture trustee to inform the bondholder's committee.

Is there a risk of PADICO and APIC of bonds repayment? This question because they had to issue new bonds to pay for the old ones. If they used installment sales method would be better than full payment at maturity.

3. MoLG, Mr. Musa Gaith, Mr. Mahmoud I'mar, (Budgets Department)
MR. Atta and Ms. Ghadeer

MoLG will have a monitoring role and approvals to issue municipal bonds. It is not clear yet if the MoLG wants to interfere. The ministry might examine the creditworthiness of the municipalities in coordination with the Palestinian Monetary Authority. Creditworthiness is examined to make sure that bonds could be repaid. Municipalities are obliged to generate revenues and to pay their liability of water and electricity.

Generating more revenues and income is necessary to achieve financial sustainability.

Nowadays MoLG gives approvals to municipalities on loans and line credit and other bank facilities. Details of interest rates and repayments are based on municipalities' decisions without the knowledge of MoLG. However, municipalities propose to offer tenders from banks and take the minimum interest with the best repayment terms. Grants are not relied on; surprises may occur like the case when USA stopped their financial support.

No commitment from municipalities to send periodic reports to the system of budgets gate. Also, MoLG does not check its regulatory of sending these reports, or they miss attachments.

MoLG's role in the intergovernmental transfer is specified with the allocation percentage of transportation fees to each municipality. The transportation fee is collected by the Ministry of Transportation, and 50 percent of the total revenue is raised. This share of the MoLG is to be allocated to the LGUs; the allocation basis is from 50% to 70% on per capita basis, and the other 50% is allocated according to the vision of the minister. In 2017, the vision was to support joint councils by giving them 5%, and 15% will be given to village councils by the MoLG transportation fees share because they do not have grants from MDLF. Joint municipalities took another 50% to support their merge, and 15% was allocated to Jerusalem LGUs. Revenue-sharing mechanism of the

transportation fee is underway to make it more transparent, predictable, and regular. In parallel, MoFP has improved transparency in reporting the annual amounts of property tax transferred to local governments.

As we explained in the theoretical framework, the sources of shared revenues which is centrally collected and then split between LGUs include the property tax, occupational license taxes, and the transportation fee. Ministry of Transportation collects the Transportation Fee, and 50 percent of the total revenue collected is to be allocated to the LGUs on per capita basis, however; in practice, the majority of the 50 percent share is intercepted by the MoFP to compensate for the arrears accumulated to their electricity suppliers. Property tax has traditionally been collected only in around 30 municipalities, although this number has been expanding more recently and has now reached 70 municipalities in total .

Transfers depend on liquidity determined by the cash available at MoFP; all municipalities are paid in turn, the only difference between their transfers can be noticed if there is an interception to the arrears. According to MoLG and MoFP, this interception creates the communication trouble between municipalities. On the other hand, municipalities think that MoFP does not transfer their money; their transfers are intercepted with their arrears. MoLG asks for balances periodically but has no access to the system of MoFP to be updated and informed directly with transfers. Based on the most updated balances available at MoLG, the ministry answers LGUs question.

What are the most profitable projects suitable for LGUs?

MoLG's experience in projects suitable for municipalities depends on the needs of each LGU, but every municipality should provide the best possible quality as the service providers. Projects should be related to LGUs assignments by law.

Some municipalities need projects implemented in other municipalities, like a parking complex and a slaughterhouse. Private Placement partnership is encouraged to conduct investment projects. In order to start investment projects, MoLG condition establishing sustainable development unit, this unit is mandatory for A and B LGUs. Suggestion from MoLG concentrated on solar energy and solid waste management projects. Ajja municipality started a solar energy project, success resulted, and Ajja continued stage two of the project by the revenues from step one. Ajja vision to provide a farming area under the solar cells with a particular system to generate diverse revenues other than energy.

An important question is raised concerning the sustainable development unit, and how it is going to be financed. Projects need financing; however, the ministry cannot depend on the operating budgets to fund this unit. In practice, some municipalities originated this unit 2 years ago, but no financing was economized, and this resulted in closing the unit. Before forcing municipalities by MoLG to originate such a unit, municipalities should study how to operate the unit, finance its projects and pay salaries to its employees.

4. MDLF, Mr. Mahmoud Ramahi

How is the funding function being developed?

There are many reasons for not providing the funding function from MDLF. MDLF's customers are LGUs, and they are the targeted party of funds and grants. Performance-based grant allocation mechanism has a supreme target; its target is to improve the performance of municipalities, reformation, and mediation of public services. Criteria for grants has many financial ratios, but these ratios are not specified to measure creditworthiness. MDP3 is designed to have more financial ratios and capacity building for staff to reach creditworthiness. MDLF ultimate goal is to be transformed into a financial institution that provides funding to municipalities in the form of loans or securities.

Grants in total declining or increasing?

It is somehow stable, but the population is increasing. Also, the number of municipalities has increased.

Municipalities status and financial analysis results determine the creditworthiness. It measures the ability of municipalities to pay back the loan service which is the sum of the principal and interest. Also, creditworthiness results are proper planning, good governance, high collection efficiency to maintain liquidity, transparency defined by full disclosure, creditability from the point of community and surplus in budgets. Budget execution without variances, right tenders' procedures

using each available resource effectively. Based on the analysis most LGUs did not reach creditworthiness yet, and they need to work on themselves and improve their performance to achieve creditworthiness. Very few municipalities numbered of four are described to be close to creditworthiness.

