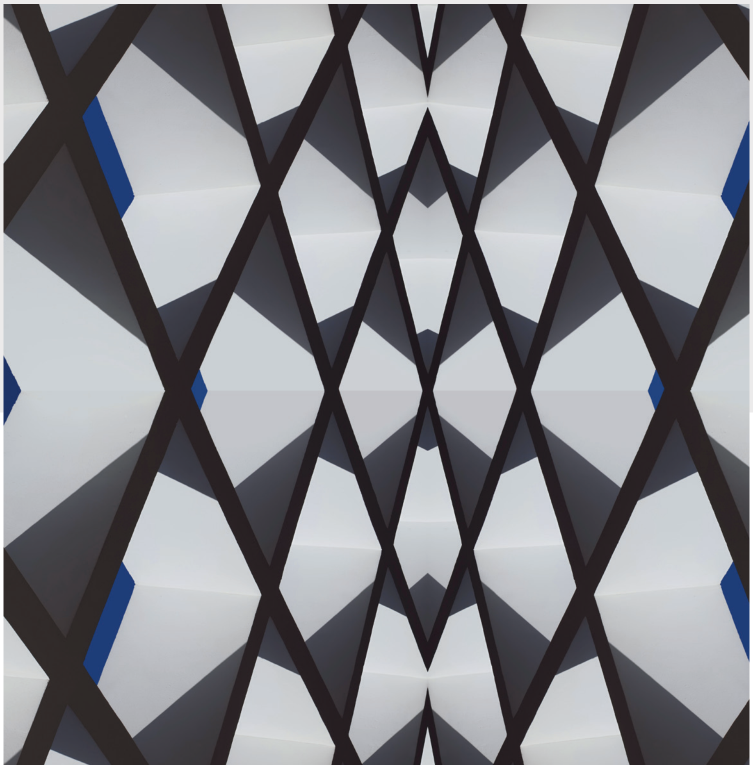
# Doing Business in Israel



## DEAR FRIENDS,

**It is our pleasure to present "Doing Business in Israel 2018", a comprehensive guide for anyone wishing to engage in the Israeli market.**

Over the last two decades, the Israeli economy has been enjoying a remarkable macroeconomic and fiscal performance. Its GDP growth rate has averaged 4% annually since 2003, and has exceeded that of most other OECD countries.

Israel is currently experiencing strong growth. Its labor market continues to stabilize itself at high levels, and is in fact currently at full employment capacity. Private consumption continues to demonstrate strength due to low interest rates and ongoing improvements in the standard of living, driven by high employment rates and an increase in wages.

In recent years, the Israeli government's fiscal policy has been stable and responsible. In 2017, the budgetary deficit was 2% of GDP, and as a result, the ratio of Israel's government debt to GDP fell for the first time ever below 60%. Short term prospects are predicting an increasing robust growth rate, estimated at around 3.7% in 2018, and 3.6% in 2019. Israel's international position is solid, mainly thanks to the success of the high-tech sector.

The monetary policy of the Bank of Israel continues to be expansionary, with a low interest rate of 0.1%, due to the low inflationary environment. In the coming years, the inflation rate in Israel is expected to increase at a moderate rate. The low interest rates in Israel, in combination with the US Federal Reserve Bank's increase in interest rates, are expected to contribute to a weakening of the Shekel, relative to the effective "currency basket". The depreciation of the Shekel will further stimulate the economy, contributing to export profitability and increased investments.

Over the years, Israel has been facing periodic geopolitical and security related challenges. However, past experience clearly shows that the Israeli economy is able to sustain itself even through severe conflict situations.

We hope that this publication will serve as a valuable tool for business organizations and investors who wish to gain a wide view of the up-to-date information regarding critical aspects of the Israeli economy and its business environment. The information presented below touches on recent macroeconomic developments, socioeconomic and demographic trends, Israel's general business environment, accounting considerations, taxation and government tax incentives.

**Israel's economy has remained stable throughout 2017. Furthermore, encouraging prospects are on the horizon, emphasizing the fact that Israel remains an excellent place of business.**

Sincerely,

Dan Margalit
Chairman & CEO
BDO Israel

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## 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 investment decision, it is recommended to seek the advice of Israeli financial consultants in the relevant sectors. Our partners and associates at BDO Ziv Haft Israel provide reliable and professional services to all investors who are considering making investments 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 ministries in Israel.

BDO Ziv Haft Israel is the fifth largest international network. The firm has 1,400 offices in 154 countries worldwide, with a total of approximately 64,300 partners and professional staff.

The information presented in this document was updated in June 2018, based on data available at the time of printing. The publication is intended for information purposes only and does not in any way constitute a replacement or amendment of any of the laws and regulations mentioned herein. Although we have conducted extensive research to prepare this publication, we bear no liability with regards to any inaccuracies that may have been made.

# THE ISRAELI ECONOMY IN 2017

01

## FOREWORD

In 2017, Israel exhibited solid economic performance compared with most developed countries. While the average annual growth rate in developed countries stood at 2.4%, (due to uncertainties in the global context, against the backdrop of the geopolitical crisis), in 2017, Israel exhibited a rapid growth rate of 3.3%. This figure is unsurprising, as the Israeli economy has already proven its stability in the past.
Such was the case during the global financial crisis of 2008-2009, which spurred only a moderate recession in this country. This was thanks to a solid economic basis, a prudent fiscal policy and a resilient banking sector.
Israel's major exports are comprised of cut diamonds, high technology equipment, and pharmaceuticals, while imports include crude oil, grains, raw industrial materials for industry, and military equipment.

In 2017, the Gross Domestic Product in Israel grew at a rapid pace of 3.3% compared with 4% in the preceding year. Against this background, the rate of unemployment in Israel dropped between 2016 and 2017 from 4.8% to only 2.4%. This occurred as the result of the recruitment of employees in the private sector following large foreign investments. Furthermore, given that tax revenues were significantly higher than expected, along with a surplus in the National Insurance Institute and a lower than expected government spending, the deficit in 2017 totaled 2.2% of GDP, lower than the anticipated 2.9%. With respect to the upcoming year, and corresponding with the predicted improvements in global economic growth and trade, the pace in Israel is expected to remain the same. This is largely due to decline in the effect of self gas production and the strengthening of the Shekel, which is likely to make export more difficult. Furthermore, the monetary committee of the Bank of Israel has reduced the interest rate to its lowest rate ever (0.1%). This might make it difficult to weaken the Shekel in order to encourage export. According to the Bank of Israel's forecasts, economic growth in 2018 is expected to stand at 3.4%.

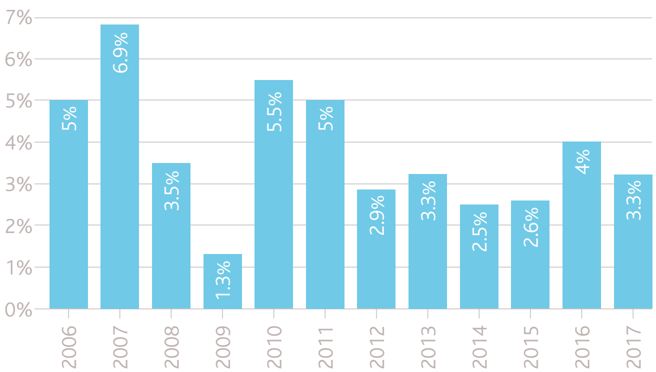
Below is a summary of the main economic indicators in Israel. This section includes a forecast of major economic developments based on several sources, including, among others, the Bank of Israel's Research Department, the Ministry of Finance, and a number of commercial banks.

# MACRO-ECONOMIC DEVELOPMENTS IN 2017

## Gross Domestic Product (GDP)

In 2017, the Israeli GDP increased by 3.3%, compared with a growth rate of 4% in 2016 and 2.6% in 2015.
Israel's population grew by 1.9% in 2017. The GDP per capita increased by 1.3%, compared with 1.9% in the previous year and 0.6% in 2015. By comparison, based on OECD data, the GDP per capita in OECD countries increased by 1.3% in 2016. In nominal values, GDP per capita in 2017 totaled 144.9 thousand ILS ($40.3 thousand).

Annual Growth Rate in Gross Domestic Product




Source: Central Bureau of Statistics Israel.

## Investments

Investments in fixed assets in the Israeli economy increased by 3.6% in 2017, after an increase of 13.9% in 2016. The total amount of investment in fixed assets in 2017 was 254 billion NIS, or 171 billion ILS, excluding residential construction. Investments in various fields of the economy (including the non-residential construction sector, machinery, equipment and vehicles, but excluding ships and aircraft) increased in 2017 by 4% compared with 2016, following a rapid increase of 12.9% from 2015 to 2016. Investments in residential housing increased by 1.2%  in 2017, and 8.2% in 2016.

## Employment

The number of employed population in 2017 rose by 2.4%, reaching 3.8 million people, compared with the corresponding period in 2016, while the average gross salary increased by 3.2%. The average monthly wage per employee in December 2017 amounted to ILS 10,376 ($2926).
According to data recorded by the Central Bureau of Statistics, unemployment in 2017 reached a rate of 4.2% of the civilian labor force.

## Fiscal Developments

In 2017, the current balance of payments account in the government sector showed a deficit of ILS 14.3 billion - compared with ILS 13.1 billion in 2016. In terms of GDP, this amount equals to a deficit of 1.1% in 2017, compared with 1% in 2016 - representing current income minus current expenditure for all public sector entities: the government, local authorities, national institutions and non-profit organizations, which obtain the majority of their funding from the government. The increase in the government's budget deficit in 2016 reflects a 4.4% increase in tax collection, compared to a more moderate rise of 4.2% in government spending.

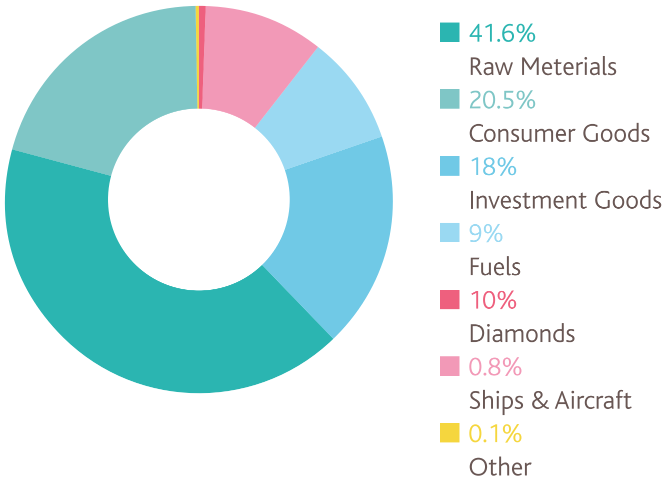
## Balance of Payments

The year of 2017 marked an increase of 6.4% in exported goods and services, after an increase of 3.2% in 2016. Industrial exports, excluding diamonds, decreased in 2016 by 1.6%, compared with 2015. Revenue from the export of tourist services rose by 3.4% in 2016, following a decrease of 1.2% in 2015. Export of services, excluding tourism and start-up companies, which primarily include software and research services, rose by 6.1 % in 2016, after a decrease of 2.4% in 2015. Diamond exports increased by 6.4%
Import of goods and services (excluding defense imports, ships, aircraft and diamonds), marked an increase of 8.2% this year, after an increase of 1.4% in 2015. Import of goods and services, including defense imports, ships, aircraft, and diamonds, rose by 9.5% after a decrease of 0.5% in 2015.

## Monetary Development and Capital Markets

The Consumer Price Index (CPI) decreased by 0.2% in 2016, compared with a decrease of 1% in 2015, and 0.2% in 2014.

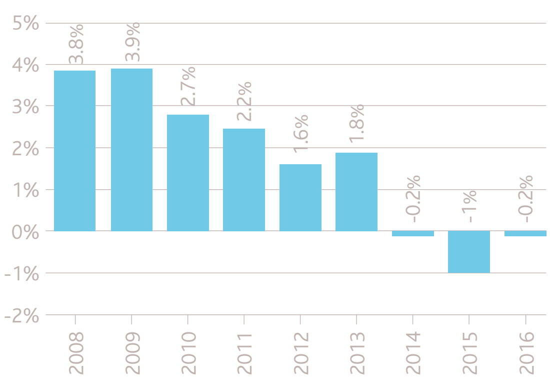
## Composition of Israel's international export in 2017:



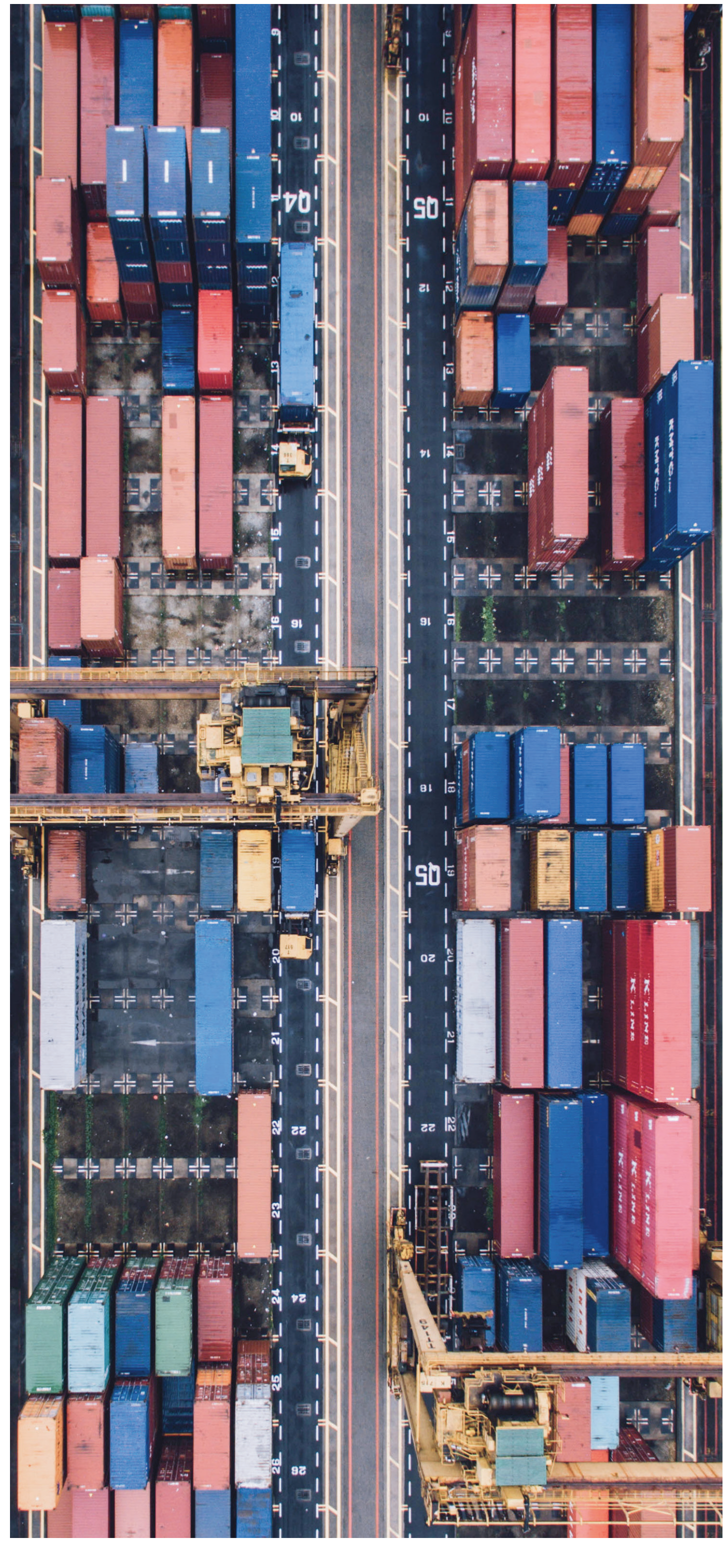

Source: CBS, 2017

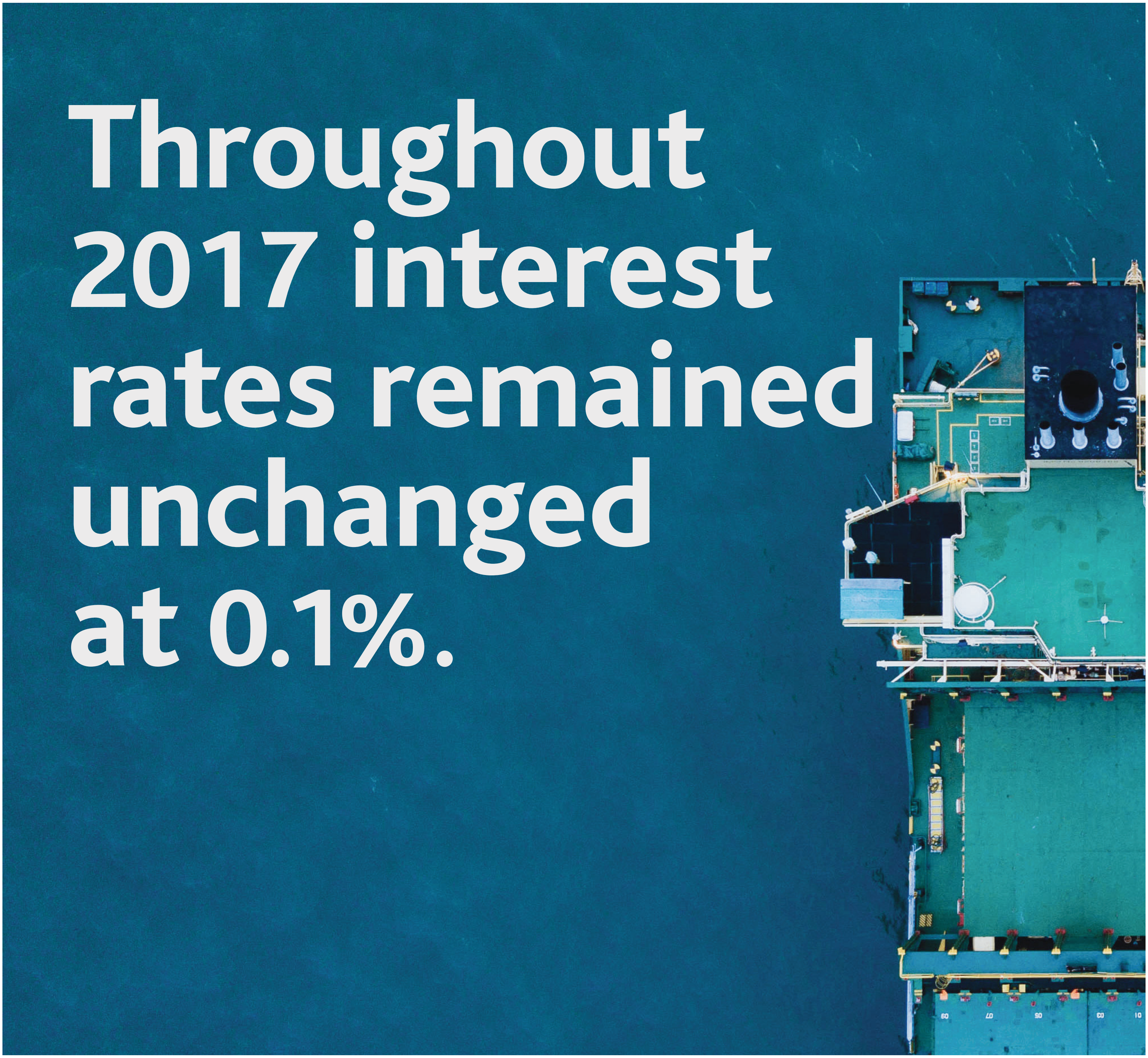
In 2016, the government's annual inflation target of 1%-3% was not accomplished. Just as in 2015, the main contributors to the CPI drop in 2016 were the energy prices. Throughout 2017, interest rates remained unchanged at 0.1%. The interest rate has remained unchanged since March 2015. The monetary policy, reflected by leaving the interest rate unchanged through 2016 and 2017, is explained by the

## Inflation Rates:




Source: Bank of Israel





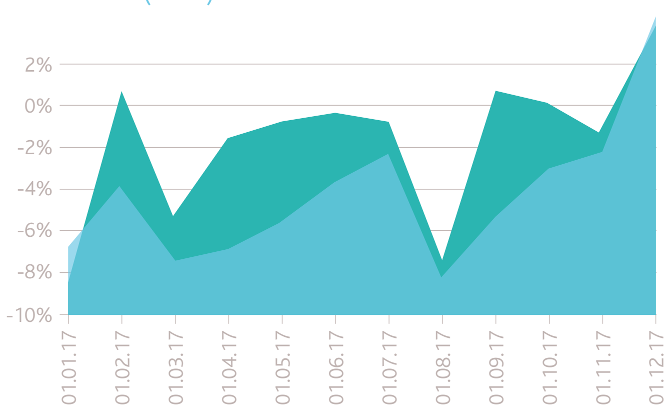
# Throughout 2017 interest rates remained unchanged at 0.1%.

attempt to achieve the inflation target of 1%-3% and to minimize the negative impact of global economic activity on the Israeli market, in order to encourage economic growth. Owing to a low inflation environment over recent months, alongside continued moderation in private home prices, the Bank of Israel was able to pursue its expansionary monetary policy.

**The TA 35 index showed a positive trend throughout 2017, representing an annual increase of 2.3%.**

After a negative trend at the end of 2016 and the beginning of 2017, the index increased until mid-2017, and decreased

TA 35 Index (Maof)




% Change   Accumulative Change

Source: Tel Aviv Stock Exchange, April 2018

by 4% in August. After that, the index increased until the end of 2017. The daily trading turnover in the stock market (on and off the stock exchange, including ETFs in the stock market) in 2017 totaled ILS 1.4 billion a day - 11% higher than the average turnover in the previous year. The daily trading turnover in the share market alone (excluding ETFs) amounted to ILS 1.1 billion in 2017- 19% higher than the daily turnover of 2016.

In the corporate bond sector, both the high-yield bonds and the general corporate bonds provided a positive return. The corporate bond yield increased by 6% compared to 3.9% in 2016, attaining a market value of ILS 328 billion.

The net amount of capital raised by the government in 2017 decreased to a total of ILS 46 billion, compared with the amount of ILS 48 billion in 2016. The stability in the Ministry of Finance's gross IPOs was made possible due to an increase in tax revenues and a decrease in governmental deficit – which dropped to 1.9% the GDP from October 2016 to September 2017. Industry indices mostly experienced price increases. The TA-Finance index marked a 24% increase over the year, alongside an increase of 20% in TA-Real Estate. The TA Global Blue Tech marked a 3% decrease.

In 2017, until November, the public sales of ETFs on local share indexes totaled at ILS 5.9 billion. The public's holdings this year increased by ILS 1 billion to a total of ILS 113 billion in November 2017. The daily trading volume in ETFs over share indices (domestic and international) decreased in 2017 (on the TASE and elsewhere) by ILS 305 million, 12% lower compared to 2016. This volume was comprised of 22% of the overall share trading volume, compared with 27% in the preceding year. This year has marked an increase in IPOs and private placements in Israel, reaching ILS 11.3 billion – compared with ILS 6.8 billion in the preceding year.

Seventeen companies jointed the TASE this year, an increase compared with 14 companies in the preceding year. These companies include 5 real estate companies, 3 technology companies, 3 oil and gas companies, and the rest are service, energy, industry and finance companies. Real estate companies raised ILS 3.8 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, 458 companies were listed on the TASE, compared with 451 in 2016. At present, there are 61

dual companies listed in the USA and Europe, and 4 additional companies listed in both the TASE and Europe.

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## FORECAST OF ECONOMIC DEVELOPMENT IN 2018

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

| Annual Change in | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|---|---|---|---|
| Inflation | 2.7% | 2.2% | 1.6% | 1.8% | -0.2% | -1% | 0.2% | 0.3% | 1.1% |
| Revaluation vs. US$ | 6.0% | -7.7% | 2.3% | -7% | 12% | 0.3% | -1.5% | -10% | |
| GDP | 5.5% | 5% | 2.9% | 3.3% | 2.6% | 2.5% | 4% | 3% | 4% |
| GDP per capita | 2.7% | 2.7% | 1.5% | 1.3% | 0.6% | 0.5% | 2% | 1.3% | 1% |
| Investment in fixed assets | 13.6% | 16.0% | 3.2% | 1.1% | -1.3% | -1% | 11.3% | 2.8% | 3% |
| Unemployment | 7.0% | 5.6% | 6.7% | 5.8% | 5.9% | 5.2% | 4.8% | 3.7% | 3,6% |
| Export | 13.4% | 5.5% | 1.0% | -1.6% | 1.5% | -3.2% | 3.0% | 3.9% | 3.5% |
| Import | 12.6% | 11.1% | 3.2% | 4.3% | 3% | 0.6% | 8.2% | 5.5% | 4% |
| Public consumption | 3.7% | 2.9% | 3.2% | 3.2% | 3.2% | 2.9% | 4.2% | 2.8% | 2% |
| Private consumption | 3.3% | 1.9% | 3.2% | 4.0% | 3.7% | 4.9% | 5.7% | 3% | 4% |
| Housing starts | 9.9% | 9.0% | -15.1% | 5.5% | -1.6% | 3.9% | -0.7% | -14.1% | |


Family Rules
work hard
LAUGH OUT LOUD
be grateful be kind
LOVED
LONDON
אהבה
אושר
שפע
HAPPINESS IS NOT A DESTINATION IT IS A WAY OF LIFE.
LOVE IS ALL YOU NEED
Keep your promises
SHARE
Say I love you
Listen to your parents
DO YOUR BEST
Always Tell the Truth
Laugh at Yourself
Hug Often
Use Kind Words
Love Each Other
LOVE IS ALL YOU NEED
HAPPINESS IS NOT A DESTINATION IT IS A
BLESS THIS HOME
FOLLOW YOUR DREAMS
Home Sweet Home
HOME
HOME

DREAMS
COME TRUE
LOVE
WILL SAVE THE DAY
TRUST
IN YOURSELF
CHERISH
EVERY MOMENT
CREATE
YOUR OWN
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WILL SAVE THE DAY
TRUST
IN YOUR
HAPPINESS
IS NOT A
DESTINATION.
IT IS A
WAY
OF LIFE.
ALWAYS
KISS ME
GOODNIGHT
HOME
WELCOM

# ISRAEL - GENERAL OVERVIEW

# 02

# ISRAEL - GENERAL OVERVIEW

## BACKGROUND

Since declaring its independence in 1948, Israel has been the home of Jewish immigrants from all over the world. The country's population - comprised of approximately 74.7% Jews, 20.8% Arabs, and 4.5% others - grew from 870,000 inhabitants in 1948 to over 8.7 million in 2017.
Over the past decade alone, Israel's population has grown by 18.3%. However, since 1992, the immigration rate has gradually declined. In 2016, 26 thousand people immigrated into Israel, compared with 28 thousand in 2015.
An important economic landmark affecting the development of the modern Israeli economy was the intensified negotiations in the 1990s with the neighboring Arab countries. This process attracted a large number of direct and indirect foreign investors to Israel. This trend came to an end following the high-tech bubble burst in the early 2000s, as well as the deterioration of the geopolitical situation.

