"Proposed Reforms to the 2011 Income Tax Law and its Amendments"

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Introduction

As part of the effort by the Palestinian civil society to follow up and evaluate the taxation policy of the PA, of which the 2011 income tax law and its amendments is one of its most important components, MIFTAH, in cooperation with other partners prepared a paper at the end of 2015 to evaluate the tax law and its amendments from a socioeconomic justice perspective.

Overview:

During the discussion, MIFTAH's position paper was presented. The paper was prepared in consultation with the Civil Society Team to Enhance Public Budget Transparency and based on an analytical study conducted by MIFTAH in 2015. This was followed by an in-depth and evidence-based research that justified proposed amendments to tax brackets with the view of increasing fairness towards Palestinian citizens as taxpayers. The study included the proposed amendments to the income tax law of 2011 and the premises and justifications for these amendments with a focus on the tax brackets proposed for a more just taxation law. It also focused on tax brackets and exemptions. This law and its amendments did not succeed in achieving the required balance between the three goals (financial, economic and social). Instead it seemed that its focus was on improving the financial goal of tax collection at the expense of the other economic and social goals. Meanwhile, the tax rates and brackets remained narrow and were not sufficiently progressive. As for the special articles on exemptions and deductions on taxed income, these seemed biased in favor of the wealthier sectors of society (companies and senior taxpayers) due to exemptions and several deductions for companies, which total 11% of the profits of these companies. At the same time, the amended law granted an exemption of NIS 36,000 to individual taxpayers irrespective of the discrepancies between individual capabilities, needs and circumstances.

The paper called for making amendments to the law's articles that determine taxable income (tax base), exemptions, income deductions and tax brackets in order to improve its level of fairness.

With the view of achieving more fairness in the 2011 income tax law and its amendments, the paper suggested amending Article 7 regarding tax-exempt income, whereby Paragraph 4 would be amended, pertaining to end-of service benefits in accordance with enacted legislation whereby it does not exceed one month for every year of service and will be unconditionally exempt from taxes. This suggested amendment is justified for two reasons; the first is for conformity with the labor laws and second is the difficulty in implementing the article in its current form on taxpayers according to the opinions and experiences of legal accountants and auditors. This is in addition to granting tax exemptions for profits accrued on deposits and increasing annual exemptions to NIS 42,000 instead of NIS 36,000. It also called for cancelling Paragraph D pertaining to pensions and employee contributions to pension and savings funds; as well as Paragraph E which sets a maximum of two university students for each family for receiving university exemptions, calling for this number to be unlimited given the importance of education to Palestinian families. The paper called for granting an additional tax exemption of NIS 4,000 a year for regular taxpayers who support three or more people and NIS 2,000 for those who support a person with disability. It also called for the addition of a new article that would subject profits reaped from individual real estate transactions (sales and purchase of land and apartments) to a unified tax rate of 10 percent or three percent of the net value of the transaction.

The paper recommended that amendments be made to articles in the law that would determine taxable incomes (tax base), exemptions and deductions on income and tax brackets in order to improve the level of fairness.

The amendments propose a decrease in taxation on brackets. For the first bracket whose annual income is between NIS 1- 75,000 it proposes a decrease from the 5% in the current law to 3%; for the second bracket whose annual income ranges between NIS 75,000 and 150,000, the proposed decrease is from 10 percent in the current law to five percent. The third bracket, whose annual income ranges from NIS 150,000 and NIS 240,000, the proposed decrease is from 15 percent to seven percent. The fourth bracket, which is communications companies, monopolistic companies and individuals whose annual income ranges between NIS 240,000 and NIS 360,000, the decrease would be from 20 percent to 15 percent. A fifth bracket of 20 percent taxation should be added for those whose annual income ranges between NIS 360,000 and NIS 480,000. A sixth bracket of 30 percent taxation should be added for those whose income exceeds NIS 480,000.

The paper calls for imposing varying tax percentages among the previously mentioned brackets whereby taxes on monopolistic and holding companies would stand at 30 percent, banking and financial companies and services at 25 percent, real estate companies at 25 percent, industrial public shareholding companies at 20 percent, agricultural production shareholding companies at 10 percent, hotels and tourist companies at 15 percent and family and private companies at 15percent.

Palestinian legislators (in this case, the executive authority) took an important step in that the 2015 amendment excluded communications companies and companies that have monopolies or franchises in the Palestinian market from the tax percentage which, according to the amendment was 15 percent after they were being taxed 20 percent.

The paper also recommends that agricultural companies are exempt from paying high taxes as encouragement for land reclamation and to expand the scope of growing food security products. It is also so that the land does not remain abandoned which makes it easier to be confiscated by Israeli occupation authorities. As for other companies, monopolistic companies anywhere in the world pay taxes on profits reaching up to 35 percent except for franchise fees and rights that are renewed every five or 10 years. The same applies to the profits tax for banks and telecommunication companies; in many countries, profit taxes on banks and cellular phone companies reach 35 percent. As for real estate companies (construction and marketing), the profit margin (revenues) is high, which is why a tax of 35 percent is considered fair, as the profit margins in the real estate sector (construction) are relatively high.

Presentations and recommendations

The presentations showcased in numbers the tax structure in the PA's general budget and the relatively low share of the income tax – 4.7 percent -- in the overall revenues in comparison to other taxes, especially the Value Added Tax, whose share stands at 26.6 percent. The participants confirmed that the income tax must achieve fairness through the progressive income tax system; meanwhile the VAT is fixed and therefore does not achieve justice, especially for the poor.

The participants also pointed to the need to study the relationship between the income and Value Added Tax; the importance of expanding the number and percentage of tax brackets to achieve more fairness; to reconsider the tax system and financial policies and necessarily subjecting them to review so as to determine more just policies in light of the growing gap between high income and limited income citizens. Sociological studies have shown that one sector is growing wealthier while other vast sectors of families have become poorer at varying levels. Meanwhile, there is a small sector which has transformed into a group that lives in increasing luxury under the occupation, especially since the finance ministry's general policy is to depend on local revenues to cover public expenditures. This is a holistic policy that is not coherent or congruent even with the strategy and priorities of the government itself. The participants called on PLC members to take a stand on the general budget and tax distributions. They reaffirmed that the absence of the PLC in the current situation is a disaster, calling on political parties, factions and unions to discuss this financial policy at the grassroots level.

The presentations confirmed that the Cabinet was in violation of the law by granting itself the authority to amend taxes, pointing that this was the task of the PLC. They said the PLC must work towards addressing all of the proposed issues, stressing the importance of having a tax system that responds to the needs of the poor and includes a just redistribution of tax revenues on individuals and companies.

They also reiterated the need to adopt amendments to the income tax law that would guarantee just income redistribution and would contribute to achieving social justice, especially in light of the continued actions of the private sector towards creating a climate that further increases their wealth even if at the expense of the poor.

The representative of the Ministry of Finance indicated that the ministry launched a plan for 2017 to promote collection and to horizontally expand in order to reach new sectors and motivate taxpayers to pay.

They recommended that this policy paper be presented to decision-makers and place pressure towards its adoption, especially since a prototype has been drawn up to execute the amendments.