PTE ÁJK-KTK Könyvtár
KG 80

University of Pecs
The International Ph.D Program in Business Administration

The "Combined Solution" to Taxation of Foreign Trusts in Israel

by

Daddy Yacov

2008

KTK
OT
336.2
Y 10

University of Pecs

The International Ph.D Program in Business Administration

The "Combined Solution" to Taxation of Foreign Trusts in Israel

Submitted to

Prof. Ivan Belyacz

by

Daddy Yacov

2008

5 db
MELLÉKLETTEL

PTE Egyetemi Könyvtár

P000850032

PÉCSI TUDOMÁNYEGYETEM
KG 80
Benedek Ferenc Szakkönyvtár

Acknowledgements

I would like to take this opportunity to thank those who helped me throughout the recent years when writing this doctoral thesis occupied all my waking hours:

Special thanks to my tutor, **Prof. Ivan Belyacz**, for his insightful notes and comments to this study;

Roni **Aberdam,** Shai **Dover,** Alon **Kaplan,** Katy **Katz,** Anat **Tenne** and Pnina **Pwolicki** for their input, helpful comments and interest

Yehuda **Schwartz**, for his help and guidance – the right piece of advice in the right place;

Colleagues who worked with me and answered the questionnaires, without which this thesis would lack content, and who provided me with important and current data on innovations in legislation and taxation from around the world in this domain, some of which have yet to be published;

And special gratitude to my dear wife **Debra** and my loving family who supported me in the difficult moments on this long journey.

Table of Contents

Acknowledgements _____ *I*

List of Illustrations _____ *V*

List of Tables _____ *V*

Chapter One: Introduction _____ *1*

1.1Pros and cons of taxation of foreign trusts _____ **7**

1.1.1 The pros of taxing trusts _____ 7

Chapter Two: Review of the Literature _____ *9*

2.1Preface _____ **9**

2.2A survey of the situation worldwide _____ **9**

2.3Tax evasion solutions – Trusts and tax havens _____ **10**

2.3.1Profile of an investor in tax havens _____ 10

2.4Foreign trust funds and tax havens as added value _____ **11**

2.4.1Lists of tax havens _____ 11

2.4.2Additional lists _____ 12

2.5What is a trust? _____ **13**

2.6Tax avoidance trusts _____ **14**

2.6.1Problems with trust assets _____ 14

2.6.2The trust as a corporation _____ 14

2.6.3Reasons for creating trusts _____ 14

2.7Types of trusts _____ **15**

2.8Trust usage in private banking _____ **18**

2.8.1Holding of financial assets in a private bank _____ 18

2.9Legal solutions _____ **19**

2.10A comparative review of trusts worldwide _____ **19**

2.10.1The situation in Israel compared to other countries _____ 21

2.10.2A global survey of the handling of tax planning _____ 22

2.11Taxation of trusts in American law _____ **25**

2.11.1Types of foreign trust income subordinate to American taxation _____ 26

2.11.2Additional issues _____ 27

2.12British law _____ 27

2.12.2Taxation of local trusts under British law _____ 29

2.12.3International taxation of British trusts _____ 33

2.13South African trust taxation _____ **34**

2.13.1Interpretation according to general law _____ 34

2.13.2Two possible obligations _____ 34

2.14Taxation of trusts in Australia _____ **35**

2.14.1Interpretation of basic concepts according to general trust law _____ 35

2.14.2The definition of trustee 35

2.15Taxation of trusts according to Canadian law 36
2.15.1Canadian domestic taxation of trusts 36
2.15.2Taxation of non-resident trusts 38

2.16Taxation of trusts in New Zealand 38
2.16.1The principles of the trust taxation method in New Zealand 39

2.17Trust-like entities 42
2.17.1Trusts according to the continental method (Switzerland) – Fiducie 42
2.17.2Trusts in Liechtenstein 43

2.18The trust as a corporation 46

2.19Offshore trusts as will substitutes 47
2.19.1Special characteristics of foreign trusts 47
2.19.2Problems taxing foreign trusts and accepted solutions 49
2.19.3Characteristics of beneficial tax regimes 50

2.20Between trusts and inheritance 52

2.21The main findings of the theoretical literature 52

2.22Relevant global research and the Laffer curve 55

.2.23Recent research in Israel 57

2.24The impact of fiscal policy on investments in OECD countries 58

Chapter Three: The Economic Significance of Trusts 61

3.1The economic meaning of trust funds 61

3.2Who do foreign trusts serve? 61

3.3The principles of taxation of trust funds today in Israel 63

3.4The reasons for a foreign (American) resident creating a foreign trust fund 65
3.4.1Why are trust funds preferred to offshore investments? 66
3.4.2The clear disadvantages of creating a trust fund 67
3.4.3A case of a clear advantage to create a Trust Fund 68

Chapter Four: The Research Methodology 72

4.1The research approach 72

4.2The research population 73

4.3The Delphi group research method 73
4.3.1Versions of the Delphi method 74
4.3.2The procedure for choosing participants 76
4.3.3The theoretical framework 77
4.3.4Summary of the method 77

4.4The research field 78

4.5The research objective 78

4.6The research question 78

4.7The relevance of the research ______ **79**

4.8The research tools ______ **79**

4.9The qualitative research ______ **79**

4.10The quantitative research ______ **79**

4.11The research process ______ **80**
4.11.1Data gathering ______ 80
4.11.2Data processing methods ______ 80
4.11.3Reliability and methods of validation ______ 81

4.12Research ethics ______ **81**

4.13The research limitations ______ **82**

Chapter Five: The Research Findings ______ ***84***

5.1Summary of the qualitative research – open questions ______ **90**

Chapter Six: Discussion ______ ***97***

6.1General ______ **97**

6.2The main findings and their discussion ______ **97**

6.3Discussion of the impact of government investments ______ **100**
6.3.1The impact of government expenditures and tax burden on growth in Israel 100

Chapter Seven: Summary, Conclusions and Recommendations ______ ***102***

7.1Summary ______ **102**

7.2Conclusions ______ **104**

7.3Recommendations ______ **106**
7.3.1Principles of the combined solution ______ 108
7.3.1Principles of the combined solution ______ 108

7.4Recommendations for further study ______ **108**

Bibliography ______ ***109***

Appendices ______ ***115***

Appendix 1: The research questionnaire ______ **115**

Appendix 2: Income of tax authorities – January to December 2005 ______ **121**

Appendix 3: Tax authority income 2004-2005 and real change rate each month versus parallel month previous year (NIS billions) ______ **122**

Appendix 4: State income from taxes (NIS billions) ______ **123**

Appendix 5: Gross National Product 1995-2005 ______ **124**

Appendix 6 ______ **125**

Appendix 7: The distribution of the Consumption over the last Decade (1995-2005) ______ **126**

List of Illustrations

Graph no. 1: Expenditure for social services (including development budgets) – 2005 (in NIS billions)........1
Graph no. 2: Development of social spending as a percentage of government spending (without return of debt): 1980-2004........2
Graph no. 3: The indirect tax burden as a percentage of the GNP globally, 2002........3
Graph no. 4: Distribution of state income for 2005 (percentages)........3
Graph no. 5: Decrease in direct taxes 2010 vs. 2005........4
Graph no. 6: Decreasing corporate tax rates to 25%........5
Chart no. 1: Discretionary Trust/ Common Law Trust........32
Chart no. 2: Foundation (Panama)........47
Chart no. 3: Growth rate per capita........53
Chart no. 4: Principles of taxation of trust funds today in Israel........64
Chart no. 5: Advantages of taxing trusts........70

List of Tables

Table no. 1a: Distribution of respondents on the topic of taxing foreign trusts and foreign investors........84
Table no. 1b: Distribution of respondents regarding taxation of foreign trusts and foreign investors........85
Table no.1c: Distribution of responses regarding taxing foreign trusts and foreign investors........86
Table no. 2: Matrix of correlations between the research variables........87
Table no. 3: Matrix of correlations between items in the research questionnaire........88
Table no. 4: Matrix of correlations between research questionnaire items........89
Table no. 5: Comparison of tax laws of different countries........107

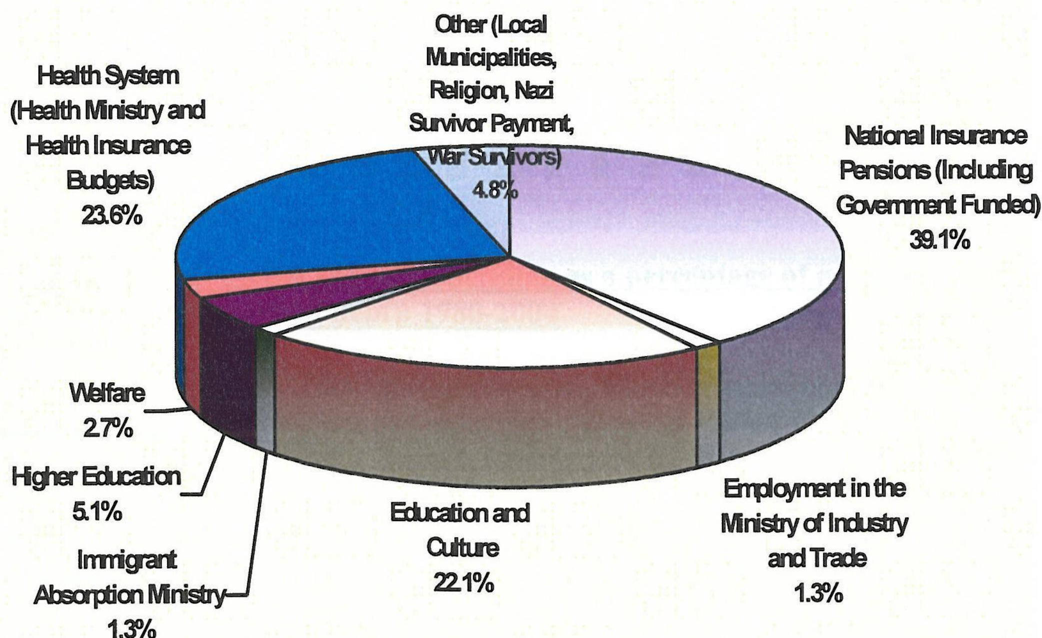
Chapter One: Introduction

Since the beginning of humanity, from the beginning of the time when taxes were collected from citizens, creative solutions have been sought to decrease the tax burden or even to evade tax payment.

One of the original methods used is the "tax haven" (Doggart, 1987).

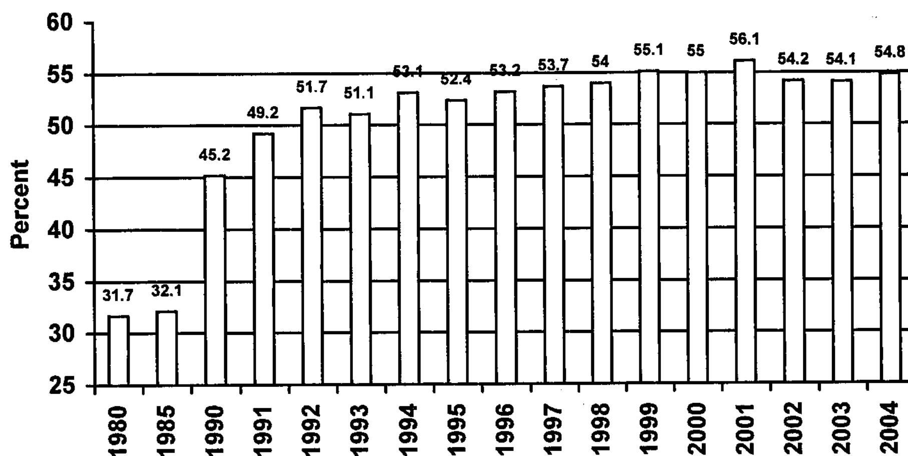
How is the need for a tax haven created? The root of the problem lies in the fact that in most normal countries, the tax burden falls on a relatively limited section of the population. Actually, this is a sort of Paretto, in which 20% of the population pays taxes for 80% of the population.

In Israel, the tax threshold, i.e. the level of income from which one begins to pay taxes, is a monthly income of approximately $1000 (income from salary, occupation or a business). Therefore, the lower deciles do not pay any tax at all. But moreover, in order for these people to live with dignity, they receive stipends and welfare payments from the Welfare Ministry and National Insurance (see graph no. 1).



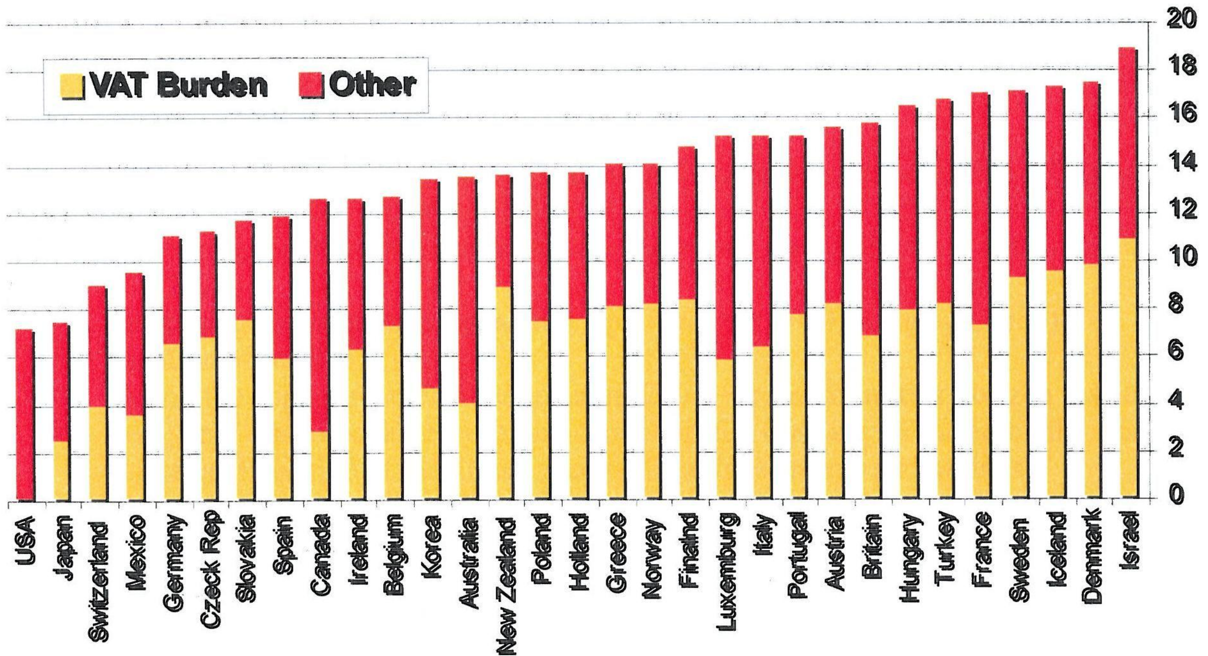
Graph no. 1: Expenditure for social services (including development budgets) – 2005 (in NIS billions)

Most of these payments come from taxes paid by honest citizens on whom the tax burden is particularly high. This government social spending only continues to grow as part of the total government spending as illustrated in the graph below.



Graph no. 2: Development of social spending as a percentage of government spending (without return of debt): 1980-2004

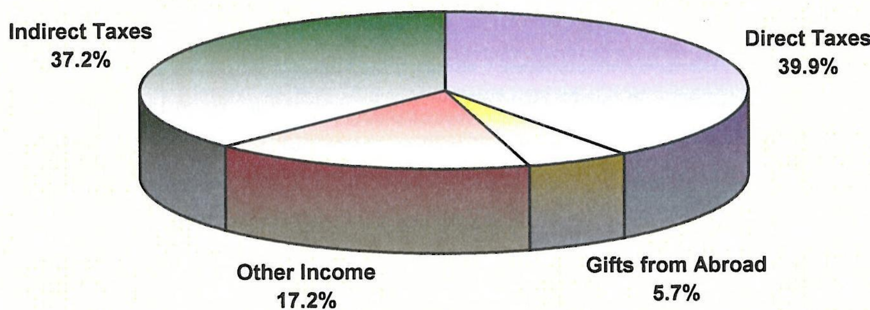
The tax problem results from the conflict in which simple honest citizens find themselves. This problem is defined in layman's terms as "Black Capital". This means that because of the creation of a heavy tax burden on citizens (from direct and indirect taxes) (see graph no. 3 below) there is pressure to overlook certain income when reporting to the tax authorities. In other words a "Black Economy" exists that, according to cautious estimates, has reached the scope of the entire GNP of the State of Israel!



Graph no. 3: The indirect tax burden as a percentage of the GNP globally, 2002

A complex situation has been created according to which a certain number of problematic conditions exist. Government income, particularly from direct taxes, has declined greatly (see graph no. 4) for the following reasons:

a. Inequality in the distribution of the tax burden;
b. An enforcement policy that is not strict enough;
c. A social mood according to which the establishment itself is corrupt and therefore there is legitimacy in not reporting income;
d. The profit overrides the risk (small chance of being caught);
e. Many of the tax laws are obsolete and irrelevant.

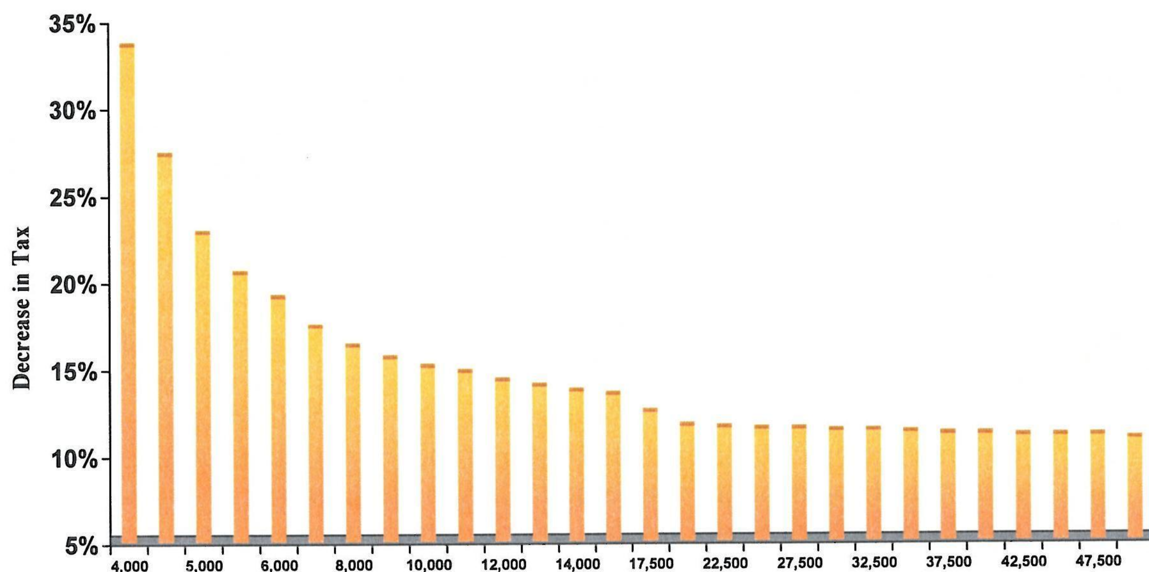


Graph no. 4: Distribution of state income for 2005 (percentages)

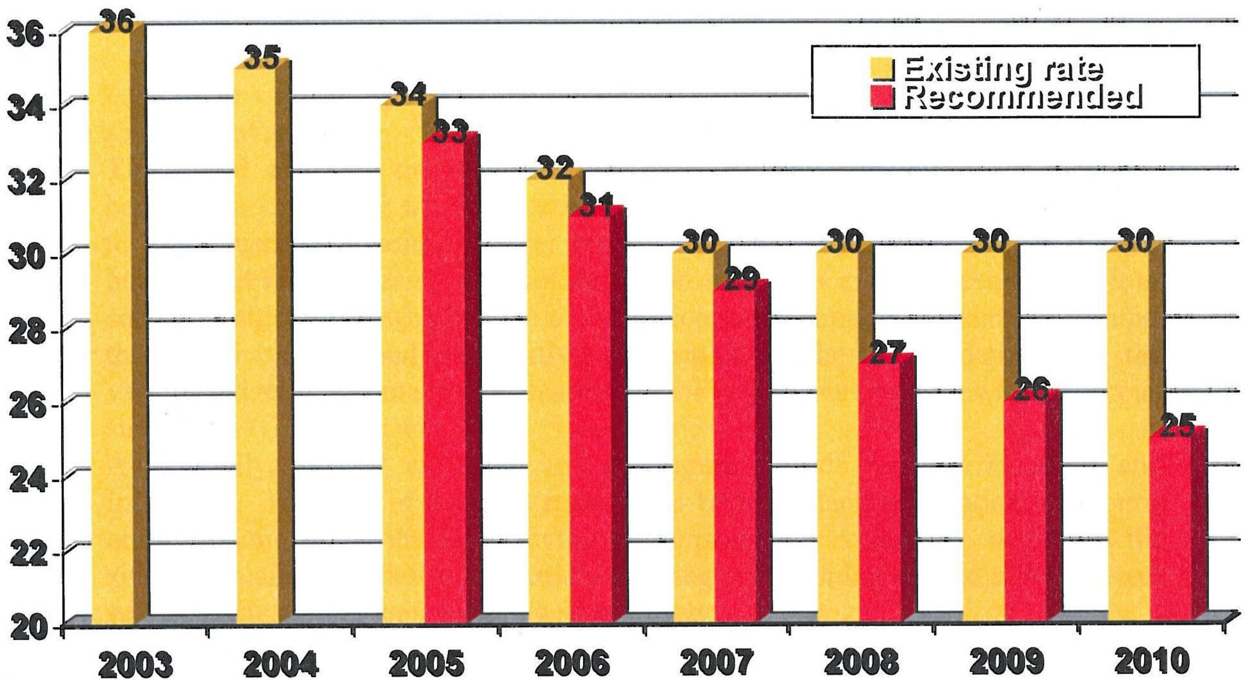
In light of the above, a number of committees were created, and in June 2002 a recommendation was made by the committee headed by Mr. Eitan Robb, the director of the Israeli Tax Authorities. The decisions that were taken are known as the 2003 "Rabinowitz Committee", (Report, 2003), whose recommendations were implemented by the Israeli government, and a new tax reform went into effect that year. The basis of

the tax reform was expanding the tax burden and improving tax collection. This was done through legislation, mainly:

1. Decreasing the direct tax burden on the individual (see graph no. 5 below) by the year 2010.
2. Decreasing corporation tax gradually up to the year 2010 (see graph no. 6)
3. Taxation of retirees
4. Taxing the capital market, whereas until 2003, income from this horizon was tax free. This was to be done by taxing capital profits from stocks traded on the stock market and taxation of maximum income from investments and savings.
5. Decreasing tax rates on capital gains from non-commercial assets and real estate, to a rate of up to 25%.
6. Changing the taxation method from territorial to personal taxation. Territorial taxation means the obligation to pay tax on income connected to Israel, i.e. income derived or received in Israel. The territorial method includes income from work that an individual did in Israel, or a business for which control or management were in Israel. Upon the implementation of the tax reform, beginning on 1.1.2003, the taxation method changed to one based on personal taxation, as a result of which Israeli residents will be taxed in Israel for all income that was derived or found within or outside of Israel.
7. International taxation: Within the framework of the transition to the personal taxation method the Israeli legislator was forced to adapt existing laws in all areas related to taxation of trusts in general, and taxation of trusts managed abroad specifically. Because of the importance of this issue, the committee decided to leave the work to a separate committee, and therefore no recommendations were consolidated on this issue, leading to the need for this study.



Graph no. 5: Decrease in direct taxes 2010 vs. 2005



Graph no. 6: Decreasing corporate tax rates to 25%

This researcher has been working by profession for many years as an accountant and Chief Tax Supervisor for the Taxation Authorities in Israel. In general, the position defines the preparation of tax assessments for large companies and factories for the purpose of collecting actual taxes. The position is both professional and operational, and this researcher has frequently encountered the problems mentioned above, raised and presented by taxpayers regarding the taxation method and regime in Israel, and the question of whether the taxation laws are just or not.

This leads to questions regarding the legitimacy of decreasing the right for tax planning, such as:

- Do individuals have the right to plan their business such that they will have to pay a minimum tax? Is this an absolute right?
- Is this right, although legitimate, a relative right that must be in keeping with other rights and interests?
- Is tax planning for the purpose of tax evasion, i.e., avoiding tax, legally defendable, on the criminal plane of taxation laws?
- In tax planning, has the taxpayer gone too far when there is no commercial reason for the transaction or any marginal or real purpose, entering frameworks in which the tax is decreased, not in keeping with the intent of the legislator (as is seen from the main purpose of the transaction and the general group of circumstances)?

These forms of tax planning can raise the questions of justice, morals, equality and more – questions that relate to the fine line between legitimate tax planning and tax planning that is not legitimate, and what the right of the government is in its support of

the public interest in collecting taxes and maintaining a just and egalitarian tax system, becoming involved in tax planning and ignoring it.

This leads us to various aspects of the legitimacy of limiting the right to tax planning from a number of angles:

a. **The social aspect** – the results of tax planning may hurt society as a whole, because they decrease tax payments by certain individuals within society leading to the government holding fewer shared resources. Determination of the tax burden and its manner of distribution within society is a direct result of various social considerations which relate to social-economic aims. Tax planning disrupts this social balance and the relative distribution of the tax burden among the various citizens, and makes the distribution of the tax burden unjust from a social standpoint (Gross, 2004).
Additionally, use of the right to tax planning leads to discrimination and inequality. The lack of equality stems from both the lack of identical economic ability among taxpayers in receiving this type of tax counseling, and from the situations caused by faulty legislation allowing tax planning only to a limited part of the public, and certain sectors within society.

b. **The economic aspect** – Tax is one of the central sources of budgetary financing for the government, allowing the government to determine goals and national priorities, and apply them. Increased tax planning and a significant drop in tax collection, leading to a decrease in the tax base, may cause an increased tax burden for a more limited group of the population, and as a result, increase the government's involvement in free markets, then leading to increased distortions and lack of economic efficiency, caused by this involvement (Glicksberg, 2003).

c. **The moral aspect** – The moral aspect involves social issues. According to this aspect, tax planning increases the tax burden on those who do not use tax planning. Tax planning damages the horizontal and the vertical justice of taxation. Damage to horizontal justice is expressed in areas where two tax payers with identical financial abilities and identical income carry different burdens as a result of the tax planning implemented by one of them. Vertical damage is expressed when the difference between two tax payers with different financial abilities is not reflected in their tax burden, as a result of tax planning. In other words, the damage caused to the group of non-tax planners stems from the fact that the division of the tax burden within society is not determined solely according to the principle of the ability to pay, but is also affected by the ability to implement and to fund tax planning (Glicksberg, 2003).

d. **The political-democratic aspect** – The taxation establishment is based on the idea of partnership, and is one of the cornerstones of a democratic regime, as society agrees to a democratic process of taking on the tax burden, as determined by public appointees. Tax planning may cause stress stemming from the disparity between the legal-formal tax regime and the tax regime stemming from tax planning. This stress, in the very sensitive area of private property, may erode social agreement regarding taxation arrangements, and be expressed as public protest, whether as a direct protest against tax laws or as an indirect protest against other government activities.

The question of legitimacy of tax planning in the context of tax laws touches on the issue of the balance of individual interests *versus* the public interest. Should the interest of the individual citizen be favored, as expressed in freedom to create contracts and plan taxes in an optimal manner for himself, or should the public interest be a priority, collecting taxes and maintaining a just and egalitarian taxation system?

This is connected to section 7, mentioned above, according to which the new method of taxation is on the channels of investment that till now were not taxed, and the many foreigners who invested in Israel and were tax exempt till now.

Hence the question, what is the government's role when applying fiscal policy? Is expanding the tax base by taxing foreign investments from abroad the correct way to increase the tax pie? Or should it support encouraging foreign investment and investment by foreign funds in order to create employment and growth.

This leads to the question of the weight of the burden and how to fight the problem of searching for tax havens, i.e. setting up foreign trusts in the desire to evade or avoid paying taxes.

If we want to be more specific in defining the problem we can ask : “How can taxation of trust funds in countries that have a treaty with Israel be applied in Israel, when they are set up to avoid payment of tax in Israel?

Definitions of these issues will be detailed in chapter 2.

This problem is not simple at all, particularly in the situation when opinions are mixed regarding the effectiveness of the step of taxing this channel.

1.1 Pros and cons of taxation of foreign trusts

There are many opinions regarding this issue. Attorneys' offices and large companies oppose taxation and raise arguments such as:

1. The escape of rich Israeli residents/citizens, with dual citizenship
2. Limiting foreign investments from foreign investors
3. Business transactions that are outside of the country
4. Legislation in this area has caused more aggressive tax planning by lawyers and accountants

1.1.1 The pros of taxing trusts

Those who support taxation of foreign trusts support this with a number of arguments:

1. The loss of hundreds of millions of dollars in taxes for the country annually (Globes, 6.7.05).
2. The tax loophole that has not yet been closed for the well-to-do will be open to many others also. There are already many trusts that were established abroad, estimated at $1-2 million that are not taxed in Israel.
3. Closing this tax loophole in order to create uniformity and in order to decrease the direct tax burden (Kaplan, 2000).

4. Israel's change of position *vis-à-vis* other countries that have already applied such laws as regards attracting capital after application of the law, and lowering taxation rates.
5. The tax monies that will be collected will be used for important aims, such as:
   a. Increasing social expenditure as a percentage of government spending (see graph no. 2).
   b. Increasing expenditures on social services (see graph no. 1).
   c. Improving the GNP and per capita consumption (see graph no. 6). (Central Bureau of Statistics - CBS, 2005).

In conclusion- this study aims to examine whether the final product is for the benefit of the "little" citizen. Will we, by taxing foreign trusts, increase the tax pie, and as a result achieve social goals such as equality in the distribution of the tax burden, or, will the opposite occur. It is possible that non-taxation of trusts may lead to positive results, such as:

- Avoiding the escape of foreign capital
- Causing an increase in investments in Israel
- The formation of new businesses
- Israel becoming a tax haven

In the end, the flow of capital from abroad will create the same cash flow, and perhaps even more than monies that would have been collected by the taxation of foreign trusts.

The issue in this research is to examine the benefits of taxation of foreign trusts in Israel according to the new tax reform, on the hypothesis that lowering the barriers will better serve the main goals of the Israeli treasury than intensifying the tax burden. The study further aims to examine the impact of applying different types and rates of taxes on change in the growth rate of the Israeli national economy. It also strives to examine the balance between individual and public interests concerning taxation issues with a focus on taxation of foreign trusts.

Due to embarrassing financial affairs in recent years, the importance of this and other studies is further sustained. These exploited malpractice accounting loopholes, the most recent of them such as Worldcom, Enron etc. The need to fight Complex accounting structures including the establishment of daughter companies and legal entities in off- shore countries and tax shelters for creating complex financial deals that served the needs of very few.

Both the European Commission and the OECD paid attention to reducing the risk in such practices. Consequently, this researcher considers trust fund investments to be a preferable alternative to tax exemptions for offshore investments, especially following the implementation of the new Israeli tax reform as of 1.1.06 .

The study can be divided into two main parts: The first part includes three chapters - the review of the literature, the relevant definitions and classifications. The second part presenting the dissertation plan, the empirical research, the findings, conclusions and recommendations

Chapter Two: Review of the Literature

The present literature review will discuss various forms of tax planning, including aggressive tax planning and creative solutions found by owners of capital, such as removing capital to tax havens, and characteristics of these havens, the establishment of a foreign trust as an instrument for tax avoidance, types of foreign trusts and their goals, and the situation in Israel and other countries regarding these issues focusing on Anglo-American countries, and the United States primarily. This writer will then discuss entities that are like trusts that are accepted in countries such as Switzerland and Liechtenstein.

Summary of the review the writer will discuss problems that arise when taxing foreign trusts .The recent research worldwide and in Israel in this topic, his hypotheses and the reasons for choosing this comparative resources .In due course he will offer solutions to these problems.

2.1 Preface

Since the dawn of humanity, from the beginning of the era in which taxes were collected from citizens, creative solutions have been sought to decrease the tax burden or even to evade tax payment. One of the original methods used is the creation of a trust. A trust is an entity created and governed under the State law in which it was formed (Trust Law, 1979). A trust involves the creation of a fiduciary relationship between a grantor, a trustee and a beneficiary for a stated purpose. A trust may be created by any of the following methods:

- A declaration by the owner of property that the owner holds the property as a trustee;
- A transfer of property by the owner during the owner's lifetime to another person as a trustee;
- A transfer of property by the owner, by will or by another instrument taking effect upon the death of the owner, in trust, to another person as trustee;
- An exercise of a power of appointment to another person as trustee or an enforceable promise to create a trust (http://www.irs.gov/businesses/small/article/0,,id=106551,00.html).

2.2 A survey of the situation worldwide

In recent years there has been increased activity in aggressive tax planning on a global scale. The tax losses in various countries are considerable and investment in planning and consulting has been increasing, both regarding costs and regarding personnel. Consequently, various countries have begun to take steps against damaging tax planning, in order to fight against and eradicate the phenomenon (Report of the Committee for Trust Taxation, 2003).

In some countries special emphasis is placed on tax planning in corporations and financial structures, including *via* countries considered tax havens, and malicious use of tax conventions (treaty shopping).

Most of the steps that have been taken are in the field of obligation of disclosure, fines, and internal instructions to focus handling of taxes on the issue, and bringing files of

taxpayers to the courts for decisions (Convention between Israel and the US, 2005). An additional type of step, particularly backed by the OECD and the European Union, relates to international cooperation as a means for increasing enforcement, and understanding international transactions.

2.3 Tax evasion solutions – Trusts and tax havens

"Most of the players of the international money game are overseas because of taxes. They share with all the peoples of the world a desire to pay less taxes" (Gross, 2001:31).

2.3.1 Profile of an investor in tax havens

In the short history of the field, there have been a few hints according to which it is possible to sketch the profile of investors in offshore investments. They include residents of countries such as the US and Britain, which have profit taxes when transferring from investment to investment. Such people clearly are interested in investing outside of their countries. The high rate of offshore trust funds managed by administrative groups in those countries prove the effectiveness of this incentive.

Second, the cash pool held outside of the area of jurisdiction of countries in which taxation is high is increasing. Clearly, it is impossible to estimate its size. Part of this pool belongs to former residents of countries with high taxation rates who left to enjoy the more comfortable fiscal climate in the tax haven. Part stems from Middle Eastern or South American petroleum income, and part stems from the anonymous money, that in better days, preceding inflation, collected dust in numbered accounts in Swiss banks.

A third group of investors in offshore foreign trusts, whose importance is continually growing, is composed of individuals who live outside their countries. Among these are "nomadic" employees of international companies who receive healthy salaries (in which special benefits and additions raise the salaries), or self-employed workers who receive high salaries in places where the opportunity to waste money is not great. For such individuals, an offshore trust fund is an ideal means for accumulating capital. It allows flexibility in transfer from country to country without any worries regarding local taxation of income or capital profits. As of now, it offers the advantages of investment management by experts, and avoids problems of communications stemming from investment in foreign stock exchanges. The tax planning of an individual who lives outside of the country retires from his work may be very simple.

