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Certified Public Accountants (Isr.)

# TAXATION AND REPORTING OF TRUSTS IN ISRAEL



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## Does your trust have any Israeli beneficiaries?

Since 1/1/2006 trusts that had Israeli resident settlors were subject to Israeli taxation and reporting, while foreign settlor trusts were generally not taxable. As of January 1, 2014, foreign settlor trusts that have an Israeli tax resident beneficiary are subject to Israeli taxation and reporting. This type of trust (for tax purposes), the Israeli Beneficiary Trust (IBT) replaced the old Foreign Settlor Trust. The reporting and taxation of the IBT applies to the "portion" to be attributed to the Israeli beneficiaries; Trusts are required to report their underlying companies which are taxable (at trust tax rates).

There are two types of IBT's:

1. **Family/relatives Trust** – in which settlor and beneficiaries are close family relatives, and the settlor or his spouse is still alive, may elect to be taxed annually at 25% or defer tax payment to distribution date at a 30% rate (capital portion exempt).
2. **Non Family/relative trusts** – in which settlor and beneficiaries are not relatives, are taxed annually at regular individual rates.

Trustees of IBT's are required to:

1. Open a tax file for each IBT and disclose its assets.
2. Elect the preferred tax route (See B2).
3. Sign and submit annual tax returns (annual tax route).
4. Report and pay taxes upon distributions (distribution tax route).
5. Check whether any beneficiaries are over the age of 25, and the value of the assets of the trust exceeds 500,000 NIS. Tax files require to be opened for such beneficiaries.

Important notes for trustees:

1. Trustees should obtain documentation as to the value of trust's assets as at December 31<sup>st</sup>, preceding the first year of reporting.
2. Where possible trustees should prepare a schedule with a breakdown of the original trust capital and the profits.
3. Obtain a schedule (and documentation) of taxes paid on trust income (by trust, beneficiaries or underlying companies) to date.
4. All distributions starting August 1, 2013, are reportable by recipients.

***This brief synopsis is intended to enable evaluation of trusts for Israeli tax purposes. Additional bylaws and directives may impact materially. It is recommended that specific professional advice be sought before any action is taken.***



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## TAXATION OF TRUSTS IN ISRAEL – Brief Memo

### A. Classification of Trusts

1. The Laws governing taxation of trusts in Israel came into effect as of January 2006. More recent legislation – effective as of 2014 – includes the taxation of foreign-settled trusts in Israel.
2. The donor/transferor of assets to the trust is also considered a settlor/grantor. There may be more than one settlor/grantor. The definition includes a beneficiary where able to exercise direct or indirect control of the trust.
3. Where the trust has Israel-resident beneficiaries, it will be taxable in Israel, subject to certain exceptions.
4. A family trust (close family relationship between settlor/grantor and beneficiaries) is defined in the Law and is also conditional on the settlor or spouse being alive.
5. Where the trust is fully irrevocable/discretionary – as defined – then where all the beneficiaries are foreign, the income of the trust will not be taxable in Israel, subject to various conditions. There is a provision for taxing only that part of the trust income that relates to Israel-resident beneficiaries.
6. On the death of the settlor/grantor, where there is an Israel-resident beneficiary, the trust will be considered an Israel-resident trust.
7. A trust settled by a new immigrant/resident is entitled to certain Income Tax benefits (“the 10-year tax holiday”) available to the settlor; subsequent to August 1, 2013, there are certain limitations, particularly as relates to beneficiaries resident in Israel but not falling within the ambit of the “10-year” rule.

### B. Income Tax Factors

1. Rates of tax on passive income will generally be 25% (additional 3% “Wealth Tax” where taxable income exceeds the ceiling).
2. Trustees of family trusts (see A4 above) may elect to be taxed at 25% of the taxable income of the trust or 30% on distributions (with allowance for neutralizing the capital contributed). This election is not reversible.



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**B. Income Tax Factors (Cont'd)**

3. The residence of the trustees will not impact on the taxability of the trust.
4. Underlying companies, (holding trust assets and owned by the trust), will generally be treated as part of the trust structure and taxed accordingly (subject to certain conditions).
5. Dissolution of existing trusts may have tax consequences.
6. Beneficiaries are required to report on distributions received in kind or cash, and irrespective of whether taxable.

**C. General**

1. It should be noted that ITA directives may impact.
2. An arrangement, whereby a trustee holds assets for a beneficiary, may be defined as a trust, even where not formally established under Trust Law, locally or abroad.
3. Under certain conditions, the settlor/grantor may report to the Tax Authority (and thus be the taxable entity) and not the trustees.
4. Where the beneficiaries of a foreign-settled charitable trust are public institutions – as defined – then they will retain their foreign status.

This is a very brief synopsis of the Tax Laws pertaining to taxation of trusts in Israel, and is intended for reference only. The original Law in Hebrew is the final and authoritative basis for making decisions.

Whilst every care has been taken in compilation, no responsibility can be accepted for inaccuracies or errors. Changes in the Law or practice occur periodically; it is recommended that specific professional advice be sought before any action is taken.



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## PLAN IN ADVANCE – TRUSTS

- There are planning opportunities during the 10-year period:
  - ❖ Freedom to create, change or cancel.
  - ❖ The exemption is relevant to IBT's, which are exempt from paying tax and reporting trust income during the 10-year exemption period.
- IBT's created during the 10-year period will also enjoy the exemption.
- Serious planning before the end of the 10-year period.



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## **Preliminary Questionnaire**

### **Taxation of Trusts\* in Israel: For Clients**

#### **A. Settlor/Grantor (incl. 'economic' settlor)**

1. Is/was settlor/grantor resident outside Israel?
2. Is settlor/grantor alive? (If not, date of death).
3. Has the settlor/grantor immigrated to Israel or become a new resident? If so, indicate date (earlier of immigration or residence).

#### **B. Beneficiaries**

1. Are there Israel-resident beneficiaries? What was their date of immigration/becoming resident?
2. What is their family relationship to the settlor/grantor?
3. Is an Israel-resident beneficiary able to exercise control (direct or indirect) of the trust?
4. Are distributions to beneficiaries conditional on the death of the settlor/grantor or other beneficiaries?
5. Are there non-Israel-resident beneficiaries?
6. Have beneficiaries contributed assets to trust? Or made or received loans?

#### **C. General**

1. Is trust taxable in any other tax jurisdiction?
2. Is there any underlying company which holds trust assets?
3. Is trust fully discretionary/irrevocable?
4. What is nature of trust assets? (e.g. shares, bonds, property, etc.)

**\*Includes Foundations**

***This questionnaire is intended to enable preliminary evaluation of the trust for Israeli tax purposes; further information and documentation will be required at a later stage. By-laws and ITA directives may create additional requirements.***



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### **Registration of Trust with the Israel Tax Authority**

The following documents and information are required in order to register a trust:

- a. Copy of Trust Deed, subsequent amendments and related documents.
- b. Copy of most recent Financial Statements. (Trust and underlying companies)
- c. Details:
  - Date of formation
  - Name of Trust
  - Relationship of Settlor/Grantor to beneficiaries
  - Protector/s ]
  - Trustees ] including names, addresses
  - Settlor/s/Grantor/s ] ID/passport numbers/Company number
  - Beneficiaries ]
  - Assets held by trust, including date of acquisition, description, original cost and value at year-end (schedule/report).
- d. Copies of passports or corporate documents for trustees.
- e. Holding company, owning assets of trust (“underlying company”) - copy of corporate documents and details of shareholders and assets.