

MIDDLE EAST & WEST ASIA

ISRAEL

UNITARY COUNTRY

BASIC SOCIO-ECONOMIC INDICATORS

INCOME GROUP: HIGH INCOME

LOCAL CURRENCY: NEW ISRAELI SHEKEL (ILS)

POPULATION AND GEOGRAPHY

Area: 21 643 km²**Population:** 8.709 million inhabitants (2017), an increase of 1.7% per year (2010-2015)**Density:** 402 inhabitants / km²**Urban population:** 92.3% of national population**Urban population growth:** 2.0% (2017)**Capital city:** Jerusalem (10.4% of national population)

ECONOMIC DATA

GDP: 333.4 billion (current PPP international dollars), i.e. 38 276 dollars per inhabitant (2017)**Real GDP growth:** 3.3% (2017 vs 2016)**Unemployment rate:** 4.2% (2017)**Foreign direct investment, net inflows (FDI):** 18 169 (BoP, current USD millions, 2017)**Gross Fixed Capital Formation (GFCF):** 20.3% of GDP (2016)**HDI:** 0.903 (very high), rank 22 (2017)

MAIN FEATURES OF THE MULTI-LEVEL GOVERNANCE FRAMEWORK

Israel is a unitary parliamentary democracy established in 1948 by the Declaration of the Establishment of the State of Israel. Israel has no formal written constitution but thirteen “Basic Laws” (and a temporary one) that were passed in 1957 to set up a legal framework. The first basic law established the parliament in 1958. It is a unicameral parliament (*Knesset*) composed of 120 members elected every four years by direct universal suffrage. The Knesset elects the President of the State in a secret vote for a single, seven-year term. The country’s prime minister is the head of government and chief executive, entrusted with the task of forming the cabinet, which is the government’s main policy-making and executive body. Following the Knesset elections, the prime minister is nominated by the President from among the Knesset members after asking party leaders whom they support for the position.

Israel has a rather centralised system of governance that is influenced by three factors: 1) British colonial Municipal Ordinances of 1934 and 1941 that are still in place, 2) socialist traditions of Israel’s early governments (1948-1977), and 3) its economic model called the “developmental state”. No major decentralisation reform or devolution of powers has officially taken place and the central government retains most of the powers and strict oversight of local government activities and finances. Bylaws and ordinances adopted by councils, as well as their budgets, are subject to approval by the Ministry of the Interior.

However, some de-facto decentralisation of political power has taken place since the 1970s, starting with the direct election of mayors and chairpersons by universal suffrage since the 1975 Law on Local Authorities, which went into effect in 1978 (“the Law on the Direct Election of Local Authorities”). Previously, they were elected by local councils from among their members. Councils members are elected on the basis of proportional representation for a five-year term. Since then, the country has aimed to improve public administration and enhance accountability, transparency and financial responsibility of local governments. In fact, the central government has gradually withdrawn from delivering and overseeing local services. Some additional responsibilities have been transferred to local governments.

TERRITORIAL ORGANISATION

2018	MUNICIPAL LEVEL	INTERMEDIATE LEVEL	REGIONAL OR STATE LEVEL	TOTAL NUMBER OF SNGS
	257 local authorities			
	Average municipal size: 33 253 inhabitants			
	257			257

OVERALL DESCRIPTION. The 257 local governments are divided into three categories: 77 municipalities, 124 local councils, and 54 regional councils. There are also two local industrial councils, which only manage industrial zones and do not have residents.

MUNICIPAL LEVEL. The status of municipalities is granted to cities with at least 20 000 inhabitants while that of local councils is reserved for towns between 2 000 and 20 000 inhabitants. Regional councils operate at the local level, bringing together settlements spread across rural areas (mainly *kibbutzim*, *moshavim* and *bedouin* villages) to unite local communities and provide local services. In regional councils, each village or community elects one candidate by a simple majority, who becomes a member of the council. In 2016, around 75% of population lived in municipalities, 15% lived in local councils and 10% in regional councils. SNGs are large by international comparison. Their average demographic size is 33 500 inhabitants vs 9700 inhabitants in the OECD. Around 30% of municipalities have fewer than 5 000 inhabitants (vs 44% in the OECD) and 3% fewer than 2 000 inhabitants (vs 28% in the OECD). Israel has 15 cities with populations over 100 000, including Jerusalem, Tel Aviv, Haifa, Rishon LeZion, Ashdod, and Petah Tikva. Four metropolitan regions have been identified (Tel Aviv, Haifa, Jerusalem, and Beersheba). To provide a more comprehensive assessment of both the resources and the economic and social needs of each local government, the Central Bureau of Statistics (CBS) defined 10 socio-economic clusters which are used by the government in the implementation of a number of policies related to local governments.

