# The Foreign Investment Regulation Review: Israel

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## Overview

Israel, widely recognised as the 'start-up nation', is known for its abundance of cutting-edge technological innovations in a wide variety of fields (autonomous mobility, cybersecurity, energy, digital health, fintech, agritech and others), which garner great interest from a variety of international investors and acquiring parties, such as venture capital firms, private equity funds and strategic players.

Israel does not have any general unified foreign direct investment (FDI) legislation or approval regime. As a result, there are no broad cross-sector consolidated controls on foreign investments in the country. Generally, foreign entities can purchase and sell assets and securities in Israel at will, and FDI is not categorically prohibited in any particular sector. That said, there is a series of stand-alone, sector-specific FDI regulations and requirements.

These restrictions and requirements often pertain to investments in companies operating in public utility and infrastructure fields, or those affecting national security. FDI requirements may also stem from terms included in government licences, public tenders or concessions.

Under Israel's regulatory structure, regulators overseeing a specific sector can generally exercise relatively wide discretion regarding the issuance and revocation of licences, concessions and permits. As such, regulators can include specific conditions, restrictions or approval requirements regarding FDI, and subsequently alter them as they see fit. 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 the FDI-related obligations that may be implemented in licences, concessions and permits, contractual regulations have become increasingly common in Israel. FDI conditions can also be found in agreements between the government and private entities.

Despite the generally decentralised nature of FDI regulation in Israel, a central mechanism for examining foreign investments from a national security perspective was formulated in 2019, in the form of the Advisory Committee for National Security Affairs in Foreign Investments (the Advisory Committee), which is discussed below.

## Year in review

During the past year, foreign entities have participated in extensive activities in Israel. This, despite the aftershocks of the global covid-19 crisis, international instability resulting from the war in Ukraine, and Israel's own political instability, as reflected by its five national elections in just three years.

FDI in Israel in 2021 totalled approximately US$29.6 billion, as compared with the US$24.3 billion invested in 2020 and US$17.4 billion invested in 2019. The current scope of foreign investments in Israel in the first quarter of 2022 stands at around US$6 billion.[2] This level of foreign investment activity exemplifies the ease with which foreign investors can do business in Israel.

Foreign investments and the involvement of foreign companies in Israeli innovation reached a broad range of diverse fields in 2022, including high-tech, energy, infrastructure and others. Recent and outstanding examples are the tender for the privatisation of Haifa Port, the second-largest port in Israel, won by a consortium of Indian and Israeli companies, and the official opening and operation of the new port of Haifa, on 1 September 2021, by Shanghai International Port Group.

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 Ministry of Finance's chief economist was established and subsequently charged with the responsibility for examining national security concerns arising 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. These can include cases devoid of previous FDI regulatory requirements. The committee bases its recommendations on confidential criteria. Formally, the regulator is charged with making the final decision about the transaction. However, the national security committee's recommendations carry substantial weight with sectoral regulators.

Thus far, the advisory committee has published a single report on its activity between the beginning of 2020 and Q3 2021. Neither the transactions it monitors and evaluates nor its recommendations to regulators are made public. However, it was specified that the committee examined potential transactions worth approximately 43 billion shekels during that period. In comparison, the total amount of foreign investment transactions made during the same period are estimated to be worth approximately US$32 billion.

Existing legislation also includes substantial oversight powers over national security considerations in foreign investments, as used by 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 across those sectors that the government views as critical to the economy and national security.

## Foreign investment regime

### Laws and regulations

At present, there are no centralised FDI regulations in Israel. As a result, regulators have no unified cross-sector considerations to refer to when 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 national security considerations, restrictions on transactions that entail the purchase of land and requirements linked to state tenders.

#### National security legislation

In addition to the recent establishment of the advisory committee, Israel has implemented various laws designed to protect its security interests, particularly with respect to national security concerns pertaining to investments made by foreign entities. A summary of each of the main laws is provided below.

