ANNUAL SURVEY 2002-2003

EDITED BY
LEAH ACHDUT

NATIONAL INSURANCE INSTITUTE
RESEARCH AND PLANNING ADMINISTRATION

JERUSALEM, APRIL 2004

Forward

The present Annual Survey is an additional link in the series of Annual Surveys published by the National Insurance Institute of Israel (NII). It covers the activities of the NII for 2002-2003, in view of the turnabout in the government's social policy as reflected in the five economic plans approved by the Knesset (Israel's Parliament) during those years.

The first chapter summarizes the main points of the new social policy, surveying the changes introduced into the various programs under the responsibility of the NII and those in the means of financing these programs. A distinction is drawn between programs aimed at the working-age population and those meant for the population that has left the workforce. Both immediate and long-term implications of the new legislation on the conditions of entitlement to benefits and on their level are discussed.

The second chapter presents the picture of poverty and income inequality in Israel in 2002, focusing this time on additional approaches to the measurement of poverty in Israel and in selected Western countries.

Special chapters are devoted to developments in the income support system (Chapter Three), in the sphere of collection of national and health insurance contributions (Chapter Four), and in the main insurance branches (Chapter Five). The Survey also includes an English summary of the first chapter and of the trends in poverty and income distribution.

The Survey includes three Appendices: an Appendix of Publications – summaries of research reports and surveys published by the Research and Planning Administration in 2002-2003 and of the research reports of the Fund for Demonstration Projects – an Insurance Branch Table Appendix and a Poverty and Inequality Table Appendix.

I extend my thanks to the employees of the Research and Planning Administration who assisted in the preparation of the Survey and bringing it to print, and particularly to Mia Orev-HaTal, who carried out the linguistic editing. A special thanks is due to Or-el Abutbul and Nira Amir, who bore the burden of the typing, for work carried out with willingness, initiative and devotion.

Leah Achdut

Deputy Director-General for Research and Planning

Preface
by the Director General

The years 2002-2003, covered in this Survey, were overshadowed by a severe economic recession in Israel and a turnabout in the government's social policy. The recession led to a fall in the standard of living, an expansion of unemployment and an erosion of wages. Further, in the framework of five economic plans approved by the Knesset (Israel's Parliament), deep structural changes were instituted in the benefit system of the National Insurance Institute (NII), including significant reductions in the level of most of the benefits. This Survey discusses the depth of the cutbacks in the benefits and their implications on the lives of families in Israel.

There is a general consensus that the growing deficit of the State budget did not enable a cut in public expenditure without touching the transfer payments. The debate focused on the depth of the cut in social security benefits and on the government's order of priorities, particularly regarding the mixture of the cutback in expenditure as compared to the decrease in the tax burden.

In total, benefit payments were reduced in 2002-2003 by over NIS 5.5 billion, and the extent of their continued reduction in the coming years was pre-determined in the legislation. Total benefit payments (both cash and in-kind) in these two years fell by 7.2% in real terms, most of the decline (5.7%) taking place in 2003. Were it not for the increase in the number of benefit recipients, a sharper decrease in payments would have been observed, more accurately reflecting the depth of the cutback.

All population groups were affected by the new government policy, but the benefits aimed at the working-age population – unemployment, income support and child (family) allowances – were struck the hardest. The cutback in each one of these systems has thus far amounted to about a third of the total benefit payments paid previous to the new legislation, and in child allowances it will continue till the end of the decade. In addition, the government abandoned the perception according to which the standard of living of benefit recipients should be maintained by linking the benefits to the average wage. This relative perception has guided the NII since the mid 70’s and played an important role in reducing poverty and income gaps in the country. The government decided to freeze benefit levels in 2002-2003, and as of 2006, link them to price rises only. In the coming years, the standard of living of the population at large will rise – but that of the elderly, the widows, the disabled and the other weak population sectors will remain behind.

The picture of poverty and economic gaps in 2002 reflects some of the effects of the policy measures enacted in that year; their full influence will be expressed in data to be published in 2003. The cuts in payments to income support recipients and to families with children will be reflected in 2003 as well, but in the data for 2004 only. Still, the picture for 2002 is sufficient cause for concern, and most indicators point to deterioration in the country’s social situation. The decline in standard of living characterizes all strata of the population, but is particularly evident among families in the lower income deciles. In net income per standard person, the income level of the first and second deciles declined by 12% and 7% in real terms, respectively, as compared to 4.6% in the total population. The net income of families with children and working-age families without a breadwinner has eroded the most. The situation of the elderly, particularly the low-income elderly, was less affected; their income was eroded at lower rates. These trends are reflected in the 2002 poverty measures: the incidence of poverty among families remained the same – 17.7% of total families – but the poverty itself became more severe. The average poverty gap per poor family rose from 26% to 29%, and the rate of poor children out of the total number of children continued to rise, reaching 28.1%. On the other hand, the incidence of poverty among the elderly declined from 24% to about 20%.

According to preliminary estimates, the incidence of poverty will rise to 18.5% by the end of 2003, and the average poverty gap per poor family will climb to 30% due to the deep cuts in the income support benefits and the child allowances, likely to lead to a smaller contribution of benefits to a reduction of income inequality. It may also be surmised that the gaps according to net income – before the cuts – will widen even further. Not all strata of the population will benefit from the fruits of the economic growth, just beginning to bud at the time of this writing. Not only will benefits not be adjusted, but it will take time for the economic growth to filter down to the low deciles, particularly to the weak links of the labor force.

As every citizen is aware, these years have been difficult ones for the National Insurance Institute and its employees. The NII is doing its utmost to fight the economic decrees in the government and Knesset, and to lessen the blow to the weak population groups. By all the means at our disposal, we have tried to convince the policy-makers that this new policy dangers the very existence of thousands of families in Israel and the integrity of society as a whole. Our efforts, unfortunately, have not been successful.We have had to invest huge resources in the preparation and implementation of a torrent of amendments to the National Insurance Law and other social security legislation.

This legislation of the past two years has verily changed the face of the social security system of Israel. Some of it has been enacted due to budgetary stress; others reflect the policymakers' stand regarding the nature of the welfare state and the role of the National Insurance Institute. This stand is not accepted in all circles, and the policy it has yielded is the subject of dispute. However, history teaches us that welfare perceptions come and go, according to changing economic and social circumstances.

In 2004, the National Insurance Institute of Israel celebrated its fiftieth birthday. Many challenges await us, and intensive efforts are required to meet them. As the main body responsible for social security, we need to reconsider our targets in the coming years and our role in the formulation of social policy. We must seek to improve our image in the government, the Knesset and the public at large, since support of the NII is an essential condition for success in reaching fuller take-up of rights, without exploitation of the system, and for promoting the welfare and well-being of the population entrusted to our care.

Dr. Yigal Ben Shalom
Director General

Chapter 1

Trends of Development in National Insurance

Leah Achdut

1.1 Introduction

In 2002-2003, the government of Israel decided on a complete turnabout in its social policy, to mark its stamp on the welfare state in the country for many years to come. Under five different economic programs approved by the Knesset (Israel's Parliament), deep structural changes were introduced in the benefit system of the National Insurance Institute (NII), together with a significant reduction in the level of most benefits. The list of decrees hurting benefits that were implemented in 2002-2003 and the ones expected in the coming years is lengthy, and affected all population groups. The depth of the immediate cutbacks was particularly notable in the benefits aimed at the working-age population – unemployment, income support and child (family) allowance. The cutback in each one of these systems has thus far amounted to about a third of the total benefit payments paid previous to the new legislation, and in child allowances it will continue till the end of the decade. The influence of the structural changes was already partially felt in 2002-2003, and will become intensified in the coming years. Deeply implanted perceptions of the welfare state, formulated over two to three decades – such as maintaining the standard of living of benefit recipients relative to that of the population at large – were abruptly abandoned, from one day to the next, without any comprehensive public discussion. The new policy has punctured the social security net of the country and wiped out hard-gained achievements of many years.

The turnabout in the government's social policy stemmed originally from the budgetary distress resulting from the 2001-2003 recession, expressed in a fall in the standard of living, an expansion in unemployment and an erosion of wages. The government's income from taxes dropped drastically, the deficit in the state budget grew, and NII benefits were cut in keeping with the policy to reduce government expenditure. No one disputes the fact that the new fiscal policy had to include transfer payments, which constituted a significant share of government expenditure. The debate on the new policy focused on the depth of the cuts in benefits and on the government's order of priorities, particularly with regard to the mixture of the cutback in expenditure as compared to the decrease in the tax burden. In 2002-2003, NII benefits were cut by about NIS 5 billion. Total benefit payments (both cash and in-kind) in those two years fell by 7.2% in real terms, most of the decline (5.7%) taking place in 2003, decreasing from 9.42% to 8.88% of the GDP. Were it not for the increase in the number of benefit recipients, a sharper decrease would have been observed, more accurately reflecting the depth of the cutback.

There is general agreement, even among those who support the government's path, that the new policy did not arise solely from budgetary distress, but also reflected the domination of those believing in small government at the junction of policy-making.

This perception is what actually led to a reduction in public expenditure, which was first accompanied by an increase in the tax burden – and later on by its decrease. The public debate in 2003 was not about the implementation of the income tax reform in principle, but rather about its implementation earlier and within a shorter period of time than originally determined. Social considerations such as guaranteeing a minimum income for subsistence and preventing an expansion of poverty or a deepening of economic polarization were not given adequate consideration; on the contrary, they were completely alien to the set of considerations underlying the government's policy. The population groups in need of state social services and particularly those most hurt by the recession were made to carry the heaviest burden of the economic recovery. In a very brief period of time the government implemented a policy that deeply eroded the benefits paid to the elderly, the unemployed and families with children. Even if it is agreed that changes in the benefit system were required in order to reduce its inherent disincentives to work, these did not demand such deep and sharp cuts, which in fact preceded any attempt on the part of the active policy leadership to help unemployed benefit recipients find work.

Government policy in 2004-2006 and afterwards proves that the perception of "less public expenditure and lower taxes" will continue to make its mark on the economy and on society in Israel. The legislation enacted in 2002-2003 determined benefit levels not only for those specific years but for the future as well. Even if the economy grows in 2004-2006, the level of benefits will not go up in 2005, due to the freeze imposed upon them till 2006. Furthermore, cuts in benefits will continue due to the cancellation of the linkage to the average wage.

The achievement of the government's economic targets in the coming years will be at the expense of the population groups in need of social services and of the benefit recipients. The government decided to limit public expenditure by means of two measures: the deficit target in the state budget will be 4% in 2004, but will be gradually reduced in the following years, and in parallel, government expenditure would not exceed 1% in real terms. Even if the economy grows and income from taxes rises, and even if the deficit target is achieved, no additional resources will be freed to increase public expenditure. A growth of 1% in government expenditure (including NII activities) does not even compensate for the natural growth of the population, and the "competition" between social and defense expenditure in the government's order of priorities will be intensified even further. Moreover, in order to prevent pressures to increase public expenditure in the coming years, the Treasury embarks time and time again on a policy of lowering taxes; in addition to advancing the income tax reform to an earlier date, it is planned to reduce the VAT and the sales tax, and it is proposed to lower the rate of national insurance contributions imposed on employers as well as profit taxes. The resources to be added to the state budget as a result of the hoped-for growth are – or will be – directed towards the lowering of taxes, and the deficit target will apparently be achieved only by means of an additional cutback in public expenditure, particularly in the social services.

Yet this is not all. The new policy has been accompanied by an undermining of public support for the welfare state in Israel, and by a campaign of de-legitimazation of the weak population groups, particularly of the unemployed, who are being blamed for their unemployment. This campaign did not omit the NII as the main body responsible for social security in Israel. At times the unemployed are blamed for cheating the NII and at times the NII is blamed for faulty administration, causing a loss of billions of shekels, which otherwise could have made the lateral cut in benefits unnecessary.

1.2 The National Insurance System After the 2002-2003 Legislation

The five economic programs approved by the Knesset in 2002-2003 and in early 2004 include a long list of changes in the two components of the national insurance system – benefits and collection. The changes are structural for the most part; to a smaller degree they include temporary or permanent reductions in benefit levels with no essential change in the structure of the programs or in rules of entitlement to benefits. Amendments were enacted in programs which pay benefits both to the working-age population and to the retired population, and they affected the basic principles that had underlined the policy of adjusting benefits – both those guaranteeing a minimum income for subsistence and those replacing wages for short periods of time. The main amendments in the various branches are summed up in the Boxes appearing at the end of this chapter.

