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STAMP TAX IN ISRAEL

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INTRODUCTION

The stamp tax typifies the Israeli economy: professionals agree that the stamp tax is anachronistic and should be abolished; yet, the government refuses to cancel the tax. This is also characteristic of the Israeli economy generally: there is wide agreement as to which reforms are needed, especially with regard to reducing the tax burden, yet the reforms are not implemented.

In addition, political parties from both the Right and the Left still cling to the socialist attitudes that were prevalent following the establishment of the State. The inevitable consequence is a heavy tax burden which reached 41.4 percent of the gross national product (GNP) in 1998.¹ Of the total tax burden faced by the beleaguered Israeli tax payer, the stamp tax represents but a small part of a much larger problem. But, it is typical in that there are many layers of wasteful and inefficient taxes imposed by a system bent on creating government revenue through taxation.

The stamp tax is levied on various documents specified by law, at rates of between 0.1 and 3 percent of the value stated in the document. In 1998, revenues from the stamp tax totaled \$203 million constituting 0.5 percent of tax revenues and 0.2 percent of GNP.²

This study describes past and present government policy regarding the stamp tax and its effects. The study is comprised of three parts: part one describes the stamp tax and presents an historical survey. Part two analyzes distortions resulting from the tax. The final section presents policy recommendations.

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SURVEY

This section includes a description of the stamp tax in its present form and a historical survey of the development of the tax in Israel. The historical survey is divided into three main periods: the first includes the Ottoman period and the British Mandate (i.e., the period prior to the creation of the State) during which the tax was first imposed. The second period is for the years 1948-1967, inclusive, and the third is from 1976 to the present day.

The Stamp Tax

As previously mentioned, the stamp tax is levied on documents at a rate of between 0.1 and 3 percent of the value of the document. Table 1 presents the principal types of documents presently requiring the payment of a stamp tax and the tax rate for each one. As can be seen from the table, the most common tax rates are: 0.4 percent for mortgages and general documents, 1 percent on the issue of securities and 1.5 percent on insurance policies:

Table 1
Principal Documents Requiring the Payment of Stamp Tax, 1999

	Document Type	Tax Rate
A	When the value is Stipulated in the Document:	
	1. Insurance contracts for ships or airplanes	0.1%
	2. Contract, memorandum, promissory note, lien and any non-transferable guarantee or obligation	0.4%
	3. Issuing of nominee shares, nominee bonds and deeds of trust	1.0%
	4. Insurance policies	1.5%
	5. Transferable guarantees or obligations	2.0%
	6. Sea freight insurance	3.0%
B	Where the value is not stipulated in the document	\$1.20

Source: Author's summary from *Stamp Tax on Documents Law*, 1961, Addition A.

It should be noted that a stamp tax is levied on the value stated in the document (for example, NIS 1 for every NIS 250 stated in the document). As a result, even though the intention is to levy 0.4 percent, this only occurs when the sum in question is NIS 250 or a multiple thereof. If the amounts stated in the document are not exact multiples of NIS 250, the actual tax rate is increased and can reach up to 0.79 percent. Thus, in the case of a contract value of NIS 251, a tax of NIS 2 must be paid (equivalent to a rate of 0.79 percent).

The stamp tax is paid in one of three ways depending upon the document type and the amount of tax to be paid. The first method is to pay at one of the Stamp Tax Offices where the document receives a special stamp upon payment. For instance, a company wishing to issue securities on the stock market is required to pay the stamp tax at the tax office. In 1998, this method of payment was used for 120,000 documents.³

The second method involves the purchase through the post office of pre-stamped guarantee notes or special stamps that are adhered to the document. A tenant for instance is required to pay a 0.4 percent stamp tax on the amount stated in the rental contract. He can make this payment using adhesive stamps on the contract. By law, this method can only be applied in cases where the amount to be paid is less than \$59.⁴ If the tax exceeds this sum, the document must be processed at the Stamp Tax Offices.

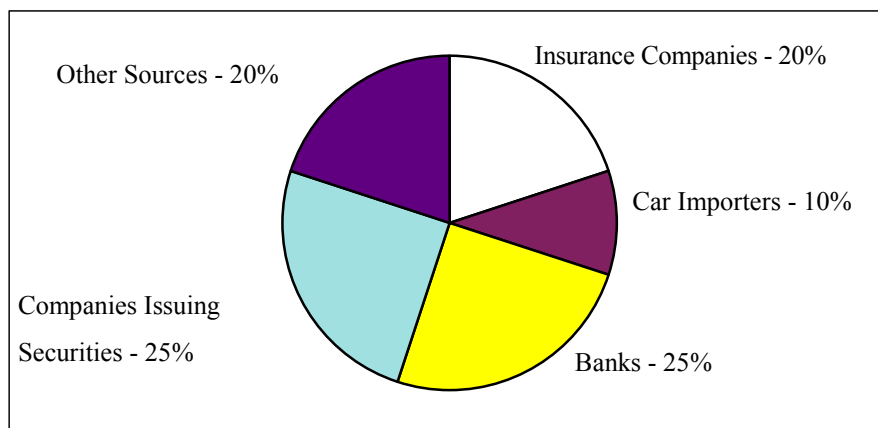
In the third method of payment, the stamp tax is included in the price of the good or service provided. In such cases, companies collect the tax and pass the funds on to the Stamp Tax Offices as part of their routine bookkeeping and tax payments. For example, an individual purchasing an insurance policy must pay 1.5 percent of its value as a stamp tax to the insurance company. The insurance company in turn transfers the funds to the Finance Ministry.

According to data of the Customs and VAT Department at the Finance Ministry, which is responsible for the collection of the stamp tax, 55 percent of stamp tax revenues is transferred directly to the Finance Ministry, 35 percent is paid through the stamping of documents at the Stamp Tax Offices and 10 percent is derived from the sale of adhesive stamps and stamped notes at the post office.⁵ It should be noted that only a small percentage of the public actually pay the stamp tax due to ignorance, lack of enforcement by the tax authorities and other factors which will be discussed below.

The law imposing a stamp tax on documents is composed of three parts: the body of the law which contains various regulations, Addition A which details the documents requiring stamping and the rates of the tax and Addition B which lists documents exempt from the tax.⁶ The law states that any document mentioned in Addition A, which was signed in Israel or signed abroad and deals with an asset or event in Israel, requires stamping. The minister of finance can initiate amendments to the Additions with the approval of the Knesset Finance Committee. Thus, the granting of an exemption or the imposition of the tax on an additional document does not require an amendment to the main body of the law with Knesset approval.

Figure 1 shows the breakdown of the revenue from the stamp tax. As shown in the figure, there are four principal sources of stamp tax revenue: insurance companies which collect a stamp tax on insurance policies; car importers which collect (since 1992) a stamp tax on the purchase contracts of new cars; the banks which collect a stamp tax on mortgages and various types of guarantees; and companies issuing shares or bonds on the stock exchange. Approximately 20 percent of stamp tax revenues come from other sources such as rental and business contracts:

Figure 1

Breakdown of Stamp Tax Revenues According to Source

Source: Data from Avi Lavon, Finance Ministry, untitled memorandum to the author on letterhead of the Economic Research and State Revenue Administration [formerly known as the State Revenue Administration], November 25, 1998. [Hebrew]

Note: Car importers began collecting stamp tax in 1992.

Historical Survey**The Pre-State Period: the Ottoman and British Mandate Periods**

The stamp tax has a long history. It was first imposed in Israel as an addition to the tax regulations during Ottoman rule; by 1894, however, it had received full legal status.⁷ The revenues from the tax were miniscule due to the unclear wording of the law, the failure to enforce it and the lack of serious penalties imposed. In 1906, the law was again amended whereby the tax would be paid in two ways: 1) a fixed sum for certain documents, and 2) a proportional tax on other documents according to the sum mentioned in the document.

In *The Tax System in Israel* published in 1933, Dr. A. Granovsky wrote the following on the stamp tax:

The 1906 law established numerous payments on all sorts of documents, all of which were a nuisance to pay....The lack of clarity in the law, the existence of two methods of payment and the large number of categories all contributed to the confusion among the public and even among tax officials. The double payment of the tax by the same business or on the same document was an almost everyday occurrence.⁸

In 1918, with the beginning of the British Mandate period in Israel, the Ottoman stamp tax was adopted. In November 1927, however, the Mandate government carried out an extensive reform with the introduction of "The Stamp Tax Regulation," which replaced the complicated Ottoman system. The reform abolished the stamp tax on many documents such as requests from the authorities, published material and invoices. In addition, each document was to be stamped only once as opposed to the many instances of double taxation in the Ottoman system. The tax rate was reduced on checks, receipts and agreements which were the most common documents.