##### Defence Corporations Law (Protection of Security Interests) 2006

The Defence Corporations Law (Protection of Security Interests) of 2006 (DCL) 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 know-how or the use of equipment by security forces,[3] provided they find that national security is likely to be harmed. Such circumstances can include 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 relating to the corporation or its activity.[4]

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.[5]

The Ministers are also entitled to set Israeli nationality requirements with respect to the control of a defence corporation and its officers, as well as residency requirements, such that ongoing management of a defence corporation and its centre of business is in Israel.[6] Additionally, they can require a defence corporation to obtain prior approval from the Minister of Defence before carrying out a joint venture or changing its corporate structure,[7] and 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.[8]

##### Defence Export Control Law 2007

The Defence Export Control Law of 2007 (DECL) regulates the sale and export of defence equipment, including any equipment or technology sold to, or intended for use by, security forces.[9] The DECL applies to the sale of defence equipment and to the transfer of defence know-how outside Israel and, therefore, is broader than the DCL in scope. Under the DECL, any company selling or exporting defence equipment or information must be registered and licensed by the Ministry of Defence and is obliged to report any changes to its control structure.[10]

The DECL also regulates the sale of dual-use equipment, as defined by the Wassenaar Arrangement on Export Controls for Conventional Arms and Dual-Use Goods and Technologies, according to who the end user of said equipment is. Dual-use equipment sold or intended to be used by security forces is considered a defence export and thus fits within the scope of the DECL including its relevant FDI restrictions.[11] Exports of equipment to civilian end users, however, must be licensed by the Ministry of Economy. That said, it is not otherwise limited or regulated with respect to foreign investments.[12]

#### Trade with the Enemy Ordinance 1939

The Trade with the Enemy Ordinance of 1939 prohibits the conduct of direct or indirect trade between the state of Israel and its citizens (including corporations), an enemy state or an entity in an enemy state, an enemy subject, or for the benefit of any of the foregoing.[13]

#### Law on the Struggle Against Iran's Nuclear Programme 2012

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

#### Law for the Prevention of Distribution and Financing of Weapons of Mass Destruction 2018

The Law for the Prevention of Distribution and Financing of Weapons of Mass Destruction of 2018 prohibits any engagement in economic activity with an entity declared (by the United Nations Security Council or by order of the Minister of Finance in consultation with the Minister of Foreign Affairs and the Minister of Defence), serving as an accessory to the distribution and financing of weapons of mass destruction, or with an entity related to that assisting entity, unless that entity has received explicit permission from the Minister of Finance.[14]

### Real estate

The Israeli government supervises the transfer of Israeli lands to non-Israelis under the Israel Lands Law of 1960 (the Land Law). According to the Land Law, it is forbidden to sell or otherwise transfer 'property rights' pertaining to Israeli land without first obtaining permission 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 extending a lease for an aggregate period exceeding five years, as well as an undertaking to transfer those ownership or leasing rights.

The transfer of property rights requires the Chairman first to consult with the Minister of Defence and the Minister of Foreign Affairs, and then consider, among other things, the buyer's identity, the buyer's relationship to Israel, the purpose of the purchase, and the public's best interests and security, before approval can be granted.

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

### Government tenders

Tenders published by the state of Israel and by public entities are governed by the Mandatory Tenders Law of 1992 (the Tenders Law). FDI oversight may be exercised through conditions set in tenders and procurement contracts.[15]

One of the sources for general authority to exercise oversight can be found in a provision of the Tenders Law, according to which the Israeli government is authorised, as approved by the Foreign Affairs and Defence Committee of the Knesset (the Israeli Parliament), to order that the state of Israel or a government corporation will not enter into a transaction with a particular foreign country or supplier,[16] based on foreign policy considerations.

The regulations promulgated under the Tenders Law also established mechanisms that encourage government procurement of goods made in Israel. These, in turn, may affect foreign entities' chances of winning government tenders.

