

# Israel: the trust law and the Hekdesh deed

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## Abstract

This article will review the provisions of the Israeli Trust Law, 1979, as they refer to the trust settled by Hekdesh deed, a legal structure with certain similarities to foundations in some foreign jurisdictions. The Israeli trust is not a separate legal entity thereby requiring an underlying company in various circumstances. The Hekdesh together with the underlying company are referred to in this article as the 'Israeli Foundation'.

## Introduction

The unique legal structure of the 'Israeli Foundation' stems from the Trust Law<sup>1</sup> coupled with professional experience and practice resulting from a number of legal issues, including the practice for a legal entity to hold trust assets. In addition, the Succession Law 1965<sup>2</sup> (the 'Succession Law') provides that *inter vivos* agreements relating to one's inheritance are invalid, and that bequests must be included in a last will and testament, and if not - they are invalid.<sup>3</sup> However, complicated and cumbersome inhabitation procedure may be avoided by properly setting up an *inter vivos* hekdeshe under the Trust Law. This article will cover the provisions of the Trust Law governing the Hekdesh deed.

## The establishment and commencement of the Israeli Foundation

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The settlement of assets for the benefit of a beneficiary or for some other purpose into a Hekdesh, also known as an endowment, requires a written document, executed by way of a deed, signed before an Israeli notary,<sup>4</sup> in which the settlor states his intent to settle a trust together with the terms, purpose and assets thereof.<sup>5</sup>

In practice, the Hekdesh is settled by a deed for *inter vivos* settlements, or as a testamentary trust within a last will and testament.<sup>6</sup> The Hekdesh deed includes the terms of the trust, such as the settlor, trustee, and beneficiary. The *inter vivos* trust is commenced upon the transfer of possession of the trust assets to the trustee,<sup>7</sup> who is permitted to accept additional trust assets at any time from the settlor and/or from third parties.<sup>8</sup> The testamentary trust is commenced upon the issuance of a probate court

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1. Trust Law, 5739-1979, 33 LSI 41 (1966-1967) (Isr.).

2. Succession Law, 5725-1965, 19 LSI 215 (1964-65) (Isr.).

3. *ibid* s 8.

4. The Hekdesh deed is one of a number of documents permitted under s 17(a) of the Trust Law.

5. Trust Law, s 17(a).

6. *ibid*.

7. *ibid* s 17(b).

8. *ibid* s 18(a).

order and the transfer of the estate assets to the trustee.<sup>9</sup>

## The Underlying Company in the legal structure of the 'Israeli Foundation'

*The Hekdesh is not recognized as a legal entity, therefore, common practice of trustees is to hold the assets of the Hekdesh via an underlying company*

The Hekdesh is not recognized as a legal entity,<sup>10</sup> therefore, common practice of trustees is to hold the assets of the Hekdesh via an underlying company incorporated in accordance with the provisions of the Income Tax Ordinance (the 'Ordinance'),<sup>11</sup> thereby creating a designated legal entity to hold the Hekdesh assets on behalf of the trustee. Such legal structure is referred to in this article as the 'Israeli Foundation'.

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The Ordinance provides for the incorporation of an underlying company defined as a company that holds trust assets for the trustee, whether directly or indirectly in accordance with the terms set forth below:

1. It is incorporated solely for the purpose of holding the trust assets.
2. Notice of the incorporation of the underlying company is to be provided to the tax authority within 90 days of the underlying company's incorporation where it is an underlying company of

the following trusts: (i) an Israeli resident trust; (ii) an Israeli resident beneficiary trust; (iii) A testamentary trust of which an Israeli resident is a beneficiary; (iv) any trust in which the trust assets are in Israel.

3. The trustee holds all of the underlying company's shares, directly or indirectly; the term 'indirect holding' is only a holding through another company which is one that meets the provisions of paragraphs (1) and (2) and all of the shares are held by the trustee.

## The trustee

The trustee is responsible to act for the benefit of the beneficiary or for another purpose.<sup>12</sup> The trustee of a Hekdesh is appointed within the Hekdesh deed, and if no trustee is appointed at any time during the term of the trust, an appointment may be made by the court.<sup>13</sup> The trustee must manage the bookkeeping of the trust and report to the beneficiaries, at least annually on the activities of the trust.<sup>14</sup> The trustee may not be a minor, legally incapacitated, in bankruptcy or a corporate entity under receivership. In addition, a beneficiary may not be appointed as trustee unless specifically permitted in the Hekdesh deed.<sup>15</sup> A trustee may resign at any time upon providing written notice to the parties authorized to appoint successor trustees and may be removed by the court for failure to fulfil the duties of trustee or for other reasons in the trustee's discretion.<sup>16</sup> The trustee is not entitled to remuneration for the services of trustee unless such services are within the realm of the trustee's business activities. Nonetheless, a court may award a trustee a fee for services in the court's discretion, based on the realm of activities.

9. *ibid* s 17(a).

