

### XIII. Taxation of Resident Individuals

#### A. Scope of Taxation and Residence

As of January 1, 2003, Israeli resident individuals, are subject to tax on their worldwide income, including capital gains.<sup>778</sup>

Section 1 of the Income Tax Ordinance defines an Israeli resident as a person whose “center of life” is in Israel.<sup>779</sup> In determining residence, several indicators are taken into consideration, for example, permanent home, ties to the community, the location of the nuclear family and economic interests, much like under the center of vital interests test found in tax treaties. Although the term is elaborated in the Ordinance, the center of life of a person can be established differently in various circumstances.

Consequently, in the cases in which the courts have been required to decide on questions of residence, various decisions have been reached in application of differing combinations of the above factors. It is therefore not possible to conclude that the presence or absence of any given factor is decisive; instead the various factors need to be considered from all relevant perspectives.<sup>780</sup>

The Supreme Court’s ruling in *Sapir*<sup>781</sup> is a significant decision regarding the determination of residency status based on a family’s place of residence. The court established that family units can be split for fiscal purposes in appropriate cases, acknowledging that some families choose to live separately, and this should not be a determining factor of residency in the special circumstances of the case. In *Sapir*, although the woman concerned was an Israeli resident, the husband was not regarded as one. Similarly, in *Lederman*,<sup>782</sup> the court determined that a distinction should be made between the taxpayer’s center of life in the United States and his partner’s center of life in Israel. The district court recognized that there may be various reasons for a nuclear family to have separate centers of life and that it is possible to separate the centers of life of spouses, even if their relationship is good. The court emphasized that while a complete separation might support the taxpayer’s claim, this is not always the case, as some couples may maintain a good relationship from a distance, resulting in each spouse having a separate center of life despite their personal closeness.

In the first instance, the following two tests apply for purposes of determining an individual’s center of life and thus his or her residence status in Israel. If either is met, this creates a rebuttable presumption that an individual is resident in Israel, subject to further detailed consideration of the “center of life” test and the factors outlined above that may override this deter-

mination (or *vice versa* — a person not meeting either of the tests below may still have his or her center of life in Israel if the facts so demonstrate):

- (i) Presence in Israel for 183 days or more during the tax year; or
- (ii) Presence in Israel for 30 days or more during the tax year and 425 days during the two preceding tax years.

The days test merely shifts the burden of proof and serves as an additional tool for determining a person’s center of life. Case law and the tax authorities have agreed that days spent in Israel by taxpayers who were in Israel as a result of exceptional circumstances (such as caring for a sick family member) should not be taken into account.<sup>783</sup> The tax authorities focus on the number of days a taxpayer spends in Israel or another country to determine residency in cases where the place of residence is unclear.<sup>784</sup>

Should an Israeli resident decide to exit the country to reside elsewhere, he or she is taxed on a deemed capital gain on the assets he or she holds on the day before he or she leaves Israel. Section 100A in the Ordinance establishes the rules for determining the value of such assets (see V.C.4.b.(11), above).

#### B. Determination of Gross Income

The gross income of an individual is determined in the same manner as that of any other taxpayer. An individual is taxable with respect to all nine categories of income enumerated in section 2 of the Income Tax Ordinance,<sup>785</sup> as well as other sections of the Ordinance, such as section 3. However, a number of items of an individual’s income are exempt from tax.

Most notable among the items of exempt income are the following:

- (i) Severance pay on retirement from employment, up to a maximum amount set by the Ordinance based on the number of years of employment.<sup>786</sup> This amount is a multiple of the last monthly salary and the number of years of employment. In special circumstances, the Director General of the Israel Tax Authority (ITA) is entitled to increase the exemption, but not beyond the statutory limit. Severance pay payable in the event of death is exempt to the extent of a multiple of twice the last monthly salary and the number of years of employment but may not exceed the statutory limit. Again, in special circumstances, the Director General is entitled to increase the exemption, without exceeding the statutory ceiling.
- (ii) Compensation paid as a result of death or bodily injury.<sup>787</sup>
- (iii) The higher of: any part of a pension paid by a provident fund or a pension fund managed by an insurance company, derived from a net after tax payment; or 35%

<sup>778</sup>Income Tax Ordinance, s. 2. The section further enumerates the 10 sources of taxable income — see V.C.4.a., above, and Income Tax Ordinance, s. 89.

