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## INCOME TAX ORDINANCE [NEW VERSION] 5721-1961

### PART ONE – INTERPRETATION

#### Definitions

1. In this Ordinance –
  - "person"** – includes a company and a body of persons, as defined in this section;
  - "house property"**, in an urban area – within its meaning in the Urban Property Ordinance 1940;
  - "Exchange"** – a securities exchange, to which a license was given under section 45 of the Securities Law, or a securities exchange abroad, which was approved by whoever is entitled to approve it under the statutes of the State where it functions, and also an organized market – in Israel or abroad – except when there is an explicitly different provision;
  - "spouse"** – a married person who lives and manages a joint household with the person to whom he is married;
  - "registered spouse"** – a spouse designated or selected under section 64B;
  - "industrial building"**, in an area that is not urban – within its meaning in the Rural Property Tax Ordinance 1942;
  - "retirement age"** – the retirement age, within its meaning in the Retirement Age Law 5764-2004;
  - "income"** – a person's total income from the sources specified in sections 2 and together with amounts in respect of which any statute provides that they be treated as income for purposes of this Ordinance;
  - "chargeable income"** – income, after the deductions, set-offs and exemptions from it, which are allowed under any statute;
  - "linkage differentials"** – any amount added to a debt or to a claimed amount in consequence of linkage to the currency exchange rate, the consumer price index or to some other index, including exchange rate differentials; however, for purposes of tax exemption, any amount added to a debt or to the amount of a claim in consequence of linkage to the currency exchange rate or to the Consumer Price Index – including exchange rate differentials – shall be deemed linkage differentials;
  - "linkage differentials and interest"** – within their meaning in section 159A(a);
  - "exchange rate differentials"** – any amount added – in consequence of a change in the currency exchange rate – to the principal of a loan, which is a foreign currency deposit or a loan repayable in foreign currency;
  - "work income"** – income under section 2(2);
  - "real estate association right"** – within its meaning in the Real Estate Taxation Law;
  - "real estate right"** – as defined in the Real Estate Taxation Law;
  - "body of persons"** – any public body, incorporated or amalgamated, and any company, fraternity, fellowship or society, whether incorporated or not;
  - "company"** – a company incorporated or registered under any Law in effect in Israel or elsewhere, including a cooperative society;
  - "month"** – includes a part thereof;
  - "Taxation under Inflationary Conditions Law"** – the Income Tax Law (Taxation under Inflationary Conditions) 5742-1982;
  - "Inflationary Adjustments Law"** – the Income Tax Law (Inflationary Adjustments) 5745-1985;
  - "Investment Encouragement Law"** – the Encouragement of Capital Investments Law 5719-1959;
  - "Real Estate Taxation Law"** – the Real Estate Taxation (Appreciation, Sale

and Acquisition) Law 5723-1963;

**"VAT Law"** – the Value Added Tax Law 5736-1975;

**"Companies Ordinance"** – the Companies Ordinance [New Version] 5743-1983;

**"Companies Law"** – the Companies Law 5759-1999;

**"Savings Encouragement Law"** – the Encouragement of Savings (Income Tax Reductions and Guaranty of Loans) Law 5716-1956;

**"Securities Law"** – the Securities Law 5728-1968;

**"Amutot Law"** – the Amutot (Nonprofit Societies) Law 5740-1980;

**"Industry Encouragement Law"** – the Encouragement of Industry (Taxes) Law 5729-1969;

**"Control of Benefit Funds Law"** – the Control of Financial Services (Benefit Funds) Law 5765-2005;

**"Joint Investment Trusts Law"** – the Joint Investment Trusts Law 5754-1994;

**"adjusted amount"** – any amount, plus that amount multiplied by the index increase;

**"Israel resident" or "resident"** –

(a) in respect individuals – a person, the center of whose life is in Israel, and the following provisions shall apply to this matter:

(1) in order to determine the place that is the center of a person's life, the totality of his family, economic and social ties shall be taken into account, including inter alia:

- (a) the place of his permanent home;
- (b) his and his family's place of residence;
- (c) his regular or permanent place of business or the place of his permanent employment;
- (d) the place of his active and substantive economic interests;
- (e) the place of his activity in organizations, societies and various institutions;

(2) it is assumed that the center of an individual's life during a tax year is in Israel –

- (a) if during the tax year he spent 183 or more days in Israel;
- (b) if during the tax year 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 years before it was 425 days or more;

for purposes of this paragraph, "**day**" includes part of a day;

(3) the assumption in paragraph (2) may be refuted both by the individual and by the Assessing Officer;

(4) the Minister of Finance may, with approval by the Knesset Finance Committee, prescribe conditions under which an individual who is not an Israel resident under paragraphs (1) and (2) shall be deemed an Israel resident, on condition that one of the following holds true for him:

- (a) he is an Israel State employee;
- (b) he is an employee of a local authority in Israel;
- (c) he is an employee of the Jewish Agency for Israel;
- (d) he is an employee of the Jewish National Fund, Keren Hayessod – United Israel Appeal;
- (e) he is an employee of a Government corporation;
- (f) he is an employee of a Government Authority or of a body corporate set up under a Law;

and he may also prescribe as aforesaid that categories of individuals deemed Israel residents under paragraphs (1) and (2)

- shall not be so deemed, all on conditions that he shall prescribe;
- (b) in respect of a body of persons – a body of persons for which one of the following holds true:
- (1) it incorporated in Israel;
  - (2) its business and management are activated from Israel, except for a body of persons, the business of which is controlled and managed in Israel by an individual who became an Israel resident for the first time or is a veteran returning resident, as said in section 14(a) and ten years have not yet passed since he became an Israel resident as aforesaid, or by any person on his behalf, on condition that that body of persons would not be an Israel resident if the control and management of its business were not by a said individual or by a person on his behalf, unless the body of persons requested otherwise.

**"foreign resident"** – a person who is not an Israel resident, and also an individual for whom all the following hold true:

- (a) he stay abroad for at least 183 days in each year, in the tax year and in the following tax year;
- (b) the center of his life was not in Israel, as said in paragraph (a)(1) of the definition of "Israel resident" or "resident", during two tax years after the tax years said in subparagraph (a);

**"income from personal exertion"** includes –

- (1) a pension paid by a former employer;
- (2) a pension paid by a benefit pension fund in respect of employment or by virtue of membership in it during not less than five years, to a person most of whose chargeable income – in the five years before payment of the pension began – was from personal exertion;
- (3) a pension paid to the survivor of a person to whom paragraphs (1) or (2) apply, by virtue of his entitlement to a pension as said there;
- (3a) a loss of working capacity pension paid by a pension benefit fund or by a savings benefit fund, or paid under loss of working capacity insurance; for this purpose, "loss of working capacity" – an impairment of working capacity due to disease, invalidity or accident, which caused the loss of wage income or profits under section 2(1) or (2);
- (4) a taxable pension paid by the National Insurance Institute;
- (5) a grant received in consequence of retirement or death;
- (6) an amount received in consequence of the capitalization of one of the pensions said in paragraphs (1) to (4);
- (7) an amount received by a person as rent for renting out an asset, which served that person during at least ten years before its rental for the production of income from personal exertion from business or vocation; for this purpose, "person" includes whoever was his spouse immediately before his death;

**"index"** – the consumer price index published by the Central Bureau of Statistics;

**"rate of index increase"**, in a certain period – the difference between the index last published before the end of the period and the index last published before the beginning of the period, divided by the index last published before the beginning of the period;

**"preferred loans"** – loan or deposits under savings schemes, on which interest is wholly or partly exempt of tax under any statute, unless otherwise provided in that statute, and also participation certificates therein;

**"income tax" or "tax"** – either income tax or companies tax imposed under this Ordinance;

**"foreign taxes"** – as defined in section 199;  
**"reciprocating state"** – within its meaning in section 196;  
**"vocation"** – a profession and any other vocation, other than a business;  
**"security"** – as defined in section 88;  
**"assessee"** – a person who had income during the tax year;  
**"Director"** – the Director appointed under section 229, including the Deputy Director;  
**"business"** – including commerce, handicraft, agriculture or industry;  
**"output"** – as defined in the Computers Law 5755-1995;  
**"acceptable books"** – account books that the Assessing Officer did not refuse to accept and did not reject, or that he refused to accept or rejected, but a committee under section 146 or the Court set aside his decision, but books shall not be deemed acceptable if the assessee admitted that they are not acceptable, and if he certified in writing that the legal consequences of his admission were explained to him;  
**"legal incompetents"** – a minor, a mentally defective or insane person, and any person not competent for a legal act;  
**"Assessing Officer"** – an officer authorized by the Minister of Finance to make assessments under this Ordinance, including a Deputy Assessing Officer, an Assistant Assessing Officer or a Chief Collector, whom the Director authorized in writing to exercise a certain power of Assessing Officers under this Ordinance or to carry out certain of their functions; appointments of Assessing Officers, of Deputy Assessing Officers, of Assistant Assessing Officers or Chief Collectors authorized as aforesaid shall be published in Reshumot;  
**"deposit"** – an amount deposited with a banking corporation or with a banking institution abroad, which operates under the Law of the country in which it operates;  
**"benefit fund", "savings benefit fund", "severance pay benefit fund", "pension benefit fund", "training fund" and "insurance fund"** – as defined in the Control of Benefit Funds Law;  
**"land"**, in an urban area – within its meaning in the Urban Property Tax Ordinance 1940; in an area that is not urban – within its meaning in the Rural Property Tax Ordinance 1942;  
**"debenture interest"** – interest which an incorporated body must pay according to or by virtue of a debenture or of a debenture trust deed, whether in the form of a mortgage or in the form of a document or certificate of some other kind, which includes acknowledgment of the obligation;  
**"local authority"** – a municipality, local council, or other similar authority established under a Law that is in effect at the time, which provides for the creation of local Government authorities, including a cooperative society or any other body which at the time performs the functions of a local authority;  
**"organized market"** – a system whereby trading in securities is conducted according to rules prescribed by whoever is entitled to prescribe them under the statutes of the State in which it is conducted;  
**"urban area"** – an area in which urban property tax is payable under the Urban Property Tax Ordinance 1940;  
**"tax year"** – a period of twelve consecutive months that begins on January 1, and if a special assessment period was determined, then the assessment period determined as aforesaid;  
**"banking corporation"** – within its meaning in the Banking (Licensing) Law 5741-1981;  
**"savings program"** – in a banking corporation, including a savings plan approved under the Savings Encouragement Law and also the savings

component of a life insurance policy or a savings plan attached to a said policy and approved by the Controller of Insurance, within the meaning of the term in the Insurance Business (Control) Law 5741-1961.

## **PART TWO: IMPOSITION OF TAX**

### **CHAPTER ONE: SOURCE**

#### **Sources of income**

2. Subject to the provisions of this Ordinance, income tax shall be payable for each tax year, at the rates specified below, on the income of a person resident in Israel, which was produced or which accrued in Israel or abroad and on the income of a foreign resident which was produced or which accrued in Israel from the following sources:

#### **Business and vocation**

- (1) wages or profits from any business or vocation exercised for any length of time, or from any incidental transaction or deal of a commercial character;

#### **Employment**

- (2) (a) wages or profits from employment; any benefit or allowance given to an employee by his employer; payments made to employees to cover their expenses, including payments for maintaining a vehicle or telephone, travel abroad or the acquisition of professional literature or of clothing, but exclusive of aforesaid payments which for the employee are deductible as expenses; the value of the use of a vehicle or of a mobile radio-telephone placed at an employee's disposal; all whether paid in cash or in kind, whether given to the employee directly or indirectly or given to another for his benefit;
- (b) the Minister of Finance shall, with approval by the Knesset Finance Committee, determine the value of the use of a vehicle or of a mobile radio-telephone placed at the employee's disposal as aforesaid;

- (3) Repealed

#### **Dividends, interest and linkage differentials**

- (4) dividends, including dividends paid out of a company's capital gains, and interest, linkage differentials or discounts;

#### **Benefits**

- (5) pension, usufruct or annuity;

#### **House property and land**

- (6) rents, royalties, keymoney, premiums and other profits derived from house property, land or industrial buildings; if a person built a house property and let it and received keymoney or a premium for the letting, and if after he let it he sold that house property directly or indirectly to another, under an agreement made when or before the property was let,

then the purchaser shall be deemed to have received keymoney or a premium of the same amount on the date of the purchase; if the purchase is made within one year after the letting, that shall be prima facie evidence that there was an aforesaid agreement;

#### **Other assets**

- (7) gains or profits derived from any asset other than house property, land or industrial buildings;

#### **Agriculture**

- (8) gains or profits derived from agriculture, land cultivation, afforestation or crops, including the value of any produce received in consideration of the use of capital, assets, seed or domesticated animals, for purpose of the sources of income said in this paragraph, and including a share of profits received in respect of the aforesaid use;

#### **Patent and copyright**

- (9) consideration received for the sale of a patent or design by the inventor, or for the sale of a copyright by the author, if the invention was made or the work produced not within the scope of the inventor's or author's ordinary occupation;

#### **Other sources**

- (10) gains and profits from any other source not included in paragraphs (1) to (9), but not explicitly excluded from them and no exemption having been granted on them in this Ordinance or in any other statute.

#### **Gains or profit from gambling, lotteries or prizes**

- 2A. (a) Gains or profits of an Israel resident person, produced or accrued in Israel or abroad, as well as gains or profits of a foreign resident person, produced or accrued in Israel, the source of which is gambling, lotteries or prize winning activity, shall be taken into account in determining his profits or income and for the purposes of this Ordinance they shall be deemed income, except in respect of the set-off of losses.
- (b) The provisions of subsection (a) shall not apply to each of the following:
  - (1) gains or profit, which under this Ordinance constitute income from some other source;
  - (2) gains or profits from prizes given within a personal framework;
  - (3) gains or profits from lotteries or prizes designated by the Minister of Finance with approval by the Knesset Finance Committee.

#### **Other income**

- 3. (a) An amount received by a person under insurance against loss of profits or under insurance against the loss of working capacity shall be taken into account in determining his profits or income; for this purpose: **"insurance against loss of working capacity"** – insurance against injury to the working capacity, against a loss of earnings or against a loss of profits due to disease, invalidity or accident, all irrespective of whether the money under the insurance was paid all at once or in periodic payments, whether it was paid by a benefit fund or by somebody else.
- (b) (1) If a debt or part of a debt was waived for a person in a certain tax year, and if that debt arose out of an expenditure deductible in

determining his chargeable income, then the debt shall be deemed part of his income in that year.

- (2) If a person received a loan and, had he been paid a grant instead, the grant would have been income, and if the lender gave him a grant before the loan is repaid or within one year after the day of its repayment, then the grant shall, up to the amount of the loan, be deemed part of the recipient's income in the tax year in which it was given; for this purpose, the remission of a loan shall be treated like giving a grant.
- (3)
  - (a) If a person's debt or a part of his debt was remitted or written off in a certain tax year, and if that debt stems from sums he received for the production of his income from any business or vocation, or if he was given a grant for the production of his income as aforesaid, and if that person is not liable to tax on it under section 2 or under paragraphs (1) or (2) of this subsection and if the provisions of sections 20A and 21(b) also do not apply to it, then the debt shall be deemed income in the year in which it was remitted or written off, and the grant as income in the year in which it was given, and on them that person shall be liable to tax at a rate of not more than 50%.
  - (b) On application by a person who had income said in subparagraph (a), that income shall – for purposes of section 28(b) – be deemed business income.
  - (c) Tax under subparagraph (a) shall, for purposes of section 92(a), be deemed tax on a capital gain.
- (4) The provisions of paragraphs (2) and (3) shall not apply to a waived or written off grant or loan, which was given by the State, the Keren Kayemet le-Israel, the Keren Hayessod – United Israel Appeal, the Jewish Agency for Israel, the World Zionist Organization or the Rural and Suburban Settlement Company Ltd. (RASSCO) to a cooperative society classified by the Registrar of Cooperative Societies as an agricultural society or to a member of a said society; however, if the society or the member suffered a loss as said in section 28, then the amount of that loss shall be reduced by the amount of the grant or of the loan that was waived or written off.
- (5) For purposes of this subsection, a person whose debt has been waived includes a person who treats a debt owed by him as if it had been waived or written off.
- (c)
  - (1) If a person received amounts from the redemption of redeemable shares issued by a company free of charge, or if a person received from the redemption of redeemable shares amounts in excess of the amount he paid for them to the company (in this section: the amount of income) – except for the redemption of shares in a cooperative society upon the resignation or death of a member or upon the winding up of the society and except for the amounts from the redemption of shares that were allocated to an employee or to a service provider within their meaning in section 3(i) – then he shall be liable to tax at the rate of 35% on the part of the amount up to the determining date, even if he is exempt of tax or if the tax rate to which he is liable is less than 35%, and on the balance of the amount of income – at the rate of 20%, but if the individual is a substantive shareholder, as defined in section 88 –

at the rate of 25%, even if he is exempt of tax or if the tax rate to which he is liable is less than the said rate; for the purposes of this section –

**"the part of the amount of income up to the determining date"**

– the part of the amount of income, the ratio of which to the total amount of income is as is the ratio of the period from the date of issue of the share until the determining date, to the period from the date of issue of the share until the day of its redemption;

**"balance of the amount of income"** – the amount obtained by subtracting the part of the amount of income until the determining date from the amount of income;

**"determining date"** – as defined in section 88;

- (2) the paying company shall deduct the tax when it pays the amounts said in paragraph (1) and pay it to the Assessing Officer within one week after the day of payment, accompanied by a report;
  - (3) the amounts said in paragraph (1), which were paid by the company, shall not be deductible under sections 17, 127 and 128;
  - (4) liability under paragraph (1) or (2) shall not apply to amounts a foreign resident received in addition to the amounts paid by him to the company for shares, in consequence of a change in the official exchange rate.
- (d) (1) Amounts paid to an employer by a benefit fund, within its meaning in section 47, including interest, linkage differentials and other profits that stem from the employer's payments to the fund, shall be taken into account in the determination of his income; for this purpose: **"amounts paid to an employer"** include amounts which the employer treated as if they had been received from the benefit fund and were redeposited in it, and he claimed their deduction under section 17(5);
- (2) the Minister of Finance may, with approval by the Knesset Finance Committee, make rules on exemption from tax of amounts transferred from one benefit fund to another, or of amounts the designation of which was changed within the same benefit fund.
- (e) Amounts paid by an employer for his employee to training funds within limits prescribed in a collective agreement, within its meaning in the Collective Agreements Law 5717-1957 (hereafter: collective agreement), and in respect of an employee to whom no collective agreement applies – within limits set in a collective agreement applicable to employees whose profession, seniority and working conditions are similar, but no more than 8.4% of the determining salary in respect of a teaching employee, and no more than 7.5% of the determining salary in respect of any other employee, shall be deemed the employee's work income when he receives them, but amounts paid by an employer above the aforesaid limits shall be deemed the employee's work income when they are paid to the fund; for this purpose:
- "determining salary"** – work income, exclusive of payments to the employee to cover his expenses, overtime pay and payments for special efforts or for a certain event – but not more than double the amount that is the ceiling for the payment of the cost-of-living bonus, as determined from time to time by agreement between the Coordinating Office of the Economic Organizations and the General Federation of Labor in Israel; *(in tax years 1999 to 2004 the said double amount was NS 15,400; from March 2004: NS 15,712 – Tr.)*
- "teaching employee"** – a member of one of the following training funds:



- (a) Keren Hishtalmut Lemorim Vegananot Ltd.;
- (b) Keren Hishtalmut Lemorim Alyessodiim, Morei Seminarim Umefakchim Ltd.
- (c) Keren Hishtalmut Lemorim Alyessodiim Ltd.
- (e1) Repealed\*\*
- (e2) Amounts received by an individual from a training fund for the selfemployed, as defined in section 17(5a), including interest, linkage differentials and other profits, and exclusive of amounts which he deposited and which were not deductible under section 17(5a), shall be deemed that individual's income or profit from business or occupation when he received them; however, the amounts of interest, linkage differentials and other profits received from the training fund on the dates designated in section 9(16b) shall be deemed income from interest, as said in section 2(4).
- (e3) (1) Amounts which all employers of an employee paid for him to savings benefit funds and to pension benefit funds on account of the employer's benefit component and which exceed the rate for deposit, multiplied by the employee's salary or by the ceiling amount, whichever is less, shall be deemed work income of the employee when they were paid to the benefit funds; amounts paid as aforesaid to benefit funds, which do not exceed the rate for deposit, multiplied as aforesaid, shall be deemed the employee's work income when he receives them;
- (2) in this subsection –
  - "average wage in the economy"** – the average wage calculated for the purpose of benefits and insurance contributions under section 2(b) of the National Insurance Law [Consolidated Version] 5755-1995, as the National Insurance Institute publishes them;
  - "the rate for deposit"** – the rate set under section 22 of the Control of Benefit Funds Law for deposit on account of the employer's benefit component, or the percentage of the employee's salary which the employer deposited in a benefit fund on account of the employer's benefit component, whichever is less;
  - "employer's benefit component"** – within its meaning in section 21 of the Control of Benefit Funds Law;
  - "salary"** – within its meaning under section 22 of the Control of Benefit Funds Law, in respect of which the employer paid to a benefit fund;
  - "ceiling amount"** – one of the following, as the case may be:
    - (1) if amounts for the employee were paid only to pension benefit funds – an amount equal to four times the average wage in the economy per month;
    - (2) if amounts for the employee were paid only to savings benefit funds – one twelfth of the ceiling of entitling income;
    - (3) if amounts for the employee were paid to pension benefit funds and also to savings benefit funds –
      - (a) in respect of the amounts paid to pension benefit funds – the amount said in paragraph (1);
      - (b) in respect of the amounts paid to savings benefit funds – the amount said in paragraph (1), less the salary in respect of which the amounts were paid to pension benefit funds, on condition that it does not exceed the amount said in paragraph (2);

**"ceiling of entitling income"** – the amount stated in paragraph (1) of the definition of "entitling income" in section 47, as the case may be.

- (e4) (1) Profits an individual received from a benefit fund, which he was entitled to receive under the provisions of section 23 of the Control of Benefit Funds Law, and also interest and other profits which he received from a training fund at the times designated in section 9(16a) or (16b), as the case may be, shall be deemed interest income; however, profits he received as aforesaid as an amount of linkage differentials calculated on payments paid to the benefit fund or to the training fund shall be deemed income from linkage differentials.
- (2) repealed
- (e5) Profits received by an individual from the savings program in a life insurance policy shall be deemed income from interest; but aforesaid profits received as an amount of linkage differentials calculated on the payments paid to the savings program shall be deemed income from linkage differentials.
- (e6) Income from partial linkage differentials shall be deemed interest income; in this subsection, **"partial linkage differentials"** – as defined in section 9(13)(1), but for this purpose the index shall be the Consumer Price Index, a foreign currency exchange rate, including exchange rate differentials, or any other index ;
- (f) If the occupation of a person ceased in a particular tax year and his income is determined by assessment on a cash basis, then all the amounts which, due to the determination of income on a cash basis, were not charged with tax in the hands of that person before the cessation, shall be deemed income of the person entitled to them at the time of their receipt; for this purpose: "cessation of occupation" includes a change of occupation or death; however, aforesaid amounts which are included in the estate of that person shall, for purposes of estate duty under the Estate Duty Law 5709-1949, be reduced by the amount of tax due on them under section 125A.
- (g) If, during the tax year, a body of persons was a public institution, within its meaning in section 9(2), or if it did not operate for profit or all its income was exempt of tax, or if in its respect legislation determined that – for the purpose of tax payment – it be treated like the State, then it shall be liable to tax at the rate of 90% on the amounts specified below, without any right to exemption, deduction or set off whatsoever:
  - (1) amounts expended for purposes specified in regulations under section 31, which under those regulations are not deductible, or which exceed the deductible amounts;
  - (2) amounts it expended, which are not deductible under section 32(11);
  - (3) amounts it paid to a severance pay benefit fund in excess of the amounts that would have been deductible, had it not been exempt of tax.
- (h) If a person received amounts as interest on debentures, and in the case of debentures that do not relate to a preferred loan, if he received interest – including linkage differentials – in respect of a period when the debenture was owned by another (hereafter: accrued interest), then the following provisions shall apply:
  - (1) if for its recipient the accrued interest does not constitute income under section 2(1), then the accrued interest shall be deemed

income in respect of which there is no right to any exemption – other than the exemption granted on the interest itself – credit, deduction or set off; this provision shall not apply to that part of accrued interest received by a certain benefit fund that accrued in other benefit funds, as long as continuity is maintained by sale from one benefit fund to another; for this purpose: "benefit fund" – a benefit fund exempt of tax under section 9(2);

(2) if the accrued interest constitutes income for its recipient under section 2(1), and in respect of a linked debenture – if the following two conditions hold:

(a) the interest accrued in respect of a period of more than one year;

(b) the debenture was acquired within a year and a half before its redemption or before the date of the interest payment;

and in respect of an unlinked debenture – if the following two conditions hold:

(a) the interest accrued in respect of a period of more than three months;

(b) the debenture was acquired within three years before its redemption or before the date of the interest payment,

then, for purposes of calculating the profit or loss of the recipient of the interest from the sale or redemption of the debenture, no account shall be taken of that part of the amount he expended on the debenture's acquisition which equals the accrued interest, less the tax due thereon.

The provisions of this subsection on interest shall apply, mutatis mutandis as the case may be, also to discounts as defined in section 9(13b), which are not tax exempt under the said section.

(h1) The Minister of Finance may, with approval by the Knesset Finance Committee, determine that the provisions of subsection (h) shall not apply to certain categories of investments or to certain categories of assesseees, all on conditions and with adjustments that he shall prescribe.

(i) (1) If a person realized a right received in the past to acquire an asset or service, and if at the time of the realization there was a difference between the price normally payable for that asset or service and the price that person paid, or if a person received a loan, whether given directly or indirectly to him or to another for his benefit, and if that loan was free of interest or bore a lower rate of interest than the Minister of Finance set for this purpose with approval by the Knesset Finance Committee – either in general or for particular categories of loans or for loans for specific purposes – then the difference shall be deemed –

(a) if the right or loan was given in connection with an employee / employer relationship – work income;

(b) if the right or loan was received from someone to whom its recipient provides services – income within the meaning of section 2(1), unless he proves that it was not given in connection with the services he provides;

(c) if a right or loan to which subparagraphs (a) or (b) do not apply was received by a controlling member or by his relative from a company under his control – income under section 2(4);

for this purpose:

**"relative"** – as defined in section 76(d)(1);

**"controlling member"** – a person who holds or is entitled to acquire, directly or indirectly, alone or together with his relative, one of these:

- (1) at least 5% of the issued share capital;
- (2) at least 5% of the voting power in the company;
- (3) the right to receive at least 5% of the company's profits or of its assets upon winding up;
- (4) the right to appoint a director.

For purposes of this subsection – **"loan"** includes any debt; **"interest"** includes linkage differentials.

- (2) The tax on the differential in realizing an aforesaid right shall, on the assessee's application, be calculated as if that differential were income received in a number of equal annual installments, as is the number of years from the day when the right was conferred until it was realized, but not more than six years that end with the year of the realization.
  - (3) The Minister of Finance may prescribe the way of calculating the differential said in paragraphs (1) and (2), and the way of calculating every datum necessary for that purpose.
  - (4) repealed
- (j) (1) If a person extended a loan which is entered in account books kept in respect of income for which books must be kept by the double entry method, or if a body of persons gave a loan and that loan carries no interest or interest at a rate lower than the rate set for this purpose by the Minister of Finance with approval by the Knesset Finance Committee, then the interest differential shall be deemed interest under section 2(4) for whoever gave the loan; for purposes of this subsection –
- "interest"** includes linkage differentials;
- "loan"** includes any debt that is not one of the following:
- (1) a debt of customers or of suppliers in respect of goods or services;
  - (2) a tax debt;
  - (3) a loan to a certain person or to a certain category of persons or for a certain purpose, extended directly or indirectly against made by the State or by the Jewish Agency for Israel and in accordance with the depositor's instructions.
  - (4) a loan to which subsection (i) applies;
  - (5) a fixed term deposit or the balance of a current account with a banking corporation that is a bank or a foreign bank licensed under the Banking (Licensing) Law 5741-1981;
  - (6) a deposit deposited with the State, a local authority, a Government company or a Government subsidiary and a loan extended to them;
  - (7) a loan extended by a financial institution in the ordinary course of business, except for a loan extended to a company under its control or to a sister company; for this purpose –
- "financial institution"** –
- (a) within its meaning in the Value Added Tax Law;
  - (b) an institution for which interest income is income under section 2(1) and said income is its main income;

**"sister company"** – a company that is controlled by some third company, which also controls the financial institution that extends the loan;

- (8) a loan extended by a public institution, as defined in section 9(2) of the Ordinance, for a public purpose;
- (9) a loan that is an international transaction, within its meaning in section 85A;
- (10) a loan that is not linked to any index and does not bear any interest or any yield, extended by a body of persons under its control against a capital note that was issued for a period of at least five years, provided the loan cannot be repaid before the end of the said period, is of lower rank than other obligations and precedes only the distribution of surplus property at liquidation;
- (11) capital notes and debentures issued by another body of persons, on conditions prescribed in paragraph (5) of the definition of "fixed assets" in Schedule Two of the Inflationary Adjustments Law, which on December 31, 2007, were a fixed asset for whoever extended the loan;

**"control"** – at least 25% of the voting power or of the right to profits, whether direct or indirect, on at least one day during the tax year.

- (2) The Minister of Finance may prescribe the manner in which the interest differential is to be calculated, as well as the manner of calculating every datum necessary for that purpose.

#### **Income from an area**

3A. (a) For purposes of this section –

**"Israel citizen"** – each of the following:

- (1) an Israel citizen, within its meaning in the Citizenship Law 5712-1952;
- (2) an Israel resident;
- (3) a person entitled to enter Israel under the Law of Return 5710-1950, who is a resident of an area;
- (4) a body of persons, in which an Israel citizen, within its meaning in paragraphs (1) to (3), is a controlling member; for this matter – "controlling member" – as defined in section 32(9);

**"area"** – each of these: Judea and Samaria and the Gaza District, including the areas included within the territorial jurisdiction of the Palestinian Authority in accordance with the Agreement about the Gaza District and the Jericho Area between Israel and the Palestine Liberation Organization, which was signed in Cairo on May 4, 1994;

**"resident of an area"** – like the definition of "Israel resident" or "resident" in section 1, except that, instead of "in Israel", everywhere there read "in an area";

**"profits"** – within their meaning for purposes of tax in the tax law applicable in the area.

- (b) The income of an Israel citizen, which accrued or was generated in an area, shall be treated like income that accrued or was generated in Israel.
- (b1) The income of an Israel citizen resident of an area, which accrued or was generated outside Israel and outside an area, shall be treated like the income of an Israel resident that accrued or was generated outside Israel.

- (c) (1) If an Israel citizen belongs to a body of persons resident in an area, then part of that body's profits, proportional to that citizen's share in the rights to the body's profits, is deemed his income;
- (2) for the purposes of paragraph (1), if the income of a body of persons was produced in Israel or in an area, then the income of the Israel citizen shall be treated as if it had been produced in Israel; if the income of the body was produced outside Israel and outside an area, then the income of the Israel citizen shall be treated as if it were the income of an Israel resident that was produced outside Israel;
- (3) dividends received by an Israel citizen out of profits on which he paid tax under this subsection are exempt of tax.
- (d) Repealed
- (e) If an Israel citizen paid tax to area authorities on income said in subsection (b) or in subsection (b1), then he shall receive an Israel tax credit in the amount of the tax he paid in the area; in respect of income said in subsection (c), an Israel citizen shall receive credit for part of the tax paid by the body of persons on its profits, proportional to his share in the rights to the body's profits; tax paid as said in this section shall not be considered foreign taxes, as defined in section 199.
- (f) The provisions of this Ordinance shall apply – mutatis mutandis as the case may be and subject to the provisions of this section – to an Israel citizen who resides or works in an area, as if he were an Israel resident.

## **CHAPTER TWO: LOCATION**

### **Location of income from sale abroad**

- 4. If a person carries on an agricultural, manufacturing or any other productive enterprise in Israel, then the following provisions shall apply to him:
  - (1) if that person wholesaled any product of his enterprise abroad or for delivery abroad, whether the contract was concluded in Israel or abroad, then all the profit derived from that sale shall be deemed that person's income accrued or derived in Israel, except that, if it is proven to the Assessing Officer's satisfaction that the profit was increased by anything done to that product abroad – other than handling, grading, fattening, sorting, packaging or converting – then that enhancement of profit shall not be deemed income accrued or derived in Israel;
  - (2) if a person otherwise converted, used or dealt abroad with any product of his enterprise, then the profit he might have obtained if he had wholesaled the product abroad under optimal conditions shall be deemed his income accrued or derived in Israel.

### **Place where income is produced**

- 4A. (a) The place where income or profit accrued or was produced from any of the sources specified below shall be –
  - (1) in respect of business income – the place where the income yielding business activity takes place;
  - (2) in respect of income from business or from incidental business of a commercial character – the place where the transaction or the business takes place;
  - (3) in respect of income from an occupation – where the service is performed;

- (4) in respect of work income – where the work is performed;
- (5) in respect of interest, discount and linkage differentials – the payer's place of residence;
- (6) in respect of rent or fees for the use of an asset – where the asset is used;
- (7) in respect of gain or profit, including royalties, that stem from an intangible asset – the payer's place of residence;
- (8) in respect of a pension, usufruct or annuity – the payer's place of residence;
- (9) in respect of income from agriculture – the place of the asset that yields the income;
- (10) in respect of dividends – the seat of the body of persons that pays the dividend.
- (11) in respect of gains or profit from gambling, lotteries or prize winning activity, as said in section 2A – the place of residence of the person who pays the said gains or profits.
- (b) (1) Notwithstanding the provisions of paragraphs (4) and (8) of subsection (a), Israel will be deemed the place where income under the said paragraphs was produced, if the employer is one of the bodies specified in paragraph (a)(4) of the definition of "Israel resident" or "resident" in section 1, on condition that the work relationship with the said employer began when the employee was an Israel resident.
- (2) Notwithstanding the provisions of paragraphs (5), (7) and (8) of subsection (a), the following will be deemed the place where the income was produced:
  - (a) in Israel, also when the payer is a foreign resident – if the payment constitutes an expense of the foreign resident's permanent enterprise in Israel;
  - (b) abroad, also when the payer is an Israel resident – if the payment constitutes an expense of the Israel resident's permanent enterprise abroad.
- (c) The Minister of Finance may prescribe, with approval by the Knesset Finance Committee –
  - (1) in respect of income produced in more than one place and for which there is no other provision – rules to relate production of the income to different places;
  - (2) the place where income was produced in certain instances, for which no other provision has been prescribed.

#### **Special provisions on the location of income**

- 5. Notwithstanding the provisions of any statute on the location of income, the following shall be deemed income produced in Israel:
  - (1) repealed
  - (2) repealed
  - (3) repealed
  - (4) (a) repealed
  - (b) the Minister of Finance may, with approval by the Knesset Finance Committee and on conditions to be prescribed by him, exempt of the tax, in whole or in part, rent paid for chartering an aircraft or vessel that operates on international routes, as well as interest and linkage differentials on loans for the acquisition thereof; this exemption may be general or for particular categories of charters or loans;

- (5) (a) income produced by a foreign occupational company, which stems from activity in a special occupation – in the amount of the income of the Israel resident shareholders;
- (b) in respect of income under this paragraph and dividends distributed out of it to shareholders said in subparagraph (a), the foreign occupational company shall be treated as if its business were controlled and managed in Israel;
- (c) the income, chargeable income and profits of a foreign occupational company said in subparagraph (a) shall be calculated according to the applicable tax laws; for this purpose:
  - "applicable tax laws"** – one of the following, as the case may be:
    - (1) in respect of a foreign occupational company resident in a reciprocating state within its meaning in section 196 (in this section: reciprocating state), which files a return of its income or is assessed in the said state – the tax laws in that state;
    - (2) in respect of a foreign occupational company to which the provisions of subparagraph (1) do not apply – bookkeeping principles accepted in Israel, other than bookkeeping principles on equity gains or equity losses, and on changes in the value of securities;
- (d) notwithstanding the provisions of Part Ten, Chapter Three, Article Two on credit for foreign taxes, the taxes paid by a foreign occupational company to tax authorities of a country abroad on its income said in subparagraph (a) in respect of income which under section 4A was produced abroad shall be treated like foreign taxes, as defined in section 199, and the said income shall be treated like foreign income, as defined in the same section;
- (e) for the purposes of this paragraph –
  - "foreign occupational company"** – a foreign resident body of persons, for which all the following hold true:
    - (1) if it is a company, then it is a small company, within its meaning in section 76(a);
    - (2) 75% or more of one or more of the means of control in it are directly or indirectly held by individual Israel residents or by Israel citizen residents of an area, as defined in section 3A; for this purpose, the proportion of indirectly held means of control shall be calculated in accordance with the provisions of section 75B(a)(1)(d)(2); and for this purpose the direct or indirect rights of individuals who became Israel residents for the first time or of veteran returning residents, as said in section 14(a), shall not be taken into account before ten years have passed since they became Israel residents as aforesaid;
    - (3) the controlling members or their relatives, who jointly or severally, directly or indirectly hold 50% or more of one or more of the means of control, work for the company in a special occupation, either directly or through a company in which they directly or indirectly hold means of control to the extent of at least 50%;
    - (4) most of the income or of the profits of the company during the tax year, other than equity profits and losses and changes in the value of securities, stem from the special



occupation;  
**"special occupation"** – an occupation or profession designated by the Minister of Finance with approval by the Knesset Finance Committee;  
**"income of the Israel resident shareholders"** – the chargeable income of a foreign occupational company derived from activity in a special occupation, multiplied by the proportion of the direct or indirect entitlement of shareholders who are Israel residents or Israel citizen residents of an area, as defined in section 3A, to the company's profits; and for this purpose the share in the direct or indirect rights of individuals who became Israel residents for the first time or of veteran returning residents, as said in section 14(a), shall not be taken into account before ten years have passed since they became Israel residents as aforesaid;  
**"means of control", "controlling member" and "relative"** – as defined in section 75B.

### CHAPTER THREE: ASSESSMENT PERIOD

#### Tax Year

6. Tax for each tax year shall be charged on a person's chargeable income in that year.

#### Special assessment period

7. (a) Notwithstanding the provision of section 6, the Director may – on application by the assessee specified below – prescribe that the tax for each tax year be imposed on their income during a period of twelve consecutive months that begins on a date other than January 1 (hereafter: special assessment period):
  - (1) a joint investment trust, within its meaning in the Joint Investment Trusts Law 5721-1961;
  - (2) a Government company, within its meaning in the Government Companies Law 5735-1975;
  - (3) a company, the shares of which are listed for trading on a Stock Exchange recognized for purposes of the Joint Investment Trusts Law 5721-1961;
  - (4) a company, at least 51% of whose share capital and voting power are held by a foreign resident company, the shares of which are traded on a Stock Exchange abroad, or by a company in which the rights to at least 51% of the profits are held by an aforesaid foreign resident company.
- (b) In addition to the provisions of subsection (a), the Director may set a special assessment period also for an assessee who has a special relationship, direct or indirect, with a company for which a special assessment period was set under subsection (a)(2) to (4), but he shall do so only if the assessee agreed.
- (c) When the Director has set a special assessment period for an assessee under subsections (a) or (b), then tax shall be imposed for each said period subject to all the adjustments that the Director deems just and reasonable.
- (d) The Director may make the setting of a special assessment period under

- this section conditional, and he may refrain from setting a special assessment period for a company said in subsection (a)(2) to (4), if no special assessment period was set under subsection (b) for the assessee with whom it has, directly or indirectly, a special relationship.
- (e) When the Director has set a special assessment period, he may cancel his decision, whether or not on the assessee's application, if he finds reasonable cause for doing so, and – for purposes of that cancellation – he may prescribe any adjustment he deems just and reasonable; such a cancellation, made not on the assessee's application, shall go into effect at the end of the special assessment period during which it was made.

**Apportionment of income over more than one year**

8. (a) The Director may permit keymoney or a premium under section 2(6), which is a participation in the cost of construction, or a similar payment to be apportioned as income over the entire period of the rental contract or over any other period which the Director may designate.
- (b) The Director may permit income from the sale of a patent or design by the inventor, or from the sale of a copyright by the author, to be apportioned as income over a period to be prescribed by the Director; this provision shall not apply to income under section 2(9).
- (c) On application by an assessee or his heirs, the following types of income shall be deemed, for purposes of tax computation, to have been received as said here:
- (1) wage differentials – in the years to which they refer, but not during more than six tax years up to the year in which they were received;
  - (2) pay in lieu of vacation received by an employee – in equal annual installments over a period of not more than six tax years that ends in the year in which they were received, but not more than the number of years of his employment;
  - (3) income from personal exertion, as said in paragraphs (5) or (6) of the definition of that term in section 1 – in equal annual installments in the work years for which the grant is paid or in the period in which the right to the pension was created, as the case may be, but over no more than six tax years up to the tax year in which the grant was received or the pension capitalized; however, the Director may, if requested, permit such apportionment over a different period, including years to come, under conditions which he may determine, including the payment of an advance.
- (d) If the Director permitted income to be apportioned under this section or under section 9A(d) and the assessee dies, or the assessed company begins to be wound up before the end of the period set by the Director, then any income which under the apportionment belongs to years subsequent to that tax year shall be added to the assessee's income in the tax year in which he died, or to the income of the company in the tax year in which it began to be wound up; however, on application by the assessee's heirs, the administrator of his estate or the executor of his will, the whole income shall be reapportioned over a period of years ending with the tax year in which the assessee died, or, on application by the assessee's heirs, all the income which under the apportionment relates to years subsequent to that tax year, shall be deemed the heirs' income in those years, in proportion to their respective shares in the assessee's estate, and that after they have provided collateral to the Director's satisfaction for payment of the tax which will be due from them under this calculation; but if the assessee paid the advance under

subsection (c)(3) or section 9A(d), or if tax was withheld at the source under section 164 – then the said advance paid or the said tax withheld at the source in respect of years after the death shall be deemed the amount of tax due.

**Division of income from work, the performance of which takes longer than one year**

8A. (a) In this section –

**"extended work"** – work, the performance of which takes longer than one year, including construction work on a building by a person who performs the work at the order of another, and exclusive of the construction of a building by its owner;

**"income from extended work"** – income from extended work which is income under section 2(1), either from performance or from sale.

(b) If an assessee engages in extended work, he shall report his income from it in the following manner:

(1) in the tax year in which he completed at least 25% of the monetary volume of the work, as calculated for that year, or of the quantitative volume of the work, whichever he chooses, he shall report on the estimated income earned by him from the part of the work he has performed, and in every tax year thereafter he shall report on the estimated income earned by him in accordance with the part of the work he performed in that year, calculated on the basis which he chose when he first calculated the volume of work completed; in the tax year in which he completed the work he shall report on the business results in their entirety, deducting income which he reported in previous years;

(2) a loss from extended work shall be taken into account for purposes of determining chargeable income during the tax years before the tax year in which the work was completed, only after the assessee completed at least 50% of the monetary volume of the work, as calculated for the year in which he claimed the set-off of the loss, or at least 50% of the quantitative volume of the work;

(3) if subparagraphs (1) or (2) apply to an assessee, then he shall append to his return under section 131 a return, certified by an auditor, as defined in the Auditors' Law 5715-1955, specifying the manner of determining the income or the loss, as the case may be, and the manner in which the volume of accomplished work was calculated.

(c) (1) In this subsection –

**"building"** – a building built by its owner, the construction of which takes longer than one year;

**"building fit for use"** – a building or part thereof, which has been connected to the electricity grid, or a building in respect of which the conditions for the receipt of a building completion certificate under the Planning and Building Law 5725-1965 (hereafter: Planning Law) have been met;

**"income from a building"** – income from the sale of the building, which is income under section 2(1).

(2) The following provisions shall apply to an assessee who has income from a building:

(a) In the first tax year in which the building was fit for use the assessee shall report all the income he had from the building until that tax year and in that tax year, and in every

- tax year thereafter he shall report all the income he had from the building in that tax year;
- (b) for the purpose of determining the assessee's chargeable income from the sale of part of a building that is fit for use, the proportional part of the total cost of the building shall be taken into account, as is the proportion of the area sold in that tax year to the area of the entire building, as specified in the building license issued under the Planning Law, but for this purpose sold parking spaces shall not be included in the sold area;
  - (c) the loss from a building shall not be taken into account for the determination of chargeable income in the tax years that preceded the tax year in which the building became fit for use.

#### **Income under Section 2(6) or (7)**

- 8B. Income under section 2(6) or (7) shall be included in the assessee's chargeable income in the year in which he actually received it, even if it constitutes deferred income, and expenses incurred in subsequent tax years in the production of the income under the said provisions shall be deductible from any source in the year in which they were incurred, but if they cannot be deducted in the year in which they were incurred, provided that – if the expenses cannot be deducted in the tax year in which they were incurred - they may be deducted in the year in which the income was received, and the assessment for the said year shall be deemed to have been amended accordingly; however, in consideration thereof there shall be no obligation to pay interest and linkage differentials under section 159A.

#### **Date on which income from exchange rate differentials is charged**

- 8C. A person's income from exchange rate differentials shall be deemed income in the year in which it accrued, even when returns are filed on a cash basis.

## **PART THREE: CALCULATION OF INCOME FOR TAX PURPOSES**

### **CHAPTER ONE: EXEMPTIONS**

#### **Article One: Statutory Exemptions**

##### **Exempt income**

9. The following are exempt of tax:

##### **The President**

- (1) Payments, services and benefits paid or given by the State Treasury to the President or to a former President or to his survivors, in respect of his performance of the functions of President, except for salary and pension;

##### **Local authority, benefit fund and public institution**

- (2) (a) the income of a local authority, of Mif'al Hapayis and of a public

institution, to the extent that it was not derived from a business carried on by it or from dividend, interest or linkage differentials paid by a body of persons under its control that engages in business, as well as the income of a benefit fund, if it was not obtained from any business in which the benefit fund engages or from any income paid by a body of persons that engages in a business and which is under the control of the benefit fund or in which the benefit fund has a substantive holding; however, the Minister of Finance may, by Order for a period and on conditions which he shall set, exempt of tax the income obtained from the said sources by a local authority, by Mif'al Hapayis or by a public institution that is a free loan fund, if he is satisfied that doing so is in the public interest;

(b) in this paragraph –

**"benefit fund"** – other than an insurance fund;

**"income"**, in respect of a retirement age benefit fund – including appreciation from the sale of a real estate right or of a real estate association right;

**"tax"**, in respect of a retirement age benefit fund – including tax under sections 6 or 7 of the Real Estate Taxation Law;

**"retirement age benefit fund"** – a pension benefit fund, a savings benefit fund of a severance pay benefit fund;

**"public institution"** – a body of at least seven persons most of whom are not related to each other, or an endowment, most of the trustees of which are not related to each other, which exists and functions for a public purpose, its property and income being only used for the public purpose, and which submits annual reports on its assets, income and expenses to the Assessing Officer's satisfaction according to regulations made for this purpose by the Minister of Finance; for this purpose –

**"relative"** – within its meaning in section 76(d);

**"public purpose"** – a purpose concerned with religion, culture, education, science, health, social welfare or sport and any other purpose approved by the Minister of Finance as a public purpose;

**"means of control"** in a body of persons – any of the following:

- (1) the right to appoint a Director;
- (2) the right to vote;
- (3) the right to profits;
- (4) the right to the balance of the body's assets upon liquidation, after its debts have been paid;

**"control"** – the ability to direct the activity of a body of persons, alone or together with others, directly or indirectly; without derogating from the generality of the aforesaid, the ability to prevent the adoption of business decisions by a body of persons shall be deemed control thereof, except for the ability to prevent adoption of substantive business decisions by the body of persons; for this purpose: **"substantive business decisions"** – decisions about the issue of means of control in the body of persons, or the sale, liquidation or substantive change of most of the business of that body of persons; without derogating from the generality of the aforesaid, it will be deemed that such ability exists in a local authority, in Mif'al Hapayis, in a benefit fund or in a public institution when one of the following holds true:

- (1) the local authority, Mif'al Hapayis or the public institution has

the power to appoint – directly or indirectly – a Director of that body or has a right – direct or indirect – to at least 25% of the voting power in it or to the balance of its assets upon its liquidation after its debts have been paid, or to most of its profits;

(2) repealed

(3) several bodies from among the following – a local authority, Mifal Hapayis, a public institution or a benefit fund – hold or have the right to hold, jointly or severally, directly or indirectly, more than 50% of the means of control in a body of persons;

**"substantive holding" –**

(1) in a single benefit fund – holding or having the right to hold, directly or indirectly, more than 10% of one or more of the means of control in a body of persons;

(2) in several benefit funds, which are directly or indirectly managed or held by one person – holding or having the right to hold, directly or indirectly, jointly or severally, more than 20% of one or more of the means of control in the body of persons; and if they are managed or held as aforesaid by a bank – more than 10%; for this purpose several benefit funds shall be deemed to be managed by one person also if their investments are directly or indirectly managed by him, and several benefit funds shall be deemed to be held by one person, if he is able to direct the activity of the benefit funds; without derogating from the provisions of this paragraph, a said ability is deemed to exist also if that person directly or indirectly has at least 50% of one or more of the means of control of each of the benefit funds;

**"bank"** – within its meaning in the Banking (Licensing) Law 5741-1981, and several banks shall be deemed to be one bank if one has the ability to direct the activity of the other directly or indirectly, or if one person has the ability to direct their activity as aforesaid, all if they do not have separate systems for the management of benefit funds, as prescribed under section 26 of the Control of Benefit Funds Law

(c) (1) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions on the calculation of the amount of indirect control and of indirect substantive holdings of benefit funds in a body of persons.

(2) The Minister of Finance may prescribe that holding one or more means of control in a body of persons by several aforesaid bodies, in amounts that bring them to control that body of persons or to have a substantive holding in it shall not constitute control or substantive holding, as the case may be, if it was for a period which in the aggregate did not exceed three months during the tax year or a shorter period prescribed by the Minister, at the end of which the amount of the holding dropped to an amount that does not constitute control or a substantive holding, as the case may be, all in accordance with the rules made by him.

### **Professional Organization**

(2a) (a) The income of a professional organization, including income from

membership dues, on condition that it was not obtained from any business in which it engages or from any income of a body of persons under its control, which engages in business, including dividend, interest or linkage differentials;

- (b)
  - (1) notwithstanding the provisions of subsection (a), the balance of income of a professional organization that exceeds 50% of its expenses shall not be exempt of tax;
  - (2) an amount of expenditure in excess of the amount of income in a certain tax year shall be treated like an amount of expenditure incurred in the following tax year, it having been adjusted at the rate of index increase during the said following tax year;
  - (3) for this purpose:
    - "balance of income"** – income exempt under subparagraph (a), after the expenses incurred in generating that income were deducted from it;
    - "expenses"** – deductible expenses other than depreciation, and expenses for acquisition of a depreciable asset used for the organization's purposes or to create a said asset;
    - "depreciable asset"** – as defined in section 88, including a real estate right, within its meaning in the Land Appreciation Tax Law;
- (c) in this paragraph, **"professional organization"** – a body of persons approved by the Director, for which all the following hold true:
  - (1) it has at least 70 members, or its members include the State and at least ten members; if the number of members in the body of persons includes a professional organization, then the number of that professional organization's members shall be taken into account;
  - (2) its entire purpose is the advancement of joint professional interests, professional training or the public representation of members of a certain occupation or of persons engaged in a certain branch or sector of the economy, all its assets and income serving the advancement of those purposes;
  - (3) its activity is not aimed at the enhancement of the income of certain of its members;
  - (4) it submits an annual report on its assets, income and expenditure to the Assessing Officer's satisfaction, according to regulations made by the Minister of Finance;

#### **Cooperative society**

- (3) the income of a cooperative society, which does business only with its members, or whose business with non-members is inconsiderable in extent or of an incidental nature, if it was proven to the Assessing Officer's satisfaction that the society's business is the supply of goods, equipment and services for domestic or private use only, and not for the purposes of the business or vocation of that member or person;

#### **Diplomats and consuls**

- (4) sums payable to diplomatic representatives and consular officers in the regular service of a foreign state for their offices or for services rendered by them in their official capacities, to the extent that that foreign state reciprocates with such exemptions for the State of Israel;

### **Blindness and 100% disability**

- (5) (a) the income from the personal exertion of a blind person or of an invalid, whose invalidity has been established at 100%, or at no less than 90% due to invalidity in different parts of the body, the said percentage being the result of a special computation of disability in different parts of the body, without which invalidity would have been established at no less than 100%; as specified below:
- (1) if the said invalidity was determined for a period of 365 days or longer – income up to the amount of NS 522,000 (*in 2008; in 2007: NS 507,600; in 2006: NS 510,000; in 2005: NS 496,800 – Tr.*);
  - (2) if the said invalidity was determined for a period of between 185 and 364 days – income up to the amount of NS 62,640 (*in 2008; in 2007: NS 60,960; in 2006: NS 61,080; in 2005: NS 59,520 – Tr.*);
- for this purpose:
- (a) if the invalid's degree of invalidity was determined under one of the following Laws, then the said determination shall apply:
    - (1) the Invalids (Benefits and Rehabilitation) Law [Consolidated Version] 5719-1959;
    - (2) the Invalids of the War Against the Nazis Law 5714-1954;
    - (3) the Invalids from Nazi Persecutions Law 5717-1957;
    - (4) the Benefits for Victims of Hostile Actions Law 5730-1970;
    - (5) repealed
    - (6) Part Three, Chapter Six "B" and Chapter Nine "B" of the National Insurance Law [Consolidated Version] 5728-1968;
    - (7) the Compensation for Ringworm Sufferers Law 5754-1994;the Minister of Finance may, with approval by the Knesset Finance Committee, add to the said Laws;
  - (b) if the invalid's percentage of invalidity was not determined as aforesaid, then it shall be determined under regulations, which the Minister of Finance shall make with approval by the Knesset Finance Committee;
- (b) if the income from personal exertion of an aforesaid invalid or blind person was lower than NS 62,640 (*in 2008; in 2007: NS 60,960; in 2006: NS 61,080; in 2005: NS 59,520 – Tr.*) (or if he had no said income, then his income other than from personal exertion shall also be exempt of tax, up to a total sum of NS 62,640; however, if he had income from interest paid on money deposited in a deposit, a savings program or a benefit fund, which stemmed from compensation or insurance payments received by the individual because of bodily injury – up to a total amount of NS 223,200 (*in 2008; in 2007: 217,080; in 2006: 217,680; in 2005: NS 118,680 – Tr.*) or a greater amount prescribed by the Minister of Finance with approval by the Knesset Finance Committee.



- (c) (1) in respect of a blind person or an invalid, for whom invalidity was determined as said in subparagraph (a)(1) in respect of part of the tax year, the provisions of this subparagraph shall apply to part of his income in the tax year, the proportion of which to all his income in the tax year is as is the proportion of the number of days in the tax year, for which his invalidity was determined, to 365 (in this subparagraph: the invalidity period ratio), and the amounts stated in subparagraphs (a)(1) and (b) shall be read as amounts, the ratio of which to the stated amounts is as is the invalidity period ratio;
- (2) in respect of a blind person or an invalid, for whom invalidity was determined as said in subparagraph (a)(2), the provisions of this subparagraph shall apply to part of his income during the tax year, the proportion of which to all his income in the tax year is as is the invalidity period ratio, but if the invalidity period determined for him is in two tax years, the total amount of exemption in the two tax years shall not exceed the amount stated in subparagraph (a)(2).

#### **Pensions for war invalids**

- (6) pensions payable in respect of war injuries, border injuries or enemy inflicted injuries, and pensions paid by the State Treasury to dependents of soldiers who died in consequence of belligerent acts; for this purpose: **"war injuries"** – illness, aggravation of illness or injury which occurred to an individual during the period of his service in consequence of military service, within its meaning in the Invalids (Pensions and Rehabilitation) Law [Consolidated Version] 5719-1959, or in consequence of war service within its meaning in the Invalids (War Against the Nazis) Law 5714-1954, or under circumstances that entitle him to a benefit under the Invalids (Nazi Persecution) Law 5717-1957; **"enemy inflicted injury"** – within its meaning in the Victims of Hostile Action (Pensions) Law 5730-1970;

#### **Vehicle maintenance for leg invalids**

- (6a) amounts that a person with leg invalidity lawfully receives for the maintenance of his vehicle;

#### **Pensions for Palestine Government employees**

- (6b) pensions paid by the State, in respect of employment by the Palestine Government;

#### **National Insurance invalidity and old age pensions**

- (6c) invalidity pensions paid under Article Five of Chapter Three, Chapter Six "B" and Chapter Nine "B" of the National Insurance Law, old age and survivors' pensions paid under Chapter Two, and dependents' pensions paid under Chapter Three of the said Law;

#### **Benefits for prisoners of Zion**

- (6d) social benefits or compensation paid to Prisoners of Zion or to relatives of prisoners of Zion and Jewish martyrs, by virtue of Law;

#### **Invalidity pensions from foreign states**

- (6e) invalidity pensions paid by a foreign state by virtue of its Laws;

**Survivors' pensions**

- (6f) survivors' pensions paid under Law or collective agreement, to which paragraphs (6) and (6c) do not apply, in an amount that does not exceed the entitling pension within its meaning in section 9A, but if exemption is also due under sections 9A or 9B, then the larger of the two exemptions shall apply;

**Righteous gentiles**

- (6g) benefits paid under the Benefits for Righteous Gentiles Law 5755-1995;

**Orphan's compensation**

- (6h) benefits for an orphan, payable under the Benefits (Child Orphaned in Consequence of Violence in the Family) Law 5755-1995;

**Consolidated compensation**

- (7) any capital sum received as inclusive compensation for death or injury;

**Grant in consequence of retirement or death**

- (7a) (a) (1) a capital grant received in consequence of retirement, up to an amount equal to one month's salary for each year of employment, according to the last salary; if the amount of the grant exceeds the aforesaid amount, then the Director may exempt all or part of the excess, taking into consideration the period of service, the amount of salary, the terms of employment and the circumstances of the retirement;
- (2) in no case shall the amount exempt under this subparagraph exceed NS 10,500 (*in 2008; in 2007: NS 10,220; in 2006: NS10,250; in 2005: NS 9,980 – Tr.*) for each year of employment and a proportional part of that amount for a fraction of a year's employment;
- (3) for purposes of this subparagraph, "**retirement**" includes the change in the status of an employee of a cooperative society from hired employee to member;
- (4) (a) if, when he retires from employment by his employer, an employee has to his credit in a compensation fund an amount intended for a retirement grant, or if he received a retirement grant, and if he notified the Director at the time of his retirement that he opts for the application of the provisions of this item, then the sums he left in the compensation benefit fund or deposited in that fund immediately upon his retirement shall not be deemed to have been received by him if, within one year of his retirement, he begins work with another employer, who makes retirement compensation payments on his behalf to that same fund;
- (b) if the conditions of subitem (a) have been met and the employee subsequently retires from employment by the other employer (hereafter: the last employer) without having met the conditions of subitem (a), then the provisions of items (1) through (3) shall apply to him, subject to the following provisions:
- (1) the periods of employment with the different

- employers that involved consecutive retirements, as said in subitem (a), shall be combined, and he shall be deemed to have worked for the last employer for all the said years of employment;
- (2) the amounts to his credit with the compensation benefit fund at the time of his retirement from the last employer, derived from retirement grants said in subitem (a), including linkage, interest differentials and other profits on them (hereafter in this item: profits on the grant), shall be deemed part of the retirement grant from the last employer;
  - (b1) if the provisions of subitem (a) were met and the employee died, then the provisions of subparagraph (b) shall apply, subject to the provisions (1) and (2) of subitem (b) and mutatis mutandis as the case may be;
  - (c) if an employee received, at the time of retirement said in subitem (a), part of the retirement grant accrued to his credit, then he shall be liable to tax on the amount received;
  - (d) if an employee opted for the application of the provisions of this item, then he may retract that decision within two years, and if he does so, the profits on the grant shall be deemed part of the grant; as for the exemption – his last salary shall be the salary paid to him when he retired, increased in proportion to the increase of the consumer price index in the period between his retirement and the retraction of his decision, and the ceiling of the exemption shall be as it was when he retracted the decision, but the period of employment after retirement from his last employer shall not be taken into consideration; subject to that, any amount which he withdrew from a compensation benefit fund before his retirement from employment with his last employer, and which derived from the retirement grant said in subitem (a), and the profits thereon, shall be liable to tax;
  - (5) notwithstanding the provisions of section 164, if a person pays a retirement grant which is exempt under item (4), then he shall be exempt of the obligation to withhold tax at the source, on condition that he received approval therefor from the Director or from a person authorized by him;
  - (b) (1) a capital grant received in consequence of death, up to an amount equal to the salary of two months' employment for each year of employment, according to the last salary; if the amount of the grant exceeds the said amount, then the Director may exempt all or part of the excess, taking into consideration the period of service, the amount of salary, the terms of employment and the circumstances of the death;
  - (2) the amount exempt under this paragraph shall in no case exceed NS 21,010 (*in 2008; in 2007: 20,440; in 2006: NS 20,500; in 2005: NS 19,970 – Tr.*) for each year of employment and a proportional part of this amount for a

- fraction of a year's employment;
- (c) if the Director concludes that the salary was increased unreasonably shortly before the date of retirement in order to increase the amount of exempt grant, then he may set the amount of exempt grant without taking the increase into account;
  - (d) if the last salary was for part time employment, then, in respect of the years in which the employee was employed full time, the last salary which would have been paid for full time employment shall be taken into account;
  - (e) a decision by the Director under subparagraphs (a) to (c) may be appealed in accordance with sections 153 to 158;
  - (f) if an employer paid a grant in consequence of retirement or death, he shall add prescribed particulars about the grant to the return, which he submits under section 166 for the month in which the grant was paid;
  - (g) subject to the provisions of subparagraph (a)(4)(a), a capital grant in consequence of retirement, as well as a capital grant in consequence of death, shall be deemed to have been received, even if it remains deposited in a benefit fund; this provision shall not apply to sums in a pension benefit fund to the credit of a retired employee if, when he retired, he notified the Director that he wishes to leave them there for purposes of the payment of a pension; if he so notified, he may subsequently revoke the notification by notice to the Director; if he so revoked, the whole amount, including interest, linkage differentials and other profits on it shall, subject to paragraph (17), be deemed a retirement grant and the following provisions shall apply to it:
    - (1) if he did not receive a grant when he retired, he shall be entitled to exemption under subparagraph (a), and the ceiling of the exemption shall be as it was when he revoked his decision;
    - (2) if he received a grant when he retired, the ceiling of the exemption shall be reduced at a rate equal to the amount of grant for each year of employment, divided by the exemption ceiling, as it was when he retired;

#### **Foreign ship owner**

- (8) the profits of a ship owner who is not an Israel resident, subject to the provisions of section 70;

#### **Concessionaire**

- (9) income derived by a person from a concession granted him by the State, to the extent that it was tax exempt under the terms of the concession; however, nothing in this section shall be construed to exempt of tax any dividends, interest, linkage differentials, bonuses, salaries or wages received by any person, wholly or in part, out of income exempted as aforesaid;

#### **Interest to a foreign state**

- (10) interest payable to a foreign state, or to a person recognized by the Minister of Finance, with approval by the Knesset Finance Committee, as acting in the name or on behalf of that state;
- (11) and (12) – repealed

### **Linkage differentials on bank deposits or savings programs**

- (13) linkage differentials received by an individual in respect of an asset, on condition that all the following apply:
- (1) the linkage differentials are not partial linkage differentials; for this purpose: "**partial linkage differentials**" – as prescribed by the Minister of Finance with approval by the Knesset Finance Committee;
  - (2) the individual did not claim the deduction of interest or linkage differentials in respect of the asset;
  - (3) the linkage differentials are not income under section 2(1) and are not and do not have to be entered in his account books;
- the provisions of this paragraph shall not apply to an asset that is an account in a benefit fund;

### **Linkage in respect of expropriation**

- (13a) linkage differentials paid in respect of the expropriation of an asset that is not stock in trade, as defined in section 85;

(13b), (14) and (14a) – repealed

### **Exchange rate differentials in a company controlled by foreign residents**

- (14b) exchange rate differentials on a company's foreign currency deposit, derived from payments by foreign residents on account of the acquisition of shares in that company, in so far as the money in that deposit has not yet been used, on condition that most of the share capital of the company, a majority of the voting rights and most of the rights to profits are in the hands of foreign residents;

### **Exchange rate differentials on loans**

- (15) exchange rate differentials on a loan made by a foreign resident, except for a loan he gave from his permanent enterprise in Israel;

### **Insurance against change in exchange rate**

- (15a) amounts received by a foreign resident under a policy to insure a loan against changes in the shekel exchange rate in relation to the principal of a loan he made in a lawfully held foreign currency or in shekalim derived from the lawful conversion of foreign currency, and which under its conditions is repayable in shekalim without linkage differentials, but the exempt amount shall not exceed the amount of the differential resulting from the exchange rate change;

### **Exemption for a foreign resident who gets no double taxation relief**

- (15b) (a) in this paragraph –  
"**security**" – a share or debenture issued by a company for a period of at least twelve years and traded on an Exchange, within its meaning in section 88;  
"**foreign currency**" – including Israel currency obtained by the lawful conversion of foreign currency and Israel currency obtained by the redemption of State of Israel bonds that were floated abroad;
- (b) (1) income from dividend or interest received by a foreign resident on a security which he acquired with foreign

- currency and on which he gets no double taxation relief in his country of residence, or on which, under an agreement for the prevention of double taxation on income, he is deemed to have paid – in his country of residence – the tax which he would pay, if not for the provisions of this paragraph;
- (2) the exemption shall be granted from the day on which the security is first included in the list of securities traded on an Exchange;
  - (c) a foreign resident who with foreign currency acquired participation units in a non-restricted fund under the Joint Investment Trusts Law 5721-1961, shall be entitled to the exemption under subparagraph (b) in respect of that part of his income from his fund units, as bears to the total of that income the same proportion as the securities acquired by the fund, which would entitle a foreign resident to exemption as aforesaid if he acquired them, bear to the aggregate of securities within the meaning of the said Law on the day on which the accounts of the fund are drawn up under section 20 of the said Law;
  - (d) notwithstanding the provisions of this paragraph, the Minister of Finance may prescribe, with approval by the Knesset Finance Committee by notice published in Reshumot, either generally or in respect of a particular category of companies, that aforesaid exemption from tax on income shall not be granted, if the proportion between the company's paid up share capital and the aggregate of loans received by it is not to his satisfaction;

**Interest on debenture acquired by foreign resident**

- (15c) interest on a debenture issued by virtue of a Law that exempts its owner from interest, if he is a foreign resident and if it is paid to a person who was a foreign resident when he acquired the debenture;

**Interest, discount and linkage differentials on debentures traded on the Exchange by foreign residents**

- (15d) Interest, discount and linkage differentials paid to a foreign resident on debentures traded on the Exchange in Israel, which were issued by an Israel resident body corporate (in this paragraph: issuer body corporate), provided the income is not in the foreign resident's permanent enterprise in Israel; in this paragraph, "foreign resident" – a person who is a foreign resident on the day the interest, discount and linkage differentials, as the case may be, is received, unless he is one of the following:
  - (1) a substantive shareholder, as defined in section 88, in the issuer body corporate;
  - (2) a relative, as defined in paragraph (3) of the definition of "relative" in section 88, of the issuer body of persons;
  - (3) a person who is employed in the issuer body of persons, provides services to it, sells products to it, or has other special relations with it, unless he proved to the Assessing Officer's satisfaction that the interest or the discount, as the case may be, was set in good faith without being affected by the existence of the said relations between the foreign resident and the issuer body of persons;
- (16) repealed

### **Withdrawal of employer's payments from training fund**

- (16a) (a) amounts withdrawn by an employee from his account in a training fund, including linkage differentials as well as interest and other profits that stem from a benefited deposit – if six years have passed since the first payment to that account, and for an employee who has reached the retirement age – if three years have passed since the first payment to that account; and in respect of amounts used by the employee for his training – if three years have passed since the time of the first payment to that account; if the employee died, then the persons entitled to receive the said amounts may withdraw them from the training fund exempt of tax;
- (b) the exemption under this paragraph is conditional on the account being closed to additional payments, once the employee withdraws any amount from his account; when an account has been closed in this manner, the provisions of subparagraph (a) shall apply to the withdrawal of the balance in the account; however, if an amount no larger than one third of the amount at the account holder's disposal at the time of the withdrawal was withdrawn for training in Israel, and no other withdrawal was made within the 12 months preceding the said withdrawal, then it shall not be deemed a withdrawal for the present purpose;
- (c) for purposes of this paragraph,  
**"date of the first payment"** – the earlier of these:  
(1) the end of the month in which the first payment was paid;  
(2) the end of the month in respect of which the first payment was paid, but no earlier than the beginning of the tax year in which it was paid;  
**"benefited deposit"** – each of the following:  
(1) an amount that the employer paid, up to the amount or up to the rate which under section 3(e) was not considered work income when it was paid to the fund;  
(2) an amount paid by the employee that is one of the following:  
(a) an amount that is not more than one third of the amount paid by the employer at the rate prescribed in section 3(e) in respect of the employee's determining pay, as defined in the said section;  
(b) an amount that does not exceed 2.5% of the employee's determining pay;  
(c) a payment in a different amount, prescribed for the employee's payments in accordance with a collective agreement approved under the Collective Agreements Law 5717-1957 before June 12, 2002;  
(3) an amount paid to a training fund for kibbutz members, as defined in section 58A, up to the amount of NS 15,720 per year (*in 2008; in 2007: 15,240; in 2006: NS 15,360; in 2005: NS 14,880 – Tr.*)
- (d) the Minister of Finance may, in regulations, make rules about closing accounts to additional payments and about conditions under which an employee's different accounts in one or more training funds shall be deemed a single account for purposes of this paragraph;
- (e) repealed

### **Withdrawal from a training fund for the selfemployed**

- (16b)(a) amounts withdrawn by an individual from his account in a training fund for the selfemployed, as defined in section 17(5a), including linkage differentials as well as interest and other profits that stem from a benefited deposit – if six years have passed since the first payment to that account, and for an individual who has reached the retirement age – if three years have passed since the first payment to that account; and in respect of amounts used by the individual for his training – if three years have passed since the first payment to that account; if the individual died, then the persons entitled to receive the said amounts may withdraw them from the training fund exempt of tax; the Director may prescribe rules on the entitlement to withdraw amounts exempt of tax for training purposes; for this matter, **"benefited deposit"** – NS 15,720 per year (*in 2008; in 2007: NS 15,240; in 2006: NS 15,360; in 2005: NS 14,880 – Tr.*);
- (b) the provisions of paragraphs (16a)(b) to (d) shall apply to withdrawals of amounts under this paragraph, mutatis mutandis.

