THE FOREIGN INVESTMENT REGULATION REVIEW

NINTH EDITION

Editors
Calvin Goldman QC, Michael Koch and Alex Potter

THE LAWREVIEWS

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PREFACE

This ninth edition of *The Foreign Investment Regulation Review* provides a comprehensive guide to laws, regulations, policies and practices governing foreign investment in key international jurisdictions. It includes contributions from leading experts around the world from some of the most widely recognised law firms in their respective jurisdictions. This year, in keeping with the considerable increase in prominence of foreign investment review, we are delighted to include new chapters on Austria, Belgium, India, Israel, Japan and the Netherlands, along with several new contributors for countries covered in previous editions. We have also revised the format to focus on the aspects of foreign investment rules that are most critical for dealmakers.

Unprecedented challenges have arisen in 2020–2021 not only to the health and well-being of persons around the globe, but also to globalisation itself and, with it, the flow of capital. Whereas foreign investment has for a number of years been attracting increased attention, this trend has accelerated throughout the past 18 months. Prior to the covid-19 pandemic, the global economy was continuing its trend towards further integration, even with indications of emerging protectionism, and the number of cross-border and international transactions was increasing, while national governments continued to intervene in foreign investment based on a broadening set of criteria. Foreign investment reviews of cross-border mergers could not help but be affected by shifts in economic relations between countries, which in turn were driven by evolving geopolitical considerations. These included structural developments such as Brexit, now in its early post-implementation stages, as well as increased tensions over trade and related policies, as we have seen between the United States and China. These increased tensions have heightened concerns over national interest considerations such as the export of jobs, essential supply chains and industrial policies, as well as heightened national security concerns over cybersecurity, new technologies, communications and other strategic areas.

These and other developments discussed below have led, in the case of certain merger reviews, to increased tensions between normative competition and antitrust considerations, on the one hand, and national- and public-interest considerations on the other hand, the latter sometimes weighing heavily against the former. An example of the kind of differing regulatory decisions between the competition authorities and the Ministerial decision making in relation to concurrent foreign investment reviews occurred when BHP Billiton, the global leader in mining based in Australia, which has already engaged in previous significant mining investments in Canada, proposed to acquire the Potash Corporation of Saskatchewan, at an amount of approximately US$40 billion. Both Australia and Canada are members of the Five Eyes with respect to national security matters. That regulatory review process became a highly publicised matter of public interest through much of 2010. In the end, while the Canadian

Competition Bureau cleared the proposed merger, the federal Minister of Industry, following his review under the Investment Canada Act and consultation with his Cabinet colleagues, issued an interim negative decision, in November 2010, on national interest grounds that were never really articulated. Rather than trying to then make further submissions, BHPB decided to withdraw the proposed acquisition. Some commentators at that time suggested that the reasons for the Ministerial position had more to do with the pending elections at the provincial level in Saskatchewan and at the federal level than any significant national interest issue (Potash Corp had a long standing perception among people in Saskatchewan as a historical corporate leader in that province).

A similar split in such regulatory decision making subsequently occurred in November 2013 in relation to the proposed acquisition of Grain Corp of Australia by Archer Daniels Midland Company of the United States. That also was cleared by the competition authority (the Australian Competition and Consumer Commission) following its competition review; however, following subsequent concerns raised by the Foreign Investment Review Board, the Treasurer of Australia, one of the most senior Cabinet members, decided to block the proposed acquisition. Farmer concerns and distribution networks were apparently factors in that decision. Again, some commentators suggested real-world political considerations had some bearing on that negative decision.

As a result of cases such as these and other evolving considerations discussed below, more cross-border mergers have been scrutinised more intensely, with the process delayed or in some cases thwarted, by foreign investment reviews that are increasingly broader in scope.

Since the pandemic has taken hold, the underlying considerations that had been driving trends in the review of foreign investment moved to the front of national agendas, with the result that these trends have both been accelerating and increasing in scope. Concerns about the benefits of globalisation have been on the rise in an environment where nations have found themselves competing for supplies of critical medicines, equipment and personal protective equipment necessary to meet the public health emergency. This has led to a broadening of the types of businesses the takeover of which might be viewed as raising strategic, public interest or national security considerations. The increased focus on the stream of capital flowing from state-owned enterprises (SOEs) that had already driven greater scrutiny of proposed investments took on heightened importance, particularly in economic sectors viewed as being critical to the pandemic response, such as public health and supply chains. As the impacts of the worldwide economic shutdown on the valuation of domestic businesses began to be felt, concerns around opportunistic hollowing-out of domestic sectors rose to the forefront of considerations of such matters as lowering financial thresholds that trigger foreign investment reviews.

This has all taken place in the context of efforts to overhaul the regulatory landscape that were already under way in the United States and Europe. In the United States, which saw the introduction of a mandatory notification regime and expansion of the review authority of the Committee on Foreign Investment in the United States (CFIUS) following the enactment of the Foreign Investment Risk Review Modernization Act (known as FIRRMA) in August 2018, greater resources are now being allocated to monitoring and enforcement activities. This is making the voluntary filing calculus even more complex as there is no statute of limitations on CFIUS's jurisdiction if it has not cleared a transaction. As the policy focus has shifted to supply chain security across the globe, CFIUS is being used in conjunction with other US government authorities to wean critical US supply chains off their reliance on Chinese inputs; for example, by either blocking or subjecting to review even ordinary

course transactions with blacklisted Chinese companies. Heightened CFIUS interest and commentary pertaining to certain China-related transactions, such as occurred in relation to TikTok, is a reflection of some of these evolving developments.

