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## Israel: Cross Border Joint Venture and Strategic Alliance Guide

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### Structures

#### ***What are the standard forms of joint ventures / strategic alliances and common features of each?***

Joint ventures (JVs) are not recognized in Israel as particular legal entities; therefore, there are no specific regulations that apply to JVs. Most legal structures applicable in Israel can be used for the purpose of forming a JV. A JV may be formed by organizing a company (JV Company) or a general or limited partnership (JV Partnership), or without incorporating a new entity, such as in the case of a contractual engagement (Contractual JV). Each such structure is further discussed below.

#### *Contractual JV*

A Contractual JV is not required to be registered, as no separate legal entity is established. The parties memorialize their cooperation through a contract that may be made for any purpose and for any time frame—limited or not. The contractual engagements are subject to the Israeli Contracts (General Part) Law – 1973, and to the Contracts (Remedies for Breach of Contract) Law – 1970 (collectively, the Contract Law), and enable the parties to define their engagement and their internal relationship with very few limitations in a short period of time.

The contract forming the Contractual JV usually defines the objectives of the JV, the contributions to be made by each of the parties, allocation of profits and losses between the parties, the functions of the parties within the JV, terms for termination of the JV, and similar matters. Each Contractual JV must be examined on a case-by-case basis to analyze exposure for liability among the parties.

A contract that creates a JV without defining the organizational form may be interpreted as the formation of an unregistered partnership (as further described below).

Parties to a JV sometimes prefer a Contractual JV over a JV Company or a JV Partnership for the following reasons:

- A Contractual JV enables the parties to retain control over their assets and business, as these are not transferred to a separate legal entity.
- A Contractual JV is subject to fewer procedural requirements, as registration is not required.
- It is easier to terminate the Contractual JV than a JV operating through a separate legal entity.
- A Contractual JV has no effect on the direct taxation of the parties.

#### *Limited Liability Companies*

Companies are subject to the Israeli Companies Law – 1999 and the regulations promulgated thereunder (Companies Law), and must be registered with the Israeli Companies Registrar as a condition to their formation. The registration process requires the submission of initial Articles of Association (in Hebrew, or in English together with a Hebrew translation), declarations executed by the initial directors and shareholders of the company, and payment of a registration fee. The process takes approximately four business days to complete and usually lawyers handle it, as they are required to attest the registration documents. Israeli law does not require any minimum equity, but a JV Company's initial Articles of Association must include the company's registered share capital (in New Israeli Shekel), including the number and categories of the registered shares. Companies may issue shares with no par value.

In the event that the shareholders of a JV Company wish to regulate their internal relationship, they may draft a shareholders agreement to complement any arrangements in the JV Company's Articles of Association. Such agreement is not required to be submitted with the Companies Registrar; therefore, it will not be binding on third parties unless they have consented to be bound by its terms.

In a JV Company, the shareholders' liability is limited to their investments (or commitments to invest) and each shareholder holds an interest equal to its pro rata portion of the Company's issued and outstanding shares. Under Israeli law, the court may allocate a JV Company's debt to its shareholders or suspend a shareholder's right to redeem shareholders' loans until debt to third-party lenders is repaid, in the following events: the use of a separate entity for the JV Company was deceptive or unjust towards the creditor or was harmful to the JV Company's objective and reflected an unreasonable risk as to the JV Company's ability to pay its debts.

Private companies are required to submit an annual report and audited financial statements to their shareholders and to the Israeli Companies Registrar. The records of the Israeli Companies Registrar are open to the public and include basic information regarding the company, such as its name, address, incorporation number, registered share capital, par value of each share, registration date, purpose of incorporation, name of its directors, shareholdings in the company, and pledges over the company's assets. In addition, companies are subject to corporate tax, and payments of dividends are subject to withholding by the JV Company.

Following its incorporation, a JV Company is required to register with the Israeli VAT Authority (this process requires at least one Israeli resident to act as the VAT representative of the JV Company), the Income Tax Authority, and the National Insurance Institute. These procedures usually require approximately 15 business days.

### *Partnerships*

JV Partnerships are subject to the Israeli Partnership Ordinance (New Version) – 1975 (Partnership Ordinance). There are two forms of partnerships: General Partnership (GP), which is an unlimited liability partnership, and Limited Partnership (LP). The Partnership Ordinance requires that an LP has at least one general partner that is liable for all the partnership's obligations, and at least one limited partner, whose liability is limited to the amount that it invested or agreed to invest. A limited partner is not allowed to participate in the management of the partnership and its actions may not bind the partnership; if they do, the limited partner will be liable as a general partner. In Israel, it is common for a company to be the general partner in an LP.

In a GP, all of the partners jointly and severally share unlimited liability for the partnership's obligations, and such liability may extend to the partners' personal assets. Each of the partners is permitted to participate in the management of the business and is held to be an agent of the partnership.

