



The Eli Hurvitz Conference
on Economy and Society

II DALIA AND ELI HURVITZ
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Two Economies – One Society

June 19th-20th, 2017

Conference Background Materials
Research Abstracts and Project Team Summaries

Conference chair: Prof. Eugene Kandel



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Opening Remarks – Yohanan Plesner, President, Israel Democracy Institute

Greetings,

For the 24th time, the Israel Democracy Institute is holding the annual Eli Hurvitz Conference on Economy and Society (formerly the Caesarea Forum). This year, for the first time, the conference will embark on an exciting multi-year process, led by IDI and in cooperation with senior government officials, business sector representatives, academic and research institutes, as well as prominent members of Israel's civic and social sectors.

The initiative will create a continuum of joint strategic research and thinking that aims to ultimately bring about real change to Israel in specific areas.

Beginning this year, status updates regarding the progress being made by our think and do tanks will be presented at each Eli Hurvitz conference, as well as elaborated on in the published conference materials. These preliminary findings and analyses will serve as a basis for fruitful discussions, both at the conference and afterwards. This year, the various think tanks will address the central theme of the 2017 conference, *Two Economies - One Society*, about which Prof. Eugene Kandel will expand upon in the following pages.

As part of this new approach, the think tanks' research topics were incorporated into the Institute's multi-year action plan.

For example, IDI launched a working group this year, which is formulating recommendations on how Israel should best prepare for **tomorrow's labor market**. We assembled this group once we realized that without proper preparation, the changes expected to undermine the stability of regimes and democracies may actually be caused by the erosion of the existing employment model, as well as a growing fear of a sharp rise in unemployment rates around the world.

This project team, which includes representatives from a variety of government ministries, research institutes, business sector representatives and employers' representatives, began a process of mapping the challenges, conducting research and formulating strategic policy recommendations for future labor market preparations. Even after this year's conference is concluded, the team will continue its work, with

the aim of deepening the research and formulating recommendations – to be presented at the next conference in 2018.

Relatedly, the Institute launched a multi-year pension reform initiative this year that will develop recommendations for enhancing the stability and increasing the equitability of Israel's pension system.

Another multi-year project launched by IDI in 2017 aims to help government agencies **reduce the regulatory and bureaucratic burden**. Our working assumption is that an effective regulatory system increases economic resilience and strengthens the stability of our democracy. Moreover, excessive regulation and stifling bureaucracy can incentivize government corruption and thereby undermine the foundations of democracy.

This project was also incorporated into the Institute's multi-year action plan, reflecting IDI's expertise in **behavioral economics as a tool for improving government work**. The fruits of this project, developed in cooperation with relevant government agencies, will be presented for the first time at this year's conference.

We believe that the 2017 Eli Hurvitz Conference on Economy and Society is an excellent opportunity for an unfiltered, professional and productive meeting between leaders of Israel's economy from across various sectors, who will conduct an open discourse that will challenge the conventional wisdom and accepted practices.

This year will be the fifth conference that bears the name of Eli Hurvitz z"l, the founder of Teva and one of the titans of Israeli industry. Eli was the chairman of the Institute's executive committee and for many years headed the Caesarea Forum (the conference's previous name).

For us at IDI, the relationship with the Dalia and Eli Hurvitz Foundation is simultaneously special and natural. We thank Dalia and the entire Hurvitz family for enabling this important enterprise to continue and grow.

I thank all the researchers and research assistants, chairpersons of the various groups, our partners on these teams and those who put their studies to paper, plenary session chairs and the entire Israel Democracy Institute staff.

Special thanks to Prof. Eugene Kandel, Chairman of the conference.

Best regards,

Yohanan Plesner

President, Israel Democracy Institute



The Eli Hurvitz Conference on Economy and Society

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Eli Hurvitz, Z"L – A Life of Achievements

Tzofim

Bagrut

Table of Contents

Two Economies – One Society	9
The Future of Labor Market – Will There be Room for Everyone? Israel Must Prepare for Tomorrow's Job Market Today	17
The Challenges to Israel's Pension System The Association between Income and Life Expectancy – The Israeli Case Allotment of Designated Bonds in Pension Funds	23 35
Reducing the Bureaucratic and Regulation Burden Streamlining Regulation in Israel and Easing the Bureaucratic Burden – Multi-Year Program Applying Behavioral Economics to the Streamlining and Reduction of Regulation Behavioral Methods for Streamlining the Work of Government Public Attitudes in Israel towards Nudges	47 59 69 77
Credit for Small and Medium Businesses: The Key for Growth? New Options for Financing Small and Medium Businesses through the Capital Market	97



Two Economies, One Society

Introduction – Prof. Eugene Kandell, Conference Chair

Two Economies – One Society

Initial thoughts to stimulate a discussion

Dear Eli Hurvitz Conference Participant.

As Yohanan Plesner wrote to you, The Eli Horowitz Conference this year is embarking on a three-year project that will focus on long-term strategic issues of relevance to the government and the country. This process will establish a continuity of research and discussion, engage a wider set of experts, facilitate more productive interactions with the government, and showcase the intermediate results - in annual conferences that will undoubtedly spark lively debates.

We chose a unifying theme for the launch of the three-year project, **Two Economies-One Society**. The goal of this document is to shed light on this initiative's defining features, and outline the topics that will be discussed within this theme.

In general, every economy can be divided into two components: the **innovative**, which pushes the envelope of best technologies and practices worldwide, and **everything else**. While this is not a customary partition in national statistics or academic papers, I would argue that, with regards to Israel, such a categorization is not only appropriate, it is necessary. Indeed, to not to look at the Israeli economy through such a lens is to miss very important trends. As such, I maintain that Israel has two, very weakly-connected economies, which I call (for the lack of better terms) the **Innovative Economy**, and the **In-Need-of-More-Innovation Economy**.

Allow me to demonstrate why this partition is indeed reasonable in the case of Israel, and may in the future also be applicable to the rest of the world.

First, I'll begin with the **Innovative Economy**. In a variety of ways, the nature of this economy is quite cosmopolitan: its markets, main competitors, financing and reference points are all based abroad.¹ It has very high productivity and generates large amounts of wealth, attracting equally large amounts of investments. Moreover, the Innovative Economy is relatively lightly regulated, and is sometimes exempt from certain regulations. Moreover, its firms and workers are highly mobile, and, in general, members of the Innovative Economy are comfortable in cosmopolitan environments.

As result, many foreign firms and governments are willing to pay significant amounts to attract these companies and their employees. However, even without this inducement, many Israeli firms and their investors choose to move significant parts of their operations overseas, so as to be closer to key markets and sources of financing. While some of the firms do get direct government support, the firms and workers in this economy are of the mindset that they are not dependent on government largesse, and don't feel that the government is either their partner or savior. The Innovative Economy is characterized by very high salaries, due to its high productivity, and in the last two decades has been the primary source of vast wealth accumulation by a significant number of people in Israel.

There is near consensus in the government and the public discourse that Israel must become a very competitive place for this value-generating, yet mobile economy. Thus, it is regulated and taxed much more lightly than the rest of the economy. The Innovative Economy is also a source of great pride for Israelis, and a topic of great interest around the world, which makes our work at SNC - to promote Israeli innovation – that much easier.

In Israel, this economy is larger than in any other country in terms of employment rate and percentage of GDP. As a result, its macro effect on the overall economy is much higher than in any other country. Not surprisingly, when National Accounting world-wide was modified to better measure the impact of innovation on GDP, Israel's GDP rose the most. This highly diverse economy has evolved into a self-sustaining ecosystem, with many supporting institutions and norms. In the foreseeable future, Israel's Innovative Economy could become the most consistent driver of economic growth, making its share of the overall economy even bigger. At

1 This does not mean that the definition Innovative Economy is equivalent to Tradable Goods and Services. The vast majority of its products are indeed tradable (when they are successful), but definitely not all tradables are innovative.

the same time, such an outcome is not at all assured, as Israel faces strong competition from abroad, and the Innovation Economy thus needs to grow, to maintain the interest of investors and customers, as well as provide enough of an incentive for firms to stay in Israel.

The **In-Need-of-More-Innovation Economy** (For the sake of brevity, I will also use the term the **Main Economy**) is completely different. The former has a very low aggregate rate of productivity – almost 50% lower than the Innovative Economy, according to a rough estimate. Its productivity is much lower by industry comparison with other developed countries (services, construction, logistics, etc.). Much of its markets are in Israel, though it does export. The Main Economy is very local in its mindset, heavily regulated, and more heavily taxed. It depends on the government not only in terms of regulation, but also as a state of mind: if something goes wrong its managers and employees frequently blame the government and expect it to bail them out. The government, on the other hand, feels that this economy is its captive client (even when it is not), and treats it heavy-handedly. This economy pays high salaries only to members of strong unions, or to employees in monopolistic industries, while the public foots the bill. For the rest, wages are low - in accordance with productivity.

Moreover, the firms, owners and managers operating in the Main Economy are viewed by the public with suspicion, sometimes with outright hostility. Such attitudes are fueled by media campaigns and heated political rhetoric.

This economy does not generate much interest from abroad, except in rare cases when a firm may be acquired, which is difficult due to majority holdings and strong unions. However, the Main Economy's rather problematic state also represents an opportunity, and it could become a source of economic growth – should it adopt existing best practices and technologies, and increase productivity.

Clearly, these two economies are very different in practically all aspects. So, let's explore their separate trajectories.

In the last twenty years the two economies have been developing in parallel, without much interaction, but at very different speeds. The two economies have very segregated labor forces – that rarely move across the divide. Specifically, the skilled professionals comprising the Innovative Economy are predominantly highly educated/trained males from middle-class and upper-middle-class families

originating from the four metropolitan areas and a few other strong communities. Until recently, this economy included few women and people from Israel's geographic or social periphery, and practically no Haredi and Arabs. Basically, the pool of talent for this economy comes from less than 50% of the general population.

As was mentioned earlier, the two economies diverge in terms of their wages and benefits, thus contributing to an increase in economic inequality. Should such a pattern continue for much longer the majority of the Israeli population is at risk of becoming alienated. Such a development will in time translate into political intervention, higher taxation and regulation. Given that the companies in the Innovation Economy are highly mobile, broad-based feelings of alienation are a grave danger to the Israeli economy and society.

So, the first goal we must postulate is how do we stop the divergence of the two economies, so as to maintain the cohesion of **One Society**? There are two required processes: The first is to increase the percentage of people engaged in the Innovation Economy, so as to help it expand and grow, thus maintaining its relative place in the world. There is also a need to educate the public and the decision makers about the great benefits of having a growing Innovation Economy in Israel.

The second process is to change the unfortunate title of the In-Need-of-Innovation Economy, by drastically increasing its productivity. Both are required to achieve the goal of One Society. What we definitely do not want is to slow down the Innovation Economy, as such a development may catalyze a vicious cycle leading to its demise in Israel.

But while pursuing the first goal, we must realize that the two economies have completely different needs, and must be provided with distinct solutions to flourish. Recall that the aim is to allow the Innovation Economy to stay on the cutting technological edge, grow and expand, while remaining in Israel, despite the forces that are pulling at it from overseas. Meanwhile, the goal for the Main Economy is to increase productivity by adopting best practices and technologies, while reducing regulations that hinder it, and improving labor relations.

It turns out that the actions required to achieve these goals are very different in every relevant domain: Human Capital, Financing, Regulation, and Knowledge. This fact is not always understood, and while sometimes policies address the two economies specifically, in most cases regulation and legislation are applied uniformly, making it difficult to develop effective policies for both the Innovative and Main economies.

As such, the 2017 Eli Hurwitz Conference will focus on raising the issue of Israel's two economies, by presenting some of the specific challenges in each of the aforementioned domains, and addressing them in greater detail. We intend to outline the necessary conditions needed for the process to move forward – separately for each economy and for each specific area of focus. In addition, we will set up teams after the conference's conclusion that will then embark on an exciting three-year journey.

If you would like to contribute your time and expertise to a particular domain, or the task of bringing Israel's two economies together, please let us know by sending an e-mail indicating your areas of interest to Ms. Lital Zilka litalz@idi.org.il

We hope that a wide variety of relevant stakeholders will participate in this process. We are pleased to announce that representatives from the government and related agencies, such as the Prime Minister's Office, National Economic Council, Ministry of Finance, Bank of Israel, Ministry of Education, Ministry of Economy, Ministry of Labor, Ministry of Justice, Israeli Securities Authority, Central Bureau of Statistics and others will be joined by academic researchers, Employers' Association, Histadrut, and industry representatives from the two economies at this year's conference. The idea is to have everyone focus on the strategic long-term view, while simultaneously ensuring that the topics appeal to all participants. As my previous experience shows, this is doable.

I wish you a very insightful conference and hope that you will join us in preparations for our better common future.

Sincerely,

Prof. Eugene Kandel

Conference Chair

Professor of Economics, School of Business Administration, Hebrew University of Jerusalem

CEO Start-Up Nation Central



The Future Labor Market – Will There be Room for Everyone?



Israel Must Prepare for Tomorrow's Job Market Today

Outline

Team Leaders:

Daphna Aviram-Nitzan Former head of the migration research unit at Aharon Meir Center for Banking and Economic Policy at Bar-Ilan University and the former director of the economic research division at the Manufacturers Association of Israel (MAI).

Prof. Yuval Feldman Co-Director, Labor Market Reform Program; Professor Yuval Feldman is a full professor on the Faculty of Law at Bar-Ilan University and a former fellow of Institutional Corruption Lab at the Edmond J. Safra Center for Ethics at Harvard University.

Team Members:

Representative of: The National Insurance Institute of Israel; Bank of Israel; JDC Israel Tevet; Histadrut; Manufacturers Association of Israel; Central Bureau of Statistics; Knesset Research and Information Center; Samuel Neaman Institute, Technion; The National Economic Council; Prime Minister's Office; The Aaron Dovrat Institute for Economic Policy; Taub Center for Social Policy Studies in Israel; Ministry of Finance; Ministry of Economy and Industry; Social Affairs and Social Services; Millennium Project; Israeli Employment Service; Ministry of Labor

According to many experts from around the world, extensive changes are expected to take place in the labor market over the next few years. These developments stem from a combination of technological advances, demographic shifts, deepening globalization processes and perceptual changes.

As such, countries that do not prepare for these expected changes will face **real threats to the stability of their economies and governments**. Possible risks include:

- A significant increase in unemployment for populations that will not adapt themselves to the needs of the evolving market
- Lack of professional, specialized employees, which will serve as a bottleneck for economic growth
- On the other hand, a sharp rise in the salaries of in-demand skilled workers is expected
- Reduced competitiveness
- Destabilizing of relations between employers and employees
- Growing social polarization due to widening gaps between employees

However, countries' preparation for the labor market's changing needs could lead to improved competitiveness and robustness of their economies, while accelerating innovation and growth, as well as increasing employment levels.

In response, the Israel Democracy Institute (IDI) established a working group several months ago, which aims to formulate a multi-system strategic plan on the future of the labor market. The working group is in its earliest stages and is comprised of representatives from relevant government ministries (including the Ministry of Finance, Ministry of Labor, Ministry of Economy and Industry, Prime Minister's Office, Bank of Israel and National Insurance Institute), employers, employees, research centers and academia. As such, this working group is a unique forum for collaboration among major players in the Israeli labor market and has adopted an approach that takes into account the interrelationship between different facets of the labor market. These aspects include the market's needs (employers and employees) and a system to provide for those needs (training, education, labor laws, and more).

Upon completion of this initial stage of mapping and gaining a deeper understanding of the challenges ahead, the team's work will then shift to formulating operational policy recommendations in three main areas: education, training and labor legislation and regulation.

During the preliminary stage, the team identified a number of recommended courses of action, focusing mainly on vocational training, education and labor relations. Specifically, this refers to: **reducing the mismatch** between workforce supply, as provided by the education system and professional training institutions, and workforce demand, as defined by the needs of the business sector; **strengthening Israel's active labor market policy (ALMP)**, by focusing on the training of employees in their workplace, so as to enhance their job security and set of skills, while meeting the demands of the employers' changing needs; **reinforcing life-long learning (LLL)**; and arranging **flexible labor agreements** that will enhance both the employees' welfare and the employers' flexibility.



