

# Doing Business in Israel

This document describes some of the key commercial and taxation factors that are relevant on setting up a business in Israel.



## Background

### Country overview

Israel known also as SUN – Start Up Nation is a 20,770 square km middle east country with a population of 8.8 million people. 80% are Jews, 19% Arabs and 1% others. The official languages are Hebrew Arabic and English and after the big immigration from Russia in the 90's Russian is also very common.

Israel is highly urbanized and economically developed country. The main sea ports are Eilat in the south, Ashdod in the center and Haifa in the North. Ben Gurion Airport is the main airport in Israel and is located in Lod – in the center of Israel.

Israel's parliament – the Knesset is elected every four years at general election where the voters elect a Party. The Prime Minister is the head of the party who received most votes or was able to form a coalition. The President has mainly a representative role.

The country's main problem is the conflict with the neighbor Arab countries and the Palestinians.

### Economic overview

According to the Doing Business report of the World Bank Group Israel is ranked in the 54th place –down 2 places from the previous year report. This is considered a blow to the ease of doing business target considered to be very important by our Prime Minister. Israel is ranked in the 130th place in the easiness of registering properties and 89th place in the easiness of enforcing contracts.

In the last 10 years large reserves of offshore gas have been discovered but Israel still depends on imports of crude oil. Other imports are raw materials, grains and military equipment. The Shekel is considered to be a stable currency and in the last years Israel has a budget surplus. Approximately half of Israel's foreign debt is owed to the US which is its major source military and economic aid.

SUN – Start UP Nation – Israel is one of the most important technologies centers in the world. With highly army trained and highly motivated work force, supportive government programs, active venture capital funds Israel has fertile environment for innovations. Almost every multinational company has a development center and investments in Israel. Export of software, technology, medical equipment, nano technologies and sale of R&D companies to multinationals contributes to the budget surplus and the strong Shekel.

### Transport infrastructure

Busses are the country's main form of transportation. In the last few years a big investment is made in order to modernize the railway system. As a Jewish country public transportation does not operate on the Shabbat. There are approximately 20,000 km of roads that get to everywhere. Israel has 47 airports the main – Ben Gurion in the center of the country and the Ovda in the south Near Eilat and 3 major sea ports Eilat in the south, Ashdod in the center and Haifa in the north.

## Choice of Legal Form



### Limited liability company

A limited liability company with a share capital is the most common form of business to do business in Israel.

Incorporation is fast and easy. The Registrar of company's fee is about \$ 700, and once you submit the documents it will take a few days to register a company.

The shareholders can be individuals or any registered entity, Israeli or foreign.

Once the company is registered you have to open a bank account in order to open an income tax and VAT files.

The companies tax rate is currently 23% and dividends are taxed at 25% (30% for a substantial shareholder who has 10% or more of the shares of the company).

If there is no Israeli shareholder a fiscal representative must be nominated and registered with the tax authorities.

### Public limited company

A limited liability company can have maximum 50 members, a public limited company must have a least 7 members. According to the Israeli Company's Act a public company is a company that its shares are traded in the stock exchange or its shares were offered to the public. A public company in Israel is regulated by the Israel Security Authority and must comply with its regulations.

### General partnership

Partnerships are less common than companies. Partnership can be either registered with the Registrar of Partnerships or not. In any case a partnership must register with the VAT authorities and gets a special registration number for a partnership.

The maximum number of general partners is 20 and there is a partnership ordinance that governs the relationship between the partners unless otherwise agreed.

### Limited liability partnership

A partnership can be either a general partnership or a limited liability partnership.

In a limited liability partnership usually one partner with a minimal share in the partnership is the unlimited partner and all other partners are limited. This kind of partnership in Israel is common in venture capital partnerships and oil and gas exploration partnership.

### Subsidiary and branch

Many foreign entities have subsidiaries in Israel. Many are R&D centers that were established by the foreign entity, agencies of foreign entities or became a subsidiary after the foreign entity bought the Israeli company. Branches are less common. The main advantage of a branch is that a branch avoids the tax on dividend when profits are paid to the parent company.

The registration of a branch is more complicated than registering an Israeli company as the subsidiary. For legal protection a subsidiary is preferred. In any case if there is no Israeli as an owner an Israeli fiscal representative must be nominated.

### Sole trader

To register as a sole trader is fast and easy. Once you have a bank account you register with the Inland Revenue and with VAT authorities and you can start your business.

There are bookkeeping regulations that are accustomed to the nature of the business, turnover and number of employees. A sole trader will have to prepare a profit and loss account and submit a tax report once a year.

### Nonprofit organization

There are several kind of nonprofit organization in Israel. The most common one are an association or a public benefit company. A nonprofit entity is exempt from paying tax, donation can receive a tax credit and regarding VAT a nonprofit organization cannot claim the VAT on expenses and pays VAT at a reduced rate on salary expenses.