<sup>779</sup>Income Tax Ordinance, s. 1.

<sup>780</sup>See, *inter alia*, C.A. 477/02 *Aryeh Gonen v. Assessing Officer Haifa*, Missim K/9 (February 2006), E-71; I.T.A.7038/03 + I.T.A. 8017/04 + *Soler Giora v. the Assessing Officer of Jerusalem 3*, Missim K/1 (February 2006), E-143; C.A. 4862/13 *The Assessing Officer of Kfar Saba v. Michael Sapir*, Missim KH/3 (June 2014), (“*Sapir*”) E-139; I.T.A. *Yael Zur v. The Assessing Officer of Haifa*, Missim KH/6 (December 2014), E-211; I.T.A 517/04 *Zaiger v. Assessing Officer Eilat*, Missim T-3, E-37 (2005).

<sup>781</sup>See *Sapir*.

<sup>782</sup>TA 41182-01-19 *Lederman v. Tel Aviv Tax Assessor 5* (published in Taxes Online, March 24, 2021).

<sup>783</sup>24557-02-15 *Yehuda Talmi v. Tax Assessor Kfar Saba*, published in Missim 50/1 (March 2018) p. 20 (21.01.2018) (“*Talmi*”). The decision was affirmed by the Supreme Court (1779/18 *Yehuda Talmi v. Tax Assessor Kfar Saba*, Missim 50/4) on Civil Appeal (December 2020) p. 10 (02.12.2020).

<sup>784</sup>Tax Ruling 9857/12.

<sup>785</sup>Including the “catch-all” of Income Tax Ordinance, s. 2(10).

<sup>786</sup>Income Tax Ordinance, s. 9(7A)(a).

<sup>787</sup>Income Tax Ordinance, s. 9(7).

of a pension received on retirement from work up to the statutory ceiling set by the Ordinance.<sup>788</sup> Where the pension is not received as a result of employment or from a pension fund, 35% of the entire pension is exempt from tax regardless of the amount of the pension,<sup>789</sup> provided it is paid on the individual reaching retirement age.<sup>790</sup>

(iv) Certain income derived by disabled persons from their personal exertions or from any other source, if the income is within the limit set by the Ordinance.<sup>791</sup>

(v) Payments made to an employee resulting from his/her employer's contributions to a provident fund that were nontaxable when paid to the fund.<sup>792</sup>

(vi) Profits accruing from contributions of employers or self-employed persons to educational funds,<sup>793</sup> provided certain qualification periods, set out in section 9(16A)(a) of the Ordinance, have elapsed when the deposit matures.

(vii) The value of employees' travel to and from work,<sup>794</sup> provided the travel is necessary due to the location and conditions of work and is organized in a collective fashion for the employees and in accordance with the terms set down by the Commissioner.

(viii) Linkage differentials and interest accruing on compensation paid for a delinquency in the payment of employment income.<sup>795</sup> Where the compensation is paid with respect to employment income exceeding a prescribed ceiling, the part of the compensation awarded for that element of income that would have been paid as income tax, had the income been paid when due, is in fact regarded as and paid as tax.<sup>796</sup>

(ix) Certain allowances paid to taxpayers wounded or disabled as a result of military operations or to dependents of soldiers who died as a result of acts of war.<sup>797</sup>

(x) Maternity grants; widows' allowances and other survivors' allowances; and old age allowances paid by the National Insurance Institute.<sup>798</sup>

(xi) Allowances received by victims of Nazi persecution.<sup>799</sup>

<sup>788</sup> Income Tax Ordinance, s. 9B.

<sup>789</sup> In November 2024, a proposal for the Economic Efficiency Law was published in the Official Gazette, which includes a proposed amendment to Income Tax Ordinance, s. 9A extending the 52% tax exemption rate for qualifying pensions, pension buyouts and exempt capital balances for the year 2025 and beyond.

<sup>790</sup> Income Tax Ordinance, s. 9B.

<sup>791</sup> Income Tax Ordinance, s. 9(5). The District Court has held that compensation paid by a company to a disabled shareholder for his services as an employee should be at arm's length, and any excess paid to the shareholder should be viewed as a deemed dividend, which qualifies for less favored tax-exemption. I.T.A. 278/01, 322/01 *Asher Korenbloom v. Assessing Officer Ako*, Mism R-6 (Dec. 2004), E-140.