The Challenges to Israel's Pension System

The Association between Income and Life Expectancy

The Israeli Case

Abstract

Team leaders

- Prof. Eytan Sheshinski** Senior Fellow, Israel Democracy Institute, and Professor (Emeritus) of Economics, Hebrew University of Jerusalem
- Prof. Daniel Gottlieb** Deputy Director General; Research and Planning, National Insurance Institute. Baerwald School Of Social Work And Welfare.

Team members

National Insurance Institute:

- Dr. Ofir Pinto** Adviser to Director General; Director of Special Projects Unit Research and Planning Department
- Rafaela Cohen** Senior Manager Collection and Financial Sustainability Division
- Dr. Gabriela Heilbronn** Director of Research on Old Age & Survivors Pensions, & Income Support
- Miriam Schmeltzer** Head Director of Research on Old Age & Survivors Pensions, Long-Term Care, Child Support, Maternity, Income Support & Unemployment

The Israel Democracy Institute:

- Rachel Zaken** Researcher, Israel Democracy Institute

To access the complete study (in Hebrew): <https://tinyurl.com/EHC17a>



Summary

Income inequality and poverty in Israel as measured in the Household Expenditure Survey of the Central Bureau of Statistics (CBS) have increased significantly, both by international standards and historically. In recent years, there has been a decline in economic inequality (before state intervention in taxes and allowances), after peaking in 2006. However, the overall level of inequality after government intervention has not changed. Moreover, the expenditure and income surveys, while providing cross-sectional data, do not allow for analysis based on permanent income nor an examination as to the effects of ongoing poverty and inequality.

In this study, we examine the association between the level of working age income and life expectancy, based on administrative data collected over time. The population groups in this study include men born between 1930 and 1935 and women born between 1935 and 1940, whose income is identified on the basis of National Insurance Institute (NII) data. By estimating standardized and average annual incomes in the eight years prior to the formal retirement age, the study examines the association between income level and mortality rates in Israel.

The main finding of the study is the inverse relationship between income and mortality rates; the higher the level of income, the lower the mortality rate. The high mortality rates are particularly pronounced among men with very low incomes (up to NIS 175,000 a year). The findings are especially relevant to people and families living in chronic poverty, as high mortality rates and low life expectancy limit their chances of benefiting from the social security system's old age pensions, as well as pensions from the insurance companies.

Introduction

In recent decades, we have witnessed growing economic disparities around the world. In 2014, income inequality in OECD countries reached its highest level since the start of the index. The average Gini index among OECD member countries was 0.318, while the average wage among the highest decile was nine times higher than the average wage among the lowest decile. In Israel, according to OECD data, the share of the population whose income is 50% lower than the median income is the highest of all OECD member countries, and stands at 18.6%¹. Similar to the trend among OECD countries, the rates of inequality and poverty in Israel are increasing. According to the Gini coefficient for measuring inequality in income, distribution has steadily increased since the state of Israel was established, and stood at 0.365 in 2014.

Many studies are based on cumulative income data over the life of an individual and life expectancy is either calculated by the NII or the information is obtained from National Insurance files. For example, a study in the United States that examined differences in life expectancy between income groups based on region (Chetty et al., 2016) found a positive correlation between income and life expectancy, as well as sizeable national gaps that continue to widen. This study also found that the life expectancy of men in the upper percentile was 14.6 years higher than that of men in the lower percentile and that the life expectancy of women in the upper percentile was 10.1 years higher than that of women in the lower percentile.²

A similar study has not yet been conducted in Israel. However, the Bank of Israel published a report in 2016 that examined the effect of socio-economic level on health status. Among other things, the study found that the mortality rates in socio-economically 'weak' localities are 11% higher than the mortality rate in 'strong' localities.

In this study, we examine the relationship between income and life expectancy in Israel, based on National Insurance Institute data. Our research explores the gap in life expectancy that relates to economic variables as well as its development over time. An examination of these changes across the population according to income level will enable us to find out the relationship between income level and life expectancy, as well as measure the strength of this relationship via the use of regression analysis.

1 OECD, Inequality and Income; 2014 data.

2 We emphasize that differences between people according to income percentiles are more extreme and pronounced than differences between people who are divided according to quintiles of income.

The findings of our study are significant for the examination of a range of public policy issues, including the eligibility criteria for old age pension benefits and the pension model used by insurance companies. Any reforms to the pension system should be based on an examination of possible implications, taking into consideration demographic changes and shifting patterns of adult labor force participation, which may create actuarial deficits.

The Study

As part of a collaboration between the Israel Democracy Institute and National Insurance Institute, it was decided to conduct a study examining the gaps in mortality and life expectancy by economic status and the development of inequalities over time. In the future, this study could serve as a basis for more research to gain a greater understanding as to the implications of these gaps on pension and NII benefits. It will then be possible to formulate policy recommendations to reduce inequality. Our study, based on administrative data from the National Insurance Institute, examined mortality rates, changes in income distribution and shifts in the Gini coefficient, among men and women in Israel over time.

Research Population. Our research uses data of male cohorts born between 1930 and 1935, and female cohorts born between 1935 and 1940. These populations reached retirement age in the years 1995-2000 and therefore it is possible to estimate their income levels, assuming that they were of working age for at least eight years. Reliance on income data over a period of eight years is intended to overcome income level volatility over short periods, which commonly is the result of changes in employment or health status.

For this study, we used only data of people who had immigrated to Israel no later than December 31, 1989, or who had died not earlier than January 1, 1990. Neither does our research include persons identified as permanent army personnel, since the National Insurance Institute does not have complete income information about them.

The income data is based on the information available at the National Insurance Institute, and includes income from salaried and independent work of the surveyed population and their spouses, as well as income from early retirement or insurance companies in the years prior to their retirement.

Assuming that investment in one's personal wellbeing is affected by the household's income level, total gross household income (in 2015 prices) was divided equally between spouses. The level of income of an individual in the research population

was determined according to the average adjusted annual income in the eight years prior to reaching retirement age. This study is based on approximately 93,000 men born between 1935 and 1930, about 62% of the potential population according to the Israeli Population Registry, and about 84,000 women born between 1935 and 1940, about 48% of the women in the Population Registry.

Study Results

Mortality Rates Based on Income Level

Tables 1 and 2 present the mortality rates among men born in 1930 and 1935 and among women born in 1935 and 1940. The focus is on income levels 15 years after the research subjects' formal retirement. As can be seen, the mortality rate decreases as income level increases, both among men and women. However, it appears that the decline in mortality rate in relation to income level exists primarily among men with low incomes. From an annual income level of approximately 175,000 NIS, the relation between mortality and income ceases. The high volatility in high income levels is probably due to the low number of observations in these categories.

Figure 1 Mortality Rate Based on Income Level, 15 Years after Formal Retirement Age, Men

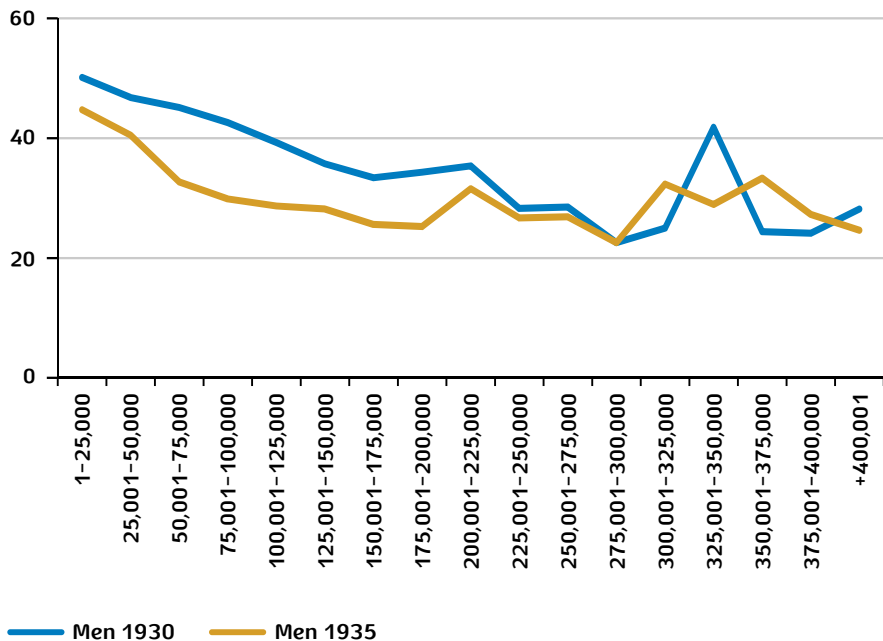
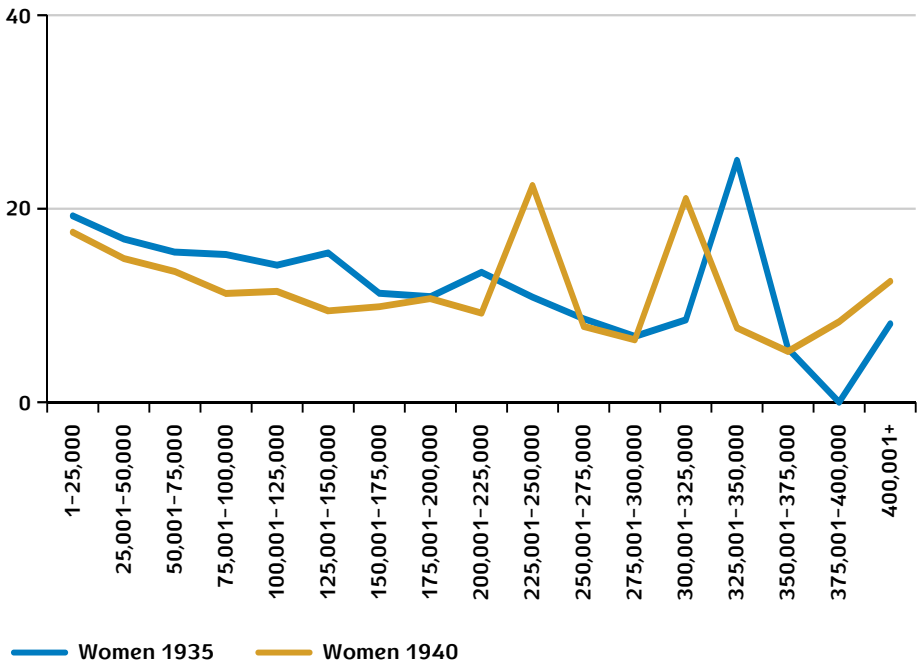


Figure 2 Mortality Rate Based on Income Level, 15 Years after Formal Retirement Age, Women



Gini Index over Time

Changes of the Gini coefficient (figures 3 and 4) over time exhibit the development in income inequality levels for men and women between two periods. If the index declines, it means that inequality has narrowed and the population is more homogenous with regards to income. Along with lower mortality rates among those with higher incomes than people with lower incomes, this indicates that in the surviving population the income level is higher. The graphs show that the Gini changes pattern for men born in 1930 and men born in 1935 is the same and that the Gini index has declined over the years at a growing rate. The results indicate that in the 20 years measured (five years before retirement and 15 years after retirement), the Gini index decreased equally among the two cohorts, by about 17 percentage points, in light of the differences in the life expectancy of high income earners as compared to people with low incomes.

With regards to the female population group, the picture is similar to what was found among men. In both cases, there was a decline in the Gini index over a period

of time for both years measured. However, the decrease among the female cohort was much smaller. Moreover, the inequality index for the younger age group (born in 1940) is lower than that of the older cohort (born in 1935). Yet, the gap between the age groups is significantly higher than that of the male groups, about seven percentage points (greater inequality among the older group). It is worth exploring further the reasons for the different pattern for males and females.

Figure 3 Development of Gini Coefficient for Income Inequality, Men Born in 1930 and 1935

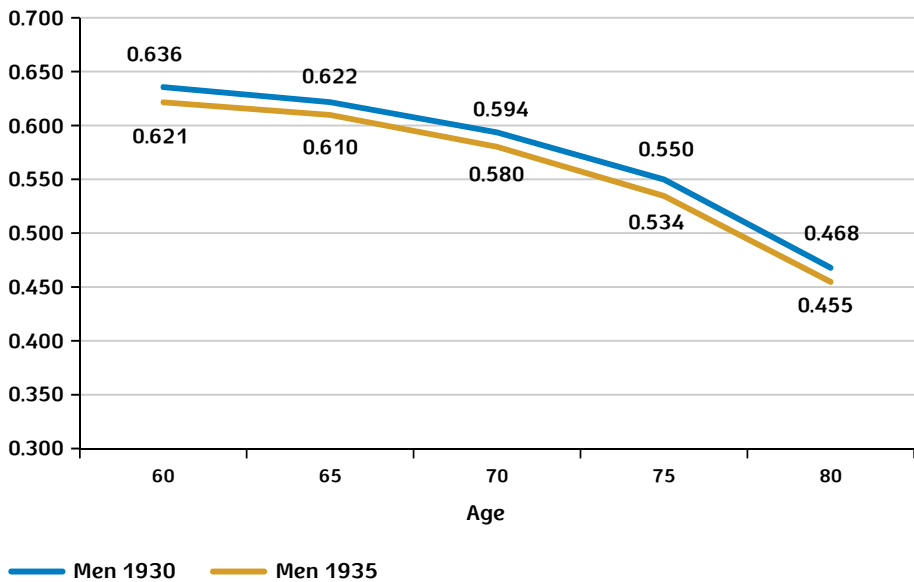
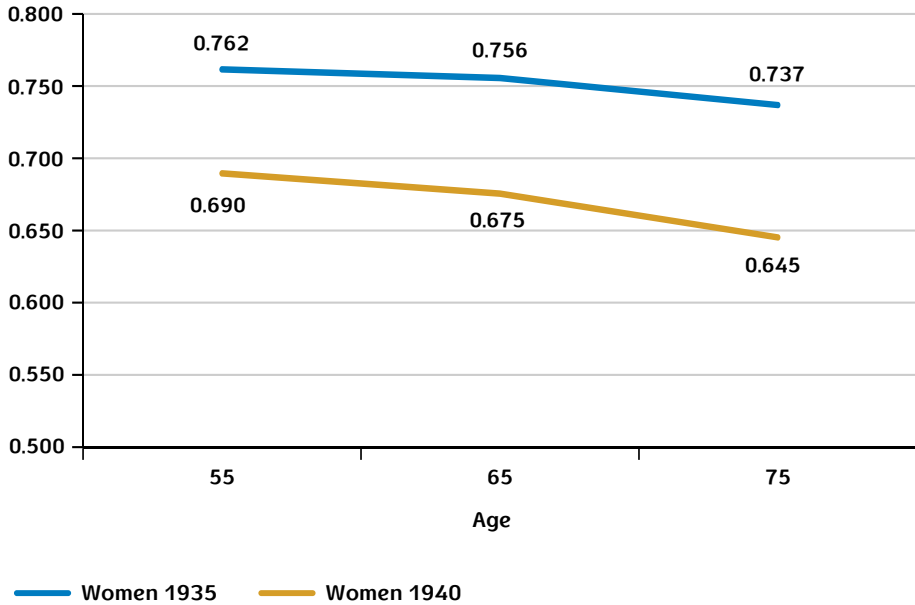


Figure 4 Development of Gini Coefficient for Income Inequality, Women Born in 1935 and 1940



Survival Regression Test

A survival regression test for estimating life expectancy differences was conducted for all men born from 1930 to 1935 and all women born between 1935 and 1940. The dependent variable is the age as of December 2016 (for the living) or the age of death, whichever comes first. The independent variables are: sex; year of birth; ethnicity (Jews except ultra-Orthodox, ultra-Orthodox Jews and Israeli Arabs); number of years residing in Israel prior to retirement; in a relationship prior to retirement; and income quintiles (differences in relation to the upper quintile).³ It

³ Since the income we based our research on is annual income, the presentation of differences in life expectancy as a function of income quintiles is intended to enable the identification of these differences.

should be noted that the regression's findings are preliminary and, subsequently, we plan to further invest this model.