### **Employee's money from a benefit fund**

- (17) money received by an employee – other than money he received under insurance against loss of working capacity, as defined in section 3(a) – up to the amount of the employer's payments to a savings benefit fund and not chargeable with tax under section 87, but in respect of payments made in and after tax year 1964, only money up to the amount of the employer's payments is exempt within the limits of amounts based on rates prescribed under section 22 of the Control of Benefit Funds Law, as well as amounts taxed under section 3(e3);

### **Linkage differentials from a savings benefit fund**

- (18) linkage differentials not chargeable with tax under sections 3(d) or section 87, received by an individual from a savings benefit fund, which stem from payments the individual and his employer deposited in the benefit fund;

### **Interest and profits at age of entitlement**

- (18a) (a) interest and profits that stem from the ceiling of the benefited deposit, which are not liable to tax under sections 3(d) or section 87 and were received by an individual from a savings benefit fund when he reached the age of entitlement, if the savings period in the benefit fund was not less than 15 years since the date of the first payment to the benefit fund, and if the first payment date after he had reached the age of entitlement was five years after that date, or upon his death;  
in this paragraph –  
**"date of the first payment"** – as defined in paragraph (16a)(c);  
**"ceiling of benefited deposit"** – a deposit to a savings benefit fund that does not exceed the amount of NS 19,200 in the tax year (*in 2006 and 2007; in 2005: NS 19,440 – Tr.*)
- (a1) for the purposes of this paragraph, the age of entitlement of an individual shall be the age of entitlement prescribed for him according to the month of his birth, as specified below:

for men

for women



month of birth	age of entitlement	month of birth	age of entitlement
until December 1944	60 yrs	until December 1944	60 yrs
Jan. - April 1945	60 yrs 8 mos.	Jan. - April 1945	60 yrs 8 mos.
May - Dec. 1945	61 yrs	May - Dec. 1945	61 yrs
Jan. - Aug. 1946	61 yrs 4 mos.	Jan. - Aug. 1946	61 yrs 4 mos.
Sept. 1946 - April 1947	61 yrs 8 mos.	Sept. 1946 - April 1947	61 yrs 8 mos.
May - Dec. 1947	62 yrs	May 1947 - Dec. 1949	62 yrs
Jan. - Aug. 1948	62 yrs 4 mos.	Jan. - Aug. 1950	62 yrs 4 mos.
Sept. 1948 - April 1949	62 yrs 8 mos.	Sept. 1950 - April 1951	62 yrs 8 mos.
May - Dec. 1949	63 yrs	May - Dec. 1951	63 yrs
Jan. - Aug. 1950	63 yrs 4 mos.	Jan. - Aug. 1952	63 yrs 4 mos.
Sept. 1950 - April 1951	63 yrs 8 mos.	Sept. 1952 - April 1953	63 yrs 8 mos.
May - Dec. 1951	64 yrs	May 1953 and after	64 yrs
Jan. - Aug. 1952	64 yrs 4 mos.		
Sept. 1952 - April 1953	64 yrs 8 mos.		
May - Dec. 1953	65 yrs		
Jan. - Aug. 1954	65 yrs 4 mos.		
Sept. 1954 - April 1955	65 yrs 8 mos.		
May - Dec. 1955	66 yrs		
Jan. - Aug. 1956	66 yrs 4 mos.		
Sept. 1956 - April 1957	66 yrs 8 mos.		
May 1957 and after	67 yrs		

- (a2) Notwithstanding the provisions of subparagraph (a1), if – under the provisions of Chapter 4 of the Retirement Age Law 5764-2004 – the Minister changed Part Two of the Schedule of the said Law in respect of women born in January 1950 and thereafter, then the retirement age set for a woman in Part Two of that Schedule shall be her age of entitlement for the purposes of this paragraph.
- (b) The Minister of Finance may prescribe, with approval by the Knesset Finance Committee and on conditions he shall set, a savings period shorter than that specified in subparagraph (a);

### **Life insurance**

- (19) an amount received under a life insurance policy, except –
  - (1) an amount received by a person from insurance of the life of another who is not his relative, within its meaning in section 88, if the premium for his insurance was not recognized as an expense of the insurer;
  - (2) an amount not exempt under paragraph (7a) or (17) or on which tax must be paid under sections 3(d) or 87;
 in this paragraph, "**amount received under a life insurance policy**" – an amount received upon the death of the insured only on the death risk element included in the life insurance policy, exclusive of the amount received or derived from the savings component;

### **Employers rebates and gifts to their employees and the value of organized transport**

- (20) the value of an employee's travel from his home to the place of employment and back by collective transport, organized and financed by the employer, if the Director or a person empowered by him finds that the collective transport of employees to the place of employment is

necessary, because of the working conditions and the location of the work place, and that the said transport is in accordance with conditions prescribed by him;

#### **Wage delay compensation**

- (21) (a) an amount received by an employee as wage delay compensation under the Wage Protection Law 5718-1958, within the limits of linkage differentials and interest on the amount of delayed wage;
- (b) notwithstanding the provisions of subparagraph (a), if a person's chargeable income in any one of the 24 months that preceded receipt of the compensation exceeded the ceiling for that month, then the tax element in the exempt compensation shall be paid as tax;
- (c) in this paragraph –
- "tax element"** – the compensation paid for that part of the wage which would have been paid as tax, had the wage been paid on time;
- "ceiling"** – the amount of NS 6,960 (*in 2008; NS 6,720 in 2006 and 2007; in 2005: NS 6,600 – Tr.*), adjusted as if it were an income ceiling, as defined in section 120A;

#### **Alimony**

- (22) alimony received by an individual from the person to whom he was married or from the person to whom he is married but from whom he is separated, and a maintenance allowance received by an individual for his children from the other parent, or a payment received by an individual for himself or for his children from the National Insurance Institute under the Maintenance (Assurance of Payment) Law 5732-1972;

#### **Amounts under living legacy agreements**

- (23) (a) part of a pension received by a person under an agreement for the bequest of a living legacy to the Keren Kayemet le-Israel, the Keren Hayessod – United Israel Appeal, or any other institution designated by the Minister of Finance, as follows:
- (1) if the person who bequeathed the living legacy had not reached age 50 at the time of the bequest – 50%;
- (2) if the donor had reached age 50, but had not reached age 60 at the time of the bequest – 60%;
- (3) if the donor had reached age 60, but had not reached age 70 at the time of the bequest – 75%;
- (4) if the donor had reached age 70, but had not reached age 80 at the time of the bequest – 80%;
- (5) if the donor had reached age 80 at the time of the bequest – 90%;
- (b) the exemption under sub-paragraph (a) is in lieu of an exemption under section 9B, and the person who bequeathed the living legacy shall not be entitled to credit or deduction under any statute for that living legacy;

#### **Linkage differentials and interest on excess tax payments**

- (24) interest and linkage differentials received by an assessee in consideration of excess tax payments, interest and linkage differentials received by a dealer under section 105 of the Value Added Tax Law

5736-1975, and interest and linkage differentials received by an assessee by virtue of section 103A of the Land Appreciation Tax Law; this provision shall not apply to an assessee, for whom interest and linkage differentials constitute income under section 2(1);

**Rental income received by elderly person**

- (25) rental income received by an elderly person who lives in an old age home, for the dwelling unit in which he lived before he entered the old age home – up to half of the annual amount paid during the tax year for his stay in the old age home;

for this purpose: "**old age home**" – a permanent place of residence for at least 30 individuals aged more than 65, which was given a license under the Homes (Supervision) Law 5725-1965;

**Contribution to a candidate in primary elections**

- (26) a contribution to a candidate in primary elections, which is permitted under Chapter Two of the Political Parties Law 5752-1992.

**Discharged Soldiers Law**

- (27) money received by a fund or by a discharged soldier under the Absorption of Discharged Soldiers Law 5754-1994;

**Gambling, lotteries or prizes**

- (28) gains or profit, as said in section 2A, the value of which is less than the amount set by the Minister of Finance with approval by the Knesset Finance Committee, all on the conditions and with the adjustments prescribed by him.

**Exemption on pension payable by employer or benefit fund and on pension payable under insurance against loss of working capacity**

- 9A. (a) For the purposes of this section –

"**pension**" – a pension payable by an employer or payable by a benefit fund, and also a pension payable under insurance against loss of working capacity, as defined in paragraph (3a) of the definition of "income from personal exertion" in section 1;

"**recognized pension**" – part of a pension paid by a pension benefit fund that is managed by an insurance company, or paid by another pension benefit fund that was set up after January 1, 1995, and which stems from exempt payments; for this purpose, "exempt payments" –

- (1) amounts charged with tax as said in section 3(e3);
- (2) amounts that the recipient of the pension deposited and on which he was not entitled to a deduction said in section 47;

"**entitling pension**" – that part of a pension or of the total of all pensions received by a person which does not exceed NS 7,200 (*in 2008; in 2007: NS 7,000; in 2006: NS 7,020; in 2005: NS 6,840 – Tr.*); if part of a pension was capitalized, then that pension shall be taken into account for the present purpose, which would have been paid if not for the capitalization;

"**retirement age**" – as defined in section 1, but for the purposes of this section a person is also deemed to have reached retirement age if –

- (1) repealed
- (2) he retired early because of a stable invalidity of a degree of 75% or more, determined under one of the Laws specified in section 9(5)(a) or under regulations made by virtue of section 9(5)(b);

**"exempt grant"** – that part of a retirement grant or half of that part of a death grant in respect of which tax exemption was granted under section 9(7a) and which was received after March 31, 1973, exclusive of a grant in addition to a pension paid –

- (1) under section 18 of the Israel Defense Forces (Permanent Service) (Benefits) Law 5714-1954;
  - (2) to a police man or prisons service member under section 22 of the State Service (Benefits) Law [Consolidated Version] 5730-1970, subject to section 77 of the said Law;
  - (3) to a security services employee, as the Prime Minister shall prescribe;
- (b) the recognized pension or 35% of the entitling pension, whichever is larger, received by any of the following shall be exempt of tax:
- (1) a person who reached retirement age;
  - (2) repealed
  - (3) survivors;
- however, if the pension is paid by an employer, otherwise than under a Law or collective agreement, then the exempt amount shall not exceed NS 101 per month in 2008 (*in 2006 and 2007: NS 98; in 2005: NS 96 – Tr.*) in respect of each year of employment.
- (b1) the recognized pension, received by an individual who has reached age 60 and who is not entitled to a benefit under subsection (b), is exempt of tax.
- (c) (1) If, after payment of the pension began or within fifteen years before payment of the pension began, a person also received grants for the years in respect of which the pension is paid, and if the total of exempt grants, divided by the number of years of employment in respect of which they were received, together with the amount of the monthly entitling pension (hereafter: the total amount) exceeds NS 7,200 per month (*in 2008; in 2007: NS 7,000; in 2006: NS 7,020; in 2005: NS 6,840 – Tr.*) (hereafter: the total amount), then the monthly exempt amount of the pension shall be reduced by an amount equal to the entitling pension multiplied by the difference between the total amount and NS 7,000 (hereafter: the difference), divided by the total amount; this provision shall not apply if the recipient of the pension elected to pay tax on that part of the exempt grants which is equal to the difference multiplied by the number of years of employment in respect of which the grants were paid.
- (2) The following shall be taken into account for purposes of computing the total amount:
- (a) if the grant was received after payment of the pension began or within five years before it began – the whole amount;
  - (b) if the grant was received between the sixth and the fifteenth year before receipt of the pension began – the amount said in subparagraph (a), less 10% for each year from the said sixth year to the year when the grant was received, up to the fifteenth year.
- (d) If an assessee elects to pay tax on part of the grant, as provided in subsection (c), then that part shall be apportioned equally over a period of up to six tax years, ending with the year in which the grant was received, but the Director may, on the assessee's application, permit apportionment over a different period on conditions he may prescribe, which may include an advance payment.

- (e) (1) An amount received by way of capitalization of an exempt pension is exempt of tax, on condition that this amount is not greater than the amount that would have been received from capitalization of 35% of the entitling pension;
- (2) if tax exemption under paragraph (1) was granted for part of a capitalized pension, then from the monthly pension exempt under subsection (b) shall be subtracted – in the tax years in respect of which that part of the pension was capitalized – an amount equal to the capitalized exempt monthly pension, multiplied by the ratio between the amount stated in the definition of "entitling pension" in the tax year in which the pension is being paid and the amount that was stated in that definition in the tax year in which the capitalization was carried out.

#### **Exemption of other pensions**

- 9B. 35% of the income under section 2(5), received by a person upon reaching retirement age within its meaning in section 9A(a), or received by survivors, and which is not a pension within its meaning in section 9A(a), is exempt of tax; an amount received in consequence of the capitalization of a pension exempt under this section is exempt of tax.

#### **Allowance for pension of ~~an~~ a first time Israel resident and for a veteran returning resident**

- 9C. Notwithstanding the provisions of sections 9A, 9B and 121, as the case may be, and subject to the provisions of section 14(a) the amount of tax on a pension from abroad for his work abroad, received by an individual who became an Israel resident for the first time or by a veteran returning resident, as said in section 14(a), shall not exceed the amount of tax which he would have paid on that pension in the state in which the pension is being paid, had he remained a resident of that state.

#### **Exemption of certain rental income**

- 9D. (a) 35% of the benefited rental income received by an entitled individual is exempt of tax, if all the following apply:
- (1) the individual or his spouse have no pension income to which the provisions of sections 9A or 9B apply, or interest income to which the provisions of sections 125D or 125E apply;
  - (2) the rent is not paid by a relative, as defined in section 105K, and not by a body of persons of which the individual is a controlling member.
- (b) An exemption under subsection (a) shall be granted only to one of the spouses.
- (c) In this section –
- "controlling member"** – as defined in section 32(9);
- "benefited rental income"** – income from rent chargeable under section 2(6) or (7), received by an individual for the rental of a property that had been his own, was used by him directly in the production of income from personal exertion from a business or occupation in Israel, up to the income ceiling multiplied by the rate of entitlement;
- "entitled individual"** – any one of the following:
- (1) an individual who has reached the retirement age;
  - (2) an individual, if he or his spouse has reached the retirement age; all if he is an Israel resident and had reached age 55 by the determining

date, as defined in section 88;

**"rate of entitlement"** – a rate of 2% for each tax year in which the property was used by the individual directly for the production of income from personal exertion from a business or occupation in Israel, but not more than 70%;

**"income ceiling"** – the amount stated in the definition of "entitling pension" in section 9A, multiplied by twelve.

## **Article Two: Authority to Exempt**

### **Tax reduction on productivity bonus and shift work pay**

10. (a) In this section –

**"tax benefit"** – tax credit, deduction from income or tax rates lower than those prescribed in section 121;

**"productivity bonus"** – a bonus, benefit or premium, which is work income paid under a work contract approved for the purposes of this section as prescribed by regulations, which is in addition to the customary salary or wage prescribed by the work contract, for productivity in excess of ordinary productivity as determined by measured norms approved by the Israel Institute of Productivity or by some other body designated by the Minister of Finance on the Institute's recommendation;

**"second and third shift"** – as defined by the Minister of Finance in regulations, after consultation with the Minister of Labor and Social Welfare.

(b) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe by regulations tax benefits in respect of income from second and third shift work or from grants paid for productivity in industrial enterprises most of whose activity in the tax year is productive activity, within its meaning in the Encouragement of Industry (Taxes) Law 5729-1969, which the Minister of Finance specified after consultation with the Minister of Industry and Trade, and for this purpose he may specify certain enterprises or branches of industry.

(c) A person entitled to a total income of more than NS 109,200 (*in 2008; in 2007: NS 106,320 – Tr.*) (hereafter: ceiling) from the employer who pays him income as said in subsection (b), is not entitled to the benefit under this section in respect of the part of the income that exceeds the ceiling, and for this purpose the income to which subsection (b) applies shall be deemed the highest of his income brackets; the ceiling amount shall be adjusted, as if it were an income ceiling, as defined in section 120A.

(d) The regulations said in subsection (b) may prescribe –

- (1) that the tax benefit apply to all the income as said in them or to part of it;
- (2) tax benefits at different rates or in different amounts for different branches of industry, for different professions or for different categories of assesseees;
- (3) rules and regulations for application of the tax benefits;
- (4) categories of employees to whose income the tax benefits shall not apply.

### **Tax benefits in settlements**

11. (a) In this section –

**"soldier"** – a soldier who serves under an undertaking for permanent service in the Israel Defense Forces, a policeman, including a policeman in the Border Guard in the Israel Police, a prison guard and also an employee of the General Security Service or of the Institute for Intelligence and Special Assignments, on condition that they serve in combat units;

**"special pay"** – the total salary that includes the level A activity bonus, paid during at least three consecutive months;

**"level A activity bonus"** – a salary supplement paid to soldiers because of activity in a combat unit in a development area, which under the statute that applies to the soldier is defined as a level A activity bonus and was approved by the Director for this purpose;

**"development area"** – each of the following:

- (1) the area of Judea, Samaria and the Gaza Strip;
- (2) any place north of latitude line 270;
- (3) any place south of latitude line 070, including the Dead Sea area;

**"resident"** of a certain settlement – an individual, the center of whose life is in that settlement;

- (b)
  - (1) if a person was a resident of one of the settlements specified in Part One of Schedule One during the entire tax year, then in that tax year he is entitled to a tax credit at the rate of 13% of his chargeable income from personal exertion, up to the amount of NS 205,800 (*in 2008; in 2007: 199,560; in 2006: NS 200,160; in 2005: NS 194,880 – Tr.*);
  - (2) if a person was a resident of Kiryat Shmonah during the entire tax year, then in that tax year he is entitled to a tax credit at the rate of 25% of his chargeable income from personal exertion, up to the amount of NS 205,080 (*in 2008; in 2007: NS 199,560; in 2006: NS 200,160; in 2005: NS 194,880 – Tr.*);
  - (3) if a person was a resident of a settlement specified below during the entire tax year, then in that tax year he is entitled to a tax credit at the rates specified below of his chargeable income from personal exertion, up to the amount of NS 136,680 (*in 2008; in 2007: NS 132,960; in 2006: NS 133,320; in 2005: NS 129,840 – Tr.*);
    - (a) Mitzpe Ramon – 25%;
    - (b) Dimona and Yeroham – 20%;
    - (c) Ofakim, Aroar, Tel Sheva, Ramat Hanegev Regional Council – 16%;
    - (d) Ben Ami, Gonen, Yehiam, Yessod Hamaaleh, Kfar Vradim, Lehavot Habashan, Netiv Hashayara, Netivot, Evron, Acco, Shavei Zion, Sderot and Sheikh Danun – 13%;
    - (e) a settlement specified in Part Two of Schedule One – 13%.
  - (4) Notwithstanding the provisions of paragraphs (1) to (3), if – in the course of the tax year – a person became a resident of any of the settlements specified in those paragraphs or ceased to reside there, then he is entitled to the tax credit said in those paragraphs in proportion to the period of his residence in the settlement, on condition that he resided in the settlement at least twelve consecutive months.
  - (5) The amount of credit under this section shall not exceed the amount of tax to which the assessee is liable in respect of the income, on which the credit is granted.
  - (6) The amount stated in paragraphs (1) to (3) shall be adjusted under

the provisions of section 120B, and the provisions that apply to income ceilings shall apply to it for this matter.

- (c) A soldier, to whom special pay is paid, is entitled to a tax credit of 5% of his special pay, up to the amount of income stated in the opening passage of subsection (b)(3), but if he is entitled to the said credit and also to a credit under the provisions of subsection (b), then he shall choose one of the credits.
- (d) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe an additional deduction in respect of assets of an enterprise located in a new settlement area or in a development area, as he shall prescribe and on the conditions he shall prescribe.

11A and 11B – Repealed

#### **Limit on reductions or benefits**

11C. A tax reduction or benefit under sections 11, 11A or 11B shall not be granted in respect of income said in Part Five "C" or in respect of income said in section 125C, if the tax rate applicable to it is not greater than 15%.

12 and 13 – Repealed

#### **Dividend from preferred income**

- 13A. (a) The Minister of Finance may, with approval by the Knesset Finance Committee, direct by Order that dividends paid by certain categories of companies out of preferred income specified in the Order shall be treated like preferred income; in this section, "**preferred income**" – income from interest or dividend in respect of which a tax concession or tax exemption is granted under any enactment.
- (b) Dividends paid by a company said in subsection (a) in a particular tax year shall be taken to include preferred income at a rate equal to the ratio of the company's preferred income to its total income in the year, in which accrued the income out of which the dividend is distributed.

#### **First time Israel residents and returning residents**

14. (a) An individual who became an Israel resident for the first time and a veteran returning resident shall – during ten years after the date on which they became residents as aforesaid – be exempt of tax on their income from all the sources enumerated in sections 2, 2A and 3 that were produced or accrued abroad or that are derived from assets abroad, unless they made a different request in respect of all or part of the income; in this section:
- "asset"** – except for assets that reached the individual completely exempt of tax under section 97(a)(5), beginning with January 1, 2007;
- "veteran returning resident"** – an individual who returned and became an Israel resident after he stayed abroad during at least ten consecutive years.
- (b) (1) Notwithstanding the provisions of paragraph (a) of the definition of "Israel resident" or "resident", an individual who became an Israel resident for the first time or a veteran returning resident shall not be deemed an Israel resident during one year after the date on which he came or returned to Israel, as the case may be (in this subsection: adjustment year), provided that – within ninety days after he arrived in Israel as aforesaid – he gave notice on a form



prescribed by the Director that he chose to have this subsection applied.

- (2) Notwithstanding the provisions of paragraph (1), if an individual gave notice that he opted for the adjustment year as said in that paragraph, the adjustment year shall be included for purposes of the periods specified below:
- (a) the period of exemption said in subsection (a);
  - (b) the period said in paragraph (b)(2) of the definition of "Israel resident" or "resident";
  - (c) the period said in paragraph (2) of the definition of "foreign occupational company" and in the definition of "income of the Israel resident shareholders" in section 5(5)(e);
  - (d) the period said in the definition of "Israel resident" in section 75B(a)(15);
  - (e) the period said in section 75P1(a1) and (c)(2)(a);
  - (f) the period said in section 97(b)(1);
  - (g) the period said in section 134B;
  - (h) the period said in section 135(1)(b).
- (c) A returning resident shall be exempt of tax during five years from the date on which he became an Israel resident in respect of income produced or accrued abroad or that stems from assets abroad, such as are not income from business, as specified below, unless he made a different request in respect of all or part of the income:
- (1) income from pension, royalties, rent, interest and dividends, that stems from assets abroad, which the returning resident acquired during the period of his stay abroad after he ceased being an Israel resident;
  - (2) income from interest and dividends that stem from assets abroad, which are benefited securities;
- in this subsection:
- "benefited securities"** – securities traded on an Exchange that the returning resident acquired during the period of his stay abroad after he ceased being an Israel resident and that are kept in an account with a banking institution, and also securities traded on an Exchange, which the returning resident acquired out of income that is interest or dividends derived from benefited securities or out of income that is a capital gain from the sale of benefited securities and which was deposited in the same account;
- "Exchange"** – a securities exchange abroad, which was approved by whoever is entitled to approve it under the statutes of the state where it operates, and also an organized market abroad;
- "account with a banking institution"** – an account with a banking institution in which no deposits were made after the returning resident became an Israel resident, except for the deposit of income that is interest or dividends derived from benefited securities or income that is a capital gain from the sale of benefited securities;
- "returning resident"** – an individual who again became an Israel resident after he was a foreign resident during at least six consecutive years.
- (c1) If an individual became an Israel resident and is a controlling member

and a Director of an approved enterprise, within its meaning in the Encouragement of Capital Investments Law, then in tax years 2003 to 2006 he shall be exempt of tax on his income from interest, dividends and rent that do not constitute income from business and stem from assets abroad, which he owned before he became an Israel resident, or from other assets that replaced them and remained his property after he became an Israel resident, and also on profits from the sale of those assets, unless he requested otherwise in respect of all or part of the income. *(NOTE: Under the provisions of Amendment No. 132 this subsection (c1) is in effect for tax years 2003 to 2006 – r.*

- (d) (1) The Minister of Finance may, with approval by the Knesset Finance Committee, make regulations according to which full or partial tax exemption will be granted to an individual specified below on his income that originates abroad, during a period set by the Minister of Finance and on conditions and with adjustments prescribed by him, on condition that most of his business activity is abroad:
  - (a) an individual who for the first time became an Israel resident and before he became a said resident he made investments in Israel;
  - (b) an individual who ceased being an Israel resident, permanently stayed abroad during the determining period, and again became an Israel resident and made investments in Israel when he was not an Israel resident; for this purpose: the "**determining period**" –
    - (1) for a person who ceased being an Israel resident before he had reached age 18 – at least ten consecutive years;
    - (2) for a person who ceased being an Israel resident after he had reached age 18 – at least twenty consecutive years.
- (2) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe that regulations made under paragraph (1) also apply to an individual said in subparagraphs (a) or (b) of the said paragraph, if he made the investments in Israel within one year after the regulations under this paragraph went into effect, on condition that he became a resident as said in those subparagraphs between January 1, 2002, and the day on which regulations under this paragraph go into effect, and the Minister of Finance may set conditions for granting tax exemptions in addition to the conditions set in regulations under paragraph (1).

#### **Income of company whose business is controlled from abroad**

14A. If a company's business and management are controlled from abroad, and if it receives in Israel income derived or accrued abroad, then the Minister of Finance may, on its application, direct that it shall pay tax at a rate of not more than 15% on that income and in special cases he may even exempt it of tax.

#### **Authority to exempt**

14B. The Minister of Finance may, with approval by the Knesset Finance Committee, grant tax relief in respect of income of a social nature or in respect of compensation, which an Israel resident individual receives, if it is paid to him by a foreign State or by its welfare authority, and he may also exempt the aforesaid of income tax, all as he shall prescribe.

### **State Loan**

15. The Minister of Finance may, with approval by the Knesset Finance Committee, direct that the interest and linkage differentials payable on a loan secured by State revenue be exempt of tax, either generally or in respect of interest and linkage differentials payable to foreign residents; he also may, with the said approval, direct that the interest paid on a loan, the repayment of which is guaranteed by a foreign state or by a person recognized by the Minister of Finance as acting in the name of and for a foreign state, or interest on a loan received by the Jewish Agency for Israel, be exempt of tax.

### **Authority to exempt interest and linkage differentials on deposits, savings programs and debentures**

- 15A. The Minister of Finance may, with approval by the Knesset Finance Committee, exempt of tax, in whole or in part, linkage differentials or interest in the amount of the linkage differentials, that is payable on categories of deposits, categories of savings programs and categories of debenture to categories of assesseees, in accordance with conditions which he set in the said approval.

### **Calculation of real interest**

- 15B. The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe a method for calculating the part of the interest that exceeds the rate of the index increase, on conditions and with adjustments he prescribed, and he may prescribe as aforesaid in respect of the categories of assets or categories of assesseees, all according to the period during which an asset was held or according to some other criterion.

### **Exemption of certain interest**

16. The Minister of Finance may direct, by an Order published in Reshumot –
- (1) that income from interest payable on bonds issued to a foreign resident not engaged in any business or vocation in Israel be exempt of tax on the amount in excess of the 25% interest deducted under section 161(a) of the Ordinance, and that all or part of the linkage differentials payable on aforesaid bonds be exempt of tax;
  - (2) that a tax exemption or a tax reduction be granted on income from interest payable by the State or payable, with approval by the Controller of Foreign Exchange, by a banking institution, within its meaning in the Bank of Israel Law 5714-1954, on foreign currency deposits held by it;
  - (3) that income from interest payable on debentures issued by an Israel borrower to the International Bank for Rehabilitation and Development be tax exempt, also when it is received by a foreign resident, to whom the debentures were transferred;
  - (4) that interest paid by an Israel resident body of persons on a foreign currency loan received from a foreign resident who does not conduct business or a vocation in Israel – the loan being used for one of the purposes specified in section 1 of the Encouragement of Capital Investments Law 5719-1959 – be wholly or partly exempt of tax.

### **Authority to refund tax to foreign resident**

- 16A. The Minister of Finance may direct that all or part of tax be refunded to a person who is not an Israel resident, if the amount of tax he paid in Israel exceeds the amount which – because of that payment – he is allowed to deduct in his country of permanent residence as a credit against the tax due in

that country on the income he earned in or derived from Israel, also if he was not allowed to deduct the amount or it was not given him as a credit in the country of his residence, because of provisions in that country for the set-off of losses.

#### **Certain linkage differentials**

16B. The Minister of Finance may, with approval by the Knesset Finance Committee, exempt of tax part or all of linkage differentials added to the amount of a debt or claim in designated categories of debts or claims; for this purpose: "**linkage differentials**" – including interest in a total amount that does not exceed the amount that would have had to be added in accordance with the consumer price index increase, as said in section 159A(a), had the debt or claim been linked to the index during the corresponding period.

#### **Income from sale of water**

16C The Minister of Finance may, by Order with approval by the Knesset Finance Committee and on conditions set in the Order, exempt of tax income from the sale of water by a person whose entire business is the supply of water.

16D and 16E. Repealed

## **CHAPTER TWO: DEDUCTIONS AND SET-OFFS**

### **Article One: Deduction of Expenses**

#### **Permitted deductions**

17. In ascertaining the chargeable income of any person, all disbursements and expenses that person incurred during the tax year wholly and exclusively in the production of his income shall be deducted – unless the deduction is limited or disallowed under section 31 – including –

#### **Interest and linkage differentials**

- (1) (a) sums payable as interest or linkage differentials on money he borrowed, if the Assessing Officer is satisfied that they are payable on capital used in obtaining the income;
- (b) if an assessee claims the deduction of interest or linkage differentials under subparagraph (a) in a year in which he received interest or linkage differentials exempt of tax under section 9(24), then he shall not be allowed to deduct an amount equal to the amount of the said exempt interest and linkage differentials, except for the larger of the following two amounts:
  - (1) an amount received in consideration of excess tax paid by him because the Assessing Officer demanded its payment, or because it was deducted from him at the source;
  - (2) an amount received by him in consideration of that part of the excess tax payment which does not exceed 15% of the tax due from him according to his self assessment.

#### **Rent**

- (2) rent a tenant paid on land or buildings occupied by him for the purpose of acquiring income;

#### **Repairs**

- (3) amounts expended for the repair of premises, plant and machinery used in acquiring the income, and also for the renewal, repair or alteration of work implements, utensils or objects used as aforesaid;

**Bad debts**

- (4) bad debts incurred in a business or vocation, proved to the satisfaction of the Assessing Officer to have become bad during the tax year, as well as doubtful debts to the extent that they are estimated, to the Assessing Officer's satisfaction, to have become bad during the tax year, even if such bad or doubtful debts were due and payable before the beginning of the tax year; however, sums collected during the tax year on account of amounts previously written off or deducted in respect of bad and doubtful debts shall, for purposes of this Ordinance, be treated as receipts of the business or of the vocation in that year;

**Employer's payments to a benefit fund**

- (5) sums an employer paid – on conditions and at rates prescribed under section 22 of the Control of Benefit Funds Law – as regular annual contributions to a benefit fund, as well as sums at the said rates and conditions, but mutatis mutandis as the case may be, paid by an employer to the State, to a local authority or to some other body designated by the Minister of Finance for this purpose, in order to protect his employee's pension rights and any amount or part thereof paid by an employer – with the Director's approval – to a said benefit fund or to any said institutions or body, otherwise than as a regular annual contribution;

**Payments to a training fund for selfemployed persons**

- (5a) amounts paid by an individual to a training fund for the selfemployed, after they were reduced by an amount equal to 2.5% of his determining income; said amounts shall not exceed 4.5% of his determining income; for this purpose:  
"determining income" – the individual's chargeable income from business or vocation, before the deduction under this paragraph, up to an amount of NS 218,000 (*in 2007; in 2006: NS219,000; in 2005: NS213,000 – Tr.*) per year;  
"training fund for selfemployed persons" – a training fund that is designated for individuals who have income from a business or occupation.

**Damage by natural agencies**

- (6) expenditures on measures for the prevention of soil erosion, against floods and against other natural disasters that will be designated;

**Air raids**

- (7) expenditures on air raid precautions;

**Depreciation**

- (8) deductions for depreciation, as specified in Article Two;

**Bonuses of a cooperative society**

- (9) amounts which a cooperative society returned to its members as an annual bonus in proportion to the business it conducted with each member, on condition that –  
(a) no deduction shall be allowed in an amount that exceeds that part

of the taxable income before payment of the bonus, the ratio of which to the total taxable income is the same as that of the sum of its business with its members to the total of its business transactions;

- (b) the bonus was given to members within nine months after the end of the accountancy year to which it relates, or at a later date set by the Director;
- (c) the bonuses shall be deemed to have been received by the members at the end of the accountancy year to which they relate;

(10) repealed

#### **Expenses connected with the payment of tax**

- (11) (a) expenses in connection with the preparation of returns and the handling of tax matters in all assessment or appeal proceedings; however, if a Court or a books acceptability committee determined that an appeal or objection was vexatious and that there was no reasonable justification for submitting it, then legal expenses incidental thereto shall not be deductible; if legal expenses were awarded to the assessee, then the amount of expenses awarded shall be deducted from the amount of expenses claimed by him;
- (b) expenses said in this paragraph shall not be deductible in connection with income from a business or vocation in respect of which no account books were kept, or if the return is not based on account books;

#### **Rent paid by individual who moved temporarily**

- (12) rent paid by an individual for a dwelling which he rented in Israel and to which he moved temporarily because of his work or vocation, during five years after the day on which he moved to the said dwelling; that rent shall be deductible from rent he receives in respect of his permanent dwelling during the same period;

#### **Lodging expenses and rent in development area**

- (13) (a) amounts paid by an assessee for lodgings or for the rental of a dwelling in an area designated a development area under section 11, where the assessee is permanently employed, but where he does not live with his family with whom he would live, if he did not work there;
- (b) the Minister of Finance may prescribe the ceiling amount deductible under subparagraph (a) and the period of the deduction;

#### **Other deductions**

- (14) other deductions to be prescribed by regulations under this Ordinance.

#### **Restrictions on the deduction of certain expenses**

- 18. (a) A retirement grant, leave pay, convalescence pay, holiday pay, sick pay and other similar expenses are deductible under section 17 only in the tax year in which they were paid to the person entitled to them or to a benefit fund, but aforesaid payments made to a benefit fund in respect of the last month of the tax year are deemed to have been made during the tax year if they were made within one month after the end of the tax year.
- (b) Work income, management fees, linkage differentials or interest, or

- other payments paid by a company controlled by not more than five persons, within its meaning in section 76, to one of its members who is a controlling member, within its meaning in section 32(9), shall be deductible under section 17 in a given tax year if they were paid to him during that tax year or if he included them in the return of his income in that tax year and if tax on them was deducted under regulations for deduction from wages no later than three months after the end of the tax year or of the special assessment period, as the case may be, and if it was transferred to the Assessing Officer within seven days after the deduction, together with linkage differentials and interest from the end of the tax year or special assessment period until the date of the deduction.
- (b1) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe that the provisions of subsection (b) not apply to categories of payments that constitute tax exempt income for a controlling member, and he may make a said determination conditional.
  - (c) If a person's income includes income for which a special tax rate has been set or which is exempt of tax (hereafter: preferred income), then the expenses incurred by that person in order to acquire the preferred income shall be deductible under section 17 only against that income; if the aforesaid expenses cannot be ascertained, then a proportional part of the expenses incurred in producing the total income shall be deducted from the preferred income, in the ratio of the preferred income to the total income, but the Minister of Finance may prescribe a different apportionment of the expenses if he sees fit to do so under the circumstances.
  - (d) (1) In this section –
    - "work unit"** –
      - (1) a building, construction of which takes longer than one year, including its components the execution of which takes as aforesaid and including work said in paragraph (2) that constitutes a part thereof, and if it is a capital asset – as long as its use for the production of income has not begun in the first half of the tax year or of the special assessment period, irrespective of whether income from it constitutes income under section 2(1) or as a capital gain or land appreciation;
      - (2) excavation work, sewage work, highway and road paving and earth works – execution of which takes longer than one year;
    - "interest expenses"** – interest and linkage differentials deductible under section 17, as well as interest and linkage differentials on capital used for the construction or acquisition of a capital asset, less income from interest and linkage differentials on loans extended to a financial institution, to the State, to a local authority, to a Government company, to a Government subsidiary or to any other person designated by the Minister of Finance;
    - "other income"** – income that is not from one of these:
      - (1) the sale of a work unit;
      - (2) the sale of land;
      - (3) interest and linkage differentials on loans extended to a financial institution, to the State, to a local authority, to a Government company, to a Government subsidiary or to any other person designated by the Minister of Finance;
      - (4) (a) during the period in which the Taxation under Inflationary Conditions Law is in effect – the sale of a

capital asset other than unprotected negotiable securities, within their meaning in the said Law;

(b) during the period in which the Inflationary Adjustments Law is in effect – the sale of the asset, as defined in section 104;

(c) in the period after the effect of the Inflationary Adjustments Law – the sale of an asset, as defined in section 104;

however, in respect of income from securities said in this paragraph only the amount of their change in value or profit from them, as the case may be, shall be taken into account as other income;

**"financial institution"** –

(1) a company or cooperative society that engages in the acceptance of monetary deposits in current accounts, in order to pay out of them on demand by check;

(2) a company that lawfully uses the word "bank" as part of its name, except for a company the name of which mentions the name of a company or cooperative society to which paragraph (1) applies;

**"management expenses and overhead"** – any expense that is not an interest expense, and which the assessee does not customarily charge directly against a work unit, land or other income.

(2) If an assessee, whose business is the construction of work units, had in the process of execution in any given tax year work units or land that constitute stock in trade, then his management expenses and overhead and interest expenses in that tax year shall be charged to each of the aforesaid work units or land, as follows:

(a) a proportional part of the management expenses and overhead shall be charged to each work unit, in the ratio of the assessee's expenses in that tax year for the execution of that work unit to the total of expenses in that tax year for the execution of all work units, plus the amount of his other income in that tax year;

(b) (1) a proportional part of interest expenses shall be charged to each work unit or land, in the proportion between the assessee's total cumulative expenses until the end of the tax year for the execution of that work unit or the acquisition of that land and the assessee's total cumulative expenses until the end of the tax year for the execution of all work units and the acquisition of all the land, plus the amount of his other income in that tax year; for this purpose: **"expenses for the execution of a work unit and the acquisition of land"** includes expenses to be charged against a work unit and against land under this section until the end of the preceding tax year;

(2) the balance of interest expenses not charged as said in paragraph (1) shall be deductible, so that part thereof, in the proportion of the preferred income within its meaning in section 18(c) to the total of other income, shall be related to the said preferred income.

(e) The income of a foreign resident, from which tax must be deducted



under sections 164 or 170, shall be deductible under section 17 in the tax year to which it relates only if it was paid in that tax year or if the tax on it was deducted not later than three months after the end of the tax year or of the special assessment period, and was transmitted to the Assessing Officer within seven days after the deduction, together with linkage differentials and interest from the end of the tax year or special assessment period until the date of the deduction.

19. Repealed

**Power to prescribe rules about certain deductions**

20. (a) The Minister of Finance may, with approval by the Knesset Finance Committee, make rules on the deduction of amounts specified below, in whole or in part, its period during and its annual rate:
- (1) amounts paid by the owner of a building, rented in whole or in part under protected rental, in order to vacate a protected tenant, or as participation in the construction of a sidewalk or road next to the building, or of drainage connected to the building and for similar purposes;
  - (2) amounts paid by a lessee of real estate in respect of the lease or for investment in the leased real estate or in connection therewith;
  - (3) amounts expended by an assessee for replanting;
  - (4) other capital expenses.
- (b) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe rules –
- (1) on granting additional depreciation in respect of a building let wholly or in part under protected rental, its rate and the period during which it is to be granted;
  - (2) on depreciating the undepreciated balance of a wholly or partly uprooted plantation, if its owner planted another plantation before or after the uprooting, and on how to deal with depreciation in the determination of the original cost for purposes of depreciation and of capital gain on the new plantation.

**Deductions for scientific research**

- 20A. (a) (1) In determining the chargeable income of a person who incurred expenses – including capital expenses – for scientific research in the fields of manufacture, agriculture, transportation or energy, approved for this purpose by a person authorized by the Minister in charge of the Ministry within whose field of activity the research falls, he shall be allowed to deduct them from his total income in the tax year during which they were incurred, on condition that one of the following holds true:
- (a) the research is carried out by the owner of an enterprise in one of the said branches, or on his behalf, for the development or advancement of his enterprise;
  - (b) the expenses are those of the person who conducts the research, who is not the owner of an enterprise in the said fields, or they constitute participation in the financing of research carried out by another person, in return for a right to results of the research, which is reasonable in proportion to the participation in research costs, and all that on condition that the State participates in financing the research by way of a grant; for this purpose: "**grant**", includes a loan

of a type designated by the Minister of Finance with approval by the Knesset Finance Committee; however, expenses that constitute such participation shall be deducted as follows: in the tax year in which the expenses were paid out – a proportional part, in the ratio between the number of months from the month after the month in which they were paid until the end of the year, divided by 12, and the remainder in the following tax year; for purposes of calculating the said proportional part, an undertaking to pay expenses in 12 equal monthly installments shall be deemed an expense paid in their entirety when the first installment is paid;

- (1a) if a person participates in the financing of research carried out by another, as said in paragraph (1)(b), then he may set off the tax saved against tax deducted at the source from work income or against advance payments due from him under section 175 of the Ordinance, beginning with the month after the month in which he paid the expenses; if, in respect of any tax year, a balance remains to be set off, its set off will be allowed when the return for that year is delivered; for this purpose: **"the tax saved"** – the amount of tax from the payment of which the assessee was exempted by virtue of the deduction under paragraph (1), but for purposes of setting off only against advance payments the saved tax shall be calculated at the 55% tax rate for an assessee who is an individual, and at the average tax rate for the preceding tax year for an assessee who is a body of persons;
- (1b) for purposes of section 190A, a set off against deduction at the source or against advance payments under paragraph (1a) shall be treated like a sum deducted at the source, as said in section 177;
- (1c) if a person, who carries out research approved by whoever is authorized to give approval as said in paragraph (1), raises from investors in research and development amounts which, together with the amounts he himself invests in the said research, exceed the amounts spent to conduct that research, then the excess amount shall be deemed chargeable income for him on which the applicable tax rate is 100% without any right whatsoever to exemption, deduction or set off, and the date of its payment, for purposes of computing interest and linkage differentials under section 159A of the Ordinance, is the date on which the excess amount was created; the Minister of Finance shall prescribe, with approval by the Knesset Finance Committee, ways of calculating the excess amount and of determining the day on which it was created;
- (2) capital expenditures for scientific research, incurred by a person for the advancement or development of his enterprise, to which the provisions of subsection (1) do not apply, may be deducted in three equal annual installments, beginning with the tax year during which they were incurred;
- (3) the amount of a grant said in paragraph (1)(b), given by the State to finance scientific research, shall be subtracted from the amount of expenses, deduction of which is allowed under this subsection.
- (b) Any amount of expenditure invested in an asset, in respect of which depreciation is allowed under section 21, shall not be deductible under subsection (a).

### **Overall ceiling on deductions for research and development**

- 20A1.(a) The amount deductible in consideration of participation in the financing of research and development carried out by another person, under section 20A(a) and under any other statute, shall not exceed 40% of the assessee's chargeable income in the tax year in which the expenses were paid.
- (b) The provisions of subsection (a) shall not apply to amounts of participation by an industrial holding company in a company under its control; for this purpose:
- "industrial holding company"** – a company at least 80% of whose assets during the entire tax year, exclusive of assets derived from funds received from an issue on an Exchange abroad until one year after the date of the issue, are invested in the share capital of industrial companies, or in loans for at least three years extended to industrial companies;
- "industrial company"** – within its meaning in the Encouragement of Industry (Taxes) Law 5729-1969;
- "control"** – within its meaning in section 25.

### **Deduction because of research and development – addition to base for advance payments**

- 20A2 The amount of tax, from the payment of which the assessee was exempted because of participation in the financing of research and development conducted by another, under section 20A(a) and under any other statute, shall be added to the amount of tax that constitutes the base for the determination of advance payments under section 175.

20A3. Repealed

### **Deduction for maintenance of foreign resident**

- 20B. In determining the chargeable income of an individual Israel resident who pays for the maintenance of a foreign resident in accordance with the judgment of a competent judicial authority abroad, handed down while the payor also was a foreign resident, he shall be allowed to deduct that part of the maintenance paid which exceeds an amount set by the Minister of Finance with approval by the Knesset Finance Committee, and which does not exceed a maximum amount set as aforesaid.

## **Article Two: Deduction of Depreciation**

### **Depreciation of assets**

21. (a) A deduction shall be allowed for the depreciation of buildings, machinery, installations, furniture or other assets that are owned by the assessee and used for the purpose of producing his income, including live and other agricultural stock and plantations; the amount of deduction shall be calculated according to percentages – set with approval by the Knesset Finance Committee for each case or each category of cases – of the original cost to the assessee, exclusive of the cost of land on which a building was erected or a plantation planted, all as the case may be, on condition that the prescribed particulars have been duly produced; for purposes of this section, a lease of real estate for a period

of 49 years or more shall be treated like ownership thereof; a person who, although he has disposed of an asset, is liable to tax on it under sections 83 or 84, and a person who has transferred an asset, but reserved to himself the right to enjoy its proceeds, shall also be deemed its owner, and the depreciation allowed him shall be the depreciation which would have been allowed him but for the said disposition or transfer.

- (b) If a grant is received because of the acquisition of an asset, in respect of which depreciation is deductible under subsection (a), or if a debt that stems from a loan for the acquisition of an aforesaid asset is remitted or written off within five years after the year in which it was received, or if value added tax was paid on the acquisition of an asset and the assessee deducted the tax as input tax in accordance with the Value Added Tax Law 5736-1975, then the original cost of the asset, both for this purpose and for the purposes of section 88, shall be its aforesaid cost, less the amount of the grant, the debt or input tax, as the case may be; this provision shall not apply to an amount charged with tax under section 3(b)(2).
- (c) If a person incurred expenses, in order to comply with instructions issued to him for the installation of special arrangements for invalids in a public building, under section 158C of the Planning and Building Law 5725-1965, then he shall be allowed to deduct depreciation on those expenses at the rate of 16.5% per year; this provision shall not apply to a person who incurred the said expenses on a building, construction of which was finished after March 31, 1981.
- (d) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe that, if a dwelling was rented out for residential use in a certain tax year, and if its owner is not entitled to benefits for it under Chapter Seven "A" of the Encouragement of Capital Investments Law 5719-1959, then the deduction of depreciation shall be allowed as calculated as a percentage of the value of the dwelling, and he may – with the said approval – make rules for calculating the value of the dwelling.

#### **Carrying depreciation forward from one year to another**

22. If all or any part of depreciation cannot be deducted in a particular tax year because the source in respect of which depreciation is claimed did not yield any income in that year or yielded less income than the amount deductible as aforesaid, then the amount not deducted shall be deemed a loss for the purposes of section 28; this provision shall not apply if the source in respect of which depreciation is claimed is not a business or vocation, and in that case the amount not deducted shall be deemed a loss permitted to be set off in the succeeding years against the same source only.

#### **Restriction on depreciation deductions**

23. The total of depreciation deductions deductible under the Ordinance, plus the total of wear and tear, calculated at the prescribed rates, during the period before the date on which depreciation was allowed under this Ordinance, shall not exceed the original cost of the assets to the assessee, as said in section 21, without the cost of the land on which a building is built or on which a plantation is planted, as the case may be; however, for the purpose of the original cost of citrus plantations, depreciation deductions and wear and tear during the period before 1950 shall not be taken into account.

### **Depreciation upon transfer of an asset without transfer of control**

24. (a) If a depreciable asset was transferred from one person to another, and if the Director found and decided that control of the transferred object remained with the person who held it before the determining date, then the amount of depreciation which the transferee is entitled to deduct under sections 21 to 23 shall be the amount which the transferor would have been entitled to deduct, if not for the transfer; and if the transfer took place before April 1, 1946, and the transferee deducted depreciation under sections 21 to 23 in an amount that exceeds the amount which he would have been entitled to deduct under the provisions of this section, then the excess shall not be deemed to have been deducted unlawfully, but it shall be taken into account in calculating the total depreciation permitted under section 23.
- (a1) If a depreciable asset was sold and the seller acquired it again, then the amount of depreciation which the seller is entitled to deduct under sections 21 to 23 after the reacquisition shall be the amount to which he would have been entitled, had he not sold it.
- (b) The provisions of subsection (a) shall apply to a transfer of assets by two or more persons to another person, as they apply to such a transfer by one person to another, if the Director finds and decides that all of the control of the object transferred remained with the persons, each of whom had held a part of the transferred object before the determining date.
- (c) The provisions of this section shall not apply to a transfer charged with capital gains tax under Part Five, or if the capital gain was set off against a loss, on condition that an amount equal to the inflationary amount, within its meaning in section 88, on which tax was paid at the rate of 10%, shall be subtracted from the original cost; this subtraction shall also be taken into account for purposes of the definition of "original cost" in section 88.
- (d) The Director's decision under this section may be appealed under sections 153 to 158.

### **Definition of control**

25. For purposes of section 24, "**control**" – direct or indirect control or the ability to exercise or the right to acquire aforesaid control and, particularly, but without derogating from the generality of the aforesaid –
- (1) if control is by virtue of shares – holding or having the right to hold or to acquire a majority of the share capital or of the issued share capital, or of the voting power, or the right to hold or to acquire them, and also the right to receive most of the profits or to appoint a majority of the directors, or the right to acquire an aforesaid right;
- (2) if control is by other means – the right to most of the capital, to most of the profits, to a majority of the voting power, or to appoint a majority of the directors, or the right to acquire an aforesaid right.

### **Who holds control**

26. (a) In determining – for purposes of section 24 – whether control is or was held by a certain person, the relative of that person, within its meaning in section 76(d), shall be deemed to be identical with that person.
- (b) If, at any time within three years after the transfer, control of the transferred object is again held by the transferor, then it shall be deemed to have been held by him throughout.

**Definition of determining date**

26A. For purposes of section 24, "**determining date**" – the date of the transfer of a business or asset, or the date on which a transaction was performed of which the said transfer is a part or to which it is connected, or the date on which the first of several transactions was performed of which the said transfer is part or to which it is connected, all as the case may be.

**Deduction for the replacement of machinery and equipment**

27. (a) If a person engaged in any business or vocation expended a certain amount during a certain tax year for the replacement of machinery and equipment used or formerly used in that business or vocation, then – for the determination of his chargeable income – he shall be allowed to deduct an amount equal to the amount of the expenditure incurred by him in the acquisition of the old machinery and equipment, less all the depreciation he deducted on that machinery and equipment and the amount received by him for their sale, or an amount equal to the amount expended by him on the new machinery and equipment, whichever is less; if an amount was deducted under this subsection, then any loss permitted to be set off under Part Five in respect of the sale of the old machinery and equipment shall be reduced by that amount.
- (b) Subsection (a) shall not apply to private motor vehicles, within their meaning in the Traffic Ordinance.

**Depreciation deduction at an exchange of land and in Evacuation and Compensation**

- 27A. (a) In this section every term shall have the meaning it has in the Real Estate Taxation Law, unless a different meaning is explicitly provided.
- (b) When real estate rights are exchanged under Chapter Five AC of the Real Estate Taxation Law, the following provisions shall apply to the deduction of depreciation and also to additional deduction for depreciation or amortization, within their meaning in section 3 of the Inflationary Adjustments Law:
- (1) the original cost of the replacement right shall be one of the following:
    - (a) if the adjusted value of the replacement right is equal to the sale value of the sold right – the balance of the original cost of the sold right;
    - (b) if the adjusted value of the replacement right is less than the sale value of the sold right – the balance of the original cost of the exempt sold right;
    - (c) the provisions of subsection (b) shall apply, mutatis mutandis, also to the sale of another unit in the compound to an entrepreneur, in consideration whereof another unit was received, as said in Chapter Five AD of the Real Estate Taxation Law, up to the ceiling value;
  - (2) the balance of the original cost of the sold right shall be the original cost of the part of the replacement right;
  - (3) the value of the additional replacement right on the day of its acquisition shall be its original cost;
  - (4) the depreciation rate prescribed for the deduction of depreciation in respect of the replacement right or of the additional replacement right, as the case may be, shall be the rate of depreciation;

- (5) the depreciation said in this section shall be allowed only if the replacement right, part of the replacement right or the additional replacement right is a depreciable asset.

### Article Three: Set Off of Losses

#### Setting off a loss

28. (a) A loss incurred by a person during the tax year in a business or vocation, which – had it been a profit – would have been assessable under this Ordinance, may be set off against that person's total chargeable income from other sources in that tax year.
- (b) If all of the loss cannot be wholly set off in the said tax year, then the amount of loss not set off shall be carried forward to the subsequent years in succession and it shall be set off against that person's total chargeable income from business or vocation in those years, including capital gains from business or vocation, or it shall be set off against that person's entire chargeable income in those years under section 2(2), all the conditions specified below having been met, provided that – if the loss can be set off in one of these years – it shall not be allowed to be set off in the following year:
- (1) that person had no income from business or vocation in the year of the set-off,
  - (2) that person ceased engaging in the business or vocation in which he suffered the loss that he wishes to set off;
  - (3) the loss suffered by that person does not stem from a house company, within its meaning in section 64, from a family company within its meaning in section 64A or from a transparent company, as defined in section 64A1(a).
- (NOTE: Under the provisions of Amendment No. 154, the provisions of subsection (b) apply to losses from business or vocation created in 2007 and thereafter – Tr.)*
- (c) Notwithstanding the provisions of subsections (a) and (b), if the assessee so requests a loss shall not be set off under this section against a capital gain which is an inflationary amount, or against a capital gain, interest or dividend, if the tax rate applicable to them does not exceed 20%.
- (d) A loss incurred by a person in a citrus plantation, planted in grafted condition, in the fifth and sixth years after the beginning of the tax year in which it was planted, shall only be set off against his income from that plantation in the sixth and seventh years.
- (e) A loss incurred by a person in a citrus plantation, planted in ungrafted condition, in the sixth and seventh years after the beginning of the tax year in which it was planted, shall only be set off against his income from that plantation in the seventh and eighth years.
- (f) The provisions of subsection (b) shall apply to any loss which cannot be set off as said in subsections (d) and (e).
- (g) For purposes of subsections (d) and (e), a citrus plantation planted after November 30 of any year shall be treated as if it had been planted in the first month of the following tax year.
- (h) A loss incurred by a person from the letting of a building may be set off against his income from that building in subsequent years.
- (i) Repealed

- (j) In this section, "**chargeable income**" and "**capital gain**" – including appreciation within its meaning under section 6 of the Land Appreciation Tax Law 5723-1983 (hereafter: land appreciation).

**Loss incurred outside Israel**

29. Notwithstanding the provisions of section 28, the following provisions shall apply to a loss incurred abroad:

- (1) (a) If during the tax year an Israel resident incurred a loss abroad which – had it been a profit – would have been liable to tax as passive income, then it shall be set off against chargeable passive income from abroad; however, a loss from renting a building, which stems from depreciation, may also be set off against a capital gain upon the sale of that building; for the purposes of this section, "**passive income**" – income from interest, linkage differentials, rent or royalties, which is not income from a business or a vocation;
- (b) if it is not possible to set off the entire loss in the tax year, as said in subparagraph (a), the amount of loss that was not set off shall be transferred to the following years, one after the other, and shall be set off against chargeable passive income produced abroad during those years, on condition that – if it is possible to set the loss off in one of the years – it shall not be allowed to be set off in the following year; however a loss from renting a building, which stems from depreciation and which was brought forward from previous years, may also be set off against a capital gain from the sale of that building;
- (2) if an Israel resident suffered a loss abroad from business or vocation, and which – had it been a profit – would have been chargeable to tax in Israel, then the following provisions shall apply to it:
- (a) a loss suffered during a tax year shall be first set off against his chargeable income, including capital gains, in the same tax year from business or vocation abroad;
- (b) if a balance of loss remained after the set off said in subparagraph (a), then the said balance shall be set off against chargeable passive income from abroad, which was left in that tax year after the set off said in paragraph (1)(a);
- (c) if a balance of loss remained after the set off said in subparagraphs (a) and (b) and the said balance of loss is in a business abroad which is controlled and managed from Israel (in this section: the controlled business), then it shall be set off – if the assessee so requests – against chargeable income produced or accrued in Israel in that tax year;
- (d) if it is not possible to set off the entire loss in that year, as said in subparagraphs (a) and (b), and if he elected that the provisions of subparagraph (c) apply to him, then the amount of a said loss that cannot be set off under subparagraphs (a) to (c) shall be brought forward to the following years, one after the other, and shall be set off against the assessee's chargeable income, including capital gains, from business or vocation abroad in those tax years;
- (e) notwithstanding the provisions of subparagraph (d), if a balance of loss remained after the set off said in that subparagraph and if the balance of loss stems from a controlled business, then the balance of loss shall be set off – if the assessee so requests – against his chargeable income, including capital gains or land appreciation



within its meaning in the Real Estate Taxation Law, from business or vocation in Israel; an amount set off as aforesaid shall not be carried forward for setting off in subsequent tax years under the provisions of subparagraph (d);

- (3) set off shall not be permitted of a loss suffered abroad by an Israel resident, for which – had it been a profit – no tax would have been payable in Israel;
- (4) section 28(c) shall also apply, mutatis mutandis, to the subject of this section;
- (5) a loss said in this section shall be allowed to be set off only if a return, as said in sections 131 and 132, was submitted to the Assessing Officer for the tax year in which the loss was suffered;
- (6) the Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions for the implementation of this section, inter alia on the matter of how to prove the loss.

#### **Article Four: General Provisions**

##### **Restriction on deductions**

30. No deduction shall be allowed for expenses under sections 17 to 27 in an amount greater than was necessary for the production of the assessee's income; any question on the subject of this section shall be decided by the Director, but nothing in this section shall be construed as preventing a person, who considers himself aggrieved by the Director's decision, from appealing against it in accordance with the provisions of sections 153 to 158.

##### **Regulations on the deduction of expenses**

31. The Minister of Finance may, with approval by the Knesset Finance Committee, make regulations – whether in general or for particular categories of assessees – on the limitation or disallowance of the deduction of certain expenses under sections 17 to 27, and in particular on –
- (1) the method of calculating or estimating expenses;
  - (2) the amounts or rates of deductible expenses;
  - (3) the conditions for allowing expenses;
  - (4) the manner of proving expenses.

##### **Deductions that are not to be allowed**

32. In determining the chargeable income of a person, deductions shall not be allowed in respect of –
- (1) household or private expenses;
  - (2) payments or expenses, which are not money wholly and exclusively expended for the production of income;
  - (3) capital withdrawn or a sum used or intended to be used as capital;
  - (4) the cost of improvements;
  - (5) any loss or expense which is recoverable under insurance or under a contract of indemnification;
  - (6) rent for and the cost of repairs of premises or of any part thereof, which were paid or incurred not for the purpose of producing income;
  - (7) amounts paid or payable as income tax;
  - (8) repealed
  - (9) (a) (1) payment of amounts of grant in consequence of retirement or in consequence of death, which are exempt of tax under

section 9(7a), paid by a company controlled by not more than five persons, within its meaning in section 76, to a controlling member or to another in his stead, in respect of years of employment up to the year 1975;

- (2) payments to a benefit fund paid by a company said in subparagraph (1) for a member, except payments to a benefit fund for severance pay or pension at rates and on conditions prescribed under section 22 of the Control of Benefit Funds Law, but not more than NS 10,500 (*in 2008; in 2007: NS 10,220; in 2006: NS10,250; in 2005: NS9,980 – Tr.*) and exclusive of payments to a training fund, and provided that deductions of a sum in excess of 4.5% of the member's determining salary shall not be allowed; the provisions of subparagraphs (1) and (2) shall also apply to a person, if two years have not yet elapsed since the day on which he ceased being a member; notwithstanding the provisions of this paragraph, the Director may direct otherwise if he sees fit to do so under the circumstances;

for this purpose:

**"controlling member"** – a person who, directly or indirectly, alone or with a relative holds one of the following:

- (a) at least 10% of the issued share capital or at least 10% of the voting power;
- (b) the right to hold at least 10% of the issued share capital or at least 10% of the voting power, or the right to acquire them;
- (c) the right to receive at least 10% of the profits;
- (d) " the right to appoint a director;

**"relative"** – within its meaning in section 76(d);

**"member"** – a controlling member who has, alone or together with his spouse, or whose spouse has, directly or indirectly, not less than 5% of the issued share capital, or of the voting power, or of the right to hold or to acquire each of these, or of the right to receive profits; however, the rights of a spouse that was acquired before marriage or inherited shall not be taken into account for this purpose:

**"determining salary"** – as defined in section 3(e);

- (b) the provisions of subparagraph (a) shall not apply to the amount of a grant in consequence of death, which is exempt of tax under section 9(7a), or to an amount of grant in consequence of death which does not exceed NS 10,220 (*in 2007; in 2006: NS10,250; in 2005: NS9,980 – Tr.*) per working year, whichever is the smaller amount.
- (10) (a) premiums paid by a company to insure the life of a controlling member in its own favor, within its meaning in paragraph (9), except aforesaid premiums paid to a benefit fund;
- (b) premiums paid by a partnership in its own favor to insure the life of a partner, or paid by a partner in his own favor to insure the life of his partner, when the insured person has at least 10% of the capital of the partnership or of the right to its profits;
- (11) expenses in respect of a benefit granted by an employer to his employees which cannot be attributed to a particular employee, except for expenses that by their nature are proved not to be intended to confer personal benefits on an employee; expenses within the limits of amounts prescribed in regulations under section 31 for the maintenance of a

vehicle in the employer's possession and used by his employees and the benefit of its use cannot be related to a certain employee; expenses that cannot be deducted as aforesaid shall be deemed work income of the employees.

- (12) amounts paid for an activity which is prohibited under sections 5A and 5B of the Wireless Telegraph Ordinance [New Version], 5732-1972;
- (13) payments paid as supplements under section 179 of the National Insurance Law [Consolidated Version] 5728-1968;
- (14) (a) expenditures for the acquisition of insurance against loss of working capacity;  
(b) notwithstanding the provision of subparagraph (a), if the income in respect of which insurance against loss of working capacity was acquired is income under section 2(1) or (2), and if the insurance is preferential insurance, then deductions will be allowed for expenditures for the acquisition of the preferential insurance up to 3.5% of the income under section 2(1) or of the employee's salary, as the case may be, which is liable income, on condition that deductions under this subparagraph not be allowed in respect of the said income that exceeds the amount that equals the total average wage in the economy in the tax year, divided by three; however, if the employer paid for his employee to a benefit fund on account of the employer's benefit component an amount that exceeds 4% of the employee's salary, then the differential between the rate paid as aforesaid by the employer in respect of income under section 2(2) and 4% shall be subtracted from the rate said in the opening passage;  
for the purpose of this paragraph: "**preferential insurance**" – insurance against loss of working capacity, and if the insurance was acquired before the insured person had reached age 60, if the following two conditions also hold true for the insurance:
  - (1) the insurance period – other than group insurance – continues at least until the insured person reaches age 60;
  - (2) if the insurance event occurs before the insured person reaches age 60, then the moneys under the insurance will be paid from the date on which the insurance event occurred until the end of the period of loss of working capacity or until the insured person at least reaches age 60, whichever comes first;"**insurance against loss of working capacity**" – as defined in section 3(a);  
"**average wage in the economy**" and "**employer's benefit component**" – as defined in section 3(e3)(2);  
"**salary**" – work income other than the value of the use of a vehicle made available to the employee;
- (15) educational expenses, including expenses for the acquisition of an academic education or for the acquisition of a profession, other than expenses for supplementary professional training that is not for the said acquisition of an education or profession, but for the maintenance of the what exists.

#### **Restrictions on deductibility and on reduction of advances because of faulty returns**

32A. Notwithstanding the provisions of any statute, an assessee shall not be allowed to deduct expenses or to reduce advance payments under section

175(d) in respect of payments to which the obligation to deduct at the source applies, unless returns which the assessee must submit under sections 161, 166 or 171, as the case may be, have been submitted to the Assessing Officer, in which are stated the name, address and identity number of the person to whom or for whom payments were made, and in respect of a body of persons – another identifying number, all in an accurate manner that enables the Assessing Officer to identify the payment's recipient.

**Restriction on deductions, credits and set-offs because of unacceptable books**

33. (a) The Assessing Officer may refuse to allow the deduction of expenses according to accounts submitted by an assessee who did not keep acceptable books, and he may assess the expenses to the best of his judgment.
- (b) If an assessee did not keep acceptable books in a particular tax year, then he shall not be allowed to set-off losses from earlier years against his income in that year, and if the assessee was required to keep books in a particular tax year and his books were found to be unacceptable under aggravating circumstances, then no deductions or set-offs shall be allowed him in that year for bad debts and losses and a loss for that year shall not be recognized.
- (c) If an assessee was required to keep books in a particular tax year and did not keep books, or kept books but did not base his return on them, then in that year he shall not be allowed deductions and set-offs for depreciation, interest, lost debts and losses, and a loss for that year shall not be recognized.
- (d) If an assessee was required to keep books in a particular tax year and did not keep acceptable books, then in that tax year he shall not be allowed a tax credit under section 121A.

**CHAPTER THREE: DEDUCTIONS, CREDITS  
AND CHILDREN'S PENSIONS**

**Definitions**

33A. In this Chapter –

**"credit point"** – an amount of NS 2,136 (*in 2004 to 2008 – Tr.*), linked to the index as said in section 120A, set off against the tax for that year; (*Amendment No. 136 provides that the underlined words shall not apply in tax years 2005 to 2008; however, if at any time during those years the index rises to more than 5% above the index known on January 1, 2004, then this reservation no longer applies, beginning with the next following tax year – Tr.*)

**"pension point"** – an amount equal to the amount of a credit point, at its value on December 31, 1996, adjusted under the provisions of section 120B in respect of pension points and divided by twelve.

**Credit for Israel resident**

34. Two credit points shall be taken into account in calculating the tax of an individual who was an Israel resident in the tax year.

**Credit for oleh**

35. (a) In calculating the tax of an oleh (*new immigrant – Tr.*), the following shall be taken into account –
- (1) 1/4 credit point for each of the first eighteen months after his aliyah (*immigration – Tr.*) to Israel;

- (2) 1/6 credit point for each of the twelve months thereafter;
- (3) 1/12 credit point for each of the twelve months thereafter.
- (b) If the chargeable income of a registered spouse includes income of his spouse who is an **oleh** and if the tax on their income is calculated jointly, then the credit points said in subsection (a) shall be taken into account, but if the income of the spouse who is not the registered spouse does not exceed an amount equal to five times the amount of the credit points said in subsection (a) and in section 38, then the income of the spouse who is not the registered spouse shall not be included in the chargeable income of the registered spouse and the said credit points shall not be taken into account in calculating the tax of the registered spouse.
- (c) The said credit shall be granted for a tax year wholly or partly within the period of the said 42 months, according to the number of months that the **oleh** resided in Israel in that year, and it shall only be granted the first time he becomes an **oleh**; on his application, a consecutive period of absence from Israel of not less than six months and not more than three years shall not be included in the count of 42 months.
- (d) In this section, "**oleh**" – a person who holds an **oleh's** visa or an **oleh's** certificate under the Law of Return 5710-1950, or a person entitled to a said visa or certificate who holds a visa and permit of temporary residence under the Entry into Israel Law 5712-1952, or a person who belongs to a category of persons who the Minister of Finance determined shall for the present purpose be treated like **olim**, but exclusive of a person whose Israel citizenship was withdrawn under section 10(d) of the Citizenship Law 5712-1952.
- (e) Notwithstanding the provisions of subsection (c), the Minister of Finance may, with approval by the Knesset Finance Committee, prescribe –
  - (1) rules for the grant of credits under subsection (a) to a person who in the past came within the definition of **oleh**;
  - (2) other provisions, either generally or in respect of particular cases, on the beginning of the 42 month period and the interruption of its continuity.

#### **Credit for travel to place of work**

36. In calculating the tax of an individual Israel resident, 1/4 credit point shall be taken into account as a travel credit.

#### **Credit for women**

- 36A. In calculating the tax of a woman, 1/2 credit point shall be taken into account.

#### **Credit for a spouse**

37. In calculating the tax of a beneficiary individual Israel resident, who proved to the Assessing Officer's satisfaction that he supported his spouse during the tax year, one credit point shall be taken into account; for purposes of this section, "**beneficiary individual**" – an individual, if he or his spouse has reached the retirement age, or if he or his spouse is blind or disabled within the meaning of those terms in section 9(5)(a).

#### **Credit for a working spouse**

38. (a) If the chargeable income of an individual Israel resident, who is a registered spouse, includes the income of his spouse, and if it is proved to the Assessing Officer's satisfaction that his spouse's income was obtained by personal exertion from any business or vocation or from

employment, including income from personal exertion as said in paragraphs (1) to (6) of its definition in section 1, then in calculating his chargeable income 1/4 credit point shall be taken into account under section 36, 1 1/2 credit points if they are not entitled to a pension point under section 40(a) and 1 3/4 credit points if they are entitled to an aforesaid pension point, and in respect of a beneficiary individual, as defined in section 37, a credit point said in that section shall also be taken into account.

- (b) Notwithstanding the provisions of subsection (a), if the income of the spouse who is not the registered spouse does not exceed an amount equal to five times the amount of the said fractional credit points, as the case may be, then the income of the spouse who is not the registered spouse shall not be included in the chargeable income of the registered spouse and the said fractional credit points shall not be taken into account.

#### **Credit for spouse who helps**

- 39. In calculating the tax of an individual Israel resident whose spouse helps him in obtaining his income from any business or vocation during at least 24 hours in each week during nine months of the tax year, then 1 1/2 credit points shall be taken into account if he is not entitled to a pension point under section 40(a) and 1 3/4 credit points if he is entitled to an aforesaid pension point, and in respect of a beneficiary individual, as defined in section 37, a credit point said in that section shall also be taken into account, provided that – if in respect of his spouse he is also entitled to credits under section 38, then he shall be granted the credits under one of the two sections, at his choice.

#### **Credit for discharged soldier**

- 39A. In calculating the tax on the income from personal exertion of a discharged soldier, part of a credit point shall be taken into account for each month of the first 36 months after the month in which he concluded his regular service, as specified below:
  - (1) 1/6 of a credit point – if he or she served regular service –
    - (a) if a man – of at least 23 whole months;
    - (b) if a woman – of at least 22 whole months'
  - (2) 1/12 of a credit point – if he or she served regular service –
    - (a) if a man – of less than 23 whole months;
    - (b) if a woman – of less than 22 whole months;for this purpose: "**discharged soldier**" and "**regular service**" – as defined in the Absorption of Discharged Soldiers Law 5754-1994.

#### **Pension and credit points for children**

- 40. (a) An individual Israel resident is entitled to pension points for each of his children, as prescribed in section 109 of the National Insurance Law [Consolidated Version] 5728-1968; the pension points shall be paid by the National Insurance Institute under the National Insurance Law.
- (b) (1) If an Israel resident individual, who is the parent of a single parent family, has children who during the tax year had not yet reached age 19 and were maintained by him, but is not entitled to credit points under section 37, then, in calculating his tax, in addition to the pension points under subsection (a) in respect of the children who live with him, 1/2 credit point shall be taken into account in

respect of each child in the year of its birth and in the year of its maturity, and one credit point in respect of each child beginning with the tax year after the year of its birth until the tax year before the year of its maturity; and in respect of his being the parent of a single parent family – one additional credit point only.

- (2) If parents live separately and the maintenance of their children is shared by them, then the parent who is not entitled to a credit point under paragraph (1) shall receive one credit point or part thereof, according to his share in the maintenance.
- (3) For purposes of this subsection:  
"year of birth" – the tax year in which the child was born;  
"year of maturity" – the tax year in which the child reached age 18.

#### **Credit point for divorced man who has remarried**

40A. In calculating the tax of a divorced person who pays, or whose spouse pays maintenance to his former spouse and who is married to another spouse, one credit point shall be taken into account.

#### **Credit point for a juvenile**

40B. In calculating the tax of an individual, if he or his spouse has reached age 16, but has not yet reached age 18, one credit point shall be taken into account.

#### **Half a credit point for individual who completed studies for a bachelor's or master's degree**

- 40C. (a) In calculating the tax of an individual Israel resident (in this section: individual) a credit point shall be taken into account, if he is entitled to receive a bachelor's degree and half a credit point if he is entitled to receive a master's degree from an institution of higher education.
- (b) The credit point or half credit point said in this section, as the case may be, shall be taken into account during a number of years equal to the number of years of his academic studies, on condition that not more than three tax years be taken into account for studies for a bachelor's degree and not more than two tax years for studies for a master's degree.
  - (c) One credit point said in this section for studies for a bachelor's degree shall be taken into account beginning with the tax year after the tax year in which his studies for the bachelor's degree were completed, and half the credit point for studies for the master's degree beginning with the tax year after the tax year in which his studies for the master's degree were concluded.
  - (d) Notwithstanding the provisions of subsections (a) to (c) –
    - (1) if the individual is entitled to receive a doctorate in medicine or dentistry, then a credit point shall be taken into account during three tax years and half a credit point during two tax years, beginning with the tax year after the tax year in which his studies for the degree of doctor were concluded;
    - (2) if the individual studied in a direct program towards the degree of doctor, then one credit point for studies for a bachelor's degree shall be taken into account beginning with the tax year after the tax year in which his studies for the bachelor's degree were concluded, and during the number of tax years said in subsection (b) in respect of studies for the bachelor's degree; furthermore, half a credit point shall be taken into account during two tax years,

beginning with the tax year after the tax year in which his studies for the doctorate were concluded.

- (e) The credit point or the half credit point said in this section, as the case may be, shall be taken into account for studies toward only one bachelor's degree or only one master's degree, and after the individual presented to the Assessing Officer certification that he had completed his studies and that he is entitled to the said degree.
- (f) in this section –  
    **"Council of Higher Education Law"** – the Council of Higher Education Law 5718-1958;  
    **"institution of higher education"** – within its meaning in the Council of Higher Education Law;  
    **"degree"** – a recognized degree, within its meaning in the Council of Higher Education Law.

#### **Half a credit point for concluding professional studies**

- 40D. (a) In calculating the tax of an individual Israel resident, half a credit point shall be taken into account, if he completed professional studies and is entitled to a professional certificate, on condition that he submitted certification of the conclusion of his studies and of his entitlement to the said professional certificate to the Assessing Officer.
- (b) The half credit point said in this section shall be taken into account during a number of tax years that is equal to the number of years of professional studies, on condition that it be taken into account in not more than three years.
- (c) The half credit point said in this section shall be taken into account beginning with the tax year after the tax year in which his studies were concluded.
- (d) In this section,  
    **"professional studies"** – studies for a certain profession, with a study program identical at least with the 1,700 study hours common at institutions of higher education, as defined in section 40C;  
    **"professional certificate"** – a certificate awarded at the conclusion of professional studies and recognized by a Government Ministry.

#### **No duplication**

- 40E. If the conditions set in section 40C and 40D hold true for an individual, then he shall be entitled to choose whether a credit point or half a credit point be taken into account in the calculation of his tax under section 40C or half a credit point under section 40D.

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*Note: Section 72 of Amendment No. 147 inserts the following section 40F, with effect in tax years 2005 and 2006:*

#### **Credit point for person who returned to work**

- 40F. In the tax calculation of an individual Israel resident one sixth of a credit point shall be taken into account per month of work, in the course of six consecutive months of work, if all the following hold true:
- (1) before the month, in respect of which he claimed the credit said in this section, he had work income in at least six consecutive months;
  - (2) the employment in respect of which he had the work income said in paragraph (1) began between July 1, 2005, and June 30, 2006;
  - (3) before he began to work, as said in paragraph (2), he did not have any work income during at least twelve consecutive months;
  - (4) during the period of 36 months that preceded the period said in



paragraph (3) he had work income during at least twelve consecutive months;  
for the purposes of this section:  
"work income" – income under section 2(1) or (2);  
"work" – includes engagement in a business or vocation.

