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The Use of Real Estate Trusts for Investments and Holding of Property in Israel

By Dr. Alon Kaplan and Meytal Liberman

Introduction

Trusts in Israel are governed by the Trust Law.¹ In addition, other laws contribute to the enhancement of the various uses of trusts, such as the Agency Law,² and the Real Property Taxation Law.³ This framework is augmented by court cases and rulings of the Israeli Tax Authority.

Real Estate Trusts ("RETs") have been used in Israel for many years and for various purposes, including legitimate tax planning, asset protection and commercial transactions.

For instance, the RET was used in the 19th century by Jewish people living in Jerusalem in order to purchase land and protect their property from confiscation by the Ottoman rulers. This was achieved by placing the property in a Moslem trust known as a *Waqf*, thus ensuring that the Moslem government would not interfere with the ownership rights of the land.⁴

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Another old example of the historical use of a RET can be found in the establishment of Tel Aviv in 1909. At that time, it was prohibited for Jewish residents to purchase land; thus the land was purchased by a non-resident investor, who acted as trustee for the new settlers.⁵

Taxation of Real Estate in Israel

Under the Real Property Taxation Law, two main taxes are imposed upon a sale of real estate: a capital gains tax on the seller, and a purchase tax on the purchaser. The capital gains tax is calculated in accordance with the increase in the value of the property since its purchase; the time period during which the seller owned the property; and the existence of other real properties owned by the seller. The purchase tax represents a certain percentage of the purchase price. This percentage is set in accordance with other real properties owned by the purchaser.

A sale for the purposes of the Real Property Taxation Law is considered as such, whether it was made for consideration or not. However, it should be noted that the transfer of real estate under inheritance procedure is not considered as a sale, and therefore does not trigger the imposition of any of the taxes mentioned above. In fact, Israeli law does not provide for any estate tax; thus the transfer of any property upon death, including real estate, is not subject to any tax in Israel.

Real Estate Trusts in Israel

The real estate trust in Israel is a legal structure under which real estate is purchased by a trustee, or is transferred to a trustee, and the trustee acts as a nominee or bare trustee for an identifiable beneficiary. Israeli law, namely the Real Property Taxation Law and the Trust Law, provide the legal structure for such a RET.

Under such a structure, the trustee is registered as the legal owner of the real estate but under Israeli tax laws, namely the Income Tax Ordinance⁶ and the Real Property Taxation Law, the beneficiary of the real estate is considered as the real owner, similar to a beneficiary of a bare trust in the common law.⁷

An example of how this presumption works can be gleaned from a recently published case where a father purchased an apartment in Israel and invested most of the funds required to purchase the property.⁸ The apartment was registered in the name of his daughter. The apartment was used alternatively for the parents and the daughter upon her visits to Israel. After the demise of the mother, the daughter filed a claim against the father demanding the eviction of the father from the apartment, claiming that she had the ownership of the apartment. The court dismissed the claim, recognizing the ownership rights of the father who provided evidence that the apartment was his property held by the daughter as a trustee for the father.

"The Israeli Tax Authority confirmed that the transfer of the real estate property to the trust was exempt from tax, thus recognizing in this case a RET."

Another interesting case was ruled upon by the Supreme Court.⁹ In that matter, a trustee was registered

in the Land Registry as the owner of a real estate property. The registration did not reference the fact that the property was held in trust.¹⁰ The trustee was declared bankrupt and a creditor tried to attach the property for the satisfaction of his claim against the trustee. The court was presented with evidence that the property was held in trust for beneficiaries, and, upon accepting this evidence, ruled that the creditor had no right against the real estate property even though the Land Registry did not have any reference to the rights of the beneficiaries.

This was an important precedent reconfirming the concept of holding real estate in trust for a beneficiary, and ensuring beneficiaries' rights against third parties.

Tax Exemption for a Real Estate Trust

A pre-ruling published in 2012 by the Israeli Tax Authority¹¹ dealt with the transfer of real estate properties into a private trust. In this case, an elderly person created a trust in his favor and in favor of other beneficiaries. The Israeli Tax Authority recognized the establishment of a trust regulated under Section 17 of the Trust Law known as *Hekdesh*. The Israeli Tax Authority confirmed that the transfer of the real estate property to the trust was exempt from tax, thus recognizing in this case a RET.

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The importance of the ruling is in the clarification given, for the first time, regarding the existence of tax exemption for the transfer of real property by a beneficiary into a RET.

Until this ruling there had been no orderly source showing that when an owner of real property transfers the property to a trustee and becomes a beneficiary of the RET, the transfer is tax exempt. The ruling stated as follows:

If the creation of a trust (by the settlor/beneficiary) and the vesting of the trust's properties to the trustee, designated until the end of his days to benefit the beneficiary, his welfare and quality of life, while still alive, and after his death, in favor of specific beneficiaries, which the beneficiary determined in

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the trust document and in the aforementioned will, will not be deemed to be a "sale of a right in land" in the sense of the law.

Conclusion

The real estate market in Israel is in great demand by both Israeli and foreign investors, and some investors choose to hold properties they purchase in the name of a trustee. This structure may be found particularly useful and efficient for American families that decide to invest in real estate in Israel or have a second home there.