In turn, there is greater focus on foreign investment in Europe, where the European Union's foreign investment screening regulation, which became fully operational in October 2020, gives the European Commission a new central advisory role in coordinating increased scrutiny by Member States and obliges Member States to notify other Member States and the European Commission of foreign investments that they are screening under their national regimes. Furthermore, Member States have themselves introduced new foreign investment regimes (e.g., the Czech Republic and Denmark), are planning to do so (e.g., the Netherlands and Slovakia) or have further updated or tightened their existing foreign investment laws (e.g., Germany by introducing a variety of new sectors that it considers to be sensitive such as artificial intelligence, robotics and nanotechnology). Currently, 18 EU countries have an FDI screening mechanism in place and a senior EU trade official has confirmed that dozens of foreign-investment vetting requests have been notified to the European Commission through the new EU screening mechanism since it came into force.

The United Kingdom has now aligned itself more closely with other countries by significantly strengthening its powers to intervene in deals that may threaten national security. The National Security and Investment Act 2021 marks a step change in the UK government's power to screen, impose conditions on and block deals that pose unacceptable risks. Once the new regime comes into force on 4 January 2022, it will require mandatory notification of investments in 17 strategically sensitive sectors that cross certain share or voting rights thresholds – a significant change in light of the UK's (continuing) voluntary merger filing regime. Transactions in all other sectors will be susceptible to 'call in' by the government should there be concerns.

The United States and Europe are not alone in elevating concerns over foreign investment during the pandemic and in response to increasing concerns over China's global influence. In Canada, during 2020–2021, timelines for national security reviews were temporarily extended and investments by SOEs as well as in Canadian businesses related to public health or the supply of critical goods and services were subjected to heightened scrutiny in response to the pandemic. The Canadian government has issued more detailed guidelines for the review of foreign investments, among other things, to include national security concerns relating to the potential of the investment to enable access to sensitive personal data that could be leveraged to harm Canadian national security through its exploitation, including personal data concerning government officials, such as members of the military or intelligence community. In Australia, on 1 January 2021, the Foreign Investment Reform Act came into effect, ushering in sweeping changes to that country's foreign investment review law. The temporary A$0 monetary screening thresholds for all investments that had been introduced in response to covid-19 were removed; however, this threshold was continued through provisions for the mandatory review of investments in sensitive national security businesses. New Australian regulations list businesses in critical infrastructure, telecommunications, military goods or defence or intelligence technology, the provision of service to defence or intelligence forces, the storage or access to classified security information and the storage, collection, or maintenance of personal information of defence and intelligence personnel. The symmetry between the Canadian guidelines and the Australian regulations should not be considered coincidental. Both countries are members of the Five Eyes together with the United States, the United Kingdom and New Zealand. The

Australian Treasurer has also been given new, stronger enforcement and review powers under the legislation, including a new 'last resort' power, under which the Treasurer may review previously approved transactions where national security risks have emerged after approval by the Foreign Investment Review Board.

In addition to these significant developments, differences in foreign investment regimes (including in the timing, procedure and thresholds for and substance of reviews) and the mandates of multiple agencies (often overlapping and sometimes conflicting) continue to contribute to the relatively uncertain and at times unpredictable foreign investment environment. This gives rise to greater risk of inconsistent decisions in multi-jurisdictional cases, with the potential for a significant 'chilling' effect on investment decisions and economic activity. Foreign investment regimes are increasingly challenged by the need to strike the right balance between maintaining the flexibility required to reach an appropriate decision in any given case and creating rules that are sufficiently clear and predictable to ensure that the home jurisdiction offers the benefits of an attractive investment climate notwithstanding extraordinary circumstances.

The recently increasing breadth, scope and timelines for proposed acquisitions by SOEs and other proposed acquisitions giving rise to national security considerations have raised a potentially challenging issue in the context of proposed acquisitions of failing firms. There is a widely held view that, as a result of the disruptive economic effects of the covid-19 pandemic, there may be a sizeable number of distressed industries and failing firms in sectors that have been most significantly impacted by the pandemic. The number of failing firm cases is likely to increase the longer the pandemic continues to substantially affect the timeline for economic recovery from the effects of the pandemic.

In this exceptional environment, there may be failing firm cases where the proposed acquirer is an SOE, which in some foreign direct investment reviews includes a corporation that may be influenced directly or indirectly by a foreign government. There may also be proposed acquisitions of failing entities in the public health or supply chain markets, which may be regarded as more sensitive transactions in the context of the pandemic. If these types of proposed acquisitions are subjected to increased scrutiny and longer timelines in foreign investment reviews where the acquiree is a failing firm, and to the extent that there may be a parallel competition review conducted on a considerably more expeditious basis, the proposed acquisition risks not being completed if the acquiree cannot be sustained during that period. That may lead to an anticompetitive acquirer with existing operations in the same jurisdiction becoming the only purchaser in a position to complete the proposed acquisition, thereby avoiding liquidation of the assets and loss of jobs. The same result may follow even where the proposed acquirer is not an SOE or the failing firm is not in an apparently sensitive business because the increasing scope and timelines for foreign investment reviews, coupled with continuing geopolitical tensions, may raise sufficient uncertainty to dissuade a foreign entity from making a proposed acquisition. These developments could have a significant impact on domestic market concentrations going forward.

With respect to the interface of national interest and public interest considerations and the evolving breadth of national security reviews, including, in some cases, as they may relate to or interface with, normative competition reviews, the American Bar Association Antitrust Law Section (ABA ALS) Task Force on National Interest and Competition Law prepared a report that was considered and approved by the Council of the ABA ALS in August 2019. In that report, the Task Force examined a number of cases in selected jurisdictions where these issues have been brought to the forefront. In addition, the ABA ALS Task Force on

the Future of Competition Law Standards has delivered a further report in early August 2021 to the Council of the ABA ALS that, among other subjects, has considered recent developments pertaining to national interests and national champions in competition reviews. These evolving considerations in competition reviews cannot be viewed in isolation from the increasing scope of national interest factors in foreign investment reviews.