MUNICIPAL MERGERS AND INTER-MUNICIPAL COOPERATION. Several attempts have been made to reduce the number of local councils through mergers. In 2003, 23 local councils were consolidated into 11. However, in subsequent years some of these mergers were later reversed. Inter-municipal cooperation is increasingly popular. It started as a voluntary bottom-up process with the creation of the Western Galilee Cluster in 2009, under the form of “Regional cluster”. A pilot programme to establish Voluntary Regional Clusters was created in 2012 under the initiative of the Ministry of Interior, the Ministry of Finance and several civil society organisations. Subsequent legislation passed by the Knesset formalised the legal status of clusters on December 2016. In 2018, their number increased from 5 to 10, the number of associated local authorities increased from 59 to 109, and the scope of budgetary activity

increased from about USD 4.16 million to about USD 61 million. Clusters deal with responsibilities such as environmental protection, waste, veterinary services, transportation, specialised education, economic development, etc.

STATE TERRITORIAL ADMINISTRATION. Israel has six statutory administrative districts – North, South, Centre, Jerusalem, Tel Aviv and Haifa – subdivided into 15 sub-districts. Headed by an officer of the Ministry of the Interior, districts are in charge of overseeing SNGs. Other ministries also have administrative districts, but they are not statutory. Districts act solely as administrative zones delimiting national policy plans.

SUBNATIONAL GOVERNMENT RESPONSIBILITIES

The 1934 and 1941 Municipal Ordinances provided the legal framework for the local government system including a detailed breakdown of municipalities' responsibilities. This framework is, by and large, still in place today. Other regulations have been adopted since to delimit more precisely between central and local functions and provide a more robust legal framework for local government responsibilities. However, Israel does not have a comprehensive modern law on SNG functions, despite past attempts to adopt a new Municipalities Bill, especially in 2007.

Local councils' responsibilities are divided between compulsory responsibilities, devolved competences, and voluntary services. Services under the statutory responsibility of councils as specified by law concern supervision of public works within boundaries, sewerage services, sanitary services, veterinary services and more. Most responsibilities in education and social welfare are national services delegated and operated through SNGs, and their delineation is often unclear. Moreover, local councils sometimes provide additional services according to their preference and depending on their available resources, in particular in the fields of culture, recreation and environmental protection.

Over the last few years, decentralisation has occurred. For example, Amendment 101 to the Planning and Building Law (2014) contributed to giving more responsibility and discretion to SNGs in this area. Land-use planning authority was shifted to local level in 2014 to make it more efficient. By contrast, municipal water and sanitation services have been gradually transformed into corporatised utilities that are owned by local municipalities and regulated under licenses by the Israeli Water Authority (IWA). There are now 56 regional water and sanitation utilities serving 187 municipalities and local councils. 27 municipalities serving approximately 4.5% of the population remain without a corporatised water utility.

MAIN RESPONSIBILITY SECTORS AND SUB-SECTORS

MUNICIPAL LEVEL	
1. General public services	Internal administration (including tax and fees collection)
2. Public order and safety	Municipal supervision
3. Economic affairs/transport	Physical infrastructure; Roads; Development of a long-term employment strategy (since 2006); Local tourism; Municipal transport infrastructure
4. Environmental protection	Parks and public gardens
5. Housing and community amenities	Water supply and sanitation (see above); Refuse collection and disposal system; Town and land-use planning; Housing; Street cleaning and sanitation; Veterinary services
6. Health	
7. Recreation, culture & religion	Sports activities; Cultural activities (libraries, museums, arts, crafts, orchestras, choirs, theatres and similar enterprises); Youth clubs; Religious services; Recreation areas
8. Education	Construction and maintenance of schools buildings but only for pre-schools and secondary education institutions; Provision of equipment; Student registration; Schools' day-to-day operations; Informal education
9. Social protection	Social care of families in need; Elderly; Drug addicts; Social services and day care for infants (shared)

SUBNATIONAL GOVERNMENT FINANCE

Scope of fiscal data: : local government units (local councils, municipalities and regional councils), as well as approximately 180 religious councils.	SNA 2008	Availability of fiscal data: High	Quality/reliability of fiscal data : High
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GENERAL INTRODUCTION. The subnational fiscal framework is spelled out mainly in by-laws and ordinances approved by the Ministry of Interior. The characteristics of the local funding system result in strong fiscal disparities among municipalities, and it has generated a fiscal and organisational crisis in weaker local governments. To fix the imbalance between councils, an equalisation system was set up by the government. Disparities remain strong, however, primarily between SNGs that are: urban vs rural; central vs peripheral; and predominately-Jewish vs predominately-Arab.

