Narrative Report on Israel

Israel is ranked at 38th position on the 2013 Financial Secrecy Index. This ranking is based on a combination of its secrecy score and a scale weighting based on its share of the global market for offshore financial services.

Israel has been assessed with 57 secrecy points out of a potential 100, which places it in the lower mid-range of the secrecy scale (see chart 1).

Israel accounts for less than 1 per cent of the global market for offshore financial services, making it a tiny player compared with other secrecy jurisdictions (see chart 2).

Chart 1 - How Secretive?

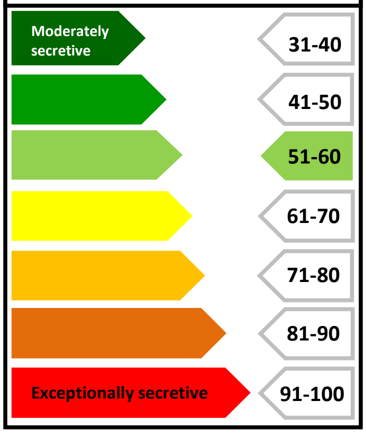
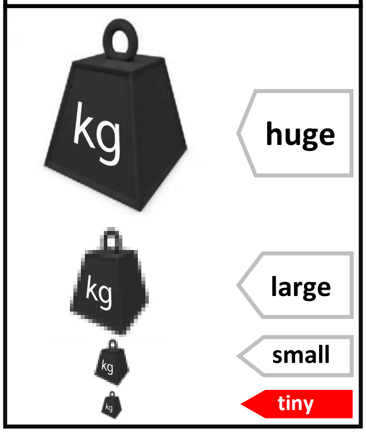


Chart 2 - How Big?



Part 1: Telling the story

30 October 2013

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, *"Israel introduced Controlled Foreign Corporation (CFC) rules, worldwide Vocational Taxation provisions, extensive reporting requirements and a revolutionary trust law reform, all of which intend to significantly increase tax collection while combating tax evasion"*[1].

In addition, on January 1, 2006, the Income Tax Ordinance [new version], 5721-1961 (hereinafter: "Income Tax Ordinance") was amended to include a list of tax planning actions which must be reported to the tax authority[2].The regulations list became effective as of January 1, 2007.

However, and contrary to this trend, in September 2008 Israel amended the Income Tax Ordinance (Amendment No.168) and granted tax exemptions for "New Immigrants" (a person who has never held an Israeli residency) and for "Veteran Returning Residents" (an Israeli citizen who has resided abroad for at least ten years). To a certain extent, this amendment has turned Israel into a 'limited tax haven' for many Jewish individuals[3]. Pursuant to the amendment, 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 Income tax returns and capital declaration) for a ten year period starting with the year in which they became Israeli residents (sections 134B and 135 of the Income Tax Ordinance). In practice, the amendment “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”[4]. It is unclear, however, how such an amendment is in line with the bilateral tax treaties provisions that Israel has concluded with more than 50 other countries (up to date)[5], and which impose certain obligations to exchange information. Moreover, in 2009 Israel even broadened the exemption from such filing obligations for an additional ten year period (up to 20 years altogether) to individual filers who will make substantial investment in Israel within two years of their arrival to Israel [Section 165(4) of the Israeli Economic Arrangement Law, 2009]. Due to pressure from the OECD’s Global Forum on Transparency and Exchange of Information for Tax Purposes, a suggestion to repeal the reporting exemption (albeit without changing the tax exemption) was included in the Israeli Economic Arrangement Bill, 2013. However, the suggestion was not accepted[6] and as of August 2013 it is not clear whether the government intends to promote such a change in separate legislation[7].

Perhaps this is one of the reasons why the International Narcotics Control Strategy Report (INCSR) noted in 2013:

> "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"[8].

The INCSR further noted regarding money laundering:

> "Israel is not regarded as a regional financial center. [...] Criminal groups in Israel, either home-grown or with ties to the former Soviet Union, United States, and European Union, often utilize a maze of offshore shell companies and bearer shares to obscure beneficial owners. Israel's illicit drug trade is regionally focused, with Israel more of a transit country than a market destination."[9]

In 2010, the World Bank estimated the black economy as equal to almost 23% of Israel's GDP in 2007[10]. This estimation was confirmed later in 2012 by Taub Center for Social Policy Studies in Israel[11]. In addition, 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 (Globes.co.il). The Israeli Tax Authorities (ITA) estimate that aggressive tax planning constitutes 80% of this black economy[12].

