



# **ANNUAL SURVEY 2006**

EDITED BY  
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## Forward

The present Survey, like its predecessors, covers the varied activities of the NII in the previous year – benefit payments and collection of insurance contributions, social policy and research.

The first chapter presents benefit payments in 2006 and describes developments in public welfare expenditure in Israel in an international perspective. Several social aspects of the budgetary policy – both public expenditure and taxes – are presented, based on a model constructed by the NII. The second chapter presents the picture of poverty and income gaps in Israel in 2005 and 2005/6. In addition to poverty findings according to the relative approach, the chapter presents updated findings on the scope of poverty according to the essential needs approach. Special chapters deal with developments in the income support system to the working-age population (Chapter 3), in collection of national and health insurance contributions (Chapter 4) and in the main insurance branches (Chapter 5). Many of the chapters include Boxes focusing on topics high in the social agenda in Israel. Summaries of the first chapter and of the chapter on trends in poverty and inequality appear in English.

The Survey includes three Appendices: an Appendix of Publications – summaries of research reports and surveys published by the Research and Planning Administration in 2006 – a bilingual Insurance Branch Table Appendix and a bilingual 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 Nira Amir and Ani Cohen-Frushman, who bore the burden of the typing, for work carried out with willingness, initiative and devotion.

Dr. Yigal Ben Shalom  
Director-General



## **Preface** **by the Director General**

The encouraging economic data in the fields of growth and employment in Israel continued in 2006, for the third straight year. In the field of social policy, however, the data show a trend of stability or even slight improvement, but not a real turning point. The adjustment of benefits in accordance with price levels (after a three-year freeze) and the NII position, accepted and implemented in 2005 and 2006, to increase the income of the elderly, particularly of those with low incomes, moderated the negative trends that had characterized the benefit system in the previous three years. The marked recovery of the labor market led to a moderate improvement in economic income gaps – before transfer payments and taxes. The poverty picture in 2005/6 shows a halt in the negative trend and even the buds of a positive trend, and the policy of increasing old-age pensions led to a decline in poverty in this group.

However, the data presented in this Survey still show high rates of poverty in Israel, with about a fifth of families and over a third of children defined as poor. The budgetary policy of 2002-2006, together with an analysis of developments in public welfare expenditure, show that most of the cuts were in NII benefits, but that public expenditure was eroded in real terms in social services (health and education) as well. Quantified estimates of the social implications of budgetary policy show that while the low deciles bore most of the burden of the recession and benefit cuts in 2001-2003, it was mainly the higher deciles that enjoyed the fruits of the economic growth that began in 2004 and continued until the year under review.

NII data contributed to the increase in public awareness necessary for a change in social policy in Israel. A state committee was set up to proposing ways of improving the social situation in Israel, and in 2006 the “Bachar Committee”, set up by the Minister of Finance to recommend policy measures of reducing poverty in Israel,

discussed the implementation of a negative income tax, among other measures. In addition, in April 2007 the National Economic Council of the Prime Minister's Office presented a socioeconomic program in a document entitled "The Socio-economic Agenda in Israel 2008-2010." This program, which was adopted by the government, suggests methods of achieving two main goals: the lowering of poverty rates while maintaining economic growth, and increasing the rate of participation in the labor force. The new component of this program was in its actual setting of measurable social goals. Most of the policy tools put forth in the program are those that have been recommended by the NII at various opportunities<sup>1</sup>; these include taking care of poverty pockets (ultra-Orthodox Jews and Arabs), implementing a negative income tax, vocational training, making the benefit system more efficient and enforcing labor legislation. However, the program almost completely ignores the weak population groups in whose case the solutions lie not only within the realm of the labor market. State interventions in the labor market enjoy a relatively broad consensus among decision-makers, while increasing benefits to needy population groups in order to reduce gaps is considered by many to be less desirable – despite the facts that the generosity of benefits in Israel is low in an international perspective, and that the solution to the distress of these population groups is not limited to the labor market alone.

The perception of the NII regarding the war on poverty and the reduction of income gaps in Israel is that the wide range of causes of poverty requires a similarly wide range of interventions: in the labor market, but also in the area of benefits and social services. Thus, in addition to its recommendations to introduce a negative income tax, to enforce labor laws and to focus interventions on employment and social mobility in those sectors that suffer from a lack of opportunities in the labor market (such as the Arab sector and the periphery), the NII also recommends a range of measures in the field of benefits.

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<sup>1</sup> See, for example, Annual Survey 2005, Boxes 1A and 1C in the Introduction.

After the difficult recession years that are now behind us, it would be appropriate to consider removing or lowering the ceiling of the growth in public expenditure (for example, a 2% growth instead of 1%) and to work towards adjusting benefits again to the average wage instead of to price changes. As an intermediate stage, it is recommended to adjust the benefits (such as old-age and survivors' pensions, disability pensions, income support benefits and alimony benefits) every year at a rate equivalent to that of price rises<sup>2</sup>, with the addition of half the rate of the real rise in wages.

The benefits paid to the elderly were increased in 2005 and in 2006, and it is proposed to continue this policy. At the same time, the universal allowance for children should be raised, since the deep cut in these allowances in recent years led to a soaring of poverty rates among children, putting Israel at the head of the list of countries rated according to their share of poor children.

The National Insurance Institute suggests adopting a policy of income support upon retirement that would include two tiers: the National Insurance pension and a compulsory occupational pension. The introduction of a negative income tax and the enforcement of labor laws, together with an increase in the income support benefit to those with low occupational potential, are measures that are necessary in order to reduce poverty and inequality in the working-age population.

Dr. Yigal Ben Shalom  
Director General

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<sup>2</sup> Under law, today the amounts of benefits are not reduced when prices decline.



## **Chapter 1**

# **Trends of Development in National Insurance**

**Miri Endweld**



## 1.1 Introduction

The positive economic developments over the past two years continued throughout 2006 and were manifested in the impressive overall market indicators in terms of GDP, growth and employment. However, these positive developments did not prompt a true turnaround in Israel's social policy. The findings pertaining to welfare in 2006 primarily reflect a halt to the decline typical of the last few years rather than an improvement. For the first time since 2001, there has been a rise in real terms in the benefits paid by the National Insurance Institute; however in terms of benefits as a percentage of the GDP, the consistent erosion that began in 2003 persisted. The results of the last survey on the dimensions of poverty and inequality are indicative of deceleration and stabilization; however, their levels from an international perspective and in comparison to Israel itself in previous periods have remained unchanged.

In 2006, the cash and in-kind National Insurance benefit payments increased by 3.5% in real terms, after having decreased by 12% in 2002-2004 and remained stable in 2005. In terms of average benefit payments **per capita**, this rate is lower – approximately 2%. There was a rise in benefit payments in various sectors, stemming from an increase in the number of recipients combined with pension rate adjustments: child allowances increased by 8.5% – after their cumulative decrease in real terms in the five years preceding 2006 reached about 45%; there was also a relatively high increase of 6.4% in maternity allowances; disability payments increased by 5.5% and the 3.4% increase in the old-age and survivors' pensions can primarily be explained by the policy of boosting old-age pensions in 2005 and 2006.

Conversely, benefits paid to the working-age population generally remained stable or declined: unemployment benefit payments declined by 3.6% and income support benefits by 6.5%. These decreases reflect the trend of the last few years: from 2002 to 2006, unemployment benefit payments declined by 48.7% in real terms while income support

benefits declined by 30.5%. The continued decline in unemployment benefit payments in 2006 can be credited to the recovery of the labor market; however, the cumulative decline that began in 2002 reflects the increasingly stringent eligibility criteria for unemployment benefits, which primarily affected the weaker segments of the labor market. The impact of tightening the eligibility criteria for unemployment benefits on benefit expenditure was more or less exhausted in 2004, and persisted over the next two years: only a fifth to a quarter of the jobless population was entitled to unemployment benefits, which is a low coverage level from an international perspective. The cumulative decrease in income support payments in 2003 also reflects the tightening of the eligibility criteria and the harsh cutback in benefits. In the last two years, however, the decrease in the number of income support recipients is linked to the implementation of the *Mehalev* welfare-to-work plan (known as the “Wisconsin Plan”); half of the decrease in the number of benefit recipients in 2005-2006 can be explained by the denial of entitlement to the benefit within the scope of this plan (as a result of finding a job or pulling out of the system without any corresponding job entry), and about another third of the decrease can be credited to pulling out of the system for other reasons.

The changes in the payment rates are the result of the changes in the number of benefit recipients as well as the modifications to the legislation made during the year in question. While there was a decline in the number of unemployment and income support benefit recipients in 2006 as compared to 2005 (of 4.8% and 6.9% respectively), there was an increase in the number of recipients of all other benefits. There were relatively high increases in the various disability benefits, which are partially attributable to the deferral of the age of entitlement to old-age pension, as well as in long-term care benefits and maternity allowances<sup>1</sup>. There were more moderate increases in old-age and survivors’ pensions and child allowances – of 1.1% and 1.3%, respectively.

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<sup>1</sup> A partial explanation for the rise in the number of recipients of long-term care benefits lies in the broadening of the definition of a “single person”.

Due to the economic growth, there was a marked erosion in benefit payments in terms of GDP that lasted throughout 2006. After benefit payments reached a record 8.9 GDP percentages in 2001-2, they dwindled to 7.2%, thereby resuming the level that prevailed in the 1980s. From 2001 to 2006, the rate of national insurance benefits decreased by 8.2% in real terms, the sharpest declines being in unemployment insurance (about 49%), child allowances (about 40%) and income support benefits (about 31%). These decreases were primarily offset by increases in the general disability pensions (about 26%) and the long-term care benefits (about 18%).

Tables 1 and 2 present the structure of social expenditure in Israel and the trends of change in this structure between 2000 and 2006, in accordance with the OECD<sup>2</sup> classification rules. Public social expenditure includes the expenditure of all public institutions on cash and in-kind benefits and on health (but not on education). Public social expenditure in terms of GDP percentage was 16.9% in 2000 and rose to about 18% in the three following years, until it resumed an identical rate in 2004. This rate further dwindled to 16.3% in 2005 and 16.0% in 2006. From 2003 to 2006, social expenditure lost about 2 GDP percentages.

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<sup>2</sup> OECD – Organization for Economic Co-operation and Development

**Table 1: Public social expenditure, 2000 - 2006 (percentages of GDP)\***

	2000	2001	2002	2003	2004	2005	2006
Total public social expenditure	16.9	18.37	18.62	18.04	16.88	16.28	15.99
Total cash benefits	9.96	11.07	10.94	10.65	9.8	9.31	9.11
Benefits to working-age population	5.28	5.87	5.77	5.31	4.7	4.4	4.29
NII	4.28	4.86	4.79	4.37	3.82	3.56	3.49
War and acts of hostility	0.49	0.55	0.56	0.57	0.55	0.52	0.51
Other**	0.51	0.46	0.42	0.37	0.32	0.31	0.29
Benefits to the elderly	4.69	5.2	5.17	5.35	5.1	4.91	4.82
NII	2.7	3.01	2.95	2.93	2.84	2.76	2.71
Pension to civil servants	1.56	1.71	1.76	1.93	1.85	1.79	1.79
Other***	0.43	0.47	0.47	0.49	0.41	0.37	0.32
Total in-kind benefits	6.94	7.3	7.67	7.39	7.08	6.96	6.89
Health and long-term care	5.31	5.6	5.88	5.73	5.43	5.37	5.35
Other****	1.62	1.7	1.8	1.66	1.65	1.59	1.54

\* Source: NII and CBS data, processed by the Research and Planning Administration according to OECD classification rules.

\*\* Includes benefits to demobilized soldiers, absorption basket and cash benefits as rental assistance.

\*\*\* Includes benefits to Nazi victims and cash benefits as rental assistance.

\*\*\*\* Includes in-kind benefits of NII, local authorities, national institutions, State non-profit organizations and Ministry of Labor and Social Affairs.

Table 2 presents the real change in the various components of the total social public expenditure from 2001 to 2006. The data show that the total expenditure remained virtually unchanged between these two years, however whereas the in-kind benefits (mainly consisting of health and long-term care services) increased by 8%, there was a decrease of 5.8% in the cash benefits as a result of a 16.3% drop in the benefits to the working-age population. When pension payments (which are in fact part of the job pension) to civil

servants are deducted, the cash benefit expenditure is even smaller in real terms. Conversely, cash benefits to the elderly have increased at a cumulative rate of 6%.

**Table 2: Public social expenditure, 2001, 2003 and 2006\***

	Expenditure - NIS billion, in current prices			Rate of real change: 2006 as compared to 2001
	2001	2003	2006	
Total public social expenditure	91.2	94.6	100.1	0.19
Total cash benefits	55.2	55.8	57.0	-5.8
Benefits to working-age population	29.3	27.8	26.9	-16.3
NII	24.2	22.9	21.8	-17.7
War and acts of hostility	2.7	3.0	3.2	-6.2
Other**	2.3	1.9	1.8	-28.0
Benefits to the elderly	25.9	28.0	30.2	6.2
NII	15.0	15.4	17.0	3.1
Pension to civil servants	8.5	10.1	11.2	19.4
Other***	2.4	2.6	2.0	-22.3
Total in-kind benefits	36.4	38.7	43.1	8.0
Health and long-term care	27.9	30.0	33.5	9.4
Other****	8.5	8.7	9.6	3.6

\* Source: NII and CBS data, processed by the Research and Planning Administration according to OECD classification rules.