However, current global economic conditions continue to affect Israel's development as an open market exposed to economic trends. The impact of the recent events on the global environment is relatively moderate, but is expected to increase in the future. Indications of such impact are evident, represented by a 3.3% GDP growth rate after the 4% growth rate in 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 given to each party in the Knesset is proportional to the number of votes. The only limitation is the 3.25% qualifying threshold. According to this system, voters vote for a party list and not for any particular candidate on the list.
Since the establishment of a 'primary election' system in some of the parties, these parties directly elect their candidates to the Knesset. In other parties, candidates are elected through the party's organs.
All Israeli citizens over the age of 18 are entitled to vote,

whilst those over 21 may be elected to parliament.
After the elections, the Israeli President consults with representatives from all parties, and delegates the task of forming a government to the chairman of the party most likely to succeed. If he or she succeeds, then he or she is appointed as Prime Minister and becomes 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. He is elected by the Knesset every seven years, for a limited single-term period. The President holds statutory power to accredit diplomatic senior staff, pardon criminals, sign laws, and so forth.
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, Lod and Beer-Sheva). The District Court is the first court for filing certain proceedings, and it operates 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 an 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 the State Comptroller, which is responsible for auditing and overseeing all activities of the Ministries, municipalities and other institutions subject to oversight by law.

## FACTS AND FIGURES

Israel is located on the Mediterranean coast, across 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 as part 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 in the southwest.
Israel has numerous ancient sites with ongoing excavations, constantly exposing new archeological finding. Israel's terrain varies from hilly, mountainous landscapes, with rich agricultural land in the north, to barren desert sites in the south. The lowest place on the globe, the Dead Sea, is located in the south of Israel.

### Israel's major cities:

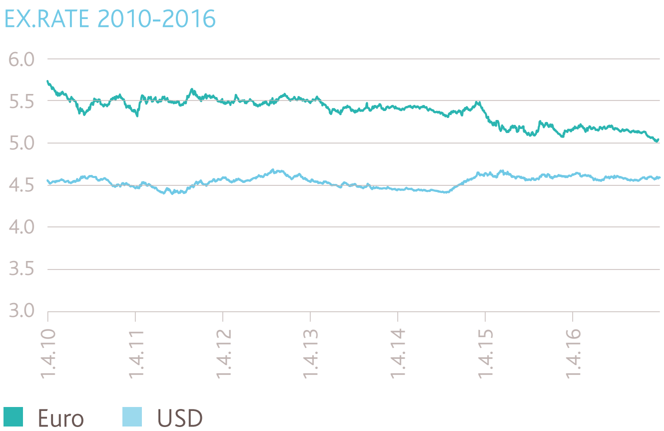
**Jerusalem:** The capital of Israel and seat of the Knesset, Jerusalem houses numerous historic and religious sites; population - approximately 883 thousand.
**Tel-Aviv:** Israel's major city - financial, commercial and industrial center, with a population of approximately 439 thousand.
**Haifa:** Principal port city in the north of Israel, with a population of approximately 280 thousand.
**Beer Sheva:** The largest city in the Negev desert (in the south), with a population of approximately 206 thousand.

Israel has a Mediterranean climate, characterized by long, hot, and dry summers (June to September), with temperatures ranging between 80-90 F (27-32°C). The climate varies significantly throughout Israel. Winters are short, mild and wet, 50-60 F (10-15°C) in most places, but reaching 40 F (5°C) in Jerusalem.
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 of measurement is the metric system.

## ISRAEL'S CURRENCY

Israel's monetary unit is the New Israel Shekel (ILS). One ILS is comprised of 100 agorot.
The representative USD rate is an indicator for its exchange rate in the foreign currency market. It is based on the average buying and selling rates published by the banks.
Other foreign currency rates, besides the USD, are calculated according to their rate in international currency markets, at the time when the representative rate is being determined. Accordingly, the ratios for the representative rates of various currencies reflect their international exchange rates at the time in which they are determined.
The Bank of Israel calculates representative exchange rates once a day on foreign currency business days only.

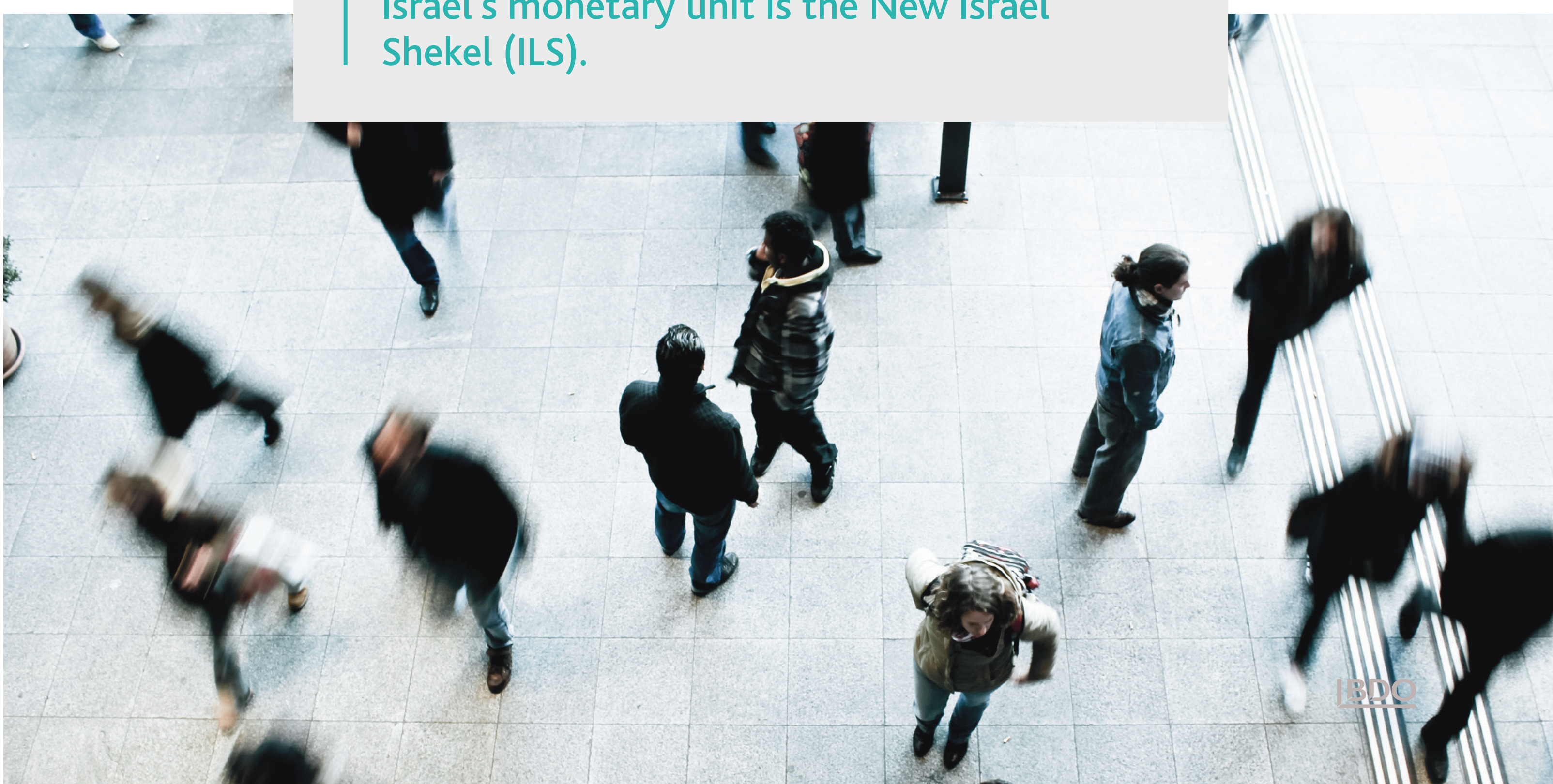
The representative exchange rates of the Israeli Shekel




in relation to some major currencies were as follows in December 31, 2017:

| Currency | NIS |
|---|---|
| US Dollar | 3.4670 |
| Euro | 4.0418 |
| UK Pound Sterling | 4.6819 |
| Swiss Franc | 3.5546 |
| Japanese Yen (100) | 3.0803 |
| Chinese Yuan "Renminbi" | 0.5341 |

**The prevailing system of measurement in Israel is the metric system. Israel's monetary unit is the New Israel Shekel (ILS).**



## INFRASTRUCTURE

Israel offers a broad and solid infrastructure to entrepreneurs, investors and business people in all sectors. The Israeli banking system is advanced, automated, and digitized, comprising a significant component of the international banking system. Diverse services required by businesses, such as insurance, legal services, temporary manpower, communications, IT systems etc., are available in the most advanced formats.
The transportation system in Israel is well developed, both domestically and internationally, with an extensive inter-urban highway network. New highways are constantly being built to enable fast and safe movement 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.
According to the "Law of Return", immigrants are entitled to a "permanent resident" status, or an A-1 visa, granting them 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 afternoon. 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 pm to 6:30 pm on two weekday afternoons. Other banks are close on Sundays, but open on Fridays. Stores are regularly open until 7:00 pm or later. On Saturdays (the Jewish Sabbath) almost all businesses and offices are closed. Legal holidays are set in accordance with the Hebrew calendar. On the eve of Jewish holidays, business hours usually end in the early afternoon.
Legal holidays in 2017 and 2018 are as follows:

| Holiday | 2018 | 2019 |
|---|---|---|
| Passover | March 30 | April 19 |
| Independence Day | April 18 | May 8 |
| Shavu'ot | May 19 | June 8 |
| Jewish New Year | September 9 | September 29 |
| Day of Atonement (Yom Kippur) | September 18 | October 8 |
| Feast of Tabernacles (Sukkot) | September 23 | October 13 |


2017
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# M&A ACTIVITY IN ISRAEL

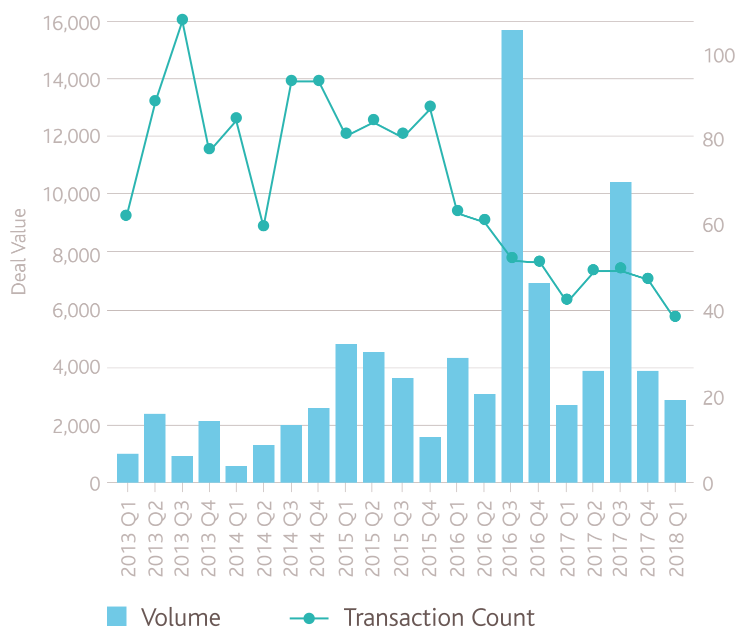
03

## M&A Activity in Israel

### GENERAL

The M&A activity of Israeli companies was quite significant during 2017. Three hundred and fifty three transactions were conducted at an overall value of $20.9 billion, compared with 323 in 2016 at $30 billion. The largest transaction that took place in 2017 was the acquisition of Mobileye by Intel for $15.3 B, also being the largest transaction ever recorded in Isreal.

M&A ISRAEL




Source: Bloomberg

According to the data shown above, the Israeli M&A market declined in activity during 2017 compared to the levels displayed in 2016. In overall perspective, transaction value levels have been significantly higher in 2015-2017, compared with the levels of 2013-2014, despite a gradual decrease in the volume of transactions.

The Israeli business environment is expected to generate significant M&A opportunities in the upcoming years due to new regulations/legislation, liquidity matters and other reasons discussed below.

## REGULATION AND LEGISLATION

Until recently, the Israeli corporate sector was dominated by large conglomerate groups. There were roughly 20 families controlling 25% of the companies registered in Israel, and 50% 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 creation of the Committee on Increasing Competitiveness in the Economy (CICE).
CICE's recommendations were published in the beginning of 2012, and in the six years since the law was enacted, a considerable amount of transactions have been excuted according to its requirements.

The law is divided into two main pillars:

### Pyramid holding structure

Holding companies must limit their pyramid structure to no more than three public layers. The Anti-Concentration Law has already significantly succeeded in reducing the number of layers in the pyramids of many Israeli public companies.

### Cross-Holdings

Holding companies must reduce cross-holdings in financial and industrial businesses. We are already witnessing many transactions and separation actions in the market. For example, Delek Group attempted to sell its Phoenix Insurance Company numerous times. In another case, Bino Group, which was required by the Anti-Concentration Law to choose between retaining their holding in a non-financial asset (Paz) and retaining their holding in a financial asset (First International), chose the latter and ceased to be the controlling shareholder in Paz Oil Company.

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. Additionaly, these restrictions create opportunities for new players. From the viewpoint of non-Israeli investors, the Concentration Law constitutes a jumping-off point, giving them an advantage over existing concentrated players.