Banks are ready to provide loans to municipalities, and they have the liquidity needed. My opinion as MDLF financial manager's opinion; it is easier for municipalities to borrow than to issue bonds. Although borrowing is carried out on higher interest rates and short- terms, but the question to municipalities is that: are you ready for the loan repayment? The surplus for municipalities from all revenues after deducting all expenditures should be sufficient for loan repayment. In reality, municipalities who take line credit and bank facilities have a deficit.

The surplus for municipalities if existed is not enough to do strategic projects. It is exceptional to aggregate surplus over the years to do strategic projects. Other countries' projects lifted global civil standards; higher civilization level requires more projects. As a result, this new level is considered a burden on municipalities due to the lack of financing.

MDLF questioned the type of projects the municipality should establish. There are a variety of revenue generating projects that do not to compete for the private sector, but the better projects are the local government's monopolized projects which are connected to service delivery. Municipalities' monopolism on service projects pulls out the

community's needs; these needs are concentrated on parking's lots and public parks. MDLF is discussing these bankable projects as they should be a short-term target. Palestinian cities have a high potential of tourism; therefore, tourists need full streets to reduce traffic, sidewalks for walking, and the need for better waste management to look clean.

Developed countries target feasible projects that generate revenues, like the loan Ramallah municipality took to invest a commercial mall in the downtown land, in the past Nablus took a loan to establish downtown mall with parking complex, but didn't run it and had a private company to collect rents, even in Nablus they have a high number of staff, this has raised the issue of the ability of municipalities for operating and maintenance of projects.

On the long run the projects should be carried to achieve many targets, as to deliver services that are related to municipalities functions by law, to reach the higher standards of civilization like construction of bridges, ports and highways, to carry out city's planning, to preface industrial zones of streets, water, and electricity. No citizen is ready to live in nearby factories, and local governments are the only body that could guarantee this citizen right. Another target is the local economic development to encourage the private sector in the local governments; the private sector will pay more taxes, licenses and signs fees, which will enhance the community's wealth. Other countries have shared taxes system for local revenues. Municipalities may get a share of the local private sector

value-added tax and corporate tax. This shared tax encourages competition between municipalities to attract private projects and factories.

Financing depends on credibility and increases more in bonds; In Japan, they have reached the highest level of credibility, citizens finance their local governments to get better services, without looking at the required return, they have zero interest bonds.

In Palestine local governments should increase their credibility with their citizens, investors prefer to deposit their money in banks than investing them, losing the possible return but guaranteeing to have their money back, fragile trust in the public sector compared to the private sector. Also, the unique situation of the economic-political risk. So, people are depositing their money in banks, but banks are not investing in Palestine as the international investment position shows. Why banks are not loaning municipalities even, they have all the capabilities. This because banks determine the interest based on the risk associated and take guarantees on assets. MDLF explained municipalities are asking banks for loans. Banks are cautious due to socio-economic functions of municipalities, if municipality defaulted bank will not be able to take the guarantees and liquidate them, liquidation of municipalities assets will have a very negative impact on people, banks are afraid that this might cause bad reputation and make people leave the bank and withdraw their deposits. Is it legally to liquidate municipalities guarantees and are banks protected in courts.

MDLF is a semi-governmental institution, tried to reduce the burden on municipalities by creating distributing companies and other utilities, mainly to increase the collection rates for electricity and water services, net lending is exaggerated with municipalities not paying their electricity bills and distribution companies not paying for the electricity they are distributing, that's why central government disburse their transfers. MDLF will be very careful to be a custodian bank or trustee for the bond issuance, another scenario for MDLF to act as the issuer of bonds on behalf of municipalities. These scenarios endure higher risk if municipalities default, it is not about losing but creating a success story. The MDLF strategy is to have firm steps smoothly other than jumping randomly. The roadmap is prepared to have stages of short-term, mid-term, and long-term plans, to reach the desired results.

The MDLF modality of financing have many ways, a model of MDLF acting as a guarantor of loans to make the financing envelop bigger, for example, loaning municipality from governments or donors 100 million guaranteed by 20 million of MDLF. Another advantage of this model is banks will manage this type of loans, as banks having the required cash to give the loans so that the public sector will not compete for the private sector. By MDLF guarantee risk for banks will decrease resulting in lower cost of borrowing. The disadvantage of this model is the responsible party; the risk is in the case of default would loans weigh on the shoulders of MDLF, who will vary the weights? The mentality of non-payment among municipalities is terrifying. It is going to be very bad if municipalities repeat what happened with water and electricity net lending. The second

modality is the revolving fund as taking a cluster of municipalities and lend them for example 20 million after they repay the funds the turn goes to the second cluster. The disadvantage of this modality is in the case of default the fund sets back, and the funds' cycle will be ruined. Third modality MDLF acting as the bank and lending municipalities, it was experienced in Jordan the bank for cities and villages, and it was not a pleasant experience, the disadvantage of this modality is the competition with banks as they are a private sector, the banks sector in Palestine is powerful, for transferring to a bank MDLF needs high capital and reserves.