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#### **Spouse who was married during part of the year**

41. If a spouse who is not a registered spouse was married during part of the tax year, then – for purposes of calculating the tax to which he is liable – he shall be entitled –
- (1) in respect of the period in which he was not married – to one twelfth of the credit points under sections 34, 36, 40(b) and 40B, multiplied by the number of months of the tax year during which he was not married;
  - (2) in respect of the period in which he was married – to one twelfth of the credit point under section 66, multiplied by the number of months of the tax year during which he was married.

42 and 43 – Repealed

#### **Credit for expense of maintaining a relative in an institution**

44. In calculating the chargeable income of an individual Israel resident, if during the tax year he or his spouse paid for the maintenance of a completely paralyzed, permanently bedridden, blind or mentally unsound child, spouse or parent and also of a retarded child, in a special institution, then a 35% tax credit shall be allowed on that part of the amounts paid that exceed 12.5% of his chargeable income; the Minister of Finance may, by regulations, set conditions for entitlement to tax credits under this section. (*Ceiling of entitling income: in 2008: NS 144,000 for an individual, NS 230,000 for a couple; in 2006 and 2007: NS140,000 and NS224,000; in 2005: NS136,000 and NS 218,000 – Tr.*)

#### **Credit for incapacitated persons**

45. (a) If an Israel resident had a paralyzed, blind or retarded child during the tax year, or if his spouse had an aforesaid child, then in calculating his or his spouse's tax two credit points shall be taken into account for each such child.
- (b) repealed
- (c) An individual shall be entitled to credit points under subsection (a) only if he did not receive tax credit under section 44 for the same child.
- (d) The Minister of Finance may set conditions for entitlement to credit points under this section. (*Ceiling of entitling income: in 2008: NS144,000 for an individual, NS 230,000 for a couple;; in 2006 and 2007: NS140,000 and, NS224,000; in 2005: NS136,000 and NS 218,000 – Tr.*)

#### **Credit for insurance premiums and benefit fund contributions**

- 45A. (a) An individual shall be given a tax credit of 25% of the amount paid by him or his spouse in the tax year –
- (1) for insuring his life or the life of his spouse with an insurance company, if he is an Israel resident;
  - (2) as payment to a benefit fund to the credit of one of them, other than payments to a pension benefit fund and other than payments to a benefit fund which is a training fund.
- (b) An individual shall be given a tax credit of 35% of the amounts he or his spouse paid in the tax year to a pension benefit fund, or which they paid

- as aforesaid to the State, to a local authority or to some other body designated by the Minister of Finance in order to maintain his or his spouse's pension rights, or paid as aforesaid for survivors' pension insurance.
- (b1) A beneficiary member shall receive a tax credit, as said in subsections (a) and (b), also for amounts he paid for the insurance of his child's life in an insurance company, to a benefit fund to his child's credit or for the maintenance of his child's pension rights, subject to the conditions said in those subsections, as the case may be, on condition that in that tax year that child was of age eighteen or older.
- (c) In this section –  
**"life insurance"** – insurance against the risk of the insured person's death, without any savings component, which does not include pension payments to survivors;  
**"survivors' pension insurance"** – insurance against the risk of the insured person's death, without a savings component, which includes pension payments to survivors;  
**"insured income", "entitling income" and "beneficiary member"** – as defined in section 47.
- (d) Notwithstanding the provisions of subsections (a) and (b), the total amount in respect of which credit shall be given to an individual who is not a beneficiary member for amounts paid as said in those subsections shall not exceed the larger of the amounts specified below:  
(1) the amount of NS 1,728 (*in 2008; in 2007: NS 1,680 – Tr.*);  
(2) the lower of the following two amounts:  
(a) the total of amounts paid as said in subsections (a) and (b);  
(b) (1) in respect of an individual who had no work income in the tax year – 5% of his entitling income, provided that the total amount for which he shall be given credit for payments for survivors' pension insurance, as said in subsection (b) not exceed 1.5% of the individual's entitling income;  
(2) in respect of an individual who did have work income in the tax year – 7% of his entitling income, provided that the total amount, in respect of which credit will be given for amounts paid for survivors' pension insurance as said in subsection (b) not exceed 1.5% of the individual's entitling income, and that the total amount for which credit shall be given in respect of the amounts paid for life insurance as said in subsection (a)(1), for survivors' pension insurance as said in subsection (b) and in respect of income that is not from work shall not exceed 5% of the individual's entitling income;
- (e) Notwithstanding the provisions of subsections (a) to (b1), the total amount in respect of which credit shall be given to a beneficiary member for amounts paid as said in those subsections shall not exceed the larger of the amounts specified below:  
(1) the amount of NS 1,680 (*in 2008 – Tr.*);  
(2) the lower of the following two amounts:  
(a) the total of amounts paid as said in subsections (a) to (b1);  
(b) (1) in respect of a beneficiary member who did not have insured income in the tax year – 5% of his chargeable income up to the amount of NS 180,096 (*in 2008; in*

2007: NS175,200 – Tr.) per year, on condition that the total amount, in respect of which credit will be given for amounts paid for survivors' pension insurance, as said in subsection (b), not exceed 1.5% of the beneficiary member's entitling income;

- (2) in respect of a beneficiary member who did have insured income in the tax year – the amount obtained by adding the amounts specified below:
  - (a) 7% of his entitling income that is insured income, on condition that the total amount in respect of which credit will be given for amounts paid for survivors' pension insurance, as said in subsection (b), not exceed 1.5% of his said income, and that the total amount in respect of which credit will be given for amounts paid for life insurance under subsections (a)(1) and (b1) and for survivors' pension insurance under subsection (b) does not exceed 5% of his said income;
  - (b) 5% of his chargeable income that is not insured income, up to the amount of NS 180,096 (*in 2008; in 2007: NS172,800 – Tr.*) per year, less the amount of NS 88,800 (*in 2008; in 2007: NS86,400 – Tr.*) or the amount of his insured income, whichever is the smaller amount, on condition that the total amount, in respect of which credit will be given for amounts paid for survivors' pension insurance, as said in subsection (b), does not exceed 1.5% of his liable income that is not insured income.

45B. Repealed

#### **Contribution to a public institution**

- 46. (a) If a person contributed in a certain tax year an amount in excess of NS 380 (*in 2006 and 2007 – Tr.*) to a national fund or to a public institution within its meaning in section 9(2) and designated for this purpose by the Minister of Finance with approval by the Knesset Finance Committee, then he shall be credited to the tax he owes in that year in the amount of 35% of the amount of the contribution, if he is an individual, and at the percentage of the contribution prescribed in section 126(a) if it is a body of persons, but in no tax year shall credit be given for a total amount of contributions in excess of 30% of the assessee's chargeable income in that year, or in excess of NS 4,013,000 (*in 2008; in 2007: NS 4,000,000; in 2006: NS 2,218,000; in 2005: NS 2,165,000 – Tr.*), whichever is less (hereafter: credit ceiling); any amount contributed in that tax year in excess of the credit ceiling shall be credited against tax in accordance with the provisions of this section during the following three tax years, one after the other, on condition that in each of the said three tax years no credit be allowed in respect of a total amount of contributions in excess of the credit ceiling.
- (a1) If a public institution said in subsection (a) did not submit two successive annual reports, or if the submitted reports show that it does not duly keep books or that a substantive part of its activity is not for a public purpose,

- then the Minister of Finance may cancel its designation for purposes of subsection (a).
- (a2) The renewal of a designation, which was canceled as said in subsection (a1), requires approval by the Knesset Finance Committee.
  - (b) The amounts in subsection (a) shall be adjusted in every tax year, according to the rate of index increase from the index published in August before the tax year to the index published in August of the tax year; the minimum amount increased as aforesaid shall be rounded off to the nearest sum that is a multiple of NS 10, and the maximum amount increased as aforesaid shall be rounded off to the nearest sum that is a multiple of NS 1000; the Director shall publish a notice in Reshumot on the amounts increased and rounded off as aforesaid.
  - (c) In this section, "**national fund**" – the Jewish Agency for Israel, the World Zionist Organization, the United Israel Appeal and the Jewish National Fund.
  - (d) (1) If the account books of a public institution were declared unacceptable, and if that determination is no longer subject to objection or appeal, then the Director may cancel the designation under subsection (a) from that day forward.
  - (2) The institution shall inform the public of a said cancellation, at the time and in the manner prescribed by the Director.

#### **Overall ceiling on tax benefits for contributions and R&D**

46A. Notwithstanding the provisions of any statute, the total amount in respect of which a credit will be allowed in a certain tax year for contributions under section 46 and a deduction for participation in the financing of research and development carried out by another person under section 20A and under the Income Tax Law (Benefits for Securities that Finance Scientific Research and Development) 5744-1983, shall not exceed 50% of the assessee's chargeable income in that year; for this purpose: "**chargeable income**" – before the deduction for participation in research and development.

#### **Credit for contribution – addition to base for advance payments**

46B. The amount of tax, from the payment of which a person was exempted because of contributions under section 46 and under any other statute, shall be added to the amount of tax that serves as base for the determination of his advance payments under section 175.

#### **Deduction of payments, benefits or pensions**

47. (a) In this section –
- (1) "**entitling income**" – the total chargeable income of an individual, before the deduction under this section and under section 47A, as specified below, as the case may be:
    - (1) in respect of an individual who only had work income – up to the amount of NS 88,800 per year (*in 2008; in 2007: NS 86,400 – Tr.*);
    - (2) in respect of an individual who had no work income – up to the amount of NS 126,000 per year (*in 2008; in 2007: NS 122,400 – Tr.*);
    - (3) in respect of an individual who had work income and income that is not work income, in respect of the work income – up to the amount said in paragraph (1), and in respect of the income that is not work income – up to the amount said in paragraph (2), less his work income, or less the amount said

- in paragraph (1), whichever is less, on condition that his work income be taken into account first;
- (2) repealed
  - (3) **"income of a self-employed member"** – the individual's total liable income before the deduction under this section and under section 47A, up to the amount of NS 90,000 per year (*in 2008; in 2007: NS 86,400 – Tr.*), less his insured income;
  - (4) **"insured income"** – work income, in respect of which the employer paid for his employee during the tax year amounts to a savings benefit fund or to a pension benefit fund, and also work income in respect of which the employee is entitled to a pension under a statute or contract;
  - (5) **"additional income"** – the smaller of the following amounts:
    - (1) an individual's total liable income before deduction under this section and under section 47A, which is not insured income, up to the amount of NS 90,000 per year *in 2008; (in 2007: NS 86,700 – Tr.)*;
    - (2) the individual's total liable income before the deduction under this section and under section 47A up to the amount of NS 360,000 (*in 2008; in 2007: 345,600 – Tr.*) per year, less his insured income or the amount of NS 90,000 (*in 2008; in 2007: NS 86,400 – Tr.*), whichever is larger;
  - (6) **"individual member"** – an individual who is not a beneficiary member, for whom one of the following holds true:
    - (1) he was born before 1961;
    - (2) during the tax year he had work income, in respect of which he is entitled to a pension under a statute or contract;
  - (7) **"beneficiary member"** – an individual, in respect of whose income amounts were paid for him during the tax year to a pension benefit fund in an amount that was not less than 16% of the average wage in the economy in that tax year;
  - (8) **"average wage in the economy"** – as defined in section 3(e3)(2).

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*Under the provisions of section 6 of Amendment No. 153, the above paragraph (8) shall be read as follows:*

*in tax year 2007:*

- (8) **"average wage in the economy"** – 90% of the average wage in the economy, as defined in section 3(e3)(2).

*in tax year 2008:*

- (8) **"average wage in the economy"** – 95% of the average wage in the economy, as defined in section 3(e3)(2).
- 

- (b) If during the tax year an individual member or his spouse paid to a benefit fund for pension or benefits for the benefit of one of them, or if during the tax year amounts an individual who is not a beneficiary member or his spouse paid only to a pension benefit fund for the benefit of one of them – also if he directed that after his death his right be transferred to an institution recognized as a public institution for purposes of section 9(2) – or if they paid as aforesaid to the State, to a local authority or to another body designated by the Minister of Finance, in order to maintain the pension right of one of them, then the amounts paid as aforesaid shall be deductible, on condition that the deduction

does not exceed –

- (1) 7% of his entitling income other than work income; however, if he paid only for a pension and the amount paid exceeds 12% of his aforesaid income, then – in respect of the part in excess of 12% – he shall be allowed an additional deduction of up to 4% of that income;
  - (2) the lower of these amounts:
    - (a) 5% of his entitling income which is work income that is not insured income;
    - (b) 5% of his liable income that is work income, up to an amount of NS 360,000 (*in 2008; in 2007: NS 345,600 – Tr.*) per year, less his insured income;
- (b1) if, during the tax year, a beneficiary member or his spouse paid amounts to a savings benefit fund or to a pension benefit fund to the beneficiary member's credit, and if a beneficiary member during the tax year paid said amounts to the credit of his child, who in the tax year was aged 18 or more, then he shall be allowed to deduct the amounts paid as aforesaid, on condition that the deduction not exceed the following, as the case may be:
- (1) in respect of amounts paid to a pension benefit fund – 11% of the income of a self-employed member;
  - (2) in respect of amounts paid to a pension benefit fund for which deduction was not allowed under paragraph (1), and in respect of amounts paid to a savings benefit fund – 7% of the additional income; however, if the amounts paid as aforesaid to a pension benefit fund exceed 12% of his additional income, then in respect of the part in excess of the said 12% he shall be allowed an additional deduction that shall not exceed 4% of the additional income, all on condition that no deduction be allowed under this paragraph in respect of amounts deposited for the beneficiary member with a pension benefit fund, the amount of which does not exceed 16% of the average wage in the economy.
- (b2) An amount deducted under subsection (b) is not deductible under subsection (b1), and vice versa.
- (c) An amount deducted under subsection (b) or (b1) shall not be taken into account for the purposes of section 45A.
- (d) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe for particular categories of persons deductions at rates higher than those said in subsection (b), on conditions and with restrictions which he shall prescribe,

#### **Deduction for National Insurance and parallel tax payments**

- 47A. (a) If in a tax year an individual paid insurance contributions under the National Insurance Law [Consolidated Version] 5728-1968 (hereafter: "the Insurance Law") and parallel tax under the Parallel Tax Law 5733-1973 (hereafter: "parallel tax") in respect of income that is not work income, then he shall be allowed a deduction of 52% of the amounts paid by him, except for supplementary payments under section 179(a) of the Insurance Law, provided that the deduction does not exceed his chargeable income before the deduction.
- (b) The provisions of subsection (a) shall also apply to an individual whose employer is not obligated to pay parallel tax for him or to pay National Insurance contributions for him, and who is obligated to pay them in respect of his own work income.

- (c) If an individual's employer is not obligated to pay parallel tax for him and he himself also is not obligated to pay parallel tax, and also if another individual is exempt of paying parallel tax, then he shall be allowed to deduct 52% of the amounts which he paid for health insurance – other than dental health insurance – to a body designated by the Minister of Finance after consultation with the Minister of Health, up to the amount of parallel tax which would have applied to him, had he been obligated to pay it.
- (d) The provisions of this section in respect of the Parallel Tax Law shall only apply to the period that ends on December 31, 1996.

47B. Repealed

#### **Remuneration and refund of expenses paid to pension counselor as payments to a benefit fund**

- 47C. (a) The Minister of Finance may prescribe conditions, under which – for the purposes of sections 3(e3), 17(5a), 45A and 47 – remuneration and the refund of expenses paid to a pension counselor shall be treated like payments to a benefit fund; if the Minister of Finance prescribed as aforesaid, then the conditions, ceilings and restrictions prescribed in the said sections shall apply, mutatis mutandis, to the remuneration and the refund of expenses paid as aforesaid.
- (b) In this section, "**pension counselor**" – as defined in the Control of Financial Services ( Pension Counseling and Pension Marketing) Law 5765-2005.

#### **Credits for residents of an area**

48. The Minister of Finance may prescribe, by Order with approval by the Knesset Finance Committee, that all or some of the provisions of sections 34, 36 and 37 also apply – mutatis mutandis – to some or all residents of an area who are not Israel citizens, as if they were Israel residents; for this purpose: "**area**", "**resident of an area**" and "**Israel citizen**" – as defined in section 3A.

#### **Credits for a foreign worker**

- 48A. The Minister of Finance may prescribe that some or all of the provisions of this Chapter on credits shall not apply to foreign employees or to categories of foreign employees designated by him, or that they apply to them partly on conditions he shall prescribe; for this purpose: "**foreign employee**" – as defined in the Foreign Employees (Prohibition of Unlawful Employment and Assurance of Fair Conditions) Law 5751-1991, even if for purposes of this Ordinance he is deemed a resident.

## **PART FOUR: CALCULATION OF INCOME IN SPECIAL CASES**

### **CHAPTER ONE: INSURANCE COMPANIES**

#### **General insurance companies**

49. (a) Notwithstanding the provisions of this Ordinance, if a company carries on a general insurance business, whether its earnings or profits are

derived wholly in Israel or partly in Israel and partly outside Israel, then its earnings or profits on which tax is due shall be determined in the following manner:

- (1) from the total amount of gross premiums and interest and other income received or receivable in Israel shall be deducted the total of premiums returned to insured persons and paid for reinsurance;
  - (2) from the balance computed as aforesaid shall be deducted a reserve for risks unexpired at the end of the tax year, calculated at the percentage adopted by that company for those risks in relation to all its business; and to it shall be added the balance of the reserve so calculated for risks unexpired at the beginning of the tax year, on condition that the percentage adopted shall not exceed a percentage reasonable and appropriate in each particular case;
  - (3) from the net amount computed under paragraph (2) shall be deducted –
    - (a) the amount of actual losses, less the amount recovered in respect of those losses under reinsurance;
    - (b) management and agency expenses in Israel;
    - (c) a fair share of the expenses of the head office, which is outside Israel.
- (b) If, during any period within the tax year or the year before it, the company actually discontinued its business in Israel in any category of insurance, then no reserve shall be deducted in respect of that category of insurance.

#### **Life insurance companies**

50. Notwithstanding the provisions of this Ordinance, if a company carries on a life insurance business, either exclusively or in addition to general insurance (hereafter: life insurance company), then its profits from life insurance business shall be taken to be equal to the amount of profits calculated according to section 49, while creating the reserves according to actuarial calculation and mutatis mutandis as the case may be, on condition that no reserves be allowed in an amount that exceeds the amount of reserves calculated on the basis of that actuarial calculation, which is reasonable and appropriate to each particular case.

#### **Expenses of a life insurance company**

51. Expenses incurred by a life insurance company for the acquisition of life insurance contracts, including payments to agents, shall be deemed expenses in the year in which they were incurred or transferred to the agent's credit, whether or not the company included them in its profit and loss account in respect of that year.

#### **Life insurance companies that receive premiums from abroad**

52. If a life insurance company receives most of its premiums from abroad, then its profit shall be taken to be a proportional part of its investment income, in the ratio of the amount of premiums received in Israel to the total amount of premiums received, or its actual income from investments in Israel, whichever is the larger amount, after the expenses of the branch or agency in Israel and a fair share of the expenses of the company's head office, which is located outside Israel, were deducted from the amount of the profits.

#### **Foreign insurer who received premiums from insurance in Israel**



53. If a person who is not an Israel resident carries on an insurance business and if premiums were paid to him for the insurance of assets in Israel, or for insurance against a contingency liable to arise only in Israel, or if they were paid by insured persons who are Israel residents, otherwise than through a branch or agent in Israel authorized to issue policies on his behalf, then he is deemed to have derived profits in Israel from that insurance business and those profits are deemed to be 10% of the total amount of premiums paid to him as aforesaid; however, if that person submitted to the Assessing Officer a return of his profits from the said transactions, and if that return satisfies the Income Tax Director, then those profits shall be calculated in accordance with the provisions of section 49 or sections 50 to 52, all as the case may be.

## **CHAPTER TWO: COOPERATIVE BODIES**

### **Article One: Kibbutzim**

#### **Definitions**

54. (a) In this Article –  
    **"kibbutz"** – a kibbutz or a kvutza incorporated as a cooperative society under the model rules approved by the Registrar of Cooperative Societies for societies of that category;  
    **"member"**, in relation to a kibbutz – an individual who was a member of that kibbutz at the end of the tax year.  
(b) The provisions of this Article do not derogate from the provisions of section 9(2).

#### **Assessment of a kibbutz**

55. Notwithstanding the provisions of this Ordinance, the assessment of a kibbutz and of all its members shall be made according to the provisions of sections 56 to 60.

#### **Chargeable income**

56. The value of the maintenance which the kibbutz, by virtue of membership, provided for its members and for their spouses and children who are not members, is deemed part of the chargeable income of the kibbutz and not income of its members.

#### **Tax**

57. (a) A kibbutz shall pay tax in an amount equal to the total amount of tax which its members would have to pay, if all its chargeable income were equally distributed among them and if it were their only chargeable income; for this purpose sections 34 to 46A and 47, and the provisions of Chapter Three in Part Four, except for section 66 therein, shall apply in accordance with the composition of the kibbutz members' families; however, in respect of the allowance of deductions under section 47, a member's income from outside the kibbutz, in respect of which he is entitled to benefits, a grant or a pension, shall not be taken into account.  
(b) (1) In order to calculate the tax, to which the kibbutz is liable, the kibbutz may demand that a separate calculation be made of its chargeable income after it was divided among its members under subsection (a), up to the amount of NS 43,080 (in 2008; *in 2007 – NS 41,880 Tr.*) for each married couple of kibbutz members on

condition that all the following hold true:

- (a) the two kibbutz member spouses work at entitling work;
  - (b) the following conditions prescribed in section 66(e) have been complied with –
    - (1) in paragraph (2) –
      - (a) subparagraph (a), and for this purpose it shall be read as if "at the regular place of business" had been replaced by "at entitling work";
      - (b) subparagraph (c);
    - (2) in paragraph (3);
  - (c) the kibbutz kept accurate records about the work of all kibbutz members, both within the kibbutz and outside it.  
For the purposes of this paragraph, the chargeable income of the kibbutz that was calculated for the purposes of subsection (a), less chargeable income that is not income under section 2(1) or (2), shall be deemed the chargeable income in respect of which the kibbutz may demand separate calculation.
- (2) Notwithstanding the provisions of subsection (a), the provisions of section 66(c) shall apply to the separate calculation.
  - (2a) The provisions of sections 38 and 39 shall not apply to the income, in respect of which separate calculation was demanded, as said in this subsection.
  - (3) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe additional conditions and adjustments – also on the matter of chargeable income in respect of which the kibbutz may demand separate calculation – in respect of the application of the provisions of section 66(c), and as part thereof he may designate categories of workers who shall be deemed to have worked at entitling work during 36 hours per week, all on conditions which he shall prescribe;

in this section –

**"entitling work"** – work in a branch of the kibbutz, which directly or indirectly produces income under section 2(1) or work for which income is paid under section 2(2), all on condition that it is not work that – directly or indirectly – is work of supplying daily needs of kibbutz members;

**"kibbutz"** – as defined in section 54.

### **Credit points for children**

58. A kibbutz shall be entitled to the credit points to which its members would be entitled under section 38, if the children were maintained by them.

### **Training fund for kibbutz members**

- 58A. (a) In calculating the chargeable income of a kibbutz, amounts shall be deductible that were paid by the kibbutz to training funds for kibbutz members and kept in the names of the kibbutz members, after an amount equal to 2.5% of the kibbutz' determining income was subtracted from them; the said amounts shall not exceed 4.5% of the kibbutz' determining income.
- (b) Amounts paid to a kibbutz member by a training fund for kibbutz members, as said in subsection (a), shall be deemed income for purposes of this Article when they are received, and the provisions of section 9(16a) shall apply, mutatis mutandis, as if the kibbutz member were an employee.
- (c) For purposes of this section –

**"determining income"** – the chargeable income of the kibbutz before the deduction according to subsection (a), up to an amount of NS 218,000 per year (*in 2007; in 2006: NS219,000; in 2005: NS213,000 – Tr.*), multiplied by the number of kibbutz members for whom the kibbutz pays to a training fund for kibbutz members;

**"kibbutz member"** – a member as defined in section 54, on condition that the following hold true for him:

- (1) he has reached age 21 in the tax year and has not yet reached age 70;
- (2) no amounts in addition to the amounts said in subsection (a) are deposited for him with a training fund;
- (3) he regularly and permanently works in the kibbutz or on its behalf;

**"training fund for kibbutz members"** – a training fund designated for kibbutz members.

59 and 60 – Repealed

## **Article Two: Moshavim and Agricultural Societies**

### **Moshavim shitufiyim and the like**

61. The Director may, at his discretion, direct that the provisions of Article One apply to the assessment of moshavim shitufiyim or of other cooperative societies for agricultural settlement and of their members, if it is proved to his satisfaction that the way business is conducted in the said societies is similar in character to that of a kibbutz.

### **Agricultural cooperative society**

62. A cooperative society classified as an agricultural cooperative society for purposes of the Stamp Duty Ordinance shall, in any particular tax year, be treated like a partnership for the purposes of this Ordinance, if the society so claimed in a return under section 131 in respect of that tax year, specifying the names and addresses of its members and the share of its chargeable income due to each of them in that tax year, on condition that the decision to claim as aforesaid was adopted at a general meeting of the society in compliance with its bylaws, and that a majority of its members gave their written consent thereto.

## **Article Three: Partnerships and House Property Companies**

### **Partnerships**

63. (a) If it was proven to the Assessing Officer's satisfaction that a business or vocation is carried on by two or more persons jointly, then –
- (1) the share of the partnership's income, to which each partner is entitled in the tax year, ascertained in accordance with the provisions of this Ordinance, is deemed that partner's income, and it shall be included in the return of income which he must make under the provisions of this Ordinance;
  - (2) the precedent partner – that partner whose name is the first of the

names of Israel resident partners to appear in the partnership agreement or, if that precedent partner is not active, the precedent active partner – shall, at the Assessing Officer's request, make and deliver a return of the partnership's income in every year, as ascertained in accordance with the provisions of this Ordinance, and there he shall specify the names and addresses of the other partners in the firm and the share of the said income to which each partner is entitled for that year; if none of the partners is resident in Israel, then the return shall be made and delivered by the Israel resident attorney, agent, manager or factor of the firm;

- (3) the provisions of this Ordinance on non-delivery of returns or of particulars required by notice from the Assessing Officer shall apply to the said return.
- (b) If it was not proven to the Assessing Officer's satisfaction that a business or vocation is carried on jointly by two or more persons, then the gains or profits from that business or vocation shall be deemed to have accrued to that one of the persons entitled to a share thereof, whom the Assessing Officer shall choose, and the assessment shall be made accordingly; if an assessment was made as aforesaid, then the partnership shall not be deemed a body of persons for the purposes of section 162.
- (c) No provision of this section shall prevent an Assessing Officer's decision – in the exercise of the discretion given to him by this section – from being appealed according to sections 153 to 158.
- (d) The Minister of Finance may, by Order, designate categories of partnerships that shall be deemed companies for purposes of this Ordinance; when he has so designated, then the partnership shall – for the purposes of this Ordinance – be treated like a company, and an amount distributed by the partnership to the partners shall be treated like a dividend; for this purpose: "**partnership**" – a partnership, the units of which were issued according to a prospectus and are listed for trading on the Tel Aviv Stock Exchange or on any other Exchange designated for this purpose by the Minister of Finance.
- (e) (1) The Director may order, in respect of certain limited partnerships which he designated and which have income from business under section 2(1), that all or some of the chargeable income of a limited partner, who meets all the conditions set by the Director, be deemed a capital gain under Part Five, during a period of not more than 183 days, all on conditions and with adjustments which he prescribed; for this purpose: "**limited partnership**" and "**limited partner**" – within their meaning in the Partnership Ordinance [New Version] 5735-1975.
- (2) The Minister of Finance may, in regulations with approval by the Knesset Finance Committee, extend the effect of an order made by the Director under paragraph (1) to a period, on conditions and with adjustments which he shall prescribe.

### House property companies

- 64. The income of a small company, within its meaning in section 76, all the assets and business of which is the holding of buildings, shall – on the company's application – be deemed the income of the company's members, and the apportionment of that income among some or all of the company's members for purposes of assessment shall be made as the Director may direct; if a person believes that a direction by the Director discriminates against him, then

he may appeal against it to a Court, as said in sections 153 to 158.

*NOTE: The following Article Four and section 64A were repealed by Amendment No. 132, but that repeal will only go into effect when regulations are promulgated under the provisions of section 64A1. Since those regulations – in respect of "transparent companies" – have not yet been promulgated, Article Four and section 64A on "family companies" still remain in effect. - Tr.*

## **Article Four: Family Companies**

### **Family companies**

- 64A. (a) The chargeable income and the loss of a company, the members of which are relatives who under section 76(d)(1) are deemed one person (hereafter: family company), shall be deemed – according to an application submitted to the Assessing Officer not later than one month before the beginning of a certain tax year or three months after its incorporation, all as the case may be – the income or loss of the member with the right to the largest part of the company's profits, or of the member designated by the company in its application as one of the persons with rights to the largest equal shares of its profits, his written consent having been attached to the application (in this section: the assessee), and the following provisions shall apply:
- (1) profits distributed out of the company's profits in years, in which the tax to which it is liable was calculated under this section (hereafter in this section: benefit period) shall be treated as if they had not been distributed, and that even if they were distributed after the benefit period or after the company ceased being a family company;
  - (2) if the company paid salaries or wages to its members, then it shall not have the obligation of employers to pay in their respect employers tax and savings loan;
  - (3) retirement grants or death grants paid by the company to its members in respect of the years in which it was a family company shall not be allowed as its expense and shall not constitute income for its members; payments paid by the company to benefit funds in respect of the said years shall not be recognized as expenses, and the members' wages shall not be deemed work income for purposes of section 47;
  - (4) in respect of advances, the amounts that are the basis for the assessee's and the company's advances shall be joined;
  - (5) the tax on the company's income, including advances, may be collected either from the company or from the assessee;
  - (6) losses incurred by the assessee before the benefit period cannot be set off against the company's income;
  - (7) when a share in a family company is sold, the consideration shall be reduced – for the purposes of section 88, both for the seller and the buyer – by an amount equal to that part of the profits accrued in the company during the benefit period and not distributed by it, which is proportional to the share's right to the company's profits; amounts subtracted as aforesaid shall not be deemed profits available for distribution for the purposes of section 94B.
- (a1) If, within the tax year, one of the conditions said in subsection (a) ceases to apply to the assessee, then another member, to whom the condition

applies and about whom the company gave notice when it submitted the return under section 131 for that year, shall become the assessee; if the company did not notify as aforesaid, then the company shall cease to be a family company entitled to the application of the provisions of subsection (a) (hereafter: entitled family company).

- (b) (1) An entitled family company may inform the Assessing Officer, up to the date on which the return under section 131 is submitted, that it withdraws its application to be deemed an entitled family company in the tax year to which the return refers; when the family company has informed as aforesaid it shall cease to be an entitled family company, and it shall have to pay – on the date of submission of the said return – employers tax for that year, which shall be treated – notwithstanding the provisions of section 4 of the Employers Tax Law 5735-1975 – as if it had been income tax and not a deduction for which the employer is responsible.
- (2) A company that ceased being a family company cannot apply again to be an entitled company before three tax years have passed after the year in which it ceased to be an entitled company.
- (c) The provisions of this section shall not remove a family company from being a company for the purposes of sections 9(14) and 19 and for the purposes of the Encouragement of Industry (Taxes) Law 5729-1969, other than Chapter Five thereof.

## Article Five: Transparent Companies

### Transparent company

64A1. (a) In this section –

**"shareholder"** – a member of a transparent company;

**"chargeable income"** – including land appreciation, within its meaning in the Real Estate Taxation Law;

**"transparent company"** – an Israel resident company for which all the following hold true:

- (1) it is not a public company, as defined in section 1 of the Companies Law, and under its Articles it cannot be converted into a public company;
- (2) the number of its shareholders does not exceed 50 or a larger number, if the Director so approved on conditions he set, and for this purpose spouses and their children, heirs of a shareholder or purchasers from a shareholder by an involuntary sale shall be deemed a single shareholder;
- (3) all its shareholders are individual residents of Israel;
- (4) its shares are of one category, except for shares that carry voting rights, and shareholders are not able to change the rights vested by virtue of their shares, except for changes in voting rights;
- (5) the right to the company's profits is accorded only by virtue of the shares;
- (6) a shareholder's right to profits is equal to his right to the company's assets upon its liquidation;
- (7) the company is not a financial institution, as defined in the Value Added Tax Law;
- (8) the company requested that it be deemed a transparent company, by a notice signed by all its shareholders and delivered to the

Assessing Officer within 60 days after its incorporation;  
"benefit years" – the tax years in which the company was a transparent company;

- (b) The chargeable income of a transparent company, including its income from dividends and its losses, shall – for the purposes of tax calculation, the tax rate and the set off of losses, and also for purposes of tax exemption – be deemed the income or loss of its shareholders, according to their parts of the rights to the company's profits, and the following provisions shall apply:
- (1) profits distributed out of the company's chargeable income shall not be deemed income;
  - (2) for this matter, "**profits distributed**" – the chargeable income, plus income exempt of tax, less the tax that applies to the shareholder in respect of the income, if it was paid by the company and it did not debit him accordingly;
  - (3)
    - (a) the transparent company's losses during the tax year, which were related to a shareholder, shall first be set off against that shareholder's income from the transparent company, in accordance with the provisions of the Ordinance;
    - (b) losses that were related to a shareholder in previous tax years shall be allowed to be set off only against that shareholder's chargeable income and shall not be allowed to be set off against the transparent company's income;
    - (c) repealed
  - (4) classification of the chargeable income or the loss, as the case may be, which was related to a shareholder as said in this section, to a source of income shall be according to the source of income from which it was produced or accrued for the transparent company, but such income shall not be deemed income from personal exertion, unless the shareholder played an active role in the company;
  - (5) in respect of credit for foreign taxes, as defined in section 199, a shareholder is entitled to his proportional share of the foreign tax that the transparent company paid;
  - (6) in respect of a shareholder's advances, as said in section 175, his proportional part of the transparent company's chargeable income, including its income from dividends or its losses, shall be added to the turnover that is the basis for advances;
  - (7) the tax on a transparent company's income, including advances, may be collected either from the company or from its shareholders, in the amount of the tax due on their proportional parts of the transparent company's profits;
  - (8) the following provisions shall apply to the sale of a share in a transparent company:
    - (a) for purposes of section 88, there shall be subtracted – from the consideration in respect of the seller, and from the original cost in respect of the purchaser – an amount equal to part of the amount of undistributed profits accrued in the company during the benefit years, the proportion of which to the total of undistributed profits is as the proportion of the share's rights to the profits of the transparent company to all rights to its profits; for this purpose:  
"profits" – the chargeable income of the transparent company in the benefit years, less its losses in those years,

- on condition that the result obtained is not a negative amount;
- "purchaser"** includes a person who bought shares from the transparent company;
- (b) the provisions of section 94B shall not apply in respect of the benefit years;
  - (c) for purposes of calculating capital gains, an amount equal to the losses related to the seller of the share during the benefit years shall be subtracted from the adjusted original cost, up to the amount of the adjusted original cost; for this purpose: **"losses"** – an amount equal to the chargeable income related to a shareholder, less losses related to him, provided it is a negative amount;
- (9) if the holder of a share in an transparent company sold shares, then he shall inform the transparent company of the sale within 90 days after the sale;
  - (10) the provisions of Part Five "B", except for Chapter Three there, shall not apply to a transparent company;
  - (11) (a) the transfer of assets from a transparent company, liquidation of which has begun, to its shareholders in accordance with their parts of the rights in it shall not be charged tax under this Ordinance or under the Real Estate Taxation Law (in this paragraph: the taxes), on condition that the transferred asset did not change its designation during the transfer, as said in sections 85 and 100 and in section 5B of the Real Estate Taxation Law; however, if the sale does not become liable to Land Appreciation Tax because of the provisions of this paragraph, the sale shall be liable to acquisition tax at the rate of 0.5%; the Minister of Finance may, with approval by the Knesset Finance Committee, designate instances in which exemption from the taxes under this subparagraph shall not apply when the company is liquidated, on conditions he shall set; for this purpose: **"Land Appreciation Tax"** and **"Acquisition Tax"** – within their meaning in the Real Estate Taxation Law;
  - (b) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe conditions, provisions and restrictions in respect of this paragraph, including the matter of determining the original cost of the assets of a transparent company in liquidation, the day of acquisition and the acquisition cost, as defined in the Real Estate Taxation Law, as well as provisions in respect of losses and the distribution of income and also on instances, in which an increase in the value of assets is to be taxed.
- (c) (1) The Minister of Finance may, with approval by the Knesset Finance Committee, make rules in respect of a transparent company that has ceased to comply with the conditions and provisions prescribed in this section, including the determination that the company shall cease to be a transparent company; if he so determined, then it cannot again come to be considered a transparent company;
  - (2) if a company ceased being transparent, because of a violation of one of the provisions of this section, then it may – with the Director's approval and on conditions set by him – request that it



- be wound up according to the provisions of subsection (b)(11) within one year after the end of the tax year in which the said violation occurred; for this purpose, the day of the violation shall be deemed the day on which liquidation proceedings began.
- (d) Notwithstanding the provisions of this Ordinance, the following provisions shall apply to matters of assessment, objection and appeal:
- (1) if an assessment was made for the transparent company, then the Assessing Officer may – notwithstanding the provisions of this Ordinance – determine or amend the assessment of a shareholder in accordance therewith within two years after the end of the year in which the company's assessment was made or at a time when he may assess the shareholder's income, whichever is later;
  - (2) the transparent company may object to or appeal against the assessment made for it according to the provisions of sections 150 or 153, as the case may be; a shareholder may object or appeal as aforesaid against relating the transparent company's chargeable income or losses and against the effect, which the assessment made for the transparent company had on his income, but not against the assessment made for the company.
- (e) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe rules, provisions, conditions and restrictions for purposes of this section, including –
- (1) determination of the original cost;
  - (2) the consideration;
  - (3) assessment proceedings;
  - (4) the right to appeal and appeal procedures;
  - (5) prescribing an advance for the company – notwithstanding the provisions of subsection (b)(6) – according to the company's calculated basis for advances, at the rate he shall prescribe, rules for relating the said advance to the shareholders, and rules for setting off an advance for excess expenditure, as said in section 181B;
  - (6) relating and distributing the income according to the rights to profits, and rules for rounding off the shareholders' proportional parts of the rights to profits;
  - (7) tax obligation and tax payment under circumstances, under which the company's shares are sold in the course of the year;
  - (8) returns to be submitted by the transparent company and its shareholders;
  - (9) provisions on the restriction on a set off of losses;
  - (10) provisions on active officers of the company, as said in subsection (b)(4).

## CHAPTER TWO "A": REAL ESTATE INVESTMENT FUND

### Definitions

64A2. (a) In this Chapter –

**"means of control"**, **"substantive shareholder"**, **"original cost"**, **"relative"** and **"real capital gain"** – as defined in section 88;  
**"income in the amount of depreciation expenses"** – income in the amount of the depreciation expenses deductible in respect of productive real estate under the provisions of this Ordinance or under the provisions

of the Inflationary Adjustments Law;

**"chargeable income"** – including land appreciation;

**"exceptional income"** of a real estate investment fund – the following:

- (1) income from the sale of business stock;
- (2) income other than income specified in subparagraphs (a) to (c), the total of which exceeds 5% of the Fund's total income in the tax year;
  - (a) income from productive real estate and income from the sale of building rights on real estate that was productive real estate on the day of its acquisition;
  - (b) income from securities traded on an Exchange, from State loans and from deposits;
  - (c) income which is deemed business income under section 7 of the Inflationary Adjustments Law;

for the purposes of this paragraph:

**"income"** includes real estate appreciation;

**"tax"** – including Land Appreciation Tax under sections 6 or 7 of the Real Estate Taxation Law;

**"real estate"** – including real estate abroad and exclusive of real estate association rights;

**"real estate held for a short time"** – real estate, for which less than four years passed from the day of its acquisition by a real estate investment fund until the day of its sale, including a tax exempt sale;

**"productive real estate"** – real estate, the rental of which and activities connected with its rental produce income under section 2(1) or (6) for the real estate investment fund, on condition that buildings stand on it with a total area equal to at least 70% of the area that can be built under the scheme that applies to it, including movables used directly for activity on that real estate, other than –

- (1) real estate for uses designated by the Minister of Finance, if the management services of that real estate are provided by that real estate investment fund or by its relative;
- (2) real estate that is business stock of the Fund; for the purposes of this definition,

**"scheme"** –

- (a) in respect of real estate in Israel – within its meaning in the Planning and Building Law 5725-1965;
- (b) in respect of real estate abroad – the scheme under the Law of the state in which it is located;

**"asset"** – any property, real or movable, and also any prospective or vested right or benefit, all whether located in Israel or abroad;

**"issue and consideration assets"** – State loans, deposits or cash derived from money specified in paragraphs (1) to (3) of this definition, held during periods no longer than the periods specified in those paragraphs:

- (1) money received from a first issue of the Fund's securities, which were listed for trading on the Stock Exchange in Israel – during two years after the day of issue;
- (2) money received from an additional issue of the Fund's securities, which were listed for trading on the Stock Exchange in Israel – during one year after the day of

- issue;
    - (3) consideration from the sale of real estate – during one year after the day of the sale;
  - "real estate investment fund" – a company for which the conditions said in section 64A3 hold true.
- (b) Every other term in this Chapter shall have the meaning it has in the Real Estate Taxation Law, except when a different provision is expressly stated.

### **Real estate investment fund**

- 64A3. (a) A real estate investment fund is a company for which all the following hold true:
- (1) it was incorporated in Israel and the control and management of its business is in Israel;
  - (2) its shares were listed for trading on an Exchange in Israel within twelve months after its incorporation, and they are traded there;
  - (3) from the time of its incorporation until the provisions of this Chapter began to apply to it, it had no assets, activity, income, expenses, losses or obligations, other than for its activity as a real estate investment fund;
  - (4) the provisions of Part Five "B" or the provisions of section 70 of the Real Estate Taxation Law did not apply to the transfer of an asset to it;
  - (5) all the following took place on June 30 and on December 31 of each tax year:
    - (a) the value of its assets that are productive real estate, debentures, securities traded on an Exchange, State loans, deposits and cash was not less than 95% of the total value of all its assets;
    - (b) the value of its assets that are productive real estate and issue and consideration assets was not less than 75% of the total value of its assets, or less than NS 200 million;
    - (c) the value of its assets that are productive real estate in Israel is not less than 75% of the value of all its assets that are productive real estate;
    - (d) the amount of loans it took, also by way of issuing debentures or capital notes, does not exceed an amount equal to 60% of the value of the assets that are productive real estate, plus 20% of the value of its other assets;
  - (6) 50% or more of the means of control in it are held – directly or indirectly – by more than five shareholders; for this purpose:
    - (a) members of a benefit fund, persons insured by an insurance company in respect of its insured persons' investment, and unit holders in a joint investment trust fund shall be deemed shareholders in the Fund;
    - (b) a person and his relative shall be deemed one shareholder;
  - (7) the chargeable income was transferred to the shareholders as said in the provisions of section 64A9;
  - (8) an auditor's certification of compliance with the conditions enumerated in paragraphs (1) to (7) was attached to the return it submitted under section 131.
- (b) For the purposes of subsection (a)(5), the "value" of an asset – one of the following, at the Fund's choice, on condition that its choice in respect of each tax year apply to all its assets:

- (1) the original cost or the acquisition value of the asset, as the case may be, its amount having been adjusted from the day of acquisition to the date on which the value is examined;
- (2) the price to be expected at a sale of the asset by a willing seller to a willing buyer, the asset being free of any encumbrance to secure any debt, mortgage, or other right intended to secure a payment.
- (c) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions on determining the value, also in respect of assets that will or will not be taken into account for the purposes of subsection (a)(5).
- (d)
  - (1) If one of the conditions enumerated in subsection (a) ceases to hold true for the company, then it shall cease being a real estate investment fund.
  - (2) Notwithstanding the provisions of paragraph (1), if one of the conditions specified under subsection (a)(5) ceased to hold true on one of the dates prescribed there, then it shall be deemed to have held true on that date if it comes to hold true again within three months and continues to hold true continuously during at least one year; if it did not come to hold true again as aforesaid, then the company shall cease to be a real estate investment fund on the date specified in subsection (a)(5), on which the said condition first ceased to hold true.
  - (3) If the company has begun to be wound up, then it shall cease to be a real estate investment fund.
  - (4) The company may inform the Assessing Officer that it elected not to be a real estate investment fund; when it has notified as aforesaid, it shall cease to be a real estate investment fund from the day it stated in the notification, or on the thirtieth day after the notice was given, whichever is later.

#### **Income from a real estate investment fund**

- 64A4. (a) For the purposes of tax calculation, tax rates and the set-off of losses, the chargeable income of a real estate investment fund, which was transmitted to the shareholders as said in section 64A9, shall be deemed the shareholders' chargeable income (in this Ordinance: shareholders' chargeable income).
- (b) The shareholders' chargeable income shall be charged tax on the day on which it was transferred to them.
  - (c) Notwithstanding the provisions of subsection (a), in respect of tax rates –
    - (1) exceptional income shall be charged tax at the rate of 70%, without any right to exemption, deduction, credit or set-off;
    - (2) chargeable income from the sale from real estate held for a short time shall be charged tax at the rates said in sections 121 or 126, as the case may be.
  - (d) The chargeable income of shareholders shall be classified as to its source according to the source from which it was produced or accrued to the Fund, and the following provisions shall apply to this matter:
    - (1) the income shall not be deemed income from personal exertion;
    - (2) income in the amount of depreciation expenses shall be deemed income from capital gain or from appreciation, as the case may be.
  - (e) The chargeable income of a Real Estate Investment Trust, which is not chargeable income of the shareholders, shall be charged tax according to the following provisions:
    - (1) chargeable income from the sale of real estate held for a short

- time shall be charged tax at the rate prescribed in section 126;
- (2) exceptional expenses shall be charged tax at the rate of 60%;
- (3) other chargeable income shall be charged tax under the provisions of any statute.
- (f) The chargeable income of a shareholder shall be exempt of tax, on condition that it is not exceptional income, if the shareholder is one of the following:
  - (1) a pension benefit fund, a savings benefit fund and a severance pay benefit fund;
  - (2) the resident of a reciprocating state, who manages a retirement age savings plan or a long term savings plan that essentially resembles a savings benefit fund, and also a pension fund that is the resident in a reciprocating country or is managed by the resident of a reciprocating country, on condition that the profits they receive are exempt of tax in their country of residence because they are profits on savings for the retirement age.
- (g) Foreign taxes paid by a real estate investment fund may be deducted from the income, in respect of which they were paid, and notwithstanding the provisions of this Ordinance the Fund and its shareholders shall not be given any credit for them.
- (h) Losses suffered by a real estate investment fund shall not be set off against the income of its shareholders.

#### **Tax deduction**

- 64A5. (a) When a real estate investment fund pays the chargeable income of its shareholders, it shall deduct tax according to the following provisions:
- (1) from real estate appreciation or from capital gains, other than from the sale of real estate held for a short time, and also from income in the amount of depreciation expenses – at the rates prescribed in section 91, or in section 48A of the Real Estate Taxation Law, as the case may be;
  - (2) from exceptional income – at the rate of 70%;
  - (3) from other chargeable income – at the maximum tax rate prescribed in section 121 or at another tax rate set by the Minister of Finance with approval by the Knesset Finance Committee, or at the tax rate prescribed in section 126(a), as the case may be;
  - (4) from chargeable income transmitted to a shareholder that is an exempt trust fund, as defined in section 88 – as specified in subparagraphs (a) to (c) of this paragraph, as the case may be, and notwithstanding the provisions of section 129C tax paid under this paragraph shall be deemed the final tax to which the exempt trust fund is liable, and in its respect it shall not be entitled to any exemption, deduction, credit or set-off whatsoever:
    - (a) from real estate appreciation or from capital gains, other than from the sale of real estate held for a short time – no tax shall be deducted;
    - (b) from exceptional income – at the rate of 60%;
    - (c) from other chargeable income – at the rate of 25%.
  - (b) Notwithstanding the provisions of subsection (a), when income other than exceptional income is paid to shareholders said in section 64A4(f), tax shall not be deducted.
  - (c) (1) If chargeable income was transferred to shareholders and before its transfer it was charged to tax under the provisions of section 64A4(e), then it shall be deemed dividend income and the

provisions of subsection (a) shall not apply to it, and the tax that the Fund shall deduct shall be the tax that it must deduct from dividend payments to its shareholders or from dividend payments to its substantive shareholders, as the case may be.

- (2) The shareholder shall not be given any credit for the tax paid by the Fund, as said in section 64A(e).
- (d) The Assessing Officer may give written permission that tax shall not be deducted as said in subsection (a), or that less than the prescribed rates be deducted, if he concludes that the shareholder's chargeable income is not liable to tax or that the tax on it is less than the rates prescribed in subsection (a).
- (e) The deducted amounts shall be paid to the Assessing Officer on the prescribed date and a return shall be attached to them, as prescribed.

### **Assessment, objection, contestation, appeal and collection**

64A6 Notwithstanding the provisions of this Ordinance and the provisions of the Real Estate Taxation Law, the following provisions shall apply to assessment, objection, contestation, appeal and collection:

- (1) The Assessing Officer or the Director, as defined in the Real Estate Taxation Law, as the case may be, may – according to the provisions of the Ordinance or of the said Law – determine the chargeable income of a real estate investment fund and assess the tax it must pay even after the chargeable income was transmitted to the shareholders;
- (2) the real estate investment fund alone has the right to object, contest or appeal against the assessment made for it according to the provisions of the Ordinance or of the said Law; a shareholder may contest or appeal against the effect of the real estate investment fund's assessment on his income, but not against the assessment of the Fund;
- (3) any additional tax on the shareholders' chargeable income in consequence of assessment proceedings shall be collected only from the real estate investment fund and tax refunds in respect of the said income shall be refunded only to the Fund.

### **Reduced acquisition tax**

64A7. Notwithstanding provisions under the Real Estate Taxation Law, if a real estate investment fund acquired a real estate right from a company against the allocation of shares in the Fund, then the Fund shall pay acquisition tax at the rate of 0.5%, on condition that the acquisition was made no later than twelve months after the date on which it became a real estate investment fund and before its shares were listed for trading on an Exchange, and that the Director approved the real estate sale in advance.

### **Set-off of loss suffered by a shareholder**

64A8. A loss suffered in the tax year by a shareholder from the sale of a share in the real estate investment fund may be set off as said in section 92 or against the chargeable income of shareholders that the fund transferred to him in that year, except for exceptional income transferred to him.

### **Transferring chargeable income to shareholders and distribution of profits**

64A9.(a) The chargeable income of a real estate investment fund shall be transferred to the shareholders according to the provisions of paragraphs (1) or (2), as the case may be, on the date prescribed in them:

- (1) at least 90% of the Fund's chargeable income, other than real

- estate appreciation or profits from the sale of productive real estate, plus exempt income and less nondeductible expenses – until April 30 of the year after the year in which the income was produced or accrued;
- (2) capital gains or real estate appreciation earned by the fund upon the sale of productive real estate – up to twelve months after the date of sale of the real estate; this provision shall not apply to real estate appreciation upon the sale of a real estate right, if the following two conditions hold true:
    - (a) the appreciation was exempt of tax, as said in the provisions of Chapter Five "C" of the Real Estate Taxation Law, because the right sold by the Fund was exchanged against a real estate right in other productive real estate;
    - (b) the exchange was made during the period prescribed in the said provisions.
  - (b) (1) Notwithstanding the provisions of the definition of "profits" in section 302(b) of the Companies Law, a real estate investment fund may make a distribution also out of income in the amount of the depreciation expenses, on condition that the distribution was made until April 30 of the year after the year in which the income was produced or accrued.
  - (2) If the Fund distributed income as said in paragraph (1), then the income shall be reduced by the amount of depreciation expenses distributed out of profits distributable to shareholders under the provisions of the Companies Law and also out of the capital gains or real estate appreciation from the sale of that productive real estate.

#### **Provisions for a company that ceased being a real estate investment fund**

64A10. If a company ceased being a real estate investment fund, then the following provisions shall apply:

- (1) the provisions of this Chapter shall apply to chargeable income produced by or accrued to the Fund up to the day on which it ceased to be a real estate investment fund (in this section: the last day) and to the chargeable income transferred to the shareholders until April 30 of the year after the year in which it was produced or accrued;
- (2) the provisions of this Chapter shall not apply to income produced or accrued to the company after the last day.

#### **Powers of the Minister of Finance**

64A11. The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe the following provisions in respect of the income of a real estate investment fund and of the income transmitted to its shareholders, including the matter of land appreciation tax:

- (1) taxation of chargeable income, which a shareholder received in respect of the period in which the share was owned by another person, including the determination that in respect of aforesaid income there shall be no right to a tax exemption, and including the determination of the tax rate applicable to some or all the profits and of the rate applicable to the tax deduction, notwithstanding the provisions of section 64A5;
- (2) classification of part of the capital gain upon the sale of a real estate investment fund share as income to which the provisions of Part Two apply, with prescribed conditions and adjustments;
- (3) transmission of the chargeable income to the shareholders, the ways of

- transmission and how it is to be related to the Fund's income, profits or real estate appreciation to which it is entitled, and also provisions that rule out the setting off of losses;
- (4) other conditions and adjustments necessary for the implementation of this Chapter, also on the matter of a company that ceased to be a real estate investment fund.

### CHAPTER THREE: INCOME OF SPOUSES

#### Registered spouse

- 64B. (a) The Assessing Officer may determine, by notification to both spouses, that one of them is a registered spouse for purposes of this Law, when his chargeable income – in the tax year two years before the tax year first under consideration for this purpose– was more than 50% of the total chargeable income of the two spouses.
- (b) Notwithstanding the provisions of subsection (a), the two spouses together may notify the Assessing Officer in writing, at least three months before the beginning of a certain tax year, that they choose that the other spouse be deemed the registered spouse, on condition that his income in the tax year before the tax year in which the notification was given amounted to at least 25% of the income of his spouse; for purposes of this subsection and of subsection (d)(2): **"income during the tax year"** – exclusive of a spouse's income from a source dependent on the source of income of his spouse according to section 66(d).
- (c) If neither of two spouses had any chargeable income in the tax year said in subsection (a), then the Assessing Officer may decide that one of them is the registered spouse, and that without derogating from their right to act under subsection (b).
- (d) (1) Subject to the provisions of subsection (b), the determination or choice of the registered spouse shall remain in effect for no less than five tax years, except when the spouses no longer are spouses or by a decision of the Director.
- (2) Notwithstanding the provisions of paragraph (1), if during a tax year the income of the spouse registered by choice was less than 25% of his spouse's income in that tax year, then the Assessing Officer may designate a registered spouse for that tax year.
- (e) The Director may prescribe, by rules, ways of determining and choosing a registered spouse.

#### Joint calculation

65. The income of spouses shall – for the purposes of this Ordinance – be deemed the income of the registered spouse and shall be charged in his name; in respect of income from a transparent company, as defined in section 64A1, and of income from interest, discount or linkage differentials (for purposes of this section: interest) and also of income transmitted from a real estate investment fund, as defined in section 64A2, or of capital gain, the registered spouse's said income shall be deemed to include also the said income of his child who in the tax year has not yet reached age 18, unless the assets from which came the interest income, from the real estate investment fund or from capital gain, were received by way of inheritance or if they stemmed from compensation or insurance payments received for a bodily injury;



for the purposes of this section:

**"preferred interest"** – interest or discount and also profits paid on assets that are savings programs, deposits, benefit funds or debentures listed for trading on an Exchange, or joint investment fund units, unless those assets were received by inheritance;

**"preferred capital gain"** – each of the following, unless it was received by inheritance:

- (1) capital gain from the sale of a security listed for trading on an Exchange in Israel or abroad;
- (2) capital gain from the sale of a joint investment fund unit;
- (3) income from a futures transaction, to which applies the tax rate that applies to the sale of a security listed for trading on an Exchange;

**"unit"** – as defined in the Joint Investment Trusts Law.

### **File in the name of spouses**

- 65A. (a) The file kept by the Assessing Officer on the income of spouses shall bear the names of both spouses.
- (b) The provision of subsection (a) shall not apply until the end of tax year 1998, in respect of files opened before January 1, 1989, except by decision of the Director or according to a written application submitted by the spouses or by one of them to the Assessing Officer.

### **Separate calculation**

66. (a) Notwithstanding the provisions of section 65 –
- (1) a spouse who is not the registered spouse may demand that the tax on his income from personal exertion in business or vocation or from employment – including income from personal exertion as said in paragraphs (1) to (7) of the definition of that term in section 1 – be calculated separately, but in respect of aforesaid income which is a pension, a separate calculation shall be made if it is paid in respect of work income for which the spouse who is not the registered spouse would have been entitled to a separate calculation or if the spouse who is not the registered spouse was entitled – during the last five years before payment of the pension began – to a separate calculation in respect of the income by virtue of which the pension is paid;
  - (2) for the purposes of tax calculation, the income of both spouses other than from personal exertion shall be added to the income of that spouse, whose income from personal exertion is greater; if the spouses had no income from personal exertion, then the income not from personal exertion shall be deemed the income of the registered spouse;
  - (3) for the purposes of income from a transparent company, as defined in section 64A1, of income from a real estate investment fund, as defined in section 64A2, and of income from interest or from capital gain, the income of the registered spouse shall be deemed to include also the said income of his child who has not yet reached age 18; for the purposes of this section: **"interest"** – as defined in section 65.
- (b) Notwithstanding the provisions of subsection (a) and of section 65, if a spouse had income from property which he owned a year before his marriage, or from property which he inherited while he was married, then he may claim separate tax calculation on the said income; however, if the said spouse has other income on which tax is calculated separately,

then the income said in this subsection shall be added to the other income.

- (c) The following provisions shall apply to the separate tax calculation:
- (1) each of the spouses is entitled to the deductions, credits and credit points under sections 34, 35, 36, 45A, 47, 47A and 121A, to the tax benefit under section 10 and to the tax reduction under section 11, and the woman shall be entitled to an additional credit point against the tax on her income from personal exertion;
  - (2) for the purpose of a beneficiary individual's entitlement under section 37, as defined in that section, only half a credit point shall be taken into account, and there shall be no entitlement to credit points under sections 38 and 39;
  - (3) only the registered spouse shall be entitled to pension points under section 40(a); the woman shall be entitled to half a credit point under section 36A, and – further against the tax due on her income from personal exertion – to credit points for her children as follows:
    - (a) half a credit point for each of her children in the year of its birth and in the year of its maturity;
    - (b) one credit point for each of her children beginning with the tax year after the year of its birth until the tax year before the year of its maturity;For this purpose: "**year of birth**" and "**year of maturity**" – as defined in section 40(b)(3).
- (d) The provisions of subsection (a) shall apply only if the income of one spouse came from a source independent of the income of the other spouse, and the income of one spouse shall not be deemed as aforesaid if it came – inter alia – from one of the following:
- (1) the business or vocation of the other spouse;
  - (2) a company, in which both spouses or the other spouse, directly or indirectly, have a management right or 10% of the voting rights, unless the recipient of the income received aforesaid income from the company during a reasonable period of not less than one year before the marriage or of five years before his spouse had any right, direct or indirect, in the company;
  - (3) a partnership, in which both spouses or the other spouse, directly or indirectly, have not less than 10% of the capital or of the right to profits, unless the recipient of the income received aforesaid income from the partnership during a reasonable period of not less than one year before the marriage or of five years before his spouse had any right, direct or indirect, in the partnership.
- (e) (1) In this section, "**regular place of business**" – the place where the spouses regularly conduct their business or occupation or the place where they regularly work, on condition that it is not a dwelling unit used for residential purposes by the spouses or by one of them, but the Minister of Finance may – with approval by the Knesset Finance Committee – prescribe conditions under which a dwelling unit may be recognized as a regular place of business.
- (2) Notwithstanding the provisions of subsection (d), spouses may claim that the tax be calculated separately on their income as specified in subsection (a) up to the amount of NS 43,080 (*in 2008; in 2007: NS41,880; in 2006: NS 42,000; in 2005: NS 25,008*

– *Tr.*), if the following conditions apply:

- (a) in order to obtain the income for which separate calculation is claimed each of the spouses worked at the regular place of business at least 36 hours per week during a period of ten or more months during the tax year; if a separate calculation is claimed in respect of part of a tax year – if each of the spouses worked as aforesaid during a period, which stands in proportion to the period in respect of which separate tax calculation is claimed as is the proportion between the aforesaid ten months to the entire tax year; for this purpose, lawful absence from work shall be treated like work;
  - (b) the spouses have no income under sections 2(1) or (2), other than the said income designated by the Minister of Finance in regulations with approval by the Knesset Finance Committee;
  - (c) notice of the claim was delivered to the Assessing Officer at least one month before the beginning of the period for which the separate tax calculation is claimed; if the Assessing Officer is satisfied that it was not possible to deliver the notice until the said time, then it may be delivered at another time.
- (3) The effect of the notice of a claim for separate tax calculation is for three tax years, which begin at the beginning of the first tax year in respect of which the separate calculation was claimed, and as long as the conditions that entitle to separate calculation hold true for the spouses.
  - (4) The provisions of sections 38 and 39 shall not apply to income, in respect of which separate calculation is claimed, as said in this subsection.

#### **General provisions**

- 66A. (a) (1) The spouse who is not the registered spouse may also object or appeal on any matter under this Ordinance in respect of his part of the income
- (2) If one of the spouses objected or appealed, then the other can do so in respect of the same tax year only within 30 days after the Assessing Officer informed both spouses of the objection or appeal submitted by one of them.
- (b) Provisions of this Ordinance on collection and penalties shall also apply to the spouse who is not the registered spouse in respect of his part of the income, but the spouse who is not the registered spouse shall not be accused of an offense and shall not have to pay an administrative fine for any act or omission, which the registered spouse is obligated to perform or to omit, if he proves that the act or omission was committed without his knowledge and that he took all reasonable steps to prevent it.
  - (c) The Assessing Officer shall inform the spouse who is not the registered spouse of any action by the Assessing Officer, which is likely to affect his tax liability, and the times set for procedures which a person may take under this Ordinance shall, for this purpose, begin on the day on which the notification was received.
  - (d) If the spouses gave notice that they have chosen the registered spouse under section 64B(b), then tax debts created during the period of marriage may be collected from whoever was the assessee or from the previous registered spouse, or from the spouse registered when the

collection is made; the provisions of this subsection shall also apply, mutatis mutandis, to tax refunds.

#### **Income of a foster family**

66B. Out of the income of a foster family, received from the State or from a local authority for the care of children referred to it, three quarters shall be deemed income from the wife's personal exertion, and she or her husband may demand that a separate calculation be made in respect thereof under section 66.

#### **Income of husband and wife on an agricultural farm**

67. (a) Income obtained by the personal exertion of husband and wife on an agricultural farm and which, under section 2(8), is chargeable in respect of one of them shall, for the purposes of this Ordinance, be deemed income of the husband and the wife in equal parts, and the provisions of section 38 shall apply to it, but a separate tax calculation under section 66 shall not be permitted.
- (b) Notwithstanding the provisions of subsection (a), if income is obtained by the personal exertion of a spouse and it has been proven to the Assessing Officer's satisfaction that his spouse works mainly outside the farm, then three fourths of the income from the farm shall be deemed the income of the person who works mainly on the farm, and the man or the woman may demand that a separate calculation under section 66 be made in respect of the three fourths or the one fourth of the income from the farm, as the case may be, which is credited to the woman.

### **CHAPTER THREE "A": ISRAEL RESIDENT WHO STAYS ABROAD**

#### **Israel resident who stays abroad**

67A. The Minister of Finance may, with approval by the Knesset Finance Committee, make rules concerning the deductions and credits that will be allowed an individual Israel resident who has income from personal exertion that was produced or accrued abroad, including said income that was related to a shareholder in a transparent company, as defined in section 64A1, and on the tax rate applicable to the said income and to other income accrued to him in the year in which he had the said income, all after considering especially the length of time abroad, the fact that he was sent from Israel to produce the said income and of the living conditions in the country in which that individual stayed in order to produce the said income.

### **CHAPTER THREE "B": PARTICIPATION EXEMPTION FOR ISRAEL HOLDING COMPANIES**

#### **Definitions**

67B. In this Chapter –

**"substantive shareholder"** and **"relative"** – as defined in section 88;

**"income"** includes real estate appreciation;

**"Israel holding company"** – a company for which the entitling conditions said in section 67C(a) hold true;

**"held company"** – a body of persons for which the provisions of section 67D

hold true;

**"share package"** – shares in a held company, which give the right to at least 10% of the profits and which the Israel holding company held for at least twelve consecutive months;

**"entitling share"** – a share that is part of a share package;

**"shares"** in a body of persons that is not a company – rights to its profits or voting rights in it;

**"asset"** – as defined in section 64A2;

**"undistributed profits"** of an Israel holding company – all the following:

- (1) chargeable income produced or accrued in the tax year;
- (2) real estate appreciation from the sale of a real estate right or a real estate association right during the tax year;
- (3) income exempt of tax during the tax year;

all after subtracting from the income the taxes paid on it Israel or abroad, and profits distributed out of it during that year;

**"chain of companies"** – two or more bodies of persons, which directly or indirectly hold each other.

### **Israel holding company**

67C. (a) An Israel holding company is a company for which all the following conditions hold true (in this Chapter: the entitling conditions):

- (1) it was incorporated in Israel and all its business is controlled and managed only from Israel;
  - (2) it is not a public company, as defined in section 2 of the Companies Law, and not a financial institution, as defined in the Value Added Tax Law;
  - (3) it is not a family company, to which the provisions of section 64A apply, and not a transparent company, as defined in section 64A1;
  - (4) the provisions of Part Five "B" did not apply at its incorporation, and provisions of the said Part or of section 70 of the Real Estate Taxation Law did not apply to the transfer of an asset to it;
  - (5) the following two conditions holds true in the course of 300 days or more of each tax year, beginning with the tax year after the year in which it was incorporated:
    - (a) the original cost of its shares in held companies, plus the balance of loans it extended to the held companies, amounts to no less than NS 50 million;
    - (b) the original cost of its shares in held companies, plus the balance of loans which it extended to the held companies amounts to 75% or more of the original cost of all its assets, including the balance of loans which it extended to held companies;
  - (6) it did not have any income under section 2(1), except for income for services provided to a held company, and except for income which – under section 7 of the Inflationary Adjustments Law – is deemed income from business;
  - (7) it chose that the provisions of this Part apply to it, by a notice that was signed by all its shareholders and was delivered to the Assessing Officer within ninety days after its incorporation.
- (b) If an entitling condition did not apply to the company in the year of its incorporation and in the following year, then it shall be deemed never to have been an Israel holding company.
- (c) If one of the entitling conditions ceased to hold true for an Israel holding company after the period said in subsection (b), then it shall cease to be

- an Israel holding company from the beginning of the tax year in which the entitling conditions ceased to hold true.
- (d) An Israel holding company may inform the Director, by a notice signed by all its shareholders, that it chooses to cease being an Israel holding company; having so announced, it shall cease being an Israel holding company from the beginning of the tax year after the tax year in which the notice was delivered to the Director.

### **Held company**

67D. A body of persons, for which all the following hold true, is a held company:

- (1) it is a foreign resident located in a reciprocating state and it submits a return of its income in that foreign state, or it is a foreign resident the place of residence of which is in a state where the tax rate applicable to the income of bodies of persons from business activity was 15% or more when the Israel holding company first bought its shares;
- (2) 75% or more of its income in the tax year, which was produced or accrued outside Israel, is income that – if it were liable to tax in Israel – would be chargeable as business income under section 2(1); when calculating the said income a proportional part of the income of linked companies shall be added, but income from management fees paid by a relative, the consideration from asset sales and dividends out of the income of linked companies shall not be taken into account; for the purposes of this paragraph:  
**"asset"** – other than securities traded on an Exchange, which were issued by a company in which the held company is not a controlling member;  
**"proportional part of the income of linked companies"** – the proportional part of a body of persons in the income of a foreign resident body of persons, in which it has a direct or indirect right to profits, in the proportion of its right to profits, provided that a right to less than 10% of the profits shall not be taken into account; the indirect share of the body of persons in the said rights shall be calculated by multiplying the percentages of the right to profits in each body of persons in the chain of companies, which it holds directly or indirectly;
- (3) the cost of its assets in Israel does not exceed 20% of the cost of all its assets throughout the tax year; for purposes of this paragraph: **"assets in Israel"** includes rights in a foreign resident body of persons, the main assets of which are direct or indirect rights to assets located in Israel;
- (4) its income in the tax year that was produced or accrued in Israel – including from the sale of real estate or of real estate association rights – does not exceed 20% of all its income in the tax year.

### **Exemption for the income of an Israel holding company**

- 67E. (a) An Israel holding company shall be exempt of tax on all the following:
- (1) capital gains on the sale of entitling shares;
  - (2) dividends received in respect of entitling shares, if distributed during a period of not less than twelve consecutive months, during which the Israel holding company was a substantive shareholder of the held company;
  - (3) interest, dividends and capital gains from securities traded on the Exchange in Israel;
  - (4) interest and linkage differentials received from a financial institution, as defined in the Value Added Tax Law.
- (b) No credit shall be given for foreign taxes in respect of income that is tax

- exempt under the provisions of subsection (a).
- (c) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe tax exemptions for interest received by an Israel holding company from a held company, if the interest was paid during a period he prescribed and at an interest rate he prescribed, all on conditions and with adjustments which he prescribed.

**Dividends distributed by an Israel holding company**

- 67F. (a) A dividend received by a foreign resident shareholder in an Israel Holding Company shall be charged tax at the rate of 5%.
- (b) A dividend received by an Israel resident shareholder in an Israel holding company shall be charged tax at the rates said in paragraphs (1) or (2), as the case may be;
- (1) if the recipient of the dividend is an individual – at the rate prescribed in section 125B, as the case may be;
- (2) if the recipient of the dividend is a body of persons –
- (a) if the dividend was distributed out of earnings said in section 67E(a)(3) or (4) – at the rate prescribed in section 126(a);
- (b) if the dividend was distributed out of earnings said in section 67E(a)(1) or (2) – at the rate prescribed in section 126(c);
- (c) in the case of any other dividend – at the rate prescribed in section 126(b) or (c), as the case may be.

**Conceptual dividend**

- 67G. (a) An Israel resident, who at the end of the tax year was a direct or indirect shareholder of an Israel holding company, shall be deemed to have received his proportional share of the undistributed profits as a dividend at the end of the tax year, and he shall be charged tax on those profits as said in section 67F(b).
- (b) The provisions of subsection (a) shall not apply to a shareholder who indirectly was a shareholder in an Israel holding company through another shareholder who is an Israel resident, if the provisions of subsection (a) apply to the other shareholder, and that in respect of the part of undistributed profits, in respect of which the other shareholder was charged tax according to subsection (a).
- (c) If an Israel resident shareholder received a dividend, the direct or indirect source of which is the income of an Israel holding company, then the dividend shall not be charged tax, if tax under the provisions of subsection (a) was paid in its respect by him or by the person from whom he received the shares by a tax exempt sale or by inheritance; if a loss was set off against the income said in subsection (a), then for the purposes of this subsection it shall be deemed that tax under subsection (a) was paid on the income set off as aforesaid.

**Special provisions for persons who were Israel residents**

- 67H. Notwithstanding the provisions of section 67F(b) and section 67G, the following provisions shall apply to an individual shareholder in an Israel holding company, who held its shares before he first became a veteran Israel resident or a returning resident, as said in section 14(a) and (c):
- (1) dividends he received from an Israel holding company during the period in which he was entitled to benefits under section 14(a) or (c), as the case may be, shall be charged tax at the rate of 5%;
- (2) the provisions of section 67G in respect of his share of undistributed profits shall not apply to aforesaid profits, which stem from dividends

received by the Israel holding company from a foreign resident company, the shares of which it acquired before he became an Israel resident as said in section 14(a) or (c), and to the profits that stem from the Israel holding company's capital gains upon the sale of shares in a foreign resident company, the shares of which were acquired as aforesaid, all during the period in which – under sections 14(a) or (c) or 97(b) – said income would have been exempt of tax for the shareholders, had they received it directly.

#### **Selling the share of an Israel holding company**

- 67I. (a) When a share in an Israel holding company is sold by an Israel resident, he shall be given credit against the tax that applies to the capital gain, in an amount equal to the tax he or the person from whom he received the shares in a tax exempt sale or by inheritance paid on undistributed profits under section 67G in respect of the sold share, on condition that he had not yet received them as a dividend; the amount of tax paid as aforesaid shall be adjusted at the rate of the index increase from the end of the year in which the undistributed profits were treated as if they had been received as a dividend, until the date of the sale, but credit shall not be given in an amount greater than the tax that applies to the sale of the share.
- (b) The provisions of section 94B shall not apply to the sale of a share in an Israel holding company in respect of profits available for distribution, as defined in section 94B, in respect of which the seller paid tax under section 67G(a).