For example, the Mandatory Tenders Regulations (Duty of Industrial Cooperation) of 2007 (the Industrial Cooperation Regulations)[17] stipulate that the Israeli government and other public entities must engage in reciprocal purchases when purchases are made from a foreign company and through government tenders. In such a case, when purchases exceed US$5 million, the foreign supplier is obliged to purchase products and services in certain amounts from Israeli entities as well.[18]

The scope of this purchase requirement varies according to the type of transaction.[19] In non-military transactions with companies from countries that are parties to the Government Procurement Agreement (GPA), the foreign company is obliged to reciprocate with a purchase from Israeli suppliers worth 20 per cent of the value of the contract. In national security transactions, the obligation would be for the purchase to be worth 50 per cent of the value of the contract. In all other transactions, the obligation would be 35 per cent.[20] 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) of 1995 (the Made in Israel Regulations), the state and government corporations must give priority to bidders that undertake to supply Israeli-made goods within the frame of public tenders. For example, priority must be given to bidders seeking to purchase goods made in Israel, insofar as the price of a bid is no more than 15 per cent higher than any other bids.[21] If the winning bid is made by a foreign supplier, the tender's publisher must split the win between the foreign supplier and the next highest bidder offering goods made in Israel (provided 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).[22]

## Sector-specific requirements

### i Prohibited sectors

Foreign investments are not categorically prohibited in any particular sector. Rather, Israeli government policy is generally encouraging towards foreign investments. Several main examples of sectoral regulatory limitations and oversight powers on foreign investments in Israel are discussed below.

### ii Restricted sectors

#### Former state-owned entities that have undergone privatisation

Companies that were formerly under government control, and companies that are undergoing or have undergone privatisation, are subject to specific regulations regarding foreign investments, with the government having special oversight authority over such companies. The main legislative act in this context is the Government Companies Act of 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. Among other things, these essential interests may include the need to maintain the company's Israeli identity and to keep its centre of business and management in Israel.

To transfer control of entities subject to such an order, prior approval must first be obtained from the Minister of Finance and the Minister in charge of the company's field of activity.[23] 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 Israel; Israeli nationality requirements regarding the company's officers; and a condition requiring the company's centre of business and operations to be established, and remain, in Israel.

To date, the state has issued five Essential Interest Orders, all of which include restrictions concerning the former state-owned entity's Israeli identity.[24]

#### Communications sector

Activity within Israel's communications infrastructure fields may require companies to obtain licences, permits or concessions from the state. Depending on the specific area of activity, these government approvals may also include FDI requirements.

The Telecommunications (Telecommunications and Broadcast) Law of 1982 (the Telecommunications Law) was significantly amended in July 2022, replacing the licensing regime for many telecommunications services with a registration regime. However, the amendment does not significantly change the existing regulatory regime in areas considered sensitive, which still include certain limitations on foreign investments in Israeli telecommunications companies.

Various Israeli nationality requirements serve as preconditions for the issuance of licences for the provision of certain communication services, such as television broadcasting and satellite services based in Israel.[25] These include, inter alia, the corporation's place of registration, and the nationality of its executives, directors and shareholders.

In addition, the Prime Minister and the Minister of Communications may set out similar requirements with regard to a telecommunications corporation declared as an 'essential service provider'.[26] The transfer or acquisition of control, 'significant influence' or means of control in an 'essential service provider' require prior approval to be obtained from the aforesaid ministers.

#### Natural gas sector

There has been accelerated development in Israel's natural gas field since the discovery of three vast reservoirs of natural gas in 2009. Foreign entities are extensively involved in Israel's natural gas exploration and drilling. Since 2016, the Ministry of Energy has been issuing tenders for obtaining licences for natural gas exploration in Israel's waters. To date, 18 licences for natural gas and oil exploration have been issued, many to foreign entities, with additional tenders taking place.[27]

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

This regulatory framework also addresses foreign entities' ability to operate within this field. The Petroleum Regulations (Principles of Action for Petroleum Exploration and Production at Sea) of 2016 (the Petroleum Regulations)[28] grant the at the Ministry of Energy's Commissioner of Petroleum Affairs the authority to reject an application for petroleum rights 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 national security, foreign relations or international commercial trade considerations.