After the municipality reaches creditworthiness, it should consider good investment regarding quality and specifications not just feasibility, this is in addition to serving more possible citizens. Bonds depend on political and economic independence, strong institutions, public sector acting in the mind of private investors to have the best returns. MDLF has a neutral opinion for issuing municipal bonds; their opinion is built on experience and realization of municipalities status. If municipal bonds are issued, they should be big size and ideal municipalities. Determinants of issuing municipal bonds:

- project feasibility
- revenue generation and profits
- the ability of the local government for operating & maintenance projects
- tenders' timing to finish projects as fast as possible
- long-term projects increase the risk
- Political Risks due to the -economic situation- called force major

Appendix 2

Analysis Tables

MDPII grant allocation for the years 2014,2015, 2016, and part of 2017 is used to reach grant per capita based on 2016 population for each municipality

#	Municipality Name	Population 2016	Grant per capita in shekels	Comparison MDPIII to MDPII CI
1	Tubas municipality	21,487	112.09	11%
2	Salfeet municipality	10,947	108.40	10%
3	Hebron municipality	215,452	104.07	19%
4	Jenin municipality	48,479	101.40	-7%
5	Qalqilia municipality	51,969	96.49	-2%
6	Ramallah municipality	35,140	92.26	35%
7	Tulkarm municipality	60,173	88.68	39%
8	Al- Bireh municipality	48,887	86.71	41%
9	Nablus municipality	153,061	84.97	-2%
10	Jericho municipality	23,220	82.91	66%
11	Bethlehem municipality	31,799	82.19	55%

Macroeconomic Variable Analysis:

Ratio	2015	2016	growth rate	Avg
Average Revenue Per Capita	912	873	-4%	893
Average expenditure Per Capita	719	751	4%	735

Municipality	Tubas		Tulkarm		Jericho		Al- Bireh		Hebron		Jenin	
Year	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016
Population	20,801	21,487	59,114	60,173	22,609	23,220	47,540	48,887	208,750	215,452	47,305	48,479
Total Revenues	6,142,069	5,103,837	73,288,131	69,833,428	27,671,104	20,689,282	45,979,268	39,107,291	77,075,813	74,252,031	21,175,905	17,783,973
Revenue Per Capita	295	238	1,240	1,161	1,224	891	967	800	369	345	448	367
Total expenditure	3,919,237	5,113,619	74,616,187	69,216,774	21,770,801	22,762,574	14,901,438	28,309,135	62,020,238	49,032,573	7,708,127	11,713,729
expenditure Per Capita	188	238	1,262	1,150	963	980	313	579	297	228	163	242

Municipality	Bethlehem	Ramallah	Salfeet		Qalqilia		Nablus	
Year	2016	2016	2015	2016	2015	2016	2015	2016
Population	31,799	35,140	10,711	10,947	50,700	51,969	149,772	153,061
Total Revenues	17,048,242	61,245,669	15,672,065	17,102,780	68,378,617	68,636,455	128,031,661	98,750,417
Revenue Per Capita	536	1,743	1,463	1,562	1,349	1,321	855	645
Total expenditure	12,515,145	32,117,279	13,069,780	13,966,898	67,210,912	75,138,181	110,920,779	124,653,319
expenditure Per Capita	394	914	1,220	1,276	1,326	1,446	741	814

Cost of the labour variable is measured by administrative and salaries expenses sheet from budgets gate:

Municipality	Salfeet			Qalqilia			Jenin	
Year	2015	2016	2017	2015	2016	2017	2015	2016
Total revenues	15,672,065	17,102,780	19,367,249	68,378,617	68,636,455	79,923,548	21,175,905	17,783,973
Total expenditure	13,069,780	13,966,898	13,745,042	67,210,912	75,138,181	50,133,226	7,708,127	11,713,729
Administrative and salaries analysis								
Operating budget	2,359,139	2,907,404	3,108,865	9,446,511	10,695,754	4,747,375	280,816	1,515,790
Profitable budgets	694,144	649,481	693,955	12,881,507	12,458,658	3,345,859	163,809	1,732,332
Total administrative and salaries	3,053,283	3,556,885	3,802,820	22,328,019	23,154,412	8,093,234	444,625	3,248,122
Percent from total revenues	19%	21%	20%	33%	34%	10%	2%	18%
Percent from total expenditure	23%	25%	28%	33%	31%	16%	6%	28%

Municipality	Tubas			Nablus			Al- Bireh		
Year	2015	2016	2017	2015	2016	2017	2015	2016	2017
Total revenues	6,142,069	5,103,837	6,956,008	128,031,661	98,750,417	108,101,417	45,979,268	39,107,291	33,989,618
Total expenditure	3,919,237	5,113,619	5,696,195	110,920,779	124,653,319	127,538,056	14,901,438	28,309,135	27,279,191
Administrative and salaries analysis									
Operating budget	2,260,025	1,958,186	2,643,104	64,140,859	835,804	54,693,881	5,529,839	19,599,008	17,253,833
Profitable budgets	565,006	1,698,091	1,364,959	18,091,011	82,744,643	30,765,308	4,103,615	2,767,676	2,156,729
Total administrative and salaries	2,825,031	3,656,277	4,008,063	82,231,870	83,580,447	85,459,189	9,633,453	22,366,684	19,410,562
Percent from total revenues	46%	72%	58%	64%	85%	79%	21%	57%	57%
Percent from total expenditure	72%	72%	70%	74%	67%	67%	65%	79%	71%