## FOUNDERS

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

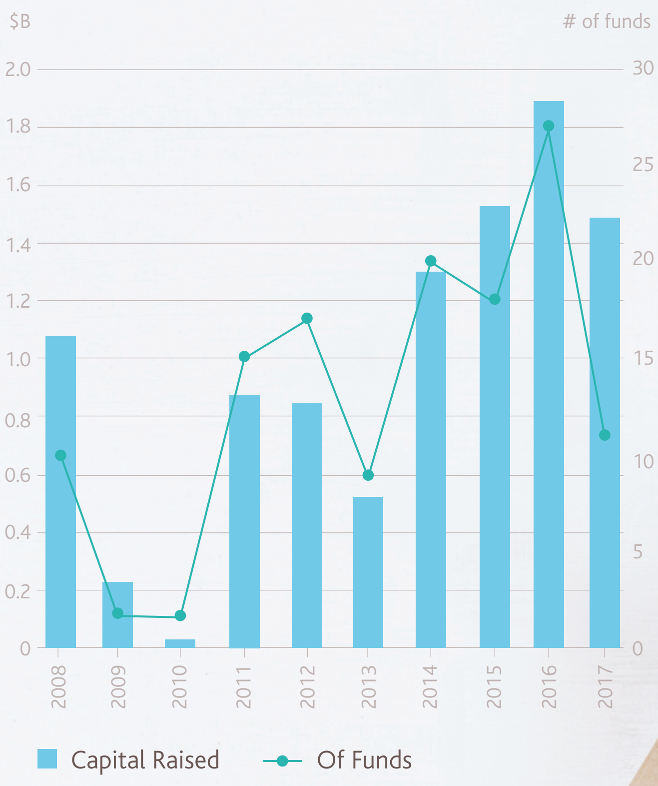
## PRIVATE EQUITY ACTIVITY

Israel has recently been enjoying a growing interest in both local and foreign Private Equity Funds (PEs). According to an analysis by IVC Research Center, 41 Israeli private equity management companies are currently active, managing a total of $13 billion in capital, with an estimated $1 billion available for new investments.
In recent years, the successful local PE activity has also attracted large global PE funds and investment companies such as Berkshire Hathaway (Iscar), Apax Partners (Bezeq, Psagot, Tnuva), Permira (Netafim). Other companies, notably Blackbone, Blackrock, KKR, are expected to launch their operations in Israel in the near future.
PE activity is also expected to generate significant "sell side" opportunities. Most funds are obligated to exit their investments within 6 to 10 years of their accusation. In light of the significant PE fund activity during 2010-13, various opportunitis are expected to come out into the market in **the** following years.

## VENTURE CAPITAL FUND RAISING

Israeli VC funds raised $1.48 Billion in 2017 vintage. This rise was a result of a 58% increase in the VC's first investments. During 2017, investors poured more capital into fewer selected companies, providing portfolio companies with the necessary means to mature. Young technology companies are likely to enjoy this situation in the course of 2018. During 2017, as in the past two years, companies in growth stages (mid and late stages) attracted the largest portion of capital - raising $3.9 billion, compared with $3.4 billion in 2016. Mid-stage companies increased their share to $2.1 billion in 2017, compared with $1.8 billion in 2016. Seed and early stage companies raised $1.36 billion in total throughout 2017, compared with $1.43 billion gained in the previous year. In 2017, the volume of capital raising increased, continuing the consistent growth trend of the past five years. The high-tech industry matures and settles as the source of innovation and interest for investors and entrepreneurs from all over the world. At the beginning of 2017, over $3 billion was available for investments (dry powder) by Israeli venture capital funds.

Capital Raised by Israeli VC Funds by Vintage Year 2008-2017




Source: IVC Researh Center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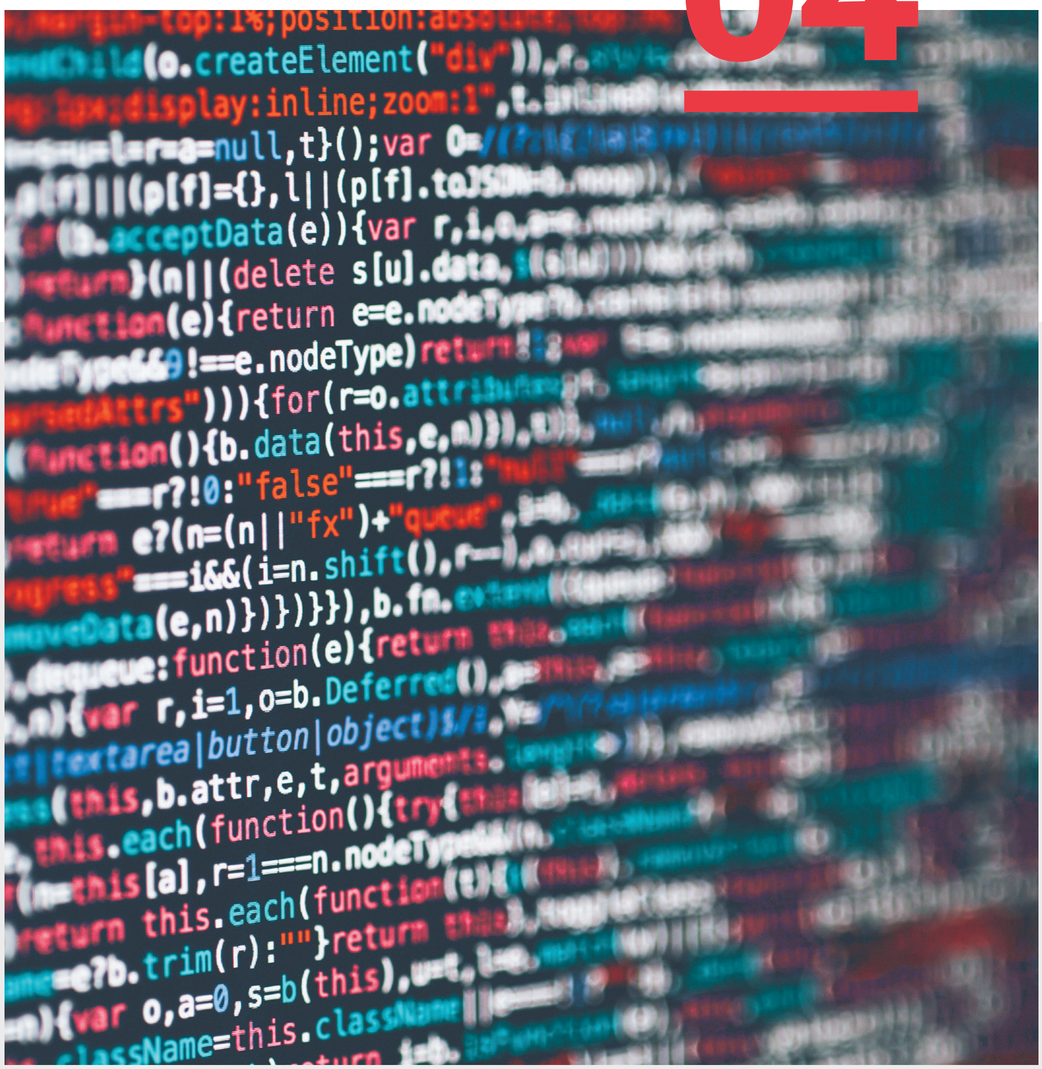
## ISRAELI MARKET MULTIPLES

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 traditionally "enjoys" lower EBITDA multiples most commonly in the range of 5-10, 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 get a negative size premium.
**Perceived Geopolitical 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.

> Developed countries tend to have lower multiples, supported by lower market expectations, even though the perceived risk is considered to be relatively low.

# 04

# OVERVIEW OF ISRAEL'S HIGH-TECH INDUSTRY



# ISRAEL'S HIGH-TECH INDUSTRY

## INTRODUCTION

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 last decade. Only 25 years ago, most of the country's technology was concentrated in military/security-related industries. While 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.

Despite recession in the early 2000s, the high-tech sector became the primary engine for economic development in Israel. Its recovery in 2005 was essential in bringing Israel's economy back to a sustainable growth path. However, given the credit crunch in 2008, the financial resources available to the high-tech industry have declined significantly, causing high-tech and start-ups companies to lay off employees or shut down completely. This trend continued during the first half of 2009, until 2010, when the market began moving towards an upward trend.

In 2017, the High-Tech sector was in the midst of a positive trend that began in previous years, despite slightly weak figures compared to 2016. Exits amounted to $23 billion as part of 112 completed transactions, a drop of 8% compared with 120 exits in 2016. Exits in 2017 were mostly compromised of 2 mega-deals of more than $1 billion each: Mobileye was purchased by Intel for $15.3 billion, and Neuroderma was purchased by Mitsubishi Tanabe Pharma for $1.1 billion. These two transactions alone accounted for more than 70% of all the transactions in 2017.

Looking at exits by transaction scope in comparison with 2016, the number of medium scope exits ($20m-$100m) decreased by 18% in 2017, with a total of 87 exits in 2017, compared with 106 exits in 2018. The number of large scope exits (>$100m) increased by more than 60% in 2017, with a total of 18 exits in 2017, compared with 11 exits in 2016.

Comparing VC-backed exits versus non-VC-backed exits, data shows a decline in the number of exits involving non-VC-backed companies, with an average of 59 exits in 2017, compared with an average of 74 in years 2014-2016. Furthermore, data of non-VC backed exits shows stability

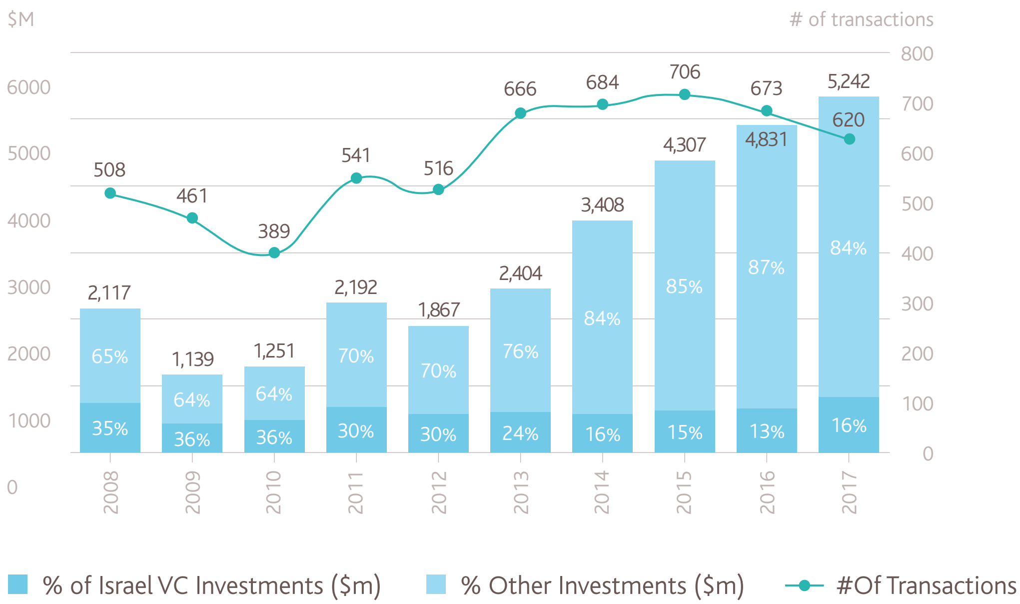
This chapter is based on data gathered by IVC Research Center.

with 46 exits in 2017 compared with an average of 49 in years 2014-2016. However, non-VC-backed exits in 2017 totalled in $18.62 billion, the highest value in the past 5 years, mainly due to the acquisition of Mobileye, while VC-backed exits totalled in $2.88 billion of VC-backed exits, similar to an average value of 2.97 in years 2014-2016.

## THE HIGH-TECH CAPITAL RAISING IN 2017

In 2017, approximately 620 Israeli high-tech companies raised $5.2 billion from local and foreign investors. This figure is 8.5% higher than the $4.8 billion raised in 2016, and 22%

Capital Invested in Israeli High-Tech Companies by Israeli VC Funds, Foreign and Other Investors (%) Year 2008-2017

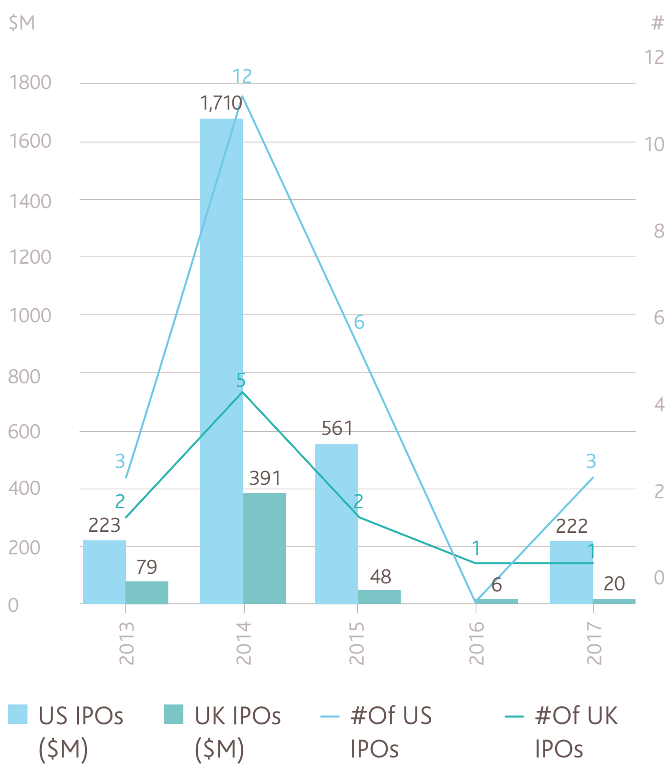



Source: IVC - ZAG High Tech Survey 2017

higher than the $4.3 billion raised in 2015.
In 2017, venture capital funds comprised 16% of the overall capital invested in Israeli high-tech companies, compared with 13% in 2016 and 15% in 2015. There are some indications of a coming increase in the value of investments made by foreign and other investors.
In 2017, 3 companies were listed on the NASDAQ, raising an accumulated amount of $222 million, compared with no companies listed in 2016, and 6 companies listed in 2015,

which raised an accumulated amount of $561 million. In addition, one company was listed on the European stock exchange, raising an amount of $20 million, compared with one company listed in 2016 which raised $6 million, and 2 companies listed in 2015, which raised an accumulated amount of $48 million.
The following graphs illustrate the amount of capital raised in the U.S. and European IPOs:

### Capital Raised in IPOs on the European & US Stock Exchange by Israeli High-Tech Companies in 2013-2017

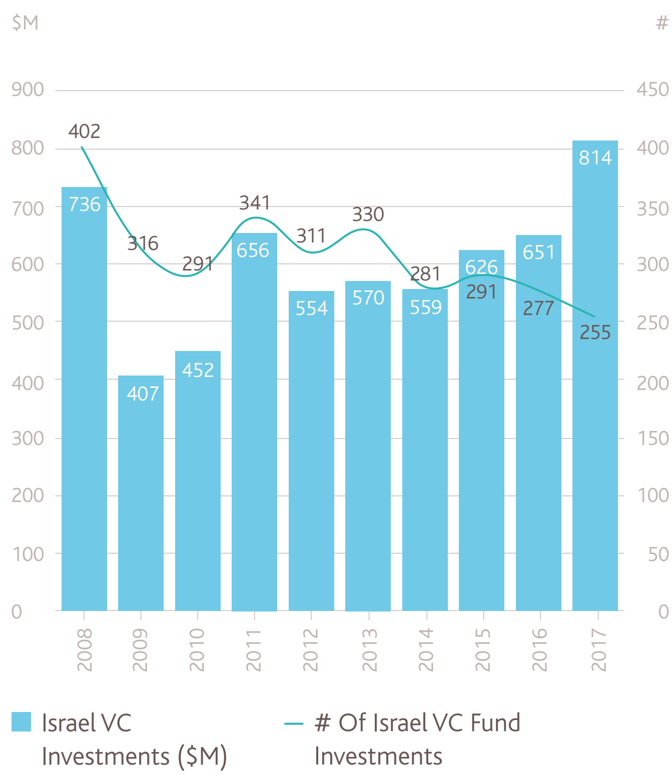



Source: IVC - ZAG High Tech Survey 2017

## 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 last few years. By providing and allocating funds, 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, it is 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 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 2017, Israeli VC funds invested $814 million in Israeli high-tech companies, compared with $651 in 2016 and $626 million in 2015.

### Capital Invested in Israeli High-Tech Companies by Israeli VC Funds (M$), 2008-2017




Source: IVC - ZAG High Tech Survey 2017

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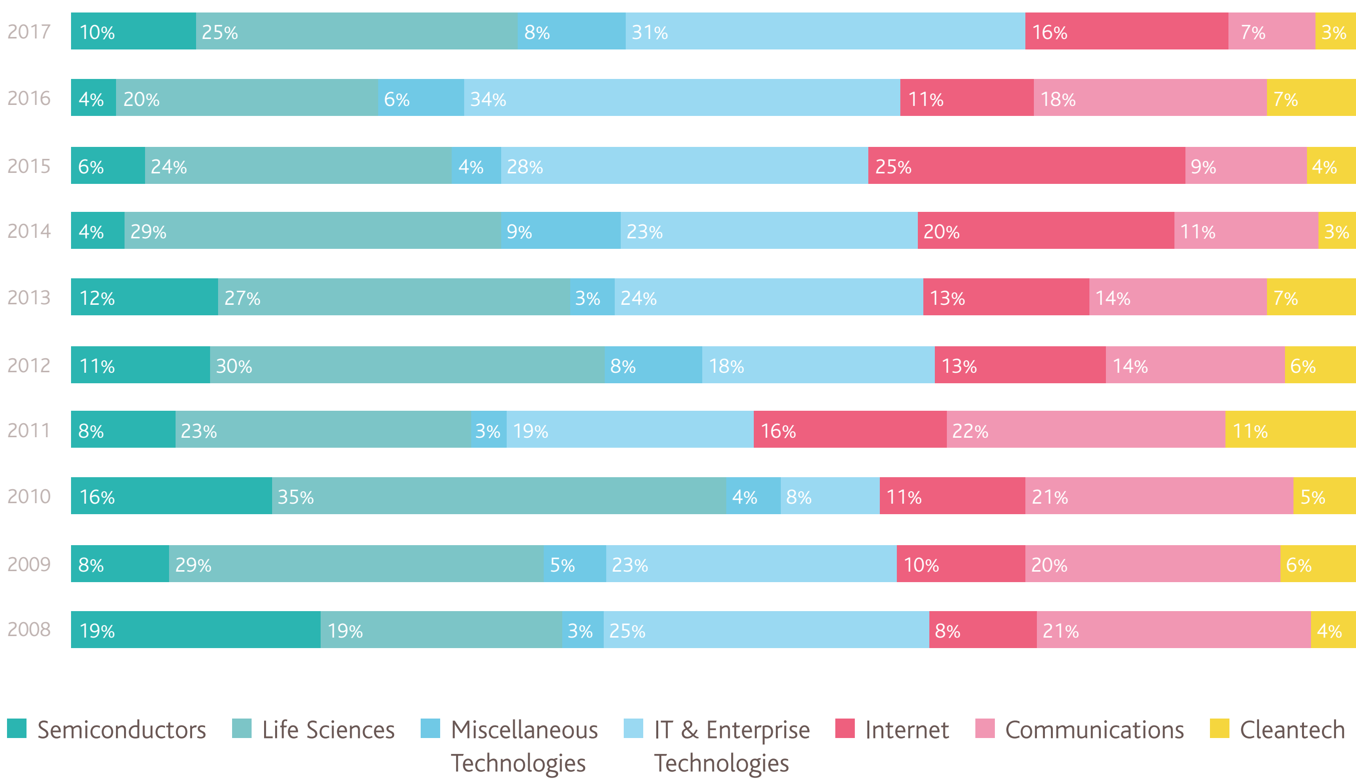
## ANALYSIS OF VENTURE CAPITAL RAISED BY INDUSTRY

Capital Raised by Israeli High-Tech Companies by Sector (%), 2008-2017




Source: IVC - ZAG High Tech Survey 2017

Israeli companies have a distinct presence among the various high-tech industries. The capital ratio raised by its different sectors has varied over the last few years.

In 2017, the IT/software, life science sectors attracted the largest share of investments and raised approximately $1.6 & $1.3 billion, respectively, comprising 31% and 25% of the aggregate capital raised by Israeli high-tech companies. The internet sector followed with approximately $0.8 billion, comprising 16% of the aggregate capital raised by high-tech companies. The semiconductors sector attracted approximately $0.5 billion, comprising 10%.

The following graph displays the relative share of the different sectors out of the total amount of capital raised over the past years:

Below is an analysis of the capital raised by Israeli companies in leading sectors of the economy. This data is based on analyses by the IVC Research Center.

### Communications

Communications is considered a major field for raising capital. However, since 2011 there has been a decline in this sector's share. Year 2017 shows further decline in the sector's share, with only 7% out of the aggregate amounts raised.

The capital raised by the communications sector in the five years previous to 2017 accounted for an average of 12% of the aggregate amounts raised. The year of 2016 was exceptional in this regard, as capital raised in this year reached 18% out of the aggregate amounts. It should be noted that the local media and telecommunications field has undergone various changes over the past decade, making it into an attractive and accessible market for investors. One example is the vigorous competition evident in the multi-channel broadcasting field.

### Software

Capital raised by Israeli high-tech companies via software companies amounted to a 31% share of the aggregate amounts of capital raised in 2017 - indicating a steady status. This is compared with a share of 34% in 2016, and a slight increase compared to an average share of 28% in the last five years.

### Internet

Capital raised by Israeli high-tech companies via the Internet sector amounted to a 16% share of the aggregate amounts of capital raised in 2017 – an increase compared with a share of 11% in 2016, and similar to an average share of 17% in the last five years.

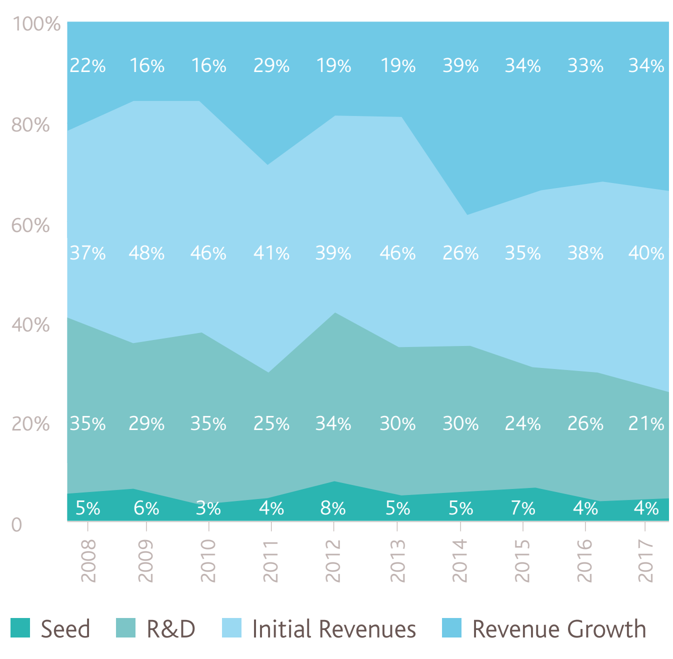
### Life Sciences

Capital raised by Israeli high-tech companies via the life sciences sector amounted to a 25% share of the aggregate amounts of capital raised in 2017 – an increase compared with a share of 25% in 2016, and similar to an average share of 25% in the past five years.

## CAPITAL RAISED BY ISRAELI HIGH-TECH COMPANIES BY STAGES

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 companies' development stages has changed. In the 1990s and in the beginning of the last decade, investments during the initial phase were more common. Today, the majority of investments are made during the intermediate and later stages, in order to lower risk levels.

Capital Raised by Israeli High-Tech Companies by Stage (%), 2008-2017




Source: IVC - ZAG High Tech Survey 2017

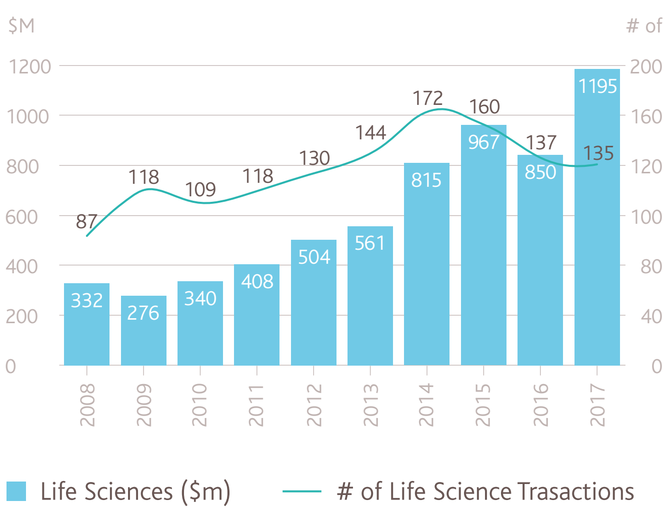
In 2017, initial revenue stage companies led capital raising with 40% of total funds raised, equal to $2.1 billion. This is an increase compared with 38% in 2016 and 35% in 2015. Late stage companies raised $1.8 billion or 34%, similar to the amount of funds raised in 2015 and 2016. Early stage companies (R&D) accounted for 21%, marking a decrease from 26%
in 2016 and 24% in 2013. Seed companies attracted 4%, similar to 2016.

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

## THE BIOTECHNOLOGY INDUSTRY IN ISRAEL

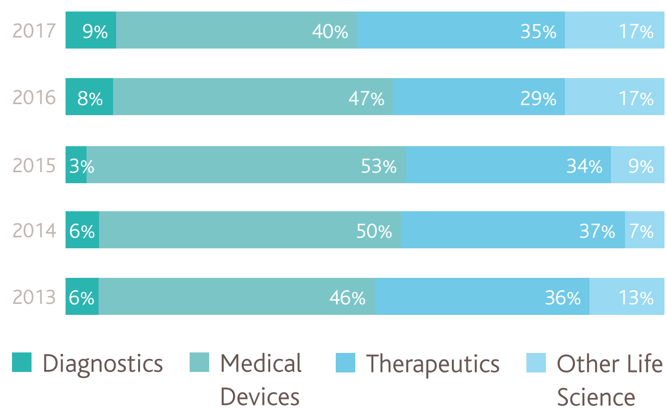
Modern science utilizes biological information accumulated over 150 years - mainly the genetic code and DNA structure decoded some 50 years ago. The biotechnology business environment has evolved as a result of the breakthrough in genome development over the past few years. The information accumulated in a genome project, in which whole platforms of the human genome were discovered, has created new opportunities for many start-up companies. It is assumed 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. In the past five years, investments in life science companies have been on a rise. The total investment in life science companies during 2017 amounted to $1.2 billion, a 40% increase compared with $850 million raised in 2016, and a 113% increase compared with investments made in 2013, which amounted to $561 billion. The following graph illustrates the capital raised by the life science industry over the last few years:

Capital Raised by Israeli Life Science Companies ($M), 2008-2017




Source: IVC - ZAG High Tech Survey 2017

Capital Raised by Israeli Life Science Companies (%), 2013-2017




Source: IVC - ZAG High Tech Survey 2017

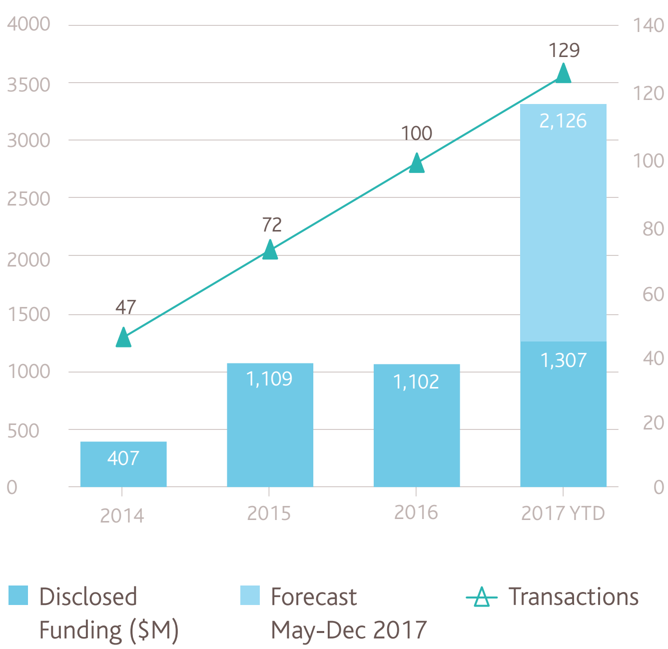
A major sub-branch of biotechnology is the field of medical devices. In 2017, this sector drew 40% of the aggregate capital raised for the industry - a decrease of 7% of its share compared with the previous year. The decrease in medical devices is followed by an increase in other sectors, such as therapeutics and diagnostics, which have experienced an increase in 2017. The Israeli government has encouraged investments in the medical devices 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:

## VALUING COMPANIES IN THE AUTONOMOUS VEHICLE INDUSTRY

Over the last few years, autonomous vehicle technology – and in particular, advanced driver-assisted systems ("ADAS") - has garnered much attention in the investment world, as the underlying technology has become more sophisticated and accurate.
ADAS is defined as a type of system that assists with tasks involved in operating a motor vehicle. For example, it includes functions assistance with monitoring, warning, braking and steering. The global automotive ADAS market is expected to reach an estimated $29.7 billion by 2022, and is expected to grow at a CAGR of 21.1% from 2017 to 2022. ADAS technology is expected to disrupt the traditional automotive industry, with estimates that self-driving vehicles will become standard by the end of the 2020s.

