



Trust Distributions – View from Israel

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Dr. Judith Taic TEP, Dr. Judith Taic Tax Law Office

Dr. Judith Taic
LLM Taxation (NYU), TEP
Rechtsanwältin – Germany
Attorney at Law - New York
Advocate – Tel Aviv

drjtaic@law-intax.com

Overview

- Some Facts about Israel
- Possible Classification of Trust in Israel
- Israeli Resident Trust
- Israeli Beneficiary Trust/Relative Trust/ Family Trust
- Foreign Resident Trust
- Foreign Beneficiary Trust
- Testamentary Trust
- Contribution of Israeli Real Estate to a trust
- Reportable Position that affects Trusts

Some Facts about Israel

Population: 9 million people

Location: Israel is located at the junction of three continents with access by air and sea to main locations around the world



Trusts under Israeli Law

- Since 1979 Israel has a separate trust law
- A Trust is created by law, by a contract with the trustee or by a deed/instrument hekdesch
- Israeli has not signed the Hague Convention 1985, but will recognize use of trusts established under foreign jurisdiction
- Taxation of trusts in Israel since 2006 with major amendments in 2014

Basics of Taxation of Trusts in Israel

- Definition: for Israeli tax purposes a trust is an arrangement by which a trustee holds assets for the benefit of a beneficiary, whether made or carried out in Israel or abroad.
- Liability of taxation of trust depends on the residence of the settlor/or beneficiary
 - Residence of an individual determined by Center of Life Test
 - Israeli resident subject to taxation on worldwide income
 - 10 Year tax holiday for New Immigrants and Long Absent Returning Residents
- The default rule: the trustee, whether local or foreign, liable to pay the tax and to fulfill the reporting obligations for the trust
- Trust subject to tax rates that are applicable for individuals
 - Trusts not entitled to tax brackets (highest marginal tax rate will apply)
 - Trusts are not entitled to credit points and exemptions that are limited by cap

Different Classification of Trusts

- Israeli Resident Trust
- Israeli Beneficiary Trust/Relative Trust/Family Trust
- Foreign Resident Trust
- Foreign Beneficiary Trust
- Testamentary Trust

