INDIA UNLEASHED

2017 LEGAL AND INVESTMENT GUIDE

Gateway to India

An end-to-end deep dive into Indian and overseas regulations essential for business and investors

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Israel: Startup Nation Open to India and the World

FBC & Co examine the business and legal aspects of investing in one of the world's most technologically advanced economies.

OVERVIEW

Established in 1948, Israel is the world's only Jewish state, and the sole democracy in its vicinity. Israel has a diverse open market economy. Being a relatively young state, Israel is recognized as a developed market by many major indices. Israel has been a member of the high-income sector of the OECD since 2010.

Israel's current economy is diversified, with technology-based industries (such as software and manufacturing of technology based products, TMT, life science, and agriculture technologies) at the frontline, followed by medium and lower tech industries, such as chemicals, plastics and agriculture.

Israel's skilled workforce and concentration of venture capital allow the country to lead in industries such as high-tech and life sciences.

The development of the Israeli economy over the country's short history was accompanied by dramatic events and evolutionary changes. But as breakthroughs were witnessed and crises were overcome, the features of stability, resilience and solvency were always present, as well as the values encouraged by the Israeli government of entrepreneurship, innovation and liberalization. Over the years the Israeli economy has established itself as stable and yielding, providing a solid investing environment for both local and international investors.

While the traditional business thrust in diamonds, agriculture, chemicals, information & communication technology, and pharmaceuticals remains strong, there is a growing interest from Israeli companies in clean energy, water technologies, biotech, nanotech, homeland security, real estate, infrastructure, e-commerce, and financial services.

Israel has one of the most resilient and technologically advanced market economies in the world, and is home to many international high-tech companies. Its skilled workforce and concentration of venture capital allow the country to lead in innovative industries such as high-tech and life sciences. The Israeli economy also showed great resilience during the latest global economic crisis and in 2010, Israel was ranked 1st in the 'Resilience of the Economy' Index, as part of the World Economic Forum's Global Competitiveness Report.

In 2015, Israeli exports totalled $53.4 billion, an increase compared to $47.9 billion in 2014. Hi-tech exports accounted for $22.5 billion, compared to $19.9 billion in 2014. Imports totalled $61.3 billion in 2015, compared to $62.5 billion in 2014. Exports to Asia peaked in 2015, reaching $11.6 billion, compared to $9.8 billion in 2014. Import levels from Asia remained stable, with $13.3 billion in 2015,

compared to $13.8 billion in 2014.

ISRAEL AND INDIA

Relations between Jerusalem and New Delhi were not always warm. Although both countries gained their independence from the United Kingdom within months of each other, they found themselves headed in pointedly different directions for nearly four decades - India as a leader in the Non-Aligned Movement that maintained close relations to the Arab world and the Soviet Union; Israel, which linked its future to close ties with the United States and Western Europe.

Since the establishment of diplomatic relations between India and Israel in 1992, bilateral trade and economic relations have progressed rapidly and both countries have benefited immensely. According to the Foreign Trade Administration at the Ministry of Economy and Industry of the Government of Israel, from a base of US$ 200 million in 1992 (comprised primarily of diamonds), trade between India and Israel has been steadily growing, with business between the two countries adding up to over $6 billion in 2013.

Major exports from India to Israel include diamonds and precious stones, chemical products, textile, plants and vegetable products, mineral products, rubber and plastic products, base metals and machinery. Major exports from Israel to India include defence products and technology, diamonds and precious stones, chemical and mineral products, agriculture products and technology, and hi-tech.

In recent years, India has become one of Israel's largest trading partners, and many of the world's leading high-tech companies in Israel and India are forging joint ventures that are successfully competing in the tough international marketplace. Trade and cooperation between the countries now centers primarily on security-related deals, hi-tech, and in areas such as agriculture and water desalination.

Israel, known as the Startup Nation, and India, one of the largest bases for startups in the world, each in its way is leading the global tech world. With a population of eight million people, Israel has over 6,000 startups, attracts more venture capital per person than any other country in the world, and has more companies listed on the NASDAQ than any country outside the USA, except China. With a population of over 1.3 billion, India has over 3,000 startups and is looking to have more than 10,000 by 2020. The positioning of India as a startup country is thought of in the light of other famous startup scenes such as the US, Israel, and Singapore.