The undustry is facing considerable challenges and is working to analyze the following questions:




Source: CB Insights

1. How can investors in the ADAS market make informed choices when many details of recent transactions are not publicly available, and when multiple stakeholders, with different interests, are investing in ADAS technology?

2. What directions can investors take from publicly traded companies in the industry?

In analyzing the above questions, we hope to provide relevant valuation considerations for a burgeoning industry.

### Increased Investment in ADAS Startups

The overall auto tech industry has been seeing an increased number of transactions and fundraising since 2014, with 2017 set to be a record year:
Of the 2017 YTD investments, 67% of total investments were for companies raising seed to series B financing. Startup companies are not easy to value, because of the uncertainty

> **Israel's venture capital industry has played a fundamental role in the dramatic development of the global high-tech industry over the past few years.**

[2] "Growth Opportunities in the Global Automotive ADAS Market," August 2017, Research & Markets

in their ability to succeed on an ongoing basis. One of the most challenging aspects of valuing a Company in the ADAS industry is the lack of publicly available information that is normally used to establish valuations.

**Investments in Privately Held Companies**

| Notable Investor/ Buyer | Target | Transaction | Date | Amount ($M) | Target Location | Technology Description |
|---|---|---|---|---|---|---|
| General Motors | Cruise Automation | Acquistion | 11-Mar-16 | 1,000 | San Francisco, USA | Artificial Intelligence Software |
| Ford | Argo Al | Investment | 10-Feb-17 | 1,000 | Pittsburg, USA | Robotics & Artificial Intelligence Software |
| Uber | Otto Motors | Acquistion | 17-Aug-16 | 680 | Ontario, Canada | Robotics & Software Intelligence for an Integrated Inventory Movment Platform |
| General Motors | Lyft | Investment Funding | 04-Jan-16 | 500 | San Francisco, USA | Ride Sharing Network |
| Volvo | Uber | Joint Venture | 18-Aug-16 | 300 | San Francisco, USA | Ride Sharing Network |
| Lux Capital Blackbird Ventures | Zoox | Investment | 27-May-16 | 250 | Menlo Park, USA | Robotics & Artificial Intelligence Software |
| Herman | TowerSec Automotive | Acquistion | 05-Jan-16 | 70 | Kfar Saba, Israel | On-Board Cyber Security Software |
| Omnitracs, Lockheed Martin, DENSO Intrantional America, Intel Capital | Peloton Technology | Funding Round B | 05-Apr-17 | 60 | Mountain View, USA | Sensors, Break Control, Vehicle Connectivity for Truck Platooning |
| Accel | DeepMap | Funding Round B | 04-May-17 | 25 | Palo Alto, USA | 3D Mapping Software |
| Alibaba | WayRay | Funding | 14-Mar-17 | 18 | Lausanne, Switzerland | Augmented Reality Technology |
| Lockheed Martin, DENSO Intrantional America, Intel Capital | Peloton Technology | Investment | 31-Aug-15 | 17 | Mountain View, USA | Sensors, Break Control, Vehicle Connectivity for Truck Platooning |
| Highland Capital Partnetrs, Devlopment Board, Ford, Signal Ventures, Samsung Ventures | NuTonomy | Funding Round B | 24-May-16 | 16 | Cambridge, USA | Algorithms, Software |

Furthermore, the increasing interest in investing in auto tech startups, including ADAS, raises questions about how to value these disruptive technologies. While large capital investments in autonomous vehicle startups provide good indications of interest in the field, there is limited information on the valuation multiples used, as these private companies often do not publish financial reports or the valuations used as a basis for investments.

### Investment from Different Investor Types

The following table shows select investments, in order of investment amount, in privately held ADAS companies over the last two years:

The table above illustrates the wide variety of investors interested in the ADAS industry. The total amount of investments in the table above is approximately US $3.7 billion.

Investors range from traditional venture capitalists, later stage startup companies such as Uber, traditional automotive companies who have decided to acquire the technology rather than develop it in house, and high-tech companies with vast semiconductor operations that plan to integrate ADAS technology into their future self-driving car computer system (IBM, Intel).

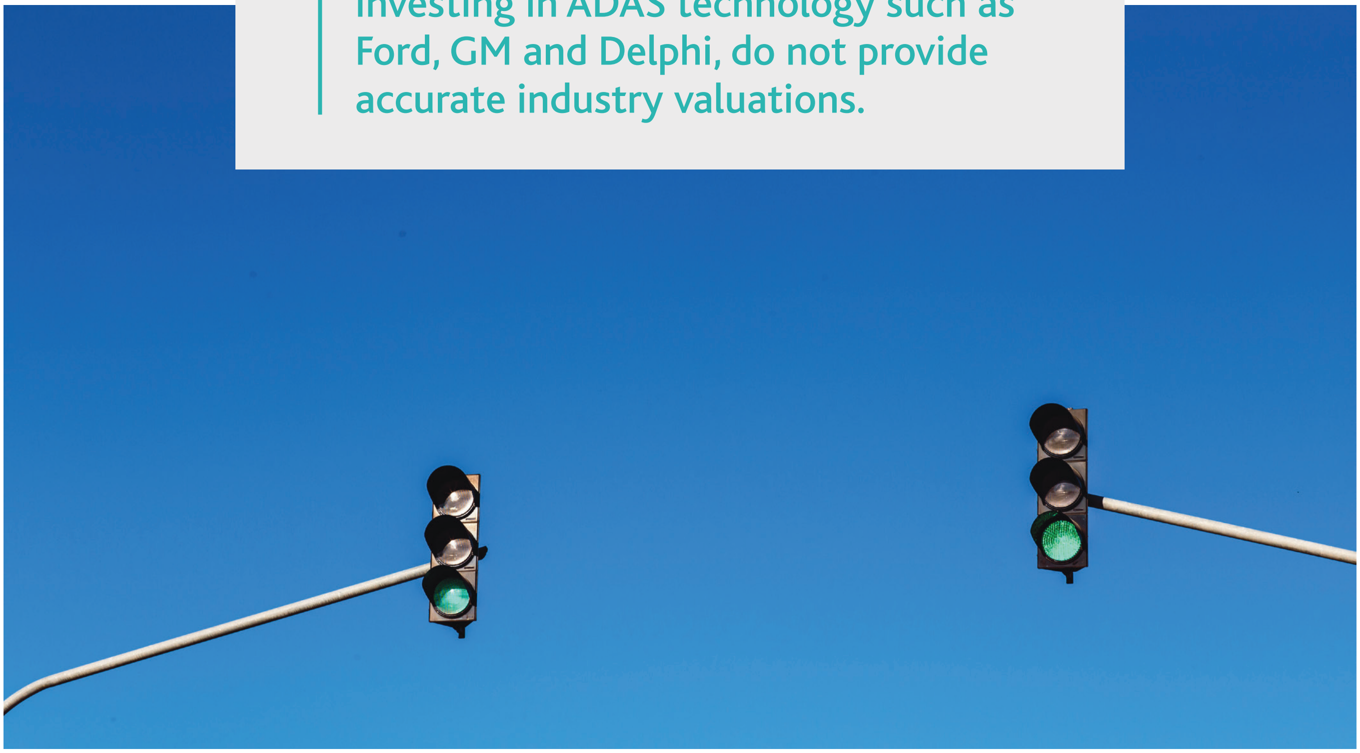
All of these investors are seeking to gain exposure to the ADAS market, and each stakeholder has different interests and objectives from the other.

For example, a venture capitalist's valuation would not include potential product synergies such as a traditional automotive company like GM or Ford. The consideration of synergies would likely create a more optimistic forecast and could potentially realize a higher valuation than if a venture capitalist has been the sole investor.

### Public Companies Analysis

As mentioned earlier, a majority of the pure ADAS companies are startups. Most public companies currently investing in ADAS technology, such as Ford, GM and Delphi, do not provide accurate industry valuation multiples for the autonomous vehicle market, because autonomous driving is

> **Most public companies currently investing in ADAS technology such as Ford, GM and Delphi, do not provide accurate industry valuations.**



not part of their core business.
However, a few pure-play ADAS companies do exist, and their involvement in recent transactions may shed light on the valuations placed on ADAS technology.
We selected four public companies for the following reasons:

### Mobileye

Acquired by Intel for US $15.3 billion in March 2017, Mobileye is currently the leading supplier of ADAS software, with over 25 automakers as partners. Their technology supports sensing, mapping and driving policies.

### Foresight Autonomous

Another Israeli ADAS company, dual listed on the Tel Aviv Stock Exchange and NASDAQ. Foresight's current offering includes Eyes-On, a two-to-four camera system, which provides 3D stereo visions.

### Harman International Industries

Acquired by Samsung for US $8 billion in March 2017, Harman International Industries offers connected car solutions to automakers, including 3D and augmented navigation, telematics

| Name | Ev | Maket Cap | Revenue T12M | EBITIDA T12M | Transaction/ Traded | Revenue Multiple | EBITIDA Multiple | As of |
|---|---|---|---|---|---|---|---|---|
| Mobileye NV | 13,053 | 13,727 | 408 | 139 | Acquired | 33.7 X | 99.0 X | 26-Sep-17 |
| NXP Semiconductors NV | 42,165 | 38,011 | 8,344 | 2,805 | Acquired | 4.6 X | 13.6 X | 26-Sep-17 |
| Harman International Industries | 7,794 | 7,793 | 5,031 | 592 | Acquired | 1.5 X | 13.2 X | 06-Mar-17 |
| Foresight Autonomous Holding | 128 | 132 | 0 | -13 | Traded | N/A | N/A | 26-Sep-17 |

[3]On September 28, 2016, shares of the Dutch automotive chipmaker, NXP Semiconductors, closed at US $82.24. On the 29th, rumors of Qualcomm's interest in a takeover of NXP boosted the company's shares by around 17% to a closing price of US $96.12. The two companies reached a definitive agreement on October 27, 2016, in which Qualcomm undertook to purchased NXP for US $100 per share. The two companies have since been handling the hurdles of regulatory approval; however, NXP has been trading above US $100 since March of this year. Currently, major NXP shareholders, including Elliott Management Corp, are pressuring NXP to renegotiate with Qualcomm for a higher purchase price.
On November 14, 2016, Harman International Industries was trading at around US $88. When Samsung announced their intended acquisition of Harman International Industries for US $112.00, a 27% premium.
On Friday, March 10 2017, Mobileye's shares closed at US $47.27. On Monday, March 13, 2017, Intel announced its acquisition of Mobileye, and its shares closed at US $60.62 that evening, an increase of 28%.

control units and connected safety features, such as rear-view and wide-angle camera applications.

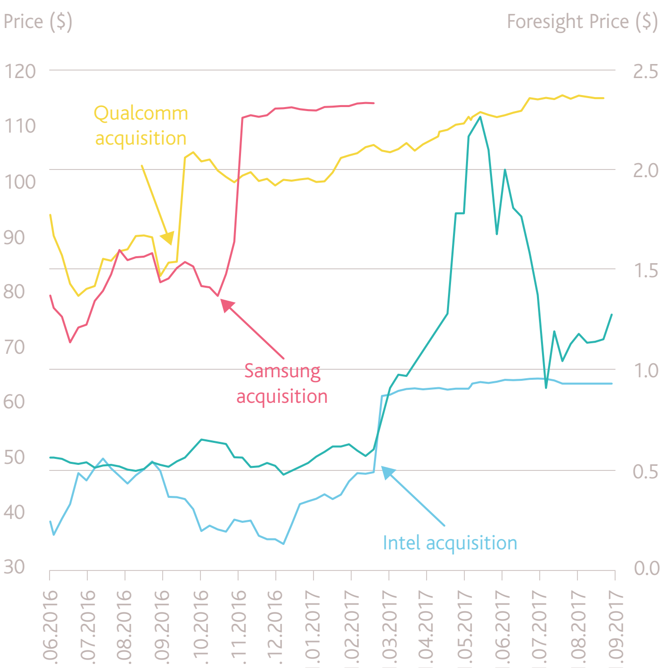
### NXP Semiconductors

Pending acquisition by Qualcomm for US $39 billion, the largest transaction in the chipmaker's history. NXP develops automotive semiconductors- and has multiple ADAS technology offerings across the sensing and controlling segments.