<sup>792</sup> Income Tax Ordinance, s. 9(17).

<sup>793</sup> Income Tax Ordinance, s. 9(16A).

<sup>794</sup> Income Tax Ordinance, s. 9(20).

<sup>795</sup> Income Tax Ordinance, s. 9(21)(a).

<sup>796</sup> Income Tax Ordinance, s. 9(21)(b).

<sup>797</sup> Income Tax Ordinance, s. 9(6).

<sup>798</sup> Income Tax Ordinance, s. 9(6c).

<sup>799</sup> Income Tax Ordinance, s. 9(6).

(xii) Allowances paid to invalids under the National Insurance laws of a foreign country.<sup>800</sup>

(xiii) Alimony paid to a person, whether for himself or for his/her children by his/her spouse, or by a former spouse or received from the National Insurance Institute.<sup>801</sup>

(xiv) Passive foreign income of new immigrants, veteran returning residents, and Returning Residents deriving from assets they owned during five to ten years of residence and foreign business income earned during the first four years after immigration (see XVII.B.1., below).

(xv) Interest on a foreign currency deposit accruing to an Israeli resident during the first 20 years after his/her immigration to Israel if the source of the deposit dates to pre-residence days and the deposit was made within 90 days of the transfer of the fund to Israel.<sup>802</sup>

(xvi) Certain rental income derived by a resident employee on a change in his/her place of work (the exemption results from the allowing of rental expenses as a set off against rental income).<sup>803</sup>

(xvii) Rental income (up to a statutory limit) derived by an individual under the Income Tax Law (Exemption from Tax on Income Derived from Rental of Residences) 1990.

(xviii) Non-business linkage differentials on government bonds and on bank deposits.<sup>804</sup>

(xix) Exchange differentials received by a nonresident on a loan made in foreign currency unless made by an Israeli permanent establishment (PE) of the nonresident.<sup>805</sup>

(xx) Life insurance proceeds (only the "risk" proceeds), unless paid to a nonrelative, where the premium was not allowed as a deduction in the computation of the policyholder's taxable income.<sup>806</sup>

(xxi) Proceeds received by a nonresident under a policy insuring the nonresident against changes in the exchange rate of the Israeli Shekel with respect to the principal of a loan made by the nonresident in foreign currency.<sup>807</sup>

(xxii) Linkage differentials accruing: on compensation payable on the expropriation of property; on compensation payable because of a loss in the value of real estate as a result of a building plan; on the consideration received for the sale of property where the sale is taxable, except in the case of property used for business or professional purposes; on account of the cancellation of a transaction to acquire property; and with regard to a loan made to another

<sup>800</sup> Income Tax Ordinance, s. 9(6E).

<sup>801</sup> Income Tax Ordinance, s. 9(22).

<sup>802</sup> Income Tax Ordinance, s. 16; Income Tax Order (Exemption from Tax on Interest on Foreign Currency Deposits), 2002, s. 2.

<sup>803</sup> Income Tax Ordinance, s. 17(2) and (12).

<sup>804</sup> Income Tax Ordinance, s. 9(13).

<sup>805</sup> Income Tax Ordinance, s. 9(15).

<sup>806</sup> Income Tax Ordinance, s. 9(19).

<sup>807</sup> Income Tax Ordinance, s. 9(15A).

person (on condition that the loan was not made as part of the taxpayer's business or profession).<sup>808</sup>

(xxiii) Capital gains derived from the sale of a "qualifying residential apartment," as defined in the Taxation of Land (Appreciation and Purchase) Law, 1963 (see XVII.M., below).

(xxiv) Capital gains derived: from gifts to the state, a local authority or other public institutions;<sup>809</sup> from the realization of an asset held outside Israel and sold within 10 years of immigration; on the sale of personal belongings; and from the receipt of "key money," but only with respect to premises used for residential purposes.<sup>810</sup>

(xxv) Scholarships for students during their studies at higher educational institutions and for researchers during their studies at research institutions or religious research institutions not in excess of NIS 90,000, as long as no consideration was given for the scholarship.<sup>811</sup>

### C. Allowances, Deductions and Credits

In 1975, the Israeli tax system underwent a major reform, as a result of which personal deductions were replaced by a "credit system." In effect, the credit system permits the paying of allowances based on the taxpayer's personal status or circumstances. Many personal deductions were not transformed into credits. Instead, they found their way into pensions, or increased allowances granted by the National Insurance Institute, or other forms of compensation. For example, the deduction for soldiers serving compulsory military service was replaced by an increase in pay accorded directly to the soldiers.

