DOING BUSINESS IN ISRAEL

BDO

Dear Friends,

It is our pleasure to present "Doing Business in Israel 2016", a comprehensive tool for anyone wishing to engage in the Israeli market.

The Israeli economy is enjoying its 14th consecutive year of growth, demonstrating strong resilience to global crises and to the regional geopolitical situation. Israel was less affected by the 2009 crisis than many other developed countries, with GDP growth rate averages of nearly 4% annually since 2003, which has exceeded that of most other OECD countries.

Like most other developed countries, Israel is currently experiencing a mild slowdown in economic activity. The growth rate is expected to be around 2% in 2016, projected to pick up to 2.5% in 2017, and then return to the long term average of approximately 3.5-4% by 2020.

An accommodating central bank monetary policy, fiscal easing in 2016, lower oil prices, a further increase in the minimum wage over the next two years and an expected recovery in foreign markets are all expected to contribute to boosting local demand. Low interest rates should contribute to a continued weakening of the Shekel relative to the effective "basket of currencies." The depreciation of the Shekel will further stimulate the economy, exports and investments.

Israel faces ongoing geopolitical and security related challenges. However, past experience clearly shows that the Israeli economy is able to contain even severe conflict situations. The Israeli defense burden has dropped from 10% of GDP in 1990 to 4.5% in 2015, a drop that allows Israel to allocate more national resources to growth promoting investments, such as infrastructure.

Today, Israel has flourished into one of the leading high-tech countries in the world. The high-tech industry has contributed greatly to Israel's economy and will continue to be a key driver in the future.

This publication can serve as a valuable tool for business people and investors who wish to gain a wide scope of updated information of critical aspects relating to doing business in Israel. The information presented here touches on recent macroeconomic tendencies, socioeconomic and demographic trends, Israel's general business environment, accounting considerations, taxation and government tax incentives.

Furthermore, encouraging prospects are on the horizon that strengthens the fact that Israel remains an excellent place to do business.

Sincerely,

Danny Margalit
Chairman
BDO Ziv Haft Israel

PREFACE

This publication has been prepared by BDO Ziv Haft Israel to provide our clients, associates and foreign investors with an overview of Israel's economy and business environment.

Our goal in this publication is to summarize useful information, so as to provide our readers with a "taste" of Israel. The publication aims at covering most, but not all, aspects of doing business in Israel and should therefore not be regarded as a manual or a textbook on the subject. Prior to making any investing decision, it is recommended to seek the advice of Israeli economic consultants in the relevant sectors.

Our partners and associates at BDO Ziv Haft Israel provide reliable and professional service to all investors considering investing in Israel.

BDO Ziv Haft Israel is one of the leading accounting firms in the banking and financing sectors, in addition to our proven leadership in other areas such as health care, real estate and high-tech. We also act as a principal financial service provider to government offices in Israel.

BDO Ziv Haft Israel is the fifth largest international network. The firm has 1,400 offices in 152 countries worldwide, with a total of approximately 64,300 partners and professional staff.
The information presented here was updated in July 2016, based on data available at the time of printing.
The publication is intended for information purposes only and does not in any way replace or amend any of the laws and regulations mentioned.
Although we have conducted extensive research to prepare this publication, we are not responsible for any inaccuracies that may have arisen.

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In 2015, Israel showed a solid economic performance compared with most developed countries. While the average growth rate in developed countries stood at 2%, owing to uncertainties in the global context against the backdrop of the geopolitical crisis, Israel in 2015 showed a growth rate of 2.5%.

FOREWORD

This figure is not surprising, as the Israeli economy has proven its stability in the past, during the global financial crisis of 2008-2009, which spurred a moderate recession in the country. However, this was curbed thanks to a solid economic basis, a prudent fiscal policy and a resilient banking sector.

Israel's major exports comprise cut diamonds, high-technology equipment, and pharmaceuticals, while imports include crude oil, grains, raw materials for industry, and military equipment.

In 2015, the Gross Domestic Product in Israel maintained a moderate pace of 2.5% compared with 2.6% in the preceding year. Against this background, the rate of unemployment in Israel dropped in 2015 from 5.6% to only 5.2%, a consequence of recruitments in the private sector due to high foreign investments. Furthermore, given that tax revenue was significantly higher than expected, along with the collection of confined profits and the measures introduced to curb government spending, the deficit in 2015 was lower than anticipated, totaling 2.4% of GDP. With respect to the upcoming year, despite the predicted improvement in global economic growth and trade, the pace in Israel is expected to remain the same, largely due to the decline in the effect of gas production and the strong Shekel which is likely to make it more difficult for exports, furthermore the Monetary Committee of the "Bank of Israel" reduced the interest rate to the lowest rate ever (0.1%) which may make it difficult to weaken the Shekel in order to encourage export . According to Bank of Israel forecasts, economic growth in 2016 is expected to stand at 2.8%.

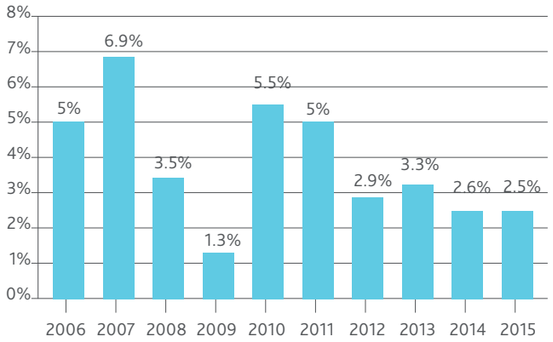
Below is a summary of the main economic indicators in Israel. This chapter includes a forecast of major economic developments based on several sources including, inter alia, the Bank of Israel's Research Department, the Ministry of Finance and number of commercial banks.

MACRO-ECONOMIC DEVELOPMENTS IN 2015

Gross Domestic Product (GDP)

In 2015, Israeli GDP increased by 2.5%, compared with a growth rate of 2.6% in 2014 and 3.2% in 2013. Israel's population grew by 2% in 2015, while GDP

Annual Growth Rate in Gross Domestic Product



Source: Central Bureau of statistic Israel, Monthly Bulletin of Statistic, January 2016.

per capita increased by 0.5%, compared with a 0.6% increase in 2014. In 2015, GDP per capita totaled NIS137.5 thousand ($35.4 thousand). By comparison, based on OECD data, GDP per capita in OECD countries increased by 1.5% in 2015.

Investments

Investments in fixed assets decreased by 3.2% in 2015, after a decrease of 2.8% in 2014 and 3.6% increase in 2013.

Investments in various fields of the economy (including the non-residential construction sector, machinery, equipment and vehicles, but excluding ships and aircraft) decreased in 2015 by 1.4%, and by 1.3% in 2014, after a 3.1% increase in 2013.

Investments in residential housing increased by 2.4% in 2015, after a 0.5% decrease in 2014 and a 6.3% increase in 2013.

Employment

The number of jobs in the overall economy as of December 2015 rose by 24.5%, compared with the corresponding period in 2014, while the average gross salary increased by 2.3%. The monthly average wage per employee in December 2015 amounted to NIS 9,591 ($2,471).

According to data recorded by the Central Bureau of Statistics, unemployment in December 2015 reached a rate of 5.2% of the civilian labor force.

Fiscal Developments

In 2015, the current balance of payments account in the government sector showed a deficit of NIS 24.5 billion - compared with NIS 29.9 billion in 2014. In terms of GDP, this amount equals to a 2.15% deficit in 2015, compared with 2.8% in 2014 - representing current income less current expenditure for all public sector bodies: the government, local authorities, national institutions and non-profit organizations, which obtain the majority of their funding from the government.

The increase in government budget deficit in 2015 reflects a 5.3% increase in tax collection, compared with 2014 in which a 5.9% rise in tax collection was reflected.

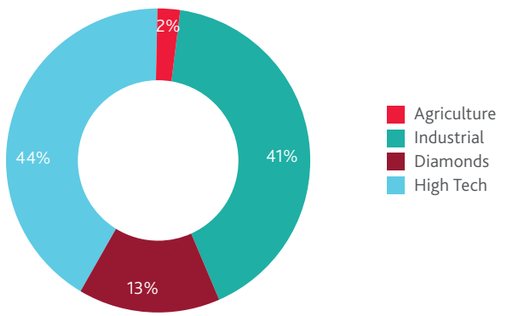
Government spending rose this year by 4.9%, compared with 3.5% in 2014.

The overall balance of payments for the government sector, obtained from summing-up the net balance in the current account and the net balance in the capital account, reflects a GDP deficit of 2.15% in 2015, compared with 2.8% in 2014.

Balance of Payments

2015 marked a decrease of 3.1% in exported goods and services , after a rise of 1.5% in 2014 and 0.1% in 2013. Industrial exports, excluding diamonds, remained at the same level this year compared to 2014, after an increase of 3.9% in the previous corresponding period. Revenue from the export of tourist services dropped by 1.2% in 2015 following the decrease of 2.1% in 2014. Export of services excluding tourism and start-up companies, that primarily include software and research services, decreased by 2.4% in 2015, after an increase of 9.2% in 2014. Diamond exports decreased by 20.4% while agricultural exports dropped by 12.2% in 2015. Import of goods and services (excluding defense imports, ships, aircraft and diamonds), marked an increase of 1.9% this year, after an increase of 3.3% in 2014 and a decrease of 2% in 2013. Import of goods and services, including defense imports, ships, aircraft and diamonds, has dropped by 0.2% after an increase of 3% in 2014 and of 0.5% in 2013.

The composition of Israel's international export in 2015:

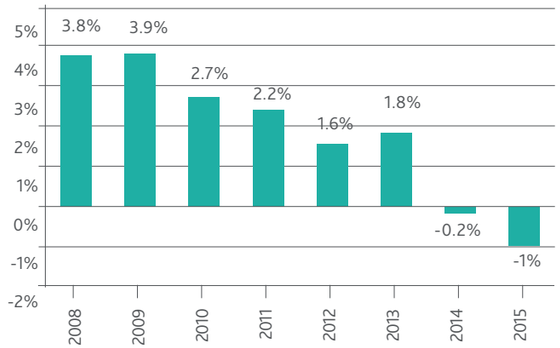


Source: The Israel Export & International Cooperation Institute, Summary of export data for 2015 and forecast for 2016, January 2016.

Monetary Development & Capital Markets

The Consumer Price Index (CPI) decreased by 1% in 2015, compared with decrease of 0.2% in 2014 and increase of 1.8% in 2013. In 2015, the government's annual inflation target of 1%-3% was not accomplished. The main contributors to the CPI drop in 2015 were the energy prices.

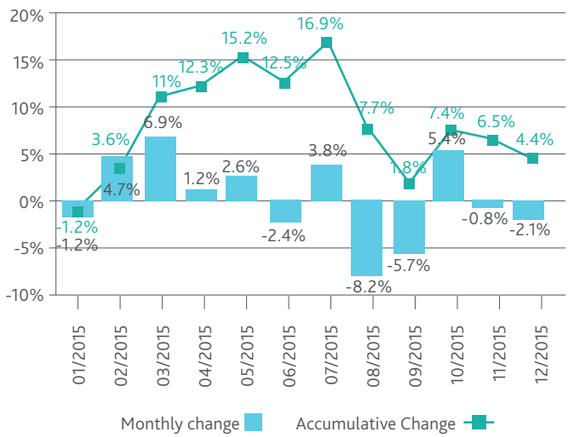
Inflation Rates



Source: Bank of Israel, January 2016.

During 2015 interest rates dropped by 0.15 percentage points in March, setting it at 0.1%. Between March and the end of the year, the interest rate remained unchanged. The monetary policy change, reflected by a decrease in interest rates, is explained by the attempt to minimize the negative influence of the global economic activity on the Israeli market in order to encourage economic growth. Owing to a decline in the inflation environment over recent months, alongside the continued moderation in private home prices, the Bank of Israel was able to pursue its expansionary monetary policy.

TA 25 Index (Maof)



Source: Tel Aviv Stock Exchange, January 2016

The year 2015 opened with negative trend, after a positive trend that began in the last quarter of 2014, shown a drop of 1.2% in January. Since February, however, the trend was changed and during the following six months TA 25 increased by 18.1%. During August and September TA 25 decreased by 15.1%, and over the last quarter of 2015 it increased by 2.6%.

In total, TA 25 increased by 4.4% in 2015, compared with 10.2% increase in 2014. In the corporate bond sector, both the high-yield bonds as well as the general corporate bonds provided a positive return. The corporate bond yield increased by 1.5%, attaining a market value of NIS280 billion.

The net amount of capital raised by the government in 2015 decreased to a total of $4.96 billion, compared with $5.17 billion in 2014. The reduction in Finance Ministry gross IPOs was made possible inter alia due to budget deficit cuts – which dropped to 2.4% of GDP this year, compared with 2.8% in the previous year.

Industry indices experienced price increases. The TA-Finance index marked a 3.96% increase over the year while the Blue Tech 50 marked a 1.64% increase.

In 2015, the public purchased ETFs totaling $1 billion. The public's holdings this year dropped by $1.54 billion to a total of $31.6 billion in November 2015, when most of the decrease stemmed, as aforesaid, from public sales, mainly of ETFs over domestic share indices due to a very low interest rate.

The daily trading volume in ETFs over share indices (domestic and international) rose in 2015 (on the TASE and elsewhere) by $119.6 million, higher by 28% than in 2014. This volume comprised some 32% of the overall share trading volume, compared with 30% in the preceding year.