In addition, the Natural Gas Economy Law of 2002 (the Natural Gas Economy Law) provides that a licence to operate in the natural gas field may be granted only to a company incorporated in Israel.[29] It also authorises the Minister to stipulate in the licence that licence holders must be physically managed in Israel, and that certain officers and officials must be Israeli citizens and residents with suitable security clearance.[30]

### Electricity sector

Israel's electricity sector is highly regulated, with a single entity, the Israel Electric Company, controlling most of its conduction and production infrastructure. However, the privatisation of existing power plants, the construction of privately owned production facilities and the transfer of system management capabilities to a separate entity has opened up the electricity production market in recent years.[31]

Although the Israel Electricity Authority has declared its commitment to decentralise the Israeli power grid and allow entrepreneurs easier access to the electricity production and conduction markets, this remains a highly regulated sector. The ability to operate within each of its segments is subject to first obtaining the relevant government licences.[32]

The Electricity Market Law of 1996 (EML) imposes limitations on foreign investments, as pertaining to licences issued under its virtue. For example, the transfer or acquisition of control of a licensed entity is subject to prior approval by the Israel Electricity Authority. If the licence pertains to an 'essential service provider',[33] approval is also required for holding any means of control.

The EML also authorises the Minister of Energy to stipulate Israeli nationality requirements on 'essential service provider' licence holders. For example, control over an 'essential service provider' licence may have to be held by Israeli citizens and residents. Additionally, there could be an imposed limit on the rate of means of control held by non-Israelis, and certain officers within the licence holder may be required to be Israeli citizens and residents.

### Financial sector

The financial services and banking sectors are also 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 regulatory permits.[34] Financial regulations stipulate many preconditions for receiving such permits, including unique limitations on foreign investments. It is within the relevant regulators' purview to determine whether a foreign applicant is compliant with such preconditions and qualifies for the requested permit.

#### Investment in insurers and provident funds

Any entity holding more than 5 per cent of a particular means of control in an 'institutional entity'[35] requires a 'permit to hold a means of control', granted by the Commissioner.[36] Investments involving the purchase of 'control' are subject to a 'control permit' obtained from the Commissioner.

A foreign banking corporation or foreign institutional entity applying for a permit to hold a means of control in an Israeli institutional entity must meet unique requirements. Among these conditions, the foreign banking corporation or foreign institutional entity must have sufficiently large operations and sufficient experience in the field, as determined by the Commissioner. The foreign corporation or entity must be subject to supervision in its home country, where banking or financial institution regulations must apply a model of capital, corporate and risk management requirements similar to those in effect in Israel (or provide a level of supervision at least similar to that in Israel). Additionally, the parties holding control of the foreign entity must satisfy at least the same standards of reliability as are required for a controlling shareholder in an Israeli institutional entity.[37]

#### Investment in a banking corporation

To hold more than 5 per cent of a certain type of means of control in a banking corporation, the investor must obtain a 'permit to hold a means of control' from the governor of the Bank of Israel (the Governor)[38] (i.e., acquiring 'control' is subject to obtaining a 'control permit' from the Governor).[39]

An application for a control permit by a foreign bank will require the Governor to examine certain criteria (in addition to the criteria examined regarding an Israeli investor). The foreign bank must be from a country in which banks are subject to significant supervision that meets international standards (including that the Basel Committee Guidelines be implemented), and it must be a 'first tier global bank'.[40] Furthermore, there must be reciprocity with respect to corporate banking licensing between Israel and the applicant's country of origin.[41]

#### Investment in a processing or credit card company

A foreign entity's acquisition of control or a means of control in a credit card company or a processing company is subject to special conditions (in addition to those applied to an Israeli investor). These include, inter alia, that:

a. a foreign processing company holds a processing licence in a member country of the Organisation for Economic Co-operation and Development, 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 as are customary in Israel;
d. the parent countries are not at high risk of falling prey to money laundering or the financing of terrorism;
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 transferring information to the Supervisor of Banks in Israel concerning the foreign processing company and its activities.[42]

It should also be noted that more extensive reporting duties are required of a foreign investor applying for a control permit for a processing company, than those that would apply to an Israeli investor.

#### Regulation encouraging foreign investments in Israel

Israeli regulation is generally encouraging towards foreign investments. As an example, the Law for the Encouragement of Capital Investments of 1959 (the Investment Law) provides incentives for industrial enterprises to make capital investments in productive assets, such as in production facilities.