#### **Company that ceased to be an Israel holding company**

- 67J. (a) For the purposes of this section:
- "entitling part of the real capital gain"** – the real capital gain, multiplied by the ratio of the period from the day of acquisition until the end of the final year to the period from the day of acquisition until the day of sale;
- "balance of real capital gain"** – the differential between the real capital gain and the entitling part of the real capital gain;
- "final year"**, for the purposes of a company that ceased being an Israel holding company – if it ceased under section 67C(c) – the year before the year in which the entitling condition ceased to exist, and if it ceased under section 67C(d) – the year in which it gave notice under the said section.
- (b) When a company ceased to be an Israel holding company, then the following provisions shall apply:
- (1) if, in any year after the final year, the company sold an asset in respect of which – had it been sold while it was an Israel holding company – the company would have been exempt of tax on its sale under the provisions of section 67E(a), then the company shall be exempt of tax on part of the entitling real capital gain and liable to tax on the balance of the real capital gain;
  - (2) if in any year after the final year the company distributed to foreign residents a dividend, the source of which are profits the company accrued during the years when it was an Israel holding company, or if its source is the entitling part of the real capital gain, then it shall be charged tax at the rate of 5%;
  - (3) if an Israel resident directly or indirectly is a shareholder in the company, then he shall be treated as if, at the end of the year in which the company sold an asset said in paragraph (1), he



received his proportional part of the entitling real capital gain as a dividend, and on it he shall be charged tax as said in section 67F(b), and the provisions of sections 67F and 67G, respectively, shall apply.

#### **Restriction on applicability of section 75B**

- 67K. (a) In this section, "**controlled foreign company**" and "**unpaid profits**" – as defined in section 75B(a).
- (b) If a held company is a controlled foreign company, then the provisions of section 75B shall not apply to the Israel holding company that holds it and to its controlling members who are Israel residents, in respect of profits not paid by the held company; a shareholder shall not be deemed an Israel resident only because he is shareholder of an Israel holding company.

### **CHAPTER FOUR: FOREIGN RESIDENTS**

68. Repealed

#### **Conditions for granting relief to foreign residents**

- 68A. (a) A foreign resident body of persons shall not be entitled to tax relief, reductions or exemptions under this Ordinance because of its being a foreign resident, if Israel residents are controlling members of it, or are the direct or indirect beneficiaries of or entitled to 25% or more of the income or profits of the foreign resident.
- (b) The Minister of Finance may prescribe ways of proof for the purposes of this section.
- (c) In this section:  
"**means of control**" and "**together with another**" – as defined in section 88;  
"**controlling members**" – shareholders who directly or indirectly, alone, with another or together with another Israel resident, hold more than 25% of one or more of the means of control.

#### **Appointing a representative**

- 68B. (a) If, under section 60 of the Value Added Tax Law, a foreign resident is required to appoint a representative, then he shall appoint as representative – also for the purposes of the Ordinance – an individual Israel resident or an Israel resident body of persons that has a business in Israel.
- (b) The representative shall be authorized to report to the Assessing Officer, to accept income and profits for the foreign resident, and to pay the tax that the foreign resident must pay only out of the foreign resident's assets.
- (c) If the foreign resident did not appoint a representative as said in subsection (a), then the representative appointed under the Value Added Tax Law shall be his representative for the purposes of the Ordinance.
- (d) The Minister of Finance shall, with approval by the Knesset Finance Committee, prescribe provisions for the implementation of this section and also provisions on the returns the representative must submit.

### **Non-residents**

69. The Minister of Finance may make rules in respect of individuals who are not Israel residents, in order to prescribe –
- (1) what deductions and credits may be allowed a said individual;
  - (2) the individuals or the categories of individuals to whom those deductions or credits shall apply.

### **Exemption of foreign resident ship owner**

70. The profits of a person who is not an Israel resident and who engages in the business of a ship owner or ship charterer (in this Ordinance: foreign resident ship owner) are exempt of tax, to the extent that the exemption was determined by agreement between the state to which the foreign resident ship owner belongs and the State of Israel, or if the Minister of Finance certified that that state acts as if an agreement providing for the said exemption were in effect between that state and the State of Israel.

### **Profits of foreign resident ship owner from Israeli cargo**

71. Subject to the provisions of section 70, the entire profit of a foreign resident ship owner whose owned or chartered ship calls at an Israel port, which was derived from the carriage of passengers, mails, domestic animals or goods (all hereafter: cargo) loaded in Israel, shall be deemed income produced in Israel; this provision shall not apply to goods brought to Israel only for transshipment.

### **Calculation of profits of foreign resident ship owner with certificate**

72. (a) If a foreign resident ship owner produces a certificate from any income tax authority, certifying the following two data:
- (1) the ratio of his profits or losses from shipping business during any accounting period, as computed by that authority for income tax purposes and without deducting depreciation, to his total receipts from the carriage of cargo;
  - (2) the ratio of the amount of deducted depreciation, as computed by that authority, to his total receipts from the carriage of cargo;
- then his profits derived in Israel from shipping business for that period, before deducting any depreciation, shall be an amount proportional to his receipts from the carriage of cargo shipped in Israel, as is the ratio of his total profits according to the certificate, for that period, to his total receipts from the carriage of cargo.
- (b) The said certificate shall be one issued on behalf of any income tax authority, with regard to which the Assessing Officer is satisfied that it computes and assesses the ship owner's full profits from his shipping business on a basis that is not materially different from that prescribed by this Ordinance.

### **Calculation of profits of foreign resident ship owner in other cases**

73. If, when the assessment is made, the provisions of section 72 cannot for any reason be applied satisfactorily, then the profits derived in Israel may be calculated as a fair percentage of the full amount of receipts from the carriage of cargo loaded in Israel; however, if any person was assessed in any tax year on the basis of such a percentage, then he shall be entitled to demand – at any time within six years after the end of that tax year – that his tax liability for that year be recalculated on the basis prescribed in section 72.

### **Ship on a casual call**

74. If the Assessing Officer decides that a ship that belongs to a particular foreign

resident ship owner called at a port in Israel incidentally and that further calls by that ship or others under the same ownership are improbable, then the provisions of sections 71 to 73 shall not apply to the profits of that ship and no tax shall be charged on them.

#### **Air transport and wireless communications**

75. If a foreign resident carries on the business of air transport or the business of transmitting messages by cable or by wireless telegraphy, then he shall be assessable to tax as if he were a foreign resident ship owner; the provisions of section 70 to 73 shall apply, mutatis mutandis, to the computation of the profits or earnings of such business.

#### **Foreign journalist and foreign sportsman**

- 75A. The Minister of Finance may, with approval by the Knesset Finance Committee, make regulations on the deductions and credits to be allowed foreign journalists from journalistic work, as well as on the tax rate applicable to the said income, and he may also make aforesaid regulations in respect of foreign sportsmen on their income from sports activity; for this purpose:

**"foreign journalist"** – a foreign resident registered with the Foreign Press Association of Israel, who came to Israel in order to engage in journalistic work, his income from journalistic work being received from a foreign resident;  
**"journalistic work"** – the preparation of journalistic articles for periodicals or of reports broadcast by electronic mass media, or assistance in the preparation of aforesaid reports;

**"foreign sportsman"** – a foreign resident who came to Israel in order to engage in sports activity;

**"sports activity"** – regular participation in games and sports competitions, in training or in preparation for them, other than activity as a trainer in the sphere of sports, all in an Israel sport association or sport club.

### **CHAPTER FOUR "A": CONTROLLED FOREIGN COMPANY**

#### **Israeli controlling members in a controlled foreign company**

- 75B. (a) In this section –

(1) **"controlled foreign company"** – a foreign resident body of persons, for which all the following hold true:

- (a) its shares or the rights in it are not listed for trading on an Exchange; however, if they are listed in part, then less than 30% of the shares or of the rights of that body of persons were offered to the public;
- (b) most of its income in the tax year is passive income or most of its profits derive from passive income, and in respect of a body of persons in a chain of companies, which is directly held by a business company (in this section: held body), and also in respect of any body of persons that is directly or indirectly held by the held body – if most of the business company's total income or profits stem from passive income; for this purpose, the amount of income, the amount of profits and the amount of passive income shall be calculated according to the applicable tax laws, as defined in section 5(5)(c);

- (c) the tax rate that applies to its passive income in the foreign countries does not exceed 20%;
- (d) (1) more than 50% of one or more of its means of control are directly or indirectly held by Israel residents or by Israel citizen residents of an area, as defined in section 3A, or more than 40% of one or more of its means of control are held by Israel residents, who – together with a relative of one or more of them – hold more than 50% of one or more of its means of control, or an Israel resident has the right to prevent the adoption of substantive management decisions in it, including decisions on dividend distributions or on winding up, and all that at one of the following times:
  - (a) at the end of the tax year;
  - (b) on any day during the tax year and on any day in the following tax year;
 for this purpose, "**relative**" – as said in section 76(d), who is a foreign resident;
- (2) the proportion held, as said in subparagraph (1), in respect of indirect holdings in a certain body of persons in a chain of companies (in this section: the certain body) shall be calculated according to the following provisions:
  - (a) if the holdings in each of the bodies of persons in the chain of companies that indirectly hold the certain body exceed 50%; then the proportion of the holding in it shall be calculated according to the rate of direct holdings in it;
  - (b) if the rate of holdings in one of the bodies of persons in the chain of companies that hold it indirectly is less than 50%, then the indirect holdings in it by means of that chain of companies shall be taken to be a holding at the rate of zero;
- (2) "**means of control**" – as defined in section 88;
- (3) "**controlling member**" – an Israel resident who directly or indirectly, alone or with another, holds at least 10% of one of the means of control in a body of persons at one of the following times:
  - (1) at the end of the tax year;
  - (2) on any day during the tax year and on any day during the following tax year;
- (4) "**together with another**" – together with his relative and also together with a person who is not his relative, if they are Israel residents and if there is regular direct or indirect cooperation between them by agreement concerning substantive matters of the company;
- (5) "**passive income**" –
  - (a) each of the following kinds of income, other than income which – had it been produced or accrued in Israel – would under Israel tax laws have been deemed income from business or profession:
    - (1) income from interest or linkage differentials;
    - (2) income from dividends;

- (3) income from royalties;
- (4) income from rent;
- (5) consideration for the sale of an asset, within its meaning in section 88, which was not an asset used by the company in a business or in a vocation;
- (b) any income that stems from an income or a consideration said in subparagraph (a), even if it is income from business or occupation;
- (6) **"total income and profits"** of a business company – its income and profits and also its proportional part, direct or indirect, of the income and profits of any body of persons in the chain of companies which it directly or indirectly holds; for this purpose, the business company's indirect proportional part of aforesaid profits shall be calculated by multiplying the proportional right by the profits of each body of persons in the chain of companies which the business company holds indirectly;
- (7) **"business company"** – a foreign resident body of persons, most of the income and profits of which are not passive income;
- (8) **"controlling member's proportional part of unpaid profits"** – a proportional part of all unpaid profits, in accordance with the controlling member's direct and indirect right to profits in the controlled foreign company on the last day of its tax year; for purposes of this section, a controlling member's indirect part of unpaid profits shall be calculated by multiplying the right to the profits of every body of persons in the chain of companies which he holds indirectly;
- (9) repealed
- (10) **"foreign tax"** – the tax which – under the tax laws applicable in a foreign country – is due on income in that country;
- (11) **"relative"** – as defined in section 88, who is an Israel resident;
- (12) **"unpaid profits"** – profits that stem from the passive income of a controlled foreign company that was produced during the tax year, other than profits that stem from dividends received from a foreign resident body of persons that was proven – to the Assessing Officer's satisfaction – to stem from income on which foreign tax was paid at a rate in excess of 20%, which in the course of that year were not paid to persons with rights in it; in the calculation of said profits the taxes due on the passive income of the controlled foreign company and its losses in that year and its losses brought forward from preceding years that stemmed from the said sources shall be subtracted; for this purpose, the amounts of profit, of foreign tax and of loss shall be calculated in accordance with the applicable tax laws, as defined in section 5(5)(c);
- (13) **"applicable tax rate"** – the amount of foreign tax which the controlled foreign company was charged in respect of its passive income in the tax year, divided by the total of its profits that stem from passive income in that year;
- (14) **"chain of companies"** – two or more bodies of persons, which directly or indirectly hold each other;
- (15) **"Israel resident"** – including an Israel citizen resident in an area as defined in section 3A, and exclusive of a person who became an Israel resident for the first time or a veteran returning resident, as said in section 14(a), when ten years have not yet passed since he became an Israel resident as aforesaid.

- (b) (1) if a controlled foreign company has unpaid profits, then its controlling member shall be treated as if he had received his proportional share of those profits as a dividend;
- (2) if means of control were acquired in the course of the year, then the controlling member's proportional part of the unpaid profits shall be calculated according to the proportional period in which he held means of control in the course of the tax year in which they were acquired;
- (3) the provisions of paragraphs (1) and (2) shall not apply to a controlling member who controls another controlling member in respect of unpaid profits of the controlled foreign company, if the provisions of the said paragraphs apply to the other controlling member in respect of the unpaid profits.
- (c) (1) If an obligation to pay foreign tax applies to the controlled foreign company in the state of its residence, inter alia by deduction at the source in respect of a dividend distribution, then a tax credit shall be allowed in the amount of the foreign tax that would have been paid if the unpaid profits had been distributed as a dividend; however, if the income under this section is income that stems from a company in a chain of companies that is not held directly by the controlling member, then to the aforesaid credit shall be added the foreign tax that would have been paid in respect of the distribution of dividends by each of the companies in the chain of companies and for which full or partial credit cannot be obtained by any of the companies in the chain; for purposes of the calculation of the credit under this paragraph the amount of foreign tax that would have been paid as aforesaid and for which no credit can be obtained shall be taken into account, multiplied by the proportional right to profits in each body of persons in the chain of companies, which is directly or indirectly held by the controlling member.
- (2) The amount of credit said in paragraph (1) shall not exceed the tax, to which the controlling member is liable in Israel on his chargeable income under this section.
- (3) If the company is the resident of a state that is not a reciprocating state, then a credit under paragraph (1) shall be given on unpaid profits in a controlled foreign company only if the controlling member proved to the Assessing Officer's satisfaction that a foreign tax obligation would apply if the said profits were distributed as a dividend in that year and the rate of the foreign tax that would have applied to a said distribution.
- (d) If a dividend was actually paid to the shareholder of a controlled foreign company out of profits on which he or his alternate paid tax under the provisions of subsection (b), then a credit shall be given against the tax that applies to the actually paid dividend; the credit shall be in the amount of tax paid under the provisions of subsection (b), but not more than the amount of the tax he paid on that part of the said profits which were paid as a dividend, and it shall be adjusted according to the rate of the index increase from the end of the tax year in which the profits were charged to him under subsection (b) and until the date of the actual dividend payment; if a credit balance remains under the provisions of this subsection, then it may be subtracted in coming the tax years, one after the other, from the tax that will be paid on dividends actually paid out in those years out of the undistributed profits of that controlled

foreign company; for this purpose: **"his alternate"** – whoever received a share from a shareholder in a tax exempt sale.

- (e) (1) If a controlling member sold all or some of his means of control in a controlled foreign company, then he shall be exempt of the tax that applies to that sale in the amount of the tax he paid in preceding tax years as said in subsection (b) on unpaid profits in respect of the means of control that are being sold, and which had not been distributed as dividends until the date of the sale; the amount of tax paid as aforesaid in preceding tax years shall be adjusted at the rate of the index increase from the end of the tax year in which it was paid until the date of sale of the said means of control;
- (2) the amount of the credit shall not exceed the tax that applies to the said capital gain after any lawfully allowed set-off and deduction.
- (f) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions on trusteeship and also provisions for the implementation of this section, rules on reports by a controlling member on his means of control in a controlled foreign company and on reporting the controlled foreign company's income.

## CHAPTER FOUR "B": TRUSTEESHIPS

### Definitions

75C. In this Chapter –

**"means of control"**, **"substantive shareholder"**, **"relative"** and **"consideration"** – as defined in section 88;

**"trustee income"** – income produced or accrued from trusteeship assets;

**"vesting"** – transferring an asset to a trustee under a trusteeship, not for consideration;

**"trust asset holding company"** – a body of person that directly or indirectly holds trusteeship assets for the trustee;

**"distribution"** – transfer of an asset or of income by the trustee to the beneficiary or to his credit, while the trusteeship is in existence or because of its liquidation;

**"creator"** of a trusteeship – within its meaning in section 75D;

**"trusteeship protector"** – the person who – under the trusteeship documents – has the power to appoint and to dismiss the trustee, to give the trustee orders, or whose approvals are needed for the trustee's acts;

**"trustee"** – a person in whom assets or income from assets were vested, or who holds assets in trusteeship; wherever in this Chapter the word "trustee" appears, that means a trustee in this position in the trusteeship at hand; for this purpose vesting in a trust asset holding company shall be treated like vesting in the trustee, and a body corporate specified in Schedule One "A" shall be deemed a trustee; the Minister of Finance may add, by Order, bodies corporate to Schedule One "A";

**"trusteeship"** – an arrangement, under which the trustee holds the trusteeship assets for the benefit of the beneficiary in Israel or abroad, whether defined as a trusteeship under statutes applicable to it, or defined in some other manner;

**"irrevocable trusteeship"** – a trusteeship that is not a revocable trusteeship, on condition that a lawfully certified affidavit by the creator of the trusteeship and by the trustee was delivered to the Assessing Officer on a form and at the time prescribed by the Director, stating that it is an irrevocable trusteeship;

**"revocable trusteeship"** – a trusteeship for which at least one of the following holds true:

- (1) it is possible to cancel it or to transfer or return the asset or the income to the creator, his spouse, his estate or to a held body of persons, all either directly or indirectly;
- (2) the creator or his spouse are one or more of the beneficiaries, or the creator or his spouse can become a beneficiary;
- (3) one or more of the beneficiaries is a child of the creator, who in the tax year has not reached age eighteen, or there is a possibility to transfer an asset or income directly or indirectly to his aforesaid child, on condition that the creator or his spouse is still alive;
- (4) one or more of the beneficiaries are bodies of persons, which are not public institutions as defined in section 9(2), in which 10% or more of any means of control are held by the creator, by his spouse or by his child who has not yet reached age eighteen if the creator or his spouse is still alive, all either directly or indirectly (in this definition: held body of persons);
- (5) the trustee or the protector of the trusteeship is the creator or a held body of persons;
- (6) the trustee or the protector of the trusteeship is a relative of the creator, unless it was proven to the Director's satisfaction that there was a special justification for the relative's appointment as trustee, and that the appointment does not demonstrate any ability to direct the trustee's activity or to issue instructions on the matter of the trusteeship; for purposes of this definition: **"relative"** – as defined in paragraphs (1) to (3) of the definition of "relative" in section 88;
- (7) the creator or his relative are able to direct the trustee's activity or to give him instructions on the way the trusteeship and its assets are managed, its beneficiaries are changed, or trust assets and trust income are distributed to beneficiaries, or his approval is required for acts of the trustee, or he is able to order the trusteeship to be cancelled or the trustee to be replaced, otherwise than for statutory grounds, all whether directly or indirectly;
- (8) the identity of one or more of the beneficiaries is not known, or the identity of a direct or indirect holder of shares in a beneficiary that is a body of persons is not known, unless it is proven to the Assessing Officer's satisfaction that that beneficiary cannot be the creator, his spouse, the creator's child who has not reached age eighteen, or a held body of persons,
- (9) the beneficiaries of a trusteeship have been replaced or new ones were added, without instructions to that effect having being included in the trusteeship documents;
- (10) no certified affidavit was delivered on the form and at the time prescribed by the Director, as said in the definition of "irrevocable trusteeship";

**"trusteeship created by foreign residents"** – a trusteeship said in section 75I;

**"trusteeship under a will"** – a trusteeship said in section 75L;

**"foreign resident beneficiary trusteeship"** – a trusteeship said in section 75J;

**"trusteeship of Israel residents"** – a trusteeship said in section 75G;

**"beneficiary"** in a trusteeship – within its meaning in section 75E;

**"asset"** – any property, real or movable, and also any prospective or vested right or benefit, all whether in Israel or abroad;

**"trustee assets"** – assets vested in the trustee or acquired or received by him,



also if held for him by a trust asset holding company, even if registered in its name;

**"foreign resident"**, in respect of a creator – including a creator who was a foreign resident at the time of his death;

**"Israel resident"** – including an Israel citizen who is resident in an area, as defined in section 3A, and in respect of a creator – including a creator who was an aforesaid Israel resident or Israel citizen at the time of his death.

#### **Creator of a trusteeship**

- 75D. (a) A person who directly or indirectly vested an asset in a trustee is the creator of a trusteeship, and the following shall also be deemed creators:
- (1) a person who directly or indirectly was a substantive shareholder in a body of persons, when the body of persons vested the asset in the trustee;
  - (2) a person who directly or indirectly held one or more categories whatsoever of means of control in a body of persons, when the body of persons vested the asset in the trustee, and he or his relative are beneficiaries of that trusteeship;
  - (3) if a trustee vested an asset or income in another trustee after the last of the creators died or after the beneficiaries of the trusteeship were changed, all without a provision to that end having been included in the trusteeship documents, then the beneficiary shall also be deemed a creator of the trusteeship under which the other trustee operates or in a trusteeship in which the beneficiaries were changed, as aforesaid, as the case may be, unless it was proven to the Assessing Officer's satisfaction that the beneficiary had no influence on the said vesting or on the change of beneficiaries;
  - (4) if the beneficiary was able to control or influence – directly or indirectly – the manner in which the trusteeship is managed, the trust assets, the designation of beneficiaries otherwise than by virtue of designation by the creator, the appointment or replacement of trustees, or the distribution of trust assets or trust income to beneficiaries, then the beneficiary shall also be deemed a creator;
  - (5) if, in a trusteeship created by foreign residents, an asset vested in the trustee was transferred from an Israel resident – he and his Israel resident relative being beneficiaries of the trusteeship – then the said Israel resident shall be deemed a creator of that trusteeship.
- (b) If a trustee vested an asset or income in another trustee, then the creator who vested the asset or income in the trustee shall be deemed the person who vested it in the other trustee, and the trustee shall not be deemed a creator.

#### **Beneficiary of a trusteeship**

- 75E. A person entitled to benefit directly or indirectly from the trust assets or trust income is a beneficiary of the trusteeship, including the following:
- (1) a person who will be entitled to be an aforesaid beneficiary when a condition is fulfilled or when a date prescribed in the trusteeship documents has been reached; however, if a person's rights are conditional on the demise of the creator or of another, then he shall not be deemed a beneficiary as long as the creator or the other beneficiary still are alive;
  - (2) a still unborn beneficiary;

- (3) an indirect beneficiary through a chain of trusteeships;
- (4) a person who directly or indirectly holds one or more of any category of means of control in the beneficiary, which is a body of persons other than a public institution defined in section 9(2).

#### **Tax liability of trust income**

- 75F. (a) Trust income shall be charged tax in the year in which it was produced or accrued.
- (b) Trust income shall be treated as the creator's income or the beneficiary's income, as the case may be, as specified in sections 75G, 75I, 75J or 75L.
  - (c) The trustee shall be the person assessed and charged tax in respect of trust income and of acts with trust assets.
  - (d) The tax rate at which trust income shall be charged is the maximum tax rate prescribed in section 121.
  - (e) Notwithstanding the provisions of subsection (d), if a special tax rate is prescribed for a certain category of an individual's income, then trust income of the same category shall be charged at the tax rate so prescribed.
  - (f) A tax exemption for income limited by a ceiling shall not apply to trust income, and the provisions of section 11 and the provisions of Chapter Three in Part Three also shall not apply to it.
  - (g) Trust income or chargeable trust income shall be determined under the provisions of this Ordinance, also if the trustee is a foreign resident and also if the trusteeship is under foreign Law or if the provisions of foreign Law apply to it.
  - (h) Losses suffered by a trust (in this Chapter: trust losses) cannot be set off against the income of the creator or the beneficiary, and the tax that applies to trust income cannot be set off against the tax that applies to income of the creator or of the beneficiary, except when this Chapter explicitly makes a different provision.
  - (i) Losses by the creator or by the beneficiary cannot be set off against the trust income, and the tax that applies to the creator's and the beneficiary's income cannot be set off against the tax that applies to the trust income, except when this Chapter explicitly makes a different provision.
  - (j) In respect of the calculation of capital gain on the trustee's sale of an asset that was vested in the trustee exempt of tax or not liable to tax, which was vested in him for no consideration, and in respect of the calculation of depreciation on a said asset, the original cost of the asset, the balance of its original cost and the day of the asset's acquisition shall be determined as they would have been for the creator, and the amount of depreciation shall be the amount the creator was entitled to deduct in respect of that asset.
  - (k) The place of residence of an unborn beneficiary shall be determined according to the place of residence of his parents.

#### **Charging the trustee's income in the hands of the creator or the beneficiary**

- 75F1. (a) Notwithstanding the provisions of section 75F(c), the following are assessable and chargeable to tax in respect of the trustee's income and in respect of acts with trust assets:
- (1) in a trusteeship of Israel residents –the creator who was an Israel resident in the tax year, and if more than one creator was an Israel resident in the tax year, then only one of them (hereafter:

- representative creator);
- (2) in a trusteeship under a will that under section 75L is deemed an Israel resident – a beneficiary who is an Israel resident in the tax year, and if more than one beneficiary was an Israel resident in the tax year, then only one of them (hereafter: representative beneficiary);
- on condition that that all the conditions specified in subsection (b) , as the case may be, were complied with in the said trusteeships and the provisions in subsection (c) shall apply.
- (b) (1) There is no Israel resident trustee in the trusteeship;
- (2) the trustee in the trusteeship gave notice that he elected the application of the provisions of this section and declared that he undertakes to communicate to the representative creator or to the representative beneficiary, as the case may be, all the information he needs in order to have full information about the trustee's income or the trust assets;
- (3) in respect of a trusteeship of Israel residents – all the creators, including the representative creator, gave notice of their choice of the representative trustee as assessable and chargeable and of the applicability of the provisions of this section;
- (4) in respect of a trusteeship under a will that under section 75L is deemed an Israel resident – all the beneficiaries, including the representative beneficiary gave notice of their choice of the representative beneficiary as assessable and chargeable and that the applicability of the provisions of this section;
- (5) notices said in paragraphs (2), (3) or (4) shall be submitted to the Assessing Officer on forms prescribed by the Director, together with the return under section 131(a)(5b)(4) for the first tax year in which the trustee and all the creators or the trustee and all the beneficiaries opted for the applicability of the provisions of this section.
- (c) (1) The choice of the trustee and creator or of the trustee and beneficiary, as the case may be, shall also apply in the tax years after the first tax year as said in subsection (b)(5), and they shall not have the right to retract their decision if the representative creator or the representative beneficiary, as the case may be, is still alive and still is an Israel resident or as long as there is no Israel resident trustee of the trusteeship.
- (2) The provisions of section 75F, other than subsection (c) thereof, shall apply to the representative creator or the representative beneficiary, as the case may be, all in the manner and in the amount that the trustee would have been assessed or charged, if not for the choice of the provisions of this section.
- (3) The provisions of any statute on the tax payment, reporting, collection and penalties shall apply to the representative creator or the representative beneficiary, as the case may be, in respect of the trustee's income and in respect of the trust assets.
- (4) A final tax debt of the representative creator or the representative beneficiary, as the case may be, may be collected from the trustee, and a final tax debt of the representative creator also from all the creators, also if he ceased being an Israel resident; for this purpose, "final tax debt" – as defined in section 75O(f).
- (5) The provisions of section 75O(d) shall apply, except that "if the trustee" shall be replaced by "if the representative creator or the

- representative beneficiary, as the case may be".
- (d) Wherever this section speaks of a representative creator or a representative beneficiary, that is in the relevant trusteeship.

#### **Trusteeship of Israel residents**

- 75G. (a) (1) A trusteeship of Israel residents is a trusteeship in which – at the time of its creation – at least one creator and at least one beneficiary were Israel residents, and at least one creator and at least one beneficiary thereof were Israel residents in the tax year.
- (2) A trusteeship that is not a trusteeship created by foreign residents and not a foreign resident beneficiary trusteeship shall also be deemed a trusteeship of Israel residents.
- (3) Notwithstanding the provisions of paragraphs (1) and (2), a trusteeship under a will shall not be deemed a trusteeship of Israel residents.
- (4) A trusteeship shall be deemed a trusteeship of Israel residents, whether it is a revocable or an irrevocable trusteeship.
- (b) In a trusteeship of Israel residents the trust income shall be treated like the creator's income and the trust assets shall be treated like the creator's assets.
- (c) A trusteeship of Israel residents shall be deemed an Israel resident, also when the creator ceased being an Israel resident, and the trust income shall be treated like the income of an individual Israel resident and the trust assets like the assets of an individual Israel resident.
- (d) In a trusteeship of Israel residents vesting in the trustee by an individual, carried out not for consideration, shall not be deemed a sale for the purpose of the provisions of Part Five.
- (e) If a trusteeship became a trusteeship of Israel residents after one creator thereof became an Israel resident for the first time, a veteran returning resident or a returning resident, as said in section 14(a) or (c), then the provisions under sections 14(a) or (c), 16 or 97(b) or (b3), as the case may be, shall also apply to the trust income, in addition to the provisions of section 75F.
- (f) Distribution of an asset of a trusteeship of Israel residents shall be charged tax or shall be exempt of tax for the purposes of Part Five, as it would have been if the asset had been transferred directly from the creator to the beneficiary; for this purpose the creator shall be deemed an Israel resident, even if at the time of the distribution he is a foreign resident; if a trusteeship had several creators, and if the transfer from at least one of them to the beneficiary would have been liable to tax, had it been carried out directly, then the distribution shall be liable to tax.
- (g) The provisions of section 75F(a) to (i) and (k) and of subsections (b), (c) and (e) shall not apply to trust income in a trusteeship of Israel residents that is an irrevocable trusteeship distributed to an Israel resident beneficiary, and it shall be deemed the beneficiary's income on condition that all of the following hold true:
- (1) the distribution took place before six months had elapsed after the end of the tax year in which the income was produced or accrued or up to the date for submission of the return for the said tax year, whichever was earlier;
- (2) the income was included in the return submitted by the trustee under section 131 as distributed income, and it was not taken into account in the calculation of the trustee's income or chargeable income;

- (3) the income was included in the return submitted by the beneficiary under section 131 for that tax year;
  - (4) the trustee and the beneficiary attached to their returns under paragraphs (2) and (3), as the case may be, a notice of the distribution and of their choice that the distributed trust income be deemed the beneficiary's income;
  - (5) if income was produced by or accrued from different sources of income, then it shall be deemed to have been distributed proportionally from each said source of income, unless the writ of trusteeship prescribed that the distributed income was earmarked for the beneficiary who received it.
- (h) The provisions of section 75F and of subsections (b) to (h) shall not apply to a trusteeship of Israel residents that is a revocable trusteeship, in which there is only one creator who is an Israel resident, if the creator and the trustee gave notice of their choice that the creator be assessable and chargeable to tax for the trust income; for this purpose a creator and his spouse shall be deemed a single creator, provided the spouse is an Israel resident; a said application shall be submitted to the Assessing Officer together with the return under section 131 for the tax year in which the trusteeship was created; when such an application has been submitted, the following provisions shall apply:
- (1) the creator shall be the assessee and the person liable to tax in respect of the trust income, and he must submit a return thereon under section 131 as long as the creator still is alive;
  - (2) the creator's final tax debt in respect of the trust income may also be collected from the trust assets and from trust income;
  - (3) the creator's and trustee's choice shall also apply in coming tax years, and they cannot withdraw their choice as long as the creator is alive and an Israel resident.
- The provisions of this subsection shall apply as long as the creator is an Israel resident.
- (i) The provisions of section 100A shall not apply to a trusteeship of Israel residents on the day on which the creator ceases to be an Israel resident, as long as the trusteeship is an aforesaid trusteeship.

#### **Trusteeship that ceased being a trusteeship of Israel residents**

- 75H. (a) A trusteeship shall cease being a trusteeship of Israel residents from the date on which one of the conditions prescribed in section 75G(a) ceased to apply (in this section: the final day).
- (b) If a trusteeship ceased being a trusteeship of Israel residents and became a foreign resident beneficiary trusteeship, then for the purposes of the provisions of Part Five the trust assets shall be deemed to have been sold to a foreign resident on the final day.
- (c) If a trusteeship ceased being a trusteeship of Israel residents and became a trusteeship created by foreign residents, then the provisions of section 100A shall apply on the final day, mutatis mutandis.

#### **Trusteeship created by foreign residents**

- 75I. (a) A trusteeship created by foreign residents is a trusteeship, all creators of which were foreign residents when it was created and in the tax year, or all its creators and all its beneficiaries are foreign residents in the tax year.
- (a1) A trusteeship shall be deemed a trusteeship created by foreign residents, irrespective of whether it is a revocable trusteeship or an

- irrevocable trusteeship.
- (b) The provisions of section 75G – except for its subsections (a), (c) and (h) – shall apply to a trusteeship created by foreign residents, *mutatis mutandis*.
- (c) A trusteeship created by foreign residents shall be deemed a foreign resident, and the trust assets shall be deemed assets held by a foreign resident and the trust income the income of a foreign resident individual; if the creators are residents of several foreign countries, then the trust assets shall be deemed to be held in proportional parts by individual residents of their creators' countries of residence, and the trust income shall be deemed to have been produced or accrued for individual residents of those countries, in proportion to the value of the assets vested in the trustee by each creator, as it was on the day of vesting.

#### **Foreign resident beneficiary trusteeship**

- 75J. (a) A foreign resident beneficiary trusteeship is a trusteeship in respect of which all the following held true in the tax year, on condition that the provisions of section 75G(a)(1) do not hold true for it and that it is not a trusteeship under a will:
- (1) it is an irrevocable trusteeship; for purposes of this section a trusteeship shall not be deemed a revocable trusteeship only because of the provisions of section 75D(a)(3) or (4);
  - (2) all its beneficiaries are individual foreign residents, whose identity is known; for this purpose an unborn beneficiary shall be deemed a beneficiary whose identity is known;
  - (3) at least one of its creators is an Israel resident;
  - (4) if, at the time it was created, the conditions said in paragraphs (1) to (3) held true for it, then the following also held true –
    - (a) the trusteeship documents explicitly provide that no Israel resident beneficiary can be added;
    - (b) in a notice that the creator submitted under section 75P1 it was declared that in it there is no Israel resident beneficiary and no Israel resident beneficiary whose entitlement under the trusteeship is conditional on his ceasing to be an Israel resident, and that no beneficiary as aforesaid can be added to it.
- (b) In a foreign resident beneficiary trusteeship the trust assets shall be deemed the beneficiary's assets and the trust income the beneficiary's income.
  - (c) A foreign resident beneficiary trusteeship shall be deemed a foreign resident, and the trust assets shall be deemed assets held by an individual foreign resident, and the trust income shall be deemed the income of an individual foreign resident; if the beneficiaries are residents of several foreign countries, then the trust assets shall be deemed to be held in proportional parts by individual residents of the beneficiaries' countries of residence, and the trust income shall be deemed to have been produced or accrued for individual residents of those countries, in proportion to their shares of the trust income and the trust assets.
  - (d) In respect of the provisions of the Ordinance, vesting a trustee in a foreign resident beneficiary trusteeship shall be charged tax, as it would have been if the asset had been transferred directly by the creator to the foreign resident beneficiary.
  - (e) A distribution to the beneficiary of a foreign resident beneficiary trusteeship shall not be deemed a sale for purposes of the provisions of

Part Five.

- (f) Every year the trustee shall attach to the return he submits under section 131, on a form prescribed by the Director, a notice about every distribution made in the course of the tax year, including the names of the beneficiaries and the amounts distributed to them, as well as a declaration said in subsection (a)(4)b), but if the trustee does not have to submit a return under section 131 for that tax year, then he shall submit the said declaration to the Assessing Officer until April 30 of the year after the tax year.

**Partnership that ceased to be a foreign resident beneficiary trusteeship**

- 75K. (a) If one of the beneficiaries of a trusteeship became an Israel resident for the first time, a veteran returning resident or a returning Israel resident, as said in section 14(a) or (c), then the trusteeship shall cease being be a foreign resident beneficiary trusteeship; beginning with that day, the provisions of section 75G shall apply to the trusteeship, as well as provisions under sections 14(a) or (c), 16 or 97(b) or (b3), as the case may be, as they would have applied, if the income were produced directly by the beneficiary who became an Israel resident.
- (b) If the trustee did not submit the notification and declaration said in section 75J(f) for a certain tax year, then it will be deemed that there was an Israel resident beneficiary in the trusteeship in that tax year and the provisions of section 75G shall apply.
  - (c) If the Assessing Officer concluded that – in spite of the creator's and the trustee's declarations – the conditions said in section 75J(a)(4)(b) were not complied with, or that the trusteeship is a revocable trusteeship, then the trusteeship shall be deemed not to have been a foreign resident beneficiary trusteeship from the beginning and the Assessing Officer shall assess the trust income accordingly; for the purposes of this section, a trusteeship shall not be deemed a revocable trusteeship only because of the provisions of section 75D(a)(3) or (4); if, when the said assessment is being made, the trustee has final assessments for preceding years, then the Assessing Officer may – notwithstanding the provision of any statute – assess the trust income in those years within two years after the end of the tax year in which he concluded as aforesaid.

**Trusteeship under a will**

- 75L. (a) A trusteeship under a will is a trusteeship for which all the following hold true:
- (1) the trusteeship was created under a will;
  - (2) all creators of the trusteeship are testators who were Israel residents at the time of their demise.
- (b) In a trusteeship under a will the trust income shall be deemed the beneficiary's income and the trust assets shall be deemed the beneficiary's assets.
  - (c) (1) If there is at least one Israel resident beneficiary in the trusteeship under a will, then the trusteeship shall be deemed an Israel resident, and the trust income shall be treated like an Israel resident's income and the trust assets shall be treated like assets held by an Israel resident.
  - (2) If there is no Israel resident beneficiary in the trusteeship under a will, then the provisions of subsections (c) and (e) of section 75J shall apply to the trusteeship.

- (d) Vesting in the trustee in a trusteeship under a will and distribution to a beneficiary in a said trusteeship shall not be deemed sales for the purposes of Part Five.
- (e) The provisions of section 75F and of this section, other than subsections (d) and (g), shall not apply to a trusteeship under a will with only one beneficiary who is an Israel resident, if the beneficiary and the trustee requested that the beneficiary be assessable and chargeable to tax; for this purpose, a beneficiary and his spouse shall be deemed one beneficiary, provided the spouse is an Israel resident; a said request shall be submitted to the Assessing Officer as said in section 75G(h), and the provisions prescribed in paragraphs (1) to (3) of the said section shall apply, mutatis mutandis.
- (f) The provisions of section 75G(g) shall also apply, mutatis mutandis, to trusteeships under a will.
- (g) If under the trusteeship under a will at least one beneficiary becomes an Israel resident for the first time, a veteran returning resident or a returning resident, as said in section 14(a) or (c), and if in that tax year there was no other Israel resident beneficiary in the trusteeship, then – in addition to the provisions of section 75F – the provisions of sections 14(a) or (c), 16 or 97(b) or (b3), as the case may be, shall also apply to the trust income.
- (h) If the beneficiary of a trusteeship under a will ceased to be an Israel resident, then on that date the provisions of section 100A shall apply, mutatis mutandis.

#### **Vesting by a body of persons**

- 75M. If a body of person vested an asset in a trustee, then the following provisions shall apply: (1) the vesting shall be deemed a sale for purposes of the provisions of the Ordinance;
- (2) the vested asset shall be treated like a dividend distributed to the individual shareholders, who directly or indirectly hold rights in that body of persons.

#### **Distribution to the beneficiaries after the end of the trusteeship**

- 75N. (a) If a trusteeship of Israel residents or a trusteeship created by foreign residents came to an end and if, after its assets were distributed, losses remained that had not been set off and which – had they been profits – would have been liable to tax in Israel, then the losses shall be deemed losses of the creator; if the trusteeship had several creators, then a proportional part of the losses shall be deemed the loss of each of the creators, according to the value of assets vested in the trustee, as it was at the time of the vesting.
- (b) If a foreign resident beneficiary trusteeship or a trusteeship under a will came to an end, and if, after its assets were distributed, losses remained that had not been set off and which – had they been profits – would have been liable to tax in Israel, then the losses shall be deemed losses of the beneficiary; if the trusteeship had several beneficiaries, then a proportional part of the losses shall be deemed the loss of each of the beneficiaries, according to his proportional part in the distribution of the assets and the income, as it was during the four year period that ended at the end of the year in which the trusteeship ended.
  - (c) At the end of the trusteeship the trust losses shall be classified according to sources of income, as they were classified by the trustee, and the losses of the trustee transferred from previous tax years shall be



deemed transferred losses of the creator or of the beneficiary, as the case may be.

- (d) In respect of the calculation of the capital gains by a beneficiary to whom an asset was distributed and in respect of the asset's depreciation, its original price, the balance of its original price, and the day of its acquisition shall be as they would have been for the trustee, and the amount of depreciation shall be the amount which the trustee was entitled to deduct in respect of that asset.

#### **Provisions on tax payments, collection, returns and penalties**

- 75O. (a) The provisions of any statute on the payment of tax, on returns, collection and penalties shall apply to the trustee in respect of the trust income and the trust assets, except where an explicitly different provision is made in this Chapter.
- (b) In a trusteeship of Israel residents a final tax debt of the trustee may be collected from each of the creators, even if he ceased being an Israel resident.
  - (c) The provisions of subsection (b) shall also apply, if the Assessing Officer found in respect of a certain foreign resident beneficiary trusteeship that – notwithstanding the creator's and the trustee's declarations – the conditions prescribed in section 75J(a)(4)(b) were not complied with.
  - (d) If the trustee has a final tax debt, then it can also be collected from every beneficiary, to whose credit distribution was made after the beginning of the tax year, in respect of which the debt exists, whether the trusteeship has ended or not; however, no more shall be collected from any beneficiary than the final tax debt or than the amount or the value of the assets he received in the distribution, whichever is less.
  - (e) The trustee of a trusteeship created by foreign residents, the trustee of a foreign resident beneficiary trusteeship, and also a trustee of a trusteeship created under a will in which there is no Israel resident beneficiary does not have to submit a return under section 131 about the trust income created or accrued abroad, also if the trustee is an Israel resident and if he submitted a return under section 131 about income produced or accrued in Israel.
  - (f) In this section, "**final tax debt**" – as defined in section 119A(d), and also fines imposed under this Ordinance or under the Taxes (Arrears Fine) Law 5741-1980.

#### **General provisions**

- 75P. (a) If a trusteeship had more than one trustee, then the trustees are jointly and severally liable for the tax applicable to the trust income.
- (b) A trust asset holding company shall not be obligated to submit a return under section 131 or to pay tax in respect of trust income or in respect of trust assets that it holds for a trustee.
  - (c) The fact that a trustee is an Israel resident does not create a tax liability or an obligation to submit a return in respect of trust income, in addition to the obligations specified in this Chapter, such as would not exist if all the trustees were foreign residents.

#### **Creator's obligation to give notice**

- 75P1.(a) If, in a tax year, an Israel resident creator created a trusteeship or vested an asset or income from an asset in a trustee, then he must submit a notice to the Director within 90 days after creation of the trusteeship or after the vesting, as the case may be.

- (a1) In respect of a creator who became an Israel resident for the first time or a veteran returning resident as said in section 14(a) the provisions of subsection (a) shall not apply during ten years from the date on which he became an Israel resident as aforesaid, on condition that – during the entire said period – he vested only assets abroad or income from assets abroad; at the end of the said ten years the provisions of subsection (a) shall apply, but the notice said there shall be submitted until April 30 of the first tax year after the end of that period; if the obligation to submit a return under section 131 applies to the creator, then the said notice shall be submitted when the return is submitted.
- (b) The notice said in subsection (a) shall be submitted on the form prescribed by the Director, and the following shall be specified in it:
  - (1) the particulars of each of the creators and of each of the beneficiaries, the particulars of the trustee and of the trusteeship protector, if there is one, and the residential status of each of these;
  - (2) the particulars of the assets vested in the trustee or of which the income was vested in the trustee, including the original cost, the balance of the original cost and the day of acquisition, all as defined in section 88, the value of the acquisition and the date of acquisition within their meaning in Chapter Three of the Real Estate Taxation Law, and the balance of the acquisition value, as defined in section 47 of the said Law, as the case may be, as well as particulars of the income from the said assets that was vested in trustee;
  - (3) the date on which the said assets or income, as the case may be, were vested.
- (c) (1) Without derogating from the provisions of subsection (a), a creator of a trusteeship created by foreign residents that became a trusteeship of Israel residents or a foreign beneficiary trusteeship because the creator became an Israel resident must submit a notice to the Director by April 30 of the tax year after the tax year in which the creator became an Israel resident, but if the creator is under obligation to submit a return under section 131 – at the time for submitting the return; a said notice shall be submitted on a form prescribed by the Director and the particulars said in subsection (b) shall be specified in it, but in respect of the particulars of the assets and income, as said in subsection (b)(2), the creator shall specify the particulars of the assets and income that he vested in the trustee during the five years before the tax year in which the creator became an Israel resident.
- (2) Notwithstanding the provisions of paragraph (1) –
  - (a) a creator said in paragraph (1), who became an Israel resident for the first time or a veteran returning resident as said in section 14(a) shall not be obligated to give notice as said in that paragraph during ten years after the date on which he became an Israel resident as aforesaid, on condition that – when he became an Israel resident – the trustee in the trusteeship had only assets abroad or income from assets abroad and that during that entire period only aforesaid assets or income were vested in the trustee; at the end of the said ten years the provisions of paragraph (1) shall apply, but the dates for the submission of the notice said in that paragraph shall be in the first tax year after the

- said period ended, as the case may be; if, during the said ten years assets in Israel or income from assets in Israel were vested in the trustee, then the provisions of paragraph (1) shall apply, but the dates for the submission of the notice said in that paragraph shall be in the first tax year after the said period ended;
- (b) a creator said in paragraph (1), who became an Israel resident for the first time or a veteran returning resident as said in section 14(a) shall have to give notice as said in that paragraph at the times stated there, if – when he became an Israel resident – the trustee in the trusteeship had assets in Israel or income from assets in Israel; however, in respect of the particulars of the assets and of the income said in subsection (b)(2) the creator shall only specify the particulars of the assets in Israel and of the income from assets in Israel, which the creator vested in the trustee during the five years before the tax year in which the creator became an Israel resident.

**Obligation of trustee to submit notice**

- 75P2.(a) The trustee of a trusteeship shall submit a notice to the Director, on a form prescribed by the Director, on the following matters:
- (1) the creation of a trusteeship under a will – within ninety days after provisions of the will on setting up the trusteeship were carried out;
  - (2) a change of the category of a trusteeship – until April 30 of the tax year after the tax year in which the category of the trusteeship was changed, but if the trustee is under obligation to submit a return under section 131(a)(5b) in respect of that trusteeship – at the time for submitting the return; the provisions of this paragraph shall not apply to the change in the category of a trusteeship to a trusteeship of Israel residents because one creator thereof or one beneficiary thereof, as the case may be, became an Israel resident for the first time or a veteran returning resident as said in section 14(a), on condition that – when he became an Israel resident as aforesaid – the trustee in the trusteeship had only assets abroad or income from assets abroad.
  - (3) the conclusion of a trusteeship of Israel residents, the conclusion of a trusteeship under a will that is deemed an Israel resident trusteeship under section 75L(c)(1) or the conclusion of a trusteeship that at its conclusion held assets in Israel – until April 30 of the tax year after the tax year in which the trusteeship was concluded; however, if the trustee or the creator is under obligation to submit a return under section 131(a)(5b) in respect of that trusteeship – at the time for submitting the return; a said notice shall include the particulars of the assets that were distributed to beneficiaries because of the conclusion of the trusteeship, and in respect of a trusteeship that held assets in Israel at the time of its conclusion – particulars of the assets in Israel that were distributed to beneficiaries because of the conclusion of the trusteeship.
- (b) The provisions of subsection (a) shall apply to a creator who elected to be assessable and chargeable, to a representative creator and to a representative beneficiary, as the case may be, according to provisions under sections 75F1, 75G(h) or 75L(e), *mutatis mutandis*.

### **Obligation of beneficiary to submit notice**

- 75P3. (a) If an Israel resident beneficiary received an asset that is not money from a trustee in a distribution, even if the distribution is not liable to tax in Israel, then he must submit a notice to the Director until April 30 of the tax year after the tax year in which the said distribution took place, but if the beneficiary is under obligation to submit a return under section 131 – on the date for submission of the return.
- (b) A notice said in subsection (a) shall be submitted on a form prescribed by the Director, and on it the beneficiary shall specify the particulars of the asset he received in the distribution and the date of the distribution.

### **Restrictions on applicability**

- 75Q. The provisions of this Chapter shall not apply to each of the following:
- (1) a trust fund, as defined in section 88, and also a joint investment trust fund abroad;
  - (2) a benefit fund;
  - (3) a trusteeship created to secure a certain obligation;
  - (4) an estate manager, a Court-appointed custodian, a trustee in bankruptcy, an appointee under section 350 of the Companies Law, a company liquidator, a receiver;
  - (5) a religious endowment that is a public institution, as defined in section 9(2);
  - (6) a trustee as defined in section 102.

### **The Minister's authority**

- 75R. The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe as follows:
- (1) provisions on granting credit to a trustee, creator or beneficiary in respect of taxes which the trustee, creator or beneficiary in that trusteeship paid to a foreign state on income that was charged tax both in Israel and abroad;
  - (2) provisions on how to calculate the trustee's chargeable income or the capital gain upon the sale of trust assets, including the matter of setting the original cost and the day of acquisition;
  - (3) provisions on taxing the trustee's income proportionally, according to the shares of individual foreign resident beneficiaries or individual foreign resident creators, on the conditions he prescribed, and the necessary adjustments, and for this purpose provisions on capital gains tax liability in respect of vesting, the amendment of assessments and the determination of income also after the dates prescribed in this Ordinance;
  - (4) conditions, limitations, provisions and adjustments for the purposes of this Chapter, including the matter of a trusteeship that ceased being a trusteeship of Israel residents, a trusteeship created by foreign residents or a foreign resident beneficiary trusteeship.

## **CHAPTER FIVE: UNDISTRIBUTED PROFITS OF A SMALL COMPANY**

### **Applicability**

76. (a) The provisions of this Chapter apply to every company which is under the control of at most five persons and which is not a subsidiary or a company in which the public has a real interest (hereafter: small

- company).
- (b) For purposes of this Chapter: "**company under the control of at most five persons**" – a company in which five or fewer persons, directly or indirectly, jointly control, are able to control, or are entitled to acquire aforesaid control of the company's affairs, and particularly, but without derogating from the generality of the aforesaid, jointly hold or are entitled to acquire most of the share capital or of the voting power in the company, or most of the company's issued share capital or that part of it which would, if the company's entire income were distributed to the members, entitle them to receive most of the amount distributed.
  - (c) For the purposes of this section: "**subsidiary**" – a company, in which shares representing not less than 80% of its share capital are held or controlled by a company or companies to which the provisions of this Chapter do not apply.
  - (d) When determining whether a company is or is not under the control of five persons, the following shall be deemed a single person:
    - (1) a person and his relative; for this purpose: "**relative**" – spouse, brother, sister, parent, parent's parent, descendant, the spouse's descendant and the spouse of any of these;
    - (2) a person and his representative;
    - (3) partners in a partnership.
  - (e) Nothing said in this Chapter shall prevent from appealing according to sections 153 to 158 against a decision by the Director in the exercise of powers conferred on him by sections 77 and 78.

#### **Undistributed profits that are deemed to have been distributed**

77. (a) If the Director finds that a small company did not, by the end of twelve months after any tax year (hereafter: the said period) distribute its taxable profits for that year or some part of them to its shareholders in the form of dividends, and that it is able to distribute its profits or part thereof without detriment to the existence and development of its business, and that the effect of non-distribution is an avoidance or reduction of tax, then he may – within three years after the end of the said period, after he consulted with the committee for which provision is made below and after he gave the company a reasonable opportunity to be heard – direct the Assessing Officer to treat those undistributed profits as if they had been distributed as dividends.
- (b) When an aforesaid direction has been issued, the shareholders concerned shall be assessed or have their assessments amended, as if the sums treated as distributed had been received by them as dividends on the date or dates which the Director may find it just to determine, having regard to the date or dates on which the company distributed dividends, if any (hereafter: hypothetical dividend).
- (c) The Director shall not issue aforesaid directions if – before the end of twelve months after any tax year – the company distributed as dividends an amount that is not less than 75% of its taxable income in that tax year.

#### **Hypothetical dividends of small companies**

78. A hypothetical dividend from a certain small company (hereafter: the first company) to a shareholder that is also a small company (hereafter: the second company) shall not be liable to tax as income of the second company, but shall be treated as a dividend distributed by the second company on the date prescribed by the Director under section 77, and the shareholders of the

second company shall be assessed or have their assessments amended accordingly; if a shareholder of the second company also is a small company, then the provisions of this section shall apply, mutatis mutandis as the case may be, to the hypothetical dividend as though any reference here to the first company were a reference to the second company, and any reference to the second company were a reference to that shareholder, and so on until, applying the same principle, no part of the profits to which the Director's directions relate and which must be treated as distributed to a small company remains undistributed.

#### **Unpaid tax to be debt of company**

79. If a person was assessed to tax or had his assessment amended in accordance with the provisions of sections 77 or 78, and if he did not pay all or part of the tax attributable to his share in a hypothetical dividend on time, then the unpaid amount shall become a debt due to the Government from the company, because of whose failure to distribute the profits the directions of the Director under section 77 were made, and it may be recovered the way a debt is recovered.

#### **Undistributed profit that was subsequently distributed**

80. When undistributed profits liable to tax under sections 77 and 78 are subsequently distributed, then they shall not be treated as taxable income of their recipients.

#### **Advisory Committee**

81. A committee of five, at least three of them not State employees, shall advise the Director on the use of the power conferred upon him by this Chapter; that committee shall be chosen – when the need arises – by the Director from a list drawn up by the Minister of Finance in a notice published in Reshumot.

## **CHAPTER SIX: SPECIAL TRANSACTIONS**

#### **Interpretation**

82. (a) **"Disposition"**, for purposes of section 83, 84 and 86 – includes vesting, a contract, an agreement, an arrangement or a transfer of assets.  
(b) In cases to which these sections do not apply, no provision of sections 83 and 84 shall prevent income by virtue of disposition from being treated as if it were the income of the disposer.

#### **Dispositions in favor of juveniles**

83. If income is payable to a person or to his benefit during a certain tax year by virtue or in consequence of a disposition made during the disposer's life and while the disposer is still living, and if that person had not yet reached age 20 at the beginning of that tax year and was not married, then that income shall, for purposes of this Ordinance, be treated as if it were the disposer's income in that tax year and not the income of any other person; it is immaterial, for this purpose, whether the income is paid directly or indirectly, whether to that person or to his benefit, whether at present or in the future, and whether it is paid upon the fulfillment of a condition or after an event, the occurrence of which is in doubt, or as the result of the exercise of a power or discretion conferred on any person, or in any other way, and whether it is income which – under Chapter Five – the person is deemed to have received as aforesaid.

### **Revocable dispositions**

84. (a) If income is paid to a person in any tax year by virtue or in consequence of a revocable disposition, whether made before or after this Ordinance came into effect, as well as said income which under Chapter Five is deemed to have been received by that person, then – for purposes of this Ordinance – it shall be treated as the disposer's income in that tax year and not as any other person's income.
- (b) For the purposes of subsection (a), a disposition shall be deemed to be revocable if it includes any provision for the direct or indirect transfer or return of the income or of the asset from which it is derived to the disposer or to his spouse, or if the disposer or his spouse has the direct or indirect power, in any manner whatsoever, to receive or to recover direct or indirect control over the income or over the asset from which it is derived.

### **Valuation of trading stock in certain cases**

85. (a) In calculating the earnings or profits from business for the purposes of this Ordinance, trading stock which belongs to that business shall, in the cases said below, be deemed as having been sold at the amount of its value:
- (1) trading stock that belonged to a business when it was discontinued or transferred;
  - (2) trading stock which was removed or transferred out of the business not for consideration or not for full consideration, as well as trading stock in a business which was converted into a fixed asset of that business.
- (b) For the purposes of sections 21 and 88, the amount of the value of trading stock which was converted into a fixed asset and which is taken to have been sold as said in subsection (a) shall be its original cost
- (c) In this section –
- "trading stock"** – any movable or real asset that is sold in the ordinary course of the business, or which would be so sold if it were ripe or if its manufacture, preparation or construction had been completed, and any material used in the manufacture, preparation or construction of that asset;
- "business"** – includes part of a business;
- "amount of value"** – the amount which it was possible to obtain for the trading stock upon its sale by a willing seller to a willing buyer, free of any encumbrance intended to secure a debt, mortgage or other right to secure a payment; however, if the Assessing Officer is satisfied that the price of the stock was set in good faith, without being affected, directly or indirectly, by the existence of special relations between the seller and the buyer – and in the case of real assets also on condition that the sale was made in writing – then the price set shall be the amount of value.
- (d) (1) Notwithstanding the provisions of subsection (a)(2), trading stock specified below shall be deemed to have been sold at cost:
- (a) a building converted into a rental building, as defined in section 53A of the Encouragement of Capital Investments Law 5719-1959 (hereafter in this subsection: the Encouragement Law);
  - (b) a plot of land included in a project approved for the erection of a rental building under the Encouragement Law, within its meaning in the said Law, on which a rental building, within

- its meaning in section 53A of the said Law, was built;
  - (c) a building or a plot said in subparagraphs (a) or (b), which was transferred to the ownership of a company, all members of which are owners of the business, giving them rights to the property that are equal to their rights in the business, if the transfer to the company was according to a demand by the Board of the Investment Center, within its meaning in the Encouragement Law.
- (2) If a building or a plot on which a building was erected is sold – after some or all the provisions of subparagraph (1) were applied to it – by whoever received it under the circumstances said there, and if the Land Appreciation Tax Law 5723-1963 or section 4 of the Income Tax Law (Encouragement of Dwelling Rentals) (Ad Hoc Provisions and Law Amendments) 5741-1981 or Chapter Seven "A" of the Encouragement Law applies to the sale, then the day of acquisition and the seller's acquisition price for purposes of the said Laws shall be that day and that price which would have been determined, if the property had been sold by whoever transferred it to the seller; for this purpose: **"building"** – even if its construction has not yet been completed.

#### **Transfer prices in an international transaction**

- 85A. (a) If, in an international transaction, there are special relationships between the parties to the transaction, because of which the price for the asset, right, service or credit was determined, or other conditions for the transaction were set so that a smaller profit was realized therefrom than would have been realized, under the circumstances of the case, if the price or the conditions had been set between parties without a special relationship (hereafter: market terms), then the transaction shall be reported in accordance with market terms and charged tax accordingly.
- (b) For purposes of this section:
- "means of control"** – as defined in section 75B(a)(2);
  - "together with another"** – as defined in section 75B(a)(4), even if not Israel residents;
  - "special relationships"** – including relations between a person and his relative, and also control of one party to the transaction over the other, or control of one person over the parties to the transaction, whether direct or indirect, alone or together with another;
  - "control"** – the holding, direct or indirect, of 50% or more of one of the means of control;
  - "relative"** – as defined in section 76(d).
- (c) (1) An assessee must deliver to the Assessing Officer, at his demand, all the documents and data he has and that relate to a transaction or to a foreign resident party to the transaction, and also about the manner in which the price of the transaction was determined.
- (2) If the assessee delivered documents said in paragraph (1) and documents prescribed under subsection (e) to the Assessing Officer, then the onus of proof shall be on the Assessing Officer, if he prescribes anything that differs from what was agreed between the parties.
- (d) (1) A party to a transaction may apply to the Director and request advance certification that the price of a certain transaction or of a series of similar transactions, agreed between parties that have special relationships, is according to market terms.



- (2) The application shall include all the substantive facts and particulars that relate to the transaction and also the way its price was set, and documents, certifications, opinions, declarations, valuations, the transaction agreement or a draft thereof and every other document or particular, all as the Director shall prescribe in rules, shall be attached to it.
- (3) The Director may demand any additional document or particular, which he deems necessary for his decision on the application.
- (4) The Director shall announce his decision and the reasons for it within 120 days after the application and all the documents said in subparagraphs (2) and (3) reached him, but – for reasons that shall be recorded – he may extend the time up to 180 days, on condition that he informed the applicant of the extension before the end of the original period.
- (5) If the Director did not reply to the application within the period set in subparagraph (4), then that shall be deemed a priori certification that the transaction was carried out on market terms.
- (e) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe:
  - (1) in respect of all assessees or of categories of assessees, ways or methods of recognizing the price or conditions of a transaction as the market price or market terms, as the case may be, as well as provisions on relating income, expenses, deductions, credits and exemptions, all in cases to which the provisions of subsection (a) apply;
  - (2) a fee for the application for approval said in subsection (d) in the amount he shall set, and he may prescribe that the fee be a proportion of the value of the transaction;
  - (3) provisions on returns and documents to be submitted to the Assessing Officer and provisions on registration and documentation.

#### **Power to disregard certain transactions**

86. (a) If the Assessing Officer concludes that a certain transaction – which reduces or is liable to reduce the amount of tax payable by a certain person – is artificial or fictitious, or that a certain disposition was not in fact carried out, or that one of the principal objectives of a particular transaction is an improper avoidance or improper reduction of tax, then he may disregard that transaction or disposition and the person concerned shall be assessed accordingly; an avoidance or a reduction of tax may be deemed improper even if it is not contrary to Law; for this purpose, "**transaction**" includes an act.
- (b) No provision in this section shall prevent an appeal according to sections 153 to 158 against a decision by the Assessing Officer in the exercise of the discretion given to him by subsection (a).

#### **Allocations to unapproved funds and unlawful payments**

87. (a) The Minister of Finance may prescribe by regulations, with approval by the Knesset Finance Committee, rules on liability to tax, the person liable and the tax rates in respect of moneys specified below:
- (1) moneys paid by an employer, whose income is exempt of tax, to a fund or insurance scheme intended for the payment of savings, pension, severance pay, sick leave, vacation pay or for any other similar purpose, in respect of which no benefit fund certification

- was given under the Control of Benefit Funds Law, as well as moneys paid to a benefit fund, the said approval of which was canceled or which is managed by a company that does not hold a management company permit under the said Law, provided that no tax be imposed on money paid to a benefit fund before the date set as the date of cancellation of its permit, or as the date of cancellation of the management company permit, as the case may be;
- (2) moneys paid by a benefit fund to its members in violation of provisions under section 23 of the Control of Benefit Funds Law, or when a fund is wound up when there is no justifiable reason for the winding up in the Director's opinion, in consultation with the Commissioner, as defined in the said Law; the Director's decision under this paragraph shall, for the purpose of sections 153 to 158, be treated as if it were an Order under section 152(b).
- (b) For purposes of subsection (a) and of regulations made by virtue of it, the following shall also be deemed moneys paid in violation of regulations under section 23 of the Control of Benefit Funds Law:
- (1) money paid to a member not by way of a pension, including money paid by way of the capitalization of a pension by a pension benefit fund (hereafter in this section: pension benefit fund)
  - (2) money paid to a member not by way of a pension, including money paid by way of the capitalization of a pension by a benefit fund, including a pension benefit fund, that stems from deposits that enjoyed one of the following benefits:
    - (a) deposits to which the provisions of section 3(e3) were not applied;
    - (b) deposits, in respect of which he was entitled to tax credits at the rates set in section 45A(b);
    - (c) deposits, in respect of which he was entitled to an additional deduction under the closing passage of section 47(b)(1);
    - (d) deposits, to which rates of payment were applied as prescribed in regulations under section 22 of the Control of Benefit Funds Law, in respect of payments to pension benefit funds, and the rate exceeded the rate applicable at that time to a benefit fund that is not a pension benefit fund.
- (c) The provisions of subsection (b) shall not apply to the following:
- (1) moneys exempt of tax under section 9A(e);
  - (2) moneys payable because of an employer's obligation under the Severance Pay Law 5723-1963, to which section 9(7a) applies;
  - (3) money on which the amount of tax under section 2(5) and under sections 9A and 9B is greater than the amount of tax applicable under regulations made under subsection (a), and tax at the rates prescribed under the said sections shall apply to them;
  - (4) money withdrawn from a benefit fund in instances, for which the Minister of Finance prescribed in regulations under subsection (a) that the aforesaid tax not apply to them.

## PART FIVE: CAPITAL GAINS

### Definitions

88. In this Part –

**"means of control"** in a body of persons – each of the following:

- (1) the right to profits;
- (2) the right to appoint a Director or General Manager of the company, or holders of similar offices in other bodies of persons;
- (3) the right to vote at the company's General Meetings, or in the corresponding body of another body of persons;
- (4) the right to a share of the balance of assets after debts have been paid at liquidation;
- (5) the right to instruct the holder of one of the rights said in paragraphs (1) to (4) how to exercise that right;

all whether by virtue of shares, rights to shares or other rights, or in any other manner, including through voting or trusteeship agreements;

**"substantive shareholder"** – a person who directly or indirectly, alone or with another, holds at least 10% of one or more categories whatsoever of the means of control in a body of persons;

**"together with another"** – together with his relative, and also together with a person who is not his relative, if they regularly – directly or indirectly – cooperate by agreement on matters substantive to the body of persons.

**"asset"** – any property, real or movable, as well as any contingent or vested right or benefit, all whether they are in Israel or abroad, except –

- (1) movable property of an individual held by him for his personal use or the personal use of members of his family or of his dependents;
- (2) trading stock;
- (3) a right of possession, whether in Law or in equity, of real estate used for residential purposes, and not for earnings or profit;
- (4) real estate rights and association rights, within their meaning in the Land Appreciation Tax Law 5723-1963, the sale of which is chargeable with Land Appreciation Tax or would have been so chargeable, if not for the exemption under the said Law;

**"depreciable asset"** – an asset, for which a depreciation rate is set by regulations under section 21 or in respect of which depreciation was allowed, and which the assessee used for the purpose of producing income;

**"trading stock"** – within its meaning in section 85;

**"index"** – the consumer price index, as last published before the relevant date on behalf of the Central Bureau of Statistics and – in respect of the period before 1951 – the index determined by the Minister of Finance with the Knesset Finance Committee's approval; however, if a person, while a foreign resident, lawfully acquired any asset with foreign currency, then he may request that the exchange rate of the currency for which the asset was acquired be deemed the index; notwithstanding the aforesaid, in respect of a security held by an individual, denominated in foreign currency or value linked to a foreign currency, the currency exchange rate shall be deemed the index;

**"determining date"** – January 1, 2003;

**"original cost"** –

- (1) for a purchased asset – the amount spent by the assessee on that asset's acquisition;
- (2) for an asset obtained by way of exchange – the consideration at the time of the exchange;
- (3) for an asset received by way of gift –
  - (a) before December 3, 1951 – the asset's value when the assessee received it;
  - (b) from December 3, 1951 until March 31, 1968 – the balance of the original cost of the asset when it was given as a gift by the last acquirer who acquired it otherwise than as a gift, and for the

purposes of section 21, deduction of the depreciation shall be allowed, as if the asset had not been given as a gift;

- (c) on and after April 1, 1968 –
  - (1) if the asset was received as a gift not from a relative – the consideration on the day of the sale, and the said amount of consideration shall also be the original cost for purposes of section 21;
  - (2) if the asset was received as a tax exempt gift under section 97(a)(4) or (5) – the balance of the asset's original cost when it was given as a gift by the last acquirer who acquired it otherwise than as a tax exempt gift, and for the purposes of section 21 deduction of depreciation shall be allowed as if the asset had not been given as a gift;
- (4) for an asset received by inheritance – the asset's value on the day of the testator's death; if the asset's value was determined for purposes of inheritance tax, within its meaning in the Inheritance Tax Law 5709-1949, then that shall be the value for this purpose; however, if the testator died after March 31, 1981, then the value shall be that which would have been determined if the testator had sold the asset; the said value shall also be the original cost for purposes of section 21;
- (5) for an asset that the assessee produced – the amount expended by the assessee to produce the asset;
- (6) for an asset which came to the assessee in any other way – the amount expended by the assessee on the acquisition of that asset;

all with the addition of expenses incurred by the assessee for the asset's improvement or maintenance from the day he acquired it until the day he sold it, provided that they were not allowed to be deducted in the past in calculating the assessee's chargeable income (hereafter: improvement or maintenance expenses, as the case may be);

**"day of acquisition"** – the day on which, in any manner whatsoever, the asset came into the assessee's possession or on which the assessee became entitled to it, whichever is earlier; however –

- (1) if the asset came into the assessee's possession or the assessee became entitled to it by way of a gift before April 1, 1968, or even thereafter if the asset came into the assessee's possession by way of a tax exempt gift under section 97(a)(4) or (5) – the day on which the asset came into the possession of the last acquirer who acquired it not as a tax exempt gift;
- (2) if the asset came to the assessee by way of inheritance from a testator who died after March 31, 1981, or by way of another person's renunciation of his right to inherit from a said testator – the date that would have been set as the date of acquisition, had the testator sold the asset;

**"depreciation"** – the amounts deductible in respect of an asset under section 21, and also the amounts deducted from chargeable income in respect of the original cost of the asset;

**"balance of original cost"** – the original cost of an asset after the amounts of depreciation were subtracted from it;

**"balance of adjusted original cost"** – the balance of the original cost, not including the balance of improvement expenses and half the balance of maintenance expenses, multiplied by the index on the day of sale and divided by the index on the day of acquisition, plus the balance of each improvement expense multiplied by the index on the day of sale and divided by the index on the day the improvement was finished;

**"sale"** – includes exchange, renunciation, disposition, transfer, grant, gift, redemption and also any other act or occurrence in consequence of which the asset passes out of the control of a person, all whether directly or indirectly, but exclusive of inheritance;

**"security"** – according to the definition of "securities" in the Securities Law, including bonds or loans of the State of Israel or with its guaranty, bonds of foreign states, units, oil prospecting participation units, motion picture participation units, real estate association rights, securities issued abroad and also futures;

**"commercial security"** – according to the definition of "commercial securities" in the Securities Law;

**"future"** – an undertaking or a right to deliver or to receive any of the following: differentials between foreign currency exchange rates, index differentials, interest differentials, an asset or the price of an asset, all in the quantity, in the amount, at the time and on the conditions prescribed in the undertaking or in the right, as the case may be, and also the sale of a security not yet acquired by the seller;

**"oil prospecting participation unit"** and **"motion picture participation unit"** – within their meaning in regulations under sections 20, 31 and 93, as the case may be;

**"consideration"** – the price to be expected from the sale of an asset by a willing seller to a willing buyer, the asset being free of any encumbrance intended to secure a debt, of any mortgage and of any other right intended to secure payment; however, if the Assessing Officer is satisfied that the price of the asset was set in good faith and without being directly or indirectly affected by the existence of special relations between the seller and the buyer – and in respect of real estate, also on condition that the sale was made in writing – then the price set shall be the consideration; all less selling expenses incurred by the assessee in respect of that sale; when debentures or commercial securities are redeemed, the linkage differentials shall be deemed part of the consideration;

**"relative"** – each of the following:

- (1) spouse, brother, sister, parent, parent's parent, offspring and spouse's offspring, and the spouse of any of these;
- (2) offspring of a brother or sister, and brother or sister of a parent;
- (3) a body of persons controlled by a person or his relative, the person who holds it and a body of person held by the person that holds it; for the purposes of this definition: **"holding"** – direct or indirect, alone or with another, of at least 25% of one or more categories whatsoever of means of control;
- (4) a trustee, as defined in section 75C, in respect of the creator of a trusteeship of Israel residents or of a revocable trusteeship, as well as a trustee for the beneficiary of a foreign resident beneficiary trusteeship or in a trusteeship under a will;

however, in respect of a tax exemption under section 97 only those enumerated in paragraphs (1) and (2) shall be deemed relatives;

**"capital gain"** – the amount by which the consideration exceeds the balance of the original cost;

**"inflationary amount"** –

- (1) the part of the capital gain that equals the amount by which the adjusted balance of the original cost exceeds the balance of the original cost;
- (2) and (3) repealed

**"chargeable inflationary amount"** – each of the following:

- (1) repealed
- (2) the amount that would have been deemed the inflationary amount, had the asset been sold on December 31, 1993, the consideration being the adjusted balance of the original cost;
- "real capital gain"** – the capital gain, less the inflationary amount;
- "real capital gain up to the determining date"** – real capital gain, multiplied by the ratio between the period from the day of acquisition until the day before the determining date and the period from the day of acquisition until the day of the sale; the Minister of Finance may prescribe rules for rounding off the said periods;
- "balance of real capital gain"** – the differential between the real capital gain and the real capital gain up to the determining date;
- "capital loss"** – the amount by which the balance of the original cost exceeds the consideration;
- "real estate investment fund"** – as defined in section 64A2;
- "trust fund", "unit", "unit holder", "fund agreement" and "prospectus"** – within their meaning in the Joint Investment Trusts Law;
- "chargeable trust fund"** – a trust fund, in the fund agreement or in the prospectus of which it was determined – by a determination that cannot be changed – that it shall be a chargeable trust fund;
- "exempt trust fund"** – a trust fund, in the fund agreement or in the prospectus of which it was determined – by a determination that cannot be change – that it shall be an exempt trust fund.