2015 has marked a decline in IPOs and private placements in Israel, reaching $1.44 billion – compared with $1.9 billion in the preceding year. There were two IPOs in 2015, for a total of $38.6 million. The two companies are real estate companies: Vitanya and Oron Group.

Nine further companies jointed the TASE in 2015, through operations in "shell companies"; 3 of them were operations in the biomed and technology sectors.
Real estate companies raised $0.7 billion through share offerings. This amount comprises half of the amount raised this year through share offerings to the public.
By the end of the year, 462 companies were listed on the TASE, compared with 473 in 2014. At present, there are 55 dual companies listed in the USA and Europe and 4 additional companies listed on both the TASE and Europe.

FORECAST OF ECONOMIC DEVELOPMENT IN 2015

The main sources for the following table are publications of the Ministry of Finance, Bank of Israel and commercial banks.

Annual Change in	2008	2009	2010	2011	2012	2013	2014	2015	F2016*
Inflation	3.8%	3.9%	2.7%	2.2%	1.6%	1.8%	-0.2%	-1%	0.8%
Revaluation vs. US$	1.1%	0.7%	6.0%	-7.7%	2.3%	-7%	12%	0.3%	-
GDP	3.5%	1.3%	5.5%	5%	2.9%	3.3%	2.6%	2.5%	2.8%
GDP per capita	3.0%	-1.1%	2.7%	2.7%	1.5%	1.3%	0.6%	0.5%	0.3%
Investment in fixed assets	4.1%	-5.8%	13.6%	16.0%	3.2%	1.1%	-1.3%	-1%	3.8%
Unemployment	6.1%	7.4%	7.0%	5.6%	6.7%	5.8%	5.9%	5.3%	5.6%
Export	5.9%	-12.6%	13.4%	5.5%	1.0%	-1.6%	1.5%	-3.2%	2.0%
Import	2.4%	-14.0%	12.6%	11.1%	3.2%	4.3%	3%	0.6%	3.4%
Public Consumption	3.2%	2.5%	3.7%	2.9%	3.2%	3.2%	3.2%	2.9%	3.4%
Private Consumption	3.9%	1.7%	3.3%	1.9%	3.2%	4.0%	3.7%	4.9%	4.3%
Housing Starts	6.1%	6.0%	9.9%	9.0%	-15.1%	5.5%	-1.6%	3.9%	-

* Forecast for 2016

ISRAEL GENERAL OVERVIEW

BACKGROUND // GOVERNMENT // FACTS AND FIGURES // ISRAEL'S CURRENCY // INFRASTRUCTURE // WORKING IN ISRAEL // BUSINESS HOURS

Since declaring its independence in 1948, Israel has been the home of Jewish immigrants from all over the world. The country's population - comprising approximately 74.9% Jews, 20.7% Arabs, and 4.4% others - increased from 870,000 inhabitants in 1948 to over 8.46 million in 2015.

BACKGROUND

Over the past decade alone, Israel's population has grown by 18.3%. However, since 1992, the immigration rate has gradually declined. In 2015, about 28 thousand people immigrated to Israel. This is the largest number of immigrants in a decade, compared with 26.5 thousand in 2014.

An important economic landmark influencing the development of the modern Israeli economy was the intensified negotiations in the 1990's with the neighboring Arab countries, which attracted an increasing number of direct and indirect foreign investors to Israel. This was followed by the high-tech bubble burst at the beginning of the last decade and the deterioration of the geopolitical situation.

However, the global economic conditions continue to affect Israel as an open market exposed to economic trends. The effect of the recent events in the global environment is relatively moderate, but their impact is expected to be greater in future. Indications of an economic slowdown are evident, represented by a moderate GDP growth rate of 2.5% in 2015, and the Bank of Israel's 2.8% growth forecast for 2016.

GOVERNMENT

Israel is a secular democracy whose parliament (Knesset) is elected through general elections every four years, unless the Knesset or Prime Minister decide to hold them earlier. Under certain circumstances, the Knesset can also serve for more than four years.

Israel has an electoral system based on nation-wide proportional representation, and the number of seats which each party receives in the Knesset is proportional to the number of voters. The only limitation is the 3.25% qualifying threshold. According to this system, voters vote for a party list and not for a particular candidate on the list.

Since the establishment of a 'primaries' system in some of the parties, these parties directly elect their candidates for the Knesset. In other parties, candidates are elected through the party's institutions.

All Israeli citizens over 18 are entitled to vote, whilst those over 21 may be elected to parliament.

After the elections, the Israeli President consults with representatives of all parties and, subsequently,

delegates the task of forming a government to the chairman of the party most likely to succeed. If he or she succeeds, he or she is nominated as Prime Minister and is responsible for forming a government and appointing ministers.

The last general elections in Israel were held in March, 2015. The President appointed Benjamin Netanyahu, head of the Likud party and incumbent prime minister, to form a government.

The function of the President of the State is primarily a representative one. The president is elected by the Knesset every seven years, for a limited period of one term. The President holds the statutory power to accredit diplomatic senior staff, pardon criminals, sign on laws etc.

The judicial system is independent of the executive and legislative systems. The Supreme Court is the highest court of the State, serving both as the High Court of Appeal and the High Court of Justice.
Below the Supreme Court are the District Courts (located in Jerusalem, Tel-Aviv, Haifa, Nazareth and Beer-Sheva). The District Court is the first court of submission for certain judicial matters - in addition to administrative courts, family courts, municipal courts, religious courts, etc. Each type of court has a clearly defined area of jurisdiction.

Israel's central bank, the Bank of Israel, serves as economic advisor to the government. It defines and implements monetary policy, controls local banks, supplies notes and coins, manages the State's foreign currency, etc. Another administrative institution is that of State Comptroller - responsible for auditing and checking all the activities of the ministries, municipalities and other institutions subject to inspection by law.

FACTS AND FIGURES

Israel is situated along the Mediterranean coast, with an area of 22,000 km. (8,500 sq.). This is exclusive of the territory of the Gaza Strip and parts of the West Bank, which were given to the Palestinians in the context of the Peace Process and the Disengagement Plan.

Israel is about 430 km (265 miles) long and 110 km (70 miles) wide. It borders Lebanon in the north, Syria in the northeast, Jordan and the West Bank in the east, the Gaza Strip and Egypt on the southwest.
Modern Israel has numerous ancient sites with ongoing archeological digs. New archeological findings are constantly discovered.

Israel's terrain varies from hilly, mountainous landscape, with rich agricultural land in the north, to barren desert sites in the south. The lowest place on the globe, the Dead Sea, is situated in the south of Israel.

Israel's major cities:

Jerusalem - The capital of Israel and location of the Knesset and numerous historic and religious sites; population - approximately 872 thousand.
Tel-Aviv- Israel's largest city - financial, commercial and industrial center, with a population of approximately 1.37 million.
Haifa- Principal port city in the north of Israel, with a population of approximately 568 thousand.
Beer Sheva- The largest city in the Negev desert (in the south), with a population of approximately 692 thousand.

Israel has a Mediterranean climate, characterized by long, hot, dry summers (June to September), with temperatures usually in the high 80's (27C), 90's (32C). Jerusalem is dryer and cooler, Eilat extremely hot but dry. Winters are short, mild and wet, 50-60's (10-15C) in most places, but in the 40's (5C) in Jerusalem.-, where it can be very cold at night.

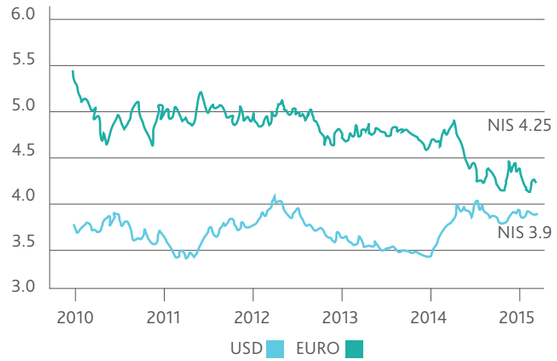
Israel's average annual rainfall varies from over 800 mm (31 inches) in the north (Upper Galilee) to less than 40 mm (1.6 inches) in the south (Eilat).

The prevailing system for measurement is the metric system.

ISRAEL'S CURRENCY

Israel's monetary unit is the New Israel Shekel (NIS). One NIS is comprised of 100 Agorot.
The representative Dollar rate is an indicator for its exchange rate on the foreign currency market. It is based on the average buying and selling rates published by the banks.
Other foreign currency rates, besides the Dollar, are calculated at their rate on international currency markets, when the representative rate is being determined. Accordingly, the ratios for the representative rates of various currencies reflect their exchange rates abroad at the time they are determined. The Bank of Israel calculates representative exchange rates once a day on foreign currency business days only. The following graph presents the foreign exchange rates in Israel during the years 2010-2015:

Exchange rates 2010-2015



The representative exchange rates of the Israeli Shekel in relation to some major currencies on December 31, 2015, were as follows:

	NIS
US Dollar	3.9020
EURO	4.2468
UK Pound Sterling	5.7840
Swiss Franc	3.9246
Japanese Yen (100)	3.2406
Chinese Yuan "Renminbi"	0.5986

INFRASTRUCTURE

Israel offers a broad and solid infrastructure to entrepreneurs, investors and business people in all sectors. The Israeli banking system is modern, automated, highly computerized and a well-established component of the international banking system.

Diverse services required by businesses, such as insurance, legal, temporary manpower, communications; IT systems etc. are available in the most advanced formats.

There is an advanced domestic and international transportation system, with an extensive inter-urban highway network. New highways are constantly being built to enable fast and safe mobility throughout the country. Israel is linked to the rest of the world via air and sea.

WORKING IN ISRAEL

In order to work in Israel, a non-resident is required to obtain a work permit (usually B-1 visa) or hold a status other than "tourist". To obtain work permits, Israeli employers are required to apply to the Ministry of Labor and Social Affairs and, where applicable, to the Investments Center as well.

According to the "Law of Return", immigrants are entitled to a "permanent resident" status, or an A-1 visa, granting immigrant a "temporary resident" status.

BUSINESS HOURS

Full time work hours are generally 40-45 hours per week in a 5-5.5 day week, beginning on Sunday and ending on Thursday, or Friday at noon.

Work hours in administrative offices are generally from 8:00-9:00 am to 4:00-5:00 pm. Some banks are open from 8:30 am to 12:30 pm from Sunday through Thursday and from 4:30 to 6:30 pm on two afternoons, while others are closed on Sundays, but open on Friday.

Stores are regularly open until 7:00 pm or later. On Saturday (the Jewish Sabbath) almost all businesses and offices are closed.

Legal holidays are determined in accordance with the Hebrew calendar. On the eve of Jewish holidays, business usually ends in the early afternoon.

Legal holidays in 2015 and 2016 were as follows:

Holiday	2015	2016
Passover	April 3	April 22
Independence Day	April 23	May 12
Pentecost (Shavuot)	May 23	June 11
Jewish New Year	Sep 13	October 2
Day of Atonement (Yom Kippur)	Sep 22	October 11
Feast of Tabernacles (Sukkot)	Sep 27	October 16

M&A ACTIVITY IN ISRAEL

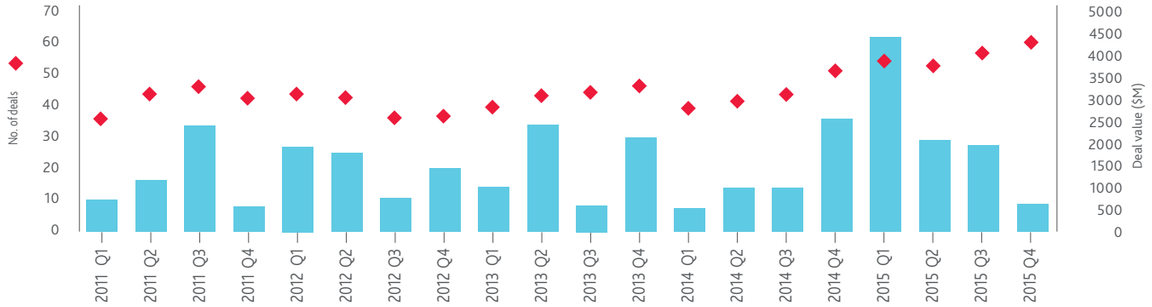
GENERAL // REGULATION AND LEGISLATION // FOUNDERS // PRIVATE EQUITY ACTIVITY // ISRAELI VENTURE CAPITAL FUND RAISING // ISRAELI MARKET MULTIPLES

2015 generated new M&A activity records and preserves the positive trend of recent years. The substantial increase of volume and value of deals in 2015 was partly due to a continued low interest rate environment, characterizing the global market. The improving macro environment also has helped boost the confidence in the Israeli economy, proven by interest of local and foreign investors alike.

GENERAL

M&A activity of Israeli companies is quite significant. 223 transactions were conducted during 2015 for an overall value of $8.9 billion, compared with 173 in 2014 for $4.9 billion.

M&A Israel



Source: Bloomberg

Even though both 2012 and 2013 seemed to reflect a certain slowdown in M&A activity in the country, 2014 and 2015 showed a significant improvement. The Israeli business environment is expected to generate significant M&A opportunities in the upcoming years due to new regulations/legislation, liquidity issues and other reasons discussed below.