1.2.1 Adjustment of Benefits

One of the most far-reaching structural changes introduced in the national insurance system under the new legislation is that pertaining to the method of adjusting benefits and to the parameters of collecting insurance contributions, both linked until 2002 to changes in the average wage. The formulation of the policy of adjusting national insurance benefits in the mid 70’s was one of the most important stages in the development of the welfare state in Israel. The benefits were linked to changes in the average wage, out of the perception that benefit levels should be adapted to the standard of living of the population as a whole, and to prevent a situation whereby this standard of living rises and that of the weak population sectors lag behind. Since the mid 70’s, the old-age and survivors’ pensions, general disability pensions, income support benefit and alimony benefit were all determined in the law as percentages of the average wage and adjusted in accordance with the changes thereof. The average wage also served as a measure for adjusting the wage-replacing benefits, the collection parameters, and later on, for adjusting the minimum wage as well. Only the child allowances, linked to the income tax system, were adapted to price fluctuations. This policy of benefit adjustment has had an overriding role in reducing poverty (which also had been measured in Israel by means of the relative approach) and income gaps in the country. Even at times of crisis, when a stringent economic policy was put forward, such as the Economy Stability Policy of 1985, policymakers were careful to retain – and even to improve – the adjustment mechanisms.

In 2002, for the first time since the mid 70's, the Knesset approved a government decision not to adjust most benefits, as a temporary order for ten months, later extended in two stages: first till the end of 2003 and afterwards till the end of 2005. Further, it was broadened to cover all benefits paid by the NII. What is more, the government determined that beginning in 2006, benefits would be adjusted in accordance with price rises only, and not according to changes in the average wage, out of a new perception that the state's task should be limited to maintaining the purchasing power of the benefits only.

1.2.2 Changes in Benefits to the Working-age Population

The legislation of 2002-2003 changed beyond recognition three out of the four programs providing benefits to the working-age population: unemployment insurance, income support and child allowances. Legislative changes were introduced in work injury insurance and maternity insurance as well, such as lowering the benefit level (beyond the lateral reduction of 4% till the end of 2006) and shortening the maximum period of entitlement. On the other hand, the benefits provided in the framework of general disability insurance were barely affected in 2002-2003 by the government's socio-economic policy; the 4% lateral reduction did not apply to disability benefits; they were adjusted in 2002 (but not in 2003) in accordance with wage rises. It should be noted that in 1999-2002, following the strikes of the disabled population, amendments were enacted that improved the situation of people with disabilities, particularly those with severe disabilities – both adults and children.

Unemployment

Since the early 70's the government has embarked on a policy that gradually undermined the role of unemployment insurance as a safety net for workers who lost their jobs and as a mechanism for helping the unemployed utilize their earning potential by searching for work suitable to their skills. This policy was intensified in 2002-2003, during which extremely stringent changes were made in unemployment insurance: benefits were reduced, the maximum period for payment of benefits was shortened, and the conditions of entitlement were made stricter, mainly by means of lengthening the qualifying period. Even before the many amendments to the unemployment insurance came into effect, it was one of the strictest in Western countries – all the more so after the changes of 2002-2003.

Children

The legislation approved in 2002-2003 led to far-reaching changes in the system of child (family) allowances. These included, in addition to a structural change in the level of allowance in accordance with family size, a sharp reduction in allowance rates and in the public expenditure on support to families with children. These changes were anchored in four economic programs, and from one program to the next the cut in the allowances deepened. When the implementation of all the changes is completed in 2009, the level of the child allowance will be equal for every child, and lower than that paid to each of the first two children before this policy was instituted.

Income Support to the Working-age Population

The public debate on the social policy of the government in 2002-2003 reached its height when the government decided on a series of far-reaching changes in the income support system to the working-age population, the main ones being anchored in the Economy Arrangements Law of 2003. This policy was introduced as part of a labor force reform and was aimed – according to those who formulated it – at reducing the extent of the reliance of benefit recipients on the support system and encouraging them to join the labor market. The rise in the number of income support recipients, particularly in the past decade, was attributed to the “exceptional generosity” of the benefit and the range of various bonuses granted to benefit recipients in the fields of housing, health, public transportation, etc. This was in addition to the consideration of the failure of the employment service to carry out the employment test strictly and efficiently, and to find employment solutions to those benefit recipients who sought work – whether as a result of the expansion of unemployment, a lack of resources, or the fact that the employment service did not change its method of operation or adapt more modern approaches of dealing with its special clientele.

The new legislation applied to all components of the Income Support Law: level of benefit, income test and employment test.

Table 1: Income Support Benefit and Child Allowances: February 2004 Compared to January 2002

	Income support benefit				Reduction of benefit	
	Without child allowance		With child allowance			
	January 2002	February 2004	January 2002	February 2004	In NIS	Rate of change
Single-parent family with 2 children						
Without income from work	3,527	2,607	3,875	2,847	**1,028**	-26.5
Half minimum wage	3,267	1,927	3,615	2,167	**1,447**	-40.0
Minimum wage	2,286	967	2,634	1,207	**1,427**	-54.2
Couple with 2 children – regular rate						
Without income from work	2,961	2,240	3,309	2,480	**829**	-25.1
Half minimum wage	2,701	1,531	3,049	1,771	**1,278**	-41.9
Minimum wage	1,067	531	1,415	771	**644**	45.5
Couple with 2 children – increased rate						
Without income from work	3,490	2,607	3,838	2,847	**991**	-25.8
Half minimum wage	3,229	1,899	3,577	2,139	**1,438**	-40.2
Minimum wage	1,595	899	1,943	1,139	**804**	-41.1
New entrants – couple with 2 children, one spouse aged 46-54						
Without income from work	3,490	2,240	3,838	2,480	**1,358**	-35.4
Half minimum wage	3,229	1,531	3,577	1,771	**1,806**	-50.5
Minimum wage	1,595	531	1,943	771	**1,172**	-60.3
Couple with 4 children – increased rate						
Without income from work	3,490	2,607	4,888	3,448	**1,440**	-29.5
Half minimum wage	3,229	1,899	4,627	2,740	**1,887**	-40.8
Minimum wage	1,595	899	2,993	1,740	**1,253**	-41.9

The above table shows the aggregate damage resulting from the cut in the income support benefit in June 2003 and the accumulated cut in the child allowance up to February 2004, as compared to the situation in January 2002. The minimum income guaranteed to families with children without income from work fell drastically by amounts ranging from NIS 830 a month to those receiving income support benefit at the regular rate, to almost NIS 1,031 a month to single-parent families: a decrease of 26% as compared to January 2002. The income supplement benefit and the child allowance to families with two or more children having an income from work equivalent to half the average wage was shrivelled by about 40% (a cut ranging from about NIS 1,280 to families who received benefit at the regular rate, to about NIS 1,450 to single-parent families or couples who received the benefit at the increased rate). The income supplement to families whose income from work was equivalent to the minimum wage fell at a rate ranging from 45% to couples with children to 55% to single-parent families.

1.3 Changes in Benefits to the Retirement-Age Population

1.3.1 The Reform in the Pension System

In 2002-2003 the government decided on a far-reaching reform in both tiers of the pension system in Israel – The NII pension and the occupational pension. From the point of view of income support to persons retiring from the workforce, it is important to examine government policy in relation to both tiers of the pension system, since each has a different role: the first tier aims at guaranteeing a minimum income to pensioners by means of a basic pension, while the second aims at maintaining the relative standard of living of the pensioners and preventing it from falling drastically.

The most significant change introduced in the first tier is the cancellation of the linkage of pensions to the average wage. The implications of this change on the future level of benefits have been discussed above – the pensions were greatly eroded and the ability of the first tier to reduce poverty among the elderly was severely hampered. Only about 42% of the elderly population presently have pension from work, and the gaps in pension level among those who do have pension are even higher than the wage gaps in the economy. About 64% have pension up to half the average wage. The incidence of poverty among the elderly before transfer payments – mainly NII benefits – reaches some 60%. Even after the pensions extract about two-thirds of the elderly families from poverty, about a fifth of them remain poor.

In 2003 the government decided on a structural reform in the occupational pensions, to supplement the pension reform of the mid 90's. The 2003 reform included both insured persons of working-age and retired persons, and was focussed on covering the deficit of the veteran pension funds. The reform was in principle important and inevitable, but entails many risks. The implications will be felt, for better or worse, in the coming years. The government should re-examine the place of the first tier in the "new" pension system, from a social viewpoint, and in particular, should re-consider its policy regarding adjustment of NII pensions.

1.3.2 Raising of Retirement Age and Age of Entitlement to Old-Age Pension

The raising of the retirement age as a means of meeting the need to allocate more and more resources to the financing of pension payments – mainly due to the rise in life expectancy at the older ages and to early retirement – applies to both tiers of the pension system. In the spirit of the recommendations of the public committee to examine the retirement age (Netanyahu Committee, July 2000), the Retirement Age Law-2004 determined that the retirement age would be raised gradually to 67 for both men and women, although women aged 64-67 may choose to continue working, or to retire without any reduction in their pension. The law determined that the conditional age of entitlement in old-age pension would be raised as well: for men to 67, and for women to 62 at first and to 64 at the second stage. The absolute age of entitlement to pension (without income test) will also be raised gradually: from 65 to 70 for women, thus equalizing it to the present absolute age of entitlement for men. The payment of the old-age pension for housewives will be gradually postponed from age 65 to age 70.

The raising of the retirement age will be adapted to the other NII benefits as well. Benefits such as survivors' pension, disability pension, attendance allowance, income support benefit and unemployment benefit will be paid up to the new age of retirement and the long-term care benefit will be postponed until after this age.

It is estimated that the raising of the age of entitlement to old-age pension will considerably improve the NII's financial situation; however, government policy is not consistent in this respect. The savings resulting from the raising of the retirement age will be almost entirely set off by the loss of receipts of insurance contributions following the cancellation of the linkage to the average wage of the income ceiling liable for contributions. The entire population, both working and non-working, will contribute to the savings in old-age pension payments and in the additional collection of contributions, whereas only the better-off workers will benefit from the reduction in the burden of contributions resulting from the erosion in the income ceiling liable for contributions.

1.4 Benefit Payments

In 2003, total NII benefit payments –contributory and non-contributory benefits as well as additional payments carried out by the NII, mostly for government ministries – amounted to about NIS 44.9 billion, as compared to NIS 47.3 billion in 2002 and NIS 45.5 billion in 2001. These sums do not include the various administrative or operative expenses of the national insurance system.[1]

In 2002-2003, for the first time in decades, NII payments decreased in real terms by about 7.2%. Most of the decrease – 5.7% – took place in 2003. The benefit payments paid by the NII decreased from 9.42% of the GDP in 2001-2002 to 8.88% in 2003. This decrease would have been sharper, reflecting the scope of the cuts in the various benefits, had it not been for the rise in the number of benefit recipients. The estimated accumulated cut in 2003 is about NIS 5 billion.

The decrease in real terms in benefit payments characterized most national insurance branches and programs administered by the NII. Payments decreased in real terms by about 35% in the unemployment branch, by about 24% in the children branch and by about 12% in income support. In 2003 there was a sharp decline in payments of reserve service benefits, after a sharp rise in 2001-2002. The real decrease in payments characterized the old-age and survivors branch as well – 3.7% in 2002 but no change in 2003 – as well as the maternity branch – 3.3%.

There was a notable slowdown in the real growth rate of the work injury branch. Had it not been for the rise in payments of benefits to hostile action casualties, included in this branch, the total payments would have gone down by about 1% in real terms. Payments to hostile action casualties grew 2.3 times in the past three years, reaching about NIS 350 million in 2003. Even in the disability branch, which expanded considerably in 1999-2002 – following the favorable legislation put into effect after the strikes of the disabled population – the growth in payments slowed down (3%), more or less reflecting a rise in the number of recipients only. Payments in the long-tem care branch decreased by about 2% in real terms in 2003, while payments in the bankruptcy branch increased as a result of the deepening recession.

---

[1] These expenses are estimated at about 1.2 billion in 2003.

Payments of the contributory benefits under the National Insurance Law decreased by about 6.6% in real terms in 2002-2003, while payments of the non-contributory benefits under other state laws or under agreements with – and completely financed by – the Treasury (such as income support, alimony, old-age and survivors to new immigrants and reserve service benefits) decreased in real terms by 9%. The sum of non-contributory payments amounted to about NIS 9.45 billion in 2003, constituting some 21% of total benefit payments (as compared to 22.4% in 2002).

Diagram B presents the distribution of benefit payments by branch. There was a decrease in 2003 in the share of the children, unemployment and income support branches in total payments, as well as in the share of reserve service benefits, and a parallel increase in the share of other branches, especially of the two largest branches, old-age and survivors and general disability.

