



FACT SHEET

(FAIR TAX MONITOR)

2019-2024

Introduction

The tax system is a financial and economic policy tool through which society's goals and objectives are realized based on its intellectual philosophy and ideology. Thus, the tax system is based on certain economic, social, and political pillars and foundations that differ from one society to another, from one country to another, and in the same country from one stage to another. Taxation has become not only a source of revenue for the state, but also a social and economic function, in addition to its traditional financial function, by becoming one of the economic tools through which economic development can be achieved, addressing inflation and stagnation, redistributing incomes, and raising the standard of living of citizens to advance the national economy in general[1].

The analytical review of the philosophy of tax systems shows that it is based on social, financial, and economic foundations. Its social function is to redistribute wealth to ensure social justice in the state, and to use tax revenues to achieve social stability and provide social services, and social protection for marginalized, vulnerable, and poor groups. Its financial function is to secure revenues for the state treasury to cover public expenditures, while its economic function is represented by the fact that it is a major tool of the state's fiscal policy, which it uses in order to stimulate economic growth, reduce inflation levels, protect the national economy, or stimulate some economic sectors, by imposing certain taxes, tax cuts, and others.

Based on these foundations and principles, the Palestinian tax system must achieve the philosophy of taxation by maximizing revenues, protecting the national economy, and, most importantly, achieving and enforcing social justice for all social groups[2]. And responding to gender issues.

[1] Al-Dahla, Samar, "Tax Systems, 2004 A Comparative Analytical Study", published master's thesis, An-Najah National University.

[2] Afaneh, Moayad "What Tax System Do We Want" 2022, article published in the Low Dialogue website, issue 7459.

In 2024, the FairTax Monitor-FTM in the Palestinian Territories was updated, complementing the previous monitor's data, which was published in 2018. The current update focuses on the years 2019-2024 and presents a set of conclusions and facts, the most important of which are:

Tax legislative framework in Palestine:

The legislative framework for taxation in Palestine is incomplete while during the 2019-2024 FMT update period, no new legislation was adopted, except for the issuance by the Council of Ministers of the Education Tax Law, No. (24) of 2021. The existing tax system is a combination of several legislations from previous periods. It lacks modern Palestinian legislation, despite the existence of several draft VAT and customs laws. Still, they have not been approved, and the Income Tax Law has not been updated and amended.

Developments since 2018: The legislative framework has not been changed other than introducing the education tax system in 2021.

The National Development Plan 2021-2023, the Public Finance Management Strategies 2021-2023, and the Reform Plan 2022 covered tax reform, as the National Development Plan 2021-2023 included policy interventions towards increasing revenues by focusing on expanding the tax base[3]. As for the sectoral strategy for public finance management, it stipulated reducing tax evasion and avoidance, modernizing and developing laws and legislation, and activating tax compliance and social justice issues in the tax system[4]. It set a target towards combating tax and customs evasion and smuggling and horizontal simplification. The Reform Agenda 2022 included reforming and implementing the Palestinian tax system, especially VAT, income, customs, and property tax and stipulated an initiative towards a comprehensive reform of the tax system, including laws, policies, procedures, and the use of technology to this end[5].

[3] National Development Plan 2021-2023 (Resilience, Disengagement and Cluster Development towards Independence), page 70.

[4] Sectoral Strategy for Public Finance Management 2021-2023, page 84.