The following table represents the trailing twelve-month revenue and EBITDA multiples as of September 26, 2017 or the last day it was publicly traded:

All three of these companies have since been purchased, and it's interesting to note the vast difference in multiples. NXP and Harman, two well established companies with revenues greater than US $5 billion, have slightly similar multiples, with a revenue multiple ranging from 1.5X-4.6X and an EBITDA multiple of 13.2X-13.6X. However, these companies have other operations that are not in the ADAS space and therefore may have diluted the pure ADAS multiple. Mobileye, on the other hand, has multiples that are 11 and 7 times greater than that of NXP and Harman. How Intel arrived at the acquisition price is based on many internal considerations that are not public information, and likely include synergy opportunities. Foresight has no revenues and a negative EBITDA; therefore it does not have multiples that can be properly analyzed.
The following graph displays additional considerations with regards to how market sentiment can affect valuations (updated September 26th, 2017):

Selected Share Price Data




### Acquisition Premiums

Three of the above companies have been purchased over the last year. In all cases, the buyer paid a premium of over 15%. These acquisitions were made by well-known technology providers, and the premium paid for the share price could be a result of internal analyses with regards to synergies that the public did not take into consideration.

### Industry Momentum

Significant industry events can directly and indirectly impact other companies in the ecosystem. Shortly after Mobileye was acquired by Intel, Foresight's price sharply rose, with an increase of 254% from March 10th, 2017 to its peak on June 5th 2017. This increase was a result of the strong interest in Israel in companies similar to Mobileye. The momentum from the asquisition of Intel allowed Foresight to raise over ILS 40 million, through three separate offerings on the Tel Aviv Stock Exchange, in a short period of two weeks.

### Dual Listing Impact

In June 2017, Foresight began trading on the NASDAQ. Since its dual listing, Foresight's share price has fallen 44%, after its peak of $2.19 on June 5th, 2017. After gathering much local hype in the Israeli market, the public listing in one of the most active stock exchanges broadened Foresight's exposure to worldwide investors, and impacted overall sentiment in the valuation. However, Foresight is still up 150% since the beginning of the year, a sign that individual company milestones and overall market sentiment have still created a net positive impact on the company's valuation this year.

## Conclusion

The ADAS industry is one of many emerging industries that will impact our daily lives in the near future. However, while aspects of self-driving technology are already present in the market, it will take several years before this technology becomes prevalent in everyday lives. The timeline to becoming a mature technology can create volatility and uncertainty in the market. We believe that the above analyses lead to three important valuation considerations:

1. Variety of Investors: Investors have ranged from traditional venture capitalists, technology providers, and automotive companies. Investments by well-known companies such as IBM, Intel, GM, and Ford signal that self-driving car technology is closer to becoming prevalent rather than a far-off fantasy.

2. Start-Up Market: The industry is driven by innovative younger companies who disrupt the traditional ecosystem. Since little information is publicly available on investments made in startups, one needs to conduct their own due diligence to arrive at a valuation. How developed is the company's technology? What is the time to market? Does the budget make sense in light of the time to market? When can the company expect sales? If it already has sales, how stable are future revenue streams?

3. The impact of Synergies: Large companies are investing in this field, and some have paid large premiums to acquire technology. Especially when valuing a younger company, does the forecast include revenues from potential synergies with another entity?

4. Market Momentum: With growing excitement around the overall industry, and the large variety of players in the industry, its important to block out the noise and analyze the Company on a stand-alone basis to understand its value proposition in comparison to the market.

**The ADAS industry is one of many emerging industries that will impact our daily lives in the near future.**


Israel has extensive business relationships worldwide.

# BUSINESS ENVIRONMENT

05

## 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:

| | |
|---|---|
| 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, 2017

### Distribution of Employees

The work force in 2017 consisted of approximately 3.8 milliom employees. The following table summarizes the distribution of employed persons according to economic sectors in average for the year 2017:

| | |
|---|---|
| Other service activities | 3.3% |
| Arts, entertainment and recreation | 2.1% |
| Human health and social work activities | 11.3% |
| Education | 14.3% |
| Local, public and defence administration and social security, and extraterritorial organization and entities | 3.8% |
| Administrative and support service activities | 8.3% |
| Professional, scientific and technical activities | 6.7% |
| Real estate activities | 0.8% |
| Financial and insurance activities | 3.0% |
| Information and communications | 5.0% |
| Accomodation and food service activities | 6.5% |
| Transportation, storage, postal and courier activities | 3.8% |
| Wholesale and retail trade, and repair of motor vehicles | 13.6% |
| Construction | 5.4% |
| Electricity and water supply, sewage and waste management | 0.9% |
| Manufacturing | 9.8% |
| Mining and quarrying | 0.1% |
| Agriculture, forestry and fishing | 1.3% |

Source: Central Bureau of Statistics, Israel, 2018

Salaries and wages paid to Israeli employees are highly diversified. The following table presents the average wages per employee post. The figures are rounded and presented in 2017 US Dollars, per month:

| Industry | US$ per month |
|---|---|
| Agriculture, forestry and fishing | 1,926 |
| Mining and quarrying | 6,687 |
| Manufacturing | 3,887 |
| Electricity and water supply, sewage and waste management | 5,069 |
| Construction | 2,574 |
| Wholesale and retail trade and repair of motor vehicles | 2,394 |
| Transportation, storage, postal and courier activities | 3,126 |
| Accommodation and food service activities | 1,305 |
| Information and communications | 5,552 |
| Financial and insurance activities | 4,906 |
| Real estate activities | 3,166 |

Source: Central Bureau of Statistics, Israel, Statistical Abstract of Israel, 2018.
US$1 = NIS 3.59.

As of July 2017, the minimum monthly salary in Israel was set at ILS 4,825 [ILS 25 per hour]. In December 2017 the minimum monthly salary in Israel was raised to ILS 5,300 [ILS 28.49 per hour]. In addition to their salary, employees are also entitled to receive compensation for travel expenses to and from their 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 receive special compensation for work on Saturdays and holidays.
In addition to salary, the employer is required to pay/contribute various social benefits, as follows:

## Compulsory Contributions:

### National Insurance (Social Security)

Comprises 6.72% of gross salary (in addition to the employee's contribution). The National Insurance Institute provides welfare in respect of unemployment, disability, retirement, military reserve duty, child allowances, maternity leave, etc.

### Severance Pay

Comprises 8.33% of gross salary. Any employee whose employment has been terminated is entitled to receive severance pay based on their latest salary amount for each year of employment.

### Sick Leave

Consists of the accumulation of 1.5 days per month. In many cases, the sick leave allowance may reach 30 days per annum. Employees may accumulate up to 90 sick days.

### Vacation

The 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 for over 14 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 its employees' regular salary, including all social benefits, for the entire period of reserve duty. National Insurance reimburses the employer for the gross salary amount during his reserve duty.

### Convalescence Pay

Employees are entitled to convalescence pay according to seniority at work and based on their 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 their previous workplace is entitled to receive contribution as of the first day of work, payable 3 months after the start of employment at the new workplace.

Contribution by the employer is set at 6%, and contribution by the employee is set at a minimum rate of 5.5%, together comprising 17.5% of the employee's salary. As of July 16, the contribution by the employer will be set at 6.25% and contribution by the employee was set at a minimum rate of 5.75%.
In addition to the social benefits described above, other legislation and regulations exist to regulate working conditions; however, they cannot be directly "converted" into money. Among these laws and regulations are the following:

### Employment of Women Law

The law protects women employees and specifies the terms and restrictions imposed on employers regarding their women employed by then. These include night work, pregnant women's rights, maternity leave, etc.

### Employment Law (Equal Opportunities) Law

Prohibits discrimination against employees in all matters and for any reason.

### Equal Pay Law

Legislates women 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 and sector of the business, and requires licensing from ministries, municipalities, authorities, and other statutory entities.
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, according 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, or between that party and an entity that is not a party to the agreement.
Any agreement that determines prices, market share, profit margins, or quotas is considered a restrictive agreement. However, the law excludes some agreements from its general definition, are not considered restrictive (e.g. entitlement to use proprietary rights, international transport, etc.).
Participation in any restrictive agreement is prohibited unless the agreement was 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 Israel's growing awareness of the advantages of competitive markets.

Block exemption: In 2000, the Director General of the Antitrust Authority defined block exemptions that exclude 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. This exemption is given in respect of the arrangement relating to wholesale produce and marketing of local agricultural products. As a result, 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 mentioned above. In this framework, all the parties concerned grow products that are included under the arrangement, or 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 approval by the Antitrust Authority prior to becoming effective:

- If, 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 exceeds 50%.

- If the combined turnover of the merged companies (domestic turnover only) in the fiscal year prior to the merger exceeded ILS 150 million (approximately US $38.6 million), and at least two of the merged companies have a turnover of over ILS 10 million (approximately US $2.57 million) each.

- In case one of the parties is already a monopoly.
- The lastest amendment as of 2012 prescribes the composition of the mergers exemptions committee, such that it would be comprised 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, responsible for the subject of the test, as well as 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 website 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 the court to order the member of a cartel group or of a monopoly owner to sell assets. This is done in cases where necessary, in order to prevent damage or fear of causing substantial damage to competition, or to the public. In case of a cartel, this is done if required in order to substantially increase competition, on the terms stipulated by law.
Amendment No. 17 refers to the changes introduced within the law subsequent to the amendment of the Standard Contract Law – 2010, dealing with the examination of a standard contract.

## INTERNATIONAL TRADE

Israel has extensive business relationships worldwide. The table below summarizes Israel's international trade in 2017 (including diamonds).

| | Exports | | Imports | |
|---|---|---|---|---|
| | US$ million | % | US$ million | % |
| **GRAND TOTAL** | **60,573.2** | **100%** | **65,804.5** | **100%** |
| **EUROPE - TOTAL** | **19,481.1** | **32.2%** | **35,515.4** | **54.0%** |
| **European Union** | **15,758.8** | **26.0%** | **27,362.8** | **41.6%** |
| Italy | 958.3 | 1.6% | 2,693.7 | 4.1% |
| Belgium and Luxembourg | 2,526.7 | 4.2% | 4,066.6 | 6.2% |
| Germany | 1,519.9 | 2.5% | 4,069.6 | 6.2% |
| Netherlands | 2,139.6 | 3.5% | 2,700.8 | 4.1% |
| United Kingdom | 3,909.1 | 6.5% | 3,667.9 | 5.6% |
| Spain | 896.1 | 1.5% | 1,577.3 | 2.4% |
| France | 1,448.0 | 2.4% | 1,690.3 | 2.6% |
| Other EU countries | 2,361.1 | 3.9% | 6,896.6 | 10.5% |
| European Free Trade Association (EFTA) | 1,524.4 | 2.5% | 4,468.1 | 6.8% |
| Switzerland | 1,466.4 | 2.4% | 4,288.1 | 6.5% |
| Other European countries | 2,197.9 | 3.6% | 3,684.5 | 5.6% |
| Ukraine | 160.9 | 0.3% | 107.8 | 0.2% |
| Turkey | 1,297.7 | 2.1% | 2,601.7 | 4.0% |
| Russian Federation | 620.3 | 1.0% | 938.9 | 1.4% |
| Other countries | 119.0 | 0.2% | 36.1 | 0.1% |
| **ASIA - TOTAL** | **15,611.9** | **26%** | **17,321.6** | **26%** |
| India | 2,399.5 | 4% | 1,768.7 | 3% |
| Hong Kong | 4,435.5 | 7% | 1,977.4 | 3% |
| Taiwan | 696.0 | 1% | 784.4 | 1% |
| Japan | 759.2 | 1% | 2,354.2 | 4% |
| China | 3,327.8 | 5% | 5,896.2 | 9% |
| Singapore | 450.6 | 1% | 1,519.2 | 2% |
| South Korea | 580.0 | 1% | 1,316.3 | 2% |
| Thailand | 409.3 | 1% | 621.0 | 1% |
| Other countries | 1,808.3 | 3% | 685.2 | 1% |

| | Exports | | Imports | |
|---|---|---|---|---|
| | US$ million | % | US$ million | % |
| **AFRICA - TOTAL** | **885.3** | **1%** | **238.6** | **0%** |
| **AMERICA - TOTAL** | **19,987.9** | **33%** | **9,417.0** | **14%** |
| **North America** | **18,564.2** | **31%** | **8,528.2** | **13%** |
| United States | 17,589.0 | 29% | 8,076.3 | 12% |
| Mexico | 380.7 | 1% | 168.7 | 0% |
| Canada | 594.5 | 1% | 283.2 | 0% |
| **Central America** | **218.7** | **0%** | **99.8** | **0%** |
| **South America** | **1,205.0** | **2%** | **789.0** | **1%** |
| **OCEANIA - TOTAL** | **567.6** | **1%** | **198.0** | **0%** |
| UNCLASSIFIED COUNTRIES | 4,039.4 | 7% | 3,113.9 | 5% |

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

The rate of incoming tourism decreased by 1.2% in 2017, compared with the previous year. The table below illustrates tourist traffic to Israel in recent years:

**VISITORS ARRIVALS**

| 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 |
| 2016 | 3,070 |
| 2017 | 3,612 |

Source: Central Bureau of Statistics Israel, Arrivals and Departures of Israelis and visitors from abroad, 2018.

