Socioeconomic Inequality in Israel

A Theoretical and Empirical Analysis

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2016

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Horizontal Inequality in Israel's Welfare State: Do Arab Citizens Receive Fewer Transfer Payments?

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Introduction

It is well known that the Palestinian-Arab citizens of Israel (hereafter Arabs) suffer a far higher risk of poverty than the vast majority of Jewish citizens. Moreover, as the National Insurance Institute (NII) documents year after year, the welfare state in Israel lifts far fewer Arab than Jewish families out of poverty. Compared to a hypothetical world with no redistribution, in 2012 taxes and transfer payments combined reduced the proportion of Arab households in poverty by only 8.4 percent.[1] The parallel rate for Jews was 45.5 percent.

We are aware of only two previous studies of the Arab-Jewish gap in poverty reduction through redistribution. Gera and Cohen (2001) analyzed the first official data set with comprehensive coverage of both the Arab and Jewish populations. Whereas in 2012 poverty reduction for Jews was more than five times greater than for Arabs (up from a ratio of around 4:1 in preceding years), their findings indicate that in 1998 the gap was far lower—about 2:1 (Gera and Cohen 2001:Table 9). At that time the Palestinian residents of East Jerusalem were not included in the Arab poverty rate, yet this alone cannot account for the apparent deterioration of social protection for the Arab poor relative to their Jewish counterparts.

To the extent that the state offers Arabs less protection from poverty than Jews, what are the explanations? Do the socioeconomic and demographic characteristics of the Arab poor render them less likely to be eligible for transfer payments, or reduce their effectiveness? If there is a mismatch between

Arab and Jewish needs, why hasn't the benefit system adapted to it? If the benefit gap is not rooted in compositional differences, then presumably it derives from variation in benefit generosity or inadequate take-up of benefits for which Arab citizens are eligible. If that is the case, is it indicative of unequal treatment of Arabs and Jews by the benefit system?

These questions are not easy to answer, but Lewin and Stier (2002) took an important step forward by carefully comparing Arabs with several other sectors of Israel's population and showing that unequal rates of poverty reduction survive a statistical analysis in which Arab and Jewish households are constrained to have similar attributes. According to this study, the "net" odds of Arab families with children being lifted from poverty were 57 percent of the odds obtained for the largest category of Jews.[2] However, Lewin and Stier's pioneering research was conducted using data for 1996, before the neoliberal reforms implemented in the first decade of the new millennium reined in redistribution by imposing stricter eligibility criteria for cash benefits and reducing their generosity (Aviram, Gal, and Katan 2007).

In addition to providing an updated analysis of redistributional gaps in Israel, the present study makes several additional contributions. To begin with, instead of focusing only on the poor and the degree to which the welfare state lifts them above the poverty line, we look at the entire spectrum of the income distribution. This broader focus is important. Poverty is deeper among Arabs than Jews—meaning they tend to be positioned further below the poverty line.[3] As a result, even if they received the same amount of government assistance, fewer Arabs than Jews would be lifted out of poverty. To compare like with like, we ask whether Arab and Jewish households with similar levels of income before transfer payments receive different amounts of cash benefits.

Another reason for considering redistribution at all levels of the income hierarchy is that although slightly more than half of Arab households remain under the poverty line after the effects of redistribution, a growing entrepreneurial, professional, and commercial middle class has emerged among Arab citizens. Symptomatic of this trend, even though Arab households continue to be strongly overrepresented at the low end and underrepresented at the high end of the income distribution, in the middle they are equally and proportionately represented. Based on the data and methods described below, one-fifth of both Jewish and Arab households are found in the third quintile of the national distribution of market income.[4]

Transfer payments to households have varied purposes and are by no means directed solely at the impoverished or those at risk of poverty. Some benefit programs are intended to insure working people against risks like unemployment or old age. Others aim to compensate specific categories of the population for suffering misfortunes (e.g., disability), or for performing socially valued actions (e.g., child benefits and parental leave). "Categorical" benefits like these are provided irrespective of the income of the recipients. They are especially widespread in Israel (Gal 1998), where many are "loyalty benefits"

designed to reward citizens for contributing to collective projects like immigration and national security (Shalev 2010). Even though this type of transfer income is directed almost exclusively to Jews, its contribution to Arab-Jewish inequality is bound to be understated by studying poverty reduction alone, since the beneficiaries of categorical benefits come from all classes.

Accordingly, our study asks whether inequality between Arabs and Jews in Israel is evident in the magnitude of redistribution through cash benefits to more as well as less economically advantaged households. Since taxes on income (income tax and compulsory social insurance contributions) are another instrument of redistribution, it would be desirable to evaluate differences in the impact of taxes as well as transfers on different population groups. Unfortunately this is not possible because, as we explain below, available data are unsuitable for making intergroup comparisons.

In order to sharpen the analysis we single out two comparison groups that are of particular interest, because while sharing similar economic and demographic characteristics with Israel's Arab citizens they differ in their social and political status and power. One of these groups is the ultra-Orthodox community of *Haredi* Jews. The reported poverty rates of Arabs and Haredim are almost identical,[5] and the two sectors share several poverty risk factors—relatively large numbers of dependent children coupled with low rates of adult labor force participation. However, the Haredim, even those segments ideologically opposed to Zionism, enjoy far greater political clout than Arabs (Cohen and Susser 2000), which they have used to obtain access to a tailor-made system of cash benefits that grants them unique privileges.[6] Members of our second reference group, the Palestinian residents of East Jerusalem, are even more economically disadvantaged than Israel's Palestinian citizens (reported poverty rates are 77 percent and 54 percent, respectively).[7] In addition, as permanent residents without citizenship whose presence in Jerusalem is frequently contested by the Israeli authorities, they enjoy limited capacities to make good on their entitlements to social rights, which for most cash-benefit schemes are in principle no different from those of Israeli citizens (Amusin 2010).

These three population sectors are ideally suited for investigating horizontal gaps between sectors in the redistributional impact of the Israeli welfare state, despite differences in their quantitative weight. Of Israel's total population of around 8 million, Palestinian-Arab citizens are by far the largest of the three minorities (1.3 million), compared with just over 300,000 Palestinians living in Jerusalem. The Haredi population of Israel is more difficult to define, but is believed to number between 500,000 and 800,000.[8]

Data and Measurement

The empirical analyses in this chapter are based on a large household-level data set constructed by pooling the Integrated Incomes and Household Expenditure Surveys (hereafter Income Survey) conducted and collected annually by

Israel's Central Bureau of Statistics between 2007 and 2011. This survey covers most of the population of Israel, in all types of localities except for collective Moshavim or Kibbutzim, and Bedouin living outside of recognized localities.[9] Each annual data set consists of an individual file (N~=35,500) and a household file (N~=15,000). Our effective sample comprises around 175,500 individuals aged 15 or older nested in 73,573 households. The table below shows the distribution of the sample across the four population sectors on which our research focuses (as well as a fifth group—recent immigrants—which we sometimes refer to).

The Income Survey collects information supplied by a representative of the household, who is questioned and requested to provide documentation regarding the incomes of each household member from all sources, including transfer payments. The data set also includes information on the income forfeited by households in direct taxation, but the amounts are imputed from the rates officially in force. Because this *de jure* estimate cannot indicate whether the *de facto* tax burden on households with similar incomes varies across different sectors of the population, this dimension of redistribution cannot be reliably analyzed.

