Should an Excess Profit Tax be Imposed on Israeli Banks? A Global Perspective

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In June 2023, a bill proposing to impose an excess profit tax on banks was introduced in the Knesset, Israel's parliament. According to the bill, the tax will be imposed on banks due to the growing gap between interest rates charged by banks on loans they grant and interest rates paid by them on clients' deposits.

This research examines the proposed legislation and recommends avoiding imposing the tax at this stage. The recommendation is based on critiques raised by regulators and academics as well as on lack of substantial evidence: as of now, such taxes have been levied in a handful of countries and have been in effect for a short period of time. Furthermore, the evidence accumulated thus far is not unequivocal, making it too early to draw conclusions regarding both its implications and its success. In light of the banks' critical role in the economy, it is inappropriate to take the risk and impose the tax before its full consequences in other countries can be assessed. This conclusion does not preclude an examination of the matter in question using other tools.

"We Were Wrong!" – On Errors in Financial Statements

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The Israel Securities Authority (ISA) recently clarified how to assess whether an error in financial statements is material (Decision 99-4 and Legal Position 105-24). This study examines the causes and consequences of errors in public company financial statements. According to the ISA, an error is material if it could change users' behavior and decision-making. Specifically, an error is material if it amounts to 5% or more of equity, net earnings, or comprehensive earnings. We find that material errors are widespread in small public companies that do not meet high internal control standards per ISOX rules. The likelihood of discovering a material error is higher in companies adopting small company exemptions. The consequences of a material error include increased audit hours and fees and a higher chance of changing the audit firm. This raises questions about the efficacy of internal audits in small companies.