Narrative Report on Israel

Rank: 38 of 133

How Secretive? 59

Moderately secretive — 0 to <25

25 to <50

50 to <75

Exceptionally secretive — 75 to 100

How big? 0.3%

huge

large

small

tiny

huge: >5% large: >1% to 5% small: >0.1% to 1% tiny <0.1%

Israel accounts for 0.3 per cent of the global market for offshore financial services. This makes it a small player compared to other secrecy jurisdictions.

The ranking is based on a combination of its secrecy score and scale weighting.

Full data is available here: http://www.financialsecrecyindex.com/database.

To find out more about the Financial Secrecy Index, please visit

http://www.financialsecrecyindex.com.

The FSI project has received funding from the European Union's Horizon 2020 research and innovation programme under grant agreement No 727145.

If you have any feedback or comments on this report, contact us at info@taxjustice.net

PART 1: NARRATIVE REPORT

Israel is ranked at 38th position in the 2020 Financial Secrecy Index (four places down from its 2018 position), based on a secrecy score of 59 and a scale weight which accounts for 0.3% of the global market in offshore financial services.

History of Israel as a secrecy jurisdiction

In 2003, influenced by a global trend to combat hidden bank accounts and tax haven entities, Israel shifted its tax system to a new tax base - imposing income tax on a worldwide basis. As part of this shift, and in an attempt to combat tax evasion, Israel has introduced Controlled Foreign Corporation (CFC) rules, worldwide Vocational Taxation provisions, extensive reporting requirements and a new trust law reform.[1]

Three years later, on January 1, 2006, Israel amended the Income Tax Ordinance [new version], 5721-1961 (hereinafter: "Income Tax Ordinance") to include a list of tax planning schemes which must be reported to the tax authority.[2] The list became effective as of January 1, 2007 and was updated with additional tax planning schemes in 2016 and 2017.[3] In addition, in 2016 new reporting requirements were introduced when certain tax opinions are received by tax payers, e.g. opinions in which the adviser's fee depends on the tax savings which are derived from receiving the opinion; opinions which are considered "off-the-shelf opinions"; and opinions which hold a position contradicting that of the tax authorities.

"Milchan Law"- an exemption for newcomers and returning veterans

In September 2008, contrary to this trend towards clamping down on tax dodging, Israel amended its Income Tax Ordinance (Amendment No.168) and granted tax exemptions for "New Immigrants" (persons who have never held an Israeli residency) and for "Veteran Returning Residents" (Israeli citizens who have spent abroad at least ten consecutive years as foreign residents). To a certain extent, this amendment has turned Israel into a tax haven for billionaires.[4] As a result, new immigrants and veteran returning residents are exempt from Israeli income tax and reporting obligations regarding their non-Israeli source income and gains (as well as from filing tax returns and capital declarations) for a ten-year period commencing in the year in which they became Israeli New/Veteran residents (sections 134B and 135 of the Income Tax Ordinance). In practice, this amendment, known also as 'Milchan Law',[5] "provides (high) net wealth individuals with a unique opportunity to transfer funds from off-shore jurisdictions and financial centers into Israel, while enjoying the 'protection' of a respectable country, which is not classified as a low tax jurisdiction".[6] Moreover, in 2009 Israel even amended the law to provide the Head of the Israeli Tax Authorities (ITA) a discretion to extend the exemption from such filing obligations for an additional ten-year period (up to 20 years altogether) to individual new immigrants/veteran returning residents who will make substantial investment in Israel within two years of their arrival in Israel.

As a result of these reporting exemptions, the Israeli Tax Authority cannot receive financial and identity information regarding the non-Israeli source income and gains of new immigrants and returning veterans. A clear restriction exists, for example, regarding trusts. As the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes reports in 2016[7] (p.33): "Israeli law does not ensure the availability of identity information in respect of the settlors, trustees and beneficiaries of foreign resident trusts having a trustee resident in Israel and for trusts created by new immigrants and veteran returning residents which are vested with assets or income from assets abroad for a period of 10 years if the trust is operated by a resident trustee who is not an attorney or an accountant covered by AML obligations."