In the context of these significant developments, we hope this publication will prove to be a valuable guide for parties considering a transaction that may trigger a foreign investment review, which often occurs in parallel with competition reviews. It provides relevant information on, and insights into, the framework of laws and regulations governing foreign investment in each of the 21 featured jurisdictions, including the timing and mechanics of any required foreign investment approvals, and other jurisdiction-specific practices. The focus is on practical and strategic considerations, including the key steps for foreign investors planning a major acquisition or otherwise seeking to do business in a particular jurisdiction. The recent trends and emerging issues described above and their implications are also examined in this publication. Parties would be well advised to thoroughly understand these issues and to engage with regulatory counsel early in the planning process so that deal risk can be properly assessed and managed. Having regard to the changing regulatory environment pertaining to foreign investment reviews and the evolving protectionism as well as geopolitical considerations across a number of jurisdictions, regulatory counsel may recommend approaching the relevant government authorities at a comparatively early stage to engage in constructive discussions and to obtain an initial view from government officials of the proposed transaction.

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Please note that the views expressed in this book are those of the authors and not those of their firms, any specific clients, or the editors or publisher.

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Chapter 11

ISRAEL

Adi Wizman and Idan Arnon[1]

I OVERVIEW

Israel, widely recognised as the 'start-up nation', is known for its abundance of cutting-edge technology in a wide variety of fields (e.g., autonomous mobility, cybersecurity, energy, digital health, fintech and agritech). This technology attracts great interest from a variety of investors and acquiring parties such as venture capital firms, private equity funds and strategic players from around the world.

The first half of 2021 saw record-breaking transactions in venture capital technology investments and it is expected that 2021 will be one of the strongest, if not the strongest, year ever for Israeli venture capital investment. This level of foreign investment activity exemplifies the ease with which foreign investors can do business in Israel.

Israel does not have general unified foreign direct investment (FDI) legislation or approval regime and, as a result, there are no broad cross-sector consolidated controls on foreign investments. Generally, foreign entities can freely purchase and sell assets and securities in Israel, and there are currently no sectors in which FDIs are categorically prohibited. Israel does, however, possess a series of stand-alone, sector-specific FDI regulations and requirements.

These restrictions and requirements are sometimes found with respect to investment in companies whose area of activity impacts national security or public utilities and infrastructures. These requirements may also be the result of terms included in governmental licences, public tenders or concessions.

Under Israel's regulatory structure, regulators overseeing a specific sector will generally be able to exercise relatively wide discretion regarding the issuance and revocation of licences, concessions and permits. In the framework of such discretion, regulators can include specific conditions, restrictions or approval requirements regarding FDIs and to alter them. Generally, the exercise of regulatory discretion, as well as any action by a regulator, is subject to the principle of legality, the rules of the administrative process and the principles of judicial review of administrative discretion.

Alongside such regulatory obligations that may be implemented in licences, concessions and permits, contractual regulations have become increasingly common in Israel. Therefore, adverse terms regarding FDI can also be found in agreements between the government and a private entity.

1 Adi Wizman is a partner and Idan Arnon is an associate at Tadmor Levy & Co.

Despite the generally decentralised nature of FDI regulation in Israel, a central mechanism for examining foreign investments from a national security aspect was recently formulated in Israel, in the form of an Advisory Committee for National Security Affairs in Foreign Investments (the Advisory Committee) (further explained below).

II YEAR IN REVIEW

This past year has been characterised by extensive activity of foreign entities in Israel, and an increase in the scope of foreign investments in the country, despite the global crisis caused by covid-19 and the political instability reflected in Israel's four national elections over the past two years. Direct investments in Israel from foreign players totaled approximately US$24.8 billion in 2020, in comparison with US$19 billion in 2019 and US$21.5 billion in 2018.[2] To date, the scope of foreign investments in Israel for the first quarter of 2021 stands at approximately US$7 billion.[3]

Foreign investments, and the involvement of foreign companies, reached a broad range of diverse fields and projects in Israel, in areas such as hi-tech, energy and infrastructure.

In October 2019, the Ministerial Committee for National Security Affairs resolved to establish a protocol for the examination of national security concerns in foreign investments. Pursuant to this decision, an advisory committee headed by the chief economist at the Ministry of Finance was established and charged with examining national security concerns that arise from foreign investments.

The committee began its activity during 2020, establishing a mechanism for handling queries from regulators concerning transactions that may give rise to national security considerations, including in cases that have no existing FDI regulatory requirements. The criteria upon which the committee bases its recommendations are not made public. Formally, the final decision with regard to the transaction remains with the relevant regulator; regardless, as a national security committee, its recommendations carry substantial weight with sectoral regulators.

The Advisory Committee has been operating for approximately 18 months, but the transactions that undergo its scrutiny were not made public and neither were its recommendations to the regulators.

As will be elaborated below, substantial oversight powers with regard to national security considerations in foreign investments are also found in existing legislation and are used by the Israeli defence establishments to control foreign investments. The Advisory Committee, however, serves as a centralising body that aims to ensure more encompassing and effective scrutiny of national security concerns in sectors that the government views as critical to its economy and national security.

2 The Central Bureau of Statistics – Summary of Balance Sheet Payments for 2020.

3 According to Bank of Israel data, available at https://www.boi.org.il/he/DataAndStatistics/Pages/MainPage.aspx?Level=2&Sid=26&SubjectType=2.

III FOREIGN INVESTMENT REGIME

i Laws and regulations

No centralised FDI regulation exists in Israel and, thus, there is no unified cross-sector set of considerations used by regulators for examining foreign investments. At the same time, there are general FDI regulatory requirements that may apply to a broad range of transactions, regardless of their sector; primarily restrictions deriving from considerations of national security, restrictions on transactions that entail the purchase of land and requirements that arise in state tenders.

National security legislation

In addition to the recent establishment of the Advisory Committee in charge of examining national security aspects of foreign investments, Israel has various laws designed to protect its security interests with regard to the conduct of economic activity with foreign entities, the main ones being detailed below.