Municipality	Tulkarm		Jericho		Hebron		Bethlehem	Ramallah
Year	2015	2016	2015	2016	2015	2016	2016	2017
Total Revenues	73,288,131	69,833,428	27,671,104	20,689,282	77,075,813	74,252,031	17,048,242	72,554,235
Total expenditure	74,616,187	69,216,774	21,770,801	22,762,574	62,020,238	49,032,573	12,515,145	46,745,729
Administrative and salaries analysis								
Operating Budget	15,418,686	16,599,212	13,062,118	13,658,461	19,500,121	15,839,619	7,249,150	38,785,487
Profitable budgets	7,987,914	8,776,843	5,206,578	5,180,796	6,407,635	5,204,814	-	-
Total administrative and salaries	23,406,600	25,376,055	18,268,696	18,839,257	25,907,757	21,044,433	7,249,150	38,785,487
Percent from total revenues	32%	36%	66%	91%	34%	28%	43%	53%
Percent from total expenditure	31%	37%	84%	83%	42%	43%	58%	83%

Questionnaires and Ratio Analysis:

Municipality Name: Qalqilia					
English	2013	2014	2015	2016	2017
Current assets	84,985,374	85,613,193	73,445,269	78,799,846	77,879,863
Accounts receivables	75,936,961	81,734,330	70,534,742	75,208,373	69,429,928
In details					
Debts on government (mainly property tax)		2,443,576	-	1,700,000	-
Debts on the public		77,884,313	67,035,186	71,886,085	68,986,002
Fixed assets	472,978,295	478,007,056	464,124,130	451,493,988	448,054,378
land		369,500,631	373,844,504	375,993,577	375,993,577
Total Assets	557,963,669	563,620,249	537,569,399	530,293,834	525,934,241
Current liabilities	123,465,020	131,886,270	124,481,632	133,130,815	130,570,069
Accounts payables	123,070,989	131,881,652	123,289,427	131,972,368	127,912,273
Total liabilities	124,684,296	133,178,531	126,338,001	134,972,549	132,691,197
Net Assets	433,279,373	430,441,718	411,231,398	395,321,285	393,243,044
Net income	12,202,796-	4,734,503-	1,487,576-	2,654,193-	3,156,040

Municipality Name: Qalqilia

Vertical analysis

English	2013	2014	2015	2016	2017
Current assets	15%	15%	14%	15%	15%
Accounts receivables	14%	15%	13%	14%	13%
In details	0%	0%	0%	0%	0%

Debts on government (mainly property tax)	0%	0%	0%	0%	0%
Debts on the public	0%	14%	12%	14%	13%
Fixed assets	85%	85%	86%	85%	85%
land	0%	66%	70%	71%	71%
Total Assets	100%	100%	100%	100%	100%
Current liabilities	99%	99%	99%	99%	98%
Accounts payables	99%	99%	98%	98%	96%
Total liabilities	100%	100%	100%	100%	100%
Net Assets	78%	76%	76%	75%	75%

Municipality Name: Qalqilia	2013	2014	2015	2016	2017
Current ratio		0.69	0.65	0.59	0.59
Net working capital		38,479,646-	46,273,077-	51,036,363-	54,330,969-
Debt to assets		0.22	0.24	0.24	0.25
Return on Assets		-0.02	-0.01	0.00	-0.01
Net lending	47,134,028-	50,147,322-	52,754,685-	56,763,995-	58,482,345-

Municipality Name: Tubas					
English	2013	2014	2015	2016	2017
Current assets	15726440	15354191	13902512	13547632	12106720
Accounts receivables	14931039	13519910	11808099	11470897	8977737
In details					
Debts on government (mainly property tax)	1,443,456	1,440,575	837,815	1,564,464	-
Debts on the public	14,931,039	12,079,335	10,945,374	9,906,432	8,977,737
Fixed assets	144,871,313	145,290,540	145,290,540	145,290,540	145,290,540
land available for sale	33,865,369	33,865,369	33,865,369	33,865,369	33,865,369
	1,528,096				
Total Assets	160,597,753	160,644,731	159,193,052	158,838,172	157,397,260
Current liabilities	6,921,174	6,700,592	6,766,591	8,520,221	8,129,403
Accounts payables	4,108,701	3,749,818	3,655,909	5,218,462	4,637,168
Total liabilities	6,921,174	6,700,592	6,766,591	8,520,221	8,129,403
Net Assets	153,676,579	153,944,139	152,426,461	150,317,951	149,267,857
Net income	35,538-	946,007	691,633	83,108	1,302,225
Current ratio	2.27	2.29	2.05	1.59	
Net working capital	8,805,266	8,653,599	7,135,921	5,027,411	
Debt to assets	0.04	0.04	0.04	0.05	
Return on Assets	0.00	0.01	0.00	0.00	

Vertical analysis

English	2013	2014	2015	2016	2017
Current assets	10%	10%	9%	8%	8%
Accounts receivables	9%	8%	7%	7%	6%
In details					
Debts on government (mainly property tax)	1%	1%	1%	1%	0%
Debts on the public	9%	8%	7%	6%	6%
Fixed assets	90%	90%	90%	90%	90%
land available for sale	21%	21%	21%	21%	21%
Total Assets	100%	100%	100%	100%	100%
Current liabilities	100%	97%	98%	123%	117%
Accounts payables	59%	54%	53%	75%	67%
Total liabilities	100%	100%	100%	100%	100%
Net Assets	96%	96%	96%	95%	95%