\*\* Includes benefits to demobilized soldiers, absorption basket and cash benefits as rental assistance.

\*\*\* Includes benefits to Nazi victims and cash benefits as rental assistance.

\*\*\*\* Includes in-kind benefits of NII, local authorities, national institutions, State non-profit organizations and Ministry of Labor and Social Affairs.

The analysis of an international comparison between developments in public social expenditure is based on 2003 data. From an international perspective, Israel of 2003 (when the benefit system was at its peak) was ranked 21<sup>st</sup> on the scale classifying the OECD countries by public social expenditure relative to GDP, with a negative gap of about 3 percentage points versus the OECD country average and of about 6 GDP percentage points versus EU15 countries<sup>3</sup>. In 2006, Israel dropped to the 27<sup>th</sup> place with 16.2 GDP percentages versus an average of 20.9 GDP percentages for the OECD countries and 23.9 GDP percentages in EU15 countries.

The chapter will further provide a review of several of the social aspects of the government's policy as well as a breakdown of the main changes in benefit payments and the National Insurance's financing sources. The chapter also features three boxes: Box A expands the range of information regarding the international comparison between the OECD countries and Israel in the realm of social expenditure; Box B briefly reviews a comparison between cash and in-cash benefits with a focus on food-related aid; and Box C summarizes the legislative changes in 2007 pertaining to the various benefits.

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<sup>3</sup> The first 15 countries to join the European Union.

**Box A<sup>1</sup>****Development of public support in Israel and OECD countries, 1998-2003**

Within the scope of the publication of the international comparison data pertaining to public support, which includes both cash and in-kind support (through services), this box will present the findings adjusted to 2003 (last year the data adjusted to 2001 were presented).

This year the international data are especially significant in light of the intensive negotiations regarding Israel's joining the OECD. There is a great deal of importance attached to Israel's joining the organization, *inter alia*, because of the necessity and historic need to create a uniform platform between Israel and the OECD countries for the entire range of OECD disciplines.

This box will present the development of public support in Israel and OECD countries according to the standard OECD benefit categories<sup>2</sup> from 1998 to 2003. For Israel, we will provide the most up-to-date data up to 2006. We will start by reviewing a few indices we published in the last few years regarding social expenditure. In 2003, Israel was ranked 21<sup>st</sup> for total public welfare expenditure, similarly to 2001. However in 2006, Israel sunk to the bottom of the ladder – to 28<sup>th</sup> place – thereby distancing itself from the OECD average and even more from the European Union average (assuming that there were no major changes in the other countries). In-kind benefits, which amount to 41% of the overall public expenditure, dropped drastically from 10<sup>th</sup> place in 2001 (7.7%) to 21<sup>st</sup> place in 2003 (7.4%) and 23<sup>rd</sup> place in 2006 (6.9%). The bulk of the decline stems from the overall increase in OECD member countries rather than from a decrease in the consumer price index itself. Proof of such is in the rise in the OECD average from 7.7% in 2001 to 8.3% in 2003, and the rise in the EU average from 8.2% in 2001 to 8.8% in 2003. In 2003, Israel ranked 20<sup>th</sup> on the welfare expenditure scale – the same place it occupied in 2001 – however, in 2006, Israel dropped to 24<sup>th</sup> place.

We will assess two additional characteristics pertaining to financial public support – one being the development of public support over time in two populations: the working-age

<sup>1</sup> Prepared by Michal Ophir

<sup>2</sup> Social Expenditure Database (SOCX), (2006) OECD [www.oecd.org/els/social/expenditure](http://www.oecd.org/els/social/expenditure). The data published in the OECD are adjusted to 2003 and amended retroactively.

population and the elderly, and the other being the relative generosity of individual social expenditure, namely financial support proportionate to the relevant population. It should be noted that financial support for the elderly also includes survivors' pensions –both pensions for civil servants and compensation for the victims of Nazism. Diagrams A and B below refer to the working-age population while Diagrams C and D refer to the elderly. Diagram A shows the development of financial support for the working-age population from 1998 to 2003 for Israel and a few other countries. According to the diagram, financial support for the working-age population in Israel up to 2001 was clearly on the rise and its situation in relation to the other countries was respectable. In fact, only Denmark ranks higher than Israel and financial support there for the working-age population is higher than 8% of the GDP. In 2001, Israel reached a record 5.9% following an increase in the benefits for this population in 1999-2001 – namely even higher than the OECD country average, which was 4.3% that year. As of 2001, the economic plans that cut back on national insurance (social security) benefits left their mark until Israel dropped to 4.3% in 2006 – much lower than several countries and the OECD average. During the entire period, the United States remains at the bottom of the diagram and financial support there for the working-age population as a percentage of the GDP was only about 2%.

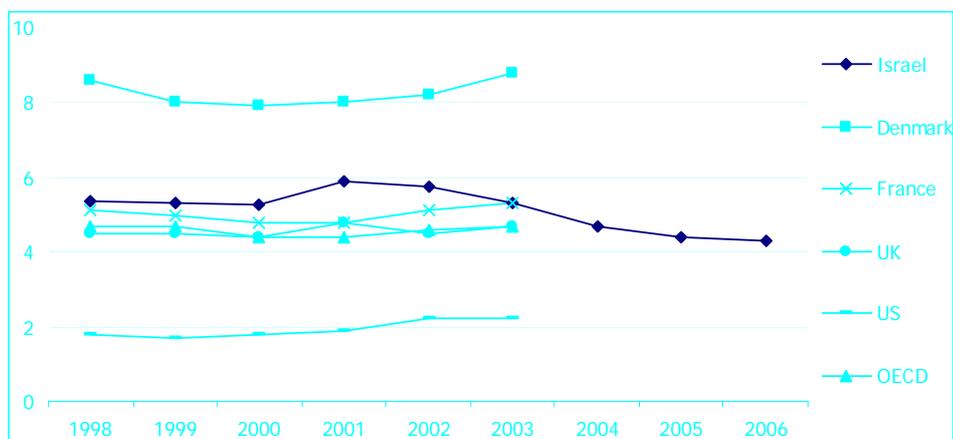
Diagram 2 presents an overview of the financial support per person of working-age as a percentage of the GDP per capita in OECD countries and in Israel in 2003. The diagram shows that in 2003, Israel ranked 10<sup>th</sup>, with 8.6% financial support per person as a percentage of the GDP per capita, close to the EU average, but much higher than the OECD average, which stood at 7.3% that year. In 2006, it dropped to 20<sup>th</sup> place, with 7% – and in this instance as well, the huge impact of the reduction of benefits for the population as a whole, and for the working-age population in particular, is clearly evident. Diagrams C and D provide an international comparison pertaining to the elderly population. Diagram C shows that during the entire period, Israel is positioned below European countries and the United States, and far below the OECD average, which in 1998-2003 was about 7% of the GDP. In 2003, financial support for the elderly as a percentage of the GDP in Israel reached a record high. Up to that point, financial support for the elderly was on the rise and in 2003, amounted to 5.7%. However, from

that year on, the support declined by about 0.5% of the GDP, reaching 4.8% of the GDP in 2006, which was actually its level in 1998. Payments for old-age and survivors' pensions rose slightly in 2005-2006, due to the cumulative increase of about 13% in the basic old-age pension, including the increase in income supplements. However, due to the greater increase in the GDP, the ratio of payments relative to the GDP is still gradually diminishing and the impact of the rise in the old-age pension may only be felt in the next few years. France, whose support reached about 12%, stands out among the countries generous to the elderly. The financial support component for this population out of the overall public welfare expenditure in France amounted to approximately 42% in 2003, as compared to the average financial support component in Israel and the OECD countries, which amounted to about 30% in 2003.

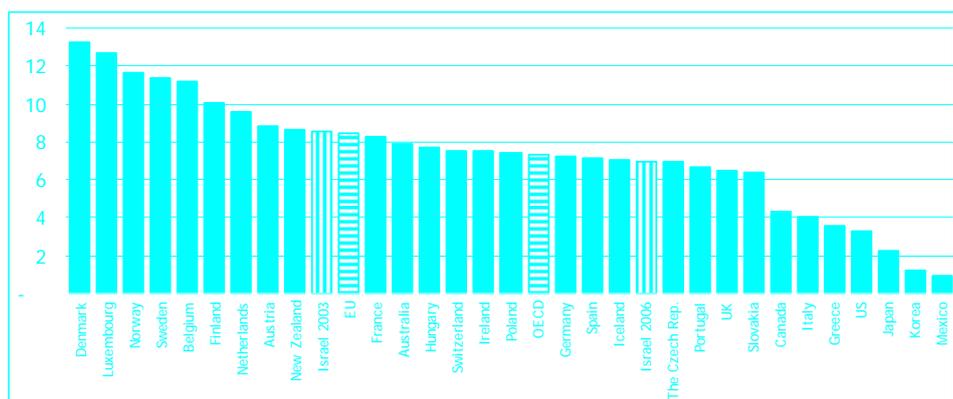
The international comparison of the financial support for the elderly as a percentage of the GDP per capita in 2003 points to a different picture. Diagram D presents Israel in a more positive and generous light as compared to the other countries. In 2003, Israel's position was reasonable, with about 54% GDP; however in 2006, it dropped to 38.5%, and came close to the OECD average (11<sup>th</sup> and 16<sup>th</sup> place, respectively). Israel's relatively high position on this scale stems from the unique composition of the financial support for the elderly. This expenditure also includes pension payments for civil servants. When deducting these payments, Israel drops to the bottom of the scale. In 2003, financial support there minus pension payments amounted to 34.5% and in 2006, to 30.5% only (26<sup>th</sup> and 28<sup>th</sup> place, respectively). This dismal picture reflects the pension system in Israel, which provides rather minimal basic support as compared to the other countries.

The picture portraying development over time is also quite similar in the two groups that were not addressed in this box – social services expenditure and health expenditure. In these two groups, Israel is positioned below most of the compared countries; until the beginning of the 2000s there was a rising trend, which was followed by a decrease in costs, as opposed to a moderate, but continuous increase in the other countries, which is also evident in the financial support for the working-age population and the support for the elderly.

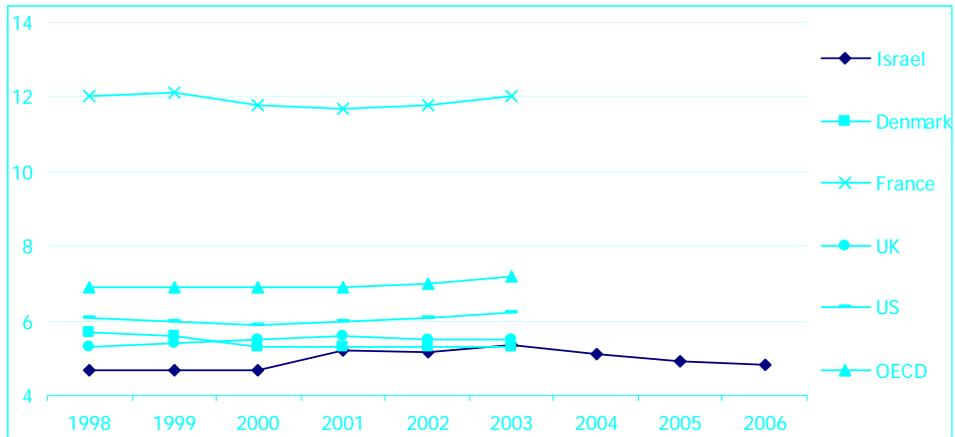
**Diagram A: Financial support for the working-age population as a percentage of the GDP in selected countries and in Israel, 1998-2003**



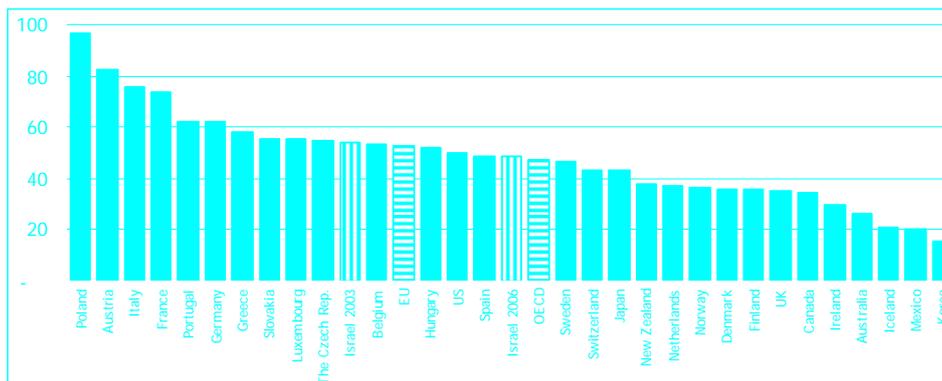
**Diagram B: Financial support per person of working age as a percentage of the GDP per capita in OECD countries and in Israel, 2003**



**Diagram C: Financial support for the elderly as a percentage of the GDP in selected countries and in Israel, 1998-2003**



**Diagram D: Financial support for the elderly as a percentage of the GDP per capita in OECD countries and in Israel, 2003**



## 1.2 The social aspects of the government's policy

This portion of the chapter will feature findings regarding some of the social aspects of the government's policy from 2001 to 2006 related to the dimensions of poverty and the economic gaps, as well as to the changes in government-funded health and education expenditure.