REGULATION AND LEGISLATION

The Israeli corporate sector is generally dominated by large conglomerate groups. There are roughly 20 families controlling 25 percent of the listed Israeli companies and 50 percent of the total market share in the Tel Aviv Stock Exchange (TA-25), one of the highest concentrations among developed economies. Concerns that the growth

of market power and control might have an adverse effect on competition have led to the recent creation of the Committee on Increasing Competitiveness in the Economy (CICE).
CICE's recommendations were published at the beginning of 2012 and were followed by adequate legislation during 2013, and are intended to take effect within the next four years:

- **Pyramid holding structure** - Holding companies will have to limit their pyramid structure to no more than three public layers.
- **Cross-Holdings** - Holding companies must reduce cross-holdings in financial and industrial businesses. The outcome of the new regulation and legislation will lower the risk of highly-leveraged companies and reduce their relative strength in the economy, while increasing the influence of minority shareholders. Furthermore, the new regulation and legislation would compel holding companies to divest some of their holdings, while bringing dynamism and change of ownership, thereby increasing competition among businesses and reducing consumer prices in the market.

FOUNDERS

The Israeli business environment and culture has always supported entrepreneurship and start-ups, and during the 70's a significant number of businesses were established, encouraged by government regulations and economic reforms. Consequently, many business owners have now reached the retirement age, in some cases without the emergence of the next generation to succeed them, thereby creating an inevitable need to sell the business.

PRIVATE EQUITY ACTIVITY

Israel is enjoying a growing interest in both local and foreign Private Equity Funds (PE's).
The successful local PE activity has in recent years also attracted the large global PE funds and investment companies - such as Berkshire Hathaway (Iscar), Apax partners (Bezeq, Psagot, Tnuva), Permira (Netafim); others, notably Blackstone, Blackrock, KKR, are expected to introduce their operations in Israel in the near future.

PE activity is also expected to generate significant "sell side" opportunities. Most funds are obliged to exit their investments within 7 to 10 years since their acquisition. As the major activity of most funds had occurred during 2005-2008, various opportunities are expected to be out in the market in the upcoming years.

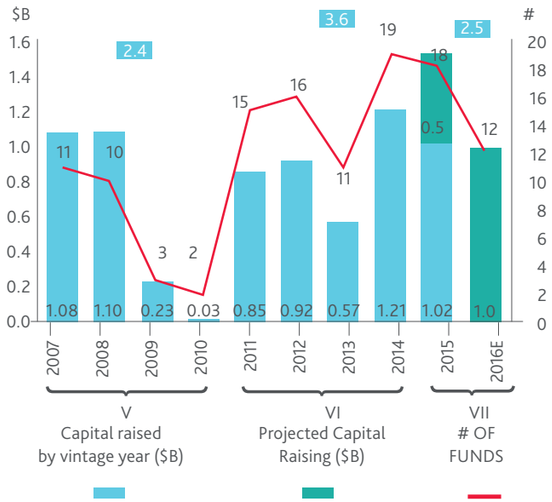
ISRAELI VENTURE CAPITAL FUND RAISING

Israeli VC funds raised $1.02 billion in 2015 vintage. Four VC funds raised more than $100 million each, 59% of total capital.

The seventh venture capital raising cycle that started early in 2015 - with 83North's $204 million closing announcement - followed a successful sixth cycle between 2011 and 2014, concluding with a total of $3.6 billion raised by 61 funds. The sixth cycle had been the strongest one since the early 2000s, ending with $1.2 billion for vintage 2014 funds, the strongest vintage year in the past decade. The sixth cycle's most evident trend was the increase in the number of micro-VC funds, with 33 micro funds raising capital during this period, more than three times the number of such funds in the previous two cycles.

2015 vintage was marked by the emergence of six new growth funds, an outstanding number of funds dedicated to growth stage companies. While it may be a bit early to tell, it seems this might be a new trend for the seventh cycle.
At the beginning of 2016, over $2 billion is available for investments by Israeli venture capital funds. Of this amount,

Chart 1: Total Capital Raised By Israeli VC Funds By Vintage Year ($B) 2007-2016(E)



a little over $500 million is earmarked for first investments. The remainder is reserved for follow-on investments.

ISRAELI MARKET MULTIPLES

The developed countries tend to have lower multiples, supported by lower market expectations, even though the perceived risk is considered to be relatively low. Although there are no formal sources tracking the Israeli market multiples over time, the domestic market is traditionally "enjoying" lower EBITDA multiples most commonly in the range of 5-10 (there are always exceptions, such as Given Imaging acquisition for roughly $1 billion with an EBITDA multiple of 35) - significantly lower than the global average. The main reasons are:

- **Size Premium -** Israeli companies are usually smaller than the average company in the global market, and thus receive a negative size premium.
- **Geopolitical Perceived Risk -** Foreign investors perceive a higher geopolitical risk in Israel than in their homeland.
- **Limited Competition –** Even though the Israeli market attracts various foreign investors, the local Israeli market has a relatively limited amount of potential bidders, which drives lower prices in M&A deals.
- **Capital Market -** The Israeli capital market provides a pricing reference for M&A deals. Since the market volume and attraction is globally limited, so is its pricing.

In 2010, Israel joined the OECD and was added to the MCSI index, reflecting its change of status to a "developed country". Accordingly, the Israeli market's relatively low multiples are expected to increase in the future, yielding a potential extra capital gain as a higher return on investment, compared with other developed countries and the global average in general.

OVERVIEW OF ISRAEL'S HIGH-TECH INDUSTRY

INTRODUCTION // CAPITAL RAISING IN 2015 // THE VENTURE CAPITAL INDUSTRY // ANALYSIS OF VENTURE CAPITAL RAISED BY INDUSTRY // COMMUNICATIONS // CAPITAL RAISED // THE BIOTECHNOLOGY INDUSTRY

The technology industry in Israel has been the driving force of the nation's economy, and has played a prominent role in Israel's economic development, particularly over the past decade. 2015 was characterized by a positive trend in the high-tech sector, reflected by an impressive number of 104 exits for a total amount of $9.02 Billion, an increase of approximately 16% from 2014.

ISRAEL'S HIGH-TECH INDUSTRY: INTRODUCTION

Only 25 years ago, most of the country's technology was concentrated in military/security-related industries. Although Israel was not a major factor in the global high-tech industry at the time, Israeli companies now have a strong foundation in high-tech industries worldwide and Israel ranks among the leading countries in the number of Nasdaq-listed high-tech companies.

As the high-tech sector - despite the recession in the early 2000s - became the primary engine for economic development, its recovery in 2005 was essential in bringing Israel's economy back to a sustainable growth path. This was reflected in the boost in investments, recruitment of capital, cutback in unemployment, high-tech exports and corporate mergers - all of which have demonstrated precisely this. Various indicators show that, after a slight rise in 2005, growth was sustained in 2006 and 2007, marking an improvement in the high-tech sector.

However, given the credit crunch in 2008, the financial resources available for the high-tech industry have declined significantly, causing high-tech and start-up companies to lay off employees or shut down completely. This trend continued during the first half of 2009. But in mid-2009 it became evident that the effect of the global crisis on Israel was relatively mild. Consequently, the market began moving towards an upward trend, which persisted through 2010 to 2013.

2015 was characterized by positive trend in the high-tech sector, reflected by an impressive number of 104 exits in total amount of $9.02 Billion, an increase of approximately 16% from 2014. One of the more outstanding deals of the year was the acquisition of Fundtech by D+H, an international FinTech company for total of $1.25 billion. The acquisition of Valtech by HeartWare followed, with $929 million. Furthermore, 2015 was characterized by significant decline in both the number and size of IPO exits. Eight IPOs accounted for $0.6 billion, compared to seventeen IPOs that brought proceeds of some $2.1 billion in 2014.

Alongside the success, however, various high-tech companies were faced with major challenges, including budget cutbacks, shutdown of divisions and staff dismissals.

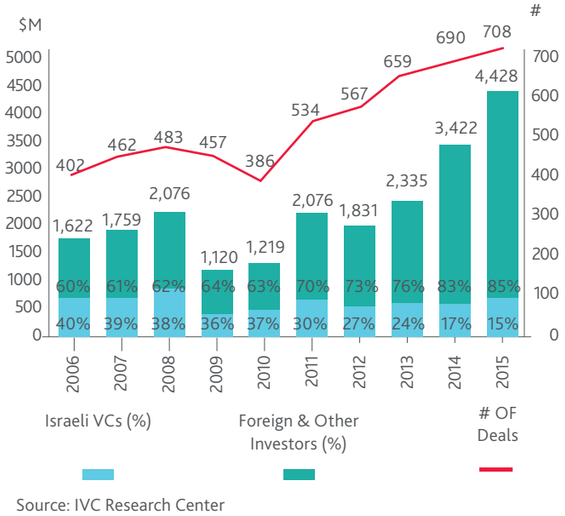
[1] This chapter is based on data gathered by IVC Research Center, July

THE HIGH-TECH CAPITAL RAISING IN 2015

In 2015, approximately 708 Israeli high-tech companies raised $4.4 billion from local and foreign investors. This figure is 29% higher than the $3.4 billion raised in 2014, and 90% higher than the $2.3 billion raised in 2013.

Capital invested in Israeli High-Tech Companies by Israeli VC Funds, Foreign and Other Investors (%) 2006-2015.

Israeli High-Tech Capital Raising ($m) 2006-2015



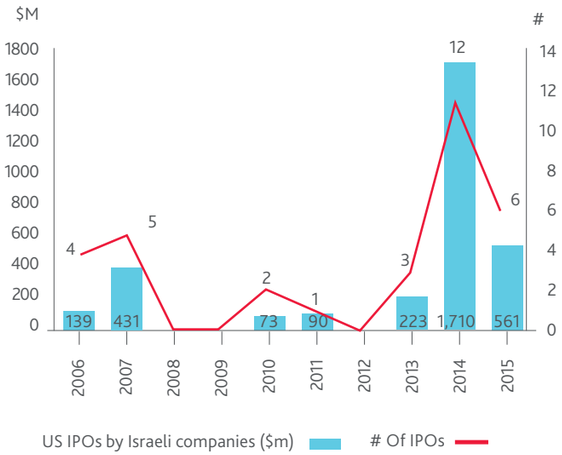
Source: IVC Research Center

In 2015, venture capital funds constituted 15% of the overall capital invested in Israeli high-tech companies, compared with 17% in 2014 and 24% in 2013. There are signs of an increase in the number of investments made by foreign and other investors.

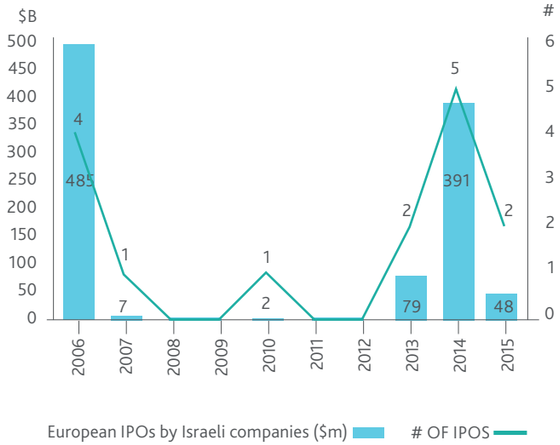
In 2015, 6 companies were listed on the NASDAQ, raised an accumulated amount of $561 million, compared with twelve companies listed in 2014 which raised an accumulated amount of $1,710 million. In addition, 2 companies were listed on the European Stock Exchange, raised an accumulated amount of $48 million, compared with 5 companies listed in 2014 which raised an accumulated amount of $391 million.

The following graphs illustrate the amount of capital raised in the U.S. and European IPOs:

Capital Raised in IPOs on the US Stock Exchange by Israeli High-Tech Companies in 2006-2015



Capital Raised in IPOS on the European Stock Exchange by Israeli High-Tech companies in 2006-2015



THE VENTURE CAPITAL INDUSTRY

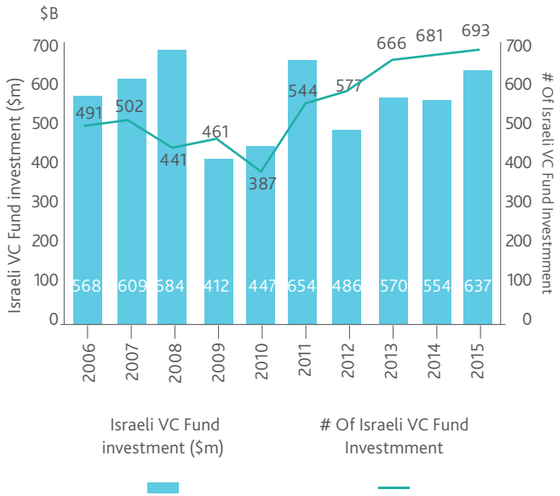
Israel's venture capital (VC) industry has played a fundamental role in the dramatic development of the high-tech industry over the past years. By providing and allocating funding, VC has served as a link between start-up companies and investors, and is regarded as essential infrastructure for any technological environment. It is also an effective tool for financing, supporting and guiding companies towards a successful course, in addition to being one of the leading VC industries worldwide, with dozens of funds operating from Israel ("Israeli VC Funds").

The funds are supplemented by other investors, including public companies, private investors and non-Israeli-based VC funds.

The VC industry has grown tremendously over the past decade. This is due to several factors, including: tax exemptions on Israeli VC investments, funds established in conjunction with large international banks and financial companies, and the involvement of major organizations wishing to capitalize on the numerous technology companies originating in Israel.

In 2015, Israeli VC funds invested $637 million in Israeli high-tech companies, compared with $554 in 2014 and $570 million in 2013.