The Defence Corporations Law (Protection of Security Interests), 2006 (DECL), authorises the Prime Minister, the Minister of Defence and the Minister of Economy and Industry (the Ministers) to declare a corporation as a 'defence corporation' when its principal activity is engagement in defence-related knowhow or equipment used or intended to be used by security forces,[4] if they find that national security is likely to be harmed in circumstances such as the acquisition or holding of control or means of control in the corporation; a venture or merger of the corporation with another entity; or the transfer of know-how related to the corporation or its activity.[5]

Corporations declared as 'defence corporations' are subject to regulatory oversight, including in the form of restrictions on the transfer, acquisition and ownership of their means of control – activities contingent upon approval by the Minister of Defence.[6]

The Ministers are also entitled:

a to set Israeli nationality requirements with respect to the control of a defence corporation and regarding its officers;

b to set residency requirements such that ongoing management of a defence corporation and its centre of business be in Israel;[7]

c to require a defence corporation to obtain prior approval from the Minister of Defence to carry out a joint venture or a change in its corporate structure;[8] and

d to place restrictions on the transfer of security know-how to officers or shareholders to any corporation that has considerable influence on the defence corporation.[9]

4 Pursuant to Section 3(a) of the DECL, a corporation may be declared a 'security corporation' even if most of its activity is not security activity, if that security activity is of significant security importance.

5 Section 3(b) of the DECL.

6 Section 5(a) of the DECL.

7 Section 6(b)(a) of the DECL; Section 6(2)(b)–(c) of the DECL.

8 Section 6(5)(a) of the DECL.

9 Section 6(3)(a) of the DECL.

Trade with the Enemy Ordinance, 1939, prohibits the conduct of direct or indirect trade between Israel and its citizens (including corporations) and an enemy state or an entity in an enemy state, an enemy subject, or for the benefit of any of the above.[10]

The Law on the Struggle Against Iran's Nuclear Program, 2012 (SINPL) imposes sanctions against foreign entities that act in a foreign country to assist Iran in advancing its nuclear programme or in obtaining weapons of mass destruction. The SINPL sets restrictions and sanctions on corporations that sustain business connections with Iran, for its benefit, or in its territory.

The Law for the Prevention of Distribution and Financing of Weapons of Mass Destruction, 2018 prohibits engaging in economic activity with an entity declared (by the UN Security Council or by order of the Minister of Finance in consultation with the Minister of Foreign Affairs and the Minister of Defence), to be assisting in the distribution and financing of weapons of mass destruction, or with an entity related to such assisting entity, unless permitted by the Minister of Finance.[11]

Real estate

The Israeli government supervises the transfer of land in Israel to non-Israelis under the Israel Lands Law, 1960 (the Land Law). According to the Land Law, it is forbidden to sell or otherwise transfer 'property rights' in Israeli land without obtaining prior approval from the Chairman of the Israeli Lands Council (the Chairman).

The Land Law defines 'property rights' very broadly, including ownership rights, the right to lease property for more than five years or obtaining an option to extend a lease for an aggregate period exceeding five years, as well an undertaking to transfer such ownership or leasing rights.

The approval process of such transfer of property rights requires the Chairman to consult with the Minister of Defence and the Minister of Foreign Affairs, and consider the identity of the buyer, their relations to Israel, the purpose of the purchase, and the public's best interests and security, among others.

Any transaction that requires pre-approval by the Chairman and does not receive such approval is void. The Attorney General, or any interested party, is entitled to file a motion to court to declare the transaction void; to negate any registration made in respect of such transaction in any official registry; or to request any other remedy that the court may find appropriate.

10 For the purposes of the Ordinance, Iran, Iraq, Syria and Lebanon are considered 'enemy states'. However, an order issued by the Minister of Finance applies until the end of 2021; the order gives temporary permission for trade activity with Iraq. A person is viewed as having conducted trade with the enemy if he or she had any commercial, financial or other relations with the enemy or for the benefit of an enemy, and especially: (1) if such person supplied, received, transported or traded goods with the enemy or for his or her benefit; if the person paid or transferred money, a tradable document or security to the enemy or for the benefit of the enemy, or to a location within an enemy state; (2) fulfilled any obligation towards an enemy; or (3) executed any obligation on behalf of the enemy. Purchasing enemy currency (banknotes or coins that are in circulation, banknotes and coins in any territory subject to the sovereignty of a power that is at war with Israel) is also considered to be trading with the enemy. The transfer or allocation of securities by the enemy or on his or her behalf or the allocation of securities to the enemy will not be valid, except with the consent of the Minister of Finance.

11 Section 5(a) of the DECL.

Government tenders

Tenders published by the state of Israel and by public entities are governed by the Mandatory Tenders Law, 1992 (the Tenders Law). FDI oversight may be exercised through conditions set in tenders and procurement contracts.[12]

One origin of general authority to retain such oversight can be found in a provision of the Tenders Law, according to which Israeli government is authorised, with the approval of the Foreign Affairs and Defence Committee of the Knesset (the Israeli Parliament), to order, based on foreign policy considerations, that Israel or a governmental corporation will not enter into a transaction with a particular foreign country or supplier.[13]

The regulations promulgated under the Tenders Law also established mechanisms that encourage government procurement of goods made in Israel, which may affect the chances of foreign entities to succeed in government tenders.

One example of such a mechanism is a mandatory reciprocal purchase obligation in government tenders, established in the Mandatory Tenders Regulations (Duty of Industrial Cooperation), 2007 (the Industrial Cooperation Regulations).[14]

According to the Industrial Cooperation Regulations, the Israeli government and other public entities making a purchase from a foreign company in an amount exceeding US$5 million are required to obligate the foreign supplier to purchase products and services in certain amounts from Israeli entities.[15]

The scope of such purchase requirement varies according to the type of transaction:[16] in non-military transactions with ccompanies from countries that are parties to the Government Procurement Agreement (GPA), the foreign company is obligated to purchase 20 per cent of the value of the contract from Israeli suppliers; in national security transactions, the obligation would be to purchase 50 per cent; in all other transactions it would be 35 per cent.[17] In certain situations, the requirements may be revoked or reduced by the Industrial Cooperation Authority at the Ministry of Economy.