Table 2: Benefit Payments and Collection from the Public (percentages relative to the Gross Domestic Product), 1980-2003

Year	Benefit Payments		Collection from the Public	
	Total	Contributory Benefits	Total*	National Insurance Contributions**
1980	6.09	4.98	6.77	5.15
1985	7.14	5.51	6.57	4.45
1990	8.36	7.04	7.21	5.28
1991	7.41	6.14	6.75	5.00
1992	7.40	5.99	5.84	4.93
1993	7.77	6.28	6.96	5.11
1994	8.01	6.62	7.07	5.19
1995	7.69	6.02	8.02	4.49
1998	8.46	6.80	6.52	4.45
1999	8.40	6.73	6.48	4.42
2000	8.48	6.75	6.65	4.52
2001	9.62	7.56	7.07	4.79
2002	9.42	7.32	6.92	4.70
2003	8.88	7/02	6.81	4.60

* Including collection for the sick funds.

** Including *Treasury indemnification* for the reduction of national insurance contributions of employers.

1.5 Benefit Level

There was real erosion in the level of all benefits paid by the NII in 2002-2003, whether as a result of government policy or of the erosion in wages. During these years the basic old-age pension lost about 10% of its purchasing power, while the pensions paid to survivors and to elderly persons entitled to income supplement (not reduced by 4% in 2002) eroded by a lower rate – about 6% – in real terms. Due to the erosion of about 10% in real wages, there was no change in the level of the basic old-age pension relative to the average wage, while the minimum income guaranteed to the elderly and survivors even rose in terms of wages.

The maximum amounts of the income support benefit were highly eroded in real terms; for example, the benefit to a single person (under age 55) entitled to the increased rate was eroded by 15%, the benefit for a single parent with two children plus child allowances was eroded by about 28%, and the benefit to a couple with two children – by about 21%. The average benefit to a family declined between 2001-2003 by 20% in real terms.

Table 3: The Old-Age and Survivors' Pension and the Minimum Income Guaranteed to Pension Recipients (constant prices and percentage of average wage*), Monthly Average, 1975-2003

Year	Basic old-age & survivors' pension				Guaranteed minimum income (including child allowances)			
	Single elder		Widow/er with 2 children		Single elder		Widow/er with 2 children	
	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage
1975	618.5	14.9	1,027.3	24.8	1,061.8	25.5	1,997.2	48.1
1980	679.9	13.5	1,317.8	26.3	1,183.3	23.8	2,420.8	48.2
1985	768.1	15.2	1,487.7	29.5	1,535.0	30.5	3,070.8	61.2
1990	967.1	15.9	1.870.6	30.7	1,517.8	25.0	3,077.7	50.5
1995	978.9	15.5	1,897.5	30.1	1,638.3	26.0	3,397.0	53.9
2000	1.093.4	14.9	2,116.9	28.8	1,826.6	24.9	4,018.8	54.7
2001	1,185.3	15.8	2,296.1	30.5	1,982.2	26.3	4,344.3	57.7
2002	1,101.8	15.6	2,177.8	30.8	1,879.9	26.6	3,996.5	56.4
2003	1,114.0	16.2	2,158.0	31.4	1,863.0	27.1	4,031.3	58.7

* As measured by the Central Bureau of Statistics.

Table 4: Minimum Guaranteed Income to Working-age Population (at set prices and as percentages of average wage), monthly averages, 1985-2003

Year	Single				Single parent with 2 children* (incl. child allowances)		Couple with 2 children (including child allowances)			
	Regular rate		Increased rate				Regular rate		Increased rate	
	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage	2003 prices	% of average wage	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage
1985	1,228	24.5	1,532	30.5	3,069	61.2	2,764	55.1	3,223	64.3
1990	1,215	20.0	1,519	24.9	3,077	50.5	2,801	46.0	3,257	53.5
1995	1,227	19.4	1,532	24.3	3,392	53.9	2,936	46.6	3,395	53.8
2000	1,365	18.6	1,707	23.2	3,759	51.2	3,236	44.0	3,747	51.0
2001	1,482	19.7	1,852	24.6	4,072	54.1	3,476	46.2	4,031	53.6
2002	1,378	19.6	1,772	24.5	3,753	53.4	3,199	45.5	3,752	53.4
2003**	1,337	19.5	1,573	22.9	2,914	42.5	2,767	40.3	3,199	46.6
2003***			1,671	24.4	3,636	53.0			3,599	52.4

* 1985 and 1990 data refer to wodow wth two children who was entitled to income support.

** The eldest of the family is not yet 55.

*** At least one member of the famly is over 55.

The child allowance was highly eroded as well; the allowance to a family with two children was eroded by about 20% in 2002-2003, and the allowance to a family with four children – by about 27%.

The average daily unemployment benefit was eroded in real terms by 6%, due to the erosion in wages between 2001-2003. On the other hand, it rose a little relative to the average wage, due to the higher wage level of the unemployed persons just prior to their unemployment. In 2002-2003 there was a rise in the share of academics and veteran workers in the unemployment population as compared to previous years. This population earned higher wages, entitling them to higher unemployment benefits.

Table 5: Child-Allowance Point and Child Allowances* (constant prices and percentage of the average wage), Monthly Average, 1975-2003**

Year	Value of child-allowance point		Allowance for 2 children**		Allowance for 4 children		Allowance for 5 children	
	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage	2003 prices (NIS)	% of average wage
1975	182	4.4	365	8.8	1,140	27.4	1,550	37.3
1980	142	2.8	284	5.6	887	17.7	1,205	24.0
1985	161	3.1	182	3.6	1,244	24.7	1,767	35.1
1990	186	2.9	89	1.5	1,441	23.4	2,044	33.2
1995	181	2.8	361	5.8	1,452	23.4	2,065	33.4
2000	184	2.5	368	5.0	1,482	20.2	2,109	28.7
2001	182	2.4	364	4.8	1,468	19.5	2,379	31.6
2002	173	2.4	307	4.3	1,229	17.3	1,992	28.1
2003	171	2.5	290	4.2	1,071	15.6	1,711	24.9

* Including Special Allowance for Veterans.

** As measured by the Central Bureau of Statistics.

*** The allowance level in 1985-1993 relates to a family (up to 3 children) not eligible for the first child allowance, and since October 1990 – for the second child allowance as well. In March 1993 the payment of child allowance on a universal basis was renewed.

1.6 Benefit Recipients

In 2002-2003, there was a slowdown in the growth in the number of benefit recipients in most branches, and a sharp decline in the number of recipients of unemployment benefits and work injury allowance. In comparison with previous years, the slowdown was particularly notable in income support, while the numbers of recipients of child allowance and long-term care benefit barely changed. In some branches, the developments result from the legislative changes introduced in 2002-2003 or previously, or from changes in work procedures; in other branches, they can be explained by demographic factors or by the diminishing influence of the recession.

In old-age and survivors, the largest national insurance branch, the number of recipients grew by 2.3% in each of the years 2002-2003, as compared to an average of about 3.4% in each of the five previous years. In 2003 the NII paid benefits to about 700,000 elderly persons and survivors. The slowdown in the growth in the number of recipients stems only from the decrease in the scope of immigration to the country; the numbers of recipients of special old-age & survivors pensions declined by 1.4% in 2002 and by 3.9% in 2003. A significant slowdown occurred too in the growth of the number of recipients in the long-term care branch, providing in-kind benefits to elderly persons limited in their daily functioning – from 10% in 2001 (a similar rate for the previous five years) to 6.5% in 2002 and to about 1% only in 2003. An analysis of the entries to and exits from the system shows that the steep decline in the pace of growth stems from a decrease in the number of entrants (about 15%) and a decline in the rate of claims approved. In 2003, the number of claims for long-term care benefit declined unexpectedly (10%) for the first time in 12 years, mainly due to the decrease in the number of first-time claims. The rate of approved claims went down from about 49% in 2001 to about 43% in 2003. This development apparently stems from administrative and organizational changes.

In the children branch, a slowdown occurred for the third straight year in the number of families receiving child allowances. Following an average growth of 23% in 1997-200 (in keeping with the natural growth of the population), the growth rate went down in 2001-2003 from 1.7% to 0.4%. The number of children for whom allowance was paid went up by only 1% in each of the years 2001-2003, reaching about 2.18 million children living in about 940,000 families in 2003. It is not clear to what extent this trend is due to demographic factors or to more thorough examinations of entitlement of persons residing abroad, or persons not defined as residents, to child allowance.

In the general disability branch, the growth in the number of recipients of the general disability pensions remained more or less stable in 2001-2003; it rose by about 5%-5.5% every year, as compared to about 6%-7% a year in 1997-2000 and 11% a year in

Table 6: Number of Benefit Recipients in Main Insurance Branches, Monthly Average, 1985-2003

Year	Old-age and Survivors	General Disability: Disability Pension	General Disability: Attendance Allowance	General Disability: Benefit for Disabled Child	General Disability: Mobility Allowance	Work Injury: Injury Allowance*	Work Injury: Permanent Disability Pension	Maternity: Maternity Grant	Maternity: Maternity Allowance*	Children Families Receiving Child Allowances**	Unemploy-ment***	Income Support to Working-age Population	Long-term Care
1985	390.2	62.1	4.6	4.0	10.6	56.9	9.9	101.3	42.7	546.9	19.6	24.6	-
1990	442.6	73.4	6.5	5.8	11.4	56.7	11.6	103.6	43.7	532.5	50.6	31.8	25.0
1995	553.9	94.0	10.2	10.3	13.2	88.3	14.6	113.3	55.2	814.7	61.5	75.3	59.0
2000	657.1	135.3	16.6	15.3	16.8	76.2	19.8	131.8	70.6	912.5	92.6	128.4	95.7
2001	677.0	142.4	18.9	16.4	19.3	69.1	20.8	129.1	71.2	928.2	103.0	145.5	105.4
2002	692.9	150.5	20.6	17.5	20.9	70.0	521.8	128.5	71.4	935.0	97.1	151.6	112.2
2003	709.3	157.3	21.7	18.4	22.3	61.5	23.0	136.4	73.9	939.1	70.5	155.2	113.3
Annual Growth (percentages)													
1986-1990	2.6	3.4	7.2	7.7	1.5	-0.1	3.6	0.5	0.5	-0.5	20.9	8.6	17.4
1991-1995	4.6	5.0	9.4	12.2	3.0	8.4	4.4	1.8	4.8	8.9	4.0	19.4	18.7
1996-2000	3.5	7.6	10.2	8.2	4.9	-2.1	6.3	3.1	5.0	2.3	8.5	11.4	10.2
2000	3.4	6.4	16.9	8.5	17.5	3.1	4.8	4.9	7.3	2.3	-3.6	12.6	8.8
2001	3.0	5.2	13.9	7.2	14.9	-9.3	5.1	-3.6	0.8	1.7	13.1	10.6	10.1
2002	2.3	5.7	9.0	6.7	8.3	1.3	4.8	1.1	0.3	0.7	-7.3	6.5	6.5
2003	2.4	4.5	5.3	5.1	6.7	-12.1	5.5	6.1	3.5	0.4	-27.4	2.4	1.0

* The number of different recipients throughout the year.

** The figures for 1985 and 1990 include families to whom the allowance for the first and second child were reimbursed through the employers.

*** The figure for 1985 refers to the average number of payments. The figures for 1990 onward refer to the number of recipients.

1991-1995. There was a marked slowdown in the growth in the numbers of recipients of attendance allowance and mobility benefit, after sharp rises following the implementation of the legislation expanding coverage in 1999.

Regarding wage-replacing benefits, the decline in the number of recipients of injury allowance was sharply renewed in 2003 by 12%, continuing the trend that characterized 1997-2002. The number of recipients of injury allowance as a monthly average went down from about 92,8000 in 1996 to about 61,000 in 2003: an accumulated decline of about 33%. The rate of recipients of injury allowance out of total employees decreased from 4.3% in 1996 to 2.6% in 2003. This downward trend began with the cancellation of payment of injury allowance by the NII, for the first nine days, and continued with the shortening of the maximum period for payment of injury allowance from 182 days to 91 days. The recession in employment – and particularly in high-risk branches from the point of view of work injury, such as construction, agriculture and industry – also contributed to the trend of decline in the number of injury allowance recipients. However, the number of recipients of work disability pension rose by an average of 5% a year in 2001-2003, reaching about 23,000 in 2003.

The legislative changes led to a sharp fall – of about a third – in the number of recipients of unemployment benefit, from about 105,000 as a monthly average in 2001 to about 70,000 in 2003. This occurred despite the expansion of unemployment in those years. It is surmised that had it not been for the legislative changes, the number of recipients of unemployment benefits would have shot up to about 120,000 a month.

The number of women receiving maternity allowances also decreased in 2001-2002; in both years together this number grew by only 1%. On the other hand, the number of recipients went up in 2003 by 3.5%. The slowdown in employment in the past three years and the expansion of unemployment slowed down the growth in the number of employed women, and, therefore, also of the number of women entitled to maternity allowance.