The fourth and last group of investors includes institutions and trustees. For institutional fund managers or trustees with difficulties, who are interested in achieving the advantages of professional specialization in a certain sector, the offshore trust fund, managed by a reputable group, may be the ideal solution. The daily management of the fund is in the hands of others, and the manager is not worried about the technical problems involved in foreign stock exchanges, or, for example, investment in real estate. A few groups in the insurance field have jumped at this opportunity, in addition to private funds and pension funds.

One of the methods of aggressive tax planning today is the establishment of trust funds in order to save on taxes. According to publications in the Israeli press, trusts and

aggressive tax plans have become the most significant tax loopholes. Recently the creation of foreign trusts for the purpose of avoidance of tax payment has been identified, estimated conservatively at $1-2 million (Klogman and Kaputa, 2004). This is in contrast to the scope of trusts in recent years that had been at a reported rate of hundreds of millions of dollars. This was revealed to the Finance Committee by the Senior Deputy of the Tax Authorities, Jacky Maza. He explained the phenomenon saying that more Israelis have discovered the fund as a tool for a tax haven and are interested in it as a result of the media attention given recently to taxation of the trust framework.

It has also been said that the use of foreign trusts to avoid taxation has expanded in recent months. The director of the Taxation Authority has said that hundreds of millions of dollars in income have already been lost.

In addition, it has been estimated that the part played by the banks, according to these publications, may reach $25 million in service charges alone.

We therefore see that the amount of money stemming from taxation of foreign trusts may reach several percent of the income from taxes (the rate of taxation for the 2005 tax year stands at $18.6 billion – see distribution in graph no. 4).

2.4 Foreign trust funds and tax havens as added value

The US, British and other fiscal authorities demand that the control and management related to reputable foreign trust funds will take place within the chosen tax haven. This is the return that the tax havens receive for freedom from supervision of the currency and taxes that they provide to foreign funds. Fund transactions create opportunities for employment in the tax havens and send capital flowing into them. They also create secondary income from taxes stemming from registration fees, stamp tax and consumption taxes paid by those who are employed. These are all wind in the sails of development plans within tax havens. New jobs are added, not only in the area of offshore activity of the fund. The impact of financial prosperity in this field has a strong ripple effect in the areas of construction, and industrial and professional services, in the media sector and even in agriculture and fishing (Ginossar, 1999). Tax havens which have thus produced the maximum advantage from external business, are the Bahamas, Bermuda, the Cayman Islands, and even more so, the Channel Islands and the Isle of Man. Luxembourg, and Curacao have also been successful, but the impact of this for them is not as great because of the scope of other offshore and onshore activities in these countries.

2.4.1 Lists of tax havens

Germany was the first country to compile a methodical list of countries serving as tax havens. This list appears in the "*Aussensteuergesetz*", the 1972 tax law related to foreign relations and does not define the countries mentioned as tax havens (Doggart, 1987).. Using diplomatic language, the law describes the countries listed as countries in which taxation is low. At first, the purpose of the list was only tax havens for individuals, not corporations, and was organized as follows:

1. *Countries in which there is no income tax at all*: Andorra, Bahrain, Monaco (excluding French citizens), the Bahamas, Bermuda, Turks and Cayman Islands, Tonga, and the New Hebrides (now Vanuatu).
2. *Countries in which income tax is at a low rate*: The Channel Islands, Gibraltar, the Isle of Man, Liechtenstein, parts of Switzerland (excluding Geneva, Neuchatel, Valais, Woo and various municipalities in Aargau, Berne, Lucerne, Ticino, Torgau and Zurich, which are included in category 3), Anguilla, the Dutch Antilles, Gilbert and Ellice Island and other places such as the Norfolk Island, Papua New Guinea and the Solomon Islands.
3. *Countries which hold clear advantages in taxation*: Switzerland (taxation based on consumption in a federal taxation system), and Panama (exemption of taxation on dividends abroad and income received abroad).

Several territories on this list have achieved independence since 1972 and received new names and more demanding taxation systems. Papua-New Guinea, Kiribati, Tuvalu, Solomon Islands and Anguilla are not considered to be countries in which income tax is low any more. In all areas related to corporations, a red light regarding tax havens will light up when a foreign corporation owned by a certain countries are taxed abroad at an effective rate lower than 30% (Doggart, 1987).

Germany was the first country to present data regarding preferred tax havens for its citizens. In a response of that country's Ministry of Finance to questions in Parliament, it was found that the number of corporations registered in low taxation countries in which German residents had holdings reached 17,635 in 1986. Preferred tax havens for Germans were Switzerland and Liechtenstein. In these two countries alone, 12,200 of all of the above-mentioned corporations were registered, followed by Luxembourg with 4,200 corporations, Panama (608), the Bahamas (220), the Dutch Antilles (167), the Channel Islands (101), the Cayman Islands (70), Monaco (55) and the Isle of Man (14).

2.4.2 Additional lists

Australia, the US, Britain, Japan, France and Canada have also composed lists of countries that seem to be tax havens (black lists), or are not considered tax havens (white lists). In the classification offered by Britain, there is an additional gray list, in which counties that are occasionally considered tax havens are recorded. The legal status of these lists differs from country to country.

Australia: The list of countries suspected to be tax havens by the Australian government is part of the Banking Law, and is fully validated by it. In any case of a foreign currency transaction in a country appearing on the list (of tax havens), the transaction must be brought to the attention of the Tax Commissioner, who may cancel or change it if there is a suspicion that it involves tax evasion or tax avoidance, or if it involves a case of capital depletion. In addition to the tax havens that appear in the West-German list (see above), the Australian list includes the Virgin Islands, the Cayman Islands, Grenada, Hong Kong, Liberia, Luxemburg and Nauru.

Canada: The Canadian list is included in the Income Tax Ordinances and is validated by law. This is a white list that relates to taxation of dividends through Canadian organizations, from foreign corporations with partial Canadian ownership of at least 10%. Surprisingly, it includes a number of countries that generally appear on black

lists such as Barbados, Liberia and Switzerland). This stems from existing or pending tax conventions between Canada and these "white" tax havens.

France only has an unofficial list of tax havens. This list is part of an internal administrative document, apparently leaked with the agreement of the government. A foreign corporation in French control is considered to be in a tax haven if the tax on it is less than two thirds of the tax that would be obligatory in France. The list overlaps the German and Australian lists, but also includes Uruguay, Djibouti, Jamaica, Venezuela, Kuwait, Lebanon, French Polynesia, and Costa Rica.

Japan: The Japanese black list of tax havens is also validated by law. A country that is not on the list will not be considered a tax haven even if the taxation rate is lower than half of the rate in Japan (this list defines tax havens as countries in which the tax burden is less than half of the tax burden in Japan). This list, published in 1978, adds Barbados, Cyprus, Djibouti, Macao, and Saint Vincent to the original German list.

In Britain a white list was added to the 1984 Budget Law. This list serves the tax authorities in handling foreign corporations under British control (CFCs). Countries were removed from the list whose tax burden is less than half of that in Britain. Ireland, the US, Belgium, Holland, Luxemburg, Malta, Singapore, and 22 other countries appear on a restricted gray list. The eligibility of a foreign corporation under British control listed in one of the countries on the list for certain tax benefits is determined whether the corporation is considered a corporation operating in a tax haven or not. An example of this is the American foreign sales corporation. A foreign corporation in British control that operates in one of the countries on the white list is not taxed in Britain.

2.5 What is a trust?

A trust is a legal concept. It is a web of legal relationships according to which the creator of the trust (the trustor) transfers ownership of his assets to a trustee. The trustor provides the trustee with legal ownership of the assets and the right to act as a trustee according to the instructions of the trust deed, and according to the law (Trust Law, 1979).

Sometimes the trustor provides a letter of wishes along with the trust deed, in which he expresses his desires regarding the manner of managing the property in the fund by the trustee.

The letter of wishes, given to the trustee, has no legal validity, and seemingly the trustee may ignore these instructions. In practice, trustees tend to consider the contents of this document and a legal mechanism may even be created ensuring upholding the wishes.

The trust is not the same as an agency. The trustee does not hold the assets for the original owner. The trustee holds the assets for the beneficiary or beneficiaries. There is no reason for the trustor, the creator of the trust, to be appointed over the assets.

What is special about this legal arrangement is that the identity of the beneficiaries may be changed during the existence of the trust (using a certain legal technique), and it is

possible to determine who will replace a beneficiary who passed away. This change does not involve legal processes such as an order of probate or the existence of a will.

The beneficiaries have no rights to the assets in the trust. They only have rights regarding the integrity of the assets, according to the rules and instructions determined in the trust deed (Tzlenter, 1999).

There are a number of cases in which a trust is established for beneficiaries who will be born in the future, or who are unidentified and will be determined according to the considerations of the trustee. This type of trust is called a Discretionary Trust.

2.6 Tax avoidance trusts

2.6.1 Problems with trust assets

In most countries the trust is not recognized as a separate legal entity that may hold, acquire or sell assets. In certain countries, such as the US, the tax authorities are willing to recognize the trust as a taxpayer, and relate to it as a body separate from the beneficiary for whom it was created. However, in most cases, if assets are purchased or held by a trust, they will be registered to the trustee (Shekel, 2001).

2.6.1.1 The solution to holding assets

There is no reason to prevent the trust assets from being registered to the trustee, but such registration could be problematic if the trustee passes away, or becomes involved in bankruptcy proceedings. Therefore, trustees tend to set up companies in which they hold shares for the trust. This company is managed by the trustees (directly or through appointed managers), and becomes a holding company for the trust's assets.

When there are monies or financial assets at hand, the company will open a bank account and hold the assets of the trust.

2.6.2 The trust as a corporation

Several countries recognize the trust has having a separate legal identity. Liechtenstein, and recently, Panama and the Antilles, have also recognized other legal structures such as foundations.

Illustrations illustrating the structure of a foundation *versus* the structure of a trust are shown in appendices 6 and 7.

2.6.3 Reasons for creating trusts

The trust institution has existed for hundreds of years. There are many reasons for establishing a trust of which tax planning is only. The following are the main reasons for establishing a trust:

- Planning the benefits of assets for a number of generations of beneficiaries: The creator who is taking care of his descendents, whom he knows, and sometimes even those who have not yet been born and will be born only after his death, transfers his assets to a trust. By appointing an entity external to his family to

manage the family assets professionally, he ensures the welfare of his descendents for the coming generations, and, during his life, may direct the manner in which the assets will be handled and the manner in which they are distributed to his descendents. For example, the creator of the trust determines in the trust letter that the trustee must distribute the profits of the assets such that his descendents enjoy a reasonable quality of life, but not a wasteful one.

- Protecting property against the litigation of creditors: This issue has developed particularly in the US, and is called asset protection. By transferring one's assets to a trust (generally a foreign trust), the owner of the assets ensures that his property is not taken from him to pay creditors for his debts. This method has become increasingly popular in the free professions in the US, after a number of malpractice suits were accompanied by high punitive damages that actually destroyed the plaintiff's capital. For example, high punitive damages against a surgeon for results of an operation that he conducted, wiped out his entire life savings.
- Coping with inheritance laws: Coping with complex problems created as a result of inheritance laws is unique to certain countries. Without going into details, we will bring the example of continental Europe, in which a will must consider minimal eligibility determined in inheritance laws. Sometimes trusts are established to bypass inheritance laws, in order not to bequeath to an undesirable heir even if the law requires it.
- Caring for disabled individuals (the disabled, the sick, etc.): Taking care of people with special needs is one of the classic goals of the trust. For example, parents who would like to ensure that after their death there is someone to care for their sick child, set up a trust for this purpose.
- Protecting family property from a family member with personal problems: Setting up this type of trust aims to ensure the welfare of a family member, who, if he had access to the capital, would waste it, such as a child who is suspected of using drugs, being a gambler or wastrel, etc.
- Pension plans for employees: Setting up this type of trust aims to ensure the future of retired employees and their families.
- A trust program for investment purposes: It is common to invest in cooperative trust funds in the stock market.
- Trusts for charitable purposes: Use of trusts for various public activities, particularly charitable works, is common.
- Ensuring control over family assets: A trust may serve to coordinate family property holdings and ensure control of diverse businesses.

2.7 Types of trusts

There are a number of methods for classifying trusts: According to the degree of influence of the creator, according to the method of establishment, according to goal, etc. The following are the various classifications affecting the manner of taxation, according to most recognized taxation methods, including Israel's (Hendrickson and Silverman, 1982; Jantscher, 1967; Scott, 1997).

1. Classification of trusts according to control remaining in the hands of the creator of the trust.

- Revocable trust: This type of trust is a trust in which, after delivery of the trust letter to the trustee, the creator maintains the power to affect the actions of the trustee regarding the trust. Power is usually defined as control of the creator or his ability to obtain control over assets transferred to the trust, or their profits. The term "control" does not only mean the ability to enjoy the assets or the profits of the trust personally, but also the ability to attribute the assets or profits to another individual. The tests for defining a trust as revocable may differ from country to country, but all include basic tests.
- Irrevocable trust: In this type of trust, the creator does not have the power to affect the actions of the trustees after establishment. The trustee must act only according to the trust letter and the law. In any area that the trust letter allows freedom of action the discretion is of the trustee only.
- Sham trust: According to all legal methods, common to all types of trusts is the basic condition that ownership of the assets is transferred from the creator of the trust to the trustee, and financial benefits of the property and its profits are transferred to the beneficiaries. Accordingly, every legal system has defined a clear framework for the existence and management of trusts. Transfer of assets for management, in contrast to the basic condition and legal instructions regarding a trust, will not be considered a trust. Such a trust is only a sham trust, i.e. an artificial trust. For example, in certain cases the creator of the trust or a beneficiary ignores transfer of legal ownership of assets to the trustee and maintains control over the assets or their manner of management. Under such circumstances, the courts have determined that in light of the fact that the power and authority for management of the trust assets remained in the hands of the creator or were given to a beneficiary, the trustee was not allowed to act independently, as he is authorized to do, and the trust is a sham trust.

2. Classification of trusts according to goal

- Charitable trusts: This is a trust that is established for charitable purposes only. Charitable trusts are usually registered in a public register and are supervised by the government in order to ensure that the monies in the trust are in fact reserved for public purposes. In certain countries there is an enforcer, a position similar to a protector, who may ensure that the goals of the trust are realized for charitable purposes. In other countries there are various mechanisms for supervising such trusts, in order to ensure that they do, in fact, operate for charitable purposes. Such trusts are not limited by time.
- Private trusts: There are different types of private trusts. A private trust, in contrast to a charitable trust, operates for the benefit of individuals or commercial bodies and is limited by time. A private trust is not registered in an open public register. The following are types of private trusts:
- Discretionary trusts: The beneficiaries or their rights are not predetermined, but are given to the determination of the trustees, at their discretion. This is the most common and accepted manner of setting up a trust, based on the great flexibility that it allows the trustees.
- Interest in possession trusts: In this type of trust, a certain beneficiary is determined for the entire length of the trust, to receive its profits or assets. After the death of the beneficiary, his rights will be transferred to a

group of eligible people (such as his descendents). These rights do not generally transfer to eligible individuals whose names were listed ahead of time, but rather the trustee is given the power to act according to his discretion and determine the identities of the beneficiaries and the amount budgeted to them from the trust assets or profits.

- Fixed trusts: The identities of the beneficiaries and their rights are predetermined in a clear and precise manner. The trustee is given authority to manage the assets of the trust, but he has no discretion in determining the beneficiaries or changing the rights of the beneficiaries when distributing assets or profits. For example, determining the eligibility of the wife of the creator to receive only profits from the trust, and after her death, the distribution of the capital among the descendents of the creator.
- Cumulative trusts with current payments: This type of trust is usually created for the children or grandchildren of the creator of a trust fund. The trustees are authorized to pay monies for the benefit of the education and welfare of the beneficiaries during their adolescence, and are authorized to accumulate income that will not be used for the abovementioned goals, as assets of the trust. When the beneficiaries reach a certain age, as determined by the creator, they will be eligible to a certain portion of the trust's assets.
- Protective trusts: In this type of trust, the rights of the beneficiary to the assets of the trust will decrease or be cancelled if the beneficiary attempts to sell or transfer his rights or his income from the trust fund. In principle, this type of trust protects the beneficiary from the temptation of giving up his rights to the trust assets.
- Asset protection trusts: A trust established in order to protect the assets of the trust against bankruptcy or future legal obligations. A number of offshore countries have legislated laws allowing the creation of asset protection trusts. In other countries that have not legislated laws recognizing this type of trust, the courts may not recognize a trust that is established in order to avoid future creditors.
- Commercial trusts: The main applications of commercial trusts are for the purposes of pension funds, unit trusts, cooperative trusts, trusts for bond holders, etc.

Egyetemi Könyvtár
Pécs

3. Classification of trusts according to method of establishment

There are a number of methods for establishing a trust or a number of events on which establishment of a trust is based. Trusts may be classified according to their method of establishment:

- Expressed trusts: This is the most accepted manner, according to which the trust is established by a detailed trust letter.
- Implied trusts: An implied trust relates to cases in which, from the behavior of the parties and their actions, it is clear that the intent existed to create a trust, but for some reason was not clearly expressed. An implied trust will be recognized as a trust should the intentions of the trust creator or the testator are implied from his words (without the explicit use of the word "trust") or in the case that the legal meaning of the action taken is a trust. Because of the nature of such trusts, there are no formal demands to recognize them, and the trust is inferred from the circumstances of the

case. Generally, the existence of such a trust is determined in a legal process and the conditions of the trust are detailed in a court decision.

- Constructive trusts: Trusts that are imposed by the courts serving as a tool to achieve just results. This type of trust is established based on the hypothesized intents of the trust creator or testator, or, when intent is lacking, from the force of the laws of integrity, when the court feels that it would be unjust to allow the individual holding the assets to continue to hold them for his personal use, when there is another individual who is eligible to receive the assets or its profits.

2.8 Trust usage in private banking

2.8.1 Holding of financial assets in a private bank

In recent years, three myths have been shattered regarding holding of assets and transfer of their ownership or endowment from father to son. Several 'myths' are related to the following actions:

- Numbered accounts: A numbered account is an account that does not carry the name of its owner but is marked by a number or a code. In contrast to common public opinion, a numbered account is not a legal entity separate from the individual. The code is only a screen hiding the identity of the account holder. Should the account holder die, the assets held in the account will be subordinate to estate laws and will be divided accordingly.
- Power of attorney: Customers of a bank will often give signatory rights to a legal representative to ensure that the money in the account will be transferred to the legal representative or to a third party at the time of death of the account holder. This goal is generally not achieved, since upon the death of the account holder the legal validity of the power of attorney expires. In order to receive permission to act upon the monies in the account, there is a need for a will or an order of probate. Opening of a joint account, allows overcoming this difficulty.
- Holding a bank account through a tax haven corporation: Often, a bank account is held for a customer through a company that was established in a tax haven country. In this case, the death of the customer, the account holder, would not create a problem for continued management of the account from the bank's standpoint.

  However, since shares of the company, registered as the account holder, are part of the estate of the deceased, an order of probate or will is necessary to determine the identity of the individual with the right to inherit the shares. Therefore, the fact that the shares are not registered on someone's name, but only to the bearer, is of no significance. A share registered to a name or to the bearer of the share, is an asset that belongs to the estate and will be distributed according to inheritance laws.

  In addition, under certain circumstances, the sum of money in the company account will be a sum belonging to the estate.

  The problem involved in holding bearer shares may arise in all of its severity in the case that the deceased was holding the share, for example, if one of the heirs held a bearer share of the deceased's assets and argued that he has become the owner of the assets. In such a case it is necessary to check if ownership of stocks

was provided from a legal standpoint (by receipt of the shares as a gift or acquisition of the shares). If ownership of the shares was not transferred from the deceased to his son during his lifetime, there is a need to determine the right of ownership of the shares in an order of probate or a will.

2.9 Legal solutions

- Will or Order of Probate: Usually, property holders' tend to leave a will. Validation of the will is a complex and sometimes costly procedure. Often, the representative of the legal advisor of the government will intervene (in the case of minors or protected individuals). The process may be lengthy because of differences of opinion among the heirs. Additionally, validation of the will or discussions regarding an order of probate, include publication in the media, which often infringes on individual privacy and may cause damage to families in countries in which the existence of assets outside of its territory may cause confrontation with the authorities.
- The trust: The solution for transferring assets from generation to generation without the need for an order of probate or validation of a will is found in the trust. This institution has existed for many years in countries ruled by English law. The trust was instituted in England in the Middle Ages, when Crusaders transferred their assets to a trustee in order to ensure the future of their families in the case that they did not return from their Crusade. The Franciscan monks made different use of the trust institution. They lived a life of modesty and personal and monetary abstention. Since monks may not own any property, they registered the lands that they worked to a trustee, and thereby could continue to work the land and enjoy its fruits, although, legally, ownership of the land was not in their hands (Grundy, 1988).
  The Israeli Trust Law does not satisfy all of the needs mentioned above. The main problem is that Israeli law does not allow the existence of instructions according to which the assets of the trust may be transferred from generation to generation ("Skipping a generation"), without the existence of a legal procedure to validate inheritance or a will. This is because instructions "skipping" a generation contradict the instructions of the Estate Law (Income Tax Ordinance, 2004).

In many other countries, the situation differs. The Trust Law, in these countries, allows determining instructions in the trust letter according to which the assets of the trust will be transferred to family members or other individuals, after the death of the creator of the trust, without the need for inheritance proceedings.
This type of trust is recognized worldwide and even serves as an important basis in the economies of many countries.
In general, private trusts can be divided into two types:
1. Countries following common law– England, the US, and Australia, and territories in which British law applies, such as the Virgin Islands, the Cayman Islands, Gibraltar.
2. Countries following continental law– Liechtenstein, Panama, and the Antilles.

2.10 A comparative review of trusts worldwide

One of the basic principles of taxation law is that one may not tax any individual or entity that is taxable, twice for the same profits. This means that the taxpayer will pay a maximal sum of tax, which is known and quantifiable, for a given income, whether paying it to one government or more.

This principle involves the desire to maintain individuals' basic rights, such as ownership, equality, freedom of occupation, etc., in developed economic societies.

This process has been doubly validated over the past decade, in light of the globalization processes taking place in the economic world in general, and in light of the liberalization which has taken place in control of foreign currency in Israel, specifically (Refael and Efrati, 2002).

In order to prevent the problem of double taxation, the Israeli legislator has appointed an organization on behalf of the State to sign anti-double taxation conventions. In fact, as of today, Israel has signed over 30 such conventions with different countries.

Often, the parties to a given economic transaction which goes beyond national borders, are not aware of the problems of double taxation that they will experience during their business activities, and even if they are aware of them, they are not aware of all of the different problems that may arise.

Resolution of double taxation problems is the task of tax experts, and in the early stages of negotiations, they must draw the attention of the different parties to the business transaction, towards the implications of the different tax sums that they will be paying, whether in their country of origin, or another country. These facts have important implications in profit considerations for both sides.

On June 12, 2002, the recommendations of the Committee for Tax Reform were published. The law for tax reform was passed in July 2002, and became applicable beginning 1.1.2003.

One of the main principles of the tax reform was a global change in methods of personal taxation. This means that residents of Israel (including companies and corporations, etc.) pay taxes to the Israeli government on their entire income, regardless of location.

The committee determined that it could not discuss the issue of trusts because of its complexity and scope. However, the committee recommended examining the taxation arrangements that should be applicable for trusts and, if necessary, to set them forth in primary legislation.

The present dissertation will aim to discuss the issue of double taxation as expressed in light of the recommendations of the committee, in a number of situations, among them the case of a resident of Israel setting up a foreign trust, according to American Law, with the beneficiaries being residents of Israel or the United States. Of course, this issue will be examined in light of the Conventions for the Prevention of Double Taxation, signed between Israel and the US.

As in any analysis of a business transaction, questions of double taxation will be discussed, for which the answers will be determined by the "taxation pie", set up between Israel and the US. These will include citizenship of the trustee, who has first rights, who has residual rights, and the timing of taxation and its payment.

2.10.1 The situation in Israel compared to other countries

The State of Israel has signed 36 conventions with different countries for the prevention of double taxation. Taxation conventions are an international agreement between two countries reflecting their agreement, among other things, over the division of taxation rights for different types of income (Arnold and McIntyre, 2001).

The stated goal of these anti-double taxation conventions is to prevent taxpayers paying double taxes on the same income. In the case of international business, double taxation situations may arise if more than one country realizes its right to tax the same income. This is therefore a form of clear cooperation between countries regarding taxation, which is particularly significant in an era of globalization.

The goal of such conventions is for the maximal sum of tax applying to a transaction to be no higher than the highest amount of tax charged by either country. Accordingly, there is usually no situation of double exemption from taxation, i.e., that the transaction is exempt from tax in both countries (double non-taxation). The rationale behind this is that the convention leads to neutrality regarding the tax, between the activity of the taxpayer in the country of residence and the action of the country in which the income was generated (country of origin).

The policy of the US and other countries on this issue is that the convention should not limit the right of taxation of the country of residence of the taxpayer, beyond what is necessary in order to prevent double taxation. This policy is called the "saving clause" (Hadari and Altar, 1994). In order to apply this policy, certain instructions are determined in the tax convention preventing the creation of double non-taxation. The meaning of these instructions is that tax benefits that the resident of one country enjoys (in the country of residence) do not apply in the case where the income is not taxable in the country of origin.

It should be noted that provision of "Treaty Relief" is not the sole path to relieving this situation of double taxation. An additional manner is through providing unilateral relief. Unilateral relief is relief which does not depend on mutual relations between the two countries. Relief, whether through a convention or through unilateral relief, is expressed in determining a limited taxation rate or a tax exemption for the income, or a full or partial return for tax that was paid in the other country.

Although double taxation may be prevented through unilateral relief, there are additional goals and advantages that may arise for a country which uses taxation conventions. On the other hand, there are various faults in these taxation conventions which make it difficult to apply and effectively implement the mechanisms laid out in the conventions.

Therefore, there is an obvious disparity between the goals and advantages of taxation conventions and reality, as expressed in implementation of the conventions. Countries must be aware of this disparity, find solutions, and consolidate a clear policy regarding existing and future taxation conventions.

It may be assumed that the traditional outlook regarding tax conventions will change, and this should have a beneficial effect over limiting the gap between the vision and reality.

2.10.2 A global survey of the handling of tax planning

As mentioned, most steps that have been taken worldwide are steps in the fields of legislation, court decisions and internal instructions. In general, they obligate disclosure and reporting by taxpayers and tax planners such that tax havens that are defined will be brought to the knowledge of the tax authorities, so that they may cope with them and eradicate them. It should be noted that in many countries worldwide, there exist general and specific anti planning instructions, aimed to prevent tax planning. A relatively new method is using the obligation of disclosure and reporting, and focused treatment of taxpayers and tax planners, budgeting significant material and financial resources.

The following is a survey of the various methods used to fight against tax planning in a number of countries.

2.10.2.1 The United States

In the US, a significant revolution has taken place in the attitude towards tax planners, and the obligation of disclosure and reporting has been placed on taxpayers and tax planners. This significant revolution occurred as a result of the Senate Finance Report (2003), which analyzes the problem of tax planning, the increased phenomenon of tax avoidance, an estimate that this phenomenon was leading to a short term loss in income from taxes and a long term negative influence over the taxation system in all areas regarding decreasing the tax base, lack of respect for the tax system, and non-economical use of resources (Department of the Treasury, 1999).

During the past decade, corporations have significantly increased their use of tax havens, using sophisticated techniques to significantly decrease their tax obligations in a harmful manner (abusive tax shelters).

In 1999, the President of the US recommended that a law be proposed to fight against corporation tax planning. In July 1999, a comprehensive document was published by the American Treasury, presenting the problem and how to treat it. The central problem, according to the report, was that coping with the phenomenon of tax planning had been specific to each case, if it was discovered at all, and there was no overall and comprehensive method for handling the phenomenon.

The following are the various instructions regarding the fight against tax planning in the US:

1. Taxpayers' Obligation of Disclosure: Beginning in February 2003, individuals are obligated to provide a statement detailing "reportable transactions" in their annual tax statement.
   A reportable transaction is a transaction that fits into one of the six categories determined in the legislation:
   - "Listed Transactions" – this category includes various specific transactions that are considered to be or suspected of being an abusive tax shelter. This category changes from time to time through amendments, and today includes 30 transactions.
   - "Confidential Transactions" – these are tax shelters offered to a taxpayer by a consultant on the condition that the taxpayer not expose the tax shelter, the structure of the transaction and the taxation handling of the transaction. Confidentiality relates to the tax planning and is aimed to allow the tax planner to continue to sell his shelters to other tax payers.
   - "Contractual Protection" transactions – these are transactions for which the taxpayer has a contractual right to partial or full return of the consultant's fees, if the desired taxation results are not achieved.
   - Loss transactions – these are transactions that create a loss, whether a true loss or a "paper" loss, for tax purposes only.
   - Transactions with a significant disparity between the income that is taxable and the mathematical profit on the books.
   - Transactions that involve holding assets for a short period.

   In certain cases, an exemption is given from reporting transactions.
2. The planner's obligation of disclosure: In the US, the obligation to report and register tax shelters has been determined. Anyone organizing or initiating a tax shelter must register the "shelter" at the tax authorities, on the day he first sells the shelter. This means that every shelter will be registered before marketing it to the public. Reporting to the tax authorities includes a description of the shelter and the expected tax advantages for those using it.
   Furthermore, according to the recent Internal Revenue Code Amendment, in the US, beginning from October 22nd 2004, the obligation to report and register is applied to anyone who assists, provides consulting or advises, whether a lawyer, accountant, tax consultant, investment house, or any other entity.
3. The obligation to maintain a user list: As of February 2003, the organizer or seller of tax shelters is obligated to prepare and maintain a list of "users" to be presented to the tax authorities, for any transaction suspected to be a potentially abusive tax shelter.
4. Systemic and operational changes: The Office of Tax Shelter Analysis (OTSA) was established within the American IRS in 1999. It was intended to focus on handling tax shelters and increasing the transparency and obligation of disclosure regarding transactions taking advantage of the complexity of the American Income Tax Code.
5. Increased enforcement and punishment: The existing methods of punishment in the US regarding aggressive tax planning include deficit fines for incomplete reporting, whether essential or negligent, fines for lack of reporting to those who prepare reports for taxpayers, promote tax shelters, assist in preparing documents related to incomplete reporting, anyone who does not register a transaction that must be registered, without good reason, and anyone who does not manage lists as required.

6. Gathering of information: In September 2002, the US tax authorities presented a penalty amnesty offer regarding tax shelters. According to this offer, taxpayers who disclose all information related to the tax shelters that they used would pay tax by law without any fines related to incomplete reporting (in general, 20% of the sum that was not reported). After four months this process ended and the OTS registered 1660 disclosures of 1206 tax payers who described new tax shelter structures.
7. Instructions to the public and representatives: The IRS plans to renew its instructions to the public and representatives. The guideline will place responsibility on lawyers and other representatives to act with integrity towards the tax system. The goal is to make it difficult to promote and market tax shelter tools.

In England, too, the tax authorities took significant steps in 2004 to fight tax avoidance schemes, based on the recognition that this was a phenomenon signifying a significant tax loss for the British Treasury (www.legislation.hmso.uk). The main steps taken in England are:

1. Taxpayers' obligation of disclosure: The Disclosure of Tax Avoidance Schemes was within the framework of the budgetary law of 2004. The obligation for disclosure and reporting was placed on the taxpayer if he himself performed the planning.
2. Planners' obligation of disclosure: The Disclosure of Tax Avoidance Schemes was within the framework of the budgetary law of 2004. Obligation for disclosure and reporting was placed on the promoter of tax plans of the types detailed in the regulations.
3. Systemic changes and infrastructure: The Tax Authorities set up the Tax Avoidance Intelligence Unit. In addition, special forms were distributed for reporting by promoters and taxpayers.

2.10.2.2 Australia

In Australia, too, the tax authorities prepared for an intensive struggle against aggressive tax planning (Baxt, 1978). The main steps taken in Australia were in the field of operation and systemic changes in the tax administration, as detailed below:

1. Infrastructure and systemic changes: The Australian tax authorities embrace 400 full time employees directly involved in handling aggressive tax schemes, who report directly to the director of the authorities. In order to treat the problem, several unique entities were established in Australia:
   - The Steering Committee for the Fight against Aggressive Tax Planning: This staff focuses on promoters, their associates, tax schemes, and taxpayers, and additional issues.
   - The Information Gathering and Information Analysis Unit for Aggressive Tax Schemes.
2. Special task force: A task force for handling "problematic" promoters, and particularly for the early treatment of methodical tax planning that promoters market at a wide rate of distribution. The task force operates on the following planes: Management of an internal list of "problematic" promoters and taxpayers who make methodical use of aggressive tax schemes; surprise audits among "problematic" promoters, including confiscation of client lists and computers;

investigation of promoters in cooperation with external authorities; handling of sensitive cases which involved particularly aggressive schemes. The authority encourages severe treatment of "problematic" promoters and their clients. The authority distributes warning letters to clients of "problematic" promoters, listing the aggressive tax schemes that these promoters market, and the manner in which they have been handled by the authorities.

3. Cooperation with internal organization: The taxation authority cooperates with the stock exchange, the authority for business limitations, the organization against crime, and the general prosecutor's office for the issues of aggressive tax schemes. This cooperation is subordinate to legal limitations preventing transfer of information between various bodies.

2.10.2.3 The OECD

Based on the existence of a tax avoidance phenomenon, the OECD recommends a number of general solutions, as follows:

1. Increased bilateral mutual assistance treaties, including enforcement and tax collecting.
2. Improving access to bank information for tax purposes (OECD, 1997).
3. Improved exchange of information between countries, including use of automatic exchange of information and spontaneous exchange of information (Section 26 of the model treaty discussing exchange of information).
4. Handling of harmful tax practices: The OECD examines harmful tax practices in countries that are and are not members of the organization are not (OECD Committee on Fiscal Affairs, 1997). Regarding company policy, from 47 harmful tax practices that have been identified, 45 have been cancelled or changed so that they are no longer considered harmful. Management companies in Switzerland and holding companies in Luxembourg from 1929 are still marked as harmful tax practices and are under investigation by the organization. Regarding countries that are not members of the organization, 41 harmful tax practices were originally identified, and according to the last report published in 2004, five countries still refuse to cooperate with the OECD: Andorra, Liberia, Liechtenstein, the Marshall Islands and Monaco.

The criteria determined for identification of a harmful tax practice are:

1. An effective taxation rate that is low or 0%
2. An isolated tax practice, aimed to provide tax benefits for foreigners only
3. A lack of transparency of the taxation system, i.e., laws implemented in certain cases only, making different tax decisions for different taxpayers, etc.
4. No mechanisms for transfer of information between countries.

