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Israel Proposes Personal Stock Investment Accounts With Tax Perks



By Matthew Kalman

Israel's parliament will debate legislation that would allow individuals to operate stock investment accounts with special tax benefits.

Set for debate late summer, a bill tabled May 23 by Roy Folkman, chief whip of the Kulanu party headed by Finance Minister Moshe Kahlon, proposes accounts with deferred tax benefits of up to 70,000 shekels (\$19,464) each year or 2.5 million shekels for those depositing the proceeds of real estate sales.

Tax on the profit from securities investments would be deferred until funds are withdrawn, when the gains would be taxed at 10 percent instead of 25 percent. To encourage savers to withdraw the account money as an annuity, there would be no capital gains tax on transfers of cash or securities from an investment account to an annuity provident fund or an investment provident fund.

"It's more flexible and it will give you the ability to manage your money better and it will be more liquid. You can sell it whenever you want," Folkman told Bloomberg Tax May 28.

Until now, tax incentives were available only for funds lodged within pension schemes or provident funds managed by insurance companies and financial institutions with attendant management fees. The new investment accounts would be held at banks and managed directly by their holders.

Some 200,000 of Israel's 8.8 million people own second homes, according to the finance ministry. The primary aim of the bill is to encourage investors to sell real estate to help reduce spiraling housing costs and to help increase the liquidity of the Tel Aviv Stock Exchange, Folkman said.

Placing the new accounts at the banks will also increase competition in the financial services sector, Folkman said.

Israel's bourse has long been lobbying for tax incentives that will attract more individual stockholders to a market dominated by institutional investors. A spokesperson for the exchange welcomed Folkman's "important proposal" and Kahlon's support.

Tax Authority, Other Opposition

The legislation should be approved by the end of the year but it must first overcome fierce opposition from the Israel Tax Authority and other finance ministry officials, Folkman said.

"The biggest opponents are the tax authority," he said. "They are already very angry at me. It's clear they will be very opposed and they will pressure the Knesset and finance minister as much as they can to block it. They will try to convince him on the professional side that it's wrong."

The attempt to use a tax benefit to encourage investors to liquidate their real estate holdings and transfer the funds to securities is consistent with Kahlon's goal of reducing real estate prices in Israel but it may not be enough to achieve that aim, said Zvi Gabbay, former head of enforcement at the Israel Securities Authority and now head of capital markets at Barnea law firm in Tel Aviv.

"In order to convert real estate investors to capital market investors, a more comprehensive plan needs to be put forward; one that focuses on making investments in securities and financial products more attractive to the general public," Gabbay said in a May 27 email. "Tax incentives are one aspect of it," but such a plan also requires diversity in the products and service providers, creating financial structures that provide more stability at lower costs, and "a comfort level that securities and financial products struggle to provide," he said.

Snapshot

- Finance minister's party wants to divert funds from real estate to securities
- Practitioners say tax exemptions illegitimate, will not achieve aim

Using Tax to Influence Free Market?

The anomaly created by the special tax exemptions for real estate investment—granted to help solve a housing crisis during a massive influx of one million Russian immigrants in the early 1990s—shouldn't be solved by creating more anomalies, said Daniel Paserman, partner and head of tax at Gornitzky and Co. law firm in Tel Aviv.

“They are trying to catch two birds in one hand—to encourage investments in the Israeli stock exchange and also to address the housing crisis,” Paserman said May 28.

“You shouldn't try to use the tax system in order to try to influence the operation of the free market,” he said.

“They are trying to combine between those who sell real estate and trying to apply tax benefits only to those who will invest in this special savings scheme. I think it's really not the proper way to do it. I'm not sure it will achieve the goal.”

“In principle there should be no exemptions. Perhaps they ought to abolish the exemption, not provide other exemptions,” he said.

“If all the tax rates are equal, then people decide how to invest based on the economics of the investment and not based on the tax consequences of the investment. I think that from an economic perspective that's the way it should be done. You don't want to encourage people to invest in things that are inefficient or not right for the economy just because it gives certain tax benefits,” he said.

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