

Israel Expands Tax Incentives for New Immigrants and Returning Residents: New Exemption for Israeli Employment and Business Income

As part of the 2026 Economic Efficiency Law, Israel has enacted the Encouragement of Immigration to Israel and Return to Israel (Temporary Order), 2026, introducing a significant new tax incentive for new immigrants (*olim*) and veteran returning residents (individuals returning to Israel after at least 10 years of foreign residence).

The legislation reflects the Israeli government's desire not only to encourage immigration and return to Israel, but also to encourage internationally mobile professionals, entrepreneurs and business owners to relocate their economic activity and work functions to Israel.

Existing 10-Year Tax Holiday Remains in Place

Under the existing rules of Section 14(a) of the Israeli Income Tax Ordinance, new immigrants and veteran returning residents enjoy a 10-year exemption from Israeli tax on:

- Foreign employment income;
- Foreign business income;
- Foreign rental income;
- Foreign dividends, interest and royalties;
- Capital gains derived from non-Israeli assets; and
- Other foreign-source income.

The new legislation does not replace these benefits. Rather, it adds a new and separate exemption for certain Israeli-source earned income.

A New Exemption for Israeli Employment and Business Income

Historically, income generated from work physically performed in Israel remained taxable, even when paid by a foreign employer or foreign company.

The new Temporary Order changes this position by granting a tax exemption for certain employment and business income earned in Israel.

The exemption applies to:

- Employment income under Section 2(2) of the Ordinance; and
- Business or professional income under Section 2(1) of the Ordinance.

Passive Income Does Not Qualify

Importantly, the new exemption is limited to active earned income and does not apply to passive income.

Accordingly, Israeli-source income such as:

- Dividends;
- Interest;
- Royalties;
- Rental income;
- Capital gains; and
- Other investment income,

does not qualify for the new exemption and remains subject to the ordinary Israeli tax ,

Such income may nevertheless continue to benefit from the existing 10-year exemption where it constitutes foreign-source income under Section 14(a).

The distinction between active earned income and passive investment income is therefore critical when evaluating eligibility for the new regime.

Who Qualifies?

The benefit is available to individuals who become new immigrants or veteran returning residents (individuals returning to Israel after at least 10 years of foreign residence) between **5 November 2025 and 31 December 2026**.

Individuals claiming the benefit must hold the appropriate status and documentation issued by the Israeli Ministry of Aliyah and Integration. New immigrants should hold a Teudat Oleh (Oleh Certificate), while veteran returning residents must obtain a Teudat Toshav Chozer Vatik (Veteran Returning Resident Certificate) as a condition for claiming the benefit.

Exemption Amounts

The exemption applies to qualifying Israeli-source earned income up to the following annual limits:

| Tax Year | Maximum Exempt Amount |
|-----------------|------------------------------|
| 2026 | NIS 600,000 (pro-rated) |

| | |
|------|---------------|
| 2027 | NIS 1,000,000 |
| 2028 | NIS 1,000,000 |
| 2029 | NIS 350,000 |
| 2030 | NIS 150,000 |

The benefit expires after 2030.

Mixed Income – An Increasingly Important Issue

The new legislation significantly increases the importance of correctly determining whether income is Israeli-source or foreign-source.

Many professionals, consultants, executives and entrepreneurs perform services partly in Israel and partly abroad. In such situations, the income may constitute "mixed income" and must be allocated between Israeli and foreign activities.

According to Income Tax Circular 1/2011, the allocation may generally be based on the ratio of workdays performed outside Israel compared to total workdays. The Circular further suggests that where only a limited amount of work is performed abroad, the income may remain entirely Israeli source.

However, the Circular does not define a minimum threshold. In Tax Ruling 2316/18, the Israel Tax Authority expressed the view that at least 60 business days outside Israel are required before a portion of the income may be attributed to foreign activities. Whether this position is fully supported by the legislation remains open to debate.

This distinction has become particularly important because:

- Foreign-source income may continue to benefit from the unlimited 10-year exemption under Section 14(a); whereas
- Israeli-source income relies on the new temporary exemption, which is capped and expires after 2030.

As a result, allocating too much income to Israel may result in tax becoming payable on income that could otherwise have benefited from the unlimited 10-year exemption for foreign-source income if properly characterized and allocated.

Importantly, this issue can arise even where the employer is Israeli. If part of the work is physically performed abroad, it may be possible to allocate a corresponding portion of the remuneration to foreign-source income eligible for the existing 10-year exemption.