Since private economic lives are typically conducted within families that pool incomes and share expenses, the household is the appropriate unit of analysis when studying income inequality and redistribution. In order to

Table 10.1 Population sectors analyzed and their share of the sample

Sector	*Definition*[1]	*Share*
Baseline Jews	Non-Arab residents excluding Haredim and immigrants	71.0%
Haredim	Household with *yeshiva*-educated adult male[2]	4.1%
Arabs	Arab citizens	11.5%
East Jerusalem	Palestinians resident in East Jerusalem	2.4%
Recent immigrants	Immigrated up to 8 years before the survey	3.3%
All other	Immigrated 9 to 16 years ago or mixed origin[3]	7.7%
Total (n = 75,573)		100.0%

1. Sectors were defined using information on the parent(s) in households with children, or else the household head (and spouse if relevant) if no parents were detected. Since the CBS Income Survey provides incomplete or inadequate information on the status of household members (and hence the composition of households), we devised our own rules and criteria. Further information on these and other technical issues will be provided on request.
2. For a detailed review of possible consequences of using this definition to detect and measure Haredi households, vis-à-vis other options, see (Friedman et at. 2011).
3. Households with inconsistent origin definitions of their constituent individuals were defined as "Mixed."

create a comprehensive household-level data set, we utilized variables from the individual-level file as well as the household file provided by the CBS. In some cases this required pooling data for different members of the same household.

Given that household income received via transfer payments is our main dependent variable, our first step was to differentiate it from all other sources of income. We define transfer payments as household income that originates from either the NII or any other government institution. Traditionally, research on redistribution analyzes the impact of transfer income on market income, meaning income derived from either work or returns on assets. However, the question addressed in the present study concerns the impact of transfer payments on the counterfactual distribution of income that would prevail in their absence. Accordingly, even when using the term "market income" we actually refer to all sources of household income other than transfer payments.[10]

To reiterate, we compare horizontal differences in transfer income while holding vertical inequalities in market income constant. Since transfers do not change in a linear fashion in response to increases in other sources of income, we have divided the income hierarchy of households into five equally sized categories (quintiles). Households with zero market income are a special case, and we treat them as a separate category. Note that transfer payments have been converted to constant values by adjusting for inflation over the five years for which data sets were pooled. In addition, incomes were top- and bottom-coded following Luxembourg Income Study recommendations.[11]

Recognizing that the adequacy of a household's income depends on the number of people that it supports, unless otherwise stated all analyses reported in this study are based on income figures that have been standardized on a per capita basis. However, in keeping with standard practice in studies of income distribution, the denominator in the per capita calculation is the number of "equivalent persons," not the actual number of household members. The rationale is that as the number of persons in a household increases, less additional income is needed to sustain them. No one equivalence scale is considered ideal, but a simple method favored by the OECD is to calculate the number of equivalent persons in a household as the square root of the actual number.[12] This method of standardization results in substantially less deflation of the income of large households than the official Israeli standard.

The importance of the choice of equivalence scales is underscored by a pioneering comparison of Israel and nine OECD countries, in which Buhmann et al. (1988) compared the effect of using a wide variety of different scales on measures of national income inequality. They showed that the results for Israel were exceptionally sensitive to which scale was used, and attributed this to the comparatively large size of Israeli families. They warned that the choice of equivalence scales can powerfully affect not only cross-country rankings of poverty and inequality, but also comparisons within one country between population subgroups that differ in household size. Indeed, in the next section we

show that the OECD scale results in sectors with large families having a lower risk of poverty, but being more affected by redistribution, than is suggested by NII calculations based on the official Israeli scale.

Our primary independent variable, population sector, is straightforward except for the identification of Haredi households, for which only a rough criterion is available in the Income Survey. Households were classified as Haredi if at least one adult male reported that his highest educational attainment was attendance at a postsecondary "large" institution of religious studies (Yeshiva).[13]

Sectoral Differences in Poverty and Inequality

The opening paragraph of this chapter cited the official rates of poverty reduction for Arabs and Jews in 2012. We begin our examination of horizontal inequalities in redistribution by reporting parallel calculations carried out using our data set and the definitions and methods just described. In Figure 10.1 the darker bars show the percentage of households with market incomes below the poverty line, and the four sectors of interest are ordered from highest to lowest on this indicator. The gray bars refer to *disposable* income, which is market income after adding transfer payments and subtracting direct taxes. The order of the groups remains the same, meaning that inequality in redistribution by the state did not reshuffle the poverty hierarchy among the four sectors, which is characterized by both an overall Arab-Jewish gap and internal Jewish and Arab hierarchies. The baseline Jewish group (defined in Table 10.1) is more likely to

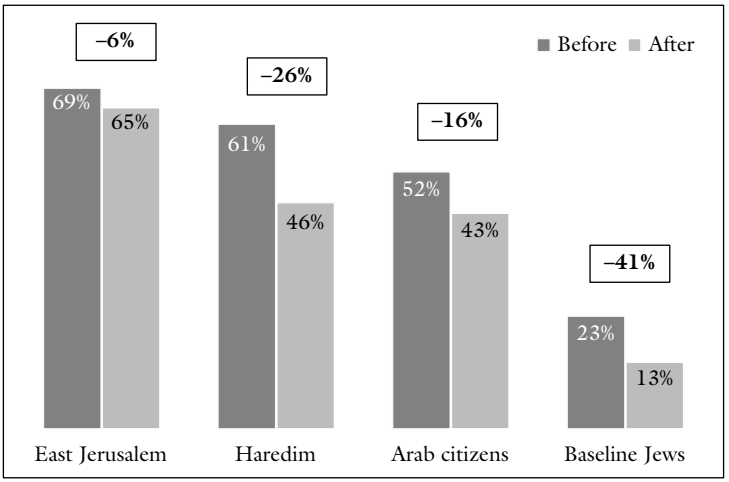

Figure 10.1 Poverty before and after transfers and direct taxes, by sector.

be lifted from poverty than Haredim, while Arab citizens benefit more from redistribution than residents of East Jerusalem. The most extreme difference in rates of poverty reduction is between the baseline Jewish category (41 percent) and East Jerusalem (a mere 6 percent). In the middle of the hierarchy, similar proportions of both Haredi and Arab households remain under the poverty line after state intervention. But since pretransfer poverty was higher among Haredim, the state must have intervened far more on their behalf in order to achieve this outcome.

Based on the figures just reviewed, there is a difference of 25 percentage points between the rates of poverty reduction for Arab citizens and the baseline Jewish population. Dramatic as it is, this gap is well below the 37 points that separate the official Jewish and Arab rates cited earlier. Part of this difference results from the broad definitions of the Arab and Jewish sectors adopted by the NII and the fact that we cited their figures for only one recent year, while our own data refer to a longer and slightly earlier period. However, by far the most important explanation for the contrast is the use of different equivalence scales. When we perform the same calculation that resulted in an Arab-Jewish redistribution gap of 25 points but substitute the official Israeli equivalence scale for the OECD scale, the result is a gap of 33 points.

Whichever equivalence scale is used there is a clear hierarchy in the impact of the redistributive system on the different sectors. All Arabs are seriously disadvantaged relative to Jews, and Arab citizens enjoy less poverty reduction than Haredi Jews but more than Arabs in East Jerusalem. However, evaluating the impact of redistribution by asking whether taxes and transfers lift households above the poverty line has many drawbacks. First, it ignores possible variations in the *depth* of poverty suffered by the four population sectors. Second, as a binary indicator it cannot measure the *degree* to which redistribution reduces poverty. Third, it is unable to shed any light on the impact of the state's redistributive system—be it equal or unequal—on households with market income *above* the poverty line. Finally, analyzing horizontal inequalities by measuring the combined impact of transfers *and taxes* is ill-advised since, as noted above, available data on taxes are incapable of revealing variations in the effective tax burden on different sectors. We deal with these issues by dropping taxes from the analysis and expanding the analysis of income from transfer payments to encompass households at all levels of market income. Instead of dividing households into those above and below the poverty line, we define the income hierarchy by starting with a homogenous category of "indigent" households (those with no other sources of income except government transfer payments) and dividing the remaining distribution into quintiles. The transfer income of different population sectors can then be compared within each level of nontransfer income.