Growth rate analysis

2014	2015	2016	2017
-2%	-9%	-3%	-11%
-9%	-13%	-3%	-22%
0%	-42%	87%	-100%
-19%	-9%	-9%	-9%
0%	0%	0%	0%
0%	0%	0%	0%
0%	-1%	0%	-1%
-3%	1%	26%	-5%
-9%	-3%	43%	-11%
-3%	1%	26%	-5%
0%	-1%	-1%	-1%

Salfeet

English	2013	2014	2015	2016	2017
Current assets	25,196,403	31,741,037	25,073,223	30,289,613	35,402,202
Accounts receivables	19,529,578	24,062,105	18,316,740	23,908,150	29,112,782
In details					
Debts on government (mainly property tax)	2,259,238	2,259,238	2,906,226	2,996,226	4,025,554
Debts on the public	18,217,297	18,217,297	15,058,533	18,041,077	21,679,103
Fixed assets	9,458,429	11,074,186	152,309,378	151,604,186	150,489,921
land available for sale	2,483,252	2,483,252	67,763,063	67,850,466	68,082,537
			177,382,601	181,893,799	
Total Assets	34,654,832	42,815,223	177,378,601	181,937,799	185,892,123
		-	4,000-	44,000	
Current liabilities	11,576,907	18,710,108	10,674,150	12,817,565	15,049,212
Accounts payables	10,763,845	18,075,051	9,854,217	12,059,495	14,252,266
Total liabilities	11,738,215	18,884,738	10,871,909	13,038,502	15,293,142
Net Assets	22,916,617	23,930,485	166,506,692	168,899,297	170,598,981
Net income	4,133,728	1,398,546	1,605,358	1,968,119	2,108,149

English	2013	2014	2015	2016
Current assets	33,093,936	43,786,398	49,341,572	57,919,987
Accounts receivables	27,529,143	38,225,586	42,592,932	49,768,466
In details				
Debts on government (mainly property tax)			9,138,159	18,431,882
Debts on the public			1,069,514,593	31,053,102
Fixed assets	821,479,546	812,243,718	807,089,052	807,031,544

land available for sale				686,505,118	686,915,060
Total Assets	854,573,482	856,030,116	856,430,624	864,951,531	
Current liabilities	41,478,257	49,411,158	39,780,242	44,603,850	
Accounts payables	7,461,758	10,757,773	5,236,283	8,429,397	
Total liabilities	61,035,000	71,141,455	62,958,802	68,586,037	
Net Assets	793,538,482	784,888,661	793,471,822	796,365,494	
Net income	-12,774,052	-8,329,203	68,597,814	71,191,397	
Municipality Name: Ramallah		Vertical analysis		Growth rate analysis	
English	2013	2014	2015	2016	
Current assets	4%	5%	6%	7%	
Accounts receivables	3%	4%	5%	6%	
In details	0%	0%	0%	0%	
Debts on government (mainly property tax)	0%	0%	1%	2%	
Debts on the public	0%	0%	125%	4%	
Fixed assets	96%	95%	94%	93%	
land	0%	0%	80%	79%	
Total Assets	100%	100%	100%	100%	
Current liabilities	68%	69%	63%	65%	
Accounts payables	12%	15%	8%	12%	
Total liabilities	100%	100%	100%	100%	
Net Assets	93%	92%	93%	92%	
Net income					
Current ratio	0.80	0.89	1.24	1.30	
Net working capital	8,384,321-	5,624,760-	9,561,330	13,316,137	
Debt to assets	0.07	0.08	0.07	0.08	
Return on Assets	-0.01	-0.01	0.08	0.08	

*					
Municipality Name: Nablus					
English	2013	2014	2015	2016	2017
Current assets	580,212,973	503,820,808	519,608,908	533,094,185	550,772,570
Accounts receivables	259,784,406	304,053,533	310,884,816	322,789,777	321,953,524
In details					
Debts on government (mainly property tax)	22,963,124	43,567,662	53,052,355	55,699,359	47,778,133
Debts on the public	276,325,609	255,721,071	253,977,748	262,874,667	268,554,672
Fixed assets	707,314,747	810,239,973	785,739,653	759,650,930	748,574,004
land		114,148,834	121,907,332	122,436,052	123,928,364
Total Assets	1,287,527,720	1,314,060,781	1,305,348,561	1,292,745,115	1,299,346,574
Current liabilities	128,142,851	180,724,158	172,314,284	190,369,298	205,383,205
Accounts payables	110,848,804	140,664,007	129,435,318	139,790,695	152,691,727
Total liabilities	279,675,431	328,554,070	327,535,901	353,351,995	376,515,036
Net Assets	1,007,852,289	985,506,711	977,812,660	939,393,120	922,831,538
Net income	42,728,988	-38,507,797	9,558,677	-25,902,899	-19,436,650

Municipality Name: Nablus		Vertical analysis			
English	2013	2014	2015	2016	2017
Current assets	45%	38%	40%	41%	42%
Accounts receivables	20%	23%	24%	25%	25%
In details	0%	0%	0%	0%	0%
Debts on government (mainly property tax)	2%	3%	4%	4%	4%
Debts on the public	21%	19%	19%	20%	21%
Fixed assets	55%	62%	60%	59%	58%
land	0%	9%	9%	9%	10%
Total Assets	100%	100%	100%	100%	100%
Current liabilities	46%	55%	53%	54%	55%
Accounts payables	40%	43%	40%	40%	41%
Total liabilities	100%	100%	100%	100%	100%
Net Assets	78%	75%	75%	73%	71%
Current ratio		4.53	2.79	3.02	2.80
Net working capital		452,070,122	323,096,650	347,294,624	342,724,887
Debt to assets		0.22	0.25	0.25	0.27
Return on Assets		0.03	-0.03	0.01	-0.02