Finally, the trend characterizing many branches did not pass over the income support system for the working-age population. Already in 2001-2002, even before the changes in the Income Support Law came into effect, the rate of growth in the number of income support recipients declined from about 13% in 1998-2000 to about 10.5% in 2001 and to about 6.5% in 2002. The amendments implemented in June 2003 ruled out benefits to about 4,500 families and made entry of new recipients difficult.

In 2003, a monthly average of about 155,000 families received income support, as compared to 151,000 in 2002: a rise of only 2.6%. It should be noted that the work sanctions that took place towards the end of 2003 and the changes introduced in the employment test contributed to the slowdown in the growth of number of income support recipients. This conjecture is strengthened by the rise in the number of claims in the first two months of 2004.

1.7 Collection of Insurance Contributions from the Public and the Sources of Financing Benefits

The NII benefit payments are financed from four sources: collection of national insurance contributions (direct collection from the public as well as Treasury indemnification against the reduction in employer and self-employed contribution rates); government participation in the financing of contributory benefits; and receipts from interest in investments of surpluses in government bonds. In addition to collection of national insurance contributions, the NII collects health insurance contributions and transfers them to the sick funds.

Many changes were introduced into the collection system of the NII in the years 2002-2003 – whether as temporary orders or as permanent amendments. During these years the government policy was to increase the burden of insurance contribution payments on the workers and employees, while lowering its own participation (indemnification) in these payments, with the aim of reducing the deficit in the state budget. The government preferred to increase the tax burden by means of national insurance contributions, even temporarily, so as not to interfere with the implementation of the income tax reform. Moreover, the changes in the benefit system and the adjustment methods affected the scope of collection by means of the NII as well as the government participation in financing both contributory and non-contributory benefits.

1.7.1 Collection of Insurance Contributions from the Public

Total collection from the public for national insurance branches and for the health system in 2002-2003 was influenced by the recession and by the government policy of raising the tax burden by means of national insurance and health insurance contributions. This policy – even if parts of it were only temporary – was actually in opposition to the government policy of easing the tax burden, as expressed in the recommendations of the Rabinowitz Committee for Income Tax Reform.

Box 8 presents the legislative changes in the NII collection system in 2002-2003, including those enacted under the Economic Policy Law of 2004. The two central changes that influenced the scope of collection during these years were the cancellation of the income ceiling liable for national insurance contribution rate and the raising by one percentage point of the national insurance contributions imposed on employers and self-employed. The former change was determined at first as a temporary order for July 2002-December 2003, but the ceiling was returned to a level of five times the average wage before the temporary order expired – in June 2003. The aim of this policy was to reduce the deficit in the state budget. Increasing the insurance contribution burden, particularly by canceling the ceiling, was criticized in several quarters, including within the Treasury.

The Minister of Finance at the time, Silvan Shalom, justified his policy on the basis of considerations of income distribution; when benefits to the weak population groups and the child allowances are sharply reduced, a more equitable distribution of the burden arising from the reduction in the state budget requires heavier taxation of the more affluent sectors. The NII supported the raising of contribution rates imposed on employers and self-employed persons as a source of reducing the budget, mainly in view of the significant lowering of these rates since the ‘80’s and out of concern that the alternative to increasing the burden of contributions would be an additional cut in benefits. On the other hand, the NII opposed canceling the ceiling, even on a temporary basis. The NII believed that in view of the cuts in benefits to the weak population groups, the tax burden on the higher-income employees and self-employed should be increased; however, it claimed that this increase should be carried out by raising the income tax rate, not by canceling the ceiling. Two reasons were given for this stand; the first, the fact that in every social security system, the income liable for insurance contributions has a ceiling; and the second, the concern that the gap that would be created between the taxation of individuals and that of companies would motivate individuals to organize themselves as companies in order to evade the additional tax burden. The NII estimated that this change in behavior would lead to a loss of about 15% of the collection potential stemming from the cancellation of the ceiling. Looking back, it is clear that the NII was correct; a relatively small percentage of individuals having an income level above the ceiling indeed organized themselves as companies. Those who wanted the ceiling restored invested great efforts in giving the impression (in the public and in media) that its cancellation led to the creation of tens of thousands of companies – even when the NII and the State Income Administration contended that the scope of collection did not exceed the estimates that had been presented during discussion of the new legislation.

According to the data of the company register for June 2002-March 2003, about 4,400 individuals (mainly lawyers, accountants, doctors and consultants) decided to act as companies. These constitute about 11% out of the approximately 40,000 individuals whose income was above the ceiling (about NIS 35,000 a month) before this policy was implemented.

There is no doubt that the persuasion campaign of the “wealthy” succeeded, since the government decided to restore the ceiling even before the temporary order expired. The loss of collection stemming from the restoration of the ceiling – about NIS 1.6 billion annually – created a deficit in the state budget and was followed by an additional cut in government expenditure and in NII benefits.

The restoration of the ceiling was only the first step in the Treasury’s policy of easing the burden of national insurance contributions on the higher-income employees and self-employed persons. In the framework of the overall policy of easing the burden of tax on income from work – and as part of the income tax reform – the government decided to cancel the linkage of the income ceiling liable for insurance contributions to changes in the average wage, and to adapt its level to price fluctuations only.

The efforts of the NII to ease the burden of national insurance contributions on low-wage earners were successful in July 2002. In discussions on a private bill regarding the contributions imposed on kibbutzim (collective settlements), the NII proposed a universal change to apply to all low and middle-wage earners, and not only to the kibbutzim. Under this proposal, anchored in an amendment (No. 50) to the NII Law, the reduced rate for employees was lowered to 1.4% of the income liable for contributions and in parallel, the regular rate was raised to 5.58% – without changing the scope of collection. All employees with income of up to one and a half the average wage benefited from a reduction in contribution payments, while all other employees had to pay more. The reduction in contributions was particularly significant for the low-wage earners – those whose income was up to half the average wage.

The government policy of increasing the burden of contributions was reflected in additional amendments, actually aimed at correcting distortions in the system. Work injured were obligated to pay national insurance contributions on their injury allowance, which constitutes a replacement of their wages, similarly to other wage-replacing benefits; the health insurance contributions imposed on soldiers in the standing army were equalized to the rate deducted from employees’ wages: recipients of early pensions were obligated to pay national and health insurance contributions on their full pension, at the rates imposed on employees (except for unemployment), with the aim of discouraging early retirement[2] The last change, implemented in 2004,

[2] It is more complex to relate to pensions as wages for purposes of income contributions, especially with regard to disability pensions.

benefited recipients of pensions up to the average wage, who will pay lower contributions, while the remainder will be obligated to pay more – sometimes much more. At the same time, it should be recalled that the government increased the tax burden on recipients of early pension (cancellation of the 35% exemption for income tax purposes) and on recipients of pension from the veteran funds (obligation of 2% as payment of administrative fees).

The policy of increasing the contribution burden was applied to the weak population groups as well, although in their case it has not yet been implemented. An amendment proposed in June 2003, but not yet implemented, obligates housewives, previously exempt from health insurance contributions, to pay these contributions of an amount of NIS 70 monthly. Data presented by the NII show that about 70% of housewives are in the lower five income deciles and that many housewives – or their husbands – receive NII benefits, such as unemployment, general disability or income support. However, collection of health contributions from housewives required resources from the NII that were not available. Furthermore, the Finance Committee of the Knesset set up a sub-committee to examine the changes in the contribution amounts to be imposed on certain groups of housewives (including an exemption from payment), to achieve the Treasury's aim of higher total collection. The committee discussions focused on an alternative to the law that was passed (in the framework of the credit point allotted to workers for non-working spouses) but not yet completed.

The cancellation of the ceiling in July 2002, its restoration in July 2003 and the raising of the contributions imposed on employers and self-employed persons in July 2003 (for an unlimited period of time) are the two amendments that affected collection from the public during the years 2002-2003[3] – although the raising of the health contributions imposed on soldiers in the standing army was also partially expressed in 2003 collection. The other changes will be reflected in the collection of 2004 and beyond. Of course, collection from the public was also affected by economic developments, particularly in the areas of wages and employment. During those two years wages were eroded by about 10% in real terms (by about 6.5% in 2002 and about 3% in 2003), while the number of employees grew by about 0.9% only in 2002 and 2% in 2003. There has been no change in the number of employee posts since 2001. The economic recession was also expressed in collection from self-employed and other non-employee insured.

[3] The raising of contributions imposed on employees and the self-employed persons influenced collection for five months in 2002, but for all of 2003. On the other hand, cancellation of the ceiling influenced collection for five months in 2002 and for seven months in 2003.

The potential for additional collection of national and health insurance contributions from the public stemming from the removal of the ceiling was estimated as approximately NIS 1.8 billion for a full year. However, even at the time of the estimations, it was assumed that the collection would amount to about 85% of the potential – some NIS 1.55 billion. The potential for additional collection from employers and self-employed persons was estimated as about NIS 2.1 annually; and after deducting the influences of the change in individual behavior (becoming companies) – about NIS 1.9 billion. On the basis of these estimates, and taking into account the number of months in 2002-2003 for which the amendments affected collection, the NII was meant to collect about NIS 1.45 billion as a result of the amendments. The data of Table 7 show that in 2002, the NII collected a sum of about NIS 31.4 billion from the public – a growth of about 5.6% in nominal terms as compared to 2001. Not taking the amendments into account, the growth would have been 0.7% – only slightly higher than that observed, considering the fact that the volume of wages did not increase between 2001 and 2002. The scope of collection did not change in real terms between 2001 and 2002, but were it not for the amendments, it would have declined by 4.8%.

These data show that the estimates presented by the NII on the influence of the legislation in collection from the public were verified, and they disprove the claim that the removal of the ceiling did not increase state income from taxes.

The table presents a similar analysis for 2003. It should be recalled that the potential of additional collection in 2003 resulting from the amendments was lower than in 2002; the volume of income above the ceiling not liable for contributions decreased in 2002 due to the establishment of the companies, and in 2003 the erosion in minimum wages continued. Furthermore, the influence of the recession on the income of self-employed persons became even stronger in 2003. In that year the NII collected a sum of NIS 32.3 billion – a nominal growth of 2.8% and a real growth of 2.2%. Were it not for the amendments, collection from the public would have decreased by 2.4%. It should be stressed that the influence of the legislation in 2003 included the additional collection resulting from the raising of the health contributions imposed on soldiers in the standing army.

Table 7 shows that the scope of collection from the public by means of the NII continued to grow in 2003 in relation to the GDP, reaching 6.5% as compared to 6.3% in 2001 and 5.9% in 2000. The trend of growth in the share of collection from the public out of total direct taxes collected from individual also continued, reaching 38.8% in 2003 as compared to 35.8% in 2001. The weight of the national insurance contributions out of total collection from the public went up from 64.7% to 66.2%, due to the differences in the influence of the legislation on collection of national and health insurance contributions.

Table 7: Collection for National Insurance Institute & Health System 1999-2003

	1999	2000	2001	2002	2003
In Current Prices (NIS Million)					
Total receipts from contributions	27,412	30,511	32,814	33,995	33,653
Total collection from public	24,771	27,655	29,724	31,378	32,268
For nat'l insurance branches	16,045	17,893	19,147	20,595	21,364
For health system	8,726	9,762	10,577	10,883	10,904
Total Treasury indemnification	2,641	2,856	3,090	2,617	1,385
Indicators of development of collection from the public					
A. Percentage of real change					
Total collection from public	4.4	10.4	6.3	-0.1	2.2
For nat'l insurance branches	4.1	10.3	5.8	1.3	3.5
For health system	4.9	10.7	7.2	-2.7	-0.5
B. As percentage of GDP					
Total collection from public	5.8	5.9	6.3	6.4	6.5
For nat'l insurance branches	3.7	3.8	4.0	4.2	4.3
For health system	2.0	2.1	2.2	2.2	2.2
C. As percentage of direct taxes to individuals					
Total collection from public	35.8	35.1	35.8	37.8	38.8
For nat'l insurance branches	23.2	22.7	23.0	24.7	25.7
For health system	12.6	12.4	12.7	13.1	13.1
D. As percentage of direct taxes					
Total collection from public	29.1	27.0	28.3	30.8	32.5
For nat'l insurance branches	18.9	17.5	18.2	20.1	21.5
For health system	10.3	9.5	10.1	10.7	11.0

1.7.2 Sources of Financing Benefits

Total NII receipts for financing its branches amounted in 2003 to about NIS 47.9 billion, in current terms. As compared to 2002, financing sources went down by 2.3% in real terms. Receipts from national insurance contributions (collection from the public and Treasury indemnification) declined in real terms by 2.3%, while government participation in the finance of contributory benefits – amounting to about NIS 10.8 billion – rose by 2%. Since government participation in the finance of contributory benefits (under article 32 of the NI Law) stems from the scope of collection of contributions from the public, the former should have declined at the same rate as the latter. However, in 2003, the government also transferred its debts from the previous year to the NII. Government financing of non-contributory benefits – amounting to about NIS 9.45 billion in 2003 – decreased sharply in real terms: by

Table 8: Sources of Financing National Insurance Branches, 1995-2003

Year	Total receipts	Collection of national insurance contributions	Government participation	Government financing of benefits	Receipts from interest
NIS (current prices)					
1995	23,581	12,171	4,222	4,650	2,507
2000	41,207	20,751	8,336	8,148	3,907
2001	46,110	22,237	9,952	9,756	4,075
2002	48,659	23,112	10,520	10,594	4,266
2003	47,912	22,749	10,802	9,453	4,500
Real annual growth (percentages)					
2000	7.6	9.8	1.6	10.8	3.6
2001	10.7	6.0	18.1	18.4	3.2
2002	-0.2	-1.7	0.0	2.7	-1.0
2003	-2.2	-2.3	2.0	-11.4	4.8
Distribution (percentages)					
1995	100.0	51.6	17.9	19.7	10.6
2000	100.0	50.4	20.2	19.8	9.5
2001	100.0	48.2	21.6	21.2	8.8
2002	100.0	47.5	21.6	21.8	8.8
2003	100.0	47.5	22.5	19.7	9.4

11.4%. This decrease stems from the cuts in benefits, particularly in the income support and alimony benefits paid by the NII, and from the decline in the scope of payments of the reserve service benefit.