According to the Mandatory Tenders Regulations (Preference of Israeli Produce), 1995 (the Made in Israel Regulations), state and governmental corporations are obligated to prefer bidders that undertake to supply Israeli-made goods within the frame of public tenders. Such

12 Notably, the Tenders Law prohibits the inclusion of terms in a tender that are not necessitated by the character and essence of the specific tender itself.

13 Section 3b of the Tenders Law.

14 Section 3 of the Industrial Cooperation Regulations. The requirement also applies to a continuation contract following an original contract that was valued at US$5 million, if the value of the continuation contract exceeds US$500K, made within five years of the original engagement.

15 Section 3 of the Industrial Cooperation Regulations. The requirement also applies to a continuation contract following the original contract that was valued at US$5 million, if the value of the continuation contract exceeds US$500,000, made within five years of the original engagement.

16 Section 6 of the Industrial Cooperation Regulations. Foreign corporations can realise their reciprocal purchase obligations, through direct purchase – for example, using an Israeli subcontractor in the project, or through indirect reciprocal purchase – for example, purchase from domestic industries that are not part of the specific project and are intended for export, investments, service purchases, among others. In 2020 alone, new reciprocal purchase obligations were registered in the amount of US$1.21 billion, following transactions made by the Israeli government with foreign suppliers (The Industrial Cooperation Authority – Annual Summary, December 2020).

17 As of 2029, Israel will no longer be permitted to include a reciprocal purchase obligation condition in transactions involving any entities or transaction types that are covered by the GPA (Ministry of the Economy and Industry 'Reciprocal Purchase Terms Under the GPA Treaty' (May 2019).

preference may be reflected in various manners, as stipulated in the said regulations. For example, preference will be given to bids in which the bidder undertakes to purchase goods made in Israel, when the price of such bid does not exceed 15 per cent of a bid that offers goods that are not made in Israel.[18] Another example is a provision according to which if the successful bid is of a foreign supplier, the publisher of the tender will split the win between the foreign supplier and the bidder who offers goods made in Israel, whose offer was ranked second (in cases where the terms set in the regulations are met). Among other factors, the bidder whose offer is ranked first is given the opportunity to offer goods made in Israel).[19]

IV SECTOR-SPECIFIC REQUIREMENTS

i Prohibited sectors

There are no sectors in which FDIs are categorically prohibited and the Israeli governmental policy is generally encouraging towards foreign investments. We shall discuss below several main examples of sectoral regulatory limitations and oversight powers on foreign investments in Israel.

ii Restricted sectors

Former state-owned entities that have undergone privatisation

There is a specific regulatory regime that applies to companies that were formerly under government control and that are undergoing or have undergone a process of privatisation. The government holds special powers with respect to such companies, including in relation to preserving their Israeli identity. The main legislative act in this context is the Government Companies Act, 1975 (the Government Companies Act).

Under the Government Companies Act, the Ministerial Committee on Privatisation is entitled to declare, via order, that the state has essential interests in a government company that is about to be privatised. Such essential interest may include the need to maintain the character of the company as an Israeli company, whose centre of business and management is in Israel.

A transfer of control of entities that is subject to such an order will require prior approval from the Minister of Finance and from the Minister in charge of the company's field of activity. Under such an order, the government may also apply further restrictions, including, inter alia, restrictions on the transfer of means of control in the company to foreign investors; restrictions on the transfer of company assets outside of Israel; Israeli nationality requirements regarding the company's officers, and a condition requiring that the company's centre of business and operations will be in Israel.

18 Section 3 of the Made in Israel Regulations. A similar requirement is set out regarding municipalities under the Municipalities (Tenders) Regulations, 1987.

19 Section 4(b) of the Made in Israel regulations; Ministry of Finance – Accountant General's Division, TAKAM Directive 7.11.4; Preference for Made in Israel. On 11 November 2020, the government announced its decision to apply the said mechanism to a wider range of tenders, including those issued by local authorities and by local authorities corporations.

The obligation to obtain the requisite approval before transfers of means of control in entities that are subject to an Essential Interests Order is imposed upon both the transferor and the transferee.

As at August 2021, the state has issued five Essential Interest Orders, all of which include restrictions concerning the Israeli identity of the company.[20]

Communications sector

Activity in the communication infrastructure fields in Israel may require the receipt, in advance, of various licences, permits and concessions from the state; these may also include certain FDI requirements.

The Telecommunications (Telecommunications and Broadcast) Law, 1982 (the Telecommunications Law) sets certain limitations on foreign investments in Israeli companies in the telecom industry.

Various Israeli nationality requirements (regarding, inter alia, the corporation's place of registration, and the nationality of its executives, directors and shareholders) are preconditions for the issuance of licences for the provision of communication services, such as TV broadcasting, satellite services and cell phone services.[21]

In addition, the Prime Minister and the Minister of Communication may set out similar requirements, with regard to a telecom corporation declared as an 'essential service provider';[22] furthermore, transferring or acquiring control, 'significant influence', or means of control in an 'essential service provider', requires obtaining prior approval from said Ministers.

Natural gas sector

The field of natural gas has been in accelerated development in Israel since the discovery of three vast reservoirs of natural gas in 2009. There is extensive involvement of foreign entities in the field of natural gas exploration and drilling in Israel. Since 2016, the Ministry of Energy has been conducting tenders for obtaining licences for natural gas exploration in Israel's waters, from which 18 licences for natural gas and oil exploration have been issued, many to foreign entities.[23]

The field of exploration, development and production of natural gas and oil in Israel is subject to extensive regulation, which is primarily regulated by the Petroleum Law, 1952. This Law regulates the granting of 'petroleum rights' (a licence or possession rights). A licence grants the right to explore for petroleum in a defined area, the right to drill in this area and to extract petroleum from it, and the right to take possession if petroleum is discovered.

