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# Foreign resident banking in Israel



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An advanced international banking system, a solid currency and advantageous tax benefits, together with ongoing growth and ability to adapt to changing conditions, make Israel an attractive investment option for foreign residents, including opening a bank account.<sup>1</sup>

The structure of the Israeli banking system is similar to that of other developed countries. The Bank of Israel reports that there are 16 Israeli commercial banks and four foreign banks active in Israel. According to the 2005 annual report of the Bank of Israel, Bank Hapoalim, Bank Leumi, Discount Bank, Bank Mizrachi and First International Bank of Israel hold 95 percent of all banking assets.

Banks in Israel offer the same services provided by all the world's leading banks including corporate banking, private banking and asset management, though some use a foreign company or subsidiary for the latter purpose. They provide term deposit and savings plans in all major currencies, and with different interest-earning options. Most of the banks also provide securities trading services for transactions executed on the Tel Aviv Stock Exchange as well as in foreign markets, using either personal accounts or the bank's mutual funds.

Banking secrecy is well enshrined in the Israeli system. The obligation to maintain bank secrecy stems from the contractual

relations between banks and their clients, from the public interest in maintaining a regulated banking system, and from the provisions of the Protection of Privacy Law, 1981 ("PPL"). Under the PPL, an infringement of privacy is, inter alia, a violation of an obligation to maintain secrecy regarding a person's private affairs, established by explicit or implicit agreement.<sup>2</sup> The bank's obligation of secrecy extends not only to the details of the client's account but also to all transactions related to the account and survives the death of the account holder. Banking secrecy is, however, subject to certain exceptions that allow disclosure: public interest; protection of the bank's interests; court order or legal obligation; and explicit or implied consent of the account holder. The banking secrecy afforded by the PPL also applies to companies.

The Israeli Income Tax Ordinance ("the Ordinance") provides some interesting tax benefits for foreign residents who open an account in Israel. For example, under certain conditions,<sup>3</sup> foreign residents are exempted from tax on interest on foreign currency deposits, on capital gains upon sale of securities traded on a stock exchange, and from capital gains of future transactions that are not traded.<sup>4</sup> Foreign residents wishing to benefit from any of the exemptions must, however, file a special declaration with the bank regarding their residency status. Generally, the declaration

must be filed prior to the relevant tax year or within 14 days of opening the account.

These benefits are relevant only for foreign residents. The Ordinance defines a "Foreign Resident" as anyone who is not an Israeli resident. An individual will be considered an Israeli resident if the center of his life is located in Israel. The center of life test takes into consideration the financial, economic and social ties of the individual, including: the location of the individual's permanent home, the place of residence of the individual and his family, the location of his regular activities, jobs, assets and investments, clubs, unions and institutions of which he is a member. Refutable presumptions, based on the number of days a person stays in Israel<sup>5</sup> and a total of 425 days or more during the tax year and the two previous years have been fixed to assist in determining residency status. Legal entities (whether incorporated or not) incorporated/registered in Israel will be deemed resident by the mere act of incorporation/registration in Israel. Foreign entities will also be deemed resident if the control and management of their business are carried out from Israel.

With respect to the above benefits, the banks are obliged to disclose to the tax authorities information on clients receiving interest payments in excess of NIS 12,000 (approximately \$2,800) per annum on their deposits, whether or not they are Israeli



residents. The information required is very detailed and consists, inter alia, of the client's name, identity number and income arising from interest paid.

The Prohibition on Money Laundering Law 2000 ("PML") and its subsequent regulations ("the Orders") stipulate additional reporting obligations on financial services providers, including banks. The rules impose duties of identification, reports, registration and record keeping in relation to the banks' clients and their accounts. Banks are required to report banking transactions of a certain amount, or which appear to be, or are defined as, irregular transactions, to the Israel Money Laundering and Terrorism Financing Prohibition Authority of the Ministry of Justice (the Authority). Failure to report can

result in personal criminal liability of the bank employee. Information held by the Authority may be transferred to the Israeli police or General Security Services ("Shin Bet"). Last year, the Orders were expanded to cover the prohibition on financing terrorism, and now include obligations to check the identity of parties to a transaction as well as obligations of reporting by size and type of transaction. The minimum size of transaction that requires reporting has been set at NIS 5,000 (approximately \$1,200) for transactions with a high risk country or territory.

Further, clients of all banks in Israel are required to declare the identity of the beneficial owners of their accounts, and to declare if the accounts are operated on behalf of a third party. Companies must file a declaration detailing the individuals controlling the company and provide photo identification and information on all authorized signatories. The banks may take any reasonable steps to verify the true identity of the account holders, the beneficiaries, holders of powers of attorney, etc. The bank must create a "personal profile" of the foreign resident client, including the client's name, identity number, date of birth and address, which must be kept up to date.

Moreover, at most of the banks, only a senior position holder may approve an account opening to clients classified as "affluent" or "politically exposed", though once an account is opened such clients enjoy favored bank services.

In conclusion, opening a bank account in Israel offers diverse benefits to foreign residents and is usually not a complex procedure. Nevertheless, in order to stay in line with developed country standards, the client is required to reveal details about his identity, and the bank is subject to several reporting duties.

- ① *"The Economist" recently published its emerging markets survey and placed Israel as one of the five fastest growing emerging markets in the past 20 years; as well, Fitch, Standard & Poor's and Moody's Ratings have recently improved Israel's foreign and local currency Issuer Default Ratings (IDR) to 'positive' from 'stable'.*
- ② *The right of privacy has been elevated to a basic right under the Basic Law on Human Dignity and Freedom (1992).*
- ③ *All the account holders must be foreign residents, and the deposit is not used for a loan or a loan guarantee to a resident relative or controlled company.*
- ④ *Income Tax Order (Tax Exemption of Capital Gains from Future Transaction), 183 days or more during the tax year, or 30 days or more during the tax year 2002.*
- ⑤ *183 days or more during the tax year, or 30 days or more during the tax year, and a total of 425 days or more during the tax year and the two previous years.*

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