Limitations on the Use of Cash in Israel

A NEW LAW

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General

In February 2018, following a long and bitter battle that caused a three-year delay in the legislative process, an agreement was finally reached between Israel's orthodox and religious coalition parties and the non-religious parties of the coalition. This agreement enables the Israeli Parliament (the Knesset) to legislate a new law that limits the use of cash in Israel. After voting within three readings in the Knesset Plenum, the new law will go into effect on January 1st 2019 for cash and July 1st 2019 for checks.

Because of the religious parties' fierce objection to the bill, the final version looks nothing like the original one submitted to the Knesset in 2015. Indeed, critics say that the bill underwent such significant changes that have resulted in it being almost completely emptied of its content.

As mentioned in my previous articles (see list of publications below), the changes were a result of the demands of religious parties who were concerned about satisfying their voter's cash needs. Indeed, their constituencies are heavy cash users. There was therefore a fear that these populations, communities (mainly religious ones), and transactions, would be affected by its provisions.

Even if the global debate about whether cash limitations diminish tax evasion is ignored (although this has yet to be proven) there is no doubt that the Israeli government totally lost track of its original objective when finalizing the bill. Indeed, the wide range of exemptions and exceptions resulted in a law that only applies to sporadic cash users.

Because the government failed to meet its own original goals, the sharp criticism from economists and the media is fully justified. In fact, the question arises whether the final outcome is indeed a battle against criminals or rather a measure against innocent consumers?

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10 years as Currency Department Director, 32 years in the Banking Supervision Department, and 3 years as the Bank's representative to the World Bank and IMF in Washington D.C.

In 2004, Fein became the Director of the Currency Department at the Bank of Israel. He retired in 2014.

The Committee to Examine Reducing the Use of Cash in Israel's Economy - Locker Committee

In 2014, the government of Israel nominated a committee headed by former Director General of the Prime Minister's Office, Har'el Locker, whom was instructed to examine the necessity to reduce the use of cash in the Israel.

The government instructed the Committee to examine limiting the use of cash in order "to combat the black economy in Israel - black market capital, deepening tax collections and expanding the tax base, and fighting economic crime and money laundering".

Without any proof to support their argument, Israeli authorities assumed that limiting the use of cash would automatically heal all illnesses linked to the black economy. The estimation that the black economy in Israel amounts to 22%-23% of GDP was the main driver for the Locker Committee's recommendation to reduce and restrict the use of cash transactions (report published in August 2014).

This despite the fact that the theory that limiting cash usage prevents tax evasion or money laundering has never been proven and that the lessons drawn from terror events of the last few years clearly point out that these were not financed with cash, Israeli authorities were obligated to accept the committee's recommendations which are in line with the global trend to reduce the use of cash.

As discussed in my previous articles, the tax enforcement system in Israel is very weak. But it seems that instead of firstly reforming the system to strengthen it, authorities chose not to face reality and instead selected a "quick fix". Unfortunately, this will most probably not serve the government's aims. On the contrary, instead of diminishing tax evasion, it will only significantly hurt decent people and honest tax payers from the most vulnerable echelons of society.

After adopting the Locker committee's recommendations, a governmental bill to reduce the use of cash was published in July 2015 and submitted to the Knesset. According to the bill and its proposals, "cash" - Israeli banknotes and coins, and foreign currency – will be considered an illegal payment method when the transaction value exceeds NIS 10,000 (US $2,150) for: receipts by a business, payments to a business, payments of salary, donations, gifts and loans to non-relatives (except bank loans); payments to public bodies e.g. taxes. If the transaction price exceeds NIS 50,000 (US $14,000), it is proposed to make cash payments illegal for: receipts by a person not in business, payments between non-business parties, receipts by Israeli lawyers and accountants for certain business services, payments of salary, donations, gifts and loans to relatives (except bank loans).

There will also be a ban on no-name check payments and an exception for transactions made by tourists below NIS 25,000 (US $7,000) or more if a report is filed with the Tax Authority.

The payment method will need to be disclosed when reporting real estate transactions and in the books of business.

Offenders may face a 30% penalty. Business offenders would also have their names published on the Tax Authority's website for 2–4 years. A wilful intent to bypass these rules may result in a 3-year prison sentence.