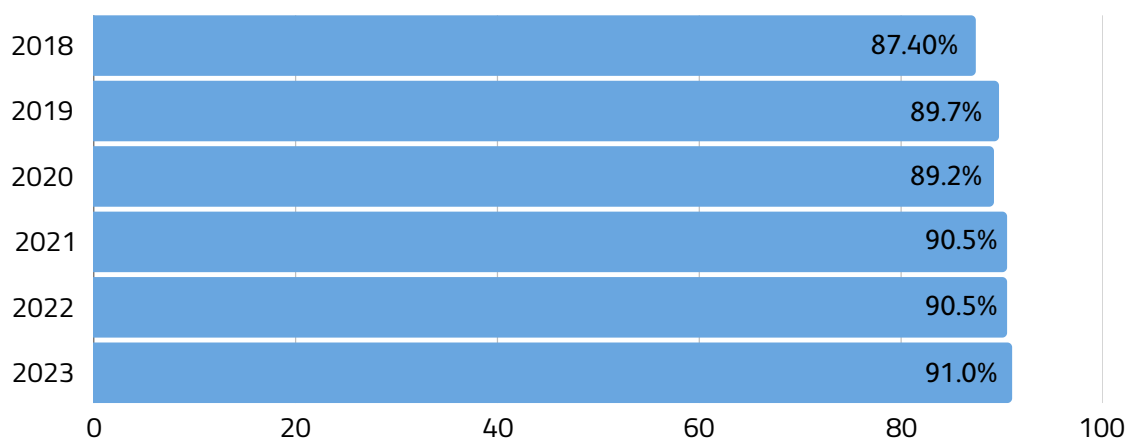
[5] Reform Agenda, General Secretariat of the Council of Ministers, 2022, page 21

Developments since 2018: The national plans, the global financial management strategy, and the government's reform plans included reforming the tax system. In practice, measures have been taken in this regard, such as shifting towards automation, identifying taxpayers who are not registered in the tax system and registering them, enhancing the effectiveness of the tax system, and combating tax evasion and avoidance. Nevertheless, no new laws have been approved, nor existing ones have been amended or modernized in a way that responds to social justice.

Quantitative Context of Taxation in Palestine

According to the data of the actual expenditure reports for the public budgets in the years 2019-2023, the reliance on self-generated revenues (local and clearing), of which taxes are the largest component, increased year after year, as net tax revenues increased from 89.7% of total public revenues (NIS 11,107.7 million) to 91% of total public revenues (NIS 16,158.9 million) in 2023.

Figure showing the evolution in the proportion of tax revenues in public revenues between 2018 and the period of the FTM update in 2019-202

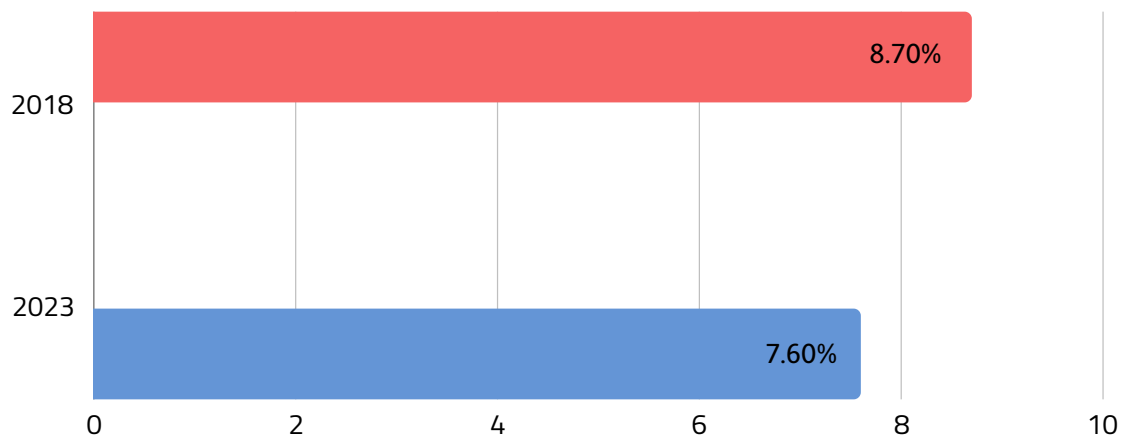


Developments since 2018: The percentage of tax revenues in total public revenues increased from 87.4% of total revenues in 2018 to 91% in 2023, indicating an increased reliance on tax revenues in Palestine.

Direct and indirect tax revenues in Palestine

The proportion of direct taxes in total tax revenues (income tax + property tax) decreased from 9.2% of total tax revenues in 2019 to (7.6%) in 2023, with a value of (986.8) million ILS in 2019 to (1,230.3) million ILS in 2023, while indirect taxes increased from (90.8%) in 2019 to (92.4%) in 2023. 3) million ILS in 2023, while the percentage of indirect taxes (customs, VAT, fuel tax, excise tax) increased from (90.8%) in 2019 to (92.4%) in 2023, with a value of (9,754.5) million ILS in 2019 to (14,920.6) million ILS in 2023.