To provide the context for this expanded analysis, Figure 10.2 documents inequalities between the four population sectors across the six categories of pretax and pretransfer income just described. The overall position of each sector can be visualized by the balance between darker segments (indicating lower

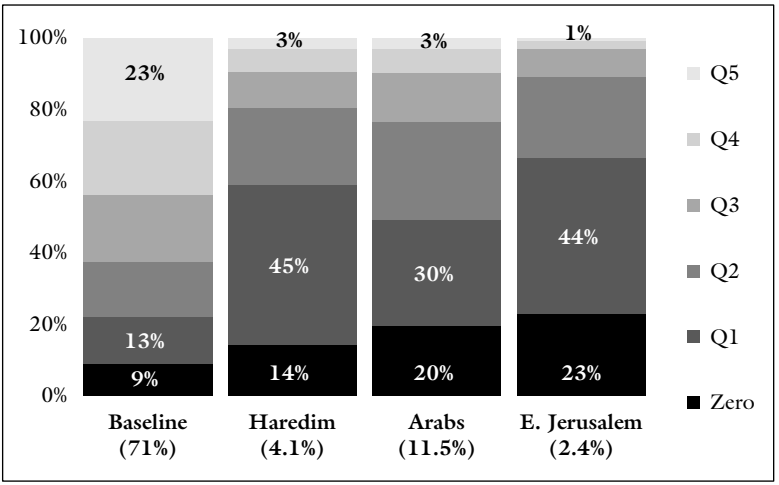

Figure 10.2 Distribution of nontransfer income by sector.

market income) and lighter ones (higher income). It is evident that there is a vast difference between all three minority sectors and the baseline Jewish population. Between one-half and two-thirds of the minorities are located in the two darkest segments, compared with little more than one-fifth of the baseline. The lightest segment—the top quintile—is almost exclusively populated by the baseline Jewish sector.

Note that the two darkest segments combined are almost equivalent to the population under the poverty line.[14] The distinction between the two—that is, between poor households that are indigent and those with at least some market income—is revealing. We have already seen that more Haredim than Arab citizens are poor. But it is now evident that a larger share of Arabs under the poverty line has no income at all. This indication that Arabs suffer from deeper poverty implies that even though more Haredim are poor, more redistributive effort would have to be directed to Arabs in order to achieve a similar rate of poverty reduction. The findings presented in subsequent sections show that if anything, Arabs are the target of less effort rather than more. But before reviewing the results, we turn first to a discussion of our analytical strategy.

Understanding Benefit Gaps

It is one thing to demonstrate the existence of gaps in the incidence of transfer payments between Israel's Arab citizens and other population groups, and quite another to pin down their causes. To simplify, horizontal inequalities in redistribution may reflect two types of inequality in the efforts made to assist different sectors. (1) *Unequal entitlements*: advantaged groups benefit from

special programs to which only they are entitled, or that are directed primarily to meeting their needs. (2) *Unequal treatment*: under a program for which everyone is formally eligible, sectors vary in their likelihood of receiving the benefit or in the amount they receive. A quantitative study of redistribution, like the present one, cannot by itself pin down the role of these two mechanisms. Other types of research would be needed in order to reconstruct the intentions of policymakers, explain why some citizens fail to apply for benefits to which they are entitled, and document the behavior of the street-level bureaucrats in charge of administering transfer payments.

Quantitative analysis can contribute by evaluating whether the expected transfer income of different sectors would be less unequal *if there were no differences between them in measurable attributes relevant to benefit entitlement*. In choosing to investigate sectoral variations in transfer income conditional on market income, we have already incorporated group differences in material deprivation. However, as has already been emphasized, assisting the poor is only one of the purposes of transfer payments systems. Even when benefits are directed toward the disadvantaged, income is not usually the only criterion governing benefit eligibility and generosity. The data at our disposal permit us to statistically control for sectoral differences in two types of compositional factors. A first set of controls are socioeconomic indicators that potentially capture aspects of *economic need* beyond a household's current income stream. They are indicative of earnings capacity (proxied by education and number of earners). We recognize, however, that these indicators may be capturing more than material needs. In particular, education implies cultural and other noneconomic resources (including language fluency, familiarity with welfare programs, laws and rights, practical understanding of the system, and facilitating social ties) that influence whether potential beneficiaries are aware of and able to actualize their social welfare entitlements.

Our second set of control variables is demographic. One key demographic feature of households—their size—has already been incorporated into our standardized measures of market and benefit income. Two more specific attributes—the presence of children or elderly—are especially relevant because they are the basis for Israel's most far-reaching benefit programs, child and old-age allowances. Table 10.2 indicates that the four comparison groups differ greatly in their eligibility for these two programs. First, compared with the baseline Jewish population, all three minorities have much larger proportions of families with children and much smaller proportions of households with at least one elderly member. Second, among the minority sectors, Haredim stand out for the prevalence of children and the absence of seniors.

The data thus attest to marked sectoral differences in *demographic eligibility*, meaning the degree to which demographic characteristics are aligned with entitlements. The effect of such differences on transfer income is compounded by the fact that benefit levels vary greatly between different schemes. For families of average size, child allowances are much smaller than old-age

Table 10.2 Selected demographic differences between population sectors (averages 2007–2011)

	Baseline Jews	*Haredim*	*Arabs*	*E. Jerusalem*
% households with 2 parents and children	33.9%	75.7%	64.5%	64.6%
Mean number of children	2.2	3.7	2.9	3.3
% households with 1 parent and children	4.5%	0.8%	3.6%	3.5%
Mean number of children	1.7	1.7	2.5	2.9
% households with 1 or more elderly	27.1%	8.5%	14.3%	15.1%

allowances—especially for indigent households, whose elderly are entitled to an income-tested supplement. Consequently, the joint workings of entitlement and benefit generosity can profoundly influence the benefit income of different sectors. Furthermore, beyond the role of benefits earmarked for particular family situations, the composition of households can also play a role if programs use household composition as a criterion for determining benefit generosity.

When measuring demographic eligibility, qualitative as well as purely numerical dimensions should be considered. Among them are distinctions between families headed by married couples and those headed by single parents; between dependent and grownup children; and between seniors living alone, in couples, or with other family members. Accordingly, along with measures of the number of dependent children and seniors in the household, our demographic controls include 14 dummy variables representing different household types.

Before leaving the topic of demography, we note that its role is not only technical, since sectoral advantages and disadvantages may be purposefully engineered by endogenizing demography into the benefit structure. The case of single mothers illustrates how demographic differences between sectors may motivate entitlements (Lewin and Stier 2002). A sizable component of the mass immigration that followed the collapse of the Soviet Union consisted of mothers who arrived in Israel with children but not their fathers, motivating the introduction of new or enlarged benefits for single mothers. Single mothers from all sectors may have benefited equally, but the main intended consequence of the benefits was to boost poverty reduction among new immigrants.

More typical of Israel are "loyalty benefits," which clearly imply unequal entitlement. As Peled (1992) has argued, throughout the history (and the prehistory) of Israel, the Republican notion that individuals who contribute to the "common good" are especially deserving of recognition and reward has been utilized to legitimate what are actually privileges for Jews received on ethno-national grounds. Many of Israel's loyalty benefits reflect the scope of its military commitments, which render many citizens needed by the state

regardless of whether they are needy (Gal and Bar 2000). Special benefits to war widows, reserve soldiers, those disabled during military service, and other recognized beneficiary groups can be understood as part of an exchange relationship between citizens and the military (Levy 2008). Given that the vast majority of Arab citizens are not conscripted by the Israeli army, they are automatically excluded from both the burdens and entitlements associated with military service.

A range of Republican deservingness criteria unrelated to military service underpin a variety of other loyalty benefits from which Arabs are also automatically excluded, including those offered to new immigrants, Holocaust survivors, and Haredi men engaged in full-time religious studies (Friedman and Shalev 2010). In one noteworthy instance, a supplementary child allowance established in the early 1970s and abolished two decades later, eligibility was made conditional on military service specifically in order to exclude Arabs (Rosenhek and Shalev 2000).