MARKET ACCESS

The State of Israel supports its investment initiatives by developing and granting a wide range of incentives and benefits in order to achieve a favourable balance of trade, improve revenues, maximize productivity in designated industrial sectors, ensure healthy competition in the relevant markets and facilitate overall growth. To attain these goals, Israel offers substantial benefits and concessions through a number of laws and regulations. Special emphasis is laid on high-tech companies and R&D activities, as considerable importance is attached to these fields.

Many of the world's leading high-tech companies in Israel and India are forging joint ventures that are successfully competing in the international marketplace.

The State of Israel welcomes foreign investments particularly in projects related to technology and R&D. Most benefits available to Israelis are also available for foreign investors, and in some cases foreign investors enjoy even broader support than domestic investors. Investment incentives are outlined in different laws and regulations, and are managed by the Israel Investment Center (IIC). Two main laws governing these benefits are as follows:

The Law on the Encouragement of Capital Investment: The law was originally introduced in 1959, in order to boost the Israeli economy by

attracting local and foreign investors to contribute capital investments to the Israeli industry. The law's main goal is to amplify the attractiveness of the Israeli economy in the international competition over local and foreign capital for investment and development. The law grants various incentives for foreign and domestic investors. Companies that meet the criteria are entitled to preferential tax treatments and various grants related to land development, constructions and capital equipment. Increased grants and benefits are offered to investors who invest in certain priority areas determined by governmental policies from time to time. As Israel is a small country, a priority area may be located just one to two hours away from Israel's international airport and Metro Tel Aviv.

The Law on the Encouragement of Capital Investment grants various incentives for foreign and domestic investors, including preferential tax treatments and various grants.

The Law on the Encouragement of Industrial Research and Development: The main objective of the law is the development of science-intensive industry. The law provides grants, loans, exemptions and reduction in taxes.

The Israel Innovation Authority (formerly known as the Office of the Chief Scientist (OCS)) of the Ministry of the Economy and Industry is responsible for implementing government policy regarding the support and encouragement of industrial research and development in Israel. The variety of support programs provided by the Israel Innovation Authority have played a major role in enabling Israel to become one of the most important global centers for high-tech entrepreneurship.

On the international level, the executive agency of the Israel Innovation Authority, MATIMOP, offers international programs carried out in cooperation with foreign governments and institutions. The international support programs provide support through bi-national funds, and enable joint R&D ventures with foreign counterparts. MATIMOP collaborates with Indian counterparts at the federal and state level, as well as with stakeholders in the private sector, to facilitate and implement access to funding schemes dedicated to the development of R&D-driven partnerships between Israeli and Indian companies. These programs provide access to the OCS funding schemes in Israel and to similar, parallel funds in India, as well as provide companies with assistance in identifying potential R&D partners. Through these programs, funding support is provided to joint industrial R&D projects in all technology fields, aimed at the development of products or processes leading to commercialization in the global market.

Israel has entered into several trade agreements in order to strengthen its position in the international markets. The most significant agreements are the Free Trade Area with the European Union, Free Trade Area with the United States and Free Trade Area with the European Free Trade Association States (EFTA). The agreements with the European Union, the United States and the EFTA countries place Israel in the unique position of being a Free Trade Area partner with the world's main economic regions.

While a free trade agreement between the countries has been in discussion for several years but is yet to be entered into, Israel and India are party to several cooperation agreements in agriculture, medicine and health, telecommunication, and research and development, among other areas.

The India-Israel Initiative for Industrial R&D (i4RD) provides partner matching assistance and access to funding for Israeli companies and companies based anywhere in India. This federal level program is based on the bilateral agreement signed in 2005 between the Ministry of Science and Technology, Department of Science and Technology (DST), the Government of India and the Ministry of Economy of the State of Israel. The

bilateral framework is jointly implemented by the Global Innovation and Technology Alliance (GITA) in India and MATIMOP.

The Karnataka-Israel Industrial R&D (KIRD) Program provides partner matching assistance and access to funding for Israeli companies and Indian companies based in the state of Karnataka. This program – the first on the state-level in India – is based on a Memorandum of Understanding signed in 2013 between MATIMOP and the Karnataka Science and Technology Promotion Society (KSTePS) and the Karnataka State Council for Science and Technology (KSCST). This bilateral framework is jointly implemented and promoted by KSTePS, KSCST, and MATIMOP.

