



Iron Dome Economics with "Gaps"



The Ministry of Finance determined a criteria for the payment of compensation for indirect damage suffered by the inhabitants of the south, up to 40 kilometers from the border with Gaza. The understanding contemplated, *prima facie*, allows for the provision of compensation also for additional expenses paid by businesses in order to preserve their activities during hostilities.

However the "Authorities", instead of declaring "areas" of hostility as the law requires, declared "special areas", offering various methods of compensation which do not "cover" the full extent of the financial loss incurred even during armed hostilities. Apparently the "Israeli bluff"-is alive and kicking, also during periods of hostilities.

Together with the existential anxiety, including those deriving from armed missiles and concern for children and friends actively participating in the fighting during the hostilities, the inhabitants of the South and the Center suffer economic hardship during the period of hostilities.

An example is an enterprise which suffers damage as a result of an enemy attack, including those deriving consequentially such as to stock, which is fire damaged or delayed at ports or warehouses, either as a result of having to cease activities or as consequence of drivers of trucks having to drive a tank or armored car carriers; production lines which have come to a halt because of a shortage of employees, including those deriving from the need to take care of their children as

a result of the closure of schools, including nursery schools, sea side restaurants in which hundreds of thousands of Israel Shekels have been invested prior to their opening in the summer, shops which have a limited number of purchasers, halls and other places used for recreation and places of entertainment which all experience countless cancellations. The list of those suffering economic hardship both immediately and thereafter, is endless.

The "model" under which the government "acts", is to declare that certain settlements situated at the borders of the conflict area as "areas of hostility" with the addition of further areas by Government Promulgation, as the continuing "war-like" activities may demand, from time to time. In a promulgation issued on 23 July 2014, the Minister of Finance, Yair Lapid, the Chairman of the "Workers Union" and the Chairman of Chamber of Commerce, agreed the principles for providing for "indirect" losses for the inhabitants located in the South. For the area extending 40 kilometers from the border with Gaza, as will become apparent hereafter, the

understanding in the process of formulation provides certain relief to those affected in that, contrary to the procedures for compensation in the past provision is made to compensate for additional business expenses in order to preserve the scope of business activity during the military operation known as "Tzuk Eitan". The above provisions were contained in Regulations known as the "Property Tax and Compensation Fund" (Payment of Compensation) (War Damage and Consequential Damage) Regulations 2014, which were brought for confirmation before the Finance Committee of the "Knesset" (the Israel Legislature) on 3 August 2014.

permanent and temporary border settlement

Before considering the scope of the above "war" compensation, it is necessary to introduce some "order" to the situation. At the beginning of 1961 the "Property and Compensation Fund Law" was promulgated. The Law, on the one hand provided for a "compensation fund" financed by "Property Tax" (being 10% of the annual amount collected) and "Land Betterment Tax" (being 15% of the annual amount collected).

The Law provided that the beneficiaries of the Fund were to be compensated for "war damage", "consequential damage" and "drought" damage (which is not relevant for our purposes). After a number of years, Property Tax was abolished and it is not known what the amounts of the funds were and how much was collected or distributed, however the mechanisms for compensation, in principle remained, subject to various "inroads" or deductions of the Finance Ministry.

War damage is direct damage caused, namely the costs of repairing physical damage caused to a structure or a motor vehicle, irrespective of whether the damage occurred in a "hostile area" or in any other area in Israel, the right to compensation exists.

However consequential damage is a loss or the prevention of profit as a result of damage to property in a declared "special area" or the lack of an ability to utilize an asset in such an area as a result of war like activities in a "special area" being an area so declared by the Ministers of Finance under the authority of the

Finance Committee of the Knesset. A "special area" may be declared for an indeterminate period or if, for a defined limited period, the Minister of Finances Declaration in itself, is sufficient.



As the Declaration of a "special area" has wide reaching economic budgeting consequences, the model adopted by the Israeli Government is to declare certain special areas as being "permanent", being those areas adjacent or near to "hostile borders" adding to them further temporary "special areas" under the Ministry of Finances Declaration having regard to the hostilities existing at the time. At the time of the "temporary special areas" Declarations, instructions are also issued regarding the methods of obtaining compensation.

The Law empowers the Minister of Finance, under the promulgation of Regulations, to determine the rates of compensation including varying rates for differing assets. Under Regulations issued in 1973, the "injured" party is entitled to 100% compensation, except for aircraft where the rate is 50%. The Regulations also provide compensation for consequential damages including for expenses included in order to minimize losses, for example, the purchase of alternative goods in replacement of goods delayed in the ports. However, this compensation is limited to a "special area"

Administrative Instructions in Place of Regulations

The experience of the Second Lebanese War rendered the Regulation as having no relevance. Although Declarations were made and maps were published of "Limited Areas" covering areas which were within Katusha rocket range. The Residents of these areas did not receive full compensation for consequential damage as the relevant areas had not been declared as being "Border Areas". In lieuthereof, three sets of Administrative Instructions were issued.