20 These orders were published thus far in the fields of security, aviation and petroleum.

21 For example, requirements regarding Israeli nationality are set as conditions for issuance of a general cable broadcasting licence, for a licence to produce news as an independent producer and for a 'unified genera' licence. See Sections 6h3, 6t, 6t1 of the Telecommunications Law; Section 10(a) of the Telecommunications (Telecommunications and Broadcasting) (Procedures and Conditions for Obtaining a Unified General Licence) Regulations, 2010.

22 An 'essential service provider' order may be issued by the Prime Minister and the Minister of Communication with government approval; the order may establish that the communication service is an essential service for national security considerations or if it is required for the adequate provision of the services to the public, or for government policy considerations, including competition.

23 Ministry of Energy website at https://www.gov.il/he/departments/news/press_070121.

This regulatory framework also addresses foreign actors' ability to operate in this field. The Petroleum Regulations (Principles of Action for Petroleum Exploration and Production at Sea), 2016 (the Petroleum Regulations)[24] grant the Commissioner of Petroleum Affairs at the Ministry of Energy the authority to reject an application to receive a petroleum right, under different circumstances including, inter alia, the controlling shareholder of the applicant being a foreign country. The commissioner holds wide discretion to reject such applications based on considerations of national security, foreign relations or international commercial trade.

In addition, the Natural Gas Economy Law, 2002 (the Natural Gas Economy Law) provides that a licence to operate in natural gas may only be granted to a company incorporated in Israel.[25] It also authorises the Minister to stipulate in the licence that the management of the licence holder must be physically located in Israel, and that certain officers and officials must be Israeli citizens and residents with suitable security clearance.[26]

Financial sector

The financial services and banking sectors in Israel are heavily regulated. Investments in financial entities supervised by the Supervisor of Banks (the Supervisor) or the Commissioner of the Capital Market, Insurance and Savings (the Commissioner) are subject to obtaining regulatory permits.[27] The financial regulation stipulates many preconditions for receiving such permits, including unique limitations on foreign investments. It is within the discretion of the applicable regulators to determine whether a foreign applicant is compliant with such preconditions and qualifies for the requested permit.

Investment in insurers and provident funds

Holding more than 5 per cent of any particular means of control in an institutional entity[28] is subject to obtaining a 'permit to hold a means of control', granted by the Commissioner.[29] Investment involving the purchase of 'control' is subject to obtaining a 'control permit' from the Commissioner.

A foreign banking corporation or foreign institutional entity that applies for leave to hold a means of control in an Israeli institutional entity must meet unique requirements that arise from its foreign nationality. Among such conditions, it must:

a have sufficiently large operations and sufficient experience in the field, as determined by the Commissioner;

b be subject to supervision in its home country, where banking or financial institution regulations must apply a model of capital requirements and regime of corporate and risk management requirements similar to those in Israel (or provide a level of supervision at least similar to that in Israel); and

24 Section 11 of the Petroleum Regulations.

25 Section 8 of the Natural Gas Economy Law.

26 Section 17 of the Natural Gas Economy Law.

27 The specific permit required depends on the amount of the investment, as a percentage of the total holdings, and the rights accompanying the investment.

28 Defined as an insurer holding an Israeli insurer licence, or a licence as a foreign insurer according to the statute's provisions, as well as provident funds.

29 Section 32(a) of the Financial Services (Insurance) Supervision Law, 1981.

c the parties that hold control of the foreign entity must satisfy at least the same standards of reliability as are required for a controlling shareholder in an institutional entity in Israel.[30]

Investment in a banking corporation

An investor who holds more than 5 per cent of a certain type of means of control in a banking corporation must first obtain a 'permit to hold a means of control' from the Governor of the Bank of Israel (the Governor).[31] If such an investment involves the purchase of 'control', a 'control permit' must be obtained from the Governor.[32]

If a foreign bank applies for a permit to hold a means of control, the Governor will examine the following criteria (in addition to the criteria examined with respect to an Israeli investor):

a the foreign bank must be from a country in which banks are subject to significant supervision that meets international standards (including a requirement that Basel Committee Guidelines be implemented); and

b the foreign bank must be a 'first tier global bank';[33] and there must be reciprocity with respect to corporate banking licensing between Israel and the applicant's country of origin.[34]

If the foreign bank that requests the permit has holdings of institutional entities that are not supervised by a stability oversight authority at international standards, its holding cannot exceed 15 per cent of the means of control that constitute the controlling core.

Investment in a processor and credit card company

To purchase control or a means of control in a credit card company or in a processing company, a foreign processing company will be required to satisfy special conditions (in addition to those applied to an Israeli investor). These include, inter alia, that:[35]

a the foreign processing company holds a processing licence in an OECD country, of a type and range that is not less than that of the processing company that it wishes to acquire;

b the country in which the processing company and the companies in its chain of control are incorporated ('the parent countries') do not place any restrictions on capital transactions;

c the parent countries impose supervision at the same standards customary in Israel;

d the parent countries are not countries that present high risks regarding money laundering and terrorist financing;

30 Policy for Controlling Institutional Entities, Ministry of Finance – Capital Market, Insurance and Savings Authority, 12 February 2014.

31 Section 34(a) of the Banking Law (Licensing), 1981 (the Banking Licensing Law).

32 Section 34(b) of the Banking Licensing Law.

33 Israel Bank – Supervisor of Banks, Criteria and General Terms for an Applicant for a Permit to Control and [for a Permit to] Hold a Means of Control in a Banking Corporation, 11 July 2013, Section 3.2.4.

34 Section 6(6) of the Banking Licensing Law.

35 Israel Bank – Supervisor of Banks, Criteria and General Terms for an Applicant for a Permit to Control and Hold a Means of Control in a processing company and Credit Card Company, 29 May 2018.

e the supervisory authorities in the parent countries must provide consent to the holding of a processing company in Israel; and

f the supervisory authorities in the parent countries must confirm that there are no restrictions on the transferring of information to the Supervisor of Banks in Israel concerning the foreign processing company and its activities.