The tax rate on other documents, however, such as rental agreements and insurance policies, was increased. From the beginning of World War II, a stamp tax was also levied on movie tickets.

It is important to note that during this period, the stamp tax was relatively important fiscally since there was no income tax or value added tax (VAT). Therefore, the stamp tax was the only tax levied on many types of businesses. The proportion of total tax revenues from the stamp tax amounted to 3.8 percent in 1926 and decreased to 2.5 percent in 1945.

The Period Since the Establishment of the State: 1948-1976

With the establishment of the State in 1948, the government of Israel adopted the stamp tax regulations from the British Mandate period. In 1954, however, the government significantly raised the stamp tax rates. Former Member of Knesset Yisrael Guri, then the chairman of the Finance Committee, explained during a discussion in the Knesset in September 1954 that the Committee had tried to ensure that the tax rate increases would be no more than five times the previous levels.⁹ The tax on insurance policies, for example, was raised by “only” twofold from 0.05 percent to 0.1 percent.¹⁰ During a discussion of the proposed legislation to increase the stamp tax in March 1954, Levy Eshkol, the minister of finance at the time, explained to the Knesset why he had decided to raise tax rates:

The existing stamp tax regulations were established in 1927. Since then, only a few changes have been made. Most of the tax rates have remained almost the same since then. Most of the categories of the tax are levied as a fixed amount on each document rather than proportionally on the value of the document. Thus, the tax must be adjusted to the changes in the value of money since 1927....While increasing the tax rates, we have at the same time moved from a fixed sum payment to a proportional tax in many cases.¹¹

During the period 1954-1961, only minor changes were made in the stamp tax. For example, in 1954, the use of pre-stamped forms was introduced in order to improve the enforcement of the tax on documents. The law determined that various documents had to be written on these forms. The attempt to introduce pre-stamped forms, however, was not successful and was later dropped.

In April 1961, the government passed “The Stamp Tax on Documents Law,” which brought together the various regulations concerning the stamp tax on documents. Interestingly, the law did not cancel the stamp tax regulations of 1927, which included the tax on entertainment and the adhesive tax stamps for requests to various government offices, but rather merely added another layer of tax legislation upon that which already existed. It should be noted that these laws, “The Stamp Tax on Documents Law” and “The Stamp Tax Regulations,” are still in force today.

Over the years, the gradual increases in stamp tax rates continued. The passing of the law in 1961 gave the government an excuse to significantly increase the stamp tax rates in addition to the technical changes that were made. In the introduction to the law, it states that one of its principal objectives is to “change the system by which the stamp tax is levied on certain documents with the goal of increasing revenues.”¹² As a result of the increase in rates in 1954 and

1961, the proportion of the stamp tax in total tax revenues increased from 0.9 percent in 1951 to 2.0 percent in 1964.¹³

In comparison to the Mandatory regulations, the main change made to the Israeli law in 1961 was in the method of collection. According to the Mandatory regulations, most documents required an adhesive stamp. The adhering of stamps on a document was to be done at the initiative of the various parties to the agreement without any intervention by the tax authorities. Consequently, the tax authorities had, and continue to have, little ability to enforce the collection of the stamp tax in this case.

Beginning in 1961, however, a stamp tax exceeding a certain amount required the stamping of the document by a special stamp at the tax offices (this amount is periodically updated and presently stands at \$59). This technical change allowed for better enforcement of the law and reduced avoidance of the tax since the parties to an agreement were forced to bring the document to the tax authorities. In order to reduce the burden on large institutions, which might be required to stamp hundreds of documents each day, the law permitted stamp machines to be used. This system became more widespread over the years and today many businesses such as insurance companies and vehicle importers stamp their documents with a special rubber stamp without having to adhere stamps. These firms collect the tax from their customers as part of the price of the goods or service and transfer the revenues straight to the Finance Ministry.

Table 2 summarizes the main events in the development of stamp tax legislation in Israel between 1881 and 1961:

Table 2

Principal Milestones in the Development of Stamp Tax Legislation 1881-1961

	Year	Description
1	1881	Stamp tax first imposed in Israel as part of the general tax regulations of the Ottoman authorities.
2	1894	Passing of new stamp tax law by the Ottoman authorities.
3	1906	Comprehensive reform of the Ottoman law.
4	1927	Stamp tax reform: the British Mandatory government passed the "Stamp Tax Law" replacing the 1906 law. Only minor changes were made in the law up until 1961.
5	1961	The Israeli government passes "The Stamp Tax on Documents Law." The Israeli legislation replaces most of the clauses in the 1927 law but does not completely abolish it.
6	1961-1999	Since 1961, a number of changes have been made to "The Stamp Tax on Documents Law" of 1961 and the "Stamp Tax Law" of 1927, although both are still in force.

Source: Compiled by the author.

In April 1966, the government once again increased stamp tax rates. For example, the tax rate on agreements was raised from 0.1 to 0.2 percent of the value of the document. The rates on notes and on similar credit documents were raised from 0.3 to 0.4 percent while the rate on invoices was raised from 0.06 to 0.16 percent. These changes increased stamp tax revenues by 47 percent during that year.¹⁴

The tax rate increases of 1966, however, did not, satisfy the tax authorities. In March 1969, the government raised stamp tax rates by between 25 and 100 percent. These changes increased stamp tax revenues by 33 percent in 1969 and by 41 percent in 1970.

1976-1999

In 1976, the government introduced VAT, which is an indirect tax levied on almost all economic activity. The introduction of VAT changed the attitude toward the stamp tax insofar as VAT was meant to replace most of the indirect taxes, including the stamp tax. Since 1976, the government has taken the position that the stamp tax is about to be abolished. Despite this, the government has not abolished the stamp tax and has only cancelled the tax on invoices, receipts and checks. This cancellation reduced the proportion of the stamp tax in total tax revenues from 1.8 percent in 1965 to 0.9 percent in 1978.¹⁵

Moshe Baraket, who was responsible for the collection of the stamp tax as director of the Customs and VAT Department from 1980-1991, wrote the following after the introduction of VAT:

Economic logic dictates that most of the indirect taxes should have been abolished, especially purchase tax and stamp tax, with the introduction of VAT. And, in fact, this was the promise made by policymakers, including the minister of finance, to the public. However, the abolishment of these taxes was only partially carried out due to budgetary constraints. For example, it was decided at least five times to cancel the stamp tax which contains numerous flaws. However, the stamp tax still exists and brings in hundreds of millions [of NIS] in revenues.¹⁶

In 1982, Yoram Aridor, then the minister of finance, decided to consolidate the stamp tax on real estate purchase contracts with the purchase tax on real estate, which is levied as a percentage of the value of the transaction. Up to that year, a stamp tax was imposed on real estate purchases at the rate of 0.4 percent of the value of the contract in addition to a purchase tax, which was imposed at various rates. The consolidation of the taxes was a natural step and eliminated a case of double taxation. The Finance Ministry, however, exploited this opportunity to increase the general tax burden. Instead of raising the purchase tax on real estate by the amount of the stamp tax (0.4 percent), it decided to raise the purchase tax by 0.5 percent.¹⁷

In 1986, the government decided to cancel the stamp tax on subsidized housing loans which are given primarily to young couples and new immigrants. However, these loans usually do not cover the cost of an apartment in Israel and the stamp tax remained on commercial mortgages at the rate of 0.4 percent.

In 1987, it appeared that the government would keep the promise it made in 1976 to abolish the stamp tax. The national unity government, which included a broad coalition of the Left and the Right, proposed a bill to abolish the stamp tax. It was stated in the introduction to the bill that the stamp tax should be abolished due to “the small amount of revenue it generates and the burden it imposes on the public.”¹⁸ Moshe Nissim, then the minister of finance, stated during a Knesset session which discussed the State Budget for the fiscal year 1987-1988 that, “The stamp tax should be totally abolished since it has no justification, economic or otherwise.”¹⁹ Adi Amorai, the deputy minister of finance at the time, stated at a Knesset session on February 3, 1987, which discussed the proposed bill to cancel the stamp tax, “[that] the tax is anachronistic and has no place in a modern economy.”²⁰

In view of the broad consensus, the Knesset approved the bill on its first reading on February 18, 1987.²¹ Following this, however, members of Knesset pushed to postpone the abolishment of the tax in exchange for not instituting a planned education fee. Using the justification of a shortfall in tax revenue, the government decided not to move forward with the proposed bill.