Are Arabs also disadvantaged in relation to benefits that have no apparent Republican component? The literature on "non-take-up" of benefit entitlements (e.g., Van Oorschot 1998) reveals that lack of awareness of social rights, or the willingness and capacity to actualize them, varies across programs, populations, and countries. Entitlement to the two universal programs based on life-course events that have already been mentioned is almost automatic for Israeli citizens. A study of child benefits and old-age allowances based on Income Surveys from roughly a decade ago found that in both cases take-up by eligible citizens is close to universal among Arabs and Jews alike. However, entitled households in East Jerusalem had somewhat lower chances of receiving both benefits (gaps of about 10 percentage points) (Gal, Shalev, and Ajzenstadt 2009).

In contrast, social assistance is an example of a program with more complex eligibility requirements that depend on investigation and interpretation by benefit administrators. Moreover, in Israel there are two parallel systems of what is termed Income Security. As mentioned earlier, one of these is designed for Haredi families with male household heads engaged in full-time religious studies, who are exempted from demonstrating their readiness to take on paid employment (Parliamentary Research and Information Center 2010). No such willingness to adjust eligibility criteria to group-specific circumstances is evident in relation to the Arab population, for which cultural prohibitions on women's activity in the public sphere and some specific features of land ownership both potentially hamper access to social assistance. Moreover, applications must be made in person, and many potential Arab applicants are hampered by their assignment to short-staffed, geographically inaccessible offices.[15] Similar barriers confront Palestinians in East Jerusalem, where readiness to apply for benefits is further constrained by fear that it could bring about investigations by the Ministry of the Interior into applicants' right to reside in the city (Amusin 2010).

Horizontal Gaps in Redistribution—A First Look

Before probing the effects of differences in economic need and demographic eligibility, we take a broad look at sectoral differences in transfer income. To begin with, what are the differences between population groups in Israel in the proportion of households receiving transfer payments? This comparison includes the new immigrant sector, which has access to unique benefits including a global cash allowance (the "absorption basket") and the right to unfunded "special" old-age allowances if they reach retirement age without a sufficient history of social insurance contributions (Gal 2008). Figure 10.3 reports the rate at which benefits are received, overall and excluding child and old-age allowances, which between them cover a very high proportion of households. The sectoral hierarchy observed earlier in rates of poverty and poverty reduction cannot be discerned at all in the overall figures. Setting aside the two "catch-all" programs, Haredim (followed by immigrants) have the highest proportions of recipients, whereas East Jerusalem residents have the lowest. Yet there is hardly any difference between baseline Jews and Arab citizens, in fact slightly more Arabs than Jews receive benefits.

It is only when the focus shifts from access to benefits to their value that the expected inequalities come into view (Figure 10.4). Looking at the average benefit income received by recipient households, the figure shows that (1) immigrants get more than veteran non-Haredi Jews (the baseline category); (2) all Jewish sectors receive more than Arabs; and (3) among Arabs, citizens get substantially more than residents of East Jerusalem.

In addition to the average incidence and size of cash benefits, it is also interesting to ask how sectors differ in terms of who benefits. Redistribution can

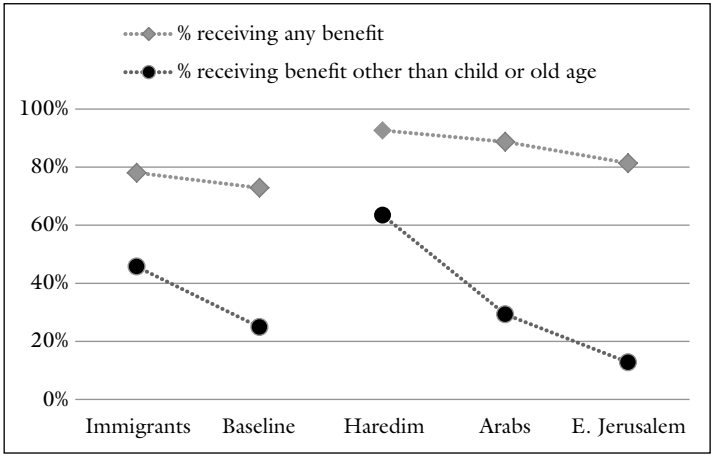

Figure 10.3 Rate of benefit receipt by sector.

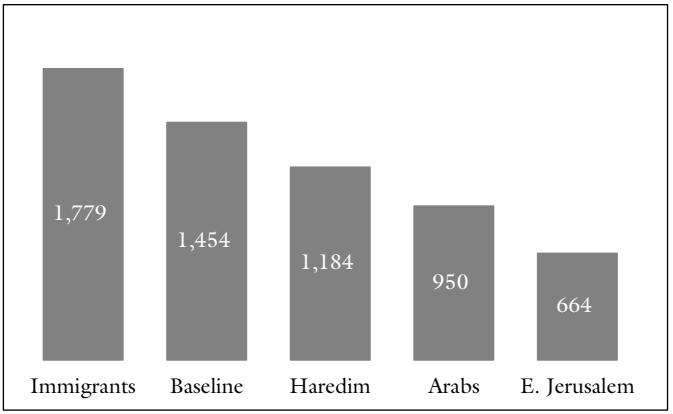

Figure 10.4 Benefit income per recipient household, by sector.

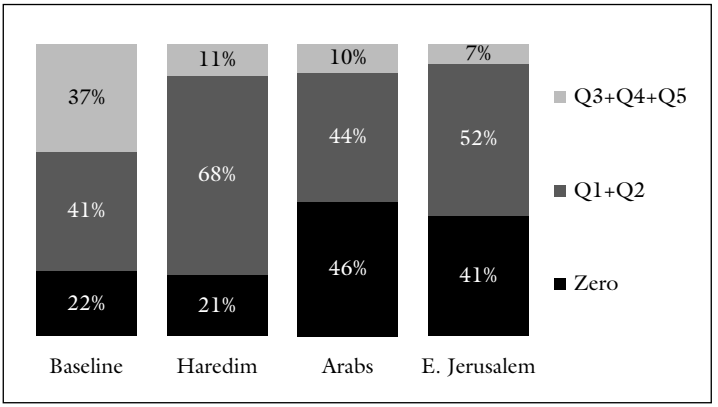

Figure 10.5 Distribution of aggregate benefit income by sector.

impact all levels of the vertical class hierarchy. Here we show how the aggregate benefit income of whole sectors is distributed across three segments: the indigent (zero income), low-income households (the lowest two quintiles), and the middle and higher classes (represented by the upper three quintiles).

Figure 10.5 reveals clear sectoral differences in who benefits from redistribution. (Since new immigrants are an explicitly privileged sector in Israel and lack the resemblances to Arab citizens of the two targeted comparison groups, they are not included here or in the remainder of our analysis.) For all three of the minority groups on the right, transfers function predominantly as a mechanism of poverty relief. In contrast, well over a third (37 percent) of all transfer

income received by the baseline sector reaches relatively affluent families. In addition, the share of aggregate benefits received by the indigent is roughly twice as high in the two Arab sectors than for all three of the Jewish ones.

These differences are largely, but by no means fully, explained by the dramatic sectoral inequalities in market income documented earlier (Figure 10.2). Consider the two poles of the income hierarchy. At the bottom there is a 25-point difference between Arabs and Haredim in the percentage of all benefit income that reaches the indigent, even though the Arab proportion of indigent households is only 6 points higher. Toward the top of the hierarchy, the large share of aggregate benefit income reaching the higher quartiles of baseline Jews undoubtedly derives in part from their almost exclusive access to military-related loyalty benefits.

Not only are Arabs subject to partially unequal entitlements, but the detailed results yet to come suggest that they may also experience unequal treatment. At nearly all levels of the income hierarchy we find that the benefit income of Haredi households is higher than Arab citizens, who in turn receive more than East Jerusalem residents. In proportional terms the size of these inequalities diminishes as market income rises—but they do not entirely disappear. Importantly, we will show that both absolute and relative gaps are usually smaller once compositional differences are statistically controlled. Yet with a few interesting exceptions, the same horizontal hierarchy is nearly always present.

