

# Setting up your Business in Israel

## Issues to consider



Israel is a global centre for hi-tech design and R&D, providing opportunities for investment and co-operation. Most foreign companies are interested doing business in Israel in the business of: ICT technologies, safety and security equipment and services, agriculture technology, defence equipment, medical technologies and biotechnology

### What type of Business Structure should we use?

There are advantages and disadvantages to all of them, and there is no one correct answer, it's all dependent on your specific business circumstances and needs. A brief overview of the main structures is below:

#### Establishment (a branch of your overseas business)

- Not a separate legal entity but an extension of the overseas parent company
- No limited liability or ring-fencing of the Israel operations
- If have a permanent establishment in Israel then profits from this PE are liable to Israel Corporation tax, subjected to treaty between countries.

#### Limited Company:

- Provides limited liability and ring-fencing to [Israel] operations
- Gives a perception of a local business, with longevity
- Corporation tax to be paid on company profits
- Filing to tax authorities (subject to auditing by CPA).
- Each company should file, yearly, tax return audited by an Israeli CPA.

#### Limited Liability Partnership:

- Members (partners) have limited liability
- Profits are allocated to members who then pay Income Tax on these profits personally
- The tax residence of the member, and where the profits in the LLP originated will determine in what jurisdiction and how these profits are taxed, subject to treaty between countries.

### How much Corporation Tax will the business pay?

Current Corporation Tax rates in Israel are:

Until 31.12.2017 tax rate is 24%. From 1.1.18 tax rate will be 23%

According to the law for encouraging investments, foreign investors meeting certain criteria will be taxed only 15% and if the business is built in certain Development zones the tax rate will be only 7.5%.

### What if we use Israel to set up our holding company?

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The rate tax for Holding company in Israel is the same as any other form of a company. The holding company doesn't pay tax for dividend from daughter companies.

### What if we make cross-border transactions between group companies?

Israel follows internationally recognized **Transfer Pricing (TP)** rules where cross-border trading and financial transactions between affiliated entities have to be conducted on an arm's length basis. The price and terms should be the same as if the transactions had been between completely independent parties.

Typical transactions between affiliated entities that are covered by TP regulations are:

- Sale and purchase of goods
- Provision of management services
- Property rental charges
- Transfer of intangible assets e.g. trademarks, patents
- Sharing of knowledge, expertise, business contacts etc.
- Provision of financial support e.g. inter-group loans and charging a "market" interest on loans

A business will need to prepare a Transfer Pricing Report proving the arm's length basis of transactions. The report will include a functional and risk analysis, analysis of the adopted pricing model and benchmarking of the arm's length basis.

### What Employment Taxes and Social Security will need to be paid?

If an individual is resident in Israel then they are subject to Israel tax laws.

We would advise any new entrant to Israel or person who spends time working in Israel to take professional advice to determine whether they are Israel tax resident.

### Current Personal Income Tax rates in Israel are:

Current Personal Income Tax rates in Israel are: Band of income (NIS)	Tax rate (%)
0 – 74,640	10
74,641 – 107,040	14
107,041 – 171,840	20
171,840 – 238,800	31
238,801 – 496,920	35
496,921 – 640,000	47
Over 640,001	50

An individual whose total taxable income exceeds 640,000 NIS will be taxed at a rate of 3% on every additional NIS.

Employers and employees also have to pay Social security, which is called National



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Insurance:

**Current Social Security rates are:**

Band of yearly income) (NIS)		Rate
Employer	Up to 69,648	3.5%
	Up to 518,880	6.95%
Employee	Up to 69,648	12%
	Up to 518,880	7.5%

It is the employers' legal responsibility to pay over employee's tax and social security deductions to the Israel tax authorities.

Israel has a Reciprocal Agreement with the USA, EU countries and many others whereby when an overseas national of those countries is seconded to the Israeli for a defined period of time and continues to pay social security in their home in Israel, then the employer and employee are exempt from paying Israel social security.

### Pension Fund

According to the Israeli law, every employer must insure their employees in pension insurance (i.e. set aside a certain percentage of the employee's salary and transferred the pension fund chosen by the employee) The provisions are financed partly by the employers and partly by the employees.

This duty applies even when the employee is foreign worker.

#### Pension insurance contribution rate

Pension insurance provisions are calculated as a percentage of the employee's salary and paid in part by the employer and partly by the employee (salary deduction)

- 6% - employees' provisions
- 6.5% - the employer's share of pension provisions, or 12.5% in the case of the provision for severance pay component.

The total rate of provisions - 12.5%, or 18.5% in the case of the provision for severance pay component.

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### **What is Value Added Tax (VAT) and should the business be registered?**

VAT on goods and services is 17%  
Any new business in Israel needs to consult with an Israeli CPA.

VAT paid in Israel is deductible  
Eilat is Tax free zone  
Goods and Services exported from Israel are VAT free.

### **Can we provide Share option plans to our staff?**

Many companies see Share Option plans as being an important way of attracting, motivating and retaining key staff.

Israel has a number of “approved” share option plans which give tax benefits to employees and employers alike and it is often possible to adapt an overseas stock option plan to fit into one of these “approved” plans.

However this is a very technically complex area and careful planning needs to be undertaken as soon as share option plans are being considered for implementation in Israel.

### **How else can we compensate our employees?**

Israel has a very comprehensive range of compensation and benefit options available for companies to offer their employees.

Pensions, private medical insurance, life and disability cover are now commonplace benefits provided by many Israel businesses to their workforce.

Flexible benefit packages are also gaining in popularity, giving employees options on how they wish to “spend” their benefits allowance; which can range from “purchasing” additional holiday entitlement to obtaining full family medical cover.  
All benefits are taxed.

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