In 1990, the Finance Committee approved an exemption from the stamp tax upon the issuance of commercial securities. Commercial securities are defined by law to be short term bonds not linked to inflation or foreign exchange rates.²² Prior to the amendment, a stamp tax was paid on all bond issues at the rate of 1 percent of the revenues to be generated from the issue. Following the amendment, unlinked bonds, whose redemption date was between 30 days and nine months from the date of issue, were exempt from the stamp tax.²³

The government continued to hesitate on the matter of abolishing the stamp tax. In 1992, the government decided to enforce the collection of the tax on contracts to purchase new cars at the rate of 0.4 percent.²⁴ Thus, while for more than 30 years the authorities had not enforced the law on purchase contracts for new cars, the situation changed in one day. Apparently, the government could not resist the temptation to impose an additional tax, especially when there was no need for new legislation. In addition, the collection of the tax was very easy since it was to be imposed on car importers who transfer the revenues directly to the Finance Ministry. Car importers pass the cost onto the buyer and are careful to point out in their price lists that prices do not include the stamp tax. It should be noted that apart from the stamp tax, the government collects a customs duty at the rate of 7 percent and a purchase tax of up to 95 percent on new cars.²⁵

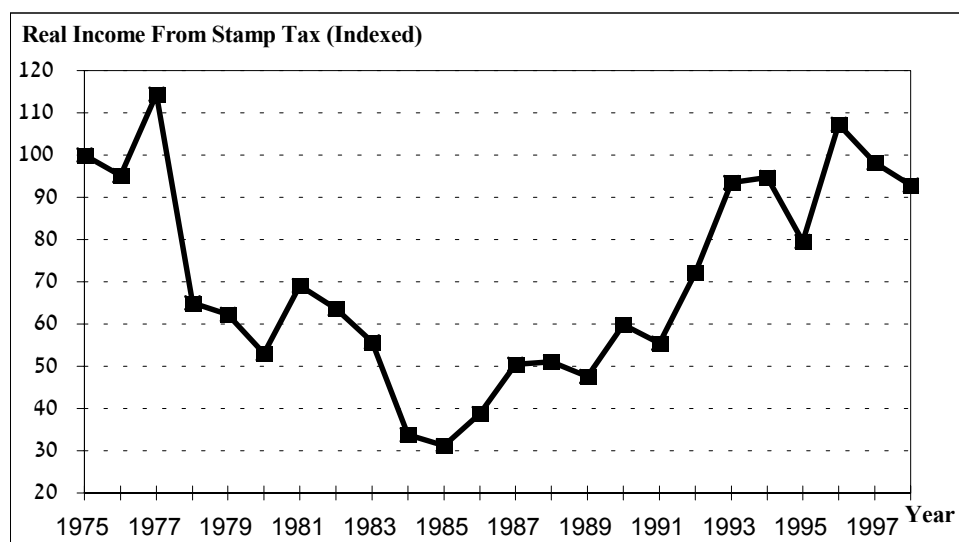
In October 1992, the attitude toward the stamp tax changed dramatically and it was almost abolished. In the proposed budget for 1993, it was stated explicitly that the stamp tax would be abolished starting from January 1, 1994.²⁶ Furthermore, the abolishment of the tax was taken into account in the forecasted tax revenues in the following years. Dr. Yoram Gabbai, then the state revenue director, stated that the stamp tax was anachronistic and should be abolished.²⁷

Before a year had passed the trend was again reversed. In July 1993, during the discussion of the 1994 budget, the government decided to reduce the planned decrease in taxes from \$424 million to only \$353 million.²⁸ As a result, the Finance Ministry cancelled its decision to eliminate the stamp tax.²⁹

Figure 2 shows the trend in revenues from the stamp tax in real terms from 1975 until 1998. The main trends, which were discussed above, can be seen clearly in the figure: first, the steep decline beginning in 1977 following the cancellation of the stamp tax on invoices and receipts after the imposition of VAT; second, a further decline following the cancellation of the stamp tax on real estate purchase contracts in 1982; third, an increase following the imposition of the tax on contracts for the purchase of new cars in 1992; and, finally, a sharp increase during the period 1985-1998 as a result of an increase in economic activity.

Figure 2

Real Income from Stamp Tax Index 1975-1998 (1975=100)



Source: Data from Avi Lavon, Finance Ministry, letter to the author, November 25, 1998. [Hebrew]

There is no shortage of good intentions when it comes to canceling the stamp tax. A few examples will suffice. In June 1998, Moti Eilon, the director of Customs and VAT and the official responsible for collecting the stamp tax, stated, in response to a demand to cancel the stamp tax on the issue of securities on the stock market, that in his opinion the stamp tax should be totally abolished but it would be difficult to abandon the tax as a source of revenue.³⁰ In August 1998, the *Ha'aretz* newspaper reported that Tsipi M. Galyam, director-general of the Economic Research and State Revenue Administration of the Finance Ministry, wrote to Member of Knesset Ophir Pines, then the chairman of the Subcommittee for Taxes, in reaction to a demand for the abolishment of the stamp tax, as follows:

For the last few years we have been planning the abolishment of the stamp tax and this will be carried out as soon as the budget situation allows.³¹

Yaakov Neeman, the minister of finance during this period, made a similar statement regarding the stamp tax, in response to Gad Soen, director-general of the Association of Tel Aviv Stock Exchange Listed Corporations:

No one disagrees that this is an outdated law which has no place in a modern tax system. Nonetheless, a shortage of fiscal revenue has prevented its cancellation until now.³²

It is clear that the theoretical view of the professionals within the Finance Ministry is that the stamp tax should be cancelled. They claim, however, that the need for sources of revenue to finance government expenditure prevents its cancellation. Table 3 shows the revenue from the stamp tax during the last few years and the relative proportion of stamp tax revenue to gross domestic product (GDP):

Table 3

**Stamp Tax Revenue in Dollars and the Proportion of the Tax
In Gross Domestic Product, 1995-1998**

	Year	Stamp Tax Revenue (Millions of Dollars)	Proportion of Stamp Tax in GDP
1	1995	166.0	0.19%
2	1996	235.6	0.25%
3	1997	217.1	0.22%
4	1998	202.6	0.21%
5	Average 1995-1998	205.3	0.22%

Source: Central Bureau of Statistics, *Monthly Bulletin of Statistics* 3 (Jerusalem: Central Bureau of Statistics, March 1999), p. 19; Data from Avi Lavon, Finance Ministry, untitled memorandum to the author on letterhead of the Economic Research and State Revenue Administration, November 25, 1998. [Hebrew]

In June 1999, the Finance Committee of the Knesset decided to exempt mortgage backed securities from the stamp tax in an effort to encourage a secondary mortgage market in Israel. It seems that decision makers were aware that the stamp tax results in a distortion of the capital market but preferred to deal only with commercial securities (in 1990) and mortgage-backed bonds rather than dealing with the issue of all securities in the capital market. It should be noted that until the granting of these two exemptions, no mortgage-backed bonds or commercial securities were issued and therefore no stamp tax was collected. Thus, these exemptions did not result in any reduction of the tax burden since these activities did not exist prior to 1999.

Stamp Tax: Exemption Policy

Over the years, numerous exemptions to the stamp tax have accumulated. These exemptions violate the concept of equality and complicate the implementation of the law. Many of the exemptions involve government documents or documents in which the government is one of the parties as well as municipal government documents. There is also a long list of exemptions whose justification is unclear. These include: the opening of a bank account, the document granting the right to travel on behalf of the government, the agreement for insuring the revenue from a foreign exchange transaction, a compromise agreement between two parties in the civil courts, a non-disclosure agreement, an agreement for leasing an airplane to fly tourists to Israel, bills of exchange or bonds issued by an agricultural cooperative, and an agreement for insuring export

cargo shipped by sea.

In addition to exemptions found in the stamp tax law itself, there are numerous exemptions in other laws. These include exemptions for the Broadcasting Authority, the Employment Service, the National Insurance Institute and the Bank of Israel.³³ Exemptions found in other laws include agreements to end work disputes, collective wage agreements, and literally dozens of other similar exemptions.