Growth rate analysis			
2014	2015	2016	2017
-13%	3%	3%	3%
17%	2%	4%	0%
90%	22%	5%	-
-7%	-1%	4%	2%
15%	-3%	-3%	-1%
N/A	7%	0%	1%
2%	-1%	-1%	1%
41%	-5%	10%	8%
27%	-8%	8%	9%
17%	0%	8%	7%
-2%	-1%	-4%	-2%

Municipality Name: Jericho				
English	2014	2015	2016	2017
Current assets				
Accounts receivables	23,775,241	63,187,835	57,193,301	64,027,606
In details				
Debts on government (mainly property tax)	6,000,000	9,000,000	15,000,000	20,000,000
Debts on the public	17,775,241	54,187,835	42,193,301	44,027,606
Fixed assets				
land	1,306,581	1,306,581	13,065,803	13,065,803
Total Assets				
Current liabilities				
Accounts payables	-	-	-	1,860,765
Net income		4,926,635	-5,386,562	

Municipality Name: Jericho

Growth rate analysis

English	2014	2015	2016	2017
Current assets	N/A	N/A	N/A	N/A
Accounts receivables	N/A	166%	-9%	12%
In details				
Debts on government (mainly property tax)	N/A	50%	67%	33%
Debts on the public	N/A	205%	-22%	4%
Fixed assets	N/A	N/A	N/A	N/A
land	N/A	0%	900%	0%

Municipality Name: jenin

English	2014	2015	2016	2017
Current assets				
Accounts receivables			154700576.9	
Total Assets	2,014	2,015	2,016	2,017
Current liabilities				
Accounts payables			116,382,110	
Total liabilities				
Net income	4,138,478	6,715,430	8,190,816	4,580,289
Growth rate analysis		62%	22%	-44%

Municipality Name: Hebron				Vertical analysis		Growth rate analysis			
English	2013	2014	2015	2016		2014	2015	2016	2017
Current assets	20%	21%	23%	39%		14%	15%	25%	-100%
Accounts receivables	18%	17%	21%	36%		5%	26%	25%	32%
In details	0%	0%	0%	0%					
Debts on government (mainly property tax)	1%	1%	3%	6%		9%	465%	40%	-99%
Debts on the public	0%	13%	13%	20%		N/A	5%	10%	136%
Fixed assets	80%	79%	77%	61%		7%	3%	-43%	79%
land	0%	25%	25%	35%		N/A	4%	0%	-100%
Total Assets	100%	100%	100%	100%		9%	5%	-28%	-100%
Current liabilities	88%	90%	90%	91%		22%	9%	15%	-100%
Accounts payables	73%	77%	77%	74%		26%	8%	9%	-4%
Total liabilities	100%	100%	100%	100%		20%	9%	13%	-100%
Net Assets	48%	43%	41%	8%		-3%	1%	-86%	-100%
						8%	-62%	-53%	-100%

Municipality Name: Hebron

English	2013	2014	2015	2016
Current ratio	0.43	0.40	0.43	0.47
Net working capital	215,757,730-	276,745,240-	288,173,826-	308,424,517-
Debt to assets	0.52	0.57	0.59	0.92
Return on Assets	-0.05	-0.05	-0.02	-0.01

Municipality Name: Al- Bireh				
English	2013	2014	2015	2016
Current assets	69,779,769	74,648,499	88,788,074	111,206,476
Accounts receivables	40,879,984	44,243,275	50,247,778	50,608,371
In details				
Debts on government (mainly property tax)	17,853	17,923	17,922	30,078
Debts on the public	40,862,131	44,225,352	50,229,856	50,578,293
Fixed assets	1,038,167,883	1,037,185,196	1,040,357,517	735,665,379
land	433,754,267	435,043,965	435,840,191	523,044,697
Total Assets	1,107,947,652	1,111,833,695	1,129,145,591	846,871,855
Current liabilities	7,529,029	11,117,309	11,986,373	13,991,163
Accounts payables	7,319,363	10,856,242	11,820,607	13,441,016
Total liabilities	12,583,531	17,051,467	20,165,236	22,747,797
Net Assets	1,095,364,121	1,094,782,228	1,108,980,355	824,124,058
Net income	1,241,866-	581,893-	14,369,325	20,897,187

Municipality Name: Al- Bireh		Vertical analysis			Growth rate analysis		
English	2013	2014	2015	2016	2014	2015	2016
Current assets	6%	7%	8%	13%	7%	19%	25%
Accounts receivables	4%	4%	4%	6%	8%	14%	1%
In details	0%	0%	0%	0%			
Debts on government (mainly property tax)	0%	0%	0%	0%	0%	0%	68%
Debts on the public	4%	4%	4%	6%	8%	14%	1%
Fixed assets	94%	93%	92%	87%	0%	0%	-29%
land	39%	39%	39%	62%	0%	0%	20%
Total Assets	100%	100%	100%	100%	0%	2%	-25%
Current liabilities	60%	65%	59%	62%	48%	8%	17%
Accounts payables	58%	64%	59%	59%	48%	9%	14%
Total liabilities	100%	100%	100%	100%	36%	18%	13%
Net Assets	99%	98%	98%	97%	0%	1%	-26%
Net income					-53%		
Current ratio	9.27	6.71	7.41	7.95			
Net working capital	62,250,740	63,531,190	76,801,701	97,215,313			
Debt to assets	0.01	0.02	0.02	0.03			
Return on Assets	-0.001	-0.001	0.01	0.02			