Findings of the regression test:

- Life expectancy is shorter for the lower income quintiles: **on average, the risk of people in the lowest income quintile for a shorter life expectancy is 57% higher than those in the highest income quintile. This negative effect decreases as the economic status increases.**⁴
- Relative to women, men's risk of a shorter life expectancy is 47% higher.
- Among the Arab population, life expectancy is shorter than that of the general population.
- Among the Haredi population, life expectancy is significantly higher than that of the general population.⁵
- The likelihood that people in relationships prior to retirement will live longer is greater than those who lived alone right before retiring.
- Life expectancy is increasing for younger cohorts.
- Number of years living in Israel prior to retirement has a positive and significant effect on life expectancy.

4 In the future, we will add a Wald test with regards to the significance of the gaps in these coefficients.

5 The algorithm by which we identify Jews as ultra-Orthodox may be problematic for people of advanced age. In the future, we intend to reexamine this hypothesis.

Table 1 COX Survival Regression Test to Examine the Factors Correlated with Life Expectancy
(Explained variable: age as of December 2016 or date of death, whichever comes first)

Variables	Estimates	Standard Deviation	Level of Significance
Men	-0.469	0.014	0001.>
Date of Birth	0.032	0.002	0001.>
Arabs	-0.180	0.015	0001.>
Haredim	0.756	0.033	0001.>
Number of Years Residing in Israel Prior to Retirement	0.001	0.000	0.0001
In a Relationship Prior to Retirement	0.105	0.008	0001.>
Quintile 1	-0.572	0.013	0001.>
Quintile 2	-0.430	0.013	0001.>
Quintile 3	-0.365	0.013	0001.>
Quintile 4	-0.236	0.013	0001.>
-2 LOG L	1,506,558.2		
Pseudo R-Square	5.1%		
Number of Observations	176,937		

Discussion and Conclusions

The results of the study indicate a negative correlation between life expectancy and income. This effect was found mainly at annual income levels of up to 175,000 NIS. People with a very low income level (lower quintile) had a 57% chance of not living as long as people who are at higher income levels (upper quintile), with all other variables being consistent. This result is probably correlated with the level of access to health services in Israel. The findings also indicate that, over time, the mortality rate among the general population has been declining.

Similar to previous studies conducted around the world, these trends are more pronounced among men. Among other things, this can be attributed to the low variance in women's income, as women's rate of employment at these ages is rather

low.⁶ However, it is important to remember that the income variable reflects the average income of both spouses. As such, it is possible that the spouse's income level influences this trend among women from the outset.

The decline in the Gini index over time shows that the group of people from the same cohort becomes more homogenous as they grow older; while a higher rate of those with lower incomes pass away. Thus, the decline in the Gini index means that inequality has narrowed and people have more similar incomes. Given the finding that mortality rates are higher among those with low incomes, it can be said that the remaining population is "richer."

These results may have significant implications for policies guiding Israel's social security and pension systems. If our findings are correct, the chances of people and families who live in persistent poverty to benefit from pensions and old-age allowances are low compared to the people and families of Israel's upper class.

In the near future, we will look in depth at the differences in life expectancy among the various income deciles and explore the implications of these differences on the pension system. Moreover, we intend to analyze whether the current pension system supports cross-subsidization between the poor and rich, so that the former, whose life expectancy is shorter, are effectively subsidizing payments to the latter.

Sources

Bank of Israel, 2016. "The Relationship between Socio-Economic Status and Health: Periodic Fiscal Review and Research Analysis."

Chetty, Raj, Michael Stepner, Sarah Abraham, Shelby Lin, Benjamin Scuderi, Nicholas Turner, Augustin Bergeron, and David Cutler, 2016. "The Association between Income and Life Expectancy in the United States, 2001-2014": www.equality-of-opportunity.org/assets/documents/healthineq_slides.pdf

6 In addition, the employment rate among women in Israel has increased significantly in recent decades, with a bias in favor of educated women.



Allotment of Designated Bonds in Pension Funds

Policy Paper

Team members

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The Israeli pension system operates on two levels: first, the **old age pension** that is intended to enable a minimal standard of living; the second, the **employment pension**, is designed to provide savers with a standard of living that is similar to what they had prior to retirement. In recent decades, the pension system has undergone changes aimed at strengthening and stabilizing the structure and adapting it to the evolving labor market so as to prevent actuarial deficits. The changes include a transition from programs that define benefits (DB) to programs that define contributions (DC); changes with regards to ownership of pension funds; tax benefits for retirement savings only; and the widening of the base mandatory pension contributions. However, the primary reform to the pension system was the application of an adjusted financial savings model (similar to the "Chilean Model"), two years ago. The model divides pension fund investments in the capital market by age, into three periods:

- a. From entrance to the workforce until the age of 50: 20-30 years.
- b. From age 50 to 60: 10 years.
- c. Over the age of 60: on average, a period of between two years for women and seven years for men.

The earmarked bonds are those issued by the State to pension funds exclusively, and they guarantee an annual interest of 4.86%, plus linkage to the Consumer Price Index (CPI). Until now, savings in pension funds were eligible for earmarked bonds, and they represented 30% of savings portfolios. Meanwhile, the State guarantees 30% of the money invested in pension savings, while the rest of the portfolio is invested in the capital market. With the aim of providing greater protection for elderly savers, the Ministry of Finance's Capital Market Authority announced in 2016 that a change in the way designated bonds were allocated would be implemented. According to the plan, savers over the age of 60 would be eligible to receive 60% of these bonds, while the balance would be dispersed to other savers, with this remainder to decrease for younger ages¹. While the new scheme refers to age, it does not address differences in salary levels. However, many recent studies

1 The implementation of the plan will gradually take place over a 30 year period. In approximately 20 years the rate of bonds designated for young people will fall to 15% and only after 30 years will it be completely eliminated. By the end of the process, retirees will receive 60% of the designated bonds, savers between the ages of 50 and retirement will receive 30% and young savers under the age of 50 will not receive designated bonds at all.

show an increase in income inequality as well a growth in income gaps, which have a differential effect on life expectancy. An increase in life expectancy for individuals with high income levels leads to additional profits, via earmarked bonds, which are now being used not only as a fixed-rate anchor but also as a substantial subsidy for longer periods of time, through the National Insurance Allowance.

Beside institutionalizing inequality, the growing gap between various income groups may undermine the pension system's ability to function, as well as weaken its financial position and solvency, since it is obliged to finance high annuities over a continuous and long period of time.

We estimate that if the plan is implemented in its current form, it could seriously harm the pension benefits of Israel's low wage earners. We therefore propose two alternatives, taking into consideration, both age and level of income, maintaining the overall limit of designated bonds (30%). This design ensures both better performance and equity.

Outline of Proposed Earmarked Bonds Allocation: Adding an Income Variable

Since the model has already been adopted, this document will discuss only the manner in which the designated bonds are distributed according to the basic assumptions of the Ministry of Finance, without discussing advantages and shortcomings. In order to present the outline for the allocation of designated bonds, we will refer to the basic model adopted by the Capital Market Authority as Model A. The two alternatives we propose (B and C) meet the aggregate limit of the earmarked bonds as issued by the Ministry of Finance, and do not exceed the growth rate of the public's savings in pension funds. However, in addition to the age variable, these models also take levels of income into account.

Below, are the three alternatives:

1. **Model A: Outline of the New Government's Capital Market Authority, by age.** Starting in 2022, eligible members up to the age of 50 will not receive designated bonds at all; members up to the age of 60 will receive 30%, and members over the age of 60 will receive 60%.

2. **Model B: Alternative Approach, by Age and Income.** This proposal is based on the same amount of designated bonds as in the Ministry of Finance's model, but with a different distribution scheme, one based also on wage levels. Specifically, for given age, low wage earners would receive a higher proportion of designated bonds relative to high wage earners.
3. **Model C: Alternative Approach, by Age, Income and lower Rate of Return.** This proposal is based on the same cost of allocating earmarked bonds as in the Ministry of Finance's model, but the distribution would be according to wage levels (similar to Model B.) In addition, Model C proposes to reduce the rate of return of designated bonds to 4%, instead of 4.86%. This would be done without exceeding the budgetary framework, allowing a larger total amount of bonds, so that in this model, low-wage earners would receive higher rates of earmarked bonds relative to high-wage earners.

The main point to keep in mind is that designated government bonds today serve not only as a fixed return anchor but also as a significant subsidy to members. Long-term CPI-linked government bonds, which are the equivalent financial products for designated bonds, are traded in the market at rate of about 2.2% (for the first quarter of 2017). Such a rate implies a 2.66% subsidy for bondholders. Thus, the more a person deposits in a pension fund, the higher the subsidy he/she receives from the Ministry of Finance. According to the Capital Market Authority's model, all members receive designated bonds, so that those whose salary is double the minimum wage (10,000 NIS and 5,000 NIS, respectively) enjoy double the subsidies, those who earn four times minimum wage receive a subsidy of four times the rate, etc.

Integrating the Income Dimension in the Allocation of Bonds in the Pension Fund: Analysis of Alternatives

As previously stated, the plan proposed by the Capital Market Authority (alternative Model A) does not take the income variable into account. In contrast, the alternatives we propose do combine this dimension. In order to determine how the inclusion of income affects monthly pension payments, we will present an analysis of the three alternatives, according to three income levels:

- a. Minimum wage earners: 5,000 NIS gross.
- b. Those earning double the minimum wage: 10,000 NIS gross.
- c. Wage earners with a salary of four times the minimum wage: 20,000 NIS, the approximate deposit ceiling for a new pension fund expected for 2017.

In analyzing the alternatives according to wages, whereby low wage earners receive a higher rate of designated bonds, we maintained the same level of risk as the Capital Market Authority's model - by adjusting other assets' risk levels in the portfolio. According to the Capital Market Authority's guidelines, young people up to the age of 50 with low wages do not receive any designated bonds. However, according to the outline that we suggest, they can get either 32% (unchanged interest rate) or 39.6% (if the interest rate is 4%), while the highest-paid young people would not receive designated bonds at all. From the age of 50 and over, low-wage earners would, in our proposal, receive 44% of designated bonds (unchanged interest rate) or 55% (if the interest rate is 4%), and high wage earners would receive only 24.3% and 18.3%, respectively.

Methodology

We carried out our analysis using an advanced mathematical simulation tool that ran tens of thousands of statistical possibilities in a few minutes, taking into account an unlimited number of possibilities for combining financial assets and working assumptions in the investment portfolio, including various distributions for each component of the portfolio (corporate bonds, shares, assets abroad), and their correlations. To the best of our knowledge, such a model was not implemented by the Capital Market Authority. Our simulation was performed by running 10,000 scenarios for each of the three models presented, multiplied by three salary levels, with a total of 90,000 runs. For each model, we present the median probability (50%) for accumulation at retirement age and the possibility of a worse scenario of at a probability of 5%.

Simulation Results

The following table shows the default pension allowances for a male. These are the expected monthly allowances, as of 2017, in accordance with the annuity coefficients as listed in the general plan. Variables include spouse's survivor's

pension, according to wage levels and various models (in NIS). Percentiles in the table reflect the distribution of benefits according to market performance. The 95 percentile reflects the optimal scenario in which a high pension is obtained, while the 5 percentile shows the worst case scenario.

Table 1 Expected Monthly Pension According to Model, Income Level and Scenario, in NIS

Monthly Wages in NIS	Model A: Capital Markets Outline			Model B: 4.86% Yield on Designated Bonds			Model C: 4% Return on Designated Bonds		
	5,000	10,000	20,000	5,000	10,000	20,000	5,000	10,000	20,000
95 Percentile	4,837	9,675	19,350	4,724	9,670	19,555	4,218	8,898	18,357
50 Percentile (median)	3,324	6,648	13,296	3,642	6,516	12,296	3,544	6,395	12,450
5 Percentile	2,299	4,598	9,195	2,835	4,447	7,862	2,773	4,647	8,545

Table 2 Expected Differences in Allowances between Alternatives B and C and Model A

Monthly Wages in NIS	Model B: 4.86% Return on Designated Bonds			Model C: 4% Return on Designated Bonds		
	5,000	10,000	20,000	5,000	10,000	20,000
95 Percentile	-113	-5	205	-619	-777	-993
50 Percentile (median)	318	-132	-1,000	220	-253	-846
5 Percentile	536	-151	-1,333	474	49	-650

The data show that if we adopt our proposed alternatives, the situation of low-wage earners will improve and inequality will be reduced.

According to Model B, in the median scenario, the average allowance of low-wage earners increases by 318 NIS or about 10%, compared to the Capital Market Authority's model. In the worst case scenario (5 percentile), where the anchor of designated bonds plays a central role (guaranteed return), the allowance rises by 536 NIS, or 23%, compared to the outline presented by the Capital Market Authority. According to Model C, in the median scenario, the average allowance of low-wage earners increases by 220 NIS, or about 7%, compared to the Capital Market Authority's plan.

In the worst-case scenario (5 percentile), the allowance rises by 474 NIS, or about 20%, compared with the Capital Market Authority's outline.

Conclusions

The results of the simulations prove that the Capital Market Authority's policy is correct, though it can be improved. The outline decided upon by the Capital Market Authority does not take into account previous findings, nor does it incorporate advanced research methodologies and simulations so as to examine the effects of changes in designated bond distributions on future households' pension.

Moreover, while the gradual distribution of designated bonds over a period of time is appropriate, a uniform issuance for all salary levels is mistaken.

- a. Such a distribution scheme perpetuates the subsidizing of the highest decile households (from the 9th decile and up) and actually increases it, in comparison to low-income households. There is no apparent logic to distributing this allowance in such a manner.
- b. Such a division increases the chances that low income households will reach retirement age with low and even deficient pensions.
- c. There is a clear advantage to increasing the allocation's percentage of designated bonds, even if at a lower interest rate, especially for weak households. Thanks to the anchor, the increase in earmarked bonds would enable the pension fund to maintain the rest of the assets' portfolio, with supposedly risky assets (shares), without an increase in the overall risk.

Recommendations

- a. To conduct a comprehensive study on the implications of the distribution of earmarked bonds.
- b. To introduce, either in legislation or regulations, the alternative approach of designated bonds allocation that takes into account the amount of wages, which would result in the optimal distribution of earmarked bonds.



Reducing the Bureaucratic and Regulatory Burden



Streamlining Regulation in Israel and Easing the Bureaucratic Burden: Multi-Year Program Abstract

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To access the complete study (in Hebrew): <https://tinyurl.com/EHC17b>



Introduction

Effective regulation clearly defines the interface between the public and private sectors. Its purpose is to deal with market failures and achieve social policy goals. In many cases, however, the bureaucracy that accompanies government regulation and the costs derived from it create a real barrier to growth and prosperity. The impact of "bad" regulation on economic growth is severe: it reduces investments, makes it difficult to open businesses (especially small ones), constitutes a barrier to international trade and foreign investment, hampers productivity, and more.

Israel's Ranking on Regulatory Quality Indicators

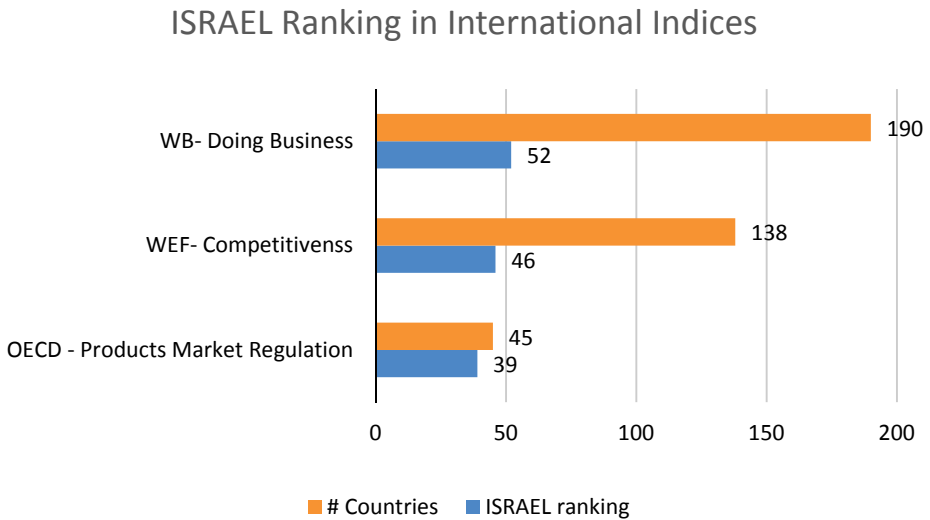
Various international organizations, such as the World Bank, the OECD, and the World Economic Forum (WEF) work to help streamline regulations worldwide. One way they do so is by publishing indices that rank different countries according to quality of regulations and governance, across various parameters.