The stamp tax is a perfect example of bureaucratic discrimination since well-connected organizations can use their influence to receive an exemption. A good example of this is the exemption granted many years ago on numerous documents of agricultural cooperatives that were connected to the ruling Mapai party. And this system continues to operate today — in February 1997, a special exemption was granted on guarantees provided by the non-profit organization, “Talmud Torah,” to the “Independent Education Center” following pressure from the ultraorthodox parties in the coalition.³⁴

Summary

The stamp tax is an anachronistic tax which was introduced by the Turkish authorities 120 years ago at a time when there was no income tax or VAT in Israel. Since the establishment of the State, two main trends are evident: the first lasted until 1976, during which time the government raised the stamp tax rates a number of times. In 1976, VAT was introduced and was meant to replace most of the indirect taxes, including the stamp tax. From 1976 on, the government began reducing the stamp tax base. Checks, invoices and receipts were first removed from the tax base; subsequently, real estate purchase contracts, government subsidized mortgages, commercial securities and mortgage-backed bonds were also removed. Furthermore, numerous exemptions were granted over the years which were intended to deal with specific problems or were granted for political reasons. In the last few decades, successive governments have realized the need to abolish the tax but have never quite managed to do so.

The following section first discusses the principal distortions resulting from the stamp tax. The section then analyzes the burden on apartment purchasers and the distortions in the capital market resulting from the stamp tax.

Difficulty of Enforcement, Inefficient Administration and Outdated Legislation

The stamp tax suffers from three basic problems which are interrelated: first, the difficulty of enforcing the tax resulting in an unequal sharing of the tax burden; second, a small, yet poorly administered bureaucracy, which is charged with the collection of the tax; and third, the stamp tax legislation itself, which has not been updated for many years.

Enforcement

The stamp tax is imposed on contracts and documents which are often made without the knowledge of the tax authorities. For example, the stamp tax should be paid on a rental agreement; however, if the rent is exempt from taxes, the tax authority will not know of its existence. The collection of the tax is based primarily on Paragraph 10 of the law:

(a) A document which requires stamping but which has not been stamped, will not be accepted by a court of law, an arbitrator or any judicial authority. (b) A document as mentioned in (a) will not be accepted by any government office or government employee.³⁵

It should be emphasized that the validity of a document is not lessened if it lacks the required stamp. If the document is to be presented in a legal proceeding, however, the stamp tax must be paid.³⁶ If the stamp tax is less than \$59, the document can be stamped, in most cases, using adhesive income stamps. In these cases, if a document is not stamped and must be presented in a court of law, it can then be stamped at the original cost without linkage to inflation. Thus, in most cases, individuals don't bother paying the stamp tax on contracts until such time as it becomes a necessity.

If the amount of the tax exceeds \$59, the document must be stamped at the tax offices. Even in this case the stamp tax can be, and is in fact, avoided. If the need arises to present the document in court, it can then be stamped once a late fine and interest have been paid. Thus, the enforcement clauses of the law do not facilitate the collection of the tax, and, in the case of the lesser amount, may even hinder it.³⁷

As a result, the stamp tax is often referred to in the professional literature as a "voluntary" tax.³⁸ This situation contradicts the concept of equality in the distribution of the tax burden. For example, the Municipality of Jerusalem requests a stamped contract from landlords wishing to update them of a change in the tenancy. Many other municipalities do not have this requirement.³⁹

1. Outdated Administration of the Tax and Poor Service

In addition to enforcement problems, the administration of the Stamp Tax Offices is inefficient and outdated. For example, even though the stamp tax must be paid at these offices, they lack a cash register. Thus, in order to pay the stamp tax, an individual must first acquire a payment slip and then take it to a bank. In addition, payments are recorded by hand. As a result, the tax authorities have no way of analyzing the collection of the stamp in order to improve efficiency and draw conclusions as to the effect of the tax on the economy. Finally, since tax payments are recorded by hand, there are no clear rules specifying how payments are to be recorded and no uniformity between payments on the various types of documents.

Another related problem is the inability to put in place and to maintain audit controls, given the small number of employees in the Stamp Tax Offices (less than ten in the whole country) working manually without the efficiencies of computerized collection. The failure to conduct audits on a regular basis at the various institutions, such as the banks, which are now permitted to collect

the stamp tax on their own, raises the spectre of additional issues such as mismanagement, lack of accountability and even theft.

Furthermore, there are only five stamp tax offices in the whole country (Jerusalem, Haifa, Tel Aviv, Beer Sheva and Eilat). In order to stamp a document, an individual may have to travel a significant distance. The situation is particularly absurd if there is only a small amount of tax to be paid. The cost to the taxpayer, added to the cost of administering the tax, will likely exceed the amount of the tax itself.

The use of adhesive stamps is also inconvenient to the taxpayer since they must be purchased at a post office. In addition, the tax authorities must print these stamps and maintain an inventory.

For the past twenty years, the stamp tax has been considered to be on the brink of abolishment. As a result, the Customs and VAT Department has no intention to computerize or improve the collection of the tax.⁴⁰ One possible reason that the collection of the stamp tax has never been computerized or improved is the puzzling fact that the State Comptroller has never examined the stamp tax in its reports.

2. Outdated and Complicated Legislation

Moreover, the Stamp Tax Law is outdated and overly complex. The law relates to the type of document to be taxed rather than the type of transaction. One result is that a tax is paid on, for example, a contract even if the transaction is not completed. In 1976, the Supreme Court, acting in the capacity of a civil appellate court, ruled that: "The fact that a transaction is not completed does not require the refund of the stamp tax paid on that transaction."⁴¹

An additional problem is the complexity of the law. The rules for the payment of the stamp tax are not written clearly. On the one hand, the tax applies to almost every document, but on the other hand, there is a long list of exemptions and a list of tax rates which complicate the administration of the tax. A legal opinion is frequently required in order to decide which tax rate should be applied to a certain document.

An interesting example of the effect of the complexity of the law appeared in the *Ha'aretz* newspaper in October 1999:

The comptroller of a commercial company with bank accounts at both Discount Bank and Bank Hapoalim was surprised to discover that while a stamp tax at the rate of 0.4 percent had to be paid on a request for credit at Bank Hapoalim, none was required on a similar request at Discount Bank. It appeared that the only difference was in the titles of the loan documents. At Bank Hapoalim the document was entitled "Promissory Note for a Line of Credit." This is a legal contract and as a result the bank must collect a stamp tax for the Finance Ministry. The document at Discount Bank was entitled "Request for Line of Credit on a Checking Account." This document is not considered to be a contract but only an application. Although it may sound strange, a slight change in wording is enough to create the difference.⁴²

Furthermore, the legislation has been neglected for many years. For example, paragraph 15 of the law requires the stamping of receipts, invoices and checks. In practice, however, this is no longer done.⁴³ The state of the law has earned it some rather uncomplimentary descriptions. For example, in 1990, in an article in the journal *Taxes*, attorney Yaakov Potchebutzky describes the stamp tax as a “nature reserve” for the licking and sticking of stamps in the age of bank transfers and computerized communications.⁴⁴ In a 1991 article in the *Israeli Tax Quarterly*, Asher Arin, a Finance Ministry employee, wrote that the law is outdated and all the law should be rewritten.⁴⁵

Cost to Mortgage Owners

The purchase of an apartment is the largest single expenditure for most individuals. Despite this, the government collects a long list of taxes on the purchase, construction and ownership of an apartment. These include a purchase tax, a sales tax (which was introduced in early 1999 and was meant to replace the property tax), a property improvement tax, building taxes, municipal taxes, VAT and an income tax on rental income. To this list can be added the stamp tax in cases where a mortgage is obtained in order to finance the purchase of an apartment.