### Setting up and organization

A company must register with the Registrar of Companies. Companies must have at least one shareholder and there is no minimum of the share capital. Registration is fast (will take a few days). A company must have at least one Israeli director and if not must nominate a fiscal representative, that can be an Israeli entity, in order to represent it and take its

liabilities to the tax authorities. A company must have audited financials by an auditor who is registered with the Board of Certified Public Accountants in Israel. Tax reports must also be certified by the auditors and are submitted to the Inland Revenue once a year. The Tax Year ends at December 31 but in some circumstances the tax year can be change to March 31st.

## Audit Requirements



Limited companies and registered entities like foundations, nonprofit organizations and public institutions must be audited by registered auditors in Israel.

## Taxation



For Israeli tax purposes, an Israeli resident is defined as an individual whose center of living is in Israel taking into account the person's family, economic and social links.

An important presumption will apply in either the following circumstances:

- The individual is present in Israel at least 183 days in a tax year ending 31 December,
- The individual is present in Israel at least 30 days in the current tax year, and 425 days cumulative in the current and two preceding tax years.

The center of living test is based on the following criteria:

- Location of permanent home
- Place of residence of the individual and his/her family
- Place where the individual regularly works or is employed
- Location of active and material economic interests
- Place where the individual is active in various organizations, associations or institutions
- An Israeli resident pays tax on his worldwide income.

The current tax rates are:

Annual income level (NIS)	2018 tax rate	Other Income Sources	2018 tax rate
0 – 74,880	10%	Capital gains	25-30%
74,881 – 107,400	14%	Interest	10-35%
107,401 – 172,320	20%	Dividends	15-30%
172,321 – 239,520	31%	Inheritance	None
239,521 – 498,360	35%		
over 498,361	47%		

Income above ILS 641,880 is subject 3% surtax.

### National insurance

	up to 5,944 monthly salary	5,944 - 43,370 monthly salary
Employee's share	3.45%	12.00%
Employer's share	3.45%	7.50%

Additionally, self-employed individuals pay between 5.97%-17.83%.

National insurance payments include the Health Tax payments that cover HMO payments and hospital costs.

### VAT

VAT current rate is 17%. There is transaction at zero rate VAT or that are exempt from VAT. Among such transactions are selling intangible assets and services to foreign residents, services and hotel costs for tourists, fruits and vegetables and residential rentals for a period less than 25 years.

### Corporate tax

Current rate of corporate tax is 23%. Dividends between corporates are tax free. Dividends to a private shareholders are taxed at 25% however dividends to shareholders of 10% or more of the company's capital are taxed at 30%. At this rate the corporate tax plus tax on dividends equals to the highest rate of income tax.

### New immigrants and returning citizens

New immigrants and returning citizens are exempt for 10 years on reporting and paying tax on income that its source is outside Israel.

### Foreign residents' taxation in Israel

The territorial tax regime still applies for foreign residents in Israel. A foreign resident will pay tax on his business and capital income that were generated in Israel subject to tax treaties.

As from 2009 there are exemptions on Israeli income earned in Israel by a foreign resident among them are:

Interest, discount fees, and index income on corporate bonds. Capital gains on nonmarketable securities and capital gains on marketable securities.





## Allowances



### Depreciation

Depreciation is recognized on a straight line method base on the cost of the asset.

Rate of Depreciation	%
Buildings	1.5 - 4
Furniture and fixings	6 - 12
Machinery	7 - 25
Cars	15
Electronic equipment	15
Computers	33

### The arm's length principal

In an international deal where special relation exists between the parties and as a result of these relations a different price or conditions were determined, such a deal must be reported for tax as it was done at market price and conditions. Such a deal must be revealed in the yearly tax reports and be indicated what method was used to determine the market price and conditions.

The tax payer can apply for a pre ruling to determine the criteria he must stand up to.

According to market pricing regulations a survey of market conditions must be prepared in order to determine if the international deals between the related parties are at market price.

## Employment



### National insurance

National Insurance (includes Health Tax) is paid at the following rates:

	up to 5,944 monthly salary	5,944 - 43,370 monthly salary
Employee's share	3.45%	12.00%
Employer's share	3.45%	7.50%

Additionally, self-employed individuals pay between 5.97%-17.83%.

### Labor and employments laws

The law to increase the enforcement of labor laws is just one of the laws in Israel that controls every aspects of employer employee relationship. You will find the work and rest hours, days of joy and mourning, sick leave, convalescence, women's labor law, youth work, severance pay, and wage delay compensation are just some of these laws.

Usually an employee is entitled to severance pay at the rate of one month per year of employment. The employer pays to a pension and disability fund 6.5% - 7.5% of the salary with a 6% payment by the employee. Payment to an education fund is 7.5% employer and 2.5% employee.