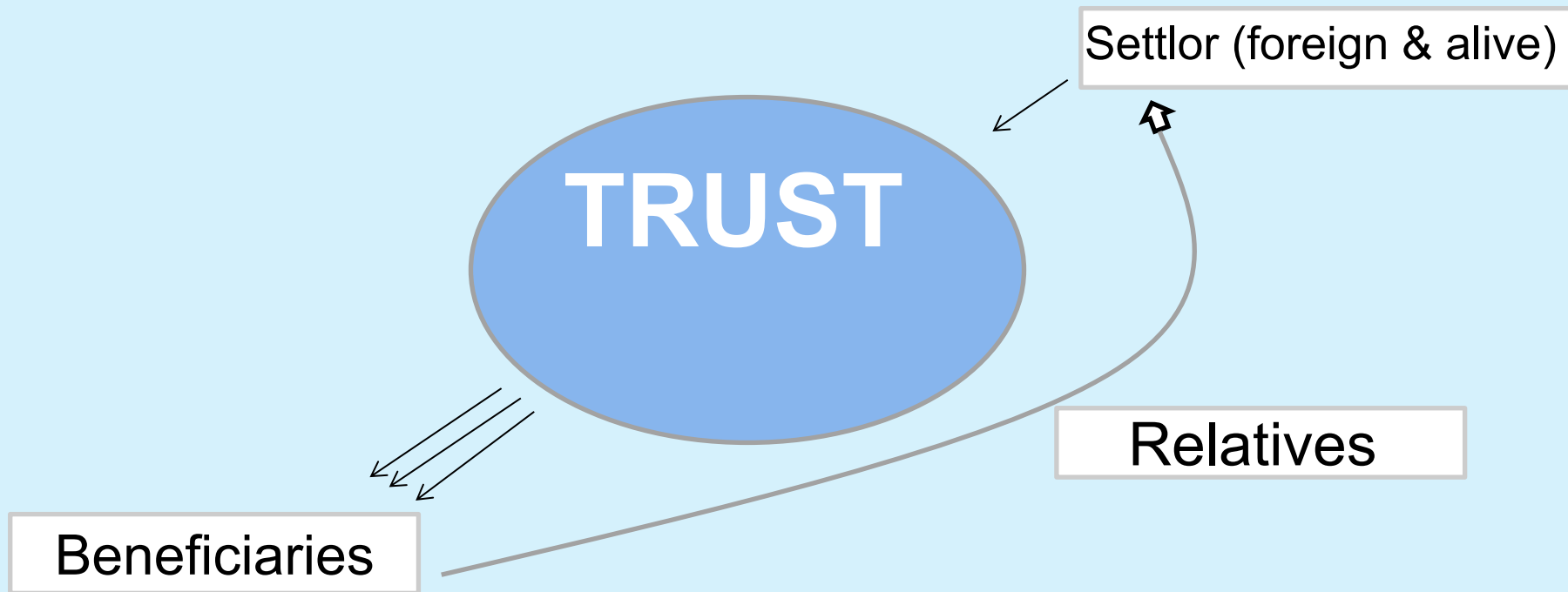
Israeli Resident Trust – General

- Definition: one of the following trusts:
 - A trust in which, at the date of creation, at least one settlor and one beneficiary were Israeli residents, and ,during the relevant tax year, at least one settlor or one beneficiary are Israeli residents
 - A trust in which all settlors are deceased and at least one beneficiary is an Israeli resident
 - Any trust that does not qualify as any other type of trust

Israeli Resident Trust

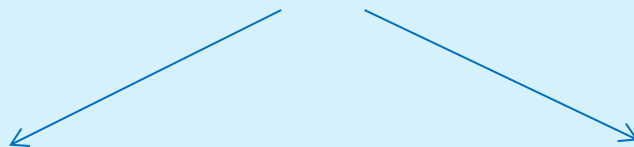
- Taxation of the trust: subject to tax as an Israeli resident on its world-wide income with highest marginal tax rate
- Contributions will generally not trigger a tax event
- Distributions will be regarded as a transfer from the settlor to the beneficiary and generally shall not trigger a tax event
- Under a circular published by the ITA (3/2016), as well as a published ruling (3792/16, tax credit may be available

Israeli Beneficiary / Relative Trust



Israeli Beneficiary Trust – General

- Definition: Foreign settlor, who is alive and at least one Israeli resident beneficiary



Relative Trust

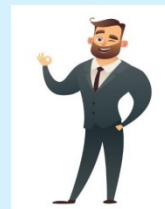
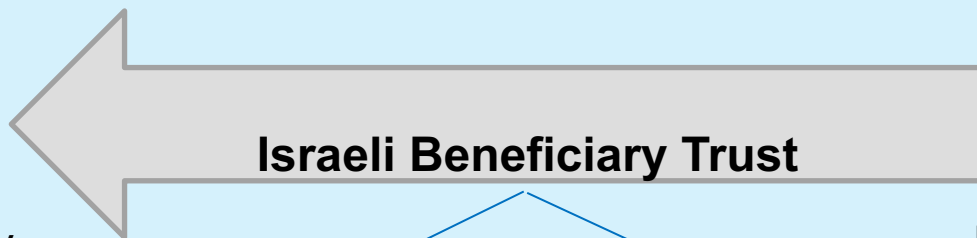
If all beneficiaries related to the settlor

Israeli Resident Trust

If not all beneficiaries related to the settlor



Israeli Beneficiary



Foreign Settlor

Relative Trust

Family relationship between settlor and all beneficiaries

2 options for taxation of **foreign** source income/election by trustee:

- Taxation at distribution – 30 %
- Taxation on current income - 25 % to the Israeli beneficiary

Israeli source income taxed in Israel

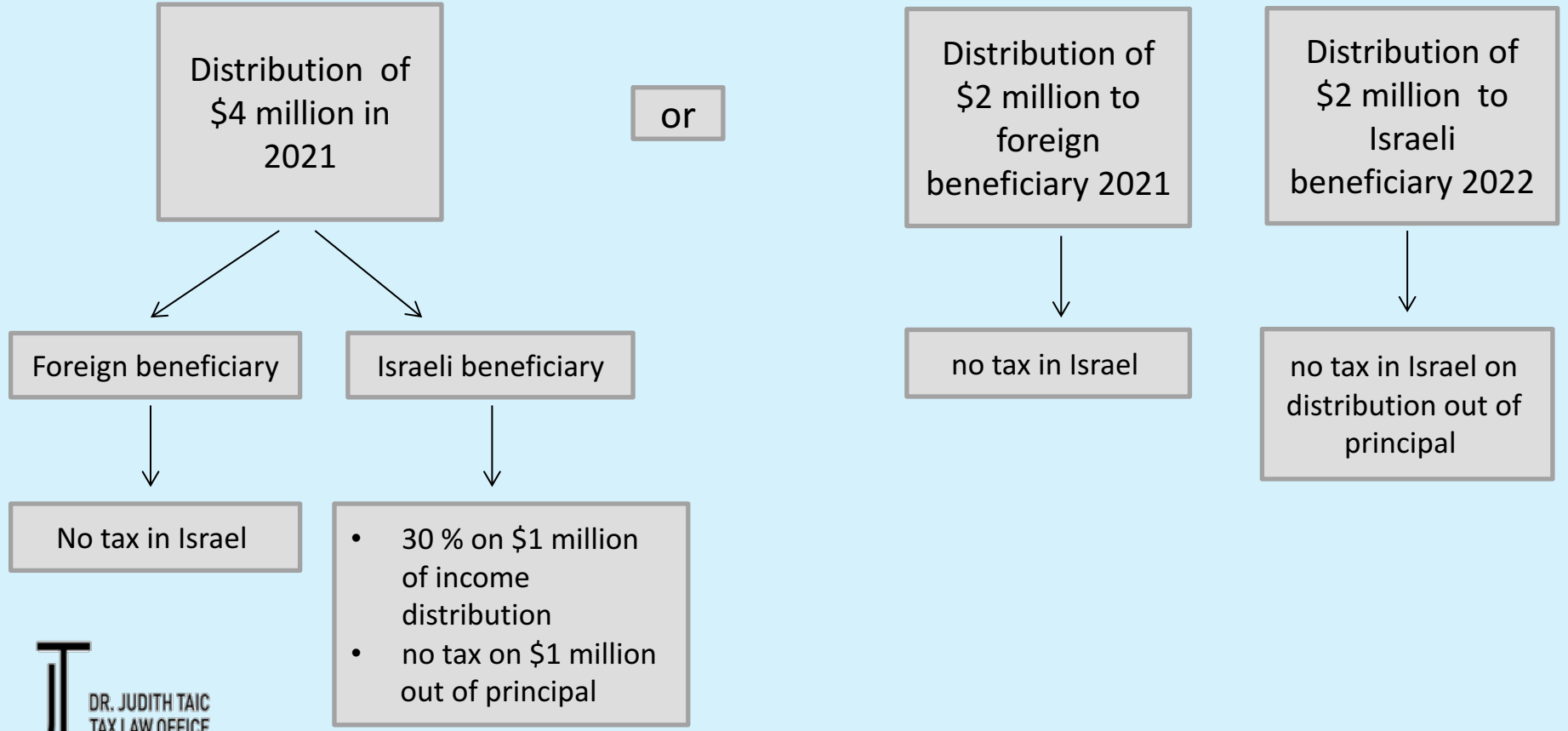
Trust which is not Relative Trust

No family relationship between the settlor and all beneficiaries

Taxation: Trust is considered Israeli resident trust and taxed on its worldwide income