However, if any of your clients are considering using this structure to purchase real estate in Israel, it should be noted that there are some issues of trust, inheritance and tax laws that require proper consultations and clarifications. Therefore, expert advice is recommended.

Endnotes

1. Trust Law, 5739-1979, 33 LSI 41 (1966-1967) (Isr.).
2. Agency Law, 5725-1965, 19 LSI 231 (1964-1965) (Isr.).
3. Real Property Taxation Law (Capital Gains and Purchase), 5723-1963, 17 LSI 193 (1963) (Isr.).
4. Ron Shaham, *Christian and Jewish "Waqf" in Palestine During the Late Ottoman Period*, 54(3) Bulletin of the School of Oriental and African Studies, University of London, 460-472 (1991).
5. Shimon Rubinstein, *Constraints and Hope in the Matter of Land Purchases by Jews in the Land of Israel at the End of the Ottoman Period* (Hebrew), available at http://www.kkl.org.il/files/HEBREW_FILES/machon-mediniut-karkait/karka-41/karka-41-1996-10.pdf.
6. Income Tax Ordinance [New Version], 5721-1961, 6 LSI [N.V.] 120 (1961) (Isr.).
7. *Trusts and Taxes*, available at <https://www.gov.uk/trusts-taxes/types-of-trust>.
8. Family Case (TA) 19831-04-10 R. G. v. M. P. (July 7, 2013), Nevo Legal Database (by subscription) (Isr.).
9. CA 5955/09 *Amster (Receiver) v. Tauber Tov* (July 19, 2011), Nevo Legal Database (by subscription) (Isr.).
10. Such a reference is possible under a procedure named "caveat" under Section 4 of the Trust Law, and Land Law, 5729-1969, 23 LSI 293, §127 (1968-1969) (Isr.).
11. Tax Ruling no. 3324/12, *The Establishment of a Hekdesh—Tax Ruling in Agreement*, available at <https://www.misim.gov.il/tmmisuyweb/frmShowLinkedAbs.aspx?num=20120030> (Hebrew).

Book Review: *Trusts and Estate Planning in Israel*

Written by Alon Kaplan

Reviewed by Ziva Robertson

Trusts have formed part of English law for many centuries. They first arose in feudal times, when a landowner called by his lord to go to the battlefield entrusted his property to a relative, only to discover on his return that his land had been appropriated by the relative for himself. The doctrine of equity intervened to protect the interest of the soldier by holding that although the title to the land—the legal interest—was held by the relative, the beneficial owner entitled to enjoy the asset was the soldier. And we never looked back.

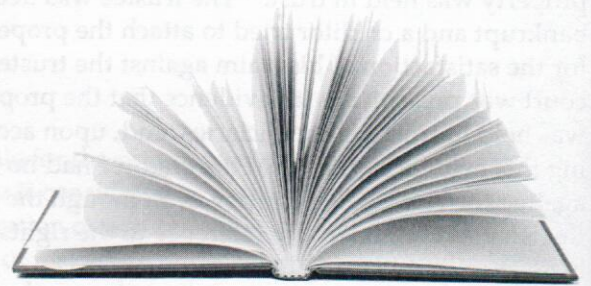
“And there is such a lot of it that you could spend years studying it and practising it before you can say with confidence that you truly understand it.”

With the growth of the British empire—including the Mandate over Palestine before the Israeli war of independence—the trust concept traveled far and wide, and continued to grow and evolve so as to provide solutions for very modern problems. While retaining many of its original features, the concept has developed a little differently in different jurisdictions. Layer upon layer, it has become an instrument in wealth and estate planning.

Which is why many trust practitioners, in a moment of honest reflection, will admit that Trust Law was their pet hate as students. It is fluid but difficult. It is modern, yet archaic. It is clear in parts, but obscure in others. And there is such a lot of it that you could spend years studying it and practising it before you can say with confidence that you truly understand it.

“This book should take pride of place on the bookshelf of any Israeli private client practitioner who strives for a better understanding of this area of the law.”

Few people take the trouble. Alon Kaplan is one. With years of practice and teaching in this area, Kaplan founded the first Israeli branch of STEP, the Society of Trust and Estate Practitioners, which now numbers 150 members in Israel (and 20,000 worldwide). His book, *Trusts and Estate Planning in Israel*, is the fruit of his Ph.D. thesis and research in this complex legal field. In Israel, like elsewhere, trusts constitute a flexible tool for suc-



cession planning, tax structuring, charitable giving, an umbrella for corporate holdings and many other uses. Kaplan navigates these complexities with clarity, elegance and erudition and explains the interplay between civil and Rabbinical law; trusts according to Islamic law; the creation of trusts by deeds and by contracts; their uses as testamentary instruments; and, significantly in the current climate, their tax treatment in Israeli law.

As trusts and their uses continue to evolve, it is important for private client and tax practitioners in Israel to understand them, their various uses, their tax treatment, their advantages and their limits. Few Israeli practitioners understand them as thoroughly as Kaplan, and few (if any) modern books have been written about trust law in Israel with the same depth and attention to detail as Kaplan's book. This book should take pride of place on the bookshelf of any Israeli private client practitioner who strives for a better understanding of this area of the law.

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