

MEMORANDUM

FROM: George Rosenberg / Inbal Faibish
RE: Increased tax benefits for new immigrants and returning residents
DATE: September 11, 2008

On September 9th, 2008 the Israeli Parliament (the "Knesset") adopted an important amendment of the Income Tax Ordinance ("the Amendment") regarding the taxation of New Residents and Returning Residents. The Amendment will be in force upon publication in the Official Gazette ("Rashumot"), and includes the following benefits:

- New Residents will enjoy tax and reporting exemptions on every type of income, both ordinary and capital gains¹, which is not sourced in Israel, for a period of 10 years.
- In their first year as residents, New Residents will be entitled to a tax-free "adaptation year".
- A non-resident company, which is controlled by a New Resident, will not be deemed resident even if its business is managed and controlled by the New Resident from Israel, and consequently any income derived from such company by the New Resident, during his first ten years of residence in Israel, will be tax exempt.
- Returning Residents, who have lived out of Israel for over 10 years, will be entitled to the same benefits as New Residents above. Transitionally, Returning Residents who have returned to Israel after January 2007 or will return until December 31, 2009 will be eligible for the same benefits even if they were non-residents for only five years prior to their return.
- Returning Residents who returned before January 1 2007, after having been non-residents for at least three years, will continue to enjoy the current five-year exemption from certain passive income and the current ten-year exemption from capital gains.² Returning Residents who will return from January 1, 2010 onwards, after having been non-residents for at least six years, but less than ten, will be eligible for the same benefits as those who returned before January 1, 2007.

Finally, in order to avoid the inherent uncertainty in the definition of "non-resident" (foreign resident), the definition has been eased so that any Israeli resident who has resided abroad for four consecutive years, will be deemed non-resident from the first day that he resided abroad,

¹ The ten-year exemption re capital gains already exists under current law; it does not terminate at the end of the ten-years, but continues on a proportionately reduced basis calculated on the proportion between the period from the end of the ten years to date of sale, and the period from the date of acquisition to the date of sale.

² See footnote 1.

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even if he is able to satisfy the test of having shifted the centre of his life abroad only for the third and fourth year.

Following is a comparison between the current situation and the new law:

Subject	Current situation	Amendment
Tax exemption on foreign passive income (not including capital gains)	New Residents and Returning Residents (3-year absence) enjoy five-year exemption	10-year exemption, both for New Residents and Returning Residents (10-year absence)
Tax exemption on foreign business/vocational/salaried income	New Residents enjoy 4-year exemption from business income only, provided the business was owned by the new resident at least five years prior to his arrival to Israel	10-year exemption, both to New Residents and Returning Residents on all three types of income, without the existing restrictions.
Tax exemption on capital gains	10-year exemption, both for New Residents and Returning Residents (3-year absence)	10-year exemption, both for New Residents and Returning Residents (6-year absence)
Companies controlled by a New Resident or a Returning Resident	No legislation	In the first 10 years the company will not be subject to the "management and control" residence test, and its income will be exempt.
Adaptation period	No legislation	First year from the date of immigration to be a tax-exempt "adaptation period", for both New Residents and Returning Residents
Reporting duties	Exemptions apply under certain conditions	No reporting obligations, for both New Residents and Returning Residents

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This memorandum is by way of a general guide only and should not be regarded as a legal opinion, or relied upon without seeking legal advice. Moreover, this memorandum is subject to fine-tuning once the official text of the Amendment will be published.

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September 2008

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