Unequal Transfers to the Indigent

Our first detailed analysis focuses on the poorest of all households—those with no income other than transfer payments. Several features of the presentation of our results in Figure 10.6 should be noted. Instead of showing the shekel value of the mean benefit income of each sector, it is calculated relative to the national median level of disposable income. This makes it easy to locate each sector relative to the poverty line (50 percent of the disposable income of the median household). In addition, to demonstrate the importance of standardizing benefit income by the number of equivalent persons in the household, the figure displays results both before and after standardization.

Perhaps the most striking result is that in no sector does the average indigent household receive sufficient funds to elevate it above the poverty line.[16] But our main concern here is with horizontal gaps between the indigent of different sectors. Comparing the average unstandardized amounts (gray diamonds), the benefit income of households in different sectors is surprisingly similar, except for the deep divide between residents of East Jerusalem and all others. However, once standardization takes into account the larger families prevalent among the minority sectors, a different picture emerges (black circles). Due primarily to the difference in their average household size, Haredim and the baseline become sharply differentiated. In the baseline sector the

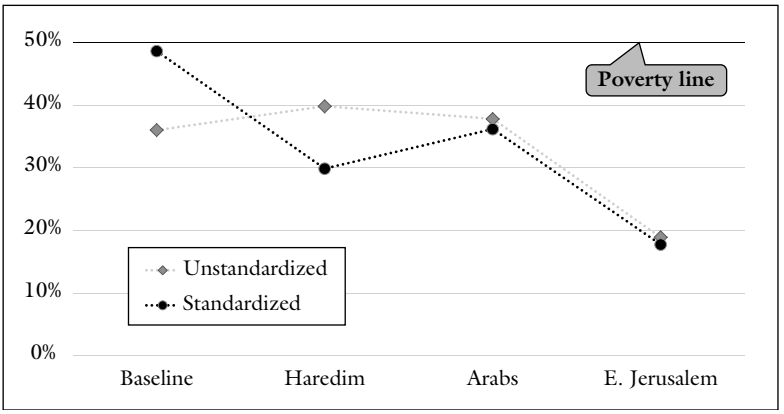

Figure 10.6 Mean benefit income of households with no other income, by sector and standardization by household size (as a percentage of median disposable income).

average value of benefit income rises sharply after standardization, almost reaching the poverty line. In contrast, the result for Haredim is much lower than before, so much so that their average household now receives significantly less than Arab citizens. The gap between the two Arab populations remains unchanged: Palestinians in East Jerusalem receive only half as much benefit income as Arab citizens.

What could explain the surprising difference between these results for Haredim and the sectoral hierarchy indicated by previous findings? The gap between the two Jewish groups is undoubtedly connected to their starkly different demographic profile. While Haredi households are predominantly (almost four-fifths) families with dependent children, the critical mass of the baseline (nearly two-thirds) consists of households with seniors. As mentioned earlier, except for extremely large families, the value of child allowances is inferior to old-age allowances. Moreover, indigent households in the two sectors may be covered by any one of three different social assistance programs. The program earmarked for Haredim is less lucrative than either the old-age supplement (key for the baseline) or Income Security (which plays a significant role among Arab citizens).

In an attempt to set aside demographic and other compositional differences between sectors that do not necessarily reflect unequal effort or unequal treatment by the welfare state, we carry out a multivariate regression of variations in benefit income that controls for the indicators of demographic eligibility and economic need that were specified earlier (see the section Understanding Benefit Gaps). Figure 10.7 presents two sets of estimates. The first set ("before controls") is almost identical to the results for average standardized benefit income presented in the previous figure, except that amounts are expressed in constant

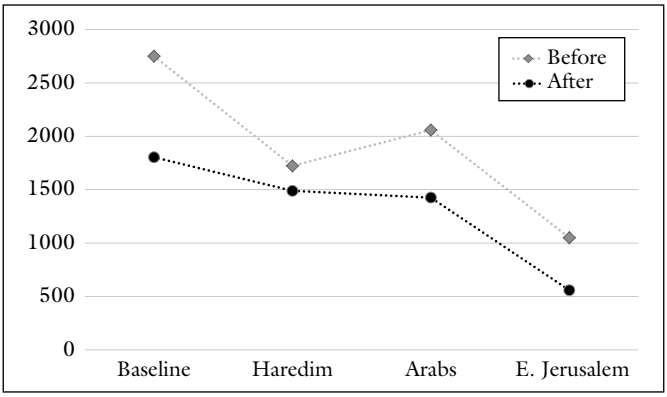

Figure 10.7 Estimated benefit income of indigent households, before and after statistical controls.

shekels rather than as a percentage of median disposable income.[17] The "after controls" estimates are based on simulations derived from the regression results, in which the value of control variables is fixed at their means.[18] This provides an indication of the expected benefit level for households at a given level of market income (zero in this case) within each sector if their other characteristics were the same as the average Israeli household.

Not surprisingly, the simulation shows that indigent households in all sectors would receive less benefit income if their demographic profile, education, and number of earners were more typical. However, the size of the adjustment varies greatly across sectors. It is particularly profound for baseline Jews but makes very little difference to the Haredi sector. The consequent shift in the position of the Haredi sector reinstates the typical sectoral hierarchy. This is important since it challenges the contention that lower rates of poverty reduction among disadvantaged groups are due to the depth of their poverty. In fact all three minority sectors receive lower income compared to the baseline, and this gap is not explained by either degree of need or differences in demographic composition. Nevertheless, in the simulated results, the baseline retains a much smaller (albeit still significant) advantage. Both Haredim and Arabs receive about 80 percent as much simulated benefit income as baseline Jews. In contrast, the gap between the indigent of East Jerusalem and Arab citizens is hardly diminished. In fact it is nearly three times the gap between Haredim and the baseline. Therefore, the poorest citizens appear to be treated very similarly once their compositional differences are taken into account.

A puzzling feature of the simulation results is that despite the atypical demographic and economic profile of indigent Haredim, applying compositional controls has very little impact on their estimated benefit income. Demography

is the critical factor. Fully 79 percent of Haredi households with no market income are families with dependent children, and their mean number of children is also relatively high (4.1 compared with 3.2 for all indigent families). In contrast, whereas just over half of all indigent households include seniors, the parallel Haredi figure is only one-tenth. We have already noted the negative implications for the value of the Haredi benefit package, which are confirmed by the results of our multivariate analysis. Consequently, in a world without sectoral differences in demography, the benefit income of indigent Haredim ought to rise. However, as stated, the relatively large household size of Haredim pushes the simulation results in the opposite direction. If Haredi families were of average size their benefits would be substantially larger (less deflated) than they are in the real world.

From the perspective of our interest in Arab-Jewish gaps, two findings stand out from this analysis of indigent households. The sector of the indigent that is most unequally treated by Israel's benefit system is the noncitizen Palestinians in Jerusalem. In contrast, with or without controlling for compositional differences, there is no evidence that Arab citizens receive inferior treatment to Haredim, their closest Jewish counterpart in terms of multiple disadvantages. As we proceed to extend the same counterfactual simulation to households with successively higher levels of market income, it will become evident that the lack of a Haredi advantage over Arabs is almost unique to the indigent. It is to this analysis that we now turn.

Unequal Transfers to Households with Market Income

Figure 10.8 reports simulated benefit income for quintiles 1, 2, and 3, which are derived from the same regression model as the previous simulation for households with no market income. Quintiles 4 and 5 are not included in the analysis because, as we saw earlier (Figures 10.2 and 10.5), there are few minority households in these quintiles, and their benefit income is limited.

A first finding is that, in line with previous indications, benefit income per household declines as market income rises. Percentage calculations not reported here show that the declines are larger for actual than for simulated benefit income. This implies that while the benefit system is progressive (smaller transfers are made to more affluent households), sectoral compositional differences account for part of this progressivity.[19]

Turning to sectoral gaps, all three parts of Figure 10.8 reproduce the same horizontal hierarchy already observed for the indigent. Regardless of which quintile of market income is in focus, and whether we look at actual or simulated benefits, the two Jewish sectors precede the two Arab sectors, and the baseline group leads while East Jerusalem lags behind.[20] Yet there are also differences.