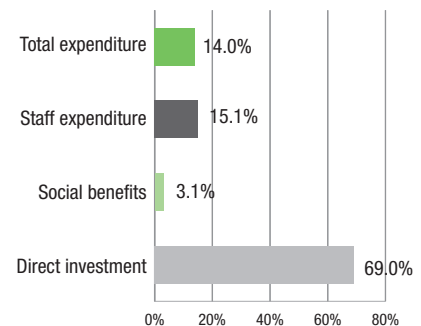
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SUBNATIONAL GOVERNMENT EXPENDITURE BY ECONOMIC CLASSIFICATION

2016	DOLLARS PPP / INH.	% GDP	% SNG EXPENDITURE	% GENERAL GOVERNMENT EXPENDITURE (SAME EXPENDITURE CATEGORY)
Total expenditure	2 062	5.5%	100%	
Incl. current expenditure	1 613	4.3%	78.2%	
Staff expenditure	574	1.5%	27.8%	
Intermediate consumption	568	1.5%	27.5%	
Social expenditure	100	0.3%	4.7%	
Subsidies and current transfers	322	0.9%	15.6%	
Financial charges	19	0.1%	0.9%	
Others	33	0.1%	1.6%	
Incl. capital expenditure	449	1.2%	21.8%	
Capital transfers	13	0.0%	0.6%	
Direct investment (or GFCF)	436	1.2%	21.1%	

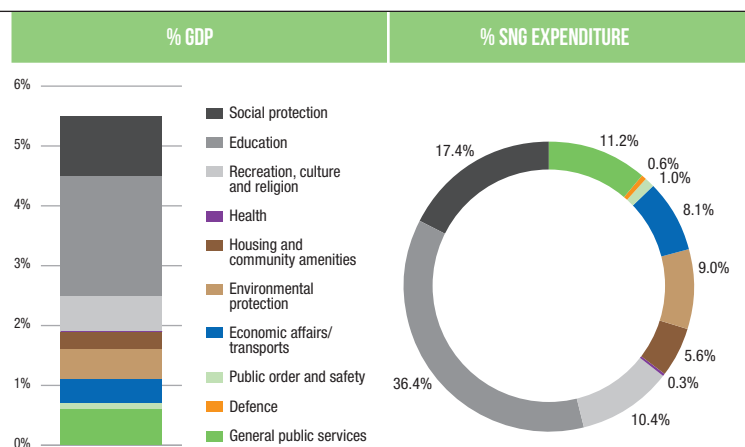


EXPENDITURE. Although some responsibilities have been decentralised, Israel remains a centralised country from the spending perspective. In 2016, SNGs accounted for 14.0% of public expenditure i.e. 5.5% of GDP, which is well below the OECD average for unitary countries (9.2% of GDP and 28.7% of public expenditure). The budgets for recurring resources and for investment are divided (ordinary and non-ordinary budgets) and managed separately, and are supplemented by their own resources. Staff expenditure accounted for nearly one-third of local expenditure and a significant part of the ordinary budget in 2016. However, local staff expenditure represented a small share of total public staff expenditure, especially compared to other OECD countries, including OECD unitary countries on average (43.0%).

DIRECT INVESTMENT. SNGs are significant public investors in Israel as investment is one of their main functions, amounting to 21.1% of local expenditure, well above the OECD average for unitary countries (13.8%). As a share of public investment, the ratio of 69% is particularly high but it does not reflect the real situation. In fact, most of central government investment is done by public companies whose investment is not recorded in the general government sector. As a result, the real extent of central government investment is under-estimated, and consequently, the share of SNGs in public investment is significantly over-estimated. This is confirmed by the low level of local investment in GDP (1.2% vs 1.7% in OECD unitary countries on average).