As mentioned above, the stamp tax on the purchase contract of an apartment was consolidated with the purchase tax in 1992 and no longer had to be paid separately. In most cases, however, the buyer of an apartment takes out a mortgage to finance his purchase. The mortgage contract, the required guarantee and the lien on the asset, all require the payment of a stamp tax. Thus, most apartment buyers still indirectly pay a stamp tax. The following equation shows the calculation of the stamp tax to be paid before receiving a mortgage:

Equation 1: Calculation of Stamp Tax on Mortgages

$$\begin{array}{ccccccc} \text{Official Stamp} & & \text{Monthly} & & \text{Number of} & & \text{Amount of} \\ \text{Tax Rate (0.4\%)} & \times & \text{Payment} & \times & \text{Payments} & = & \text{Stamp Tax} \end{array}$$

The monthly mortgage payment depends on three factors: amount of the mortgage, the interest rate and duration of the mortgage. Thus, mortgage owners pay a stamp tax on both interest and principal payments. Table 4 shows the stamp tax on mortgages of \$80,000 and \$100,000 with a term of 25 years as a function of the rate of interest:

Table 4

Stamp Tax on a 25-Year Mortgage as a Function of the Rate of Interest

Amount of Mortgagee (A)	Annual Interest (B)	Number of Monthly Payments (C)	Monthly Payment (D)	Official Tax Rate (E)	Pre-Paid Stamp Tax G=(CxDxE)	Actual Tax Rate (G/A)
\$80,000	5%	300	\$468	0.4%	\$562	0.70%
\$100,000	5%	300	\$585	0.4%	\$702	0.70%
\$80,000	6%	300	\$515	0.4%	\$618	0.77%
\$100,000	6%	300	\$644	0.4%	\$773	0.77%
\$80,000	7%	300	\$565	0.4%	\$678	0.85%
\$100,000	7%	300	\$707	0.4%	\$848	0.85%

Source: Calculations of the author.

Note: Appendix A contains additional graphs which analyze a wider selection of mortgage amounts.

The table also illustrates, via the regressivity of the stamp tax, the absurdity of imposing taxes to help the poor. Assuming that the wealthier the buyer, the less likely he is to take a mortgage, one could make the argument that the affluent are less likely to pay a stamp tax altogether. The poor, on the other hand, have little choice but to take mortgages and end up paying a stamp tax. A similar line of reasoning dictates that the less affluent home buyer will seek a mortgage contract providing for lower monthly payments (i.e., resulting in higher interest payments) than his wealthier counterpart for the same mortgage. In such a case, the poorer home buyer pays a higher stamp tax.⁴⁶ Appendix A illustrates this point: when the payment period of the mortgage is extended, and therefore the amount of the monthly payments are reduced and made more affordable, the greater the stamp tax that is paid. *In other words, the result is an inverse relationship to wealth: the poorer one is, the greater the likelihood that he will pay a higher stamp tax on his mortgage contract.* This viscous cycle is typical of government policy in Israel. In order to finance a socialist economy, taxes are imposed, which, first and foremost, hurt the poor, who are the very people the socialist policy was meant to help.

According to data from the Ministry of Housing and Construction, the average price of an apartment in Israel stood at \$160,000 in 1998.⁴⁷ Thus, on the assumption that the average mortgage ranges from \$80,000-\$100,000, the average individual taking a mortgage will pay between \$562 and \$848 in stamp tax immediately upon receiving the loan. In other words, the average Israeli who takes out a mortgage works more than two weeks in order to pay the stamp tax.⁴⁸

Young Couples and Low-Income Families

As indicated above, the stamp tax hurts the poor and young couples by increasing the cost of a mortgage. In order to analyze this phenomena, one can examine, on the one hand, the effect of the stamp tax on the cost of a mortgage and, on the other hand, the subsidization of mortgages by the government.

Table 5 shows the gross rates of financing and subsidization for government subsidized mortgages according to the main groups of eligible mortgage holders:

Table 5
Rates of Financing and Subsidization for Subsidized Mortgages, 1998

Ratio of Subsidization of Government Mortgage to Price of Apartment	Percentage of Apartment Price Financed by Government Mortgage	Eligible Group
3.0%	13.9%	Young Couples – Minimal Eligibility
14.6%	31.1%	Young Couples – Maximum Eligibility
7.8%	19.3%	New Immigrants

Source: Bank of Israel, *Annual Report 1998* (Jerusalem: Bank of Israel, March 1999), p. 250. [Hebrew]

Note: The rates of financing and subsidization are in relation to a 2.5-3 room apartment.

In order to compare the government subsidization of mortgages to the stamp tax imposed on commercial mortgages, it is necessary to calculate the ratio of the stamp tax to the apartment price. Table 6 shows the proportion of the stamp tax to the apartment price as a function of the ratio of the mortgage to the apartment price, the range of interest rates normally charged and the term of the mortgage. As the table shows, the rate of stamp tax as a percentage of the apartment price ranges from 0.3 to 0.5 percent.

Table 6
**The Rate of Stamp Tax as a Percentage of the Apartment Price
As a Function of the Mortgage Conditions**

Percentage of Mortgage within Apartment Price	6% Interest		7% Interest	
	20 Years	25 Years	20 Years	25 Years
40%	0.28%	0.31%	0.30%	0.34%
50%	0.34%	0.39%	0.37%	0.42%
60%	0.41%	0.46%	0.45%	0.51%

Source: Calculation of author.

Note: The numbers are the percentages of the stamp tax in relation to the apartment price. The calculation involves multiplying the actual rate of the stamp tax in relation to the rate of the mortgage (calculated in a similar manner to the numbers in Table 4) by the relative proportion (in percentage terms) of the mortgage to the apartment price.

Table 7 presents the net offset resulting from the government subsidization of mortgages, on the one hand, and the imposition of a stamp tax on commercial mortgages, on the other:

Table 7
Rate of Offset in Stamp Tax Revenue Due to The
Subsidization of Mortgages, 1998

Group	Ratio of Stamp Tax to Price of Apartment (A)	Ratio of Government Mortgage Subsidization to Price of Apartment (B)	Offset of Mortgage Subsidization Resulting from Stamp Tax C=(A/B)
1	0.3%	3.0% (Minimum Eligibility)	10.0%
	0.3%	7.8% (New Immigrants)	3.8%
	0.3%	14.4% (Maximum Eligibility)	2.1%
2	0.4%	3.0% (Minimum Eligibility)	13.3%
	0.4%	7.8% (New Immigrants)	5.1%
	0.4%	14.4% (Maximum Eligibility)	2.7%
3	0.5%	3.0% (Minimum Eligibility)	16.7%
	0.5%	7.8% (New Immigrants)	6.4%
	0.5%	14.4% (Maximum Eligibility)	3.4%

Source: Calculation of author

Note: Data on subsidization are those of the Bank of Israel (see Table 6 above).

The table shows that between 10 and 16.7 percent of the basic mortgage subsidy for those who meet the minimum eligibility returns to the government in the form of a stamp tax. In the case of maximum eligibility, the government receives between 2.1 and 3.4 percent in return. It should be noted that the majority of young couples are eligible for the basic minimum mortgage subsidy and they are the most hurt by this policy.

The following example highlights the influence the stamp tax has on a typical young couple in Israel buying an average apartment costing \$150,000:

1. The net gain to the apartment buyers from the state-subsidized mortgage will be a maximum of 3% of the apartment's value (see Table 5 above), or \$4,500.
2. The cost of the stamp tax on the commercial mortgage (on principal of approximately \$90,000, and interest), is approximately \$765.
3. Thus, in this example, approximately 17 percent of the state subsidy is taken from the recipient by the government in the form of the stamp tax.

The absurdity of subsidizing mortgages while at the same time collecting a stamp tax on those mortgages is demonstrated by Finance Ministry data. The budget for housing assistance in 1999 amounted to \$1.85 billion.⁴⁹ In other words, a reduction of 1 percent in the budget for housing assistance (\$18.5 million) would be equivalent to reducing the stamp tax by 9.1 percent (\$18.5 million of the total \$203 million revenues from the stamp tax). If the stamp tax were to be abolished, the government could cut 10 percent of the housing assistance budget without reducing the subsidization for most of those eligible for mortgages.

Effect on the Capital Market

One of the principal sources of stamp tax revenue is the issue of stocks or bonds to the public. A stamp tax is paid by the issuing company at the rate of 1 percent of the revenue from a stock issue or of the nominal value of the stock, whichever is higher. The rate for a bond issue is also 1 percent.⁵⁰

The stamp tax results in significant economic distortions in the capital market. First, the cost of issuing shares or bonds in the capital market is increased by the amount of the tax. The cost of raising capital (including stamp tax) ranges from 6 to 16 percent of the funds raised depending on the company, the type of security and market conditions.⁵¹ For example, Malam Systems Ltd., a computer and information systems company, issued bonds with a value of \$6.2 million in March 1999. The cost of the issue was 6.9 percent (approximately \$430,000) of the funds raised. This cost covered underwriting, management of the issue, distribution of the bonds, commissions, stamp tax, etc. The amount of the stamp tax paid was \$62,000.⁵²

Table 8 presents the percentage of the stamp tax in the total costs of issuing stocks or bonds:

Table 8

Percentage of Stamp Tax in Total Cost of Issue

The Cost of the Issue as a Percentage of Funds Raised (A)	Stamp Tax on the Issue of Bonds or Shares (B)	Percentage of Stamp Tax in Total Cost of Issue $C=(B/A)$
6%	1%	16.6%
8%	1%	12.5%
10%	1%	10.0%
12%	1%	8.5%
14%	1%	7%
16%	1%	6%

Source: Calculation of the author.