#### **How to deal with consideration and capital gain**

- 89. (a) The consideration shall be treated like income under section 2, and a capital gain like chargeable income, all mutatis mutandis as the case may be, as long as there is no other explicit or implicit provision in this Part or in Part Five "A".
- (b) (1) An Israel resident is liable to tax on a capital gain accrued or produced in Israel or abroad; for this purpose: **"Israel resident"** – including an Israel citizen within its meaning in paragraphs (1), (3) and (4) of the definition of "Israel citizen" in section 3A, who is a resident of an area, as defined in the said section;
- (2) a foreign resident is liable to tax on a capital gain accrued or produced in Israel;
- (3) in any of the following instances the place where a capital gain was produced or accrued is Israel:
  - (a) the sold asset is in Israel;
  - (b) the sold asset is abroad and in essence it is a direct or indirect right to an asset or to stock in trade, or it is an indirect right to a real estate right or to an asset in a real estate association located in Israel (in this section: the property), in respect of the part of the consideration that stems from the property located in Israel;
  - (c) a share or the right to a share in an Israel resident body of persons;
  - (d) a right in a foreign resident body of persons, which in essence is the owner of a direct or indirect right to property located in Israel, in respect of that part of the consideration that stems from the property located in Israel.
- (c) If the profit from the sale of any asset may be liable to tax both under Chapter One of Part Two and under this Part or Part Five "A", then it shall be deemed liable to tax only under Chapter One of Part Two; the

Minister of Finance may, with approval by the Knesset Finance Committee, prescribe that certain sales of rights to an intangible asset for periods he designated shall be classified as income under Chapter One in Part Two, all on conditions that he shall prescribe.

- (d) An amount received under a life insurance policy, the premiums for which were not allowed as an expense under section 32(10), shall, after the deduction of those premiums, be deemed chargeable with tax only under this Part.
- (e) Notwithstanding the provisions of subsection (c), linkage differentials received upon the redemption of debentures or commercial securities, from which income does not constitute income from a business or vocation, shall be deemed liable to tax only under this Part.

90. Repealed

### **Tax on capital gain**

91. (a) A body of persons shall be liable to companies tax on real capital gain at the rate at the rate prescribed in section 126(a).

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*NOTE: Under section 74(1) of Amendment No. 147, the following replaces the above subsection (a) in tax years 2006 to 2009 – Tr.*

- (a) A body of persons shall be liable to tax on real capital gain at the rate of 25%; however, the capital gain from the sale of a security, within its meaning in section 6 of the Inflationary Adjustments Law, as formulated before its repeal in the Income Tax Ordinance Amendment Law (Amendment No. 147) 5765-2005, other than a said capital gain by a body of persons to which the provisions of section 6 of the Inflationary Adjustments Law or provisions under section 130A did not apply before the publication of that amendment, shall be charged tax at the rate prescribed in section 126(a).

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- (b) (1) An individual shall be liable to tax on a real capital gain as said in section 121, at a rate no greater than 20%, and the capital gain shall be deemed the highest bracket of his chargeable income.
  - (2) Notwithstanding the provisions of paragraph (1), real capital gain as said in section 121, upon the sale of securities in a body of persons where the seller is an individual who was a substantive shareholder when the shares were sold or at any time within twelve months before the sale, shall be charged tax at a rate of no more than 25%.
  - (3) (a) Notwithstanding the provisions of paragraphs (1) and (2), capital gains from the sale of debentures, commercial securities, State loans and loans that are not index linked, shall be charged tax at a rate of no more than 15%, or 20% in respect of a substantive shareholder, and all the capital gain shall be deemed the highest bracket of his chargeable income.
  - (b) The Minister of Finance may, by Order, change the tax rate prescribed in subparagraph (a), in accordance with an index change.
  - (c) For purposes of this paragraph: "**not index linked**" – their nominal value or amount is not index linked, or is partly linked to all or part of the rate of increase of the index, all up to the redemption or repayment.

- (b1) (1) Notwithstanding the provisions of subsection (b), in respect of an asset, the day of acquisition of which was before the determining date, other than an asset that is good will for the acquisition of which nothing was paid, the real capital gain shall be charged tax at the following rates:
  - (a) on the real capital gain up to the determining date – as said in section 121;
  - (b) on the balance of the real capital gain – at the rate prescribed in subsection (b)(1), (2) or (3), as the case may be;
- (1a) upon the sale of a security of which the date of acquisition was before the determining date, for purposes of calculating the real capital gain up to the determining date and of the balance of capital gain, the real capital gain, after its reduction by the profits available for distribution, calculated as said in section 94B, shall be the real capital gain.

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*NOTE: Under section 74(2) of Amendment No. 147, the following replaces the above paragraph (1a) in tax years 2006 to 2009 – Tr.*

- (1a) notwithstanding the provisions of subsection (a), a body of persons shall be liable to tax at the following rates in respect of an asset of which the date of acquisition was before the determining date, other than an asset that is a security within its meaning in that subsection or an asset that is good will, for the acquisition of which nothing was paid:
    - (1) on the real capital gain up to the determining date – at the rate prescribed in section 126(a);
    - (2) on the balance of the real capital gain – at the rate of 25%;
- 
- (2) For the purposes of this subsection, the capital gain shall be deemed the highest bracket of the chargeable income.
  - (b2) Notwithstanding the provisions of subsections (a), (b) and (b1), upon the sale of an oil prospecting participation unit or a motion picture participation unit, part of the capital gain, in the amount of the depletion allowance, in the amount of prospecting and development expenses or in the amount of the motion picture production expenses, which were allowed under regulations under sections 20, 31 and 98, as the case may be, shall be charged tax as said in section 121 in respect of an individual, and at the rate prescribed in section 126(a) in respect of a body of persons.
  - (c) The tax on the chargeable inflationary amount shall be 10%.
  - (d) (1) When an asset has been sold, then within thirty days after the sale the seller shall submit a return to the Assessing Officer on a form prescribed by the Director, specifying the calculation of his capital gain or capital loss and the tax calculation in respect of the said sale, and he shall pay an advance in the amount of the tax that applies to the profit under this section;
  - (2) If a return said in paragraph (1) was not submitted to the Assessing Officer, and if the Assessing Officer concludes that a certain person sold an asset and must pay an advance, then he may demand that a return be submitted and the advance paid within seven days after the demand, and if there is no response, then he may determine the original cost of the sold asset, the consideration received, and the amount of advance which the



seller must pay in respect of the capital gain; when the Assessing Officer has determined as aforesaid, then the advance shall be paid within seven days after the determination was served on the seller.

- (2a) If the Assessing Officer had reasonable cause to assume that the advance which the seller must pay in respect of the capital gain is at least 20% greater than the amount of advance specified in the return submitted under the provisions of paragraphs (1) or (2), then he may increase the amount of the advance by the amount of the expected differential; when the Assessing Officer has determined as aforesaid, then the differential shall be paid within thirty days after he gave his decision.
- (2b) A decision said in paragraphs (2) and (2a) shall be treated – in respect of contestation and appeal – like an assessment under section 145(b), but a decision under paragraph (2) can be contested only by submitting the return said in paragraph (1).
- (2c)
  - (a) The provisions of this subsection shall not apply to capital gain from the sale of a security, which is listed for trading on an Exchange, or from a single sale, if – at the time of the sale – capital gains tax was deducted under section 164.
  - (b) If the tax was not deducted as said in subparagraph (1) and if the seller must file a return under section 131, then – notwithstanding the provisions of paragraph (1) – the return about the capital gain shall be submitted on July 31 and on January 31 of each tax year in respect of securities sales during the six months that precede the month in which the reporting date occurs; when the said return is submitted as aforesaid, the advance shall be paid in the amount of the tax that applies to the capital gain under the provisions of this Ordinance.
  - (c) The Minister of Finance may – with approval by the Knesset Finance Committee – prescribe further instances to which the obligation to report and to pay an advance as said in this paragraph shall apply, both in respect of categories of assets and in respect of categories of assesseees, all with prescribed adjustments, conditions and changes.
- (2d) Notwithstanding the provisions of paragraph (1), upon the sale of a share in a body of persons, the liquidation of which was begun under section 93(a), the seller shall – within thirty days after liquidation was begun – give the Assessing Officer notice of the beginning of liquidation proceedings; if the liquidator transferred an asset to a member of that body of persons, as said in that section, then the member shall report his capital gain, as said in this subsection, within thirty days after the asset was transferred to him, and he shall pay tax at the rates prescribed in this section, as the case may be, of the value of the asset transferred as aforesaid; for purposes of this paragraph: "**asset**" – as defined in section 93(b6).
- (2e) If there is sufficient reason for doing so, the Assessing Officer may extend the time for the payment of an advance, and he may also postpone payment of the tax or reduce the amount of the advance, if he concludes that there it is reasonable that the capital gains tax will not apply or that the applicable tax will be in a different amount.
- (3) If the assessee did not pay all or part of the advance said in

paragraphs (1) or (2) on time, or if he paid a said advance and it subsequently is found that the tax due from him exceeds the tax paid, then he shall – from the end of the said 30 days until the date of payment –

- (a) pay linkage differentials and interest, within their meaning in section 159A(a), on the difference between the amount he paid and the amount of tax due from him;
- (b) repealed
- (3a) If the assessee was obligated to pay an advance under section 48A of the Land Appreciation Tax Law, or if a self assessment or final assessment was made for him under that Law, and if it is found that the tax he owes is greater than the tax which he was charged under the Land Appreciation Tax Law (hereafter: amount due), then he shall have to pay linkage differentials and interest, within their meaning in section 159A(a), on the difference between the amount payable and the amount of tax he was obligated to pay, from the end of the period prescribed in the Land Appreciation Tax Law until the day of payment.
- (4) If a person was obligated to pay linkage differentials and interest and a fine under paragraph (3), then he shall not – in respect of the same amounts and periods – be liable to the payments said in sections 187 and 190.
- (5) (a) If the assessee paid an advance said in paragraphs (1) or (2) or the amount of tax to which he is liable under the Land Appreciation Tax Law in excess of the amount due under the return filed by him under section 131, then the balance shall be refunded to him as provided in section 159A(b), with the addition of linkage differentials and interest within their meaning in section 159A(a) for the period from the day of payment until the day of the refund.
- (b) The provisions of section 159A(c) and (d) and of section 160 shall not apply to a refund said in subparagraph (a).
- (6) An amount deducted under sections 93(b4), 164 and 170 in respect of capital gains, shall be deemed a payment on account of the advance which the assessee must pay and he may set it off against the advance, on condition that he holds written certification of the deduction; however, a set-off against tax, to which a substantive shareholder is liable, shall be carried out only after the deducted amount was paid to the Assessing Officer, except when the substantive shareholder holds less than 50% of a certain category of means of control and he proved to the Assessing Officer's satisfaction that he did not know that the deducted amount had not been paid to the Assessing Officer, or that he took all reasonable steps to assure the payment.
- (e) (1) On the assessee's application, tax on a real capital gain shall be calculated as if the profit had accrued in equal annual installments over a period of not more than four tax years or over the period in which he owned the asset, whichever is shorter, ending with the year in which the profit accrued; however, in order to determine the advances under sections 174 to 181, the income in each year of the said period shall be deemed to have been increased by the annual installment; the tax calculation shall take into account the tax rate prescribed in subsection (b), and in respect of Appreciation Tax – take into account the tax rate prescribed in

section 48A(2) of the Real Estate Taxation Law, and also taking into account the tax rates that apply to the assessee's overall chargeable income and the balance of credit points to which the assessee is entitled in each of the tax years during the said period; for the purposes of this section, "**period of ownership of the asset**" – the period that began at the beginning of the tax year after the tax year in which the asset came into the assessee's possession and ended at the end of the tax year in which the asset left his possession.

- (2) If an asset is sold and the day of its acquisition was before the determining date or if a real estate right is sold or a real estate association act is carried out and the acquisition date of the real estate right or of the right in the real estate association, as the case may be, was before the initial day, then the provisions of paragraph (1) shall apply with the following changes:
  - (a) the real capital gain up to the determining date and the balance of real capital gain, or the real appreciation up to the initial date and the balance of the real appreciation, as the case may be, shall be calculated as they would have been calculated, if the assessee had not submitted the application said in paragraph (1);
  - (b) the tax calculation shall take into account the tax rates prescribed in subsection (b1) or in section 48A(b1) of the Real Estate Taxation Law, as the case may be, and it shall also take into account the tax rates that apply to all of the assessee's income and the balance of credit points to which he is entitled, as said in paragraph (1);
  - (c) in this subsection, **Areal estate right**, **Areal estate association right**, **"initial day"**, **Aappreciation tax**, **Areal appreciation up the initial day** and **Abalance of real appreciation** – as defined in the Real Estate Taxation Law.
- (f) (1) In respect of an asset acquired until tax year 1948, tax shall not exceed 12% of the capital gain, and in respect of an asset acquired in tax years 1949 to 1960 tax shall not exceed 12% of the capital gain, plus 1% for each year from tax year 1949 until the year of acquisition.
- (2) Beginning with tax year 2005, the tax rate said in subparagraph (1) shall be increased by 1% for every tax year or part thereof, but if the tax rate on capital gains in the year of the sale under the provisions of this subsection exceeds the rates prescribed in subsection (a) or (b)(1) or (2), as the case may be, then the capital gain shall be charged at the rates under the provisions of subsections (a) or (b)(1) or (2), as the case may be.
- (g) The tax on a capital gain upon the expropriation of any asset shall be half of the tax due according to subsections (a) to (f).
- (h) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe that – in respect of special occurrences or special circumstances under which assets were transferred between controlling members or linked parties – the tax rates said in sections 121 or 126 shall apply, as the case may be, notwithstanding the provisions of this section.

### **Set off of capital loss**

92. (a) (1) The amount of capital loss suffered by a person in a given tax year, which – had it been a capital gain – would have been chargeable with tax, shall be set off first against the real capital gain, and every new shekel of the balance shall be set off against NS3.50 of the chargeable inflationary amount; for this purpose, appreciation and loss shall be taken within their meaning in the Real Estate Taxation Law 5723-1963, as if they were a capital gain or a capital loss, as the case may be.
- (2) repealed
- (3) If a person incurred a capital loss from the sale of an asset abroad which – had it been a profit would have been liable to tax in Israel – then the provisions of paragraph (1) shall apply to it, but the capital loss from the said asset shall first be set off against a capital gain from abroad.
- (4) If a person incurred a capital loss from the sale of a security during the tax year, then the provisions of paragraphs (1) or (3) shall apply to him, as the case may be, but the capital loss shall also be set off against the following:
- (a) interest or dividend income paid in respect of that security;
- (b) interest or dividend income in respect of other securities, on condition that the tax rate applicable to the interest or dividends received by that person not exceed 25%;
- (5) expenses in respect of securities, as the Minister of Finance determined with approval by the Knesset Finance Committee, which were not deducted during the tax year, shall for this purpose be treated like capital losses from securities.
- (b) An amount that wholly or partly cannot be set off in a certain tax year, as said in subsection (a), shall be set off only against capital gain, as said in subsection (a), during the tax years that follow the year – one after the other – in which the loss was incurred, on condition that a return for the year in which the loss occurred was submitted to the Assessing Officer, as said in sections 131 and 132; if the amount that could not be set off is the loss from the sale of an asset abroad, then the loss shall first be set off against capital gains from the sale of assets abroad.
- (c) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions for the implementation of this section and provisions on returns and on ways of proving aforesaid losses, and he may also prescribe provisions to restrict the set off of some or all losses from the sale of securities, or prohibit said set-offs, prescribe the order in which losses are set off and profits are related, as well as ways of proving and provisions for the implementation of this section.

### **Capital gain in body of persons that was wound up**

93. (a) The following provisions shall apply to a body of persons, winding up of which has begun:
- (1) profit from the sale of an asset by the liquidator shall be deemed a taxable capital gain of that body of persons;
- (2) if the sale is by way of the liquidator transferring an asset from the body of persons to its member, then the consideration shall be taken to be as it was on the day of sale;
- (3) shares or other rights of a member in that body of persons shall be deemed to have been sold, and the assets received by that

- member from the liquidator shall be deemed the consideration for the said shares or rights;
- (4) capital gain in respect of a member of that body of persons shall be calculated after all the assets have been distributed; however, if distribution is not completed within two years after the day on which winding up began, then the assets shall be deemed to have been distributed at the end of that period, but the Director may extend the period if it is proved to his satisfaction that distribution was not completed for a reasonable cause.
- (b) repealed
- (b1) The provisions of this section shall also apply to the liquidation of a real estate association.
  - (b2) If there was a tax exempt transfer of real estate from the liquidator to a member under the provisions of section 71 of the Real Estate Taxation Law, then the following provisions shall apply:
    - (1) the original cost of the shares shall be deemed the original cost, less the original cost multiplied by the ratio of the value of the real estate right or of the association right, as the case may be, the sale of which was exempt of tax, to the amount obtained by adding the consideration received as said in section 93(a)(3) and the value of the real estate right or of the association right, the sale of which was exempt of tax, as it was on the day on which liquidation of the association began;
    - (2) for purposes of the provisions of section 94B of the Ordinance, the profits available for distribution – as defined in that section – shall be reduced by an amount equal to the additional profit, as it would have been if the real estate right had been sold on the day on which liquidation of the association began, on condition that the said additional profit is a positive amount;
  - (b3) in respect of subsections (b1) and (b2), every term shall have the meaning it has in the Real Estate Taxation Law, including section 71A there, unless a different meaning is explicitly provided;
  - (b4) a liquidator who transferred an asset of a body of persons, liquidation of which began, to a member thereof shall deduct from it – at the time of the transfer – tax at the following percentage of the asset's value:
    - (1) if the asset was transferred to a member that is a body of persons – at the rate said in section 91(a);
    - (2) if the asset was transferred to a member who was an individual substantive shareholder in the body of persons when the liquidation began or at any time within twelve months before that date – at the rate of 25%;
    - (3) if the asset was transferred to a member who is an individual for whom the conditions said in paragraph (2) do not hold true – at the rate of 20%;
 unless the Assessing Officer certified in writing that no tax be deducted, or tax at a lower rate than the aforesaid rates.
  - (b5) The tax said in subsection (b4) shall be paid to the Assessing Officer within seven days after the asset was transferred to the member; a return about the transferred asset and about the deducted tax shall be attached to the payment; within the said period the liquidator shall transmit to the member certification of the deduction on a form

- prescribed by the Director.
- (b6) For the purposes of subsections (a)(2) to (4), (b4) and (b5): "**asset**" – any property, real or movable, as well as any vested or prospective right or benefit, all whether in Israel or abroad, other than a real estate right or a real estate association right transferred to the member exempt of tax under section 71(a) of the Real Estate Taxation Law.
  - (c) The Minister of Finance may – with approval by the Knesset Finance Committee – prescribe special provisions on the definition of "asset" and "consideration", and he may also determine that this section apply to the winding up of real estate associations, as defined in the Real Estate Taxation Law, and the adjustments made necessary by aforesaid determinations.

### **Special provisions on liquidations in tax year 2003**

- 93A. (a) The provisions of section 93 shall not apply to the voluntary liquidation of a company, which began and was concluded in tax year 2003, and the sale of assets or activities shall not be charged tax under this Ordinance or under the Inflationary Adjustments Law, as the case may be, if all the following hold true:
- (1) the company was formed during a period from tax year 2002 until June 1, 2003, or it was formed before the said period, but had no assets, activity, income, expenses or losses before that period;
  - (2) the company was formed by an individual who has income from an vocation as said in section 2(1) or from employment as said in section 2(2) (in this section: service provider) and who is the controlling member of that company;
  - (3) the activity of the service provider was transferred to the company, and if assets or real estate rights, as defined in the Real Estate Taxation Law, were also transferred, then their purpose was not changed in the course of the transfer;
  - (4) the sale of the assets or activities is a sale without consideration to those shareholders, from whom the assets or activities were transferred to the company in accordance with their proportional share in the rights in the company, and their purpose was not changed in course of the sale;
  - (5) the company and the shareholders requested that the provisions of this section apply to the liquidation proceedings;
  - (6) in the course of the liquidation proceedings all profits available for distribution, all surpluses and all amounts of money left in the company (in this section: surpluses) were paid to the shareholders, all as the Minister of Finance prescribed with approval by the Knesset Finance Committee and they were charged tax for the shareholders under sections 2(1) or 2(2);
  - (7) other conditions, restrictions and adjustments prescribed by the Minister of Finance with approval by the Knesset Finance Committee.
- (b) Notwithstanding the provisions of Chapter Three in Part Five "B", a liquidation to which the provisions of this section apply shall not be deemed a violation of the conditions set there.
  - (c) The Director may approve application of provisions under this section to the voluntary liquidation of a company, even if it was concluded after tax year 2003, on condition that the conditions in subsection (a) and the following two conditions were met:
    - (1) the company did not have any income after tax year 2003;

- (2) all assets and activities of the company were sold to the shareholders, as said in subsection (a)(4), by the end of tax year 2003, and all the surpluses said in subsection (a)(6) were paid to them.
- (d) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions for the implementation of this section, as well as conditions and adjustments, inter alia in respect of original cost, the day of acquisition, setting off losses, calculation of the surpluses and calculation of capital gains, and he may also prescribe that – against the tax on the surpluses – credit shall be allowed on the tax paid by the company, if it had a loss that stems from the surpluses and can be carried forward to tax year 2004, all on conditions set by the Minister of Finance and on condition that no credit be allowed that is greater than the applicable amount of tax.

#### **Bonus shares and option certificates**

94. (a) When a person sells bonus shares allotted to him or the shares on which the bonus shares were allotted (hereafter: principal shares), then the following provisions shall apply:
- (1) a bonus share shall be treated as if it had been acquired on the day on which the principal share was acquired;
  - (2) the original cost of a single bonus share or a single principal share shall be an amount proportional to the original cost of the total of bonus shares and principal shares, in the ratio of the nominal value of that individual share to the nominal value of the total of those shares.
- The provisions of this subsection shall apply, mutatis mutandis, to units of a joint investment trust fund, within its meaning in the Joint Investment Trusts Law.
- (b) repealed
  - (c) If a person sold an option certificate in a company, the securities of which are not listed for trading on an Exchange, or if he sold the shares which he obtained by way of realizing the option certificate, then the Minister of Finance shall determine, by regulations with approval by the Knesset Finance Committee, the original cost and the acquisition date of the securities by virtue of which the option certificate was allotted, of the option certificate and of the securities obtained by realizing the option certificate.
  - (d) In this section –  
**"option certificate"** – a security that entitles its owner to acquire shares issued by a company against a realization supplement, at a price or on terms prescribed in the option certificate;  
**"bonus shares"** – including the bonus component in rights allocations or in shares that stem from aforesaid rights.
  - (e) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe rules for calculating the amount of the bonus component.

#### **Sale of loan together with shares**

- 94A. If an unlinked interest free loan is sold at least three years after a shareholder extended it to the company, together with shares or other rights which he has in that company, then the consideration for the loan shall be taken to be that part of the total consideration for shares and loan, as is equal to the adjusted balance of the original cost of the loan; a capital loss from the sale of shares,

due to the aforesaid calculation, shall be set off, shekel for shekel, against the capital gain from the loan.

**Profits available for distribution**

- 94B. (a) When the share of a company, the shares of which are not listed for trading on an Exchange, is sold by an individual and the day of acquisition of the shares was before the determining date, or by a body of persons, then the following provisions shall apply:
- (1) the tax rate on the part of the real capital gain that equals part of the profits available for distribution, in the proportion of the seller's part of the right to profits in the company to all rights to profits in the company, shall be the tax rate that would have applied to them under sections 125B or 126(b), as the case may be, if they had been received as dividends immediately before the sale.
  - (2) Notwithstanding the provisions of paragraph (1), the tax rate on the real capital gain that equals the part of the profits available for distribution – as said in paragraph (1) – until the determining date shall be 10%; for purposes of this section: **"the profits available for distribution until the determining date"** – the amount that would have been deemed profits available for distribution, if the share had been sold on the determining date.
- (a1) The provisions of subsection (a) shall apply, mutatis mutandis, to the sale of a share in a company, the shares of which are listed for trading on an Exchange, on condition that – on the date of the sale or on any date within the preceding twelve months – the seller of the share was a substantive shareholder in the company the shares of which are being sold.
- (b) For purposes of subsection (a):
- (1) **"profits available for distribution"** – aforesaid profits accumulated by the company from the end of the tax year before the year in which the share was acquired, until the end of the tax year before the year in which it was sold, and in the case of winding up – until the day on which winding up procedures are concluded, on condition that aforesaid profits available for distribution, which accrued before January 1, 1996, not be taken into account, all according to the company's balance sheet at the end of the tax year before the year of sale or before the day on which winding up began, as the case may be, including profits that were capitalized; however, amounts accumulated in a capital stabilization fund, within its meaning in section 53K of the Encouragement of Capital Investments Law 5719-1959, or amounts that were deductible under section 53Q of the said Law, or aforesaid profits in a cooperative society in those years, in which sections 56, 57, 61 and 62 applied to the calculation of its income and those profits were included in the balance of the original cost, shall not be deemed profits available for distribution, and the amount of profits available for distribution shall not exceed the amount of profits that were chargeable with tax – including Land Appreciation Tax – during the said period, less the tax on them and less dividends distributed out of them and with the deduction of any loss created and not set off in the company the shares of which are being sold, and with the addition of profits that would have been chargeable with tax as aforesaid, had they



- not been exempted;
- (2) an increase – within the two years that preceded the sale – of the part of the seller of the share in rights to the company's profits shall not be taken into account.
- (c) The provisions of subsection (a) shall apply, if the seller submitted to the Assessing Officer a calculation that shows the profits available for distribution, as said in subsection (b).

#### **Deduction of dividends**

- 94C When a share is sold by a body of persons, then the amount of capital loss due to the sale of the share shall be reduced by the amount of dividends, which the body of person received in respect of the share during the 24 months before the sale, but not by more than the amount of the loss; for this purpose:
- "**dividend**" – other than a dividend on which tax was paid at a rate of 15% or more;
- "**tax**" – other than tax paid abroad.

#### **Redemption of share in a cooperative society**

- 94D. (a) When the share of a member in a cooperative society is redeemed by the society at the society member's retirement after 25 years of work or membership in the society, or when the member retires because of his loss of working ability or at his death, and if the day of its acquisition was before the determining date, then the following provisions shall apply:
- (1) the redemption amount, multiplied by the ratio of the number of months from the acquisition of the share until the determining date to the number of months from the acquisition of the share until the redemption day (in this section: the exemption period ratio) shall be tax exempt up to an amount of NS317,000 (*in 2003 to 2008 – Tr.*), and the balance of the redemption amount shall be chargeable to tax;
  - (2) the original cost of the balance of the redemption amount, less the original cost multiplied by the exemption period ratio, shall be the original cost;
  - (3) the day on which the share was acquired shall be the day of acquisition of the balance of the redemption amount; however, if the amount exempt under subparagraph (1), less the adjusted original cost of the share, is less than NS 317,000 (*in 2003 to 2008 – Tr.*), then the day of acquisition or the first day of tax year 1961, whichever was later, shall be the day of acquisition.
- (b) For the purposes of this section: "**cooperative society**" – a society registered under the Cooperative Societies Ordinance, which in accordance with its objectives operates in one of the following spheres: transportation, haulage, production or services.

#### **Capital gain from the sale of shares in a company**

95. (a) If one or more persons derive a capital gain from the sale of an asset to a company only against shares in that company, then that profit shall not be charged with tax if, immediately after the sale, the seller or sellers hold at least 90% of the voting power in that company.
- (b) When the asset acquired by a company as said in subsection (a) is sold, and also when the shares received by the seller for the said asset are sold, then the balance of the original cost of that asset for the seller

said in subsection (a) shall be their original cost, and the date on which it was acquired by the person who sold it to the company shall be the date of the asset's acquisition.

- (c) This section shall apply to a capital gain obtained by one or several persons from an asset sold up to January 1, 1994.

#### **Capital gain from asset for which a depreciation rate was set**

96. If a capital gain accrued to an assessee from the sale of a depreciable asset and if – within twelve months after or four months before the day of its sale – he acquired another asset to replace the sold asset at a price that exceeds the balance of the original cost of the sold asset, then the assessee may claim that only the amount by which the consideration received for the sold asset exceeds the price of the acquired asset be deemed a capital gain and he may do so in respect of the entire capital gain or only in respect of the real capital gain; when he has done so, the original cost – for purposes of calculating the capital gain on the acquired asset when that is sold, and of the amount of depreciation allowed on it under section 21 – shall be reduced by any amount of capital gain which accrued to him upon the previous sale and which was not charged with tax because of the assessee's claim; the tax rates prescribed in sections 121 or 126, as the case may be, shall apply to the amount reduced as aforesaid, which equals the capital gain partly accrued before the determining date; for the purposes of this section: **"part of the capital gain accrued before the determining date"** – part of the capital gain, the ratio of which to the total capital gain is as is the ratio of the period between the day of acquisition and the determining date to the period between the day of acquisition and the day of the sale.

#### **Tax exemption**

97. (a) A capital gain shall be exempt of tax if it arises out of one of the following –
- (1) the sale of a debenture that is not convertible into a share and is traded on an Exchange in Israel, on condition that the debenture was issued before May 8, 2000, and was listed for trading on an Exchange in Israel before the determining date;
  - (2) the sale of a debenture or of a loan certificate issued or guaranteed by the State, on condition that it was issued before May 8, 2000;
  - (3) repealed
  - (4) a gift to the State, to a local authority, to the Keren Kayemet Le-Yisrael, to the Keren Hayessod – United Jewish Appeal for Israel, or to a public institution, within its meaning in section 9(2);
  - (5) a gift to a relative, as well as a gift to another individual, if the Assessing Officer is satisfied that the gift was made in good faith and on condition that the recipient of the gift is not a foreign resident;
  - (6) repealed
  - (7) an individual's capital gain from the sale or redemption of a unit in a chargeable trust fund.
- (b) (1) An individual became an Israel resident for the first time and a veteran returning resident, as said in section 14(a), shall be exempt of tax on the capital gain from the sale of any asset he had abroad, if he sells it within ten years after the day on which he became an Israel resident; for this purpose: **"asset"** – other than an asset received by the individual fully exempt of tax under subsection (a)(5) on or after January 1, 2007.

- (2) A returning resident, as defined in section 14(c) is exempt of tax on capital gains from the sale of assets he acquired abroad while he was a foreign resident, if the asset – including the right or the right in a foreign resident body of persons – is not a direct or indirect right to an asset located in Israel, all if he sold it within ten years after the day on which he became a returning resident; for this purpose, "**asset**" – including assets abroad that are benefited securities, as defined in section 14(c).
- (3) If the asset said in paragraphs (1) and (2) was sold after ten years had passed since the day on which the individual became an Israel resident as said in those paragraphs, then the part of the real capital gain until the end of the exemption period is tax exempt, and the balance of the capital gain is liable to tax at the rate prescribed in section 91(b); for this purpose: "**part of the real capital gain until the end of the exemption period**" – the real capital gain, multiplied by the ratio between the period from the day of acquisition until ten years after he became an Israel resident and the period between the day of acquisition until the day of sale.
- (b1) repealed
- (b2) A foreign resident is exempt of tax on capital gains from the sale of securities traded on an Exchange in Israel, if the capital gain is not in his permanent enterprise in Israel; if the day of acquisition of the security was before the day on which it was listed for trading on an Exchange, and if – had it been sold before the said listing – the foreign resident would not have been entitled to an exemption under subsection (b3), then the part of the capital gain that would have accrued if the security had been sold on the day before it was listed for trading on the Exchange and not more than the amount of the capital gain on the day on which the security was sold shall be charged tax at the rate prescribed in section 91, on condition that its value on the day of its listing is greater than its value on the day of its acquisition and that the consideration on the day of its sale is greater than its value on the day of its acquisition; the provision of this section shall not apply to the capital gain from the sale of a share in a real estate investment fund.
- (b3) (1) A foreign resident is exempt of tax on the capital gain he earned upon the sale of the security of an Israel resident company, or upon the sale of a right in a foreign resident body of persons, the main assets of which are rights, direct or indirect, in assets located in Israel, if all the following hold true:
  - (a) the capital gain is not in his permanent enterprise in Israel;
  - (b) repealed
  - (c) the security was not acquired from a relative and the provisions of Part Five "B", or the provisions of section 70 of the Real Estate Taxation Law did not apply to it;
  - (d) repealed
  - (e) repealed
  - (f) at the time of the sale the security is not traded on an Exchange in Israel
- (2) The provisions of paragraph (1) shall not apply to the capital gain from the sale of the security of a company, if – on the day of its acquisition and during two years before its sale – most of the assets it directly or indirectly held were real estate rights or real

- estate association rights.
- (3) The provisions of this subsection shall also apply, mutatis mutandis, to an individual who became an Israel resident for the first time or who is a returning veteran resident, as said in section 14(a), provided that he was a foreign resident when on the date of acquisition of the security, and the provisions of subsection (b) shall apply to the matter of capital gain, as if the security were an asset he had abroad before he became an aforesaid Israel resident.
  - (4) The Minister of Finance may – with approval by the Knesset Finance Committee – prescribe conditions, restrictions and provisions for purposes of this section.
- (c) Repealed
- (c1) The Minister of Finance may, by Order with approval by the Knesset Finance Committee, exempt of the payment of tax, in whole or in part, a capital gain that is one of the following:
- (1) a capital gain derived from certain types of transactions, on condition that they are not with assets traded or listed for trading on an Exchange or on an organized market, or in respect of assets traded or listed for trading as aforesaid;
  - (2) a capital gain from the sale of a debenture convertible into a share that is traded or listed for trading on an Exchange or on an organized market in Israel or abroad, either in general or for categories of assesseees, all on conditions he shall prescribe.

#### **Method of calculating capital gain**

98. Notwithstanding the provisions of this Part, the Minister of Finance may, by regulations, prescribe the method of calculating capital gains, both in general and for the purpose of deduction at the source, provided that such a general prescription requires approval by the Knesset Finance Committee.

98A. Repealed

#### **Demand for information**

99. The Director may require of a banking institution, within its meaning in the Bank of Israel Law 5714-1954, of a person whose business or part of whose business is trading in securities on behalf of other persons, or of a person who holds securities in his own name for others, that they deliver to him full particulars on the aforesaid trade in or the said holding of securities.

#### **Transfer of an asset to trading stock**

100. When the Assessing Officer is satisfied that a person transferred an asset that he owns to his business as trading stock, or that he converted a fixed asset in his business into trading stock in his business (hereafter in this section: transfer), then the following provisions shall apply:
- (1) if four years passed between the day on which the assessee acquired the asset and the day of the transfer, then the transfer shall be deemed a sale, but the assessee shall not be required to pay tax on it until the sale of all or part of the said trading stock; if he sold part thereof, he shall not have to pay tax to an amount exceeding the consideration received by him for that sale;
  - (2) if four years have not passed as aforesaid, the transfer shall not be deemed a sale, and the price at which the asset was acquired by the assessee shall be the balance of the original cost.

### **Person who ceased being an Israel resident**

- 100A. (a) The asset of a person who was an Israel resident and ceased being an Israel resident shall be deemed to have been sold one day before he ceased being an Israel resident.
- (b) If a person said in subsection (a) did not pay the tax on the day he ceased being an Israel resident, then he shall be deemed to have applied to postpone payment of the tax until the asset is realized, and at the time of the realization he shall pay the tax that was due for the sale of the asset when he ceased being an Israel resident, in an amount equal to the amount of tax on the part of the chargeable profit; however, linkage differentials and interest, as defined in section 159A, shall be added only from the date of the realization until the actual payment of the tax.
- (c) Notwithstanding the provisions of subsection (b), if the sale of the asset was liable to payment of tax in Israel when it was realized, then the tax due on the capital gain at the time of the realization shall be paid instead of the tax under the provisions of subsection (b).
- (d) For purposes of this section:
- "part of the chargeable profit"** – the real capital gain at the time of the realization, multiplied by the period of ownership from the day on which he acquired the asset until the day he ceased being an Israel resident, and divided by the entire period from the day of the asset's acquisition until the day of its realization;
- "realization"** – the actual sale of the asset;
- "asset"** – including shares and rights granted as said in sections 3(i) and 102.
- (e) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions for the implementation of this section, including provisions for the prevention of double taxation and on the submission of returns.

### **Conversion of private shares into shares traded on an Exchange**

101. (a) (1) The listing of a company's shares on an Exchange in Israel or the listing of the shares of a company resident in Israel on an Exchange abroad before tax year 2006 shall be treated like a sale of the shares on the date of the listing, unless the shareholder applied – when he first submitted a return under section 131 after the listing – that it not be so treated.
- (2) If a shareholder requested that listing the shares not be treated like their sale, as said in paragraph (1), then he shall be charged the tax when the shares are first sold after they had been listed and the provisions of section 97(b2) shall not apply.
- (3) Notwithstanding the provisions of paragraph (2), the shareholder may rescind his application when he first sells the shares as aforesaid and pay the tax that would have been due from him because of the listing, plus linkage differentials and interest – within their meaning in section 159A(a) – from the day on which he would have had to pay the tax as said in paragraph (1), had he not applied as aforesaid, plus the tax from the day of listing on the Exchange up to the day of the sale, as prescribed in sections 91(a) or (b), or 97(b2), as the case may be; if a shareholder was charged tax as said in paragraphs (1) and (3), then the day on which the shares were listed for trading on the Exchange shall be deemed the day of acquisition of the shares, and the

- consideration set for the purpose of those paragraphs shall be deemed their original cost.
- (b) For the purposes of subsection (a):
    - (1) "**shares**" – including rights to shares and exclusive of aforesaid shares and rights that were acquired after they were offered to the public for sale under a prospectus, in which it was stated that the Exchange's agreed to list them for trading;
    - (2) if the shares were sold to a person (hereafter: the recipient) while an exemption applied to the sale or when no tax was imposed on the sale, then that shall not be deemed a sale; when the recipient sells them – that shall be deemed the first sale.
  - (c)
    - (1) The provisions of subsection (a) shall not apply to shares listed for trading after December 31, 1991, to which section 6(g)(1) of the Inflationary Adjustments Law applies at the time of their sale, and to shares listed for trading after December 31, 1999, the rules under section 130A applying to their owners at the time of their sale;
    - (2) the provisions of paragraph (1) shall not apply to the sale of shares said in the said paragraph, if Chapter Two of the Inflationary Adjustments Law or the rules under section 130A did not apply to their owners at the time of their listing, provided that – at the time of their sale – their owners elected to withdraw the application said in subsection (a).
  - (d) If – after the shares were listed for trading on the Exchange – bonus shares, as defined in section 94, were issued in respect of shares that were listed for trading as said in this section, then the bonus shares or the bonus component, as said in section 94, shall for all intents and purposes be deemed part of the shares that were listed.
  - (e) Notwithstanding the provisions of section 94B, when a share is sold under this section, then the provisions of that section shall apply to the profits available for distribution, which the company accumulated from the end of the tax year before the year in which the shares were acquired until the end of the tax year before the date on which they were listed for trading on the Exchange; however, if the shareholder requested that listing the shares not be deemed their sale and if he did not rescind that request when he sold the shares, then the provisions of the section shall apply to the profits available for distribution until the end of the tax year before the date on which the shares were actually sold; for the purposes of this section: "**profits available for distribution**" – as defined in section 94B.
  - (f) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe rules on the original cost and on the day of acquisition in respect of shares that were listed for trading on an Exchange without any issue to the public.
  - (g) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe the adjustments required for shares acquired before the determining date or listed for trading on an Exchange before the determining date.

#### **Powers of the Minister of Finance**

- 101A. (a) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions on the following matters in respect of capital gain from the sale of securities:
- (1) the way and method of calculating capital gain and real capital gain, setting its timing and tax calculation, in general or for

- purposes of tax deduction, including the matter of setting off losses when tax is deducted;
- (2) allowing expenses and how they are to be related;
  - (3) in respect of an asset acquired before the determining date, or acquired before it was listed for trading on an Exchange, or in respect of which provisions of the Inflationary Adjustments Law or provisions under section 130A apply – adjustments and transitional provisions, including provisions on the tax rate, calculation of the capital gain and the set-off of losses.
  - (4) circumstances and conditions, under which income from the sale of a security will be deemed income under section 2(1), either generally or according to the length of time in which the security was held;
  - (5) the method for calculating the discount, including the determination of instances in which the discount will be added to the consideration;
  - (6) categories of cases in which a future will be deemed a hedging operation, and circumstances under which a said transaction will be deemed a transaction from which the income constitutes income under section 2(1), or in which its result will be added to the hedged asset or obligation, on prescribed conditions; for purposes of this paragraph: **"hedging transaction"** – a future carried out in order to protect the value of the asset or of the obligation, whether present or prospective, on condition that it was reported in accordance with prescribed rules;
  - (7) in respect of futures, and in respect a transaction of borrowing or lending a security, selling a security short, and also said transactions between linked parties – circumstances under which the transaction shall be deemed a sale and the way of calculating the income and its timing;
  - (8) tax exemptions or reduced tax rates on a foreign resident's income from a security traded on an Exchange or in a banking corporation, from the sale of a unit or its redemption or on profits received in respect of a unit;
  - (9) provisions and conditions for the allowance of deductions of real interest expenses and linkage differentials, the method for their calculation, restrictions on real interest rates deductible when special relationships exist between lender and borrower, and also ways of proving the connection of the loan, of real interest expenses and of linkage differentials to a security;
  - (10) provisions and conditions on the matter of sales and transactions between relatives or between parties to a sale or transaction, between whom there are special relationships, including provisions on determining the consideration, the original cost and the day of acquisition;
  - (11) conditions and circumstances, under which a shareholder shall be deemed a substantive shareholder, in addition to the provisions of section 88, if the provisions of Part Five "B" apply to the company;
  - (12) instances in which a unit in an exempt trust fund shall be deemed to have been sold and repurchased, in respect of certain unit holders or in respect of all unit holders, all on conditions and with adjustments he ordered;
  - (13) conditions and circumstances, under which a resale of securities

or a transfer for the restriction of exposure, as defined in the Agreements on Financial Assets Law 5766-2006, shall be deemed a loan and not a sale of securities, notwithstanding the provisions of section 4 of the said Law.

- (b) If an assessee claimed the deduction of real interest expenses and linkage differentials before the provisions said in subsection (a)(9) were prescribed, then his capital gain from the sale of securities shall be charged tax at the rate of 25%.

#### **Powers of the Director**

101B. In respect of capital gains from the sale of securities the Director may prescribe rules on returns to be submitted to the Assessing Officer by the assessee and by an Exchange member, banking corporation, investment portfolio manager and real estate investment fund, and also on the certifications they must give the assessee; in this section: "**investment portfolio manager**" – as defined in the Regulation of Investment Counseling and Portfolio Management Law 5755-1995.

## **PART FIVE "A": SHARE ALLOCATIONS TO EMPLOYEES**

#### **Share allocations to employees**

102. (a) In this section –

"**choice**" – an employer company's choice of one of two courses of taxation for share allocations to employees through a trustee – the work income course or the capital gains course;

"**controlling member**" – as defined in section 32(9);

"**share allocation through a trustee**" – the allocation of an employer company's shares to an employee, on condition that the employee is not a controlling member of it at the time of the allocation and thereafter, and that all the following conditions are complied with:

- (1) the shares, including any right vested by virtue of them, were deposited with a trustee at the time of their allocation, at least until the end of the period;
- (2) the company informed the Assessing Officer of its choice as part of its application for the plan's approval, which was submitted at least 30 days before the date of the allocation;
- (3) the allocation plan and the trustee were approved by the Assessing Officer, but if the Assessing Officer did not reply within 90 days after he received the notification, then the allocation plan or the trustee, as the case may be, shall be deemed to have been approved;

"**employer company**" – any of the following:

- (1) an employer that is an Israel resident company or a foreign resident company with a permanent enterprise or a research and development center in Israel, if the Director so approved (for this purpose: the employer);
- (2) a company that is a controlling member of the employer or of which the employer is a controlling member;
- (3) a company, if the same person controls it and the employer;

"**date of realization**" –

- (1) in respect of a share allocation through a trustee – the date on



- which the shares are transferred from the trustee to the employees or the date on which the shares are sold by the trustee, whichever is earlier;
- (2) in respect of a share allocation not through a trustee – the date on which the shares are sold, including the sale of a share that stems from the right to acquire it;
- "share"** – including the right to acquire a share;
- "share listed for trading on an Exchange"** – including a share in a company, all or some of the shares of which are listed for trading on an Exchange in Israel or abroad;
- "trustee"** – a person approved by the Assessing Officer as trustee for purposes of this section, including an employee;
- "employee"** – including an officer of the company, but exclusive of a controlling member;

**"value of benefit"** – the consideration or the value at the time of the realization, less expenses incurred by the employee in acquiring the share, adjusted from the day of issue until the date of the realization, and also expenses incurred by the employee in respect of the sale;

**"end of the period"** – each of the following:

- (1) if the company chose the work income course – a period of 12 months after the day on which the shares were issued and deposited with the trustee;
  - (2) if the company chose the capital gains course – a period of 24 months after the day on which the shares were issued and deposited with the trustee;
  - (3) in the case of an involuntary sale, as defined in section 103 – the date of the said sale.
- (b) An employee's income from an allocation of shares in the employer company through a trustee shall not be charged tax at the time of the allocation, and the following shall apply on the date of realization:
- (1) if the employer company chose the work income course, then the employee's income shall be deemed income under section 2(1) or (2), as the case may be, in the amount of the value of the benefit;
  - (2) if the company chose the capital gains course, and if the trustee held the shares at least until the end of the period, then the employee's income shall be deemed a capital gain in the amount of the value of the benefit, and on it he shall be charged tax at the rate of 25%;
  - (3) notwithstanding the provisions of paragraph (2), if the allocated share is a share that is listed for trading on an Exchange or a share in a company, the shares of which were listed for trading on an Exchange within 90 days after the allocation, then the part of the value of the benefit in the amount of the average value of the company's shares on the Exchange at the end of the 30 trading days before the allocation or at the end of the 30 trading days after the said listing for trading, as the case may be, less expenses, shall be deemed income under section 2(1) or (2), as the case may be, and the balance of the value of the benefit shall be deemed a capital gain that is liable to tax at the rate of 25%, on condition that the amount determined to be income under section 2(1) or (2), as aforesaid, does not exceed the value of the benefit at the time of realization; for the adjustment of expenses

- incurred by an employee in acquiring the allocated share, said expenses shall be multiplied by the index on the day of the allocation or on the day of listing for trading, as the case may be, and divided by the index on the day of the expenditure, and all shall be adjusted from the day of the allocation or of the listing until the date of the realization.
- (4) Notwithstanding the provisions of this section, if the company chose the capital gains course and the date of the realization comes before the end of the period, then the employee's income shall be deemed to be income under section 2(1) or (2), as the case may be.
  - (c) (1) An employee's income from an allocation of shares that is not an allocation through a trustee shall be charged tax at the time of the allocation as income under section 2(1) or (2), as the case may be, and at the time of the realization as income said in Part Five or in Part Five "C", as the case may be.
  - (2) Notwithstanding the provisions of paragraph (1), an employee's income from the allocation of a right – not listed for trading on an Exchange – to acquire a share not through a trustee shall not be charged tax at the time of the allocation, and at the time of the realization it will be charged tax as income under section 2(1) or (2), as the case may be.
  - (d) (1) When shares are allocated as said in subsections (b)(1) and (3) and (c)(1), then the company that employs that employee will be allowed to deduct the said allocation as a wage expense, in the amount of the employee's income under section 2(1) or (2), or in the amount of its participation, which it was charged because of its obligation to the allocating employer company, whichever is lower, and all that in the tax year in which tax was deducted in respect of the employee's income and transmitted to the Assessing Officer.
  - (2) The company shall not be allowed any expense in respect of the sale of a share, in respect of which the employer company chose the capital gains course, even if the share was sold before the end of the period said in subsection (b)(4).
  - (e) The provisions of section 3(i) shall not apply to share allocations to employees in an employer company, including undertakings to allocate as aforesaid.
  - (f) Notwithstanding the provisions of section 100A, the rate of tax that shall apply to the chargeable part of the profit of an employee who ceased being an Israel resident, as defined in that section, shall be at the tax rate prescribed in section 121, in each of the following instances:
    - (1) in the case of a share allocation through a trustee, in respect of which the company chose the work income course;
    - (2) in the case of a share allocation through a trustee, in respect of which the company chose the capital gains course, but the share was realized before the end of the period;
    - (3) in the case of a share allocation not through a trustee, to which the provision of subsection (c)(2) applies .
  - (g) The choice under this section shall apply to every employee to whom shares were allocated, and to every share allocation in the year after the end of the year of the first allocation, and thereafter as long as the company did not make a different choice; a company shall be entitled to choose differently only if a year has passed since the end of the year in

- which the first allocation was made after the previous choice.
- (h) The Director may prescribe any of the following:
    - (1) conditions in respect of the allocation;
    - (2) provisions on charging with tax an employee, in respect of whom all or some of the conditions prescribed in and under this section were not complied with because the shares were realized by involuntary sale;
    - (3) repealed;
    - (4) rules on the allocation of shares to a foreign resident employee in respect of the period of his work in Israel;
    - (5) rules for the deduction of tax at the source and the submission of reports by the employer company and the trustee, and setting times for their submission.

## PART FIVE "B": STRUCTURAL CHANGE AND MERGER

### CHAPTER ONE: INTERPRETATION AND APPLICABILITY

#### Definitions

103. In this Part each term shall have the meaning it has in Part Five or in the Land Appreciation Tax Law, as the case may be, unless there is an explicitly different provision in this Part;

**"merger"** –

- (1) the transfer of all assets and obligations of one or several companies (hereafter: transferor company) to another company (hereafter: merged company) and the transferor company's liquidation without winding up, in accordance with a merger Order or in accordance with Chapter One of Part Eight of the Companies Law;
- (2) for the purposes of section 103T, a transfer of at least 80% of the rights in a company or in each of the companies (hereafter: transferee company) to another company in consideration of shares that will be allocated in the other company, on condition that the holders of rights and the parties affiliated with them who transferred their rights in the transferee company transferred all their rights in the said transfer to the other company (hereafter the other company shall also be called a merged company);
- (3) the performance of a succession of mergers;

**"asset"** – any property, whether real or movable, and every right or benefit, contingent or vested, whether in Israel or abroad;

**"merger Order"** – an Order made under section 351 of the Companies Law;

**"date of merger"** –

- (1) for purposes of a merger under a merger Order – the end of the tax year in which the merger Order was made, or the end of the preceding tax year, on condition that that was not before the date on which the petition for the merger Order was submitted;
- (2) for purposes of a merger under Chapter One of Part Eight of the Companies Law – the end of the tax year in which the merger took place, on condition that that was not earlier than the decision by the General Meeting of each of the merging companies under section 320(a) of the Companies Law;
- (3) for purposes of a merger under section 103T – the date of the

exchange of shares;

**"approved merger"** – a merger approved by the Court under section 321 of the Companies Law or a merger which – by a decision of the Court under section 319 of the Companies Law – must not be delayed and the implementation of which on the date set by the Court must not be prevented;

**"the required period"** –

- (1) in respect of a merger under paragraph (1) of the definition of "merger" – the longer of the following two periods: a period of two years that begins on the merger date, or a period that began on the merger date and ended one year after the end of the tax year in which the merger Order was issued or the merger was approved, as the case may be;
- (2) in respect of a merger under paragraph (2) of the definition of "merger" – the period that began on the merger date and ended two years after the end of the tax year in which the merger date occurred;

**"succession of mergers"** – one or more additional mergers (hereafter: additional merger), in which a company that participated in a previous merger participates and which is carried out during the required period of the previous merger, on condition that the following two conditions apply:

- (1) the conditions for entitlement under section 103C are met by each of the merging companies;
- (2) the conditions prescribed under section 103C(6) would also have been met, if the first merger in the succession of mergers and each additional merger had been carried out as a single merger on the date of the additional merger; for that purpose the market value of each of the companies that participated in the merger on the date of the first merger and on each of the additional merger dates shall be taken into account, adjusted at the rate of the index increase from the date of the merger in which each of the companies participated until the date of the last additional merger;

**"associated party"**, of a body of persons (in this definition: body corporate) or of an individual – a person for whom one of the following holds true:

- (1) a relative, as defined in section 76;
- (2) a controlling member of the body corporate;
- (3) a body of persons, of which the body corporate or the individual is a controlling member;
- (4) the body corporate and the body of persons have the same controlling member;

**"right in a body of persons"** – a right in a body of persons, which gives one of the rights enumerated below, whether assigned in or under the charter and by-laws of the body of persons, or by agreement with a member of the body of persons:

- (1) membership in a body of persons or a right to its assets upon winding up, or a right to its profits, or the right to manage it or the right to vote in it, as well as any other right in the body;
- (2) a right of choice or a right to claim in respect of any of the rights specified in paragraph (1), from the body or from the owner of any of the said rights;
- (3) the right to order – directly or indirectly – the holder of any right specified in paragraphs (1) and (2) how to exercise his right;

**"split"** – the transfer of assets and obligations of one company (hereafter: split company) to one or more other companies (hereafter: new company);

**"capital reduction Order"** – the Order of a competent Court under the Companies Ordinance, which allows a company to reduce its capital;

**"market value"** – the amount which could have been obtained by a sale by a

willing seller to a willing buyer, between whom there are no special relationships;

**"involuntary sale"** – a sale which is one of the following:

- (1) an inheritance;
- (2) a sale as part of involuntary winding up proceedings under the Companies Ordinance;
- (3) a sale under bankruptcy proceedings;
- (4) some other kind of sale prescribed by the Minister of Finance in regulations;

**"controlling member"** – as defined in section 3(i)(1)(c);

**"structural change"** – a merger, a split or a transfer of assets against shares, all according to this Part.

**Applicability to cooperative societies, trust funds, nonprofit societies, Government companies, Government subsidiaries and research and development intensive companies**

- 103A. (a) The provisions of this Part shall also apply to structural change in cooperative societies and nonprofit societies, or to a structural change in which one party is a cooperative society or a nonprofit society, and also to trust funds of the same type, all mutatis mutandis and with additional changes that the Director will prescribe.
- (a1) The Director may, in consultation with the Director of the Government Companies Authority, certify that the provisions of this Part apply to Government companies and Government subsidiaries with changes he prescribed, including the non-applicability of part of the provisions of this Part, on condition that the proportion of the direct or indirect holding of the Government or of the Development Authority, within its meaning in the Development Authority (Transfer of Assets) Law 5710-1950, of rights to profits or of rights to assets upon liquidation of the said companies is not less than 90% on the date of the structural change; in this subsection: **"Director of the Companies Authority"**, **"Government company"** and **"Government subsidiary"** – as defined in the Government Companies Law 5735-1975.
- (b) It is also permissible to prescribe, in regulations with approval by the Knesset Finance Committee, that provisions of this Part apply to structural change in research and development intensive companies, as shall be defined in the regulations, with the changes specified there.

**Power to change conditions**

- 103A1.(a) The Minister of Finance may, in regulations with approval by the Knesset Finance Committee, increase every ratio set in section 103C, change the proportions of holdings required in the same section, or shorten the required period, all in respect of the conditions that qualify for entitlement to the tax benefits under this Part; regulations under this section may be made for certain categories of structural change or for certain categories of structural change in certain companies, taking the said companies' unique position in the economy into consideration.
- (b) Notwithstanding the provisions of the definition of "date of merger" in section 103, and notwithstanding the provision of section 105C(9), the Director may designate a different merger date or a different date of a split, on conditions that he prescribed.

## CHAPTER TWO: MERGER OF COMPANIES AND COOPERATIVE SOCIETIES

### Tax exemption

- 103B. (a) A sale of rights in a transferor company in connection with a merger, and the transfer of a transferor company's assets or obligations to a merged company in connection with a merger shall not be charged tax under this Ordinance, under the Inflationary Adjustments Law or under the Land Appreciation Tax Law.
- (b) In every instance, in which a sale is not charged Land Appreciation Tax by virtue of the provisions of subsection (a), that sale shall be charged acquisition tax at the rate of 0.5% of its value.

### Conditions for entitlement

103C. The benefits under this Chapter shall apply to a merger, if all the following conditions are met:

- (1)
  - (a) The companies propose to merge for a business and economic purpose, the main objective of their merger being to make the joint management and operation of their businesses possible;
  - (b) improper tax avoidance or tax reduction are not among the major purposes of the merger;
- (2) most of the assets transferred in the merger to the merged company from each of the transferor companies and most of the assets in its possession just before the merger were not sold during the required period and during the said period they were used in a manner that under the circumstances is customary in the conduct of the company's business; for this purpose:
  - (a) "**asset**" – an asset defined in section 104, except for securities that are traded on an Exchange and are not held by a controlling member;
  - (b) "**most of the assets**" – assets, the market value of which on the date of the merger was more than 50% of all the company's assets on that date;
  - (c) for purposes of subparagraph (b), on application by the merging companies all assets shall not include assets, the sale of which the Director approved, or categories of assets designated by the Director, all on conditions he prescribed, including the setting of a higher percentage than the percentage stated in subparagraph (b);
  - (d) for purposes of subparagraph (b), a replacement of assets to which sections 96 or 27 have been applied, shall not be deemed a sale of assets, on condition that in the determination of all assets the new assets shall be treated like the replaced assets;
  - (e) "**sale**" – exclusive of involuntary sale;
- (3) the main economic activity of each of the merging companies, as it was just before the merger, is continued in the merged company during the required period;
- (4) in the course of the merger the merged company allotted shares with equal rights to all shareholders in the transferor company according to their proportional holdings of all rights in the transferor company, and no additional consideration whatsoever was given in the course of the merger – directly or indirectly – by the merged company or by any other person;
- (5) the rights held in the merged company after the merger by all the holders of rights in each merging transferor company are in accordance

- with the ratio of the market value – at the time of the merger – of the company in which they were shareholders immediately before the merger to the total market value – at the time of the merger – of all the companies that participate in the merger; the Director shall prescribe the necessary adjustments, if the merged company holds shares in a transferor company;
- (6) (a) the total of rights of all holders of rights in each of the merging companies shall – during the required period – be at least 10% of the market value of the rights in the merged company on the merger date;
  - (b) the market value of every company that participates in the merger shall not exceed four times the market value of any other merging company, all on the date of merger;
  - (c) the Minister of Finance may, with approval by the Knesset Finance Committee, designate categories of mergers, in which restrictions different from those said in subparagraphs (a) and (b) shall apply;
  - (7) the merged company is one of the following:
    - (a) an Israel resident incorporated in Israel under the Companies Ordinance, the Companies Law or a cooperative society incorporated in Israel under the Cooperative Societies Ordinance;
    - (b) a company approved by the Director for this purpose, which is a foreign resident company or an Israel resident foreign company, as defined in the Companies Ordinance or in the Companies Law; an aforesaid approval may be conditional on the provision of collateral and on other conditions, as the Director may prescribe;
  - (8) (a) each of the holders of rights in the companies that participate in the merger continues to hold – during the required period – all the rights which he had in the merged company immediately after the merger;
  - (b) holders of rights that are traded on an Exchange shall not be included among holders of rights for the purposes of subparagraph (a), unless they were controlling members on the date of the merger; for this purpose: "**controlling member**" – other than a benefit fund or a trust fund;
  - (9) notwithstanding the provisions of paragraph (8), if one of the events specified in subparagraphs (a) to (c) occurs, that shall not be deemed a change in rights after the date of the merger, on condition that the rights of the persons who held rights in the merging companies do not decrease – at any time during required period – to less than 51% of each of the rights in the merged company;
    - (a) during the required period one or more holders of rights in the merging companies voluntarily sold less than 10% of the rights he held in the merged company immediately after the date of merger or – if the other holders of rights agreed – a higher percentage, on condition that the total of rights sold by all holders of rights does not exceed 10% of the total of rights in the company, before any allocation to persons who were not holders of rights before the merger;
    - (b) new shares were allocated to persons who were not holders of rights in the company before the allocation, to an extent of not more than 25% of the share capital before the allocation;
    - (c) shares as defined in section 102 were offered to the public on a

- Stock Exchange, on the basis of a prospectus in which it is stated that the Exchange agreed to list the shares for trading;
- (9a) notwithstanding the provisions of paragraph (8) and in addition to the provisions of paragraph (9), it shall not be deemed a change in rights after the merger, if one or more holders of rights in the companies that participate in the merger –
    - (1) sells his rights involuntarily;
    - (2) sells all the rights he had in the merged company, including rights held by persons that were his associated party, during the period that begins one year after the merger date only against cash; the conditions said in this section shall apply to the purchaser of the rights, as if at the time of the merger he had been the holder of rights in the company that participated in the merger; the Minister of Finance may, with approval by the Knesset Finance Committee, set additional conditions for this matter;
  - (10) repealed
  - (11) notwithstanding the provisions of this section, the Director may prescribe rules, according to which the split of a merged company or the transfer of assets by a merged company shall not be deemed a violation of any of the conditions specified in this section.

#### **Restriction on receipt of consideration in cash**

- 103D.(a) Notwithstanding the provisions of section 103C(4), if a merger Order prescribes that minority shareholders in a transferor company, who opposed the merger Order in Court, be paid cash for their shares in the transferor company and receive no rights in the merged company, that shall not negate any of the benefits prescribed in this Chapter, provided that the said benefits not apply to the minority shareholders who received aforesaid payment and they shall be charged the taxes that apply under any statute; for the purposes of this subsection:
- "minority shareholders"** – shareholders who together hold no more than 25% of any right in the company, none of them being relatives of a person who holds shares in the merged company after the merger;
- "relative"** – each of the following:
- (1) a relative, as defined in section 88;
  - (2) a person who is a controlling member of a body of persons that holds shares in the merged company;
  - (3) any person controlled by a shareholder in the merged company.
- (b) The Director shall, in rules, prescribe adjustments that shall be made for the purposes of section 103C(4) and (5), in respect of a merger in which consideration was paid in cash, as said in this section.

#### **Asset transferred in a merger**

- 103E. (a) The original cost of an asset transferred to a merged company in a merger, the balance of its original cost, the cost of its acquisition and the date of its acquisition, each as the case may be, shall be – for purposes of this Ordinance, of the Inflationary Adjustments Law and of the Land Appreciation Tax Law – as they would have been in the transferor company, if the asset had not been transferred; in respect of an aforesaid asset that is stock, the amount set as final stock for purposes of the transferor company's assessment for the tax year that ends on the date of merger shall be deemed the cost of the stock.
- (b) The transfer of an asset in a merger shall be deemed a sale for purposes of the number of periods under section 21A of the Industry



## Encouragement Law.

### Capital gain from sale of shares

103F. If rights in the merged company and in the transferor company were not listed for trading on an Exchange on the day of the merger, then the following provisions shall apply to the shares of the merged company, which were allocated in the merger (hereafter: the new share):

- (1) the original cost of the rights which the transferor had in the transferor company (hereafter: the old share), adjusted at the rate of index increase from the day of its acquisition to the date of the merger, less any real loss if the share had been sold on the date of the merger, shall be the original cost of the new share, on condition that it is not less than the original cost of the old share (hereafter: the adjusted cost); the differential between the original cost of the old share and the adjusted cost is hereafter called the "**adjustment differential**"; for this purpose: "**real loss**" – the amount by which the share's market value is lower than its adjusted original cost;
- (2) the adjustment differential, which is part of the original cost of sold shares, shall be added to the consideration from the sale of the shares, and it shall be deemed an additional inflationary amount;
- (3) the date of merger shall be deemed the date of acquisition of the new share; however, when a new share that was received against an old share acquired before the determining date is sold, the day of acquisition of the old share shall be taken to be the day of acquisition of the new share for purposes of calculating the real capital gain until the determining date;
- (4) if the shareholder is a foreign resident on the date of merger, and if at the sale of the share he requests that the exchange rate at which he acquired the old share be deemed the index for calculating the adjusted price, then the adjustment differential shall be exempt of tax;
- (5) the Director shall make rules on the determination of profits available for distribution, within their meaning in section 94B, which accrued in the merged company or accrued in the transferor company up to the date of the merger and which are to be taken into account in the merged company.

### Adjustments for shares traded on an Exchange and for associated companies

- 103G. (a) The Minister of Finance shall prescribe, by regulations with approval by the Knesset Finance Committee, adjustments required for the merger of one or more companies, the shares of which are traded on an Exchange on the date of the merger, or the shares of which were listed for trading on an Exchange after the date of the merger, or the shares of which were removed from the list of securities traded on an Exchange on or after the date of merger.
- (b) The Minister of Finance shall prescribe, by regulations with approval by the Knesset Finance Committee, adjustments required for the merger of companies, one of which holds rights in the other.
- (c) Notwithstanding the provisions of section 101(b)(1), the provisions of section 101 shall also apply to shares allocated by a merged company by prospectus, as said in section 103C(4).

### Setting off losses of transferor company and merged company

- 103H. (a) A loss said in section 28, which a transferor company or a merged company suffered up to the date of merger and which can be carried

forward to subsequent years, may be set off against the merged company's income, beginning with the tax year after the merger, but in each aforesaid tax year it shall be allowed set off an amount no greater than 20% of all losses of transferor companies and of the merged company, or no greater than 50% of the merged company's chargeable income in that tax year before the set off of losses from preceding years, whichever is the smaller amount.

- (b) A loss said in section 92, which a transferor company or a merged company suffered up to the date of the merger and which can be carried forward to subsequent years, may be set off against the merged company's capital gain beginning with the date of merger, but in each tax year it shall be allowed to set off an amount no greater than 20% of all the capital losses of the transferor companies and of the merged company, or no greater than 50% of the merged company's capital gain, whichever is the smaller amount; a period of five years after the day of merger shall not be taken into account for the restriction set in section 92 for the set off of an aforesaid loss.
- (c)
  - (1) Notwithstanding the provisions of subsection (a), a loss said there, which cannot be set off in that year because of the limitation of 50% of the chargeable income, shall be set off in the following years, one after the other, on condition that no loss said in this paragraph is set off which, together with the loss said in subsection (a), exceeds 50% of the company's income before the set off of losses from preceding years.
  - (2) Notwithstanding the provisions of subsection (b), a loss said there, which cannot be set off in that year because of the limitation of 50% of capital gain, shall be set off in the following years, one after the other, on condition that no loss said in this paragraph be set off which, together with the loss said in subsection (b), exceeds 50% of the company's capital gain before the set off of losses from preceding years.
- (d) A loss or capital loss said in subsections (a) to (c), which could not be set off until the end of the fifth year after the merger date, may be set off beginning with the sixth year, subject to the provisions of sections 28 and 92, as the case may be.
- (e) Notwithstanding the provisions of subsection (b), a capital loss incurred by one of the merging companies before the merger may be set off in full against a capital gain or land appreciation of the merged company, which stems from the sale of an asset that belonged to the said company just before the merger, or which the merged company owned before the date of merger, as the case may be; the provisions of subsections (c) and (d) shall apply to a balance of loss which cannot be set off under this subsection.
- (f) Notwithstanding the provisions of subsection (a), a loss incurred by one of the merging companies from the rental of a building before the merger may be set off under section 28(h).
- (g) The Director may prescribe, during the four year period said under section 103J(b), that a loss or a capital loss to which the provisions of this section apply cannot be set off in the merged company, or that only part of it may be set off, if he is satisfied that the merger will result in an improper reduction of tax because of the set off of the said loss; the Director's decision may be appealed, and for this purpose it shall be treated as if benefits had been denied, as said in section 103J(g); however, if the merging companies requested the Director's advance

certification under section 103I, then the Director must inform them of his decision under this paragraph together with the notification under section 103I(e).

(h) In this section :

**"capital gain"** – includes land appreciation;

**"chargeable income"** – before the set off of losses, but without income against which a loss has been set off under section 92.

#### **Advance certification of a merger plan by the Director**

- 103I. (a) If a merger proposal was submitted to the Companies Registrar in accordance with Chapter One of Part Eight of the Companies Law, or if an application was submitted to the Court for a merger Order or for Court approval of a merger, then application may be made to the Director for certification that the plan complies with the conditions specified in section 103C, on condition that the application to the Director is submitted before the merger date.
- (b) An applicant for certification under this section shall pay an application fee in an amount to be set by the Minister of Finance in regulations, and the Minister may prescribe that the fee be proportional to the assets of the merging companies or to their inflation adjusted capital, or according to some other calculation.
- (c) The application shall include all the substantive particulars and facts on the expected merger, and attached to it shall be documents, certifications, opinions, affidavits, valuations, the merger contract or its final draft, the merger application submitted to the Court, and every other substantive particular, all as the Director shall prescribe in rules; the Director may require any additional particular, which he deems necessary for his decision on the application.
- (d) The Director may certify that particulars of a merger plan meet the conditions specified in section 103C, or that they will meet them if certain conditions are met or certain steps to be prescribed by the Director are taken, and he may also make the said certification subject to conditions that he will prescribe.
- (e) The Director shall inform the companies of his decision and of his reasons within 90 days after the day on which he received the application and all the documents said in subregulation (c), but he may extend the said period – for reasons that shall be recorded – to up to 180 days, and – with the Finance Minister's approval – for an additional period, on condition that he informed the companies of the extension before the end of the original period.
- (f) The Director's decision under subsection (e) is not subject to appeal.
- (g) If the Director did not respond to the application within the period set under subsection (e), that shall be deemed prima facie certification that the merger meets the conditions specified in section 103C.
- (h) (1) If the Director certified that the particulars of a merger plan meet the conditions specified in section 103C, then he cannot withdraw that certification, unless it is shown that particulars delivered to him are substantively incorrect or incomplete, or if it is shown that substantive particulars specified as aforesaid were not implemented or that substantive conditions set by the Director, as said in subsection (d), were not complied with.
- (2) The Director's decision to withdraw his certification may be appealed, as if it were an Order under section 152(b).
- (i) When the Director has given certification, as said in subsection (d),

then the benefits specified in this Chapter shall apply, beginning with the day of merger and as long as the particulars of the merger plan, as submitted to the Director, and the conditions set in section 103C are complied with.

**Benefits – their grant and withdrawal**

- 103J. (a) If benefits under this Chapter were given in a certain year, and if thereafter it is shown that one of the conditions specified in section 103C was not met on time, then the Assessing Officer shall so inform the parties to the merger; when that notification has been made, the benefits shall be canceled retroactively from the day on which they were given, and the parties to the merger and their shareholders shall be charged the taxes and obligatory payments, from which they had been exempted, with the addition of linkage differentials and interest from the day of the merger until the day of payment; the Director shall make rules for purposes of this subsection, in order to prevent double taxation.
- (b) (1) A notification said in subsection (a), as well as demands for reports from the parties to the merger or their shareholders (hereafter: merger reports), shall be issued within four years after the end of the tax year in which the Assessing Officer received a report under section 131, the subject of which is the tax year in respect of which the Assessing Officer argues that an aforesaid condition was not complied with; when a said notice has been given, the Assessing Officer shall draw up – not later than two years after the tax year in which the merger report was submitted, or within one additional year, if the Director concurred – amended assessments for the parties to the merger and their shareholders.
- (2) For the purposes of contestation and appeal, an assessment under this subsection shall be treated like an assessment under section 145.
- (c) Taxes, fees and other obligatory payments, which a transferor company owes under a tax law, within its meaning in the Taxes Set-Off Law 5740-1980 (hereafter in this section: tax law) in respect of tax years before the merger, and – if benefits were withdrawn under subsection (a) – also aforesaid payments in respect of tax years after the date of merger, may be collected from any of the following:
- (1) the merged company;
- (2) a person who was a controlling member in the transferor company immediately before the merger and received shares in the merged company as part of the merger; however, it shall not be permissible to collect from him an amount that exceeds the proportional part of those payments according to his share in the transferor company immediately before the merger, as it was determined for purposes of section 103C(4).
- (d) If any amount could have been charged against a person or could have been collected from him under a tax law, if not for the merger, then the person responsible for the implementation of that Law may charge that person or collect from him even after the merger.
- (e) Notwithstanding the provisions of subsection (b), if benefits under this Part were granted in any tax year, and if one of the conditions set in section 103C is not complied with in a later tax year in which the date for compliance with that condition occurs, then the Director may determine that benefits not be denied in respect of all or some of the

- merging companies or in respect of a certain shareholder, if he is satisfied that noncompliance was caused by the unilateral action of a minority of shareholders, without the knowledge and beyond the control of the majority of shareholders, or that the noncompliance was caused without the knowledge or beyond the control of the shareholders.
- (f) The Minister of Finance may determine, in regulations with approval by the Knesset Finance Committee, that there shall be different results for different shareholders, in line with the degree of their responsibility for noncompliance with a condition, because of which benefits were canceled.
  - (g) A decision under this section to cancel benefits may be appealed as part of an appeal against an assessment for a tax year, and if no assessment was made for that tax year within a year after delivery of the notification said in subsection (b) (hereafter: day of notification), then it may be appealed separately within 30 days after the day of notification, as if it had been an Order under section 152(b).