The economic recovery began in the middle of 2003 and the growth in its wake led to an improvement in the economic income which the working-age population in the low deciles also benefited from. Nonetheless, the findings show that whereas the burden of the recession and the cutback in benefits from 2001 to 2003 was primarily borne by the low deciles, it is mostly the upper deciles that benefited from the fruits of the growth that began in 2004. Diagrams 1A to 3A present the development in the **real** disposable income per standard person, which serves as an index of standard of living, according to deciles, from 2001 to 2005/6<sup>4</sup>. The first diagram depicts the years of severe economic recession from 2001 to 2003 and the harsh cutbacks in benefits, especially child allowances and income support benefits; the second diagram presents the years of growth from 2004 to 2005/6, whereas the third diagram shows the cumulative change in the period from 2001 to 2005/6. Diagram 1A shows the erosion of the standard of living among the population as a whole between 2001 and 2003 wherein the disposable income per standard person lost 6% of its real value. Whereas in the upper deciles there was an erosion similar to that of the average erosion in the population as a whole, the income of the first decile dropped by about 17% and that of the second decile, by about 10%. Diagram 2A shows the income recovery in the overall population between 2004 and 2005/6 and its increase of approximately 9%. This positive change did not manifest equally among the deciles: in the upper deciles, the income rose at a higher rate than that

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<sup>4</sup> The data for 2005/6 relate to the period including the second half of 2005 and the first half of 2006. For further details, see Chapter 2 in this Survey – “Trends of development in poverty and income inequality (summary)”.

of the general population (about 12%), whereas among the middle deciles, not only did they not benefit from an increase in disposable income, but the latter continued to decline by about 4% in the first decile and by about one percent in the second decile. A summary of the effect of the economic recession, the income tax reform, the cutbacks in benefits and the subsequent growth in the following years is featured in the third diagram, which shows that while the three upper deciles benefited from an increase in their disposable income twice or more that of the overall population, the lower decile's income dropped by about 21% and that of the second decile by about half this rate. During this period, the status of the four lower deciles deteriorated in direct relation to their position, the fifth decile maintained its real standard of living and only the sixth to tenth deciles benefited from a growing increase in their real income.

Data on the status of Israel from an international perspective were published in last year's Annual Survey and the files of the countries participating in the Luxembourg Income Study (LIS) have not been adjusted since then. According to the findings for the beginning of the 2000s, Israel ranked among the "leading" countries from the point of view of dimensions of poverty and inequality and at the bottom of the list of countries contributing (cash) transfer payments to reduce the dimensions of poverty. Updated figures on Israel's place in relation to other countries participating in the Luxembourg project will be calculated once the new databases are received, however – based on the findings accumulated to date – it is hard to imagine that there has been any dramatic change in Israel's status from this point of view.

An analysis of the impact of the government's policy on family welfare generally focuses on cash transfers and direct taxation. However, family welfare is also dependent on services granted by the government free of charge or at reduced cost within the scope of the social budget. These primarily health and education services are defined as "in-kind transfers" from the government to the families.

**Diagrams A1 to A3: The real change in the disposable income per standard person according to deciles, 2001-2005/6**

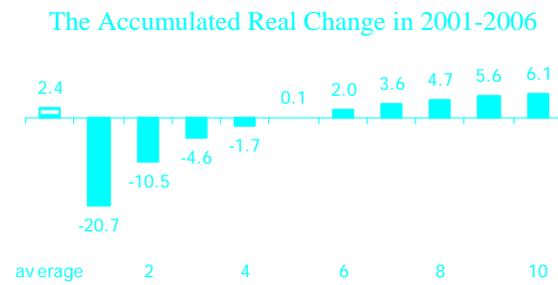
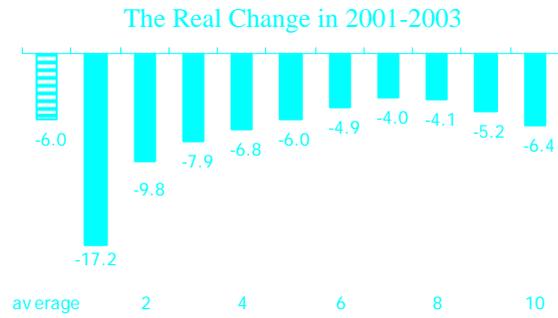


Table 3 presents current government-funded national health and education expenditure when discounted by the civilian public consumption index, from 2001 to 2006. The Table shows that during this period, education expenditure at constant prices rose by less than one percent while health expenditure<sup>5</sup> rose by 2%. During the transition from 2005 to 2006, government expenditure for social services decreased despite the market's impressive growth data during that time.

The table also shows the **amended per capita** expenditure estimates at constant prices: the **amended per capita** health expenditure according to the capitation scale<sup>6</sup>, as well as the government-funded national expenditure **per pupil**. Whereas the total education expenditure has remained virtually unchanged in real terms, expenditure per pupil – which takes into account the increase in the number of students in the education system – decreased by an average of 5.6% in real terms. Similar results are obtained when examining the amended per capita government health expenditure, which declined in real terms by 7.7% between 2001 and 2006, whereby from the past year to the year being surveyed, the amended health and education expenditure decreased by 2 to 3 percent.

These calculations are based on the budget data published by the Ministry of Finance, adjusted to March 2007. Since the calculation model<sup>7</sup> is updated regularly, the expenses

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<sup>5</sup> The definition of government health expenditure in this section differs from that presented previously in the discussion of public social expenditure. This section refers to expenditure according to funding sector whereas the previous one refers to the implementing sector according to the OECD definitions.

<sup>6</sup> The capitation scale (or capitation formula) takes into account the size and composition of the population by age, thereby reflecting the population's health needs. Health insurance contributions are allocated between the health funds according to this scale. For further details, see Chapter 4 of this review.

<sup>7</sup> For a breakdown of the calculation methods used to obtain the estimates, see: Sabag-Endweld, Miri: "Government Financing of Education and Health Services and Income Distribution, 2001-2005" publication no. 88 in the "Research and Special Surveys" series, National Insurance Institute, 2005 (in Hebrew).

for 2006 and even earlier years will vary according to the new data received from the CBS on government-funded expenditure and the Ministry of Finance budget data.

**Table 3: The real change in government-funded health and education services:**

**Total expenditure and amended per capita expenditure, 2001-2006\***

	2001	2002	2003	2004	2005	2006	Cumulative change 2001-2006
<b>Total expenditure</b>							
<u>Education**</u>							
At current prices	31,614	31,664	33,190	32,479	34,404	35,546	12.4
<b>Real change</b> percentage		-2.9	4.7	-5.1	5.3	-0.7	0.8
<u>Health***</u>							
At current prices	26,904	27,886	28,522	29,076	29,689	30,607	13.8
<b>Real change</b> percentage		0.4	2.2	-1.1	1.5	-1.0	2.0
<b>Amended per capita expenditure - real change</b>							
<b>(%)</b>							
Education: expenditure per pupil		-4.1	3.3	-6.3	3.9	-2.1	-5.6
Health: per weighted capita expenditure		-1.6	0.2	-3.1	-0.5	-2.9	-7.7

\* Minus the civilian public consumption index.

\*\* The latest data published by the CBS refer to 2001, and expenditure in 2002-2006 was factored according to the change in the Ministry of Education and higher education budgets.

\*\*\* The 2004 expenditure data published by the CBS were factored for 2005 and 2006 according to the changes in the Ministry of Finance budget, health insurance premium proceeds and health expenditure within the scope of National Insurance.

The in-kind transfer embodied in government-funded health and education services constitutes almost one quarter of the adjusted income (disposable cash income plus in-kind transfer). This rate stands at approximately 60% in the bottom decile, but gradually decreases to less than 10% in the top decile. Since the sum of the in-kind transfer to families in the lower deciles is higher than that to families in the upper deciles, and the size of the in-kind transfer constitutes a greater share of their cash income, the extent to which the real decrease in government expenditure for social services affected them is greater than the extent to which the upper deciles were affected.

In April 2007, the National Economic Council in the Prime Minister's Office submitted a socioeconomic plan in a document entitled "Socioeconomic Agenda for Israel, 2008-2010". The plan adopted by the government proposes *modus operandi* to achieve two main goals: to reduce the incidence of poverty while upholding growth objectives and to increase the number of participants in the workforce. Committees made up of government and relevant public institution representatives have been set up in order to follow up on and integrate the plan. The plan's innovative component consists of setting measurable social objectives. For the most part, the recommended policy tools coincide with those recommended by the National Insurance Institute on several occasions<sup>8</sup>, namely handling poor sectors of the population (ultra-Orthodox Jews and Arabs), instituting a negative income tax plan, providing vocational training, optimizing the allowance system, enforcing labor laws, etc. Nonetheless, according to the NII, the plan almost overlooks the weaker population groups for whom the solutions to their hardships do not (or only partially) lie in the labor market, and for whom the goal of reducing poverty must go hand-in-hand with a rehabilitation of the existing benefit system, including a return to adjusting benefits to the average wage, increasing child allowances, reviewing the sharp cutbacks in income support benefits for the working-age population and further increasing income supplements for the elderly, as well as expanding employment insurance coverage.

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<sup>8</sup> See for example the 2005 Annual Survey, in Boxes 1A-1C in the Introduction.

**Box B****Ensuring nutritional security – cash and in-kind benefits**

At the beginning of 2007, the “Latet” Organization filed a petition to the High Court of Justice, demanding that the court rule that it is the State’s obligation to ensure the minimal nutritional security of its citizens. The petition further demanded that the State set up, finance and run the logistics required to distribute food to the needy. A committee set up at the Ministry of Social Affairs is currently assessing the various aspects of this issue.

Inarguably, the right to minimal nutritional security is a basic right and it is the State that is responsible for finding a solution to the shortage of food (as well as other basic products) and not a variety of non-profit organizations, which supply goods in a haphazard and uncontrolled manner. Nonetheless, the NII and the petitioners are divided about how to eradicate the food shortage problem, which has seemingly greatly spread in the last few years.

The advantages usually attributed to offering in-kind benefits cash benefits have to do with tailoring the specific service to those who require it, while supervising the quality of the in-kind products or services provided and preventing the misuse of resources granted to the needy.

However, food, clothing and hair care products are not usually supplied through an “in-kind” benefit, but rather through a cash benefit. The main reason for this is that these are personal items for which it is essential to give the recipients autonomy and freedom of choice. However, there are advantages to supplying other services that are more public in nature – such as education and health – through in-kind benefits. Moreover, distributing food through an in-kind rather than cash benefit also has a paternalistic, and even contemptuous aspect, which carries a hidden message whereby the population

benefiting from it does not have enough judgment or capacity to play its cards wisely and is likely to misuse the resources it is granted.

Economic theory also usually supports cash benefits over in-kind benefits. The arguments for this lie in the loss of choice, flexibility and planning ability of the individual who requires the products, the need to set up a complex logistic system for tracking purposes, setting criteria, setting up an enforcement system and the distribution itself – the price of which is likely to be very high, assuming that the products are supplied more efficiently on the free market.

This perception is compatible with that of most welfare states. The United States, which has the highest poverty and inequality rates among the western countries, is one of the only countries that opted for food stamps over financial support.

It is worthy of note that research recently conducted in the US, of all places, proved the inefficiency of distributing food stamps to the needy population: the population whose food stamps were converted into money made more efficient use of food products and even freed available resources for other basic needs.

Lastly, the phenomenon described in the petition, or at least its expanding scope, is a consequence of the economic policy and the deep cutbacks in the various benefits, and especially the income support benefits and the child allowances as of 2002. In the last few years, the National Insurance Institute repeatedly warned of the harsh social implications of this policy and the expanding dimensions of poverty in Israeli society; as such the NII has proposed operative measures, namely increasing benefits, in order to circumvent these implications.

### 1.3 Benefit payments

In 2006, total NII cash and in-kind benefit payments – both contributory and non-contributory – amounted to approximately NIS 45.8 billion, as compared to NIS 43.3 billion in 2005. These sums also include additional payments made by the NII primarily to government ministries for expenses relating to the development of community services. They further include the various administrative and operative expenses of the national insurance system (in the amount of about NIS 1.1 billion). For the first time in four years, there has been a 3.5% real increase in the total benefit payments. The cumulative decline in the scope of NII payments between 2002 and 2005 amounted to 11.3%. The increase would have been more temperate had it not been for the rise in the number of benefit recipients, particularly in the central NII branches. In terms of GDP percentages, on the other hand, the benefits paid by the NII remained more or less at their 2005 levels (Table 4).