In addition to access to national and state-level funding schemes, the i4RD and KIRD programs offer Israeli and Indian companies assistance in identifying potential partners for R&D projects in the target country/state.

Israel is a party to many tax treaties with various countries including India, which are meant to avoid double taxation. According to the tax treaty between Israel and India, companies involved in trading between the two countries are entitled to a substantial tax reduction related to dividends and royalties.

BUSINESS ENTITIES

Israeli business entities include companies, partnerships, cooperatives, and non-profit organizations. Individuals may conduct business without establishing any legal entity.

The most common form of business entity in Israel is a limited liability company with capital stock (share capital). The Israeli Companies Law defines a company as a corporation formed and registered in Israel, in accordance with the Israeli law. No requirements exist regarding the nationality or residency of stock holders and company directors. There are no restrictions regarding non-residents holding shares in Israeli companies. However, there are certain restrictions on the ownership by non-Israeli entities or persons of interests in Israeli companies in certain sensitive industries (e.g., banks or bank holding companies, insurance companies, telecommunications companies, companies managing pension funds, and companies controlling natural resources or essential services).

A company may be registered as a "Private Company" or a "Public Company", with securities registered on a Stock Exchange. Both types of companies must present annual reports, including audited financial statements to their shareholders. A private company may not offer or sell debentures or shares to the public. A public company may offer stock or debentures to the public, but only after issuing a prospectus in accordance with the requirements of applicable laws, and is obliged to publish an annual report that includes the audited financial statements and directors' report.

The Partnership Ordinance defines a partnership as an entity that consists of persons who contracted to form a partnership. Personal liability of the partners is not limited unless they are limited partners of limited partnerships. A foreign partnership is also permitted to do business in Israel.

Foreign (i.e., non-Israeli) companies ("Foreign Company") operating in Israel generally do so in one of two ways – by incorporating an Israeli corporate subsidiary of the Foreign Company ("Subsidiary"), or by the Foreign Company registering a branch in Israel ("Branch").

Under Israeli law, a Foreign Company may maintain a place of business in Israel only if it is registered as a 'foreign company' under the Companies Law.

An Israeli company is similar to a US corporation or an English company. The liability of its shareholders is limited, it has one or more class of shares, it is owned by its shareholders, it has a board of directors, and may have, if active, a chief executive officer. The company's capital structure and the authority and rights of the shareholders, the board and the chief executive officer are set by

the company's Articles of Association, except for those matters that are regulated by the main law governing Israeli companies, the Israeli Companies Law.

A Subsidiary is a separate legal entity whose shareholder is the Foreign Company. The liability of the Foreign Company is limited to the amount of its investment in the Subsidiary, subject to piercing the corporate veil considerations. As a separate legal entity, a Subsidiary may take any legal action in its own name, including all of the following: (i) hold all appropriate local licenses, (ii) enter into agreements (including with local vendors, suppliers and services providers), (iii) hold local bank accounts and (iv) hold a subcontract or service level agreement with its parent company to perform services under various customer contracts.

Large transactions involving Asian acquirers which took place in recent years include the acquisition of controlling stakes in some of Israel's largest corporations.

Under Israeli law, a Foreign Company may maintain a place of business in Israel only if it is registered as a 'foreign company' under the Companies Law. A Branch (a registered Foreign Company) is not a separate legal entity from the Foreign Company, even if their commercial and financial activities are separate. There is no corporate veil separating the Foreign Company from the Branch and, as a result, the Foreign Company is deemed to have legal presence in Israel, generally making the Foreign Company directly responsible for liabilities of the Branch (to creditors, tax authorities, etc.). As a Branch is not a separate legal entity, the following would need be done by and in the name of the Foreign Company: (i) hold all appropriate local licenses, (ii) enter into agreements (including with local vendors, suppliers and services providers), (iii) hold local bank accounts; the Branch's authorized representative in Israel may act on behalf of the Foreign Company in connection with such matters. Further, as a Branch is not a separate legal entity from the Foreign Company, there will be no subcontract or service level agreement with the Foreign Company to perform services under various customer contracts.

From a pure corporate structure and liability protection perspective, foreign companies tend to prefer to operate in Israel through an Israeli corporate subsidiary rather than by way of a local branch. Tax considerations should be taken into account as well.