10. PCA 46/94 *Zacks-Abramov v Land Registry Officer* 50(2) PD 202 [1996] (Isr.).

11. Income Tax Ordinance (New Version), 5721-1961 (Isr.).

12. Trust Law, s 1.

13. *ibid* s 21.

14. *ibid* s 7. s 11 of the Trust Law provides that s 7 is subject to the terms of the trust, therefore, the trustee's obligation to report to the beneficiaries can be altered or cancelled in the trust deed. Such exemption does not, however, exempt the trustee from filing tax reports with the Israeli Tax Authority as required under law.

15. Trust Law, s 21.

16. *ibid* s 22.

Notwithstanding, a trustee may be entitled to the reimbursement of expenses in the performance of the trustee's duties.<sup>17</sup>

## Trust assets

The trustee must hold the trust assets separate and apart from other assets in a manner easily identifying the trust assets.<sup>18</sup> Holding the trust assets via and underlying company as mentioned above assists the trustee to fulfil this requirement. The trust assets that are not required for the daily activities of the trust, must be invested by the trustee with the purpose of preserving them and of increasing their value.<sup>19</sup> Only debts resulting from the trust assets or from the trust's activities may be paid from the trust assets.<sup>20</sup>

## Beneficiary rights

A beneficiary's rights under the Hekdesh deed may not be assigned, hypothecated or subjected to a lien unless permitted by the Hekdesh deed. Notwithstanding the preceding paragraph, a court may permits liens or other forms of hypothecation of the trust assets in order to cover alimony payments and/or taxes owned by the beneficiary or under special circumstances payment of other debts of the beneficiary from the trust assets in the court's discretion.<sup>21</sup>

## Revisions and termination of the 'Israeli Foundation'

The terms of a Hekdesh deed may not be amended by the settlor nor may he remove trust assets or terminate the trust without specifically reserving these

powers to the settlor in the Hekdesh deed. Alternatively, such amendments may be made by the settlor if all of the beneficiaries confirm said amendments, or upon receipt of court approval.<sup>22</sup>

Under certain circumstances, the court may authorize the trustee to use the trust assets for the fulfilment of the vital needs of a beneficiary, or those dependent on the beneficiary, in a manner that is contrary to the Hekdesh deed.<sup>23</sup> The court may also amend or terminate Hekdesh deed provisions if it is satisfied that circumstances warrant said revisions, which are in accordance with the settlor's intentions.<sup>24</sup>

## Recognition of foreign trust structures in Israel

*Common practice in Israel shows that various trust structures operate in Israel. These structures include not only common law trusts, but also foundations, establishments, and settlements*

Common practice in Israel shows that various trust structures operate in Israel. These structures include not only common law trusts, but also foundations, establishments, and settlements under the laws of jurisdictions such as Liechtenstein and Panama. Such legal entities can be found, for example, in the records of the Registrar of Companies as foreign corporations.<sup>25</sup>

Moreover, the Ordinance defines a trust as:

an arrangement, according to which a trustee holds the trust's assets in favour of a beneficiary, which was established in Israel or outside Israel, whether it is

17. *ibid* s 8.

18. *ibid* s 3(c).

19. *ibid* s 6. s 11 of the Trust Law provides that s 6 is subject to the terms of the trust, therefore the settlor may determine otherwise, thereby exempting the trustee from liability should any losses occur to the trust assets. Such exemption may be required, for example, if the trustee holds a family business in trust.

20. Trust Law, s 3(b).

21. *ibid* s 20.

22. *ibid* s 18(b).

23. *ibid* s 19(b).

24. *ibid* s 23.

25. Review of the records of the Registrar of Companies of 7 January 2019 shows, for example, a company named 'Favorit Establishment', which was incorporated on 19 November 1987 in Liechtenstein.

defined under the law applicable to it as a trust or whether defined otherwise.

The Ordinance further provides that a trustee is:

a person to whom assets or income of assets were attributed, or who holds assets in trust. . . For this purpose, attribution to an underlying company shall be regarded as an attribution to the trustee, and a legal entity listed in the First Schedule A shall be regarded as trustee.<sup>26</sup>

The legal entities listed in said First Schedule A are the following: a foundation under the laws of Liechtenstein, Panama, the Bahamas, and the Netherlands Antilles; an Establishment under the laws of Liechtenstein; and

Trust Reg. under the laws of Liechtenstein. The Ordinance states that the Ministry of Finance may add other corporate trust entities to the First Schedule A.<sup>27</sup>

## Conclusion

Israel recognizes foreign trust structures. Nonetheless, as trust practice has evolved over the past few years, there is an increase in the settlement of Israeli trusts coupled with Israeli underlying companies to hold assets in Israel and internationally. While the Trust Law has been valid since 1979, precedents are not as common as in other jurisdictions due to the infancy of the practice.

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26. Income Tax Ordinance, s 75C.

27. Income Tax Ordinance, First Schedule A.