NII receipts from interest on its investments amounted to about 4.5%, and they rose by about 4.8% in real terms, as compared to 2002.

An examination of the distribution of benefit finance by source of finance shows that the share of receipts from insurance contributions remained without change – 47.5% of total sources.

The share of the government participation in the financing of the contributory benefits rose from 21.6% in 2002 to 22.6% in 2003, but its share in the financing of the non-contributory benefits fell from 21.8% to 19.7%, respectively. The share of receipts from interest rose from 8.8% to 9.4%.

1.7.3 Surpluses/Deficits & Financial Reserves

The government policy in 2002-2003 was reflected in the shrinking of the current deficit in NII activities. A budgetary examination of NII branches shows that if income from interest in NII investments is not taken into account, the deficit was reduced by about 2 billion shekels – from about NIS 3.5 billion in 2001 to about NIS 1.5 billion in 2003. This development is in contrast to the trend of increase in the deficit that had characterized the NII since 1995. The decline of the current deficit in the past two years was particularly notable in the work injury and unemployment branches, while the current surplus in the children branch rose by about 2.4 billion.

On the other hand, the growth in the current deficit continued in the other branches, particularly in the disability branch in which expenditure grew as a result of the favorable legislation enacted following the strikes of the disabled population. The deficit in this branch grew by about NIS 1.2 billion between 2001 and 2003.

The improvement in the NII's financial situation is also expressed by taking into consideration income from interest on past surpluses. Total surpluses, including interest, went up by about NIS 2.3 billion in current terms, reaching about NIS 3 billion in 2003.

The branches in deficit are general disability, unemployment and long-term care. The assets of the unemployment branch ran out since 1999, and it is being financed entirely from the children branch.

Table 9: Surpluses/Deficit in National Insurance Branches, 2001-2002

Insurance Branch	Surplus/Deficit Without Interest on Investments			Surplus/Deficit Including Interest on Investments		
	2001	2002	2003	2001	2002	2003
	NIS million (current prices)					
Total	-3,446	-2,896	-1,526	629	1,370	2,974
Old-age & survivors	-643	-316	-930	1,023	1,490	1,010
General disability	-1,782	-2,504	-2,962	-936	-1,694	-2,202
Work injury	-1,196	-1,221	-897	-829	-891	-587
Maternity	-864	-897	-940	-692	-757	-830
Children	5,335	6,493	7,737	5,890	7,243	8,717
Unemployment	-3,080	-?	2,076	-3,080	-3,113	-2,076
Long-term care	-1,402	-1,496	-1,522	-1,045	-1,191	-1,262
Other	186	158	64	298	283	204

Diagram A: The National Insurance Institute - Resources and Uses

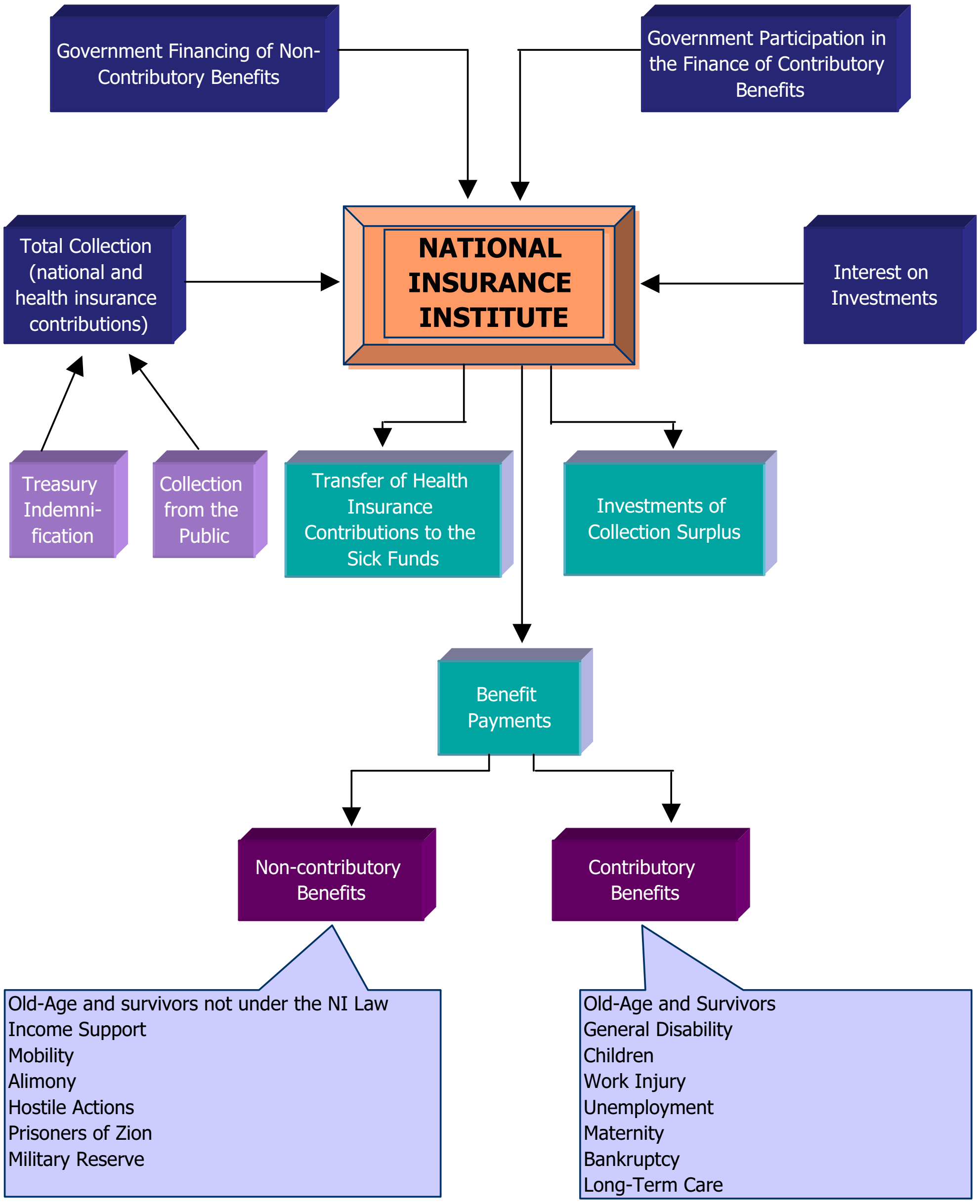
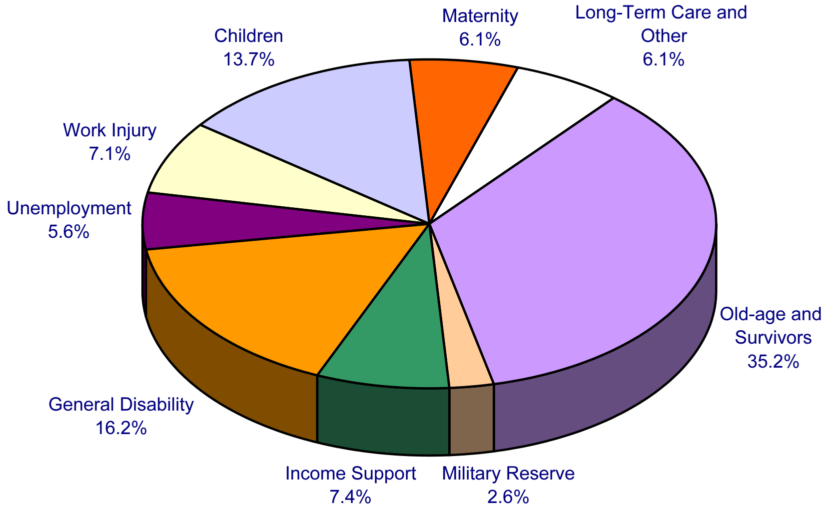
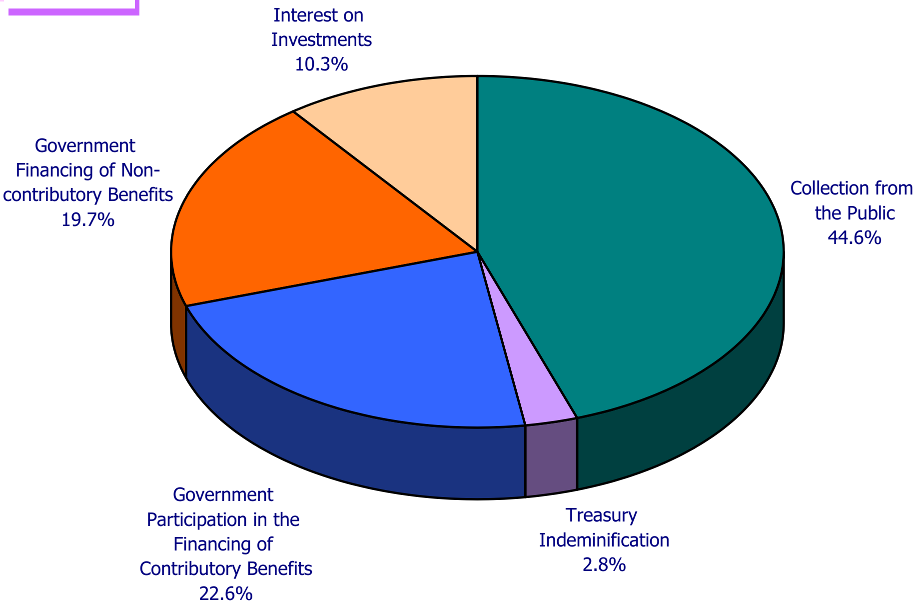


Diagram B: The Distribution of NII Benefit Payments and Receipts - 2003

Benefit Payments



Receipts



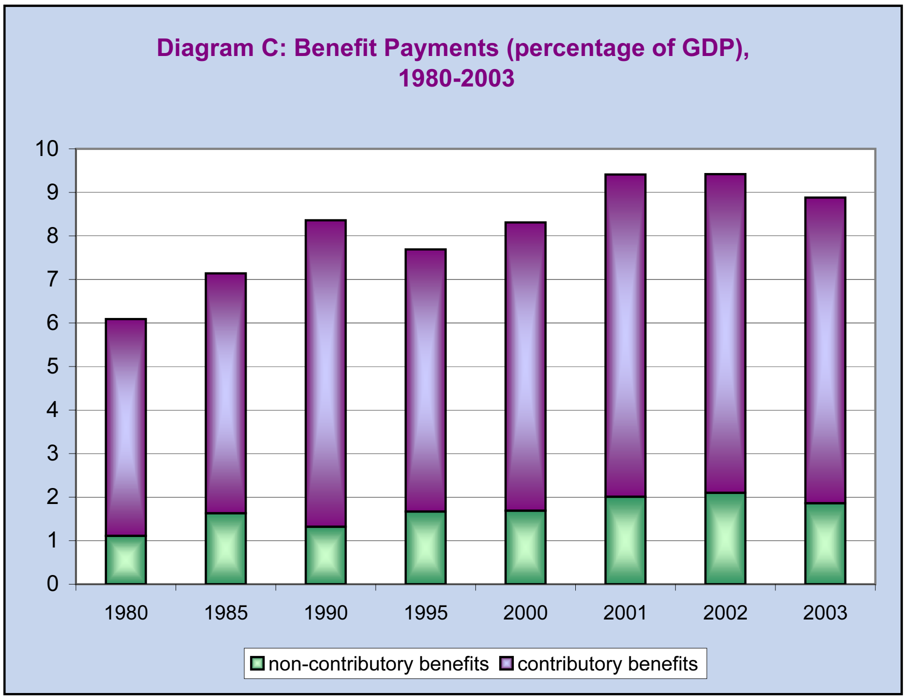


Diagram C: Benefit Payments (percentage of GDP), 1980-2003
10
9
8
7
6
5
4
3
2
1
0
1980
1985
1990
1995
2000
2001
2002
2003
non-contributory benefits
contributory benefits