SUBNATIONAL GOVERNMENT EXPENDITURE BY FUNCTIONAL CLASSIFICATION – COFOG

Education is by far the biggest area of local spending, representing almost 37% of SNG expenditure, a much larger share than the OECD average of 24.8%. Local governments are also particularly active in the social protection sector, for which they also have delegated functions, like for education. Social expenditure accounted for 17.4% of their expenditure, above the OECD average (14.0%). Expenditure in economic affairs/transports and health are below the OECD average (respectively 13.6% and 18.1%). Israeli local governments are responsible for the vast majority of overall public spending in the areas of environmental protection (87% of public spending) and housing and community amenities. In most sectors, such as education and social affairs, SNGs are still subject to control by the central government and only have limited discretionary powers.



SUBNATIONAL GOVERNMENT REVENUE BY CATEGORY

2016	DOLLARS PPP / INH.	% GDP	% GENERAL GOVERNMENT REVENUE (SAME REVENUE CATEGORY)	% SNG REVENUE
Total revenue	2 092	5.6%	15.0%	
Tax revenue	923	2.5%	9.5%	44.1%
Grants and subsidies	1 004	2.7%		48.0%
Tariffs and fees	95	0.3%		4.5%
Property income	28	0.1%		1.3%
Other revenues	42	0.1%		2.0%

OVERALL DESCRIPTION. Tax revenue accounted for a significant part of local revenue in 2016, above the OECD average for unitary countries (38.7%). Consequently, the share of grants and subsidies in local revenue is slightly smaller than in the OECD unitary countries on average (48.8%). However, there are major disparities among councils and clusters, municipalities belonging to lower clusters depending significantly more on grants from the central government.

TAX REVENUE. Although tax revenues are a major source of SNG revenues, they amounted to only 2.5% of GDP in 2016 (vs 4.7% in the OECD unitary countries on average) and 9.5% of public tax revenues (vs 19.8% in the OECD unitary countries on average). The largest source of SNG tax revenue is by far the local property tax (*Arnona tax*). In 2016, it accounted for 81% of SNG tax revenue and 36% of their revenue. This tax is levied on land and buildings according to the size of the property, its location, use and age. It has two components: one for residential properties (around 44% of total receipts in 2016) and the other for non-residential properties (around 56%). Tax autonomy remains limited. Until 1985, the city council rates were autonomously determined by the local councils. In 1985, as part of the stabilisation programme, the council tax orders were suspended. They have not been reinstated, although the rate is adjusted based on CPI fluctuation, an adjustment that requires the approvals of the ministers of the Interior and the Treasury. In 1993, properties were assigned to various categories depending on how they are used. Depending on the classification, minimum and maximum rates are applied. The central government has set 13 main property categories at the national level. Each council has its own subclasses. It has the authority to change sub-classifications (i.e. the type of property) and to propose changes to specific *arnona* rates. However, both increases and decreases must be approved by the Ministers of Finance and Interior. Due to a significant imbalance in the level of tax rate between the *arnona* on residential and non-residential buildings, the property tax system is regressive and tends to exacerbate fiscal disparities among municipalities. Other tax revenues include the “betterment tax” or levy (*Hetel Hashbacha*, 13.8% of local tax revenue i.e. 6.1% of local revenue), which relates to the change in the real estate value of the property due to a land-use zoning change or the approval of additional building rights. Local government can also charge levies for the development of infrastructure in the local council.

GRANTS AND SUBSIDIES. There are three categories of central government transfers: transfers earmarked to delegated responsibilities (education and social welfare), a general balancing grant and other grants, including the new equalisation fund grant (*Arnona fund*).

Earmarked transfers for education and social welfare originate from the Ministry of Education and the Ministry of Welfare. They are granted according to the “matching” principle. In the social sector, for every service financed by the local authority, it receives 75% funding from the State. Local authorities are often unable to fund the remaining 25%, and they have to cut welfare costs at the expense of their local citizens. In the education sector, this percentage varies depending on what is being funded (on average, 85% of total spending in education comes from central transfers). The general balancing grant is designed as an equalising grant targeted to SNGs with limited amounts of own-revenues so they can meet their public service responsibilities. Individual allocation is determined annually by the Ministry of Interior, based on a complex formula. While most of the balancing grant is distributed as a block grant in support of local governments’ regular budgets, a portion of the grant (no more than 15%) is conditional on meeting certain criteria (e.g. performance in tax collection). In 2017, a new equalisation fund was implemented (*Arnona fund*) to redistribute resources derived from the property tax more equally across municipalities. Drawing on the *Arnona* paid by the central government on its own assets, the amount is set by the Law of Finances. Eligibility to the fund and distribution keys are based on criteria such as socio-economic index, lack of non-residence *arnona*, periphery index, and financial management.