Due to pressure from international organisations[8] (p.54), a bill to repeal the reporting exemption, while leaving the tax exemption as is, has been included almost every year since 2013 in the Israeli Economic Arrangements Bill. Nonetheless, despite the strong internal and international criticism, as of December 2019, no legislative proposal was able to secure enough support from members of the Knesset to be approved.[9]

These exemptions also have serious implications regarding money laundering. As the US State Department emphasised for several years in its International Narcotics Control Strategy Report (INCSR) reports,

> "Israel's 'right of return' citizenship laws mean that criminal figures find it easy to obtain an Israeli passport without meeting long residence requirements. It is not uncommon for criminal figures suspected of money laundering to hold passports in a home country, a third country for business, and Israel".[10]

In its 2016 INCSR report, the US State Department added[11] (p.146):

> "Criminal groups in Israel, either home-grown or with ties to the former Soviet Union, United States, or EU, often utilize a maze of offshore shell companies and bearer shares to obscure ownership".[12]

The shadow economy in Israel

Israel has a large shadow economy. In 2010, the World Bank estimated the black economy as equal to almost 23 percent of Israel's GDP in 2007.[13] This estimate was confirmed in 2014 by the Taub Center[14] for Social Policy Studies in Israel. According to research carried out by Visa Europe in 2013, the black economy is equal to NIS 185 billion (approximately US $51.2 billion) a year.[15] The Israeli Tax Authority estimates that tax evasion is the underlying motive for about 80 percent of this black economy.[16] One of the reasons for such a high figure is that in practice, due to several exemptions provided in the Income Tax Ordinance for filing tax returns, and because neither gifts nor inheritances are taxed, most Israeli residents are not required to file income tax returns.[17]

In light of these estimates, in February 2012, the Israeli Tax Authority declared a 'war on tax evasion'[18] and submitted to the Minister of Finance "recommendations for the struggle against black capital and tighter enforcement, with the goal of tripling the ministry's promise of higher tax collection". The recommendations included making tax evasion a predicate offence for Anti Money Laundering. Other recommendations included halving cash transactions from NIS 20,000 to NIS 10,000 and levying a 15% fine on exceeding the limit.[19]

As a result of these recommendations, on 31st July 2013 Israel enacted[20] a law requiring money changers and currency service providers to report any transactions involving sums in excess of NIS 50,000 to the tax authority. The law requires the establishment of a database comprised of this information, which the tax authority can use to locate tax evaders through market exchange service providers. Additional amendments[21] (p.225) were made in 2014, including subjecting lawyers and accountants to customer due diligence (CDD) requirements as well as obliging money service businesses to implement CDD requirements. In an effort to ensure legislative alignment, the Prohibition on Money Laundering Law was amended in April 2016 to include serious tax offences as predicate offences and to allow a direct transfer of information between the Israel Money Laundering and Terror Financing Prohibition Authority (IMPA) and the ITA.[22]

Alongside these amendments, the Financial Action Task Force (FATF) on money laundering announced in February 2016 that Israel would join the organisation as an observer, starting in June 2016.[23] One of the amendments required by the FATF for Israel to become a full member was imposing limitations of the usage of cash and the cross-border transportation of currency (recommendation n. 3224 of the FATF). In January 2018, following long delays and strong resistance from the Jewish religious community, the plan to reduce the use of cash to NIS 10,000 for businesses and NIS 50,000 for individuals was approved as part of the 2018 Israeli

Israel

Arrangements Law. In December 2018 Israel was finally accepted as a full member of the FATF.[25]

Exchange of banking information

There have also been several developments in respect of exchange of information for tax purposes. On 30th June 2014 Israel signed[26] an inter-governmental agreement with the United States to implement FATCA provisions (according to Model I IGA which provides for reciprocity between the two partners). In addition, on 27 October 2014 Israel declared its intention to join the OECD's Common Reporting Standard (CRS) by end of 2018 and to make the necessary legislation amendments for it.[27] An amendment[28] (p.16) to the Income Tax Ordinance came into force on 1 January 2016 , following which Israel has signed the Multilateral Competent Authority Agreement in June 2017.[29] However, political disagreements led to Israel violating its commitment until a new law was passed in February 2019 that enabled Israel to start exchanging information.[30]

Tax incentives in Israel

For many years Israel provided tax incentives for the encouragement of foreign investments. Prior to 2011, the Investment Law for Encouragement of Capital Investment, 5719-1959 ("the Investment Law") gave preferential treatment to foreign investments in Israel. Companies that invested a substantial amount of money in Israel, as determined by law, were granted zero corporate tax rates for ten years. However, Amendment 68[31] to the Investment Law, in force as of 2011, abolished this preferential treatment and eliminated the exemption from corporate income tax granted to corporations.