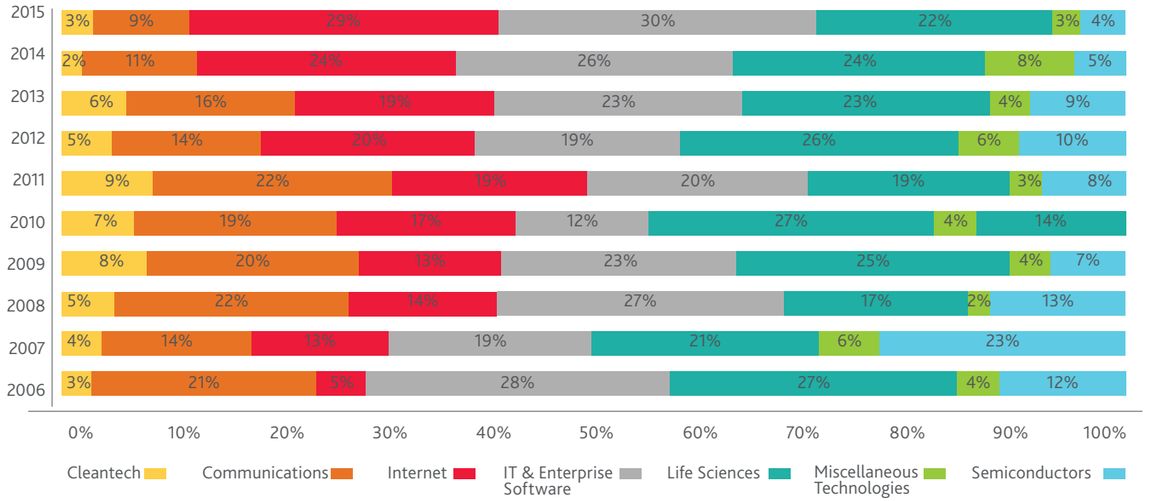
Capital Invested in Israeli High-Tech Companies by Israeli VC Funds (M$), 2006-2015



ANALYSIS OF VENTURE CAPITAL RAISED BY INDUSTRY

Israeli companies have a distinct presence among the various high-tech industries. The capital ratio raised by the different sectors has varied over the past few years.
In 2015, the IT / Software & Internet sectors attracted the largest share of investments and raised approximately $1.3 billion each, or 30 & 29 percent of the aggregate capital raised by Israeli high-tech companies. Life Sciences sector followed with approximately $1 billion, or 22 percent of the aggregate capital raised by high-tech companies, and the communications sector attracted approximately $0.4 billion, or 9 percent.
The following graph displays the relative part of the different sectors out of total capital raised over the past years:
Below is an analysis of the capital raised by Israeli companies in leading sectors of the economy. The data is based on IVC Research Center analyses.

Capital Raised by Israeli High-Tech Companies by Sector (%), 2006-2015



COMMUNICATIONS

Communications is considered a major field for raising capital. Whilst in 2006 communications related venture capital reached 21% out of the aggregate amounts, recent years, however, have been marked by a decline in this sector's share. The capital raised by the communications sector during 2013, 2014 and 2015 reached 16%, 11% and 9% respectively out of the aggregate amounts.

It should be noted that the local media and telecommunications field has undergone various changes over the past decade, turning it into an attractive and accessible market for investors generally. One example is the vigorous competition evident in the multi-channel broadcasting field.

Software

Software companies raised 30% of the overall amount of capital invested in 2015 - indicating an increase compared with 26% in 2014 and 23% in 2013.

Internet

The capital raised by Israeli high-tech companies via the internet sector amounted to 19%-29% over the past three years, compared with 5%-14% during 2006-2008. In 2015, capital raised by this sector amounted to 29%.

Life Sciences

The life sciences is a major field as far as capital recruitment is concerned. In 2015, Life science companies raised 22% of the overall capital invested.

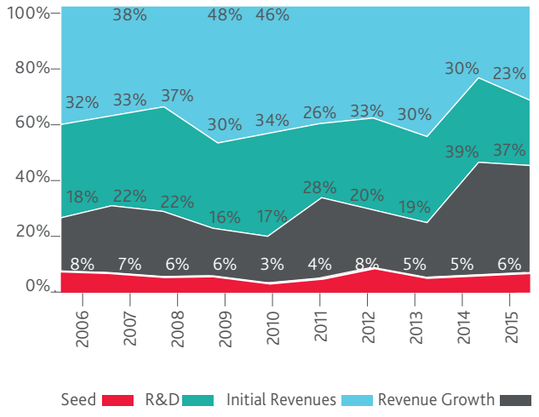
CAPITAL RAISED BY ISRAELI HIGH-TECH

The life span of a company is defined by several stages - from the earliest, known as the "seed" stage, to the last - known as the "revenue growth" stage (when a company operates as a selling entity).
Over the last several years, the capital structure in a company's development stage has changed. In the 90s and at the beginning of the last decade, investments during the initial phase were common. Today, the majority of investments are made during the intermediate and later stages, in order to lower risk levels.

In 2015, late stage companies led capital raising with $1.6 billion or 37% of total funds raised. Seed companies attracted 6%, slightly above the 5% of 2014. Early stage companies (R&D) accounted for 23%, marking a decrease from 30% in 2014 and in 2013. Initial revenue stage companies raised 34% which is $1.5 billion, an increase of approximately 70% from 2014.

The following graph illustrates the distribution of capital raised over the past ten years by stages:

Capital Raised by Israeli High-Tech Companies by Stage (%), 2006-2015



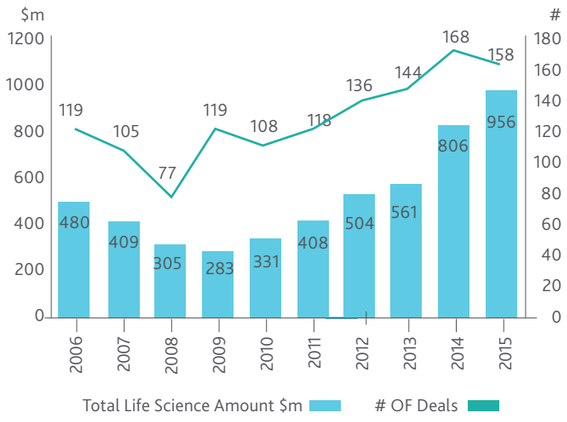
THE BIOTECHNOLOGY INDUSTRY IN ISRAEL

Modern science utilizes biological information accumulated over 150 years - mainly the genetic code and DNA structure decoded some 50 years ago. The biotechnology business environment has evolved as a result of the breakthrough in genome development over the past years. The information accumulated in a genome project, in which whole platforms of the human genome were discovered, has created new opportunities for many start-up companies. The assumption is that Israel's fast and cost-effective development cycle is the key advantage relative to United States counterparts, attracting investment funds from various parts of the world.

Total investment in the life science companies during 2015 amounted to $956 million, reflecting an increase of 19% compared with $806 million raised during 2014.

The following graph illustrates the capital raised by the life science industry over the past years:

Capital Raised by Israeli Life Science Companies ($M), 2006-2015

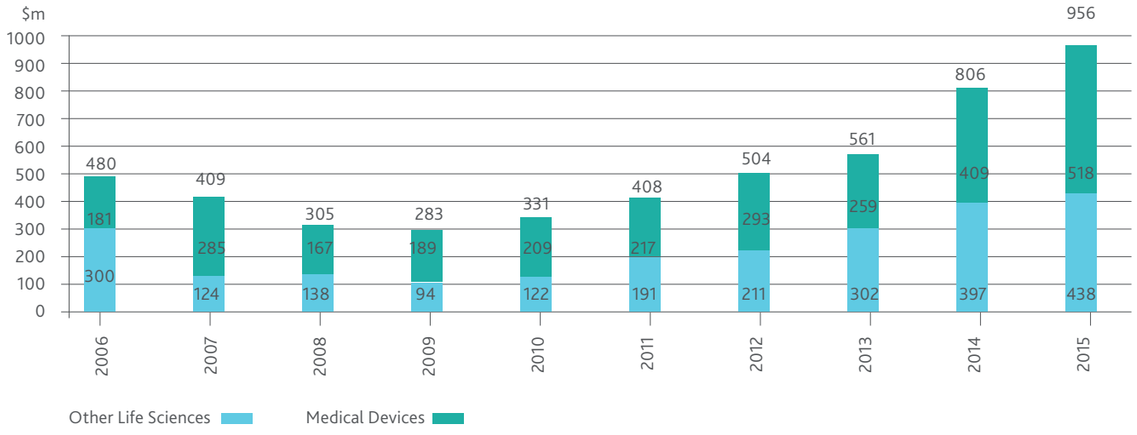


A major sub-branch of biotechnology is the field of medical devices. This sector drew, in 2015, 55% of the aggregate capital raised for the industry - marking an increase of 4% of its share compared with the previous year.

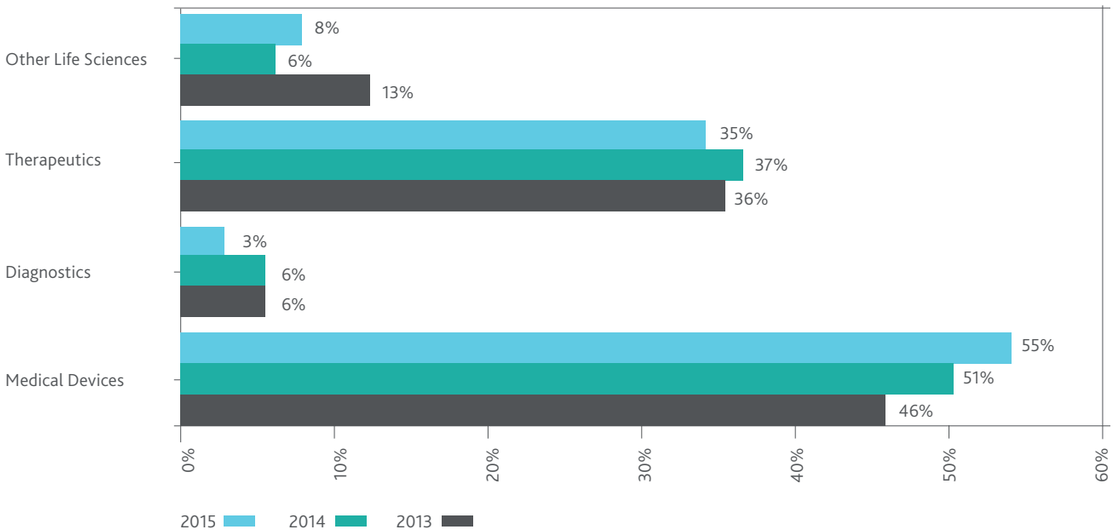
The Israeli government has encouraged investments in this sector, by initiating plans to establish incubators dedicated to bio-technological development.

The following graph shows the capital raised by the Israeli life science industry and the dominance of medical device companies vis-a-vis other sectors over the past years:

Capital Raised by Israeli Life Science Companies (%), 2006-2015



Capital Raised by Israeli Life Science Companies (%), 2013-2015



BUSINESS ENVIRONMENT

HUMAN RESOURCES // ANTITRUST LAW // INTERNATIONAL TRADE // TRADE AGREEMENTS // PROPRIETARY RIGHTS

Business activity is subject to various laws and regulations, depending on the nature, scale, sector, etc. of the business, and requires licenses from ministries, municipalities, authorities, and other statutory authorities. In general, common business and trade practices are restricted by rules and regulations similar to those prevailing in other Western countries.

HUMAN RESOURCES

Education

Israel's labor force is relatively well educated. The following table provides data regarding the years of schooling of Israelis aged 15 and over:

Years of schooling	
0	2.2%
1-4	0.8%
5-8	5.9%
9-10	9.4%
11-12	33.9%
13-15	22%
16+	25.9%

Source: Central Bureau of Statistics, Israel, Statistical Abstract of Israel, 2015

Distribution Of Employees

The work force in 2014 totaled approximately 3,293,400 employees. The following table summarizes the distribution of employed persons according to economic sectors in average for the year 2014:

Economic Sector	
Agriculture	1.49%
Manufacturing	11.21%
Electricity and water supply	0.81%
Construction	5.27%
Trade (Retail and Wholesale)	14.31%
Accommodation services and restaurants	6.49%
Transportation, storage and communication	3.52%
Banking, insurance and finance	3.23%
Education	14.53%
Health, welfare and social work	11.96%
Administrative and support service activities	9.04%
Information and communications	4.88%
Professional, scientific & technical activities	8.4%
Art, entertainment and recreation	4.86%

Source: Central Bureau of Statistics, Israel, Statistical Abstract of Israel, 2015

Salaries and wages paid to Israeli employees are highly diversified. The following table presents the average wages per employee sector. The figures are rounded and presented in US Dollars, per month:

Industry	US$*
Agriculture	1,732
Manufacturing	3,427
Electricity and water supply	4,987
Construction	2,508
Trade (Retail and Wholesale)	2,200
Accommodation services and restaurants	1,102
Transportation, storage and communication	2,850
Banking, insurance and finance	4,354
Education	1,928
Health, welfare and social work	2,191
Administrative and support service activities	1,283
Information and communications	4,572
Professional, scientific & technical activities	3,575
Art, entertainment and recreation	1,513

*Per month. US$1=NIS 3.8869
Source: Central Bureau of Statistics, Israel, Statistical Abstract of Israel, 2015

As of April 2015, the minimum monthly salary in Israel was set at NIS 4,650 [NIS 25 per hour]. As of July 2016, the minimum monthly salary in Israel will be raised to NIS 4,825 [NIS 26 per hour]. In addition to salary, the employee is entitled to compensation for travel expenses to and from his regular place of work (public transportation tariffs).