As a result, in February 2012, the ITA declared a 'war on tax evasion' and submitted to the Minister of Treasury "recommendations for the struggle against black capital and tighter enforcement, with the goal of tripling the ministry's promise of higher tax collection"[13]. The recommendations include "making tax evasion the original crime, which among other things will consolidate information held by the Tax Authority and the Prohibition of Money Laundering Authority. [...] Other recommendations include halving cash transactions from NIS 20,000 to NIS 10,000, and levying a 15% fine on exceeding the limit; legislation to allow sending information to the Tax Authority from the Currency Services Registrar and for the Tax Authority to become the regulator of foreign exchange traders; amending family firm regulations to close tax loopholes; delaying foreign travel by people with tax arrears; permit offsets by taxpayers to prevent hiding assets between spouses; impose guarantees on court-ordered payments; foreclosures on taxes of local authorities and religious councils; and levy taxes on guarantors."[14]

Some of these recommendations have already been approved at a first reading in the Knesset (the Israeli Parliament)[15]. However, at the time of writing (3rd September 2013) it is too early to determine when and if these recommendations will finally be approved. The recommendation to make tax evasion a predicate offence was finally removed from the Israeli Economic Arrangement Bill, 2013[16] and may be promoted again as a separate legislation. However, on 31st July 2013 Israel enacted a law that obligates money changers and currency service providers to report to the tax authority in any transactions involving sums in excess of NIS 50,000. The law further stipulates the establishment of a database comprised of this information, which the tax authority can use to locate tax evaders through market exchange service providers.[17]

As for Israeli laws for the encouragement of foreign investments, prior to 2011, the Investment Law for Encouragement of Capital Investment, 5719-1959 ("the Investment Law") determined preference to foreign investments in Israel. In addition, 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 to the Investment Law, in force as of 2011, abolished the preference for foreign investment and eliminated the exemption of zero corporate tax rate granted to corporations.[18].

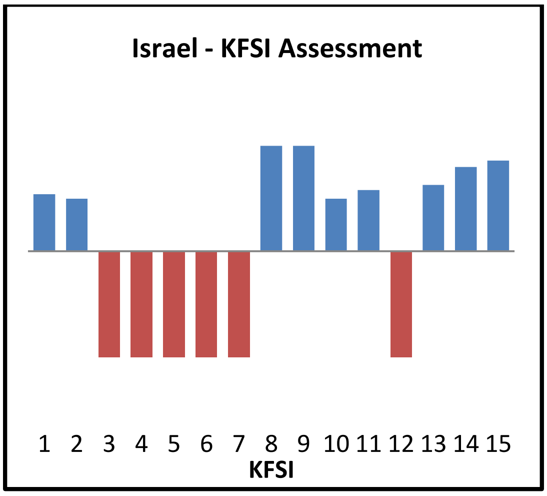
Source: Moran Harari, The Academic Center for Law and Business, Israel.

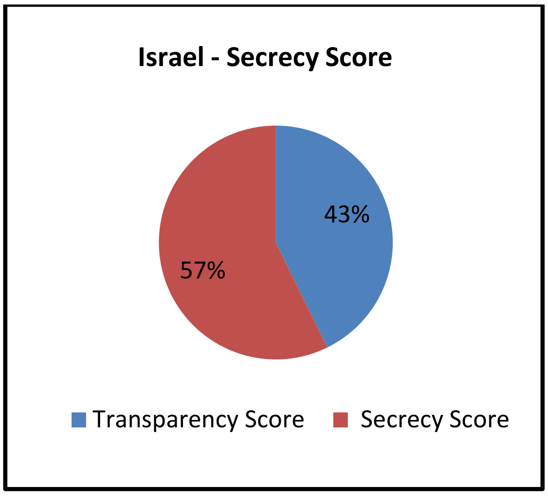
Next steps for Israel

Israel's 57 per cent secrecy score shows that it must still make major progress in offering satisfactory financial transparency. If it wishes to play a full part in the modern financial community and to impede and deter illicit financial flows, including flows originating from tax evasion, aggressive tax avoidance practices, corrupt practices and criminal activities, it should take action on the points noted where it falls short of acceptable international standards. See part 2 below for details of Israel's shortcomings on transparency. See this link http://www.financialsecrecyindex.com/kfsi for an overview of how each of these shortcomings can be fixed.

Part 2: Secrecy Scores

The secrecy score of 57 per cent for Israel has been computed by assessing the jurisdiction's performance on the 15 Key Financial Secrecy Indicators, listed below.





The numbers on the horizontal axis of the bar chart on the left refer to the Key Financial Secrecy Indicators (KFSI). The presence of a blue bar indicates a positive answer, as does blue text in the KFSI list below. The presence of a red bar indicates a negative answer as does red text in the KFSI list. Where the jurisdiction's performance partly, but not fully complies with a Key Financial Secrecy Indicator, the text is coloured violet in the list below (combination of red and blue).

This paper draws on key data collected on Israel. Our data sources include regulatory reports, legislation, regulation and news available at 31.12.2012[19]. The full data set is available here[20]. Our assessment is based on the 15 Key Financial Secrecy Indicators (KFSIs, below), reflecting the legal and financial arrangements of Israel. Details of these indicators are noted in the following table and all background data can be found on the Financial Secrecy Index website[21].

