

## **Israeli Taxation Of Rental Income Received By Individuals**

Do you have one or more apartments in Israel rented for residential purposes? A frequently asked question is the taxation of rental income of residential property received by an individual taxpayer.

The Israeli tax law offers three different tracks for the taxation of rental income: **The regular taxation track, the exemption track and the 10 % track on the gross rental income.**

### **I. Regular Taxation Track**

According to this track, rental income from residential property is taxed at a tax rate of not less than 30 %. This rule applies generally to all individuals, except for individuals who are at least 60 years old in the respective tax year. For the latter, the tax bracket starts even for rental residential income at a 10 % tax rate.

By choosing this track, all expenses incurred in the creation of rental income are allowed to be deducted, including deductions for depreciation and for interest expenses.

In addition credit points and all exemptions for individuals are applicable in determining the amount of tax to be paid.

### **II. Tax Exemption Track**

This track is based on a special income tax law (exemption from taxation on income from the rent of residential property, 1990). According to these rules, an individual who rents property to another individual for residential purposes, is exempt from taxation for the rental income, provided that the rental income of the individual ( or his spouse or his children under the age of 18 years old ) does not exceed 5070 Shekel per month ( the exemption limit amount of 2015 ).

In case the accumulated rental income of the individual exceeds the aforementioned exemption amount of 5070 Shekels per month, however not the double amount of 10,140 Shekel, partial exemption is possible. Any rental income above the so calculated exemption amount is subject to regular progressive taxation at a tax rate starting at 31 %, except for individuals, who are at least 60 years old, for whom the tax rate starts at 10 %.

Also here, the taxpayer is allowed to deduct the expenses incurred from the partial taxable income. However, if there is partial income exemption requested, not all expenses are allowed to be deducted, but only an amount limited to the ratio between the amount of taxable rental income and the total income from rent.

In case of the sale of the property and of the determination of capital gain upon the sale, the law requires that the acquisition value ( the original cost ) is reduced by the depreciation amount allowed, as if the taxpayer had not chosen the exemption track, thereby basically increasing the capital gain.

### **III. The 10 % Track On Gross Rental Income**

This 10 % rule is applicable if the property is situated in Israel, rented for residential purposes and the rental income is not connected to business income.

It has to be emphasized that by choosing this track, no deduction of expenses incurred in the creation of income is allowed, as well as no depreciation deduction, no offsets, no credit points and no deduction for exemption amounts. In addition, in case of sale of the residential property, the sales price is to be increased by the depreciation amount allowed but not taken.

Furthermore, the 10 % tax on the gross amount of the rental income is due within 30 days after the end of the tax year.

#### **IV. What Track To Choose?**

Every tax year the taxpayer can choose any track.

If the rental income is less than the exemption amount of 5070 Shekel for the year 2015, the taxpayer would probably choose the exemption track, unless the expenses for that year are higher than the rental income and there is a loss for tax purposes.

If the rental income is above the exemption amount, one can choose between the regular track or the 10 % track. The regular track can lead to less tax than the 10 % track especially when the expenses incurred in the creation of rental income are relatively high.

In addition, the regular track opens the possibility that it can be used in connection with a partial exemption and credit points are taken into account to determine the tax burden.

The 10 % track is definitely the simpler way of taxation. However, if this track is chosen, even the partial exemption track for the same residential property is not possible.

A taxpayer with more than one residential rental property can choose the regular track for one apartment and the 10 % track for another apartment.

There is no clear cut answer as to which track to choose for a particular tax year. It is important to make a careful analysis taking into account the respective results under all three tracks to determine which track offers the optimal tax obligation for a certain tax year.