FBC&Co

Where Clients Make Partners

Legal Update **March 2016**
Capital Markets Department

Israeli Court Ruling Regarding Proxy Process of Israeli Companies Listed on Stock Exchanges Outside Israel

On February 23, 2015, the District Court of the Central District handed down a decision in *BlueMountain Capital Management LLC & others v Taro Pharmaceuticals Industry Ltd* that will be of particular interest to Israeli companies whose shares are listed on non-Israeli stock exchanges.

The decision sets forth certain procedural requirements with respect to the vote by proxy of shares of an Israeli company whose shares are listed on a stock exchange outside Israel, particularly with respect to resolutions that require the approval of a disinterested majority pursuant to the Israeli Companies Law, 1999 (the "**Companies Law**").

BACKGROUND

Taro Pharmaceuticals Industry Ltd. ("**Taro**") is an Israeli company listed on the New York Stock Exchange. Minority shareholders sought an order from the Court to declare shareholder resolutions adopted at a general meeting for the appointment of external directors, approval of director compensation and adoption of a compensation policy, all of which require the approval of a majority of disinterested shareholders under the Companies Law, to be void because of procedural flaws in the approval process. Although the Court ruled that the resolutions were duly adopted, the Court's decision has important ramifications for the proxy voting process in Israeli companies whose shares are listed on a stock exchange outside Israel.

Since the majority of Israeli public companies are companies with a controlling shareholder, the Companies Law includes special mechanisms to address the relationship between the controlling shareholder and minority shareholders of a public company. These mechanisms include a requirement for certain resolutions, such as the approval of transactions with the controlling shareholder or approval of director compensation, by a majority of disinterested shareholders. To that effect, the Companies Law requires that each shareholder voting on such resolutions state whether it has a "personal interest," as defined in the Companies Law, in such resolutions, and provides that the vote of a shareholder who has not made such statement will not be counted in the disinterested majority.

THE DECISION

The key rulings arising from the judgment are as follows:

- **No requirement for a disinterested shareholder to identify itself in order for its vote to be counted in the votes of the disinterested majority for resolutions that require the approval of a disinterested majority under the Companies Law.** Although Section 276 of the Companies Law requires shareholders to declare whether they have a "personal interest," as defined by the Companies Law, when voting on resolutions that require the approval of a disinterested majority under the Companies Law (otherwise their vote will not be counted), the Court determined that shareholders claiming to be disinterested are not required to identify themselves to the company as a condition for including their votes in the tally of the disinterested majority. The Court also determined that the company is not required to ensure the accuracy of the shareholders' declarations with respect to the absence of a personal interest (on the proxy card or voting instruction form), unless it knows or should know that the statements are false.
- **Israeli companies whose shares are listed on a stock exchange only outside Israel may include on the proxy card and voting instruction form the recommendations of the Board of Directors with respect to the resolution(s) to be voted on; where a shareholder signs the proxy card or voting instruction form but does not specifically indicate its votes, the shareholder's shares may be voted on such resolution(s) in the manner recommended by the Board of Directors, in both cases where this is the applicable foreign practice.** While it is common practice in the United States to include the recommendations of the Board of Directors on the proxy card and voting instruction form, and for the proxy card and voting instruction form to provide that by signing it, without indicating specifically how to vote on the proposal(s), the shareholder authorizes it shares to be voted on such proposal(s) in accordance with the recommendations of the Board of Directors, the plaintiffs argued that these practices are contrary to the Companies Law. The Court rejected the argument on the grounds that Israeli companies whose shares are listed on an exchange only outside Israel (such as Taro) are exempt from certain procedural requirements of the Companies Law relating to voting cards under the Israeli Companies Regulations (Relief for Companies with Securities Listed on a Stock Exchange Outside Israel), 2000, so long as they are acting in accordance with the foreign practice and in this case, the foregoing practices are commonplace in the United States. We note that while the ruling specifically relates to Israeli companies whose shares are listed on a stock exchange only outside Israel, it is arguable that the same conclusion should apply with respect to Israeli dual-listed companies.
- **Shareholders are required to affirmatively declare the absence of their personal interest in a resolution requiring the approval of a disinterested majority under the Companies Law, on the proxy card or voting instruction form, in order for their vote to be counted in the disinterested majority.** The Court noted that it is common practice for foreign-listed and dual-listed companies to state in the proxy card that by signing the proxy card, a shareholder that has not declared (i.e., "ticked the box") whether it has a "personal interest" in a resolution requiring the approval of a disinterested majority, shall be deemed not to have a personal interest in such resolution. The Court held, however, that this practice is contrary to Section 276 of the Companies Law, which requires a shareholder to inform the company "whether he has a personal interest" in a resolution requiring the approval of a disinterested majority under the Companies Law. Therefore, the Court determined that Israeli companies listed on an exchange outside Israel must

state in their proxy cards and voting instruction forms that shareholders that fail to declare that they have no personal interest in a resolution requiring the approval of a disinterested majority under the Companies Law, will be deemed to have a “personal interest” in such resolution and their vote shall not be counted in the disinterested majority.

COMMENT

While foreign-listed and dual-listed companies are generally entitled to follow the common proxy practices in the jurisdictions of the markets where they are listed, the Court's decision establishes that this principle does not override the Israeli law requirement for shareholders to declare whether they have a personal interest in resolutions that require the approval of a disinterested majority under the Companies Law. The result of the Court's ruling is that without affirmative statements on proxy cards (or, if applicable, voting instruction forms) of the absence of shareholders' personal interest in such resolutions, it may prove challenging for companies to adopt resolutions that have “interested party” aspects and require the approval of a majority of disinterested shareholders, such as resolutions concerning director remuneration.

Companies listed on a foreign exchange must ensure that shareholders are aware that, even where they are a disinterested party, they are required to declare that they have no “personal interest” in resolutions that require the approval of a disinterested majority, on their proxy cards (or, if applicable, voting instruction forms), in order for their vote to be counted in the disinterested majority. Where possible, proxy cards (and, if applicable, voting instruction forms) should clearly state this “Check-the-Box” requirement. We also recommend that companies include explanatory notes to this effect in their proxy statements, and particularly where foreign law or practice precludes companies from including such a statement on the proxy cards (or, if applicable, voting instruction forms).

*****

FBC advises Israeli companies traded abroad and dual-listed companies on various securities laws, corporate and compliance matters. We would be pleased to provide you with further advice in this area.

For further information, please feel free to contact Sharon Rosen, Ron Lehmann or Nitzan Sandor of FBC’s Corporate and Capital Markets practice group, or your regular FBC contact.

Sharon Rosen	972.3.6944145	srosen@fbclawyers.com
Ron Lehmann	972.3.6944145	rlehmann@fbclawyers.com
Nitzan Sandor	972.3.6944131	nsandor@fbclawyers.com

This communication is distributed with the understanding that the author, publisher and distributor of this communication are not rendering legal, accounting, or other professional advice or opinions on specific facts or matters and, accordingly, assume no liability whatsoever in connection with its use.

All rights reserved to Fischer Behar Chen Well Orion & Co.

In order to subscribe to or be removed from the distribution list please e-mail: newsletter@fbclawyers.com