Betterment Levy – A Conceptual Rather than Outcome-Based Tax: "Came to Bless but Went Out Cursing"

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ABSTRACT

This paper examines Israel's betterment tax, arguing that in its current form as a conceptual tax rather than an outcome-based one, fails to achieve its stated objectives. The tax is justified by two main rationales: capturing part of the land value increase created by public planning decisions, and financing municipal development costs. Using comprehensive data on all Israeli local authorities for the years 2021–2023, the paper shows that in practice the levy provides a substantial and reliable funding source only for a small number of strong municipalities. Weaker and peripheral authorities collect minimal revenues relative to their development needs, deepening fiscal inequality and dependence on central government transfers.

The paper further demonstrates that the notional nature of the tax generates high valuation uncertainty, extensive legal processes, and significant administrative and economic costs. Empirical evidence from appeals and valuation disputes shows large and systematic reductions in initial assessed valuation, particularly benefiting well-resourced developers, thereby undermining the tax's progressive intent. Additional distortions include adverse incentives for spatial planning, impediments to comprehensive master planning, and upward pressure on housing prices.

Considering these findings, the paper proposes replacing the betterment levy with a transparent, outcome-based development charge tied to actual infrastructure costs per square meter, differentiated by land use and location. Such a reform would improve certainty, efficiency, equity between municipalities, and alignment between fiscal incentives and planning policy.

Keywords: Windfall tax, Betterment tax, Development Fee, Unintended Consequences.

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