M&A

Recent years proved to be remarkably prosperous years for merger and acquisition activity in Israel. A notable trend which increased substantially in the last few years is the interest of Asian companies in Israeli companies. Large transactions involving Asian acquirers which took place in recent years include the acquisition of controlling stakes in some of Israel's largest corporations, such as food conglomerate Tnuva by China's Bright Food Group. Other notable transactions are the acquisition of Leadcom Integrated Solutions (telecommunications) by India's Tech Mahindra, the acquisition of Panaya (cloud tech) by India's Infosys, the acquisition of Viber (communication application) by Japan's Rakuten, of Servotronix (automation company) by China's Midea Group, of Tambour (paint company) by Singapore's Kusto group, and of Lumenis (minimally-invasive clinical solutions) by China's Xio Group.

The purchase of an Israeli company may be effected through acquisition of its shares or by a purchase of its assets. In addition, the Companies Law allows for a merger or consolidation of two or more companies, subject to certain conditions.

The Companies Law does not impose restrictions on the transfer of shares in a private company, but such restrictions may be included in a company charter documents. An Israeli company cannot merge with or into a foreign (non-Israeli) company and, therefore, acquisitions by foreign companies are commonly done by way of stock ac-

quisitions or reverse triangular mergers (whereby the foreign entity incorporates an Israeli subsidiary that merges into the Israeli target).

The tax aspects of each of such transactions differ and each has certain advantages and disadvantages. In some cases the transaction requires also the approval of Israeli regulatory agencies, such as the antitrust authority. Moreover, if the Israeli target company benefits from certain governmental funding (such as grants from the Israel Innovation Authority or tax benefits (under Approved Enterprise or Benefitted Enterprise programs)), then approval of the relevant government agency may be required for the acquisition of the Israeli company by a non-Israeli resident.

The rules of the Companies Law generally apply equally to private and public companies, although the internal approval processes in public companies are subject to special rules. Where a public company is involved in the transaction, certain disclosure requirements are triggered. For the most part, the acquisition of an Israeli public company will be structured and implemented in the same manner regardless of whether the company is listed solely on the TASE, listed on an exchange outside of Israel, or dual listed.

There are three primary procedures to gain 100% of the shares of a public company: (1) a reverse triangular merger, (2) a tender offer, and (3) a court approved merger (pursuant to Sections 350 and 351 of the Companies Law). There are no rules that dictate minimum offer price or other deal terms. With respect to tender offers and reverse triangular mergers, the offer must be on equal terms for all target shareholders holding the same type of security. Even where a tender is approved by the requisite majority of shareholders, in the case of a "full" tender offer, a shareholder who did not positively accept the offer may still appeal to the court to determine that the terms of the offer are less than fair value.

Although not legally required, it is often desirable to obtain pre-rulings from the Israel Tax Authority with respect to two matters: (1) clarifying the withholding obligation imposed on the acquirer in connection with payments made to the target shareholders, and (2) providing that the assumption of employees' options by the acquirer would not result in an immediate tax event for target option holders.

For companies belonging to specific industrial sectors, the acquisition of a certain ownership percentage or of control requires special regulatory approvals. For example: (1) the acquisition of 5% or more of the shares of a bank or a bank holding company requires a permit issued by the Governor of the Bank of Israel after consultation with the Bank of Israel's Licensing Committee, (2) the acquisition of 5% or more of the shares of an insurance company requires a permit from the Superintendent of Insurance Businesses, (3) the acquisition of certain percentages in companies providing telecommunications services may require a license from the Ministry of Communications, and (4) in certain cases regarding the acquisition (primarily by means of privatization of government companies) of companies controlling natural resources or essential services, the State of Israel will retain certain veto rights and other powers.

The Israeli economy is a vibrant place for transactions. The local culture in Israel plays a significant role in the thriving marketplace and the soaring number of record deals. Israelis tend to be straight, to the point and determined. Transactions and interpersonal relations during the span of a transaction in Israel are less formal than in other parts of the world, providing ease to the deals. Nonetheless, carrying out deals in Israel resembles the basics of deals in the United States, whether it is in the style of drafting transaction documents, in the standard terms and conditions which are applied, or the common way of doing business. ■

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