2.11 Taxation of trusts in American law

This researcher considers discussion of the taxation of trusts in American law necessary in order to understand the source of the American obligation for taxation in any possible situation of double taxation, and the manner of handling conventions in the case of the above.

A trust will be considered a foreign trust unless it upholds two cumulative tests – the test of the courts and the test of control. A trust that does not uphold these two tests will be considered a foreign trust for tax purposes from the standpoint of American law.

The test of the courts – a trust will be considered that of a US resident if the American court holds the main authority for supervision of trusts and providing obligatory instructions to trustees in essential issues, such as the manner of managing the trust, recording the books, protection against creditors, manner and timing of distribution of income, etc. It should be noted that in order to maintain the test of the courts, it is also necessary that specific authority and local authority be provided to American courts. Therefore, if a certain country outside of the US allows its courts to apply American law, the conditions for the test of the courts will not be fulfilled if this court that has the authority is a court that is not American.

The Test of Control – A trust will be considered a trust of a US resident only if the authority to control essential decision-making for the trust (such as decisions regarding timing and size of distribution of income to beneficiaries, investments, attribution of income to capital or current income, etc.), is given to at least one resident of the US. Provision of veto power over essential decision-making does not fulfill the Test of Control. For example, if A and B are residents of the US and beneficiaries of the trust, and C is a foreign resident who is a beneficiary of the trust who has sole authority to make decisions regarding the investments of the trust, the test of control is not upheld and the trust will be considered a foreign trust, although A and B have veto power over C's decisions.

2.11.1 Types of foreign trust income subordinate to American taxation

In principle, a foreign trust is taxable in the US, as is that of any foreign resident. In general, a foreign trust will not be taxed for income from sources of income that are not American, but American beneficiaries who receive income from a foreign source may be taxed, as follows:

- Taxation of distribution of current income to beneficiaries: Beneficiaries who are residents of the US are taxed on the overall sums distributed to them from a foreign trust until the taxation ceiling, whether the source of the sums distributed to them is from American income sources or not. An American beneficiary taxed for sums distributed from sources of income of a foreign resident is eligible for a tax refund for taxes paid by the foreign trust for this income. As regards distribution to beneficiaries who are not residents of the US – if the income that is distributed stems from non-American income sources, both the trustee and the beneficiary are not subordinate to American tax. If the income stems from American sources, a beneficiary who is not a US resident will be taxed for this income until this part of the tax ceiling.
- Taxation of distribution of accumulated income to beneficiaries: If the income of the foreign trust is distributed to beneficiaries from the accumulated income of past years, the American Code determines a mechanism for attribution of income. The goal of this mechanism is to tax the beneficiaries similarly to the tax that they would be obligated to pay if the income had been distributed to them in an ongoing manner, in the year it was accumulated, obligating the beneficiaries to pay interest for the period that has passed since the time of accumulation of the income to the actual payment date. Attribution of income according to this

mechanism aims to prevent accumulation of income by a foreign trust for the purposes of tax obligation at a lower rate than the marginal taxation rates of the beneficiaries, and late distribution of income with no tax obligation. This mechanism does not apply to local trusts.

2.11.2 Additional issues

- Transfer of losses to beneficiaries: American law does not allow the transfer of losses incurred in a trust to the beneficiaries until the end of the life cycle of the trust. In this case, the unexploited losses of the trust will be transferred to the beneficiaries who are eligible for the trust assets, according to the trust letter.
- The trustor of a foreign trust who has become a US resident: A foreign individual who is not a resident, who establishes residence in the US within five years of the day that he transferred his assets to a trust, will be considered to be the owner of the assets from the day of setting up his residence. The net undistributed income for the period prior to becoming a resident will be considered at the time of determining the part of the income to be attributed to him.
- An American trust that becomes a foreign trust: An individual who is a citizen or resident of the US, who transferred assets to a trust that was not, at the time of the transfer, a foreign trust, and which later became a foreign trust (as long as the trustor is still alive) is considered to have transferred the assets on the day that it became foreign.
- Trusts acquiring American beneficiaries: At the time that an American beneficiary joins, the income of the trust (in addition to regular incomes), will be attributed to the one transferring the assets, to the limit of the undistributed net income of the trust to date, as long as in previous years there had not been one single American beneficiary.
- Trusts considered to have American beneficiaries: It is accepted that a trust has an American beneficiary unless:
  - According to the trust letter, no income or capital of the trust was attributed to or earmarked to be attributed to an American beneficiary;
  - At the time of the ending of the trust, no part of the income or capital was attributed or could be attributed to an American beneficiary.

    Regarding such holdings, such sums will be seen as if they had accumulated or been paid to the benefit of an American beneficiary if the sum accumulated or was paid to a Controlled Foreign Company (CFC), a foreign partnership (with at least one American partner) or a foreign trust (with at least one American beneficiary).

    Furthermore, for the purposes of the abovementioned holding a beneficiary will not be considered American as regards the transfer of assets if he became an American more than five years from the day of transfer of the assets to the foreign trust.
- Tax events at the time of creating the trust: Tax events at the time of creating the trust include various aspects related to gift tax that do not exist in Israel, therefore will not be discussed.

2.12 British law

2.12.1 Trusts in the laws of English-speaking countries

Trusts have existed in Anglo-American culture for hundreds of years. The institution was created in order to cope with economic, familial and social problems.

Over the past century, the institution has changed and today often serves as a legal structure for coping with various aspects of private and international taxation. Additionally, the establishment of a trust is considered, abroad, to be a legal solution to estate and gift taxes.

It should be noted that a trust is not only created for taxation planning purposes. Most trusts are established in order to provide a response to issues of inheritance of assets, testaments and estates, and often also for the purposes of industrial transactions (Jenks, 1920).

The trust defines a legal system of relations between the creator of the trust (trustor), the beneficiary and the trustee, within which the trustee holds and manages assets that the trustor transferred to his ownership, for the benefit of the beneficiary or any other purpose. A trust is therefore a legal relationship. It is not a legal entity or a contract, an issue that will be discussed further.

Section 2 of the Hague Convention interprets the term "trust" (The Hague, 1985):

> *"For the purposes of this Convention, the term "trust" refers to the legal relationship created – inter vivos or on death – by a person, the trustor, when assets have been placed under the control of a trustee for the benefit of a beneficiary or for a specified purpose".*

The OECD has recently defined a trust as follows:

> *"In legal terms, a trust exists where a person (known as a trustee) holds or has vested in him or is deemed to hold or have vested in him property, of which he is not the owner in his own right, for:*
>
> *a. The benefit of any person (known as beneficiary) whether or not yet ascertained or in existence; or*
>
> *b. Any purpose; or*
>
> c. *For the benefit of (a) and (b) above".*

A trust is created and organized according to accepted law and the rules of integrity. The explanation of the application of the laws of integrity to the trust is historical. The trust as a legal tool was developed in England during the Middle Ages, by the courts of the Church. The English knights who left for the Crusades would transfer their assets to the ownership of the local bishop, so that they could handle and oversee their property effectively while gone. Over the years, the courts replaced the church with the courts of integrity. This development led to the application of the Laws of Integrity over trusts, and the development of legislation in England, at the end of the 19th century, making trusts an inseparable part of the English legal system (Pollock and Maitland, 1923).

Trusts are not recognized by Continental (civil) law, and they may only be established in countries that use the Anglo-American method. Therefore, use of the legal tool of the trust may be of interest, even in English-speaking countries outside England

countries, as a means for maintaining international legal and business relations. However, it should be noted that the use of trusts in these countries often causes a problem because of the lack of recognition of their existence, and as regards the law applying to them.

In the above countries, a number of approaches have developed regarding the recognition of trusts, but not all have managed to prove an appropriate response to all aspects.

Businessmen and holders of assets will be interested in a "private trust" or a "family trust", which differ from a "public trust". There are a number of reasons for creating a private trust, as follows:

- To allow more than one generation to enjoy the use of the assets
- To satisfy the needs of incompetents
- To protect family property against lavish spenders
- To allow concentration and coordination of assets throughout the world
- To prevent instructions of forced inheritance
- As part of a tax planning strategy
- To provide stipends to retired employees and their dependents
- To aid investments through investing in a trust fund (of a bank, etc.)
- As part of the financial structure of a corporation
- To recruit funds for charity purposes

2.12.2 Taxation of local trusts under British law

General law in Britain includes special legislation for "settlements" and trusts, accompanying laws and many decisions. For the purposes of taxation law, it is customary to differentiate between two types of trusts (Keeton and Sheridan, 2000).

- Revocable trusts: Similarly to Israeli law, in English taxation law a number of anti-tax planning laws have been determined, according to which trusts must be ignored, while attributing income and assets to the trustor. Accordingly, it has been determined that when the trustor maintains an interest in the assets of the trust, i.e., the assets or income of the trust may be given to his control, the income of the trust is attributed to the trustor. Similarly, subordinate to a number of conditions, it has been determined that income of a trust paid to a minor unmarried child of the trustor will be considered the income of the trust trustor.
- Irrevocable trusts: British taxation law relates to two main types of irrevocable trusts, which are then subdivided into categories:
  1. Non-accumulation trusts
  2. Accumulation trusts

  1. Non-accumulation trusts: There are two main types of non-accumulation trusts:
     - Simple trust (Bare Trust): A trust in which the beneficiary has the right to the profits and assets of the trust and is allowed to realize this right at any given moment. In this trust, as mentioned, although the assets of the trust are registered to the trustee, the trustee does not have any influence over distribution of the income and assets of the trust. For tax calculation purposes, it has been determined that the existence

of the trust will be disregarded and the income will be taxable in the same manner as if the beneficiary was directly holding the assets of the trust. The beneficiary carries the taxation obligation.

Interest in possession trust: In this trust, the beneficiary is eligible to the income of the trust, but he has no right to the assets. On a given future date, generally dependent upon a certain event, the capital will be distributed to a different beneficiary, called the "capital beneficiary". The trustee is obligated to handle the assets of the trust and distribute them at the time of the future event, and he has no right to accumulate the income of the trust. Taxation of this type of trust will take place according to the beneficiary, by collecting taxes from the trustee.

2. Accumulation trusts: There are two main types of accumulation trusts.

Accumulation and maintenance trusts: A trust in which the beneficiary is eligible to the assets of the trust, and sometimes the income, if he has achieved a certain age. The maximum eligible age varies in the various countries in Britain, but the oldest such age is 25 years old. Trustees have the authority to use the income of the trust to support the beneficiary before he reaches the predetermined age. During the period of accumulation this type of trust is taxed similarly to a discretionary trust (see below). Taxation is according to the special taxation rate determined for trusts, and not according to the beneficiary. The beneficiary will be taxed only for the part of the income distributed to him before the end of the maintenance period. Distribution of the trust capital at the end of the period, including trust income distributed as capital is not a taxable event. In England and Wales, the beneficiary is eligible for the trust assets and income from age 18, unless otherwise indicated in the trust conditions. In Scotland, this type of trust will always end when the beneficiary reaches his majority.

Example: A deposits a sum of money in a trust for the benefit of his grandchild, B. According to the conditions of the trust, B is eligible to receive the sum of money at age 25. The trust may pay from its income to ensure the welfare of B, while accumulating the balance of its income. At age 25, all of the capital of the trust will be transferred to B.

During the period when the trustee may accumulate the income of the trust, the trustee and the beneficiary are taxed in the manner of a discretionary trust. At the end of the accumulation, the taxation obligation depends on the circumstances and the re-classification of the trust. For example, if the trust becomes an "interest in possession" trust, it will be taxed according to these rules. Similarly, if the trust becomes a discretionary trust, it will be taxed according to the laws applying to this type of trust.

Discretionary trusts: In this type of trust, particularly broad discretion is given to the trustees. This, in general, is delineated by a number of limitations regarding capital or income. However, the trust documents allow the trustees much authority. For example, there are cases in

which the trustee is given the right to decide, from a list of beneficiaries, to whom to pay the income, how much to pay, if to limit the beneficiaries by any conditions, etc. Additionally, the trustees are given the authority to accumulate or not accumulate the income of the trust, where the accumulated income becomes part of the capital. Often, an end date is determined for the trust, although this is not absolutely necessary.

A discretionary trust is taxed at a regular rate of 34% (or a special rate determined in taxation tables) no matter who the beneficiaries are. In both of these types of trusts, the trustee is taxable for the profits of the trust during the accumulation stage, according to special trust rates, i.e. 34% on the current income and 25% on dividends. The tax paid by the trust is a down-payment for the tax that the beneficiary will pay at the time of receipt of the monies. The distribution date is the date at which the beneficiary receives the income or the date at which he is eligible for the income. It should be noted that for this purpose the individual income tax rate in Britain stands at 10-40%, with two main tax brackets of 22% and 40%.

Mixed Trusts: A mixed trust is a trust that contains more than one type of trust, such as, a discretionary trust and an interest in possession trust, or an interest in possession trust and an accumulation and maintenance trust. For example, A and B are brother and sister who are beneficiaries of an accumulation and maintenance trust, that accumulates its profits until the children reach maturity. When A reaches age 18, B will be 14. If part of the trust belonging to A becomes an interest in possession trust, while the part of his sister remains as it was for 4 more years, the trust will be a mixed trust. This type of trust will be taxed according to its parts. Each type of trust will be taxed according to the laws applying to it.

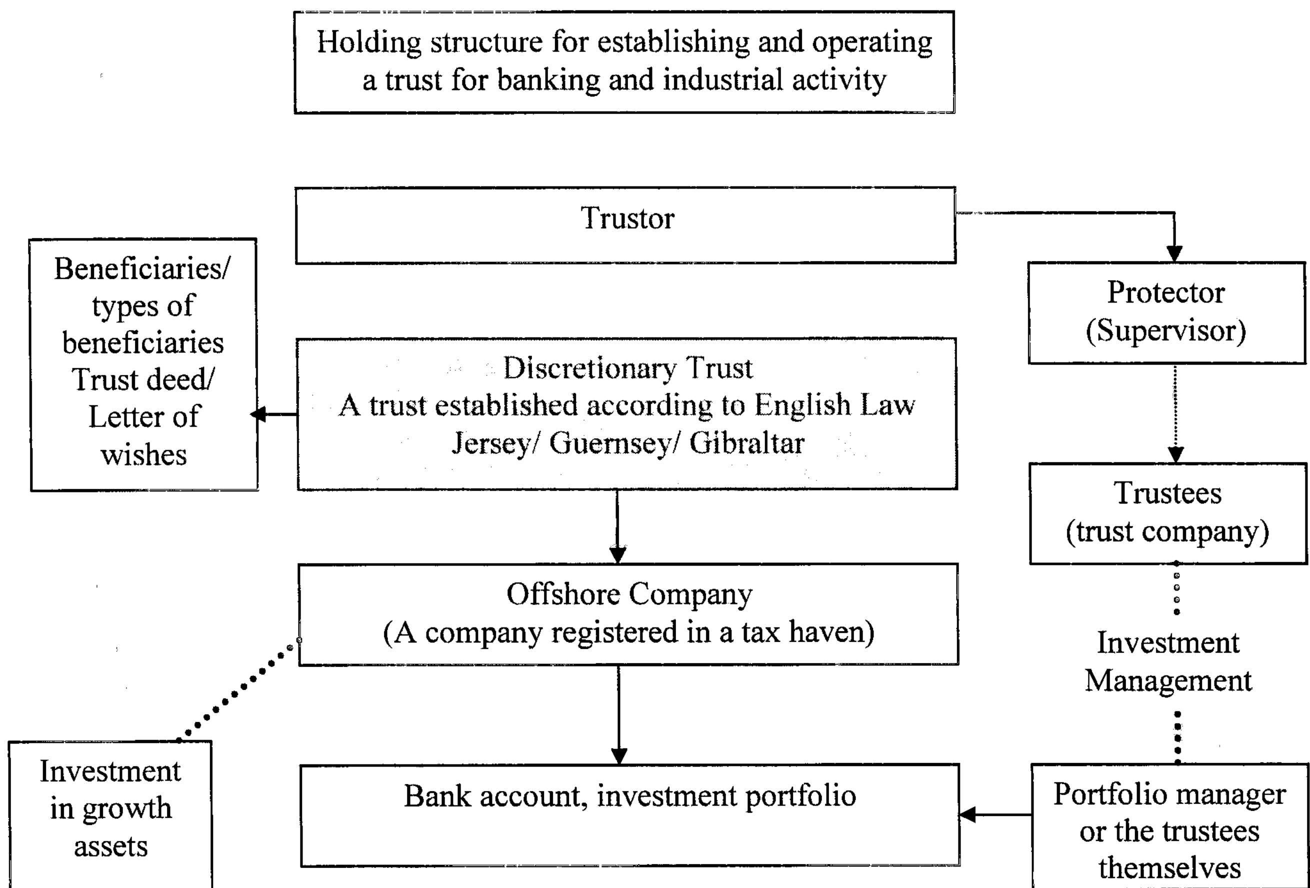


Chart no. 1: Discretionary Trust/ Common Law Trust

2.12.2.1 Taxation of beneficiaries

Taxation of beneficiaries occurs according to the type of trust, as mentioned above. However, a unique taxation issue in British law should be noted. The law has determined that the nature of the payment that the beneficiary receives from the trust will be determined according to the identity of the beneficiary and not according to the source of the income. For example, if a regular stipend was paid by the trustee to the beneficiary, this payment may be considered to be an annuity and be taxable even if it is paid from the trust capital.

2.12.2.2 Capital gains in a trust

The trustee must pay capital gains tax at the rate applying to a trust (34%) or any capital gains above the exempt rate stemming from any type of trust (excepting a simple trust in which the tax applies to the beneficiary). The beneficiary is not taxed for capital gains that were created in the trust and will not receive a tax rebate for the trustee's payment. The exempt sum is usually equal to half the sum that is exempt for individuals. Trusts for the benefit of the mentally disabled are eligible to the entire sum exempt for individuals. When one trustor sets up more than one trust, the annual exemption is divided among them.

2.12.2.3 Creating a trust, transferring trust assets to beneficiaries, and selling trust rights

According to British taxation law, transfer of assets to a trust is considered to be a sale that is taxable with capital gains tax according to the market value of the assets. Similarly, when the beneficiary becomes eligible to the trust assets these assets are considered to have been sold at the market price, and repurchased at the market price.

On the other hand, when the beneficiary sells his rights to the trust to a third party, the sale is exempt from capital gains tax, apart from the case in which the right to the trust is acquired for money and the beneficiary is not the person for whom the rights are acquired, or alternatively when the sale is of the rights to a foreign trust.

2.12.3 International taxation of British trusts

In British taxation law, there are three levels of residency. Each level is subordinate to different rules regarding taxation on the international level. The broadest level of residency is called 'domicile'. Accordingly, for general international taxation purposes in Britain there is a special status called 'British Resident of Foreign Domicile'. This resident is given a special benefit, in that he is taxed only for income from British sources, and income from foreign sources remitted to Britain.

- Rules of residency for trusts: The definition of residence of a trust for tax purposes for profit income differs from the definition for the purposes of capital gains tax. Accordingly it is possible for a trust beneficiary to be considered a resident of Britain for income from profit taxes although it would not be considered a resident of Britain for capital gains tax purposes, and *vice versa*.
- Residency of the trust for income profit purposes: For taxation of the trust profit income, the trust will be considered a resident of Britain unless:
  - All of the beneficiaries are not British residents
  - Some of the trustees are not British residents and the trustor, at the time of its establishment, was not a resident or was not domiciled in Britain
- Residency of the trust for capital gains taxation: For taxation of capital gains a trust beneficiary will be considered a British resident unless the management of the trust takes place outside of Britain and most of the trustees are not residents or hold domicile in Britain (the death of a trustee can change the balance of residency if not "corrected" within a specific time frame). An exception to this is the fact that in the case that the trustor does not reside or hold domicile in Britain and all of the income of the trust stems from property outside of Britain, a British resident trustee will be considered a foreign resident for the purposes of the test. The goal of this instruction was to prevent a situation in which tax considerations prevent the choice of a British resident trustee.
- Taxation of a foreign trust: Taxation of a foreign trust not stemming from British sources is not taxable when accumulated, and its tax obligation is delayed to the day of distribution to the beneficiary who is a resident of Britain or the time at which this beneficiary is eligible to receive the income. Accordingly, on the day of the distribution, the beneficiary is taxable for the income of the trust while maintaining the nature of the income as it was within the hands of the trust. When the beneficiary of a foreign trust is a British resident of foreign domicile, he will be taxed for the trust income, only if these incomes are remitted to Britain.
- Immigration of a trust: When a trust changes its residency it is considered to be a person who sold all of his assets in a taxable sale. This obligation of tax is not on

the assets for which the sale will be obligated to pay tax in Britain in the future or assets whose sale is exempt from tax according to double taxation conventions.

2.13 South African trust taxation

2.13.1 Interpretation according to general law

In South Africa, as in Britain, the courts interpret the laws of taxing trusts according to trust law in general law. In the case of a trust based on the South African Bankruptcy Law, it is questioned if this a trust in the context of trusts in the law of general trusts? The court ruled that the law of taxation in a certain context applies only to trusts according to general law, and therefore, the question is important. It was ruled that a trust according to the above law is not a trust according to the general law, as a trust is generally created according to an expression of will. Therefore, the section does not apply to trusts created in bankruptcy. This is an example of adopting the general law of trusts for interpreting a concept that appears in the taxation laws of South Africa (De Koker, 1982).

2.13.2 Two possible obligations

The South African courts determined that according to the general law, the one obligated to pay taxes (in the case of a stockholder who owes taxes on a dividend) can be both the trustee and the beneficiary. This is because of the interpretation of the definition of stockholder, which includes anyone who had "the right to benefits from the stocks", in addition to the registered owner. The case of two possible obligatory taxpayers is not a situation which is unique to South African law. This situation involves splitting the rights of a given asset, as in the case of property tax in Israel.

2.13.2.1 The principle of general obligation

In South Africa, it was determined that the trustee is a "representative" for taxation purposes. Definition of the trustee in Section 1 of the Taxation Law of 1962, includes, in addition to the trustee, a series of individuals, such as the executor, the estate executor, the trustee of a bankruptcy, and any other individual who manages the income of the assets of another.

Despite the rule that the trustee is the "representative", taxation obligation does not always apply to him (De Koker, 1982). In general, when he is taxable, he will be taxable as a representative, but for example, when a trust does not have a beneficiary in the present, and Section 7(5) of the Taxation Law does not apply, a trustee as a trustee does not exist if there is no one that he may represent.

2.13.2.2 Taxation of a "beneficiary eligible for income"

If the trustee must transfer income or part of the income to a certain beneficiary, the beneficiary is taxable for the income, whether he received the income or whether it was removed by the trustee for the benefit of the beneficiary (Pinson, 1980). The test of when the beneficiary is eligible for income as a "Vested Right" involves the question of his ability to demand the aforesaid income.

2.13.2.3 Turning accumulated income into capital

In South Africa there is a ruling according to which accumulating income does not make it into capital in the hands of the trustee after tax has been paid on it, and it is income when it is transferred to the beneficiary. The problem of double taxation is overcome in this ruling according to the thesis that this is not the income of the beneficiary but the income of the one creating it (Section 7[5]). Therefore, its transfer to the beneficiary is like a "gift", which is not income, on the part of the creator of the trust.

2.14 Taxation of trusts in Australia

In Australia, the issue of trusts is handled in the Income Tax Assessment Act of 1936. Sections 102A-95 are a special codex on this issue. This issue is also handled in the general obligation section, 26B, as explained below. It is important to note that Sections 102A-95 relate to *inter vivos* trusts and trusts through a testament, although they are both called "Trust Estates" (Mannix and Mannix, 1984).

In general, the beneficiary must pay tax on income he receives on a regular basis, or on income to which he is eligible that is held by the trustee. The trustee pays tax on the income for which the beneficiary is not currently eligible. The trustee also pays tax on income that accumulates for the benefit of the beneficiary, income which is irrevocable (Section 95A). We therefore see that in Australia too, like in England and the US, the obligation of the beneficiary is on regular income and income that belongs to him, remaining in the hands of the trustee. However, differentiation between "present eligibility" and "irrevocable eligibility" is resolved in Australia in a respectable manner, compared to other countries, like Britain, in which there are difficulties involved, to this day.

2.14.1 Interpretation of basic concepts according to general trust law

The basis of the interpretation of the laws of taxation of trusts in Australia is the general trust law. This is also the situation in South Africa and England regarding the interpretation of basic concepts in trust taxation. However, it should be noted that according to the arrangements in the law there is sometimes a certain deviation for the purposes of taxation law, by the essence of trusteeships according to general law (Baxt, 1978).

2.14.2 The definition of trustee

In Australia, as in South Africa, the trustee is defined as including an executor, estate executor, guardian, receivers, and any other individual who has control or administers an income or any other property, for which fiduciary responsibility applies. This definition is very broad and includes much beyond the trustee of a delineated trust, to which the present dissertation relates (Baxt, 1978).

2.14.2.1 The seat of the trusteeship

The seat of the trusteeship is the basis for determining tax on trusts in Australia. Two alternative tests have been determined for determining the existence of an Australian seat for a trust:
1. The residence of the trustee
2. The central site of control and management

The first test of the seat of the trustee is for the consideration of taxation obligation. However, if the beneficiary resides abroad there are cases in which the income of the trust is exempt. The second test is identical to the test for the seat of a corporation.

According to Mannix and Mannix (1984) the obligation of taxation on the income of trusts is based "in principle" on the beneficiary, who is the final individual eligible for the income. This principle applies in two situations:
1. When the beneficiary receives income from the trust or use is made of this income for the benefit of the beneficiary;
2. When he is "eligible in the present" for income of the trust, even if the money has not actually reached him.

"Eligible in the present", as the basis for obligation, is typical of South Africa and also somewhat, of England. However, the words have been interpreted differently in different countries, and in contradictory manners within the countries themselves, as shown in the laws of Britain.

When there is no one "eligible in the present" for the income of the trust, the trustee will be obligated to pay the taxes.

Australia thus has laws that determine the manner of taxing trust income. The main differentiation is between "eligibility in the present", "vested rights" (Section 95A), and trusts without any beneficiary who is eligible for the income (Sections 99, 99A). The Australian arrangement is sophisticated, and follows the small differences between trusts, as they are recognized in general law. The differentiation between "present eligibility" and vested right, leads to many problems in western taxation methods. In Australia, the problem has been resolved in an elegant manner. "Present eligibility" means income which the taxpayer enjoys. "Vested right" means income that the trustee is taxed on – as if he was the beneficiary. Income for which no-one is eligible, is the obligation of the trustee regarding taxation, according to Sections 99 and 99A of the Australian codex.

2.15 Taxation of trusts according to Canadian law

2.15.1 Canadian domestic taxation of trusts

Canada taxes trusts as individuals, but with certain modifications. An *inter-vivos* trust is taxed at the top tax bracket, and a testamentary trust is taxed at graduated personal tax brackets. A trust is subject to tax on its taxable income, and if income is imputed from the trust to someone else or distributed to a beneficiary, then a deduction will be given. In general terms, most types of income earned by a trust retain their nature when

taxed in the hands of a beneficiary. For example, capital gains which are only 50% taxable in Canada will, if earned by a trust and distributed to a beneficiary, be considered to be capital gains of that beneficiary. As such, they will only be 50% taxable in the hands of the beneficiary. In addition, certain other tax attributes may be allocated to a beneficiary. For example, if the trust pays tax on foreign income, then the foreign tax that is paid may be allocated to a beneficiary and the beneficiary may claim a foreign tax credit.

Certain limitations are placed on the ability of a trust to allocate deductions to beneficiaries, and, in general, losses may not be allocated from a trust to a beneficiary. They may, however, be carried back or forwards (within limits) to be applied against income of the trust in previous or future years.

Certain anti-avoidance rules prevent persons diverting income from themselves to other taxpayers through the use of trusts. These rules, called the income attribution rules, reinstate the income in the hands of the person who attempted to transfer it, and are deleted from the income of the trust. There are a series of these rules which can apply in various circumstances, but for the most part they apply where income is diverted to a spouse or a person under the age of 18.

The transfer of property to a trust is generally considered a disposition at fair market value. Therefore, if the property has appreciated in value, capital gains will result. However, when property is distributed to a beneficiary it retains its historic basis, and no gain or loss is incurred even if the property has appreciated in value.

There is an exception where property is transferred to spousal trust (which is a trust set up for the exclusive benefit of a spouse during that spouse's lifetime). In such circumstances, property may be transferred tax-free to the trust, but is taxable on the spouse's death.

In order to prevent an undue deferral of capital gains by using a trust, a special rule was introduced when Canada introduced its capital gains tax system in 1972. Under this rule, a trust is deemed to have sold all of its assets and reacquired them again at fair market value every 21 years. This rule proved to be very unpopular, and its implementation was postponed from 1993 for a number of years, pending further study, but was ultimately adopted.

Canada taxes individuals based on residency, and considers a trust to be resident where the majority of the trustees reside. Therefore, if the majority of trustees of the trust reside in Canada, then that trust will be taxable in Canada, based on global income.

Canada has a system of withholding taxes which apply when the income of a trust is distributed to a non-resident beneficiary. The rate of withholding tax on distributions to non-residents is typically 15% where a tax treaty applies, and 25% otherwise. As mentioned earlier, the trust will obtain a tax deduction for such distributions. However, in certain cases, an additional tax (at 36%) can be levied when certain types of Canadian source income are distributed.

In Canada, trusts are used extensively in estate planning, and are very often built into the design of wills (testamentary trust provisions) because of their usefulness, tax advantages, and flexibility.

Within a domestic context, it is probably fair to say that the taxation of trusts functions smoothly and reasonably. While technical issues do arise, they are generally of minor consequence. The current system has remained essentially intact for the last 30 years.

Trusts are required to file income tax returns similar to individual income tax returns. If income is allocated to a beneficiary, then the information is reported on a reporting slip which is distributed to the beneficiary, and is to be attached to the beneficiary's income tax return. This is a multi-part form, and the tax authorities receive a copy which is imputed into a data bank for cross referencing and matching (O'Brien, 2001).

2.15.2 Taxation of non-resident trusts

Canada taxes non-resident trusts where they have a link to Canada. Under current rules, the test of whether or not a non-resident trust would be taxed was a two part test, consisting of the following:

1. Whether the trust has Canadian resident beneficiaries;
2. Whether a Canadian resident has transferred property to the trust directly or indirectly.

In addition, there must be a link between the Canadian resident and a beneficiary of the trust. They must be related to one another (a defined term).

This rule was found to be unsatisfactory, and in February 1999, it was announced that the rules concerning non-resident trusts would be revised substantially. Under the new rules, if a Canadian resident contributes property to a non-resident trust, then that trust will be deemed to be a resident of Canada regardless of who the beneficiaries of the trust are. These rules have, however, been difficult to draft and have created considerable uncertainty and complexity (O'Brien, 2001).

Canada gives a tax exemption to new immigrants. This exemption is generally only available through the use of an offshore trust, where the immigrant transfers property to the trust, and the income is accumulated in the trust. The income may then be earned free of Canadian tax and distributed as capital to the immigrant and his/her family as Canadian residents, also free of tax. Consequently, if a non-resident of Canada establishes a trust for the benefit of Canadian residents, then the trust will be exempt of Canadian tax perpetually.

If a Canadian establishes a non-resident trust, and there are non-resident beneficiaries of the trust, provided all the income is paid out to these non-resident beneficiaries, then the trust will not be subject to Canadian tax. Even through the trust will be deemed to be a Canadian resident trust, there will be no income left in the trust upon which to levy tax. Furthermore, there is an exemption from withholding tax in these circumstances.

2.16 Taxation of trusts in New Zealand

Income tax was implemented in New Zealand in 1891. Since then the law has been amended a number of times, most recently in 1994. As of today, New Zealand law is composed of the Income Tax Act 1994, a system of regulations determined by the Commissioner, regulations for the prevention of double taxation, treatment of issues related to withholding tax, and rulings. Most issues related to taxation of trusts are naturally found in the Income Tax Act of 1994. The 1994 law is divided into fifteen sections according to topic, marked chapters A to O (for example, Income Chapter C, Tax Payments Chapter M, Special Entities, Chapter H, Anti Planning Laws Chapter G, Losses Chapter I, etc.). Each chapter is divided into sub-chapters, also according to letter. The main points of the general New Zealand law are as follows:

- Personal taxation of New Zealand residents on a global basis
- All income from a New Zealand source is taxable
- Taxation is progressive with two tax brackets
  - $0-38,000 (New Zealand) – 21.5%; Actual taxation from the first dollar
  - Over $38,000 – 33%

Although, unlike Israel New Zealand does not have personal credit points there are a number of tax deductions for lower income brackets who fulfill a number of conditions, particularly related to familial status.

- Credit is given for outside taxes that have been paid
- A set corporation tax at 33%
- Dividends are taxable at the rate of corporation tax but the stockholder may request a full credit for corporation taxes the New Zealand Company paid. Therefore there are two taxation events but the payment of tax at a rate of 33% takes place only once.
- There is a recognized devaluation of material assets at a lower rate than non-material assets.
- A legal Controlled Foreign Company (CFC) system.
- A special system of laws for businesses with a long life cycle that are not suited to taxation on an annual basis, such as: life insurance, foresting, oil drilling and agriculture.
- Aside from a number of exceptions, the rules of taxation apply to any source of income equally.
- There is no capital gains tax.

2.16.1 The principles of the trust taxation method in New Zealand

A trust is not a legal entity and is not a taxable body (Prebble, 1988). Taxpayers could be the beneficiary or the trustee, and no one else. The principles of the method are as follows:

- The individual who is obligated to pay the tax is the holder of the income itself, and therefore the income is divided into two types: The trustee income and the beneficiary income. Each of them must pay tax for his income. Because of the approach that the trustee is acting on behalf of the trust trustor, in certain cases the obligation to pay the tax may be placed on the trustor.
- The income of the trust is taxable on an accumulative basis. If no distribution has been made, it is considered to belong to the trustor. (For clarity's sake, this is not legal ownership but a perception that income has owners and since the beneficiary does not yet own it, it is the trustor and the trustee who acts on his behalf, i.e. the principle is that there is enough connection to the trustor if the income has not yet

been distributed.) Therefore he will be taxed by the trustee. If the income has been distributed to the beneficiary, he must pay the tax.