Under the current system, "credit points" are differentiated from "allowance points." A "credit point" is an amount adjusted annually to meet the inflation rate (for 2023, NIS 235 per month or NIS 2,820 annually), and is deducted from the tax owed once calculated on the net taxable income.<sup>812</sup> By contrast, an "allowance point" is an amount actually paid to the taxpayer regardless of whether the taxpayer derived taxable income or the fact that his/her liability to income tax did not reach the amount of the allowance payable to him.<sup>813</sup> In effect, the allowance points were the seeds of a negative income tax system, which was enacted in 2007. The law grants monthly payments for low-salaried employees (NIS 2,060 to NIS 6,750). Currently the law applies only to employees in certain areas of the country.<sup>814</sup> Grants under the law are conditional on the recipient deriving employment income.

The following credits are available:

	Taxpayer	Credit Points
(i)	Resident (also granted to a spouse filing a separate return) <sup>815</sup>	2 ¼
(ii)	Resident individual maintaining his/her spouse, if the taxpayer or his/her spouse has reached "retirement age," or is blind or disabled as defined by the ordinance <sup>816</sup>	1
(iii)	Travel to the place of gainful employment <sup>817</sup>	¼
(iv)	The registered spouse, where his/her income is assessed jointly with the income derived from personal exertion of the other spouse in addition to the first two credits mentioned above. <sup>818</sup>	
	• entitled to credit points with respect to children	1 ¾
	• not entitled to credit points with respect to children	1 ½
	• travel credit	¼
(v)	Spouse assisting in business or vocation or on an agricultural farm (return filed jointly), in addition to (ii) and (iii) above, and provided that, if entitled to credit points with respect to spouse as specified in (iv) above, he/she opted for one of the following two alternatives. <sup>819</sup>	
	• entitled to credit points with respect to children	1 ¾
	• not entitled to credit points with respect to children	1 ½
(vi)	Parent in a single parent family: <sup>820</sup>	
	• for each child during the year of birth	1 ½
	• for each child 1–5 years old	2 ½
	• for each child 6–18 years old <sup>821</sup>	1
	• for each child during the year in which he/she turns 18 years old	½
(vii)	A father in a single parent family that is not entitled to a credit according to item (vi) <sup>822</sup> or father whose wife is entitled to a credit according to item (xi). <sup>823</sup>	
	• for each child during the year of birth	1 ½

<sup>815</sup> Income Tax Ordinance, s. 34.

<sup>816</sup> Income Tax Ordinance, s. 37.

<sup>817</sup> Income Tax Ordinance, s. 36.

<sup>818</sup> Income Tax Ordinance, s. 38.

<sup>819</sup> Income Tax Ordinance, ss. 67 and 39.

<sup>820</sup> Income Tax Ordinance, s. 40(b)(1). See also Israeli Tax Authorities Circular 2/2014 re Credit Points Under Section 40 — Joint Parental Custody.

<sup>821</sup> On May 18, 2022, the Law of Increasing Credit Points for Parents with regards to Income Tax (Temporary Provision) 2022 was published in the Law Book 2972. Based on the Temporary Provision, a parent of a child who is between 6 and 12 years in tax year 2022, will be entitled to an additional credit point for the child. On April 20, 2023, the law was amended and published in Law Book 3039. Based on the amendment, a parent of a child who is between 6 and 12 in the tax year 2023, will be entitled to an additional credit point.

<sup>822</sup> Income Tax Ordinance, s. 40(b)(1a).

<sup>823</sup> Income Tax Ordinance, s. 66(c)(5).

<sup>808</sup> Income Tax Ordinance, s. 9(13A); Income Tax (Exemption from Linkage Differentials) Order, 1984.

<sup>809</sup> Income Tax Ordinance, s. 97(a)(4).

<sup>810</sup> Income Tax Ordinance, s. 88.

<sup>811</sup> Income Tax Ordinance, s. 9(29).

<sup>812</sup> Income Tax Ordinance, s. 33A.

<sup>813</sup> Income Tax Ordinance, s. 33A.