According to International Indices, Israel's Regulation Regime is in Need of Improvement (Figure 1):

- **According to the Doing Business Index of the World Bank**, in 2016, Israel was ranked 52nd out of 190 countries. Israel was ranked particularly low in these sub-indices: property registration (126), payment of taxes (96), and enforcement of contracts (89).
- **In the 2016-2017 Global Competitiveness Report**, published by the World Economic Forum, Israel ranked 46th out of 138 countries in the regulatory burden sub-index. Thus, this index downgraded Israel's overall ranking in the International Competitiveness Report.
- **In the OECD's Product Market Regulation (PMR) index**, Israel was ranked in 2013¹ in 39th place out of 45 countries - only 6 countries from the bottom.

¹ The 2013 report is the most recent report published by the OECD on this subject.

Figure 1 Israel's ranking in international indices that examine the burden of regulation and bureaucracy



Measures to Improve Regulation in Israel

In the middle of the previous decade, countries and international organizations began initiating measures to improve government regulation: the OECD initiated and implemented the Regulatory Impact Assessment (RIA) process; Britain formulated and implemented a program to simplify and streamline regulation in the framework of the Better Regulation Project; The Netherlands initiated an orderly process (subsequently adopted by the European Union) that led to considerable savings in administrative costs incurred by regulators as a result of inefficient regulation (SCM); Portugal implemented a plan to expedite and expand the process of opening businesses by setting up one-stop shops (units that allow all the procedures required to open a business to be conducted in one place).

The Israeli government only began to streamline regulations in recent years, following the recommendations of the Trajtenberg Committee, which was established after the social protests that took place across the country during the summer of 2011. The government made a series of decisions with regards to doing business in general, business licensing procedures in particular, bolstering the functioning of government and streamlining regulation.

Implementation of government decisions on improving regulation is the responsibility of the Better Regulation Unit of the Department for Governance and Social Affairs, in the Prime Minister's Office (PMO). Out of the many decisions implemented by this division, we will focus on the resolutions to reduce the regulatory burden by 25% by 2019 and implement RIA, before a new regulation is adopted. In addition, the Better Regulation Unit also deals with simplifying licensing procedures for businesses.

Based on the mapping of the government's work so far to improve regulation and reduce its bureaucratic burden, and after consulting with governmental agencies that specialize in this field, **we have come to believe that the key to achieving change in Israel is not to perform an analysis of the situation or draw conclusions. Neither will change come from developing a set of recommendations or government decisions. Rather, the situation in Israel will improve once existing reforms are actually implemented.**

Assisting Government Ministries to Implement Regulatory Reforms: A Multi-Year Action Plan

The Israel Democracy Institute's Plan of Action

The proposed plan of action was formulated on the basis of a series of meetings we held with the various entities² that deal with regulation and the promotion of foreign

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- 2 (1) The Better Regulation Unit of the Prime Minister's Office. The division, which operates within the framework of the Department for Governance and Society, is responsible for implementing government decisions on streamlining and enhancing regulation, including RIA, reducing the costs of bureaucratic burdens and improving the business sector's ability to function (Ehud Praver, Amichai Fisher).
- (2) Adv. Edna Harel, Head of Department, Legislation and Counseling Department (Economic and Fiscal Matters), Ministry of Justice.
- (3) Foreign Investments and Industrial Cooperation Authority, Ministry of Economy and Industry (Eyal Eliezer, Gilad Beer, Ilan Laufer). The activities of the Foreign Investments and Industrial Cooperation Authority include locating investment opportunities in Israel, identifying the countries from which foreign investors will come, searching out investors or companies of relevance to launching entrepreneurial endeavors in Israel, creating contacts between potential investors and the Israeli "target" and operating a service center for foreign investors.
- (4) Esti Goldhammer of the 'Kav Project' accompanied and advised the government team on the subject of doing business.

investments in Israel. During these meetings, we tried to map the main obstacles that government officials face when implementing government decisions in the field of regulation, in a way that will ultimately encourage investment in Israel. Then, we asked ourselves how IDI could help.

The program includes six projects grouped into three categories:

(A) Friendly regulation that helps investors and expedites the process.

Includes 3 projects:

- i. Preparation of a regulatory roadmap for investors.
- ii. Formulation of recommendations for the establishment of a One-Stop Shop unit, based on international experience and incorporating local characteristics.
- iii. Streamlining and improving of the regulatory consultation process, between regulators and the public they supervise.

(B) Smart regulation, which includes the integration of behavioral economics tools, for setting regulatory directives, formulating measures to improve trust between the government and business sectors, and bolstering the public's attitude toward businesses.

(C) Studied Regulation, which includes the use of international indices for the purpose of learning best practices, and serves as a tool for improving Israel's ranking in international indices.

The main points of the proposed plan are as follows:

A. Friendly regulation

1. Preparing a regulatory road map for investors and easing barriers to investment in Israel³.

In order to make it easier for foreign and local investors, we propose to develop a road map that will assist those who are contemplating investing in Israel.

The mapping process will include three main stages:

³ In cooperation with the Ministry of Economy and Industry.

- i. Creation of a basic flowchart.
- ii. Diagnosis of barriers.
- iii. Formulation of recommendations to remove identified barriers, thus improving regulation in the process. This stage will be based on in-depth interviews and round table discussions with regulatory units, in cooperation and consultation with the relevant government ministries and representatives of the business sector.

The final product will enable the creation of an online interface and app⁴ (application). To make the roadmap accessible to investors, the app will be used in the first stage to gather all information required for an investor to make his investment. In the next stage, the app will serve as an operational tool for investors, facilitating the submission of materials and contact with relevant parties.

2. Formulating recommendations regarding the possibility of establishing a One-Stop Shop in Israel.

One of the accepted ways to streamline the process of establishing a business is via a one-stop shop.

There are three possible ways of doing this:

- i. A central entity that guides, directs and accompanies the entrepreneur in his contacts with the administrative agencies responsible for issuing the necessary approvals.
- ii. A single body that coordinates between all the administrative agencies as well acts to ensure that entrepreneurs receive the guidance they need.
- iii. One entity in which all relevant authority is concentrated, enabling the entrepreneur to work with and receive all necessary approvals from one place.

We aim to present a number of conclusions regarding the feasibility and advantages of establishing a One Stop Shop unit in Israel. In addition, we propose to come up with a series of recommendations for the most appropriate model of such a unit in Israel. This analysis will be conducted by way of international comparative research, interviews, questioning of and consultation

⁴ This implementation stage will be conducted by the Ministry of Economy and Industry.

with relevant government representatives (Prime Minister's Office, Ministry of Economy and Industry and the Ministry of Finance), as well as representatives from the business sector.

3. Formulating recommendations for streamlining and improving the regulatory consultation process between the regulator and the public when determining new regulation.

In centralized industries (banking, insurance, communications, electricity), regulators maintain regular contact with a limited number of players, who are prominent enough to allocate the necessary resources for a professional, ongoing dialogue with the regulator. However, in sectors where the number of players is large in number but relatively small in individual size, the importance of representation (i.e.: trade unions such as the Manufacturers' Association or the Federation of Chambers of Commerce) becomes crucial.

According to the Department for Governance and Social Affairs of the Prime Minister's Office, the consultation process can be improved if ways are developed to directly examine the relative players who would be affected by a regulatory directive, in addition to the representative body.

As such, we propose to conduct an in-depth study of developments in the European Commission, UK and Denmark, with the aim of ultimately formulating and adopting an appropriate consultation model for Israel.

B. Smart regulation

1. Assisting government agencies to implement smart regulation.⁵

In recent years, behavioral economics methods have been implemented in many countries, which have led to an improvement in the work of government, streamlined regulation and a reduced regulatory burden. The method's applications can be expressed in several ways:

- i. Improving the methodology underlying the regulatory work and making it evidence-based.

⁵ In cooperation with the Better Regulation Unit of the Department for Governance and Social Affairs in the Prime Minister's Office.

- ii. Alleviating the regulatory burden on the business sector, by converting rigid regulation into light-handed regulation, through the creation of specific regulation that focuses primarily on markets and/or players prone to trouble as well as adapting regulation to public needs.
- iii. Creating a framework that encourages the regulator to reduce unnecessary regulation, while implementing tools that encourage deregulation, examining misconceptions that encourage redundant regulation and addressing those misconceptions.

In order to improve and streamline existing administrative processes and establish new regulation, we suggest examining a combination of tools from the field of behavioral economics.

2. Strengthening the trust between the government and business sectors.

Improving trust between the government and the business sector by promoting self-regulation and joint regulation was discussed by the Israel Democracy Institute at the Eli Hurvitz Economic and Society Conference (Caesarea Forum) in November 2014. At the time, the team concluded that implementing self-regulatory and regulatory processes that are part of the regulator's toolbox is an important step in improving government and industry planning capacity. In addition, such a development would enhance the performance of both government and industry, as well as establish trust between the regulator and the entities he supervises. Alongside promoting procedures for the adoption of self-regulation and joint regulation, in appropriate cases, it was proposed that mutual trust between the various parties in the consultation process be enhanced, so as to improve the way new regulation is formulated.

In order to identify suitable topics for promotion, within the framework of self-regulation or joint regulation, the Israel Democracy Institute will coordinate a series of meetings between **players in relevant industries**, and through them formulate a proposal for **self-regulation or joint regulation**. We suggest that this process be carried out in cooperation with the regulator. As described above, behavioral methods can be used to promote self-regulation and co-regulation.

C. Studied regulation

Improving Israel's position on international indices, specifically with regards to the regulatory and bureaucratic burdens.

In order to remove barriers to investment, it is important to improve existing regulations and reduce the burdens of compliance (bureaucracy). At the same time, it is important to reflect the changes that will inevitably take place in the field, so that they are then incorporated into the international indices.

Therefore, we propose that:

- A. The Israel Democracy Institute maintain regular contact with international bodies (the World Bank, the World Economic Forum and the OECD) whose task is to compile the international indices.

Two goals for maintaining these relationships:

- i. Using international benchmarks as an incentive to learn from best practices.
 - ii. Improving the calibration of reforms to indices, and reporting on various actions and reforms in the field.
- B. The Israel Democracy Institute hold a **series of roundtable meetings** between relevant industry entities and officials in charge of specific fields. These gatherings will be conducted in cooperation with the relevant government ministries. Each session will focus on one parameter. Participants will discuss the evaluation methodologies used in the international indices, and ways to improve measurement techniques and accurately represent Israel's performance.
 - C. **The method of deriving Israeli data used as an input in international indices**, and actions be taken to improve this method, in cooperation with survey takers in Israel and in the World Bank, World Economic Forum and the OECD.

Appendix: Highlights of the Multi-Year Action Plan (chart)

Assisting government agencies to enforce the regulatory reforms they are tasked with implementing.

Friendly Regulation	
In cooperation with the Prime Minister's Office	1. Improving the consultation process with the public: learning from the experiences of the European Union, Britain and Denmark
In cooperation with the Ministry of Economy and Industry	2. Creating a regulatory road map for investors: <ul style="list-style-type: none"> ○ Flow chart, diagnosis of barriers, recommendations for improvement of regulation ○ Online interface and application (app.) for information and operation
In cooperation with the Prime Minister's Office and the Ministry of Economy and Industry	3. Examining the possibility of a one-stop shop

Smart Regulation	
In cooperation with the Prime Minister's Office	<p>4. Integration of behavioral economics tools to improve government work:</p> <ul style="list-style-type: none"> ○ Training workshops ○ Comparative research: using behavioral economy to influence business ○ Creating a guide to implement behavioral economics in determining regulation ○ Starting a pilot program ○ Ongoing progress reports <p>5. Improving the trust between the government, the business sector and the public: promoting self-regulation and joint regulation</p>

Studied Regulation	
In cooperation with the Prime Minister's Office	<p>6a. Improving Israel's ranking in international indices:</p> <ul style="list-style-type: none"> ○ Ongoing contact with the international organizations that compile the indices ○ Improving the method of implementation of indices in Israel
In cooperation with the Prime Minister's Office and the Ministry of Economy and Industry	<p>6b. Improving Israel's ranking in international indices:</p> <ul style="list-style-type: none"> ○ Meetings between relevant government and business sector officials on subjects included in the indices



Applying Behavioral Economics to the Streamlining and Reduction of Regulation

Outline

Prof. Yuval Feldman Senior Fellow at the Israel Democracy Institute and Director of IDI's Reform of the Civil Service Program. Feldman is a full professor on the Faculty of Law at Bar-Ilan University and a member of the Israel Young Academy (IYA).

Omer Selivansky Research Assistant for IDI's Center for Governance and the Economy. Selivansky holds a master's degree in economics from Ben-Gurion University of the Negev.

This document is based on a paper currently being written by Feldman and Selivansky on the use of Behavioral methods for improving government work. This project is being conducted under the aegis of the Institute's Center for Governance and the Economy.

Highlights

Behavioral methods are a new tool in the regulatory toolbox. They enable the sovereign to actively promote the public wellbeing, even in instances where there is no justification for rigid regulation. They also allow for the reduction of the regulatory burden by prodding the public into making voluntary choices (private citizens as well as the wider business sector), instead of bringing to bear an element of coercion. As a result, the regulator is provided with new ways to conduct methodical analysis, streamline government regulation and reduce the burden that comes with regulatory compliance.

Behavioral Economics in the Service of Government

Over the past few decades, the field of behavioral economics has become very popular. It lies on the seam between economics and psychology, and uses empirical evidence to help predict human behavior in ways that traditional economics cannot. Behavioral economics methods can have powerful ramifications for policy planning, as it offers a profound understanding of the mechanisms and thought patterns that dictate human behavior.

In recent years, behavioral economics has spawned a variety of methods that exploit behavioral insights for the purpose of enhancing the effectiveness of government. These methods are for the most part based on **soft regulation** intended to point the public toward making choices that promote public wellbeing, but that leaves the final choice in the hands of the public, and steers clear of significant modification of the incentive system. Soft regulation is based on an assortment of tools, such as the setting of default choices, sending of reminders and simplification of complex information. It has made significant contributions in areas such as pension programs, environmental quality, energy efficiency and healthy living.

As part of the civil service's adoption of the behavioral method, research and methodological tools from the behavioral sciences are also being incorporated. Behavioral research tries to avoid being based on axioms of human behavior. Instead, it is based on an empirical examination of that behavior. In accordance with standard behavioral science methodologies being used by governments, most of the work of these behavioral insights teams is guided by empirical study of regulatory

interventions, with an emphasis on conducting supervised trials based on randomized controlled trials (RCTs). The behavioral insights teams take an evidence-based policymaking approach, according to which before a policy is set it should be meticulously assessed against alternative policies, along with a study of the policy's impact on control groups on which it is not being applied.

Governmental Adoption of Behavioral Insights: International Comparison

United Kingdom

In 2010 a team was formed within the Prime Minister's Office (PMO) in the UK that focused on the adoption and application of behavioral insights by the civil service (known as the Behavioral Insights Team-BIT). The team, which operated during a period of economic crisis and budget-cutting, initially functioned on a trial basis. During its first two years of existence, the BIT operated as a pilot program. It was decided that should its contributions to the civil service prove to be negligible, the program would be shut down.

However, after two years, the BIT proved to be extraordinarily successful:

1. Within two years of its advent, BIT was producing a return (ROI) of 22 times the amount of funds invested in its activities, the result of the streamlining of government work, as based on the team's recommendations.
2. Several government ministries incorporated behavioral tools into their daily operations.
3. The number of RCT public sector empirical studies carried out in the first two years of the team's work was greater than all empirical studies conducted throughout the history of the United Kingdom.

United States

The behavioral insights approach was extensively promoted by the Obama administration in the US, which appointed a behavioral sciences expert, Cass Sunstein, to head the unit responsible for examination and evaluation of federal regulations. In addition, Obama issued two presidential orders in which he instructed

units of his administration to integrate behavioral insights into their work.¹ In 2014, a dedicated team was created to incorporate behavioral insights into the functioning of various government entities, as based on the British team.