- The trustee may distribute income to the beneficiaries up to six months from the end of the tax year, and the income will still be considered the income of the beneficiaries during the tax year that it accumulated. This instruction is mainly for practical purposes in light of the fact that only after the end of the tax year does the trustee have full information on his income over the course of the year.
- Profits of the trust: The profits include profits from regular income and transfer of assets to the trust under certain circumstances, by the trustor and by the trustee of a different trust. The trust income will be taxed only once, by the trustees or the beneficiaries. These are not two tax events, but rather placement of obligation for payment of the tax on the owners of the income (unlike in a company in which there are two tax events, the company profits and dividends). The profits are distributed among the beneficiaries – "beneficiary profit" – and the trustees - "trustee profits", and tax must be paid by the beneficiaries or the trustees. Distribution is as follows:
  - Beneficiary profits are defined as follows: Any gross income derived during that income year by a trustee of the trust to the extent to which it: 1) during that income year vests absolutely in interest in the beneficiary; or 2) is paid or applied by the trustee to or for the benefit of the beneficiary during, or within 6 months after the end of that income year. That is to say, beneficiary income is the income actually distributed or paid to his benefit (for example: the trustee paid university tuition for him), within six months from the end of the income year, or income that fulfills "reserved rights". This is a permanent right in which the beneficiary has not only interest in the income but also possession.
  - Trustee Profit – reserved for the beneficiary's profits: Calculation of the tax depends on the type of the trust and the answer to the question: Is the trustor a resident of New Zealand and is the trustee a resident of New Zealand?
- Types of trusts – there are three types of trusts in New Zealand:
  - Qualifying trust – the status of a trust as qualifying will be tested each tax year in which distribution is made to beneficiaries. The trust is qualifying if, from the day of its establishment until the day of distribution to the trust, all of the tax obligations have been met. A trust cannot be qualifying in any case in which it includes certain types of income that are not taxable in New Zealand by the trustees.
  - Foreign trust – a trust for which not one of the trustors was a resident of New Zealand from the day the trust was established and thereafter.
  - Non-qualifying trust – including mainly the cases in which not one trustee is obligated to pay tax on the trustee income, in light of the fact that all are foreign residents, or in the case that the trustees have not paid their obligatory taxes.

The type of trust will determine if the profits are taxable.

- Taxation of beneficiary income and other income
  - Taxation of income of beneficiaries who are residents of New Zealand: Beneficiaries who are residents of New Zealand are obligated to pay tax on all of their income from any source whatsoever. Income of beneficiaries

from any type of trust is taxable according to regular taxation rates. Beneficiaries under the age of 16 are taxable according to special laws applying to this issue.

- The trustees must pay the tax of the beneficiaries before distribution of income, and if necessary the beneficiaries may request a tax rebate. An agreement may be reached between the trustees and the beneficiaries that the income be transferred directly to the beneficiaries, and in this case the trustees do not have to pay the tax before the beneficiaries receive the money. If the beneficiaries did not pay the tax, the trustees will be required to pay it. The beneficiaries must report any sum received from the trust. The beneficiaries will be charged regular taxation rates, i.e., up to $38,000 at 21.5%, and above this sum, 33%.
- Taxation of beneficiaries not residents of New Zealand: Such beneficiaries are obligated to pay tax on beneficiary income derived in New Zealand only. The income maintains its nature and therefore a sum of tax to be paid will be derived. The trust must pay withholding tax before distribution. If the beneficiary is temporarily not a resident and then becomes a resident again within five years, he must pay the tax on all of the beneficiary income or distribution that took place in every foreign trust or non-qualifying trust. The obligation to pay tax is in the year that he again became a resident.
- Taxation of distributions to beneficiaries that is not "Beneficiary Income": Just like income may be distributed to beneficiaries, money or assets that are not income may be distributed. The accepted modes are:
  * Distribution of trustee income that accumulated from previous years.
  * Distribution of capital gains
  * Transfer of a property or providing a service to a beneficiary below market value.
  * Acquisition of a property or receipt of a service from the beneficiary below market value.
  * Distribution of the trust capital.

- Taxation of the beneficiary who receives this type of distribution, with the taxation rates depend on the type of trust (qualifying, foreign or non-qualifying) thus necessitate defining the trusts.
  - Distribution from a qualifying trust – in the case of distribution from a qualifying trust, distribution is exempt from taxation. This is the great advantage of a qualifying trust.
  - Distribution from a foreign trust – in this case any distribution is taxable by the beneficiary at his regular taxation rate (21.5% up to $38,000 and 33% beyond), aside from a distribution from capital or capital gains from a transaction with a non-adverse party. In a foreign trust that chooses to become a qualifying trust, the trustor or beneficiary must pay tax on the trustee income from all sources worldwide. Trustee income will be taxed in New Zealand as if it was a qualifying trust (and sometimes even in cases that the foreign trust was not obligated to be taxed). This will allow the trust to distribute tax exempt distributions to the beneficiaries.
  - Distribution from a non-qualifying trust – any distribution from a non-qualifying trust is taxable unless the distribution is from the trust capital. Distributions will be included in the tax reports of the New Zealand resident and will be taxed at a flat rate of 45 cents per dollar. The high tax rate aims

to detract from the advantage of delaying tax from accumulation until actual distribution. Distribution of beneficiary income will be taxed at the regular taxation rate for the beneficiary. If the beneficiary wants to offset a loss from a given income that he received from the trust he must multiply it by the rate of beneficiary tax (33/100) and divide it by the taxation rate of the income from a non-qualifying trust (45/100).

- Taxation of trustee income: In New Zealand, trusts do not have a legal status and tax assessments are given to the trustees or the beneficiaries, as appropriate. Trustee income (income not distributed to beneficiaries and not paid to them within six months of the end of the tax year, and not budgeted to them absolutely), in all three types of trust are taxed at a rate of 33 cents per dollar. The rule is that the trustees are obligated to pay tax for any income derived in New Zealand no matter where the place of residence. In addition, tax is paid for any income from any source outside of New Zealand, if one of the trustors was a resident of New Zealand at any time during the tax year; and the trust is *inter vivos*, and the trustor dies while a resident of New Zealand, and the trustee was a resident of New Zealand at any given time during the year.
- Trustor guarantee: One of the principles of New Zealand Law is the guarantee of the trustor for any tax obligations of the trustees, as his agent, every year, if at a given time during the tax year, he was a resident of New Zealand. If there are a number of trustors, they are guarantors of the debts together and alone. The trustor will not be a guarantor for the debts if one of the following conditions exists:
  * One trustee is a resident of New Zealand throughout the entire tax year, in which case direct penalties will be applied to the trustee;
  * The trustor, who is an individual (and not a company) was not a resident of New Zealand at the time that the property was transferred to the trust. Unless he chose willingly to pay the debt of the trustees;
  * The trustor can prove to the tax authorities that the rate of taxation applied to him because of his guarantee is excessive, in relation to the assets that he transferred to the trust compared to the assets transferred by the balance of the trustors.

• Determination of the trustor is therefore critically important when taxing trusts in New Zealand and when applying the obligation for taxation to the trustee, and in certain cases to the trustor himself. For the purposes of tax laws, the trustor is not only a person who was included as a trustor in the trust letter but also any individual who:
  - Transferred property to the trust under its market value
  - Allowed the trust to use a property or capital under the market value
  - Provided the trust with a service under the market value
  - Acquired a property or a service from the trust over the market value

2.17 Trust-like entities

2.17.1 Trusts according to the continental method (Switzerland) – Fiducie

The institution most similar to the trust in Switzerland is the Fiducie, which is also called the "Acte Fiduciaire". This institution was first recognized in the Swiss federal courts in 1907 and has developed since then through rulings. The Fiducie may be

defined as a contract in which one side, the Fiduciant (the client), transfers property or rights to another party, the Fiduciaire (the representative), who commits to hold the property or the right according to the client's instructions, and who can be asked by him to return the property or the right in certain cases.

The legal differences between the Fiducie and the trust are clear. The client is not protected, according to this institution, as are the parties in a trust. Here there are no means for supervision, such as the protector in a trust. The principles of the Fiducie stem from the principles of fiduciary law. In contrast to a trust in which the beneficiary cannot give instructions to the trustee, the client may give instructions to his representative at any time.

The Fiducie is based on the legal theory which is called "Full Rights" in Switzerland. This means that the representative owns the property or the right that has been transferred to him. At the time of the death of the representative, the Fiducie contract ends unless the sides predetermined that the Fiducie would continue to exist after the death of the representative. A reasonable concern within this institution is that the property or the right will be included in the representative's estate, and will be passed on to his heirs, and not returned to the client.

The greatest disadvantage of the Fiducie is in the case of bankruptcy of the representative. In Swiss bankruptcy laws, all of the debtor's assets must be transferred to the creditors including the property within the framework of the Fiducie. There are rulings and laws in Switzerland aimed to protect the client in this case.

Switzerland has recommended a law that aims to find a solution to this problem, and to make the Fiducie more like a trust.

2.17.2 Trusts in Liechtenstein

The laws of trusts in Liechtenstein are found in the Persons and Companies Law (1926), which was updated in 1980. In order to set up a trust in Liechtenstein, a written agreement is necessary between the trustor and the trustee.

Procedure

The trust must be registered in the Public Registry within 12 months of its establishment. The trustee must prepare a document detailing the name of the trust, date of establishment, period, the trustee's personal details and place of residence. At the same time the trustee must present the original trust deed or a true copy to the registrar. This document is not open to public scrutiny such that the details of the trust are maintained in absolute anonymity.

The trustor

The laws of trusts in Liechtenstein determine that any person can create a trust as long as he is able to create an agreement. The trustor can also be a corporation. The trustor may create trusts for any property or right that he owns. The rights of the trustor in relation to the trustee and the beneficiary are detailed in the trust deed and the law.

The trustee

In order to act as a trustee it is necessary to obtain the agreement of the trustor. Certain laws apply for appointing a trustee in a will when in this case the trustor appoints a trustee without his previous permission.

The obligation of the trustee is to act according to the trust deed. The trustee holds the Duty of Care, which requires him to act carefully when managing the trust assets. Additionally, the trustee must keep books for the trust assets and update the records regularly, and report to the beneficiaries and the trustor regarding the state of the assets.

In Liechtenstein law, it is clearly stated that the personal interests of the trustee may not be in conflict with the interests of management of the trust assets, according to the desires of the trustor, determined in the trust deed.

The trustee has three rights:

- To ask for remittance for expenses that he incurred while managing the trust assets
- To ask for a salary or payment for services as a trustee
- To place a lien on the trust assets in case he accumulates a debt as a result of not receiving the above rights

The beneficiary

The beneficiary is any individual who is able to receive rights or assets from the trust, in the present or the future. The main right of each beneficiary is receipt from the trustee, the details delineated in the trust deed determined by the trustor. The trustee may, in certain cases, bypass this obligation through the courts.

2.17.2.1 Corporations in Liechtenstein

The laws of corporations in Liechtenstein are found in the Persons and Companies Law (1926), updated in 1980. Unique in Liechtenstein corporation law is that some corporations, particularly foundations serve as trusts for beneficiaries.

The main corporations in Liechtenstein are:

- The foundation
- The establishment
- The trust enterprise
- Public limited companies

The foundation

stablishment

Establishing a foundation requires transfer of assets to it for a defined purpose. Establishment usually takes place through a representative, who is a trustee who resides in Liechtenstein, so that client anonymity is assured.

In principle the foundation is considered established the moment it is registered in the registry and only then may it open a bank account, buy assets, etc. The foundation may simultaneously manage assets and hold assets for the benefit of beneficiaries according to the instructions of the foundation founder, who holds "founders' rights".

Internal structure

The supreme body of a foundation is the board of directors, which may be one or more individuals, or a corporation, as the founder desires. At least one member of the board must be a resident of Liechtenstein and be certified as a professional trustee (a similar type of foundation exists in Panama but does not require appointing a local trustee).

Authority of the board is defined in the by-laws, which are similar to the articles of association of a company. The founder can also appoint a curator (also called a protector) whose job it is to supervise the board and assure its proper functioning.

Beneficiaries

Beneficiaries are individuals or a legal corporation that have the right to enjoy the profits or the dividends of the foundation. The founder of the foundation may also be the sole beneficiary of a foundation.

The by-laws determine the parts and rights of the beneficiaries. The by-laws are an internal (non-public) document that does not have to be registered at the registrar. From a legal standpoint the internal by-laws are a "sort of will" aimed to apply the rights of the founder to the beneficiaries, without the need for an order of probate procedure.

Local representative

According to the law every foundation must appoint a local representative representing the foundation to the local authorities. The representative may also hold other roles, determined by the founder.

Dissolution and Transfer

Dissolution and transfer of the foundation may be performed according to instructions in the by-laws.

<u>The establishment</u>

An establishment is a corporation stemming from civil law, and its assets are not distributed according to shares (similar to a one-man company). Sometimes the establishment serves commercial purposes and sometimes the purpose of a trust. Usually a local representative creates an establishment and only then transfers the rights of this corporation to a client using a bill of transfer. The advantage of such an arrangement: anonymity of the client's details.

Trust enterprise

The trust enterprise is a corporation with an internal structure similar to that of the establishment. Despite its misleading name, it is not the Liechtenstein Trust Settlement, but a special corporation that can operate as a commercial company, such as a trust fund.

Public Limited Company

The PLC is a legal corporation whose assets are distributed according to shares. The structure of the corporation is not much different from that of a regular company that exists in most countries worldwide.

Tax benefits are applied if the corporations listed above are not owned by a resident of Liechtenstein and are not active in Liechtenstein itself, but all activity is foreign.

2.17.2.2 Differences between trusts and foundations in Liechtenstein

- Legal personality: In a trust the trustee is considered to be the legal owner of the trust assets, and in the foundation, as it is a legal corporation, the foundation itself owns the assets.
- The trust provides more anonymity to the beneficiaries.
- In a trust there is no limitation of commercial transactions, but in a family foundation, the transactions of the foundation are predetermined and are generally not intended for commercial activity.
- The trustee of a trust may bear greater legal responsibility and there are cases in which the trustee is responsible for the trust assets personally.
- It is easier to change the structure of a trust or transfer it to another country. A foundation is limited to Liechtenstein and Panama (see figure no. 1).
- A trust may be ended immediately by the decision of the trustee. Ending a foundation requires formal dissolution according to Liechtenstein law (similar to dissolution of a company).

2.18 The trust as a corporation

Several countries are familiar with trusts as having a separate legal entity. Lichtenstein, and recently Panama and the Antille Islands, also recognize additional legal structures, such as funds known as foundations. Below is a chart that illustrates the structure of the foundation versus the structure of the trust fund.

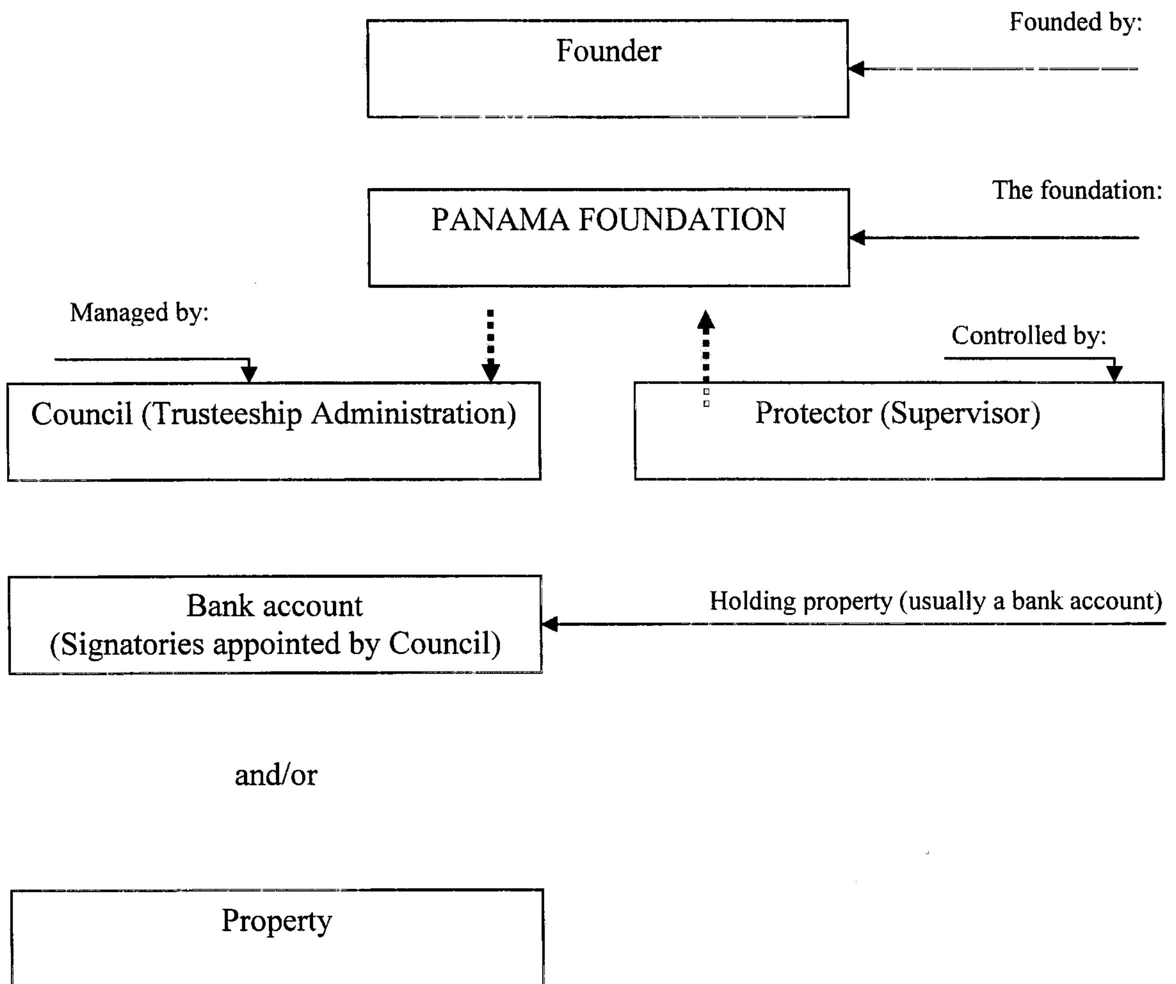


Chart no. 2: Foundation (Panama)

2.19 Offshore trusts as will substitutes

2.19.1 Special characteristics of foreign trusts

A foreign trust will generally have special characteristics (Clarke, 1999):

- It is created by the grantor in a country in which he does not reside, and in which the beneficiaries probably do not reside.
- The country in which the trust is created will usually be a common law tax haven. The Bahamas, Bermuda, the Cayman Islands, the Channel Islands, Gibraltar, Hong Kong, the Isle of Man, and Vanuatu all have numerous trusts.
- The trustee probably will be a bank or trust company with an office located in the foreign country in which the trust will be administered.
- The trust will be a living trust.
- The trust may provide for income and be accumulated for some years before any distributions are made to beneficiaries.

- The grantor will normally reserve the right to amend or revoke the trust unless tax reasons in his home country compel him to relinquish these rights.
- The grantor generally also will reserve the right to change the trustee. He may also provide for someone else to have this power after his death.

2.19.1.1 Non-tax advantages

Some of the important non-tax advantages of a foreign trust include:

- The trust as a will substitute: The trust acts as a substitute for a will. This factor may have considerable importance to a grantor who resides in a flight-capital country. A trust will eliminate the need for his foreign assets to be brought back to his country of residence for probate at the time of his death. It eliminates the need for separate wills in each country in which he has assets. The trust may conveniently own assets in several different countries either directly or through corporations. Upon the death of the grantor, the trust assets will either pass to beneficiaries or remain in the trust for the benefit, whichever is provided in the trust instrument. The grantor will establish his foreign trust in a country that has a trust law satisfactory to him.
- The trust can exist for eighty years or more: A common-law trust generally can run for eighty years or more before being required to terminate. The exact duration is restricted by the Rule Against Perpetuities. A trust can provide a great deal of flexibility. Usually the trustee is given broad powers to invest and reinvest the trust property. He/she may be given specific instructions concerning the distribution of trust income and trust capital to the beneficiaries, for example, distributions may be required to be made as each beneficiary reaches a certain age. Alternatively, the trust instrument can grant complete discretion to the trustee concerning distributions among a group of beneficiaries.
- Letter of Wishes: A discretionary trust is often accompanied by a letter of wishes that can be changed from time to time, in which the grantor informally guides the trustee to his desires. Although the letter of wishes is not legally binding, a bank or trust company serving as a trustee will invariably carry out these wishes.
- Moving the trust: It is usually possible to provide for the movement of a trust from one country to another if unforeseen changes take place in the country where the trust was originally established.
- Combining a trust and a holding company: The greatest degree of flexibility is often provided by coupling a trust with one or more holding companies. The holding company's shares are legally owned by the bank or trust company that administers the holding company. The beneficial owners are, of course, the beneficiaries for whom the bank or trust company serves as a trustee. Billions of dollars of assets throughout the world are held in this manner.
- A trust provides anonymity: Another possible advantage of creating a foreign trust is anonymity. A living foreign trust does not become a matter of public record at the time of the grantor's death, as does a will. In some countries it may be required to record the trust in a public register, but in many countries this is not required. The foreign trust probably will be completely outside the jurisdiction of any local court unless a beneficiary or other interested person brings a court action.

2.19.1.2 Possible disadvantages

Some of the possible disadvantages of creating a foreign trust include:

- Title to the trust property will have to be placed in the name of the trustee or some nominee acting for the trustee. This may involve the payment of transfer frees.
- Attorneys' fees will be required for the preparation of the trust instrument and the deeds and assignments transferring the property to the trust. These are likely to be much higher in the case of a foreign trust than they would be for a domestic trust, because several jurisdictions are likely to be involved.
- Counsel from each of these countries will have to review and approve the trust agreement and other documents. The need for approval under the laws of several countries invariably will make it impossible to use a simple standard form of trust agreement.
- The trust instrument is likely to be lengthy and complex.
- The trustee will charge commissions or fees for his services. Since the trust will be operating during the grantor's lifetime, fees will be payable during his lifetime as well as after his death.

2.19.2 Problems taxing foreign trusts and accepted solutions

1. The US – Who can use foreign trusts today?
   After the 1976 US tax reform rules there are still circumstances in which the use of a foreign trust should be considered (Reynolds, 1977).
   - A foreign grantor creates a foreign trust entirely for foreign beneficiaries.
   - A US grantor creates a foreign trust for foreign beneficiaries, none of whom is likely ever to become a US resident or citizen.
   - A foreign trust is created by a *bona fide* foreign grantor (not an accommodation grantor) for US beneficiaries. There it may be best to use a grantor trust that is currently taxable to the foreign grantor rather than an accumulation trust.
   - A nonresident alien who is planning to become a US resident creates a foreign accumulation trust with the expectation (or requirement) that the beneficiaries will be non-US persons at the time they receive distributions from the trust.
2. Moving a trust – the Canadian solution
   The Transatlantic Trust Corporation (Transatlantic) offers a unique solution for protecting offshore assets. Transatlantic is incorporated under the laws of a Canadian province, but does not administer trusts in Canada. Its shareholders are large banks in Canada, England, Switzerland and the United States and it administers trusts from branches in the Bahamas, Cayman, Hong Kong, Jersey and Switzerland. Transatlantic's executive committee can move the place of administration of any trust from one branch to another without reference to the manager of the branch where the trust is currently administered. Duplicate records are always kept outside the country of administration, so there is no loss of records if a trust must be quickly moved. The Transatlantic solution is particularly suitable for large trusts, but is expensive when used for smaller trusts. Transatlantic has reportedly obtained rulings from the Canadian tax authorities holding that its trusts so administered from foreign branches are not liable to

Canadian taxes except on Canadian-source income. If the tax situation ever changes, the private act under which Transatlantic was incorporated authorizes it to move out of Canada to any other jurisdiction where it can be legally continued.

2.19.3 Characteristics of beneficial tax regimes

In light of the fact that many countries worldwide have caused difficulties for companies positioned in classical tax havens, such as those in the exotic islands, there has been a trend, although not widespread, to search for alternative beneficial tax regimes. These are regimes that on one hand will provide the business with respectable status, but on the other hand will allow the company to enjoy comfortable fiscal conditions.

In fact, as in every case of competition, the sides attempt to find ways to overcome difficulties placed in their paths. A few countries have thus been smart enough to go through a metamorphosis in their internal tax laws, and now offer foreign residents taxation arrangements, some more sophisticated and some less, that are able to cope with the new reality and encourage the positive flow of capital and receipt of services in their country.

Two main types of beneficial tax regimes exist, in this context, for companies owned by foreign residents: The off shore regime, and the holding company regime, or participation exemption regimes. These regimes have been adopted by many countries that want to become an attractive destination for international holding companies.

1. Offshore regimes

   The classical offshore arrangement is a legal arrangement according to which the laws of a certain country determine leniencies and exemptions from taxes for resident companies or companies that are not residents (but only registered in it), in which all of its income is derived from sources outside of the aforesaid country. Often the tax exemption is absolute, and sometimes the leniency is expressed in lower to minimal taxation rates on income of the company that is based outside of the country. However, based on the OECD report on harmful tax practices and rules dictated by the European Union, the offshore arrangement has been canceled in most countries in which it had been used in Europe. Consequently, these countries have had to find alternate ways to compete with other countries in taxation. These methods meet the standards of the OECD and the European Union. There are also countries (generally not European), that still use the offshore arrangement or in which the taxation method is solely territorial, so that income derived outside of the country is taxed only if it is earned in the given country. This is the situation still in Singapore, Uruguay, Panama and other South American countries. The tax regime used in England, known as the resident non domicile arrangement, should be mentioned, according to which an individual who is a resident of England, whose domicile is not in England, i.e. a resident of England born and raised outside of England to foreign resident parents, is exempt from tax for any income not derived inside of England and not paid within England.

   Among countries that have cancelled their offshore practices are Cypress, Malta, Hungary and Ireland. These countries have now found other ways to compete in taxation with other countries. These methods including participation exemption, and conformity to the standards of the OECD and the European Union.

2. Participation exemption

As noted previously, countries that are members of the European Union have been forced to change their beneficial tax regimes to conform to the requirements of the Union and the OECD. These countries have found other ways to attract investors. One of these methods is the existence of the beneficial arrangement known as 'Participation Exemption'. Among the community of countries that apply the participation exemption regime and/or holding companies, are Austria, England, Iceland, Ireland, Belgium, Germany, Denmark, Holland, Luxembourg, China, Spain, France, Cyprus, Switzerland, Greece, Sweden, and Portugal (Boykin, 2005).

The taxation factors that are generally typical of all of these countries making them attractive for holding companies are as follows:

1. Exemption or low taxation rate on dividends received by the companies outside of the country;
2. Withholding tax at a low rate for dividends that are distributed to stockholders (individuals or companies) who are residents of another country;
3. Low or 0% tax rate on capital gains created from the sale of stock of the subsidiaries – 'Participation Exemption';
4. Additional exemptions exist in European Union countries based on the Parent-Subsidiary Directive, where a dividend is distributed from a resident company that is a member of the European Union, to another company, a company resident of the European Union.
5. A broad network of double taxation prevention conventions allowing lowering the rate of withholding tax on dividends received from foreign subsidiaries.

The combination of participation exemption regimes or holding companies, and parent-Subsidiary Directives makes these European countries a very attractive destination for establishing holding companies and foreign trusts, particularly: Luxembourg, Cyprus, Malta, Ireland, Singapore, Hungary, Romania, Switzerland, Holland, Denmark and England.

3. Underlying Companies in Israel

One of the major changes of the trust taxation law is the ability to establish an underlying company in Israel or abroad.

An "underlying company" is defined as a "group of persons" holding the trust's assets, for the trustee, directly or indirectly. This group can be a typical company, foundation, partnership, etc. The new law provides that this corporation is not regarded as a "flow through entity". This means that the Israeli tax authority ignores the company and treats the assets and the income as if they were held directly by the trustee.

As previously noted a "foreign trustor trust" is not subject to tax and does not have to file reports on income derived from outside Israel, even if the trustee is an Israeli resident. The concept of an underlying company is simple and advantageous in constructing the best arrangement possible.

2.20 Between trusts and inheritance

Every trust that is set up notes in its regulations the law according to which it was set up. Every country has its own internal rules and regulations. Israel also has the Trust Law that rules according to local legislation. Accordingly, when there is a conflict between the laws of two countries as regards taxation of the trust, the same thing occurs as in any other instance of a conflict between two internal laws of the countries, and the internal law of that country in which the trust is established is examined specifically. Hence it is fair to claim that the international law offers a solution to this question and the situation necessarily differs from one country to the next.

To illustrate this, one may state that there are many tens of trusts in Israel that were established according to foreign law, i.e., the founder is a foreign resident and the trust was established according to the law of his country of origin. Personal law of that country is generally followed and the approach to the specific issue raised is examined.

This is accepted practice in every country and follows the rules of international law.

In other countries in which foreign trusts were not recognized, as for example, in Switzerland, (discussed earlier in this chapter) the Hague Convention afforded the guiding rules until 30.6.2007. Recently, the Swiss parliament passed the Trust Law that recognizes trusts *via* a mechanism of private international law. At the intermediate stage, and since there is currently an organized law on trusts, the court will determine issues in which there is disagreement, to the point of settling the issue in legislation. (Kaplan, 2006).

2.21 The main findings of the theoretical literature

Most of the empirical literature that examines the connection between the tax burden (or public expenditure) and the long term growth rate indicates a negative correlation (i.e. high government expenditure and high taxation rates lower growth rates in the long term), or alternatively, a non-significant correlation. However, in general, it is difficult to differentiate between a high tax burden and high public expenditure in economic research frameworks, because the statistical correlation between them is quite high.

Below, we will survey a wide variety of studies that aim to estimate the impact of taxation or other fiscal variables over the growth rate:

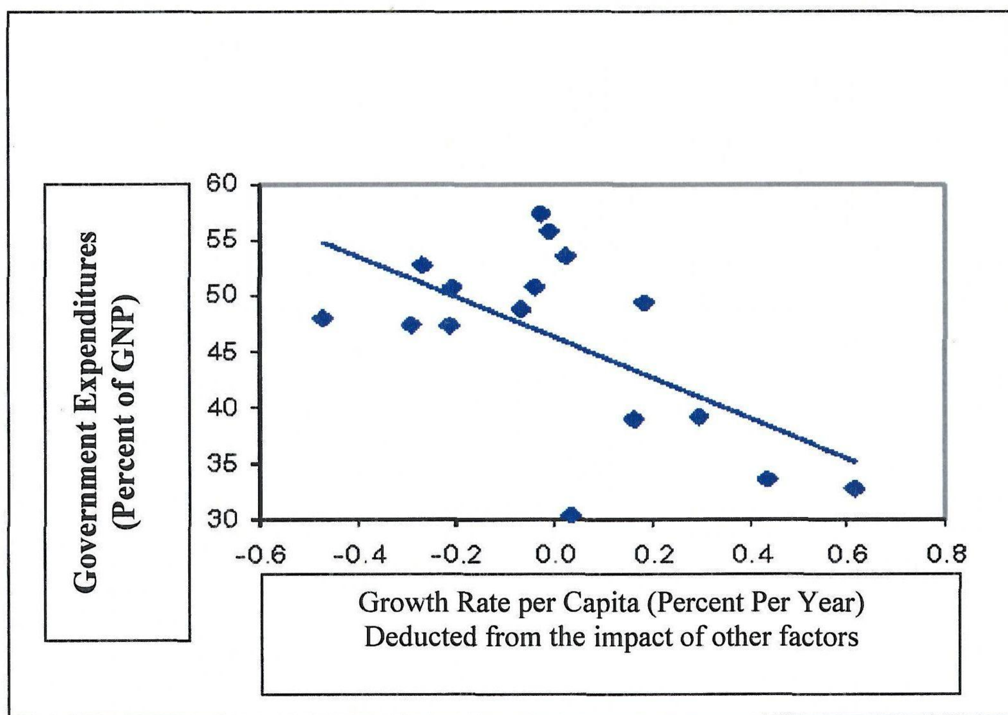
1. Use of growth models
2. Examination of cross sections of various countries
3. Analysis of the impact of tax over growth rates of small companies
4. A sectorial examination of tax influences over investment rates and geographic position
5. The impact of tax evasion
6. Studies regarding the situation in Israel

1. Use of growth models

Many theoretical and empirical studies have used growth models to simulate the influence of a basic tax reform on economic growth. One may conclude from these studies that it is possible to permanently increase economic growth by lowering the

distorting influences of the taxation system (see, for example, Engen and Gale, 1996, and Auerbach, 1996). However, a rise in economic growth depends greatly on the hypotheses of the models and therefore there is a difference in conclusions regarding the precise impact of taxation over economic growth. The following is an itemization of the results of some of these studies.

- King and Rebelo (1990) conduct a simulation according to which a rise of one tenth of one percent in the tax rate lowered the growth rate by about two hundredths of a percent. The reason for this was the disparity that the tax creates between gross and net yield in savings. Individuals are very sensitive to net savings yields and therefore a rise in tax will lead to a decline in savings and investments.
- An additional simulation model (Mendoza, Milesi-Ferretti and Asea, 1996) estimates a modest rise in growth rate, one quarter of one percent per year, as a result of lowering tax rates by one tenth of one percent (see graph no. 8).



<u>Chart no. 3: Growth rate per capita</u>

2 Examining cross-sections in various countries

Within the framework of various studies, a comparison was made of various countries at the same point in time. Most of the studies that have been conducted based on this approach found a negative correlation between the tax rate and the rate of growth. The following are a number of examples:

The impact of marginal tax and average tax

- Koester and Kormendi (1988) estimate the impact of marginal and average tax on economic activity in 63 countries over the years 1970-1979. They find that a high marginal tax lowers the growth rate (when the average tax rate is constant). An additional study showed that these results are less strong when expanding the sample period to 1970-1984, or when the sample is classified according to developed countries and undeveloped countries with low income levels (Koester and Kormendi, 1992).
- Plosser (1992) shows that a negative correlation exists between the rate of growth of the per capita GNP and average tax on income and profits in OECD countries.
- Easterly and Rebelo (1993) develop the hypothesis that direct taxation (income tax) has a negative impact on growth, based on a cross-section of 32 countries. Their findings indicate a negative yet weak correlation between tax rates and growth.
- Based on a number of approaches Engen and Skinner (1996) find that a rise of 5 hundredths of a percent in marginal tax and 2.5 hundredths of a percent in the average tax burden (total tax divided by GNP) will lower the economic growth rate in the US by 0.2-0.3 hundredths of a percent. Despite the moderate influence on the short term growth rate, the long term influence is large. For example, raising the growth rate by 0.2 percent per year will lead to a rise of 7.5% in the GNP in a range of 36 years. Their conclusion is based on an analysis of cross section data of countries and on an examination of the impact of tax over capital inventory, employment supply and investment in R&D.
- Comparison finds that income tax, company tax and import tax lead to a greater decline of the GNP compared to expert and purchase tax, based on data from African countries.
- Dowrick (1992) finds that income tax has a negative impact on growth, while company tax has no impact on growth, based on growth data from a sample of OECD countries between the years 1960-1985.

The impact of tax on the efficiency of capital allocation

A study conducted by the McKinsey Global Institute (1996) emphasizes the importance of efficiency in capital allocation between various industries. The study indicates that despite higher investment rates in Japan and Germany compared to the US, the contribution to the GNP was higher in the US because of more efficient capital allocation. Similarly King and Fullerton (1984) found a strong negative correlation between economic growth and the degree of variety of investment taxes in various sectors (damage to capital allocation efficiency).