A company in possession of an approved enterprise programme under the Investment Law (an approved enterprise) is eligible for special tax benefits, provided that it qualifies as a foreign investors' company (i.e., more than 25 per cent of the controlling rights are held by foreign residents).

Undistributed income generated by an approved enterprise is exempt from corporate tax for a period of between two and 10 years. For the remainder of the benefits period, an approved enterprise is entitled to a reduced corporate tax rate of between 10 per cent and 25 per cent, depending on the percentage of foreign investors in the company.[43]

Income generated by a 'preferred company' (including foreign companies) through its 'preferred enterprise' (including a company incorporated in Israel that has, among other things, 'preferred enterprise' status and is controlled and managed from Israel) can also be eligible for benefits, such as a reduced corporate tax rate of 16 per cent, which may be further reduced to 9 per cent and 7.5 per cent in applicable development zones.[44]

Income generated by a 'preferred company' through its 'preferred technology enterprise' is eligible for benefits, including a reduced corporate tax rate of 12 per cent.[45] In addition, and 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 preferred company's shares, a reduced withholding tax rate of 4 per cent applies.

## Typical transactional structures

### i General

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

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 foreign investors' rights.

Investors in Israeli companies can access the standard range of investment and acquisition options, 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 of 1999 (the Companies Law), which regulates the activities of corporate entities in Israel, and the Securities Law of 1968, which regulates the Israeli capital market, primarily with respect to disclosure requirements and trading regulations, placing an emphasis on public companies.

Given that many 'old industry' Israeli companies are traditionally controlled by a controlling shareholder, Israeli corporate law takes pains to protect minority rights. This is done 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 seeking to establish itself in Israel would, typically, either create a local branch (by registering as a 'foreign company') or be incorporated as an Israeli subsidiary of the foreign entity.

Becoming incorporated as 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. Further, any dividends paid by the Israeli subsidiary to its parent would be subject to withholding tax in Israel (i.e., they would be subject to any tax treaties between the jurisdictions involved).

A 'foreign company' is not separate from the foreign entity but rather an extension of the foreign entity in Israel. Establishing a 'foreign company' raises questions regarding a 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 as a 'general partnership' under Israel's Partnership Ordinance [New Version], 5735-1975.

As is generally the case with 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 Mergers and acquisitions

Generally, Israeli law does not place any major restrictions on how parties involved in a private merger or acquisition may structure the deal. Nor are there generally any limitations on the foreign ownership of Israeli companies, apart from the industry-specific legislation stated above. When multiple parties seek to acquire shares in a private company, they will customarily enter into a share purchase agreement, which includes provisions that are typically similar to those found in US private merger or acquisition deals (such as 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 in 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, according to the terms proposed to the shareholders who accepted the proposal. This 80 per cent threshold is the default. Other rates may be agreed and prescribed in a company's articles of association.

A purchaser may acquire a company via the purchase of assets or a merger, with reverse triangular mergers becoming 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.

As regards public companies, tender offers are also a possible method of acquisition. In this circumstance, 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, an offer may be made conditional on the successful acquisition thereof. 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 threshold in a company where, at the time of the offer, no single shareholder is in possession of holdings meeting that threshold.

## Other strategic considerations

### i Merger control

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

According to the Israel Competition Authority's (ICA) 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 litmus test but, rather, a substantive assessment of the transaction in question.

An important parameter is the distinction between a joint venture that creates a new activity with no transfer of existing assets into the joint venture (which will usually be classified as a restrictive arrangement), and a joint venture that gives one party influence over an existing activity of another party (which will usually be classified as a merger). Other important parameters that affect the classification of joint ventures are the nature and strength of the link created between the parties, the nature of the structural integration and the stability of such ties.

General merger thresholds apply to foreign investments. A 'merger of companies' is defined under the Competition Law as the acquisition of the principal assets of the target company or more than 25 per cent of (1) the outstanding shares, (2) the voting rights, (3) the rights to appoint directors or (4) the dividend rights of the target company. A merger transaction must be reported to the ICA pursuant to the Competition Law, provided that at least two of the parties involved have sufficient nexus to Israel, and at least one of three filing thresholds is met. Both the nexus requirement and the filing thresholds are evaluated based on a group basis (i.e., all entities that control or are controlled by the merging party, and all entities controlled by those entities, whether directly or indirectly).