International Organizations

The EU Commission set up a mission-specific behavioral insights team. Moreover, international organizations are working to promote the method² and the OECD has held several conferences devoted to promoting added use of the method.³ The World Bank even devoted its 2015 annual report to behavioral methods and how they can be utilized to reduce poverty and promote welfare in developing countries.⁴

Following the success in the UK, many other countries formed their own teams to adopt behavioral insights into the civil service (Australia, Germany, Holland, Singapore, Finland, France, Qatar, and Canada).

Israel

In Israel, too, initiatives have been promoted to adopt behavioral insights into the civil service. The PMO, in cooperation with the Center for the Study of Rationality at the Hebrew University, has led the way in using behavioral tools. At the same time, such government entities as the Ministry of Finance, Ministry of Environmental Protection, Ministry of Health, Ministry of Justice, National Insurance Institute and the Consumer Protection Authority have cooperated with many academic researchers on this issue, including researchers from the Israel Democracy Institute. As a result, the civil service has first examined and then adopted various behavioral tools.

1 The White House, Office of the Press Secretary, "Executive Order – Using Behavioral Science Insights to Better Serve the American People," September 15, 2015 (On May 7, 2017 all web sites in this document were retrieved).

2 See: The European Commission's Science and Knowledge Service, Behavioral Insights.

3 For a survey of actions taken in OECD countries, see OECD, "Behavioral Insights and Public Policy Lessons from Around the World," March 1, 2017.

4 The World Bank, "World Development Report 2015: Mind, Society, and Behavior.

Behavioral Insights and Streamlining Regulation

The method of behavioral insights has led to an improvement in the work of government work: a more efficient provision of services is creating greater financial savings and better quality of service for the public. The method is also playing a central role as a tool for enhancing regulation and reducing the regulatory burden. Behavioral insights are thus being applied in several ways: policymakers are using the method to encourage regulators to minimize regulation; facilitation of improved interactions between regulators and the businesses they oversee; enhanced interactions between the business sector and consumers, enabling less rigid regulatory requirements.

How Behavioral Methods Contribute to Better Regulation

- (1) **Evidence-based policy for reducing regulation.** This approach is effective in reducing regulation by promoting scrutiny. In practice, numerous directives and bylaws are enacted without adequate assessment of their impacts being conducted, and therefore empirical assessment can be expected to lead to the abolishment of superfluous regulations. Moreover, the demand to conduct empirical research itself places a barrier on the imposition of new regulations, which will thus be enforced only when there are clear indications of market failures and it is determined that intervention is likely to lead to a marked improvement in the functioning of the market.⁵
- (2) **Conversion of rigid regulation to soft regulation.** As stated above, the behavioral method extols the virtues of soft regulation in promoting the public wellbeing. In so doing, it puts an emphasis on voluntary tools and the conversion of meticulous compulsory regulatory directives into simple administrative principles. These are meant to guide the manufacturer into adopting the behavior expected of him, while simultaneously increasing the freedom of the players under supervision to act at their own discretion. Such

5 In this context, it should be noted that the US administration gave a high priority in terms of resources to empirically tested regulations and interventions, compared to those that were not systematically examined. See: The White House, Office of Management and Budget, “Commission on Evidence Based Policymaking”.

results are based on cooperation between regulator and regulatee, and mutual assessment of the various options for maximizing benefits for all concerned.⁶

- (3) **Simplification and clarification of regulatory directives.** A significant contribution that the behavioral insight approach can make to consumers lies in its ability to simplify relevant information and make it more accessible. Consequently, the adoption of behavioral insights by regulators can aid in simplifying and clarifying regulatory directives, making them clear and easy to carry out.⁷
- (4) **Adaptation of regulatory requirements to the needs of the public and/or businesses.** Research indicates that regulatory directives are often determined on the basis of an assumption that the public operates like a rational player who reads and understands all the available information. Subsequently, this leads to numerous legal requirements and cumbersome statutory compliance.⁸ Conversely, the behavioral approach believes that regulation should be adapted to human behavior, such that it will be straightforward and clear to the public at large, while abolishing requirements that do not contribute to the situation of the reasonable individual.⁹ Therefore, by employing the behavioral approach, regulators can reduce burdensome regulatory requirements and exchange them for more lenient and more effective requirements.
- (5) **Adaption of regulation to the markets and various players.** The behavioral methodology enables built-in assessments of different markets, and adaptation of the regulation of these markets in accordance with their distinct attributes. Therefore, an empirical and systematic examination of behaviors makes it possible to derive data on the market's conduct and the various players in it and to adjust the regulatory means to fit specific situations. These data enable the

6 See: Ian Ayres and John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate*, Oxford: Oxford University Press on Demand, 1992.

7 Cass R. Sunstein, *Simpler: The Future of Government*, New York : Simon and Schuster, 2013

8 Korobkin and Ulen, for example, elaborate on the broad influence of and problems connected with the assumption of rationality on legislation. See: Russell B. Korobkin and Thomas S. Ulen, "Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics," *California Law Review* (2000): 1051-1144.

9 For further information, see Elisabeth Costa, Katy King, Ravi Dutta, and Felicity Algate, "Applying Behavioral Insights to Regulated Markets," Behavioral Insights LTD, May 26, 2016.

establishment of defined and objective criteria to justify the intervention of the regulator in the market, thereby reducing the uncertainty arising from the vesting of too much authority over government regulation to civil servants.¹⁰

- (6) **Preventing corruption and encouraging adherence to regulation.** By creating a situation in which the regulatory directives are clearer and simpler, while the enforcement is more forceful and effective vis-à-vis those who violate the rules, one could differentiate between those factories and business owners who want to follow the law and those who seek to go around it. When regulation is convoluted and cumbersome, both those who follow the law and those who do not are similarly frustrated, with the result being an inability to act. This situation creates fertile ground for corruption, for instance by middlemen who strive for the simplification of regulation on behalf of their employers. Simple and clear regulation, on the one hand, along with prompt enforcement and strong sanctions, on the other, can pave the way for a fast and easy route that enables the majority of factories to operate at an optimal level, while posing a constant threat to those who wish to deviate from the rules of regulation.¹¹
- (7) **Using behavioral methods to improve the regulator's work.** Behavioral methods furnish tools that enable regulators to influence the players to act in ways that promote social policy goals. In this manner, it is also possible to influence the regulators, to make their behavior more fair-minded, more effective and more sensitive to the crucial importance of balancing the demands of the market with the needs of the public at large.

10 Costa et al. presented three empirical criteria that ought to be examined in order to justify regulatory intervention in a certain market: 1) differential between the average basket of goods purchased by consumers and the parallel basket they would receive if they had chosen the lowest-cost price quotes; 2) assessing the public's knowledge and familiarity with substantive characteristics of market transactions; and 3) index of consumer satisfaction with the behavior of the market. In their opinion, only if there is a gap between these findings and those that would be obtained under conditions of reasonable market behavior – then there is justification for regulatory intervention that is adapted to a criterion and/or the population group in which the gap was found.

11 For a discussion on the ability of legal rules to distinguish between law abiders and lawbreakers, see Yuval Feldman and Henry Smith, "Behavioral Equity," *Journal of Institutional and Theoretical Economics* 170 (1) (2014): 137-159.

The following are examples of behavioral-insight-based tools that can improve the work of the regulator:

- i. Creating a timetable according to which the regulator must offer a response to various types of applications within set periods of time.
 - ii. Setting a default choice in which, without active intervention or authorization at the higher echelons, regulatory approval will be given automatically.
 - iii. Fostering the idea that a specific public servant is personally responsible to issue authorizations and work directly with a specific business, instead of authorizations being issued in a decentralized and haphazard manner by an entire department. This approach would serve to increase the accountability of public servants.
 - iv. Transition to self-regulation, with heavy fines meted out to those who deviate. This would allow more personnel to be diverted to cases where direct regulation is required.
 - v. Granting bonuses to functionaries for fast and effective action, and, conversely, negative notes being placed in personnel files for instances of lateness or dysfunction.
 - vi. Transition to computer based systems that allow for as much transparency as possible and that would enable the manager to see how long an application approval took to process and where in this process did were there delays.
- (8) **Assessing the mistaken beliefs that are characteristic of regulators.** Behavioral research engages in mistaken beliefs that can lead to chronic and systemic behavioral deviations. Some of these deviations can be linked to non-optimized regulatory work. For example, people tend to place greater importance on short-term results, such as the immediate damage that could result from inadequate regulation. On the other hand, people will place lesser importance on long-term objectives, such as easing of regulation and attracting investors to Israel. People also tend to stick with the default choice and avoid change. Such a tendency is liable to encourage them to leave regulatory directives intact, even when those that have become redundant. Similarly, a World Bank study demonstrated that regulators tend to interpret information in a biased manner, such that it will seem as if their activity is vital and that the

field for which they are responsible requires active intervention.¹² In other contexts, it was found that some countries invest excessive resources in salient but uncommon dangers, due to availability bias.¹³

Based on the above, in-depth assessment of the biases of regulators and the tools used to inhibit them could contribute toward a reduction of the regulatory burden.

Conclusion

In recent years, the use of behavioral methods for fostering better regulation and easing government regulation has become widespread, and has proven effective in the promotion of effective regulation while reducing the government burden. The behavioral approach is likely to contribute toward improving and reducing the regulatory burden by transitioning into an evidence-based endeavor. Similarly, the method provides tools that make it possible to ease the burden that the regulator imposes on the business sector, replacing rigid regulation with gentle regulation, enforcing regulation that focuses primarily on the markets and/or high-risk players, and adapting the regulation to the real needs of the public.

Moreover, the method enables decision-makers to create a framework that encourages the regulator to reduce unnecessary regulation, while implementing tools that encourage the reduction of regulation and assessing the biases that encourage overregulation, and then addressing these biases. **Proper use of behavioral insights, and the cumulative global experience in the use of these insights, is likely to make a dramatic impact on the improving and reduction of regulation in Israel.**

12 Banco Mundial, "World Development Report 2015: Mind, Society, and Behavior," The World Bank, 2015.

13 Kuran, Timur, and Cass R. Sunstein. "Availability Cascades and Risk Regulation" *Stanford Law Review* (1999): 683-768.



Behavioral Methods for Streamlining the Work of Government

Abstract

Omer Selivansky | Yuval Feldman

To access the complete study (in Hebrew): <https://tinyurl.com/EHC17c>



In recent years, we have witnessed an increase in the use of behavioral science-based methods and insights to improve the work of governments around the world. Behavioral methods give the state new tools to add to the regulatory toolbox. These methods are based on a systematic examination of citizens' behaviors and allow for subtle government interventions, when there is no justification for the use of standard regulatory tools, or when the standard tools are less effective.

Behavioral Economy

The rise in use of methods and insights based on behavioral sciences stems from the growing prominence of the behavioral economics field, one that combines theories and methods from economic science with those of behavioral sciences.

Behavioral economics thus focuses on examining the factors and circumstances in which systematic behavior deviates from the "rational" decision-making process and investigates the mechanisms that lead to these deviations and their implications.

Evidence-Based Policy

The field of behavioral economics seeks to examine actual decision-making, without requiring axioms regarding normative modes of operation and the degree of "rationality" underlying certain behaviors. As such, the field relies on a methodology that seeks to estimate the actual behavior, as based on empirical studies.

The adoption of behavioral economy in particular and behavioral methods in general in the civil service requires the adoption of evidence-based policies and reliance on empirical tools and experimental procedures, for a systematic examination of public behavior and the implications of government involvement.

Behavioral Methods for Improving the Work of Government

Behavioral economics has developed several methods, based on behavioral applications and the use of subtle regulatory tools, to improve the functioning of government.

The most famous method is the 'nudge.' This approach emphasizes the ability of government officials to significantly influence the choices that the public makes by designing the "choice architecture" - the framework and context in which choices are made. In this way, people can be pushed ('nudged') to make the choice that is likely to be best for them, but without imposing regulations nor making significant changes to the incentive system.

Behavioral Insights Teams

In light of developments made in behavioral sciences and the contribution of their applied tools to the improvement of public policy, a special team was established in Britain in 2010 to examine behavioral insights for improving the work of government (BIT - Behavioral Insight Team).

The team has done a great deal for enhancing government work: it brought about greater efficiency and economic savings, conducted an unprecedented number of evidence-based studies of the civil service and disseminated the application of behavioral methods to the civil service.

As a result of its success, the team was greatly expanded, with parallel teams being established in many other countries and international organizations, working to disseminate behavioral methods and encourage the use of their applications.

Behavioral Insights and Digital Governance

Behavioral methods and methodologies have the potential to bring about real improvement in many areas, particularly in digital governance applications. There

are several reasons for this: the digital interface enables rapid and systematic studies of many subjects using advanced information processing and analytical tools. Accordingly, the digital interface makes it easier to systematically design the choice architecture, hence enabling the examination of variable elements between subjects by isolating them and estimating the effects of various interactions.

Behavioral Insights in Israel

In recent years, a variety of initiatives have been launched in Israel to improve the work of government agencies, based on the application of behavioral insights.

The Prime Minister's Office is responsible for regulation in this area and has already promoted several projects, in cooperation with the Center for the Study of Rationality at Hebrew University. In addition, a team was set up to provide advice on behavioral economics issues to the Budget Division of the Ministry of Finance and the National Insurance Institute created an infrastructure for communicating with behavioral researchers, so as to more efficiently carry out joint projects.

Moreover, a variety of other projects were promoted during the "Nudgethon" workshops, which brought together officials from various government entities with academic researchers, so as to establish dedicated task forces. Each team dealt with a concrete policy problem and designed an experiment to examine behavioral tools that could solve it (if only partially) or provide insight into its causes.

Finally, some government agencies have independently promoted projects based on behavioral insights, including the Ministry of Environmental Protection, National Insurance Institute, Division for Improving Regulation in the Prime Minister's Office, Water and Sewage Corporations, Civil Service Commission, Chief Economist of the Ministry of Finance and Consumer Protection Authority.

Summary and Recommendations

The study raises several recommendations regarding the adoption, implementation and regulation of behavioral methods in the Israeli government's operations. The recommendations can be divided into three main categories:

1. Recommendations concerning the infrastructure that should be established in order to achieve optimal adoption of behavioral methods in the civil service.
2. Recommendations regarding the regulation of various aspects of behavioral research in Israel.
3. Recommendations related to facilitating interaction between various factors, which can help one another adopt the most effective methods.

A. Establishing an infrastructure for the optimal adoption of behavioral methods in the civil service:

1. Establish a behavioral insights team that will coordinate all initiatives related to this method.
2. Provide incentives for the establishment of an evidence-based policy approach in the civil service.
3. Arrange broad-based agreements between government agencies and researchers.
4. An infrastructure should be established for dedicated information systems, tailored to evidence-based policies in general and research on behavioral insights in particular.

B. Regulation of Behavioral Research in the Civil Service:

1. Create a public framework to periodically examine the civil service's application of behavioral insights.
2. Specific transparency requirements must be established and incentives should be created to ensure maximum transparency.
3. A structured working protocol for behavioral research should be developed.
4. The public's attitudes towards the use of behavioral methods in the civil service and subsequent government involvement should be examined systematically and continuously.

C. Encouraging Interaction between Factors that Use Behavioral Methods:

1. Synchronization between entities, based on behavioral and evidence-based research in the civil service, must be confirmed.

2. An interface should be set up, between the work of the behavioral insight teams and government ICT (Information and Communications Technology) units.
3. Collaborate with researchers who specialize in behavioral research.

A broad based analysis of the field and creation of an effective research and regulation infrastructure, in conjunction with all relevant agencies, would likely catalyze a more successful adoption of behavioral tools in Israel, as well as their most effective implementation.

In addition, a clear and binding regulatory regime that takes into account relevant ethical and procedural issues will prevent the abuse of behavioral tools and reduce the risk that they will generate public resistance and weaken the citizenry's confidence in the government.

Public Attitudes in Israel towards Nudges

Research Report

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Summary

In recent years, behavioral tools have been increasingly used by government organizations around the world. These tools are often referred to as 'nudges' and include a wide range of measures that alter the choice architecture within which decision makers function, without significantly impairing freedom of choice and without substantially altering the economic incentives system. These nudges include changing the registration options for organ donations, publishing health / calorie information on food products, sending out appointment reminders and enabling automated appointment setting in advance. The public's attitudes towards this use of behavioral tools, and with nudges in particular have recently been measured in a number of countries around the world. The results of these findings may help policy leaders choose which tools to use and adapt them optimally.