According to law the employer must pay a foreign worker the same salary paid to an Israeli, take care of his medical insurance and social rights and save in a fund for foreign workers and the money in the fund will be paid to the worker once he leaves Israel.

### Employment of foreign staff

Foreign staff are divided in Israel to two main categories

1. Foreign experts and certified experts
2. Foreign worker

Foreign experts are experts in their fields who were invited to Israel by an Israeli resident who need the expertise of the foreign expert. They have a permit to stay and work in Israel and they earn more than twice the average salary (currently  $7,920 \times 2 = \text{NIS } 15,820$ ). They pay tax at the regular Israeli rate but can deduct living expenses for 12 month.

Certified experts are experts that are invited by an owner of a factory to work at the factory. Their salary is subject to 25% tax

Both foreign experts and certified experts are highly paid and are invited to work in Israel because of their expertise.

A foreign worker is a very low paid employee who receives a working permit because they are employed at areas of work like agriculture, building, nursing manpower contractors that Israelies do not like to work.

## Withholding Taxes



As a general rule payment to foreign person is taxed at flat rate of 25% unless there is a reduced rate or exemption according to a tax treaty.

Banks are obliged to deduct 25% when transferring payments abroad unless the payment falls under the list of exemptions or the payer supplies an exemption from the tax authorities.

An Israeli business must deduct at source tax on payments for assets and services. The percentage, up to 35%, is determined by nature or turnover of the business but exemptions are very common especially if the payee is in a loss or pays tax advances.

## Miscellaneous



### Vat registration

Vat registration is fast and easy.

A sole trader will get the same registration number as his ID. A company or a registered entity the same number as the registration number of the entity. In order to register you need a bank account and fill in a simple document.

Separate businesses can under some situations get one VAT registration number and act as they are one business.

Foreign entities who want to register must nominate an Israeli fiscal representative that can be either a person or an entity that conducts business in Israel.

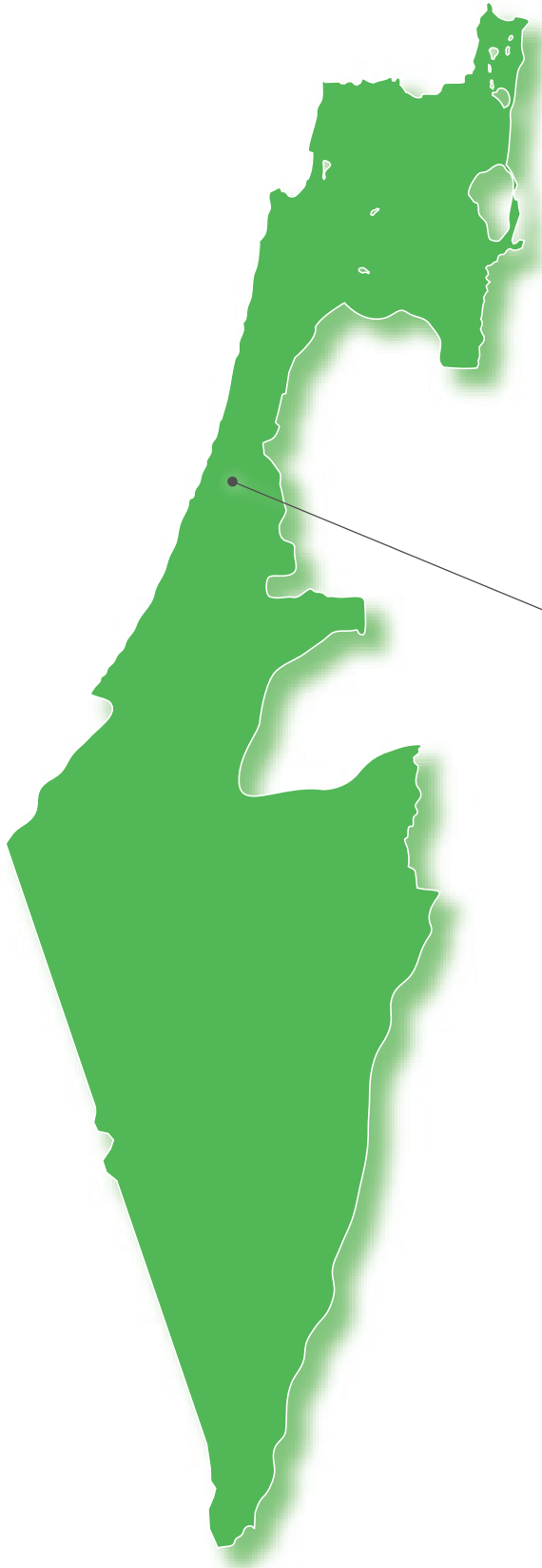
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For further information on the services available from the DFK member firms in Israel please see overleaf.



Last updated April 2019



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