



# Israel

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## Important new developments

- Israeli lawyers and accountants are subject to detailed know-your-customer (KYC) rules.
- US-Israel inter-governmental agreement (IGA) (Type 1) was implemented in September 2016.
- Israel has committed to apply the OECD Common Reporting Standard in 2018.
- The legislation regarding international agreements for exchange of information was passed at the Israeli Parliament (relevant regulations are yet to be published).
- Israeli banks are required by a Bank of Israel directive to inquire whether applicable taxes have been paid by non-resident and immigrant account holders.
- Various voluntary disclosure procedures expired on 31 December 2016.
- Any trust which has or ever had an Israeli-resident beneficiary is potentially taxable commencing 1 January 2014, unless an exemption for overseas income of a new resident or senior returning resident (who lived abroad for more than ten years).
- The Finance Minister and senior tax officials have indicated that an inheritance tax might be under consideration, but no formal announcement has been made in this regard.
- Immigrants who enjoy a ten-year Israeli tax exemption on foreign income and gains may need to report the exempt income and

gains from 1 January 2017 according to proposals published by the Israeli Treasury on 3 August 2016.

## Legal system

Israel's legal system is based on Anglo-American traditions and has been influenced by the Ottoman rule (1516-1917) and the British Mandate (1917-1948). Since 1948, Israel has enacted its own laws. Personal status is governed according to religious law (Jews, Muslims, Christians, Druze).

## INHERITANCE AND SUCCESSION

### **Succession**

The law that governs succession in Israel is the *Succession Law 5725-1965* (the Succession Law), which determines two ways of bequeathing: by will or intestate in accordance with the law. There are no forced heirship rules in Israel, and each competent adult can bequeath his estate in a valid will as he wishes. The following are eligible legal heirs: the decedent's spouse, the decedent's children and their issue, the decedent's parents and their issue, the decedent's grandparents and their issue, and the State of Israel. Four forms of wills are recognised as valid, provided they comply with the requirements of the Succession Law: handwritten will, will executed in the presence of witnesses, will executed before an authority, and oral will. The execution of a will is a personal act that must be done by the testator personally.

### **Family law and defined inheritance rules**

If the decedent died intestate, the decedent's spouse (including a common-law spouse) is entitled to all movable property, including a car that was part of the common household regime. Additional share of the estate depends on the other surviving heirs.

### **Probate process**

The Israeli court has jurisdiction over the estate of any person who resides in Israel at the time of their demise or who owned property in Israel. Upon such person's demise, an application for

probate or succession order should be filed with the Registrar of Inheritance, together with a death certificate and original will (if it is not possible for a reasonable cause to submit the original, then it is possible to request to submit a copy of the will as a substitute). If the deceased did not reside in Israel, it is also necessary to submit a legal opinion provided by an attorney who is familiar with the succession laws in the country where the deceased resided.

### **Mental capacity**

Any person over 18 years is capable of making a will and any other legal actions, unless they are declared by a competent court to be incompetent, as determined in the *Legal Competence and Guardianship Law 5722-1962*. If a person is incompetent, it is possible to appoint a guardian of the property and/or the person. According to a new amendment that was enacted to the *Legal Competence and Guardianship Law 5722-1962*, it is now possible for a person to sign a lasting power of attorney that will remain in force even in case of incapacity. Such power of attorney should be signed in accordance with the requirements of the law and should be deposited with the General Custodian.

## ESTATE PLANNING

### **Use of trusts in estate planning**

Trusts may be used for a variety of estate-planning purposes in the manners set out below.

A trust purports to cover any situation in which someone is empowered to deal with property for the benefit of another and will be valid and enforceable where there is a definite beneficiary, or where there is no definite beneficiary but there is some purpose to the trust.

A trust may be created by law, agreement or deed.

The deed must be in writing, signed before a notary (if *inter vivos*) or constitute a formal will, express the intent of the creator to found a trust and must outline the purposes, properties and conditions. The trust is settled upon the trustee gaining control of the trust assets. Where trust property exists but no deed is found, the court may declare the existence of a trust and define its purposes, properties and conditions.

A contract requires no formality but is limited



to creating an *inter vivos* trust that will require probate proceedings.

A testamentary trust, effective upon the death of the settlor, must be in writing, by making a valid testament under the Succession Law (free will of the testator, being of clear mind and being at liberty to change the testament whenever and however the testator wishes).

Where testaments would have been declared void for uncertainty under the Succession Law, the trust law will give effect to them provided that the wishes of the testator can be fulfilled by constituting a trust. The courts consider fulfilment of the wishes of the testator as the prime object of the law relating to wills.

A public endowment is one with an objective of furthering a public purpose (such as education, culture, religion). The beneficiary may be a specific group of persons with a particular shared characteristic, for example, a group of children, or a group of disabled persons.

Israel is not a party to the *Hague Convention on the Law Applicable to Trusts and on their Recognition*, 1 July 1985.