### **Application of the Inflationary Adjustments Law**

- 103K. (a) Those terms in this section, which are not explicitly defined in this Ordinance, shall be interpreted within their meaning in the Inflationary Adjustments Law and in the Taxation under Inflationary Conditions Law, as the case may be.
- (b) If an asset was a protected asset or a fixed asset, as the case may be, and if it was transferred to the merged company in the merger, then it shall be deemed to be such since the day which would have applied for that purpose, had the asset remained with the transferor company and not been transferred to the merged company.
  - (c) Repealed
  - (d) For purposes of calculating capital adjustments – as said in section 3 of Schedule One of the Inflationary Adjustments Law – in a merged company, entries in the books of a transferor company or in returns submitted by it for the period up to the date of merger shall be treated like entries in the books of the merged company or returns submitted by it.
  - (e) The provisions of section 103H shall apply to the balance of inflationary deduction of a merged company or of transferor companies, which stems from the period up to the date of merger; however, the restrictions said in section 103H shall not apply to the balance of an aforesaid deduction, which was not allowed to be deducted because of the ceiling set in section 7(b) of the Inflationary Adjustments Law, or because of the provisions of section 7(e) of the Inflationary Adjustments Law; for purposes of this subsection: "**chargeable income**" – as defined in section 7 of the Inflationary Adjustments Law.
  - (f) The Minister of Finance may, in regulations with approval by the Knesset Finance Committee, prescribe additional adjustments that are necessary for purposes of the Inflationary Adjustments Law, of Chapter Seven "C" of the Investment Encouragement Law, and in respect of persons who keep their books in foreign currency.

### **Change of an asset's purpose**

- 103L. (a) If the purpose of an asset was changed when it was transferred from a transferor company to a merged company, then the exemption said in section 103B shall not apply to the transfer of that asset, and the provisions of sections 85 or 100 of this Ordinance or of section 5(b) of

- the Land Appreciation Tax Law shall apply, as the case may be, as if the asset had originally been bought by the merged company.
- (b) If the purpose of an asset transferred in a merger is changed within two years after the merger, and if the amount of tax payable because of the sale of the said asset is smaller than the total amount of tax, which would have had to be paid at the time of the merger and at the time of its sale if the purpose had been changed at the time of the merger, then the purpose shall be deemed to have been changed at the time of the merger, and the tax due therefor shall be paid with the addition of linkage differentials and interest from the day of the merger until the date of actual payment.

#### **Real estate association**

103M. The benefits prescribed by this Part shall not apply to a merger, to which a real estate association is party; however, the Director may approve the application of this Part to a merger between companies all or some of which are real estate associations, and all that with the adjustments and on the conditions he may prescribe; for this purpose:

**"parent company"** – a company that holds all the rights in another company;

**"subsidiary"** – a company all the rights in which are held by another company;

**"sister company"** – a company, in which the holders of rights are identical with the holders of rights in another company, the share of each holder of rights being identical with his share in the other company.

#### **Tax advances of merged company**

- 103N. (a) The tax advances, which a merged company must pay for the tax year that begins on the date of the merger, shall be calculated on the basis of the advances – with adjustments as the Director shall prescribe – which the transferor company and the merged company would have had to pay for that year, if not for the merger.
- (b) If the date of the merger is the end of the tax year before the year in which the merger Order was issued, or if the merger date was at the end of the tax year before the date on which the merger became an approved merger, then the advances shall be calculated in accordance with the provisions of subsection (a), beginning with the day on which the merger Order was made or on the day on which the merger became an approved merger, as the case may be, and until the end of the tax year after that year.

#### **Assets transferred in a merger**

103O. The Director shall make rules about assets transferred in a merger, and he may prescribe that the statute which applied just before the merger in respect of depreciation, amortization and deduction and the provisions of the Inflationary Adjustments Law continue to apply to them also after the date of the merger, or that they apply with adjustments and changes as he shall prescribe.

#### **Employee transferred to merged company**

- 103P. (a) The exemption set in section 9(7a) shall not apply to an employee of a transferor company, who in consequence of the companies' merger is transferred to be an employee of the merged company, and his transfer shall not be deemed retirement for purposes of the said section; however, the period of the employee's employment in the transferor

- company shall be taken into account in the calculation of his exemption under the said section when he retires from the merged company.
- (b) The Director shall, by rules, prescribe adjustments for purposes of section 102 in connection with the merged company, the transferor company and the employees, and he may prescribe aforesaid adjustments for any other matter said in section 102.

#### **Power to deny benefits under certain circumstances**

103Q. The Minister of Finance may, in regulations with approval by the Knesset Finance Committee, prescribe circumstances under which the benefits prescribed in this Chapter shall not be allowed, provided that determination does not deny benefits in respect of a merger, for which the merger Order or the Director's certification under section 103I were given before the said regulations were published.

#### **Regulations on certain particulars**

103R The Minister of Finance may, in regulations with the consent of the Minister of Justice, prescribe particulars that must be included in the merger contract and in the memorandum and by-laws of the merged company, as a condition for the receipt of the benefits prescribed in this Chapter.

#### **Returns**

- 103S. (a) The merging companies and the holders of rights in them shall deliver to the Assessing Officer – within 30 days after the merger Order was given after the date on which the merger became an approved merger or after the merger date, as the case may be, whichever was the latest, or within 60 days if the Assessing Officer so agreed in advance – a return that includes all the particulars and facts that directly or indirectly relate to the merger, and also the merger Order or the Court's decision on the merger approved by it, the merger contract, certifications, opinions, declarations, financial reports, a report on the purpose of assets transferred in the merger, particulars of the valuations prepared in preparation for and during the merger, and every other report or particular prescribed by the Minister of Finance in regulations.
- (b) Whoever is under obligation to submit a report under this section, but failed to do so, shall be treated like a person who failed to submit a return under section 131.
- (c) For purposes of this section: "**holders of rights**" – other than holders of rights that are listed for trading on an Exchange, who are not controlling members.

#### **Merger by means of an exchange of shares**

- 103T. (a) For the purposes of this section, "**merger by means of an exchange of shares**" – a merger as defined in paragraph (2) of the definition of "merger" in section 103.
- (b) A merger by means of an exchange of shares shall not be charged tax under this Ordinance, under the Real Estate Taxation Law or under the Inflationary Adjustments Law, if it complies with all the conditions specified in section 103C, mutatis mutandis, and with the conditions specified below:
- (1) immediately after the merger and during the required period the merged company holds all the rights in the transferee company, which it held on the merger date;
  - (2) an application was submitted to the Director for certification that

the plan meets the conditions specified in this section – on condition that the application was submitted at least 60 days before the merger date – and the Director so certified; if the Director decided that the merger does not meet the conditions specified in this section, then his decision may be appealed, as if it had been an Order under section 152(b).

- (c) If any of the events specified in paragraphs (a) to (c) of section 103C(9) occurred, then that shall not be deemed a change of rights after the merger, provided that the rights of the persons who immediately before the merger held rights in the companies that participated in the merger did not – at any time during the required period – drop to less than 51% of each of the rights in the merged company, and the rights of the merged company also did not drop to less than 51% of each of the rights in the transferee company.
- (d) The Minister of Finance may make rules, with approval by the Knesset Finance Committee, in respect of losses that may be set off in a merged company and in a transferee company;
- (e) The provisions under sections 103B(b), 103E, 103F, 103G, 103I, 103J, 103Q, 103R and 103S shall apply to a merger by means of an exchange of shares, mutatis mutandis as the case may be, as long as in this section does not prescribed differently, and provided that – for the purposes of section 103E – the rights in the transferee company shall be treated as the transferred assets.

### CHAPTER THREE: TRANSFER OF ASSETS AGAINST SHARES

#### Definitions

104. In this Chapter –

**"asset"** – an asset other than –

- (1) movables of an individual that he keeps for his personal use or for the personal use of his relatives or of his dependents;
- (2) business stock;
- (3) a right, whether by Law or in equity, to occupy real estate used for residential purposes and not for earnings or profit.

**"company"** –

- (1) an Israel resident company incorporated in Israel under the Companies Ordinance or the Companies Law or a cooperative society incorporated in Israel under the Cooperative Societies Ordinance;
- (2) a company approved by the Director for this purpose, which is a foreign resident, or which is an Israel resident foreign company, as defined in the Companies Ordinance or in the Companies Law; aforesaid approval may be conditional on the provisions of collateral, or on other conditions that the Director will prescribe;

**"capital gain"** – including land appreciation.

#### Transfer of all rights to an asset

104A.(a) If a person transfers all his rights in an asset to a company in consideration of rights that exist in that company, then he shall not be charged tax under this Ordinance, under the Land Appreciation Tax Law or under the Inflationary Adjustments Law, as the case may be, if all the following conditions have been met:

- (1) during at least two years after the day of the transfer the transferor holds at least 90% of each of the rights in the



- company;
- (2) the company holds the asset transferred to it during at least two years after the day of the transfer;
- (3) the ratio between the market value of the rights allocated to the transferor and the market value of all the rights in the company immediately after the transfer equals the ratio between the market value of the transferred asset and the market value of the company immediately after the transfer;
- (4) repealed
- (b) The provisions of subsection (a) shall not apply to an asset owned by a partnership or jointly owned by several owners.
- (b1) If an asset was transferred to a company that is a real estate association or became a real estate association after the transfer of the asset, then the provisions of subsection (a) shall apply, on condition that all the transferor's rights in the asset were transferred, and that – if the transferred asset is land – construction of a building on that land was completed within four years after the transfer, according to conditions set by the Director.
- (c) Repealed

#### **Transfer of an asset by several persons**

- 104B.(a) If partners in a partnership or joint owners cause all their rights in an asset owned by the partnership to be transferred or if they transfer all rights to an asset jointly owned by them, as the case may be, to a company set up especially for that purpose and if that company owned no other asset and engaged in no other activity at that time or previously, and all that only against the allocation of shares in that company, then they shall not be charged tax under this Ordinance, under the Inflationary Adjustments Law or under the Land Appreciation Tax Law, as the case may be, if all the following conditions have been met:
- (1) during at least two years after the day of the transfer, the share of each partner or of each joint owner in each of the rights in the company is equal to the share each had in the assets transferred as aforesaid, or to his share in the partnership, as the case may be;
  - (2) the company holds the assets transferred to it for at least two years after the day of the transfer;
  - (3) the ratio between the market value of the rights allocated to each of the partners or owners and the total market value of the company immediately after the allocation is equal to the ratio between the market value of that partner's or owner's share in the asset and the market value of the company immediately after the date of transfer;
  - (4) if land was transferred to the company as said in this subsection, and if thereafter the company became a real estate association, then the exemption prescribed in this section shall be granted only if construction of a building on the land was completed within four years after the transfer, in accordance with conditions to be set by the Director.
- (b) If several jointly owned assets were transferred, or if a jointly owned asset and an asset owned by a partnership were transferred, then the provisions of subsection (a) shall apply only if the share of each of the joint owners of each transferred asset is equal to his share in all the

other assets, and in the case of a partnership also to his share in the partnership.

- (c)
  - (1) For the purposes of subsections (a) and (b), rights in a single company shall be deemed a single asset, and the holders of those rights shall be deemed partners to that asset.
  - (2) A company, to which an asset was transferred under this section in the past shall also be deemed a company said in subsection (a), as long as all the following holds true from the date of the company's establishment until two years after the day on which an additional asset was transferred under this section:
    - (a) the holders of rights in the company have not changed;
    - (b) the ratio between the market value of the rights allocated to each transferor for the transfer of an additional asset and the value of the additional asset on the day of its transfer, is the same as the ratio between the market value of the transferor's share of all the assets which he transferred to the company and the market value of the company immediately after the transfer.
- (d) If each of several individuals transfers on the same date a depreciable asset to a company set up especially for that purpose only against the allocation of shares, and if that company owned no other asset and engaged in no other activity at that time or previously, then they shall not be charged tax under this Ordinance at the time of the transfer, if all the following conditions have been met:
  - (1) the purpose of the transfer is the unified management and operation of the transferred assets;
  - (2) a proportion of all the shares in the company was allocated to each of the individuals against the transfer of the asset or assets, in the ratio between the market value of the asset which he transferred, and the market value of all the assets transferred under this subsection;
  - (3) during at least two years after the day of the transfer no change is made in the rights of the shareholders in the company that was set up;
  - (4) the transferred assets will be used by the company in the course of the company's business, in a manner that is customary under the circumstances, and they will remain in its possession for at least two years after the day of the transfer;
  - (5) not more than ten individuals will form a company under this subsection; however, the Director may permit a larger number of individuals to join in the formation of a cooperative society;
  - (6) the market value of any asset transferred by any one of the individuals shall not exceed the market value of any asset transferred by another individual more than four-fold, all at the date of the transfer; the Director may change the said ratio, for reasons which shall be recorded;
  - (7) no asset that is a real estate right shall be transferred under the terms of this subsection.
- (e) The provisions of subsection (d) shall not apply to an asset owned by a partnership or owned jointly by several owners.
- (f) If a company transfers an asset to another company, in which the holders of rights are identical with the holders of rights in the transferor company, and if the share of each in the rights of the company is identical to the share of his rights in the transferor company (hereafter:

sister company), then at the time of the transfer it shall not be charged tax under this Ordinance, under the Inflationary Adjustments Law or under the Land Appreciation Tax Law, as the case may be, if all the conditions prescribed by the Minister of Finance in regulations have been met.

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*Note: Under section 75 of Amendment No. 147 the following subsection (g) is in effect only in respect of tax years 2005 to 2007 – Tr.*

- (g) (1) If a foreign resident company transfers all its assets and activities to an Israel resident company, in which the holders of rights are identical to the holders of rights in the transferor company, and the part of each holder of rights is identical with his right in the transferor company, then the transfer shall not be charged tax under this Ordinance, if the Director certified that the conditions and restrictions prescribed by the Minister of Finance under paragraph (2) have been complied with.
- (2) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe conditions and restrictions for purposes of the tax exemption prescribed in paragraph (1), including the matter of tax postponement, the original cost, the tax rate that will apply to capital gains or profits and dividends that stem from the transferor company, and the period during which shares shall be held in order to get the exemption under this section; he also may prescribe provisions and reports for the implementation of this section.

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**Transfer of shares to parent company**

- 104C. (a) If a company transfers to the holder of its shares all the shares it holds in another company (hereafter: the transferred shares), then it shall not be charged tax under this Ordinance or under the Inflationary Adjustments Law in respect of the sale of the transferred shares, if all the following conditions have been met and on condition that the Director's approval was obtained before the transfer:
- (1) the shareholder (hereafter: the parent company) is a company that holds all the rights in the transferor company;
  - (2) no consideration is given for the transferred shares, either directly or indirectly, in cash nor in kind;
  - (3) the transferred shares will remain in the parent company during at least two years after the day of transfer;
  - (4) during at least two years after the day of transfer no change occurs in the parent company's rights in the transferor company;
  - (5) the Court gave approval under section 303 of the Companies Law, if that was required;
  - (6) the asset is transferred for a business and economic purpose, improper tax avoidance or tax reduction not being among the main purposes of the transfer.
- (b) If the transferor company had an approved enterprise, within its meaning in the Investment Encouragement Law, which – on the date of the transfer – is able to distribute dividends under section 47(b)(2) or 51(c) of that Law, then the said share transfer shall be treated like an aforesaid dividend distribution.
- (c) The Director shall make rules on the adjustments necessary for

purposes of this section and for purposes of the Inflationary Adjustments Law in consequence of the implementation of this section, in respect of the transferor company and of the parent company, in respect of the determination of the original cost or of the consideration, or in respect of any other matter.

- (d) Repealed
- (e) (1) The provisions of subsections (a) to (c) shall apply – with changes to be prescribed by the Director, also on the non-applicability of part of the said provisions – to banking corporations within their meaning in the Banking (Licensing) Law 5741-1981, and to companies under their control, which – in tax years 1996 and 1997 – transfer rights that they hold in real bodies corporate, within their meaning in the said Law, on condition that – if the transferor is the banking corporation – the company to which the shares were transferred will not have any income as said in section 2(1) in the course of two years after the date of the transfer;
- (2) the conditions said in subsection (a)(3) and (4) shall also apply to a transfer said in paragraph (1), other than in a sale of rights in a real body corporate that was transferred to a parent company that is the banking corporation, or in a sale of rights in the transferor real body corporate, when such sales are performed in order to comply with provisions of the Banking (Licensing) Law 5741-1981;
- (3) without derogating from the provisions of any statute, decisions to transfer shares said in this subsection require approval by the General Meeting of the transferor body corporate and they shall be treated like extraordinary resolutions within their meaning in section 115(a)(3) of the Companies Ordinance.
- (e1) If the Director did not approve the transfer of shares under the provisions of subsection (a), then appeal may be lodged against his decision, as if it were an Order under section 152(b).
- (f) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe provisions on the application of all or part of this section to foreign companies, with the restrictions and on the conditions he shall prescribe.

### **Sale of rights and assets**

104D. For the purposes of sections 104A to 104C:

- (1) if one of the things specified in subparagraphs (a) to (d) below occurs, that shall not be deemed to affect the continued holding of rights in the company, provided that the rights of the persons who held the rights immediately after the transfer do not – at any time during two years after the transfer – drop to less than 51% of each of the rights in the company;
  - (a) shares as defined in section 102 were offered to the public on an Exchange by prospectus, which states that the Exchange agreed to list the shares for trading on it;
  - (b) during two years after the date of the transfer one or more of the holders of rights in the company to which the asset was transferred voluntarily sold less than 10% of each of the rights held by him, or he sold a greater percentage with the consent of the other shareholders, on condition that the following holds true:
    - (1) all the rights sold by all holders of rights do not exceed 10%

- of the rights in the company;
  - (2) all the holders of rights in an asset before its transfer to the company shall not sell a percentage of their rights in the company that exceeds the difference between the percentage of their rights immediately after the transfer and 90% of the rights in the company;
  - (c) new shares were allocated to a person who did not hold rights in the company before the allocation, in an amount that does not exceed 25% of the share capital before the allocation;
  - (d) repealed
- (1a) an involuntary sale of rights shall not be deemed an infringement of the continued possession of rights in the company;
- (2) holders of rights who hold rights traded on an Exchange shall not – for purposes of paragraph (1) – be included among the holders of rights, unless they were controlling members on the date of the merger; for this purpose, "**controlling member**" – other than a benefit fund and a trust fund;
- (3) the replacement of assets to which section 96 or section 27 was made applicable or their involuntary sale shall not be deemed the sale of an asset;
- (4) the sale of any asset, which is not liable to Land Appreciation Tax because of the provisions of this Chapter, shall be liable to acquisition tax at the rate of 0.5% of its value;
- (5) Notwithstanding the provisions of this Chapter, the Director may prescribe rules, according to which the split or merger of a company, to which an asset said in this Chapter was transferred, will not be deemed a violation of the conditions specified in this Chapter.

#### **Calculation upon sale of asset**

- 104E.(a) If an asset was transferred as said in sections 104A and 104B, then its original cost, the balance of its original cost, the day of its acquisition and its acquisition price shall be – for purposes of this Ordinance, of the Inflationary Adjustments Law and of the Land Appreciation Tax Law – as they would have been for the transferor, and the seller shall also be allowed to deduct those deductions, which the transferor would have been allowed to deduct at the sale of the asset, but the original cost of a transferred asset that is a security or a future traded on an Exchange shall be determined according to the provisions of section 104F, as if the security or future were a share, as said in that section; for the purposes of this section: "**future**" – as defined in section 88.
- (b) The transfer of an asset under sections 104A to 104C shall be deemed a sale, for calculation of the periods under section 21A of the Industry Encouragement Law.
- (c) A capital gain or a capital loss created in consequence of the sale of an asset that was transferred as said in sections 104A to 104C, must not – during the period of two years after the transfer date – be set off against profit or loss under sections 28 or 92, as the case may be; those two years shall not be taken into account for purposes of the restriction prescribed in section 92 in respect of the period of the set off.

#### **Sale of shares**

- 104F. The following provisions shall apply to the sale of shares that were received for an asset, as said in sections 104A and 104B:
  - (1) the balance of the original cost of the transferred asset, adjusted from

- the day of acquisition of the asset by the transferor until the day of transfer, less any real loss if the asset had been sold on the day of transfer, but not less than the original cost of the transferred asset (hereafter: adjusted cost) shall be the original cost of the shares; the differential between the balance of the original cost of the transferred asset and the adjusted cost shall hereafter be called the "**adjustment differential**"; for this purpose: "**real loss**" – the amount by which the market value of the asset is less than its adjusted original cost;
- (2) an adjustment differential, which constitutes part of the original cost of the sold shares, shall be added to the consideration from the sale of the shares and shall be deemed an additional inflationary amount;
  - (3) the date of transfer of the asset shall be deemed the date of the shares' acquisition; however, upon the sale of shares obtained for an asset that was acquired up to the determining date, the date on which the transferred asset was acquired shall be deemed the day of acquisition of the shares for purposes of the calculation of the real capital gain up to the determining date.

#### **Miscellaneous provisions**

- 104G. (a) The provisions of sections 104A to 104C shall apply only if the transferor of the asset informed the Assessing Officer of the transfer of the asset within 30 days of its transfer, and if he attached to his notification returns, affidavits and particulars, all as the Minister of Finance prescribed in regulations.
- (b) (1) The provisions of section 103J, subject to the provisions of paragraph (2), and of sections 103L and 103O shall apply to the transferor of an asset, as if he were a transferor company or a shareholder in it, as the case may be, and as if the company to which the asset was transferred were a merged company, all *mutatis mutandis* as the case may be.
  - (2) If it turns out that one of the conditions for the grant of benefits prescribed in section 104A, 104B or 104C was not complied with on time (hereafter: violation), then the transfer of the asset that was not charged tax at the time of the transfer shall be liable to tax as said in paragraph (1), or liable to tax according to the transferred asset's market value on the day of the violation, whichever is greater, unless the Assessing Officer is satisfied that the violated obligation was violated because of special circumstances beyond the transferor's control; the value set as aforesaid in this paragraph shall be the original price of the asset for the company and the day in respect of which the said value was set shall be the day of acquisition.
  - (c) If a company transferred an asset, then – during two years after the date of the transfer – the provisions of the Inflationary Adjustments Law and of section 130A, which would have applied to the company that transferred the asset, shall apply to the asset and to the company to which it was transferred, all with adjustments to be prescribed by the Director.
  - (d) The applicant for certification under this Chapter shall pay an application fee in an amount to be set by the Minister of Finance, and the Minister may set different fees for different categories of transfers, also taking into consideration the value of the transferred assets and the manner of their transfer.

## Exchange of shares

104H (a) In this section –

**"exchange of shares"** – the transfer of shares of a company (in this section: transferee company), including rights to acquire shares (in this section: the transferred shares) as consideration for the allocation of shares of another company that are listed for trading on an Exchange, either with or without additional consideration (in this section: the merged company and the allocated shares);

**"transferor"** – whoever transferred the shares to the merged company;

**"blocked share"** – a share, the sale of which is absolutely restricted by a statutory provision or by orders from the authority that is statutorily competent to make rules for trading in securities, during the designated period (in this section: the blocked period);

**"day of sale"** – the earlier of the following:

(a) the date on which the allocated share was sold;

(b) the end of the postponement period; for this purpose: **"the postponement period"** –

(1) in respect of allocated shares that are not blocked shares –

(a) in respect of one half of them – 24 months after the day of exchange; allocated shares, including blocked shares, sold until the end of the said 24 months shall be taken into account in calculating the half;

(b) in respect of their balance – forty-eight months after the day of the exchange;

(2) in respect of blocked shares –

(a) in respect of one half of them – 24 months after the day of exchange or six months after the end of the blocked period, whichever is later, on condition that blocked shares with shorter blocked periods than other blocked periods set for the balance of the blocked shares be first taken into account; shares sold as said in subparagraph (1)(a) until that date shall be taken into account in calculating the half;

(b) in respect of their balance – forty-eight months after the day of the exchange, or six months after the end of the blocked period, whichever is later;

**"trustee"** – a person approved by the Director as trustee for the purposes of this section;

**"value at the end of the postponement period"** – the amount obtained by adding up the amounts of the share's value on the Exchange at the end of trading on each of the thirty trading days before the end of the postponement period, divided by 30;

**"additional consideration"** – a cash amount given for the transferred shares, in addition to the allocated shares;

(b) (1) An exchange of shares shall not – at the time of their exchange – be deemed their sale for purposes of Part Five, of the Real Estate Taxation Law or of the Inflationary Adjustments Law, if all the following hold true:

(a) the ratio between the market value of the transferred shares and the market value of the merged company immediately after the exchange of shares is like the ratio between the market value of the allocated shares, including the additional consideration, and the market value of all

- rights in the merged company immediately after the exchange of shares;
- (b) the merged company allocated shares with equal rights to all persons who transferred from the same company;
- (c) the transferor paid an advance in respect of the additional consideration at the tax rate that applies under section 91(a), (b) or (b1), as the case may be; the provisions of section 91(d) or the provisions that apply to a real estate association act under the Real Estate Taxation Law, as the case may be, shall apply to the advance, mutatis mutandis;
- (d) all the shares and also all the rights of the transferor and of parties associated with him to acquire shares in the transferee company were transferred as part of the exchange of shares, unless the Director approved otherwise and on the conditions he set;
- (e) an application was submitted to the Director that he certify that the share exchange meets the conditions specified in this section, on condition that the application was submitted at least 30 days before the date of the exchange of shares, and the Director so certified; certification under this paragraph may be conditional on the provision of guaranties to the Director's satisfaction and on other conditions, as the Director will prescribe;
- (f) the allocated shares shall be deposited with a trustee, to secure payment of the tax and compliance with the provisions of this section;
- (2) if the Director determined that the exchange of shares did not meet the conditions prescribed in this section, then his decision may be appealed as if it had been an Order under section 152(b);
- (3) notwithstanding the provisions of this subsection, when shares of a transferee company that is a real estate association are exchanged, then the provisions of section 104D(4) shall apply, mutatis mutandis.
- (c) If the conditions said in subsection (b) have been complied with, then the following provisions shall apply:
  - (1) the allocated shares shall be deemed to have been sold on the day of sale;
  - (2) the consideration shall be calculated according to the following provisions:
    - (a) if the allocated share was sold before the end of the postponement period – the consideration for the sale;
    - (b) if the allocated share was not sold before the end of the postponement period – its value at the end of the postponement period;
 all with the addition of the adjusted additional consideration and the amounts of dividends distributed in respect of the allocated shares during the period between the date of the exchange and the day of sale, divided by the number of allocated shares; for this purpose: **"the adjusted additional consideration"** – the additional consideration, adjusted from the date of the exchange of shares until the day of the sale;
  - (3) the provisions of section 104F shall apply, mutatis mutandis, and for this purpose the transferred shares shall be deemed an asset;
  - (4) repealed



- (5) the following provisions shall apply to the sale of the allocated shares:
- (a) the part of the capital gain up to the date of the share exchange shall be charged tax at the tax rate that would have applied, if the provisions of section 104H did not apply on the date on which the shares were exchanged;
  - (b) the part of the capital gain from the date of the share exchange up to the day of sale shall be charged tax in accordance with the provisions of section 91(a) or (b), as the case may be;
  - (c) when the allocated share is sold by a foreign resident, then the tax exemption said in section 97(b2) shall apply only if – on the date of the share exchange – the transferor would have been entitled to the said tax exemption, had he sold the transferred shares on the day of their exchange;
  - (d) for purposes of this paragraph: **"part of the capital gain up to the date of the share exchange"** – the capital gain, multiplied by the ratio of the period between the acquisition of the transferred shares and the date of the share exchange, to the period between the said acquisition and the day of the sale of the allocated shares;
- (6) if the transferor sold the allocated shares after the end of the postponement period, then the allocated shares shall be deemed to have been newly acquired, the end of the postponement period shall be deemed the day of acquisition, and the value at the end of the postponement period shall be deemed the original cost;
- (7) notwithstanding the provision of any statute, a merger or split of the merged company after the exchange of shares shall not be deemed a sale of the allocated shares, and the Director may make provisions on this matter in special rules;
- (8) (a) for purposes of section 94B, profits available for distribution, as defined in that section, which accrued in the transferee company from the end of the tax year before the year in which the transferred shares were acquired by the transferor until the end of the tax year before the year in which the exchange of shares was carried out (hereafter: year of exchange) shall be deemed profits available for distribution when the allocated shares are sold; however, profits available for distribution which accrued before January 1, 1996, shall not be taken into account;
- (b) the Director shall prescribe rules for the determination of profits available for distribution in an exchange of shares, when the allocated shares are shares of an Israel resident company;
- (9) an amount of tax which the transferor paid to the Assessing Officer in respect of dividend income on allocated shares, which was distributed during the period between the date of the exchange and the day of sale shall be adjusted from the day of the tax payment until the day of sale, and shall be divided by the number of allocated shares in respect of which the dividend was distributed, and credit in its respect shall be given against the tax due on the capital gain when the allocated shares are sold;
- (10) if bonus shares were allocated to the transferor during the period

- between the date of the exchange and the day of sale, then they shall be treated like allocated shares;
- (11) (a) if the transferor was an Israel resident on the day of the exchange of shares, then he shall be deemed to be an Israel resident also on the day of the sale;
  - (b) if the transferor was a foreign resident and section 89(b) would have applied, if he had sold the shares on the day of the exchange of shares, then the allocated shares shall be deemed an asset located in Israel.
- (d) If the conditions said in subsection (b) have been complied with, then the following provisions shall apply to the transferred shares held by the merged company:
- (1) a profit or loss created by the sale of the transferred shares shall not be allowed to be set off, in the tax year in which the shares were exchanged and during the following two years, against a loss or profit in the merged company, all in accordance with sections 28 or 92, as the case may be, and during the following three years any profit or loss created by the sale of the transferred shares shall not be allowed to be set off as aforesaid against any profit or loss created by the sale of assets, the day of acquisition of which was before the day of the exchange of shares; the periods said in this paragraph shall not be included in the restriction prescribed in section 92(b) in respect of the set-off period;
  - (2) (a) the day of the exchange of shares shall be deemed the day of acquisition of the transferred shares, and the market value of the allocated shares at the time of the exchange of shares, plus the additional consideration, if any, divided by the number of shares transferred, shall be deemed the original cost of the transferred shares;
  - (b) Notwithstanding the provisions of subparagraph (a), if the transferor and the merged company were associated parties immediately before the exchange of shares, then the Assessing Officer may prescribe –
    - (1) that the consideration, as said in subsection (c)(2), be the original cost of the transferred shares, and that the day of sale of the allocated shares to the transferor, as determined, be deemed the day of their acquisition, even if the merged company sold the transferred shares before the day of the sale;
    - (2) that – if the allocated shares were sold on several dates – the total consideration for the sale of all the allocated shares shall be the original cost of the transferred shares, and the last day of sale determined for any of the allocated shares shall be the day of acquisition of the transferred shares, even if the merged company sold the transferred shares before the said last day of sale.
- (e) For the purposes of section 102(c), an exchange of shares shall not be deemed a sale of the transferred shares; the Director may, in rules, prescribe special provisions on the applicability of some or all of the provisions of this section, mutatis mutandis.
- (f) The advance said in subsection (b)(1)(c) shall be adjusted from the date of payment to the day of sale, and a tax credit shall be allowed for

it in proportion to the number of allocated shares, which were sold by the transferor.

- (g) (1) The trustee shall give the Assessing Officer written notice when the postponement period ends;
- (2) at the time of the sale the trustee shall deduct tax at the rate said in section 91(a), (b) or (b1), as the case may be, from the consideration, or at a lower rate, as the Assessing Officer shall prescribe, and he shall transmit it to the Assessing Officer within seven days.
- (h) If it turns out that particulars delivered to the Assessing Officer were not correct or are substantively incomplete, or if it turns out that substantive particulars specified in the application to the Director do not comply with the conditions prescribed in subsection (b)(1), then the Assessing Officer may – at his discretion – determine that the consideration calculated under this section or the market value of the transferred shares on the day of the exchange of shares – whichever is greater – constitutes the consideration received by the transferor for the transferred shares; the Assessing Officer shall make the necessary adjustments in respect of the original cost and the day of acquisition of the transferred shares that are held by the merged company.

## **CHAPTER FOUR: SPLITS OF COMPANIES, COOPERATIVE SOCIETIES AND NONPROFIT SOCIETIES**

### **Definitions**

105. In this Chapter –

**"company"** – including a trust fund or a nonprofit society (amuta) incorporated in Israel under the Amutot (Nonprofit Societies) Law;

**"adjusted reports"** – financial reports drawn up and adjusted in accordance with statements by the Israel Institute of Certified Public Accountants and audited by a certified public accountant or by an audit union official, within its meaning in section 131;

**"holding company"** – a company, all assets of which are rights in companies, or assets which under a statute cannot be transferred, and which has no income except income derived from the dividend distributions or from assets which under an statute cannot be transferred;

**"continuing split company"** – a split company which is not a holding company, and from which not all its assets and obligations were transferred.

### **Procedure of split**

105A. A split may be carried out in one of the following ways:

- (1) the transfer of assets and obligations from the split company to a new company, which was established for purposes of the split, and in which the rights are held by the same owners as the rights in the split company, each holding a part of the new company that is identical with his part of the split company;
- (2) the transfer of assets and obligations from the split company to a new company, which was established for purposes of the split, and which is wholly owned by the split company.

### **Tax exemption**

105B. (a) The cancellation of shares in a split company or a reduction of its

capital in a split under section 105A(1), and the transfer of the split company's assets to the new company shall not be charged tax under this Ordinance, under the Inflationary Adjustments Law or under the Land Appreciation Tax Law, all if the requirements of this Chapter were met.

- (b) The sale of any asset, which is not charged Land Appreciation Tax because of the provisions of subsection (a), shall be charged acquisition tax at the rate of 0.5% of its value.

### Conditions of entitlement

105C.(a) The benefits under this Chapter shall apply to a split, if all the following hold true:

- (1) the company proposes to split for a business and economic purpose, improper tax avoidance or a reduction of tax not being among the main objectives of the split;
- (2) most of the assets that remain in the split company and most of the assets transferred to the new company as part of the split are not sold by either of them during two years after the date of the split, and during the said period use of them is made in the course of the company's business, in a manner customary under the circumstances; for this purpose: **"assets"** and **"most of the assets"** – within their meaning in section 103C(2), but its rights in the new company shall not be included in the calculation of the split company's assets in a split under section 105A(2);
- (3) the main economic activity, which the split company carried on during the two years before the date of the split, is continued during two years after the date of the split in the new company or in the continuing split company;
- (4) the new company and the continuing split company have independent economic activities, the income from which is liable to tax under section 2(1), and which stems from the activity of the split company, and if the split company is a nonprofit or cooperative society, then the activity of the nonprofit or cooperative society is continued in it or in the new company, as the case may be;
- (5) the split company and the new company are one of the following:
  - (a) an Israel resident incorporated in Israel under the Companies Ordinance, the Companies Law, the Cooperative Societies Ordinance or the Amutot Law;
  - (b) a company approved by the Director for this purpose, which is a foreign resident company or an Israel resident foreign company, as defined in the Companies Ordinance or the Companies Law; aforesaid approval may be conditional on the provision of guaranties and on other conditions, as the Director may prescribe;
- (6) (a) the value of the assets transferred from the split company to each of the new companies in the course of the split, or those left in the continuing split company, shall not be less than 10% of the value of the split company's assets, all according to the value specified in the returns adjusted as of the date of the split; for this purpose – the rights of the split company in the new company shall not be included in the calculation of the split company's assets in a split under section 105A(2);

- (b) immediately after a split under section 105A(1), the market value of one new company shall not exceed the market value of another new company more than four-fold, and if the split company is a continuing split company, then the market value of each new company shall not exceed the market value of the split company more than four-fold and it shall not be less than one fourth of the market value of the split company;
  - (c) the Director may, on the company's application and for reasons that shall be recorded, prescribe that the split company divide its assets otherwise than said in subparagraphs (a) or (b), if it was proven to his satisfaction that their provisions are liable to have an adverse effect on the objectives of the split, all on conditions that he may prescribe;
- (7) (a) In a split under section 105A(1) and in the case of a continuing split company, the shareholders in each of the new companies shall – immediately after the split and during two years after its date – have the same rights that they had in the split company and the same part of each of the rights, all immediately after the date of the split;
- (b) in a split under section 105A(2), the split company shall hold – immediately after the split and during two years after the date of the split – all the rights in the new company;
- (c) holders of rights that are traded on an exchange shall not – for purposes of subparagraph (a) – be included in the count of holders of rights, unless they were controlling members on the date of the split; for this purpose: **"controlling member"** – other than a benefit fund and a trust fund;
- (8) notwithstanding the provisions of paragraph (7), if one of the following occurs it shall not be deemed a change in rights after the split, on condition that – at no time during the two years after the date of the split – the rights of the persons who held the rights immediately after the split drop to less than 50% of each of the rights in each of the new companies and in the split company, as the case may be:
- (a) one or more of the holders of rights sells voluntarily less than 10% of any of the rights he holds, or he sells a greater percentage with the agreement of the other shareholders, on condition that all the rights sold by all holders of rights do not exceed 10% of all the rights in the company before allocations to persons who did not hold rights in the company before the split;
  - (b) new rights are allocated to persons who did not hold rights in the company before the allocation;
  - (c) shares defined in section 102 are offered to the general public on an Exchange by prospectus, which states that the Exchange agreed to list the shares for trading on it;
  - (d) repealed
- (8a) notwithstanding the provisions of paragraph (7) and in addition to the provisions of paragraph (8), an involuntary sale of rights shall not be deemed a change in the rights after the split;
- (9) the date of the split shall be at the end of the tax year;
- (10) no cash payments or additional consideration of any other kind

- passed between the holders of rights in the split company as part of the split;
- (11) during two years after the date of the split there are no transfers of cash or of assets, no provision of guaranties or other activity between the new companies or between them and the split company, as the case may be, except in the ordinary course of business;
  - (12) after the split the value of assets exceeds the value of obligations in each of the new companies and in the split company, as the case may be, in accordance with adjusted reports as of the date of the split;
  - (13) the plan for the split was approved by the Director before the split, as said in section 105H(b);
  - (14) if the new company or the split company is a real estate association and if land was transferred to a new company – if construction of a building was completed on that transferred land within four years after the split according to conditions to be set by the Director;
  - (15) if the split company is a trust fund, then it may split only into trust funds of the same category as the split company.
- (b) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe additional conditions and rules for implementation of the split, and he may designate categories of splits that do not require the Director's approval, as said in subsection (a)(13).

#### **Division of obligations and profits**

- 105D. (a) The obligations of the split company shall be divided among the new companies, or between the continuing split company and a continuing new company, as the case may be, according to the following rules:
- (1) obligations that do not constitute equity under section 1A of Schedule One to the Inflationary Adjustments Law, and which can be related to a specific asset or a specific activity, shall be allocated to the company that holds that asset, but no obligation shall be related to an asset if it exceeds of the value of that asset, all according to adjusted reports as of the date of the split;
  - (2) the balance of obligations, which was not allocated as said in paragraph (1), shall be allocated according to the ratio between the value of assets in that company to the total value of assets in the split company before the split, according to adjusted reports as of the date of the split; for this purpose: "**value of assets**" – the value of assets, less obligations related as said in paragraph (1), and less the value of rights which a split company holds in a new company.
- (b) The losses of a continuing split company under sections 28 and 92, as the case may be, shall be divided among the new companies or between the continuing split company and the new company in proportion to the ratio of their equities (hereafter: equity ratio), on condition that losses under section 28(h) be in the company that holds the asset from which the loss stems; for the purpose of this section: "**equity**" – the amount by which the value of a company's assets, less the value of rights which a split company holds in a new company, exceeds the value of obligations allocated to the company as said in subsection (a), all according to reports adjusted as of the date of the split.

- (c) Profits available for distribution, within their meaning in section 94B –
  - (1) shall be divided – in a split under section 105A(1) – between the continuing split company and the new company or between the new companies, as the case may be, according to the equity ratio;
  - (2) shall remain in the split company, in a split under section 105A(2);
  - (3) the Director shall make rules on their calculation.
- (d) Repealed
- (e) A deduction because of inflation, within the meaning of section 7 of the Inflationary Adjustments Law, shall be divided according to the equity ratio, but an aforesaid deduction, which under section 7(e) of the said Law relates to a work unit, as defined in section 18(d), shall be in the same company as the work unit.
- (f) Notwithstanding the provisions of this Ordinance, if a split company under section 105A(1) owns an approved enterprise, within its meaning in the Investment Encouragement Law, and if at the time of the split the company is able to distribute a dividend under sections 47(b)(2) or 51(c) of that Law, then that part of the dividend shall be charged to tax, which does not exceed the excess of assets transferred to the new company at the time of the split as said in the aforesaid sections, as the case may be, as if it had been distributed.
- (g) Obligations, contingent obligations, income, expenses, deductions and so forth, which did not appear in the reports of the split company at the time of the split and which stem from its activity before the split shall be divided between the split company and the new company or between the new companies, as the case may be, according to the Director's instructions.

#### **Setting off losses of a split company**

- 105E.(a) A loss said in section 28, which a split company suffered up to the date of the split, which was transferred to each of the companies as said in section 105D(b), and which may be carried forward to future years, may be set off against the income of the new company or of the split company, as the case may be, beginning with the tax year after the split, but in each tax year each company shall be allowed to set off an amount no greater than 20% of the total of the said loss, or 50% of chargeable income of the company where it is, before the set off of that loss, whichever is the smaller amount; in respect of this subsection and of subsection (c)(1): "**chargeable income**" – before the deduction of losses, but without income against which a loss was set off under section 92.
- (b) A loss said in section 92, incurred by a split company up to the date of the split and transferred to one of the companies as said in section 105D(b), and which can be carried forward to subsequent years, may be set off against a capital gain of the new company or of the split company, as the case may be, beginning with the tax year after the split, but in each tax year each company shall be allowed to set off an amount no greater than 20% of the total of the said loss, or 50% of capital gain in that company before the set off of that loss, whichever is the smaller amount; a period of five years after the day of the split shall not be taken into account for the time limit set in section 92 for setting off an aforesaid loss.
- (c) (1) If a loss or capital loss said in subsections (a) or (b) cannot be set

off in that year because of the limitation of 50% of chargeable income, then it may be set off successively in the following years, on condition that no loss said in this paragraph be set off which, together with the loss said in subsection (a), exceeds 50% of the company's income before the set off of losses from preceding years.

- (2) If a loss said in subsection (b) could not be set off in that year because of the limitation of 50% of capital gain, then it may be set off successively in the following years, one after the other, on condition that no loss said in this paragraph be set off which, together with the loss said in subsection (b), exceeds 50% of the company's capital gain before the set off of losses from preceding years.
- (d) A loss or capital loss, which could not be set off as said in subsections (a) to (c) until the end of the fifth year after the date of the split, may be set off beginning with the sixth year, subject to the provisions of sections 28 and 92, as the case may be.
- (e) Notwithstanding the provisions of subsection (a), a loss sustained by a split company before the split from renting a building may be set off under the provisions of section 28(h).
- (f) The Director may prescribe restrictions on the set off of a loss or of a capital loss, if he is satisfied that the split will result in an improper reduction of tax because of the set off; however, if the split company requested the Director's advance certification, then the Director must inform it of his decision under this paragraph together with his notification of that certification; a decision under this paragraph may be appealed, as if the Director had withdrawn a certification said in section 103J(g).
- (g) If, at the time of the split, a split company and a new company assumed a written obligation before the Director that their ownership will not change within two years after the day of the split, then they shall not be restricted under this section in setting off losses; an undertaking said in this subsection shall constitute a condition for the split, and its violation shall be deemed a violation of one of the conditions specified in section 105C.
- (h) In this section, "**capital gain**" – including land appreciation.

#### **Asset transferred in a split**

- 105F. (a) When an asset has been transferred in a split, then its original cost, the balance of its original cost, its cost of acquisition and its date of acquisition, each as the case may be, shall be for purposes of this Ordinance, of the Inflationary Adjustments Law and of the Land Appreciation Tax Law, as they would have been in the split company if the asset had not been transferred, and the new company shall be allowed, at its sale, the deductions that would have been allowed the split company if it had sold the asset; in respect of an aforesaid asset, which constitutes stock, its cost shall be the amount set as final stock for purposes of the split company's assessment on the date of the split.
- (b) The transfer of an asset in a split shall be deemed a sale for purposes of the number of periods under section 21A of the Industry Encouragement Law.

#### **Profit from the sale of shares**

- 105G When a person sells a share in a new company which was allocated to him at



the split (hereafter: the new share) or in a split company, and if rights in the split company and in the new company were not listed on an Exchange for trading on the day of the split, then the following provisions shall apply:

- (1) in a split under section 105A(1), the original cost of the shares of the new company shall be the proportional part of the original cost of the shares of the split company, according to the equity ratio said in section 105D(b), adjusted at the rate of index increase from the day of acquisition of the shares in the split company until the date of the split, less any real loss that would have been incurred, if the proportional part of the shares had been sold on the date of the split, on condition that it is not less than the proportional part of the original cost of the shares in the split company (hereafter: the adjusted cost); the differential between the original cost of the proportional part of the shares in the split company and the aforesaid adjusted cost is hereafter called the "adjustment differential"; the original cost of the shares of the split company shall be reduced in accordance with the equity ratio said in section 105D(b); for this purpose: **"real loss"** – the amount by which a share's market value is lower than its adjusted original cost;
- (2) in a split under section 105A(2), the original cost of the shares in the new company shall be set according to the excess of assets transferred to it, less any real loss that would have been incurred, if the assets and obligations had been sold together on the date of the split (hereafter: the adjusted cost); for this purpose:  
**"adjustment differential"** – the differential between the balance of the original cost of the transferred assets and the adjusted balance of their original cost;  
**"excess of assets"** – the excess of the balance of the adjusted original cost of assets over obligations, according to the adjusted reports as of the day of the split;  
**"real loss"** – the amount by which the market value of assets and obligations, which are transferred together, is smaller than their adjusted original cost, less the obligations;
- (3) an adjustment differential said in paragraphs (1) and (2), which constitutes part of the original cost of the sold shares, shall be added to the consideration from the sale of the shares, as the case may be, and it shall be deemed an additional inflationary amount;
- (4) the date of the split shall be deemed the date of acquisition of the shares in the new company, but for the calculation of the real capital gain until the determining date, the day on which the shares of the split company were acquired shall be deemed the day of acquisition of the shares of the new company;
- (5) in a split under section 105A(1), if the shareholder was a foreign resident at the time of the split, and if at the sale of the shares of the new company he requests that the exchange rate at which he acquired the shares of the split company be deemed the index for calculation of the adjusted price, then the adjustment differential shall be exempt of tax.

#### **Miscellaneous provisions**

105H.(a) The provisions of sections 103G, 103I to 103L and 103N to 103S shall apply, mutatis mutandis, as the case may be, to a split and for this purpose, wherever there it says –

- (1) "merger", read "split";
- (2) "date of merger", read "date of split";

- (3) "transferor company", read "split company";
- (4) "merged company", read "new company";
- (b) Notwithstanding the provisions of section 103I, the benefits said in section 105B shall not be given if the Director's approval was not obtained before the split; if the Director determined that a split does not comply with the conditions in this Chapter, then his decision may be appealed as if it were an Order under section 152.
- (c) When a company has split, then – if it is not a holding company – the provisions of section 130A shall apply to it and to the new companies after the split, if that section applied to the split company before the split.

#### **Split to an existing company**

105I. The Director may make rules, according to which the transfer of assets, obligations and capital from a split company to a company that is not a new company set up for that purpose, or the merger of a split company or of a new company after the split, shall be exempt of tax as said in this Part, on condition that the conditions specified in Chapter Two and in Chapter Four of this Part apply, mutatis mutandis.

#### **Authorization on structural changes in real estate associations**

105J. The Minister of Finance may, with approval by the Knesset Finance Committee, make regulations on the matters of sections 103M, 104A(b) and (b1), 104B(a)(4), 104H and 105C(a)(14), and he may make the exemption under them subject to conditions, including the change of periods and conditions prescribed in the said sections, and he may also prescribe circumstances under which the provisions of the said sections shall not apply.

PART FIVE "C" (Sections 105K to 105S2): Repealed

## **PART SIX: CHARGEABILITY TO TAX THROUGH A REPRESENTATIVE**

#### **Trustees, etc., of legal incompetents**

106. A liquidator or a receiver appointed by the Court or under any statute that is in effect in Israel, as well as a trustee, guardian of a person or property, or a committee that has the direction, control or management of any property or enterprise on behalf of a legal incompetent shall be chargeable to tax in the manner and amount, in which that person would be chargeable, were he not a legal incompetent.

107. Repealed

#### **Foreign resident with an agent in Israel**

108. A foreign resident, whether an Israel citizen or not, shall be assessable and chargeable through his trustee, guardian or committee, or in the name of his attorney, factor, agent, receiver, branch or manager, whether they receive the income or not, all in the manner and in the amount in which that foreign resident would be assessed and charged, if he were an Israel resident and if that income were received by him.

#### **Income of foreign resident from power of attorney, etc.**

109. A foreign resident shall be assessable and chargeable in respect of any income that arises, directly or indirectly, from any power of attorney, agency, authorization, receivership, branch or management, or through any of those, and he shall be assessable and chargeable through the attorney, factor, agent, receiver, branch or manager, all as the case may be.

**Ship's master**

110. The master of any ship owned or chartered by a foreign resident chargeable under the provisions of sections 71 to 74, shall be deemed the agent of that foreign resident for purposes of this Ordinance, without excluding any other agent of that foreign resident.

**Business with a foreign resident**

111. If a foreign resident carries on business with a resident, and it appears to the Assessing Officer that, because of the close connection between them and because of the substantial control exercised by the foreign resident over the resident, the course of business between those persons may be arranged – and that it is arranged – so that the business done by the resident in pursuit of his connection with the foreign resident produces no profit for him or less than the ordinary profit that is to be expected from that business, then the foreign resident shall be assessable and chargeable to tax through the resident, as if the resident were his agent.

**Procedure when the amount of a foreign resident's income cannot be ascertained**

112. (a) If the Assessing Officer finds that the true amount of earnings or profits of any foreign resident, which are chargeable through a resident, cannot be readily ascertained, then he may assess and charge the foreign resident a fair and reasonable percentage of the turnover of the business done by the foreign resident through or with the said resident; when the Assessing Officer has done so, the provisions of this Ordinance on the delivery of returns or particulars by persons who act on behalf of others shall apply to this case, obligating the resident to deliver returns or particulars of the said business in the manner in which persons who act on behalf of legal incompetents or foreign residents must deliver returns or particulars about chargeable income.
- (b) The said percentage shall in each case be determined by the Assessing Officer while taking the nature of the business into account, and when it has been determined, it may be appealed, as provided in sections 153 to 158.

**Transactions between foreign residents**

113. If a foreign resident executes sales or carries out transactions with other foreign residents in circumstances which would make him chargeable through a resident in pursuance of sections 110 and 111, that fact alone shall not make him chargeable in respect of gains or profits arising from the said sales or transactions.

**Assessment of a foreign resident's income from the sale of foreign products**

114. If a foreign resident is charged to tax through any attorney, agent, licensee, receiver, branch or manager, in respect of earnings or profits derived from the sale of goods or products manufactured or produced abroad by that foreign resident, then the person through whom the foreign resident was so charged may apply to the Assessing Officer to have the tax assessment in respect of

those earnings or profits made or amended on the basis of the profits which might reasonably be expected to have been earned by a merchant or retailer who buys directly, as aforesaid, from the manufacturer or producer, if the goods or products were sold or retailed by them or on their behalf, and after he proves, to the Assessing Officer's satisfaction, the amount of those profits, the assessment shall be made or amended accordingly.

**Foreign resident not to be assessed through an agent who is not his authorized agent**

115. None of the provisions of sections 108 to 114 shall render a foreign resident chargeable through a broker or general commission agent or other agent, in respect of earnings or profits that arise from a sale or transaction carried out by them, if those are not authorized agents who regularly carry on the foreign resident's agency, or if they are not authorized agents in accordance with sections 110 to 112.

**Acts that must be performed by trustees, etc.**

116. If a person is assessable and chargeable in respect of a legal incompetent, or if a foreign resident is chargeable in his name, then he shall be responsible for all matters required to be done under this Ordinance for the assessment of the income of the person for whom he acts, and for the payment of the tax payable on it.

**Manager of a body of persons**

117. The manager or other principal officer of an incorporated body of persons shall be responsible for the performance of all acts and things, performance of which is required under this Ordinance for the assessment of that body of persons and for payment of the tax.

**Records that must be prepared by a representative or agent**

118. If a person in whatever capacity receives anything in cash or in kind, which is income derived from any of the sources enumerated in this Ordinance and which belongs to a person chargeable in respect of that income, or who would be so chargeable if he were an Israel resident and not a legal incompetent, then he shall, whenever the Assessing Officer requires him to do so by a notice and within the time stated in that notice, prepare and deliver a record signed by him, containing a true and correct statement of all aforesaid income and the name and address of every person to whom the income belongs; the provisions of this Ordinance, which concern the failure to deliver records or particulars in accordance with a notice from the Assessing Officer, shall apply to the said record.

**Indemnification of representative**

119. A person responsible under this Ordinance for the payment of tax for another person may retain, out of the money that comes into his possession for that person, an amount sufficient to pay the said tax, and he is thereby indemnified against any person whatsoever for all payments made by him in pursuance and by virtue of this Ordinance.

**Tax collection under special circumstances**

- 119A. (a) (1) If a body of persons had a tax debt and is wound up or transfers its assets for no consideration or for partial consideration without being left with the means in Israel to pay the said debt, then the body's tax debt may be collected from whoever received the

- assets under the said circumstances.
- (2) If a body of persons has a final tax debt and it transfers its activity to another body of persons, which directly or indirectly has the same controlling members or their relatives (in this paragraph: the other body) for no consideration or for partial consideration, without being left means in Israel to pay the said debt, then the body's tax debt may be collected from the other body.
  - (3) Without derogating from the provisions of paragraphs (1) and (2), if a body of persons had a final tax debt and was liquidated or terminated its activity without paying the said tax debt, then the assets which the body had are deemed to have been transferred to its controlling members for no consideration and the tax debt may be collected from them, unless different facts are proven to the Assessing Officer's satisfaction.
- (b) If an individual had a final tax debt for any tax year, and if he transferred his assets without consideration or for partial consideration to a relative or to a company in which he is a controlling member, without being left with means in Israel to pay the said debt, then the debt he owes may be collected from whoever received the assets under the said circumstances, as long as three years have not passed since the end of the tax year in which the tax debt became final or in which the assets were transferred, whichever was later.
  - (c) No more shall be collected from whoever received the assets or activities under subsections (a) or (b), than the value of the assets or activities he received for no consideration, or no more than the difference between the partial consideration he paid and the value of the assets or activities, and if he paid tax in connection with the transfer of the said assets or activities, then no less than the said value or difference, less the amount of tax paid.
  - (c1) If the manager of a body of persons, who is a controlling member of that body, was convicted of not transmitting tax deducted under sections 219 or 224A, and if it is no longer possible to appeal against his conviction, or if he paid monetary composition because of offenses under those sections, then the tax deducted as aforesaid and not transmitted to the Assessing Officer may be collected from him.
  - (c2) If a body of persons was assessed because of one of the acts specified in section 220 and the body's appeal against the assessment was rejected by the Court in a judgment that no longer is subject to appeal or against which no appeal was lodged with the Court, then the tax debt not paid by the body may also be collected from a person who held a position in that body when the said act was committed, if the Assessing Officer has a priori evidence that the act was committed with the knowledge of the holder of that position, unless the holder of that position proves that he took all reasonable steps to ascertain that the act be prevented.
  - (d) In this section –
    - "tax debt"** – within its meaning in section 195A, other than a debt of advances;
    - "final tax debt"** – a debt in respect of which there no longer is any right of objection, contestation or appeal;
    - "relative"** – as defined in section 88;
    - "controlling member"** – any person who, alone or together with his relative, holds at least 25% of one of the rights enumerated in the definition of "controlling member" in section 32(9)(a);

**"holder of a position"** – an active manager, partner or controlling member.

- (e) The Taxes (Collection) Ordinance applies to the collection of amounts under this section.
- (f) A decision to collect a tax debt under this section may be contested before the Director within 21 days after the day on which notification thereof was served; a decision by the Director under this subsection may be appealed before the District Court within thirty days after the decision was served.

#### **Assessing the income of a deceased person**

120. (a) If a person died during the tax year and if that person, had he not died, would have been chargeable to tax for that tax year, or if a person died within three years after the end of a tax year and no assessment had been made for him for that year, then his legal personal representative shall be liable for the tax with which that person would have been chargeable if he were alive, and he shall pay it and shall also be responsible for the performance of all those acts and things for which that person would have been responsible under this Ordinance, if he were alive.
- (b) From the day of a person's death, the chargeable income of his estate shall be deemed income of the heirs, in accordance with their shares in the income of the estate.
- (c) If all or some of the heirs or their parts in the income of the estate are not known, then the personal legal representative of the deceased shall pay, out of the estate, tax at the rate of 40% on account of the tax due from the heirs on the income of the estate.
- (d) The provisions of sections 174 to 181 shall apply, mutatis mutandis, to payments on account of tax under subsection (c).
- (e) After the income of the estate has been distributed and included in the income of each heir, the tax paid as aforesaid by the personal legal representative shall be set off against the tax on the income of the heirs, according to the respective part of each in the income of the estate.
- (f) For purposes of this section: **"personal legal representative"** includes an heir, estate manager, executor of the deceased person's will and every person who may – under a statute or under a Court decision – deal with the assets of the estate.

## **PART SIX "A": LINKAGE OF INCOME CEILINGS, CREDIT POINTS, PENSION POINTS AND SOCIAL CONCESSIONS**

#### **Definitions**

120A. In this Part –

**"social concessions"** – the amount specified in section 9(5), the amounts of exemption of a retirement grant or death grant under section 9(7a), the amount stated in section 9(16a), (16b) and (18a), the amount exempt under section 9(20), an entitling pension within its meaning in section 9A(a), the amount exempt under section 9A(b), the amount stated in section 9A(c), the amount stated in section 17(5a), the amount stated in section 32(9), the amount stated in section 44(a)(1) as the ceiling of the amounts in respect of

which credit is to be allowed, the amounts stated in section 45A, the amounts stated in section 47, the amount stated in section 57(b)(1), the amount stated in section 58A(c), the amount stated in section 66(e)(2) and the amounts stated in section 125D;

**"income ceilings"** – the amounts of income for the purpose of determining tax rates under section 121, and for the purpose of the rates of credits under section 121A.

#### **Linkage**

- 120B. (a) On January 1 of every tax year income ceilings, the amounts of credit points and of pension points, as well as social concessions (all these hereafter in this section: "the amounts"), as they were on January 1 of the preceding tax year, shall be adjusted at the rate of the index increase during the preceding tax year. *(Amendment No. 136 provides that – as long as the index does not rise by more than 5% over the index known on January 1, 2004 – the words : "the amounts of credit points and of" in this section should not be read in tax years 2005 to 2008 – Tr.).*
- (b) If an agreement between the Coordination Office of the Economic Organizations and the General Federation of Labor in Israel determined that a cost of living bonus be paid to wage earners in the economy, in respect of work performed in a certain month and thereafter, then the amounts of pension points as of January 1 of that tax year shall be adjusted in that month at the rate of the index increase from the beginning of the tax year until the end of the said month.
- (c) Repealed
- (d) The Minister of Finance may make rules for rounding off amounts adjusted under this section.

## **PART SEVEN: TAX RATES**

### **Tax rates for individuals**

121. (a) The tax on the chargeable income of an individual in the tax year shall be as follows:
- (1) on each new shekel of the first NS 192,000 – 30%;
  - (2) on each new shekel from NS 192,001 to NS 413,400 – 32%;
  - (3) on each additional new shekel – 44%.
- (b) (1) Notwithstanding the provisions of subsection (a)(1) and subject to the provisions of paragraph (2), the following rates shall apply in the tax year to chargeable income from personal exertion or to the chargeable income of an individual who has reached age 60:
- (a) on each new shekel of the first NS 50,040 – 10%;
  - (b) on each new shekel from NS 50,041 to NS 89,040 – 14%;
  - (c) on each new shekel from NS 89,041 to NS 133,680 – 21%;
  - (d) on each new shekel from NS 133,681 to NS 192,000 – 28%.
- (2) The reduced rates prescribed in paragraph (1) shall not apply to income, in respect of which account books must be kept, if in its respect acceptable books were not kept.

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**NOTE:** The tax brackets stated in section 121 above will apply in tax year 2010 and

*thereafter. Until then different tax brackets are in effect, as provided by Section 76 of Amendment No. 147, which was again amended in Amendment No. 160*

*Below we state the amounts, as they originally appeared in Amendment No. 147 and as changed in Amendment No. 160. In respect of tax years 2006 and 2007, those amounts are also shown in parentheses, after they were adjusted for changes in the index, as shown in Karan A. In respect of tax years 2008 and 2009 those index driven changes are, of course, not yet known. – Tr.*

**Income Tax Ordinance – Ad Hoc Provisions for tax years 2006 to 2009  
in respect of section 121**

76. (a) In respect of tax year 2006, section 121 of the Ordinance shall be read as follows:

**"Tax rates for individuals for tax year 2006**

121. (a) In tax year 2006, the tax on the chargeable income of an individual shall be as follows:

- (1) on each new shekel of the first NS 133,680 (NS 137,280) – 30%;
  - (2) on each new shekel from NS 133,681 (NS 137,281) to NS 238,680 (NS 245,040) – 36%;
  - (3) on each new shekel from NS 238,681 (NS 245,041) to NS 413,400 (NS 424,440) – 37%;
  - (4) on each additional new shekel – 49%.
- (b) (1) Notwithstanding the provisions of subsection (a)(1) and subject to the provisions of paragraph (2), the following rates shall apply in the tax year to chargeable income from personal exertion or in respect of the chargeable income of an individual who has reached age 60:
- (a) on each new shekel of the first NS 50,040 (NS 51,360) – 10%;
  - (b) on each new shekel from NS 50,041 (NS 51,362) to NS 89,040 (NS 91,440) – 22%;
  - (c) on each new shekel from NS 89,041 (NS 91,441) to NS 133,680 (NS 137,280) – 29%.
- (2) The reduced rates prescribed in paragraph (1) shall not apply to income, in respect of which account books must be kept and in its respect acceptable books were not kept. "

(b) In respect of tax year 2007, section 121 of the Ordinance shall be read as follows:

**"Tax rates for individuals**

121. (a) In tax year 2007 the tax on the chargeable income of an individual shall be as follows:

- (1) on each new shekel of the first NS 133,680 (NS 136,920) – 30%;
  - (2) on each new shekel from NS 133,681 (NS 136,921) to NS 192,000 (NS 196,560) – 35%;
  - (3) on each new shekel from NS 192,001 (NS 196,561) to NS 413,400 (NS 423,240) – 36%;
  - (4) on each additional new shekel – 48%.
- (b) (1) Notwithstanding the provisions of subsection (a)(1), the following rates shall apply in the tax year to chargeable income from personal exertion or in respect of the chargeable income of an



individual who has reached age 60:

- (a) on each new shekel of the first NS 50,040 (NS 51,240) – 10%;
  - (b) on each new shekel from NS 50,041 (NS 51,241) to NS 89,040 (NS 91,200) – 21%;
  - (c) on each new shekel from NS 89,041 (NS 91,201) to NS 133,680 (NS 136,920) – 29%;
- (2) The reduced rates prescribed in paragraph (1) shall not apply to income, in respect of which account books must be kept and in its respect acceptable books were not kept. "

(c) In respect of tax year 2008, section 121 shall be read as . . . follows:

**"Tax rates for individuals**

121. (a) In tax year 2008 the tax on the chargeable income of an individual shall be as follows:

- (1) on each new shekel of the first NS 140,640 – 30%;
  - (2) on each new shekel from NS 140,641 to NS 202,080 – 33%;
  - (3) on each new shekel from NS 202,081 to NS 435,120 – 35%;
  - (4) on each additional new shekel – 47%.
- (b) (1) Notwithstanding the provisions of subsection (a)(1), the following rates shall apply in the tax year to chargeable income from personal exertion or in respect of the chargeable income of an individual who has reached age 60:
- (a) on each new shekel of the first NS 52,680 – 10%;
  - (b) on each new shekel from NS 52,681 to NS 93,720 – 16%;
  - (c) on each new shekel from NS 93,721 to NS 140,640 – 26%;
- (2) The reduced rates prescribed in paragraph (1) shall not apply to income, in respect of which account books must be kept and in its respect acceptable books were not kept. "

(d) In respect of tax year 2009, section 121 shall be read . . . as follows:

**"Tax rates for individuals**

121. (a) In tax year 2009 the tax on the chargeable income of an individual shall be as follows:

- (1) on each new shekel of the first NS 133,680 – 30%;
  - (2) on each new shekel from NS 133,681 to NS 192,000 – 32%;
  - (3) on each new shekel from NS 192,001 to NS 413,400 – 34%;
  - (4) on each additional new shekel – 46%.
- (b) (1) Notwithstanding the provisions of subsection (a)(1), the following rates shall apply in the tax year to chargeable income from personal exertion or in respect of the chargeable income of an individual who has reached age 60:
- (a) on each new shekel of the first NS 50,040 – 10%;
  - (b) on each new shekel from NS 50,041 to NS 89,040 – 15%;
  - (c) on each new shekel from NS 89,041 to NS 133,680 – 23%;
  - (d) on each new shekel from NS 133,681 to NS 192,000 – 30%.
- (2) The reduced rates prescribed in paragraph (1) shall not apply to

income, in respect of which account books must be kept and in its respect acceptable books were not kept.

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121A. Repealed

**Rental of dwelling unit**

122. (a) If, during the tax year, an individual had income from the rental of a unit used for residential purposes in Israel (hereafter in this section: rental income), he may pay on it tax at the rate of 10% thereof, instead of the tax on it to which he is liable under section 121, if the rental income is not income from business as said in section 2(1).
- (a1) Tax said in subsection (a) shall be paid within 30 days after the end of the tax year in which the individual had rental income, unless the individual paid advances under section 175 in that tax year.
- (b) repealed
- (c) Notwithstanding the provisions of any statute, an individual who elected to pay tax as said in subsection (a) shall not be entitled to deduct depreciation or any other deduction in respect of the dwelling, or expenses incurred in the creation of the rental income, and he shall not be entitled to any set off, credit or exemption on rental income or from the tax on it; however, for the purpose of calculating Land Appreciation Tax on the sale of the dwelling the maximum amount of depreciation or deduction which could have been deducted under any statute for the period in which the individual paid tax as said in subsection (a), if not for this section, shall be added to the sale price.
- (d) Repealed
- (e) Repealed

**Rental income from abroad**

- 122A. (a) If an individual had rental income in the tax year from the rental of real estate abroad, then he may pay on it tax at the rate of 15%, instead of the tax to which he is liable under section 121, if the income is not income from business as said in section 2(1).
- (b) If an individual elected to pay tax as said in subsection (a), then he is not entitled to subtract from the rental income expenses incurred in producing the income, except for depreciation, and he also is not entitled to any set off, credit or exemption from the rental income or from the tax due on it, including a credit said in Part Ten, Chapter Three.
- (c) For the purposes of this section, "**real estate**" includes a part thereof.

123. Repealed

**Rate of tax on key money and premiums**

124. Notwithstanding the provisions of sections 121, 126 and 127, the tax on income from key money or premiums derived from house property shall not exceed 35%, if the assessee paid tax on that income at the said rate to the Assessing Officer within 30 days after its receipt, or – if the assessee reports his income on an accrual basis – within the period prescribed in section 132 for filing the return or within 30 days after its receipt, whichever is earlier.

**Tax rate on the sale of rights to which the Tenant Protection Law applies**

- 124A. (a) in this section –

**"determining day"** – November 7, 2001;

**"determining period"** – the period from the determining day to the end of tax year 2003.

- (b) Notwithstanding the provisions of section 121, if on the determining day a tenant holds an asset to which the Tenant Protection Law applies, and if during the determining period he sells all his rights in the asset to the holder of rights in that asset, then he shall be liable to tax on the real capital gain at rates that shall not exceed the following:
- (1) if the sale took place between the determining date and the end of tax year 2002 – 15%;
  - (2) if the sale took place in tax year 2003 – 20%;
- on condition that – after the sale – the Tenant Protection Law ceased to apply to that asset.

#### **Tax rate on income from gambling, lotteries or prizes**

124B. Notwithstanding the provisions of section 121, the tax rate on income from gambling, lotteries or prize winning activity under section 2A shall be 25%, with no entitlement to any exemption, reduction, deduction, credit or set off whatsoever, except for an exemption under section 9(28) or a deduction under section 17(11).

#### **Tax rate on sale of patent, etc.**

125. Notwithstanding the provisions of section 121, the taxes on income received by an inventor from the sale of a patent or design, or by an author from the sale of a copyright, the invention or work not being within the scope of his regular occupation, shall not exceed 40%.

#### **Tax on income after death**

125A. Notwithstanding the provisions of section 121, the tax rate on a person's income to which section 3(f) applies, or on a person's work income received after his death, shall not exceed 40%; for this purpose: **"work income"** – including part of a grant received in consequence of death, which is not exempt under section 9(7a).

#### **Tax rate on dividends**

125B. Notwithstanding the provisions of section 121 and 126, the tax rate on income from dividends shall be as follows:

- (1) dividends received by an individual – 20%;
- (2) notwithstanding the provisions of paragraph (1), dividends received by an individual who – at the time he received the dividend or at any time during the preceding twelve months – was a substantive shareholder, as defined in section 88, in the body of person that paid the dividend – 25%;
- (3) dividends received by a family company – 20%; however, if the assessee, within its meaning in section 64A, is directly or indirectly a substantive shareholder in the body of persons that paid the dividend – 25%;
- (4) dividends that are not tax exempt and were received by a public institution or a benefit fund, as defined section 9(2) – 20%;
- (5) dividends received by a foreign resident body of persons – 20%; but if – at the time it received the dividend or at any time during the preceding twelve months – the body of persons was a substantive shareholder, as defined in section 88 – 25%.

### **Tax rate and tax exemption on an individual's profits from a trust fund**

- 125B1. (a) Profits distributed by the manager of a chargeable trust fund to an individual unit holder, for whom the income does not constitute income from business or vocation, are exempt of tax.
- (b) Profits distributed by the manager of an exempt trust fund to an individual unit holder, for whom the income does not constitute income from business or vocation, are liable to tax at the rate of 20%.
- (c) Every term in this section shall have the meaning it has in Part Five.

### **Tax rate on income from interest and discount**

- 125C. (a) In this section –
- "substantive shareholder"** – as defined in section 88;
- "index"** – the Consumer Price Index, as last published on behalf of the Central Bureau of Statistics before the day in case, and in respect of an asset, the value of which is linked to a foreign currency or that is denominated in a foreign currency – the currency exchange rate;
- "interest"** includes discount.
- (b) An individual is chargeable to tax on income from interest at a rate that shall not exceed 20%, and this income shall be deemed the highest bracket of his chargeable income.
- (c) (1) Notwithstanding the provisions of subsection (b), if the interest was paid on an asset that is not index linked, or if it is partly linked to the increase of all or part of the index, or is not index linked up to the redemption or repayment, then the individual's income from interest shall be charged tax at the rate of 15%.
- (2) The Minister of Finance may, by Order, change the interest rate stated in paragraph (1) in accordance with changes in the index.
- (d) Notwithstanding the provisions of subsections (b) and (c), an individual is liable to tax on income from interest at the rates prescribed in section 121, if one of the following holds true for him:
- (1) the interest is income under section 2(1) or is entered in his account books or should be entered as aforesaid;
- (2) the individual claimed interest and linkage differential expenses in respect of the asset, on which the interest is paid;
- (3) the individual is a substantive shareholder in the body of persons that paid the interest;
- (4) the individual is employed by the body of persons that paid the interest, or provides services to it or sells products to it, or he has some other special relationship with it, unless it was proved to the Assessing Officer's satisfaction that the interest rate was set in good faith and without being affected by the said special relationship between the individual and the body of persons;
- (5) the interest was paid by a training fund before the periods said in section 9(16a) or (16b) passed, or it was paid by a savings benefit fund and the provisions of section 3(d) applied to it;
- (6) some other condition prevails, which the Minister of Finance prescribed with approval by the Knesset Finance Committee.
- (e) The provisions of this section shall not apply to money paid by a benefit fund that is not a savings benefit fund or is not a training fund, and they shall also not apply to money paid by a savings benefit fund that is charged tax under the provisions of section 87.

### **Deduction from interest**

125D. (a) In this section –

**"determining date"** – January 1, 2003;

**"benefit ceiling"** – the amount of NS 53,280 per year (*in 2008; in 2007: NS 51,840; in 2006: NS 52,08; in 2005: 50,640 – Tr.*);

**"interest"** – interest payable on a deposit with a banking corporation or on a savings program;

(b) If the income of an individual and the income of his spouse in a tax year did not exceed the benefit ceiling, then he is entitled to a deduction of NS 8,280 (*in 2008; in 2006 and 2007: NS 8,160; in 2005: NS 7,920 – Tr.*); (in this section: the permitted deduction) from his chargeable interest income, but not more than his total interest income; however, if his and his spouse's income in the tax year exceeded the benefit ceiling, then he shall be entitled to an adjusted deduction; for this purpose: **"adjusted deduction"** – the permitted deduction, after it was reduced by the amount by which the income of the individual and of his spouse exceeded the benefit ceiling.