The data in Table 5 depict the main benefit payment trends by branch. The increase in the payment benefits in 2006 is the result of the rise in the scope of payments for most pension types. The increase in the payments to the elderly and the disabled persisted (3.4% for the elderly and 5.5% for the disabled), and there was an increase in real terms in three of the branches paying wage-replacing benefits: Maternity, Work Injury and Reserve Service; payments in the latter branch rose by a massive 18.1% as a result of the Second Lebanon War. The increase in the Old-Age and Survivors branch reflects a policy that benefited the elderly population in the last two years: the pension was adjusted to the changes in prices at the rate of 1.8% in January 2006 (following a 0.9% adjustment in January 2005) and the various old-age and survivors pensions were increased: in mid 2006, the 1.5% reduction in old-age pensions was rescinded, the basic pension increased by 1.3% and the pension for income support recipients was raised by 4%. In the General Disability branch, the increase in the scope of payments is primarily attributable to the

4.3% rise in the number of eligible recipients. In relation to the average increase in the five years preceding 2006 (about 4.8%), this increase was more moderate.

**Table 4: Benefit payments and collection from the public (without administrative expenses) as a percentage of the Gross Domestic Product, 1980-2006**

Year	Benefit Payments		Total Collection	
	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
1995	7.37	5.77	7.67	4.30
2000	7.89	6.28	6.19	4.21
2001	8.94	7.03	6.58	4.46
2002	8.94	6.94	6.56	4.46
2003	8.37	6.62	6.42	4.35
2004	7.61	6.09	6.25	4.19
2005	7.27	5.83	6.21	4.17
2006	7.15	5.75	6.04	4.03

\* Including collection for the health funds.

\*\* Including "Treasury indemnification" due to reduced national insurance contributions for employers.

In 2006 – for the first time since 2002 – child allowances also increased by 8.5%. The reason for this increase is that at the beginning of 2006, the temporary provision pertaining to the cutback of NIS 24 per month in the allowances paid for the first three children and all "new" children, and of NIS 5 for the fourth child onward, expired. At the same time, the cutbacks in the allowances for the fourth child and onward continued, as

part of the policy regarding a uniform child allowance for all children. Between 2002 and 2005, the cumulative decline in child allowance payments amounted to 44.6%.

This is the fourth consecutive year that the trend of declining payments to the working-age population has continued: unemployment benefits continued to decrease by 3.6% in 2006 (and cumulatively by 48.7% since 2002) while income support payments further declined by 6.5% (and cumulatively by 30.5% since 2002).

In 2006, payments of contributory benefits pursuant to the National Insurance Law increased by a total of 3.9% in real terms, whereas payments of non-contributory benefits under other state laws or by virtue of agreements with – and completely financed by – the Treasury (such as income support, mobility, alimony, old-age and survivors pensions for new immigrants and reserve service benefits) increased at a lower rate of 2.1%. The sum of non-contributory payments, including administrative expenses, amounted to about NIS 9 billion in 2006, namely 19.6% of the total benefit payments.

Table 5 also presents the distribution of total benefit payments by branch. Following an ongoing decline, the Children's branch increased its share of the total payments (about half a percentage point between 2005 and 2006), but still remained the third largest branch after the Old-Age and Survivors and General Disability branches. Up to 2001, the Children's branch was the second largest and between 1995 and 2006, it reduced its share by nearly half. The share of the other branches – Work Injury, Maternity and Reserves – remained virtually unchanged. In 2006, 56% of the total benefit payments were concentrated in the two largest branches – Old-Age and Survivors and General Disability.

Table 5: National Insurance Benefit Payments (including administrative costs), 1995-2006

Year	Total Payments*	Old-Age & Survivors**	General Disability	Work Injury, Hostile and Border Actions	Maternity	Children	Unemployment	Military Reserve Service*	Income Support***	Long-Term Care & Other
NIS million (current prices)										
1995	21,188	7,675	2,254	1,487	1,206	4,287	1,280	1,053	1,149	798
2000	39,706	13,670	5,128	2,569	2,423	7,000	3,023	1,039	2,957	1,897
2001	45,441	15,408	6,076	2,879	2,662	7,643	3,579	1,350	3,579	2,262
2002	47,247	15,671	7,040	3,124	2,796	6,784	3,598	1,771	3,795	2,668
2004	42,759	16,032	7,355	3,145	2,727	4,887	2,166	708	3,003	2,735
2005	43,305	16,457	7,792	3,192	2,857	4,548	2,044	713	2,859	2,842
2006	45,760	17,376	8,392	3,306	3,103	5,038	2,013	860	2,730	2,941
real annual growth (percentages)										
1995	10.1	8.6	16.1	14.6	20.8	4.5	16.2	2.9	13.7	13.5
2000	8.1	8.4	14.8	11.4	10.8	1.5	-0.9	-7.4	18.1	18.2
2001	13.2	11.5	17.2	10.8	8.7	8.0	17.1	28.6	19.7	18.0
2002	-1.6	-3.8	9.6	2.7	-0.7	-16.0	-4.9	24.1	0.3	11.6
2004	-4.2	2.2	0.8	-0.3	0.2	-20.3	-12.3	-38.1	-9.5	1.2
2005	-0.1	1.3	4.6	0.2	3.4	-8.1	-6.9	0.6	-6.0	2.5
2006	3.5	3.4	5.5	1.4	6.4	8.5	-3.6	18.1	-6.5	1.4
distribution by branch (percentages)										
1995	100.0	36.2	10.6	7.0	5.7	20.2	6.0	5.0	5.4	3.8
2000	100.0	34.4	12.9	6.5	6.1	17.6	7.6	2.6	7.4	4.8
2001	100.0	33.9	13.4	6.3	5.9	16.8	7.9	3.0	7.9	5.0
2002	100.0	33.2	14.9	6.6	5.9	14.4	7.6	3.8	8.0	5.6
2004	100.0	37.5	17.2	7.4	6.4	11.4	5.1	1.7	7.1	6.4
2005	100.0	38.0	18.0	7.4	6.6	10.5	4.7	1.6	6.6	6.6
2006	100.0	38.0	18.3	7.2	6.8	11.0	4.4	1.9	6.0	6.4

\* Payments for 1995 do not include the amounts transferred to the Ministry of Defence as reimbursement of the debt for savings in reserve service duty days.

\*\* Including payments for income support.

\*\*\* For the working-age population.

## 1.4 Benefit levels

The Economy Recovery Law (June 2003) determined that all benefits paid by the NII, with the exception of the old-age and survivors' pensions<sup>9</sup>, would not be adjusted until the end of 2005, and that from January 2006 onward, pension recipients would be compensated at the rate of price rises only rather than based on changes in the average wage, as customary thus far. Accordingly, all benefits, except for old-age pensions, were adjusted in January 2006 (for the first time since January 2002), by 2.7% according to the rate of price rises. Old-age pensions were adjusted by 0.9% in January 2005 and by another 1.8% in 2006. Had the pensions been adjusted in January 2006 according to the average wage according to the Law, they would have increased by about 6%<sup>10</sup> (old-age and survivors' pensions, income support and alimony) and by 4.7% (the pensions paid in the General Disability, Long-Term Care, Work Injury and Maternity branches).

In the wake of the method of adjusting the benefits to the price index rather than to the average wage, the clauses that previously defined the calculation of the pension sums and their adjustment method according to the average wage were changed, and as of January 2006, the calculation was made according to the "basic amount"<sup>11</sup>. This amount will be adjusted in January every year, according to the rise in the consumer price index, between the known index prior to the date of adjustment and the one known in January in the year preceding the adjustment.

The 4% decrease in the paid benefits, which began in July 2003 and was planned until December 2006 (and extended until 2007) continued to apply to most benefits. Like the other benefits, the old-age and survivors' pensions were adjusted according to the rate of price rises in January, in addition to a similar adjustment in January 2005. Moreover, in July 2006, the **basic** old-age and survivors' pensions were increased by 1.3%. After the current 4% decrease was reduced to 2.5% in 2005, in July 2006 it was completely

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<sup>9</sup> Including dependents' benefits in the Work Injury branch.

<sup>10</sup> The reference is to the average wage pursuant to the NII Law, which was NIS 7,383 per month in January 2006.

<sup>11</sup> The original "basic amount" is the average wage that served as a basis for calculating the various benefits prior to the freeze on benefits pursuant to the Economy Arrangements Law in 2002-2003.

rescinded; thus the pension increased by another 1.5%. Old-age and survivors' pensions paid to those also entitled to income supplements were increased by 4% (including a rise in the basic pensions after these too were increased in 2005). The cumulative increase in the pensions in 2005-2006 amounted to about NIS 247 per person and about NIS 330 per couple. It is worthy of note that the government policy regarding aid to the elderly as reflected in the old-age and survivors' pensions was exceptionally generous in the last two years as compared to its policy toward other pensions paid by the NII. This policy bore fruit and was reflected in a decline in the dimensions of poverty in households headed by an elderly person (see Chapter 2 "Trends of development in poverty and income inequality [summary]").

The data in Table 7 show that in 2006, the minimum guaranteed income for the working-age population increased at rates varying between one percent and 3.5%, according to the different family compositions. Nonetheless, due to the rise in the average wage in the economy, the benefit remained more or less at its real level in 2005, relative to the average wage. This stabilization follows a severe erosion of the guaranteed income for the working-age population between 2002 and 2005: a simple calculation using the data in Table 7 shows that the minimum guaranteed income for a single parent with two children, for example, has decreased in real terms by 23% between 2002 and 2006.

The basic disability pension and the benefits derived from it (the attendance allowance and benefit for disabled child) rose in real terms by about half a percent in 2006. However, relative to the average wage per employee post, they were eroded: The disability pension for a single disabled person, for example, decreased from 32.4% of the average wage in 2005 to 32.0% of the average wage in 2006, while the average benefit for disabled child decreased from 25.0% of the average wage in 2005 to about 24.6% of the average wage in 2006.

The average long-term care benefit provided to the elderly (which is translated into care hours) rose in real terms by 4.8% in 2006, thereby resuming its real level of 2002. This rise stems from an increase in the number of persons entitled to this benefit: like last year, the increase in the number of persons entitled to the high level of the benefit was substantial as compared to the other benefit recipients.

**Table 6: The old-age and survivors' pension and the minimum income guaranteed to pension recipients (constant prices and percentage of the average wage\*) – monthly average, 1975-2006**

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	
	2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage
1975	636	14.9	1,059	24.8	1,093	25.5	2,057	48.1
1980	701	13.5	1,359	26.3	1,219	23.8	2,493	48.2
1985	790	15.2	1,533	29.5	1,582	30.5	3,163	61.2
1990	995	15.9	1,928	30.7	1,564	25.0	3,170	50.5
1995	1,009	15.5	1,954	30.1	1,688	26.0	3,500	53.9
2000	1,126	14.9	2,181	28.8	1,882	24.9	4,140	54.7
2001	1,221	15.7	2,366	30.5	2,042	26.3	4,475	57.7
2002	1,134	15.6	2,243	30.8	1,937	26.2	4,117	56.4
2003	1,102	15.6	2,224	31.4	1,919	27.1	4,152	58.7
2004	1,106	15.2	2,233	30.7	1,927	26.5	4,122	56.7
2005	1,121	15.4	2,224	30.5	2,038	27.6	4,261	57.8
2006	1,143	15.3	2,232	29.8	2,135	28.5	4,468	59.6

\* As measured by the CBS.

Table 7: Minimum Guaranteed Income to Working-age Population (at set prices and as percentages of average wage\*), monthly averages, 1985-2006

Year	Single				Single parent with 2 children* (incl. child allowances)		Couple with 2 children (including child allowances)			
	Regular rate		Increased rate		2006 prices (NIS)	% of average wage	Regular rate		Increased rate	
	2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage			2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage
1985	1,265	24.5	1,578	30.5	3,162	61.2	2,848	55.1	3,320	64.3
1990	1,252	20.0	1,177	24.9	3,170	50.5	2,885	46.0	3,355	53.5
1995	1,264	19.4	1,578	24.3	3,494	53.9	3,024	46.6	3,497	53.8
2000	1,407	18.6	1,758	23.2	3,873	51.2	3,334	44.0	3,860	51.0
2001	1,526	19.7	1,908	24.6	4,195	54.1	3,581	46.2	4,152	53.6
2002	1,419	19.6	1,773	24.5	3,867	53.4	3,295	45.5	3,866	53.4
2003***	1,377	19.5	1,620	22.9	3,301	42.5	2,851	40.3	3,286	46.6
2003****	1,721	24.4	1,721	24.4	3,745	53.0	3,645	52.4	3,708	52.4
2004***	1,382	19.0	1,556	21.4	2,949	40.5	2,569	35.3	2,949	40.5
2004****	1,729	23.8	1,729	23.8	3,713	51.0	3,675	50.5	3,634	50.5
2005***	1,365	18.5	1,536	20.8	2,907	39.4	2,532	34.3	2,907	39.4
2005****	1,706	23.1	1,706	23.1	3,661	49.6	3,624	49.1	3,624	49.1
2006***	1,373	18.3	1,545	20.6	2,973	39.7	2,596	34.7	2,973	39.7
2006****	1,716	22.9	1,716	22.9	3,759	50.2	3,694	49.3	3,694	49.3

\* As measured by the Central Bureau of Statistics.