<sup>814</sup> The Law for the Increase of Engagement in Employment and for the Reduction of Income Gaps (Negative Income Tax), 2007.

	• for each child 1–5 years old	2 ½
(viii)	A parent in a single parent family who is a widow or widower and is entitled to a credit according to item (vi) or (vii)	1
(ix)	A separated parent who is entitled to credit according to item (vi) and where separated parents are sharing their children's support, if the parent is not living with the children (and therefore not entitled to credit points with respect thereto) <sup>824</sup>	1
(x)	A woman <sup>825</sup>	½
(xi)	A wife (filing separate return), mother of children under age 18, for each child. <sup>826</sup>	
	• during the year of birth	1 ½
	• ages 1–5	2 ½
	• ages 6–18	1
	• during the year in which he/she turns 18	½
(xii)	• For each child that in 2022 is between the ages of 6 and 12 <sup>827</sup>	1
	• For each child that in 2023 is between the ages of 6 and 12 <sup>828</sup>	1
(xiii)	New immigrant: where the registered spouse's income includes the income of a new immigrant spouse, the following credit points are granted provided the income of the nonregistered spouse does not exceed a certain amount. If it does exceed that amount, separate computations (returns) are made, and the points are not taken into consideration in the computation of the registered spouse's tax assessment. <sup>829</sup>	
	• during first 12 months	1 (½ per month)
	• during next 18 months	4 ½ (¼ per month)
	• during the next 12 months	2 (⅓ per month)
	• during the next 12 months following above 12 months	1 (⅓ per month)
(xiv)	Resident or spouse having a paralyzed, blind, or retarded child <sup>830</sup>	2
(xv)	Remarried divorced person or his/her current spouse liable for alimony to former spouse <sup>831</sup>	1
(xvi)	Resident holding academic degree: (i) BA — one credit point for the shorter of three years	1 or ½

<sup>824</sup> Income Tax Ordinance, s. 40(b)(2).

<sup>825</sup> Income Tax Ordinance, s. 36A.

<sup>826</sup> Income Tax Ordinance, s. 66(c)(3).

<sup>827</sup> Income Tax Ordinance, s. 66(c).

<sup>828</sup> Income Tax Ordinance, s. 40(c)(1).

<sup>829</sup> Income Tax Ordinance, s. 35.

<sup>830</sup> Income Tax Ordinance, s. 45.

<sup>831</sup> Income Tax Ordinance, s. 40A.

	or the period of study, or (ii) MA — ½ credit point for the shorter of two years or the period of study. <sup>832</sup>	
	It should be noted that, according to the provisions of the Law for the Change of National Priorities (Legislative Amendments for Achieving Budgetary Goals for the Years 2013 and 2014), 2013 the aforementioned credit points with respect to academic degrees are limited to a period of one year. This temporary provision is applicable only to students who graduated from January 1, 2014, through December 31, 2022.	
(xvii)	Resident entitled to a professional diploma for one year commencing on the year after receiving the diploma or one year later. <sup>833</sup>	1

These credits are available under the Income Tax Ordinance as indicated in the relevant footnotes to the above and are not in lieu of the “allowance points” paid by the National Insurance Institute.

In addition to the above “credit points,” the following special personal credits and deductions are available:

(i) An individual is accorded a tax credit for amounts paid for life insurance and/or as payments to a provident fund (unless allowed as a deduction); however, the credit is limited to a specified maximum amount.<sup>834</sup>

Where the provident fund is a comprehensive pension plan (i.e., pension payments for invalids and for survivors), the credit rate is 35% of the amount contributed to the plan, but may not exceed the designated statutory ceiling.<sup>835</sup> Self-employed persons and employees for whom their employer did not make a contribution to a provident fund or pension fund may deduct from their income with respect to payments made to such funds 7% and 5% respectively,<sup>836</sup> but may not take deductions in excess of a statutory designated ceiling.<sup>837</sup> Where payment is made to secure a future pension, an additional deduction is allowable at the rate of 4%, again subject to a statutory ceiling. Of course, in no event may the deduction exceed the amount actually paid to the fund.

(ii) A special credit is granted for charitable contributions.<sup>838</sup> The credit is up to 35% of the amount contributed and is limited to the lower of 30% of taxable income, or a ceiling set by the Income Tax Ordinance (NIS 9 million for 2022) subject to restrictions stated in the Ordinance.<sup>839</sup> Excess credit may be carried over to the three succeeding tax years.