In addition, in 2015 the government enacted a law to increase the Tax Benefits for Individuals Investing in R&D Companies Law ("Angels' Law").[32] As explained by the IBFD, "Amendments to the 2010 "Angels' Law" will modify tax incentives provided for new investments in Israeli start-ups in order to make the law more effective in terms of raising capital. Specifically, investors will be able to deduct, for income tax purposes, 100% of their investment during the first year (currently, a deduction over three years is possible provided the company maintains a start-up status)."[33]

Finally, in 2016, Israel approved legal amendments that introduced a patent box regime for the intellectual property (IP) of companies. The amendments include a reduced corporate income tax rate of 6% on IP-based income and on capital gains from future sale of IP. The 6% rate would apply to qualifying Israeli companies that are part of a group with global consolidated revenue of over ILS10 billion (US$2.5 billion). It appears that the new regime "was tailored by the Israeli Government to a post-base erosion and profit shifting (BEPS) world, encouraging multinationals to consolidate IP ownership and profits in Israel along with existing Israeli research and development (R&D) functions".[34]

With thanks to Moran Harari, TJN

Endnotes

1 https://www.step.org/sites/default/files/Branches/Resources/Israel-tax-system.pdf; 4.2.2020.

2 https://www.pwc.com/il/en/press-release/assets/tnn_israeltaxreform05.pdf; 4.2.2020.

3 https://search.proquest.com/openview/c6cfe7e7e8bc473f01f68d093daac7b5/1?pq-origsite=gscholar&cbl=2032112; 4.2.2020.

4 https://www.haaretz.com/israel-news/business/.premium-tax-exemption-lured-billionaires-to-israel-they-left-when-it-expired-1.8217511; 4.2.2020.

5 https://www.timesofisrael.com/what-is-the-milchan-law-that-netanyahu-is-accused-of-advancing-for-bribes/; 4.2.2020.

6 https://www.lexology.com/library/detail.aspx?g=a31f33f1-79cb-441a-9248-681061b9bad7; 4.2.2020.

7 http://www.eoi-tax.org/jurisdictions/IL#latest; 4.2.2020.

8 http://www.eoi-tax.org/jurisdictions/IL#previous_d4adedc003bf-fa533a85a75bdb27231d; 4.2.2020.

9 http://www.calcalist.co.il/local/articles/0,7340,L-3667413,00.html; (in Hebrew); 4.2.2020.

10 United States Department of State 2015: International Narcotics Control Strategy Report. Volume II Money Laundering and Financial Crimes, Country Database, Washington, DC (hereinafter: "INCSR CD 2015"), in https://2009-2017.state.gov/documents/organization/239329.pdf; 4.2.2020, p.226.

11 https://2009-2017.state.gov/j/inl/rls/nrcrpt/2014/supplemental/227904.htm; 4.4.2020.

12 See also: https://www.timesofisrael.com/did-a-little-noticed-tax-exemption-law-turn-israel-into-a-criminals-paradise/; 4.2.2020.

13 See in 24-25 in: http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2010/10/14/000158349_20101014160704/Rendered/; 4.2.2020.

14 http://taubcenter.org.il/the-shadow-economy-in-israel/; 4.2.2020.

15 http://www.globes.co.il/en/article-1000819120; 4.2.2020.

16 http://www.themarker.com/news/macro/1.1845006; (in Hebrew) 4.2.2020.

17 Income Tax Regulations (Exemption from filing income tax returns), 1988

18 http://www.globes.co.il/en/article-1000819120; 04.02.2020.

19 Ibid.

20 http://www.jpost.com/Business/Commentary/Your-Taxes-What-you-have-to-know-about-the-budget-law-323709; 4.2.2020.

21 https://2009-2017.state.gov/documents/organization/239329.pdf; 4.2.2020.

22 https://www.boi.org.il/en/BankingSupervision/LettersAndCircularsSupervisorOfBanks/LettersOfTheBankingSupervisionDepartment/201622en.pdf; 4.2.2020.

23 http://www.globes.co.il/en/article-fatf-grants-israel-observer-status-1001105328; 4.2.2020.

24 http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf; 4.2.2020.

25 https://mfa.gov.il/MFA/InnovativeIsrael/Economy/Pages/Israel-joins-the-Financial-Action-Task-Force-organization-17-December-2018.aspx; 4.2.2020.