The population of the State of Israel is composed of distinct and special groups, in terms of their needs and desires. Therefore, the aim of the research presented here is to identify the public's attitudes across various sectors of society to different nudges as applied in a variety of situations. We surveyed 609 respondents in a representative sample of the Jewish (secular and religious) and Arab population groups in Israel. Specifically, we examined these groups' respective positions on 13 nudges, in the fields of healthcare, consumerism, citizenship and the environment. The results of the study show strong support for most of the surveyed nudges, across all societal sectors. However, we also found important differences that should be taken into account when designing and implementing different nudges for these population groups.

Nudge is a change in how choices are defined and presented to the decision-maker. While nudges may predictably influence the choice of the decision maker, they do so without limiting the freedom to choose from other alternatives. Nor do nudges significantly alter the economic incentive package of these various options. Nudges aim to help decision-maker choose the option that would most benefit themselves or society. Prominent examples of nudges include setting defaults for savings and pension schemes, highlighting health information on food products and sending timely reminders for pending payments.

Findings

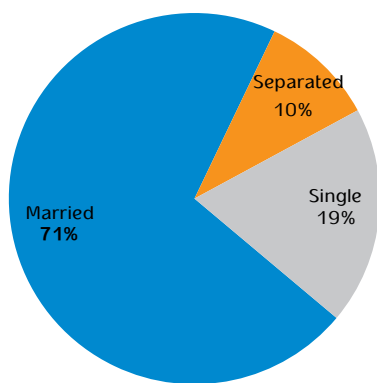
1. In the general sample, we found **high levels of support for nudges**, particularly, **automated appointment making for periodic checkups, a health-related 'traffic light' coloring scheme for products and alerts about credit card limits**. In contrast, a relatively low level of support was generated for nudges that prompt **students to sign off on a pledge to not cheat before taking an exam, distance candy from supermarket cashiers and requests to register for organ donations upon issuing or renewing driver's licenses**.
2. Respondents from the non-Haredi Jewish sector expressed greater support for most nudges than respondents from the ultra-Orthodox sector and more support than recorded from the Arab sector.
3. In the ultra-Orthodox community, there was **strong opposition to the nudge that prompts requests for organ donations**, and in the Arab sector, there was **opposition to distancing candy from supermarkets' cashiers**.
4. The nudges that received the highest levels of support were those primarily oriented **towards the individual** (as opposed to society in general) or nudges that **encourage conscious thinking** (as opposed to those that rely on automatic behavior).
5. There were some significant differences in the rates of support for certain nudges among respondents based on political affiliation, educational level and age.
6. No significant correlation was found between the **level of trust in government** and support for nudges, either across the entire sample or within each separate sector.
7. In comparison with specific nudges that were examined around the world, the rate of opposition to the use of nudges in Israel was among the lowest of all surveyed countries.

Background and Objectives. Public attitudes towards government intervention can be of great importance for the effective planning and implementation of public policy in areas such as healthcare, economics, consumerism, safety and the environment. In recent years, the use of nudges has increased around the world – a 'soft' form of intervention that does not limit freedom of choice. Surveys in several countries have shown general support for the use of many nudges, though there has not yet been a comprehensive examination of the Israeli public's views on the subject. Israel's large heterogeneity (in terms of nationality, religiosity, economic

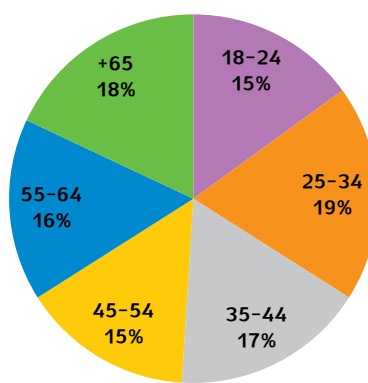
gaps, political positions, etc.) intensifies the need to explore the attitudes of the country's various populations towards different nudges. This is the goal of our study.

Sample. We commissioned a national telephone survey of a sample representative group, conducted by the Geocartography Research Institute during March 2017. The responses of 609 participants were collected. The sample included 507 respondents from the Jewish sector (82%) and 102 respondents from the Arab sector (17%). We also oversampled the ultra-Orthodox population, to obtain 100 respondents from that group.

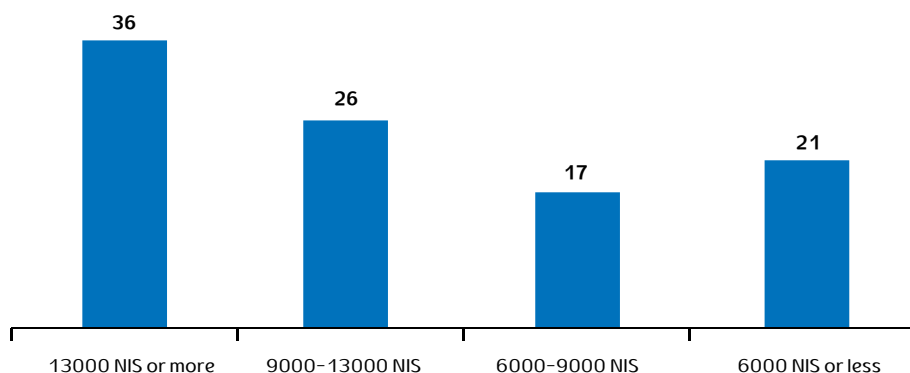
Marital Status



Respondents' Age

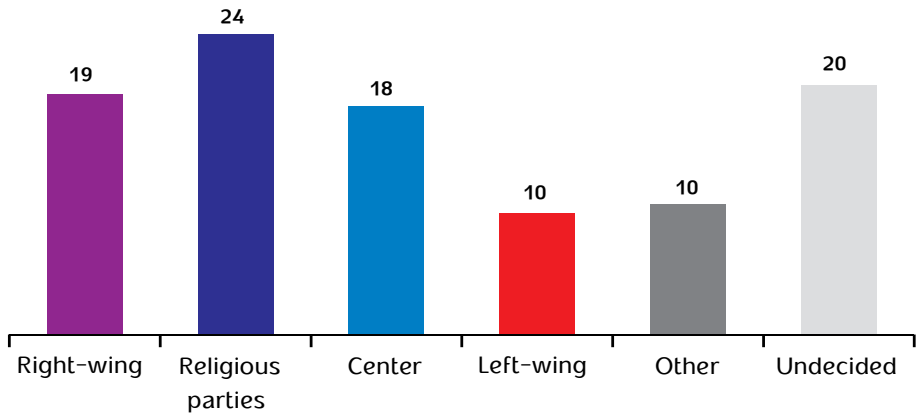


Household Income

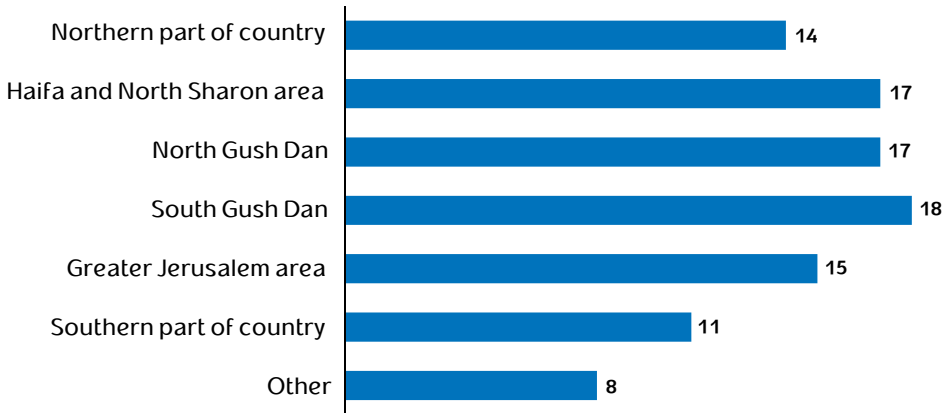


* All the charts that appear in this report were produced by its authors.

Political Affiliation



Location of Residence



Tools and Methodology

The survey began with a brief introduction about the purpose of the study, which was followed a description of 15¹ nudges to respondents, who were then asked to express their opinions, on a scale of 1 (very much opposed) to 5 (very much in favor). The reading order of the nudges was randomized. Next, the respondents were asked to express their positions on two non-nudge items, which served as points of comparison. The respondents also expressed their confidence (or lack thereof) in the government's ability to act on behalf of Israeli citizens and the government's desire to do so (two separate items).

Nudges as Presented to Survey Participants

Caloric value of menu items	1. Restaurants will display the caloric value of each item on their menus.
Health-related 'traffic light' icon on food products	2. Food manufacturers and marketers will add a health-related value label to their products, based on Ministry of Health criteria. Healthy products will be marked with a green label and unhealthy food stuffs with a red label.
Organ donations registration with driver's license	3. When issuing for or renewing a driver's license, drivers will be asked to indicate whether they are willing to join an organ donation database.
Distancing candy from cashiers	4. Food chains will not display candy for sale at the cashier stations.
Default privacy settings for online social networks	5. When content (posts or images) is uploaded to a social network, it will only be available to members, unless the user chooses another option.



1 Two nudges that were included in the original survey ("Towels left on racks during a stay at all Israeli hotels will not be washed, so as to save energy and water, and thus help the environment." and "In every will, a clause will be added stipulating the allocation for charity.") were discovered to be incomprehensible to many respondents and problematic from a psychometric perspective. Therefore, these two nudges were not included in the analyses of the study's results.



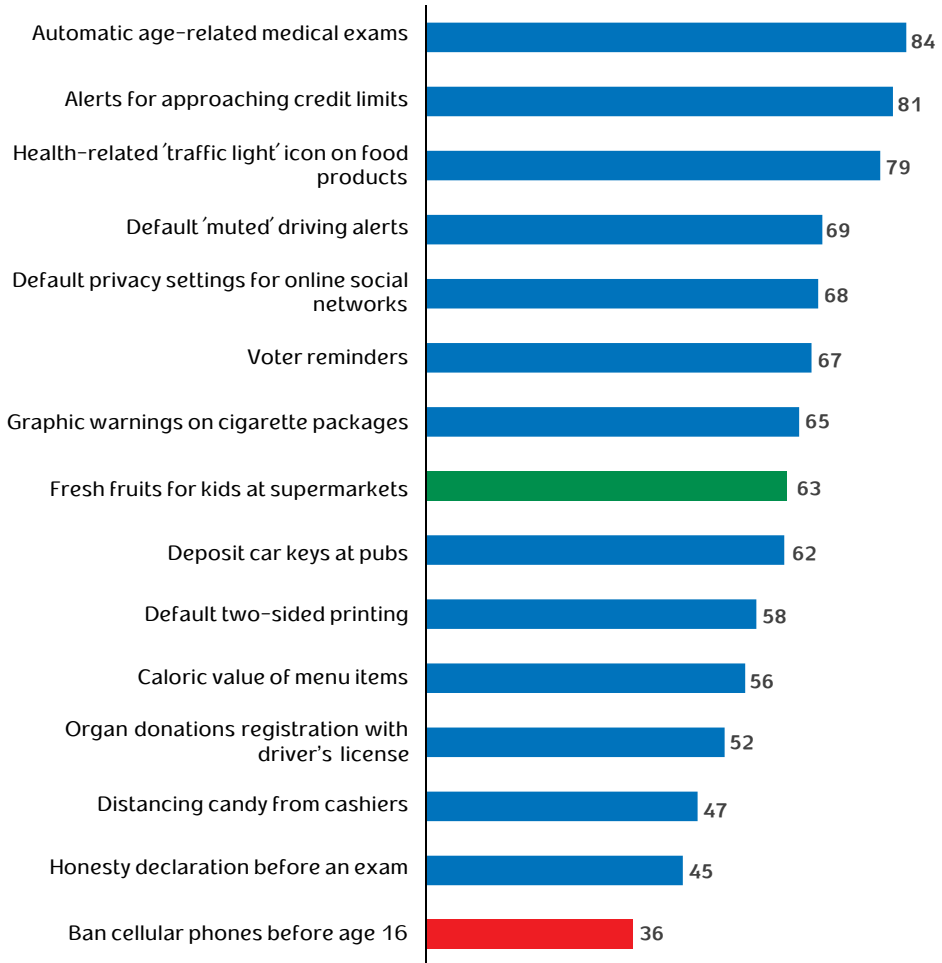
Graphic warnings on cigarette packages	6. Cigarette companies will print a visual description of the damage caused by smoking, such as a picture of black lungs, on cigarette packages.
Alerts for approaching credit limits	7. Credit companies will alert their customers (by email or SMS) as soon as they approach their credit limit.
Voter reminders	8. A day before elections, voter reminders will be sent (via email or SMS), with instructions on how to get to the polls.
Default two-sided printing	9. In new printers, manufacturers will specify that printing will take place on both sides of the page, unless the user selects otherwise.
Default 'muted' driving alerts	10. When using mobile navigation applications (such as Waze) while driving, messaging services (SMS or WhatsApp) will be muted, unless the driver specifies otherwise.
Automatic age-related medical exams	11. The HMOs will automatically set and send appointments to their patients for age-appropriate medical exams (such as a mammography for early detection of breast cancer or colonoscopy for the detection of gastro diseases).
Deposit car keys at pubs	12. Pubs and clubs will enable drivers to deposit their keys at the entrance. Drivers will receive their keys back after they pass a breathalyzer test that shows that their blood alcohol level is normal.
Honesty declaration before an exam	13. Before an exam, students will sign a form stating that they promise not cheat.
(The following non-nudge items were included as comparison items only and were always asked at the end of the survey):	
Non-nudge negative	14. Cell phone use will be prohibited for anyone under the age of 16.
Non-nudge positive	15. A basket with fresh fruits will be placed at supermarket entrances, so that every child who enters will be able to take a fruit for free.

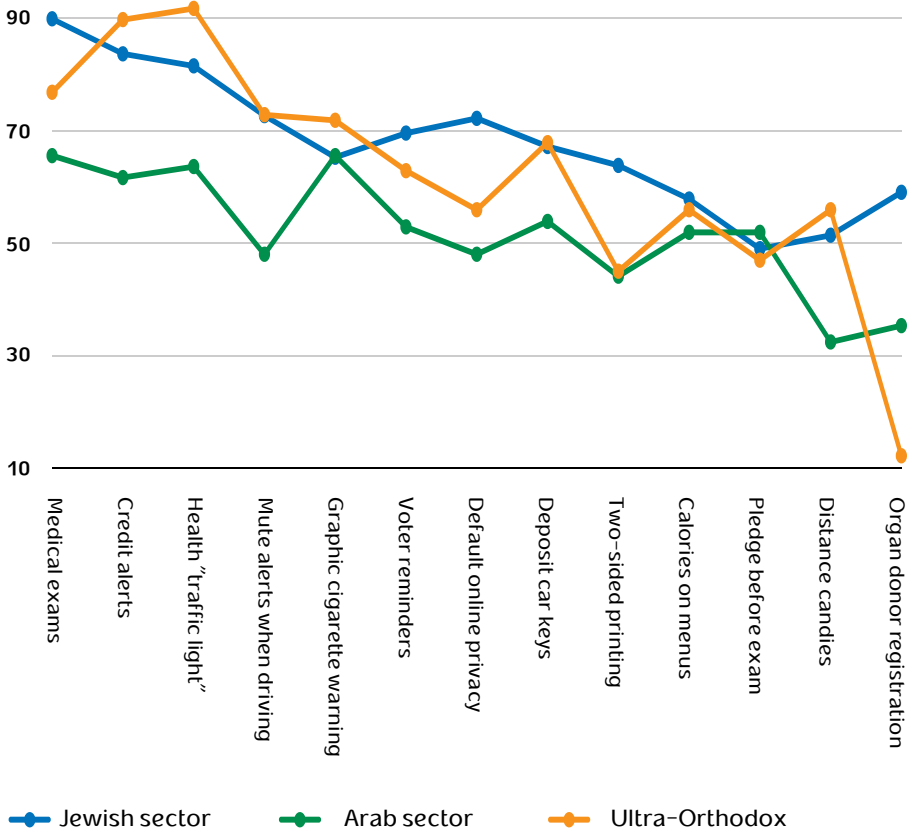
Results

Most nudges received a high level of support (over 60%), while very high support (about 80% or more) was registered in favor of three noteworthy nudges: automatic medical exams, credit alerts and health-related 'traffic-light' icon.' These three nudges also received the highest levels of support from both the non-Haredi and ultra-Orthodox sectors. In the Arab sector, support was significantly lower for most nudges, though graphic warnings on cigarette packages received a higher relative rank of support compared with other surveyed groups. Opposition to nudges among the ultra-Orthodox and Arab sectors was recorded mainly for the registration of organ donations while issuing / renewing a driver's license. The Arab sector was strongly opposed to distancing candy from supermarket cashiers. There was also low support in all sectors surveyed for students pledging not to cheat before taking a test. In addition, adding the caloric value of items to restaurant menus did not generate much support. In the ultra-Orthodox and Arab sectors, but not in the non-ultra-Orthodox Jewish sector, we noted reservations regarding the default definition of two-sided printing in printers.