Municipality Name: Bethlehem					
English	2013	2014	2015	2016	2017
Current assets		1,634,758	3,128,715	4,888,743	18,846,656
Accounts receivables		14,768,087	17,728,918	15,764,797	19,085,893
In details					
Debts on government (mainly property tax)		2,250,521	4,408,267	4,648,441	6,251,514
Debts on the public		12,517,565	13,320,651	11,116,356	12,834,380
Fixed assets		81,881,744	80,794,083	79,650,948	78,631,005
land		-	-	-	-
Total Assets					
Current liabilities		4,461,335	5,294,467	6,624,840	9,286,236
Accounts payables		-	-	-	-
Total liabilities		4,461,335	5,294,467	6,624,840	9,286,236
Net Assets					
Net income	1,167,519	1,634,758	1,493,957	1,760,328	
Did you take bank facilities? Yes/ No		Yes	Yes	Yes	Yes
The rate of bank facilities		7	7	7	4.9
Net working capital	-	2,826,577-		2,165,752-	1,736,097-

Appendix 3

Strategic Development and Investment Plans

Some municipalities disclosed their strategic plans. Wished Projects for municipalities from the available SDIP were recognized, for example, Jericho municipality had a total value of wished projects of 24,197,000 USD in the SDIP from 2018-2021. In Jenin from the years 2013- 2016 SDIP, 53% of proposed projects remained wished. According to the analysis of the actual performance, these projects with a total value of USD 53,314,160 had no financing.

As explained in this thesis, sustainable capital investment projects can be financed by municipal revenue bonds. Here are some listed projects that their nature goes consistently with the municipalities' concerns and with the significant topics discussed in this research:

Municipality	Name of the project	Amount in USD	Year of SDIP
Nablus	Parks and playgrounds	6,000,000	2012-2015
	Olympic Sports Compound	5,500,000	
	Stadiums	1,000,000	
	constructing a new poultry slaughterhouse	8,000,000	
Hebron	Establishment of parking lots and complexes for Public vehicles	5,000,000	2019 - 2016
	Develop and implement the transportation management system	4,500,000	
	Create a tunnel to facilitate traffic	4,000,000	
	Construction of vehicle inspection station (dm)	1,500,000	
	Establishment of an industrial zone	17,000,000	
	Technological Incubation Technion Innovation Techno Park	3,770,000	
Al- Bireh	Establishment of a talented center	400,000	2014- 2017
	Create a resort and club care for seniors	2,000,000	
	Establish a club and a sports pool	2,095,100	
	Create a tourist channel.	2,000,000	
	Rehabilitation of the city's heritage area and old houses. In addition to suitable facilities.	1,450,000	
Bethlehem	New solar energy station	500,000	2018-2021
	Implementing a feasibility study of slaughterhouse establishment with around village council	8,000	
	New toilets (WC) in public parks	20,000	
	New toilets (WC) in the bus station	40,000	
	New transportation complex with solid waste equipment	120,000	
Bethlehem	Promotion for tourism and heritage sites especially the Old City		2014- 2017
	Establishing and rehabilitating the roads in Bethlehem		
Jericho	Building a modern and equipped municipal building	1,500,000	2018-2021
	Preparing tourist maps	35,000	

	Development of the streets of tourist sites	400,000	And existed in 2013- 2016
	Improving services for tourists and historical attractions	299,000	
	construction of water tanks	1,500,000	
	Drilling new wells	1,400,000	
	Construction of a dam to collect rainwater	2,000,000	
	Construction of sidewalks in the city of Jericho	200,000	
	Extension of road lighting lines	300,000	
	Paving roads and construction of the bridge	2,500,000	
	Establishment of a craft zone	27,000	
	Building a commercial complex	3,250,000	
	Building the Cultural Palace	1,000,000	
	Creation of a historical museum of archaeology	2,000,000	
	Museum of Memory	1,000,000	
	Therapeutic tourist resort	700,000	
	Winter camping projects	868,000	
	Complex for extracurricular activities	3,000,000	
Jenin	Preparing sidewalks and Providing traffic signs in the central city	Total area	2012-2015
	Construction of commercial complex including parking private and public	3000 m2	
	Drilling a new water-well 200 cube/ hr		
	Building a new water tank with a capacity of 2000 cube		
	Strategic wastewater plant- Construction of wastewater treatment plant benefiting Jenin and surrounding villages		
	Rehabilitating the infrastructure of the industrial area		
	Construction of refrigeration units and cooling storages in the industrial area	500 m ² / storage	
	Construction of exhibition yards	2000 m2	
	Constructing a public park	7000 m2	
	Renovation of the Old City	5000 m 2	