According to the Partnership Ordinance, registration with the Partnerships Registrar is a constitutive requirement for the establishment of an LP. The approval of the Partnerships Registrar and the Minister of Justice are preliminary conditions for the commencement of activity of the LP. The initial partners of an LP are required to submit with the Partnerships Registrar a written Partnership Agreement (in Hebrew or in English together with a Hebrew translation) and pay a registration fee. The Partnership Agreement usually defines:

- The type of partnership
- Terms of the partnership
- The limitation and liabilities of each partner
- The amount that was invested by the limited partners
- Limitation on the rights of each partner to bind the partnership
- Provisions regarding the distribution and allocation of profits and losses
- Indemnification clauses, and similar matters

A GP is required to be registered with the Partnerships Registrar within one month from the date of its formation. Such registration, however, is only a declarative requirement that does not affect the existence of the GP.

Unlike companies, partnerships are pass-through entities for tax purposes. Therefore, a party to a JV that can take advantage of tax benefits (e.g., losses) likely would prefer a JV Partnership to a JV Company in order to use such tax benefits under a partnership structure.

An engagement between at least two individuals or entities for the purpose of conducting business, without being registered with the Partnerships Registrar, may be considered an unregistered GP. The question whether an unregistered engagement is considered as a GP is examined in light of customary criteria presented in the Partnership Ordinance and Israeli case law, such as the intention of the parties, presentation to the public, profits allocation, duration of relationship, management rights of the parties, and similar criteria. If the engagement is considered a de facto GP, the provisions of the Partnership Ordinance will apply and the liability of each of the partners will be unlimited on a joint and several basis.

JV Partnerships are common in the following industries: investments funds, private equity, and energy ventures (e.g., energy exploration such as oil and gas).

***Can a joint venture or strategic alliance be formed for any purpose?***

Any of the structures discussed above can be formed for any legal purpose.

***Are there any industries that would not permit or would not be conducive to a joint venture or strategic alliance?***

JVs can operate in any sector, subject to applicable regulations, licenses, and permits. To the extent a JV operates in a regulated sector, such as banking, electricity, or energy, the applicable laws in such sector apply to the JV.

**Management**

***How is the joint venture or strategic alliance managed in the different structures?***

The parties to a Contractual JV can define their own management and governing bodies. These bodies are not subject directly to the Companies Law, which governs the roles and responsibilities applicable to the managing body in a company. However, certain principles, including fiduciary duties, may apply to the management bodies of a Contractual JV.

In a JV Company, the managing body is the board of directors, and the Companies Law requires that a company has at least one director, who may be Israeli or foreign.

***What mechanisms are there for resolving deadlocks on major decisions?***

It is common for the documentation governing a JV to include a mechanism dealing with deadlock situations. Common approaches for addressing deadlocks are casting votes, independent third-party determination, buy me–buy you mechanisms, and arbitration.

**Becoming a Member/Partner**

***Are there any statutory or other requirements regarding the number (i.e., minimum or maximum) or type of members in a joint venture or strategic alliance?***

A party to a JV can be an individual or an entity (Israeli or foreign).

Israeli law does not impose any limitation on the number of members in a JV, but an offer to purchase shares of or interest in a JV, made to more than 35 non-qualified potential purchasers, is considered an “offer to the public” within the meaning of the Israeli Securities Law – 1968, and is subject to the requirements of the Securities Law with respect to public offerings, including the requirement for publication of a prospectus approved by the Israeli Securities Authority.

JVs Partnerships (both LP and GP) must include at least one general partner and may not include more than 20 general partners, but partners may themselves be legal entities with more than one owner, thereby multiplying the number of effective partners.

***What are the different levels of equity and voting participation in the various forms of joint ventures and strategic alliances? How flexible is each of the structures?***

Under Israeli law, very few limitations apply to the voting rights of the parties to a JV or to the contributions made to the JV by each party. The parties are free to define these issues at their discretion.

A JV Company may prescribe different voting rights for different categories of shares.

***What forms of contributions (e.g., cash versus in-kind) may be made by members/partners?***

The parties to a JV may contribute cash, services, or property.

***What documentation would typically govern the relationship between partners/members?***

In a JV Company and a JV LP, each party’s contribution must be documented, and the Partnership Agreement should define the rights of the partners to the Partnership Agreement.