For most employees, overtime is paid at the rate of 125% for the first two hours and 150% for subsequent hours each day. Employees are entitled to special compensation for work on Saturdays and holidays.

In addition to salary, the employer is required to pay/contribute to various social benefits, as follows:

Compulsory contributions:

- **National Insurance (Social Security)–** is 6.72% of gross salary (in addition to the employee's contribution). The National Insurance Institute pays compensation in respect of unemployment, disability, retirement, military reserve duty, child allowances, maternity leave, etc.
- **Severance pay –** is 8.33% of gross salary. An employee dismissed from his place of work is entitled to severance pay based on her latest salary amount for each year of employment.
- **Sick leave –** is accumulation of 1.5 days per month. In many cases, the sick leave allowance may amount to 30 days per annum. Employees may accumulate up to 90 sick days.
- **Vacation -** Israeli law prescribes a minimum vacation period of two weeks annually. The number of days increases according to seniority, reaching four weeks for those employed more than fourteen years by the same employer. The vacation allowance is payable in addition to legal and religious holidays.
- **Annual reserve military service -** The employer usually pays the employee's regular salary, including all social benefits, for the entire reserve duty period. The National Insurance reimburses the employer for the gross salary during the employee's reserve duty.
- **Convalescence pay –** Employees are entitled to convalescence pay according to seniority at work and based on the Collective Work Agreement. The minimum amount for full time employees in the business sector is US$ 486 per annum and it may reach approximately US$ 972 per annum.
- **Pension Insurance –** All employees are entitled to pension insurance after 6 months of employment. An employee with a pension fund from the previous workplace is entitled to contribution from the first day of work, which is payable 3 months after the start of employment at the new workplace. Pension contribution by the employer is set at 12% and by the employee at a minimum rate of 5.5%. Together a minimum of 17.5% is contributed. As of July 2016, the contribution by the employer will be set at 12.25% and contribution by the employee will be set at a minimum rate of 5.75%.

In addition to the above social benefits, other legislation and regulations exist to regulate working conditions, but they cannot be directly "converted" into money. Among these laws and regulations are the following:

- **Employment of Women Law** - the law protects female employees and specifies the terms and restrictions imposed on employers regarding their female employees in connection with night work, pregnant women's rights, maternity leave, etc.
- **Equal Opportunity in Employment Law -** prohibits discrimination against employees in all matters and for any reason.
- **Equal Pay Law -** legislates female employees' rights to equal pay for equal work with the same employer.
- **Youth Labor Law** - regulates the work conditions of individuals under 18.

ANTITRUST LAW

Business activity is subject to various laws and regulations, depending on the nature, scale, sector, etc. of the business, and requires licenses from ministries, municipalities, authorities, and other statutory authorities. In general, common business and trade practices are restricted by rules and regulations similar to those prevailing in other Western countries. However, particular attention ought to be paid to the Antitrust Law, 1988, enforced by the Israeli Antitrust Authority.

Restrictive Practice Agreements

A restrictive arrangement is an agreement made between individuals conducting business, pursuant to which at least one of the parties restricts itself in a way that could obviate or reduce the business competition between that party and part or all of the other parties to the agreement, or between that party and an entity that is not a party to the agreement.
An agreement that determines prices, market share, profit margins, or quotas will be deemed to be a restrictive agreement. However, the law excludes some agreements from its general definition so that they are

not considered restrictive agreements (e.g. entitlement to use proprietary rights, international transport, etc.).

Participation in any restrictive agreement is prohibited unless the agreement has been approved by court, received a temporary permit, by the Director-General of the Antitrust Authority or was granted an exemption.

In recent years, enforcement of this law has become more evident, in view of the expansion of the Antitrust Authority and the growing awareness of the advantages of competitive markets in Israel.

Block exemption: In 2000, the Director-General of the Antitrust Authority defined block exemptions that exempt specific agreements from the need for a permit. These block exemptions include R&D agreements, joint ventures, franchises, etc.

Amendment No. 14 limits the statutory exemption from prohibition of the restrictive arrangement specified in the Antitrust Law, with respect to the arrangement relating to wholesale produce and marketing of local agricultural products, such that the ability of wholesalers to make arrangements among themselves is restricted. The exemption will only apply to an arrangement whose restrictions concern wholesale produce as abovementioned, where all the parties concerned grow products included under the arrangement or they are one or more growers purchasing agricultural produce from the same grower or growers.

Mergers And Acquisitions

According to the Restrictive Business Practices Law, the following mergers and acquisitions require the approval of the Antitrust Authority prior to becoming effective:

- Subsequent to the merger or acquisition, the share of the merged parties in the production, sale, marketing, or purchase of a single product or a group of products or services will exceed 50%.
- Combined turnover of the merged companies (domestic turnover only) in the fiscal year prior to the merger exceeded NIS 150 million (approximately US$ 38.6 million), and at least two of the merged companies have a turnover of more than NIS 10 million (approximately US$ 2.57 million) each.
- In case that one of the parties is already a monopoly.
- Last amendment for 2012 prescribes the composition of the Mergers Exemptions Committee such that it will comprise of 5 women and 3 jurists.

Amendment No. 15 to the Law grants the Commissioner the authority to conduct tests on the level of competition in various sectors of the economy, including testing the existence of competition failures and obstructions. The Commissioner is also granted the authority to submit his conclusions and recommendations to the relevant minister where the subject being tested is within his area of responsibility, and also to the Minister of Finance, and in the sector where regulation according to law is under his responsibility. Additionally, the Commissioner may publish his conclusions on the Antitrust Authority's web site or in any other manner that he may consider appropriate.

Amendment No. 16 is in fact designed to deal with cartel problems and deficiencies in market competition, by extending the structural aid prescribed by law. Thus the Amendment enables a court to order the member of a cartel group or of a monopoly owner to sell assets, if this is necessary in order to prevent damage or fear of causing substantial damage to competition or to the public, and in relation to a cartel – if this is required in order to substantially increase competition, on the terms stipulated by law.

Amendment No. 17 refers to the changes introduced in the law subsequent to the amendment of the Standard Contract Law – 2010, dealing with examination of a standard contract.

INTERNATIONAL TRADE

Israel has extensive business relationships worldwide. The table below summarizes Israel's international trade in 2015 (excluding Diamonds).

	Import		Export	
	US$ million	%	US$ million	%
Grand Total	**55,178.7**	**100.0%**	**46,452.2**	**100.0%**
Europe	**27,308.9**	**49.5%**	**16,360.7**	**35.2%**
European Union	**20,876.3**	**37.8%**	**13,454.6**	**29%**
Italy	2,474.6	4.5%	802.1	1.7%
Belgium and Luxembourg	1,853.3	3%	660.8	1.4%
Germany	3,798.3	6.9%	1,389	3%
Netherlands	2,422.3	4.4%	2,152.9	4.6%
United Kingdom	2,239.2	4.1%	3,613	7.8%
Spain	1,342.8	2.4%	770.3	1.7%
France	1,593.6	2.9%	1,441.4	3.1%
Other European Union Countries	5,347.5	9.7%	2,647.3	5.7%
European Free Trade Association (E.F.T.A.)	**3,701.3**	**6.7%**	**318.6**	**0.7%**
Switzerland	3,552.2	6.4%	253.2	0.5%
Other European Countries	**2,731.3**	**4.9%**	**2,587.5**	**5.6%**

Source: Central Bureau of Statistics, Israel, Israel's Foreign Trade by Countries, January 2016.

	Import		Export	
	US$ million	%	US$ million	%
Turkey	2,444.6	4.4%	1,683.1	3.6%
Russian Federation	151.1	0.3%	649.3	1.4%
Other	16.5	0.0%	42.9	0.1%
Asia	**13,038.2**	**23.6%**	**11,322.9**	**24.4%**
India	915.4	1.7%	1,319.9	2.8%
Hong Kong	1,124.8	2%	559.4	1.2%
Taiwan	778.5	1.4%	529.7	1.1%
Japan	1,149.6	2.1%	724.9	1.6%
China	5,694.4	10.3%	3,110.7	6.7%
Singapore	682.4	1.2%	400.1	0.9%
South Korea	1,138.2	2.1%	570.5	1.2%
Thailand	504.8	0.9%	232	0.5%
Other Asian Countries	75.6	0.1%	63.9	0.1%
Africa	**268.5**	**0.5%**	**1,012.1**	**2.2%**
America	**8,590**	**15.6%**	**13,461.6**	**29%**
North America	**7,839.7**	**14.2%**	**11,977.8**	**25.8%**
USA	7,479.1	13.6%	11,040.1	23.8%
Mexico	111.5	0.2%	434.2	0.9%
Canada	249.1	0.5%	503.5	1.1%
Central America	**79.1**	**0.1%**	**211.1**	**0.5%**
South America	**671.2**	**1.2%**	**1,272.7**	**2.7%**
Oceania	**172**	**0.3%**	**559.9**	**1.2%**
Unclassified Countries	**5,801.1**	**10.5%**	**3,735**	**8%**

Source: Central Bureau of Statistics, Israel, Israel's Foreign Trade by Countries, January 2016.

The import of goods totaled $55 billion in 2015, compared with $46.4 billion in exports. Total trade deficits (excluding diamonds) totaled $8.6 billion, compared with $14.6 billion in 2014. 35.2% of goods exported (excluding diamonds) was directed to the EU countries, 23.8% to the U.S. and 24.4% to Asia.

Tourism to Israel

INCOMING TOURISTS	
Year	Thousands
2003	1,063
2004	1,506
2005	1,916
2006	1,834
2007	2,294
2008	3,034
2009	2,740
2010	3,450
2011	3,362
2012	3,520
2013	3,540
2014	3,251
2015	3,108

Source: Central Bureau of Statistics Israel, Arrivals and Departures of Israelis and visitors from abroad, 2015.

The incoming tourism in 2015 decreased by 4% in comparison with the previous year.

TRADE AGREEMENTS

Israel has entered into several trade agreements in order to strengthen its position in international markets. The most significant agreements are the Free Trade Area Agreement with the European Union, Free Trade Area Agreement (FTA) with the United States, Free Trade Area Agreement with the European Free Trade Association States (EFTA) and the Free Trade Agreement with MERCOSUR the South-American Common Market. The agreements with the European Union, the United States and South-American countries place Israel in the unique position of being a Free Trade Area partner with the principal economic regions worldwide. Thus, Israel is able to act as an intermediary for countries that do not have mutual agreements, provided that products comply with the provisions of each agreement. In addition, Israel has signed FTA Agreements with Canada and Turkey, a General Agreement on Tariffs and Trade (GATT) with the World Trade Organization, and has been granted preferences under the GSP (General System of Preferences) by Australia, Austria, Canada, Finland, Japan, New Zealand, Norway, Sweden, Switzerland, and the United States. As part of the peace process, Israel signed an Agreement for Economic Development with the Palestinian Authority.

Israel-European Union Free Trade Agreement

In 1995 Israel entered into an Agreement for the establishment of a free trade zone with the European Union for industrial products and some agricultural products.

Under this Agreement, most Israeli-made products are exempt from import duties. On its part, Israel gradually reduced import duties on European-made products.

In general, to be eligible for exemption from import duties, products are required to comply with certain "rules of origin". These rules require a minimum local-added-value depending on the origin of materials, manufacturing process, etc.

Tariff and non-tariff barriers still exist concerning agricultural products and processed foods in respect of international trade with the European Union.

Israel-USA Free Trade Area Agreement

In 1985, Israel and the United States entered into the Free Trade Area Agreement. This Agreement was fully implemented on January 1, 1995.

The Agreement eliminates all import duties and non-tariff barriers between Israel and the United States. The Agreement allows non-tariff restrictions on agricultural products.

"Rules of origin" exist, which are different from those of the European Agreement, to determine products' eligibility to benefits from this Agreement.

Israel-EFTA Free Trade Area Agreement

The Agreement between Israel and EFTA countries became effective on January 1, 1993. The Agreement is intended to eliminate or reduce duties, mainly on industrial goods, and also to reduce non-tariff barriers.

This Agreement has its own "rules of origin" as well, different from those of the above mentioned agreements.

Israel-MERCOSUR Free Trade Agreement

A free Trade Area Agreement between Israel and the Common Market of South America between Argentine Republic, the Federative Republic of Brazil, the Republic of Paraguay and the Oriental Republic of Uruguay (MERCOSUR).

The Agreement was signed on December 8, 2005 and went into effect on June 1st, 2010, Israel is the only non-South American country that has an FTA agreement with MERCOSUR, giving Israel a relative advantage in trade compared to other non-South American countries.

The "Rules of Origin" of MERCOSUR apply to this agreement; these are uniform rules for all South-American countries that are part of MERCOSUR.

Israel-Canada Free Trade Agreement

A Free Trade Area Agreement between Israel and Canada was signed in July 1996 and became effective on January 1, 1997. The Agreement expresses the parties' intention to gradually eliminate duties on industrial goods and some agricultural products.

The Agreement with Canada offers special advantages, since both parties have entered into FTA Agreements with the United States, enabling Israel to include United States origin components in its exports to Canada, and Canadian components in its exports to the United States, without breaching any "Rules of Origin".