The table shows that the proportion of the stamp tax in the cost of raising capital ranges from 6 to 17 percent. The stamp tax thus reduces the expected return on an issue which in turn reduces the firm's incentive to raise capital in this manner.

If this were not enough, issuing companies must sometimes pay the stamp tax twice as a result of outdated legislation. According to Gad Soen, director-general of the Association of Tel Aviv Stock Exchange Listed Corporations, the stamp tax imposes an additional cost on companies seeking to raise capital in the stock market.⁵³ For example, there is double taxation on the issue of convertible bonds.⁵⁴ In this case, the issuing company pays the stamp tax twice: first, when issuing the bond and again when the bonds are converted.

Double taxation is not just a theoretical possibility as the following example demonstrates: Supersol Ltd., issued convertible bonds and paid a stamp tax on the deed of trust. At a later stage, the bonds were all converted into shares. Supersol requested an exemption from the stamp tax on the share allocation report from the District Court of Tel Aviv. The court issued its verdict in May 1998 turning down Supersol's request.⁵⁵

In light of this problem, the Knesset Finance Committee approved in October 1999 a Finance Ministry proposal that in tandem with an increase in the taxation of uninsured bonds from 0.4 to 1 percent, the double taxation of convertible bonds would end. As of today, no regulations have yet been published making this official. It is noteworthy that even in cases where the need is obvious to fix a law and to end double taxation, this is accomplished only after a different tax has been raised.

An additional example of the arbitrary distortion in the capital market is the fact that the stamp tax must be paid at the rate of 1 percent of the nominal value of bonus shares, even though these shares often do not raise any funds for the company.⁵⁶

Apart from the direct costs to firms raising capital in the stock market, the stamp tax causes distortions to the economy as a whole. One example is the differential between interest paid by the banks on saving deposits and interest charged by the banks on loans. From the viewpoint of the economy as a whole, the issue of stocks or bonds in the capital market is a substitute for taking a loan from the bank. Thus, when the alternative of issuing bonds is more expensive as a result of the stamp tax, the banks can allow themselves to increase the differential between saving and lending rates at the expense of the public. In other words, the stamp tax reduces the investment alternatives available to the public on the one hand and reduces the borrowing alternatives of commercial companies on the other.

Furthermore, the capital markets in Western countries constitute an important factor in economic growth since it efficiently brings together borrowers and lenders, and forces the banks to compete with the bond market.⁵⁷ However, in Israel the stamp tax discriminates against the capital market by increasing the costs of issuing securities. The Israeli legislature understood this problem and in 1990 created an exemption from the stamp tax on short-term unlinked bonds. In 1999, an additional incentive was created for the issue of these bonds in the form of a reduction in the requirements regarding the prospectus required for a bond issue.⁵⁸ Using similar logic, the cancellation of the stamp tax will increase the financing alternatives for firms and the competitiveness of the financial markets in Israel. In turn, this should lead to the reduction of the lending interest rates and to an increase in the savings interest rates.

The stamp tax also works in the government's favor: while the private sector must pay the high costs of the prospectus and the stamp tax when issuing securities, the government is exempt. The result can be seen in the government's dominance in the issue of bonds during the years 1991-1998:

Table 9

**The Issue of Bonds on the Tel Aviv Stock Exchange
(Millions of Shekels), 1991-1998**

Year	Corporate Bonds (A)	Government Bonds (B)	Total Bonds C=(A+B)	Percentage of Government Bonds in Total D=(B/C)
1991	755	25,212	25,967	97%
1992	711	23,326	32,743	97%
1993	795	12,724	13,519	94%
1994	33	18,159	18,192	100%
1995	0	20,013	20,103	100%
1996	56	29,728	29,784	100%
1997	1,384	19,459	20,843	93%
1998	2,341	26,548	28,890	92%
Total	6,074	175,170	181,245	97%

Source: Calculation of the author based on data from: Tel Aviv Stock Exchange Ltd., *Annual Summary 1998* (Tel Aviv: Tel Aviv Stock Exchange Ltd., 1998), p. 23. [Hebrew]

Note: All figures are expressed in terms of December 1998 price levels.

Personal and Corporate Income Tax

A not insignificant portion of the revenues from the stamp tax is cancelled out by the reduction in revenue from income and corporate taxes since in most cases the stamp tax is a deductible expense for businesses. At present, corporate tax rates stand at 36 percent while non-incorporated businesses can pay up to 50 percent.

For example, if a company rents a building, it will pay a stamp tax of 0.4 percent of the amount stated in the contract. This amount is considered part of the cost of rental when the profitability of the company is calculated. The cost of rental is a deductible expense and thus reduces the company's tax payments. Thus, the payment of the stamp tax reduces the government's revenues from corporate income tax.⁵⁹ The following equation presents the savings on corporate taxes as a result of the payment of stamp tax on rental contracts:

Equation 2: Reduction in Personal/Corporate Income Tax Revenues as a Result of the Deductibility of the Stamp Tax on Rental Contracts

$$\begin{array}{ccccccc}
 \boxed{C} & = & \boxed{B} & \times & \boxed{\text{Tax}} & \times & \boxed{A} \\
 \\
 \boxed{\text{Percent of Stamp Tax Revenues Offset by Reduction in Personal/Corporate Income Tax}} & = & \boxed{\text{Percent of Stamp Tax Revenues From Rental Contracts}} & \times & \boxed{\text{Rate of Personal/Corporate Income Tax}} & \times & \boxed{\text{Percent of Companies in Revenue of Stamp Tax}}
 \end{array}$$

In a similar manner, the deductibility of the stamp tax on other corporate expenses also reduces income tax revenues. These include insurance expenses, the stamping of bank loans and guarantees, the purchase of vehicles and regular business contracts.⁶⁰

In August 1998, Yoram Blizovsky, managing director of the Manufacturers Association of Israel, claimed that the stamp tax reduces corporate profits by up to 10 percent in certain cases.⁶¹ Even if this claim were only true for a few cases, it still demonstrates the effect of the stamp tax on taxable profits.

Since the collection of the stamp tax is not computerized, exact figures are not available to calculate the offset of stamp tax revenues by the reduction in personal and corporate income tax. However, it is clear that this offset is a reality. An individual generally pays stamp tax only on the purchase of a new vehicle or insurance policy and when taking a mortgage. Corporations also pay the tax on business contracts and the issue of securities on the stock exchange. Based on the breakdown of revenues in Figure 1, the proportion of stamp tax revenues from corporations which is tax deductible can conservatively be estimated at 40 percent. Table 10 presents an estimate of the offset:

Table 10
Percentage of Stamp Tax Offset by Reduction
In Personal/Corporate Income Tax

Percentage of Stamp Tax Revenue which is Deductible A	Corporate Tax and Average Income Tax Rates B	Percentage of Stamp Tax Revenues Offset by Reduction in Personal/Corporate Income Tax C = A x B
40%	36%	14.4%
50%	36%	18.0%
60%	36%	21.6%

Source: Calculation of the author.

Note: The calculations assume that the average tax rate is 36 percent (equal to the average corporate tax rate).

The table shows that the rate of offset is dependent on the proportion of companies paying a stamp tax. As this proportion increases, the offset against income tax revenues also increases. This offset is good from the point of view of the business sector because it reduces the total taxation on a single stream of income. This offset, however, also illustrates the folly of retaining the stamp tax since it complicates the tax system. According to the above table, between 14.4 and 21.6 percent of the revenues from the stamp tax are offset by the reduction in personal and corporate taxes. In other words, the offset in stamp tax revenues amounts to between \$29 million and \$44 million (out of a total \$203 million collected).

Summary

The analysis has shown that it is difficult to collect the stamp tax and most individuals do not pay it at all. Furthermore, the collection of the tax is carried out inefficiently without a computerized database and with a low level of service to the taxpayer. The distortions to the economy include the increased cost of issuing securities on the stock exchange and the reduction of alternatives for saving and borrowing. In many cases, the tax is offset by the subsidization of mortgages or the reduction in personal and corporate income tax revenues.