The First Administrative Order: Granted compensation for consequential loss/damage to employers in industry, commerce and services at a rate of 132.5% of the average salaries of employees who did not report for work from 12 to 31, July 2006. This rate of compensation was determined by agreements during actual hostilities, on 27 July 2006, between the Finance Ministry, the General Workers Union and Industrial Employers in order to avoid dismissals of workers and to provide for continuing payment of wages, thereby preventing the dismissal of their wages and the re-imbursement to employers and also the payment to them of further compensation if due. This was based on the realization that wages due to employees comprise the major portion of employee expenses and that this method of compensation established the certainty of the amount of the compensation and a speedy mechanism for its payment.

In fact, the percentage amount of the compensation was substantially higher, 180% of the wages, less the contribution of the employees who waived their leave pay (20%) and the employers contribution (27.5%). The end result was that the compensation was at the rate of 132.5%. As will appear hereafter, and as determined by a Judgement of the High Court of Justice, the assumptions whereby the compensation was determined were incorrect in certain circumstances. In respect of medium sized and small businesses the expense of wages are not the largest type of expense and the largest impact is the loss of income during the period of the hostilities.

The Second Administrative Order: During August 2006, employers in the fields of, commerce, industry and the provision of services were given the opportunity to elect either, for compensation based on the wages of workers who were absent from their

places of work (as applicable in the month of July 2006) or upon the difference of income for the previous year less certain expenses which were saved and the payment by them of a "contributing" premium.

The Third Administrative Order: This Order enabled employers in the agricultural and tourist industries to compensation based on income declared for 2005 as compared with 2006 less certain expenses and the payment of a contributing premium.

Accordingly, the situation of those businesses in the Agricultural and Tourist Industries was preferable in that they could receive compensation for the full period of the hostilities, whilst those involved in the industrial, commercial and service industries were compensated only for the period of hostilities which took place in August.

The latter group filed legal proceedings before the High Court of Justice alleging that compensation only for the month of July 2006 discriminated against them and requested to be compensated on the same basis as those of the permanent "areas of hostility" or as for "seasonal industries" being agriculture and tourism (case No.6406/07).

The High Court determined that although the "July 2006" compensation was discriminatory and unreasonable it was not prepared to intervene and modify the decision of Ministry of Finance, which was the result of the agreement reached, as above, for budgetary reasons. The Judgment does not disclose whether the question of whether there was any consideration of the state of the "compensatory" fund or the sources of funds accumulated (or which were intended to be accumulated) for this purpose, namely compensation for consequential damage, so that, notwithstanding the fact that the Application was rejected, arguments of unreasonableness and the scope of budgetary consequences, could be relevant in future litigation.

To emphasize this point, the income to the State from "Land Betterment Tax" is estimated to be 3.25 billion shekels per annum (according to data for the years 2010-2012) and with the cancellation of property tax, as mentioned, the Ministry of Finance did not identify

other sources for the "compensation fund" in its press release preceding the present Regulations. Also the Ministry of Finance did not present any information on the amounts which had accumulated in the Fund.

In relation to the Second Lebanese War, the claim of Caspi Cruises Ltd, should be mentioned. At the time Caspi marketed cruises on the ship "Dream" which prior to the war normally sailed from Haifa port. As a result of the hostilities the departure port was changed to Ashdod. Caspi requested compensation for the extra expenses deriving from the change. Its claim was rejected on the main ground that additional expense to mitigate damages were confined to businesses operating in a defined "Hostile Area" and not to those in a "Limited Area" which did not benefit from the full scope of the compensation payable. The result was that those businesses in a "Limited Area" which endeavored to continue functioning "under fire" and suffered additional expenses as a result, did not receive realistic compensation.

The path of "Oferet Yitzukah"

In respect of the army operation known as "Oferet Yitzukah" special regulations were promulgated under which an area was stated in a map attached to the Regulations and was designated as being a "determining area" for the period of the hostilities (being from 27 December 2008 to 19 January 2009) which entitled businesses affected to claim compensation for consequential losses under one of four alternative possibilities, being :

- The Wages Possibility, under which the employer would receive compensation of 132% of the daily wages paid by the employer for each day the employee was absent from work.
- The Turnover Possibility, granting compensation calculated by the difference between Turnover for January 2008 and January 2009 multiplied by a "slow down" factor and less costs saved (85% of the average monthly expenses).
- The Expenses Possibility determining the amount of the compensation as being the difference between the business's expenses in

January 2009 (including wages) plus 10% and the income for January 2009.