Also Israel has Free Trade Zone Agreements with the following countries: Turkey, Czech Republic and Republic of Slovakia, Poland, Hungary, Mexico, Romania, Bulgaria, Jordan

PROPRIETARY RIGHTS

Israel is a member of international agreements regarding intellectual proprietary rights. The following section summarizes legislation regarding patents, trademarks, copyrights, etc.

Patents

The Patent Act, 1967, regulates the protection of patents in Israel. Regular patents are protected for 20 years from date of application, while "patents of addition" are protected for the unexpired terms of the main patent.

Patents may be granted on the invention of a product or process which is innovative, and which was never previously used or published.

Trademarks

The Trademarks Ordinance, 1972, and its provisions regulate the protection of trademarks in Israel. This protection is granted for an initial period of ten years, and may subsequently be renewed for further periods of fourteen years each, indefinitely. However, a third party may challenge trademarks that have not been used for three years or more, and may request their revocation.

Copyrights

The Israel Copyrights Law regulates the protection of original literary, musical, artistic, and dramatic works. The protection is granted for the lifetime of the creator plus 50 years for musical and artistic works, and 70 years for literary and dramatic works. Computer programs are protected under this law as well.

The 2014 Amendment provides the possibility of modifying a literary work so as to adapt it to disabled persons. Thus, reproduction of adapted works in compliance with the Law is applicable to a non-profit organization for disabled persons, and the organization may also deliver an adapted work to a disabled person or other organization in or outside Israel (subject to the restrictions prescribed in

Commercial Torts

The Commercial Torts Law 1999 is relatively new in the proprietary rights field, and still in its first years of exercise in Israel's business and legislative environment. The Commercial Torts Law incorporates several commercial torts, mainly exercised as common law by the Israeli courts up until their reversal into legislation, such as unfair interference to a business, passing-off, false description and etc. The innovativeness of the Commercial Torts Law applies especially in regards to the remedies enacted by it, for example the Anton Pillar court order.

INVESTMENT INCENTIVES AND TRADE ADVANTAGES

GENERAL // LAW FOR ENCOURAGMENT OF CAPITAL INVESTMENT // DEPRECIATION // ENCOURAGEMENT OF CAPITAL INVESTMENTS IN THE TOURIST INDUSTRY // INCENTIVES FOR BUILDING RENTAL HOUSING // OTHER INCENTIVE PROGRAMS // SPECIAL FREE ZONES // RESEARCH AND DEVELOPMENT // INTERNATIONAL COOPERATION

The State of Israel encourages investments from both Israeli and foreign residents, by offering a wide range of incentives and benefits. The principal goals include: efforts to attract foreign investments to Israel, boost economic growth, develop human resources, etc. To attain these goals, Israel offers substantial benefits and concessions through a number of laws and regulations, as summarized below.

GENERAL

Special emphasis is laid on high-tech companies and R&D activities, as considerable importance is attached to these fields. Furthermore, numerous programs have been formed, starting from the seed stage, to support the high-tech industry.

Israeli companies may also be eligible for benefits from international funds created as a result of cooperation agreements established between the Israeli and foreign governments, including the United States, Canada, the United Kingdom, the European Union, Singapore, South Korea etc.

Additionally, to promote weak economic regions within Israel, benefits are granted in a two differential manner (A and rest of Israel) - being substantially greater in the priority region (A) than in the rest of the country. As a rule, Zone A includes the following regions: the Galilee, Jordan Valley, the Negev and Jerusalem for high-tech enterprises. However, enterprises are eligible for benefits anywhere they are erected, provided they comply with the relevant criteria (see hereinafter).

LAW FOR ENCOURAGMENT OF CAPITAL INVESTMENT

Overview

The government's principal tool in this respect is the Law for the Encouragement of Capital Investment-1959 (hereinafter: "the Law"). As part of the Supplement to Economics Arrangement Law (enacted in conjunction with the 2011 - 2012 budget) (hereinafter: "the 2011 Amendment") recently ratified, significant changes were introduced in the application of the Law. The new tax benefits track will apply to income generated from January 1, 2011 onward. (For details of the previous law's provisions - see "Doing Business In Israel 2010"). It should be mentioned that in 2013 the law was amended again (hereinafter: "2013 Amendment") and the tax rates were changed.

The Law offers business enterprise promoters two types of tax breaks, under the tax benefits tracks or grants track (applicable in Zone A only). It should be noted that the 2011 Amendment prescribes that enterprises may enjoy both tracks simultaneously (in contrast to the previous law, whereby a company could not benefit from both courses at the same time).

Under the tax benefits track, an enterprise which qualified for this was granted a "beneficiary plant" status under the previous "preferable plant" law, while under the new law and grants track, such enterprise is given the status of "approved plant".

The Law applies to industrial enterprises (in diverse branches such as: textiles, food, electronics, chemicals, pharmaceuticals, computer software, biotechnology, nanotechnology, renewal energies, R&D etc.), hotels and other tourism ventures[1], industrial and residential construction, etc. (hereinafter collectively referred to as "Enterprises").

Based on a broad view of the Israeli labor force, R&D potential and the desire to maintain professional and advanced workers within its borders, the Law also applies to industrial development centers located in the country. These R&D centers can enjoy the full benefits granted by the Law, although they may not necessarily comply with the generally accepted definition of "industry". Industrial R&D services rendered to a foreign resident will be recognized as industrial activity if approved by the Head of Industrial R&D Administration.

It should be noted that a key condition for enjoying the benefits is compliance with an export rate of at least 25% of the industrial enterprise's turnover as outlined below.

Tax Benefits Track

In the framework of the 2011 Amendment, all the existing tax benefits were canceled and a unified tax rate introduced on the aggregate revenue generated from manufacturing activity, for industrial enterprises complying with the minimum export conditions established.

The tax rates to be applied, pursuant to the 2013 Amendment, are 9% in Priority Region A and 16% in all other areas (for the 2014 fiscal year; 10% and 15% respectively for the 2011-2012 fiscal years; and 7% and 12.5% respectively for the 2013 fiscal year). The rate for individual recipients of dividends under the tax benefits track will be 15%, both for Israeli as well as foreign residents, while intra-corporate dividend distributions (between Israeli companies) will be exempt from tax even if derived from the subsidiary's "preferable income".

Conditions for Enjoying the Tax Benefits Program

An enterprise wishing to enjoy these benefits is not required to apply to the tax authorities, but may independently implement them in its income tax returns.
The terms stipulated by law for obtaining tax concessions are as follows:

1. The enterprise must be owned by a company registered in Israel and the business of which is controlled and managed in Israel, apart from a

[1] Hotel and other tourism ventures remain under the previous law orders.

"family company", a "transparent company" or a Kibbutz. The law will also apply to registered partnerships, provided the partners have all been incorporated in Israel. Factories and quarries for producing natural resources (minerals, gas and oil) are excluded from the definition of "industrial enterprises" in regard to this particular activity. Companies fully owned by the government will not be entitled to the benefits granted under the law. The company must maintain admissible books and records and file any reports required under Israeli law. The company and its officers must be free of previous convictions on tax-fraud charges during the 10 years proceeding the benefits periods.

2. The enterprise must have an industrial plant.
3. The enterprise is competitive and contributes to the Gross Local Production. An enterprise will be deemed to have fulfilled this condition if it is engaged in biotechnology, nano-technology or renewal energies R&D and has obtained the approval of the Head of Industrial R&D Administration.
   Alternatively, an enterprise will be deemed to have fulfilled this condition if exports amount to 25% at least of its turnover in case of a new plant or expansion of an existing one, unlike the previous law, whereby the minimum requirement for expanding a plant was a measurement of the increase turnover as compared to the basic revenue. An enterprise with "indirect exports" may, under certain conditions, also be deemed to have fulfilled this condition. Only income from operations in Israel will be considered as "preferable income".
   As mentioned earlier, the tax benefit track does not require prior approval from the authorities. Notwithstanding the aforesaid, in order to provide greater certainty, an enterprise choosing the tax benefits program may apply to the tax authority for an advanced (or pre) ruling whereby the company complies with the terms stipulated by law, and also for regulating other issues involved in the application of the law.
   Under the new law, a particular tax benefits track exists for "special industrial enterprises" (applicable to large companies and/or investments), setting the applicable tax rates at 5% in Priority Area A and 8% in all other areas, for a period not exceeding 10 years.

Transitional Orders:

- The previous law is applicable to enterprises whose investments started before 31/12/2010 and they notified the authorities that the "elected" year for the benefit period would be no later than 2012.
- The previous law will also apply to old programs, based on the benefits prescribed by law in the "elected" year or on the date of granting approval, as the case may be.
- Notwithstanding the foregoing, enterprises wishing to apply the new law may do so while at the same time relinquishing the remaining benefits available under the previous one. Accordingly, a company eligible for tax breaks under the alternative track offered by the previous law, may apply the new law by notifying the authorities no later than the date specified for filing the annual report, and this shall apply to the fiscal year following the one for which the report had been filed. From the above, it emerges that an enterprise may pursue the new tax track from 2011, provided the authorities are notified accordingly in the context of the 2010 fiscal report.

Grants Program - General

- Pursuant to the 2011 Amendment, the stipulation prohibiting multiple benefits (tax track and grants track) has been withdrawn. As such, industrial enterprises complying with the required export conditions may benefit simultaneously from both the grants as well as the tax benefits track, as discussed earlier. Notwithstanding the above, should export conditions apply to revenue deemed as an "expansion" of previous activity, the enterprise may still benefit from the grants track even though the tax benefits will not apply. Eligibility for investment grants will be limited only to industrial enterprises located in Priority Area A. The grants program is limited to the budget framework approved annually for this track under the budget law.

- Approved enterprises are entitled to grants of up to 20% of tangible fixed assets. Nevertheless, the 2011 Amendment framework prescribes that approval of the grants will not be limited solely to investments in fixed assets but will also include investments in human resources and other ventures, provided these are in line with the defined targets. Furthermore, the Investment Center Management will be authorized to grant State-guaranteed loans.

The Main Conditions

The government provides grants as participation in financing the purchase of tangible fixed assets. The grants vary - depending on the type of enterprise and the National Priority Region.
The amount of the grant is calculated as a percentage of the original cost of land development and investment in buildings, machinery, and equipment. Machinery and equipment must be new, or used imported machinery and equipment not previously applied in Israel, provided the Investment Center Board had approved them.
Their cost includes installation and related expenses. For self-constructed or self-created assets, a determined reasonable profit, at a rate fixed by law, may be added to the costs incurred.
The investment program should be completed within 5 years from date of approval.
The grants are not deemed to be income but are deducted from the cost of the fixed assets.

The terms stipulated by law for obtaining a grant are as follows:

1. The enterprise must be an industrial plant or a hotel.
2. The enterprise contributes to the independence of the State's economy.

3. The enterprise is competitive and contributes to the Gross Local Production. An enterprise will be deemed to have fulfilled this condition if it is engaged in the fields of biotechnology or nano-technology and has obtained the approval of the Head of Industrial R&D Administration to this effect. Alternatively, an enterprise will be deemed to at least have fulfilled this condition if exports amount to 25% of its turnover. Where a plant has been expanded, an enterprise will be deemed to have fulfilled this condition if its exports amount to at least 25% of the increased turnover as compared to the basic revenue. Nevertheless, an enterprise wishing to enjoy the tax track at the same time required to export 25% of its turnover.
   An enterprise with "indirect exports" may, under certain terms, also be deemed to have fulfilled this condition.

We must note, that under the grants program, the enterprise is required to fund 24% of the scope of approved investment in equity.

Approval Procedure

As aforementioned, the law includes two principal schemes for obtaining tax concessions: one is the grants program, and the other, is the benefits program. To obtain the status of “Approved Enterprise” under the grants program, a company is required to submit a plan to the Investments Center.

The Investment Center Management is authorized to approve applications received during the relevant budget year in the context of the current or the previous year's budget.

Lately, pursuant to the comprehensive amendment of the Law, the terms for obtaining concessions were stipulated both in respect of grants as well as tax benefits. Consequently, the procedures for granting the status of "approved enterprise" differ. Whereas an enterprise applying for grants will be required to submit a plan to the Investments Center, this will not be required of an enterprise wishing to benefit from tax concessions under the status of "preferable enterprise". If the enterprise complies with the threshold conditions stipulated by law, it could enjoy these tax benefits and claim them under the income tax returns it files.

The determination by either the Investment Center or the Tax Authorities as to whether an enterprise is an "industrial enterprise" is binding upon both bodies for a 5-year period, unless substantial changes are introduced or erroneous reporting has been discovered in the enterprise.

Determining Priority Regions A and other areas

In accordance with the provisions of the Law for the Encouragement of Capital Investments, development regions will be determined according to a number of criteria. These comprise a combination of the following factors: geographic location (priority given to Jerusalem, the South and North, Sderoth and the Gaza Envelope), socio-economic level, unemployment rate, location within Israel’s industrial sectors or in the minorities settlements (settlements where 80% of the residents are non-Jews).