Sectoral ministries also provide development grants for specific local projects such as educational and cultural facilities, roads, water and sewerage systems, as well as general development grants for projects selected by local preference. In local Arab municipalities, where fiscal disparity issues related to land are particularly sensitive, a special five-year plan has been established to support development projects and reduce disparities (Israeli Government Resolution 922 of December 2015). It includes special budgetary allocations in many sectors such as education, public transportation, road infrastructure, water and sewerage infrastructure, employment, housing and public safety. The education grant and the welfare grant made up the bulk of current grants (respectively, 56% and 21% in 2017). In addition, the general balancing grant and the equalisation fund accounted for respectively 15% and 1%; and other grants added 7%.

OTHER REVENUES. Other revenues include charges and fees for the use of local educational, social, cultural and recreational services, income generated from bylaws, etc. Local councils are also empowered to collect fees for specific services provided to residents, such as sewerage, refuse, signage or security. However, the share of user charges and fees in Israel remains particularly low compared to the OECD average for unitary countries (10.1% of local revenue in 2016). Property income derive from rent and sales of local assets (land and buildings) as well as from dividends paid by water companies.

■ SUBNATIONAL GOVERNMENT FISCAL RULES AND DEBT

2016	DOLLARS PPP/INH.	% GDP	% GENERAL GOVERNMENT DEBT	% SNG DEBT
Total outstanding debt	818	2.2%	2.9%	100%
Financial debt*	477	1.3%	1.9%	58.3%

* Currency and deposits, loans and bonds

FISCAL RULES. The Ministry of Interior is responsible for overseeing SNGs. Along with the Ministry of Finance, it approves local government budget and audits their accounts. Under the Municipalities Ordinance (Budget Preparation), local councils must be financially balanced, and if a deficit exists from previous years, the council must allocate, in the budget, the sums required to cover the deficit. Since 2014, SNGs have been classified according to fiscal wealth and budgetary performance criteria. “Stable” local governments that fulfil standards have been granted more independence from central authorities, and are exempted from obtaining approval with respect to wages, hiring, bank loans, enactment of municipal by-laws and other regular operations. As of 2018, 24 councils met these criteria. Conversely, authorities that fail to meet the standards are put under administration (the “fiscal rehabilitation” programme) and run by a state accountant. The State Comptroller and Ombudsman of Israel regularly publishes an audit report on the situation of local government finance.

DEBT. Municipalities can borrow only to finance investment projects (“Golden Rule”) but they need the authorisation of both the Ministries of Interior and of Finance. In addition, they can only borrow if their total outstanding loans do not exceed 75% of their own revenue (including grants) in any fiscal year. This does not apply to the “stable” 24 local governments. The tightening of controls on councils’ budget balance and debt led to a consistent decrease in their debt level, and to the significant improvement in their financial strength. In 2016, SNG debt was low by international standards, well below OECD average for unitary countries (14.5% of GDP and 11.8% of public debt). In 2016, the share of other accounts payable (i.e. commercial debt and arrears) was high (42%) compared to financial debt (58%). Financial debt amounted to 1.3% of GDP and 1.9% of public debt in 2016. It is exclusively composed of loans, as bonds remain negligible.



Lead responsible: OECD
Last update: 02/ 2019

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Socio-economic indicators: OECD // World Bank // UNDP // UN Desa // ILO // Central Bureau of Statistics (CBS).

Fiscal data: OECD National Accounts Statistics // OECD Revenue Statistics // OECD (2018) Subnational Government in OECD countries: key data (brochure and database) // Ministry of Finance of Israel // Central Bureau of Statistics (CBS).

Other sources of information: Ministry of Finance of Israel (2019) Sector analysis – Interior and local councils // OECD (forthcoming) Review of the local taxation system // Israel Ministry of Interior (2019) Promoting Regionalism in Israel (presentation) // Israel Ministry of Foreign Affairs (2018) - OECD (2017), Spatial Planning and Policy in Israel: The Cases of Netanya and Umm al-Fahm // OECD (2017) “Israel”, in National Urban Policy in OECD Countries // World Bank (2017) Water Management in Israel Key Innovations and Lessons Learned for Water-Scarce Countries // Oser, J., & Galnoor, I. (2016). Policy analysis evolution in Israel: Building administrative capacities. // Israel State Comptroller (2015) Regulating and Auditing Municipal Finance in Israel: Cost Efficiency and Distributional (conference presentation) // Committee of the regions (2014) Israel facts on the division of powers // Beeri I. (2013), Governmental Strategies towards Poorly-Performing Municipalities.