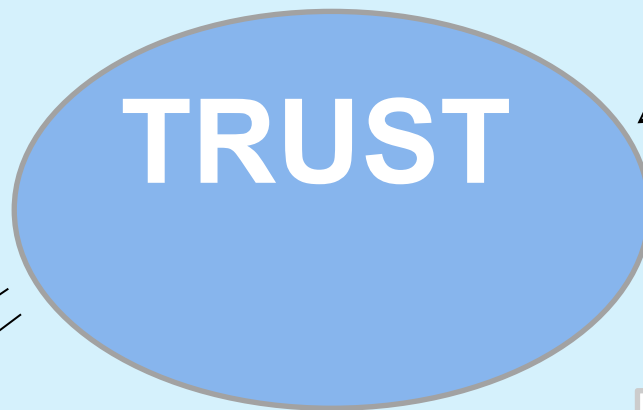
Example: Relative Trust

- Foreign settlor establishes a trust in 2018 for the benefit of his two children, one of them Israeli resident, and contributed a sum of \$10 million
- In 2020 the trust accrued income of \$2 million
- In 2021 the trustee intends to distribute a sum of \$4 million to the two beneficiaries in equal parts



- Demise of foreign settlor will result that the Israeli Beneficiary Trust/Relative Trust will be considered Israeli Resident Trust subject to Israeli tax on its worldwide income - very harsh result –
- Tax benefits for New Immigrant beneficiary