(c) (1) If in a tax year an individual or his spouse had reached the mandatory retirement age, within its meaning in the Retirement Age Law 5764-2004 (in this subsection: mandatory retirement age) and if one of them had reached age 55 by the determining date, then he is entitled to a deduction of NS 8,160 (*in 2008; in 2006 and 2007: NS 8,040; in 2005: NS 7,800 – Tr.*) from his interest income, but not more than his total interest income;

(2) if in a tax year an individual and his spouse had reached the mandatory retirement age and if they had reached age 55 by the determining date, then – instead of the deduction said in paragraph (1) – he is entitled to a deduction of NS 12,360 (*in 2008; in 2006 and 2007: NS 12,000; in 2005: NS 11,700 – Tr.*) from his interest income, but not more than his total interest income;

### **Benefited interest**

125E. (a) In this section –

**"entitling interest"** – the lesser of the following amounts:

(1) the interest income of an individual and his spouse, as defined in section 125D(a) (in this section: interest);

(2) interest income in the amount of the differential between the amount stated in the definition of "entitling pension" in section 9A multiplied by twelve, and the chargeable income of the individual or of his spouse, whichever is greater; for this purpose: **"chargeable income"** – including income exempt under sections 9A and 9B, and exclusive of income from interest, income from the tax exempt rental of a dwelling unit, capital gains and land appreciation, as defined in the Real Estate Taxation Law.

(b) 35% of the entitling interest is tax exempt for the following:

(1) an individual who has reached the retirement age;

(2) an individual, if he or his spouse has reached the retirement age; and all if they have reached age 55 by the determining date.

### **Restriction**

125F. Deductions under section 125D and tax exemptions under section 125E shall be allowed for only one of the spouses.

### Companies tax

126. (a) The chargeable income of a body of persons shall be charged with a tax called "companies tax", at the rate of 25%.

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*Note: Section 77(a) of Amendment 147 provides as follows:*

77. (a) In respect of tax years 2006 to 2009 section 126(a) of the Ordinance . . . shall be read as if, instead of "25%", the following rates were prescribed:
- (1) for tax year 2006 – 31%;
  - (2) for tax year 2007 – 29%;
  - (3) for tax year 2008 – 27%;
  - (4) for tax year 2009 – 26%.
- (b) The Minister of Finance may, with approval by the Government and the Knesset Finance Committee, prescribe that in a tax year said in subsection (a) the tax rate prescribed in section 126(a) apply to one of the following years, on conditions and with adjustments that he shall prescribe. – Tr.

- 
- (b) In calculating the chargeable income under subsection (a), income from a distribution of profits or from dividends that stem from income produced or accrued in Israel, received directly or indirectly from another body of persons that is liable to companies tax, shall not be included, and income for which a special tax rate has been set also shall not be included.
- (c) Notwithstanding the provisions of subsection (a), companies tax at the rate of 25% shall be imposed on the chargeable income of a body of persons from dividends that stem from income produced or accrued abroad and also from dividends that originated abroad; however, if at the assessee company's request or on the basis of an agreement for the prevention of double taxation the foreign taxes imposed on those dividends and on the income out of which the dividends were distributed are to be taken into account, then the income from the dividend shall be taken in the amount of the grossed up dividend and on it companies tax shall be imposed at the rate prescribed in subsection (a); in this section –
- "grossed up dividend"** – the amount of dividend income, with the addition of tax paid on the income, out of which the dividend was distributed;
- "assessee company"** – a company that received dividends from another company in which it holds 25% or more of the means of control (hereafter in this section: the other company);
- "income out of which the dividend was distributed"** – including income that stems from a company that is at least 50% held directly by the other company;
- "means of control"** – as defined in section 88.
- (d) In calculating the tax that applies under subsection (c), credit shall be given in the amount of companies tax which the body of persons that distributes the dividend was charged on the income out of which the profits or the dividends said in subsection (a) were paid, and the total tax rate that applies under subsection (c) shall not exceed the rate determined in subsection (a).
- (e) The amount of credit said in subsection (d) and in Part Ten, Chapter Three shall not be greater than the tax that applies under subsection (c)

- and the provisions of section 205A shall not apply.
- (f) If a body of persons received a dividend and a loss was set off against the income from it, and if the body of persons thereafter distributed the dividend to its share holders, then – for the purposes of subsection (c) – it shall be deemed that companies tax at the rate of 25% was paid in respect of the dividend.

### **Tax alleviation on dividend income that stems from abroad**

126A. (a) In this section –

**"controlling member"** – as defined in section 3(i);

**"dividend income"** – of a company – the company's liable income from dividends the origin of which is abroad, which a foreign resident body of persons paid to it and which it received in Israel in tax year 2009, other than said income from dividends derived from income that – had it not been distributed to the company or to another body of persons in the same chain of companies, as defined in section 75B(a)(14), would be profits that were not paid as defined in section 75B(a)(12), and on condition that – if the company is a controlling member of the body of persons that pays the dividend – the following amounts be subtracted from the income:

- (1) the amount of loans extended by the company to the body of persons that pays the dividend or to its relative during the period from December 1, 2008, until December 31, 2010 (in this definition: the determining period) and that had not been repaid in the determining period;
- (2) the amount of guaranty provided by the company for the body of persons that pays the dividend or for its relative in respect of a loan taken by the body of persons during the determining period, on condition that the guaranty was exercised during the determining period;
- (3) the amount paid by the company during the determining period for the acquisition of securities of the body of persons that pays the dividend or of its relative;

**"relative"** – as defined in paragraph (3) of the definition of "relative" in section 88;

**"use in Israel"** – a use that is one of the following, other than a direct or indirect payment to an individual who is a controlling member of the company that receives the dividend:

- (1) payment to Israel residents for services provided in Israel or for work performed in Israel;
- (2) payment for the acquisition or rental of assets that will be used in Israel, and also payments to Israel residents for the acquisition or rental of assets; for this purpose, **"asset"** – other than securities, as defined in section 88;
- (3) payment for the improvement or maintenance of assets in Israel;
- (4) investment in research and development in Israel;
- (5) repayment of debts to Israel residents, and if the repayment is to a relative body of persons – on condition that that body of persons use the repaid money in Israel;
- (6) payment of interest, discount or linkage differentials on

debentures traded on an Exchange in Israel, and also acquisition by the company that receives the dividend of said debentures that had been issued by it;

- (7) making a deposit in Israel, with an Israel resident body of persons, for a period of at least one year (in this definition: the "**deposit period**") or acquisition of securities traded on an Exchange in Israel and holding them at least for a year (in this definition: the "**holding period**"); for this purpose –
  - (a) a security shall be treated as if it had been held during the entire holding period even if it was sold before the end of the said period, if another security traded on an Exchange in Israel was acquired with the full consideration for its sale and was held for the remainder of the holding period;
  - (b) if a certain amount was deposited as aforesaid in this paragraph for a period shorter than the deposit period and if securities in the same amount were acquired and held as aforesaid in this paragraph for a period shorter than the holding period, then it shall be deemed that the said amount was used in Israel in accordance with this paragraph, if the aggregate of the periods of the deposit and of holding is at least one year;
- (8) payment of a dividend to an Israel resident company, on condition that that company make use of it in Israel.
- (b) Notwithstanding the provisions under this Ordinance, at the company's request companies tax at the rate of 5% shall be imposed on a company's dividend income that was used in Israel during the year 2009 or within one year after the actual receipt of the dividend, on condition that the company that received the dividend is not a subsidiary, within its meaning in section 64, a family company within its meaning in section 64A or a transparent company, as defined in section 64A1.
- (c) The provisions of section 126 shall apply to the part of the dividend received by the company as said in subsection (b) and used in Israel.
- (d) Notwithstanding the provisions under this Ordinance, if the company requested that companies tax on its dividend income be imposed on it under this section, then a credit shall be granted against the said tax for the deduction of tax from the said income at the source, and no credit shall be given for foreign taxes that are not imposed directly, as defined in section 203(c).
- (e) The provisions of section 205A shall not apply to foreign taxes, as defined in section 199, that were paid on the dividend income that was charged companies tax under this section.
- (f) If a company, which requested that companies tax be imposed on it under this section, proved that it made use of any amount whatsoever in Israel during any of the periods said in subsection (b), then it is assumed that the use of that amount in Israel was out of the dividend income, even if the company received that income after it had made the said use.
- (g) For the purposes of subparagraph (b) in the definition of a "controlled foreign company" in section 74B(a)(1), income received by a foreign resident body of persons in tax year 2009 and distributed to an Israel



resident company as dividend in that same tax year shall not be taken into account, if the dividend income was charged companies tax under this section. "

127. and 128. – Repealed

#### **Exemption of certain cooperative societies from companies tax**

129. (a) If a cooperative society does business only with its members or if its business with nonmembers is inconsiderable or of an incidental nature, and if most of its said business is the marketing or processing of its members' agricultural produce, then it shall be liable to tax at the rate of 20% on that part of its chargeable income which is derived from one of the following:
- (1) the marketing or processing of its members' agricultural produce;
  - (2) the supply of agricultural inputs and equipment to its members;
  - (3) its income from agriculture, on condition that more than 90% of its members' income from agriculture is derived from the marketing of farm products through it;
- the amount, to which the said reduced tax rate applies, shall not exceed 3% of its turnover in that year, but the Minister of Finance may, with approval by the Knesset Finance Committee, increase the said rate by Order.
- (b) If a cooperative society distributed or repaid to its members, directly or indirectly, profits on which it paid reduced tax under the provisions of subsection (a), then it shall be liable to pay the amount of tax at the aforesaid reduced rate within 30 days after the day of the distribution or repayment.
- (c) In this section –
- (1) **"cooperative society"** – a cooperative society whose members are cooperative societies or individuals and the greater part of the income of each of 51% of its members is from agriculture, on condition that its members number no fewer than –
    - (a) 40 members, if only individuals are members;
    - (b) five cooperative societies with a total said membership of at least 200, if all members are cooperative societies.
    - (c) 30 members and five cooperative societies, if the members are both individuals and cooperative societies;
  - (2) **"member"** includes a candidate for membership, for whom a year of candidacy has not ended.

129A. Repealed

#### **Income derived by a benefit fund from real estate and foreign securities**

- 129B. (a) Notwithstanding the provisions of section 126, the chargeable income of a benefit fund from a business of renting buildings built by itself or through others, construction of which began in or after tax year 1991, shall be liable to tax at the rate of 20%.
- (b), (b1), (c) and (d) Repealed

#### **Income of a trust fund**

- 129C. (a) Notwithstanding the provisions of section 126 –
- (1) the income and profits of an exempt trust fund are exempt of tax;
  - (2) those tax rates shall apply to the chargeable income of a chargeable trust fund, which would have applied to the said

profits or income, if they had been received by an individual, for whom the income is not income from business or occupation, unless there is a different specific provision; if no special tax rate was determined for the income, then the income shall be charged tax at the maximum rate prescribed in section 121.

- (3) repealed
  - (4) the deduction of interest and linkage differential expenses shall not be allowed in the calculation of a trust fund's income and profits;
  - (5) in respect of the determination of the chargeable income of chargeable trust funds, the Minister of Finance may, with approval by the Knesset Finance Committee, prescribe each of the following:
    - (a) repealed
    - (b) in this section, "**trust fund**", "**exempt trust fund**" and "**chargeable trust fund**" – as defined in section 88;
    - (c) special provisions on tax exemptions or special tax rates for certain types of income of chargeable trust funds that are intended for unit holders who are foreign residents, according to the tax rate that would apply to that income, if it were received by a foreign citizen;
    - (d) the method for calculating linkage or the inflationary amount according to the fund's investments or assets.
- (b) In this section, "**business unit**", "**trust fund**", "**exempt trust fund**", "**chargeable trust fund**" and "**mixed trust fund**" – as defined in section 88.

#### **Special provisions on setting off losses in a chargeable trust fund**

129D. A capital loss from foreign securities, which a chargeable trust fund suffered until December 31, 2002 (in this section: the accrued loss) shall be brought forward to the coming years, one after the other, in order to set it off against capital gains from the sale of foreign securities, on condition that a loss greater than 40% of the accrued loss shall not be allowed to be set off in each of the tax years 2003 and 2004; however, if less than 40% of the accrued loss was set off in tax year 2003, then the differential of the accrued loss shall also be allowed to be set off in tax year 2004; for this purpose: "**differential of the accrued loss**" – an amount equal to 40% of the accrued loss, less the amount of accrued loss set off in tax year 2003.

#### **Powers of the Minister of Finance on the taxation of savings programs**

- 129E. (a) The Minister of Finance may, with approval by the Knesset Finance Committee, set the rate of tax to be paid by banking corporations and insurance companies on certain income from money deposited in savings programs and which under the terms of the program is referred to the saver, provided that the tax rate so set not be greater than the differential between the tax rate that would have applied to that income, had it been received by an individual for whom the income is not income from business or occupation, and 15%; he may also set a limit for the deduction of expenses, allocations and set-offs of losses against that income, all on conditions that he shall prescribe.
- (b) The tax said in this section shall be deducted from the income which under the conditions of the program is referred to the saver, and the

- banking corporation or the insurance company, as the case may be, shall not be entitled to any deduction, credit or set off in respect of that tax.
- (c) Notwithstanding the provision of any statute, a person who saves in a savings program said in this section is not entitled to any tax refund or credit in respect of the tax paid by the banking corporation or insurance company, as the case may be.

## PART EIGHT: RETURNS, NOTICES AND INFORMATION

### CHAPTER ONE: PREPARATION AND SUBMISSION OF RETURNS

#### **Power to require keeping of accounts**

130. (a) (1) For purposes of the assessment, the Director may – either generally or in respect of certain categories of assessee – direct that account books be kept in respect of income derived from a business or vocation, and in those provisions he may prescribe rules on the method of keeping the account books, including the assessee's duty to require a person with whom he maintains any business relationship to deliver his personal particulars to the assessee and to identify himself; the directions shall go into effect three months after their publication in Reshumot, or at a later date prescribed by the Director, and he may do so either generally or for a certain category of assessee; however, the abrogation of directions or the issue of alleviating directions may take effect earlier than three months after the day of their publication.
- (2) On an assessee's application, the Director may – on conditions and for a period as he may prescribe – approve a change of the provisions applicable to him; if the Director rejects the application, then the assessee may, within three months, lodge objection with a committee established under section 146 (hereafter: books acceptability committee).
- (3) The Director may, on application of an assessee who is the owner of a small business within its meaning in section 145A, and after receiving the opinion of a committee appointed by him for that purpose, exempt that assessee from the duty of keeping books if he meets criteria set by the Director in rules published in Reshumot in respect of a physical or mental condition or illiteracy, because of which the assessee is unable to fulfill the duty of keeping books; notice of the composition of a committee appointed for the purposes of this paragraph shall be published in Reshumot.
- (4) For the implementation of this Ordinance, the Director may order that books be kept in respect of the income, expenses, intakes and payments of a public institution defined in section 9(2), of a professional organization defined in section 9(2a), or of a nonprofit institution defined in the Value Added Tax Law 5736-1975 (hereafter: institution), and in those instructions he may also prescribe rules on the bookkeeping method, including the

institution's obligation to require anyone, with whom it maintains any connection whatsoever, to give the institution his personal particulars and to identify himself; the Director may order as aforesaid in general or for a certain category of institutions, and the instructions shall go into effect three months after they were published or at a later time prescribed by the Director; the cancellation of aforesaid instructions or the prescription of alleviating conditions may go into effect earlier than three months after the day of their publication.

- (5) For the implementation of this Ordinance the Director may order a management company, as defined in the Control of Benefit Funds Law, to keep books in respect of the moneys deposited in a benefit fund under its management.
- (b) When directions under subsection (a) have been issued, the Assessing Officer may refuse to accept accounts not based on account books kept in accordance with those directions, if deviations from those directions or the defects found in the account books are material to the ascertainment of an assessee's income, and in the case of an institution – if they are material.
- (c) If the Assessing Officer refused to accept accounts as said in subsection (b), or rejected account books because aforesaid defects were found in them, he shall send a notice to that effect to the assessee or to the institution, specifying the grounds for his decision.
- (c1) Decisions by an Assessing Officer under subsections (b) and (c) in respect of an institution require the Director's approval.
- (d) (1) Objection to a decision by the Assessing Officer under subsection (c) may be lodged with the books acceptability committee within 30 days after the notification was received.  
(2) The period from the day on which objection under paragraph (1) was lodged until the committee's decision is received shall not be included in the periods said in sections 145 and 152(c).
- (e) If an objection was lodged as said in subsection (d) and was dismissed, then the account books shall be deemed unacceptable for purposes of an appeal against the assessment.
- (f) An Order under section 152(b), based on the non-acceptance or rejection of books, as said in subsection (b) or (c), shall not be issued before notice thereof under subsection (c) has been sent to the assessee, before the time for lodging objection to the Assessing Officer's decision has elapsed and – if objection was lodged – before the books acceptability committee gave its decision.
- (g) Lodging an objection under this section does not take the place of a contestation under section 150.
- (h) If no objection was lodged under subsection (d), then the Assessing Officer's decision under subsection (c) may be appealed before the District Court, together with the appeal under section 153.
- (i) The provisions of subsections (c) to (f) shall also apply to a decision by the Director under section 147.
- (j) Nothing in directions issued under subsection (a) shall be construed as requiring any person to disclose secret information given him in the exercise of his vocation.
- (k) (1) If directions were given under subsection (a) and one of the following was done, then the books shall be deemed unacceptable, unless the Assessing Officer is satisfied that there was sufficient reason for the said act:

- (a) use of an invoice issued without a sale or provision of a service, or the amount stated in it does not reflect the price of the sale or the price of the provided service, as the case may be; for this purpose: **"invoice"** – within its meaning in the instructions issued under this section and also a tax invoice, within its meaning in the Value Added Tax Law;
  - (b) income of a substantive amount was not included in a return submitted under section 131;
  - (c) in a return submitted under section 131 a private expenditure was deducted, or an expense without any purchase or acquired service, or the amount of expense deducted as aforesaid does not reflect the price of the purchase or the price of the service received, all in a manner that reduced the chargeable income or increased the loss by a substantive amount.
- (2) If a person disputes a decision made under paragraph (1), then he may request – within thirty days after he received the decision – that the Assessing Officer reconsider and change it; if the Assessing Officer rejected the request to change all or part of his decision, then appeal may be lodged against the decision, as if it were an Order under section 152(b), provided that the date for lodging the appeal be within sixty days after his decision was handed down, or together with the appeal against the assessments made for that tax year; for purposes of this paragraph: **"Assessing Officer"** – exclusive of an Assistant Assessing Officer and of a Chief Collector.

#### **Keeping books in a foreign currency and determining income accordingly**

- 130A. (a) A diamond merchant may keep the account books, which under section 130 he is required to keep for his diamond business, in terms of a foreign currency, in accordance with rules to be prescribed by the Minister of Finance with approval by the Knesset Finance Committee, which shall include the conditions on which a person who chose to keep books as aforesaid may retract that choice; for this purpose:  
**"diamond merchant"** – a person whose business, or part of whose business is the processing of or the trade in or the brokering of diamonds, as well as a controlling member, as defined in section 32(9), of a company the business of which is as aforesaid;  
**"diamond business"** – the processing of diamonds, trading in diamonds or brokering them, and for a diamond merchant who is a controlling member of a company that is a diamond merchant – any act that affects the property, the obligations or the capital which he invested in or received from the said company, or from a company which is a diamond merchant and which is under his control.
- (b) If an assessee has a permanent enterprise abroad, not in an area as defined in section 3A, then he shall keep the account books, which under section 130 he is obligated to keep in respect of his income from the said enterprise, in terms of foreign currency, in accordance with rules prescribed by the Minister of Finance with approval by the Knesset Finance Committee.
  - (c) In addition to the provisions of subsections (a) and (b), those specified below may keep the account books they are obligated to keep under section 130 in foreign currency, according to rules prescribed by the Minister of Finance with approval by the Knesset Finance Committee,

which shall include the conditions on which a person who chose to keep books as aforesaid may retract that choice:

- (1) a partnership, if all its members are foreign residents and all their investments and all the loans which they extended to the partnership are in foreign currency, and if the Director approved it for purposes of this section;
  - (2) a foreign invested company, as defined in section 53H of the Encouragement of Capital Investments Law 5719-1959;
  - (3) a company, at least 90% of whose income is from the operation of ships or aircraft in international transportation.
- (d) In respect of a diamond merchant who chose to keep books as specified in subsection (a), of an assessee who has a permanent enterprise abroad as said in subsection (b), of a company or a partnership which chose to keep books as said in subsection (c), the Minister of Finance may, with approval by the Knesset Finance Committee, prescribe rules for the determination and calculation of its chargeable income and, in particular, of expenses, income and depreciation, and rules on tax liability and tax payments and on linkage differentials and interest thereon, all taking into account that books are kept in a foreign currency as aforesaid; rules under this subsection shall apply notwithstanding anything provided in any statute.

#### **Who must make a return**

131. (a) The following shall submit a return:

- (1) an individual Israel resident who reached age 18 by the beginning of the tax year; a registered spouse may refrain from including the income of his spouse, if the spouse submitted a separate return of his income or if the registered spouse attached to his return a declaration signed by his spouse that he will report his income separately;
- (2) a spouse who is not a registered spouse who declared as said in paragraph (1) that he will make a separate return of his income;
- (3) an individual Israel resident who had not yet reached age 18 at the beginning of the tax year, if in that year he had chargeable income in an amount not less than NS 59,570 in tax year 2007, or some other amount set by the Minister of Finance for this purpose;
- (4) an individual foreign resident who had chargeable income in the tax year;
- (5) a body of persons which had income in the tax year;
- (5a) a person who during the tax year sold a real estate right or performed an association act, as defined in the Land Appreciation Tax Law, which is not exempt of tax under that Law, and who did not pay appreciation tax at the highest rate applicable under the Real Estate Taxation Law on the real appreciation that arose out of the sale or act, as the case may be;
- (5b) in respect of trusteeships, each of the following:
  - (1) a trustee in a trusteeship of Israel residents or a trustee in a trusteeship under a will that under section 75L(c)(1) is deemed an Israel resident, provided the creator did not elect to be assessable and chargeable under the provisions of sections 75G(h) or 75L(e) and that no representative creator or representative beneficiary was chosen under the provisions of section 75F1, as the case

- may be;
  - (2) a trustee who had income or assets in Israel, whether or not he is an Israel resident;
  - (3) a creator or a beneficiary, as the case may be, who elected to be assessable and chargeable under the provisions of section 75G(g) or (h), or under section 75L(e) or (f);
  - (4) a representative creator or a representative beneficiary, as the case may be, who elected to be assessable and chargeable under the provisions of section 75F1;
- every term in this paragraph shall have the meaning it has in section 75C or in section 75F1, as the case may be;
- (5c) a controlling member, as defined in section 75B, of a foreign occupational company, as defined in section 5, or in a controlled foreign company, as defined in section 75B;
  - (5d) a person who performed an act, which under subsection (g) is designated as tax planning that requires reporting;
  - (6) every person of whom the Assessing Officer so demanded, even if he does not have to submit a return under paragraphs (1) to (5).
- (a1) If a return was submitted that includes the income of both spouses, then each of the spouses shall sign it to attest the correctness of what is declared about his part.
  - (b) The return shall specify the income which the person who submits it had in the year to which it relates, as well as all the particulars required for purposes of this Ordinance in respect of that income, and to it shall be attached –
    - (1) a balance sheet and profit and loss account – if the return is based on a complete set of double-entry accounts;
    - (2) particulars of the calculation on which the declared income is based – if it is based on a set of accounts other than said in paragraph (1);
    - (3) a detailed estimate of turnover, expenses and percentage of profit, or documents or other data on which the declared income is based – if the return is not based on account books.
  - (b1) The return shall specify every act, which under subsection (g) is said to constitute tax planning that must be reported;
  - (b2)
    - (1) If an individual is under obligation to submit a return under subsection (a)(1) to (4), (5a), (5c), (5d) and (6), and if he has income under section 2(1), (2) or (8), then he shall submit the return according to the provisions of this section in an online manner, as the Director shall provide, together with a declaration on a form prescribed by the Director, according to which the particulars he gave in the return are correct and complete, as well as a printout of the said return, signed by him (hereafter: online independent return).
    - (2) If an individual said in subparagraph (1) did not submit an online independent return, then for the purposes of the provisions of this Ordinance he shall be deemed a person who did not submit a return.
    - (3) The provisions of this Ordinance about a return under section 131 shall apply to the online independent return, unless there is an explicit different provision.
    - (4) Notwithstanding the provisions of paragraph (1), the Minister of Finance may – with approval by the Knesset Finance Committee

- designate categories of individuals who will be exempt of the obligation to submit online independent returns according to criteria of economic status, amount of income and medical condition, and also because of other special reasons that will be prescribed in regulations, on condition that a said exemption not apply to individuals who submitted claims for grants under the Law For Increased Labor Force Participation and the Reduction of Social Gaps (Negative Income Tax) 5768-2007.
- (c) A return under subsection (a)(5), other than the return of a partnership, shall be certified by an auditor, within the meaning of the term in the Auditors Law 5715-1955, and adjusted by him for purposes of the tax; however, for a body of persons which is a cooperative society affiliated to an audit union the return may be certified and adjusted for tax purposes by an audit union official duly registered with the Registrar of Cooperative Societies.
- (c1) (1) The trustee, creator, representative creator, beneficiary or representative beneficiary, as the case may be, shall specify all the following in a report as said in subsection (a)(5b)(1), (3) or (4):
  - (a) the particulars of all creators and all beneficiaries, particulars of the trustee and of the protector of the trusteeship, if there is one, and the residential status of each of these;
  - (b) particulars of the assets vested in the trustee or from which income was vested in the trustee, and also particulars of the income from these assets that was vested in the trustee as aforesaid, and the date when the asset or the income was vested as aforesaid;
  - (c) particulars of the assets that were distributed and particulars of the income that was distributed, and also the date of the distribution.
- (2) The trustee shall specify all the following in a report said in subsection (a)(5b)(2):
  - (a) the particulars of all creators and all beneficiaries, particulars of the trustee and of the protector of the trusteeship, if there is one, and the residential status of each of these;
  - (b) particulars of the assets in Israel that were vested in the trustee or from which income was vested in the trustee, and also particulars of the income that was vested in the trustee from aforesaid assets, and when the asset or the income was vested as aforesaid;
  - (c) particulars of the assets in Israel that were distributed and particulars of income from assets in Israel that was distributed, and also the date of the distribution.
- (3) In this subsection, "**particulars of the assets**" – including the original cost, the balance of the original cost and the day of the acquisition, as defined in section 88, the value of the acquisition and the day of acquisition within their meaning in Chapter Three of the Real Estate Taxation Law, and the balance of the acquisition value, as defined in section 47 of the said Law, as the case may be.
- (c2) To a return under subsection (a)(5c) by the controlling member of a foreign occupational company shall be attached an audited financial



report of the foreign occupational company in accordance with bookkeeping principles accepted in Israel, and – if it is a company that reports to or is assessed in a reciprocating state, within its meaning in section 196 – the report drawn up for tax purposes in accordance with the tax laws of that state.

- (d) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe rules that obligate a partnership to file a return certified by an auditor and adjusted by him for tax purposes.
- (e) The Minister of Finance may prescribe, by Order, the form of the certification and of the adjustment said in subsection (c).
- (f) If a person did not attach the documents specified in subsection (b) to the return, or if the return submitted by him was not certified and adjusted as provided in subsection (c), then – for the purposes of sections 145(b) and 158A(c) – he shall be treated as if he had not submitted a return, unless he submits the said documents on another date permitted him by the Assessing Officer.
- (g) The Minister of Finance may, with approval by the Knesset Finance Committee, designate acts that constitute tax planning that must be reported, how they are to be reported and to what extent; in this subsection, "**act**" – includes a transaction and a sale, including those to which the provisions of the Real Estate Taxation Law apply.

#### **Additional returns**

131A. The Minister of Finance may, by regulations, prescribe additional returns which a body of persons bound to make a return under section 131(a)(5) or an Israel resident bound to make a return under section 131(a)(5b) shall attach to the return under that section.

#### **Report from auditor or audit union official**

131B. An Assessing Officer may, if he found reasonable cause for doing so, demand in writing from the auditor or from the audit union official who under section 131 certified a balance sheet or adjusted and certified an adjustment account for a body of persons, that he deliver to him a report on the extent and findings of the audit carried out by him in respect of the particulars stated in the Assessing Officer's aforesaid demand; in this section –

- (1) "**certified a balance sheet**" –
  - (a) in respect of a company other than a cooperative society affiliated to an audit union – the preparation of a report said in section 109 of the Companies Ordinance;
  - (b) in respect of a cooperative society affiliated to an audit union – the performance of an audit under section 20 of the Cooperative Societies Ordinance;
- (2) "**Assessing Officer**" – other than an Assistant Assessing Officer and a Chief Collector;
- (3) "**audit union official**" – as said in section 131.

#### **Date for submission**

132. (a) A return under section 131 shall be delivered to the Assessing Officer not later than April 30 of each year.
- (b) Notwithstanding the provision of subsection (a) –
- (1) if a person's return is based on a complete set of double entry accounts, then he shall deliver the return under that subsection not later than May 31 of each year;
  - (1a) if an individual must submit an online independent return, then he shall submit it until May 31 after the tax year in respect of which

- the return is submitted;
- (2) if a special assessment period was set for a person, then he shall deliver the said return not later than five months after the day on which that special assessment period ended.

#### **Deferment**

133. The Assessing Officer may, if it was proved to his satisfaction that there is sufficient reason for doing so, defer submission of a return under section 132(a) or (b), all as the case may be, to a date which he shall set, on condition that a person who obtains an aforesaid deferment submit, on the date stated in section 132(a) or (b), as the case may be, an estimated return of the said income, drawn up to the best of his ability to estimate.

#### **Notification of beginning or change of occupation**

134. If, in a particular tax year, a person opens a business, begins to engage in a vocation or begins to carry on his business or vocation in an additional or in a different place, or if he changes the type of his business or vocation, then he shall – no later than on the date of the said beginning or change – so inform in writing the Assessing Officer, in whose area of jurisdiction the business is located or the vocation is exercised.

#### **Power to exempt of filing of return**

- 134A. The Minister of Finance may, with approval by the Knesset Finance Committee, exempt – conditionally or unconditionally – the following from the obligation to file a return:
- (1) a person whose income is mainly work income, pension, or income on which he paid tax under section 122;
  - (2) a person whose income is not derived from employment, business or vocation, and does not exceed an amount three times the amount of credit points under sections 34 and 36;
  - (3) a foreign resident;
  - (4) a person who received income from which tax was lawfully deducted at the source or to which exemption from tax applies, and who – if not for that income – would be exempt of the obligation to submit a return;
  - (5) a trustee, whether he is an Israel resident or not, who in Israel had only income that is tax exempt or from which the full amount of lawful tax was deducted, or assets the income of which is exempt of tax.

#### **Exemption from return**

- 134B. Notwithstanding the provisions of section 131, an individual who became an Israel resident for the first time or a veteran returning resident, as said in section 14(a), shall not have to submit a return as said in section 131 in respect of all his income that was produced or accrued abroad or that stems from assets abroad during ten years after the date on which he became an Israel resident as aforesaid; the provisions of this section shall not apply to income, in respect of which the individual requested – under the provisions of subsection (a) of section 14 – that the provisions of the said subsection not apply, and in respect of income that stems from an asset that the individual received exempt of tax under section 97(a)(5) on or after January 1, 2007.

## **CHAPTER TWO: POWER TO OBTAIN INFORMATION**

**Power to demand returns, information, account books etc.**

135. In order to obtain complete information about a person's income –

- (1) (a) the Assessing Officer may demand from him, by written notice, that he deliver to him any return specified in that notice, including a return of the capital and assets of that person or of his spouse and of their children for whom they are entitled to credit points or pension points, or of assets for which he serves as trustee of another person; however, that person may refrain from including the capital and assets of his spouse in the return if he attaches to it a declaration signed by that spouse that he will submit a separate return of his capital and assets; if such a declaration was submitted, then the return shall be submitted when the spouse must submit the said return; every return under this paragraph shall be submitted to the Assessing Officer on the date specified in the notice, but in respect of a capital declaration the date shall not be set earlier than 120 days after the date to which the capital declaration is to relate or after the date of the demand, whichever is later; the Assessing Officer may also demand that the person appear before him, in person or by a representative, and that he deliver to him all the particulars required by the Assessing Officer in order to ascertain his income and that he produce for examination books, documents, accounts and returns which the Assessing Officer deems necessary; however, the Assessing Officer – other than an Assistant Assessing Officer or a Chief Collector – may demand that he appear in person, either with or without his representative, as that person wishes;
- (b) Notwithstanding the provisions of subparagraph (a), an individual who became an Israel resident for the first time or a veteran returning resident, as said in section 14(a), shall not have to submit a return of his capital and assets abroad during ten years after the date on which he became an Israel resident as aforesaid; the provisions of this subparagraph shall not apply to capital and assets, if the individual requested under the provisions of subsection (a) of section 14 – in respect of all or part of the income that stems from them – that the provisions of the said subsection not apply to it, and not to any assets the individual received exempt of tax under section 97(a)(5) on or after January 1, 2007.
- (2) the Assessing Officer, or another officer authorized by him for this purpose in writing, may enter any place in which a business or a vocation is carried on, and examine stock in trade, the cash box, machinery, books, accounts, vouchers, records and other documents that relate to that business or vocation and demand explanations in connection with them, and he may also demand that the owner of the business or the practitioner of the vocation or his responsible clerk show him where aforesaid books, accounts and documents are, enter the place where they are located, examine them and demand explanations if that appears necessary in order to ensure compliance with the provisions of the Ordinance or to prevent an evasion of compliance with those provisions;
- (3) the Assessing Officer or a person authorized by him for this purpose in writing may, while making an examination under paragraphs (1) or (2), seize books, accounts, vouchers, records and other documents that

relate to that business or vocation, if he is convinced that it is necessary to do so in order to ensure implementation of this Ordinance or to prevent evasion of compliance with its provisions; however, the thing seized –

- (a) shall be removed from the place where it was seized only by Order of the Assessing Officer, and for this purpose: "**Assessing Officer**" – other than an Assistant Assessing Officer or a Chief Collector;
  - (b) shall be returned within three months after the date of the seizure, if a criminal action for an offense against this Ordinance was not brought before then;
- (4) the Assessing Officer may summon any person who has business relations with the assessee and who he believes can testify on his income, to appear before him and he may question him under oath or not under oath and demand of the said person that he give him documents that relate to that income; however, a clerk or authorized agent or employee of the assessee or any other person employed in his affairs on a basis of personal trust may only be questioned at the assessee's demand, and the Assessing Officer shall not, on his own initiative, interrogate the assessee's spouse, children or parents.

#### **Power to demand information about suppliers and customers**

- 135A.(a) If a person owns a business or practices a vocation, then he must – if the Assessing Officer so demanded of him – deliver to the Assessing Officer information and documents about his business relations with his suppliers, customers or other persons with whom he has business relations, even though that information and those documents are not required to ascertain his income; however, if he notified the Assessing Officer within 15 days after the day on which he received the demand that it involves much administrative work, then he must enable the Assessing Officer to collect the said information and documents himself.
- (b) The provisions of subsection (a) shall not obligate an advocate, physician or psychologist to disclose any information or document which he is bound to keep secret under any statute.

#### **Power to demand a return about employees from employer**

136. (a) Every employer must, if required to do so by a notice from the Assessing Officer and within the time set by the notice, prepare and deliver a return for any year, which includes the names and places of residence of persons employed by him and the payments and allowances made to them for their employment by him; the provisions of this Ordinance about failure to deliver returns or particulars demanded by an Assessing Officer apply to the said return, but an employer shall not be liable to a penalty for omitting from the return the name or place of residence of any person employed by him and not employed in any other employment, if the Assessing Officer finds, on inquiry, that that person has no chargeable income.
- (b) If the employer is a body of persons, then the manager or other principal officer shall be deemed the employer for purposes of this Chapter, and every company director or person engaged in a company's management shall be deemed to be employed by it.

#### **Power to demand return of income received for or paid to another person**

137. When a person – no matter in what capacity – receives profits or income to which this Ordinance applies and which belong to a certain person, or if he pays said profits or income to a certain person or to his order, then the Assessing Officer may give that person notice, demanding that he submit – within the time set in it, which shall not be less than 30 days after the day of its service – a return that shall contain true and correct disclosure of all those profits and income, and the name and address of that certain person.

**Power to demand return from a house occupant**

138. The Assessing Officer may give any person who occupies any house property, land or industrial building, a written notice demanding that within a reasonable time he submit a return that includes the name and address of the owner of that house property, land or industrial building, and a true and correct statement of the rent paid and other consideration given for it.

**Power to demand return about lodgers and tenants**

139. The Assessing Officer may give a person written notice, demanding that he submit – within the time set in it, which shall not be less than 30 days after the day of its service – a return that includes the name of every lodger or tenant who resides in his house, hotel or institution on the date of the notice and who resided there during all of the preceding three months, except for temporary absences.

**Power to demand official information**

140. Notwithstanding the provisions of any other statute, the Assessing Officer may require any employee of a public body to supply any particular that is needed for purposes of this Ordinance, which that employee has or knows, but no aforesaid employee shall, by virtue of this section, be obligated to disclose any particular that he is required to keep secret in accordance with the Statistics Ordinance 1947, the Postal Bank Law 5711-1951, or the Bank of Israel Law 5714-1953; an employee, required as aforesaid, shall supply the particulars within 30 days after the day of the demand or at another time stated in the demand; for the purposes of this section: "**public body**" – the State, any body subject to audit by the State Comptroller, and any other body which the Minister of Finance, with approval by the Knesset Finance Committee, declared a public body.

**Obtaining information from the National Insurance Institute**

- 140A. (a) Without derogating from the provisions of section 140 and notwithstanding the provisions of any statute, the Director is entitled to receive from the National Insurance Institute any information designated under subsection (b), which reached the National Insurance Institute in the performance of its duties and which the Director requires for the exercise of his responsibilities under any statute.
- (b) The Minister of Finance shall – with the consent of the Minister of Justice, in consultation with the Minister of Welfare and with approval by the Knesset Finance Committee – designate the categories of information, which the Director is entitled to receive under the provisions of subsection (a).

**Duty to notify of agreement for net payment**

141. If a person undertook in an agreement to pay to another work income of not less than a certain amount after deduction of tax under section 164, then both the payor and the recipient must give notice thereof to the Director within 30

days after the day on which the agreement was made, specifying in it the particulars of the agreement and every other particular that relates to it and that the Director shall demand, and if the agreement was in writing, a copy of it shall be attached to the notice.

### **CHAPTER THREE: MISCELLANEOUS**

#### **Assessing Officer may demand supplementary returns**

142. The Assessing Officer may give a person written notice, at any time and as often as he deems necessary, in which he shall be required to furnish – within a reasonable time set in the notice – more complete or additional returns on any matter on which a return is required or prescribed by this Ordinance.

#### **Preparation of return by another person**

143. If a person helps another person, against payment, to prepare a return, notification, form or other document for a purpose of this Ordinance, then he shall declare on that document that he helped to prepare it.

#### **Returns deemed to be delivered by due authority**

144. (a) A return, statement or form purporting to be delivered under this Ordinance by or in the name of a certain person, shall for all purposes be deemed to have been given by that person or with his permission, unless the contrary is proven, and every person who signs any return, statement or form shall be deemed to be cognizant of all matters in it.
- (b) If a registered spouse alone signed any return, statement or form, then he shall be deemed to hold a power of attorney from his spouse to sign in his name.

#### **Service on the Assessing Officer of copy of an action**

- 144A. If an assessee brings action in any Court, based on the amount of his income from any source, then he shall deliver a copy thereof to the Assessing Officer with whom his file is kept; if he has no file, he shall deliver the copy to the Income Tax Director.

## **PART NINE: ASSESSMENT OF INCOME, TAXATION DECISIONS, CONTESTATIONS AND APPEALS**

### **CHAPTER ONE: ASSESSMENT**

#### **Power to assess**

145. (a) (1) When a person has delivered a return under section 131, the return shall be deemed a determination of income by that person (hereafter: self assessment), and the Assessing Officer shall send him notice of the amount of tax due from him under the return; a said notice shall be treated like a notice of assessment under section 149.
- (2) The Assessing Officer may, within three years after the end of the tax year in which the return was delivered to him – and, with the Director's approval, within four years after the end of the said tax year – examine it and do one of the following:

- (a) approve the self assessment;
- (b) determine to the best of his judgment the amount of the person's income, of the deductions, set-offs and exemptions allowable from it under any statute, and the tax to which he is liable, if he has reasonable grounds for believing that the return is not correct; an assessment under this subparagraph may be made according to an agreement concluded with the assessee.
- (2a) Within one year after the end of the period said in paragraph (2), the Assessing Officer may – at his initiative or on application by the assessee – correct any error made in the calculation of deductions, credits or exemptions in an assessment under paragraph (2)(b), if he is satisfied that the case is one of a computational error.
- (3) Notwithstanding the provisions of paragraph (1), the Assessing Officer may – within six months after receipt of the return that constitutes a self assessment – do as specified hereafter and the return shall continue to be deemed a self assessment even after the Assessing Officer did as said here:
  - (a) correct a computational error made in the return;
  - (b) apply the provisions of any statute applicable to the assessee, in connection with the obligation to keep books for any tax year or part thereof, if he did not keep them or only kept them during part of the period during which he was under obligation to keep them, or if he did not base his return on his account books;
  - (c) apply the provisions of any statute applicable to the assessee, after a final determination was made that his books are not acceptable; in this context, "**final determination**" – a determination against which there is no further right of objection or appeal.
- (b) If a person did not deliver a return and the Assessing Officer believes that that person must pay tax, then he may determine the amount of that person's chargeable income to the best of his judgment and assess him accordingly, but that assessment shall not affect any other responsibility of that person for failing or neglecting to deliver a return.

#### **Power to assess in special cases**

145A. The Assessing Officer may determine – to the best of his judgment – the chargeable income of an assessee who is the owner of a small business of a category designated by the Minister of Finance and who kept his records as required by the Director's directions under section 130, if the Assessing Officer concludes that the assessee's income according to his records is not reasonable, but the assessee's books shall not for that reason be deemed unacceptable.

#### **Power to assess diamond merchants**

145A1. Without derogating from his other powers under this Ordinance, the Assessing Officer may determine – to the best of his judgment – the amount of chargeable income of an assessee who is a diamond merchant, within its meaning in section 130A, and who kept his records as required by the Director's directions under section 130, if the Assessing Officer concludes that the diamond merchant's income according to his records is not reasonable; however, before he makes an aforesaid assessment the

Assessing Officer shall inform the diamond merchant of his decision to assess him as aforesaid, and he shall enable the diamond merchant to object before the books acceptability committee on one of the following grounds:

- (1) that the business results are reasonable;
- (2) that the extent to which he used concessions from the Director's directions, such as were prescribed by the Minister of Finance, did not affect the business results materially.

**Partial assessment in respect of tax planning that must be reported**

- 145A2. (a) If, in a return under section 131, a person reported an act designated under subsection (g) of the said section as tax planning that must be reported, then the Assessing Officer may – in addition to the provisions of section 145 – determine that person's income in connection with that act by a partial assessment to the best of his judgment, while ignoring the tax planning that must be reported, and he may also determine the deductions, set offs and exemptions allowed against the income under any statute, as well as the tax which that person must pay, on condition that until that time he had not assessed him for that tax year under section 145.
- (b) An assessment under this section may be made by agreement with the assessee.
  - (c) A partial assessment under this section shall for all intents and purposes be treated like an assessment said in section 145(a), also for the purposes of sections 147, 150, 152, 153 or 158A, but the partial assessment shall not infringe the powers of the Assessing Officer or the rights of the assessee in connection with the assessment of the rest of the assessee's income according to the provisions of this Chapter.
  - (d) If in respect of the same tax year a partial assessment and an assessment of all the assessee's income were made – including an assessment made by agreement, by order or by a judgment, then the Assessing Officer shall determine how they affect each other and he shall draw up the necessary adjustments.

**Rejection of books because intakes were not entered or no cash register was kept**

- 145B. (a) (1) If an assessee records his intakes on a cash register tape, on receipt vouchers, on invoices, in a daily receipts diary or by any other documentation that he must keep under the Director's directions by virtue of section 130, and if he did not record in them an intake which he should have recorded in accordance with those directions, then his books shall be deemed unacceptable, unless the Assessing Officer is satisfied that there was reasonable cause for the default; if a person disagrees with a decision made under this paragraph, then within thirty days after he received the decision he may request the Assessing Officer, as defined in section 130(k)(2), to reconsider and change it; if the Assessing Officer rejects the request to change all or part of the decision, then his decision may be appealed, as if it were an Order under section 152(b), provided that the date for lodging the appeal be within sixty days after his decision was handed down;
- (2) (a) If an assessee does not record an intake which he must record as said in paragraph (1) twice or more often in one tax year or in twelve consecutive months in two tax years, including at least once after the Assessing Officer



cautioned him in writing, then his books shall also be assumed to be unacceptable in the two tax years that preceded the year in which he twice did not record an intake as aforesaid, or also in the tax year that preceded the first year within the twelve months in which he twice did not record an intake as aforesaid, even if his returns were accepted and assessments were made according to them, unless the Assessing Officer was convinced that there was sufficient reason for the failure to record; an amended assessment for the said tax years may be made by the Assessing Officer in consequence of the failure to record intakes, and it shall be treated like an Order under section 152(b);

- (b) a decision by the Assessing Officer not to accept the reason for not recording as sufficient may be appealed, as if it were an Order under section 152(b), on condition that the date of submitting the appeal be within 60 days after the decision was handed down, or together with the appeal against assessments made in consequence of the failure to record the receipts; if the Court did not allow the appeal against the said decision, but did allow in full the appeal against the assessments in respect of the Assessing Officer's decision about the failure to record intakes, then the said presumption of unacceptability in respect of years preceding the year in which the failure to record was discovered shall not apply.
- (b) If an assessee, being required by the Director's directions under section 130 to keep a cash register tape, does not do so, then his books shall be deemed unacceptable.
- (c) (1) If an institution, within its meaning under section 130(a)(4), did not record an intake which it must record under the Director's instructions by virtue of section 130(a)(4) two or more times within twelve consecutive months, then its books shall be deemed unacceptable, unless the Director is convinced that there was sufficient reason for the failure to record;
- (2) a decision by the Director not to accept the reason for not recording as sufficient may be appealed within 60 days after the day on which the institution was notified thereof, as if it were an Order under section 152(b).
- (d) If the Assessing Officer concludes that an intake in an amount in excess of the amount set by the Minister of Finance was not recorded as said in this section, then he may seize and confiscate half of the amount received and not recorded as aforesaid, unless he is satisfied that there was sufficient reason for not recording it; the decision of the Assessing Officer may be appealed, as if it were an Order under section 152(b), on condition that the time for submitting the appeal be within 60 days after the decision was handed down; for purposes of this subsection: "**Assessing Officer**" – other than a Deputy Assessing Officer, an Assistant Assessing Officer or a Chief Collector.

#### **Books acceptability committees**

- 146. (a) (1) The Minister of Finance shall, in consultation with the Minister of Justice, appoint persons of whom the Director shall form books acceptability committees.

- (2) Each aforesaid committee shall consist of three members; its chairman shall be a public personality, expert in accountancy, and the two other members shall be auditors of whom only one is an employee of the State or of another governmental institution; in an objection by a diamond merchant, under section 145A1, a representative of diamond merchants, appointed by the Minister of Finance upon recommendation by the industry's representatives, shall participate only in the deliberations;
- (3) notice of the said appointments shall be published in Reshumot.
- (b) In an objection against a decision by the Assessing Officer under section 130(c) or against a decision by the Director under section 147 in connection with the acceptability of account books, or against a decision by the Assessing Officer under section 145A1, they shall have to justify their decision.
- (c) When it hears an objection against a decision of the Director under section 130(a)(2), the committee may confirm or set aside the Director's decision or make a different decision, as it sees fit.
- (d) When it hears an objection against a decision by the Assessing Officer under section 130(c) or against a decision by the Director under section 147 in connection with the acceptability of account books, the committee may do one of the following:
  - (1) confirm the Assessing Officer's decision; in this case it may declare that the books are unacceptable under aggravating circumstances;
  - (2) set aside the Assessing Officer's decision and direct him to accept the books, either because they contain no defect or deviation from the Director's directions, or because the defects and deviations they contain are immaterial to the determination of the assessee's income.
- (d1) When the committee hears an objection under section 145A1, it may decide that the Assessing Officer is not allowed to use his authority under the said section.
- (e) A committee decision on an objection under section 130(a)(2), (d) or (h), or under section 145A1 shall be final, but it may refer a legal question to the District Court for its opinion.
- (f) The committee is competent to gather evidence for the exercise of its powers under this Ordinance.
- (g) The committee may award the costs of an objection, including the fee of the assessee's representative and traveling expenses and loss of working time allowance of witnesses.
- (h) The Minister of Justice may make regulations on –
  - (1) procedures for convening objection committees;
  - (2) Law procedure in the committee;
  - (3) fees payable in respect of proceedings before the committee;
  - (4) remuneration of committee members.

#### **Director's power of review and revision**

147. (a) (1) Within the period that ends one year after the periods prescribed in sections 145(a) or 152(c), whichever is later, or within six years after the day on which an assessment under section 145(b) was made for the assessee, as the case may be, the Director may, at his own initiative or on the assessee's application ask for the record of any proceeding taken by an Assessing Officer under this Ordinance, and having received the record he may make any

inquiry he may deem appropriate or cause a said inquiry to be made, and he may – subject to the provisions of this Ordinance – make on this matter any Order that he deems appropriate.

- (2) If the assessee was convicted of an offense under sections 216(8), 216B, 217 to 220 or under sections 117(b)(1), or (3) to (8), 117(b2) or 117A of the Value Added Tax Law, or if monetary composition was imposed on him under section 221 or under section 121 of the Value Added Tax Law, then the Director may act as said in paragraph (1) within the period that ends one year after the day of the conviction or of the payment of the composition, as the case may be, or until the end of the period set in paragraph (1), whichever is the later.
- (3) If a person delivered a return under section 145(a)(1) and the Assessing Officer did not use his powers under section 145(a)(2), then the Director may act as said in this section only if the assessee was convicted of an offense under sections 216(8), 216B or 217 to 220, or if monetary composition was imposed on him under section 221.
- (b) An Order under subsection (a) shall be made by the Director or by a person so authorized by him, and an assessment made in consequence of an Order made as aforesaid shall, for purposes of an appeal, be treated like the Order.
- (c) An Order under subsection (a), which increases the assessment, shall be made only after the assessee was given a reasonable opportunity to present his arguments.
- (d) An Order under subsection (a), which increases the assessment, shall – for purposes of an appeal – be treated like an Order under section 152(b).
- (e) If an Order under subsection (a), which reduces an assessment, was made before the time for the submission of an appeal against the assessment expired, but before an appeal was submitted, then the assessee shall no longer have the right to appeal against the assessment, but he may appeal against the Order as if it were an Order under section 152(b).
- (f) If an Order was made under subsection (a) after appeal against an assessment was brought, but before appeal proceedings were concluded, then the appeal shall be heard as if it were an appeal against the Order.

#### **Lists of assesseees and notices of assessment**

148. (a) The Assessing Officer shall, as soon as possible, prepare lists of persons assessed to tax.
- (b) Such lists (hereafter: assessment lists) shall include the names and addresses of the persons assessed to tax, the amount of chargeable income of each of them, the amount of tax that he pays, and other prescribed particulars.
- (c) If complete copies of all notices of assessment and of all notices that amend assessments are filed in the office of the Assessing Officer, then they shall constitute assessment lists for purposes of this Ordinance.

#### **Notice of an assessment to the assessee**

149. The Assessing Officer shall cause each person, whose name appears on the assessment list and who was assessed under this Ordinance, to be served –

in person or by registered mail – a notice sent to him at his regular place of residence or place of business, in which shall be specified the amount of his chargeable income, the amount of tax payable by him and his rights under section 150 or section 153, as the case may be.

## **CHAPTER TWO: OBJECTION AND APPEAL**

### **Right of objection before Assessing Officer**

150. (a) If a person disputes the assessment, then he may apply to the Assessing Officer by a written notice of objection that he review and change the assessment; a said application shall state precisely the grounds for the objection to the assessment and shall be submitted within 30 days after the day on which the notice of assessment was served; however, if it was proven to the Assessing Officer's satisfaction that the person who disputes the assessment was prevented from submitting the application within that period because of his absence from Israel, sickness or any other reasonable cause, then he may extend the period, for as long as appears reasonable under the circumstances.
- (b) If an assessee did not submit a return in respect of a certain tax year and an assessment was made for him for that year under section 145(b), then only a return submitted by him for that year shall be deemed an objection, unless it was proven to the Assessing Officer's satisfaction that the assessee was not obligated to submit a return or that it was not possible to submit it.

### **Hearing of objection**

- 150A. Whoever made the assessment shall not hear an objection to it.

### **Powers of the Assessing Officer in connection with objections**

151. When an Assessing Officer receives the notice of objection said in section 150, then he may demand from the objector that he deliver all particulars that the Assessing Officer deems necessary in respect of the assessee's income and that he produce all books or other documents in his custody or possession that relate to that income, and he may summon any person whom he thinks able to give evidence on the assessment to appear before him, and he may interrogate him under oath or not under oath; however, a clerk, agent, or employee of the assessee or any other person employed in his affairs on the basis of personal trust shall be interrogated only at the assessee's demand; this section shall not derogate from any power of investigation under any other statute.

### **Agreement or decision on an objection**

152. (a) If the assessed person who objected to an assessment made for him reaches an agreement with the Assessing Officer on the amount at which he is to be assessed, then the assessment shall be amended accordingly and notice of the tax he must pay shall be served on the assessee.
- (b) If no agreement is reached, then the Assessing Officer shall determine the tax by written Order, and in it he may confirm, increase or reduce the assessment.

- (c) If, within three years after the year in which the return under section 131 was submitted, and – with the Director's approval – within four years after the end of the said tax year, or within one year after the objection was submitted, whichever is the latest, no agreement was reached as said in subsection (a), and if the Assessing Officer did not exercise his powers under subsection (b), then the objection shall be deemed to have been allowed; however, if the objection was submitted against an assessment made under section 145(b), then it shall be deemed to have been allowed only if the Assessing Officer does not use his powers said in this section within four years after the end of the tax year in which it was submitted and – with the Director's approval – within five years after the end of the said tax year.

#### **Right of appeal**

- 153. (a) Any person who deems himself injured by a decision of the Assessing Officer under section 152(b) may appeal before the District Court in whose area of jurisdiction the Assessing Officer acted.
- (b) The appeal shall be submitted and heard in accordance with the provisions of the Ordinance and of procedural regulations made thereunder, and the Assessing Officer shall be the respondent to the appeal.

#### **Court of Appeal**

- 154. (a) Appeals under section 153 shall be heard by one or more judges, as the President of the District Court may prescribe, either generally or for purposes of a certain appeal.
- (b) The Court to which an appeal was submitted may, on the appellant's application, direct that the appeal or a certain stage of proceedings in it be heard at the venue of another District Court.
- (c) Every appeal to the District Court under this Chapter shall be heard in camera, if the Court did not direct otherwise on the appellant's application.

#### **Burden of Proof**

- 155. The appellant shall bear the burden of proving that the assessment is excessive; however, if the appellant kept acceptable books or, in the case of an appeal under section 130(h), if the account books were audited by an auditor and his opinion on the financial reports based thereon does not include any reservation, or a reservation which in the Court's opinion is not relevant to the question of the books' acceptability, then the Assessing Officer or the Director, as the case may be, shall have to justify his decision.

#### **Power of Court of Appeal**

- 156. The Court shall confirm, reduce, increase or annul the assessment or rule otherwise on the appeal, as it deems proper, and notice of the chargeable income and of the amount of tax to be paid by the appellant according to the Court's decision shall be served on both parties.

#### **Appeal to Supreme Court**

- 157. A decision of the District Court under section 156 may be appealed to the Supreme Court as Court of Civil Appeals.

#### **Procedural regulations on appeals**

- 158. The Minister of Justice may make procedural regulations on any matter

connected to the lodging and hearing of appeals under sections 153 to 157, including the payment of Court fees, the provision of collateral, making a deposit with the Court and the presentation of evidence.

## **CHAPTER TWO "A": HEARING ARGUMENTS ABOUT ASSESSMENTS BASED ON THE ASSESSING OFFICER'S JUDGMENT**

### **Hearing arguments and presenting reasons**

- 158A. (a) An assessment according to the best judgment under section 145, and an Order under section 152 shall not be made without the assessee having been given a reasonable opportunity to present his arguments.
- (b) In a notice of assessment or in an Order said in subsection (a) the Assessing Officer shall specify – in addition to the reasons for not accepting the return or the contestation – also the manner in which the assessment was made.
- (c) The provisions of subsections (a) and (b) shall not apply, if the assessee did not submit a return as said in sections 131, 135, 161, 166, 171, or 181B.

## **CHAPTER TWO "B": TAX DECISIONS**

### **Definitions**

158B. In this Chapter –

"the tax laws" – each of the following:

- (1) this Ordinance;
- (2) the Value Added Tax Law;
- (3) the Real Estate Taxation Law;
- (4) the Inflationary Adjustments Law;
- (5) the Encouragement of Capital Investments Law;
- (6) the Encouragement of Capital Investments in Agriculture Law 5741-1980;
- (7) the Encouragement of Industry (Taxes) Law 5729-1968;
- (8) every provision on tax in or under a Law, which relates to one or more of the enactments enumerated in paragraphs (1) to (7).

"**tax decision**" – a decision about any aspect of an applicant's tax liability, about the resulting tax or about the implications of an act he performed for his tax liability, his income, profit, expense or loss;

"**tax decision by agreement**" – a tax decision made by way of agreement with the applicant;

"**applicant**" – the person who requested that the Director make a tax decision under the provisions of this Chapter;

"**tax**" – a tax imposed under one of the tax laws;

"**act**" – includes transaction and sale;

"**profit**" – includes land appreciation.

### **Authority in respect of tax decisions**

- 158C. (a) The Director may give a tax decision at an applicant's application, and he may also give a tax decision by agreement.
- (b) When an application for a tax decision has been made, the Director

may make giving the decision conditional on another person being joined as applicant, and he may also refuse to give a tax decision or decide that the answer to the application be given by an Assessing Officer otherwise than by way of a tax decision.

- (c) A decision under subsection (a) may be limited in time, subject to other limitations or conditional, as shall be prescribed in it.
- (d) A decision under subsection (a) shall only be made after the applicant was given a reasonable opportunity to present his arguments.
- (e) There shall be no appeal against a tax decision by agreement; a tax decision not by agreement may be appealed as part of an objection or appeal against an assessment.

#### **Application for a tax decision**

- 158D. (a) An application for a tax decision – other than a application about tax under the Value Added Tax Law or under the Real Estate Taxation Law – may be submitted before or after the act is performed, on condition that it is submitted before the time set in section 132 or 133 for submitting a return under section 131, in which the act, income, profit, expense or loss that are the subject of the application have been taken into account.
- (b) An application for a tax decision about tax under the Value Added Tax Law or under the Real Estate Taxation Law shall be submitted before the act that is the subject of the application is performed.
  - (c) The application shall include all the substantive facts and particulars relevant to it, and all the documents, certifications, opinions, declarations, valuations, contracts – and if contracts have not yet been signed, then their drafts – shall be attached to it, together with every other substantive particular, as the Director prescribed, and certification that the fee prescribed under section 158E has been paid shall be attached.
  - (d) The Director may demand every particular or document he deems necessary for his decision on the application.
  - (e) If the name and ID number of the applicant were not stated in the application, then those particulars shall be provided later, and no tax decision shall be given before they have been provided.
  - (f) An applicant must not withdraw his application before a decision is given, except with the Director's consent.
  - (g) If other provisions on applications for tax decisions by the Director are prescribed in the tax laws, then the provisions of this Chapter shall apply, *mutatis mutandis*, as far as they do not contradict the other provisions.

#### **Application fee**

- 158E. The Minister of Finance may – with approval by the Knesset Finance Committee set a fee for an application for a tax decision, either as an amount or as a graduated percentage in relation to the value of the transaction, to the applicant's income or to some other criterion.

#### **Additional provisions**

- 158F. (a) When the Director has made a tax decision, he shall not have the right to withdraw it, unless he finds that one of the particulars or one of the documents necessary for the decision was not submitted to him, or that the circumstances relevant to the decision have changed, or that he was given a false, erroneous or misleading particular.

- (b) If the Director made a tax decision by agreement, then the applicant shall comply with the conditions and provisions prescribed in it, unless the act that is the subject of his application was not performed, or the income or the expense, in respect of which the application was submitted, was not received or not incurred.
- (c) Notwithstanding the provisions of the tax laws, the Director may publish a condensed version of tax decisions he made in the manner and formulation he determined, also if the applicant did not agree thereto; the published condensation of a decision shall not include the applicant's name and ID number.
- (d) The Director may make rules on tax decisions and on the circumstances, under which a decision shall not be given.

### **CHAPTER THREE: ERRORS AND TAX REFUNDS**

#### **Defects and errors that do not invalidate**

159. (a) An assessment, payment Order or any other proceeding that appears to have been made according to the provisions of this Ordinance shall not be canceled or deemed fundamentally void or voidable because of an error of form, and it shall not be affected by an error, defect or omission in it, if it substantially and in effect conforms to the provisions of this Ordinance or of any Ordinance that amends it, or to their intent and meaning, and if the person assessed or to be assessed or the person to be affected is designated in it clearly or in commonly understood terms.
- (b) An assessment shall not be impeached or affected because of a mistake in it in the name or surname of the person liable to tax, or in the description of any income, or in the amount of tax charged, or because of any difference between the assessment and the notice thereof, on condition that the assessment notice was duly served on the person to be charged to tax and that it includes – in substance and in effect – the particulars on which the assessment was made.

#### **Refund of excess tax in consequence of return**

- 159A. (a) In this section: "**linkage differentials and interest**" – an addition to the amount in question, equal to the said amount multiplied by the rate of increase of the consumer price index during the period in question, plus 4% annual interest on the amount in question after the said linkage differentials were added to it, or at another rate set by the Minister of Finance with approval by the Knesset Finance Committee.
- (b) If a person paid tax for a particular tax year, whether by way of deduction or in any other manner, in excess of the amount to which he is liable according to a return submitted under section 131, that return being based on account books or – if he is not required to keep account books – on appropriate documents, then the excess shall be refunded to him within 90 days after the day on which he submitted the return or on July 31 of the tax year following the tax year in respect of which the return was submitted, whichever is later, unless his account books were found unacceptable in the last tax year, in respect of which an assessment was made for him, and he does not prove to the Assessing Officer's satisfaction that the grounds for the books' unacceptability did not exist in the year in respect of which the refund is



- claimed.
- (b1) If a person was under obligation to submit a return under section 131 or under section 135 before the time for the refund of excess tax under subsection (b) (hereafter: tax refund date) and if he did not submit it by the tax refund date, then the Director may delay the refund for a period of not more than 90 days after the said returns have been submitted.
  - (c) The refund of an excess during the period from the end of the tax year or the day of payment, whichever is later, until the date of the refund shall be paid with the addition of linkage differentials and interest; in the case of a person with a special assessment period, the end of the special assessment period shall, for this purpose, be substituted for the end of the tax year.
  - (d) If amounts were refunded to an assessee under this section and it turned out that they were not due to him, then those amounts – exclusive of linkage differentials and interest – shall be deemed a tax debt due from him from the end of the tax year to which relates the return, on the basis of which they were refunded.

#### **Refund of excess payment in consequence of assessment**

160. (a) If it is proved to the Assessing Officer's satisfaction that a person paid tax for a tax year – by deduction or otherwise – in excess of the amount to which he is liable and if the return for that year was submitted not later than the end of six years after that year, then that person shall be entitled to have the excess refunded to him within one year after the day on which the assessment that established the excess amount was made, or within two years after the end of the tax year in which the tax was paid, whichever is later, with the addition of linkage differentials and interest within their meaning in section 159A(a) from the end of the tax year in respect of which the return was submitted, or from the date of payment, whichever was later, until the day of the refund.
- (b) No refund shall be paid to any person in respect of a tax year for which he did not deliver a return or neglected to deliver it, or for which he was assessed in an amount that exceeds the amount in his return and for which he received notice of assessment made for him in that year, unless he proved to the Assessing Officer's satisfaction that the failure or the neglect to deliver a true and correct return did not stem from any fraud or willful act or omission; this provision does not apply to sums to be refunded after an objection or appeal.
  - (c) Any person who deems himself injured by the Assessing Officer's decision on the amount to be repaid under this section has the same right to appeal against the decision, as he would have if he deemed himself injured by an assessment made on him.

#### **Delaying a tax refund during an assessment procedure**

- 160A. (a) Notwithstanding the provisions of sections 159A or 160, the Assessing Officer may delay the refund of tax that was paid in excess of the amount the assessee owes according to a return or assessment, as said in those sections, up to half the aforesaid amount that is due to the assessee, or up to the amount in dispute, whichever is lower, if the Assessing Officer ordered the return to be examined.
- (b) The delay of a tax refund said in subsection (a) shall apply up to 90 days after the return was received; however, if before the said 90 days elapsed the Assessing Officer determined the assessment to the best of his ability, as said in Chapter One of Part Nine, then he may delay

- the refund of up to half the amount of tax he determined in the said assessment for an additional ninety days, and if an objection under section 150 was submitted – for an additional period that shall not exceed 180 additional days after submission of the objection.
- (c) If, within 180 days after the date of the objection, a decision on the objection is handed down under section 152, then the Assessing Officer may delay the tax refund up to the amount of the tax set in the said assessment, until the date on which it becomes possible to collect the tax debt under the assessment he made under the Taxes (Collection) Ordinance, unless the Court before which the appeal under sections 154 or 158 was brought decides otherwise.

## PART TEN: PAYMENTS AND COLLECTION

### CHAPTER ONE: DEDUCTIONS ON ACCOUNT OF TAX

#### Article One: Deductions from Dividend and Interest

161. Repealed

#### **Set off of tax on dividend and interest**

162. If a body of persons deducted tax from interest or dividends, and if that interest or dividend or part of it is included in the recipient's income, then the tax deducted shall be set off against the tax imposed on that income.

#### **Relief from tax on the dividends of foreign companies from Israel income**

163. (a) If an ordinary dividend was paid to a person who under this Ordinance is liable to tax on it, and if he proves to the Assessing Officer's satisfaction that the dividend was paid by a company that is not resident in Israel and that the company's income, out of which the dividend was paid (hereafter: the relevant income) includes income on which the company paid tax under this Ordinance, whether by deduction or in some other manner (hereafter: Israel income), then he shall be entitled to tax relief on a proportional part of the dividend, in the proportion of the Israel income to all the relevant income (hereafter: Israel dividend).
- (b) The rate of relief shall be equal to the rate of tax paid by the company under this Ordinance or to the rate of tax applicable to the Israel dividend, treated as the highest part of that person's income, whichever is the lower rate.
- (c) If relief was granted to a person under this section in respect of an Israel dividend, then both the amount of that relief and the amount of the dividend shall be deemed his income from that dividend.
- (d) Any relief granted under this section shall, for the purposes of section 201, be deemed to reduce the amount of tax chargeable under this Ordinance in respect of the said dividend.
- (e) For purposes of this section:
- "ordinary dividend"** – a dividend on a share which is not a preferred share and also that amount of dividend on a preferred share which is not paid at a gross percentage rate;
- "preferred share"** – a share which carries the right to dividends at a fixed gross percentage rate, payable before any dividends on other

classes of shares, whether or not it also carries the right to some further participation in profits;

"tax" – not including companies tax.

## **Article Two: Deduction from Work Income and from Other Income**

### **Obligation to deduct at source**

164. Any person who pays or is responsible for the payment of work income, including the part of a grant received in consequence of retirement or death that is not exempt under section 9(7a), of earnings or profit that stem from gambling, lotteries or prize winning activity, as said in section 2A, of the amount received from capitalization of a pension which is not exempt under sections 9A or 9B, of amounts and payments to which section 18(b) applies and which constitute income for their recipient, of income under section 2(5), of chargeable income that a real estate investment fund, as defined in section 64A2, transmits to its members, of consideration within its meaning in section 88, of interest or dividends, or of any other income which the Minister of Finance with approval by the Knesset Finance Committee so designated by Order, shall – when payment is made – deduct tax from the amount to be paid in the manner and at the rates prescribed, but the Minister of Finance may prescribe that – in respect of gains or profit said in section 2A – the tax deduction shall be as he shall prescribe, even if not at the time payment is made and not out of the amount to be paid; this provision also applies to the State.

### **Set off of deduction**

165. (a) The said deduction shall be set off against the tax due from the recipient's chargeable income in the tax year in which the deduction was made or in the following tax year, at the Assessing Officer's option at the time of or before the assessment.
- (b) A set off under subsection (a) against the tax to which a controlling member, as defined in section 32(9), is liable shall only be made after the deducted amount has been paid to the Assessing Officer, unless the member's control is less than 50% and he proves to the Assessing Officer's satisfaction that he did not know that the deducted amount had not been paid to the Assessing Officer or that he took all reasonable measures to ensure its payment.

### **Obligation of person who makes the deduction**

166. (a) When a person has deducted tax under section 164, then he shall pay the amount of tax deducted to the Assessing Officer at the time prescribed by regulations, and at the same time he shall deliver to him a return as prescribed.
- (b) An employer or a person who deducted shall submit a return said in subsection (a) in respect of the payment of an employee's work income (Form 0126) and in respect of income liable to deduction (Form 0856) in the online manner, as the Director shall prescribe, until April 30 after the tax year in respect of which it is submitted, together with a declaration on a Form prescribed by the Director, according to which the particulars and the information given in the return are correct and complete, as well as a printout of the said return signed by him (hereafter: employer's online return and deductor's online return, as the case may be).

- (c) In this section –  
**"income liable to deduction"** – payments designated under section 164 as income for purposes of the said section, as specified below:
- (1) insurance commission;
  - (2) artists', examiners' and lecturers' fees,
  - (3) writers' fees;
  - (4) payments for agricultural work or produce;
  - (5) payments for construction work and haulage;
  - (6) payments for garment making, metal work, electrical and electronic work and haulage;
  - (7) payments for diamond work;
  - (8) payments for services or assets;
- "employee"** – other than an employee who works in an individual's private household.

#### **Assessing Officer may assess deductions**

167. (a) If a person, to whom the provisions of sections 161 or 164 apply, did not deduct tax as provided by them or did not deliver a return as said in sections 161 or 166, or if he delivered a said return, but the Assessing Officer has reasonable grounds for believing that the return is not correct, then the Assessing Officer may, to the best of his judgment, assess the amount that person should have deducted, and this assessment shall not relieve that person from any other responsibility under this Ordinance; an assessment under this subsection shall be treated like an assessment under section 145; the Assessing Officer may assess a person as said in this section during the period said in paragraph (1) or in paragraph (2), whichever is later:
- (1) during the period in which he may – to the best of his judgment – determine that person's chargeable income for the tax year in which is obligated to deduct tax;
  - (2) within three years after the end of the tax year in which the liable person's last deductions return for the tax year was submitted under the provisions of sections 161, 164 or 234, and with the Director's approval – within four years after the end of the said tax year.
- (b) The provisions of subsection (a) shall also apply when an assessment or an Order which is no longer open to contestation or appeal has been made for the year to which the return relates in respect of the person from whose income the tax should have been deducted, if that assessment or Order does not include the income from which the deduction should have been made.

#### **Right of objection**

168. If a person disputes the correctness of an assessment under section 167, he may, within two weeks, deliver a written objection to the Assessing Officer, and the provisions of sections 150 to 158 shall apply as if the objection had been filed under those sections; the amount of tax, determined by the assessment by Order under section 152(b) or in an appeal under section 153, shall be paid within seven days after notice of assessment was delivered or after the Order was made or the judgment handed down, all as the case may be, or by another date prescribed by regulations.

169. Repealed

### **Article Three: Deduction from Foreign Resident**

#### **Obligation of person who pays to a foreign resident**

170. (a) A person who pays to a person who is not resident in Israel – or to another for him – any income that is chargeable under this Ordinance – other than income from which tax was deducted under sections 161 or 164 – shall deduct from that income tax at the rate of 25 agorot for every shekel at the time of its payment, if the recipient of the payment is an individual, or tax at the rate imposed by sections 126 and 127 if the recipient is a body of persons, or at another rate the Assessing Officer will prescribe for them by written notice; however, the Assessing Officer may permit the income to be paid without deduction of tax, if it has been proven to his satisfaction that the tax already was paid or that it will be paid in some other manner; for this purpose: **"person who pays"** includes a financial institution, as defined in the Value Added Tax Law 5736-1975, through which the income is paid, unless the financial institution holds certification from the Assessing Officer, exempting it from the obligation to deduct at the source.
- (b) The provisions of subsection (a) shall not apply to a person who pays income said in subsection (a) and who, under sections 108 to 115, is himself responsible for paying tax on it.
- (c) Notwithstanding the provisions of subsection (a), if a real estate investment fund, as defined in section 64A2, transmits chargeable income of shareholders, within its meaning in section 64A4, to a person not resident in Israel, then it shall deduct from it tax at the tax rate that obligates it under the said section.

