

INCOME TAX PLANNING ALERT FOR 2008

With the 2008 tax year about to end, this is a "final call" for prudent, but creative, tax planning. We are available to meet, discuss and plan.

A. Last Minute Planning for Businesses and Services

There is a substantial difference between taxpayers who report on a cash basis, and those who report on a regular commercial basis. The former account for monies actually received during the tax year and expenses actually paid; the latter report on income earned - irrespective of whether received - and expenses actually incurred. This distinction is of much significance, as it relates to the tax device of timing income and expenses within the fiscal year.

Now is the time to review expenses on overseas travel, professional and related literature, entertainment of overseas customers and associates, gifts, travel, food and refreshments, overseas telephone calls, home-related expenses, and various 'borderline' type expenses that require close scrutiny. Payments for life insurance, provident and pension funds, training funds, donations, research and oil projects, film production, National Insurance and others must be made by December 31st in order to enjoy the tax benefits thereon.

Utilisation of capital losses applies only to losses actually incurred by December 31st - the particular asset or investment must actually have been sold.

B. Reducing the Tax Burden on Passive (Investment) Income

1. Give thought to early redemption/realisation of financial assets; capital gains on traded securities are taxed at 20%. However, if such assets were held prior to 2003, then the tax rates will be higher, based on a proportional calculation of the rates over the period of ownership. Thus, a low gain or capital loss situation at the present time may be opportune for re-assessment, subject, of course, to the decision/s making sound economic sense (e.g. "creating" capital loss for set-off against capital gains or, in certain cases, against other passive income.)
2. Expenses incurred in relation to such assets - as above - over the period held, may well reduce the taxable gain. These would include, in our opinion, management and administration fees, consulting and professional fees and, possibly, finance charges.
3. Similarly, these and other expenses may be deductible from regular passive income from dividends and interest on bonds; expenses are not deductible from interest earned on bank deposits (i.e. cd's). Other expenses may include travel, communications and professional fees.
4. Foreign pensions may well enjoy lower tax rates in Israel, and the double-tax treaties generally facilitate reporting according to country of residence.

C. Income from Real Estate

1. Rental income from residential property in Israel (individual tenants only) enjoys a tax exemption of individuals (only) up to NIS 4,200 monthly.
2. Alternatively, you may elect to be taxed at 10% of gross rental, without any upper ceiling. This route is now conditional on the taxes (viz. 10% of gross rental) being paid within 30 days of the tax year-end (January 30th).
3. Where there are high maintenance or other costs (including depreciation), neither of the two alternatives may be appropriate, but rather the regular tax route. Where the apartment or house is used for business (not for residential) purposes, then these tax provisions do not apply.
4. Rental income from property owned outside Israel - residential or commercial - may be taxed at 15%, but excludes claiming expenses and deductions (other than depreciation) and any foreign taxes paid thereon. High costs and/or foreign taxes render this unattractive. The alternative is the regular tax route.

D. Charitable Contributions

Recognition of charitable contributions - in order to enjoy the Income Tax credit - often encounters bureaucratic obstacles. Do ensure that receipts are originals and have Section 46 approval (printed and actual). It is advisable that the contributions be made from the bank account of the donor. Contributions exceeding the upper ceiling (the lower of 30% of taxable income or NIS 4,013,000) may be carried forward for use within the following three years. The treaty with the U.S. provides for recognition of charitable contributions to U.S. non-profits, but subject to a ceiling of 25%. The tax credit is 35% of the amount contributed for individuals, and the corporate tax rate for companies (2008 - 27%).

E. Interest and Linkage on Taxes Due

The Income Tax debts for a particular tax year bear linkage and interest for the tax year reported, as of January 1st in the year following. If you wish to avoid or reduce such interest, then interim payments may be made to the Income Tax offices during the year. Where tax debts for the previous tax year are paid by the end of January - in the year following - no interest or linkage will be charged; if settled by the end of February, only 50% will be paid; and where paid by the end of March, 75% will be payable.

F. Reporting on Aggressive Tax Planning

Clients are reminded of the new reporting requirements (as of 2007) relating to certain tax-planning devices; these include payment of management or consulting fees to related parties, sale of assets to related parties, surrender of debts to related parties, holding of equity in foreign companies and others. (We refer you to the article on our website for full details.)

G. Year-end Tips

Some tax reducing thoughts still for 2008:

1. Review inventory closely, with a view particularly for dead or obsolete items - will reduce closing inventory and taxable income.
2. Check your 2007 asset/depreciation schedules for items no longer in use or obsolete; these may be fully depreciated in 2008 if the above applies.
3. Capital gains may be reduced by realised capital losses; assets/investments that reflect paper losses, and are unlikely to rise in value in the very near future, may be suitable "candidates".
4. Capital losses on securities arising in 2008 may be offset with income from dividends received in 2008. This includes dividends from private companies.

The first two points above may be dealt with post-December 31st item 3 must be done by December 31st

This Tax Alert is prepared for the information of clients and associates. Whilst every care has been taken in compilation, no responsibility can be accepted for inaccuracies or errors. Clients are also advised that changes in the Law or practice occur periodically; it is recommended that specific professional advice be sought before any action is taken.

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