<sup>832</sup> Income Tax Ordinance, s. 40C.

<sup>833</sup> Income Tax Ordinance, s. 40D.

<sup>834</sup> Income Tax Ordinance, s. 45A.

<sup>835</sup> Income Tax Ordinance, s. 45A(b).

<sup>836</sup> Income Tax Ordinance, s. 47(b).

<sup>837</sup> Income Tax Ordinance, s. 47(a)(1).

<sup>838</sup> Income Tax Ordinance, s. 46.

<sup>839</sup> Income Tax Ordinance, s. 46A.

(iii) A credit is allowed for a youth or for his/her spouse that have reached the age 16 but not yet 18.<sup>840</sup>

An individual paying national insurance contributions<sup>841</sup> (and, until 1997, “parallel tax”) with respect to income not derived from employment is entitled to a deduction at the rate of 52% of the amount paid by him (excluding penalties paid with respect to the above), provided the deduction does not exceed his/her chargeable income before the deduction.<sup>842</sup> Where an employer is exempt from national insurance contributions on account of his/her employee, the latter is entitled to deduct from his/her income the contributions imposed on him.

#### D. Tax Rates and Calculation of Taxable Income

There are two income tax brackets: (i) a bracket for tax on personal exertion income, and all income of an individual aged 60 and above (which applies provided that books of account were kept where so required); and (ii) a bracket for tax on other ordinary income. Certain passive income enjoys reduced rates.

The tax brackets are linked periodically to the cost-of-living index<sup>843</sup> to prevent inflation from causing a steeper tax rate to apply to what, in effect, is the same real income.

The tax rates are as follows:<sup>844</sup>

Income Brackets and Tax Rates for 2024			
Any income other than personal exertion of Individuals Below Age 60		Personal exertion income or any income for individuals above 60	
Annual Income	Tax Rates	Annual Income	Tax Rates
		Up to NIS 84,120	10%
		NIS 84,121 – 120,720	14%
		NIS 120,721 – 193,800	20%
Up to NIS 269,280	31%	NIS 193,801 – 269,280	31%
NIS 269,281 – 560,280	35%	NIS 269,281 – 560,280	35%
NIS 560,281 – 721,560	47%	NIS 560,281 – 721,560	47%
Above NIS 721,560	50%	Above NIS 721,561*	50%
* An additional levy at the rate of 3% + an additional 2% on “capital”-source income is imposed on income exceeding NIS 721,560 (in 2025 <sup>845</sup> ).			

<sup>840</sup> Income Tax Ordinance, s. 40B.

<sup>841</sup> As of 1995, such payments include national health insurance. See II.E.7.

<sup>842</sup> Income Tax Ordinance, s. 47A.

<sup>843</sup> A new law has been passed that freezes tax updates for the years 2025–7, meaning no adjustments will be made according to the Consumer Price Index. The savings resulting from this measure will continue to affect the year 2028 and beyond, including with respect to adjustments to income tax brackets, tax credits, exemptions and social benefits.

<sup>844</sup> Tax rates for 2013 and subsequent years, as provided for under the Reduction of Deficit and Changes in Tax Burden Law, 2012, of August 2012.

<sup>845</sup> The law states that the surtax rate on taxable income from “capital” sources would be increased by an additional 2%. “Capital” source-income includes, among other things: dividends; interest; capital gains; rental income; and capital gains from the sale of real estate rights. It should be noted that the proposal to extend the surtax to all capital gains from the sale of a residential property that are not exempt was not accepted, and the existing provision in the Ordinance, which imposes the surtax only on capital gains exceeding 5,382,285 shekels, remains unchanged.

#### E. The Tax Unit

The general rule in Israel calls for the joint computation of the income of spouses. Section 65 of the Income Tax Ordinance provides that “For the purposes of this Ordinance, the income of spouses shall be deemed to be the income of the registered spouse and shall be charged in his/her name.”