3. The analysis of the impact of tax over growth rates of small companies.

Carrol, Holtz-Eakin, Rider and Rosen (2000) examine the impact of lowering marginal tax on income on the rate of growth of businesses owned by individuals. They find that lowering marginal tax from 50% to 33% (as a result of the 1986 US tax reform), increased the scope of returns for the average business by 28%. The authors base their conclusions on analysis of thousands of tax refunds to companies owned by individuals between 1985-1988.

Change in investment rates

Comparing the ratio between tax on income from assets to investment rates in OECD countries (Mendoza et al., 1996) indicates that a moderate negative correlation exists

between tax rates and investment rates. A decrease of one tenth of a percent on profits can affect investment rates by as much as one hundredth of a percent.

A number of studies (Auerbach and Hassett, 1991; Chirinko, Fazzari and Meyer, 1996) find a significant correlation between taxation policy and scope of investments, where investment flexibility in relation to capital cost affected by taxation rates ran in the range of 0.25 to 1 hundredths of a percent.

4 A sectorial examination of tax influences over investment rates and geographic position

The tax system affects the migration of companies between countries or the movement of businesses among subsidiaries in various countries. Companies move their activity (income) from areas with high tax rates to those with low tax rates).

5 The impact of tax evasion

Tax evasion affects the economic efficiency and equality in distribution of income. The tax authorities of the US estimate the rate of tax evasion at 15% of the sums they are supposed to collect (Slemrod, 1989). In 1993, marginal tax in the US was raised to 36% on income between $140,000-250,000 and to 39.6% on income on $250,000.

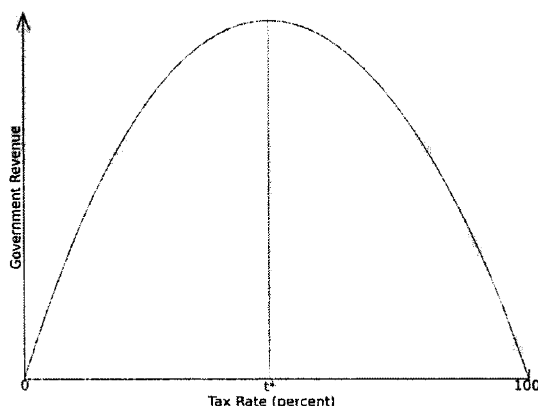
Feldstein and Feenberg (1995) examine the impact of the step on a number of factors including the scope of taxable income, the scope of receipts from taxes, and economic efficiency. The findings indicate that if tax rates had not been raised, the higher income brackets would have reported higher taxable income in 1993 by 7.8% than was actually reported. In light of this it was found that the social loss as a result of raising marginal tax was double the sum of taxes collected, to the sum of $8 billion.

Fisman and Shang-Jim (2001) investigate tax evasion among importers in China in response to a rise in customs rates. They find that the scope of tax evasion was high, such that it was possible that a rise in customs rates leads to a lowering of receipts from taxes. Estimation of the scope of tax evasion was based on comparing the reported quantities by the exporters from Hong Kong to those reported by the Chinese importers. Raising the customs rate by 1% led to an average rise of 3% in tax evasion. It was also found that the importers in China were willing to pay relatively moderate tax rates, but when the tax rates went beyond a certain threshold, they "rebelled". When tax is above 34%, the scope of evasion rises dramatically. Additionally, the elasticity of tax evasion in relation to the tax rate is higher at higher tax rates.

2.22 Relevant global research and the Laffer curve

Since the tax reform of the 1980s there has been an ongoing argument between neo-Keynesian economists and neo-liberal economists in English-speaking countries regarding the economic significance of the Laffer curve. Laffer's work is extremely important for the research hypotheses and in the analysis of this research, as will be demonstrated later

The Laffer curve, that became popularized by Arthur Laffer, is used to illustrate the concept of taxable income elasticity - the idea that government can maximize tax revenue by setting tax rates at an optimum point and that neither a 0% tax rate nor a 100% tax rate will generate government revenue. It describes how increasing taxation past a certain point might lower revenue and vice versa.



The curve is most understandable at both extremes of income taxation—zero percent and one-hundred percent—where the government collects no revenue. At one extreme, a 0% tax rate means the government's revenue is, of course, zero. At the other extreme, where there is a 100% tax rate, the government collects zero revenue because (in a "rational" economic model) taxpayers presumably change their behavior in response to the tax rate: either they have no incentive to work or they avoid paying taxes, so the government collects 100% of nothing. Somewhere between 0% and 100%, therefore, lies a tax rate percentage that will maximize revenue. Critics commonly point out that socialist states, such as the U.S.S.R., have been able to derive revenues at a 100% tax rates, though they would have derived more if tax rates had been lower.

The Laffer curve is a static model, in that it models an economy with identical productive capacity under two different sets of tax rules. In a dynamic economic model, economic growth is a relatively general phenomenon, and one would therefore expect tax revenue to increase over time even if the tax regime remains identical. This leads many to suggest that the common comparisons stated to support the Laffer curve are an unfair test.

Others respond that, even if the Laffer Curve itself is a static model, a programme of tax cuts nevertheless provides incentives for innovation and investment, which will increase the rate of economic growth, as predicted by endogenous growth theory.

The point at which the curve achieves its maximum will vary from one economy to another, depends on elasticities of demand and supply and is subject to much theoretical speculation. Another contentious issue is whether a government should try to maximize its revenue in the first place. Moreover, the ideal level of taxation is dependent upon the use of government funds, as certain types of spending do more to encourage growth than others.

The curve is primarily used by advocates who want the government to reduce tax rates (such as those on capital gains) and believe that the optimum tax rate is below the current tax rate. In that case, a reduction in tax rates will actually increase government

revenue and not need to be offset by decreased government spending or increased borrowing.

Conventional economic paradigms acknowledge the basic notion of the Laffer curve, but they argue that government was operating on the *left-hand* side of the curve, so a tax cut would thus lower revenue. The central question is the elasticity of work with respect to tax rates. Just about everyone can agree that if an increase in tax rates leads to a decrease in tax revenues, then taxes are too high. It is also generally agreed that at *some* level of taxation, revenues will turn down. Determining the level of taxation where revenues are maximized is more controversial.

It should be noted that in a progressive tax system, any given person's perspective on the validity of the Laffer curve will be influenced by the marginal tax rate to which that person's income is subject.

Laffer himself has pointed to Russia and the Baltic states who have recently instituted a flat tax with rates lower than 35%, and whose economies started growing soon after implementation.

The Laffer curve is clearly a model assuming uniform tax rates across all income ranges. It also assumes that the government will collect no tax at a 100% tax rate because, rationally, no person will choose to carry out work if they receive none of the economic return from that work. However some economists question whether this assumption is correct. For example, in classically structured Communist societies, there was an effective 100% tax rate and, whilst these societies may have been highly inefficient, people did continue to work to some extent.

A major fallacy is commonly committed with the Laffer curve, namely the assumption that the middle is a smooth, concave function merely because the two extreme endpoints are well-defined. A realistic tax curve would most certainly not resemble a smooth parabola or even any other simple function, but rather a very complex curve with many peaks, valleys, and multiple local maxima. Inside the middle, a wide range of various economic factors confound any simplistic attempt at this interpolation.

As a pedagogical tool, a Laffer curve helps illustrate a specific application of the law of diminishing returns, where the inhibitory cost of taxes may eventually outweigh the increased rate of taxation, and thus led to a counterintuitive lower realization of tax revenue. However the curve should not be taken as a literal model for a tax revenue curve, especially in debates between relatively moderate amounts of taxation. It is in this context that the Laffer curve is often abused, taken as a serious model for tax revenue when it has little to no predictive value in debates between intermediary rates of taxation.

2.23. Recent research in Israel

A central stream of economists in Israel believes that Laffer's concept, according to which lowering taxes increases the tax intake, justifies a reexamination of the issue.

Blanchard[1] states, "He (Laffer) was clearly mistaken regarding the location of the USA on the graph. The impact of lowering tax rates was a drop in income from taxes rather than in its increase."

At the same time, since this statement dates from the 1980s, this researcher believes it should be considered with great caution as the situation is the opposite in Israel since the introduction of the tax reform, known more as the correction no. 143 to the 2003 Income Tax Order, according to which there is a real rise in tax collection (see appendices 3, 4). Furthermore, the impact of the tax reform in Singapore, that partially adopted the tax reform in Israel, immediately caused an increase in income from taxes and transfers from other countries. According to the data of the Israeli organization STEP[2], the flow of investment to Singapore grew by more than $300 billion since the tax reform, some of which stems from the transfer of trust finds to that country. Hence the Israeli Ministry of Finance is fully familiar with this study in view of its determination to include the reduction in tax rates on work and personal labor on the one hand, and expanding the tax base on the other, for example, taxation on income from the money market that till 2003 was exempt (capital gains from stocks that are traded on the Israeli stock exchange). Expanding the circle of those paying tax together with reducing the tax burden became a target of the Israeli Ministry of Finance. The proposed tax reform is mentioned explicitly due to Laffer's study that it is proven that raising the tax rates results in citizens paying less taxes and the country receives less money.

In view of this, the researcher believes one can conclude also regarding the connection between lowering tax rates on foreign investments in general and of foreign trusts in particular, as will be presented below.

Lavi and Stervechinsky (2001) show that in the long term policy variables have a significant impact over GNP demand. Lowering tax by 1% of the GNP (without changing the public deficit, raises the GNP by about 2%. Taxation and deficit have a strong negative impact on productivity and investments and a relatively small impact over production factors.

Dahan and Stervechinsky (1996) study the correlation between the public sector budget and economic growth in Israel. The main findings indicate that the rate of growth per capital is negatively influenced by the tax rate. The composition of taxation affects growth because income tax affects it negatively, damaging the profitability of investments, while indirect tax has no significant impact over growth.

2.24 The impact of fiscal policy on investments in OECD countries

Alesina, Ardagana, Perrotti and Schiantarelli (2002) explore the impact of fiscal policy on investment using a sample of OECD countries, finding a strong negative correlation between public expenditure (particularly public sector salaries) and the scope of

[1]Olivier Blanchard and Francesco Giavazzi (2004),"Improving the GSP through a proper accounting of public investment". CEPR discussion paper
[2] Society of Trust and Estate Practitioners. http://www.stepisrael.org

business investments. A rise in public expenditure may harm company profits and lead to lowered private investments and a slowing of economic growth. In particular, changes in public salaries, the scope of employment in the public sector and government payments affect economic growth because of their impact over the work force, private sector salaries and company profits. Higher salaries lower profits, lower investments and consequently lower growth rate. Welfare payments to those who are not employed may also raise public sector and private sector salaries and lower growth rates. The opposite effects occur when public sector salaries are cut, and when welfare payments are lowered for those who are unemployed.

Thus this chapter of the study focuses on various countries that have introduced rules for taxing trusts in their local laws. The countries mentioned in this chapter have attributes identical to those in Israel from the economic perspective and those noted previously. Beyond this there are many identical attributes in the tax laws of countries mentioned and close considerations in the establishment of foreign trusts. Suffice it to note an example according to which the laws of many countries have an inheritance law for taxing inheritance. Legitimate tax planning is the establishment of a trust fund that exempts its initiator from tax, subject to the tax treaties between the countries (see also section 3.4.1). Israel, as a country that absorbs immigrants from many countries, also absorbed, and continues to absorb values, laws and particularly taxation laws, in particular from Anglo-American countries, a reminder of the British colonial law that existed in the country until the establishment of the independent State of Israel. Evidence of this can be found in the Israeli tax laws that are collected into the Income Tax Order and not in the Income Tax Law. Even the head of the tax authority is not known by this name, but is called the Tax Commissioner, a momento of the British government. It would thus seem that the choice of policy with an Anglo-American orientation, was not usually random. It can testify to the close connection to the State of Israel as regards tax law on the one hand, and on the other of the approach that this researcher believes should be adopted as regards shortening the bureaucratic processes. He would like to add and emphasize that the two countries are included in the review of the literature and have considerable impact with implications for other countries.

New Zealand had a major impact on the Israeli legislator who eventually chose the system used in that country and according to which trust taxation differentiates between taxation of trusts of a local resident, and taxing trusts of a foreign resident.

Lichtenstein is a source for many countries that have adopted the trust-like entities method, such as Austria and other countries of the former eastern European bloc. This method was investigated for application in Israel but was rejected.

Trusts can therefore be divided into two types: Countries adopting the accepted law – England, USA and Australia, as well as those adopting British law such as the Virgin Islands, the Cayman Islands and Gibraltar, and countries adopting continental law such as Lichtenstein, Panama and the Antilles.

Although the tax reform in Israel as regards mutual funds adopted the suitable tax laws from a list of countries mentioned above, this researcher believes the important research questions remain of whether lowering barriers (decreasing bureaucracy) in the taxation

system, and implementing taxation of trust funds abroad encourage investors in Israel and abroad, and encourage the flow of capital into and out of the country?

<u>In view of all the above, this researcher hypothesizes that</u>

1. Lowering the barriers within the Israeli taxation system will encourage investors in Israel and abroad.
2. Taxing foreign trusts will lead to money escaping from Israel abroad.

Nevertheless, this researcher maintains this should be considered with due caution. Although the flow of foreign capital from abroad is likely, on the one hand, to improve the local economy, while on the other hand generate other problems. Suffice it to mention the latest international and Israeli legislation regarding laws against money laundering. Furthermore, as noted in the introduction to this study, it is sometimes difficult to track the 'route' taken, mainly of companies with a complex legal structure, that create financial deals and complex money transfers. Thus one should also consider the issues pertaining to the origins of the money and apply paths of action taken in the European Union and in the OECD

These issues will be discussed in chapter 7.

Chapter Three: The Economic Significance of Trusts

3.1 The economic meaning of trust funds

The trust has been an accepted financial tool in the Anglo-American world for hundreds of years, and was created to cope with financial, legal and social problems. Using this method, the individual detaches himself from property and grants "ownership" of it to a third party, providing instructions on how to act with the property that was placed in third party control.

Today, trusts are used as a legal structure to cope with aspects of individual and international taxation. In other countries, trusts are considered to be a legal solution for solving problems of taxation of inheritances and gifts.

It should be noted that a trust is created not only for tax avoidance purposes, and most trusts are set up to provide a response to the issues of inheritance, wills, estates, and sometimes even for the purposes of commercial transactions. The trust defines the legal relationship between the creator of the trust, the beneficiary and the trustee, within which the trustee holds and manages the assets that the grantor transferred to his ownership, for the benefit of the beneficiary or for any other purpose.

In the present chapter, we will discuss the following topics:

- Who do foreign trusts serve?
- The principles of taxation and the reasons behind establishing trust funds in Israel
- The reasons for creating a foreign trust fund by a foreign (American) residen
- Why are trust funds preferred to offshore investments?
- The clear disadvantages of creating a trust fund

3.2 Who do foreign trusts serve?

Data of the STEP organization (from November 7th 2006) based on the Business Week magazine of November 2004, find the following data regarding the concentration of capital in the world with a few wealthy people:

- 7.7 million people were defined as having much capital in 2003
- Each had at least $1 million
- The total property held by the rich is $28.8 trillion:

Europe	$8.7 trillion
USA	$8.5 trillion
Pacific Asia	$6.5 trillion
Latin America	$3.7 trillion
Middle East	$0.8 trillion
Africa	$0.6 trillion

- 129,000 wealthy Europeans joined the global club in 2003 alone.

According to the survey conducted by STEP amongst its 3,400 members it transpires that there are 1018 trust companies in the world that hold a government license, of which 78 are in Gibraltar and 162 in the Jersey Islands. The result – the global accumulated property held in the trust is estimated to be $2-4 trillion.

The flow of investment in Singapore grew by more than $300 billion, some of which stemmed from the movement of trust funds to that country. Hence the Israeli Ministry of Finance is fully familiar with this study in view of the determination to include the drop in rates of taxation on work and personal labor on the one hand, and expand the tax basis on the other, such as taxing income from the money market that was tax exempt till 2003 (capital gains from tradable bonds on the Israeli stock exchange). These have become goals of the Ministry of Finance. The tax reform proposal even notes clearly, following Laffer's work (see section 2.3), that research has proven that an increase in the rates of taxation causes the citizens to pay less tax and the country receives less money. In view of this the researcher is convinced that one may also draw conclusions regarding the connection between reducing the rate of tax on foreign investments in general and of foreign trusts in particular, as noted below.

By nature, because of sophistication, the need for financial experts and those with legal training, and based on the large sums required for investment (at least $1-2 million), this tool is utilized by the upper thousandth of the population and well-to-do foreign residents who are looking for attractive investment horizons.

Even before the conclusions of the Israeli Committee were presented, which discussed the implications of taxing foreign trusts, it was recently published (in the Globes newspaper) that trusts and aggressive tax planning have become the most significant tax loophole in Israel. In the months prior to publication of the committee's conclusions, the Tax Authority identified an increase in use of foreign trusts as a tool to avoid taxes.

Estimates of the Tax Authority of loss of income to the treasury stand at more than hundreds of millions of dollars annually.

This was also found by tax experts of STEP Israel' that avers the total foreign currency balance of foreign investors, according to Bank of Israel data (as of 4/2007) is $29.8 billion, of which foreign resident investments in trusts comprise about $15 billion. The average rate of yield on the investment is approximately 10%, leading to a yield of $1.2 billion. At an average tax rate of 25%, income from taxes are approximately $375 million ,i.e 0.28% of the Gross Domestic Product .

3.3 The principles of taxation of trust funds today in Israel

		Israeli Resident Trust	Foreign Resident Trust		Foreign Resident Beneficiary Trust		Trust by Probate
Classification of Trust	Classification by two dates:				General for: a. The conditions to not exist regarding Israeli resident trusts. b. Not a trust by probate		
	Date of creation	Alternative A At least one grantor and beneficiary , both Israeli residents	Alternative A All grantors are foreign residents	Alternative B	Alternative A	Alternative B 1. Is an irrevocable trust and 2. All beneficiaries are foreign resident individuals who are known 3. One grantor at least is an Israeli resident	
	Tax year	At least one grantor or beneficiary is an Israeli resident.	All grantors are foreign residents	All grantors and beneficiaries are foreign residents		1. It is an irrevocable trust 2. All beneficiaries are foreign residents individuals who are known 3. At least one grantor is an Israeli resident 4. The trust papers determine that no Israeli beneficiaries may be added. 5. In the report presented in the year of creation it is stated that there is no Israeli resident beneficiary whose eligibility depends on stopping to be an Israeli resident, and no such beneficiary may be added	

	Classification of trust not dependent on creation date or tax year	Alternative B (residual) A trust that is not a trust of a foreign resident trust or foreign beneficiary trust or trust by probate					Trust created by probate and all trust grantors were Israeli residents at the time of death.
Attribution of income and trust assets		Attributed to the grantor. Trustee income will be considered income of Israeli resident and trustee assets will be considered assets of Israeli resident individual	Attributed to a (foreign resident) grantor All income and assets of trustee are attributed to a foreign resident individual		Attributed to the (foreign resident) beneficiary Income and assets of the trustee will be considered as attributed to a foreign resident individual		Attributed to the beneficiary (Israeli resident/ foreign resident) as applicable

Chart no. 4: Principles of taxation of trust funds today in Israel

Clarifications to Chart no. 4:

1. In Israel a trust is a not taxable legal entity and therefore is not considered a "taxpayer".
2. The trustee is not considered a taxpayer and his citizenship is not connected to his tax commitment in this context.
3. The taxpayer according to new laws in Israeli law is the grantor or beneficiary, if they are Israeli residents.
4. Tax laws apply to irrevocable trusts.
5. Israeli resident trusts are taxable as follows: a) for capital income 15-20%; b) from interest 20-25%; c) from dividends 20-25%.

Accordingly and in order to illustrate: An American or English resident with an attachment to Israel will have to face several considerations apart from those of taxation, as to why to open a trusteeship in Israel[3] :

- To enable more than one generation of beneficiaries to enjoy the property
- To provide the needs of disabled people
- Trade
- Protection of family property from family members who have personal problems
- Protection of property from creditors
- Assuring control of family property
- Coping with inheritance laws. In other words, in Anglo-American countries inheritance taxes are imposed at the marginal tax rate that is likely to reach 40% - 52% in the USA (inheritance tax), while in Israel there is no inheritance law and the tax, in the case of taxing trusts is extremely low (see chart no. 4). In most cases since the creator of the fund is a foreign resident he will pay reduced tax or be exempt.

3.4 The reasons for a foreign (American) resident creating a foreign trust fund

According to American law, an individual who bequeaths up to $1 million is exempt from inheritance tax. In Israel, there is no inheritance tax. This tax was applicable until the 1980s, and led to legal manipulations in order to avoid paying it so that in 1993 it was finally canceled. One of the reasons for its cancellation was that it was a tax that serves only the rich, who would get around it through experts and consultants such as lawyers and accountants.

A situation was created in which wealthy Americans, whose property was valued above this sum and wanted to bequeath it to their offspring, had a problem with tax payment, which in many cases, reached 52% on the inheritance (above $1 million).

On the other hand, the marginal tax rate on personal work was lower than that in Israel. There are leniencies in this law, for example, if the individual left the US and gave up his American citizenship, he is exempt after ten years from inheritance tax when bequeathing his property to offspring.

[3] . Kaplan, A. (2006), Trusts in Prime Jurisdictions. Globe Business Publishing, 2nd. Ed.

As a direct result of the American law, there are two strong arguments for a lack of desire to pay this tax:

a. An individual who earned money all his life and paid tax on income is actually required to pay additional tax on assets that he accumulated - when inheriting. Therefore he sees this justifiably, as double taxation.
b. Inheritance law is in principle an egalitarian tax that aims to divide wealth and transfer it from the rich to the poor. The rich, by nature look for ways to maintain their capital, without sharing with the treasury and the public coffers.

Therefore, one elegant way to avoid paying tax is by creating a trust fund in Israel, because in other countries, such as England and Canada, he will be required to pay tax .

3.4.1 Why are trust funds preferred to offshore investments?

Investment in trust funds is an ancient tool that had been in use many years prior to the Israeli tax reform. Considerations behind establishing trusts can be for the reasons mentioned above, and not necessarily due to tax considerations.

Recently, and mainly after the Israeli tax reform, use of this tool has increased, as of 1.1.2006, in view of the advantages that it provides, compared to tax exemptions through offshore investments. This researcher offers the following reasons why this tool has become so popular worldwide, and particularly in Israel:

1. The US Senate has raised a recommendation for a law aimed at attacking the flow of money to offshore tax havens.
2. As noted in the introduction, one of the main considerations in establishing a trust fund is the fact that many countries such as the USA and Europe have an inheritance law, according to which the deceased's beneficiaries are taxed according to the laws of that country.
   Legitimate tax planning allows the establishment of a trust fund in a country that is party to that treaty and to transfer money and property there that is subject to the tax treaties of the country that is likely to be tax-exempt, or taxed at rates lower than is customary in that country. In view of this fact, a phenomenon is common in Israel of rich Jews transferring their money to trusts in Israel.
3. Western industrialized countries have established organizations for economic cooperation, among them the OECD and FATF, which, among other things, aim to prevent laundering dirty money and fighting money laundering that comes from illegal commerce and various organized crime rings. Above all, the aim is to block the transfer of money to international terror organizations. Preventing tax avoidance or legitimate tax planning is a secondary aim, but the war on "black capital" related to illegal activities is harmful, even in tax havens.
4. Countries have created black lists of tax haven countries, with which there are commercial limitations.
5. Banks are not happy to open accounts for corporations that reside in tax havens, and therefore invoices of companies that reside there will not be recognized as business expenses. For example:
   (a) In Greece an invoice paid to a company in a tax haven is not recognized as an expense for tax purposes.
   (b) In Israel an Israeli company cannot make a bank transfer of money for services provided by a company in a tax haven without provision of details regarding the company proving that it pays tax in a different country.

(c) Cyprus, which until recently was a tax haven, requires discovery to their central bank of who are the stockholders in the company when stock is held by a trustee for them.
(d) Even banks in Switzerland who are known for their discretion, will not open an account for a client who does not have a recommendation from a lawyer, accountant, or bank in his resident country.

6. Until 1.1.2003 it was worthwhile to invest in offshore investments as there was no tax obligation in Israel. As of 2003, a control foreign company (CFC) is required to pay 25% tax versus tax of 20% on capital gains or on dividends from investing in a trust.
7. Individuals who invest in real estate abroad sometimes have family members and adult children in these countries. Their children's income is lower than the tax threshold in their own country. In certain cases, use of trust funds in which the individual transfers his rights to property abroad to a trust where the beneficiaries are his adult children, may, under certain circumstances, ease the tax burden by dividing it among the children, so that the rate is significantly lower.
8. Many businesses are afraid of taking the risk of moving to an offshore investment country and giving up the framework in which they worked until now, with their skilled personnel and other familiar parts of their business. The transition to an offshore company by nature cannot be done through experience. In order to enjoy a tax exemption, the company must totally detach itself from its previous form of existence.

As noted in the introduction to this thesis, one of the main considerations for establishing a trust fund is the fact that in many countries such as the USA and on the continent here is an inheritance law, according to which the inheritors of the deceased are taxed according to the countries laws.

3.4.2 The clear disadvantages of creating a trust fund

In contrast with the inherent advantages of trust funds, there are also clear disadvantages, including:

- Accompanying costs such as fees to managers/trustees, which are much higher and sometimes reach 2-3% of the principal *per annum*.
- Cash flow - the need to detach from control over the money. This is not appropriate for a person who is managing a business and is used to a turnover of large sums of money. For example, a well-to-do American citizen who has $10 million decides to move half of his capital to a trust. The problem is mainly a cash flow problem, as on one hand he will enjoy the fruits of his investment (tax exemption on interest, dividends or any other yield on the principal), but on the other hand he cannot touch the money that may provide him with an annual yield of 5-10% in a solid investment.
- Tax planning using foreign trusts is based on double taxation avoidance conventions. This may be irrelevant sometimes, as foreign trusts may be subordinate to foreign tax laws. Therefore, a double taxation problem may arise.

Anyone who wants to avoid paying tax requires some type of tax haven.

The structure of tax havens differs from country to country. Companies and individuals utilize different tools to avoid paying tax, such as:

- Holding companies
- Offshore banking and investments
- Manufacture in tax free zones

Today there are more than one hundred countries that provide low tax rates to their residents or to companies and foreigners, some even delineating free trade zones for this purpose. However, a company or individual who decides to move its business to a tax haven will encounter some complex questions, such as:

1. What type of company should be managed in a tax haven?
2. How does one construct holding of the company?
3. The quality and skills of the local work force.
4. The attitude of OECD countries and the US towards these havens (as described above).

2007 finds many countries having passed far-reaching legislation in their struggle for tax havens. The possibilities open to individuals with extensive capital to remove their wealth and profits accumulating every year from the tax basis in decreasing. On the other hand, cases in which individuals are interested in allocating significant sums of money to their descendents, or to other purposes, without having the possibility of again enjoying this money themselves have the legal and totally open possibility of using the trusteeship. It is thus possible to not pay taxes on the profits accumulated on capital via trusts.

When the trust creator lives in another country than that of the beneficiaries, he has the opportunity to create trusts in their favor and all the profits on the capital are likely to be tax-free. In parallel it is important to understand the possibilities of tax havens in off-shore companies have declined.

If in the past it seemed that capital that accumulates profits in these companies is tax-free in Israel, since they are not managed and controlled in that country, and even drawing profits from the company into an account abroad was tax free, this is no longer so since the tax reform. Nowadays, shareholders in Israel are taxed already at the company level on the profits accumulated by the company as one with passive income. How much more so in every case in which money is drawn from a foreign company to a bank account abroad where the dividends will be taxed?

In order to avoid paying tax, complex and costly structures must be established that block the possibility of taxation on passive income by establishing holding companies in which the rate of taxation at source is greater than 20%. Then too, this is only a temporary solution since full tax will be paid on all profits when drawing the money. In view of the above, the use of trusts will probably increase and the use of off-shore companies for these purposes will decrease now following legislation of taxation of trusts.

3.4.3 A case of a clear advantage to create a Trust Fund

Example of the advantage of a trust compared to regular investment we present an American investor who invests directly ('direct holding') in exchange traded funds (EFT) of the NASDAQ index, compared to holdings through a trusteeship in Israel or another country partner to the treaty. For example we assume that the investment was begun on 10.3.1999, and that the tax rates on capital gains, inheritance tax and tax at exit points (points of redemption) are known. We similarly assume that the portfolio is

realized each year and the money is reinvested at the start of the next year. On 31.12.2007 the portfolio is liquidated on the assumption that the investor died and the money goes to his inheritors.

The price of any QQQQ EFT is 50.08 on 10.3.1999, and its value on 31.12. 2007 is 51.24 (see chart no. 5 – NASDAQ source)

Advantages of taxing trusts

Assumptions

Rate of capital gains tax	25%	
Rate of inheritance tax	40%	Reduction: The entire sum is taxable – exemption ceilings are used/exploited
Tax rate on redeeming trust	25%	

People exchange their stocks every 31/12

Method of offsetting losses – only forwards as in Israel

Investment in	**QQQQ**						
	In the holding directly					**In a trust**	**Difference**
Date	Rate on	Accumulative profit	Ongoing profit from stocks	Tax this year	Accumulated, on which tax was not paid	Income tax	
10/03/1999	50.08						
31/12/1999	89.62	39.54	39.54	9.89			
31/12/2000	57.26	7.18	-32.36		-32.36		
31/12/2001	38.16	-11.92	-19.10		-51.46		
31/12/2002	23.90	-26.18	-14.26		-65.72		
31/12/2003	35.77	-14.31	11.87		-53.85		
31/12/2004	39.54	-10.54	3.77		-50.08		
31/12/2005	40.16	-9.92	0.62		-49.46		
31/12/2006	43.03	-7.05	2.87		-46.59		
31/12/2007	**51.24**	1.16	8.21		-38.38	0.29	
Tax on yield	-9.89			9.89		0.29	
Net sum	**41.36**					**50.95**	**-9.60**
Inheritance tax	-16.54					-	
Net sum to bequeath	**24.81**					**50.95**	**-26.14**

<u>Chart no. 5: Advantages of taxing trusts</u>

Since his capital profit started only in 1999 from stocks of 25%, he will pay tax of 9.89, while for the other years he in fact suffered a loss, so will not pay any tax. It should be noted that during realization, an apparently absurd situation occurred in which tax was actually paid but he is not entitled to receive a rebate on the profits and took against the apparent losses between the years 2000-2007. In addition, tax is paid on the inheritance at the rate of 40% of the balance, of a total of 16.54 so that the sum to be inherited net will be 24.81% only.

In contrast, investing in trusts produces the same rate of accumulative profit, when the calculations in a trust are only performed at the end of the period, therefore on the accumulative profit of 1.16 for the period he will only pay 25% tax, a total of 0.29. Obviously, without inheritance tax (that is exempt in a trust). Thus the sum in a trust to be inherited will be 50.95 net, compared to a total of 24.81 in direct holding. So that the savings in tax comes to 26.14 according to this example.

Thus, in view of the above, one can understand the tendency to utilize trusts ever more with the economic intention of savings in taxes, preferring this method over other tax havens, despite the disadvantages.

In Israel, as presented above, tax that foreign trust funds contribute to the national coffers is estimated to be 0.28% of the total GDP. It can be clearly seen that this fact is significant for the purposes of utilizing resources (see graph no. 2) and for increasing expenses for public consumption.

In chapters 6 and 7 we will discuss further implications of these facts.

Chapter Four: The Research Methodology

4.1 The research approach

The research approach in the present study is basically the quantitative approach. Research questionnaires were distributed in two rounds, with the first round conducted according to the qualitative method, in which six experts in the field of international taxation and who were influential over decision-makers in the Israeli economy, were sampled.

Qualitative research is a situational activity that offers a viewpoint for someone observing the world. This means that qualitative researchers study phenomena in their natural environment, attempting to find significance or interpret them in terms of how humans use them.

According to Shkedi (2003) the main role of qualitative researchers is to assist humans in telling their stories, to assist them in being aware of having stories, to assist them in exposing their stories, to clarify or to present the meaning of the story, both to themselves and to the researcher. People naturally love to tell about their own lives, their past, their present, and the future facing them.

Qualitative research became popular among researchers studying humans and their well-being. Any interview is the product of the interaction between the interviewee and the interviewer. In-depth interviews are conversations in which both the parties are active.

Qualitative researchers are an inseparable part of the investigation. They are involved as observers, as participants, interviewers or as leaders of a focus group. However, the researcher must also maintain separation from the situation being studied in order to re-think the implications of the experience. He/she must understand the viewpoint of another person, from an empathetic, and not only from a sympathetic, position.

In-depth interviews are often the main source of information. Asking questions and receiving answers is a more difficult task than it first seems. The written or spoken word may have more than one implication. Even if questions are very carefully formulated, one must report and codify the responses carefully.

Shkedi (2003) asserts that the goal of the in-depth interview is not to receive answers to questions or to test hypotheses, but rather to understand the experiences of other people and the significance that they attribute to these experiences. Lincoln and Guba (1985) view the human as a research instrument in order to illustrate the special role of qualitative researchers in the data-gathering process. The human, i.e. the human as an instrument is the only instrument flexible enough to understand the complexity, the refinement and the continual variance in the attributes of the human experience. They argue that qualitative-constructivist research is not characterized by a clear and unchanging definition, does not *a priori* provide diagnoses, and does not provide permanent and predetermined decisions. There is no way to predict the degree of use of the research instrument and the way it will be applied, because only the human instrument has the traits necessary to cope with a hazy and unclear situation. They also argue that the human instrument has the ability to respond and is characterized by

sensitivity and the ability to relate to all of the environmental and personal hints that arise. He is also able to adapt, and is able to simultaneously assemble data related to many factors. The human instrument is also able to understand multi-faceted ideas and concepts and is able to connect between the parts in a rational manner.

4.2 The research population

The research population included a total of 43 respondents out of the 60 people who were approached. Questionnaires were distributed to two groups having different levels of knowledge. The first group, which eventually included six respondents, were experts in the field, one of whom (F) did not always answer or fully answer the questions (for which reason there are not always six respondents). The second group included 37 respondents with a broad education in the field of taxation in general, and specifically international taxation - lecturers and students with second and third degrees in economics and business administration, accountants and attorneys from the private and public sector.

The research population includes all the stakeholders and influential individuals regarding the issue of taxation laws of foreign trust funds in Israel. Because of the complexity of the topic and its characterization as an issue that only affects the top one-thousandth of the population of the State of Israel, there is a limited target population (lawyers and accountants) who are able to respond to and understand the issue and its implications. Therefore, the Delphi group was chosen as a research method suited to the situation in which a small group of experts responds to a questionnaire. The group that was chosen was important as it comprises individuals who design actual policy and have influence over decision makers in the Treasury, Knesset committees, and indirectly, also over the legislative body.

The responses of the respondents in both groups were analyzed based on the Delphi method.