Comparative chart of the ratio of direct taxes to total tax revenues before and after the 2018-2023 FTM update



Developments since 2018: Concerning direct taxes, their percentage decreased from (8.7%) of total tax revenues in 2018 to (7.6%) in 2023.

Through comparative data, the Palestinian tax system is currently unresponsive to gender and social justice, as it focuses on indirect taxes, which do not distinguish between rich and poor, and in the years 2019-2023, the reliance on tax revenues increased compared to non-tax revenues, and the proportion of indirect taxes increased compared to direct taxes.

Tax burden distribution and progressivity from a social justice perspective

The Palestinian tax system is unresponsive to social justice or distributing the tax burden fairly, as indirect taxes constitute the vast majority of tax revenues in Palestine, with an average of 92.2% of total tax revenues during the years 2019-2023, which are borne by the consumer, while the average percentage of direct taxes is only 7.8%.

- Customs revenues, which constitute the largest block of taxes and an average percentage during the years 2019-2024, amounted to about (39.3%) of total tax revenues, which is an indirect tax that does not fulfill tax or social justice.
- VAT revenues accounted for about (27.3%) of total tax revenues, which is a tax borne by the end user, i.e. it is passed on to the citizen without gradation or commodity categorization, depending on whether the commodity is a luxury or essential, as practiced in countries around the world, but rather a fixed tax rate on all goods and services, which contradicts social justice.
- The fuel tax, which comes in third place in tax revenues, with an average percentage for 2019-2024 amounting to (23%) of total tax revenues, is an indirect tax that does not respond to tax justice.
- Income tax, which is the most important direct tax, is a fairer tax than indirect taxes, as it is imposed on the taxpayer's income, and is not transferred to the citizen. Despite its importance, in Palestine, it represents limited revenues of only about (7.7%) of tax revenues, which contradicts the principles of social and tax justice. Especially since the personal income tax in Palestine, as part of the amendments to the Income Tax Law, has shrunk to only 3 brackets, namely (5% / 10% / 15%), while the corporate income tax rate is (15%) only, except for monopolistic companies, which reaches (20%). This is inconsistent with social justice, lacks the principle of progressivity, and is outside the global context used in calculating income tax brackets, which are progressive for several brackets up to (5-7) brackets in countries around the world.
- Corporate income tax and individual income tax, by reviewing the distribution of income tax according to its source, it is noted that income deductions constitute (45%) of the total income tax, followed by ordinary corporate income tax (33.9%), then individual tax by (11.7%), monopolistic corporate tax by (8.7%), and automobile tax by (0.8%).

The Informal Sector

The informal labor sector undermines the effectiveness and fairness of the tax system, as it is a sector that does not properly comply with laws and legislation, whether at the level of labor legislation or tax regulations, and therefore taxes are not collected from this sector as required, which negatively affects both tax collection and tax justice, and lacks a social security law to ensure social protection.

Developments since 2018: Concerning the informal labor sector, the social security law was not passed to regulate it and protect its workers, so there has been no development on this issue.

The existing tax system does not contribute to the redistribution of wealth to ensure tax justice because blind taxation burdens the poor and marginalized groups. This system does not strengthen the resilience of citizens, especially poor and marginalized groups. The same VAT rate applies indiscriminately to all goods and services whether essential, luxury, or necessary for women or children, which does not achieve gender justice and social justice in general.