An important exception to this rule is found in section 66 of the Income Tax Ordinance, which allows a spouse to compute his/her income separately if the spouse’s income is derived from “personal exertion in any business or vocation or from employment...”<sup>846</sup> Eligibility for separate assessments was conditional on the non-dependence of the source of the income of one spouse on the source of the income of the other spouse.<sup>847</sup> Prior to Amendment no. 199 (as detailed below), the Ordinance contained specific provisions aimed at defining the dependence of one source on another source. For purposes of determining whether income is dependent or independent, the Ordinance provided that the income of one spouse was *not* regarded as generated from an independent source if it was derived from:

(i) Any business or vocation of the other spouse;

(ii) A company in which both spouses or the other spouse directly or indirectly, had the right of management or the right to 10% of the voting rights, unless the recipient of the income had income from the company for a reasonable time, and at least for one year before the marriage, or for five years before his/her spouse, directly or indirectly, had any right in the company; or

(iii) A partnership in which both spouses or the other spouse, directly or indirectly, owned at least 10% of the capital or of the rights to the profits, unless the recipient of the income had income as aforesaid from the partnership for a reasonable time, and at least for one year before the marriage or for five years before his/her spouse, directly or indirectly, had any right in the partnership.<sup>848</sup>

Although the common wisdom was that these presumptions were non-rebuttable, the Supreme Court held in a landmark decision that taxpayers may rebut the presumptions by proving that despite the “dependence” under the presumption, the spouse derives personal exertion income independently.<sup>849</sup> Following that holding, the District Court held that a wife who worked together with her husband in their joint business successfully overcame the presumption that her income had been derived from a source dependent on that of her husband and, therefore, was assessed separately.<sup>850</sup>

Naturally, a separate assessment, in most cases, proved more favorable to a couple because it allowed the progressive

<sup>846</sup> Including income from personal exertion within the meaning of paras. 1–7 of the definition of that term in Income Tax Ordinance, s. 1.

<sup>847</sup> Income Tax Ordinance, s. 66(d).

<sup>848</sup> Income Tax Ordinance, s. 66(d).

<sup>849</sup> C.A. 900/01 *Kelles v. Assessing Officer Tel-Aviv 4*, Missim Q/3 (June 2003), E-9.

<sup>850</sup> I.T.A. 1250/05 *Shkuri v. Assessing Officer Kfar Saba*, Missim W/4, E-151 (2009). In I.T.A. 540/08 *Malkiely v. Assessing Officer Ashkelon*, Missim W/4, E-191 (2009), the Be’er-Sheva District Court, in an obiter dictum, criticized the holding in *Shkuri*.

scales of taxation to be applied separately to the income of each spouse. Nowadays the courts seem to view separate assessments with greater favor.<sup>851</sup> As of 2012, married taxpayers jointly engaged in a business were allowed to opt for a separate computation if they met the stringent requirements of the law and the income of one spouse did not exceed NIS 48,960 per annum. However, in a case where both spouses worked together in a company in which the husband held 96% of its shares, the Supreme Court overturned this rule and held that in the case where income of a spouse is derived from a company in which the other spouse holds at least 50% of its shares, the income of both spouses would be assessed jointly.<sup>852</sup>

A 1998 amendment<sup>853</sup> added section 65A to the Ordinance, which provides that a tax file managed by the Assessing Officer with respect to the income of a couple must carry the names of both the husband and the wife.

Amendment no. 89 to the Income Tax Ordinance, which has been in effect since January 1993, retained most of the substantive provisions with respect to joint assessments but removed the gender distinction between the spouses. The amendment added a provision<sup>854</sup> concerning the prenuptial assets of a spouse and inherited property received during the matrimonial period. With respect to gains from such property, separate assessments are allowed. Other “non-personal exertion gains” were computed jointly by being added to the income of the spouse whose personal exertion income is higher or, if there is no such income, to the income of the “registered spouse.”

The “registered spouse” is the spouse having the higher income of the two spouses in the two years *preceding* the tax year under review; however, the spouses may jointly give notice — at least three months before the beginning of the tax year — informing the assessing officer which of them is to be the “registered spouse.” Where they have done so, or where the assessing officer determined the registered spouse, the registration is in effect for at least five tax years, unless the individuals concerned are no longer spouses or the Commissioner decides otherwise.<sup>855</sup>

Following the Supreme Court’s ruling in the *Malkiely*<sup>856</sup> case, the provisions with respect to the eligibility of separate assessments of couples with dependent sources of income were significantly altered in Amendment no. 199 of the Israeli Income Tax Ordinance effective as of January 1, 2014. Amendment no. 199 abolished the provisions of sections 66(d) and (e) and set forth requirements with respect to couples desiring that their assessment be calculated on a separate basis. These requirements are discussed above.