4.3 The Delphi group research method

The Delphi research method is a powerful instrument for examining future developments and making strategic decisions in the business and government sectors, and for supporting a process of consolidating national scientific policy. The method is based on interaction between experts, using recurring rounds of structured questionnaires, until the responses converge towards a reasonable degree of consensus.

In a typical Delphi research, experts are asked a number of questions regarding future technological developments, such expected year of realization, relative importance, constraints for realization, chance for business success, implications regarding the environment, etc.

The Delphi method for prediction and decision-making deals with a problem by gathering the separate opinions of the group members ahead of time, from each member individually (and in particularly sensitive cases, anonymously), and only later, discussing the organized results that were gathered. Thus the participants have no way of knowing the opinions of other group members regarding the topic, and the

discussion must deal with a wide variety of possibilities and directions for making a decision.

It was originally developed as a procedure for formulation and coordination of predictions among groups of experts. It mainly served to obtain precise estimates of expected dates for future events. Use of the method began at the beginning of the 1950s when the Rand company named adopted the name Delphi as the name of the procedure in an early experiment called the "Delphi Project". The experiment attempted to choose an industrial target in the US and estimate the number of bombings necessary to lower the output of ammunition at a given rate. The procedure aimed to achieve the most reliable consensus of group opinion, using a series of intensive questionnaires (five rounds), combined with controlled feedback regarding opinions, avoiding direct confrontation between the group members. The experiment was financed by the American Air Force that, for security reasons, avoided publishing the research results for at least ten years afterwards.

The procedure proffered that it was possible to accept the expert opinions of individuals as scientific testimony in areas that still had not developed formal scientific laws. The procedure aimed to replace direct discussions through a well-planned program of organized interrogation of individuals (conducted in the best possible manner using a questionnaire), combined with feedback, information and opinions based on the consensus that was calculated based on earlier stages of the program. Dalkey (1967) defines this process as a system of procedures for retrieving and refining group opinion, generally within a group of experts. Turoff (1970) also suggests a similar definition, saying that Delphi was the procedure for methodical retrieval and gathering of a specific opinion geared towards a certain topic, using a series of questionnaires that were carefully planned, in combination with information that was agreed upon, and feedback on opinions based on previous responses.

At a later stage, Turoff (1975) presents what seems today to be the most accepted definition of Delphi, as a procedure for constructing a process of group communication such that the process operates effectively, in order to allow a group of individuals, in general, to handle a complex problem.

Since it was first used at the beginning of the 1950s, implementation of the Delphi procedure has spread, and the method has been both praised and critiqued. The Delphi procedure received its metaphorical name from the Greek mythological oracle at Delphi where Apollo argued one could predict the future (Judd, 1971; McBride, 1974).

4.3.1 Versions of the Delphi method

The more popular the Delphi method became, the more versions of the procedure developed. Each version aimed to improve the procedure, based on specific needs and on criticism that was made of the procedure. Attempts to improve it were first made by Olaf Helmer (1966) himself, the inventor of the method. From then till now, many and varied versions of the Delphi procedure have been presented, reflecting and providing solutions to various issues. From the moment the original method was applied, versions were presented that developed a practical approach towards Delphi as a means for promoting formulation of group opinion and making decisions for the future.

A short time after the original Delphi method was developed, Pyke (1970) developed a version that he named the "Sequence of Opportunities and Negatives" (SOON). He expanded the Delphi procedure to include an index of the degree to which a certain event was desirable, as measured by those who would be affected by it, and an index of profitability reflecting any large difficulties that those dealing with realizing the event may encounter.

a. Policy Delphi (PD)

This is a procedure with special attributes to create a practical approach. It maintains anonymity and takes advantage of the function of feedback, but the PD procedure does not aim to achieve a consensus, but rather to promote opportunities while considering all the various opinions of the participants. It aims to create the maximum number of opposing opinions regarding potential solutions to a central policy issue. Therefore, the PD procedure is an instrument to elicit possibilities, and it is able to offer a number of alternative plans of action that policy makers may consider. The procedure helps eradicate the bottleneck problem of the "committee" that the original Delphi procedure used, by providing a clear definition of all of the different opinions, offering all the participants an opportunity to satisfactorily prepare their opinions regarding different issues (Turoff, 1975).

b. Decision Delphi (DD)

This procedure adds new attributes to Policy Delphi. The procedure does not relate to experts or to people who support a given approach, but to the decision makers themselves, in order to recruit participants based on their real position in the decision making hierarchy (Ranch, 1979). In this procedure, anonymity is not applied fully, as the names of the participants are predetermined. However, the various responses are not identifiable according to any given participant (quasi-anonymity), and the prestige of the other participants can serve as a challenge and incentive.

c. OSCAR

Another interesting procedure that provides an opportunity for conducting multiple rounds of information gathering in different contexts of face to face sessions, such as workshops and seminars, but still maintains the anonymity of the participants, is OSCAR (On Site Conferencing and Researching). OSCAR was presented by Harkins and Kurth-Schai (1983), and several colleagues, members of Anticipatory Sciences Inc. The goal of the OSCAR conference is to assist in planning and creating strategy to clarify what the future holds, and to offer methods to handle change. The method provides new ways to think and to act. This is a time and event technology that can be integrated in various ways to assist people in achieving understanding of alternative realities.

Despite the many procedures that may be applied to achieve formulation of a group opinion and group decision-making, only the Qualitative Controlled Feedback (QCF) procedure combines a series of elements that are able to overcome the weaknesses identified in other group decision making methods, such as brainstorming etc. (Press, 1983). The procedure does not require all group members who are involved in mutual interaction with one another to achieve a consensus or a group decision. It does not allow the group members to interact during judgment, and also does not allow the group members to know the identities of the other group members or their personal judgment regarding the issues at hand.

In some ways the QCF procedure operates differently than the accepted Delphi procedure. First of all, the feedback provided by QCF is qualitative, and not quantitative, and this means that the feedback is formulated in sentences explaining the individuals' judgments, and not as the average group responses and standard deviations. These qualitative responses may include information, disagreements, opinions and nuances that cannot be found in quantitative responses, but may be valuable for individual respondents, and can be used in research results. Finally, QCF does not attempt to achieve consensus. Although most or all of the participants may agree regarding one or many items, consensus is never the aim of the process.

d. Ethnographic Delphi Futures Research (EDFR)

Poolpatarachewin (1980) presents a creative synthesis of EFR (Textor, 1979) and the Delphi procedure. This method was planned to integrate the advantages of both procedures, while limiting their methodological weaknesses. Its advantage lies in assuring the intensive involvement of the participants in raising issues that will be considered for a group response, such that the scope and focus of the issues that are examined are not limited or significantly distorted by the bias of the researcher.

The present research focuses on a procedure that combines the advantages of most of the versions of the Delphi method mentioned above, but mainly uses the QCF method, in a manner reflecting the advantage of receiving heterogeneous responses that provide both accepted and creative solutions.

4.3.2 The procedure for choosing participants

The choice of participants is based on the fact that this is a specific group that handles a common issue. Feedback and interaction between the participants is possible in the form of rounds of questionnaires after which the participants are asked:

1. To read the attached forecasts and predictions prepared by the experts;
2. To imagine that the entire group of participants is sitting in front of them and reading the same material;
3. To imagine that they are given the opportunity to ask questions regarding their future in light of the research material that everyone just read;
4. To think about questions that could develop the research subject;
5. To set challenges regarding the motivations and expectations of the participant;
6. To formulate a future problem, in a manner that will challenge the participants and require them to apply their opinions, ideas and goals in order to cope with the situation.

Round one: The researcher may develop a questionnaire based on questions by the participants. Recurring attempts must be made to convince that participants that the reasons for conducting this type of research are:

1. To read the predictions and forecasts that the experts (and they themselves) have prepared.
2. To read the questions and answer them in short.

Round two: The basic goal of the second round is to promote basic reciprocal relations leading to the production of specific ideas that will be recorded as statements or task statements that the group can perform as a redefined goal regarding the issue at hand. Therefore, the questionnaires for the second round must be designed around the statements regarding recommendations for tasks that are described within the framework

of the reporting process. While the participants are completing the first round questionnaire, the facilitator will be organizing the responses that have been received. The facilitator summarizes the responses in reports that are in keeping with the issues at hand. The participants must be presented with these reports and be asked to survey the reports on the first round, and present task statements that will serve as the basis for the creation of the second round questionnaire.

The goal of this round is to organize thoughts and focus the discussion on more specific solutions (1 - preferred solutions; 2 - expected solutions; and 3 - important solutions).

This procedure aims to create some type of agreement regarding an alternative future task: Absolute lack of agreement, multiple opinions, bi-polar responses, a majority, or full consensus. The second round aims to achieve these goals. The first question (preference) aims to draw out a response on a scale of 1-5 (1 – absolutely yes; 2 – perhaps yes; 3 – almost certainly not; 4 – apparently not; 5 – absolutely not). The second question (expectations) also aims to draw out a response on a scale of 1-5 (1 – certainly; 2 – possible; 3 – unsure; 4 – reasonable; and 5 – unreasonable), as does the third question (importance) on a scale of 1-5 (1 – very important; 2 – important; 3 – not very important; 4 – average; and 5 – not important).

4.3.3 The theoretical framework

The procedure reflects a new scientific paradigm that is presented today by researchers of systems theories. This paradigm calls for significance and a new aim for science of the 21st century, based on the belief that scientific institutions must mainly serve humanity in producing reliable and specific applications and not only theoretical hypotheses, no matter how much these hypotheses are based on research.

In the scientific literature, it has been argued that the study of personal visions of the future can take the place of human thinking and help us develop clearer concepts and more reliable specific actions. Humanity is faced with a huge challenge – it must imagine its ideal, and then act to make our imperfect present into the perfect future.

According to the Dutch futurist Polak (1972) we respond as humans to this challenge by creating images of the future. By creating future images we reformulate the boundaries of the unknown, and raise the entire human race to greater heights of conceptualization. We move from the materialistic to the abstract and thus liberate ourselves from the limitations of time and space.

4.3.4 Summary of the method

Bohm and Peat (1987) argue that the divisions and specialization that are increasing in the field of science have led us to a situation in which all activity is loosing its significance. Therefore, they argue, we must change what we call science, and lead to basic changes that will be significant progress towards liberating the wave of creativity necessary if science will actually assist us in coping with the deeper problems of humanity. A combination of two methods was in fact adopted here – the qualitative and the qualitative method. Two groups were chosen due to the complexity of the subject – an inner circle and an outer circle that met a series of questions according to the Delphi method. Each of the circles was weighted differently in a manner that would afford

weight to the extent of the knowledge, understanding and degree of professionalism and expertise in the field of taxation in general and the foreign trust funds in particular.

4.4 The research field

As mentioned above, the research was divided into two circles of respondents: The experts who included six individuals, and the second circle which included an additional 37 individuals.

The research was conducted in the offices of the respondents in northern of Israel. The first circle included the following six participants:

a. A, the deputy manager of an office in Haifa, an accountant and lawyer, highly knowledgeable in the field at hand (with an M.A. on the subject), and a lecturer on taxes regarding this subject.
b. B, an accountant, holding an M.A. degree in Business Administration, the tax manager at one of the largest accounting firms in Israel, specializing in international taxation.
c. C, an accountant and lawyer with a large firm that handles this subject.
d. D, holding a doctorate in law, and an expert in the field, who has written and published many articles on the topic.
e. E, a lawyer and accountant, in the offices of Dr. Avi Alter, the largest law firm handling taxation issues, who helped this researcher with clarifications and materials from their office, regarding this topic.
f. F, the one respondent that the researcher contacted did not respond to all the questions although she is a colleague.

The second circle included the responses of the other 37 respondents, as described above.

4.5 The research objective

The aim of the present research is to examine the new tax reform and highlight how it affects the Israeli economy.

4.6 The research question

Will lowering barriers (decreasing bureaucracy) in the taxation system, and implementing taxation of trust funds abroad encourage investors in Israel and abroad, and encourage the flow of capital into and out of the country?

4.7 The relevance of the research

A study was conducted in 1985 by Dr. Avi Alter, of the Tel Aviv University Faculty of Law, on taxing the income from regular trusts in Israel. Considerable time has passed since the last study that dealt mainly with the legal aspect of trusts and less with macro-economic aspects. Accordingly, the subject should really be reexamined, first because of the lengthy period of time since the study of this subject was conducted, second, change in legislation and the new tax reform in Israel that drastically altered the situation.

4.8 The research tools

Data gathering in the present research was conducted using a combination of quantitative and qualitative research.

4.9 The qualitative research

This part of the research included standard structured interviews containing seven open ended questions:

a. What do you feel is the best way to 'deepen' the country's coffers: Taxing foreign trusts, tax exemption, or decreasing the taxation rate on this investment horizon?
b. Do you think that (financially) Israel will become a tax haven? Why?
c. According to data that you have at hand, has taxing foreign trusts contributed to the state coffers and indirectly led to an improved economic situation in Israel?
d. In your opinion, will/has taxing trust funds caused the escape of capital from Israel?
e. Internal Israeli law often differs from tax conventions signed by Israel with other countries, in which foreign trusts exist. What do you feel will most strongly influence a foreign investor when setting up a trust in Israel?
f. What do you generally feel regarding taxation of foreign trusts in Israel and abroad? Do you feel there are other alternatives that are more suited to the situation in Israel based on other models worldwide?
g. Does the social/political/security climate in Israel affect the creation of foreign trusts abroad, or vice versa (i.e., the creation of foreign trusts in Israel by well to do Jews abroad)?

The interviews that were conducted were scheduled by the researcher. During the interviews the researcher ensured two main conditions:

1. An explanation of the goals of the interview, and assuring respondents' anonymity.
2. The use of clear language.

4.10 The quantitative research

The quantitative research instrument included 32 closed questions and statements for which each respondent was asked to rate his degree of agreement on a Likert scale of 1-5, with 1 denoting a total lack of agreement and 5 denoting a high degree of agreement.

Four new variables were calculated for the research by averaging the responses of the respondents to the items relevant to the variables. Calculation of the new variables allowed testing the research hypotheses and examining the existence of correlations between the variables.

Variable	Items	Alpha Cronbach Reliability
Lowering barriers in the Israel tax system	6, 12, 17, 19, 20, 23, 24, 28, 32	0.6700
Encouraging investors from Israel and abroad	10, 11, 13, 14, 31	0.7344
Taxation of foreign trusts	8, 9, 15, 16, 18, 21, 26, 27, 30	0.7120
Escape of money from Israel abroad	7, 22, 25, 29	0.7693

All worlds of content that denote the research variables were found to be reliable. Therefore variables were calculated for each of the respondents and participants in the empirical study. Additionally, a number of personal characteristics were examined solely in order to characterize the respondents as regards age, gender, marital status, education, and tenure at work.

4.11 The research process

4.11.1 Data gathering

Completion of the questionnaires was conducted in two modes: Some respondents asked to complete the closed questionnaire in their free time, and return it via e-mail, while others completed it after their interview with the researcher.

A preliminary clarifying conversation was conducted with each respondent in order to obtain their agreement to complete the questionnaire, and to assure their anonymity. Each respondent was told what the research topic, what the research goal was and all completed the final questionnaire.

4.11.2 Data processing methods

Data processing was a combination of the qualitative and quantitative research methods. More weight was given to the responses of the first circle of respondents, compared to the responses of the second circle.

Part of the research in the present study is qualitative, using the instrumental case study method. Data processing began during the course of the research, based on the cyclic model of qualitative research in which interviews and documents were analyzed in order to understand the impact of taxation of foreign trusts in Israel over foreign investors, based on the perceptions of Israeli decision-makers.

Analysis of the data was conducted based on the unique nature of the case study as a systemic methodology, including a large number of sub-systems, groups or other cross-sections. From each one of these one may infer meanings, and then connect these to present the holistic case.

Interviews with the participants were analyzed by re-reading the transcripts focusing each time on a dimension relevant to the research.

The other part of the research was quantitative and was analyzed through quantitative data processing, using the SPSS statistical computer program. All of the questionnaire data were introduced to the statistical program and then the distributions of the variables in the questionnaires were analyzed and cross checked through statistical analysis methods.

In order to test the hypotheses through statistical analysis, Pearson and Spearman correlation tests were conducted. In the descriptive section, distributions of socio-demographic traits were examined, including testing the reliability of the research tool.

4.11.3 Reliability and methods of validation

The degree of reliability of a study indicates the degree of variable bias included in the measurement (Nachmias and Nachmias, 2005). The main instrument in qualitative research is the researcher himself.

In this study the researcher composed a questionnaire based on other questionnaires dealing with the topic of decision-making processes. To validate the qualitative and quantitative facets of the questionnaire, it was given to two expert judges, both accountants, who requested some changes in some of the questions both in content and formulation.

In his position as the main research tool, the researcher is aware of his position, his role and his possible influence over the research findings, and therefore maintained continual self-critique and examination, and avoided subjectivity while maintaining objectivity as far as possible.

The researcher used the tactic of construct validity, and diverse research instruments, notably open ethnographic interviews along with gathering documents and theoretical and research literature. Data were gathered and their reliability ensured. The researcher gathered documents from the research participants, assisting them in verifying the data gathered through other research instruments. The researcher also used varied resources and identified significant behavioral patterns regarding the impact of the research on its participants. He used triangulation that assisted him in cross-checking sources of information and identifying similarities and differences between his sources.

4.12 Research ethics

Yizraeli and Zohar (2000) argue that the demand for morality in human society is varied, and moral decisions that an individual makes are based on his conscience, his actions and based on his familiarity with universal moral laws and the social context in which he operates.

Dushnik and Sabar Ben-Yehoshua (2001) argue that qualitative research ethics deal with searching for principles, commitment and characteristics that must guide and typify the appropriate behavior of the qualitative researcher. Qualitative research sets itself the goal of understanding the personal structures that create different realities.

According to Guba and Lincoln (1989) qualitative research bases its research ethics on mutual respect, mutual trust, and cooperation between the researcher and research subjects. This action becomes an essential part of the research, an intrinsic component that may not be separated from the methodological-scientific composition of the study.

Qualitative research creates closeness between the researcher and his subjects, which requires that the researcher cope with a number of ethical dilemmas:

1. Conscious agreement: The researcher has disclosed and provided the participants with full and relevant information regarding the research goals and process, and the risks that are involved when they agree to participate.
2. Privacy and anonymity: According to Dushnik and Sabar Ben Yehoshua (2001), the qualitative researcher is not satisfied by observing his subjects' overt behavior, but wants to learn how the subjects interpret their experiences, and to understand their positions and beliefs, and even to become familiar with their life stories. However, alongside the researcher's desire to access as many levels of the subjects' reality as possible, he is committed to protect their privacy.
3. Mutuality and partnership: In qualitative research, the distance between the researcher and his subjects is smaller, and therefore there is a need to expand research ethics beyond mutuality and partnership in the researcher, with or without the subjects (Dushnik and Sabar Ben-Yehoshua, 2001).

4.13 The research limitations

a. The difficulties that arose during formulation of the questionnaire stem first from the fact that this field has not been examined in the past, and there are no data regarding expected income from taxation of foreign trusts, or its contribution, if at all, to the state's coffers.
b. Additionally, the questions were formulated by the researcher, and based on his familiarity with taxation laws in certain counties of the world, including Israel. Therefore they may reflect his opinion and the opinions of those who responded, some of whom may have an interest or a need to promote the issue.

Thus due to the complexity and uniqueness of the subject of foreign trust funds, there are but a few experts and professionals who can express an opinion based on knowledge and familiarity with the subject.

Hence this researcher considered at length which research approach to adopt: Whether to adopt the qualitative approach, relying on existing studies and literature on the subject or whether quantitative research that would embrace as many participants as possible even if many of them are not fully familiar with the subject. Eventually, and after in-depth study, the researcher chose the Delphi method as the most suitable research tool that in fact combines the two factors, and affords greater statistical weight to the first circle of participants. The chapter reviewed at length the diverse approaches to applying this method, in consideration of the relevant literature on the subject in general.

In addition, he has explained his choice of diverse sample populations in the research field, the way of gathering and processing the data including validating the reliability of the method as well as its limitations. He is convinced that together with the data noted this was the best way to obtain and properly analyze the various opinions.

Chapter Five: The Research Findings

Forty three respondents, all married men aged 36-62 with an academic education participated in the present research. 25 of them work in academia (staff members, and students of advanced degrees in economics and accounting) and 18 are people who work in finance or the legal profession in the field of taxation. Approximately half are from the private sector and half from the public sector .Six of the respondents are experts in this field. The tenure of the respondents ranges from five to twenty-five years

Table no. 1a: Distribution of respondents on the topic of taxing foreign trusts and foreign investors

Statement	Not at all	Very little to somewhat	Greatly to very much
6. The tax regime in Israel is complicated compared to that of other countries	-	75%	25%
7. There is a need to fill in the loophole of non-taxation of foreign trusts	34%	41%	25%
8. The main purpose of foreign trusts is tax avoidance	-	85%	15%
9. The main purpose of foreign trusts is decreasing tax payments	-	83%	17%
10. The main investments of foreign trusts are financial investments	-	50%	50%
11. The main investments of foreign trusts are in real estate or land	-	65%	35%
12. In Israel bureaucracy makes it difficult for foreign investors	-	22%	78%
13. Foreign investors should be given incentive to invest in Israel through tax breaks.	-	-	**100%**
14. Foreign investors should be given incentive to invest in Israel through shortening bureaucratic processes.	-	-	**100%**
15. Taxation of foreign trusts outside of Israel should be included when there is an Israeli trustor or beneficiary	-	15%	85%

The findings in table no. 1a indicate that an absolute majority (100%) of the respondents agrees greatly or very much that foreign investors in Israel should receive leniencies, by providing tax breaks. Similarly, the respondents stated that foreign investors in Israel should be given incentives by shortening bureaucratic processes. Only 78% respondents agreed greatly or very much that the existence of a bureaucracy that makes it difficult for foreign investors. However, regarding a need to overcome the existing loophole in taxation of foreign trusts, there were differences of opinion and 34% of the respondents said there was no need at all to deal with this issue,

41% said there was very little to some need to deal with the issue, while 25% felt there was a great or very large need to deal with the issue.

50% of the respondents stated that the main investments of foreign trusts in Israel were financial and/or in real estate and land.

65% of the respondents think very little or somewhat ,that trusts are established for tax evasion. However, 15% of the respondents greatly or very greatly feel this is their purpose.

Table no. 1b describes the distribution of frequencies of respondents regarding questions 16-22.

Table no. 1b: Distribution of respondents regarding taxation of foreign trusts and foreign investors

Statement	Not at all	Very little to somewhat	Greatly to very greatly
16. Taxation of foreign trusts abroad will decrease the rate of reporting in Israel	25%	25%	50%
17. Taxation of foreign trusts in Israel will lead to decreased income from taxes.	5%	75%	20%
18. Taxation of foreign trusts abroad when the trustor or beneficiary are Israeli, will decrease taxes in Israel	10%	67%	23%
19. Lowering barriers in the taxation system for investments in foreign trusts will encourage foreign investors in Israel	-	5%	**95%**
20. The benefit from removing barriers is greater than the "tax loss" that will be caused by not applying taxes.	-	-	**100%**
21. Taxation of foreign trusts abroad is in conflict with taxation laws abroad and tax conventions with them.	-	55%	45%
22. There are other more important incentives than tax considerations when establishing a foreign trust.	10%	30%	60%

The findings in table no. 1b indicate an absolute majority (100%) of respondents who greatly or very greatly agree that removing barriers is more beneficial than the tax loss that will be incurred by not taxing. 95% of the respondents think that lowering barriers in the taxation system regarding taxation of foreign trusts will be greatly or very greatly encouraging.

Taxation of foreign trusts abroad was mentioned most frequently in the research questionnaire. The existence of taxation alongside tax laws in other foreign countries, while decreasing tax on the trustor or the beneficiary, leading to a decrease in taxation in Israel or a decrease in the rate of reporting in Israel, was supported by the respondents equally in the range from not agreeing to agreeing very much, in a similar fashion.

Ninety-five percent of the respondents think that taxation of foreign trusts in Israel will lead to a decline in income from taxes, but only to a small degree.

Table no. 1c describes the distribution of frequencies of responses for statements 23-32:

Table no.1c: Distribution of responses regarding taxing foreign trusts and foreign investors

Opinion	**Not at all**	**Very little to somewhat**	**Greatly to very much**
23. The new tax reform (of 2003) did not handle taxation of foreign trusts because of the complexity of the issue	-	5%	**95%**
24. The new tax reform (of 2003) did not deal with application to foreign trusts because of the difficulty of reporting and collecting the tax	30%	70%	-
25. There is no taxation differentiation between foreign trusts including an Israeli (or foreign) trustor, beneficiary or trustee investing and operating abroad, and between those operating in Israel	62%	12%	26%
26. If foreign trusts are not taxed this will cause annual losses to the state treasury.	32%	38%	30%
27. If foreign trusts in Israel are not taxed, the country will become a "heaven" for foreign investors.	-	40%	60%
28. If foreign trusts are taxed, the tax burden between different strata of the population will be somewhat leveled	35%	65%	-
29. Reporting and collecting taxes on foreign trusts operating abroad cannot be enforced.	11%	15%	74%
30. If tax collection can be enforced the cost will outweigh the benefit	13%	71%	16%
31. If the instructions for taxing foreign trusts abroad are applied, this may cause legal disagreement with countries in which trusts have been established (i.e. USA, Britain, Australia, etc.)	35%	45%	20%
32. The tax regime in Israel is a function of social ideology	32%	55%	13%

Three statements stand out in the frequency of responses at different levels: The position of respondents regarding taxation of foreign trusts not mentioned in the tax reform of 2003, the position of respondents regarding enforcement of tax collection, for which the cost will be higher than the benefit, and the position of respondents regarding the fact that the tax regime in the state is a function of social ideology. Regarding the first statement, the majority (95%) stated that they greatly support it. Regarding the second and third statements, there was a majority of 70% who agreed only very little or somewhat.

The main findings related to table no.3 are that the respondents in general think that the new tax reform of 2003 did not deal with taxation of foreign trusts at all or only little because of the complexity of the issue. Some feel that difficulties in reporting and collection of the tax are the reason for this lack. Forty percent feel that the difficulties should be attributed to other issues that were not mentioned.

<u>As mentioned is section 4.7 the research hypotheses in this study are</u>:

1. Lowering the barriers within the Israeli taxation system will encourage investors in Israel and abroad.
2. Taxing foreign trusts abroad will lead to money escaping from Israel abroad.

Testing the research hypotheses was possible using Pearson correlations between the research variables.

Table no. 2 describes the correlations that were calculated

<u>Table no. 2: Matrix of correlations between the research variables</u>

	Lowering barriers in the Israeli taxation system	Perception encouraging investors in Israel and abroad	Taxation of foreign trusts	Money escaping from Israel abroad
Lowering barriers in the Israeli taxation system		.378(*)	.120	-.406(**)
Perception encouraging investors in Israel and abroad			.668(**)	.118
Taxation of foreign trusts				-.502(*)
Money escaping from Israel abroad				

*p<0.05; **p<0.01

The findings in the matrix (table no. 4) indicate a significant correlation between lowering barriers in the taxation system in Israel and between the positions of respondents regarding encouraging investors in Israel and abroad (rp=0.378; p<0.05). This means that the lower the barriers will be in the taxation system in Israel,

the more Israeli and foreign investors will be encouraged to invest in Israel, and *vice versa.*

Lowering barriers in the taxation system in Israel may certainly prevent money escaping from Israel abroad, to a statistically significant degree ($rp=-0.406$; $p<0.01$). The lower these barriers become, the more active the encouragement will be to reduce the amount of money escaping from Israel abroad. This correlation is also correct in the opposite direction, as some or non-lowering of barriers may contribute to an increase in the amount of money escaping from Israel abroad, and in frequency of such cases.

Taxing foreign trust funds will encourage investment in Israel and abroad ($rp=0.668$; $p<0.01$). Actually, taxation can explain approximately 40% of all of the changes that will occur in investments in Israel or abroad. However, no significant correlation was found between implementing taxation of foreign trusts funds and between lowering barriers in the Israeli tax system.

Implementing taxation of foreign trusts will help to prevent the escape of money from Israel ($r=-0.502$; $p<0.05$).

Table no. 3: Matrix of correlations between items in the research questionnaire

	The main investments of foreign trusts in Israel are financial	The main investments of foreign trusts are in real estate or land	Foreign investors must be given incentive to invest in Israel with tax leniencies	Foreign investors in Israel must be given incentive to invest in Israel by shortening bureaucracy	If tax instructions for taxing foreign trusts abroad are applied there may be legal disagreement with countries in which the trust was created
Bureaucracy in Israel makes it difficult for foreign investors in Israel	**-0.816(*)**	0.548	-0.433	0.000	-0.739
The benefit of removing barriers is greater than the tax loss caused by not applying it	-0.333	**0.894(*)**	0.000	0.000	**-0.905(*)**

The results shown in table no. 3 indicate three significant correlations: A significant negative correlation was found between the perception of the respondents regarding bureaucracy making it difficult for foreign investors in Israel, and between their perception that the main form of investments in foreign trusts in Israel are financial

investments ($rp=-0.816$; $p<0.05$). The significance behind this correlation is that respondents who feel the existence of bureaucratic difficulties for foreign investors in Israel, perceive these investments to be less in the financial arena. The greater the difficulty in investing, the fewer financial investments there are, and *vice versa.* This is a strong correlation.

Additionally, a significant positive and strong correlation was found ($rp=0.894$; $p<0.05$) between perception of the benefit of removing barriers, and between the perception of respondents regarding the main investments of foreign trusts in real estate or land. The significance of this correlation is that removal of barriers will direct more foreign investments from real estate or land to other horizons.

A third strongly significant correlation ($rp=-0.905$;$p<0.05$) was found between the perception of the benefit of removing barriers and between the respondents' perceptions regarding the legal disagreements that may arise with other countries in which foreign trusts have been established, in the event that the laws of taxation of foreign trusts abroad are applied. This negative correlation indicates that the greater the benefit is perceived, the lower the chance is to cause legal disagreements with countries in which trusts have been established, and *vice versa.*

Table no. 4: Matrix of correlations between research questionnaire items

	There is a need to close the loophole of non-taxation of foreign trusts	There are other more important incentives than tax considerations when creating a foreign trust	Taxing foreign trusts in Israel is similar to taxing trusts operating abroad	Reporting and collecting tax on foreign trusts abroad cannot be enforced.
The main goal of foreign trusts is tax avoidance	0.796	-0.518	**0.883(*)**	-0.622
The main goal of foreign trusts is lowering tax payments	0.381	-0.586	**0.875(*)**	-0.777

Two further significant correlations were found between the questionnaire items composing the second hypothesis.

A positive significant correlation ($rp=0.883$;$p<0.05$) was found between the respondents' perceptions of the main goals of trusts as used for tax avoidance, and between their perception of the taxation similarity in Israel and abroad. Collection of tax abroad is similar to the collection of tax on foreign trusts in Israel. The more the common opinion is that establishing trusts is tax avoidance the more common the perception is that collecting tax on trusts abroad is similar to collecting tax on foreign trusts in Israel.

Additionally, a significant positive correlation was found ($rp=0.875$; $p<0.05$) between the respondents' perceptions of the main goals of foreign trusts to decrease tax payments, and between their perception of the similarity of taxation of foreign trusts in Israel and abroad. A higher perception of the goal led to greater discernment, and *vice versa.*

5.1 Summary of the qualitative research – open questions

In order to examine the qualitative section of the research, the answers to the open questions are summarized.

Question 1: What do you think is the best way to 'deepen' the country's coffers: Taxing foreign trusts, tax exemption, or decreasing the taxation rate on this investment horizon?

Respondent A: A tax exemption or lower tax rate should be applied to this investment horizon. Taxation of trusts created by Israeli residents versus encouraging trusts created by foreign residents, to use Israel as a base of operations. The money that will flow to Israel will move into new industry, and into providing services to the trusts.

Respondent B: This will lead to the flow of money and activity in Israel, it will create growth and a higher rate of tax collection.

Respondent C: Encouraging investments of foreign residents in Israel, among other things, by providing tax breaks will encourage the flow of money that will get the ball rolling regarding accompanying financial services, such as attorneys, accountants, financial institutes, etc.

Respondent D: In the Western world there has been insight that tax is a barrier to the foreign trust system. The state coffers will become fuller from derivatives of managing a trust from Israel.

Respondent E; Taxing foreign trusts will lead to lowering investments from foreign entities within Israel.

Question 2: Do you think that (financially) Israel will become a tax haven? Why?

Respondent A: It would be very dangerous for Israel to appear on the black lists of countries or organizations such as the OECD. The number of investors would decline because the foreign tax authorities tend to be strict when auditing trusts in tax havens. Israel should become a solid place for trust activities by decreasing bureaucracy, getting rid of the haze surrounding reporting laws for foreign trusts, giving tax breaks for activity outside of Israel, and providing full exemptions for income from the financial system within Israel.

Respondent B: Yes the Israeli economy would grow from this.

Respondent C: The benefit of this *versus* the disadvantages should be carefully examined, and therefore it is recommended to first examine how to lower the tax obligation and simplify bureaucratic processes, as was done in Ireland. Second, the implications of exemptions from reporting foreign trust activity abroad should be examined, along with providing tax leniencies for accompanying financial activity.

Respondent D: This is not desirable because it is against the policy of the OECD, that Israel has wanted to join over the past years.

Respondent E: Israel has tax conventions with many countries that tax citizens, and therefore a tax haven is not good, and would cause other countries to cooperate with Israel.

Question 3: According to data that you have at hand, has taxing foreign trusts contributed to the state coffers and indirectly led to an improved economic situation in Israel?

Respondent A: It has not contributed because foreign trusts are waiting for the obligation for reporting that are now hazy and are not clearly formulated. If rigid reporting obligations are applied, with a requirement to uncover information about activities outside of Israel, the trusts will transfer their activities to a different country. In all areas related to Israeli trusts outside of Israel, it is too early to express an opinion as the law is still new and there are still no clear indications of all of the tax loopholes that may built into the new law. There is not yet any clear indication of the scope of actual reporting rates either.

Respondent B: I do not know

Respondent C: At this stage there is still not enough data on foreign trusts in Israel because the law only went into effect in 2006. The investors are waiting for the obligation to report, yet to be published, for foreign trusts outside of Israel for which the beneficiary or trustor is an Israeli resident. It is too early to determine because the scope of reporting has not yet been determined, and also, there is still no knowledge regarding tax evasion tactics.

Respondent D: I do not have any empirical data.

Respondent E: I have no idea.

Question 4: In your opinion, will/has taxing trust funds caused the escape of capital from Israel?

Respondent A: In all things related to trusts by foreign investors the answer is positive. There are enough decent countries that court foreign investors and their money.

Respondent B: Not in a significant manner.

Respondent C: It is necessary to differentiate between foreign investors and Israeli investors. It is reasonable to assume that foreign capital from foreign investors will make its way outside of Israel.