The Legislation Process

Naturally, any law initiated by the government is supported by the parties regardless of the coalition it is comprised of. However, since the two religious parties which are crucial for the existence of the coalition strongly opposed the law, it was almost impossible to turn the bill into legislation. Habait Hyehudy (a national religious party) and especially the orthodox party Agudat Israel, the two major swing vote parties, strongly opposed the bill to defend their constituency's interest. In fact, both parties represent a large population whose financial transactions are mostly carried out in cash. Both parties carried out a fierce battle to protect their interests and used all means possible to hinder the legislative process. They prevented discussions in the Knesset committees they chair (which are mandatory before submitting the bill for the final readings in the Knesset Plenum) which led to a standstill for a long time. Indeed, it is only until very recently that the agreement between all parties was achieved.

The New Law

In addition to the major allowances from the original recommendations of the Locker Committee, it should also be emphasized that even the recommended limitation amounts were significantly extended.

Law Provisions[1]

According to the new law it is forbidden to pay a dealer or a supplier more than NIS 11,000 [NIS 7,500] in cash - about US $3,000 [US $2,150]. Any transaction above this amount has to be executed with checks, a bank transfer or a digital transfer, debit or credit cards.

Exemptions Ok

1. Transactions between individuals (not businesses) will be limited to amounts that exceed NIS 50,000 [NIS 15,000] – US $14,000 [US $4,250]. Locker recommended 50,000 NIS only for trading used cars among individuals.

2. The limitation of NIS 11,000 – US $3,000 will be effective for wage payments, except wage payments to family relatives and providing gifts, which will be limited to NIS 50,000 – US $14,000.

3. Tourists will be allowed to trade in cash up to NIS 55,000 [NIS 25,000] - over US $15,000 [US $3000].

Groups and Transaction Exclusions

4. The Law provisions will not apply to trade with the Palestinians and non-Israelis from the region and from the Palestinian Authority as their accessibility to alternative means of payment is limited. Cash transactions between region inhabitants and non-Israeli inhabitants and the Palestinian Authority inhabitants, and transactions between Israelis and Palestinians, will not be subject to the new law. However an Israeli citizen will have to report to the Money Laundering Prohibition Authority on any transaction that exceeds 50,000 NIS (US $14,000).

5. Some state institutions and security bodies are exempted from these cash limitations: banks and other financial institutions, as well as part of state authorities such as the Executive Office at the Ministry of Justice, and specific security bodies. Recipients of charity loans (interest-free loans) are excluded from these limitations. As expected, the changes resulted from the requirements of the religious parties and the real needs of its voters; the new law excludes several communities, mainly religious and orthodox ones, from its provisions. These loans which are granted only in cash to religious and traditional people became a broad phenomenon, usually within the activity of the synagogues in Israel. Though in the background critical voices are constantly heard blaming that excluding loans in cash granted to such a large society as the orthodox one from law provisions already extends money laundering.

Religious parties have a respected and central position in the coalition, and fulfil an important role in the government's activity. They deserve the trust and faith that their fight in favour of these communities is fully justified and derived from real cash needs. It should be emphasized that it is totally unacceptable and inconceivable to think they had any improper motives to serve the interests of tax evaders or criminals. Indeed the vigorous fight and strong campaign, mainly led by the orthodox party Agudat Israel, clearly points and proves that there are large chunks of the Israeli population for whom cash is still crucial, as they have a real need for it.

It should be acknowledged that these are unique communities with specific needs even though a large amount of these charity loans are distributed among a large society of borrowers, and each loan is of a relatively low amount. Many people in these communities want to protect their privacy and hide the fact they are recipients of charity without disclosing it to their bank or to their relatives and friends. It should also be mentioned that within these communities women were strongly opposed to the bill as they deemed it disruptive to their privacy and dignity. They do not accept that every single purchase, including intimate needs, is reflected in banking documents. Men of this community are also unlikely to appreciate having all their purchases recorded as they fear the reaction of their religious leadership should it disagree with their activities (from the religious point of view).

Main Lessons

The Israeli case clearly proves that cash is still crucial to many communities. The importance of cash cannot be ignored or eliminated in a blink of an eye.

The exclusion of certain communities and the exceptions that had to be allowed in the bill should send a warning to authorities, not only in Israel, but all over the world. Authorities should realize that they cannot pass laws against using cash so easily without taking into account the true needs of different communities. These initiatives, that can be seen worldwide, will unfortunately not solve money laundering problems but they will harm the most vulnerable populations.

1. Amounts in brackets - Locker Committee's recommendations

Previous publications

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