<sup>851</sup> I.T.A. 510/99 *Itach v. Assessing Officer Ashkelon*, Missim O-1 (Feb. 2001), E-190; I.T.A. 7/95 *Kardi v. Assessing Officer Ashkelon*, Missim L-6 (Dec. 1998), E-116; I.T.A. 542/06 *Les. v. Assessing Officer Eilat*, Missim W/2, E-260 (2009).

<sup>852</sup> C.A. 8114/09 *Malkiely v. Assessing Officer Ashkelon*, Missim 26(1), E-68A.

<sup>853</sup> Law for the Amendment of the Income Tax Ordinance (No. 77), 1988.

<sup>854</sup> Income Tax Ordinance, s. 66(b).

<sup>855</sup> Income Tax Ordinance, s. 64(b).

<sup>856</sup> C.A. 8114/09 *Malkiely v. Assessing Officer Ashkelon*, Missim 26(1), E-68A.

## F. Capital Gains

Capital gain refers to the profit from the sale of a capital asset, such as real estate, stock or other investments. Capital gain is calculated as the difference between the selling price of the asset and the original purchase price. If the selling price is higher than the purchase price, it is a capital gain. In other words, capital gain is the nominal profit from the sale, while inflation is taken into account when calculating the capital gain tax. This is done by distinguishing between the real capital gain, and the inflationary amount. Distinguishing between the two is important, since real capital gain is taxable, while the inflationary amount is not taxable.

Capital gains are considered chargeable income, whether it is an Israeli resident who produced capital gain in Israel or abroad by the sale of assets, or a foreign resident who produced capital gains on the sale of the following:<sup>857</sup>

- (i) Assets located in Israel;
- (ii) Assets located abroad located abroad that are essentially a direct or indirect right to an asset or inventory, or that are an indirect right to a real estate right or to an asset in a real estate association located in Israel. The taxation applies only in respect of the part consideration that stems from the property located in Israel;
- (iii) Assets that are a share or the right to a share in an Israeli entity;
- (iv) Assets that are a right in a foreign resident entity, which in essence is the owner of a direct or indirect right to property located in Israel. The taxation applies only with respect to the part of the consideration that stems from property located in Israel.

An individual is liable to tax on real capital gains that accrued from January 1, 2012, at a rate that is no greater than 25%;<sup>858</sup> if the real capital gain accrued before January 1, 2012, the tax rate is 20%. In the case of sales of company stocks, this rule applies only where the seller did not hold a substantial amount of the stock within 12 months preceding the sale. A substantial shareholder in this context is one who holds control of at least 10% of the company stock by any means. If this condition is not met, the seller will be subject to a tax rate that does not exceed 30% for capital gains accrued from January 1, 2012; a tax rate of 25% applies for capital gains accrued before January 1, 2012. The tax on the inflationary amount (i.e., 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) is 10%.<sup>859</sup>

Once an asset has been sold, the seller must submit a form to the Assessing Officer within 30 days after the sale, specifying the calculations of the capital gains or capital loss, and the tax calculation in respect of the sale. The seller must pay an advance in the amount of the tax that applies to the profit.<sup>860</sup> Cap-

<sup>857</sup> Income Tax Ordinance, s. 89.

<sup>858</sup> Income Tax Ordinance, s. 91.

<sup>859</sup> Income Tax Ordinance, s. 91(c).

<sup>860</sup> Income Tax Ordinance, s. 91(d)(1).

ital gains shall be exempt from tax if it arises out of one of the following circumstances:<sup>861</sup>

- (i) The sale on a non-convertible bond traded in the TASE, provided that the bond was issued before May 8, 2000, and was listed for trading on the TASE before January 1, 2003;
- (ii) The sale of a bond or a bond with warrants issued by the state or guaranteed by it, provided that the bond was issued or guaranteed before May 8, 2000;

(iii) A gift to the state, to a local authority, or to a public institution (according to the meaning in section 9(2) to the ordinance);

(iv) A gift to a relative, and a gift to another individual, if the assessing officer was convinced that the gift was given in good faith, and the gift recipient is not a foreign resident; and

(v) An individual's capital gain from the sale or redemption of a unit in a chargeable trust fund.

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<sup>861</sup>Income Tax Ordinance, s. 97.