	Establishment of a national and cultural museum		
	Constructing a theatre	900 m 2	
Salfeet	Parking Complex	1,250,000	2013-2016
	Create a recreational city	5,000,000	
	Construction of a football stadium	3,000,000	
Tubas	Establishment of an industrial zone.		2014
	Drilling of rainwater wells for houses and farms.	500,000	
	Drilling and equipping agricultural water well in the Tubas Plain area	1,000,000	
	Establishment of the commercial complex (settlement + municipal stores of 150m2)	100,000	
	Create slaughterhouse	700,000	
	Establishment of a public park in the area of Einoun	350,000	
	The establishment of a national park in the bush.	500,000	
	Construction of semi-Olympic swimming pool	500,000	

Municipalities in their strategic plans mix their responsibilities with other parties' responsibilities. For example, health and education are top priorities on the ministry's functions, but they believe that municipalities should commit to their assignments as illustrated in Article (15) according to the Local Government Law of 1997 (ARIJ, 2009; Swafta, 2011; The World Bank, 2017):

1. Town planning
2. Transit management (traffic lights, signs, meters, and others)
3. Street construction, rehabs, paving, and roads
4. Street names and numbering
5. Sidewalks
6. Public transport stands and terminals
7. Street lighting
8. Electricity supply
9. Rainwater drainage system
10. Water supply
11. Sewer system
12. Wastewater treatment
13. Solid waste collection and disposal
14. Solid waste treatment
15. Public lavatories
16. Fruit and vegetable markets
17. Public parks
18. Social assistance programs
19. Sports facilities
20. Libraries
21. Museums and culture

22. Regulation, control, and monitoring
23. Cemeteries
24. Slaughterhouses
25. Firefighting
26. Schools
27. Health centers
28. Other (the law explicitly allows for other functions)

جامعة النجاح الوطنية

كلية الدراسات العليا

السندات البلدية كأداة للتمويل الرأسمالي في الهيئات المحلية الفلسطينية

اعداد

يقين عبدالله عمر عوض

إشراف

د. غسان دعاس

د. خالد زيدان

قدمت هذه الأطروحة استكمالاً لمتطلبات الحصول على درجة الماجستير في المحاسبة بكلية الدراسات العليا في جامعة النجاح الوطنية في نابلس، فلسطين.

2018

ب

السندات البلدية كأداة للتمويل الرأسمالي في الهيئات المحلية الفلسطينية

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الملخص

البلديات هي المؤسسات العامة المسؤولة عن توفير الخدمات للمواطنين. تتحمل البلديات مسؤولية انشاء مشاريع التنمية الرأسمالية والتي تعد من أهم وأصعب مهمات البلديات، وذلك بسبب ضخامة حجم الاستثمار المطلوب، وشح موارد الهيئات المحلية مع تزايد أعداد السكان. حيث ان هناك انخفاض ملحوظ في حصة الفرد من من إيرادات البلدية بنسبة 73%. لكن اللجوء الى طرق تمويل جديدة قد يحل هذه الازمة. إن استخدام الدين والاقتراض والأدوات المالية في الهيئات المحلية الفلسطينية يشكل نسبة قليلة جداً، وبالتالي يمكن استخدام ادوات الدين لتمويل مشاريع البلديات بظروف معينة وبأسلوب التحفظ تحت سيطرة التشريعات والتعليمات وسقف محدد للدين. يتم استخدام السندات البلدية في كثير من الدول لتمويل المشاريع الرأسمالية الاستراتيجية ومشاريع البنية التحتية. يركز البحث على محددات إصدار سندات البلديات؛ من حيث نوع السندات، طريقة البيع، استحقاق السند، والقيمة الاسمية، والعلاقة بين العائد والمخاطرة.

الغرض من البحث هو تطوير أدوات لقياس الجدارة الائتمانية بحيث تكون مناسبة وقابلة للتطبيق على الهيئات المحلية الفلسطينية. تشكلت العينة من 11 بلدية من محافظات الضفة الغربية الفلسطينية.

تم قياس عدة متغيرات لفحص فرضية تمويل المشاريع الرأسمالية بإصدار سندات البلدية؛ منها متغيرات الاقتصاد الكلي ومتغيرات حالة البلدية. خلال دراسة متغيرات الاقتصاد الكلي تم التطرق الى اسعار الفوائد التاريخية، وضع الاستثمار الدولي والدين الخارجي بالاضافة الى قانون

الموازنة العامة، تم قياس متغيرات الاقتصاد الكلي بحصة الفرد من الإيرادات والنفقات، معدل البطالة، تكلفة الموارد البشرية. تم تقسيم متغيرات حالة البلدية الى حجم البلدية، جودة التقارير المالية، عبء الدين والتعثر المالي. تم استخدام النسب المالية المختلفة لقياس هذه المتغيرات، بالإضافة للتحليل المقارن والتحليل الأفقي والرأسي وذلك للوصول الى الية اصدار سندات البلديات في فلسطين.

وكانت النتيجة أن متغيرات الاقتصاد الكلي ومتغيرات حالة البلدية تؤثر على إصدار "سندات البلديات الإيرادية" بشكل ايجابي ويشجع اصدارها في فلسطين، خصوصا لاعلى ثلاث بلديات تم تصنيفها البلديات في العينة.

الكلمات المفتاحية: سندات بلدية، إصدار، فلسطين، بلديات، إيرادات، التحويلات، المنح، الديون، الميزانية، العجز، الوضع المالي، الجدارة الائتمانية، المعايير المحاسبية الدولية للقطاع العام، الإفصاح، الخطط الإستراتيجية.