KEY POINTS

What is the issue?

The question of individual residency is a cross-border and relevant issue for the tax system in any country.

What does it mean for me?

This article deals with a ruling of the Supreme Court of Israel, which discusses the definition of individual residency according to the law in Israel.

What can I take away?

For the purpose of determining individual residency: certain professions should not be examined differently; significant weight should be given to the individual's family ties and less weight should be given to services that can be obtained remotely, such as banking services.

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Facts and circumstances

DANIEL PASERMAN AND SHIMON EFRATI REVIEW THE ISRAELI SUPREME COURT TAX RULING REGARDING THE DEFINITION OF INDIVIDUAL RESIDENCY

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Much has been written on the tax residency of individuals in Israel. More than once, disputes have arisen between taxpayers and the tax authorities with respect to the Israeli statutory test for the individual's tax residency: the centre-of-life test (the Test).

In the recently issued judgment in the matter of the Kiryat Shmona soccer team,[1] the dispute revolved around the residency of two of the team's players. According to Israeli tax law, residents of Kiryat Shmona, a town in the northern periphery, are eligible for special tax reliefs. The two soccer players grew up in villages near Kiryat Shmona, about an hour's drive away. One of the players was engaged to be married and the other was married with four children; however, their families have continued to live in the villages where they were born.

According to the *Israeli Income Tax Ordinance* (the Ordinance), a 'resident of a certain town' is defined as an individual whose 'centre of life' is located in that specific town. The heart of the dispute in this case revolves around determining the precise definition of the centre of life for individuals in the context of tax benefits for residents of towns entitled to such benefits. Should we refer to the definition of the Test as stated in the Ordinance regarding residency in Israel or should a different definition of the Test be considered specifically for this tax relief?

THE JUDGMENT

The justices on the panel were divided in their opinions, with the majority decision being that the Test for defining a person as a resident of Kiryat Shmona is the same as the Test used to define a resident of Israel. Hence, it was ruled

'According to the current legislation, an individual is an Israeli tax resident if their centre of life is in Israel'

that the two players were not residents of Kiryat Shmona and therefore they were not entitled to the tax benefits.

The judgment contains several interesting insights, which are worth giving thought to.

First, although the dissenting judge believed that in applying the Test in regards to a town whose residents are entitled to tax benefits, critical weight should be given to the individual's contribution to that town. The majority judges ruled that the Test should be examined the same way residency is examined for state tax residency, i.e., according to the individual's ties, including the family, social, economic and cultural connections. To these, the subjective aspect must also be added, i.e., the location that the individual views as the centre of their life.

Second, the dissenting justice believed that the occupation of professional sport has unique characteristics and therefore, as a rule, he tended to view the village in which a professional sports team plays as the centre of life of the professional player who plays for that team. However, the majority justices ruled that there are no grounds for applying a special law to certain types of occupations and that the centre of life is not a place that a person can 'simply pick up and carry on his shoulders every weekend, when he returns to his family home'. Rather, the examination of an individual's residency should be applied equally in accordance with the material test of the 'centre of the individual's life'.

Third, the court was divided with respect to the weight that should be attributed to the place where the individual's family lives. The dissenting justice believed that the place where the individual's family lives is indeed a tie that must be taken into consideration; however, it is not a decisive factor. The way in which a soccer player combines his professional career with his family life, being a parent and being part of a couple is none of the tax assessor's business. It is most certainly possible that the player would relocate, alone, to Kiryat Shmona, even though his family would stay behind.

On the other hand, the majority justices believed that great weight should be attributed to the place where the individual's family lives, because 'people connect their family to their permanent place of residence'. The majority justices also attributed weight to the fact that one of the players had set up a non-profit organisation to benefit the village he comes from. This also attested to the close connection that he still had with the place he grew up in and where his wife and children live. This social involvement in the village's life is deemed significant in terms of the most significant nexus test.

Fourth, all of the justices agreed that, from an evidentiary point of view, no significant weight should be attributed to the fact that the taxpayers' bank accounts have remained in the town where they were born, given that the physical location of bank branches has become unimportant in today's modern age of technology. However, the majority justices attributed evidentiary and material weight to the fact that the taxpayers had not presented any electricity, water or gas bills, nor credit card statements or any other evidence that they had gone shopping in Kiryat Shmona or with respect to how much time they had actually spent in the town.

From the judgment, it can be seen, yet again, that the test of an individual's residency in Israeli law is a complex factual and circumstantial test, which frequently gives rise to disputes between the Israel Tax Authority and the taxpayers. In addition, it is also evident that even among the Supreme Court justices there are differing opinions regarding the components of the Test, including with respect to the weight that should be attributed to the place where the family lives and the type of the individual's occupation.

In this regard, it is important to mention that on 24 July 2023, the Israeli Ministry of Finance published a proposed Bill addressing the tax residency definitions for individuals under the Ordinance. According to the current legislation, an individual is an Israeli tax resident if their centre of life is in Israel. This facts-and-circumstances test examines the individual's family, economic and social ties. In addition, there are two rebuttable presumptions based on the number of days an individual spends in Israel.

THE PROPOSED LEGISLATION

The new proposed legislation maintains the rebuttable presumptions but also introduces irrebuttable (conclusive) presumptions according to which an individual would be considered a tax resident of Israel or a foreign tax resident.

The new proposed legislation (if enacted) will not apply retroactively; however, previous years could be considered when examining the applicability of the proposed legislation for the years to follow. It should be noted that although the purpose of the new proposed legislation is to increase certainty, it seems that the conditions included in the proposed rules are complicated and the phrasing thereof is not clear enough. It therefore may cause complexities in interpretation and implementation of the rules set therein. However, the new legislative proposal is not yet in effect and could potentially (and hopefully) undergo certain modifications.

#ISRAEL #RESIDENCY OR DOMICILE #TAXATION

1 CA 7719/21 *Saleh Hasramah and others* v *Haifa Tax Assessing Officer (Supreme Court)* (Nevo 4 May 2023)