26 https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Israel-6-30-2014.pdf; 4.2.2020.

27 IBFD 2015: IBFD Tax News Service, in: http://www.ibfd.org/IBFD-Tax-Portal/Tax-News-Service; 19.10.2019.

28 http://www.eoi-tax.org/jurisdictions/IL#latest; 4.2.2020.

29 http://mof.gov.il/Releases/Pages/takziv19.aspx; 4.2.2020.

30 https://www.hfn.co.il/client-update-israel-approves-crs-regulations-exchange-financial-information; 4.2.2020.

31 http://www.jpost.com/Business/Commentary/New-tax-breaks-for-Israeli-industry-you-need-to-understand; 4.2.2020.

32 https://kronengold.com/israels-angels-law/; 4.2.2020.

33 IBFD 2015: IBFD Tax News Service, in: http://www.ibfd.org/IBFD-Tax-Portal/Tax-News-Service; 19.10.2019.

34 https://www.ey.com/gl/en/services/tax/international-tax/alert--israel-approves-new-innovation-box-regime-and-reduces-tax-rates-from-1-january-2017; 4.2.2020.

Israel

PART 2: SECRECY SCORE

OWNERSHIP REGISTRATION

- 44 — 1. Banking Secrecy
- 50 — 2. Trust and Foundations Register
- 100 — 3. Recorded Company Ownership
- 50 — 4. Other Wealth Ownership
- 95 — 5. Limited Partnership Transparency

LEGAL ENTITY TRANSPARENCY

- 100 — 6. Public Company Ownership
- 100 — 7. Public Company Accounts
- 100 — 8. Country-by-Country Reporting
- 88 — 9. Corporate Tax Disclosure
- 100 — 10. Legal Entity Identifier

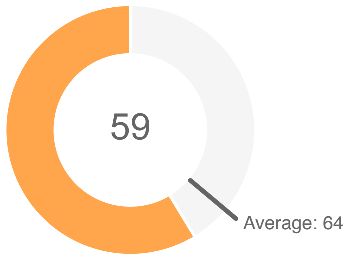
INTEGRITY OF TAX AND FINANCIAL REGULATION

- 53 — 11. Tax Administration Capacity
- 38 — 12. Consistent Personal Income Tax
- 0 — 13. Avoids Promoting Tax Evasion
- 100 — 14. Tax Court Secrecy
- 50 — 15. Harmful Structures
- 60 — 16. Public Statistics

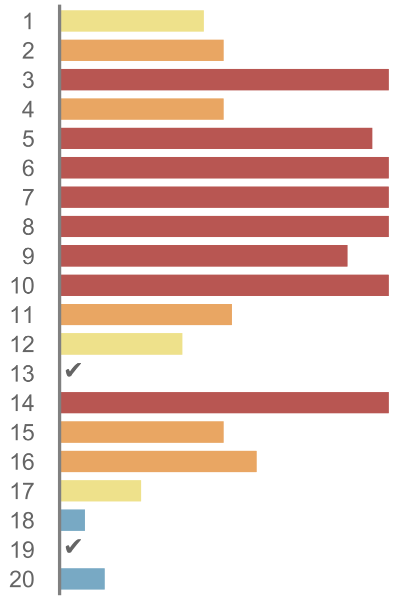
INTERNATIONAL STANDARDS AND COOPERATION

- 25 — 17. Anti-Money Laundering
- 8 — 18. Automatic Information Exchange
- 0 — 19. Bilateral Treaties
- 14 — 20. International Legal Cooperation

Secrecy Score



Key Financial Secrecy Indicators



Notes and Sources

The FSI ranking is based on a combination of a country's secrecy score and global scale weighting (click here to see our full methodology).

The secrecy score is calculated as an arithmetic average of the 20 Key Financial Secrecy Indicators (KFSI), listed on the right. Each indicator is explained in more detail in the links accessible by clicking on the name of the KFSI.

A grey tick in the chart above indicates full compliance with the relevant indicator, meaning least secrecy; red indicates non-compliance (most secrecy); colours in between partial compliance.

This report draws on data sources that include regulatory reports, legislation, regulation and news available as of 30 September 2019 (or later in some cases).

Full data is available here: http://www.financialsecrecyindex.com/database.

To find out more about the Financial Secrecy Index, please visit http://www.financialsecrecyindex.com.