#### **Obligation of the person who deducts from a foreign resident**

171. When a person has deducted tax under section 170(a), then he must pay the amount of tax he deducted to the Assessing Officer within seven days after the day of deduction, and he shall deliver a return to him, specifying the name and address of the person to whom or for whom the income was paid.

#### **Set off of deduction**

172. The amount of deduction under section 170 shall, for purposes of collection, be set off against the tax that will be imposed on the person who received the said income.

#### **Assessing Officer may assess deduction**

173. If a person is under obligation to deduct tax under the provisions of this Article and does not deduct all or part of the amount, or if he did not deliver a return said in section 171, or if he delivered a said return but the Assessing Officer has reasonable grounds for believing that the return is not correct, then the Assessing Officer may assess the amount of tax which that person was obligated to deduct to the best of his judgment; an assessment under this section shall be treated like an assessment under section 145; the Assessing Officer may assess a person said in this section during the period during which he may determine – to the best of his judgment – that person's chargeable income in the tax year in which he was under obligation to deduct the tax; that assessment shall not relieve that person from any other responsibility under this Ordinance.

## Article Four: Auxiliary Powers

### Power to enter, inspect and interrogate

- 173A.(a) If the Assessing Officer deemed it necessary to do so in order to ensure compliance with the provisions of this Chapter or with any provisions on tax deduction at the source or in order to prevent evasion from compliance with them, then he or a public servant so authorized by him in writing may –
- (1) enter the premises – except a dwelling not used for his business or vocation – of any person who must deduct tax at the source, or who has possession of the books and documents that relate to tax deduction at the source, and he may inspect any register, record, certificate or other document related to tax deduction at the source, which is in their possession;
  - (2) interrogate any person who is required to deduct tax at the source or who has possession of the books and documents that relate to tax deduction at the source or from whose income the tax must be deducted;
- for the purposes of paragraphs (1) and (2), "**tax deduction at the source**" – deduction of tax under sections 161, 164 or 170.
- (b) If a person is interrogated or if his premises are inspected under subsection (a), then he shall give the person who interrogates him or who makes the inspection every opportunity to do so, and he shall answer all questions put to him completely and truthfully.
  - (c) The provisions of this section shall not derogate from any powers of an Assessing Officer or public servant under this Ordinance.

## Article Five: Miscellaneous Provisions

### Postponement because of holidays

- 173B. The last date for the submission of a return under this Chapter shall be postponed, if there were at least three days of rest during the five days that preceded the said date, and it shall be on the fourth working day after the end of the consecutive days of rest; for this purpose: "**days of rest**" – the days of rest prescribed in the State of Israel within their meaning in section 18A(a) of the Law and Administration Ordinance 5708-1948, as well as interim festival days.

## CHAPTER TWO: COLLECTION

### Article One: Advance Payments

#### Definition

174. In this Article, "**the determining year**" – the last tax year in respect of which the income of the assessee was assessed by January 1 of the tax year, whether or not objection was lodged.

#### Assumption

- 174A Spouses shall be deemed, for purposes of this Article, a single assessee; this

provision shall not derogate from the provisions of section 66A.

#### **Advance payments**

175. (a) On the fifteenth day of each of the ten months from February to November of each tax year every assessee shall, on account of the tax for that tax year, make an advance payment of 10% of the amount of tax to which he became liable for the determining year; however, if that taxpayer was allowed to calculate his income according to a special period, as said in section 7, then he shall pay the said advance on account of tax for the tax year in which ends the special period that includes the date for the said advance payment.
- (b) Notwithstanding the provisions of subsection (a), the Minister of Finance may prescribe, with approval by the Knesset Finance Committee, in general or for categories of assessees, monthly advance payments that shall be a portion of those assessees' turnover of transactions during the period during which the advances are paid; the rate of advance payment shall be set according to the ratio between the assessee's turnover of transactions in the determining tax year and the tax he was obligated to pay in that year on that turnover; for this purpose: "**turnover of transactions**" – the total of transactions, as defined in the Value Added Tax Law 5736-1975, excluding sales to which Part Five or the Land Appreciation Tax Law 5723-1963 apply; the Minister of Finance may – in Rules – add or detract categories of transactions, of income or of sales, either in general or for categories of assessees, all on conditions which he shall prescribe.
- (c) If, during the determining tax year, a body of persons paid amounts said in section 18(b), other than a regular monthly salary and repayment of expenses (hereafter in this section: payments to a controlling member) to an individual who is a controlling member within its meaning in section 32(9), then its advances shall be in the amount it would have paid in that year, had it not made payments to the controlling member.
- (d) The amount of advance payments by a body of persons shall be reduced by the amounts of tax it withheld under section 164 from payments to controlling members.
- (e) If a transparent company received a dividend, then the amount of the first advance to be paid – after it was received – by it or by the share holders, within their meaning in section 64A1, shall be increased by an amount equal to 25% of the dividend.

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*As long as the provisions of section 64A remain in effect, subsection (e) should be read as it was before Amendment No. 132, as follows – Tr.*

- (e) If a family company received a dividend, then the amount of the first advance to be paid – after it was received – by it or by the assessee, within its meaning in section 64A, shall be increased by an amount equal to 25% of the dividend.

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- (f) The last date for payment under this section shall be postponed, if there were at least three days of rest during the five days that preceded the said date, and it shall be on the fourth working day after the end of the consecutive days of rest; for this purpose: "**days of rest**" – the days of rest prescribed in the State of Israel within their meaning in section 18A(a) of the Law and Administration Ordinance 5708-1948, as well as interim festival days.

176. Repealed

**Crediting payments against advances**

177. (a) An amount deducted during the tax year at the source – under sections 161 and 164 to 170 – from the assessee's income in that tax year shall be deemed a payment on account of advance payments to which that assessee is liable under section 175 in respect of the income from which the tax was deducted, and he is entitled to set off any sum deducted at the source during the tax year in respect of which the advance payments are to be paid against his advance payments, on condition that he has written certification of that deduction.
- (b) An amount paid as an advance under section 181B in respect of an excess expenditure incurred in that tax year shall be deemed a payment on account of the advances which that assessee must pay under section 175, and he is entitled to set it off against his advances, on condition that he holds written certification of the payment of the advance in respect of excess expenditures.
- (c) The provisions of subsection (b) shall not apply to an amount paid as an advance in respect of excess expenditures by a body of persons, to which the provisions of section 3(g) apply.

**Doubt as to tax for the determining year**

178. If the amount of tax for the determining year is in dispute, but is greater than the amount of tax last finally determined, then the monthly advance payment shall be calculated according to that part of the amount of tax for the determining year which is not in dispute, or according to the amount of tax determined as aforesaid, whichever is the larger amount; **"finally determined"**, in this section – by a determination not open to objection or appeal.

**Minister of Finance may change rates and times**

179. The Minister of Finance may, by Order, increase or reduce the rate of advance payments under this Article, change their payment dates or prescribe that they be paid once every two months or at other intervals set by him; he may also prescribe different rates of advance payments in respect of different determining years and – with approval by the Knesset Finance Committee – for each of the advance payments during the tax year, or for different categories of assesseees.

**Assessing Officer may exempt or increase**

180. (a) An Assessing Officer may exempt a person from all or part of an advance payment under this Article, if it was proven to his satisfaction that the tax for the year in which the advance payment is payable and in respect of which that assessee is likely to be liable to tax will be less than the tax to which he is liable in respect of the determining year, but he shall not so exempt a person who is required to keep account books and does not do so.
- (b) (1) If the amount of tax which the assessee must pay according to a return submitted by him under section 131 during the tax year – and for this purpose the Minister of Finance may prescribe a percentage by which the said amount of tax shall be increased – exceeds the amount of advance payments to which he is liable in respect of that year, then the Assessing Officer may increase the



amount of advance payments under this Article by the amount of the said differential.

- (2) If the Assessing Officer has reasonable grounds for believing that the tax which will be due from an assessee for a particular tax year will exceed the amount of the advance payments to which he is liable for that year by at least 20% or by at least NS 500,000, whichever is the lesser amount, then he may increase the amount of advance payments under this Article by the differential; an aforesaid decision shall, for purposes of objection and appeal, be treated like an assessment under section 145.
- (c) If an individual kept account books in the tax year and in the year that preceded it, but did not and was not required to keep account books in the year which serves as basis for the determination of advance payments in the tax year, and if the tax to which he is liable for the preceding tax year – according to the return submitted by him and based on account books – is less than the amount of advance payments, then the amount of advance payments to which he is liable in respect of the tax year shall be reduced to the amount of tax to which he is liable according to the return.

#### **Person not previously assessed**

181. If an assessee has chargeable income and previously he was not liable to tax or was not assessed, then he shall make the advance payments under section 175 or 176, as the case may be, in percentages of the projected amount of tax which he is likely to have to pay on that income in that tax year according to his estimate, and with the first payment he shall submit to the Assessing Officer a declaration of the said estimated tax, and an additional declaration six months after the first declaration was submitted; if he did not deliver the said declarations, or if he delivered such declarations, but the Assessing Officer has reasonable grounds for believing that the declarations are not correct, then the Assessing Officer may – to the best of his judgment – set the amount of the advance payment which that assessee must pay, and a said determination shall, for purposes of objection or appeal, be treated like an assessment under section 145.

#### **Power to grant reduction**

- 181A. The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe by regulations reductions to be granted to persons who make advance payments under this Article before the time prescribed for their payment or who make advance payments in amounts greater than what is due from them, all at rates and on conditions prescribed by him either generally or for particular categories of assesseees.

### **Article One "A": Advance Payment for Nondeductible Expenses**

#### **Advance payment for excess expenses**

- 181B. (a) If, for purposes specified in regulations under section 31, a body of persons spent amounts which according to the said regulations are not deductible or which exceed the amounts set as deductible, or if it spent amounts for expenses which according to section 32(11) are not deductible (in this Law: excess expenditures), or if it paid a levy under Chapter Six of the Arrangements in the State Economy (Law

Amendments) Law 5749-1989, then it shall pay the Assessment Officer at the prescribed time an advance payment at the rates specified below of the excess expenditures which it incurred, and at the same time it shall submit to him a prescribed return and it shall also submit to him an annual return specifying and summing up all the excess expenditures which it incurred in that year, all as specified below:

(1) a body of persons, to which section 3(g) applies – 90%;

(2) any other body of persons – 45%;

for purposes of this section: "**body of persons**" – exclusive of partnerships that do not include any partner that is a body of persons to which this section applies.

- (b) The provisions of subsection (a) shall not apply to amounts paid as work income from which the person who pays them or is responsible for their payment deducted tax under section 164.
- (c) If a body of persons did not make the advance payments said in subsection (a), or did not deliver a return under that subsection, or delivered a return but the Assessing Officer has reasonable grounds for believing that the return is not correct, then the Assessing Officer may – to the best of his judgment – assess the amount of advance payment which that body of persons must pay, and that assessment does not relieve it of any other obligation under this Ordinance; an assessment under this section shall be treated like an assessment under section 145; the Assessing Officer may assess a person as said in this section during the period during which he may determine – to the best of his judgment – that person's chargeable income in the tax year in which he was under obligation to pay the advance.

#### **Set off against future tax**

181C. If a body of persons, to which the provisions of section 3(g) do not apply, made advance payments under section 181B for a certain tax year in an amount that exceeds the amount of tax which it must pay in that year, then the excess shall not be refunded to it; however, if its income from the same business or vocation will be liable to tax – including Land Appreciation Tax – in subsequent tax years, then the excess amount shall be set off against the tax or the Land Appreciation Tax; the excess amount shall be adjusted at the rate of the index increase from the end of the tax year in which it was created until the end of the tax year in which it was set off.

### **Article Two: Times for Payment of Tax**

#### **Payment on submission of return**

182. (a) When a body of persons submits a return under section 131 or an estimative return under section 133, it shall pay the amount of tax due from it according to that return.
- (b) The Minister of Finance may prescribe, by Order, in respect of other assesseees – except for individuals at least 75% of whose income is chargeable income under section 2, paragraphs (2) or (5) – that the assessee to whom that Order applies shall, when he submits a return under section 131 or an estimative return under section 133, pay the amount of tax due from him according to that return.

#### **Payment after notice of assessment**

183. If a notice of assessment under section 149 was delivered to a person, then he shall, within 15 days after delivery of the notice of assessment, pay the balance of tax due from him under it, and if he filed objection under section 150 – the balance of tax that is not in dispute.

**Payment after objection**

184. If an amended notice of assessment under section 152(a) or an Order under section 152(b) was delivered to a person, then he shall – within 15 days after delivery of the notice or Order – pay the balance of tax due from him under it, and if he filed objection under section 153 – the balance of tax that is not in dispute.

**Article Three: Interest and Fines**

**Adjustment of payment after judgment**

185. If the decision of a District Court under section 156 or a decision of the Supreme Court under section 157 was delivered to a person, then the following provisions shall apply:
- (1) if the assessee paid too much, then the excess amount shall be refunded to him, plus interest and linkage differentials, within their meaning in section 159A(a);
  - (2) if the assessee paid too little, then the balance shall be paid within fifteen days after the decision is delivered, plus linkage differentials and interest as aforesaid for the period from the day the appeal was filed until judgment was given, unless the Court prescribed otherwise.

**Interest on postponement of times of payment**

186. The Assessing Officer may, if shown sufficient reason therefor, extend the times prescribed under Article Two for the payment of all or of part of the tax, or the times for payment of all or of part of the advance under Article One, for a period he deems appropriate, on condition that the assessee pay linkage differentials and interest, within their meaning in section 159A(a), for the period of postponement.

**Payment of interest and linkage differentials**

187. (a) (1) In respect of amounts of tax for a certain tax year which were not paid by the end of that tax year the assessee shall be charged linkage differentials and interest, within their meaning in section 159A(a) for the period from the end of the tax year until the date of payment; for a person with a special assessment period the end of the special assessment period shall, for this purpose, take the place of the end of the tax year.
- (2) The provisions of this subsection shall also apply to tax debts under section 159A(c).
- (b) The provisions of subsection (a) shall not apply to a period, in respect of which linkage differentials and interest are owed under sections 185(2) or 186.
- (c) (1) In respect of amounts of tax that should have been deducted, but were not deducted, or were deducted, but not transferred to the Assessing Officer at the time prescribed therefor, the person obligated to make the deduction shall be charged linkage differentials and interest, within their meaning in section 159A(a),

for the period that begins on the fourteenth of the month before the day on which he should have, but did not transfer the amounts deducted, or on which he should have transferred, if he had deducted them on time, and until their transfer to the Assessing Officer; however, if the amount liable to deduction does not relate to a specific date and therefore is determined as a total for a certain period, then linkage differentials and interest shall be charged for the period that began in the middle of the said period.

- (2) If the person required to make the deduction proves that the person, from whose income he should have deducted the amounts that were not deducted, included the said amounts in a return of his income, then the date on which the amounts should have been transferred to the Assessing Officer shall be replaced by the expiration of the tax year to which the said return relates.
- (d) If advances in respect of excess expenditure should have been paid under section 181B and were not paid to the Assessing Officer on the prescribed date and if – had they been paid on time – they could not have been set off against advances paid or tax paid in respect of that tax year, then the debtor shall be charged linkage differentials and interest within their meaning in section 159A(a) for the period from the end of the tax year until the day of payment.

#### **Incentive for early filing of return and payment**

- 187A. (a) If an assessee paid any amount on account of tax due from him in respect of a certain tax year before the last date set in section 132 for submitting the return under section 131, then in respect of that amount he is entitled to exemption from linkage differentials and interest applicable thereto under section 187(a), as specified below:
  - (1) on an amount paid until the end of the first month after the end of the tax year or special assessment period (hereafter in this section – tax year) – full exemption from linkage differentials and interest;
  - (2) on an amount paid during the second month after the end of the tax year – exemption from half the linkage differentials and interest;
  - (3) on an amount paid during the third month after the end of the tax year – exemption from one fourth the linkage differentials and interest.
- (a1) The Minister of Finance may, by Order, increase the rates of exemption said in subsection (a);
- (b) The relief under subsection (a) shall be computed first, and the relief under the closing passage of section 187(a)(1) shall be deducted from the balance of the linkage differentials and interest.
- (c) Repealed

#### **Fine for non-submission of return**

- 188. (a) If a person did not submit a return by the date set in section 132, then for each month of delay a fine of NS 200 shall be imposed on him; however, if a later date for the submission of the return was set for that person under section 133 (hereafter: delayed date), and if that person did not submit the return by the delayed date, then a fine of NS 400 shall be imposed on him for each month of delay after the delayed date.
- (a1) If, in a return he submitted under section 131, a person did not specify

an act designated under the said section as tax planning that must be reported, then the Assessing Officer may impose on him a fine of NS 500 for every month in which he did not report as aforesaid.

- (b) Repealed
- (c) If a person did not submit a return at the time set in sections 161 or 171, then the Assessing Officer may impose on him a fine of NS 200 for each month of delay.
- (d) If a person did not submit on time any of the returns prescribed for the purposes of sections 164 to 166, then a fine of NS 200 shall be imposed on him for each month of delay.
- (e) In this section, "**month**" – a whole month.
- (f) If a person, required to deduct tax at the source from amounts paid by him. does not at the prescribed time give to persons from whose payments tax was deducted the forms that certify the amounts paid to them and the tax deducted, then the Assessing Officer may impose on him a fine of NS 100 in respect of every person to whom the form was not delivered.
- (g) If a person did not submit on time a return under section 135(1), then a fine of NS 200 shall be imposed on him for each month of delay; however, if a date was initially set for delivery by that person of a return under section 135(1), and if subsequently on that person's application a later date was set for submission of the return (hereafter: delayed date), and if that person submitted the return after the delayed date, then a fine of NS 400 shall be imposed on him for each month of delay after the delayed date;
- (h) The amounts stated in this section, as they were on January 1 of the preceding tax year, shall be adjusted on January 1 of every tax year, at the rate of index increase during the preceding tax year; if income ceilings were adjusted in any month under section 120B(b), then the Director may adjust the amounts said in this section, as they were on January 1 of that tax year, as if they were income ceilings.
- (i) Repealed

#### **Saving of criminal responsibility**

189. (a) The payment of a fine under section 188 or the increase of tax rates under section 191B shall not derogate from a person's criminal responsibility under this Ordinance.
- (b) If criminal action was brought against a person for non-submission of a return, then he shall not be charged a fine under section 188 for that offense, and if he has paid an aforesaid fine, then it shall be refunded to him; if a said criminal action was brought and the defendant was acquitted, then linkage differentials and interest, within their meaning in section 159A(a), shall be paid him from the day of the payment of the fine until its refund.

#### **Fine for delay in payment**

190. (a) (1) (a) If a person is more than seven days late in paying an advance which he must pay, or in paying part of it, then to the amount in arrears shall be added a fine in the amount of linkage differentials and interest within their meaning in section 159A(a) (hereafter: linkage differentials and interest), from the day set for the payment until the payment of the amount in arrears, or until the end of the tax year in respect of which the advance was required, whichever is

- earlier (hereafter: end of period of fine).
- (b) To a fine said in subparagraph (a) shall be added linkage differentials and interest from the end of period of the fine until the payment of the fine, and the fine shall be treated like a tax debt for purposes of section 195A.
  - (c) Notwithstanding the provisions of subparagraph (a), if the date for the payment of an advance was postponed under section 175(f) and if a person paid an advance more than four days later than the date prescribed in section 175(a) or than the date prescribed under section 175(b), and if he did not pay the advance by the determining date set in section 175(f), then the fine shall be added to the amount in arrears in accordance with the provisions of subparagraph (a).
  - (d) If a person did not state the date for the payment of the advance, and if therefore the advance was set at a total amount for the entire period, then – for calculation of the fine under this section – the date for payment shall be deemed to be at the midpoint of the period in respect of which the advance was set.
- (2) If a person requested that the amount of his advance payments be reduced and it appears that the tax due according to the return filed by him exceeds the balance of advance payments after the reduction, then he shall pay on the amount of the reduction – but not on more than the difference between the tax due according to the return and the balance of the advance payments after reduction – linkage differentials and interest within their meaning in section 159A(a) from the middle of the tax year or special assessment period until the end of the tax year or special assessment period or, in respect of each payment, until the date of payment, whichever comes first; for this purpose, any amount paid on account of advance payments shall first be placed to the account of the advance.
  - (3) For the purpose of reducing the amount of advance payments in a certain tax year, as said in paragraph (2), other than in respect of participation in the financing of research and development carried out by another person under section 20A(a) or under any other statute, and other than in respect of credit for contributions under section 46A or under any other statute, the tax from the payment of which the assessee was exempted because of the said deduction or credit shall not be taken into account in the calculation of tax in accordance with the return.
  - (4) If an assessee failed to give notice of the beginning of business activity or its change in accordance with section 134, and if he consequently was not required to pay advances as said in section 181, or if consequently the amount of his advance payments was not increased as said in section 180, then he shall be charged linkage differentials and interest in respect of the determining period, for the entire amount of advance payments which he owed, or for the amount by which the Assessing Officer was entitled to increase his advance payments, as the case may be; for this purpose: "**determining period**" – the period that begins in the middle of the period between the opening of the business or of its change and between the end of the tax year or the special assessment period, and that ends at the end of the said year or

- period, as the case may be.
- (5) For purposes of paying linkage differentials and interest, and for purposes of the order in which payments are credited under section 195A, linkage differentials and interest under paragraphs (2) to (4) shall be deemed a tax debt at the end of the tax year or special assessment period, as the case may be.
  - (b) Repealed
  - (c) Repealed
  - (d) A fine imposed under this section shall not be deemed part of the tax paid for purposes of claiming relief under any of the provisions of this Ordinance.

#### **Fine for unlawful set-off of deduction at the source**

190A. If a person deducted from his advance payments a deduction at the source, for which he does not have written certification or which was not deducted during the period permitted under section 177, then he shall be liable to a fine of three times the amount of the improper deduction.

#### **Deficiency fine**

191. (a) In this section, "**deficiency**" – the amount by which the tax which an assessee owes exceeds the tax payable by him according to his return under section 131 or, if he has not submitted such a return, the amount of tax determined under section 145(b), all as the case may be.
- (b) If a deficiency of more than 50% of the tax to which he is liable was found in respect of any assessee, and if he does not prove to the Assessing Officer's satisfaction that he was not negligent in making the return delivered by him or in the non-delivery of a return, then he shall be liable to a fine at the rate of 15% of the amount of deficiency.
  - (c) If the Director or a person empowered by him for this matter has reasonable grounds for believing that the deficiency was created willfully and with the assessee's intent to evade payment of tax, then double the fines specified in subsection (b) shall be added to the amount of tax to which the assessee is liable.
  - (c1) If a final assessment that can no longer be appealed includes – in respect of an act which under section 131(g) was designated tax planning that must be reported – the determination that it must be ignored under the provisions of section 86, then the assessee shall be liable to a fine at the rate of 30% of the shortfall created by the said tax planning; when a said fine is imposed, then no fine shall be imposed in respect of that shortfall under the provisions of subsections (b) and (c).
  - (d) For purposes of sections 149 to 152, the addition of a deficiency fine under this section shall be treated like an assessment.
  - (e) Linkage differentials and interest shall be added to a fine imposed under subsections (b) or (c) after February 28, 1985, from the end of the tax year in respect of which the return was submitted or the assessment made under section 145(b), or from February 28, 1985, whichever is later, and until the day the fine is paid, and the fine shall be deemed a type of debit charge for the purposes of section 195A.

#### **Fines for failure to deduct**

191A. If a person without reasonable justification fails to deduct tax which he is required to deduct under section 161, 164 or 170, then he shall be liable to a fine at the rate of 15% of the amounts which he did not deduct.

**Increase of tax rates for not keeping books**

- 191B. (a) If an assessee is required to keep account books for a certain tax year or part of it and did not keep them, or he kept them only during part of the period during which he was obligated to keep them, or if he did not base his return on account books, then the tax to which he is liable for that year shall be increased by 10% of the amount of the chargeable income in respect of which he was required to keep accounts, and in every subsequent year in which he does not keep account books as aforesaid the tax shall be increased by 20% of the amount of the aforesaid income; however, if a person was first required to keep books in a certain tax year, but first began to do so after the date on which he was required to begin, then the said additions shall only apply to the period during which he was required to keep books and did not do so.
- (b) If an assessee was charged an addition to tax for a certain tax year, then the advance payments for the year during which the assessment for that certain tax year is made shall be increased by 20%, if the addition to the tax is 10%, and by 40% if the addition to the tax is 20%, but if the tax was also increased for the tax year according to which the advance payments were fixed, then the rate of increase of the advance payment shall be reduced by twice the rate of addition to the tax; this provision shall not apply if the assessee proves, to the Assessing Officer's satisfaction, that – in the tax year in which the aforesaid assessment was made – he kept account books or was not required to keep them.

**Fine for false record**

- 191C. If an assessee is required – under directions from the Director by virtue of section 130 – to record identifying particulars of a purchaser who pays cash, based on a document produced by him, and if he does not record them or records incorrect particulars, then a fine of 5% of the amount of the sale in respect of which he violated a said direction shall be imposed on him, or a fine of NS 12,900, whichever is more.

**Director's authority to decrease interest or fine**

192. The Director may reduce the rate of interest or of linkage differentials and interest under sections 186, 187 and 190, and the amount of fine under sections 188, 190, 190A, 191A and 191C, or waive them completely, if it is proved to his satisfaction that the delay which caused the liability to pay was not caused by any act or omission that depended on the assessee's will; the Director may, at his absolute discretion, reduce or waive as aforesaid, if it is proven to his satisfaction that the assessee did not know the exact amount of tax due from him before he filed the return; however, the Director may not reduce the amount of interest or linkage differentials and interest under sections 186, 187 and 190 only because the assessee duly made his advance payments or because tax was duly deducted from him or he paid the tax due from him in accordance with his return when he submitted it.

**Time for paying interest, linkage differentials or fine**

- 192A. The time for the payment of interest, linkage differentials and interest or fines, which the assessee must pay under the provisions of this Ordinance, shall be within 30 days after he was sent notification of that obligation.



## **Article Four: Enforcing Payment**

### **Assessing Officer may enforce payment**

193. If a person is obligated to pay any amount under this Ordinance, then the Assessing Officer may enforce its payment as provided hereafter or under the Taxes (Collection) Ordinance, and the provisions of that Ordinance, except for section 12 there, shall apply to the collection of any said amount as if it were a tax, within its meaning in that Ordinance; however, when the Assessing Officer is not the District Officer, then the Assessing Officer shall forward to the District Officer of the district in which the assessee resides or carries on his business a certificate signed by the Assessing Officer that specifies the amount of arrears due from the assessee, and upon receipt of that certificate the District Officer shall enforce payment under the provisions of the Taxes (Collection) Ordinance that apply to the collection of a said amount.

### **Collection of tax in special cases**

194. (a) If the Assessing Officer has reason to suspect that the tax on a certain income will not be collected because a certain person intends to leave Israel, or because of any other reason, then he may –
- (1) if that person already was assessed in respect of that income or is under obligation to make advance payments on it – demand by written notice that that person immediately provide collateral, to the Assessing Officer's satisfaction, for payment of the tax assessed or of the advance payments he must make;
  - (2) if that person has not yet been assessed as aforesaid – assess him according to the amount of income of which a return was made or, if that person has not made a return or has made a return which does not satisfy the Assessing Officer, in an amount which the Assessing Officer deems reasonable;
  - (3) if that person is not yet obligated to make a return of that income – require him by written notification to prepare a return immediately, and thereafter the Assessing Officer may act as said in paragraph (2).
- (b) If an assessment was made under subsection (a)(2), then the Assessing Officer shall make notification of it, and all the tax assessed under that assessment shall be paid immediately upon delivery of that notification.
- (c) If the assessee did not pay the tax or did not provide the collateral according to subsection (a)(1), then the competent Court may, on the Assessing Officer's application, make an Order even in the assessee's absence –
- (1) to stay his departure from Israel;
  - (2) to attach his property.
- (d) If an assessee paid the tax or provided collateral under this section, then he is entitled to file objection and appeal under sections 150 to 158, and the amount paid by him shall be corrected according to the results.

### **Action by Assessing Officer**

195. An action may be brought by the Assessing Officer in his official capacity for tax and all costs, and it may be recovered in a competent Court from the person who owes it, as if it were a debt to the Government of Israel, and it may be sued for and recovered by the means prescribed in section 193.

## **Article Five: Crediting an Assessee's Payments**

### **Crediting payments**

- 195A.(a) When a person pays any amount on account of a tax debt, a proportional part of the amount paid shall be credited against each type of debit in that tax debt, in the proportion of that type of debit to the entire tax debt; in this context:
- (1) if the person did not specify the amount paid as being on account of his debt as assessee or as deductor, the amount shall be credited against his debt as deductor;
  - (2) a tax refund, which under the Tax Set Off Law 5740-1980 is set off against a tax debt, and an amount collected under the Taxes (Collection) Ordinance or in any other way shall be treated like an amount paid by that person.
- (b) (1) If a person paid an amount on account of a tax debt which he owes as an assessee, without specifying the year of the debt, then the amount shall be credited against his tax debts as assessee according to the years in which they were created, beginning with the earliest tax year;
- (2) if a person paid an amount on account of a tax debt he owes as a deductor, then the amount shall be credited against his tax debts as deductor in the order in which they were created, beginning with the earliest one.
- (c) In this section –
- "tax debt"** – each of the following:
- (1) the total amount of all types of debits owed by a person under this Ordinance, as assessee for a certain tax year;
  - (2) the total of amounts of all types of debits owed by a person under this Ordinance as deductor, in respect of any payment which he paid to another person;
- "type of debit"** – each of the following: tax, interest, linkage differentials.

## **Article Six: Monetary Composition in Respect of Online Returns**

### **Monetary composition**

- 195B. Notwithstanding the provisions of Article Three, if the Director has reasonable grounds to assume that an online return was not submitted up to the date said in section 132 or 166, as the case may be (in this Article: violation), then he may impose a monetary composition on the violator in the amount specified below in respect of each whole month of delay in submitting the return;
- (1) if an individual did not submit an online independent return under section 131(b2) – NS 1,000;
  - (2) if an employer did not submit and employer's online return or if a deductor did not submit a deductor's online return – NS 1,500.

### **Demand for monetary composition and its payment**

- 195C. Monetary composition for a violation under section 195B shall be paid at the

Director's demand on a form he prescribed (hereafter: payment notice) within thirty days after the payment notice was dispatched; the payment notice shall specify, inter alia, particulars of the violation for which the monetary composition was imposed and its amount, and it shall also include information on the right to present arguments to the Director, as said in section 195D.

#### **Writ of arguments**

- 195D. (a) An individual, an employer or a deductor to whom a payment notice was sent may, within thirty days after dispatch of the said notice, submit his written arguments on imposition of the composition and its amount to the Director in writing (in this section: writ of arguments); to the writ of arguments shall be attached an affidavit in support of the facts specified in it.
- (b) When an individual, employer or deductor has submitted a writ of arguments to the Director, then the Director shall decide on the basis of the writ of arguments and of the affidavit whether to leave the payment notice in effect or cancel it, and he may – in order to reach the said decision – summon the person who submitted the writ of arguments to a hearing before him; a notice of the Director's decision under this subsection shall be sent to the person who submitted the writ of arguments.
- (c) Submitting the writ of arguments under this section shall not stay payment of the monetary composition at the time said in section 195C.
- (d) If the monetary composition was paid and the Director decided under this section to cancel the payment notice, then the monetary composition shall be refunded with linkage differentials and interest within their meaning in the Interest and Linkage Adjudication Law 5721-1961 (in this Article: the Interest Adjudication Law) from the day of its payment until the day of its refund.

#### **Updating the amount of monetary composition**

- 195E. (a) Monetary composition shall be at its updated amount on the day the payment notice is dispatched, and if a petition was brought and the Court that heard the petition ordered its payment to be stayed – at its updated amount on the day of the decision on the petition.
- (b) The amount of monetary composition shall be updated on January 1 of each year (in this section: the updating day) at the rate of increase of the index known on the updating day over the index that was known on the updating day of the preceding year, and in respect of the first updating day – over the index that was known on January 1, 2008; the said amount shall be rounded to the nearest amount that is a multiple of NS 10.
- (c) The Director shall publish the updated amount of the monetary composition in a notice in Reshumot.

#### **Linkage differentials and interest**

- 195F. If monetary composition was not paid on time, then linkage differentials and interest shall be added to it, within their meaning in the Interest Adjudication Law, for the arrears period up to its payment (in this Article: arrears supplement).

#### **Collection**

- 195G. The Taxes (Collection) Ordinance shall apply to collection of the monetary composition and of the arrears supplement.

**Reserving criminal liability**

- 195H. (a) Payment of monetary composition shall not derogate from the individual's, employer's or deductor's criminal liability for the violation.
- (b) If an indictment under section 216(4) or (4a) was brought against an individual, employer or deductor for a violation, then he shall not be obligated to pay monetary compensation for it, and if he paid, then the amount paid shall be refunded to him with the addition of linkage differentials and interest, within their meaning in the Interest Adjudication Law, from the day of its payment until the day of its refund.

**Petitioning the Administrative Affairs Court**

- 195I. (a) Petitioning the Administrative Affairs Court against the imposition of monetary composition under this Article, in accordance with section 32(5) of the Administrative Affairs Courts Law 5760-2000, shall not stay payment of the monetary composition, except with the Director's consent or if the Court so ordered.
- (b) If a petition said in subsection (a) was accepted after the monetary composition was paid, then the monetary composition shall be refunded with the addition of linkage differentials and interest, within their meaning in the Interest Adjudication Law, from the day of its payment until the day of its refund

**CHAPTER THREE: DOUBLE TAXATION RELIEF****Article One: Reciprocal International Agreement****Order that gives effect to agreement**

196. (a) When the Minister of Finance has given notice by Order, that an agreement specified in the Order was concluded with a certain state to afford double taxation relief on income tax and on every other tax of a similar character imposed by the Laws of that state (hereafter: reciprocating state) and that it is expedient to give that agreement effect in Israel, then that agreement (hereafter: agreement) shall have effect in relation to income tax, notwithstanding any provision of any statute.
- (b) An Order made under this section may be revoked by a subsequent Order.
- (c) In this section, A**State**@ – including areas outside Israel that are not a State, enumerated in Schedule One AA1@.

**Obligation of secrecy in case of agreement**

197. When an agreement has been given effect as said in section 196, then the obligation to maintain secrecy imposed by section 234 shall not prevent disclosure – to an authorized officer of the reciprocating state – of any information that is to be disclosed under the agreement.

**Power to make regulations**

198. The Minister of Finance may make regulations for implementation of the provisions of an agreement.

## **Article Two: Determining Amount of Relief**

### **Definitions**

199. In this Chapter –

**"income tax"** – exclusive of companies tax;

**"Israel taxes"** – income tax and companies tax;

**"foreign taxes"** – taxes payable by an Israel resident to tax authorities of a state other than Israel, on income produced or accrued in that state, including taxes payable to states that are parts of a federal state or to regional authorities that are parts of that state, calculated as percentages of the income and exclusive of municipal taxes;

**"foreign income"** – income produced or accrued abroad;

**"foreign income from a certain source"** – foreign income, classified by the sources of income prescribed in section 2, in Part Five or in Part Five "C", less expenses that may be deducted from them and losses that may be set off against them, all in accordance with the provisions of the Ordinance.

### **Provisions on crediting double taxation**

200. (a) Foreign taxes paid on foreign income that is chargeable to tax in Israel, shall – translated into new shekel amounts – be allowed as credits against Israel taxes under this Ordinance, in accordance with the provisions of this Article.
- (b) Israel taxes shall be credited in a certain tax year only if the person whose income is chargeable to those taxes was an Israel resident in that tax year.
- (c) The Director may prescribe rules for the implementation of this Article and rules on the matter of returns.

### **Deduction of foreign taxes**

201. (a) Foreign taxes paid in respect of foreign income that is tax exempt in Israel shall not be deducted.
- (b) The relief granted in respect of dividends under section 163 shall be deemed a reduction of the amount of tax which applies to that dividend under the Ordinance.

### **Credit against companies tax precedes credit against income tax**

202. If an agreement permits credit against companies tax and income tax, then the amount of credit shall be used first to reduce companies tax on that income and – to the extent that all of it cannot be used for that purpose – it shall be used to reduce income tax on it; if the agreement allows credit only against income tax, then section 201 shall be construed as if it said "income tax" instead of "Israel taxes".

### **Amount of credit against companies tax**

203. (a) The amount of credit against companies tax, to which an Israel resident body of persons is entitled under the provisions of this Article in respect of foreign income from a certain source shall not exceed the amount of companies tax to which it is liable on that income.
- (b) If the foreign income includes dividends, in respect of which the assessee company, as defined in section 126(c), requested that it pay tax at the rate prescribed in section 126(a), or if – under an agreement to prevent double taxation – the foreign taxes paid on that dividend and which were not imposed directly must be taken into account as credits,

then the grossed up dividend shall be added to all of the company's income and credit shall be given in the amount of the foreign taxes that were not imposed directly on that dividend, in addition to the foreign taxes; the total credit in this section shall not exceed the amount of tax that applies to the said dividend.

- (c) In this section –  
    **"foreign taxes not imposed directly"** – taxes paid by a foreign resident body of persons on income which, after the payment of tax, was distributed as a dividend;  
    **"grossed up dividend"** – the amount of income from a dividend received after tax was deducted at the source, plus the tax deducted at the source, plus foreign taxes not imposed directly.

#### **Amount of credit against income tax**

204. (a) The amount of credit against income tax to which an Israel resident individual is entitled under the provisions of this Article in respect of foreign income from a certain source, which is ordinary income, shall not exceed the credit ceiling in respect of that income.
- (b) The amount of credit against income tax to which an Israel resident individual is entitled under the provisions of this Article on foreign income from a certain source, which is chargeable to tax at a special rate, shall not exceed the amount of tax that applies to that income in Israel.
- (c) In this section –  
    **"ordinary income"** – chargeable income, on which no special tax rate is imposed;  
    **"income ratio"** – the ratio obtained by dividing the amount of foreign income from a certain source that is ordinary income, by the total amount of ordinary income;  
    **"special tax rate"** – a tax rate that applies in Israel and is different from the tax rate prescribed in section 121;  
    **"credit ceiling"** – the amount obtained by multiplying the income ratio by the amount of income tax on the individual's total ordinary income before any credit under this Article was granted.

205. Repealed

#### **Excess credit in a tax year**

- 205A. (a) If the amount of foreign taxes paid in respect of foreign income from a certain source exceeds the amount of credit granted in its respect against Israel taxes (in this section: excess credit), then the assessee is entitled to subtract the excess credit from tax to which he will be liable in respect of income produced abroad from the same source in the following five years, one after the other, adjusted at the rate of the index increase from the end of the tax year in which it was created to the end of the tax year in which it was subtracted; the excess credit shall be subtracted in accordance with this section, subject to the provisions of this Chapter, mutatis mutandis.
- (b) Notwithstanding the provisions of subsection (a), if an excess credit was created because of the set off of a loss that stems from foreign income from a certain source against foreign income from another certain source, then in the five coming years, one after the other, it may also be subtracted from the tax on foreign income from the source from which the said loss stems, adjusted as said in that subsection.

### **Rules for computing income for purposes of credit**

206. When calculating foreign income that is chargeable to tax in Israel, no deduction from it shall be allowed in respect of foreign taxes.

### **Credit for tax on dividend in special cases**

207. If the agreement provides, in respect of certain categories of dividends, but not in respect of others, that foreign taxes not imposed on them directly or by deduction are to be taken into account for purposes of credit against Israel taxes on them, and if a dividend paid is not of the said specific categories, then – if the dividend was paid to a company which directly or indirectly controls at least half the voting power in the company that pays the dividend – the credit shall be allowed as if the dividend belonged to one of those specific categories.

### **Credit for dividend**

- 207A. (a) If an Israel resident body of persons received a dividend from a body of persons, which is considered an Israel resident only because its business is controlled and managed from Israel (in this section – the other body) and if tax from the dividend was deducted at the source in the foreign state, then the other body shall be entitled to credit in the amount of the tax deducted at the source as aforesaid, against the companies tax that applies to it; the amount of the credit shall not exceed the companies tax that applies in that tax year, but an unused balance of the credit may be used against companies tax that will be imposed on the other body in the following five years, one after the other.
- (b) If an Israel resident individual received a dividend from the other body and tax at the source was deducted in the foreign state, then the individual shall be entitled to a credit in the amount of tax deducted at the source, against the tax that applies to his income from the said dividend, all subject to the provisions of this Chapter.

### **Credit for foreign taxes**

207B. Foreign tax can be credited against Israel tax that applies in a tax year only if it was paid in the foreign state no later than 24 months after the end of that tax year, except for tax that was supposed to be paid on unpaid profits, as defined in section 75B; foreign tax paid in the foreign state after the said period may be deducted in the tax year in which it was paid in the foreign state, against tax due in Israel on foreign income from the same source, and the provisions of this Chapter shall apply to it, mutatis mutandis; in the case of disagreement on the amount of the credit, the applicant for the credit has the right of objection and appeal, as said in sections 150 and 153, as part of an objection and appeal against the assessment made for him.

### **Credit for foreign taxes – employee of a certain employer**

207C. If an individual has income, the place of production of which is in Israel only because of the provisions of section 4A(b)(1), then for purpose of the provisions of this Article the individual's income shall be deemed foreign income and the taxes paid to tax authorities in the foreign state in respect of that income shall be deemed foreign tax.

### **Restriction on credit**

207D. When a loss from a controlled business has been set off against income in Israel, as said in section 29(2)(c) or (e), then no credit shall be given under

this Chapter against Israel taxes, to which the Israel resident is liable in respect of chargeable income he had from a business abroad during the two years before the tax year in which the loss was set off and in the five years thereafter, one after the other, up to the amount of the loss set off as aforesaid.

#### **Waiver of credit**

208. Credit against Israel taxes to which a person is liable in a tax year shall not be allowed, if he requested that no credit be given against his income in that year; if he so requested, then the provisions of section 205A shall not apply.

209. Repealed

#### **Error in calculating credit**

210. If the amount of credit is found to have been set too high or too low, in consequence of a change in the amount of tax payable in Israel or abroad or because of the provisions of section 207D, then no provision of any statute that limits the time for making assessments or claims for relief shall apply to an assessment or claim to which the change gave rise, if it was made not later than two years after the assessments, changes and other decisions – in Israel or abroad – which matter in respect of the question whether any credit is to be given and what it shall be.

### **Article Three: Miscellaneous Provisions**

#### **Definitions**

211. In this Article –

**"double taxation relief"** – any credit for income tax abroad, allowed for purposes of income tax under this Ordinance, including any credit or relief taken into account in determining the net Israel rate to be levied on dividends received;

**"rate of relief"** – the rate, which is the rate of the excess tax deducted from the dividend, over the net Israel rate.

#### **Effect of relief on set off and refund**

212. When the tax payable by a company is affected by double taxation relief, then the amount to be set off under section 163 or to be refunded under section 160 in respect of the tax deducted by the company from any dividend paid by it shall be reduced according to the following rules:

- (1) If the recipient of the dividend is not liable to tax on it, then the reduction shall be in an amount equal to the tax on the grossed up dividend, at the rate of relief applicable to it;
- (2) if the rate of tax to which the recipient is liable in respect of the dividend is less than the rate of relief applicable to it, then the reduction shall be in an amount equal to the tax on the grossed up dividend, calculated at the difference between those two rates.

#### **Place of dividend in scale of income**

213. For purposes of section 212:

- (1) if the income includes one dividend said in section 212, then it shall be deemed to be in the highest bracket of the income;
- (2) if the income includes several aforesaid dividends, then any dividend,



- the net Israel rate of which is lower than that of another dividend shall be deemed to be in a higher bracket in the scale of income;
- (3) if tax a dividend is chargeable at different rates on its different parts, or if the tax is chargeable on one part of a dividend and not on another part of it, then each part shall be treated like a separate dividend.

**Double taxation relief on a resident's foreign income**

214. (a) In respect of an Israel resident's income, the source of which is abroad and on which income tax or a similar tax is charged at its source, the Minister of Finance may, by Order, grant double taxation relief by exempting the income from paying all or part of the tax, as shall be specified in the Order.
- (b) The provisions of this section shall not derogate from the powers under section 196.

## **PART ELEVEN: PENALTIES**

**Offenses for which no penalty is specifically provided**

215. If a person is guilty of an offense against this Ordinance or against a regulation made thereunder, and if no other penalty is specifically provided for that offense, then he shall be liable to one year imprisonment or to a fine, or to the fine said in section 61(a)(2) of the Penal Law 5737-1977 (in this Part: Penal Law), or to both penalties.

**Failure to notify of beginning or change of occupation**

- 215A. (a) If a person opened a business or began to exercise a vocation and did not inform the Assessing Officer of that fact in time and also did not submit on time the first annual return, which he is required to submit after the said events, then he shall be liable to three years imprisonment or to the fine said in section 61(a)(3) of the Penal Law, and to one and a half times the tax to which he was liable.
- (b) If a person opened a business in or began to exercise a vocation in an additional place or if he changed his place of business or the place where he exercises his vocation and did not notify the Assessing Officer in time and also did not submit on time the first annual return he is required to submit after the said events, then he shall be liable to eighteen months imprisonment or to the fine said in section 61(a)(3) of the Penal Law, and to one and a half times the tax to which he was liable.

**Non-compliance with certain requirements, etc.**

216. If a person, without sufficient cause, committed one of the following offenses, then he shall be liable to one year imprisonment, or to the fine said in section 61(a)(2) of the Penal Law, or to both penalties:
- (1) he did not comply with a demand included in a notification given to him under this Ordinance;
- (2) he did not appear, as required by a notification under this Ordinance or, he did appear, but did not answer a question lawfully put him;
- (3) he refused to accept a notification sent to him under this Ordinance;
- (4) he did not submit a return under section 132 or 133 in time;
- (4a) he did not submit on time a deductor's online return or an employer's

- online return under the provisions of section 166;
- (5) he did not keep account books in accordance with directions by the Director under section 130(a);
- (6) he destroyed or concealed documents of value for the assessment;
- (7) he records intakes on a cash register tape, receipt vouchers, invoices, a daily intake ledger or other documentation under the Director's directions by virtue of section 130, and did not record there an intake which he was obligated to record under those directions; if the intake was not recorded by the assessee's employee or by the assessee's representative who is not his employee, then the employee or representative shall be accused of the offense, and the assessee shall be accused of it, unless he proves that the offense was committed without his knowledge and that he took all reasonable steps to ensure its prevention;
- (8) he did not report an act that constitutes tax planning that must be reported in a return, as said in section 131(g), in violation of the provisions of section 131(a)(5d) or (b1) or (g).

**Assault or obstruction in performance of duty**

- 216A.(a) If a person assaults a person who performs any function or is employed in the implementation of this Ordinance, with the intent to obstruct him, or while the aggressor is armed with a firearm or other instrument, then he shall be liable to five years imprisonment or to the fine said in section 61(a)(4) of the Penal Law.
- (b) If a person performs any act intended to obstruct any person said in subsection (a) in the due performance of his function shall be liable to three years imprisonment or to the fine said in section 61(a)(3) of the Penal Law.

**Transfer of assets with intent to prevent collection of tax**

- 216B. (a) If a person transferred his assets to another without transferring control thereof, with the intention to prevent the collection of tax to which he is liable or may become liable in respect of a period before the transfer or in the year of the transfer, or in respect of a type of income the production of which has begun but lasts several years, then he – or if the transferor is a body of persons, the person who effected the said transfer – shall be liable to two years imprisonment or to the fine said in section 61(a)(3) of the Penal Law.
- (b) If a person distributed a company's assets among its members with the intention to prevent the collection of tax to which the company is liable or to which it may become liable in respect of a period before the transfer or in the year of the transfer or in respect of a type of income the production of which has begun but lasts several years, then he shall be liable to two years imprisonment or to the fine said in section 61(a)(3) of the Penal Law, on condition that the amount of the fine not exceed the amount of the debt.

**Unlawful representation**

- 216C. If a person violates one of the provisions of section 236, then he shall be liable to one year imprisonment or to the fine said in section 61(a)(4) of the Penal Law 5737-1977, or to both penalties.

**Incorrect return and information**

217. If a person, without reasonable justification, makes an incorrect return by

omitting or understating income of which he is required to make a return under the Ordinance, or if a person gave incorrect information in relation to any matter or thing that affects his own liability to tax or the liability of any other person or of a partnership, then he shall be liable to two years imprisonment or to the fine said in section 61(a)(3) of the Penal Law, plus the amount of income missing in consequence of that incorrect return or information, or which would have been missing if the return or information had been accepted as correct, or to both penalties; if the person argues that he had reasonable justification, then he shall bear the burden of proof.

**Non-deduction of tax**

218. If a person did not deduct tax which he is required to deduct under sections 161, 164 or 170, or if a person received work income or income under section 2(5), knowing that tax was not deducted from it under those sections, then he shall be liable to one year imprisonment or to the fine said in section 61(a)(2) of the Penal Law, plus double the total of all the amounts not deducted, or to both penalties.

**Failure to transmit deducted tax**

219. If tax was deducted under sections 161, 164 or 170 and without reasonable justification it was not paid to the Assessing Officer as said in sections 161, 166 or 171, then the person required to make the deduction shall be liable to two years imprisonment or to the fine said in section 61(a)(3) of the Penal Law, and to double the total of all aforesaid deductions, or to both penalties; if he argues that he had reasonable justification, then he shall bear the burden of proof.

**Fraud, etc.**

220. If a person willfully commits one of the offenses specified below with the intent to evade tax or to assist another person to evade tax, then he shall be liable to seven years imprisonment or to the fine said in section 61(a)(4) of the Penal Law and double the amount of income which he concealed, intended to conceal or helped to conceal, or to both penalties; and these are the offenses:

- (1) he omitted from a return made under the Ordinance any income which must be included in the return;
- (2) he made a false statement or entry in a return under the Ordinance;
- (3) he gave a false answer, verbal or written, to a question asked or to information requested of him in under the Ordinance;
- (4) he prepared or maintained or allowed another to prepare or to maintain false account books or other false records, or he falsified or allowed falsification of account books or records;
- (5) he made use of any fraud, artifice or contrivance or allowed use of them;
- (6) he presented a false document to the person who paid the income, in order to prevent or reduce the deduction of tax at the source.

**Linkage of amount on which fine is imposed**

220A. For purposes of a fine under this Part or under Part Ten, the basis of which is an amount of income, the basis shall be increased in proportion to the increase of the consumer price index, from the index last published before the end of the tax year to which that basis relates, to the index last published before the fine is imposed.

**Payment of fine or of composition imposed on another person**

220B. A body of persons shall not pay, directly or indirectly, any fine or composition imposed on another person in respect of an offense under sections 215 to 220; whoever violates the provision of this section shall be liable to a fine three times the amount of the fine or composition paid; for this purpose: "**body of persons**" – exclusive of a body of persons, the members of which must place their full working capacity at its disposal and who must transfer their assets to it.

**Monetary composition**

221. If a person committed an offense under sections 215 to 220, the Director may – with that person's consent – accept from him monetary composition that does not exceed double the highest fine that can be imposed for that offense, and when he has done so, any legal proceeding against that person in respect of that offense shall be discontinued, and if he was under arrest for it he shall be released.

**Burden of proof**

222. (a) If a person is charged with an offense under section 216(4), then he bears the burden of proof that he does not have to deliver a return.
- (b) If a person is charged with an offense under section 216(6), then he bears the burden of proof that the documents he destroyed or concealed are of no value for the assessment.
- (c) If a person, to whom the provisions of section 161, 164 or 170 apply, is charged with an offense under sections 218 or 219, then he bears the burden of proof that he has complied with the said provisions.

**Presumption of guilt**

223. If a person is charged with the offense of omitting or understating income under section 217, then his guilt shall be deemed to have been established prima facie, if one of the following has been proven:
- (1) domestic or other personal expenditures incurred in the tax year exceeded the income of which a return was made to the Assessing Officer;
- (2) his capital or the capital of his spouse or of their children under age 20 increased during a certain period of not more than five years by an amount greater than the amount of the income of which the spouses or one of them made a return or returns for that period to the Assessing Officer, less tax that was paid.

**Responsibility of a person who helps to prepare return**

224. If a person helps another person to prepare any return, notification or other document for the purposes of this Ordinance, knowing that that return, notice or document contains incorrect information, or if a person appears as the representative of an assessee and gives information for the purposes of this Ordinance, knowing that it is incorrect, then he shall – for the purposes of sections 215 to 217 and 220 – be deemed to have committed the said acts.

**Responsibility of director, etc.**

- 224A. If a body of persons committed an offense under sections 215 to 220, then every person who was an active director or a partner, accountant, responsible officer, trustee or representative of that body when the offense was committed, shall also be deemed guilty thereof, unless he proves one of these –
- (1) that the offense was committed without his knowledge;

- (2) that he took all reasonable steps to ensure prevention of the offense.

**Prescription**

225. A criminal action under this Ordinance shall not be brought later than six years – or in the case of an offense against the provisions of section 220, ten years – after the tax year in which the offense was committed.

**Penal proceedings do not exempt from payment of tax**

226. The opening of proceedings for the imposition of a penalty, fine or imprisonment under the Ordinance or their imposition thereunder does not relieve any person of the obligation to pay tax to which he is or may be liable.

**Investigations and searches**

227. The Minister of Police may authorize an Assessing Officer to carry out investigations or searches in order to prevent or to detect offenses against this Ordinance, and an Assessing Officer authorized as aforesaid may –
- (1) exercise every power vested in an police officer of the rank of inspector or above under section 2 of the Criminal Law Procedure (Evidence) Ordinance and sections 3 and 4 of the said Ordinance shall apply to a statement taken by him as aforesaid;
  - (2) exercise the powers of a policeman under section 17(1)(a) of the Criminal Law Procedure (Arrest and Searches) Ordinance, except for the power to seize property other than documents;
  - (3)
    - (a) exercise the power of an officer in charge, within its meaning in section 9 of the Criminal Law Procedure (Arrest and Searches) Ordinance [New Version] 5729-1969, release a person on bail, and sections 10 to 15 of the said Ordinance shall apply to this matter;
    - (b) if a suspect was released on bail under subparagraph (a) and no indictment was brought against him within 180 days after his release, then he and his guarantors shall be released from their bail, and the provisions of section 55(b) of the Criminal Law Procedure Law [Consolidated Version] 5742-1982 shall apply to this matter.

**Saving of other Laws**

228. The provisions of this Ordinance shall not affect any criminal proceeding under another Law.

**Publication of list of offenders**

- 228A. Once a year the Director may publish a list of all assessees convicted in the preceding year, by final judgment, of an offense under section 220; the said publication shall be in at least two daily newspapers.

## PART TWELVE: GENERAL PROVISIONS

**Appointment of executive authority**

229. For the proper implementation of the Ordinance the Minister of Finance may appoint a Director, Assessing Officers and other officers or persons, all according to the need.

**Powers of the Director**

230. The powers of an Assessing Officer shall also vest in the Director.

**Order to appear**

230A. If a person was lawfully required – on at least two occasions at least 30 days, but not more than one year apart – to appear before the Assessing Officer, and if he did not do so and did not inform the Assessing Officer of reasonable grounds for his nonappearance, then a Judge or Registrar of a Magistrates' Court may, on the Assessing Officer's application, make an Order that obligates him to appear before the Assessing Officer at the time and place stated in the Order.

**Obligation of confidentiality**

231. (a) A person who has an official position in the implementation of the Ordinance or is employed in its implementation must regard all documents, information, returns, assessment lists or copies thereof, which relate to the income or to an item of the income of any person, as secret matter and as a personal confidence, and he must treat them as such.
- (b) Notwithstanding the provisions of subsection (a), a man or a woman is entitled to the disclosure of every particular in the return submitted by his or her spouse under section 131 or under section 135, and also to disclosure of the amount of income determined by the Assessing Officer or the Court, all in respect of the period during which they were married and lived together.

**Income tax employee shall not be required to reveal a secret**

232. A person appointed under the provisions of the Ordinance or employed in its implementation shall not be required to show to a Court any return, document or assessment, or to divulge or communicate to a Court anything that came to his knowledge in connection with the performance of his duties under the Ordinance, except to the extent necessary for the implementation of provisions of the Ordinance, or with the intention to bring action for an offense related to income tax, or in the course of hearing such an action.

**Publication of list of assessees**

233. (a) The Minister of Finance may publish a list of all assessees in a manner and in a place to be determined by him, and in it shall be specified the amount of chargeable income of each in a certain tax year, as stated in the return made by him or as determined by the Assessing Officer or by the Court, all as the case may be; if a change occurred in the said list in consequence of an objection or appeal lodged by an assessee, then the list shall be corrected accordingly on the assessee's application; every person is entitled to inspect the list that was published as aforesaid at prescribed times and places and also to receive a certified copy of all or of part of the list against a prescribed fee.
- (b) Notwithstanding the provisions of subsection (a), the Minister of Finance may – with approval by the Knesset Finance Committee – refrain from including a certain category of assessees in the list of assessees that is to be published as aforesaid.

**Penalty for disclosing an income secret**

234. If a person has possession or control of documents, information, returns, assessment lists or their copies, which relate to the income of a person or to a particular of his income, and if he at any time communicates or tries to

communicate aforesaid information or any contents of those documents to a person to whom the Minister of Finance did not permit him to communicate it, or if he communicates it not for purposes of this Ordinance, then he shall be liable to six months imprisonment or to a fine of NS 12,900.

#### **Restrictions on duty to give information**

235. (a) Statutory provisions that obligate to deliver information about another person's property or income, other than a said provision under the Statistics Ordinance [New Version] 5732-1972, shall not apply to any person who performs an official function or is employed in the implementation of the Ordinance, unless the Ordinance expressly so provides.
- (b) Notwithstanding the provisions of subsection (a), it is permitted to disclose information to the National Insurance Institute under the provisions of section 384A of the National Insurance Law [Consolidated Version] 5755-1995.
- (c) Notwithstanding the provisions of subsection (a), when an Order has been made under section 60A of the Bankruptcy Ordinance [New Version] 5740-1980, then it is permitted to reveal to the Official Receiver or to the Court, within their meaning in the said Ordinance, returns, information or documents specified in the said section and according to its provisions.
- (d) The provisions of sections 231, 232 and 234 shall apply, mutatis mutandis as the case may be, to every person who performs an official function in respect of information he received under this section –
- (1) in the implementation of the National Insurance Law [Consolidated Version] 5755-1995;
  - (2) in the implementation of the Bankruptcy Ordinance [New Version] 5740-1980.

#### **Interpretation**

235A. For purposes of sections 235B to 235E:

**"professional secret"** – communications between a client and an advocate, whether oral or written, which is substantively connected to the professional service rendered by the advocate to the client, including records prepared by the advocate for his own use, on condition that they are substantively connected to the said professional service;

**"privileged document"** – a document that includes a professional secret;

**"Court"** – the District Court, in whose area of jurisdiction is located the office of the advocate who claims privilege;

**"judge"** – the president or relieving president of a Court.

#### **Power to demand documents from advocate**

235B. Notwithstanding the provisions of the Chamber of Advocates Law 5721-1961, an advocate must, if he is called upon to do so by an Assessing Officer, deliver to him any document in his possession, enable him to examine and seize any aforesaid document and allow him to perform any other act in respect of a said document, all in accordance with the powers vested in him under this Ordinance, but the advocate shall not have to do so if he claims that the document is privileged.

#### **Claim of privilege**

235C. (a) If an advocate claims that a document demanded by an Assessing Officer is privileged, then the Assessing Officer shall take the document

and – without inspecting it – place it immediately and in the advocate's presence in a package, close it, write on it the name of the client to whom the document relates, sign it and deliver it to the Court; if privilege is claimed for several documents that relate to the same client, then he shall place all in the same package; the advocate may also, if he so desires, sign the package, and he may accompany the Assessing Officer when he delivers the package to the Court; for the present purpose: "**package**" – an envelope or any other container.

- (b) If, for any reason, it is impossible to deliver the package to the Court, then the Assessing Officer shall deliver it to a judge, and he shall deliver it to the Court; for the present purpose: "**judge**" – including a judge of a District Court and a magistrate.
- (c) Not later than seven days after the date on which a document said in subsection (a) was taken, the client or the advocate from whom the document was taken may apply to the Court to decide and announce whether the document is privileged.

#### **The Court's decision**

- 235D. (a) A judge, within whose jurisdiction an application said in section 235C(c) was received, shall hear the application and examine the document not later than seven days after the date on which the application was received; the judge shall hear the advocate and he may also hear the Assessing Officer, without showing the document or disclosing its contents to him.
- (b) If the judge decides that the document is privileged, he shall return it to the advocate from whom it was taken; if he decides that it is not privileged, he shall deliver it to the Assessing Officer.
  - (c) If the judge decides that the document is partly privileged, then he shall direct that a copy of the non-privileged part, certified by him, be delivered to the Assessing Officer; a said copy, delivered to the Assessing Officer, shall be admitted in evidence in any legal proceeding, as if it were the original.
  - (d) If the Court did not receive an application said in section 235C(c) about any document in a package delivered to it, then it shall deem the document for which no application was submitted to be non-privileged and it shall be delivered to the Assessing Officer.
  - (e) An application said in this section shall be heard in camera and the judge's decision shall be final.

#### **Permission to represent assesseees**

236. The following may represent assesseees, and for this purpose: "**represent**" – also before a books acceptability committee:

- (1) an auditor, within the meaning of the term in the Auditors Law 5715-1955;
- (2) a person qualified to audit the books of a cooperative society under section 20 of the Cooperative Societies Ordinance;
- (3) a representative tax consultant, as defined in the Regulation of Representation by Tax Consultants Law 5765-2005;

this provision shall not infringe the rights of any advocate under the Chamber of Advocates Law 5721-1961.

236A to 236I – Repealed



**Signature on notifications**

237. (a) Every notification, which an Assessing Officer must make or send under this Ordinance, shall be signed by him or by a person appointed by him for that purpose, and every notification on which a said signature is printed or written, or on which the Assessing Officer's name is written, is valid; however, every notification under this Ordinance, in which it is demanded that a person or a witness appear before the Assessing Officer, shall be signed in person by the Assessing Officer or by a person duly authorized by him.
- (b) A signature on any notification, that purports to be the signature of a person appointed for that purpose, shall be deemed to be that person's signature, as long as the opposite has not been proven.

**Service of notifications**

238. (a) A notification may be served on a person either in person or by registered mail to his last known business address or private residence; if sent by registered mail, it shall be deemed a notification served on the sixth day after the day of its dispatch, if sent to a person in Israel, or – if it was sent to persons outside Israel – on the day after the day on which it would have arrived if sent by mail in the ordinary way, and in order to prove service in this manner it shall suffice to prove that the letter that contained the notification was properly sent and properly addressed.
- (b) If a notification was sent as said in subsection (a) and the addressee refused to accept it, then it shall be deemed to have been duly served.

239. Repealed

**Rounding off**

240. In calculating an amount of chargeable income and every amount which a person must pay under this Ordinance, that amount shall be increased or decreased to the nearest whole new shekel.

**Rules for the conversion of foreign income and losses**

- 240A. The Director may prescribe conversion rules, according to which an assessee's income, chargeable income, losses, expenses and tax payments that stem from abroad shall be translated into new shekel amounts.

**Forms, information and returns**

- 240B. (a) Subject to the provisions under section 243(1), the Director may prescribe the forms needed for implementation of this Ordinance; said forms do not have to be published in Reshumot and they shall be published in a manner prescribed by the Director; when the Director has prescribed said forms, then no person shall use any others.
- (b) If an assessee is required to deliver information or a return under this Ordinance, he shall deliver the information or return by magnetic media, if the Director so required, all as the Minister of Finance prescribed with approval by the Knesset Finance Committee.

**Designating the tax year**

241. A special assessment period shall be designated by the number of the year in which April 1 of that special assessment period falls.

**Effect of Law concerning trade with the enemy or with absentees**

242. If the Trading with the Enemy Ordinance 1939, the Absentees' Property Law 5710-1950 or any other statute that deals with trade with the enemy or with

absentees affects a person, an income or an asset, then the provisions in Schedule Two shall apply.

#### **Power to make regulations**

243. The Minister of Finance may make regulations for the implementation of the provisions of this Ordinance, especially including regulations on –
- (1) forms for returns, claims, statements and notifications under this Ordinance;
  - (2) the deduction at the source and payment of tax in respect of benefits and pensions paid out of the State Treasury, on work income or on income under section 2(5);
  - (3) any matter on which the Ordinance authorizes him to prescribe.

#### **Power to change deductions and credits**

244. The Minister of Finance may – by an Order that requires the Knesset's approval by a resolution – change the rates of the deductions and credits specified in this Ordinance.

#### **Special powers**

- 244A. The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe conditions and necessary adjustments for the purposes of sections 5, 29, 64A1 to 64A10, 67B to 67K, 68A, 75C to 75Q, 85A, 91, 92, 100A, 102 and Chapter Three of Part Ten.

#### **Prohibition of reductions and concessions**

245. (a) Deductions or set offs shall not be allowed, and exemptions, tax reductions or other concessions shall not be granted, unless they are expressly prescribed in a Law or by virtue of a power defined in a Law.
- (b) Notwithstanding the provisions of subsection (a), the Minister of Finance may, with approval by the Knesset Finance Committee, make regulations for the grant of aforesaid concessions, but their effect shall expire three months after the date of their publication; however, the Minister of Finance may, with aforesaid approval, extend their effect until the end of the tax year in which they were published.
- (c) (1) The Minister of Finance may, with approval by the Knesset Finance Committee, prescribe for each tax year a ceiling for tax benefits to be allowed in the tax year under sections 20 and 20A, and he may prescribe separate ceilings for categories of benefits; the ceiling for benefits in respect of oil prospecting shall be set after consultation with the Minister of Energy and Infrastructure.
- (2) No regulations shall be made and no certification issued under sections 20 or 20A in a certain tax year, if that increases the total of tax benefits allowed in that year by virtue of the said sections to more than the ceiling amount set by the Minister of Finance for that tax year.

### **SCHEDULE ONE**

(Section 11)

#### **Part One**

Avivim, Abirim, Even Menahem, Idmit, Or Haganuz, Eilon, Alkosh, Bet Hillel, Baram, Betzet, Bar Yochai, Goren, Gush Halav, Gaaton, Granot Hagalil, Gesher Haziev, Dovev, Dishon, Dalton, Dan, Dafna, Hagoshrim, Hila, Ziev Hagalil, Zarit, Hossen, Hanita, Hurfeish, Yaara, Yiftah, Yiron, Kabri, Kfar Blum, Kfar Giladi, Kfar Yuval, Kfar Szold, Kerem Ben Zimra, Liman, Metulla, Miron, Malkieh, Manot, Manara, Meona, Meilya, Mayan Baruch, Maalot Tarshiha, Matzuba, Margaliot, Misgav Am, Matat,

Neot Mordechai, Nahariya, Netuah, Sasa, Saar, Safsufa, Evron, Ein Yaacov, Alma, Amir, Aramshe, Fassuta, Pekiin, New Pekiin, Tzivon, Tzuriel, Rag'el, Rosh Hanikra, Reihaniya, Ramot Naftali, Shear Yishuv, Sdeh Eliezer, Sdeh Nehemya, Shomera, Shlomi, Shamir, Snir, Shetula.

## Part Two

Avshalom, Or Haner, Ibim, Eilat Regional Council, Erez, Beeri, Bet Shean, Gibim, Gvaram, Dekel, Zikim, Zimrat, Holit, Hatzor Gilit, Yevul, Yad Mordehai, Yachini, Yesha, Yeted, Kissufim, Kfar Maimon, Kfar Aza, Carmiah, Kerem Shalom, Mivtahim, Magen, Mefalsim, Nahal Oz, Nir Yitzhak, Nir Oz, Nir Am, Nirim, Netiv Ha'assara, Suffa, Saad, Ein Habsor, Ein Hashlosha, Alumim, Amioz, Central Arava Regional Council, Arad, Pri Gan, Re'im, Sdeh Avraham, Shuva, Shokda, Tushia, Talmei Yosef, Tekuma.

## SCHEDULE ONE "A"

(Section 75C)

- (1) FOUNDATION – under the Laws of Holland, Liechtenstein, Panama, the Bahamas or the Dutch Antilles
- (2) ESTABLISHMENT – under the Laws of Liechtenstein
- (3) REG. TRUST – under the Laws of Liechtenstein

## SCHEDULE ONE AA1a

(Section 196)

Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu

## SCHEDULE TWO

(Section 242)

### Definitions

1. In this Schedule –
  - "**the Custodian**" – the Custodian of Enemy Property, appointed under section 2 of the Trading with the Enemy Ordinance 1939, or the Custodian of Absentees' Property, within its meaning in the Absentees' Property Law 5710-1950;
  - "**Trading with the Enemy Laws**" – the Trading with the Enemy Ordinance 1939, or the Absentees' Property Law 5710-1950, or any other statute that relates to trade with the enemy or with absentees, and wherever this Schedule refers to money or assets or income received or held by the person in charge of it – including money or assets or income held to his order;
  - "**asset**" – within its meaning in section 9 of the Trading with the Enemy Ordinance 1939, or absentees' property, within its meaning in the Absentees' Property Law 5710-1950;
  - "**blocked asset**" – money or an asset held by the Custodian;
  - "**blocked income**" – income payable to the Custodian, which would have been included in the chargeable income of a person for a certain tax year, if not for the Trading with the Enemy Laws, and "**owner of income**" – an aforesaid person.

**Tax on blocked income**

2. Blocked income shall be deemed the chargeable income of the owner of the income, and the Custodian may be assessed in respect of that income, in the manner in which the owner of the income would have been assessed, had it been included in his income for that year.

**Custodian's entitlement to tax benefits**

3. When the Custodian is assessed in respect of blocked income under section 2 of this Schedule, or if he received blocked income paid after the deduction of tax, and if it is proven to the Assessing Officer's satisfaction that the owner of the blocked income would have been entitled – on his claim – to tax benefits, if not for the Trading with the Enemy Laws, then that credit shall also be allowed the Custodian, whether by way of refund or in another manner.

**Assessment of individual owner of income**

4. If the Assessing Officer concludes, on the basis of information in his possession, that the chargeable income of a certain individual owner of income should have included income that is not blocked, then the Assessing Officer may assess that person in respect of that income which is not blocked without a notification of assessment.

**Custodian's obligation to pay tax on blocked income**

5. If tax was assessed on the Custodian under section 2 of the Schedule in respect of blocked income, then the Custodian shall pay it alone or through another, out of money of the owner of the income which he holds.

**Custodian's obligation to pay all the tax due from owner of blocked income**

6. The Custodian shall pay, out of the money of an individual owner of income held by the Custodian – if there is no different explicit provision in this Schedule – all the tax due from that individual according to the Assessing Officer's demand for each assessment year or tax year, and any amount paid as aforesaid shall be treated as if it had been paid by that individual; in an aforesaid demand the Assessing Officer may also include an amount, in respect of which the assessment still is, or can be, the subject of objection or appeal.

**Effect of release of income**

7. If the Custodian released to a person, to his credit or to his legal representative everything in his possession to which that person would have been entitled, if not for the Trading with the Enemy Laws, then thereafter –
  - (1) all income released as aforesaid shall be deemed the income of the person who would have received the income, if not for those statutes;
  - (2) any tax paid in respect of that income by the Custodian, whether by deduction or otherwise, shall be treated as paid by the said person and any benefit accorded the Custodian in respect of that income shall be deemed to have been accorded to that person;
  - (3) the said person or his representative may submit objections and appeals against an assessment of the Custodian in respect of that income, as if he had been assessed.

**Owner of released income liable for assessment before release**

8. If the Custodian was assessed under the provisions of this Schedule, and if – before or after the assessment – he paid or transferred or released all or part

of the income to another person or permitted that to be done, then that part of the tax which must be paid under the assessment, which the Custodian cannot pay under the provisions of this Schedule, shall constitute a debt owed to the State by the person who is deemed the owner of that income under section 7 of the Schedule, or by his legal representative, if it is a case to which this section applies, or by the person to whom the income was paid, transferred or released, and that part shall be paid accordingly and the Custodian shall cease to be responsible for the tax.

**Relaxation of time limitations**

9. Notwithstanding the limitations in the Ordinance for the preparation of assessments, for objections and for appeals, assessments may be made under sections 2 and 4 of the Schedule at any time before a date set by the Minister of Finance, and objections and appeals against an aforesaid assessment and claims for tax benefits may be submitted at any time before that date.

**Persons deemed to be owners of income**

10. For purposes of sections 2 to 4 of this Schedule it is assumed – unless the opposite has been proven – that since September 3, 1939, nothing happened to change the identity of a recipient of blocked income or of an owner of a blocked asset, and every assessment under section 2 of the Schedule shall specify the name of the owner of the income.

**Tax on income generated, but still unpaid**

11. If income from a certain source in a certain tax year should have been paid to the Custodian, if not for the fact that – during that tax year – no income from that source was available for payment, and if that income nevertheless would have been liable to tax, if not for the Trading with the Enemy Laws, then the provisions of this Schedule shall apply, as if income from that source had been available in that year and had been paid to the Custodian.

**Effect**

12. The provisions of this Schedule shall be in effect for assessment years beginning with April 1, 1947, and for all the assessment years and all the tax years thereafter.