At nearly all levels of income (including the indigent but not the third quintile), the simulated income of the baseline takes a hit because of its

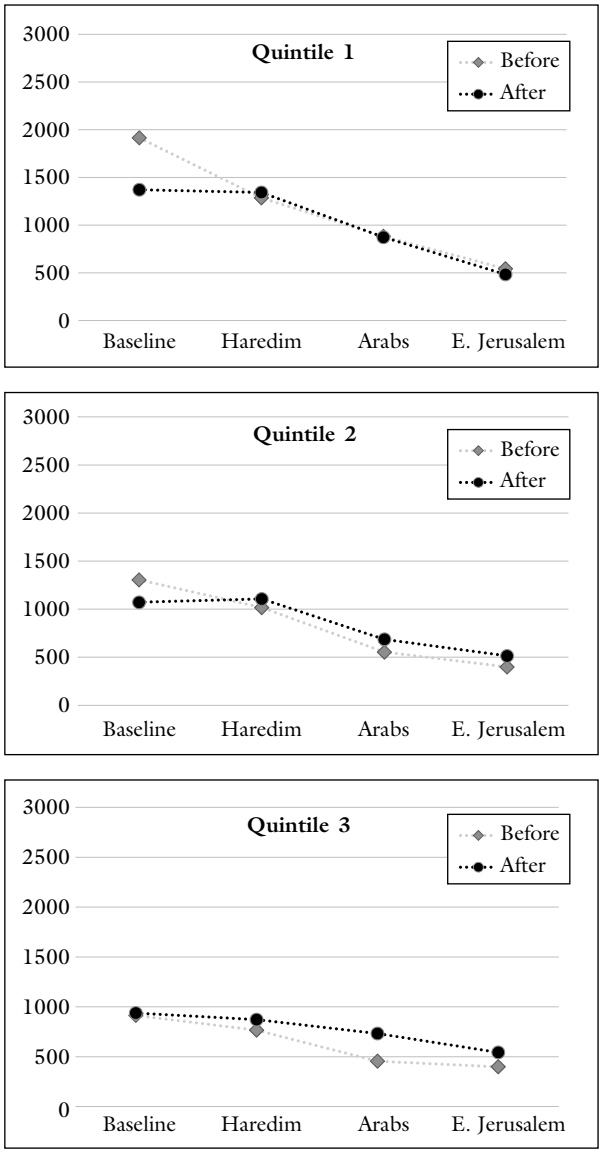

Figure 10.8 Estimated transfer payments of households with market income, before and after statistical controls.

overrepresentation of seniors and their associated entitlements. Mainly as a result of this, applying statistical controls has the effect of causing the benefit income of the baseline and Haredi Jewish groups to become more similar. But when looking at households with their own sources of income we see that

gaps between Jews and Arabs are much more resilient than inequality among Jews. While the simulation for the indigent revealed a sharp contrast between the benefit income of East Jerusalem residents and both of the other minorities, the results for households with market income show that Arab citizens are also disadvantaged (although less so). Since this is true before as well as after controlling for compositional differences, these gaps are clearly not due to compositional differences.

This does not mean that it would make no difference to the benefit income of the two Arab sectors if their attributes were similar to the average Israeli household. The controls influence both Arab groups, although their effect changes as income rises. Instead of cutting into the benefit income of all three minorities, by the second and third quintiles the effect of simulation is to increase it. However, this has no effect on the sectoral hierarchy. To repeat, in all three quintiles of positive income the simulation causes baseline Jews to converge downward with Haredim, while preserving the disadvantaged position of Arab versus Jewish citizens and the further disadvantage of Palestinians without citizenship.

The impact of vertical class differences on the position of Arabs versus Jews is ambiguous. (These remarks concern Arab citizens, since few East Jerusalem families are positioned above the second quintile.) On the one hand, the composition of Arab families compared with non-Haredi Jews—especially their higher number of dependent children and fewer seniors—partly explains the inferior transfer income of the both Arab sectors. As we move up the income hierarchy from the first quintile to the third, the gap between Arab citizens and Haredim narrows after controls are applied (a trend that continues in the fourth and fifth quintiles). An important reason for this is the changing composition of baseline families in the middle and higher classes, which is less skewed in favor of seniors than at lower levels of market income. On the other hand, the impact of loyalty benefits on the superior benefit income of baseline Jews over Arabs is most likely to be felt at medium and high levels of market income. The declining (albeit persistent) Arab-Jewish benefit gap at the second and higher quintiles of nonzero income lends indirect support to this hypothesis. However, it cannot be adequately tested without program-level data on the incidence of benefits at household level. Accordingly, this is the focus of the final empirical section of the chapter.

Sectoral and Class Differences in Benefit Packages

The preceding analysis has frequently alluded to differences between sectors in their eligibility for specific benefit programs and the difference it can make to their benefit income. The average contribution of different benefit schemes to total transfer income can be thought of as constituting a "benefit package." Earlier sections of the chapter have touched upon the many reasons why some sectors receive little or no benefit income from specific schemes,

including exclusion (unequal eligibility), lack of required demographic or socioeconomic attributes, and intended or unintended discrimination (unequal treatment). Bearing these factors in mind, sectoral variations in benefit packages are only to be expected. But these variations provide important clues for interpreting quantitative gaps in benefit income.

Unfortunately, limited disaggregated information on benefit income is available in Israel's Income Surveys. No loyalty benefits program, irrespective of its size, is among the specific programs singled out. Instead, loyalty benefits (along with some other schemes) are dispersed between two residual categories. One of these, miscellaneous NII benefits, includes a major loyalty benefit (income replacement for reserve soldiers). The other, benefits paid by government institutions other than the NII, includes both the special Income Security program for families of yeshiva students, and Ministry of Defense benefits for disabled veterans and bereaved families. The analysis that follows differentiates between these two omnibus categories and the four largest "mainstream" programs for which disaggregated data are available.

Rather than performing a separate analysis for all five income classes, since we are interested in probing the benefit packages of the three minority sectors (relative to the baseline), our primary interest is in low-income households (the indigent and the lowest two quintiles). Figure 10.9 describes the income packages for each sector, alongside a measure of the gaps between them in benefit income. Panel A documents the profound advantage of the baseline Jewish sector over both Haredim and Arab citizens. By revealing the components of each sector's benefit package, Panel B helps us understand why this is so. (Note that to avoid overcrowding, only components of the package that contribute at least 15 percent of transfer income are labeled.)

The Haredi sector's package is dominated (70 percent) by two categories: child allowances and benefits provided by public bodies other than the NII (which in this context mainly signifies the special Income Security program for Haredim). The relatively modest sums provided by both of these programs compare unfavorably with old-age allowances, which account for almost half of the benefits that reach low-income Jews in the baseline sector.[21]

The figure also reveals that while low-income Haredim and Arab citizens receive relatively similar amounts from the transfer system (15 percent less for Arabs), their benefit packages are substantially different. Driven by demographics, benefits for children and especially for seniors have differing weight. But even more striking is the almost complete absence of non-NII benefits and the much larger role of Income Security and disability benefits among Arabs. This contrast indicates that benefits earmarked for low-income Haredim perform a similar function to the mainstream NII programs that serve Arab citizens. However, the benefits available to Haredim are apparently more lucrative.