## The Regulatory Environment

### ***Are there any antitrust matters to be considered in forming a joint venture or strategic alliance?***

JVs are subject to general laws that apply to Israeli businesses. In addition, regardless of the type of JV established, an arrangement between individuals or legal entities under which at least one of the parties restricts itself in a manner that may prevent or reduce competition between that individual and the other parties to the arrangement, or between the individual and a third party, is considered a restrictive arrangement. In some cases, the cooperation between competitors will be considered a prohibited restrictive agreement. All such arrangements are prohibited by the Restrictive Trade Practices Law – 1988 (the Restrictive Trade Practices Law), unless approved by the appropriate antitrust authorities. The Restrictive Trade Practices Law provides certain statutory exemptions under which an arrangement will not be considered a restrictive arrangement if:

- It relates to a real property rights assignment
- It falls within certain specific business sectors (international air and sea transportation, agricultural, and others)
- Entered into by a company and its subsidiary, and other specified matters

Also, the General Director of the Israeli Antitrust Authority has issued a set of block exemptions that exempt parties to certain types of restrictive arrangements from having to seek a specific exemption from the General Director. It is advisable to consult with antitrust counsel prior to the entry into JVs among competitors or JVs that restrict competition.

### ***Can a public sector body be a member/partner in the joint venture or strategic alliance?***

Government organs, government companies, and public companies can enter into JV agreements, but in such cases, the relevant administrative laws or any other laws applicable to government entities or public companies may apply to the JVs.

## Allocation of Profits and Losses

### ***How are profits, losses, and distributions allocated among partners/members? Are there legal or regulatory restrictions that may limit the ability of the partners/members to make such allocations on their own?***

A JV Company may declare and pay dividends (or otherwise distribute funds or assets to its shareholders) only if, upon the determination of its board of directors, there is no reasonable concern that the distribution will prevent the JV Company from being able to meet its existing and foreseeable obligations as they become due. Under the Companies Law, the distribution amount is limited to the greater of the JV Company's retained earnings or earnings generated over the previous two years, according to the JV Company's last reviewed or audited financial statements, provided that the date of the financial statements is not more than six months prior to the date of the distribution. A JV Company may distribute dividends that do not meet such criteria subject to court approval. As companies are limited liability entities, a company's losses are not borne by its shareholders.

In a JV Partnership, the partners are entitled to determine how and when to allocate the partnership's profits without any statutory limitation, provided that in a GP all of the partners are liable for the partnership's losses, and in an LP only the general partner is liable for all the partnership's losses (while each limited partner is liable for losses up to the amount that it invested or committed to invest).

## Exit or Termination

### ***Are there statutory or other limits on the duration of a joint venture or strategic alliance?***

Israeli law does not impose any limitation on the duration of JVs. JVs can exist indefinitely, unless the parties wish to terminate such an engagement, or in the event that the parties formed a JV Partnership or a Contractual JV for a limited period of time.

### ***How does a partner/member exit a joint venture or strategic alliance? How is a joint venture terminated?***

In a Contractual JV, as in any other contract, the parties may decide to terminate the engagement at any time and for any reason subject to the contract's provisions and limitations and subject to the Contracts Law.

In a JV Company, each shareholder may exit the JV by transferring its shares in the company, subject to the JV Company's Articles of Association, which may include provisions that limit such transfer of shares. These may include a requirement of prior board approval, rights of first refusal or tag-along rights, lock-up periods or drag-along rights. In addition, the shareholders may decide to terminate the JV by the liquidation of the JV Company. The JV Company, as a separate legal entity, continues to exist until liquidation, even if the legal existence of its shareholders has been terminated.

A JV GP must be liquidated, among other things, upon one of the following events:

1. If the JV GP is set to exist for a limited period of time or for a specific business purpose, the partnership automatically dissolves at the end of the period or the business, unless the partnership continues its activity, and in that case it is considered as if it were established for an unlimited period of time.
2. If there is no set period for the existence of the GP, it dissolves upon the announcement of a partner to the other partners its intention of dissolving the partnership.
3. If one of the partners is declared bankrupt, the partnership automatically dissolves.
4. If a lien is placed on a partner's share of the partnership because of its personal debt, the other partners may liquidate the GP.
5. Similar situations.

With respect to a JV LP, a limited partner cannot request the liquidation of the JV Partnership. In the event a lien is placed on a limited partner's share of the JV LP because of its personal debt, the other partners may not liquidate the JV LP, and in an event of declaration of one of the limited partners as bankrupt, the JV LP does not dissolve.

### **Foreign Members/Partners**

#### ***What permits, consents, or registrations are required by foreign members/partners of a joint venture or strategic alliance?***

If any of the shareholders or directors of a JV is a non-Israeli citizen or legal entity, a notarized copy of the passport or, in the case of an entity, registration documents are also required to be submitted in the registration process of the JV Company or the JV Partnership.

#### ***Are there any economic incentives for foreign direct investments in a joint venture or strategic alliance?***

Israeli laws (such as the Law for the Encouragement of Capital Investment and the Law for the Encouragement of Industrial Research and Development) encourage foreign investment in Israel by offering several benefits to local business such as grants, reduced tax rates, tax exemption, and other tax-related benefits.

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