Public revenue adequacy and tax leakage and their impact on social justice and inequality among citizens

Even though revenues grew significantly during the years 2019-2024, and increased from NIS 12,383 in 2019 to NIS 17,750 million in 2023, an increase of 43%, the total expenditures and net borrowing also increased and remained higher than public revenues. In 2024, revenues were estimated at NIS 13,952 million, while expenditures were estimated at NIS 17,898 million, and revenues were estimated at NIS 13,952 million in 2024. Thus, the revenues are insufficient to pay the total expenditures, especially with the Israeli deductions and withholdings from the clearance revenues since 2019, and the accumulation of the financial crisis and its postponement year after year, which accumulated the gap between public revenues and expenditures after October 7, 2023, of additional withholding and piracy of clearance revenues equivalent to the Gaza Strip allocations and the allocations of the families of martyrs and prisoners, with a monthly amount of about (300) million ILS.

Developments since 2018: The gap between revenues and expenditure persists and has deepened sharply. While the funding gap in the 2018 budget amounted to NIS 1,794 million, this gap increased to NIS 6,808 million in the 2024 budget, with the Israeli reservations and deductions from the clearance revenues.

Tax and customs evasion and avoidance, corporate tax exemptions, and the extent of governance from a social justice perspective

There are no accurate statistics on the amount of tax and customs evasion and smuggling, but some estimates indicate that this percentage reaches 40%. During the period of updating the report, the Palestinian Authority worked to launch the computerized system of clearing between the Palestinian National Authority and Israel and worked to reduce the phenomenon of tax evasion and avoidance, by increasing the number of taxpayers registered on the computerized tax system, in addition to the establishment of the Tax Risk Department to target audit files based on risk indicators.

The exemptions in the Investment Promotion Law are still unresponsive to social justice issues, as the companies benefiting from them are large corporations. The tax exemptions from income tax for the agricultural sector are good and responsive to the principles of social justice and need to ease the burden of farmers in registration procedures, to generalize the benefit of this exemption, and the tax refund for value-added tax for agricultural production is responsive to social justice, but the procedures are affected by heavy bureaucracy and delays in implementation. The procedures suffer from bureaucracy and procrastination in implementation, and the customs exemption for vehicles for charities and persons with disabilities is responsive to social justice, but the level of governance in this file is flawed, especially in exploiting customs exemptions in favor of other groups and exploiting the need of persons with disabilities.

Developments since 2018: Virtually no significant developments on the topic of tax credits for 2018

The effectiveness of the tax system.

In the years 2019- 2024, there was progress in the effectiveness of the tax system in Palestine compared to the previous period, and this was reflected in tax revenues, which reached high levels until before the war on Gaza, and tax revenues accounted for about (22%) of GDP, and strengthened the role of women in leading and working in the tax administration, however, there are challenges facing the effectiveness of the tax system, the most important of which are the lack of control over the various crossings and borders, the lack of human resources in the tax departments, weak incentives for workers in the tax departments, and the lack of logistical support, which negatively affects the enforcement of tax and social justice, and wastes tax revenues due to tax evasion and smuggling.

Developments since 2018: The effectiveness of the tax system, digitization, and the role of women in tax administration

Government Spending in Palestine and Social Justice

Government spending in Palestine has risen steadily during the years 2019-2024. Salaries and wages constitute the largest component of government spending. Moreover, the security sector is allocated the lion's share in government spending with a percentage of about (21.7%), followed by the education sector (20.3%) and the health sector (14.3%). Despite the increase in government spending in general in the years 2019-2024, spending on the Ministry of Social Development decreased, due to the reduction of cash aid payments within the CTP program from 4 annual payments to 2 payments, while the actual spending on the agriculture sector did not progress and remains within 1% of total expenditures.

Developments since 2018: There was an increase in government spending in 2019-2024, compared to 2018, as the general budget increased from (18) billion ILS in 2018 to about 21 billion ILS in 2023. However, spending on the social welfare sector, specifically the allocations for the poor, decreased from 4 payments in 2018 to 2 in 2023.

Israeli piracy of public revenues in general, and tax revenues in particular, and their impact on tax and social justice

Throughout the thirty years of the PA's existence, Israel has seized or pirated clearing revenues many times. Israel legalized the seizure of these funds in 2018 when the Knesset approved a bill to withhold amounts equivalent to the value of the financial allocations paid by the PA to the families of martyrs and prisoners, and this decision was enforced at the beginning of 2019. Following the Israeli aggression against the Gaza Strip in October 2023, deductions were made from the clearing funds in the amount of the amounts allocated to the besieged Gaza Strip and the families of martyrs and prisoners in the occupation prisons. This led to the withholding of (255) million ILS in allowances for the Gaza Strip, and (53) million ILS in salaries for prisoners, martyrs, and their families.