- In respect of Agricultural damages for loss of produce, the compensation is determined by the daily production for each worker multiplied by the numbers of days during which the workers were absent from work provided that the absent workers were paid by the employers.

For the next military operation "Amud Anan", similar "Special Regulations" were promulgated. Areas designated on a map were deemed to be "designated areas" for the period (14-23 November 2012) and the four means of compensation mentioned above were followed. In respect of "garden function" areas, hotels and vacation rooms. For those electing compensation according to turnover, the compensation was determined according to the difference between the number of function or rooms orders for the period 23 November 2012 and February 2013 compared with those of previous years. In respect of agricultural production,

the comparison was between the quantities harvested when compared with those which were not harvested during the above period.

The "short arm" of the Legislature

Although the methods of the compensation were widened, as stated above and employers were not limited only to compensation for wages paid during the period of hostility the various means of compensation did not answer the substantial problem. For example, an industrialist in the 10 kilometer area from the border who during the period of hostilities was obliged to provide or deliver products which he had undertaken to do to a customer abroad and whose manufacturing process was affected by continual warning sirens, the curtailment of working shifts and the inability to deliver manufactured products either at the plant or at the ports because of delays, including those resulting from a shortage of drivers and in order to confront these problems, the manufacturer is forced to employ additional manpower or to purchase finished products from other manufacturers and who

somewhat manages to supply the products which he had undertaken to supply, in an attempt not to risk the possibility of "losing" his order and his customer. All these would cause such a manufacturer substantial expense.

Without necessarily experiencing a diminution of income and say, for the sake of argument his above activities resulted in a profit or a "breakeven" situation so that the "turnover possibility" or the "expense possibility" would not be relevant to such a manufacturer in that compensation for such additional expenses is not available notwithstanding the fact that the Law defines loss as including the "prevention of profit" and under a proper interpretation of the Law, the additional expenses prevent the profit he would have made in the course of his normal business activity.

It should be observed, that the Ministry of Finance did not declare those areas of conflict as a "Hostile Area" and in place thereof used expression such as "A Determined Area" or "A Limited Area" or "A Declared Area". In this manner the Minister of Finance avoided granting those affected the full means of compensation possible under the interpretation and definition of "consequential damages".

Insofar as the "Zuk Eitan" operation was concerned a map was published delimitating a line of 40 kilometers from the border with Gaza which was designated as a "special area". The "special area" is from the north of Ashdod, opposite Givat Brenner and continues east until Beersheva, Tel Sheva and Naot Hovev. In respect of this area consequential damage compensation was determined which does not provide an answer for all the financial loss, as is the situation for the defined "Hostile Areas" (an area within 7 kilometers from the Gaza border) and which is substantively similar to the methods of compensation determined previously.

Prima Facie, according to a notice published by the Ministry of Finance in respect of the Zuk Eitan operation, a further compensation possibility was added namely "The Expense Possibility" which enables the owner of a business to receive compensation for an operational loss suffered during

the relevant period. The Ministry of Finance states that the intention of the "expense possibility" was intended to compensate for additional expenses incurred in order to maintain the businesses turnover during the period of the military operation.

However, an examination of these new Regulations suggests that there is no substantial difference when compared with those Regulations which preceded the new regulation, in that the former provided for compensation based on the difference between "normal" expenses plus 10% thereof and the income received, for the period of the hostilities.

The new regulations do not meet a situation where extraordinary expenses were incurred in order to maintain the level of sales and supplies necessary to ensure that economic level required during the hostilities, in that the level of expenses would be far more than those incurred in "normal" times. The "new" regulations do not provide an adequate means of compensation for such "additional expenses" which were incurred in order to maintain that level of sales or supplies and to achieve economic parity during the period of hostilities bearing in mind that if not for the hostilities the expenses would have been far less and in respect of these additional expenses there is no compensation.

The impression received is that the Notice of the Ministry of Finance has indulged in a "superficial" description of the "expense possibility" and the notice does not comply with the reality of what is stated in the Regulation. For business owners situated in the South there are accordingly available a number of possibilities. However, notwithstanding the various declarations, and "co-operation" and understandings between the "Ministry of Finance" and the Industrialists Council, it is not at all clear or possible that there is a method of compensation which covers, all the additional expenses and indirect and financial loss, directly arising from the period of hostilities.

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