RECOMMENDATIONS

As discussed at length in this paper, the economic community in Israel long ago declared the stamp tax to be anachronistic and lacking economic justification. In addition, policymakers promised to cancel the stamp tax following the introduction of VAT in 1976. However, successive Israeli governments have evaded the moral obligation to do so.

The tax most affects young couples, new immigrants, and the less affluent who take out mortgages to finance the purchase of an apartment. From this point of view, the tax is very regressive. In addition, the tax distorts the capital market by reducing the financing alternatives available to firms. In this manner, the tax raises the rate of interest in Israel.

1. Cancellation of the Stamp Tax

In view of the above analysis, the unavoidable conclusion is that the stamp tax must be cancelled. For many firms in Israel, the cancellation of the tax will be equivalent to reducing the interest rate and will increase their financing alternatives. This in turn will encourage growth. The cancellation of the tax will benefit individuals seeking to borrow money from the banks and will strengthen the capital market. In addition, there will be a reduction in bureaucracy and less time will be wasted in paying the tax.

2. Reduction in Government Expenditure

As discussed above, government revenues will not decrease by the full amount of the lost stamp tax revenues due to the offset in income taxes of between 14 and 22 percent. In addition, cancellation of the stamp tax will allow the stamp tax bureaucracy to be eliminated.

Along with the offset in income taxes, the cancellation of the stamp tax will allow the government to reduce the amounts of subsidized mortgages. This can be done without hurting those groups eligible for subsidized mortgages. On the one hand, subsidization of mortgages will decrease, but on the other hand, the public will not have to pay the stamp tax on commercial mortgages. Today, the ironic result is that the less affluent homebuyers, seeking lower monthly payments on relatively large mortgages, will pay a greater stamp tax than their wealthier counterparts.

The conditions are ripe for carrying out this reform: the minister of finance, Avraham Shohat, presented a private member's bill in 1991 which would have cancelled the stamp tax. In the proposed bill, he wrote:

The stamp tax is outdated and its cancellation was first proposed three years ago by the government. The tax is essentially voluntary and involves a complex and inflated bureaucracy.⁶²

This reform will eliminate an anachronistic tax which causes significant distortions to both the individual and the economy as a whole.

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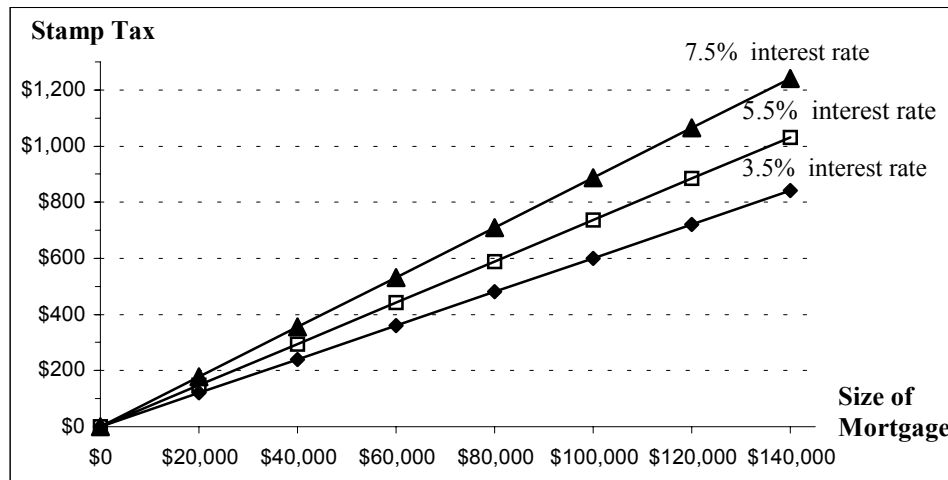
APPENDIX A

Stamp Tax on Mortgages

The stamp tax is imposed on mortgages in Israel at the rate of 0.4 percent. This is one of the main sources for stamp tax revenue. Figure 3 shows the amount of tax paid on a 25-year mortgage as a function of the interest rate and the size of the mortgage. As shown in the figure, the amount of the stamp tax increases with the interest rate and the size of the mortgage.

Figure 3

The Stamp Tax on a 25-year Mortgage
As a Function of Interest Rate and Size of Mortgage

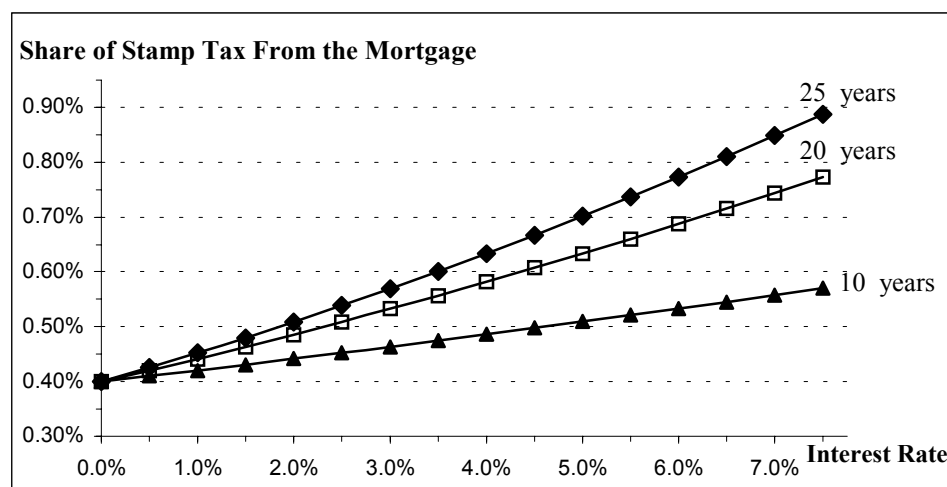


Source: Calculation of author.

The fact that stamp tax is paid on both the principal and interest payments means that the actual rate of the stamp tax is greater than the official 0.4 percent rate. Figure 4 presents the actual rate of stamp tax as a function of the interest rate and period of the mortgage. The figure shows that the stamp tax rate increases with the interest rate and period of the mortgage. The actual rate of the stamp tax can reach up to 0.9 percent which is more than double the official rate. As shown in Table 4 in the analysis, the actual stamp tax rate is not a function of the amount of the mortgage:

Figure 4

Stamp Tax Rate as a Function of the Interest Rate and Period of the Mortgage



Source: Calculation of author.

NOTES

¹ Bank of Israel, *Annual Report 1998* (Jerusalem: Bank of Israel, March 1999) p. 289. [Hebrew].

² Naphtali Grayevski, national stamp tax supervisor, letter to the author, April 8, 1999. [Hebrew] The tax revenue proportion of GNP was calculated using data from the Bank of Israel, *Annual Report 1998*, p. 289. The revenue was calculated according to the average dollar exchange rate in 1998: NIS 3.8002 to the dollar.

³ Grayevski, letter.

⁴ The sum of NIS 216 is correct for July 1988. It is updated twice annually according to the increase in the price index. The sum was converted into dollars according to the exchange rate of July 1, 1988, which was NIS 3.665 to the dollar.

⁵ Grayevski, letter.

⁶ *The Stamp Tax on Documents Law, 1961*. [Hebrew]

⁷ The survey of the pre-State period is based on the following sources:

- 1) Dr. A. Granovsky, *The Tax System in Israel: A Historical Survey* (Jerusalem: The Economic Department of the Jewish Agency in Israel, 1933), p. 253-61. [Hebrew]
- 2) Avraham Mandel, ed., *The Development of Taxes in Israel: A Historical Survey* (Jerusalem: State Revenue Administration, 1968), p. 260-69. [Hebrew]

⁸ Granovsky, *The Tax System in Israel*, pp. 254-255.