Foreign Resident Trust



Settlor (all foreign) or all settlors deceased and only foreign beneficiaries

Trusts revocable or irrevocable

Beneficiaries all foreign and never have been Israeli residents

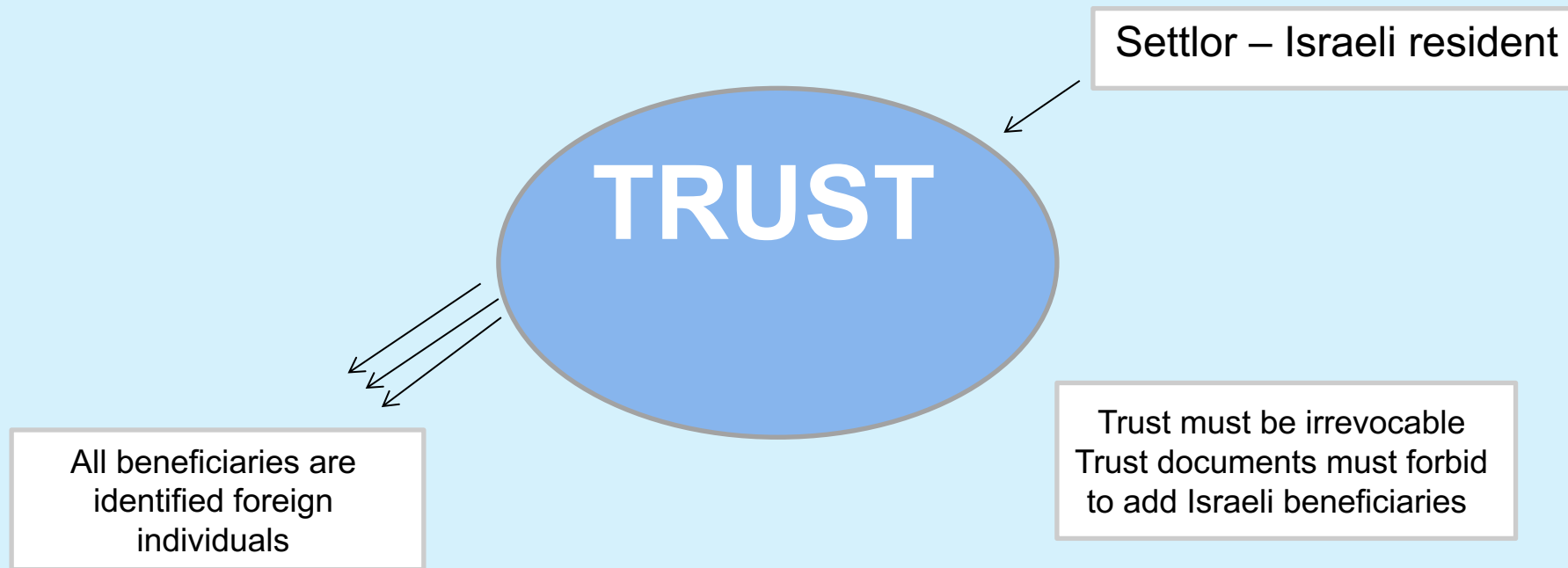
Foreign Resident Trust – General

- Definition: a trust that where there is either:
 - All settlors and all beneficiaries are foreign residents and there are no beneficiaries who were Israeli residents
 - All settlors are deceased and all beneficiaries are foreign residents and no beneficiaries have been Israeli residents
 - Trust can be revocable or irrevocable

Foreign Resident Trust – General

- Taxation: subject to tax as a foreign resident – only on Israeli sourced income
- Contribution of assets will not trigger capital gains tax
- Distribution from the trust will be considered direct transfers from the settlor to beneficiaries and may trigger a taxable event in Israel

Foreign Beneficiary Trust



Foreign Beneficiary Trust – General

- Definition: a trust that meets the following:
 - An Irrevocable trust
 - Was settled by an Israeli resident settlor
 - All of the beneficiaries are identified foreign individuals
 - Adding Israeli beneficiaries is forbidden under the trust's documents

Foreign Beneficiary Trust – General

- Taxation: subject to tax as a foreign resident – only on Israeli sourced income
- Contribution of assets will trigger a capital tax event
- Distribution from the trust will not trigger a tax event in Israel

Testamentary Trust– General

- Definition: Trust settled under a will by settlor who is Israeli resident at time of his demise



Contribution of Israeli Real Estate to a Trust

- A contribution to a trust is generally not taxable in Israel
- The ITA's position is that the contribution of Israeli Real Estate (as opposed to other assets) to a trust is taxable in Israel
- The Tel Aviv District Court ruled in the "Galis Case" that the transfer of Israeli Real Estate is not taxable, and only the distribution of the asset will constitute a sale
- The ITA has submitted an appeal to the Supreme Court



Reportable Position that affects Trusts - General

- Under Israeli law, taxpayers are required to submit a special report if they take a certain position which contradicts a position taken by the ITA and published by the ITA and the position taken by the taxpayer creates a tax saving of at least NIS 5 million in the tax year or NIS 10 million in a 4-year period

Reportable Position that affects Trusts

➤ Maximum Exemption Period

- If a settlor or a beneficiary of a trust completed his 10 year benefit period, the trust will become an Israeli resident trust, even if there are other new Immigrants settlors or beneficiaries in the trust
- The trust exemption period will end on the earliest date of which any of the settlors, or any of the beneficiaries exemption period ends, even if the others are still entitled to the benefits
- Advisable to divide the trust before the end of the exemption period

Reportable Position that affects Trusts

- Distribution to Relative Trust that chose a Distribution Route
 - A distribution to a New Immigrant from a Relative Trust that is subject to the special Distribution Taxation Route, will be subject to 30 % even if it originates from income derived by the trust within the benefit period
 - Accordingly, it is important to plan the distribution from the trust before the end of the 10 year benefit period

- Taxation of trusts very complex and technical
- Proper planning if tax benefits for trusts with New Immigrants



Thank You



drjtaic@law-intax.com

www.law-intax.com

Sources

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