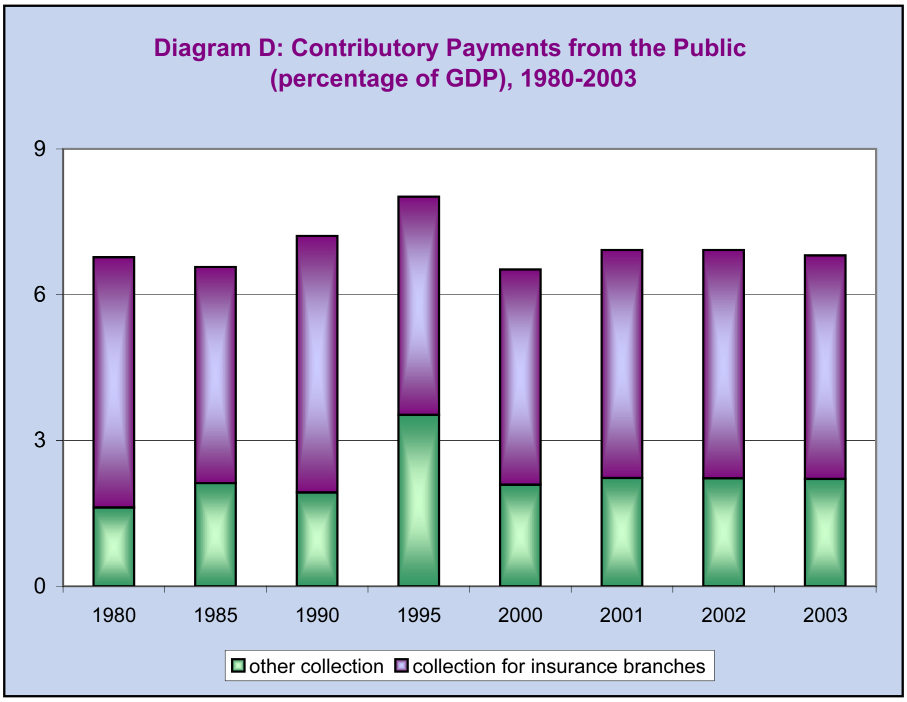


Diagram D: Contributory Payments from the Public (percentage of GDP), 1980-2003
9
6
3
0
1980
1985
1990
1995
2000
2001
2002
2003
other collection
collection for insurance branches

Box 1

I. Adjustment of Benefits and Cancellation of Linkage to Average Wage

Economy Arrangements Law-2002

* January 2002 cancellation of 1.2% adjustment of those benefits linked to average wage – benefits determined in law as percentages of the average wage (old-age and survivors, income support and alimony). This measure was carried out by freezing the average wage at its 2001 level (NIS 6,964 per month, as compared to NIS 7,500 in January 2002.)
* Cancellation of 1.4% adjustment of child allowances. The value of a full credit point was reduced from NIS 174 per month to its 2001 rate of NIS 171 per month.
* Cancellation of adjustment of benefits was anchored in a temporary order for March-December 2002.

Emergency Economy Law-July 2002

* Extension of temporary order regarding non-adjustment of benefits to additional benefits in General Disability, Long-term Care, Work Injury and maternity allowance. Were it not for the amendment, all benefits linked in one way or another to the average wage would have been updated by 0.9% in 2003, and child allowances – by 6.5%. This temporary order was meant to extend until the end of 2003.

Economy Recovery Law-June 2003

* Extension of temporary order regarding non-adjustment of most benefits linked to the average wage as well as child allowances, until the end of 2005. Benefit recipients will not be compensated for non-adjustment of these benefits upon renewal of the adjustment process in early 2006.
* Cancellation of linkage of benefits to average wage and their adjustment to price rises only, as of 2006. From 2006, all benefits will be expressed in terms of a "basic amount" adjusted in accordance with price rises.

Two exceptions were determined in the law:

a) Benefits in Old-age and Survivors and the dependents' benefits in Work Injury will be adjusted in accordance with price rises as of January 2004.

b) Benefits will be adjusted in 2004-2005 only if the index goes up by at least 5% a year.

* The replacement of the "average wage" by the "basic amount" affects wage-replacing benefits (such as unemployment benefit, injury allowance and maternity allowance) as well. The maximum sums for payment of injury allowance, maternity allowance and reserve service allowance will be increased at the rate of the price rise, as will the wage scales in the calculation of the unemployment benefit. However, the level of the latter benefit will still be limited by the rate of the average wage (or 2/3 of this wage), as to be calculated from time to time.
* Freezing of linkage of the minimum wage to changes in the average wage in 2003-2005 (but not to the cost-of-living increment). As of 2005, the minimum wage will be linked to the average wage, as was the case up to March 2002.

II. Lateral Reduction in Benefit Rates

Emergency Economy Law-2002

* 4% reduction in almost all benefits, as a temporary order for July 2002- December 2003. The following benefits were <u>not</u> reduced: general disability, survivors, dependents in work injury and old-age pensions to recipients of income supplement.

Economy Recovery Law-June 2003

* Extension of temporary order regarding the 4% reduction of benefits until the end of 2006. This reduction shall not apply to disability benefits as a result of work injury.

Box 2

Changes in Unemployment Insurance

Emergency Economy Law-July 2002

* Extension of qualifying period for unemployment benefit and reduction of period out of which this period may be accumulated. Only unemployed persons who worked at least 360 days out of the 540 days preceding their unemployment are entitled to benefit, as compared to 180 days out of 360 or 270 days out of 540 before the amendment.
* Reduction of maximum period for entitlement to unemployment benefit for persons under 25, from 100 days to 150 days.
* 30% reduction in rate of unemployment benefits paid to participants in vocational training.

Economy Arrangements Law-2003

* Payment of unemployment benefits to participants in vocational training restricted to the maximum period of entitlement to benefit.

Economy Recovery Law-June 2003

* Unemployment benefit to participants in vocational training who have less than 12 years of schooling will be paid for a period of 138 days, even if the participant is entitled to a maximum period of 50 or 100 days.
* Entitlement to unemployment benefits denied to controlling shareholders who work in their companies as well as to students who are not available for work due to their studies.
* The formula for calculating unemployment benefits was amended, to a uniform formula for those having incomes lower or higher than the average wage.

Box 3

Changes in Family and Maternity Insurance

Family

Economy Arrangements Law-2002

* 12% reduction in child allowances to all families for all children, as temporary order for March-December 2002 – carried out by decreasing the number of credit points per family, in accordance with its size (on the basis of 0.88 of a credit point instead of a full credit point – NIS 151 instead of NIS 171 per month).

Emergency Economy Law-2002 (July)

* The rate of reduction of child allowances was raised to 15% for all children and in all families (according to 0.85 of a credit point, or NIS 146 per month) as a temporary order until the end of 2003.
* Reduction of child allowance to families of 3 or more children, in which one of the members (parents or their children) did not serve in one of the security forces. This reduction was not carried out due to a petition to the court, and was later cancelled altogether under Economy Recovery Law of June 2003.

Economy Recovery Law-June 2003

* A plan to gradually (in 7 stages) reduce child allowances from August 2003 to January 2009, when a uniform allowance of NIS 144 (0.84 of a credit point) will be paid for every child, regardless of his/her place in the family.
* For "new" children (born in June 2003 or thereafter) a uniform allowance (NIS 144) will be paid, regardless of his/her place in the family.

Economic Policy Law for Fiscal Year 2004

* Child allowances will be reduced by NIS 24 for every child during February-June 2004. This reduction will continue for the first three children until the end of 2005, while for the fourth and subsequent children, there will be a reduction of NIS 5

during July 2004-December 2005. This reduction is in addition to the previous graded reductions, and does not replace it.

* For every "new" child, born in February 2004, an allowance of NIS 120 will be paid until December 2005.
* The second stage of the graded reduction under the Economy Recovery Law will be postponed from January 2004 to July 2004.
* As of July 2004, families with 3 or more children who receive income support will receive an increment to their child allowance: 0.59 of a credit point (NIS 101) per month for the third or fourth children in the family.

Maternity

Economy Recovery Law-June 2003

* Reduction of maternity grant paid for second and subsequent children in families, from 20% to 6% of average wage, and reduction of the grant paid for the fifth and subsequent children in families, from 40% to 6% of the average wage. The maternity grant for the first child remained at a level of 20% of the average wage.

Economic Policy for Fiscal Year 2004

* Raising of maternity grant for second child in families only, from 6% to 9% of the average wage.

Box 4

Changes in Income Support and Alimony Insurance

I. In NII Benefits

Economy Arrangements Law–2002

* Cancellation of income support benefit at increased rate to those entitled after received benefit at regular rate for 24 months, whether consecutive or not. (At that time the regular rate had been about 20% lower than the increased rate.) The change was implemented in April 2002.
* Taking the full amount of unemployment benefit into account for purposes of determining entitlement to income supplement and its level. Prior to this amendment, unemployment benefits were deducted by a sum equivalent to 13% or 17% of the average wage, according to family composition.

Economy Arrangements Law–2003

* Reduction of maximum amounts of income support benefit at both regular and increased rates, by8% to 23%, depending on family composition.
* Cancellation of income support benefit at increased rate to claimants aged 46-54. This change applies to "new" claimants only (who begin receiving benefits in January 2003 or thereafter, either for the first time or after a 6-month break.
* An <u>additional</u> reduction of income support benefit paid to single claimants under 25 and to couples without children, one of whom is under 25, with a few exceptions (persons unable to work for health reasons). The benefit paid to young claimants is at the rate of 80% of the <u>new</u> maximum amounts determined in this law.
* Reduction of amount of income from work not taken into account (disregard) for purposes of determining entitlement to income supplement and its level – from 13% to 5% of the average wage for a single person, and from 17% to 7% of the average wage for other family compositions.

* Determination of rate of set-off against income from work that is higher than the income not taken into account, at a level ranging from 60% to 70%, according to family composition.
* Cancellation of "determining sums"; the level of income from work ruling out entitlement to benefit is deduced from the new sums of income not taken into account and from the new set-off rates. For most family compositions, and particularly for single-parent families, the income level ruling out benefit was lowered, leading to the ruling out of entitlement to benefit to some families who would otherwise have been entitled, or could be entitled in the future.
* The changes in the level of benefit and in the structure of the income test apply also to women entitled to alimony from the NII.
* All the above changes – reduction in maximum amounts of benefit and changes in parameters of income test – do not apply to single claimants aged 55 or over, nor to families in which at least one of the spouses is over 55.
* Cancellation of exemption from employment test (reporting to the employment bureau) for mothers of children aged 2 to 7; that is, only mothers of children up to age 2 will continue to b exempt from the employment test. The exemption was also cancelled for widows receiving survivors' pension or income supplement. These widows had been exempt from the employment test regardless of the age of their children. The exemption will continue to be in effect for single parents entitled to alimony, regardless of the age of their children.
* Cancellation of the situation entitling to benefit, "a person unsuitable for placement at any job", with a few exceptions. The labor exchange is no longer permitted to exempt recipients of income support benefit from reporting regularly to the exchange – except for persons aged 55 or over, who at the time of the law's enactment were classified as "persons permanently unsuitable for placement at any job."

II. In Other Systems

Economy Arrangements Law-2003, Economy Recovery Law-June 2003 and Government Decisions

* Cancellation of automatic 70% discount on municipal tax to *new recipients* of income support benefit: those entitled to benefit on January 1, 2003 or who were previously entitled and became re-entitled after 6 months elapsed since payment of benefit ceased. These *new recipients* will be entitled to discount according to a means test specified in the relevant regulations of the Ministry of the Interior. Those aged 50 or over who began receiving benefit after January 1, 2003 will continue to receive a 70% discount, but only in 2004. These rules apply to women receiving alimony benefits from the NII as well.
* Cancellation of discount in public transportation to *new recipients* of income support and alimony, as of January 1, 2003.
* 4% reduction in rental assistance, and 40%-50% reduction in this assistance to *new recipients* under 55. Lower rates of reduction to those aged 55 or over. In addition, a 5% annual reduction from the fourth year onward to those who received assistance for three years. In 2004, an additional 7% cut was determined in rental assistance. These reductions are anchored in government decisions.
* Cancellation of exemption of *new recipients* from TV fee. The required regulations for this measure have not yet been signed by the Minister of Industry and Commerce.
* Cancellation of discount in payments for doctors' visits (amendment of National Health Law).