In total, the number of nudges that received the support of a majority (over 50%) of respondents was 12 in the non-Haredi Jewish sector, 10 in the ultra-Orthodox sector and eight in the Arab population group.

Rates of support for nudges in the entire sample



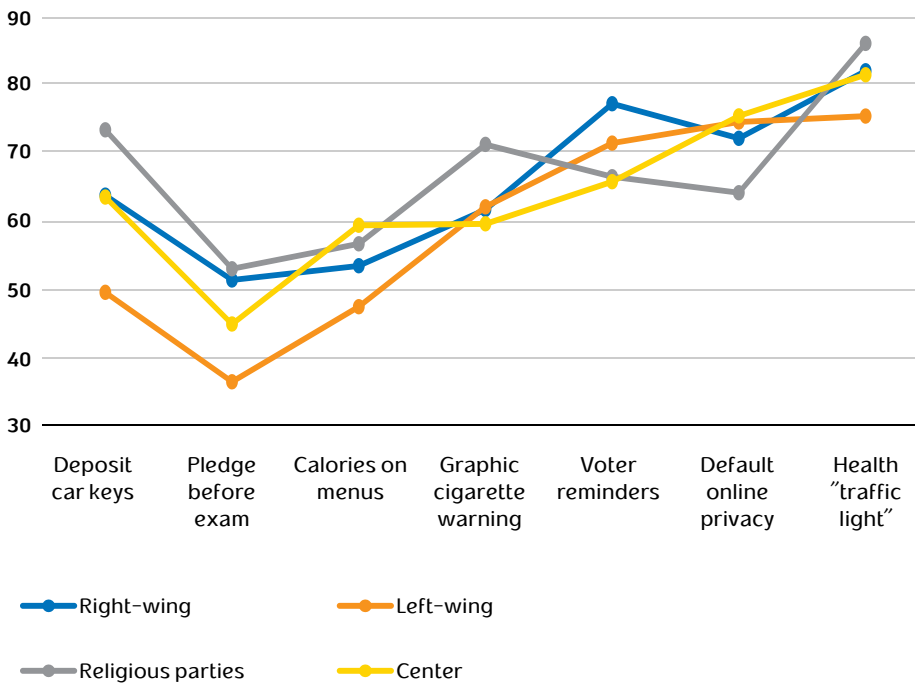


Left-wingers Like Some Nudges Less than Everyone Else

Overall, average support for nudges was very similar (approximately 66%) for respondents with all the different political views. However, there were some specific nudges where we discerned differences based on political orientation. Left-wing voters, in comparison to respondents who belong on the rest of the political spectrum, were less supportive of nudges for depositing car keys at pubs/clubs, having students sign a pledge to not cheat before an exam, displaying the caloric information of items on restaurant menus and a health-related 'traffic light' for food products. Voters for religious parties, in addition to their opposition to the introduction of organ donation registration while issuing or renewing a driver's

license, were less supportive of default privacy choices on the Internet (a finding that may be more due to general opposition to online social networks than to a specific nudge). Religious party voters also expressed greater support than the rest of the respondents for adding graphic warnings on cigarette packs. Meanwhile, Right-wing voters supported the sending of reminders to voters at a higher rate than the rest of the surveyed sample. Out of all the groups surveyed, the support rates of centrist voters most similarly reflected the attitudes of the entire sample.

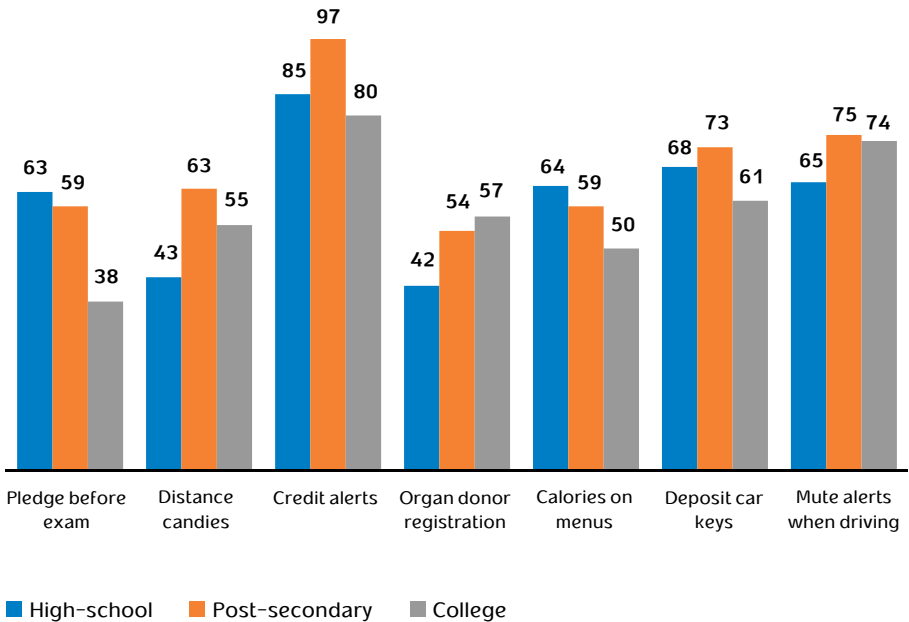
Nudges with differences by political affiliation



Post-Secondary Education: Nudges' Top Supporters

The highest support for nudges (71% on average) was found among respondents with a post-secondary education², compared with slightly lower support from other groups (66%). Particularly conspicuous was the high level of support that people with a post-secondary education had for the delivery of credit limit alerts, distancing of candies from cashier stations and depositing of car keys at the entrance to places of entertainment. In contrast, those with a college degree objected to the request for the signing of a pledge to not cheat before an examination and supported at lower levels than the rest of the respondents the nudge of adding caloric information to restaurant menus. Those with a high school education or less objected to distancing candy from cashier stations and to registering for organ donations while issuing or renewing a driver's license.

Support for nudges by education level



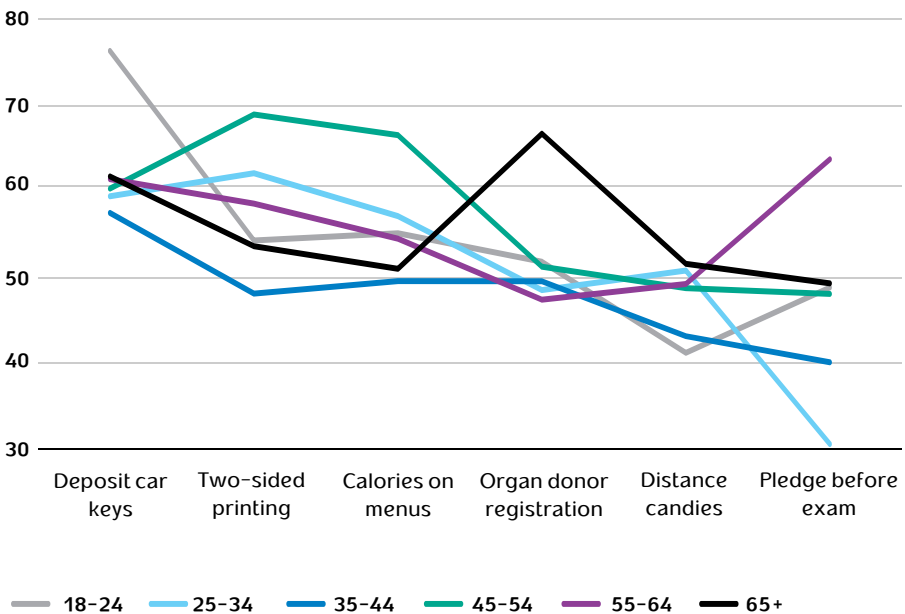
² Matriculation certificate holders and matriculation studies.

Age Only Plays a Role in Certain Nudges

In general, there were no significant differences in levels of support for nudges, as measured by age distribution, with three exceptions:

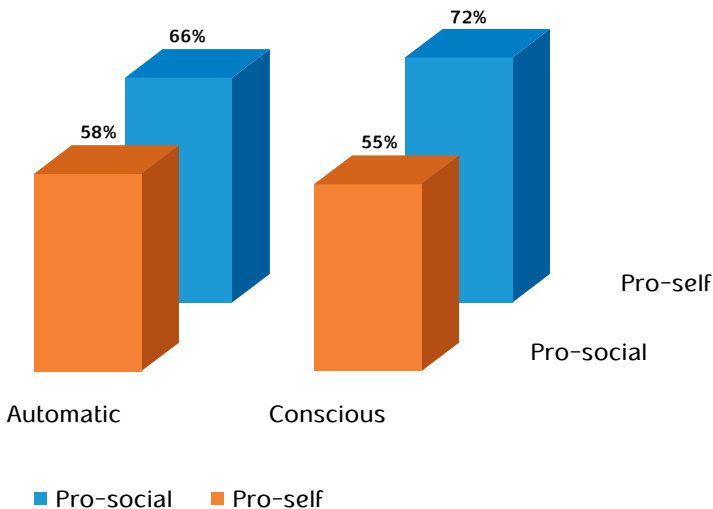
- A. As expected, those aged 65 and over supported registration for organ donations at a high rate (67%), in comparison with younger age groups (50%).
- B. Respondents aged 18-24 expressed greater support (76%) than other participants (60%) for depositing car keys at pubs. It's possible that younger people are more acutely aware of the danger of drunken driving, as well as their own difficulty in avoiding such situations. As such, this cohort may opt to use this nudge as a sort of preemptive mechanism.
- C. A similar gap was also recorded in the support for having students sign pledges not to cheat prior to taking a test: those aged 45 and over support this nudge much more (54%) than the younger strata (39%), on average.

Nudges that showed differences by age



People are More Supportive of Nudges that Encourage Informed Thinking or Benefit the Individual

Some nudges encourage a person to engage in active thinking (for example, adding caloric value to a restaurant's menu encourages a more informed comparison). On the other hand, some nudges rely on automatic behavior and habits (for example, setting a default for two-sided printing takes advantage of people's habit of not regularly checking a printer's settings). We found that support for nudges that encourage informed thinking is significantly higher than the support for nudges that rely on automatic behavior. For example, the two nudges that received the highest levels of support (automatic scheduling of medical exams and credit limit alerts) are those that are based on informed thinking. Meanwhile, the two nudges that received the least amount of support (candy removal and registration for organ donation) use more automated behavior. The survey also shows that support for nudges aimed mainly at benefiting the individual (e.g., automatic scheduling of medical exams) is higher than those whose main goal is to benefit the wider society, usually at the expense of the individual. In examining these two factors together, we found that nudges that both encourage informed thinking and pro-self behavior received the highest levels of support.



No Correlation between Trust in Government and support for Nudges

Support for nudges run by the government (for example, voting reminders or organ donor registration) was not significantly different from support for nudges operated by private organizations (such as credit limit alerts or two-sided printing). Thus, nudges operated by the government received an average of 65% support, while those run by private organizations were supported at a very similar rate of approximately 63%.

These findings are consistent with the a very weak between support for nudges and respondents' confidence in the government's ability and willingness to act on behalf of its citizens (two items that appeared at the end of the survey).

Although there were significant differences in the level of trust in government in all three surveyed sectors (non-ultra-Orthodox, ultra-Orthodox and Arab), support for nudges within each sector was similar for respondents who expressed low, medium or high levels of confidence in the government's ability and willingness to act on behalf of the citizenry.

One possible explanation for this phenomenon may be related to the fact that the nudges in our survey were presented to respondents without mentioning the government's role in their implementation. In contrast, previous surveys conducted around the world explicitly stated this fact. Therefore, the relatively high level of support found for nudges throughout this survey can perhaps be attributed to reflecting the respondents' actual preference, one that is not confounded by political affiliation.

The Objection Rates to Certain Nudges in Israel is Lower Compared to the Rest of the World

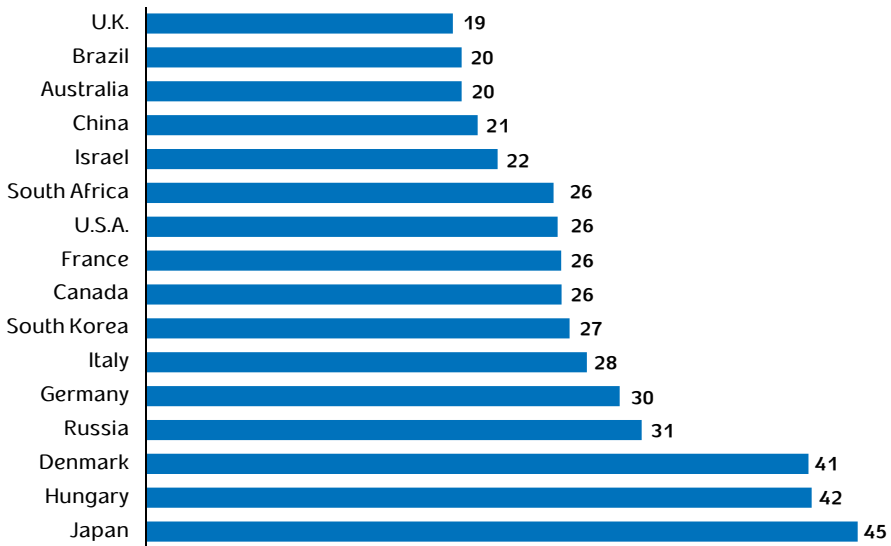
The survey included four nudges that were also examined in other countries over the past two years: adding caloric values to menus, providing a health-related 'traffic light,' registration for organ donations and distancing candy from the supermarket cashiers. Because the other surveys used different methods of measurement, the comparison made here is based on **rate of objection** (in the Israeli survey,

respondents who either answered that they were 'very opposed' or 'opposed'; in international surveys – respondents who said they 'disapprove').

As such, our survey shows that the objection rate to these four nudges is lower in Israel compared to other countries. Only 22% of respondents in Israel (on average) objected to these nudges, which is similarly low as the 19% rate in the U.K., where the lowest rate of opposition to these specific nudges was found, based on the international surveys.

However, since this is a comparison of specific nudges only, a more comprehensive comparative study is still needed to explore the attitudes of the Israeli public in comparison to other countries regarding the use of other nudges, specifically, and the use of behavioral tools in general.

Objection rates for specific nudges surveyed in other countries



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Credit for Small and Medium Businesses: The Key for Growth?



ר ש ו ת נ י י ר ו ת ע ר ך
ISRAEL SECURITIES AUTHORITY

New Options for Financing Small and Medium Businesses through the Capital Market

Prof. Shmuel Hauser Chairman, Israel Securities Authority (ISA)

Adv. Offir Eyal Senior Advisor to the ISA Chairman and Director of ISA's
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The importance of small- and medium-sized businesses to Israel's economy is enormous. These firms also constitute the vast majority of businesses in Israel, and employ the overwhelming majority of workers in the country's business sector. However, these organizations face severe financing difficulties, mainly because such financing relies almost exclusively on banking institutions, and the financing terms have been significantly toughened over the last few years. Bank financing is the main channel for raising funds because, on the one hand, these are businesses that are too small to generate much interest by institutional investors, and, on the other hand, the capital market is too big to be of relevance to such businesses.