\*\* 1985 and 1990 data refer to widow with two children who was entitled to income support.

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

\*\*\*\* At least one member of the family is over 55.

The temporary provision that was adopted in 2004 regarding the reduction of child allowances (by NIS 24 for each of the first three children and by NIS 5 for the fourth child onward) expired. Nonetheless, the gradual process of achieving a uniform allowance for all children continued. The combination of these two developments led to a rise in the child allowance for families with up to 3 children, on the one hand, and to continued erosion of the child allowance for families with 4 children and more, on the other hand. The data in Table 8 show that while among families with two children the allowance increased relative to the average wage (from 3.3% in 2005 to 4.0% in 2006) for the first time since 2000, the allowance for families with four children has remained virtually unchanged relative to the average wage. However, the allowance for larger families continued to be eroded during the long erosion process that began in 2001 and in 2006, actually reaching its lowest rate – namely half the allowance relative to the average wage in 2001. The sharp decline in the value of the child allowance point in 2006 as compared to 2005 is mostly technical in nature and can be explained by the transition to adjusting child allowances according to a “basic amount” instead of a “child allowance point” in effect until January 2006.

A real rise in the level of benefits was generally observed in the branches paying wage-replacing benefits: the average daily unemployment benefit rose by 3.4% in 2006 and the average daily maternity allowance increased by about 3% in real terms. However, the decline in the average daily unemployment benefit in relation to the average wage (from 47.4% in 2005 to 47.1% in 2006) persisted. The maternity allowance relative to the average wage also continued to be eroded, from 74.3% in 2005 to 73.7% in 2006. The hospitalization grant, which was adjusted three times during the course of 2006, rose by 2.5% in real terms in 2006 whereas the average daily injury allowance for wage earners decreased by about 1.3% in real terms.

**Table 8: Child allowance point and child allowances\* (constant prices and percentage of the average wage), monthly average, 1975-2006**

Year	Value of child-allowance point		Allowance for 2 children**		Allowance for 4 children		Allowance for 5 children	
	2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage	2006 prices (NIS)	% of average wage
1975	187	4.4	377	8.8	1,174	27.4	1,597	37.3
1980	146	2.8	293	5.6	913	17.7	1,242	24.0
1985	165	3.1	187	3.6	1,281	24.7	1,820	35.1
1990	191	2.9	92	1.5	1,485	23.4	2,105	33.2
1995	186	2.8	373	5.8	1,496	23.4	2,128	33.4
2000	189	2.5	380	5.0	1,526	20.2	2,173	28.7
2001	187	2.4	376	4.8	1,512	19.5	2,450	31.6
2002	178	2.4	317	4.3	1,260	17.3	2,052	28.1
2003	176	2.5	299	4.2	1,104	15.6	1,762	24.9
2004	177	2.4	252	3.5	862	11.8	1,358	18.7
2005	175	2.4	245	3.3	772	10.5	1,181	16.0
2006	148	2.0	296	4.0	803	10.7	1,132	15.1

\* Until 1995, including Special Allowance for Veterans.

\*\* The allowance level in 1985 and 1990 relates to families (with up to 3 children) who were not eligible for the first child allowance, and since October 1990 – neither for the second child allowance. In March 1993 the payment of child allowance on a universal basis was renewed.

\*\*\* Since 2006, child allowances are calculated according to the base sum, which was 148 NIS in January 2006.

In January 2007, there were no changes in the “basic amounts”; accordingly, the benefits paid by the NII derived from these sums were not adjusted. However, the average wage

according to articles 1 and 2 of the National Insurance Law changed in January 2007, hence a change in the benefits and parameters derived according to the average wage.

## 1.5 Benefit recipients

In the largest branch (from the point of view of the scope of benefit payments) among the NII branches – Old-Age and Survivors – the NII paid benefits to a monthly average of 727,500 elderly and survivors in 2006. This figure reflects a 1.1% increase as compared to the previous year, following a slight decline in the number of recipients in 2005, for the first time in years. The slowdown in the growth of old-age and survivors' pension recipients, which began in 2002, is attributable to the decrease in immigration to Israel, the natural decline in the number of elderly immigrants, as well as the implementation of the Retirement Law in June 2004, which raised the conditional age of entitlement to old-age pension for men and women and the absolute age of entitlement to pension for women. Similarly to previous years, the number of recipients of survivors' pensions **only** remained more or less stable in 2006 as well. This year, approximately 105,000 widows and widowers received a survivors' pension only (those who receive old-age pension plus half a survivors' pension are counted in the elderly population).

In the second largest branch from the point of view of the scope of benefit payments – General Disability – there was a 4.3% increase in the number of recipients, following a more significant rise last year. The benefits derived from the General Disability branch typically increased substantially in the last two years: the number of attendance allowance recipients increased by 6.7% (versus 5.9% in 2005) and the number of mobility allowance recipients increased by 4.8% (versus 5.9% in 2005). Similar increases were also noted in the mobility allowance and Long-Term Care branch, which grants in-kind benefits (care hours) to the elderly whose daily functioning is limited. There was a 1.3% increase in the third largest branch – Child Allowances. In 2006, about 2.3 million children living in 968.3 thousand families were paid a child allowance.

The declining trend in the number of unemployment benefit recipients resumed following one year of respite, however while the decrease of nearly 5% between 2005 and 2006 is mainly attributable to the decline in the unemployment rate, the drastic decrease (of about 45%) in the number of recipients between 2002 and 2006 is the result of the more stringent unemployment benefit requirements introduced in 2002-2003. Even though the tightening of the eligibility criteria for unemployment benefits placed Israel at the bottom of the generosity scale for unemployment insurance from an international perspective, it did not prevent decision-makers from pursuing this policy in 2007 as well<sup>12</sup>. There was also a sharp decline of about 7% in the number of income support benefit recipients. This decrease is an additional link in the chain of decreases that began in 2004, and it is attributable to a combination of several factors: the more stringent eligibility requirements introduced in 2003, the positive changes in the labor market in the last two years and the implementation of the law for the integration of benefit recipients into the workforce.

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<sup>12</sup> See Box C in this chapter.

Table 9: Number of Benefit Recipients in Main Insurance Branches, Monthly Average, 1985-2006

Year	General Disability				Work Injury			Maternity		Children Families Receiving Child Allowances**	Unemployment	Income Support to Working-age Population***	Long-term Care
	Old-age and Survivors	Disability Pension	Attendance Allowance	Benefit for Disabled Child	Mobility Allowance	Injury Allowance*	Permanent Disability Pension	Maternity Grant*	Maternity Allowance*				
1985	390.2	62.1	4.6	4.0	10.6	56.9	9.9	101.3	42.7	546.9	19.6	20.4	-
1990	442.6	73.4	6.5	5.8	11.4	56.7	11.8	103.6	43.7	532.5	50.6	31.8	25.0
1995	553.9	94.0	10.2	10.3	13.2	84.9	14.6	113.1	55.2	814.7	61.5	74.8	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	127.1	71.2	928.2	104.7	141.8	105.4
2002	692.9	150.5	20.6	17.5	20.9	70.0	21.8	128.5	71.4	935.0	97.1	151.6	112.2
2003	709.2	157.3	21.7	18.4	22.3	61.5	23.0	136.4	73.9	939.1	70.5	155.2	113.0
2004	722.3	162.4	22.7	19.5	23.5	65.8	24.0	141.2	77.5	945.6	58.4	144.7	113.4
2005	719.9	170.9	24.0	21.0	24.9	63.9	25.2	140.6	77.0	956.3	58.8	139.9	115.0
2006	727.5	178.3	25.6	22.2	26.1	64.3	26.4	143.6	82.7	968.3	56.0	130.3	120.4
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
2004	1.8	3.2	4.6	6.0	5.4	7.0	4.3	3.5	4.9	0.7	-17.2	-6.4	0.4
2005	-0.3	5.2	5.9	7.2	5.9	-2.9	5.0	-0.4	-0.6	1.1	0.7	--	1.4
2006	1.1	4.3	6.7	5.7	4.8	0.6	4.8	2.1	7.4	1.3	-4.8	-6.9	4.7

\* 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. In 1993 the allowances again became universal.

\*\*\* In the calculation of data for 2004 and thereafter, a benefit split among several recipients was accounted for one recipient only. The number of recipients for 2004 calculated for all recipients of the split benefit was 145,600 as a monthly average.

The relative stability in 2006 among injury allowance recipients (0.6%) is the result of two contrasting developments: The new legislation compelling employers and the self-employed to finance injury allowances for the first 12 days (rather than for the first 9 days, as was the case until 2004) contributed to lowering the number of recipients, while the increase in the number of employed contributed to increasing it. The number of (permanent) disability pension recipients in the Work Injury branch rose by about 5% in 2006 (similarly to the average rise in the five previous years), reaching about 26,000. In the Maternity branch, there was an increase of 2.1% in the number of women receiving maternity grants and of 7.4% in the number of women receiving maternity allowances. These increases as well are attributable to the economy's employment expansion trend.

### **1.6 Collection of contributions from the public and the benefits' financing sources**

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 reduced national insurance contributions for employers and the self employed); government participation in the financing of contributory benefits; government participation in the financing of non-contributory benefits; and proceeds stemming from the interest on investments of surpluses in government bonds. In addition to collecting national insurance contributions, the NII collects health insurance contributions and transfers them to the sick funds.

Similarly to previous years, collection from the public in 2006 was affected by a combination of factors: economic developments on the market and the changes in government policy regarding the financing of the national insurance system. The first stage of the gradual process of reducing the national insurance contributions imposed on employers was launched in August 2005, pursuant to the 2005 Economy Arrangements Law. This process will continue until 2009 and the average rate of insurance

contributions for employers will be reduced by 1.5 percentage points. This policy is part of a more comprehensive government policy to reduce both the tax burden and public expenditure.

The NII expressed its opposition to the reduction of the insurance contributions for employers, particularly in view of the policy implemented since the mid 1980s geared to lower the cost of labor. The reduction of proceeds stemming from public collection increases the national insurance system's dependence on Treasury budgets, which may indirectly lead to a further reduction in benefit expenditure.

The government policy regarding the adjustment of NII benefits also applies to collection parameters. In 2002-2005 the average wage pursuant to the National Insurance Law was not adjusted; accordingly, nor were the insurance premium brackets or the minimum income for the payment of insurance contributions for the various types of insured persons. The freeze on the average wage continued until the end of 2005, and as of 2006, the ceiling was adjusted by the rate of the rise in the price index only. However, the reduced rate bracket, as well as the minimum income for payment of insurance contributions for the various types of insured persons, will continue to be adjusted according to the changes in the average wage after 2006 as well. The change in the method of adjusting the income ceiling will ultimately lead to an easing of the burden on very high wage-earners, who will be favorably discriminated against as compared to those who pay insurance contributions at the minimum rate (such as the unemployed and students). However, the continued linkage of the reduced rate bracket to the average wage will prevent low-wage earners from being weighed down by a heavy burden of insurance contributions.

### Box C

#### Legislative amendments for 2007

This box presents the main legislative amendments pertaining to NII benefits in 2007 (not including legislative amendments made in previous years and covering several years, 2007 being one of them).

The provision regarding the 4% reduction in some of the NII benefit payments (such as income support, injury allowance, maternity benefits, unemployment, etc.) was supposed to expire on December 31, 2006. The Economy Arrangements Law of 2007 **extended the validity of this provision** until the end of 2007, except for the long-term care benefit.

The following is a breakdown of the legislative changes introduced to the various pensions in 2007, by benefit type:

Income support: Changes regarding car ownership and conditions pertaining to travelers abroad were introduced:

1. Car ownership: As of January 2007, car owners are no longer denied income support payments outright (in the past, it was only on rare occasions – such as for medical reasons – that car ownership did not rule out eligibility for income support), provided the car owned by the claimant has an engine capacity of up to 1600 cubic centimeters and 12 years have elapsed since the end of the year of the vehicle's manufacture.

Car ownership will only entitle the claimant (or his/her spouse) to income support if his/her job income exceeds 25% of the average wage (or in the case of a claimant of retirement age – 17% of the average wage). The law also applies to those who were dismissed from their jobs.

2. Travel abroad: Improved conditions have been introduced for travelers abroad regarding the number of times and duration of their stays abroad and their continued entitlement to the benefit pursuant to the Income Support Law. The amendment only applies to a person of retirement age (or his/her spouse): Travel abroad up to 3 times a year, for no longer than 72 days, shall not deny the traveler income support; traveling abroad a fourth time or deviating from the 72-day limitation will lead to a denial of the entitlement to income support for the entire duration of the stay abroad during that calendar year.

Long-term care: Amendments have been made to this allowance. Moreover, for the first time, an attempt has been made to convert the in-kind benefit into a cash benefit.