Box 5
Changes in General Disability and Work Injury Insurance

General Disability

Amendment to N.I. Law 54 – Coming into effect in March 2002

* Payment of a new pension (in addition to disability pension) to persons with a disability degree of at least 50% and medical disability of at least 75%. The rate of this "additional monthly pension" rises with the increase in medical disability.
* Payment of a special benefit to persons entitled to attendance allowance, suffering from a severe disability. The rate of this special benefit goes up with the rise in the degree of the disabled person's dependence on others.
* Payment of an additional monthly benefit to a disabled child who receives a disability pension at a rate of 100% or more.
* Payment of an old-age pension at the rate of the disability pension (including the "additional monthly pension") paid before the disabled person had reached the age entitling him to an old-age pension. This amendment applies to disabled persons who reached 65 on January 1, 2002 or thereafter.

Economic Policy Law-2001

* Raising of medical threshold for entitlement to disability pension from 40% to 60%, unless there is a disability degree of 25% or more from a single impairment.

Work Injury

Economy Arrangements Law–2002

* Shortening of maximum period of entitlement to injury allowance from 182 days to 91 days.

Economy Recovery Plan-June 2003

* Reduction of lump-sum grant paid to persons whose medical disability, as a result of a work injury, is lower than 20%: from a sum equivalent to 70 benefits to a sum equivalent to 43 benefits.

Box 6
Changes in Long-Term Care Insurance – Reduction in Number of Care Hours

Emergency Economy Law-July 2002

* 4% reduction in long-term care benefit, leading to a half hour decrease in the number of care hours (from 11 hours to 10.5 hours for dependent elderly in the lower level of entitlement, and from 16 hours to 15.5 hours for those in the higher level of entitlement). The reduction was carried out in September 2002.

Economy Recovery Law-June 2003

* 7% reduction of benefit to elderly in the lower level of entitlement led to an additional decrease of ¾ of an hour in the number of care hours (from 10.5 hours to 9.75 hours) for these elderly.

Box 7
Other Related Amendments – Residence & Retroactive Payment of Benefits

Economy Arrangements Law-2003

* Amendments in the definition of residence, as a condition of insurance and of entitlement to benefits: a person residing in Israel illegally or under one of specified visas will not be considered a resident. Also, a person who could be considered a resident according to his visa will not be considered as such if he had lived in the country for less than 183 days during the first year after having received the visa (with the exception of new immigrants).
* A person entitled to a benefit paid only in Israel who is absent from the country for a year or more will be entitled to this benefit only after he has returned and resided in the country for at least a year. This rule has exceptions applying to certain situations (such as persons leaving the country for purposes of medical treatment) and certain branches (such as Maternity, Work Injury and Bankruptcy). Furthermore, it does not apply to persons who give notice beforehand on their absence from the country and on the length of this absence. The rules will come into effect after the relevant legislation is prepared.
* Cancellation of payment of increment for dependents (spouse and children) in the framework of many benefits, when the dependents are not residents of Israel.
* A foreign worker residing in Israel illegally may receive wage-replacing benefits (work injury, maternity and bankruptcy) only when he is outside of the country. This restriction does not apply to grants (such as the maternity grant) or to in-kind medical treatment (such as hospitalization of mothers giving birth).
* Limitation of the retroactive payment of benefits to 12 months preceding the date of claim, from 48 months prior to the amendment.

Box 8
Changes in NII Collection System

Economy Arrangements Law-2002

* Cancellation of 1.2% adjustment, carried out in January 2002, in collection parameters (such as scale of reduced rates, income ceiling liable for contributions and minimum income for payment of contributions for various types of insured persons).

Emergency Economy Law-July 2002

* Cancellation of income ceiling liable for national insurance and health insurance contributions as a temporary order for July 2002- December 2003. Up to July 2002, the income ceiling liable for contributions was 5 times the average wage on the share of the employee and the self-employed as a worker, and 4 times the average wage on the share of the employer for his worker and of the self-employed as an employer.
* Raising of insurance contributions by one percentage point to employers and self-employed, as against the lowering of the contributions paid by the government (indemnification) by one percentage point.
* Extension until the end of 2003 of the temporary order regarding non-adjustment of collection parameters in accordance with changes in the average wage.

NII Law Amendment No. 50 (private bill approved by the Knesset-July 2002.

* Lowering of the reduced rates of NII contributions (imposed on income of up to half the average wage) deducted from employees – from 2.66% to 1.4% of the income liable for contributions, in parallel to the raising of the regular rates from 4.9% to 5.52%.

Economy Recovery Law-June 2003

* Extension until the end of 2005 of temporary order regarding non-adjustment of collection parameters in accordance with changes in average wage.

* Restoration of income ceiling liable for contributions to 5 times the average wage for workers, employers and self-employed, as of July 2003, before the expiration of the temporary order.
* Health insurance contributions imposed on housewives (married women who not employed outside their households). This measure has not been yet implemented.
* Injury allowance paid to work injured became liable for national insurance contributions.

Economy Arrangements Law- 2003

* Equalizing rate of health insurance contributions imposed on soldiers in the standing army to the rate deducted from workers' salaries. Previous to the change, the former paid a lower rate of these contributions.

Economic Policy Law-2004

* Obligating recipients of early pension to pay national and health insurance contributions on the full amount of their pension (instead of on half their pension), and at the same rates imposed on workers – except for the Unemployment branch.
* Cancellation of linkage of the ceiling to changes in the average wage as of 2006, and the adaptation of its level to price fluctuations. The other parameters of the contribution system determined as percentages of the average wage will continue to be adjusted in accordance with changes thereof.

Chapter 2

Trends of Development in Poverty and Income Inequality
(Summary)

Leah Achdut
Refaela Cohen
Miri Endweld

2.1 Introduction

As part of research carried out in Israel on poverty and income distribution, a relative approach to measuring poverty was formulated in the early 1970s, in line with that accepted by the majority of researchers and social policymakers in the western world. According to this approach, poverty is an expression of relative distress that should be evaluated in relation to the standard of living typical of a given society: a family is considered poor not only when it is unable to purchase a basic basket of products necessary for its subsistence, but also when its living conditions are significantly inferior to those characteristic of the society as a whole. The relative approach further recognizes that distress is not only reflected in low income, but may also be expressed in the level of assets, housing conditions, education and public services available to those in distress. Nevertheless, since there is no agreed index that takes into account all the constituent aspects of distress, and since the National Insurance Institute possesses data (taken from Central Bureau of Statistics Income Surveys) only for the current income of households in Israel, poverty is measured solely as a function of the latter. The relative approach offers several operative methods for measuring poverty based on the level of income which rely, as a common denominator, on a comparison of the level of income of families on the lowest scale of income with the level of income of all other families. Each method is predicated on a "poverty line" set as a percentage of the income which is "representative" of society. A family whose income is below the poverty line will be considered poor, without this necessarily implying that the family suffers from want in the form of hunger, malnutrition, threadbare clothing or dilapidated housing, but only that its income is significantly lower than the representative income.

In Israel, the method for measuring poverty is based on the following three principles:

a. The first principle views the family's net income as the relevant income for assessing poverty. Net income is defined as the family's market income (from work as well as from ownership of physical production means and financial assets) plus transfer payments (received not in return for economic efforts, such as national insurance benefits or support from institutions and individuals in Israel and abroad), less direct taxes (income tax, national insurance contributions and health insurance contributions).

b. The second principle regards the median net income of the population as the society's representative income. Median income is defined as the level of income which 50% of families have at least that income, while the remaining 50% have a higher level of income. The poverty line is defined as the level of income equivalent to 50% of the median net income. A family whose net income is lower than one half of the median net income is thus regarded as poor.[1] Economic growth leading to an increase in the median net income also results in the raising of the poverty line. A non-poor family whose net income has increased by less than the rate of increase of the poverty line may thus become a poor family.

c. The third principle adjusts the poverty line to the family size. This principle is based on the assumption that family size involves economics of scale, whereby the growth of a family by an additional person increases its needs not by an equivalent, but rather by a lesser, proportion. In other words, the additional income required by a family in order to maintain a fixed standard of living decreases with the increase in the number of family members. To enable a comparison between the standard of living of families of different sizes, an "equivalence scale" was developed by which the needs of each such family can be measured against the needs of a family of a given basic size. More specifically, the equivalence scale translates the number of persons in a family into the number of "standard" persons (or the number of "standard adults") in that family (Table 1). The scale is based on a two-member family which is assigned a value of two standard persons. According to this scale, a family with one member has a value of 1.25 standard persons. In other words, the needs of a one-member family are not assessed as equivalent to one half the needs of a two-member family, but as greater. Similarly, the needs of a four-member family (which has a value of 3.2 standard persons) are not set at double the needs of a two-member family (which has a value of 2 standard persons), but at less than double (only 1.6 times greater).

In keeping with these principles, the poverty line per standard person in Israel was set at 50% of the median net income per standard person. A family in Israel is classified as poor if its net income, divided by the number of standard persons in the family, is lower than the poverty line per standard person. The poverty line per family can be calculated in a similar manner – by multiplying the poverty line per standard person by the number of standard persons in the family.

The poverty line per standard person in 2002 stood at NIS 1,394 a month, compared with NIS 1,385 in 2001 (in current values for the respective survey periods). In real terms, the poverty line per standard person decreased by 4.7% compared to 2001. The average wage in the economy declined by 4.5% in real terms between the Income Survey dates. The poverty line per standard person remained 24.5% of the average wage in 2002. Table 1 presents the poverty lines for families of different sizes, in shekel values and as percentages of the average wage.

---

[1] The median income is preferable to the average income, as representing the typical standard of living, since the latter is affected by extreme values in income distribution (i.e. by very high or very low incomes).

Table 1: Number of Standard Persons and the Poverty Line per Family, by Number of Family Members, 2000-2001

Number of family members	Number of standard persons	Poverty line per family	
		percentage of the average wage	NIS per month
1	1.25	24.5	1,743
2	2.00	39.2	2,789
3	2.65	51.9	3,696
4	3.20	62.7	4,463
5	3.75	73.5	5,230
6	4.25	83.3	5,927
7	4.75	93.1	6,624
8	5.20	101.9	7,252
9	5.60	109.7	7,810

As already indicated, the Annual Income Surveys conducted by the Central Bureau of Statistics (CBS) serve as the basis for calculating the dimensions of poverty and income inequality in Israel. Up until 1997 (inclusive), the survey population included households whose head was an employee or non-working person, in urban localities with 2,000 or more inhabitants (excluding East Jerusalem)[2]. In 1998 the Central Bureau of Statistics decided to produce a combined Income Survey, based on both the current Income Survey and the Family Expenditures Survey. The combined Income Survey is based on a larger sample (1.8 times the previous sample) and encompasses 95% of all households in Israel in most forms of settlement. In addition to the employee and non-working populations in urban localities, the combined Income Survey also covers the self-employed population, the population in the moshavim and in rural and community localities, and the inhabitants of East Jerusalem.[3] However, in 2001 the inhabitants of East Jerusalem were not included in the survey, due to difficulties in data collection. For comparison purposes, the 2002 data were reproduced without East Jerusalem.

---

[2] Up until 1994 (inclusive), the Income Surveys included non-Jewish localities with 10,000 or more inhabitants (excluding East Jerusalem). Since 1995, the Income Surveys have been expanded to include non-Jewish localities numbering 2,000–10,000 inhabitants.

[3] The populations not yet included are mainly the kibbutzim and the Beduin inhabitants who do not reside in permanent localities.

The present summary surveys the dimensions of poverty and income inequality in Israel in 2001-2002 on the basis of the combined Income Survey, and presents the main findings regarding the impact of transfer payments and direct taxes in reducing their scope. The dimensions of poverty are expressed by means of the two most widely used aggregate poverty indices in empirical studies, both in Israel and abroad: the poverty incidence and the poverty gap. The poverty incidence index indicates the scope of poverty in terms of the percentage of poor families in the total population. The poverty gap index reflects the depth of poverty: the poverty gap of a poor family is defined as the difference between the poverty line (corresponding to the family's size) and the family's actual income, while the poverty gap of the population as a whole is defined as the sum of the poverty gaps of the total number of poor families in the population. The poverty gap index can be standardized and defined as the ratio between the average poverty gap per poor family and the poverty line (hereafter, the "poverty gap ratio"). Income inequality among the entire population is measured by the GINI index.