### Use of foundations in estate planning

Professionals in Israel are familiar with the concept of private trusts. The Israeli tax laws enable foreign legal structures such as foundations, establishments or trusts established under foreign laws to be recognised as trusts for taxation purposes in Israel.

Israeli professionals tend to use foundations where a civil-law structure is preferred.

The main reason for the usage of trusts and foundations under foreign laws is the lack of Israeli court precedents.

### Types of entities

Underlying company: an underlying company of a trust is a separate legal (Israeli or foreign) entity that holds a trust's assets for the trustee. All its shares are held by the trustee and it is transparent for taxation purposes and therefore taxed according to the trust categorisation in accordance with the *Taxation of Trusts Law 2005*.

## TAXATION

### Income tax system

Israeli-resident individuals and entities are subject to Israeli tax on their worldwide income and gains. Trusts with Israeli-resident beneficiaries are generally taxable, according to detailed rules. Israeli residents may claim a foreign tax credit for foreign taxes on foreign-source income and gains. An individual is generally resident if their centre of life is in Israel. A company is generally resident in Israel if it is incorporated or controlled and managed in Israel.

Businesses in Israel must register for VAT and income tax purposes as soon as they commence trading. Tax reporting is monthly or bi-monthly as well as annually. Accounting records and invoices to customers must conform to detailed rules – foreign software packages require special permission.

Consult experienced tax advisors in each country at an early stage in specific cases. The material herein cannot be used to avoid penalties.

### Personal income tax rates

Personal income tax rates in Israel in 2016 are as follows:

- Earned income from employment or self-employment – 10-50 per cent.
- Passive income: dividends – 25-32 per cent; interest – 15-50 per cent; capital gains 15-50 per cent.

National insurance (social security) rates are currently as follows:

- Resident employees – 3.5-12 per cent.
- Employers of resident employees – 3.45-7.5 per cent.
- Non-resident employees – 0.04-0.87 per cent.
- Employers of non-resident employees – 0.49-2.55 per cent.
- Self-employed individuals – 9.82-16.23 per cent.
- Non-Employment Passive Income – 9.61-12 per cent.
- No national insurance on dividends, capital gains and other income exceeding ILS43,240 per month (in 2016).
- National insurance payments unrelated to employment are 52 per cent tax deductible.
- Foreign employee payroll levy: generally – 20 per cent; in industry, construction and restaurants – 15 per cent; in agriculture – 10 per cent. The levy does not apply to personnel who earn double the national average salary (approximately ILS18,928 per month currently).

New residents and senior returning residents (after residing abroad for 10 years) enjoy an exemption for 10 years from Israeli tax on foreign-source income and capital gains and immunity from rules regarding 'control and management' and 'controlled foreign companies' and 'foreign professional companies'. More restrictive benefits apply for five to 10 years to individuals who became resident before 1 January 2007, and to returning residents who lived abroad six to 10 years and returned after 1 January 2009. New residents also enjoy certain import tax benefits.

Israeli residents enjoy various personal tax credits, which are increased for new and senior returning residents in their first 3.5 years in Israel.

Subject to any treaty, trusts and foundations with an Israeli-resident, settlor or beneficiary are generally taxable in Israel like individuals, but subject to detailed rules regarding timing, rates and extent of taxation. The taxpayer is generally the trustee unless otherwise elected jointly by the trustee and settlor or beneficiary.

Special rules apply to trusts involving new immigrants, foreign resident beneficiaries and underlying companies.

Immigrants may need to report foreign exempt income and gains from 1 January 2017, according to proposals.

### Corporate income tax rates

Israeli company tax rates in 2016 (no change anticipated in 2017) are as follows:

- Regular income – 25 per cent.
- Tax breaks for industry and technology companies from a 'preferred enterprise' according to the *Law for the Encouragement of Capital Investments, 1959* – development – 9 per cent in development area A, 16 per cent elsewhere in Israel. Dividends therefrom are taxed at 20 per cent. Proposals are being

formulated to reduce these tax rates.

- Other tax breaks exist for large scale 'special preferred enterprises', tourism and agricultural enterprises.
- Import duty breaks under Israel's free trade agreements with the EU, USA, EFTA, Canada, Mexico, Mercosur, Turkey, Jordan and Egypt.

### Capital gains tax

Capital gains are divided into real (inflation adjusted) and inflationary components. Individuals are generally taxed on realised gains at rates of 25 per cent to 32 per cent, but rates of up to 50 per cent are possible for any portion accruing before 2003. Companies pay tax on realised gains at the standard rate of company tax (25 per cent in 2016). The inflationary component is exempt from tax to the extent that it accrued on or after 1 January 1994, and is generally taxable at a rate of 10 per cent to the extent that it accrued before that date. Israeli real estate sales are subject to land appreciation tax according to separate but similar rules.