1. To date there have been two benefit levels and as of January 2007, three benefit levels will be granted as follows: those who have accumulated 2.5-5.5 points in the dependency test are entitled to 91% of a full single person's benefit according to Article 9 of the Law and will be granted 9.75 weekly care hours. Those who have accumulated 6 to 8.5 points in the dependency test are entitled to 150% of a single person's pension, which is equivalent to 16 weekly care hours (prior to the amendment, those who had accumulated 6 points were only entitled to the low level benefit). Moreover, those who accumulate 9 points or more will be granted 18 weekly care hours (168% of a full single person's benefit).
2. Attempt to convert the in-kind benefit into a cash benefit: the long-term care benefit is not paid in cash but granted to those entitled to it through organizations for whose services the NII pays. However, at the beginning of 2007, the Knesset approved NII's proposal to run an experimental cash-benefit program in four regions, to be implemented as of June 2007 for those who accumulated at least 6 points in the dependency test and require full-time care throughout most of the day.

According to the compensation law for polio victims (disability), Israelis who were affected by polio will receive a one-time compensation as well as a monthly stipend, to be added to the other benefits (disability, attendance allowance) paid to them. The claims pursuant to this law will be submitted as of September 1, 2007 and the payments will be made retroactively as of January 1, 2007.

Unemployment insurance: Unemployed persons aged 25 to 28 are entitled to a maximum period of 67 days (instead of the 100 days in effect prior to the amendment). Moreover, unemployment insurance for persons up to the age of 28 was reduced by about 25%, namely the new rates prior to and following the legislative amendment are as follows:

Percentage of salary	Unemployment rate as a percentage of the wage prior to unemployment	
	Before 2007	After 2007
Up to half of the average wage	80%	60%
From half to $\frac{3}{4}$ of the average wage	50%	40%
From $\frac{3}{4}$ of a full average wage	45%	35%
Above the average wage	30%	25%

As of July 2007, a demobilized soldier requires a qualifying period like any other unemployed person, whereby compulsory army service will be considered as 6 months out of the mandatory 12-month eligibility period.

Maternity allowance: As of May 2007, paid maternity leave will be extended by two weeks, from 12 weeks to 14 weeks.

Hospitalization grant: The hospitalization grant paid to hospitals for the birth and the mother's hospital stay was raised by 12%. Even though this expense should be entirely funded by the Treasury, it was decided that the latter would make an annual transfer of NIS 151.6 million (according to 2007 prices) to the NII, rather than the sum required as a result of the increase in the hospitalization grant in accordance with the changes in the number of births each year.

Another change pertains to the realm of collection: The reduced employer rate decreased in 2007 from 4.98% to 4.14%, as part of the process of reducing insurance contributions for employers.

### 1.6.1 Collection of insurance contributions from the public

Similarly to previous years, collection from the public in 2006 stemmed from economic developments and the changes in government policy regarding the financing of both the national and health insurance systems. The NII's proceeds from the collection of national and health insurance contributions from the public amounted to NIS 36.1 billion in 2006: NIS 23.55 billion to national insurance branches and NIS 12.55 billion to the health system. Approximately NIS 1.7 billion transferred by the State Treasury as indemnification for reduced national insurance contributions for employers and the self-employed (pursuant to Article 32C of the Law) should be added to the collection from the public. Direct collection from the public in 2006 rose by about 2.2% in real terms: collection of national insurance contributions from the public rose by 1.4% and collection of health insurance contributions, by 4.0%.

The modest rise – as compared to 2005 – in the collection of national insurance contributions from the public, despite the similar economic developments in the realm of salary and employment, can be explained by the legislative changes introduced in 2005 and 2006. A process of reducing insurance contributions for employers began in July 2005 and continued throughout 2006 as well. Were it not for these legislative changes, direct collection from the public would have risen by 4.7% – more than double the actual rate. Whereas in the area of health insurance contributions, collection was not affected by legislative changes, in the area of national insurance contributions, actual collection rose by about 70% less than its rate would have been were it not for the legislative changes (1.4% versus 5.1% respectively).

The changes in collection rates differ between salaried and non-salaried employees. Whereas the rate of collection from salaried employees rose fairly modestly in real terms – by 0.6% in 2006 (following a 3.5% increase in 2005) – the corresponding collection rate among non-salaried employees increased by 9.7% (following a 6.1% increase in

2005). The declining collection rate among salaried employees is due to the continued reduction of the insurances contributions for employers, which began in the second half of 2005.

The declining trend in the NII's collection from the public relative to the GDP is continuing. From 2003 to 2006, collection relative to the GDP decreased from 6.5% of the GDP to 5.8% of the GDP. Collection for the health system also decreased from 2.1% of the GDP to 2.0% of the GDP. In the wake of the income tax reform, the share of collection from the public in the total direct taxes collected from individuals increased to 43.2% (following a slight decline in 2005).

Table 10: Collection for the national insurance and health systems, 2001-2006

	2001	2002	2003	2004	2005	2006
<b>Current prices (NIS million)</b>						
<b>Total proceeds from insurance contributions</b>	32,814	33,995	33,660	34,331	36,137	37,792
Total collection from the public	29,724	31,378	32,275	32,971	34,597	36,112
For national insurance branches	19,147	20,495	21,424	21,661	22,759	23,554
For the health system	10,577	10,883	10,851	11,310	11,838	12,558
Total Treasury indemnification	3,090	2,617	1,385	1,360	1,540	1,680
<b>Indicators of development of collection from the public</b>						
<b>A) As a percentage of real change</b>						
Total collection from the public	6.3	-0.1	2.2	2.6	3.6	2.2
For national insurance branches	5.8	1.3	3.8	1.5	3.7	1.4
For the health system	7.2	-2.7	-1.0	4.6	3.3	4.0
<b>B) As a percentage of the GDP</b>						
Total collection from the public	6.0	6.1	6.2	6.0	5.9	5.8
For national insurance branches	3.9	4.0	4.1	3.9	3.9	3.8
For the health system	2.1	2.1	2.1	2.1	2.0	2.0
<b>C) As a percentage of direct taxes to individuals</b>						
Total collection from the public	35.2	36.8	40.2	41.8	41.4	43.2
For national insurance branches	22.7	24.0	26.7	27.5	27.2	28.2
For the health system	12.5	12.8	13.5	14.3	14.2	15.0
<b>D) As a percentage of direct taxes</b>						
Total collection from the public	28.3	30.8	32.5	32.0	31.1	28.8
For national insurance branches	18.2	20.1	21.6	21.0	20.4	18.8
For the health system	10.1	10.7	10.9	11.0	10.6	10.0

### 1.6.2 Sources of financing

The total NII proceeds for financing its branches amounted to about NIS 52.3 billion in 2006, at current prices. The data in Table 11 show that the real rise of about 3% for the second consecutive year contradicts the real declining trend in the total financing sources in the two years preceding 2005. This increase reflects a substantial rise in the government's participation in financing NII branches and in the interest on NII investments, which comprises about one tenth of the total NII proceeds (5.5% and 6.7% respectively), alongside a more moderate increase of 1.7% in the proceeds from national insurance contributions (collection from the public and Treasury indemnification) and of about 2% in government-funded non-contributory benefits, which together amount to about two thirds of the total NII proceeds.

The increase in the government's participation is attributable to its expansion according to Article 32 of the Law in order to compensate for loss of income as a result of the lowering of insurance contributions for employers<sup>13</sup>. The increase in the government's funding of non-contributory benefits – for the first time after three years of a cumulative decline of about 20% – reflects an increase in the payments of income supplements for the elderly, mobility allowances and reserve service payments that soared in the wake of the Second Lebanon War. The increased payments for these benefits were partially offset by the continued decline in benefits geared to guarantee a minimum income for the subsistence of the working-age population: income support and alimony. An examination of the distribution of benefit financing by source shows that the share of the government financing rose by an average of about 4% in 2006, versus a more moderate rise of 2.6% in NII proceeds from independent sources.

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<sup>13</sup> The NII reached an agreement with the Treasury whereby Treasury allocations pursuant to Article 21 of the Law shall not be affected by a reduction of the insurance contributions and the adjustments required by law were made accordingly.

Table 11: Sources of financing of National Insurance branches, 1995-2006

Year	Total proceeds	Collection of national insurance contributions *	Government participation**	Government financing of benefits	Proceeds from interest
NIS Million, current prices					
1995	23,581	12,171	4,222	4,650	2,504
2000	41,207	20,751	8,336	8,148	3,907
2001	46,110	22,237	9,952	9,756	4,075
2002	48,642	23,114	10,506	10,590	4,266
2004	47,513	23,021	10,996	8,548	4,617
2005	49,705	24,299	11,700	8,616	4,850
2006	52,344	25,234	12,600	8,982	5,290
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	-0.1	2.7	-1.0
2004	-0.6	1.3	2.2	-8.9	4.1
2005	3.2	4.2	5.0	-0.5	3.7
2006	3.1	1.7	5.5	2.1	6.8
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
2004	100.0	48.5	23.1	18.0	9.7
2005	100.0	48.9	23.5	17.3	9.8
2006	100.0	48.2	24.1	17.2	10.1

\* Includes Treasury indemnification.

\*\* According to Article 32(A) of the Law.

### 1.6.3 Surpluses/deficits and financial reserves

Since 2004, the NII budget shifted from current deficit to current surplus. If income from interest on NII investments is not taken into account, the budgetary surplus in 2006 amounted to about NIS 1.3 billion. Conversely in 2005, there was a slight decline in the budgetary surplus, which is attributable to the lowering of the insurance contributions for employers, the growth in the deficit in the various branches (Maternity, Disability, etc.) – due to the increase in the number of benefit recipients – and the growth in the deficit in the Old-Age branch as a result of the rise in the benefit levels.

**Table 12: Surpluses/deficits in National Insurance branches, 2001-2006**

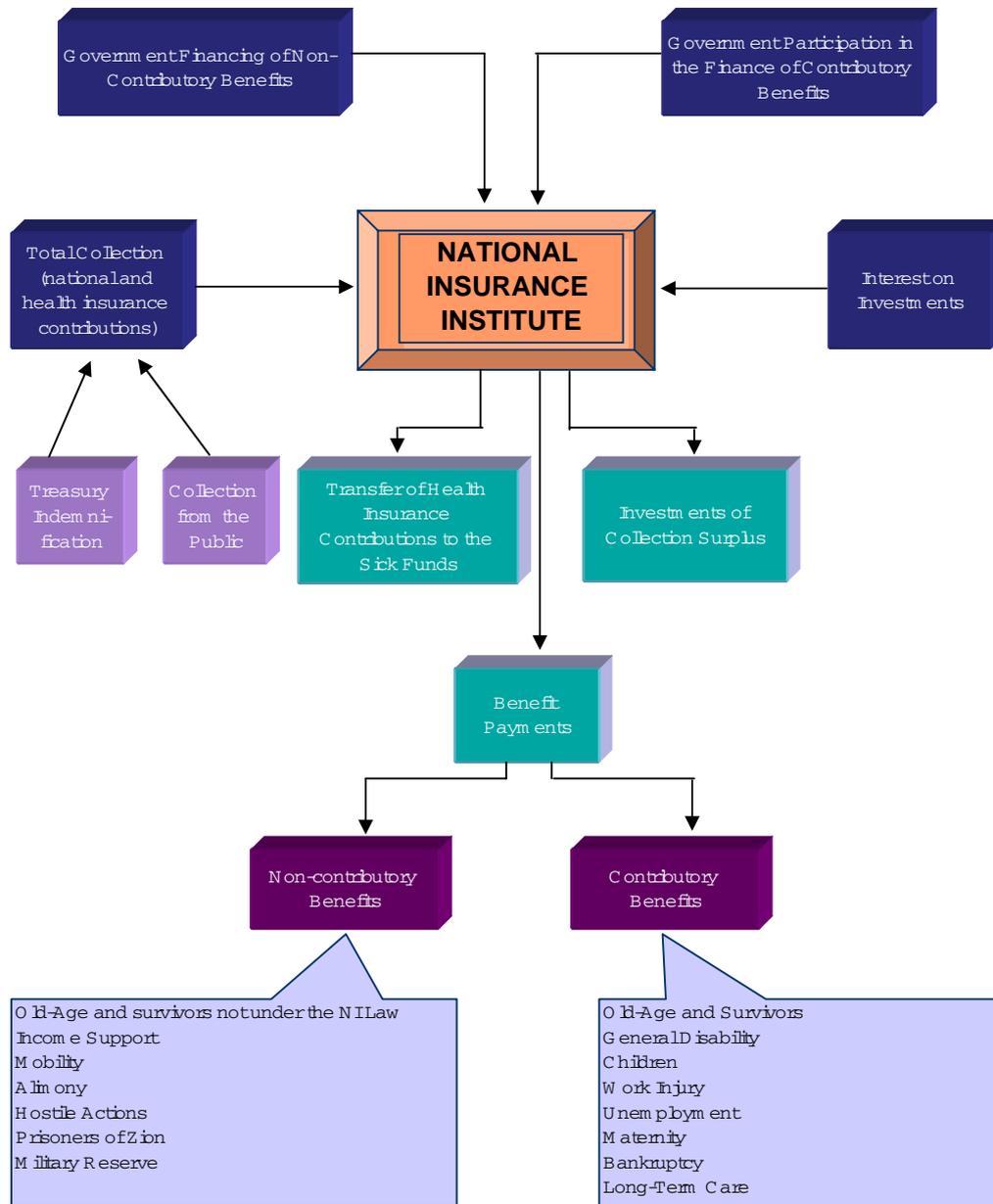
Insurance Branch	Surplus/Deficit Without Interest on Investments			Surplus/Deficit Including Interest on Investments		
	2001	2005	2006	2001	2005	2006
Millions of NIS (current prices)						
Total	-3,420	1,550	1,293	657	6,400	6,583
Old-age & survivors	-633	-725	-762	1,019	1,285	1,389
General disability	-1,762	-2,777	-2,890	-912	-2,243	-2,455
Work injury	-1,193	-987	-1,213	-821	-757	-1,013
Maternity	-852	-925	-1,019	-674	-905	-1,044
Children	5,338	10,126	10,333	5,890	11,975	12,748
Unemployment	-3,090	-1,591	-1,543	-3,090	-1,621	-1,573
Long-term care	-1,410	-1,612	-1,730	-1,049	-1,487	-1,695
Other	182	41	117	294	153	227

