

Technology and Innovation in Israel:

The Role of the Legal System

Australian Innovation Trade Delegation

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Legal Transformations behind the Economic Successes

Some highlights of 30 years of
practicing high tech law in Israel

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Lessons of 25 Years of Practicing Hi-Tech Law in Israel

- “Silicon Valley” practices have been adapted to the Israeli legal and business environment
- Corporate, tax and other fields of law have been revised slowly and steadily to level the playing field
- Local legal and accounting professions have grown increasingly sophisticated
- Israeli legal “innovations” have helped push this process

Then and Now

| | Then | Now |
|--|--|-------------------------------------|
| Currency Controls | Complex and Byzantine | Gone! |
| Stamp Tax | Inefficient, complex and sometime costly | Gone! |
| Acquisition by Reverse Triangular Merger | No – only share purchase | YES, like in the U.S. |
| Tax Free Reorganizations | Very few | Better, but not as good as the U.S. |
| Capital Gains Treatment for Founders Shares and ESOP | No | Yes |
| Capital Gains Tax on Foreign Investors | Yes | No |
| Capital Gains Treatment for VC Carried Interest | No | Yes, subject to certain rules |

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Corporate Law

- In general, Israeli companies “look and feel” like US corporations (shareholders, directors, officers, limited liability)
- Companies Law adopted in 2000 leans more towards Delaware, less towards the UK (replaced England’s 1929 Companies Act!)
- Enables acquisitions by reverse triangular merger (key to modern company acquisitions)
- Israeli companies regularly go public in the U.S.
- Israeli companies can go bankrupt (vital for a thriving hi tech industry)

Start-Up Companies

- Dramatic reduction in capital gains tax rate on founders' shares (creates tremendous incentive; no more complex tax planning)
- Employee Stock Options Plans (taxed at capital gains rates, and only upon exercise – key to incentivizing employees)
- Articles of Association (equivalent to Certificate of Incorporation in the US) can accommodate standard venture capital provisions
 - Liquidation Preference
 - Anti-dilution Protection
 - Minority Shareholder protections
 - Drag-Alongs, Co-Sales, ROFRs
- Recent trends: serial entrepreneurs, “single app” companies

Venture Capital Funds

- Industry Jump-Started by “Yozma” Funds
- Most active VCs are Cayman Island Funds with parallel Israeli funds
- Tax ruling regime protects foreign investors
- GP’s carried interest taxed at capital gains rates, subject to certain rules
- VC deals look and feel like US deals – terms are a mix between East Coast and West Coast standards
- Increasing role of foreign funds

Other Sources of Financing

- Professional Angel Investors – serial entrepreneurs and others
- OCS and Private Incubators
- Hubs and Accelerators
- Crowd funding and accredited investor clubs – the ISA struggles to keep up

IP Protection - Key to Hi Tech Success

- Patents, Copyrights, Trademarks, Trade Secrets
- Data Privacy
- Computer Law (not that long ago, Israel still used England's 1911 Copyright Act)
- Problem: Section 134 of Patent Law – new decision provides clarity

Special Incentives for Israeli Technology Companies

- Office of the Chief Scientist
 - R&D funding
 - Incubator support
- Approved/Benefitted Enterprise (tax advantages)
- BIRD Foundation
- Government Support
 - Biotech funds and incubators
 - Encouragement for Institutional Investors
- Case Study: Orbimed/J&J/Takeda Incubator

Other Relevant Israeli Legal Regimes

- Securities Laws
 - In general, based on the US-style disclosure model
- Anti-trust Laws – similar to HSR

Conclusion

- The legal infrastructure plays a key role in enabling the hi tech revolution
- Israeli laws relevant to hi tech, while not perfect, are similar in many respects to the U.S. and more attuned to hi tech than the laws of most European countries
- Israel recognized the need to unleash the power of hi tech development