### Non-residents taxable on

Subject to any tax treaty, foreign residents are subject to Israeli tax on income and certain capital gains that are accrued or derived in Israel according to detailed source rules. Living and *per diem* deductions apply to foreign residents for 12 months. Foreign residents may be exempt:

- Per any applicable tax treaty.
- On capital gains from Israeli securities unrelated to Israeli real estate or natural resources.

### Withholding tax rate (non-treaty)

Salaries are subject to detailed withholding rules similar to PAYE in the UK and some other countries. Payments to suppliers are subject to withholding tax rates, typically 30 per cent, unless the recipient holds withholding tax clearance from the Israeli Tax Authority. Passive income is subject to withholding tax at rates of 15 per cent to 30 per cent.

### Withholding tax rate (treaty)

Subject to any tax treaty, payments to foreign residents are typically subject to 25 per cent withholding tax. This tax is usually withheld by Israeli banks unless presented with clearance for any lower rate from the Israeli Tax Authority, for example, pursuant to a treaty.

### Taxation at death

Israel does not impose estate taxes upon death. Concessionary relief is available for Israeli residents who receive assets from abroad to 'step up' the cost basis for capital gains tax purposes to the market value upon receipt.

### Other taxes

Israel generally does not tax gifts made in good faith. Gifts of assets to foreign residents are subject to Capital Gains Tax (CGT). CGT applies to people who cease to be Israeli residents, payable upon departure or upon sale.

### Tax treaties

Israel has tax treaties with more than 50 countries. For further details, visit: <http://bit.ly/2aIgiNk> and <http://bit.ly/2aIAoTw>

Israel has also signed comprehensive social security conventions with the 19 countries. For details visit: <http://bit.ly/1xhusrX>

#### Tax information exchange agreements

The US-Israel IGA (Type 1) was scheduled to be implemented in September 2016.

Israel has committed to apply the OECD Common Reporting System in 2018.

The legislation regarding international agreements for exchange of information was passed at the Israeli Parliament (relevant regulations are yet to be published).

### RESIDENCE AND DOMICILE

#### Special rules on becoming resident

An Israeli resident is an individual whose centre of life (permanent home, family, social, economic ties, and so on (qualitative test)) is in Israel. It is assumed that an individual's life is centred in Israel in a tax year if they spent 183 days or more in Israel in the tax year, or if he spent 30 or more days in Israel and the total period of his stay in Israel in the tax year and in the two preceding years was 425 days or more (quantitative test). A recent ruling (the 'Sapir Case') held that it is possible for an individual to maintain his centre of life in one country while his spouse and children live in another. This is possible due to the subjective test.

#### Special rules on ceasing residence

An individual ceases to be an Israeli resident if they stay abroad for 183 days or more during two consecutive tax years and their centre of life is not in Israel for an additional two years.

#### Domicile concept for gifts and inheritance

NOT APPLICABLE

#### Taxation of holdings by non-residents on

- Gifts: none.
- Death: none.

#### Reporting/auditing requirements

YES ☒ NO ☐

An individual who met one of the days assumptions mentioned above, but claims that his centre of life is not in Israel (and accordingly he should not be regarded as an Israeli resident) should file a short notice in this regard.

### OTHER RELEVANT INFORMATION

#### Asset protection laws

YES ☒ NO ☐

There are several asset protection laws applicable under Israeli law such as the bankruptcy law or the spouse property law.

#### Foreign currency restrictions

YES ☐ NO ☒

#### Foreign ownership restrictions

YES ☐ NO ☒

#### AML/due diligence and other requirements and regulatory procedures for advisors

- To establish a trust: As of September 2015, under anti-money laundering (AML) rules, lawyers and accountants are required to identify clients in person, obtain details of the clients and that of the final beneficiaries, be familiar with their business and maintain declarations and records of the aforesaid, as a precondition for establishment and management of a trust. Certain reporting requirements for settlors, trustees and beneficiaries exist under the Income Tax Ordinance.

- For incorporation: As of September 2015, under AML rules, lawyers and accountants are required to identify clients in person, obtain details of the clients and that of the final beneficiaries, be familiar with their business and maintain declarations and records of the aforesaid, as a precondition for establishment or management of a corporation or business. The Companies' Law requires a trustee shareholder to report the existence of the trust and a notice of the trust to be registered in the company's own register of shareholders of the company, which it is obliged to maintain and open to public inspection.
- To open a bank account: AML rules require banks to be familiar with clients and their business, identify clients in person, obtain details of the clients and that of the final beneficiaries, and maintain declarations and records of the aforesaid as a condition for opening of any account.
- As of October 2016, in addition to VAT offence of issuing fictitious invoices, the only current AML tax offence, certain new severe tax offenses shall be considered as offenses under AML law, and shall therefore be subject to punishment and sanctions under AML law. Such new offences include, under certain conditions, intended evasion of income tax, VAT and real estate capital gains tax (betterment tax). These offenses are applicable not only to offenders themselves but also to any person who assisted them, including their advisors.

#### More details

The latest updates to this report are available at [www.step.org/jr-israel](http://www.step.org/jr-israel)