Israeli deductions from tax revenues under the name of Gaza Strip allocations amounted to approximately 2.55 billion ILS since the beginning of the aggression on the Gaza Strip in early October 2023 until 7/2024, an average of 255 million ILS per month, and with regard to Israeli deductions under the name of allocations for the families of martyrs and prisoners paid by the Palestinian Authority in favor of these families, the data indicated that since 2/2019 until 7/2024, it amounted to 3.48 billion ILS, an average of 53.5 million ILS per month, and Israel still withholds these funds and refuses to release them. Israel also still refuses to transfer the revenues of the Palestinian National Authority from the departure tax at the crossings to Jordan, which has accumulated for years and exceeded 900 million ILS, bringing the total amount of deductions to approximately 6.93 billion ILS[6]. Israel's piracy of tax revenues negatively affects gender issues, tax and social justice, and the availability and regularity of basic government services such as education and health services, which has negatively impacted the rights of poor and marginalized groups and the enforcement of social justice.

Developments since 2018: Before 2018, there were no regular deductions from clearing revenues, but rather detentions and releases, but after 2019, seizures and deductions were legalized, which since 2019 have amounted to about (7) billion ILS.

[6] The official Palestinian news agency "Wafa", Israel deducts about 6.93 billion shekels from the clearing funds and refuses to return them, 8/18/2024, <https://wafa.ps/Pages/Details/101649>

Key Recommendations

- Modernizing the legislative framework governing taxation to ensure that it responds to tax and social justice, and adopting the social security law as a lever for social protection, especially for the unorganized labor sector.
- Restructuring tax policies towards a focus on direct taxes, in order to promote tax and social justice.
- Adopting a progressive tax policy in the income tax, whether individual income tax or corporate income tax.
- Adopting tax policies that fulfill the principles of tax and social justice, such as tax exemptions for large families, dependents, university education, people with disabilities, and women heads of households.
- Adopting tax policies that enhance the resilience of citizens, such as tax concessions for threatened areas and the agricultural sector.
- Adopting horizontal tax expansion policies to reach out to categories and taxpayers who are not committed to paying taxes, rather than increasing tax burdens.
- Adopting a digital transformation policy in the Palestinian tax system, given its role in enhancing efficiency and effectiveness, and reducing opportunities for corruption.
- Provide the qualified human resources necessary for the work of the tax departments, whether at the level of the center or the various governorates.
- Completing the inclusion of all taxpayers on the computerized program and coordinating between the different tax departments through digital transformation.
- Combatting tax evasion and avoidance by integrating the relevant state agencies on the procedural and intelligence sides.
- Restructuring government spending by addressing the imbalance between revenue and expenditure, as the existing gap is at the expense of services provided to marginalized and vulnerable groups.

- Sparing the allocations of marginalized and poor groups from austerity plans, and secure budgets allocated to them on an ongoing basis.
- Increasing the budgets allocated to poor and marginalized groups, whether at the level of social protection systems, economic empowerment, or direct cash assistance.
- The government, in partnership with civil society organizations and the private sector, should adopt an integrated plan of action towards economic disengagement with Israel, especially in light of Israel's increasing piracy of the PA's tax revenues.
- Promoting national products through tax incentives and restrictions on Israeli and imported products to generate sufficient tax revenues to cover government spending on basic services and social justice.

Political, administrative, and financial reform, including the reform of the tax system in Palestine, cannot be achieved without an elected legislative authority, empowered by the people and capable of leading reform programs, so there is a need to hold general elections and elect a legislative authority that represents all spectrums of the Palestinian people, under the principle of separation of powers, to exercise its legislative and accountability functions. It is necessary to hold general elections and elect a legislative authority that is representative of all spectrums of the Palestinian people, in accordance with the principle of separation of powers, in order to exercise its functions of legislation and accountability.