Respondent D: Yes. In general, capital flows throughout the world and seeks high yield rates and low/exempt tax rates.

Respondent E: I do not know, but it is reasonable to assume that capital invested in Israel will decrease as a result.

Question 5: Internal Israeli law often differs from tax conventions signed by Israel with other countries, in which foreign trusts exist. What do you think will most strongly influence a foreign investor when setting up a trust in Israel?

Respondent A: Bureaucracy – the obligation for reporting income in Israel, and mainly the banks in Israel, the obligation to report income outside of Israel, exemptions for financial income from financial institutions in Israel, the possibility for setting up trust companies, contact with the authorities.

Respondent B: Increased belief regarding internal law and therefore the considerations of the investor will be a test of the convention.

Respondent C: First of all Israeli bureaucracy, and second taxation rates. Third, the heavy obligation to report.

Respondent D: There is no doubt that a rational investor will examine the implications of the covenant over such an investment.

Respondent E: I think internal law, and particularly bureaucracy, will prevent foreign trusts from investing in Israel.

Question 6: What do you generally think regarding taxation of foreign trusts in Israel and abroad? Do you think there are other alternatives that are more suited to the situation in Israel based on other models worldwide?

Respondent A: Taxation of trusts among Israeli residents is marching towards closing loopholes. In many cases, trusts created by Israeli residents are for the purpose of tax evasion. In the coming years, we will certainly see additional amendments to the law for closing loopholes that arise.

In all things related to taxing foreign trusts in Israel, there is a trend towards being strict and requiring full reporting of assets and income in Israel even if the individual was exempt from reporting, such as in the case of bank accounts. There is a requirement to obligate a beneficiary, who is a resident, to report the distribution of assets in Israel, and there is a similar obligation for trustors. This trend will lead to wasting an opportunity to promote the status of Israel as a financial center.

Respondent C: More than other countries around the world, Israel is characterized by creating trusts for tax planning purposes. However, rules pertaining to foreign trusts have changed in comparison with the situation in the past, i.e., making the rules of reporting more difficult for assets and income in Israel, that in the past were exempt from the obligation to report (such as bank accounts of foreign residents). These trends may cause foreign capital to escape (particularly amongst Jews from abroad).

Respondent D: I think there should be no difference where the trust is managed or what the identity of the trustor/beneficiary is, so that tax planning does not come into account when creating the trust.

Respondent E: I think taxing of foreign trusts abroad will not have an impact, but taxing foreign trusts in Israel will lead to lower investments in Israel.

Question 7: Does the social/political/security climate in Israel affect the creation of foreign trusts abroad, or vice versa (i.e., the creation of foreign trusts in Israel by well to do Jews abroad)?

Respondent A: The establishment of trusts by rich Jews has been accepted for many years, and is only slightly affected by the situation in Israel. It is affected much more by the personal and familial status of the trustor, and political influences within his country of residence. Regarding establishing trusts by Israeli residents, this issue has not been developed enough, and sometimes trusts serve, not for their original purpose, but for tax planning. Right now, after the law has created more certainty regarding taxation – perhaps proper use will be made of this financial entity.

Respondent B: I think that the security situation affects the establishment of foreign trusts in Israel, and vice versa.

Respondent C: The political and security situation have not had much influence in the past over Diaspora Jews investing in Israel (see for example the Iscar deal and the

purchase of large Israeli companies by foreign companies). What has more of an impact is the financial situation and taxation laws. Certainty or uncertainty regarding foreign trust law is just another part of creating a clearer picture for a potential investor.

Respondent D: I have no doubt that the political, social and security situations do affect the investment culture of any given country, and Israel also. Money looks for certainty in order to be "fruitful".

Respondent E: The security factor is the only one that has influence among the three mentioned above.

Question 8: According to a study named "The impact of physical policy over the growth rate of the economy", it was proven that lowering tax rates increases growth, contributes to the flow of foreign capital from abroad, and encourages true reporting of income (as opposed to high tax rates that lead to tax evasion). Express your opinion.

Respondent A: I think that this claim is quite correct. Lowering the tax rate together with better enforcement of collection will encourage economic activity in the economy and will not lower, but may even raise, the total sum of tax collection.

Respondent B: Very true. It is time for the Treasury to set policy accordingly.

Respondent C: I think that lowering the tax rate will also reduce the desire to evade taxation, the profitability of tax evasion (under the condition that punishment becomes more severe, and enforcement is increased, as in countries such as Italy and the US). In addition, lowering tax rates will increase income from taxation because more people will begin to report their income.

Respondent D: I think that the argument is correct. Lowering the tax rate along with better enforcement of collection will encourage economic activity in the economy and the net result will not be less, but even more tax collection.

Respondent E: Reasonable and less identical taxation rates, as are common in the western world, will significantly lower the profitability of tax evasion, which is derived from friction with the tax system and the bureaucratic burden, together with financial profit. When friction is high and there is a basic lack of trust of the authorities, the cost of handling the payment of tax – the amount of time and the number of experts involved – is high. If in addition, tax rates are high, the taxpayer will often prefer to avoid the emotional and financial burden of contact with the authorities, and will conceal his income. When the tax rates are low, and the cost of handling taxes is low (less bureaucracy, and the process of reporting foreign income is shortened), the taxpayer will think twice before committing a crime and hiding his income. It is specifically the high income brackets that are given the incentive to report when the tax rate is low, because it is difficult to use large sums of 'dirty' money without being discovered. However, if the money was clean, the taxpayer could use it without worry.

Respondent F: I think this is true. When the tax rate is low, the risk of tax evasion (if there is an enforcement and punitive system) is high, and therefore the motive for tax evasion will be lower. In addition, lowering tax rates will encourage the flow of foreign capital from abroad, and this will lead to stability in the local economy.

Question 9: What is your opinion on establishing a tax exempt trust fund aimed to reinforce the field of national activity (i.e. national infrastructures, such as – rehabilitation of the north, developing the Galilee or Negev, water channels, etc.)?

Respondent A: In general, I think positively. Tax exemption is an alternative for direct investment in the country. Investment by private entrepreneurs is generally more efficient. Of course it is necessary to closely examine what projects are given exemptions and to estimate the degree of contribution of such projects to the economy.

Respondent B: Interesting idea. Application should be looked into.

Respondent C: I think that such a possibility should be looked into (similar to national projects based on B.O.T. business enterprises). This would no doubt lead to growth of the economy in the long term, as during a time of relative recession, resources will be directed towards national projects, as occurred in the US in the 1930s, with the great amount of growth that occurred as a result.

Respondent D: I think that the statement is a correct and logical assumption both financially and psychologically, as we begin with the assumption that the more free income we have, the more it will contribute to growing consumption and growth, which will finally lead to lowering interest in income tax evasion.

Respondent E: I think that this way of thinking is correct, as it will lead to growth and improvement of infrastructures. Today strategic investment tracks (regarding the government) in specific factories, are managed according to a similar model, but not in infrastructures, only in industry.

Question 10: What changes in legislation do you think are necessary for use of trust funds for national purposes and not family purposes to begin to move ahead?

Respondent A: I think that a specific law must be legislated for this purpose, authorizing a specific body, composed of representatives of the government, the business sector, and the banks, to award this exemption according to guidelines that are determined by law.

Respondent B: A regulative system must examine the goals of the trust fund and their application through legislation.

Respondent C: I think that incentives given to this type of trust funds as given to charity funds, will promote the aim.

Respondent D: I think that there is room for this in order to improve quality of life and good infrastructures that will be the basis for investments coming from abroad.

Respondent E: For national goals, I agree with turning trusts into an acceptable method for creating a charity organization. Trusts are not suitable for project management on a national level. The main issue today is the haziness surrounding the status of trusts for charity purposes. While the trust committee recommended legislation of a special track for charity funds, the legislature chose to ignore this recommendation and leave trusts without any clear recourse. Today, the option is open through section 9(2), that is too complicated for my tastes, and not clear cut, as it should be. If the law discussed the creation of tax exempt trusts for needy groups, the country would benefit because belief in these institutions would increase, the degree of responsibility of the managers (trustees) would be much higher than the degree of responsibility of managers of random charity organizations, and money management would be done mainly by professionals, and not managers who are not experts in the field.

Respondent F: Changing legislation in the following areas: Tax exemption anchored in income tax ordinances, pre-ruling, or some such step.

Question 11: How would you improve the model? Or: What do you think is the best model to maximize growth of the public "pie" for the benefit of the state's coffers (as a means), and the benefit of the citizenry, and improving quality of life (as a goal)?

Respondent A: Significantly lowering taxes, minimal government intervention, and massive investment in education that would bear fruit in the long run.

Respondent B: The desired model can be seen in Ireland.

Respondent C: I feel that it would be worthwhile to look into the Czech model that attracted 1,200 foreign owned companies providing employment for 280,000 residents, and providing over 65% of the annual industrial export.

Foreign companies and investors are eligible for a reduced taxation rate of 25%, and for other benefits such as:

1. Full exemption from tax for 5 or 10 years;
2. Grants for training and re-training employees;
3. Grants for creating employment;
4. Government support for developing infrastructures.

Respondent D: I think that the B.O.T. model can be used, such that investment in national projects will not be a burden on the country and will not be given to political influences at the time of authorization. Therefore I feel that the idea is excellent: It will contribute to the flow of foreign capital, will encourage investments from abroad and Israeli investors, and money will be turned towards horizons that will encourage the economy and growth in the long term.

Respondent E: I would like to see Israel as the national center for trusts, with the legislature trying to create a climate that is comfortable for activity, without damaging its right to ensure that malignant use is not made and no cheating occurs regarding the tax benefits that it provides. Charity trusts worldwide, and family trusts also hold onto huge sums of money. If the State of Israel gives these trusts a tax exemption in Israel, after ensuring that there are no Israelis involved, the Israeli banks and Israeli professionals will benefit, and the Treasury will benefit from the taxes. Flow of cash inwards can have positive side effects, such as investment of trusts in local real estate, stocks, and bonds, contributing to public institutions, and to the needy in Israel.

Respondent F: I think the model that will maximize increasing the 'pie' could be the fund-trust model that will channel moneys to the benefit of the citizen and his needs. This of course must be done with supervision and guidance of a public organization, and authorization of each program with the possibility for guiding the goals and aims, i.e. decentralization of investments according to various national aims (not only roads, but also education, health, assistance for small businesses that are the backbone of the economy, etc.).

In conclusion -51% of all the respondents further noted they would recommend to invest in Israel if the trust fund is foreign, in a country that does not have a treaty with Israel, as assets in Israel will enjoy leniency in taxes. An example of this is leniencies in the rates of tax on interest and dividends (such as those in Holland that enforce tax at the rate of 5% compared to the British Virgin Islands with 20% taxation). Accordingly they will pay a similar rate as in Holland as a condition that they submit a declaration of not being an Israeli resident that enjoys such.

65% of the respondents said that benefits can be afforded in other ways such as:

1. An increment to the trustee's salary (paying less tax on his income)
2. Delaying tax on income from the trust for several years
3. Delaying paying tax on income until the sale of the trust assets
4. Awarding benefits as tax to all those involved in managing the foreign trust (banks, accountants, lawyers, and other free professions in order to encourage drawing foreign funds to invest in Israel, since the cost of their administration will be lower compared to other countries).

Chapter Six: Discussion

6.1 General

In this dissertation the researcher focuses on a true problem that faces every economy in the modern world in general, and the Israeli economy in particular. How is it possible to improve the quality of life, and standard of living of the individual (citizen), and what means/aims can be used in order to achieve this in the best possible manner, both for the individual and for the State?

The question is, What is preferable? Taxing investments such as foreign trust funds that until now have not been taxed? Or perhaps providing incentives and removing barriers, which may lead to the flow of foreign capital into the economy?

A study conducted in Israel by Shidlovsky and Sarel (2006) examines the impact of fiscal policy on the rate of growth of the Israeli economy. It explored the main channels *via* which taxation and government expenditure could influence the growth rate of the economy. It also presents empirical testimony regarding the connection between the tax burden and the scope of government expenditure, and the growth rate.

The empirical testimony regarding taxation includes surveys conducted among business-people, testing cross-sections of various countries, and the use of various growth rate models. Additionally, it presents various analyses of the impact of taxation on the growth rates of small firms, the impact of consumer tax *versus* income tax, and a sectorial examination of the impact of taxation on employment opportunities, investment rates, productivity, positioning of companies, scope of tax evasion, etc., and finally, details the findings regarding the situation in Israel.

6.2 The main findings and their discussion

This researcher would like to present the main findings for further consideration, referring to the eleven open questions that were posed in the qualitative section of this study.

The first question discussed the opinions of the respondents regarding enrichment of the country's coffers. Each respondent provided a different answer, but together, the responses may be summarized as follows:

1. An exemption or significant leniency should be given in taxation of this investment horizon.
2. The money that will be brought into Israel will motivate an entire industry for service provision.
3. Tax leniencies will contribute to cash flow and increased activity which will lead to growth, and therefore tax collection will increase. The country's coffers will be enriched by the derivatives of the trust fund industry.
4. Taxing trust funds will cause the escape of foreign investments.

The second question referred to the question of whether it is financially desirable for Israel to become a tax haven. 83% of the respondents think that this is a dangerous step for Israel because it is in opposition to the policy of the OECD, that Israel would like to

join. Moreover, the number of investors will decrease because foreign tax authorities tend to be stricter when auditing trusts in tax havens.

The third question pertained to how the respondents think taxation of foreign trusts could contribute directly to improving the Israeli economy. Most of the respondents agreed that since the law only applies as of 2006, there is not enough information to form an opinion. Additionally, since there is still no significant activity regarding the obligation to report, the scope of contribution cannot yet able be estimated.

The fourth question was concerned with the issue of whether taxing trusts would lead to the escape of capital from Israel. 50% of the respondents think that capital would in fact escape from Israel because there are enough other countries that court foreign capital, or *vice versa*, capital searches for higher yield rates and lower tax rates or exemptions. 33% of the respondents said that there was not enough data to answer the question and 17% responded that they did not think that this was a significant factor.

The fifth open question dealt with how tax laws in other countries affect the considerations of investors. 67% of the respondents said that bureaucracy involved in reporting income and contact with the tax authorities made it difficult for investors. 50% of the respondents felt that tax rates do not have any impact. 33% think that tax conventions are a consideration behind investors' decisions. 17% mentioned the difficulty of the obligation to report.

The sixth question discussed alternatives to foreign trust taxation based on other models worldwide. The respondents answered that the strict rules in Israel may:

1. Lead to loss of opportunities to promote Israel's status as a financial center
2. Cause the escape of foreign capital particularly that of wealthy investors abroad.

The seventh question explored the political, social and security climate in Israel and its implications regarding the establishment of foreign trusts. 83% of the respondents think that only the security situation impacts the establishment of foreign trusts in Israel, to some degree or another. However, they mentioned that the establishment of trusts by wealthy investors from abroad has been generally accepted for many years and is only slightly affected by the security situation in Israel.

The eighth open question dealt with a study that was conducted (cited in the previous chapter) proving that lowering tax rates increases growth, contributes to the flow of capital from abroad and encourages true reporting of income. 100% of the respondents accepted the research results and think:

1. That lowering tax rates along with increasing enforcement will encourage financial activity and will finally lead to an <u>increase</u> in tax collection.
2. This will limit the cycle of reporting income.
3. This will encourage the flow of foreign capital from abroad accompanied by stability in the local economy.

The ninth question investigated the issue of foreign trusts in a specific national area of interest being exempt or benefiting from lower taxation rates. 83% of the respondents think that this was an interesting idea that should be examined before applying. 17% said that the idea behind trust funds was more suitable for other horizons and not suitable for management of national projects.

The tenth question dealt with the changes in legislation necessary in order for trust funds to serve national purposes to move forward, to encourage less use for private purposes. 67% of the respondents answered that changing the law, particularly in tax exemptions or pre-ruling authorization, could promote this type of step.

Additional steps that could promote this issue are specific legislation and the establishment of a regulatory body to plan the goals of trust funds and their actual application.

17% of the respondents answered that the problem that exists today is the haziness of the status of trust funds for charitable purposes. While the Trust Committee recommended legislation of this type of taxation the committee chose to ignore the issue and be strict regarding legislation.

The existing legislation today is Section 9(2) of the general Israeli ordinance and is not easily understandable.

The country will profit in the event that a law is legislated that considers needy groups, since the attention provided by the responsible institutions will be far greater than the responsibility of the managers of random charity organizations, and financial management will be more professional.

The eleventh research question explored how the model may be improved and what models would be desirable according to the respondents, in order to increase the "public pie" and improve quality of life. The responses to this question were varied:

1. Lowering tax significantly and lowering government involvement to encourage growth.
2. Referral to existing models in other countries such as the Czech Republic and Ireland. Based on the Irish model, government involvement is low and every entrepreneur has <u>one address</u> to turn to, not like in Israel where many bodies are involved, such as the investment center, the Ministry of Industry and Trade, the Income Tax Authority, the Ministry of Employment, National Insurance, VAT, banks, etc.
3. Intelligent use of the BOT model, which would allow exemption from tax for a period of 25 years, if a project of national importance is created. The entrepreneur enjoys tax exemption or a significant tax break during this period, after which he has a number of options, such as returning the enterprise to the state or taxation under regular conditions.
4. Making Israel into a natural center for trusts and the creation of a comfortable climate for such activity. Charity trusts and family trusts hold large sums of money and if Israel gives a tax exemption, much money will enter the country. This cash flow will create positive impacts, such as investment in local assets, tradable and non-tradable stocks, contribution to Israeli institutions and the needy of Israel, development of local economy through expanding the work force among industries accompanying trust funds.
5. Channeling and guidance of a public non-profit organization that will examine each possible form of such investment. The organization will have the ability to determine to which purposes the monies will be channeled, such as towards national projects in the fields of health, education, small businesses, etc.

6. Adoption of the Czech model that managed to attract thousands of foreign companies some of which invested in foreign trusts, and that managed to create employment for over 280,000 residents, affecting two thirds of industrial export. Foreign companies and investors are eligible for a reduced taxation rate of 25%, and for other benefits such as:
    1. Full exemption from tax for five or ten years.
    2. Grants for training and re-training employees.
    3. Grants for creating employment
    4. Government support for developing infrastructures

6.3 Discussion of the impact of government investments

Aschauer (1989) differentiates between government consumption and investments in infrastructures, affecting capital inventory in the economy. Government assets are found to have a positive impact on growth. In an earlier study (1988) he finds that the impact of government consumption on the GNP is lower.

Levine and Renelt (1992) examine the relationship between economic policy and political and institutional factors and between the average growth rate in the long term. Their conclusion is that the impact of fiscal variables over investments is not significant.

Easterly and Rebelo (1993) reveal that public investment in transportation and telecommunication has a positive impact on growth rates, while the impact of other fiscal variables on growth is weak.

Recently, "new" growth models have been developed according to which fiscal policy may have a permanent impact over long term growth rates (Barro, 1990, 1991; King and Rebelo, 1990). These models emphasize the impact of government expenditures on productivity. King and Rebelo (1990) emphasize the distorting influences of taxation over the rate of economic growth, while Jones, Manuelli and Rossi (1993) find that government expenditure that increases investment in the economy has a clear positive influence on growth.

6.3.1 The impact of government expenditures and tax burden on growth in Israel

In order to independently test the influence of government expenditure and tax burden over growth rates, Shidlovsky, and Sarel (2006) conducted an empirical examination between 1990-2000 using data from 16 developed countries. The examination was based on linear regressions of a cross section, with the explained variable being the rate of growth per capita during the period.

The two main explanatory variables whose impact on growth rates were examined were government expenditure and tax burden, both as a percentage of the GNP at the beginning of the period.

The main findings indicate that government expenditure has a detrimental influence on growth rate, while it is not affected by the overall tax burden (after government expenditures was already taken into consideration). In light of this, the size of government expenditure (as a percent of the GNP) enter all of the equations in a

negative and significant manner, whereas the size of the tax burden (as a percent of the GNP) does not enter significantly into any of the equations (see graph no. 3).

Possible explanations for these phenomena are:
1. The tax burden is actually determined by government expenditures.
2. The overall tax burden may not be a good enough indicator and what affects growth are variables such as marginal tax rate or tax composition.

The empirical examination by Shidlovsky and Sarel (2006) reveals that lowering government expenditure by five percentage points, from 55% to 50%, may increase the GNP at the end of 10 years by 1.5% (close to $2 billion, in terms of Israel in 2003). It is not possible to examine the impact of overall taxes on growth as it may be caused by either marginal tax rates or the composition of the tax.

Chapter Seven: Summary, Conclusions and Recommendations

7.1 Summary

Many studies relate to the impact of type of tax on growth rates. Almost all find that increasing income tax is a factor that harms growth.

The influence of taxation on growth may be estimated by relating to the impact of tax on individual behavior in areas that influence growth, such as employment opportunities, human capital, investments, technological growth, geographical position, tax evasion, etc. An analysis of the results of the components of individual behavior finds that the size of the tax burden affects individual behavior in a manner that harms economic growth as follows:

1. There is a negative correlation between tax rates and investments.
2. The tax system affects the migration of companies between countries or the move of businesses between subsidiaries positioned in different countries.
3. Tax evasion rates are estimated as high and affected by tax rates.

Most of the literature that examines the correlation between government expenditure and growth rates indicates:

1. A negative correlation between the scope of government expenditure and funding methods and between economic growth rates.
2. Lowering company profits and individual profits, and even trust fund profits in our case, lowers the scope of investments and the growth rate accordingly.
3. Investments in infrastructure capital and human capital have a positive influence over growth rates.

The statistical analysis, based on table no.1a, finds respondents agreeing that it is necessary to provide leniencies to foreign investors by providing tax breaks. Similarly, they noted that foreign investors in Israel should be given incentives through shortening bureaucratic processes. The existence of such bureaucracy was agreed upon by 78% of the respondents, to a great or very large degree. Opinions were split on the need to tax foreign trusts as regards the need to overcome the existing loophole in taxation laws regarding taxation of foreign trusts, Two of the respondents felt that there was a small to intermediate need to take this step, and that there was no need to do this at all. Fifty percent of the respondents noted that the investments of foreign trusts in Israel are mainly financial investments and 65% in real estate and land. Eighty-five percent of the respondents thought that the investments of foreign trusts in Israel were either financial or in real estate and land. Eighty-five percent of the respondents also thought that the goals of trusts were to avoid tax, and only one third of the respondents thought that trusts are established for different reasons.

The findings of table no. 1b indicate that all the respondents agree that removal of barriers is preferable to the alternative of loss of taxes that would be caused by the actual taxation. Most of them felt that lowering barriers would encourage foreign investments in trust funds.

According to table no. 1c the respondents think that the cost of enforcement is higher than the purpose that it serves. Their approach is that the tax regime in Israel is a function of a social ideology, and many of them (about 60%) agree that difficulties in reporting and collecting taxes are the reason that the new tax reform did not handle this problem.

The findings of table no. 2 indicate a significant correlation between lowering barriers in the taxation system in Israel and between the positions of respondents regarding encouraging investors in Israel and abroad ($rp=0.378$; $p<0.05$). Lowering barriers certainly may prevent money escaping from Israel abroad, to a statistically significant manner ($rp=-0.406$; $p<0.01$). Taxing foreign trust funds will encourage investment in Israel and abroad ($rp=0.668$; $p<0.01$). Actually, taxation is able to explain approximately 40% of all of the changes that will occur in investments in Israel or abroad. However, no significant correlation was found between implementing taxation of foreign trusts funds and lowering barriers in the Israeli tax system. Implementing taxation of foreign trusts will help to prevent the escape of money from Israel ($r=-0.502$; $p<0.05$).

Based on table no. 3 three significant correlations are found:

1. The respondents think that the greater the bureaucracy in Israel for investors, the more financial investments decline.
2. Removal of barriers will direct more foreign investments into real estate or land.
3. The greater the benefit of removing barriers is perceived, the lower the chance for legal disagreements with countries in which trust funds are made or monies have flowed for the establishment of trust funds within Israel.

Table no. 4 shows a significant positive correlation between the perceptions of the respondents regarding the goals of foreign trusts as a means for avoiding taxation. The greater the feeling that the goal of trust funds is tax evasion, the greater the perception that an identical tax rate should be placed on foreign trust funds abroad. Additionally, a significant positive correlation was found between the perception of the respondents regarding the main goal of foreign trust funds to lower tax payments, and taxation of foreign trust funds in Israel and abroad.

The main finding as presented in chapter five is an actual breakthrough in the way of thinking regarding the concept of creating income, growth, and increasing the public pie. The committee that handled aggressive tax planning including the issue of taxation of foreign trusts (in June 2005), presented a series of recommendations to enrich the public coffers, mainly regular rates of taxation on all citizens of the State of Israel, including Israeli companies.

This committee did not see all of the considerations, as detailed in the previous chapter, perhaps for the simple reason that this research was conducted at a later date.

The research group that responded to the questionnaire is a heterogeneous group of experts in the fields of economics and taxation in Israel. This is perhaps the difference differentiating it from the Taxation Committee, which was mainly composed of taxation experts who come from the establishment and whose vision is sometimes systemic.

This anonymous research group represented the private sector, the taxation system and academia, providing it with an overall perspective on aspects of taxation touching on the issue of aggressive tax planning in general, and tax havens, such as foreign trust funds, in particular.

It should be emphasized that the tax reform as regards foreign trusts was implemented as of 1.1.2006, there are not yet any information on the economic impact of the foreign funds in Israel from the Ministry of Finance, the Bank of Israel, the establishment of large commercial and economic organizations that are likely to show interest in the issue. At the same time, one can examine the data as presented in chapter 3 of this study, as a basis for reference and estimates of the impact on the Israeli tax pie in the future.

7.2 Conclusions

Over the past decades, the theoretical and empirical literature on factors affecting economic growth has developed and grown. One of the most important findings in this literature is that a high tax burden may lower the economy's growth rate in the intermediate range and even in the long range, and therefore damage the economy's level of development and quality of life. The degree of harm caused to the growth rate by the tax burden depends on many factors, among them the various characteristics of the economy. (Data regarding the country's income from taxes may be found in appendices 6-7).

The main conclusions from this research are:

1. A rise in taxation lowers profits and investments (and vice versa), although the impact of taxation is lower than that of government expenditures.
2. A rise in public expenditures lowers profits and therefore lowers investments (the opposite influence to the case of lowering public expenditure).

According to Solow's (1956) growth model the GNP is determined by production factors, including the scope and the skills of the work force and the quantity and productivity of capital inventory. The rate of growth of the GNP is therefore dependent upon the growth rate of production factors (capital and work), and change in productivity of contribution.

Within this theoretical framework it is possible to characterize several channels through which tax may affect the rate of growth:

- **High tax rates lower the scope of investments and the rate of growth of capital inventory**, as a result of a net decline in individual income, yields on investments and company profits.
- **When tax rates are high, business decisions are not always effective** and growth rates may be damaged by this. The modern free market economy is based on the fact that relative prices of goods, services and production factors will result in efficient allocation of economic resources. Taxation, particularly high tax rates (in all areas), distorts relative prices and leads to non-optimal allocation of resources in the economy. An example of this is lowering the marginal output of capital as a result of diverting investments from areas with high tax rates to areas with lower tax rates, although they may have lower productivity (Harberger, 1962, 1966). Additionally, changing the geographical position of companies for

tax purposes and not marginal output reasons may also harm economic growth rates.

- **High tax rates on income from work, particularly at low income brackets, lower employment opportunity** (a decline in the number of work hours and rate of participation), harming the level of the economy's GNP and leading to a "poverty trap", in which a large part of the population depends on welfare payments and not on income from employment.
- **High tax rates on income from work, mainly in the high income brackets, lower the incentive to accumulate human assets** (such as higher education and professional skills), creating distortions in choice of occupation and damaging the scientific and technological levels of the economy, and of course, growth rates.
- **High tax rates lower work productivity and capital** because of the lower profitability of investing, and as a result, there is less investment in R&D and a delay in industry development.
- **High tax rates lead to tax evasion, damaging growth on a number of planes**. First of all, the act of tax evasion itself, the effort involved on the part of firms and individuals, and the preventative actions on the part of the government (such as income tax investigations) consume many resources that are not used as they should be. Second, certain taxes may be more easily evaded than others. This creates an inefficient allocation of resources and harms economic growth.
- **The migration of employees and capital to countries in which income tax and capital tax is lower**. In a small country, that allows free movement of people, goods and capital (such as Israel), there is another critical channel through which high tax rates lower growth. When there is free movement between countries, competition develops attracting investments and capital, and even people, among different countries, if the tax differences are sufficiently significant. For example, an Israeli software engineer, who in normal times would rather live and work in Tel Aviv, may consider moving to California if the tax rate differences between Israel and the US are too great. This type of migration of human capital (brain drain), can damage growth in a very significant manner.

The degree of influence of tax rates over growth depends greatly on companies' and households' expectations regarding the continued tax policy in the future. A temporary lowering of tax rates, for example, will not encourage a change in consumption habits and investments, if the decrease is perceived as temporary, and the public expects the government to raise taxes in the near future. Therefore, for it to be effective and affect growth, it is very important that tax lowering policies be accompanied by a significant change in public expenditures, that will increase the reliability of the policy and be perceived by the public as permanent.

The Solow (1956) model relates to changes in growth rates in the short term. In the long term, after the economic system suits itself to changes in tax, we return to the original growth rate, although from a lower level of production compared to the GNP that would have existed had there not been a tax increase. In actuality, taxation policy affects growth rates only in transition periods, lowering the economic GNP level as a result, but does not affect the long term growth rate that is affected by growth rates of the population, capital and productivity (that have remained unchanged). However, the short-term influences are the most important because they lead to a permanent rise in the GNP. If one assumes that lowering taxes will raise the GNP by 5%, and the amount

of time within which the economic system will achieve a balanced growth rate is 10 years, the growth rate during this transition period, until achieving stability, will be higher by 0.5% each year.

Other growth models (such as Lucas, 1990, and Romer, 1986) allow a permanent change in growth rates as a result of changes in tax rates or government expenditures.

These models emphasize the positive external influences on the entire economy, of decisions made by companies to invest in equipment or research and development, or investments of individuals in human capital. In these models, taxation may have a long and ongoing influence on the growth rate of the GNP.

7.3 Recommendations

In light of the research findings and the various recommendations regarding a recommended solution, this researcher think that in Israel could adopt some of the responses offered in other countries, and in certain cases adapted to the specific case of Israel, which is somewhat different than other countries, because of the security situation and the different environment (Comparison of tax laws in different countries showed on table no. 5).

The recommended solution is the combined solution. This is based on a combination of the recommendations that have been discussed to this point. This researcher assumes that there is a theoretical explanation for each recommendation based on the opinions of people who are knowledgeable in the field of taxation law, economics and trusts.

However, it is not sufficient for each of the recommendations to be a possible and legitimate solution – it is necessary to examine which of them is the most appropriate solution for the present thesis.

The most correct recommendation must be chosen from the standpoint of enriching the public coffers, on one hand, contributing to the Israeli economy in the end, but on the other hand, must encourage investors, particularly foreign investors, to invest and move their trust assets to Israel.

These two criteria will determine the recommendation that will be chosen as the most appropriate solution.

It is clear that there are a number of different types of trusts, and different size trusts. This writer does not argue that one single recommendation may solve all of the issues, like a magic wand. To achieve the correct combination of the two principles mentioned above, it is possible to adopt a number of recommendations, at different stages of trust income taxation, and in relation to different types of trusts. Only a combination of the recommendations surveyed to this point will be able to balance the various considerations and realize the aim of the present thesis on taxation of trusts based on existing law. Practical solutions will be found based on the findings that we have at hand.

Table no. 5: Comparison of tax laws of different countries

Country	Capital gains and dividend tax	Business profit tax	Withholding tax on dividends	Comments
Cyprus	10%/4.25%	10%/4.25%	None	Reform/ participation exemption
Malta	35% but actual (after return) 4.16% trading companies	35% but actual (after return) 4.16% trading companies	None	Receive a refund on any company tax paid aside from 4.16%. Fear of OECD
Hungary	Holding companies 0%	Holding companies 0%		
Singapore	None – subordinate to certain conditions	None – subordinate to certain conditions. Regular – 24.5%	None	Special offshore regime for companies owned by foreign residents/ taxation based on receipt; participation exemption
Holland	None	35%	0-28% according to tax conventions	Strict position regarding participation exemption
Denmark	Tax exemption of dividends and capital gains on holdings of 20% of stocks at least 12 months	30%	0-30% according to tax convention	Participation exemption
England	Dividend – graduated tax: 10%, 20%, 30%. Possible to receive indirect refund, exemption from capital gains on stocks in holding of at least 20% over one year	30%	None	Participation exemption
Belgium	Dividend – 33.39% for 5% of the sum of the dividend. Capital gains – exempt	33.39%	0-25.75% according to tax conventions	Participation exemption

7.3.1 Principles of the combined solution

Based on the recommended solution, a response will be provided for all types of foreign trust funds, with the differentiating factor being the size of the investment. Since most trust funds hold assets in the range of $1-2 million, and few trust funds invest over than $10 million, two types of trusts can be discussed.

One type of trust fund allows tax breaks and the removal of barriers (such as in the existing model in Ireland, in a situation of 'Underlying Companies'), or other beneficial tax regimes as mentioned in the literature review. Possible benefits may also be posited according to table no. 7 below that describes various tax regimes, and compares only the internal laws in various countries:

Trust funds that are $10-20 million or larger should be eligible for participation exemption, similar to the Israeli law providing tax exemption to mega-companies that invest huge amounts in Israel of over $500 million (such as Intel, Teva, and Iscar).

The Israeli participation exemption law is a unique and progressive law. It enables a foreign resident to establish an exempt business center in Israel for international activities in the form of an Israeli Holding Company. This is an Israeli company that fulfills several conditions, a major one of which is that the company's investment in foreign subsidiaries will be at least 500,000,000 NIS (approximately $120,000,000).

When the IHC distributes dividends to the foreign share holder the dividend is subject to only 5% tax.

Another option is to give tax exempt to the profits of the Trust Fund in condition that they will not be distribute for a long period of time (i.e 15 to 20 years), and they will be accumulated to the capital and continue "working" along with him.

7.4 Recommendations for further study

As discussed above, the research results are initial results and presented close in time to the implementation of taxation of trust fund ordinances that began at 1.1.2006 (Ordinances, 2006). It is therefore desirable and possible, in the future, to expand the examination of the implications of these laws over the Israeli economy, to include a larger sample of experts.

In addition, it is also possible to examine the definition of the taxation arrangement, the sizes, the types of trust funds, and their characteristics and goals.

An additional examination conducted in the future, will definitely contribute another point of view regarding the impact of this issue , over the Israeli economy.

Bibliography

Alesina, A., Ardagana, S., Perrotti, R. and Schiantarelli, F. (2002), "Fiscal Policy, Profits, and Investment", American Economic Review, 992: 571-589.

Arnold, B.J. and McIntyre, M.J. (2001), International Tax Primer. Holland: Kluwer Law International.