Related-Party Restriction - for the New Israeli-Source Income Exemption

A special limitation applies to the new exemption for Israeli-source employment and business income. While the general exemption can reach up to NIS 1 million per year (see above) the exemption is significantly reduced to **NIS 140,000 per year** (during 2026–2029) where the income is received from a related party.

For this purpose, a related party includes family members and entities in which the individual directly or indirectly holds at least 25%.

Importantly, a company that is wholly owned by the new immigrant or returning resident is generally not treated as a related party for these purposes. As a result, certain wholly owned corporate structures may remain eligible for full exemption, subject to the other requirements of the legislation.

It should be noted that this restriction applies only to the new temporary exemption for Israeli-source employment and business income. It does not affect the existing 10-year exemption under Section 14(a) for qualifying foreign-source income.

The purpose of the rule is to prevent artificial income shifting between related parties in order to benefit from the new exemption.

Foreign Companies, Mixed Income and Structuring Opportunities

Many new immigrants and returning residents conduct their international activities through foreign companies. In such cases, the distinction between Israeli-source and foreign-source income, discussed above, becomes particularly important.

The new legislation creates both opportunities and challenges in this area. For example:

- Income received directly from a related foreign company may be subject to the reduced exemption threshold applicable to related-party income.
- In certain situations, it may be preferable to operate through a wholly-owned company and receive salary or deemed income under the Israeli "wallet company" rules of Section 62A of the Ordinance.
- Where activities are performed both inside and outside Israel, it may be beneficial to separate foreign and Israeli operations into different entities. This may help preserve the unlimited 10-year exemption under Section 14(a) for qualifying foreign-source income, while allowing Israeli activities to benefit from the new exemption for Israeli-source employment and business income.

The optimal structure will depend on the individual's specific business activities, ownership structure and overall tax profile.

Relief for Foreign Companies

The new legislation also introduces a special relief for foreign companies. Where a foreign company would become subject to Israeli taxation **solely because** a qualifying new immigrant or veteran returning resident performs services from Israel, the resulting Israeli-source income may be exempt from Israeli tax.

The rule is intended to reduce the risk that a foreign company will be treated as having an Israeli permanent establishment, or otherwise become subject to Israeli taxation, merely because the individual has relocated to Israel and continues to work for the foreign company from there.

Importantly, the relief applies only where the Israeli tax exposure arises solely as a result of the individual's activities in Israel. It does not apply where the foreign company already has an Israeli permanent establishment, employees, business operations, dependent agents or any other independent taxable presence in Israel.

The relief generally does not apply where the individual is a substantial shareholder in the foreign company or where the income is attributed through a transparent entity, such as an LLC.

New Reporting Obligations applicable from 2026

Prospective immigrants should be aware that, while the 10-year tax exemption on foreign-source income remains in place, the historical reporting exemption is no longer available for individuals who become Israeli residents on or after 1 January 2026.

As a result, new immigrants and veteran returning residents will generally be required to report:

- Foreign income;
- Foreign bank accounts;
- Foreign companies;
- Trusts;
- Foundations; and
- Other foreign assets and structures,

even where the income itself remains fully exempt from Israeli tax.

Accordingly, pre-immigration planning should now include not only a review of tax exposure but also an assessment of future reporting obligations.

Anti-Abuse Rule

The new temporary exemption for Israeli-source employment and business income will not apply where an individual ceases to be an Israeli resident during 2028 or 2029 and spends fewer than 75 days in Israel during one of those years.

This rule is intended to prevent short-term relocations undertaken solely to obtain the temporary tax benefits.

This limitation does not affect the existing 10-year exemption for foreign-source income.

Conclusion

The new Temporary Order represents one of the most significant enhancements to Israel's immigration tax incentives in recent years.

For the first time, qualifying new immigrants and veteran returning residents may benefit not only from the long-standing exemption for foreign-source income, but also from a temporary exemption for certain Israeli-source employment and business income.

The new regime is particularly attractive for internationally mobile entrepreneurs, consultants, professionals, executives and business owners who are able to perform part of their activities from Israel while maintaining international operations.

At the same time, careful planning has become more important than ever. Attention should be paid to:

- the distinction between active and passive income;
- the allocation of mixed income between Israel and abroad;
- the structuring of foreign and Israeli business activities;
- company ownership arrangements and related-party rules;
- permanent establishment considerations; and
- the new reporting obligations applicable from 2026.

Proper planning before relocation can significantly enhance the value of the available tax benefits while avoiding unexpected tax and compliance exposures.