Notably, a foreign investor that requests a control permit for a processing company will also be subject to more extensive reporting duties in the framework of the application for the permit than those that would apply to an Israeli investor applying for a similar permit.

Regulation encouraging foreign investment in Israel

Israeli regulation generally encourages foreign investments, albeit there are specific sectoral restrictions and the general national security consideration.

One example for such supportive regulation is the Law for the Encouragement of Capital Investments, 1959, (the Investment Law). The Investment Law provides incentives for industrial enterprises (as defined under the Investment Law) to make capital investments in productive assets, such as production facilities.

An approved enterprise programme (a specific investment programme of a company that received an 'approved enterprise' certification, based on the scope of investment and characteristics of the facility or asset, from the Investment Center of the Israeli Ministry of Economy and Industry prior to 2005) is entitled to certain benefits and incentives, including a corporate tax exemption period and accelerated depreciation on property and equipment. A company that has an approved enterprise programme ('approved enterprise') is eligible for special tax benefits if it qualifies as a foreign investors' company (i.e., if more than 25 per cent of the controlling rights are held by foreign residents).

Undistributed income generated by an approved enterprise for a period of between two to 10 years is exempt from corporate tax and, for the remainder of the benefits period, depending on the percentage of foreign investors in the company, is entitled to a reduced corporate tax rate of between 10 per cent and 25 per cent.[36]

Income generated by a 'preferred company' through its 'preferred enterprise', which includes a company incorporated in Israel that has preferred enterprise status and is controlled and managed from Israel, among others, is also entitled to benefits, such as a reduced corporate tax rate of 16 per cent, a rate that may be further reduced to 9 per cent and 7.5 per cent in applicable development zones.[37]

Income generated by a 'preferred company' through its 'preferred technology enterprise', is entitled to benefits as well, including a reduced corporate tax rate of 12 per cent.[38] In addition, subject to the fulfilment of certain conditions, if dividends are paid to a direct foreign parent company holding at least 90 per cent of the shares of the preferred company, a reduced withholding tax rate of 4 per cent applies.

36 As introduced in a 2005 amendment to the Investment Law.

37 As introduced in a 2011 amendment to the Investment Law.

38 As introduced in a 2017 amendment to the Investment Law.

V TYPICAL TRANSACTIONAL STRUCTURES

i General

Israel's regulation of foreign investment is relatively light and Israeli corporate practitioners are influenced by US-style corporate practices. Indeed, Israeli corporate law generally looks to Delaware corporate law for trends and solutions. For example, as stated above, other than with respect to specific sensitive industries, there are generally no residency requirements for directors and officers of Israeli companies.

Israeli courts also tend to look to Delaware law for inspiration in corporate cases. They have adopted a modified version of the business judgement rule and are protective of the rights of foreign investors.

Investors in Israeli companies have the standard range of investment and acquisition options available, such as the creation of preferred shares with US-style rights and the availability of all customary investor rights in venture capital investments.

Israel's corporate law is relatively extensively codified, having undergone several evolutions over the years. Key legislation includes the Companies Law, 1999, (the Companies Law), which regulates the activities of corporate entities in Israel; and the Securities Law, 1968, which regulates the Israeli capital market, primarily with respect to disclosure requirements and trading regulations, with an emphasis on public companies.

Given that many 'old industry' Israeli companies have traditionally been controlled by a controlling shareholder, Israeli corporate law is protective of minority rights, such as through the imposition of fiduciary duties on controlling shareholders towards minority shareholders, which can be beneficial to foreign minority investors.

ii Setting up a business in Israel

A foreign entity that seeks to establish itself in Israel would, typically, either create a local branch (also known as registration of a 'foreign company') or incorporate an Israeli subsidiary of a foreign entity.

Incorporating a subsidiary in Israel means that the foreign company will own the shares of a separate legal entity in Israel. The subsidiary pays taxes in Israel, and any transactions between the Israeli subsidiary and its foreign parent would need to comply with transfer pricing rules. Furthermore, any dividends paid up from the Israeli subsidiary to its parent would be subject to withholding tax in Israel (subject to any tax treaties between the jurisdictions involved).

A 'foreign company' is not a separate entity from the foreign entity, but rather an extension of the foreign entity into Israel. Establishing a 'foreign company' raises questions regarding the foreign entity's status as a permanent establishment in Israel for tax purposes, which should be explored before using the 'foreign company and local branch' option.

iii Joint ventures

Joint ventures are possible under Israeli law. Certain joint ventures require registration of a 'general partnership' under Israel's Partnership Ordinance (New Version), 1975.

As is generally the case with respect to all corporations, Israeli law is very liberal when it comes to structuring joint ventures. Specific taxation aspects should be analysed prior to entering into a joint venture.

iv M&As

Generally, there are no major restrictions under Israeli law on the way parties to a private M&A deal may structure the deal; nor, subject to certain industry-specific legislation as stated above, are there generally any limitations on the foreign ownership of Israeli companies. Parties to an acquisition of shares of a private company will customarily enter into a share purchase agreement, which includes provisions that are typically similar to those that can be found in US private M&A deals (e.g., representations and warranties, interim period covenants, indemnification provisions and closing conditions).

The Companies Law also offers the possibility of a statutory 'bring-along' pursuant to which, if a person offers to buy shares or a class of shares of a company and shareholders holding at least 80 per cent of the shares to be transferred agree to the acquisition proposal, then the offeror may also acquire the shares of the other (non-accepting) shareholders on the terms proposed to the shareholders that accepted the proposal. This 80 per cent threshold is the default, and other rates may be agreed upon and prescribed in a company's articles of association.

A purchaser may acquire a company via the purchase of assets or a merger, particularly through a reverse triangular merger, which has come to be a preferred route for acquiring full ownership of Israeli companies. In this structure, a wholly owned Israeli subsidiary of the acquiring company, usually established for the purpose of the merger, will merge with and into the target company, with the target company becoming a wholly-owned subsidiary of the acquiring company.