The filing thresholds are as follows.

a. As a result of the transaction, the combined market share of the parties exceeds 50 per cent at any level of the supply chain of any relevant market in Israel.
b. The combined turnover of the merging parties in Israel exceeds 367,930,000 shekels and the turnover of at least two parties is at least 20 million shekels.[46]
c. A party to the transaction holds a monopoly in any defined market within Israel.[47]

### ii Additional considerations

As with any other jurisdiction, there are certain factors that foreign investors in Israeli entities, or companies wishing to acquire Israeli entities, should consider. We 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, such as those relating to where manufacturing takes place, how funded intellectual property is transferred out of Israel, and the requirement for foreign investors and acquiring companies to sign an 'undertaking' in favour of the IIA. Note that the restrictions continue to apply even after the IIA grant is repaid. It is critical to understand the commercial effects of an IIA grant.

Regarding employment law, one should verify the applicability of collective bargaining agreements, which may provide covered employees with particular benefits, beyond those included in their personal employment agreements. 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 likely classification of consultants as employees (if claimed by a consultant);
b. the requirement to conduct pre-termination hearings for employees (following the provision of prior written notice a minimum number of days before the hearing date, unless a longer – but not shorter – period is agreed contractually);
c. specific laws relating to overtime payments and their applicability to senior positions; and
d. an array of social benefits and severance pay rules.

## 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 for National Security Affairs in Foreign Investments 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 been in operation for about two years and, according to its report, has examined a significant (but undisclosed) number of potential foreign investments. It is expected that future major foreign investments in Israel will be subject to its scrutiny, especially considering the increasing involvement of foreign entities in infrastructure and public utilities projects. It is hoped that the exact nature of the relationship between the Advisory Committee and the sectoral regulators, as well as the Committee's range of considerations, will be clarified in the near future, based on cumulative experience.

FDI-related requirements, such as Israeli nationality requirements, or restrictions on ownership transfers, may also be found in agreements between the state and private entities, as well as in government permits and licence terms. Naturally, directives of this nature cannot always be predicted or detected through reference to legislation or public sources. The process of identifying these requirements must be included in an acquiring company's due diligence efforts.

The government passed the Regulatory Principles Law in 2021. The aim of this Law is the promotion of smart regulation policies in Israel, enabling the reduction of any excesses within the regulatory burden, and giving weight to the costs of complying with regulations and the implications for advancing the economy and society.

Although the new legislation has yet to come into effect fully, and its implementation has only just begun, it should be noted that it stipulates that regulation will generally be determined on the basis of customary international standards or on regulatory requirements that are already implemented in developed countries with significant markets.[48] In addition, the new legislation provides for the establishment of a unified regulation database, which may simplify proficiency and, subsequently, compliance with Israeli investment regulations.[49]

### Footnotes

[1] Adi Wizman is a partner and Idan Arnon is an associate at Yigal Arnon – Tadmor Levy.

[2] According to Bank of Israel data, available at **https://www.boi.org.il/he/DataAndStatistics/Pages/MainPage.aspx?Level=2&Sid=26&SubjectType=2** (last accessed 31 August 2022).

[3] Pursuant to Section 3(a) of the Defence Corporations Law (Protection of Security Interests) of 2006 (DCL), a corporation may be declared a 'security corporation' even if most of its activity is not security activity, but if the security activity is does carry out is of significant security importance.

[4] DCL, Section 3(b).

[5] ibid., Section 5(a).

[6] ibid., Section 6(b)(a), Section 6(2)(b)–(c).

[7] ibid., Section 6(5)(a).

[8] ibid., Section 6(3)(a).

[9] Defence Export Control Law of 2007 (DECL), Section 2.

[10] DECL, Sections 3(1), 15(a)(2), 28(d).

[11] ibid., Section 2.

[12] Import and Export Ordinance (Oversight of export of dual-use goods, services, and technologies) of 2006, Section 3(a).