Comparison of the benefit packages of the two Arab sectors reveals that they are similar in some respects while differing in others. The main difference is the much larger role played by child allowances in East Jerusalem (where

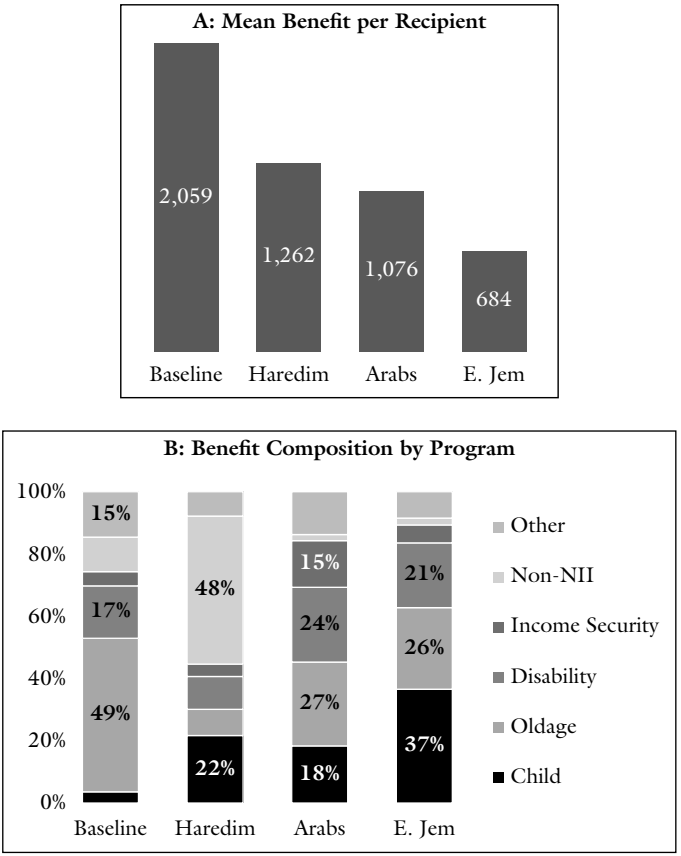

Figure 10.9 Benefit characteristics by sector, low-income recipients.

families are larger), and the more substantial contribution of Income Security and miscellaneous NII benefits to the benefit package of Arab citizens (even though their economic conditions are superior to those of households in East Jerusalem). Programs for children, seniors, and the disabled together contribute nearly 85 percent of the benefit income of low-income Palestinians in Jerusalem, compared with less than 70 percent among Arab citizens. This indicates that part of the disadvantage of the former sector derives from difficulties in realizing entitlements to all but the core NII programs.

Because so much of the benefit income of baseline Jews (37 percent) is received by relatively advantaged households (the upper three quintiles of market income), we briefly review parallel findings for high-income households (Figure 10.10). Because they are ineligible for income-tested programs, including the supplement to the old-age allowance, the average benefit yields

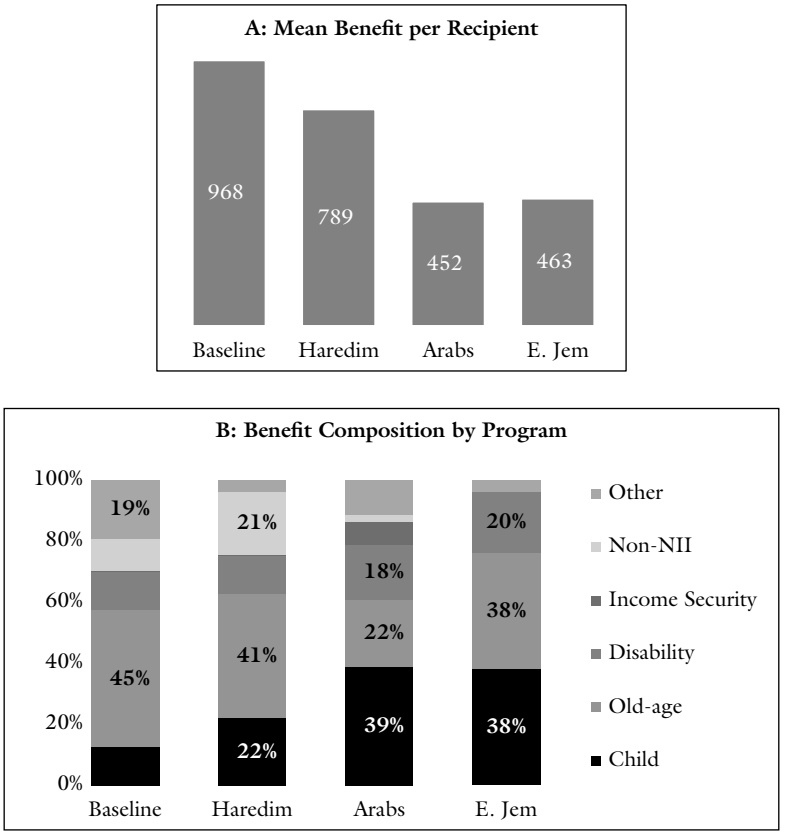

Figure 10.10 Benefit characteristics by sector, high-income recipients.

for high-income recipients in all sectors (especially the baseline) is considerably lower than for low-income beneficiaries. Panel A also confirms an earlier finding, namely that whereas among low-income recipients benefit levels are polarized between baseline Jews and the three minorities, among advantaged beneficiaries the primary contrast is between Jews and Arabs.

Panel B of the figure helps explain this. Child allowances are the most prominent source of benefit income among affluent Arabs, while they receive virtually no income from non-NII sources (and in East Jerusalem almost no unspecified NII benefits). Among baseline Jews the latter two types of benefit together account for 30 percent of the total, much of which presumably derives from benefits conditional on military service—which are known to be exceptionally generous (Gal and Bar 2000). In contrast, the relatively high benefit income of the Haredi sector derives more from the quantity of benefits received than from their value (Figures 10.3 and 10.4).

Conclusions

This chapter set out to clarify both the extent and the sources of the glaring gap between the effectiveness of redistribution in relieving poverty among Israel's Arab and Jewish citizens. The design of our study goes beyond the limited body of prior research by (1) assessing redistribution to all income classes, not only the poor; (2) analyzing the position of Arab citizens in relation to other horizontal sectors, including the Palestinian residents of Jerusalem; and (3) setting aside the incidence of direct taxes, which cannot be accurately known, and focusing solely on inequality in income from transfer payments.

Our study provides the first detailed and up-to-date analysis of sectoral differences in income from transfer payments. It probes what we term "horizontal inequalities" across three main cleavages: between Jews and Arabs, and citizens and noncitizens, and contrasting the socially, politically, and economically dominant Jewish majority compared with minorities of all origins (Haredi Jews as well as Arabs). The few previous studies of horizontal inequality in welfare provision in Israel investigated rates of poverty reduction, revealing a clear hierarchy with Arabs located at the bottom and new immigrants at the top. However, this approach fails to account for the depth of poverty and imposes a limited binary view of the impact of redistribution. Like previous researchers, we rely on data from a large official survey (the Income Survey) that requests respondents to report all of their income sources, including transfer payments. Our analyses estimate the degree of sectoral inequality in benefit income, conditional on the class location of households in the hierarchy of nonbenefit income. Linking the vertical and horizontal hierarchies makes it possible to analyze sectoral variations in both the degree to which poverty is reduced by redistribution, and its impact at higher levels of market income.

We began our inquiry by documenting the distribution of benefit income across sectors, revealing a hierarchy in which "baseline" Jews (neither Haredim nor immigrants) receive the highest average benefit income followed by Haredim, Arab citizens, and finally noncitizen Palestinians resident in East Jerusalem. Differentiating between levels of market income showed that for minorities the system mainly contributes to households in poverty, while for the baseline group the middle and higher classes also benefit. This provided a first hint of the advantage enjoyed by baseline Jews due to their privileged access to "loyalty benefits," testifying to unequal entitlements. Yet when analyzing sectoral differentials in the benefit income of indigent households (those with no market income), we found that despite the existence of loyalty benefits earmarked for Haredi families at high risk of poverty, they received less transfer income than Arab citizens.