For a detailed review of the above - see Ministry of

Economy website: http://www.tamas.gov.il/CmsTamat/Ishuvim.aspx

DEPRECIATION

The regular Depreciation rate determined in the income tax (Depreciation) regulation-1941 ("Depreciation Regulation"). Under the Depreciation Regulation, the main depreciation rates are as follows:

Assset	Depreciation rate
Equipment and machinery (general)	7%
Electricity plant (equipment)	7%
Buildings	2%-4%
Computers	25%-33%
Electronic and Computing equipment	15%
Vehicles	15%

Accelerated Depreciation

Approved beneficiary and preferable enterprises are eligible for accelerated depreciation on tangible assets, reaching 400% of standard depreciation rates on buildings (not exceeding 20% per annum and exclusive of land), and 200% on equipment. The tax authorities may allow increased rates of up to 250%, if there is evidence of a high depreciation rate of equipment. This benefit is available for a 5-year period from date of commencement of operation rather than from purchase date of asset, and implementation thereof depends on the type of each particular asset as well as various rules.

Furthermore, special provisions were enacted in the Law for the Encouragement of Industry (Taxes), 1969 to grant favored enterprises accelerated depreciation. The Income Tax (Inflationary Adjustments) (Depreciation Rates) Regulations-1986, provides special depreciation rates to industrial plants and hotels with regard to specific fixed assets. The regulations are valid despite of the annulment of the Income Tax (Inflationary Adjustments) Law. The terms "industrial plant" and "industrial company" are defined in the Law for the Encouragement of Industry (Taxes). An ''industrial company'' is defined as "a company resident in Israel deriving at least 90% of its income in a tax year from an ''industrial plant'' owned by it". An ''industrial plant'' is a term which applies to companies engaged primarily in production. The regulation offers 5% depreciation for buildings owned by industrial companies, which function as industrial plant.
Moreover regarding equipment, section 2 of the Regulations provides depreciation rates as follows:

Depreciation Rates	
If the equipment is used in 1 shift	20% (or-15%)
If the equipment is used in 2 shifts	30% (or-18%)
If the equipment is used in 3 shifts	40% (or-22%)

Alternately, a company may choose the Devalued Balance Method, in which the depreciation calculated as part of the devalued balance of the asset as for the beginning of the year:

Depreciation Rates - Devalued Balance Method	
If the equipment is used in 1 shifts	30% for 4 years and the rest at the fifth year.
If the equipment is used in 2 shifts	40% for 3 years and the rest at the forth year.
If the equipment is used in 3 shifts	50% for 2 years and the rest at the third year.

A taxpayer electing to use the declining balance method for a specific depreciable asset is bound by the election for the entire period during which the asset is in use.
It should be noted that the accelerated depreciation mentioned above depends on classifying the plant as an "Industrial Plant" and the company as an "Industrial Company".

Allowing Investments in R&D Company's Shares as a Tax Deduction

Since 2016, the Israeli legislator announced a new and more simplified route for the tax deduction. This route's scope is subject to many conditions and to the Chief Science Officer's (CSO) approval.

Individuals

An amount paid out by an individual or his relative for investing in a "special purpose company", in consideration of which company shares of up to NIS 5M were allotted to him, will be deductible against the individual's overall income in three equal annual installments (or even less), as from the fiscal year in which the capital had been invested. Amongst others, the requirement is that the capital invested ought to have been paid between 1.1.2011 and 31.12.2019, and that most of it is applied by the special purpose company to cover R&D expenses incurred in Israel. The individual is required to hold shares of a special purpose company throughout the reduction period. The Chief Scientists' approval is required for the scope of R&D expenses. The law stipulates further conditions for allowing the said deduction.

Companies

A "preferred company" or "beneficiary company" as defined in the Law for the Encouragement of Capital Investments, will be entitled to deduct the cost of shares acquired during the period between 1.1.2011 and 31.12.2019 in an "entitling company" not related to it, to the extent of 20% per annum from the year after such acquisition. It should be noted that the entitling company's equity capital will be deducted from the acquisition cost.
The law specifies a number of conditions for applying the deduction, inter alia that the investment involve the acquisition of at least 80% of the means of control (other than by way of allotment) in the entitling company; that in the year of acquisition and in each of the bonus years, the acquiring company and entitling company be a beneficiary or preferred company; a minimum number of academic employees is required in the field of engineering, computers, natural or exact

sciences and a minimum amount of R&D expenses must be incurred during the acquisition year and in each of the acquisition years both by the acquiring as well as the entitling company. For purposes of the deduction, approval must be obtained from the tax authorities that the purpose of the investment is neither the avoidance of tax nor reduction of the tax liability. The law stipulates further conditions for the tax reduction.

ENCOURAGEMENT OF CAPITAL INVESTMENTS IN THE TOURIST INDUSTRY

It should be noted that the previous law benefits (both in the tax benefit track as well as the grants track) are relevant for hotels, accommodation facilities and other tourist attractions.

It should be noted that since Amendment 60 to the Law (from 2005), only accommodation facilities meeting the "foreign residents accommodation" conditions are eligible for benefits under the Law. As a rule and in order to comply with the above, at least 25% of overnight stays in an accommodation facility must be overnight stays by foreign residents. This condition does not apply to tourist attractions.

According to law, benefits may be claimed on the construction or expansion of a "tourist facility for overnight stay". The legislator gave a distinction for the meaning of the term "tourist facility for overnight stay", stipulating that such a facility must be:

"A structure comprising 11 or more rooms, providing overnight services to guests passing by and for fixed periods of time, together with accompanying services including catering, entertainment and leisure services".

From the above, it emerges that a wide range of overnight accommodation services and other facilities are eligible for the benefits provided under the Law. Thus, one may easily determine that hotels, motels, guest houses and even hostels are eligible for such benefits, provided they fulfill the condition of the number of rooms stipulated by law.

We should also mention that the map for priority regions applicable to tourist facilities differs from the map for priority regions applicable to the industrial sector. Thus, and in regard to hotels, it was determined that Development Region A includes, inter alia, the Western and Upper Galilee, around Lake Kinneret, Nazareth, Haifa, along the Carmel Shore, Netanya, Ramle, Jerusalem and Jerusalem Corridor, and the Southern Region excluding Eilat and the Dead Sea.

Investment Grants

An entrepreneur wishing to establish an 'overnight tourist facility' is entitled to an investment grant and a capital grant, which vary according to the facility's location. Investment grants vary from 10% - 24% of the entrepreneur's investment expenses, less land costs. The investment grant is not automatically offered;

the entrepreneur must submit a detailed preliminary application to the Investment Center Management at the Ministry of Tourism. Based on established criteria, the application should address the various aspects to be considered by the Ministry (planning, minimum accommodation standards, etc.). In order to obtain the grant, the Ministry must issue a "letter of approval" for the plan. It should also be noted that the entrepreneur must submit the plan prior to proceeding with the actual investment, as grants are not approved "retroactively" on capital already invested.

In addition to the said grants, the regulations prescribe a number of tax benefits for approved tourist facilities, the principal one of which, in our opinion, is accelerated depreciation on an investment in a tourist facility structure.

Tax Benefits Track for Overnight Tourist Facilities

As mentioned earlier, the tax track applies only to "overnight tourist facilities" and not to tourist attractions. Furthermore, this track does not require the authorities' prior approval as it applies automatically, on compliance with the conditions prescribed by law. Legislation prescribes a number of conditions, beyond "foreign residents accommodation" which, on fulfillment thereof, entitle the owner of the facility to claim tax benefits.
The principal conditions for this are:

- The facility must be under the ownership of an Israeli company not fiscally "transparent" for tax purposes.
- To erect or expand the hotel, capital had been invested there in a minimum amount prescribed by law.

Under the tax benefits track, the owner of the facility is entitled to the following: a tax exemption on increase in turnover (deferring the tax until profit distribution) - currently 10 years exemption in priority Region A, 6 years in priority zone B and two years exemption in the rest of the country; accelerated depreciation and reduced tax rates (Tax at shareholders level due to receipt of dividends is generally 15%). Alternative track available in Priority region A, with a final 11.5% tax on undistributed profits at Company level on increase in turnover and (with no further taxation at the company level with profit distribution) tax at shareholders level due to receipt of dividends 15% to shareholder resident in Israel and 4% to shareholder resident abroad.

INCENTIVES FOR BUILDING RENTAL HOUSING

Building residential rental apartments is an essential social and economic goal, thus those who build and rent out apartments are eligible for diverse benefits and incentives offered through the tax system. Beyond the exemptions and benefits granted to individual property owners who rent out apartments, there are two parallel laws to encourage large-scale construction of rental housing.
The first and oldest law code is contained in Chapter Seven-1 of the Law for the Encouragement of Capital Investments. The second and relatively new law is the Law for the Encouragement of Rental Housing, enacted in 2007. In effect, after enacting the latter, two parallel systems of law were created to encourage the building of rental apartments, and an assessed may operate to apply one of them.
Pursuant to Chapter Seven-1, tax incentives are granted in regard to a building complying with the terms of the "Rental Building" designation, or the "New Rental Building" designation, which is usually one whole or several buildings located in one complex, and approved as such by the Investment Center Administration. It should be noted that there are entitlement conditions for actual tax benefits, including inter alia: the size of a minimum rented area, minimum rental periods, compliance with monthly rent limits, restrictions on the sale of part of a building for a specific period, etc.

The Law for the Encouragement of Rental Housing - 2007 is designed to increase the inventory of apartments available for rent. The Law grants benefits only to companies, by way of enabling accelerated depreciation and giving them a full exemption from Appreciation Tax. Unlike Chapter Seven-1, this concerns a track requiring no prior government approval. It is noteworthy that this Law, too, sets entitlement conditions for obtaining actual tax benefits, including inter alia: minimum number of apartments in a building, minimum rental fee, minimum rental period, restrictions on the sale of a building etc.
Below is a review of the scope of tax benefits available between these two legislative systems. (The review will address, with respect to Chapter Seven-1, the provisions applying to a "New Rental Building" only).

Rental Income - Reduced tax on income derived from the lease of a "new rental building" - at the rate of 11% for companies and 20% for individuals. Companies are liable to a lower effective tax rate of 10% on foreign investments, where the foreign investment exceeds 90%.

Dividend - 20% tax (since 2014) is chargeable on dividends distributed from the earnings of an approved enterprise which is a rental apartment building.

Total "direct to house" tax under Chapter Seven-1 is 28.8%.

Income from the Sale of a Building (Appreciation Tax) - This is liable to tax at the rates mentioned above. We must emphasize that these tax rates apply to betterment accumulated for the entire period and not merely from the effective date (November 7, 2001). It is also noteworthy that Section 72A of the Property Taxation Law denies such exemption for residential apartments, relevant only to individuals, in the sale of apartments in a rental building eligible for benefits under the Law.

Purchase Tax - There is a reduced purchase tax of 0.5%, where the Investments Center demands the transfer of title to a property which is a building or plot constituting a business inventory or fixed asset for a company held by the same owners, for purposes of a "rental building", with certain restrictions.

Accelerated Depreciation - at the rate of 20%.

V.A.T. Benefit on the Sale of a Building - Section 31(a) of the V.A.T. Law stipulates a tax exemption on the sale of such part of a building used for rent and having enjoyed the said tax benefits. The Section stipulates that if that part approved as a rental building had been rented for five years at least, the sale thereof would be exempt from V.A.T.

VA.T. on Apartment Rental - The exemption specified in Section 31(1) of the V.A.T. Law shall apply in regard to rental housing for a period not exceeding 25 years.

OTHER INCENTIVE PROGRAMS

Small Business Loan Fund

The Small Business Authority of Israel was established in 1993, to fill the need for a policy-making organization to encourage small businesses, entrepreneurs, etc. The Authority's major roles include initiation and application of government policies for encouraging small businesses, setting up local, regional, and professional centers to assist them, and initiating the establishment of capital funds and other financial resources for small businesses, etc.

Among its other roles, the fund helps to establish or expand small businesses, while the government provides bank guarantees to serve as collateral for commercial loans. The loan extended to a single business is for approximately NIS 500,000, for a five-year period, to fund the purchase of equipment or one year's working capital. The borrower is required to furnish the bank with a lien on the equipment financed by the loan, as well as personal guarantees. To be eligible for the loan, the business must meet certain criteria, as follows:

- The annual turnover must not exceed NIS 100,000,000.
- The loan should be used solely for new activities: establishing a new business or expanding an existing one. The funds should not be used for the purchase real estate, construction activities, or the acquisition of an existing business.
- Paid-in capital should not be 10-25% of the loan.

The fund is currently managed by three commercial banks. The State guarantees up to 70% of each loan amount and up to 30% of the entire loan portfolio.

State-Guaranteed Loans Offered to Medium-Sized Businesses

The Fund for Establishing and Supporting the Operation of Medium-Sized Businesses operated by the Ministry of Economy, offers State-guaranteed loans of up to 8% of an entity's annual turnover. The program is intended for medium-sized businesses with an annual sales turnover of NIS 22-100 m. The scope of collateral security required is 25%, while the Government extends a guarantee of up to 70% of the loan amount. Furthermore, the owners' personal guarantee is required.

The loan is for a term of up to five years, with a one-year extended grace period for repayment of the principal. Interest is at the customary rate prevailing in the banking system on such loans. The Fund is operated by commercial banks.

Assistance to industrial plants in financial difficulties

Pursuant to a government resolution, a committee of Ministry Director-Generals was formed to review industrial plants and submit recommendations to a ministerial team.

Government assistance is conditional on an independent investment in the plant, or a recovery plan including additional funding from the owners.