- ⁹ *Knesset Records*, 2nd Knesset, 3rd sess., p. 2656. [Hebrew]
- ¹⁰ *Amendment to Stamp Tax Regulations, 1954*. [Hebrew]
- ¹¹ *Knesset Records*, 2nd Knesset, 2nd sess., p. 1163. [Hebrew]
- ¹² State of Israel, *Proposed Legislation 1961*, no. 453, p. 149. [Hebrew]
- ¹³ Mandel, *The Development of Taxes in Israel*, p. 262.
- ¹⁴ See: *Directive for the Stamp Tax on Documents (Addition A)(Amendment no. 3)*, 1966. The directive was published in *Collected Amendments 1863*, April 1, 1966, p. 1701. [Hebrew]
- ¹⁵ The survey of the period 1964 to 1978 is based on: Moshe Danziger, “Stamp Tax on Documents During the Years 1964-1978,” *Israeli Tax Quarterly* 44 (Jerusalem: Museum of Taxes Publications – State Revenue Administration, 1980), pp. 396-397. [Hebrew]
- ¹⁶ Mordechai Baraket, “VAT – A Success Story,” *Israeli Tax Quarterly* 103 (Jerusalem: Museum of Taxes Publications – State Revenue Administration, 1999), p. 11. [Hebrew]
- ¹⁷ See: *Directive for the Stamp Tax on Documents (Additions A and B)(Amendment)*, 1982. The directive was published in *Collected Amendments 4398*, September 1, 1982, p. 1571. [Hebrew]
- ¹⁸ *Proposed Stamp Tax Law (Cancellations and Amendments)*, 1987. See: *Proposed Legislation 1815*, January 27, 1987, p. 23. [Hebrew]
- ¹⁹ *Knesset Records*, 11th Knesset, 3rd sess., volume 107, p. 1508. [Hebrew]
- ²⁰ *Ibid.*, p. 1569.
- ²¹ Israeli legislation typically requires three “readings” or votes before becoming law.
- ²² Paragraph 1 in Addition B to the *Stamp Tax on Documents Law*, 1961, defines commercial securities in the following manner: “A security...traded on the Tel Aviv Stock Exchange which was issued by a company with a prospectus, being an obligation of the company to pay the security holder, not earlier than 30 days from the date of issue and not later than nine months from the date of issue, the sum of the obligation where this sum is not linked to any index or price or exchange rate.”
- ²³ Knesset Finance Committee, 12th Knesset, 2nd sess., *Protocol 259* (June 12, 1990), pp. 7-11. [Hebrew] See also: *Jerusalem Post*, June 15, 1990. In 1999, the government improved the conditions for issuing commercial securities by streamlining the relevant legislation. See: *Arrangements Law for the State Economy (Amendments to Legislation for Achieving Budgetary and Economic Policy Objectives for the Fiscal Year 1999)*, 1999, paragraph 11. [Hebrew]
- ²⁴ *Jerusalem Post*, December 31, 1991; *Jerusalem Post*, January 8, 1992; *Jerusalem Post*, January 20, 1992.

- ²⁵ State Revenue Administration, *Annual Report 1997* (Jerusalem: State Revenue Administration, August 1998), pp. 183-205. [Hebrew]
- ²⁶ Finance Ministry, *The State Budget – Proposal for the Fiscal Year 1993: Highlights of the Budget* (Jerusalem: Finance Ministry, October 1992), pp. 179, 181, 184. [Hebrew]
- ²⁷ *Ma'ariv*, October 27, 1992; *Yediot Aharonot*, November 2, 1993.
- ²⁸ The data was translated into dollars according to the average exchange rate in 1993: NIS 2.83 to the dollar.
- ²⁹ *Davar*, July 20, 1993; *Ha'aretz*, July 19, 1993.
- ³⁰ Moti Eilon, director-general of Customs and VAT, letter to Gad Soen, director-general of the Association of Tel Aviv Stock Exchange Listed Corporations, June 29, 1998. [Hebrew]
- ³¹ *Ha'aretz*, August 20, 1998.
- ³² Yaakov Neeman, minister of finance, letter to Gad Soen, director-general of the Association of Tel Aviv Stock Exchange Listed Corporations, June 29, 1998. [Hebrew]
- ³³ These exemptions stem from the definition of an authority for purposes of taxation. See: *Broadcasting Authority Law, 1965*, paragraph 30; *Employment Service Law, 1959*, paragraph 4a; *National Insurance Law (integrated version) 1995*, paragraph 38; *Bank of Israel Law, 1954*, paragraph 63. [Hebrew]
- ³⁴ *Stamp Tax on Documents Law, 1961*, Addition B, paragraph 2 (26).
- ³⁵ *Stamp Tax on Documents Law, 1961*, paragraph 10.
- ³⁶ See for example: *Rakefet, Ltd. v. Sylvian Katz and Aviva Lehrman*, Tel Aviv 196/93, *Dinim Mehozi*, Volume 26(9), p. 233. [Hebrew]
- ³⁷ Asher Arin, "The Stamp Tax Law and the Need to Change It," *Israeli Tax Quarterly* 76 (Jerusalem: Museum of Taxes Publications – State Revenue Administration, September 1991), p. 381. [Hebrew]
- ³⁸ *Ibid.*
- ³⁹ Grayevski, interview with the author, March 14, 1999.
- ⁴⁰ *Ibid.*
- ⁴¹ *Theodore Weinberg v. the State of Israel*, Civil Appeal 99/76, Supreme Court of Israel, *Verdicts* 30, (445:3), (1976). [Hebrew]
- ⁴² *Ha'aretz*, October 15, 1999.
- ⁴³ *Stamp Tax on Documents Law, 1961*, paragraph 1.

⁴⁴ Yaakov Potchebutzky, "Proposal for Abolishing the Stamp Tax," *Taxes*, March-April D(6) (1990), p. 41a. [Hebrew]

⁴⁵ Arin, "The Stamp Tax Law and the Need to Change It," p. 381.

⁴⁶ It could be argued, however, that the very affluent home buyers purchase more expensive homes, and in fact take out larger mortgages with larger monthly installment payments, thus paying a higher stamp tax. The assumption taken in the text, however, appears reasonable to the author based upon his experience in Israel.

⁴⁷ See: Ministry of Housing and Construction, *Monthly Data* (Jerusalem: Ministry of Housing and Construction – Information and Economic Analysis Department, January 1999), p. 39. [Hebrew] The original data is in NIS and relates to the price of an apartment in July-September 1998. The data was converted to dollars according to the average representative dollar exchange rate on the fifteenth of each of the relevant months.

⁴⁸ Assuming an average net wage of \$1250.

⁴⁹ This budget totals NIS 7.6 billion, of which NIS 4 billion are given as loans and NIS 3.6 billion are given as grants and subsidies. See: Finance Ministry, *The State Budget: Proposed Budget for 1999* (Jerusalem: Finance Ministry, October 1998), p. 167. [Hebrew]

⁵⁰ *Stamp Tax on Documents Law, 1961*, paragraphs 5 and 11. The stamp tax is also paid at the rate of 1 percent on the memorandum of association of a company which has equity capital and on a document for the transfer or conversion of a company's shares. In addition, the tax is applied at the rate of 2 percent on bearer shares or a bearer bond series; however, this type of issue is no longer done in Israel. See: Ben Ami Zukerman and Amikam Lavi, *The Taxation of Securities and the Capital Market in Israel* (Tel Aviv: Cherikover Publishing Ltd., 1980), pp. 51-63. [Hebrew]

⁵¹ Nati Shilo, the legal counsel for the Association of Tel Aviv Stock Exchange Listed Corporations, telephone interview with the author, February 2, 1999.

⁵² Malam Systems Ltd., *Prospectus*, February 26, 1999. [Hebrew] The data was converted into dollars at the exchange rate of March 1, 1999 which was NIS 4.046 to the dollar.

⁵³ Gad Soen, telephone interview with the author, January 25, 1999. See also: *Ha'aretz*, April 11, 1999.

⁵⁴ Convertible bonds give their owners the right to convert them into a different security of the company, usually the company's shares.

⁵⁵ A summary of the case appears in the *Israeli Tax Quarterly* 101 (Jerusalem: Museum of Taxes Publications – State Revenue Administration, August 1998), pp. 86-87. [Hebrew]

⁵⁶ See: Zukerman and Lavi, *The Taxation of Securities and the Capital Market in Israel*, p. 57.

⁵⁷ See, for example: *Ha'aretz*, June 21, 1999.

⁵⁸ See: *Arrangements Law for the State Economy* (Amendments to Legislation for Achieving the Budget and Economic Policy Objectives for the Fiscal Year 1999), 1999, paragraph 1.

⁵⁹ It is assumed that the business pays corporate income tax. If the company is not making a profit it will of course not pay tax; however, in certain cases, the company can use present losses to offset future profits.

⁶⁰ The purchase of vehicles is not fully deductible in the first year but depreciated over a number of years, as specified by the tax authorities. The offset of stamp tax revenue by the reduction in income tax, however, is still valid even if it is spread out over a number of years.

⁶¹ *Ha'aretz*, August 17, 1998.

⁶² *Balanced Tax Law*, bill proposed by Member of Knesset Avraham Shohat, 12th Knesset, July 15, 1991. [Hebrew]

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