This seeming deviation from the typical redistributional hierarchy underlines the importance of sectoral differences in socioeconomic capacities (beyond market income per se) and household demographic composition. Using statistical controls to neutralize these differences significantly altered

the results, mainly because the sectors vary greatly in the relative weight of children and seniors, with accompanying differences in the value of universal benefit entitlements. Within indigent households the hierarchy was reinstated, with Haredim receiving more "net" support than Arabs. However, the simulation also had the effect of reducing gaps between the three largest sectors. After applying statistical controls the baseline Jewish sector still held the lead, but Haredim and Arabs citizens were not far behind, and there was only a small gap between them. The net benefit income of Palestinians in East Jerusalem is far lower, exposing the cleavage dividing noncitizens from citizens.

In households with nonzero market income a different cleavage was found, separating the two Jewish sectors from their Arab counterparts. A possible explanation lies once again in the statistical leveling of sectoral differences in the age structure of households. However, the resilient Arab-Jewish gap remaining in the higher quintiles attested in addition to the role played by loyalty benefits, from which Arabs are all but excluded. This in turn raises a wider issue, namely that sectors have access to different benefit packages, some of which are more valuable than others. Some elements of the packages are tailored to fit specific sectors. In other cases sectoral demographic characteristics either inadvertently or intentionally expose them to more lucrative benefit plans.

Our findings indicate that the baseline sector has the most lucrative package, due to a combination of access to loyalty benefits linked to military service and favorable demographics (high prevalence of old-age benefits). The vast majority of low-income Haredim lack both of these advantages; but their socioeconomic deprivation and large families are compensated for by access to sectorally-specific benefits. Low-income Arab citizens lag behind because they have the "wrong" demographics and no designated benefit plans. Yet they are able to take advantage of the mainstream NII plans, especially universal programs serving the old and the young, and targeted social assistance. This is the source of their superior benefit income compared with noncitizen Palestinians, whose benefit package is both less diverse and less valuable than that of Arab citizens. While the residents of East Jerusalem are in principle entitled to need-based plans, most of their benefit income derives from old-age and child allowances. In the higher income quintiles, in which need-based plans are less applicable, plans for which only the two Jewish sectors are eligible differentiate them from their Arab counterparts, thereby asserting the Jewish-Arab cleavage.

Returning to our original question, this study makes clear that while Israel's Arab citizens generally benefit less than Jews from the operation of the transfer payment system of the welfare state, previous assessments focusing on poverty reduction and failing to internally differentiate the binaries of Arab and Jew have exaggerated the extent of this inequality. Comparison with Haredim, a sector also at high risk of poverty but with far superior political capacities,

is especially enlightening. The benefit income of indigent Arab households is higher than that of Haredim, although it becomes slightly lower when demographic and socioeconomic differences between the two sectors are statistically controlled. However, this is not the case for households with positive market income. In all quintiles with significant Haredi and Arab representation, the latter receive less benefit income than the former, and when controls are imposed the two Jewish sectors converge at a superior level. At the same time, despite the role of privileges conferred solely or mainly on Jews, Arab citizens enjoy notably more benefit income than their counterparts in East Jerusalem, underlying the significance of the liberal dimension of Israeli citizenship (Shafir and Peled 2002).

More generally, despite the advances made here in analyzing horizontal inequalities in transfer payments—an almost nonexistent research area (but see Cohen, Steuerle, and Carasso 2001)—it is easier to establish sectoral hierarchies of redistributional inequality than to explain them. A household's income from transfer payments depends on its eligibility for benefits, whether they are taken up (applied for and granted), and their generosity (unless benefits are paid at a uniform rate). Two factors potentially explain sectoral differences in eligibility and generosity. One is unequal entitlements, exemplified in the Israeli context by loyalty benefits. The other is the demographic and socioeconomic composition of sectors in relation to both eligibility requirements and the criteria that determine benefit levels. However, a mismatch between sectoral composition and the rules governing access to benefits and their generosity may be intentional rather than circumstantial. Furthermore, barriers to take-up vary substantially across programs, depending on their eligibility criteria and how they are administered. Targeted and discretionary schemes increase the scope for discrimination against minorities, but also increase the salience of educational and cultural gaps and limited geographical accessibility among potential beneficiaries. As a result, "unequal treatment" may be unintentional. Yet it could still be interpreted theoretically as discriminatory when compared to a counterfactual welfare state that proactively encourages take-up among minorities.

Notes

1. Table 11 (Chapter 2) of the NII's Annual Survey 2013 (in Hebrew). The Arab-Jewish gap was exceptionally high in 2012. The mean reduction rate in the preceding three years was 12 percent for Arabs and 41 percent for Jews.
2. Our calculation, based on the odds ratio derived from Table 4 of Lewin and Stier (2002) in which new immigrants and Haredim are treated separately and all other Jews are the reference category.
3. Table 12 (Chapter 2) of the NII's Annual Survey 2013 (in Hebrew).
4. "Jewish" refers to the baseline category defined in Table 10.1.

5. Table 12 (Chapter 2) of the NII's Annual Survey 2013 (in Hebrew).
6. Most of these privileges are extended to Haredi men engaged in full-time religious studies and their families, including a special Income Security program that does not require a work test. For additional details see Swirski, Konor, and Yecheskel (1998); Ilan (2000); Gal (2010).
7. East Jerusalem: http://jiis-jerusalem-eng.blogspot.co.il/2014/08/palestinian-residents-of-jerusalem.html. For a rare study of the position of East Jerusalem residents in the Israeli income hierarchy, see García-Fernández et al. (2013).
8. Except for Haredim, data are for December 2012 and were downloaded from http://www.cbs.gov.il/reader/cw_usr_view_SHTML?ID=802. Haredi population estimates for 2009 are from Friedman et al. (2011:Table 34).
9. For more information on the sampling method and population coverage of the survey see CBS publication no. 1524 (http://www.cbs.gov.il/webpub/pub/text_page_eng.html?publ=11&CYear=2011&CMonth=1).
10. Hence, in contrast to the practice of the NII, our concept of market income includes pensions received from abroad and private transfers from households in Israel or individuals abroad.
11. http://www.lisdatacenter.org/workshop/spss-part-I.pdf
12. http://www.oecd.org/eco/growth/OECD-Note-EquivalenceScales.pdf
13. Definitions of some other independent variables are given in subsequent sections. All other technical information concerning our research will be provided on request.
14. A small fraction (6 percent) of poor households is located in the second quintile of nonzero income.
15. Sources for these barriers to take-up among Arab citizens are interviews that Shalev conducted with Dr. Ibrahim Mahajne (an experienced Arab social administrator) as well as discussions with senior staff of the Research and Planning Division of the NII in November and December 2009. NII personnel claimed that accessibility problems are limited and have been more than compensated for by the widespread use of intermediaries by Arab applicants.
16. Were our analysis to include obligatory deductions from income (health and social insurance, since income tax does not apply to the indigent), the average impact of redistribution would be even smaller. However, the difference would only be slight (the taxes paid by the median indigent household are equivalent to only 4 percent of its transfer income).
17. Fixed effects of survey year are also included in the model (and in all subsequent models) in order to account for possible fluctuations in the real value of nontransfer income.
18. The relevant explanatory variables are education (3 levels), number of earners (divided by the square root of the number of persons in the household), type of household (demographic composition), and number of seniors. Note that in order to carry out parallel simulations for other levels of market income the model was applied to the entire sample, controlling for sector conditional on income level.
19. These patterns are clearest for the baseline.

20. The sole exception is that in the second quartile, simulated income is higher for Haredim than the baseline. Note that conditioning our analysis of benefit income on broad categories of market income has the effect of understating the distinctive position of the two polar sectors. Results not shown indicate that in all quintiles above the first, both the baseline advantage and the East Jerusalem disadvantage would increase if we took account of the fact that they are clustered in high and low positions (respectively) within each quintile.
21. On the size of benefits under the Income Security program for Haredim, see Parliamentary Research and Information Center 2010. Note that the benefit gap between the baseline and Haredi sectors also results from the small size of baseline households, particularly those with seniors. Standardization of benefit income engenders more deflation of Haredi benefit income.

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