Whereas the current deficit is continuing to shrink in the Unemployment branch (which is entirely financed by the Children's branch), the deficit further increased in 2006 in the

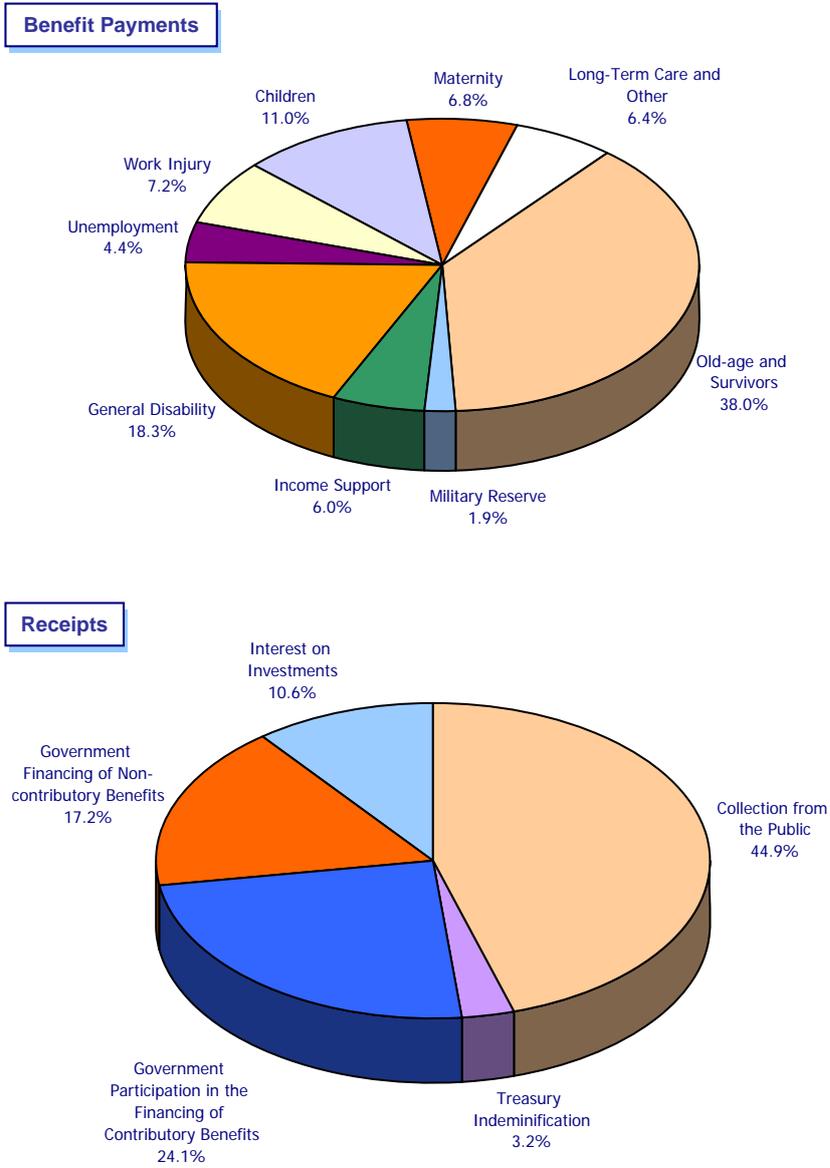
other deficit branches in 2005. In fact, the only branch that is not in deficit among those listed in the Table is the Children's branch, which has experienced a large current surplus throughout the years. Taking into account income from interest on past surpluses reflects an improvement in the financial situation of the NII branches: the surplus including interest grew from about NIS 6.4 billion in 2005 to about NIS 6.6 billion in 2006. Nonetheless, the Disability, Work Injury, Unemployment and Long-Term Care branches have remained in deficit. The disappearance of the current deficit in the NII's budget and the shift to a current surplus is of course reflected in the reduction of the deficit in the State budget.

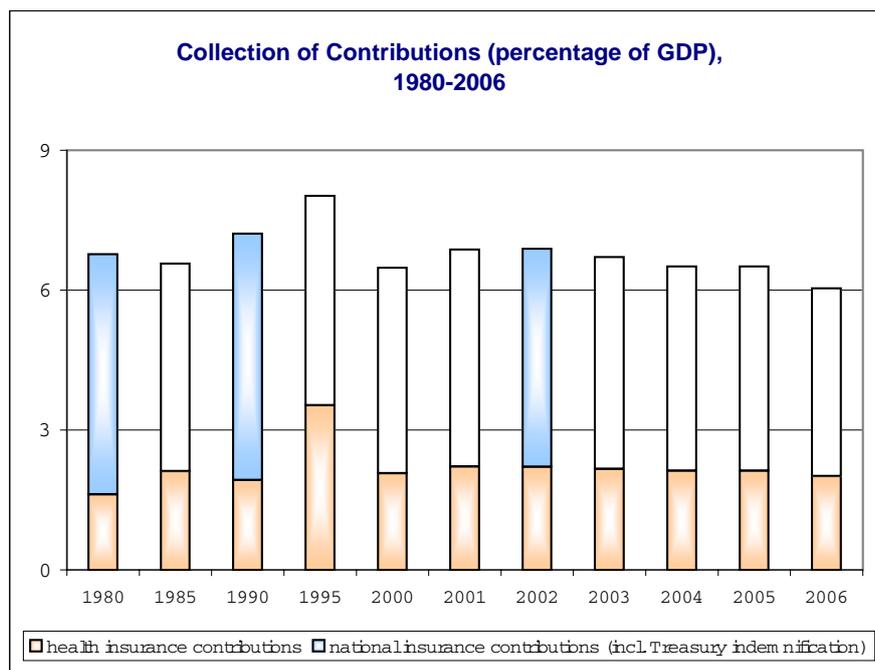
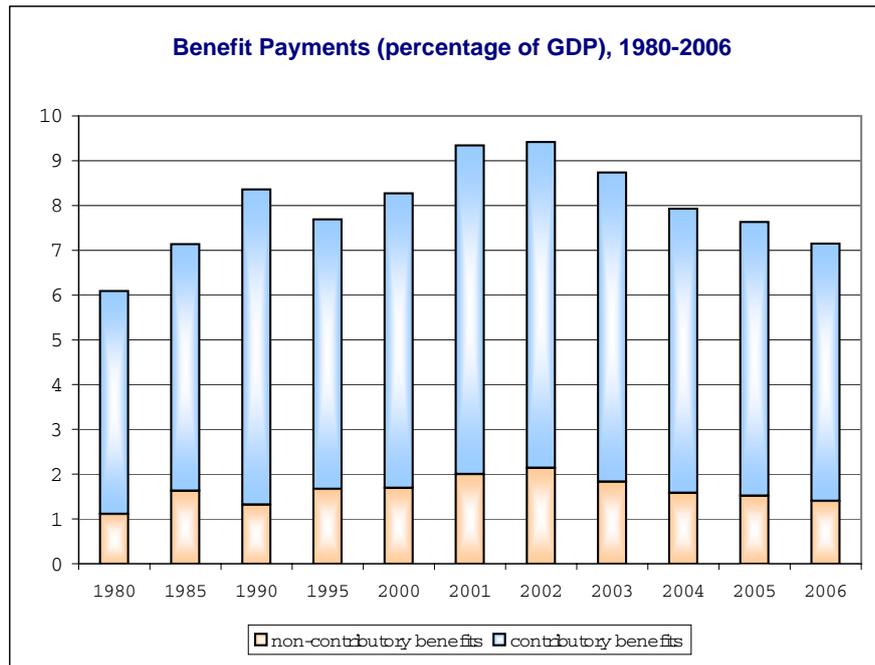
Within the scope of the discussions of the 2007 budget deliberations, the Research Administration submitted a detailed document on the status of the NII branches and the forecast for the next two years. The report reveals that the balance of assets in the Maternity and Long-Term Care branches was negative at the end of 2006. The deficit in the Maternity branch was estimated at about NIS 1.15 billion and in the Long-Term Care branch, at about NIS 0.3 billion. The NII Finance Committee approved a transfer of funds from the balance of assets of the Children's branch to the above NII branches, as well as to two additional deficit branches (General Disability and Work Injury), so as to ensure their ongoing functioning through to April 1<sup>st</sup>, 2008.

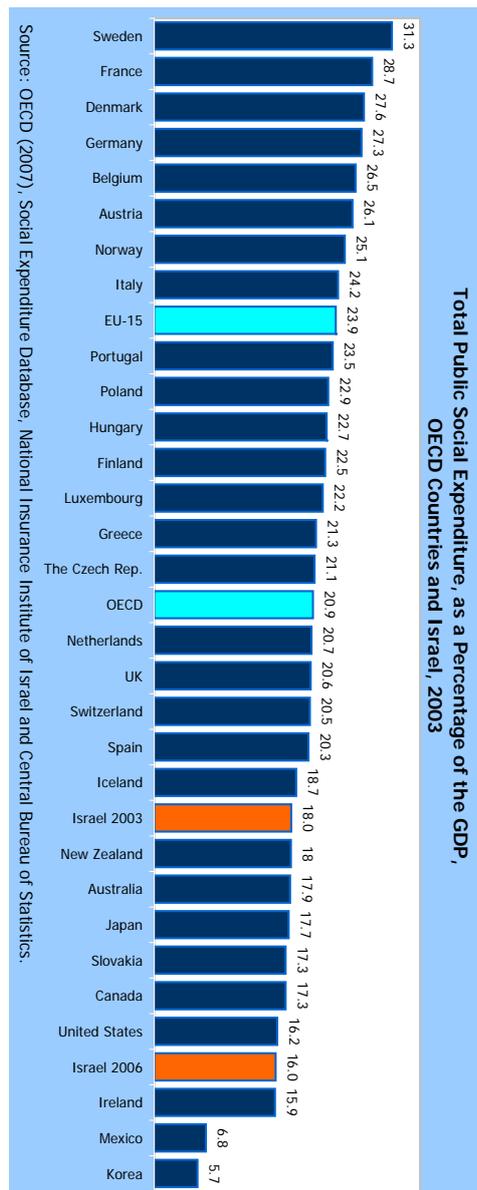
The National Insurance Institute - Resources and Uses