With regards to public companies, tender offers are also a possible method of acquisition. In this scenario, the acquirer offers to purchase all or some of the shares of the target company. If the acquiring company desires to acquire the entire company, the offer may be made conditional upon the successful acquisition of the complete acquisition. The Companies Law also includes 'squeeze out' mechanisms of minority shareholders.

A 'special' tender offer (as opposed to a 'full' tender offer) is triggered by any acquisition that results in the acquiring company crossing the 25 per cent or 45 per cent thresholds in a company where, at the time of the offer, no shareholder is in possession of holdings meeting that threshold.

VI OTHER STRATEGIC CONSIDERATIONS

i Merger control

Depending on the circumstances, joint ventures may be subject to merger control provisions or to the restrictive arrangements provisions of the Israeli Competition Law, 1988 (the Competition Law).

According to the Israel Competition Authority's Pre-merger Guidelines, the distinction between a restrictive arrangement and a merger is not always clear and may differ from case to case, as there is no conclusive test in this respect.

An important parameter is the distinction between a joint venture that creates a new activity (usually classified as a restrictive arrangement), and a joint venture that gives one party influence over the existing activity of another party (usually classified as a merger).

The general merger thresholds apply to foreign investments. A merger transaction must be reported to the Israel Competition Authority pursuant to the Competition Law, only if:

a at least two of the parties involved have sufficient nexus to Israel; and

b at least one of three filing thresholds is met.

Both the nexus requirement and the filing thresholds are evaluated based on a group of entities (all entities that control or are controlled by the merging party, and all entities controlled by such entities, whether directly or indirectly).

The filing thresholds are as follows:

a the combined turnover of the merging parties in Israel exceeds 359,300,000 shekels (approximately US$111 million and the turnover of at least two parties is at least 10 million shekels (approximately US$3 million);[39]

b a party to the transaction is a monopoly in any defined market in Israel;[40] and

c as a result of the transaction, the combined market share of the parties will exceed 50 per cent at any level of the supply chain of any relevant market in Israel.

ii Additional considerations

As in any other jurisdiction, there are certain factors of which a foreign investor in an Israeli entity or a company that wishes to acquire an Israeli entity should be aware. We will touch on two such factors, which are typical areas of confusion for foreign players in the Israeli market: government funding and employment law.

Many Israeli companies receive grants from the Israeli Innovation Authority (IIA), which come with certain restrictions in relation to the company's know-how. The main restrictions relate to the place of manufacturing of products, the ability to transfer funded-IP outside of Israel, and the requirement of foreign investors and acquiring companies to sign an 'undertaking' in favour of the IIA. The restrictions continue to apply even after the IIA grant is repaid. It is critical to understand the commercial impact of an IIA grant.

Regarding employment law, one should verify the applicability of collective bargaining agreements, which may provide covered employees with particular benefits even when their personal employment agreements provide lower benefits, or may even make no reference at all to the relevant issue. In addition, many such agreements require the employing entity to (at least) consult with the union or employees council prior to any change of control transaction. Other employment-related matters to be aware of include:

a the issue of the likely classification of consultants as employees (if claimed by a consultant);

b the requirement that a hearing be conducted prior to termination of employment and that prior written notice (of up to 30 days, unless a longer – but not shorter – period is agreed contractually) be provided in the event of termination;

c specific laws relating to overtime payments and their applicability to senior positions; and

d an array of social benefits and severance pay rules.

39 A recent proposed amendment to the relevant regulations suggested that the threshold of 10 million shekels in turnover for at least two parties be raised to 20 million shekels. In the interim period, the General Director of the Israel Competition Authority has announced that she will consider extending a waiver from filing in cases whereby a party's turnover is below 20 million shekels.

40 For the purpose of this threshold, a monopoly is defined as an entity that holds a market share exceeding 50 per cent in any defined market, even if it is irrelevant to the transaction.

VII OUTLOOK

Israel does not have a central supervision regime for foreign investments and the bulk of existing FDI regulation is sector-dependent. At the same time, certain legislative areas do set out general FDI controls that may apply to a broad range of transactions, such as FDI regulation deriving from considerations of national security, restrictions on transactions that entail the purchase of land and requirements arising in state tenders.

In 2020, the Advisory Committee was established, as a centralised mechanism for advising regulators of various sectors with regard to transactions that may give rise to national security considerations.

The Advisory Committee has only recently begun operating formally and it is expected that future major foreign investments in Israel will undergo its scrutiny, especially considering the increasing involvement of foreign entities in infrastructure and public utilities projects. As previously mentioned, neither the examining protocols nor additional products of the Advisory Committee's work are made public. Nevertheless, the nature of the relationship between the Advisory Committee and the sectoral regulators, as well as the Advisory Committee's range of considerations, should become clearer in the near future, based on cumulative experience.

Requirements in the FDI field (such as Israeli nationality requirements or restrictions on transferring ownership) may also be found in agreements between the state and private entities, and among the terms included in permits and licences. Naturally, directives of this nature cannot always be predicted nor detected through reference to legislation or public sources and identification of such requirements will be part of the due diligence process of the acquired company or activity.

A tendency worth noting is the Israeli government's policy regarding a reduction of the regulatory burden in Israel. In August 2021, the government published a resolution aimed at promoting smart regulation policies in Israel to enable the reduction of any excesses within the regulatory burden, giving weight to the costs of compliance with regulation and its implications for advancing the economy and society. For example, the resolution provided that regulation will generally be determined based on customary international standards or on regulatory requirements that are already implemented in developed countries with significant markets.

Appendix 1

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Adi represents Israeli companies and multinational entities operating in Israel with various regulatory issues. As part of the firm's regulatory and governmental practice, Adi facilitates complex interacting processes with governmental agencies and committees, often working side-by-side with a team of professional consultants (i.e., media and public relations specialists, economists and lobbyists) to achieve the best outcome for our clients.

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