The Key Financial Secrecy Indicators and the performance of Israel are:

TRANSPARENCY OF BENEFICIAL OWNERSHIP – Israel	
1.	Banking Secrecy: Does the jurisdiction have banking secrecy? **Israel does not adequately curtail banking secrecy**

2.	Trust and Foundations Register: Is there a public register of trusts/foundations, or are trusts/foundations prevented? **Israel partly discloses or prevents trusts and private foundations**
3.	Recorded Company Ownership: Does the relevant authority obtain and keep updated details of the beneficial ownership of companies? **Israel does not maintain company ownership details in official records**
KEY ASPECTS OF CORPORATE TRANSPARENCY REGULATION – Israel	
4.	Public Company Ownership: Does the relevant authority make details of ownership of companies available on public record online for less than US$10/€10? **Israel does not require that company ownership details are publicly available online**
5.	Public Company Accounts: Does the relevant authority require that company accounts are made available for inspection by anyone for a fee of less than US$10/€10? **Israel does not require that company accounts be available on public record**
6.	Country-by-Country Reporting: Are all companies required to comply with country-by-country financial reporting? **Israel does not require country-by-country financial reporting by all companies**
EFFICIENCY OF TAX AND FINANCIAL REGULATION – Israel	
7.	Fit for Information Exchange: Are resident paying agents required to report to the domestic tax administration information on payments to non-residents? **Israel does not require resident paying agents to tell the domestic tax authorities about payments to non-residents**
8.	Efficiency of Tax Administration: Does the tax administration use taxpayer identifiers for analysing information efficiently, and is there a large taxpayer unit? **Israel uses appropriate tools for efficiently analysing tax related information**
9.	Avoids Promoting Tax Evasion: Does the jurisdiction grant unilateral tax credits for foreign tax payments? **Israel avoids promoting tax evasion via a tax credit system**

10.	Harmful Legal Vehicles: Does the jurisdiction allow cell companies and trusts with flee clauses? **Israel partly allows harmful legal vehicles**
INTERNATIONAL STANDARDS AND COOPERATION – Israel	
11.	Anti-Money Laundering: Does the jurisdiction comply with the FATF recommendations? **Israel partly complies with international anti-money laundering standards**
12.	Automatic Information Exchange: Does the jurisdiction participate fully in Automatic Information Exchange such as the European Savings Tax Directive? **Israel does not participate fully in Automatic Information Exchange**
13.	Bilateral Treaties: Does the jurisdiction have at least 46 bilateral treaties providing for information exchange upon request, or is it part of the European Council/OECD convention? **As of 31 May, 2012, Israel had less than 46 tax information sharing agreements complying with basic OECD requirements**
14.	International Transparency Commitments: Has the jurisdiction ratified the five most relevant international treaties relating to financial transparency? **Israel has partly ratified relevant international treaties relating to financial transparency**
15.	International Judicial Cooperation: Does the jurisdiction cooperate with other states on money laundering and other criminal issues? **Israel partly cooperates with other states on money laundering and other criminal issues**

[1] http://www.gkhlaw.com/eng/D4Content/MenuID/870/ID/154/

[2] Subsection (g) to section 131, Income Tax Ordinance. See in:http://www.financeisrael.mof.gov.il/FinanceIsrael/Docs/En/legislation/FiscalIssues/5721-1961_Income_Tax_Ordinance_[New_Version].pdf

[3] http://www.gkhlaw.com/eng/D4Content/MenuID/870/ID/154/

[4] http://www.gkhlaw.com/eng/D4Content/MenuID/870/ID/154/

[5] Global Forum on Transparency and Exchange of Information for Tax Purposes 2013: Peer Review Report – Phase 1: Legal and Regulatory Framework – Israel, Paris, in: http://www.eoi-tax.org/jurisdictions/IL#peerreview; 28.10.2013; p.60

[6] http://www.prisha.co.il/UserFiles/File/pdf/hoz/tax20132014.pdf; 31.10.2013.

[7] http://www.israeltaxlaw.com/page791.asp

[8] United States Department of State 2010: International Narcotics Control Strategy Report. Volume II Money Laundering and Financial Crimes, Country Database, Washington, DC, in: http://www.state.gov/documents/organization/141643.pdf; 9.8.2013; in p.202

[9] See note above, p.139.

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

[11] http://www.themarker.com/news/1.1733942

[12] http://www.themarker.com/news/macro/1.1845006

[13] http://www.globes.co.il/serveen/globes/docview.asp?did=1000819120&fid=1725

[14] See note above.

[15] http://www.themarker.com/markets/1.2086703

[16] http://knesset.gov.il/Laws/Data/BillGoverment/768/768.pdf; 31.10.2013.

[17] http://www.globes.co.il/news/article.aspx?did=1000870146

[18] http://taxes.gov.il/IncomeTax/Documents/Hozrim/hoz03-2012.pdf

[19] With the exception of KFSI 13 for which the cut-off date is 31.05.2013. For more details, look at the endnote number 2 in the corresponding KFSI-paper here: http://www.financialsecrecyindex.com/PDF/13-Bilateral-Treaties.pdf.

[20] That data is available here: http://www.financialsecrecyindex.com/database/menu.xml.

[21] http://www.financialsecrecyindex.com.