An external examiner appointed by the Committee reviews applicant plants and their compliance with specific criteria, including:

- A recovery plan, its economic feasibility, the financial justification of the plant's existence for the long term, and the ability to introduce recovery measures within a specific period of time.
- The lateral implications.
- The number of employees and minimum employment period.
- The scope of assistance required.
- The participation of other entities, including the owners.
- The ability to reduce the number of employees according to the recovery plan.
- Funding must not exceed NIS 10 million, and will deprive the plant's eligibility for further government assistance. Should the plant, however, apply for other financial assistance from a government entity, the plant must repay the loan.
- The salaries of managers and employees must not exceed NIS 50,000.

If the applicant plant meets the above criteria, it will be eligible for a government loan. The amount is determined by the Committee, while its terms are specified by the Accountant General at the Ministry of Finance, in the event of additional funding from banks. Repayment terms are equivalent to those stipulated by these banks.
The owners are required to guarantee the loan.

Business Tutorage

The Minister of Economy focuses on assisting small and medium sized businesses by appointing "tutors" to cater to the specific requirements of each business (e.g. general management, financial management, production management, marketing, information systems, human resources, etc.).

Eligible businesses are tutored by independent consultants, whose fees are paid by the Ministry (75%) and the business (25%) within an agreed time frame, based on the latter's needs and the Ministry's policy and budget.

Medium sized businesses (11 - 100 employees) are entitled to up to 150 hours of tutorship; small businesses (5 - 10 employees) are entitled to up to 100 hours; very small businesses (up to 4 employees) are entitled to 20 hours only.

In addition, very small business managers may participate in special courses, in the framework of Small Business Development Centers, designed to develop their managerial skills.
The Ministry of Agriculture allocates funds for "tutorage" of agricultural businesses.

Employment Grant Program

In order complement to the revised Law for the Encouragement of Capital Investments, the government has decided to establish an additional program to increase employment in remote areas of Israel, as well as specific centers with high unemployment.

Support will be provided for the establishment or expansion of industrial plants, telephone call centers, computer service support centers or logistic centers. In order to qualify for such program, these enterprises will be required to employ a minimum number of workers at a minimum wage, as detailed below.

In order to be granted support from this program, companies are required to compete, and will be invited to submit proposals twice a year. The maximum amount of support offered is as follows:

All areas: 15% of the cost of average monthly wage for additional employees, but no more than NIS 120,000 per employee for the entire period.
Minority and Ultra-Orthodox towns - as above.
Enterprises paying wages below NIS 6,750 will be entitled to more than NIS 60,000.
Despite the above, the total average support granted to each enterprise will not exceed NIS 100,000 per employee.

The eligible areas are: Priority Development Areas "A" and "B"; and designated towns for the minority population (Arab, Druze, Circassian) or the Ultra-Orthodox Jewish population.
The enterprise must pay its employees the following minimum wages at least:

- Minority and Ultra-Orthodox towns - the minimum wages.
- In all other eligible areas - NIS 6,750 NIS monthly wage.

Enterprises should hire a minimum number of employees, depending on the region and the track (new plant or expansion).

Intra-Plant Training

The Ministry of Labor and Social Affairs assists companies (mainly manufacturers) in providing in-house training for unemployed people and undertaking to employ them. Training is provided either "on the job" for unskilled workers or those who have completed vocational courses but lack experience.

Quality Management Project

The project caters to industrial enterprises employing 50 to 500 people, for the introduction of modern management techniques. The grant covers 50% of consulting fees, up to 400 hours. The fee must be used within a period of 6 to 12 months.

"Preparation for Exposure" Fund

The fund is designed to help industrial enterprises gear up for competition due to exposure, and assists them in increasing imports and reducing customs and import

duties. Grants may reach the equivalent of US$ 500,000 and government guarantees are available as well.

Approved Foreign Expert

A foreign resident approved by the Investment Center as a foreign expert, is liable to Israeli income tax at a rate of up to 25% during the first three years of employment. This period may be extended by an additional year. The reduced tax rate is applicable to a salary of up to US$ 75,000 per annum, plus social benefits.

Capital Intensive Companies

Under the Law for Encouragement of Capital Investments, Israeli and foreign entities wholly-owned by foreign investors, whose paid-in capital exceeds US$ 30 million, of which 75% at least is applied for "qualifying activities", are entitled to the special status of a “capital- intensive” company. The Income Tax Commissioner is authorized to amend the rules for attaining this status. Capital-intensive companies are entitled to a series of tax benefits over a 30- year period, including:

- 25% corporate tax.
- 15% withholding tax on dividends.
- Corporate tax refunds in the event of distribution of dividends. In this case, the withholding tax on dividends will be 25%.
- Tax exemption from sale of shares.

Finance Ministry approval is required for this status. An approved capital-intensive company may also be an Approved Enterprise.

SPECIAL FREE ZONES

Eilat Free Trade Zone

Eilat and its surrounding area were declared to be a free trade zone. The major benefits are as follows:

- Companies providing services and/or resident in Eilat are exempt from value-added-tax.
- Employers are reimbursed for part of labor costs paid in Eilat.
- Providers of advisory services to hotels in Eilat are exempt from value-added-tax.

Free Port Zones

The ports of Haifa, Ashdod, and Eilat contain areas declared as free port zones. Companies (only) located in the free port zones are eligible for benefits, granted in addition to any other benefit to which these companies are entitled under other encouragement laws. These additional benefits include:

- Lower corporate tax rates (in Eilat).
- Lower withholding tax on dividends (in Eilat).
- Exemption from property tax.
- Unrestricted use of foreign currency.

At present, the legislation in respect of free port zones has not been enacted.

Free Processing Zones

In June 1994, the Free Processing Zone Law was enacted but its amendment in the near future is almost certain.

The first zone under this law is currently in the planning stages and will be located near Beer Sheva, in the

Negev. Free processing zones may be developed by private concessionaires only, in compliance with a number of financial and organizational restrictions. Some of the benefits to the concessionaires and enterprises operating in such zones are as follows:

- Companies are fully exempt from any direct tax for up to 20 years. Other entities are subject to direct tax of 15%.
- Withholding tax on dividends will not exceed 15%.
- Full exemption from municipal taxes (including betterment tax) and any indirect taxes (except for passenger vehicles).
- Capital gains on sale of shares are taxable at a rate of up to 15% unless reinvested within six months, in which case, they are fully exempt from capital gains tax.
- There are no custom duties or import restrictions (except in respect of health and environmental regulations, etc.)
- No foreign currency control will be imposed.

RESEARCH AND DEVELOPMENT

Numerous research and development programs provide a wide range of incentives to companies engaged in R&D activities.

Chief Scientist's Office

The Government of Israel provides cash grants, usually up to 50% of approved R&D expenses. Approval of R&D programs and actual expenses are under the responsibility of the Chief Scientist's Office at the Ministry of Economy.

The Research Committee is entitled to approve a participation grant of 20, 30, 40, or 50% of total R&D expenses and if located in National Priority Regions they are entitled to a 10% grant. Start-ups may receive certain alleviations.

There are several incentive plans under the sponsorship of the Chief Scientist's Office. Among these one may find:

- Regular grant programs, offering up to 50% of R&D expenses. The eligible program should be for know-how, processing and/or manufacturing procedures, the manufacture of new products or a significant improvement on an existing process or product.

- **Magnet -** This program, intended for generic R&D technologies, encourages the formation of a consortia of industry and academic institutions to develop key technological infrastructures. Magnet also supports the integration of advanced technologies into industry through user associations. Grants of 66% of total approved R&D costs for industrial entities, and up to 80% of approved costs for academic institutions are available, with no royalty requirements.
- **Magneton -** This program is similar to the Magnet; however, it encourages cooperation between a single academic institution and an industrial plant. The available grant is up to 66% of the approved research budget.

- **Nofar -** This program is designed to support applied academic research in biotechnology, and to promote the transfer of technology to industry. Grants are available up to 90% of the approved research budget.

- **Kamin -** This program is design to support applied academic research which is not yet ready for business involvement. The activity is done in the academic research institute's labs, and the rest of the budget is financed by the institute. The grant is limited to up to 85%-90% of the approved budget.

Expenses are approved on an itemized basis, while salaries and wages are limited, particularly those of interested parties. A set of rules determines the nature and amount of each approved expense. Unapproved expenses are not entitled to grants.

If the R&D program is successful, royalties are payable to the Chief Scientist's Office. These usually range between 3% and 5% of the sale of products developed using government aid, and are paid till full repayment of the grant, linked to the Libor + 1%.

If production is relocated overseas, the Chief Scientist's prior consent is required, while 120%-300% of the grant must be repaid respectively, according to the production percentage being relocated. Additionally, the amount of royalties will increase.

In case of selling technology or know-how outside Israel for projects sponsored by the Chief Scientist, or any other right derived from such technology for enterprises outside Israel, payment will amount to a portion of the remuneration for such know-how, set at a ratio of the total grant out of the overall investments in the project. However, the payment will not be less than the amount of grants provided to the company, and up to 300% of the total grant received if, R&D activity stays in Israel but no less than 75% of salaries paid through 3 months prior to the sale of the supported technology or know-how, and up to 600% of the grant received if R&D is discontinued in Israel.

Aid to Individual Technology Entrepreneurs

- **TNUFA-** The Israel Idea Promotion Center is a non-profit Israeli, government-supported organization, dedicated to helping individual entrepreneurs successfully commercialize their new product ideas by providing seed money grants of 85% or up to NIS200,000 in addition to free legal, marketing and business-management consultations. Most of TNUFA's budget is based on royalties from successful projects.

- **The Ministry of Absorption** also provides financial aid to immigrant entrepreneurs.

Technological Incubators

Technological incubators provide a supportive framework enabling entrepreneurs with innovations -

veteran Israelis and immigrants alike - to develop their ideas into a commercial product, and reach the point at which they can attract capital investments from the private business sector. R&D activities conducted in technological incubators are entitled to grants of up to 85% of the approved program or 100% in peripheral incubators. The grant is limited to NIS 2.1 million for a two-year period.

Biotechnological Incubators

Biotechnological incubators are aimed at supporting this type of research, given the specific nature and needs of this sector. In line with the current tendency for privatization, the private sector, in the form of franchisees, plays a key role in the project.

The government's participation in such projects is through a convertible bond, while the incubators are actually managed by the franchisees.

The franchisee obtains, for each project, a government loan of up to 85% of the approved budget in the 1st year, up to 80% in the 2nd year and up to 75% in the 3rd year. The approved budget for up to 3 years shall not exceed NIS 8,100,000. The franchisee is responsible for raising supplementary funding to cover the rest of the approved budget.

For each incubator project, the franchisee negotiates with the entrepreneur the percentage of control in the company running the project.

The franchisee provides a physical plant with adequate infrastructure for biotechnological R&D, administrative staff and accessibility to consulting services. In return for covering the operating costs of the biotechnological incubator, the franchisee receives up to 5% of the shares of each company accepted by the incubator.

INTERNATIONAL COOPERATION

The Israeli government has entered into a number of R&D cooperation agreements with foreign governments and the European Union, to foster ties between Israeli and overseas companies designed to facilitate joint ventures in the R&D, manufacturing and marketing fields. Such agreements exist with the United States, Canada, the European Union countries, and Asia.

Eureka

Eureka is a Europe-wide network for industrial R&D, uniting 40 countries by promoting 'market-driven' collaborative R&D projects in most fields of advanced civilian technology. An agreement signed in 1993 with the European Eureka Secretariat allows Israeli companies to join this prestigious program.

Bi-National Funds

BIRD-F - The Israel-U.S. Bi-national Industrial Research and Development Foundation (BIRD-F) assists R&D programs involving non-defense products and processes jointly implemented by Israeli and United States companies.

BIRD-F finances 50% of R&D projects.

As in the case of government programs, the grants, if successful, are repayable as royalties up to 150% maximum of the amount of the grant.

CIIRDF - The Canada - Israel Industry and Research Development Foundation was founded at the end of 1994 and is similar to BIRD-F. CIIRDF funds 50% of joint Canadian- Israeli projects encompassing several Canadian provinces.

SIIRD - The joint Israel-Singapore Fund began operating in 1997. At the initial stage, each country deposited into the fund annually US$2 million for grants, with the aim of increasing the capital over time. SIIRD finances bi-national R&D projects up to 50% of R&D expenses or US$ 750 thousand, and is similar in composition and activities to BIRD-F and CIIRDF.

KORIL - RDF - The Israel-Korea Fund was jointly initiated by the Chief Scientist and MOCIE (Korean Ministry of Industry and Commerce). The fund is a Korean non-profit organization run by representatives from both countries. Each country deposited US$ 1 million annually into the fund for the first three years of activity, to finance bi-national R&D projects. The fund finances R&D 3-year projects for a total of up to 50% of R&D expenses, or up to US$ 500 thousand, and is designated as a "conditional grant". If the project produces sales, the grant is repaid through royalty payments.

Other International Programs

U.S.-Israel Science and Technology Commission - The Commission was a joint initiative of the late Prime Minister Itzhak Rabin and United States President Bill Clinton, for further cooperation between Israel and the United States, and to add a new dimension to scientific and technological cooperation between Israeli and U.S. high-tech companies. The Commission has two objectives: funding long-term projects with substantial technological impact and removing any impediments - such as FDA regulations.

BSF - Israel-U.S. Bi-National Science Foundation provides assistance to scientists and start-up programs. The grants are intended to support 18 months of a two-year research program, with the objective of providing seed money to young independent scientists.

Bi-National R&D Agreements - Promotes R&D cooperation between Israeli and foreign companies, while each company is assisted by its home country. These agreements were signed with 28 countries.

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