Aschauer, D. (1989), "Is Public Expenditure Productive?" Journal of Monetary Economics 23: 177-200.

Auerbach, A. (1996), "Tax Reform, Capital Allocation, Efficiency and Growth", in: Aaron, H. and Gale, W. (eds.) The Economic Effects of Fundamental Tax Reform, Washington, DC: The Brookings Institution.

Auerbach, A. and Hassett, K. (1991) "Recent US Investment Behavior and the Tax Reform Act of 1986: A Disaggregate View". Carnegie-Rochester conference Series on Public Policy 35: 185-215.

Barro, R.J. (1990), "Government Spending in a Simple Model of Endogenous Growth", Journal of Political Economy, 98 Part 2: S103-S125.

Barro, R.J. (1991), "A Cross Country Study of Growth, Saving, and Government", in B.D. Bernheim and J. Shoven (Eds.), National Saving and Economic Performance, Chicago: University of Chicago Press and NBER.

Baxt, A. (1978), Cases and Material on Taxation. Sydney: Lawrence Erlbaum Associates.

Blanchard, O. and Giavazzi, F. (2004),"Improving the GSP through a proper accounting of public investment", CEPR discussion paper.

Bohm, D. and Peat, D. (1987). Science Order and Creativity., New York: Bantam Books.

Carroll, R., Holtz-Eakin, D., Rider, M. and Rosen, H. (2000), "Personal Income Taxes and the Growth of Small Firms", NBER Working Paper 7980, Cambridge, MA: National Bureau of Economic Research.

Chirinko, R.S., Fazzari, S.M., and Meyer, A.P. (1996), "Business Investment and the user Cost of Capital: New Evidence from US Panel Data". Atlanta, GA: Emory University (Mimeo).

Clarke, G. (1999), Offshore Tax Planning, 6th ed., London: Butterworths.

Convention between Israel and the US – Combined Formulation, International Taxation Files, Conventions for the Prevention of Double Taxation. Tel Aviv: Ronen Publishing. (Hebrew)

Dahan, M. and Stervechinsky, M. (1996), "The Public Sector Budget and Economic Growth in Israel". Jerusalem: Bank of Israel, 70. (Hebrew)

Dalkey, N.C. (1967). Delphi. USA: Rand Corporation.

De Koker, A. (Ed.) (1982), Silke On South African Income Tax, 10th edition. Cape Town: International Academic Publishers.

Department of Treasury (1999), Discussion, Analysis and Legislative Proposals, The Problem of Corporate Tax Shelters. USA

Doggart, C. (1987), Tax Havens and their Uses. London: Economist Publications.

Dowrick, S. (1992), "Estimating the Impact of government Consumption on Growth: Growth Accounting and Optimizing Models". Mimeo, Australian National University.

Dushnik, L. and Sabar Ben Yehoshua, N. (2001), The Ethics of Qualitative Research. Tel Aviv: Dvir. (Hebrew)

Easterly, W. and Rebelo, S. (1993), " Marginal Income Tax Rates and Economic Growth in developing Countries". European Economic Review, 37: 409-417.

Engen, E. and Gale, W.G. (1996), "The Effects of Fundamental Tax Reform on Saving", in: Aaron, H. and Gale, W. (eds.) The Economic Effects of Fundamental Tax Reform. Washington, DC: The Brookings Institution.

Engen, E. and Skinner, J. (1996), "Taxation and Economic Growth", NBER Working Paper 5826, Cambridge MA: National Bureau of Economic Research.

Feldstein, M. and Feenberg, D. (1995), "The Effect of Increased Tax Rates on Taxable Income and Economic Efficiency: A Preliminary Analysis of the 1993 Tax Rate Increases", NBER Working Paper 5370, Cambridge MA: National Bureau of Economic Research.

Fisman, R. and Shang-Jin, W. (2001), "Tax Rates and Tax Evasion: Evidence from 'Missing Imports' in China", NBER Working Paper 8551, Cambridge MA: National Bureau of Economic Research.

Ginossar, S. (1999), "Rights in Rem – a New Approach", 14 Israel Law Review, 286: 422-430. (Hebrew)

Glicksberg, S. (2003), The Boundaries of Tax Planning. Jerusalem: Hebrew University, Law Faculty. (Hebrew)

Gross, Y (2002), Is Transfer of Assets to a Trust Free of Taxation, Vol. 51 (2): 236. (Hebrew)

Gross, Y. (2004), "Avoiding Tax and Artificial Transactions". Taxes Journal 15(4): 68-70. (Hebrew)

Grundy, M. (1988), "Old Question New Answers". B.T.R., 309: 87.

Guba, E.G. and Lincoln, Y.S. (1985). Naturalistic Enquiry. Newbury Park: Sage.

Guba, E.G. and Lincoln, Y.S. (1989). Fourth Generation Evaluation. Newbury Park: Sage.

Hadari, Y. and Altar, A., (1994) "Civil Legislation as Reflected in Tax Law", Iyune Mishpat, 10: 429. (Hebrew)

The Hague Convention on the Law Applicable to Trusts and their Recognition, July 1, 1985.

Harberger, A.C. (1962), "The Incidence of the Corporation Income Tax", Journal of Political Economy, 70: 215-240.

Harberger, A.C. (1966), "Efficiency Effects of Taxes on Income from Capital", in: M. Krzyzanaik (ed.), Effects of Corporation Income Tax. Detroit: MI: Wayne State University Press.

Harkins, A. and Kurth-Schai, R. (1983). "OSCAR: and Applied Social Technology Variant of the Delphi Method". Futurics 7(3): 1-7.

Helmer, O. (1966). Social Technology. New York: Basic Books.

Hendrickson, R. and Silverman, N. (1982), Changing the Status of a Trust. Law Journal Seminars Press.

History of English Law , (1923), Cambridge University Press .

Income Tax Ordinance (New version), (2004). (Hebrew)

Izraeli,D. and Zohar , N. (2000) ,"Ethics and Social Responsibility -Israeli Considerations" , Cherikover Publishing , Tel- aviv (Hebrew).

Jantscher, G. (1967), Trusts and Estate Taxation. Annals of the American Academy of Political and Social science ,Vol. 374 ,Washington DC.

Jenks, E. (1920), A Short History of English Law, 2nd edition, London:Methuen.

Jones, L.E., Manuelli, R. and Rossi (1993), "Optimal Taxation in Models of Endogenous Growth". Journal of Political Economy 101: 485-517.

Judd, R.C. (1971). "Use of the Delphi Method in Higher Education". Technological forecasting and Social Change 4(2): 173-186.

Kaplan, A. (Ed.) (2000), Trust in Prime Jurisdiction. Kluwer Law International.

Kaplan, A. (2006), Trusts in Prime Jurisdictions. Globe Business Publication Ltd.

Keeton, G. and Sheridan, L. (2000), The Law of Trusts, 16th edition., Blackwell Publishing , London.

King, M. and Fullerton, D. (1984), The Taxation of Income from Capital: A Comparative Study of the United States, United Kingdom, Sweden and West Germany. Chicago: University of Chicago Press.

King, R.G. and Rebelo, S. (1990), "Public Policy and Economic Growth: Developing Neoclassical Implications". Journal of Political Economy, 98, Part 2: S126-S150.

Klogman, G. and Kaputa, M. (1993) The Conventions for the Prevention of Double Taxation Between Israel and the US, Income Tax Authorities and Government Income Administration. Tel Aviv: Ronen Press. (Hebrew)

Koester, R.B. and Kormendi, R.C. (1988), "Taxation Aggregate Activity and Economic Growth: Cross Country Evidence on Some Supply-Side Hypotheses". Economic Inquiry. Cambridge University Press .

Koester, R.B. and Kormendi, R.C. (1992), "Taxation, Aggregate Activity and Economic Growth: Further Cross Country Evidence on Some Supply-Side Hypotheses". Economic Inquiry.

Lavi, Y. and Stervechinsky, M. (2001), "The Impact of Policy Variable and the Rise of the Business Product and its Components – Production and Productivity factors – In Israel, 1960-1995". Jerusalem: Bank of Israel Survey 73. (Hebrew)

Levine, R. and Renelt, D. (1992), "A sensitivity of Cross-Country Growth Regression", American Economic Review, 82: 942-63.

Lucas, R.E. (1990), "Supply-Side Economics: An Analytical Review", Oxford Economic Papers, 42: 293-316.

Mannix, E. and Mannix, J. (1984), Australian Income Tax Guide, 29th edition. Cch Ausralia Ltd, Sydney.

McBride, A. (1974). "Delphi Technique and Futures Planning in Catholic Education". Momentum, May: 9:17.

McKinsey Global Institute (1996) with assistance from Borsch-Supan, A.. Capital Productivity. Washington, DC: McKisney and Co.

Mendoza, E.G., Milesi-Ferretti, G.M. and Asea, P. (1996), "On the Ineffectiveness of Tax Policy to Alter Long-Run Growth: Herberger's Superneutrality Conjecture". Federal Reserve Board of Governors, Mimeo.

Nachmias and Nachmias (2005) ,Research Methods in Social Sciences , Open University Publishing (Hebrew).

O'Brien, M. (2001), Canadian Income Tax. Toronto: Jones and Bartlett.

OECD Committee on Fiscal Affairs (1997), Model Tax Convention on Income and Capital. Paris.

Ordinances for Encouragement of Capital Investment (Assets and Ongoing Commitments) (2006). Tel Aviv: Ronen Publishing.

Pinson, B. (1980), On Revenue Law, 13th edition. London.

Plosser, C. (1992), "The Search for Growth"', Federal Reserve Bank of Kansas City.

Polak, F.L. (1972). In: Crossing the Frontier of the Unknown. A Toffler, (Ed.), New York: Random House.

Pollock, F. and Maitland, W. (1923), History of English Law, 2nd edition. Cambridge.

Poolpatarachewin, C. (1980). "Ethnographic Delphi Futures Research: Thai University Pilot Project". Journal of Cultural and Educational Futures 2(4): 11-19.

Prebble, J. (1988), "Taxation of Trusts, - Part II", NZCT 25: 134.

Press, S.J. (1983). Multivariate Group Assessment of Probabilities of Nuclear War. (Technical Report #121). Riverside, CA.: University of California.

Pyke, D. (1970). Distribution of characteristics of the Sulfide Ores of the Timmins Area. Toronto: Department of Mines.

Ranch, W. (1979). "The Decision Delphi", Technological Forecasting and Social Change 15(3): 159-169.

Refael, A. and Efrati, D. (2002), Income Tax Law, Tel Aviv: Shukan. (Hebrew)

Report of the Committee for Trust Taxation, (2003). (Hebrew)

Reynolds, J. (1977) "Contingency Planning – the Protection of Trust Assets", Tax Planning International, pp. 165-167.

Romer, P.M. (1986), "Increasing Returns and Long-Run Growth", Journal of Political Economy, 94: 1003-1037.

Scott, A.W. (1997), On Trusts, 3rd edition. Boston: Vol. 1-5.

Shekel, M. (2001), "Treaty Shopping – the Authority of the Tax Official in Lifting the Curtain on International Business". Taxes, 15(1). (Hebrew)

Shidlovsky, A., and Sarel, M. (2006), The Impact of Fiscal Policy over Growth Rates. Jerusalem: Bank of Israel. (Hebrew)

Shkedi, A (2003), Qualitative Research- Theory and Implementation ,Akademon Publishing, Jerusalem/

Slemrod, J.B. (1989), "Are Estimated Tax Elasticities Really Just Tax Evasion Elasticities: The Case of Charitable Contributions". Review of Economics and Statistics 71(3): 517-22.

Solow, R.M. (1956), "A contribution to the Theory of Economic Growth", Quarterly Journal of Economics, pp. 65-94.

Textor, R.B. (1979). "The National Partnership Between Ethnographic Futures Research and Futures Education". Journal of Cultural and Educationl Futures 1(1): 13-19.

The Hague Convention on the Law Applicable to Trusts and their Recognition. July 1, 1985.

Trust Law (1979) Kneset Israel (Hebrew).

Turoff, M. (1970). "The Design of a Policy Delphi". Technological Forecasting and Social Change 2(2): 51-62.

Turoff, M. (1975). "The Policy Delphi", in: Delphi Method – Techniques and Applications. H.A. Linstone and M. Turoff (eds.), pp. 6-15).

Tzlenter, Z. (1999), "Private Trusts in Israel". Hapraklitim, 15: 214. (Hebrew)

Newspapers

Globes Newspaper, 6.7.2005.

Webliography

Boykin, R. (2005), "Holding Company Regimes". International Tax Review. www.Internationaltaxreview.com

Nov, A. Convention for the Prevention of Double Taxation: Vision and Reality. http://www.mof.gov.il/museum/hebrew/oumanout_mas.pdf.

Nov, A., Tax Shelters Worldwide. http://www.hanner.co.il/offshore/tax-havens.htm

Persons and Companies Law (1926) http://scholar.google.com/scholar?q=Lichtenstein+Persons+and+company+law+1926&hl=en&rlz=1T4GGLJ_enIL223IL223&um=1&oi=scholart

Society of Trust and Estate Practitioners. http://www.stepisrael.org

www.legislation.hmso.uk

http://www.irs.gov/businesses/small/article/0,,id=106551,00.html

Appendices

Appendix 1: The research questionnaire

Dear Sir/Madam,

Within the framework of my doctoral studies in Economics and Business Administration I am conducting a study on the issue of the new taxation plan in Israel, and its implications regarding the economy in Israel and worldwide.

This questionnaire is anonymous, and will be used solely for the purposes of research. The present research includes many and varied questions, and the answers are not always "right" or "wrong". In such cases, your personal opinion is important to us.

Please choose the response that most suits you, and circle it.

I appreciate your participation and thank you for your cooperation.

Respectfully,

Daddy Yacov

Part I

Demographic data

Please fill in the answer or circle the answer as appropriate:

1. Age:
2. Gender: A. Male B. Female
3. Marital Status: A. Single B. Married C. Divorced D. Widow/er
4. Education: A. Academic B. High School
5. Tenure at work: A. 1-5 years B. 5-10 years C. 10-20 years D. 20+ years

Part II

This section surveys your personal perceptions regarding taxation and its implications

Instructions: Following are a number of statements. Please rate your agreement with the statements on a scale of 1-5: 1 is the lowest rating, and 5 is the highest rating (Questions 6-21)

Statement	**1** **Not at all**	**2** **Very little**	**3** **Somewhat**	**4** **Greatly**	**5** **Very much**
6. The tax regime in Israel is "complicated" compared to that of other countries	1	2	3	4	5
7. There is a need to fill in the "loophole" of non-taxation of foreign trusts	1	2	3	4	5
8. The main purpose of foreign trusts is tax avoidance	1	2	3	4	5
9. The main purpose of foreign trusts is decreasing tax payments	1	2	3	4	5
10. The main investments of foreign trusts are financial investments	1	2	3	4	5
11. The main investments of foreign trusts are in real estate or land.	1	2	3	4	5
12. In Israel bureaucracy makes it difficult for foreign investors	1	2	3	4	5
13. Foreign investors should be given incentive to invest in Israel through tax breaks.	1	2	3	4	5

14.	Foreign investors should be given incentive to invest in Israel through shortening bureaucratic processes.	1	2	3	4	5
15.	Taxation of foreign trusts outside of Israel should be included when there is an Israeli "trustor" or "beneficiary"	1	2	3	4	5
16.	Taxation of foreign trusts abroad will decrease the rate of reporting in Israel	1	2	3	4	5
17.	Taxation of foreign trusts in Israel will lead to decreased income from taxes.	1	2	3	4	5
18.	Taxation of foreign trusts abroad when the trustor or beneficiary are Israeli, will decrease taxes in Israel	1	2	3	4	5
19.	Lowering barriers in the taxation system for investments in foreign trusts will encourage foreign investors in Israel	1	2	3	4	5
20.	The benefit from removing barriers is greater than the "tax loss" that will be caused by not applying taxes.	1	2	3	4	5
21.	Taxation of foreign trusts abroad is in "conflict" with taxation laws abroad and tax conventions with them.	1	2	3	4	5
22.	There are other more important incentives than tax considerations when establishing a foreign trust.	1	2	3	4	5

Part III

This section surveys your positions regarding the economy and taxation in Israel.

Circle the most appropriate response (Questions 22-31)

Statements	1	2	3	4
23. The new tax reform (of 2003) did not handle taxation of foreign trusts because of the complexity of the issue	1	2	3	4
24. The new tax reform (of 2003) did not deal with application to foreign trusts because of the difficulty of reporting and collecting the tax.	1	2	3	4
25. There is no taxation differentiation between foreign trusts including an Israeli (or foreign) trustor, beneficiary or trustee investing and operating abroad, and between those operating in Israel	1	2	3	4
26. If foreign trusts are not taxed this will cause annual losses to the state treasury.	1	2	3	4
27. If foreign trusts in Israel are not taxed, we will become a "heaven" for foreign investors.	1	2	3	4
28. If foreign trusts are taxed, the tax burden between different strata of the population will be somewhat leveled	1	2	3	4
29. Reporting and collecting taxes on foreign trusts operating abroad cannot be enforced.	1	2	3	4
30. If tax collection can be enforced the cost will outweigh the benefit	1	2	3	4
31. If the instructions for taxing foreign trusts abroad are applied, this may cause legal disagreement with countries in which trusts have been established (i.e. USA, Britain, Australia, etc.)	1	2	3	4
32. The tax regime in Israel is a function of social ideology	1	2	3	4

Part IV

This section is composed of open ended questions.

Please express your opinion, in short, for each question, in order.

Open questions:

1. What do you think is the best way to "deepen" the country's coffers:

   a. taxing foreign trusts
   b. tax exemption, or decreasing the taxation rate on this investment horizon?

....
....
....

2. Do you think that (financially) Israel will become a "tax haven"? Why?

....
....
....

3. According to data that you have at hand, has taxing foreign trusts contributed to the state coffers and indirectly led to an improved economic situation in Israel?

....
....
....

4. In your opinion, will/has taxing trust funds caused "capital escape" from Israel?

....
....
....

5. Internal Israeli law often differs from tax conventions signed by Israel with other countries, in which foreign trusts exist. What do you feel will most strongly influence a foreign investor when setting up a trust in Israel?

....
....
....

6. What do you generally think regarding taxation of foreign trusts in Israel and abroad? Do you feel there are other alternatives that are more suited to the situation in Israel based on other models worldwide?

....
....
....

7. Does the social/political/security climate in Israel affect the creation of foreign trusts abroad, or vice versa (i.e., the creation of foreign trusts in Israel by well to do Jews abroad)?

....
....
....

8. According to a study named "The impact of physical policy over the growth rate of the economy", it was proven that lowering tax rates increases growth, contributes to the flow of foreign capital from abroad, and encourages true reporting of income (as opposed to high tax rates that lead to tax evasion). Express your opinion.

....
....
....

9. What is your opinion on establishing a tax exempt trust fund aimed to reinforce the field of national activity (i.e. national infrastructures, such as – rehabilitation of the north, developing the Galilee or Negev, water channels, etc.)?

....
....
....

10. What changes in legislation do you think are necessary in order for use of trust funds for national purposes and not family purposes to begin to move ahead?

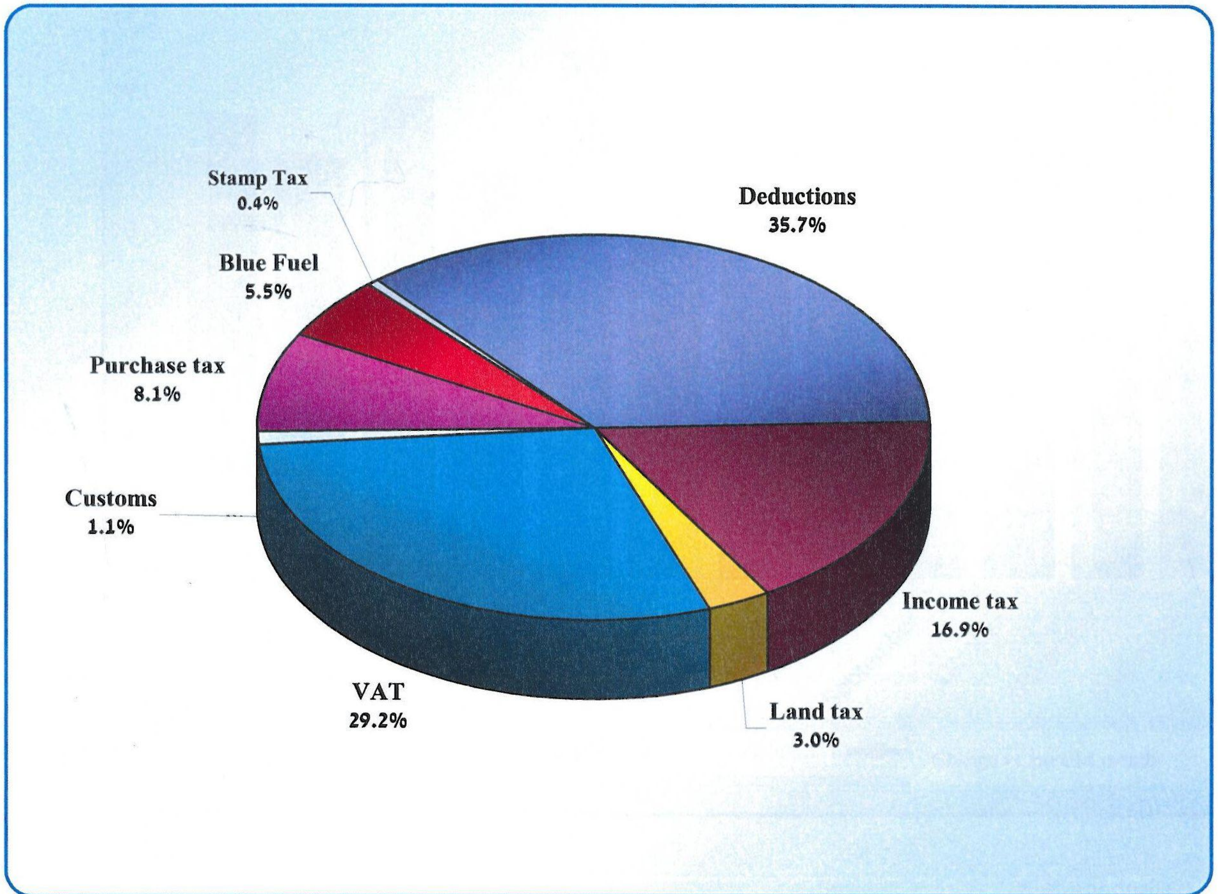
....
....
....

11. How would you improve the model? Or: What do you think is the best model to maximize growth of the public "pie" for the benefit of the state's coffers (as a means), and the benefit of the citizenry, and improving quality of life (as a goal)?

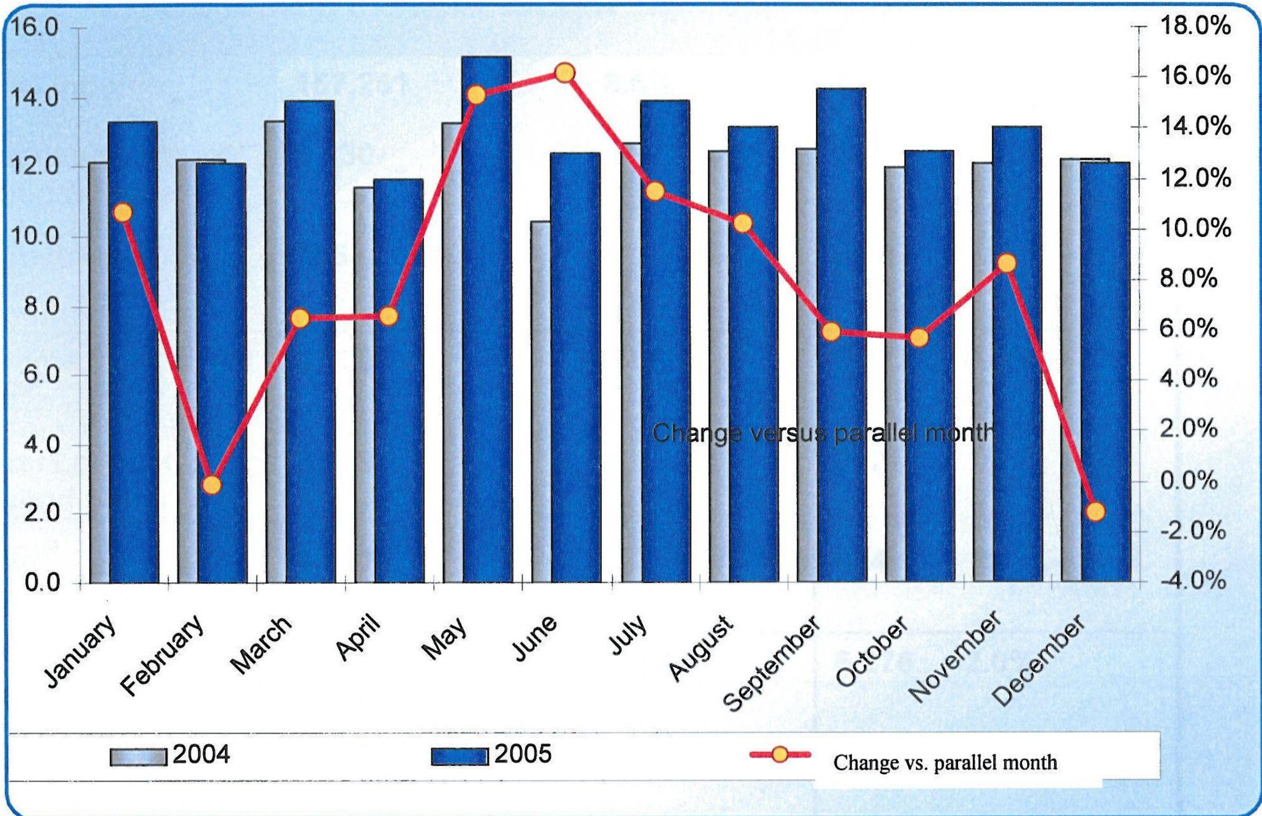
....
....
....

Appendix 2: Income of tax authorities – January to December 2005

(NIS 157.3 Billion)



Appendix 3: Tax authority income 2004-2005 and real change rate each month versus parallel month previous year (NIS billions)

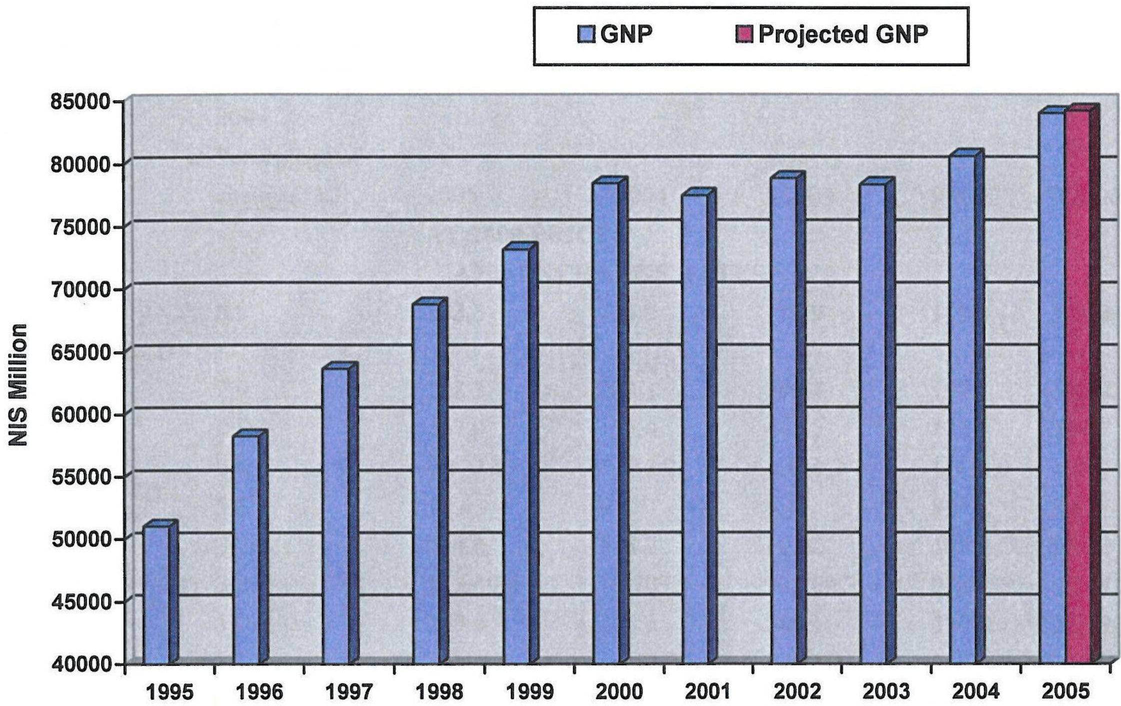


Appendix 4: State income from taxes (NIS billions)

	Jan-Dec 2005	Real calculated change rate	Dec. 2005	Real calculated change rate
Total Income	157,261	8.6%	12,07-	1.2%-
Total Legislation Amendments	3,530-		142-	
Adjustments	783-		771	
Income from direct taxes	87,307	13.5%	6,172	0.5%-
Total Legislation Amendments	3,669-		242-	
Adjustments	1,057-		444	
Income from indirect tax	69,954	2.8%	5,276	2.0%-
Total Legislation Amendments	140		100	
Adjustments	274		327	

Appendix 5: Gross National Product 1995-2005

Actual GNP 1995-2005 and projected GNP for 2005 with tax decrease of 0.1%



If income tax declined by 0.1%, the GNP income would rise by 0.25%. In the case of Israel in 2005, lowering income tax to 16.73% would raise the GNP by NIS 200M.

Appendix 6

Comparison between the GDP of Countries.
Billion dollars, at constant prices

	2005/2004 Percentage of change(1)	2005	R2004	R2003	R2002	R2000
		AT 2000 PRICES AND EXCHANGE RATES				
Israel	**5.2**	**133.3**	**126.7**	**120.9**	**119.1**	**121.0**
Members of OECD						
Austria	2.0	208.3	204.1	199.3	197.1	193.8
Australia	2.7	467.9	455.6	445.2	428.2	399.7
Italy	0.0	1,132.8	1,133.2	1,121.3	1,120.9	1,097.3
Iceland	5.5	10.4	9.9	9.1	8.9	8.6
Ireland	3.2	124.8	118.2	113.2	108.4	96.2
United States	3.2	11,049.0	10,703.9	10,269.3	9,997.6	9,764.8
Belgium	1.2	249.4	246.3	240.1	237.9	231.9
Germany	1.0	1,971.5	1,952.7	1,921.3	1,924.9	1,900.2
Denmark	3.1	171.2	166.1	163.1	162.0	160.1
Netherlands	1.1	403.0	398.5	391.8	392.3	386.5
Hungary	4.1	57.7	55.4	52.7	50.9	47.0
United Kingdom	1.8	1,619.5	1,590.5	1,542.2	1,504.4	1,442.8
Turkey	7.4	246.2	229.3	210.5	199.0	199.3
Greece	3.7	143.9	138.8	132.6	126.6	116.0
Japan	2.6	4,993.7	4,866.3	4,756.8	4,673.8	4,649.6
Luxembourg	4.0	23.8	22.9	22.0	21.5	20.3
Mexico	3.0	636.2	617.9	593.2	585.1	580.8
Norway	2.3	184.8	180.7	175.3	173.4	166.9
New Zealand	1.9	62.7	61.5	59.3	57.3	52.7
Slovak Republic	6.1	25.6	24.1	22.9	22.0	20.4
Spain	3.4	678.0	655.6	635.9	617.4	580.7
Poland	3.2	198.3	192.0	182.4	175.7	171.3
Portugal	0.4	116.3	115.9	114.5	115.8	112.6
Finland	2.9	137.8	133.9	129.4	127.1	121.9
Czech Republic	6.0	66.4	62.7	59.9	58.0	55.7
France	1.2	1,430.1	1,413.4	1,381.3	1,366.5	1,328.0
Korea	4.0	637.9	613.6	585.9	568.3	511.7
Canada	2.9	809.8	786.7	764.3	749.4	714.5
Sweden	2.7	270.3	263.2	253.7	249.5	242.0
Switzerland	1.9	258.6	253.8	248.7	249.4	246.0

Source: Central Bureau of Statistics Abstract of Israel 2006: www.cbs.gov.il

Appendix 7: The distribution of the Consumption over the last Decade (1995-2005)

									Uses of resources
							Final consumption expenditure		
			Actual individual consumption						
	Grand total	Total	Total	Private consumption expenditure	Individual government final consumption expenditure(2)	Collective government final consumption expenditure	General government consumption expenditure	Gross domestic capital formation	Export of goods and services
								At current prices	
1995	389,345	235,328	193,256	155,639	37,617	42,072	79,689	71,235	82,782
1996	450,792	275,020	225,473	180,380	45,093	49,547	94,641	81,260	94,512
1997	499,197	303,114	248,599	197,811	50,788	54,515	105,304	86,437	109,646
1998	546,906	332,861	273,320	217,936	55,384	59,541	114,925	89,071	124,974
1999	617,022	361,854	296,449	237,351	59,098	65,405	124,503	98,624	156,544
2000	683,183	391,731	323,449	259,645	63,803	68,283	132,086	102,935	188,517
2001	681,707	409,760	337,317	268,978	68,339	72,442	140,782	102,001	169,946

2002	720,898	438,285	356,747	284,438	72,309	81,537	153,847	96,201	186,412
2003	725,555	440,870	361,241	289,381	71,860	79,629	151,489	86,954	197,731
2004	783,370	456,287	378,241	305,127	73,114	78,046	151,160	90,724	236,359
2005	840,485	477,567	396,324	320,821	75,504	81,243	156,746	103,120	259,798
								At 2005(3) prices	
1995	583,675	348,382	281,147	222,132	59,203	67,537	126,740	105,450	129,621
1996	618,931	367,406	296,543	234,229	62,519	71,176	133,697	113,941	137,344
1997	638,529	376,758	304,541	240,103	64,678	72,498	137,196	112,273	149,642
1998	661,167	392,806	318,541	252,316	66,419	74,469	140,908	109,110	159,498
1999	701,157	404,843	329,063	261,020	68,229	75,936	144,197	115,986	181,533
2000	768,087	428,833	352,003	282,126	69,932	76,836	146,804	118,168	222,818
2001	753,710	441,571	361,865	289,365	72,562	79,733	152,331	114,418	197,811
2002	746,276	451,387	366,143	291,616	74,574	85,369	159,923	100,983	193,323
2003	751,329	450,208	368,148	294,104	74,087	82,125	156,211	91,333	209,106
2004	802,696	463,020	384,222	310,326	73,891	78,797	152,688	92,458	247,165
2005	840,484	477,567	396,324	320,821	75,504	81,243	156,746	103,119	259,798

Source: Central Bureau of Statistics Abstract of Israel 2006: www.cbs.gov.il

Egyetemi Könyvtár Pécs