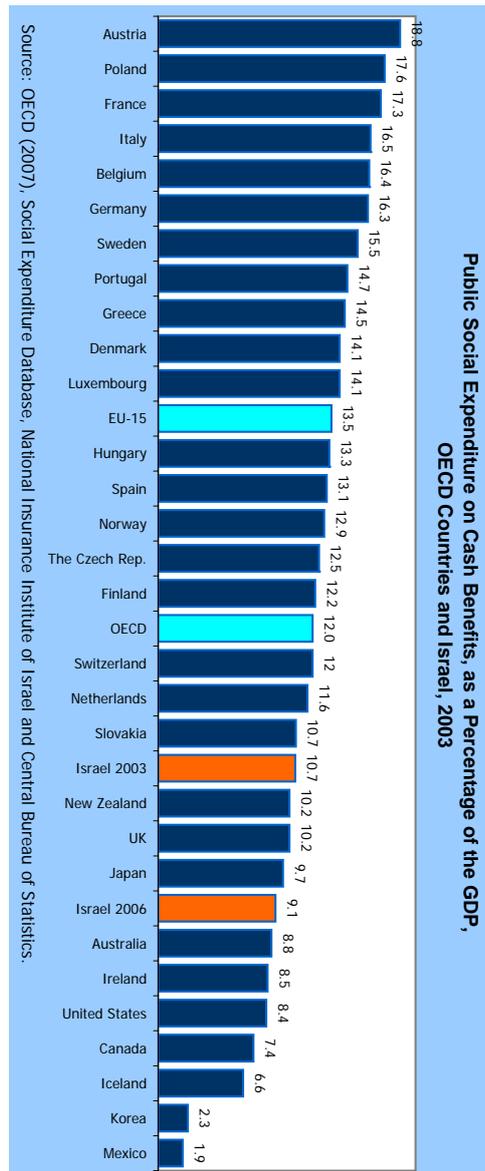


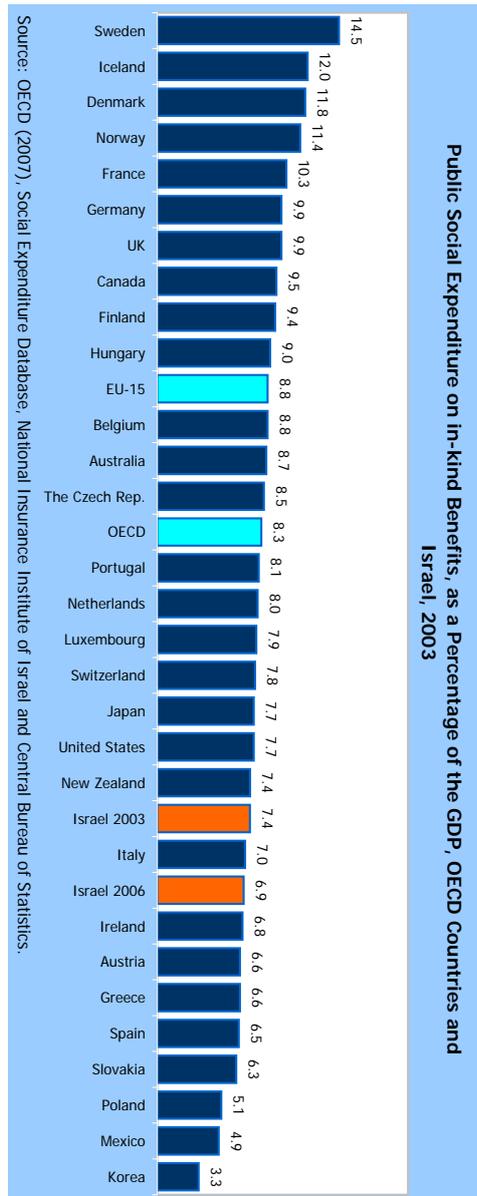
The Distribution of NII Benefit Payments and Receipts - 2006













## **Chapter 2**

# **Trends of Development in Poverty and Income Inequality (Summary)**

**Miri Endweld  
Refaela Cohen**



## 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.<sup>1</sup> 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

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<sup>1</sup> 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).

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.

## 2.2 Data base

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). 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.<sup>2</sup>

Beginning in 2005, the NII calculates poverty data twice a year. In addition to the 2005 data, poverty findings will be presented below for a period including the second half of 2005 and the first half of 2006 (July 2005-June 2006). No special sample-based survey was conducted to investigate poverty and income inequality in this period; rather, a two-part database was created: data for the second half of 2005 were taken from the 2005 Income Survey, while data for the first half of 2006 were taken from the 2006 Income Survey (not yet completed). This database and its findings will be referred to as: 2005/6. The second half of 2005 is therefore part of both survey periods (generally) referred to by the tables below.

The present summary surveys the dimensions of poverty and income inequality in Israel in 2005 and 2005/6 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

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<sup>2</sup> However, in 2000-2001 the inhabitants of East Jerusalem were not included in the survey, due to difficulties in data collection. The populations not yet included are mainly the kibbutzim and the Beduin inhabitants who do not reside in permanent localities.

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.

### 2.3 Poverty in 2005/6

The economic growth that began with the 2004 recovery from the recession, continuing into the first half of 2006, was still evident in the period between 2005 and 2005/6, when the standard of living rose at a real rate of 1.4% in terms of net income per standard person, as a family average. Since 2004 there has been a real growth of about 6%. The median net income per standard person, from which the poverty line is derived, rose moderately between 2004 and 2005/6 – by about 5.5%. Table 1 presents the poverty line by family size in 2005 and in 2005/6.

In 2005/6 the scope of poverty among families in Israel remained stable. The rate of families whose net income fell below the poverty line, 20.3% in 2004, remained at almost an identical rate – 20.2% – in 2005/6. The rate of poverty among persons and children, however, continued to rise steadily, a trend that has characterized recent years. Tables 2 and 3 present the scope of poverty in 2004 and in 2005/6, in absolute numbers and in percentages, respectively. Table 3 shows that the scope of poverty among persons rose from 23.6% to 24.4% between 2004 and 2005/6, while among children, it rose from 33.2% to 35.2%. The incidence of poverty among persons rose from 1998 to the period of the last Survey by an accumulated rate of 33%, and among children by 50%. It should be noted that the upward trend in the rate of poor persons and children was halted between 2005 and 2005/6. Table 3 also shows that the poverty gap ratio (reflecting poverty depth), 33.3% in 2004, rose slightly, reaching 33.9% in 2005/6. This means that the average net income of a poor family is about a third away from the poverty line. Similar to other measures, this measure has been

increasing consistently in recent years; in 2003, for example – when the deep cut in benefits began – it was about 30%.

**Table 1: Number of Standard Persons and the Poverty Line per Family, by Number of Family Members, 2005 – 2005/6**

Number of family members	Number of standard persons	Poverty line per family in 2005		Poverty line per family in 2005/6	
		NIS per month	percentage of the average wage	NIS per month	percentage of the average wage
1	1.25	1,866	25.6	1,927	25.8
2	2.00	2,986	40.9	3,083	41.3
3	2.65	3,957	54.2	4,085	54.7
4	3.20	4,778	65.5	4,933	66.1
5	3.75	5,599	76.7	5,781	77.2
6	4.25	6,346	86.9	6,551	87.7
7	4.75	7,092	97.2	7,322	98.1
8	5.20	7,764	106.4	8,016	107.3
9**	5.60	8,361	114.6	8,632	115.6

\* The average wage calculated for 2005 is the weighted average of the average wage per employee post (Israeli workers) in the period October 2004-November 2005. For 2005/6, the weighted average wage for the period April 2005-June 2006 was calculated.

\*\* The weight of each additional person is 0.40, so that there are 6 standard persons in a family of 10 persons.

The stabilization in the poverty rate did not characterize all population groups (Table 4). Poverty among the elderly declined from 25.1% in 2004 to 22.9% in 2005/6. This decline reflects the influence of the increase in benefits to the elderly, including the low-income elderly, in 2005. A decline in poverty was noted also in families headed by a self-employed person – from 14.6% in 2004 to 12.6% in 2005/6. Among families

with two earners, the incidence of poverty remained stable between the two periods. On the other hand, the incidence of poverty among families with children continued to rise between 2004 and 2005/6 – by an additional percentage point, to a level of 25.6%. However, in the transition between the 2005 Survey and the 2005/6 Survey, the trend of growth in poverty among families with children was halted for the first time in seven years.

**Table 2: Poverty in Total Population, 2004 - 2005/6**

Poverty measure	Before transfer payments and direct taxes	After transfer payments only	After transfer payments and direct taxes
<b>2004</b>			
Poor population			
Families	656,800	320,600	394,200
Persons	2,184,100	1,308,500	1,534,300
Children	881,600	632,100	713,600
<b>2005</b>			
Poor population			
Families	668,200	340,400	410,700
Persons	2,235,800	1,411,700	1,630,500
Children	899,600	686,500	768,800
<b>2005/6</b>			
Poor population			
Families	664,500	340,200	404,500
Persons	2,238,100	1,428,200	1,630,100
Children	906,400	699,700	775,400

Table 3: Poverty in Total Population, by Selected Poverty Measures, 2004 - 2005/6

Poverty measure	Before transfer payments and direct taxes	After transfer payments only	After transfer payments and direct taxes
<b>2004</b>			
Incidence of poverty (%)			
Families	33.7	15.8	20.3
Persons	33.6	20.2	23.6
Children	41	29.4	33.2
Poverty gap ratio (%)*	64.5	33.4	33.3
SEN index*	0.283	0.094	0.111
Gini index of inequality in income distribution of poor*	0.5499	0.2007	0.2045
<b>2005</b>			
Incidence of poverty (%)			
Families	33.6	17.1	20.6
Persons	33.8	21.3	24.7
Children	41.1	31.4	35.2
Poverty gap ratio (%)*	62.5	32.8	33.1
SEN index*	0.278	0.098	0.114
Gini index of inequality in income distribution of poor*	0.5246	0.1923	0.1953
<b>2005/6</b>			
Incidence of poverty (%)			
Families	33.1	17.0	20.2
Persons	33.5	21.4	24.4
Children	41.1	31.7	35.2
Poverty gap ratio (%)*	62.5	33.5	33.9
SEN index*	0.275	0.099	0.115
Gini index of inequality in income distribution of poor*	0.5192	0.1939	0.1984

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

The rise in poverty among large families (with four or more children) continued: poverty in these families increased from its high level in 2004 (54.7%) to 58.1% in 2005 and to 58.8% in 2005/6. This situation is a result of the deep cut in child allowances implemented beginning in 2002. Arab families and Arab children continued to be those with among the highest poverty rates. However, their poverty rates stabilized somewhat in comparison to those of large families in general, due to their greater integration in the labor market.

The high rate of poverty in families headed by a non-worker (of working age) continued to rise, from 66.6% in 2004 to 67.9% in 2005, and poverty depth in these families rose too – by an additional percentage point.

The transfer payments and direct taxes in the 2005/6 Survey period extricated 39% of the poor families from poverty. This rate reflects a continued decline in the influence of transfer payments on the reduction of poverty (in 2002, for example, about 48% of families were extricated from poverty due to government intervention). The transfer payment and direct taxation systems are able to extricate less than a third of the poor population – and only about a sixth of poor children – from poverty (as compared to over a third of poor persons and a quarter of poor children in 2002). Similarly, the contribution of the benefits and direct taxes in reducing the poverty gap ratio has lessened, from 47.5% in 2004 to 45.8% in 2005/6.

**Table 4: Poverty in Specific Population Groups, 2005 and 2005/6**

Population group (families)	2005			2005/6		
	Economic income	Net income	Concentration index*	Economic income	Net income	Concentration index*
Total population	33.6	20.6	1.00	33.1	20.2	1.00
Family head:						
Elderly	57.0	24.4	1.18	56.9	22.9	1.13
Not working (of working age)	90.4	65.8	3.19	89.7	67.9	3.36
Working:	18.4	12.2	0.59	18.2	11.9	0.59
Employee	18.8	12.1	0.59	18.6	11.7	0.58
Self-employed	15.3	13.0	0.63	15.2	12.6	0.62
Families with one earner	34.8	23.1	1.12	34.6	22.6	1.12
Families with two earners	4.7	3.1	0.15	4.8	3.1	0.15
Jews**	29.8	15.9	0.77	29.5	15.4	0.76
Arabs	58.6	52.1	2.53	56.6	51.2	2.53
Immigrants (from 1990)	42.4	20.0	0.97	41.5	18.6	0.92
Single-parent	53.3	32.5	1.58	53.4	30.9	1.53
Families with children	32.4	26.2	1.27	31.9	25.6	1.27
1-3 children	26.3	20.1	0.98	25.2	19.0	0.94
4 or more children	64.2	58.1	2.82	65.0	58.8	2.91

\* The concentration index refers to the net income.

\*\* The category of "Jews" also includes non-Jews who are not Arabs.

## 2.4 Inequality in Income Distribution in 2005/6

The opposite picture seen in recent years among the trends of inequality in economic income is also reflected in the Gini index for income distribution (Table 5). The index for **economic** income distribution went down by 0.2% between 2004 and 2005/6, whereas the index for **net** income distribution went up by 2% during the same period. The picture is even sharper in comparison to the previous year, 2003: the index decreased by 0.8% relative to the economic income, and increased by the sharp rate of 5.1% relative to net income.

**Table 5: Gini Index of Inequality in Income Distribution, 1999-2005/6**

	Before transfer payments and direct taxes	After transfer payments only	After transfer payments and taxes	Percentage of decrease stemming from transfer payments and taxes
<b>Total population</b>				
2005/6	0.5224	0.4360	0.3874	25.8
2005	0.5225	0.4343	0.3878	26.2
2004	0.5234	0.4300	0.3799	27.4
2003	0.5265	0.4241	0.3685	30.0
2002	0.5372	0.4312	0.3679	31.5
1999	0.5167	0.4214	0.3593	30.5
<b>Change in Gini Index (%)</b>				
2005/6 compared to 2005	-0.6	0.4	-0.1	
2005/6 compared to 2004	-0.2	1.4	2.0	
2005/6 compared to 1999	1.1	3.5	7.8	

The continued implementation of the tax reform and the continued erosion in most benefits paid by the NII had a stronger impact than did developments in the opposite direction, such as the expansion of employment, wage rises, the lowering of NII dues to low-wage earners and the raising of pensions to the elderly. Overall, the changes led to an additional decline in the contribution of the transfer payments and direct taxes to a reduction of inequality in economic income distribution, from 31.5% in 2002 to 27.4% in 2004 and to 25.8% in 2005/6.

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