In recent years, the Israel Securities Authority (ISA) has initiated and implemented, with the support of the Ministry of Finance and Ministry of Justice, more than 100 reliefs in regulation. These reliefs are intended to create balanced regulation for all supervised entities, based on protecting investors, encouraging competition, reducing investment costs, as well as the costs absorbed by these same supervised entities, and creating a supportive business environment. The reliefs were not randomly selected. Rather, they were developed - in an orderly and comprehensive manner - to remove regulatory barriers and incentivize every type and size of company that is considering financing its activities through the capital market.

However, upon examining the range of reliefs that have been implemented, as well as the current array of incentives available to companies to mobilize funding through the capital market, the gap is still apparent. Specifically, this chasm is noticeable with regards to the options of financing through the capital market available to companies that are neither small nor large.

The ISA's position is that these companies can potentially serve as a real engine for growth in the Israeli economy. Therefore, it is inappropriate to give up on the idea of these businesses being financed through the capital market, and at more attractive rates than those offered by the banks.

In this context, the ISA has promoted and continues to promote a variety of courses of action, including bringing small and medium (mainly) companies to the Tel Aviv Stock Exchange, or keeping them there - by easing the applicable rules; allowing small- (less) and medium-sized companies to avoid getting bogged down in regulation by using a 'crowd funding' model or P2P (Peer to Peer) lending; and launching new products on the Tel Aviv Stock Exchange that support investment in small- and medium-sized companies. The most innovative option of all is the creation of a new trading framework for small- and medium-sized companies that reduces regulation and changes the rules of the game, both in terms of disclosure obligations and corporate governance, so as to encourage small- and medium-sized companies to register for trading.

Background

The importance of small- and medium-sized businesses to Israel's economy is enormous. They are an important factor in increasing growth, production capacity and economic prosperity. These businesses also contribute to competition and are an important source of new jobs across diverse geographic areas.

There are about 520,000 businesses in Israel that are defined as tiny-, small- or medium-sized. They account for 99.5% of all businesses in Israel and employ about 61% of workers in the business sector. The contribution of small- and medium-sized businesses to Israel's GDP is 54%.

Yet despite these impressive data, small- and medium-sized businesses face financing difficulties, especially in recent years. The reason for this is probably that these companies tend to rely almost exclusively on bank financing. However, in the years following the global economic crisis (2008), bank financing became more rigid towards small- and medium-sized businesses. The data show that the costs of bank credit for small businesses are double that of credit to large businesses, although the credit losses of banks from small- and medium-sized businesses do not seem to justify this gap. Moreover, the Israeli banking system is very centralized. The two large banking groups hold about 57% of the country's total assets, and the five largest groups together possess about 94% of all banking assets. It should be noted that small- and medium-sized businesses have almost no possibility of receiving credit from non-banking sources, since, as stated above, institutional investors cannot justify such small investments in resources, while the barriers to entry into the capital market for small and medium businesses are prohibitively high.

The importance of small- and medium-sized businesses, on the one hand, and their financing difficulties or high financing costs, on the other, justify new and creative thinking about how to ease and remove barriers to financing. The intention, of course, is not to finance these businesses at all costs (literally), but rather to allow them to choose between a range of options, whereby the 'price' of their financing will be determined according to the principles of a free and competitive market and not according to desires, preferences or limitations such as those of the banking sector.

Of course, this is not just an Israeli issue. Many reports - for example, by the OECD – point to the importance of small- and medium-sized businesses to the economy, the difficulties they experience in obtaining financing and credit, the need to develop additional tools for their financing, and the most common ways in which governments intervene in this context – by establishing capital funds or granting capital investment benefits.

The ISA's Activities in Recent Years and their Effects on Small Business Financing

In recent years, the ISA initiated and implemented, with the support of the Ministry of Finance and the Ministry of Justice, more than 100 reliefs in regulation. These reliefs are designed to create a balanced regulation for all supervised entities, based on protecting investors, encouraging competition, reducing costs for investors and supervised entities, and creating a supportive business environment. A significant part of the reliefs in regulation is intended to restore the interest of quality companies in financing their economic activities via the capital market and Tel Aviv Stock Exchange.

These reliefs were not chosen by chance, but were specifically designed to remove, in an orderly and comprehensive manner, regulatory barriers and incentivize every type and size of company that is considering financing its operations via the capital market.

Examples of these regulatory reforms include:

- (1) Providing relief for Hi-Tech companies, which enables these firms companies to, among other things, file financial reports in English, in accordance with US GAAP, and receive analysis at subsidized costs as well as various tax incentives.
- (2) Promoting the 'crowd funding' and P2P (Peer to Peer) lending for financing small companies (detailed below).
- (3) Easements for small- and medium-sized companies, including: exemption from iSOX and cancellation of the requirement for quarterly reports.

- (4) Respite for companies that are considering initial public offering. These reforms apply to, among other things: approval of the terms of employment of a controlling shareholder and his/her relative/s as well as officers, exemption from appointment to the "balance committee", possibility of publishing a shelf prospectus at the time of initial issuance, exemption from requirement to file report about effective internal oversight, and allowing meetings with classified investors prior to commence before issuance proceedings have begun.

In this context, it is worth mentioning the recent demutualization of the Tel Aviv stock exchange that was approved by the Knesset, which deals with the separation between stock exchange owners (banks and institutional investors) and those who provide trading services, thereby strengthening the infrastructure of stock exchange activity as an important source of competition for capital resources. The amendment of the law regarding demutualization is expected to promote the status and efficiency of the stock exchange, and even allows for the establishment of a new secondary stock exchange.

In fact, the ISA has promoted and continues to promote solutions that will enable financing through the capital market, from the stage in which entrepreneurs start developing a product in their garage until the stage in which an established company goes public.

However, upon examining the range of reliefs that have been implemented, as well as the current array of incentives available to companies to mobilize funding through the capital market, the gap is still apparent. Specifically, this chasm is noticeable with regards to the options of financing through the capital market available to companies that are neither small nor large.

These companies may be too big for the 'crowd funding' model, but too small for institutional investors.

But we maintain that we should not give up on the idea of financing such companies through the capital market. Indeed, we believe that the most viable and equitable options for financing small and medium businesses are through the capital market.

For this purpose, we will present four courses of action, each of which may promote the financing of small businesses through the capital market. These are not alternative methods of action, but methods of action that can be implemented

simultaneously, so that their cumulative effect will achieve the desired goal. As will be shown, two of these methods of action have already been implemented or are in advanced stages of implementation. One course of action is in the advanced stages of implementation, while another approach is still in the development stage.

The underlying concept of the four methods of action is similar: recognition of the fact that one size does not fit all and that the existing regulatory framework is not sufficiently friendly towards small- and medium-sized companies. Therefore, in order to enable these companies to raise capital or debt through the capital market, new and creative ways must be found to make them accessible to the capital market, or the capital market to them, in such a way that the benefit of raising capital or debt from the public exceeds the cost involved.

The methods of action are as follows:

First Course of Action: Bring or Keep Small- and Medium-Sized Companies into the Tel Aviv Stock Exchange by Easing Relevant, Applicable Rules.

The goal of this process is to reduce the costs of listing on the Tel Aviv Stock Exchange to small- and medium-sized companies. In this context, the ISA initiated and recently implemented a number of significant amendments aimed at reducing regulatory costs, specifically to small- and medium-sized companies, in order to encourage these businesses to list for trade on the Tel Aviv Stock Exchange.

Public companies dedicate a significant portion of their time and money to the implementation of regulatory directives. But small- and medium-sized companies devote a much larger proportion than large firms. Research shows that in small companies (market value of up to NIS 300 million) regulatory costs can reach 9% of the company's value, while in large companies the regulatory costs are only 0.1% of the value of the company.

Therefore, in recent years the ISA has taken steps to reduce the scope of companies' regulatory burdens and to cancel certain disclosure requirements, in order to enable management to allocate significant portions of their companies' resources for business development.

For this purpose, the ISA initiated a series of concessions to 'small corporations,' defined as a corporation whose shares or participation units are held by the public

and whose value is less than NIS 300 million, is not included in one of the leading stock exchange indices and is an entity whose nominal bond value, held by the public, is less than NIS 200 million.

Within this framework, the ISA has promoted the following measures (which have already been implemented):

- (1) The ISA promoted legislation to eliminate the requirement of small companies (as defined above) to file quarterly financial reports in the first and third quarters of the year. This reform is relevant to more than 180 companies, out of about 530 companies reporting that their securities are traded on the stock exchange. As soon as it's implemented, quite a few companies will be eligible for this easement.

In this context, it is noteworthy that as of June 6, 2017, 123 companies and partnerships whose securities are traded on the stock exchange have announced the implementation of this change, with respect to the first quarter reports of 2017.

- (2) The ISA facilitated an exemption from publication of reports on the effectiveness of internal control (ISOX), so that small corporations will be required to include only a limited declaration by their managers.
- (3) The ISA promoted the granting of an exemption from filing a report regarding exposure to market risks and the way this risks are managed to small corporations whose exposure to market risks deriving from financial instruments is immaterial, in accordance with how materiality is determined.
- (4) The ISA made it easier to attach a valuation to reports by raising the threshold of materiality in connection with the inclusion of a valuation to 20% (instead of 10%).
- (5) The ISA streamlined the inclusion of reports of affiliated companies by raising the threshold in the interim financial statements of the companies included on the equity basis to 40% (by way of leaving the inclusion threshold for financial statements at 20%).

Second Course of Action: Allow Small and Medium Businesses to be Exempt from Regulation

As part of this process, the ISA promoted a legislative amendment allowing companies to remain nearly totally exempt from securities laws while raising

significant sums of money by means of 'crowd funding' or P2P. In fact, this is an arrangement that waives much of the regulation related to the raising of small capital or debt. The sums that were ultimately approved to raise as part of the arrangement (up to NIS 6 million per annum) may not only be attractive to only small companies.

The model of 'crowd funding' (on which the legislative process has acted) is a fundraising approach aimed at the general public and facilitated via an Internet platform. The idea is to raise small sums from a large number of people.

The regulations affecting 'crowd funding' activity have recently been approved. These include the possibility of corporations raising capital as well as issuing debt. The regulations cover the mechanism for 'crowd funding', including the maximum permitted investment volume for investors, maximum permitted amounts of funds to be issued to corporations, supervision by the ISA of the companies operating the Internet recruitment platforms (referred to as the "Offer Coordinator"), requirements for registration as a bid coordinator, and more.

According to the regulations, a company may raise capital from the public via this channel of up to NIS 4 million over the course of any 12 month period, or an additional NIS 1 million (up to a maximum of NIS 6 million) if the business has successfully passed certain examinations, or when the a venture capital fund or angel investor (called a 'leading investor') participates in an investment round of no less than 10 percent.

It should be noted that there is another business model for financing mass loans. According to this model, the investor only determines the amount he/she wants to invest and the level of risk he/she wants to assume. Meanwhile, the platform chooses and distributes to specific loans in its pool (Peer to Peer lending).

Currently, this model is in the advanced stages of the legislative process.

Third Course of Action: Bring New Products for Investing in Small and Medium Businesses to the Tel Aviv Stock Exchange

Within this framework, the ISA promotes and supports the establishment of high tech funds and of traded funds, as a means to finance small and medium businesses. These funds will provide accessibility for small- and medium-sized businesses to the capital market without them having to register for trading on the Stock Exchange

(with all that implies); enable interested investors to diversify their investment portfolio and be exposed to non-tradable investments; and facilitate a diversification of investment products on the stock exchange.

High-tech funds are designed to encourage investment of Israeli capital in fledgling high-tech companies, and enable Israeli investors to benefit from the success of these companies. Legislation has already been enacted so that high-tech funds specializing in investments in Israeli high-tech companies that are engaged in R & D, including those that are not traded on the stock exchange, can be established. These funds will be established as closed mutual funds that can be traded on the stock exchange, subject to various adjustments.

In addition, an interministerial committee established by the ISA and the Accountant General, which is currently concluding its work, has examined and recommended the establishment of designated commercial funds with the aim of creating additional sources of credit for small- and medium-sized businesses. In the first stage, the committee recommended that the funds be provided by a state guarantee for the debts that will be raised.

The committee's recommendations include many other arrangements regarding the duties of the fund manager, tax implications, types of securities that will be issued, rules for listing and trading on the Stock Exchange, and more. In general, the committee's recommendations seek to replicate and adapt the model that has already been successfully implemented with respect to REIT funds for investment in investment property in small- and medium-sized businesses.

Fourth Course of Action: Create a 'Stock Exchange' or a Designated List for Small- and Medium-Sized Companies

This is a completely different approach from what is described in the first course of action: "If Muhammad does not come to the mountain, the mountain should come to Muhammad." The aim of this method of action is to create a new, reduced regulatory framework for small- and medium-sized companies that could serve as an incubator for publicly traded companies, which will one day reach the big leagues. In this context, it will be possible to establish a new trade list or a dedicated stock exchange, with various rules - both in terms of disclosure obligations and corporate governance - that will encourage small- and medium-sized companies to register.

Public companies dedicate a significant portion of their time and money to the implementation of regulatory directives. As noted, small- and medium-sized companies devote a much higher proportion than large companies, so that listing the former in the current format is not worthwhile. As such, the existing rules described above can be remedied, in the hope that reducing regulatory costs will affect the conduct of these small and medium businesses.

However, there is another, completely different, way to keep small and medium-sized companies in the capital market or encourage them to register for trading. This could be done by establishing a separate stock exchange or designated list on the Tel Aviv Stock Exchange, whose rules would be "tailored" to the needs of small- and medium-sized companies. As a result, these businesses would be able to raise capital at low threshold requirements and lower regulation, without sacrificing the appropriate protections afforded the investor.

It should be noted that models for designated stock exchanges for small- and medium-sized companies already operate around the world. The data show a 92% increase in the number of companies traded on secondary markets worldwide since 2002, while the amount of businesses traded on main stock exchanges only grew by 13.5% during the same period.

Of course, the possibility of establishing a designated stock exchange naturally raises a large number of questions and issues:

- (1) Will this be a completely new stock exchange for small- and medium-sized companies with separate branding, or will it be a new list under the existing stock exchange?
- (2) What are the lessons that can be learned from the establishment and operation of stock exchanges for small businesses elsewhere in the world, and some that have not lived up to their expectations?
- (3) What should be the level of supervision of the designated stock exchange?

It will be necessary to design an effective, balanced monitoring model that will provide protection to investors in the capital market and at the same time not impose excessive costs on companies in a manner that will stifle the market. Some of the designated stock exchanges around the world adopted a model in which a nominated advisor (NOMAD) who reports to the local securities

authority or stock exchange performs the supervision. The advisor provides comprehensive business, legal, accounting and consulting services to companies: from registration to trade, up to current reporting and secondary listing of securities.

- (4) Who is authorized to invest in the designated stock exchange? Is it justified to impose restrictions on entry of investors as a result of the reduced supervision?

On the other hand, it may be justified to allow anyone to invest in companies that will be traded on the designated stock exchange, in order to increase demand. It may also be justified to give various incentives to investors on the designated stock exchange, while limiting the amount of investment allowed to each investor.

- (5) How will the securities issued on the designated stock exchange be offered to the public? Will it be by means of a prospectus? A 'thinner' document, to be signed by the company and whose approval will be predicated on an examination to be performed by the designated consultant?

- (6) What will be the disclosure and reporting obligations of the companies on the designated stock exchange? Will the financial reports be quarterly or semi-annual? And what will these reports will include? According to which accounting rules will they be conducted?

It may be justified to reduce the obligation to attach various documents to reports. It is also possible that in terms of the obligation to publish immediate reports, it makes sense to change today's accepted rules.

- (7) What about the rules of corporate governance?

It may also be justified to ease the rules of corporate governance that apply to companies that will be listed on the special list, specifically with regards to the definition and appointment of independent directors, approval of controlling shareholder transactions, number of independent committees, and the appointment of an internal auditor.

- (8) Are institutional investors expected to invest in the designated stock exchange?

If not, what is the liquidity level expected to be?

- (9) There may also be justification in making changes to the enforcement measures that the ISA will take against violations of the law perpetrated by these

companies. In this context, the question arises as to what will be the correct balancing point between the level of enforcement and risk that investors will be exposed to in view of the other easements offered.

All these will be examined within the framework of a committee set up by the Minister of Finance and Minister of Justice to examine possibilities for the establishment of an additional stock exchange.



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