[13] 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 that person had any commercial, financial or other relations with the enemy or for the benefit of an enemy, and especially if that person supplied, received, transported or traded goods with the enemy or for the benefit of the enemy; 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; or fulfilled any obligation towards an enemy; or executed any obligation on behalf of an enemy. Purchasing enemy currency (banknotes or coins in circulation, banknotes and coins from any territory subject to the sovereignty of a power at war with Israel) is also considered trade with the enemy. The transfer or allocation of securities by the enemy or on behalf of the enemy, or the allocation of securities to the enemy will not be valid, except with the consent of the Minister of Finance.

[14] Law for the Prevention of Distribution and Financing of Weapons of Mass Destruction of 2018, Section 5(a).

[15] Mandatory Tenders Law of 1992 (Tenders Law), Section 3(b).

[16] id.

[17] Mandatory Tenders Regulations (Duty of Industrial Cooperation) of 2007 (Industrial Cooperation Regulations), Section 3. 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$500,000, made within five years of the original engagement.

[18] id.

[19] ibid., Section 6. Foreign corporations can fulfil their reciprocal purchase obligations through direct purchases, such as using an Israeli subcontractor to complete the project, or through indirect reciprocal purchases, such as from domestic industries that are not part of the specific project but rather for the purposes of exportation, investments, service purchases, among other things. 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).

[20] 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 Government Procurement Agreement (GPA) (Ministry of the Economy and Industry: 'Reciprocal Purchase Terms under the GPA Treaty' (May 2019)).

[21] Mandatory Tenders Regulations (Preference of Israeli Produce) of 1995 (Made in Israel Regulations), Section 3. A similar requirement is set out regarding municipalities under the Municipalities (Tenders) Regulations, 1987.

[22] Made in Israel Regulations, Section 4(b); 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 said mechanism to a wider range of tenders, including those issued by local authorities and by local authorities' corporations.

[23] 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 on both the transferor and the transferee.

[24] Essential Interests Orders have been published thus far in the fields of security, aviation and petroleum.

[25] For example, requirements regarding Israeli nationality are set as conditions for the issuance of certain cable broadcasting and news production licences. See Telecommunications (Telecommunications and Broadcast) Law of 1982, Sections 6h2, 6t2.

[26] 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 communications service is an essential service for national security considerations, that it is required for the adequate provision of services to the public, or that it is needed for government policy considerations, including competition.

[27] See Ministry of Energy website, at **https://www.gov.il/he/departments/news/press_070121** and **https://www.gov.il/he/departments/news/press_300522** (last accessed 31 August 2022).

[28] Petroleum Regulations (Principles of Action for Petroleum Exploration and Production at Sea) of 2016, Section 11.

[29] Natural Gas Economy Law of 2002, Section 8.

[30] ibid., Section 17.

[31] Knesset Research and Information Center, Electricity Market Overview, 2022.

[32] Electricity Market Law of 1996, Section 3(b).

[33] Licences required for conduction, distribution or system management activities are held almost exclusively by the Israel Electric Company and Noga Ltd, the new system management entity (see Knesset Research and Information Center, Analysis of Application of Electricity Market Reform, 2021).

[34] The specific permit required depends on the size of the investment, as a percentage of the total holdings, and on the rights accompanying the investment.

[35] Defined as an insurer holding an Israeli insurer licence, or a foreign insurer licence according to the statute's provisions, and provident funds.

[36] Financial Services (Insurance) Supervision Law of 1981, Section 32(a).

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

[38] Banking Law (Licensing) of 1981 (Banking Licensing Law), Section 34(a).

[39] Banking Licensing Law, Section 34(b).

[40] 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.

[41] Banking Licensing Law, Section 6(6).

[42] 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.

[43] As introduced in a 2005 amendment to the Law for the Encouragement of Capital Investments of 1959 (Investment Law).

[44] As introduced in a 2011 amendment to the Investment Law.

[45] As introduced in a 2017 amendment to the Investment Law.

[46] Economic Competition Regulations (Registration, publication and reporting of Transactions), 5764-2004, Section 9(2).

[47] 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.

[48] Regulatory Principles Law of 2021, Section 2(4).

[49] ibid., Section 37(a).


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