2.2 Main Developments

The main developments in the dimensions of poverty in Israel in 2002 were as follows (Table 2):

a. In 2002 there was no change in the incidence of poverty in Israel compared to 2001. The percentage of families whose net income (after transfer payments and direct taxes) was below the poverty was 17.7% in 2002.

b. The number of poor families totaled 325,100 in 2002, compared to 318,400 in 2001. The increase in the number of poor families resulted entirely from the population growth in the country.

c. The percentage of poor persons in the total population of persons declined slightly – from 19.6% in 2001 to 20.0% in 2002.

d. The incidence of poverty among children rose significantly in 2002. The percentage of poor children in the total population of children rose from 24.9% in 1999 to 26.9% in 2001 and to 28.1% in 2002. The number of poor persons reached 1,212,000 in 2002 (as compared to 1,164,100 in 2001), and included 556,400 children (525,500 in 2001).

Table 2: Poverty in Total Population, by Selected Poverty Measures 2001 and 2002

Poverty measure	Before transfer payments and direct taxes	After transfer payments only	After transfer payments and direct taxes
2001			
Poor population			
Families	605,700	258,700	3189,400
Persons	1,930,400	965,100	1,164,100
Children	753,700	450,200	525,500
Incidence of poverty (%)			
Families	33.6	14.4	17.7
Persons	32.5	16.3	19.6
Children	38.5	23.0	26.9
Poverty gap ratio (%)*	65.3	26.2	26.1
2002			
Poor population			
Families	612,800	263,000	325,100
Persons	1,9541,100	1,024,500	1,212,000
Children	760,100	488,200	556,400
Incidence of poverty (%)			
Families	33.5	14.4	17.7
Persons	32.3	16.9	20.0
Children	38.3	24.6	28.1
Poverty gap ratio (%)*	67.0	28.1	28.8

* The weight given to each family in calculating the measure is equivalent to the number of persons in the family.

e. In 2002, the contribution of transfer payments and direct taxes to reducing the incidence of poverty decreased. Transfer payments and direct taxes extricated 47.2% of the total number of poor families from poverty, as measured by market income, compared to 47.4% in 2001 (Table 3). The contribution of transfer payments and direct taxes to reducing the incidence of poverty among persons decreased by 38.1% (39.7% in 2001), and among children – by 26.6% compared to 30.3% in 2001. The contribution of transfer payments alone (excluding direct taxes) to reducing the incidence of poverty among families exceeded the joint contribution of transfer payments and direct taxes: 57.0% in 2002.

The stability in the incidence of poverty by net income, which characterized the population as a whole, was not observed among all specific population groups. Specifically, while the poverty incidence among the elderly fell a bit, it rose slightly among large families and families headed by a non-worker who is of working age. Among other population groups, the incidence of poverty remained unchanged.

Table 3: The Impact of Transfer Payments and Direct Taxes on Poverty in Total Population, by Selected Poverty Measures, 2001-2002

Poverty measure	Percentage of decrease stemming from transfer payments only		Percentage of decrease stemming from transfer payments and direct taxes	
	2001	2002	2001	2002
Incidence of poverty (%)				
Families	57.3	57.0	47.4	47.2
Persons	50.0	47.7	39.7	38.1
Children	40.3	35.8	30.3	26.6
Poverty gap ratio (%)*	59.3	60.0	58.1	57.0

* See note to Table 2.

There were marked differences in the dimensions of poverty by geographical dispersion and locality. Bnei Brak, Jerusalem and Ashdod are the poorest cities of Israel according to the poverty indices: 20%-31% of families living in these cities have a net income below the poverty line.

In 2002 there was a widening of income gaps in the economy. The Gini index for distribution of economic income (stemming mainly from the family's work as employee and self-employed) increased from 0.5277 in 2001 to 0.5320 in 2002 – an increase of 0.8%. The Gini index for inequality in income distribution in housheolds headed by employees increased by 1.4% (from 0.4389 in 2001 to 0.4452 in 2002).

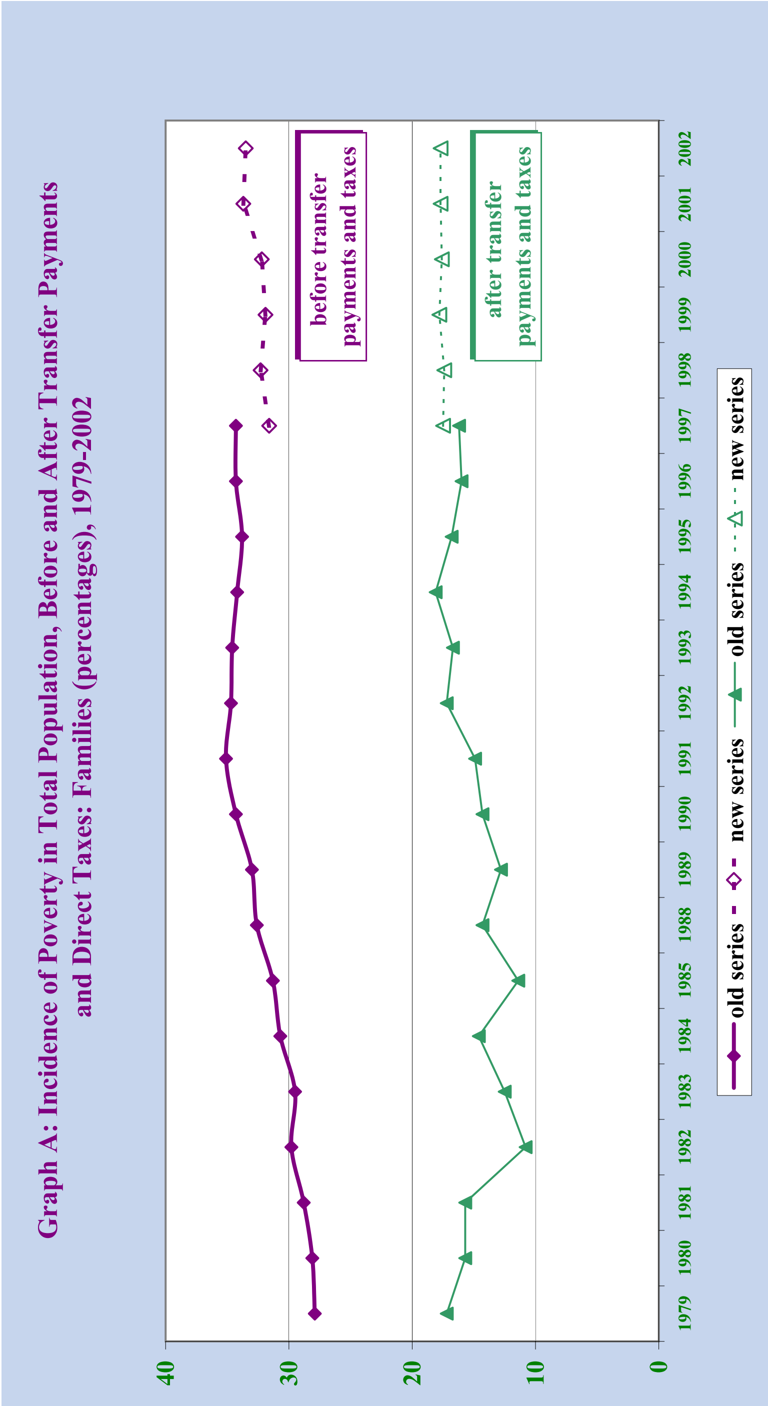
In 2002, the contribution of benefits and direct taxes – both separately and together – to reducing economic income gaps decreased (from 32.5% in 2001 to 32.0% in 2002). As a result, the Gini index for inequality in net income rose between 2002 and 2001 by 1.5% (from 0.3564 to 0.3616), reaching a total rise of 4.2% since 1998.

The expansion in inequality reflects a rise in the share of the upper decile, countering a decline in the share of the two lower deciles. Slight changes only occurred in the share of the other deciles between the two years. The share of the lowest fifth quintile in total net income amounted to only 6.3%, whereas the upper fifth quintile took 42.2% of the total net income.

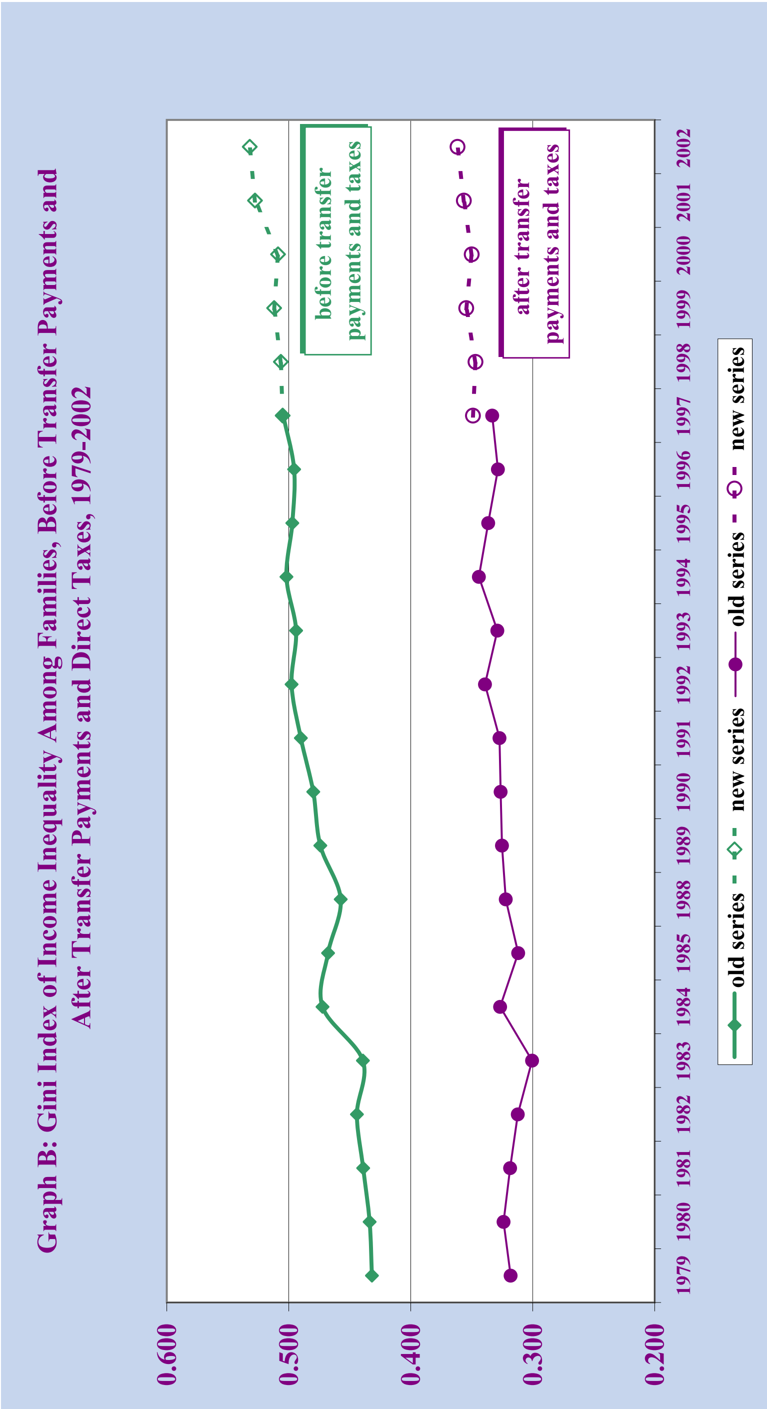
An appendix of tables and graphs appears at the end of this chapter.

Table 4: Gini Index of Inequality in Net Income Distribution, 2000-2002

	Before transfer payments and direct taxes	After transfer payments and taxes	Percentage of decrease stemming from transfer payments and taxes
Total population			
2002	0.5320	0.3616	32.0
2001	0.5277	0.3564	32.5
2000	0.5088	0.3500	31.5
1999	0.5120	0.3545	30.8
1998	0.5065	0.3469	31.5
Change in Gini Index (%)			
2002 compared to 2001	0.8	1.5	
2002 compared to 1998	5.0	4.2	
Households of employees			
2002	0.4452	0.3261	26.8
2001	0.4389	0.3215	26.7
2000	0.4390	0.3214	26.8
1999	0.4305	0.3166	26.5
1998	0.4319	0.3167	26.7
Change in Gini Index (%)			
2002 compared to 2001	1.4	1.4	
2002 compared to 1998	3.1	3.0	



Graph A: Incidence of Poverty in Total Population, Before and After Transfer Payments and Direct Taxes: Families (percentages), 1979-2002


Graph B: Gini Index of Income Inequality Among Families, Before Transfer Payments and After Transfer Payments and Direct Taxes, 1979-2002
0.600
0.500
0.400
0.300
0.200
1979 1980 1981 1982 1983 1984 1985 1988 1989 1990 1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002
before transfer payments and taxes
after transfer payments and taxes
old series
new series
old series
new series