Israel has extensive business relationships worldwide. The rate of incoming tourism decreased by 1.2% in 2017, compared 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, the Free Trade Area Agreement (FTA) with the United States, the Free Trade Area Agreement with the European Free Trade Association States (EFTA), and the Free Trade Agreement with MERCOSUR the South-American Common Market. These 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 all 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 has also 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 has 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.
This 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

This Agreement between Israel and EFTA countries became effective on January 1, 1993. It is an Agreement 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 agreements mentioned above.

### Israel-MERCOSUR Free Trade Agreement

A Free Trade Area Agreement between Israel and the Common Market of South America, the Argentine Republic, the Federative Republic of Brazil, the Republic of Paraguay and the Oriental Republic of Uruguay (MERCOSUR).
This 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, providing Israel with a relative advantage in trade, compared with 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. This Agreement expresses the parties' intention to gradually eliminate duties on industrial goods and some agricultural products. The special 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 vice versa, without breaching any "rules of origin".

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

## PROPRIETARY RIGHTS

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

### Patents

The Patents Law, 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 an innovative process, which was never previously used or published.

### Trademarks

The Trade Marks Ordinance, 1972, regulates the protection of trademarks in Israel. This protection is granted for an initial period of ten years, and may subsequently be renewed for additional periods of 14 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 Israeli Copyrights Law regulates the protection of original literary, musical, artistic, and dramatic works. This 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 non-profit organizations for disabled persons, and the organization in question may also deliver an adapted work to a disabled person or other organization in or outside Israel (subject to the restrictions prescribed in this law).

### Commercial Torts

The Commercial Torts Law, 1999, is relatively new in the field of proprietary rights, and still in its infancy within Israel's businesses 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 in a business, passing-off, false description and so forth. The innovativeness of the Commercial Torts Law applies especially with regards to the remedies enacted by it, for example: the Anton Pillar court order.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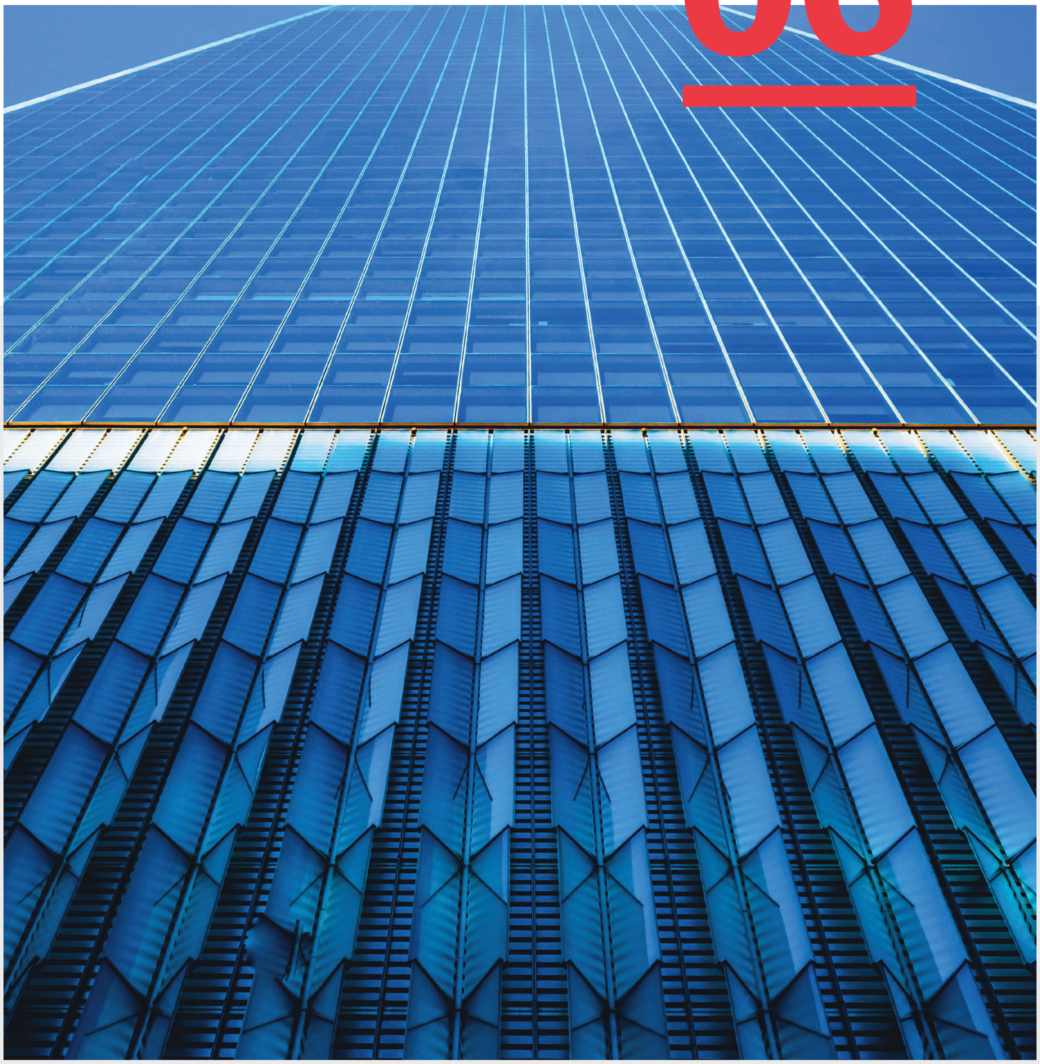
# INVESTMENT INCENTIVES & TRADE ADVANTAGES

# 06



## GENERAL

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, 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.
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, Korea, and more.
Additionally, to promote disprivileged economic regions within Israel, benefits are granted in a two differential manner (Zone A, and the rest of Israel). Incentives are higher 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 also eligible for benefits anywhere they are established, provided they comply with the relevant criteria (see below).

## ENCOURAGEMENT OF CAPITAL INVESTMENTS LAW

### Overview

The government's principal tool in this respect is the Encouragement of Capital Investments Law, 1959 (hereinafter: "the Law"). As part of the Supplement to the Economics Arrangement Law (enacted in conjunction with the
2011-2012 budget) (hereinafter: "the 2011 Amendment") recently ratified, significant changes were introduced to the application of the Law. The new tax benefits track will apply to income generated from January 1, 2011 and on (for details of this law's previous provisions, please see "Doing Business In Israel 2010"). It should be noted 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 under the 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 with the previous law, according to which a company could not benefit from both at the same time). Under the tax benefits track, an eligible enterprise was granted a "beneficial enterprise" status under the previous "preferred enterprise" law. However, under the new Law and the grant track, such enterprise is given the status of "approved eterprise". This Law applies to industrial enterprises (in diverse branches such as: textile, food, electronics, chemicals, pharmaceuticals, computer software, biotechnology, nanotechnology, renewable energy, R&D etc.), hotels and other tourism ventures, 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 inside Israel. 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 these benefits is compliance with an export rate of at least 25% of the industrial enterprise's turnover, as outlined below.

### Tax Benefits Track

As part of the 2011 Amendment, all the existing tax benefits were canceled, and a unified tax rate was introduced on the aggregate revenue generated from manufacturing activity, applying to industrial enterprises in compliance with the export threshold conditions established. The applicable tax rates are as follows (folowing a few amendments) –

### 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 implement them independently 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, whose business is controlled and managed in Israel, expecting "family companies", "transparent companies" or a Kibbutzim. The Law will also apply to registered partnerships, provided that 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" with regards to this particular activity.

| Tax Year | Tax rate for companies – Zone 'A' | Tax rate for companies – Zone 'other' |
|---|---|---|
| 2011–2012 | 10% | 15% |
| 2013 | 7% | 12.5% |
| 2014–2016 | 9% | 16% |
| 2017 and on | 7.5% | 16% |

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 preceding the benefits periods.

2. The enterprise must have an industrial plant.

3. The enterprise is competitive and contributes to gross local production. An enterprise will be deemed to have complied with this condition if it is engaged in biotechnology, nano-technology or renewable energy R&D, and has obtained the approval of the Head of Industrial R&D Administration. Alternatively, an enterprise will be deemed to have complied with this condition if its exports amount to at least 25% of its turnover in case of a new plant, or the expansion of an existing one. This is in contract with the previous law, in which the minimum requirement for expanding a plant was a measurement of the increased turnover in comparison with the basic revenue. Under certain conditions, an enterprise with "indirect imports" may also be deemed as being in compliance with this condition.
Only income from operations in Israel may be considered as "preferred income".
As mentioned earlier, the tax benefit track does not require prior approval from the authorities. However, in order to provide greater certainty, an enterprise choosing the tax benefits program may apply to the tax authority for an advanced (or preliminary) ruling whereby the company complies with the terms stipulated by the Law, in addition to regulating other issues involved with 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 Zone A and 8% in all other zones, for a period of up to 10 years.
In 2017, a new route was established for "Technological Preferred Enterprises", in which Israeli companies are receive a more favorable tax rate than that shown in the table

above, such as – 12% in Zone "other". In addition, there are special tax incentives for "huge multinational corporations", in accordance with the Law, operating in Israel through a subsidiary, such as - a corporate income tax rate of 6%, and dividend tax rate of 4%.

### Transitional Orders:

- The previous law is applicable to enterprises whose investments started prior to December 31, 2010, and have notified the authorities that the "election" year for the benefit period would be no later than 2012.
- The previous law also applies to old programs, based on the benefits prescribed by law on the “election” 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. This notice must be sent no later than the date specified for filing their annual statement. The law will apply to the fiscal year following the one for which the statement was filed.

Following the foregoing, an enterprise may pursue the new tax track starting from 2011, provided that the authorities are notified accordingly in the context of the 2010 financial statement.

### General

- According to the 2011 Amendment, the stipulation prohibiting multiple benefits (tax track and grants track) has been withdrawn. As such, industrial enterprises in compliance with the required export conditions may benefit simultaneously from both the grants and the tax benefit track, as discussed earlier. However, in the event that export conditioned applying to revenues are deemed as an "expansion" of previous activity, the enterprise may still benefit from the grant track even if tax benefits do not apply. Eligibility for investment grants are limited only to industrial enterprises located in Priority Zone A. The grant program is limited to the budget framework approved annually for this track under the budget law.
- Approved Enterprises are entitled to receive 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 targets defined. Furthermore, the Investment Center Administration is 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 that 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 set by Law, may be added to the costs. The investment program must be completed within 5 years of the date of approval.

The grants are not considered as 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 complied with this condition if it is engaged in the fields of biotechnology or nano-technology and has obtained the

1Hotel and other tourism ventures remains under the previous law orders.

approval of the Head of Industrial R&D Administration to this effect. Alternatively, an enterprise will be deemed to have fulfilled this condition if exports amount to at least 25% of its turnover.
In the event that a plant was expanded, an enterprise will be deemed to have complied with 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 is required to export 25% of its turnover. An enterprise with "indirect exports" may, under certain terms, also be deemed to have complied with this condition.
It should be noted that under the grant program, is required to fund 24% of the scope of the approved investment in equity.

### Approval Procedure

As mentioned above, 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 grant program, a company is required to submit a plan to the Investment Center.
The Investment Center Administration is authorized to approve applications received during the relevant budget year in the context of the current or the previous year's budget. Lately, in accordance with the comprehensive amendment of the Law, the terms for obtaining concessions were stipulated both in respect of grants and in respect of tax benefits. Consequently, the procedures for granting the status of "Approved Enterprise" differ. Whereas an enterprise applying for grants are required to submit a plan to the Investment Center, this will not be required of an enterprise wishing to benefit from tax concessions under the status of "Preferred 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 entities for a 5-year period, unless substantial changes are introduced, or if erroneous reporting has been discovered in the enterprise.

### Determining Priority Zones A and Other Areas

In accordance with the provisions of the Law for the Encouragement of Capital Investments Law, development areas 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 minority settlements (settlements where 80% of the residents are non-Jews).

For a detailed review of the above, please see the Ministry of Economy's website:
http://www.tamas.gov.il/CmsTamat/Ishuvim.aspx

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

## DEPRECIATION

The regular Depreciation rate set in the Income Tax Regulations (Depreciation), 1941 ("Depreciation Regulations"). Under the Depreciation Regulations, the main depreciation rates are as follows:

### Accelerated Depreciation

Approved, beneficial, and preferred 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 the date of commencement of operation rather than from the asset's purchase date, and its implementation depends on the type of each particular asset, as well as various rules.
Furthermore, special provisions were enacted in the Encouragement of Industry (Taxes) Law, 1969, to grant

preferred enterprises accelerated depreciation. The Income Tax Regulations (Inflationary Adjustments) (Depreciation Rates), 1986, provides special depreciation rates to industrial plants and hotels in respect of 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 Encouragement

| | |
|---|---|
| If the equipment is used in one shift | 20% (or 15%) |
| If the equipment is used in two shifts | 30% (or 18%) |
| If the equipment is used in three shifts | 40% (or 22%) |

of Industry (Taxes) Law. An ''industrial company'' is defined as "an Israeli resident company 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

| | |
|---|---|
| If the equipment is used in one shift | 30% for four years and the rest on the fifth year |
| If the equipment is used in two shifts | 40% for three years and the rest on the forth year |
| If the equipment is used in three shifts | 50% for two years and the rest on the third year |

engaged primarily in production. This regulation offers a depreciation rate of 5% for buildings owned by industrial companies, which function as industrial plants.
Regarding equipment, section 2 of the Regulations provides depreciation rates as follows:
Alternatively, a company may choose the devalued balance method, in which depreciation is calculated as part of the devalued balance of the asset as of the beginning of the 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

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

#### Individuals

An amount paid out by an individual or their relatives for investing in a "special purpose company", who is allotted company shares in an amount equal to no more than ILS 5 million. These are made deductible against the individual's overall income in three equal annual installments (or less), of the fiscal year in which capital had been invested. Among other things, it is required is that the capital invested is paid between January 1, 2011 and December 31, 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 in 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 "beneficial company" as defined in the Encouragement of Capital Investments Law, is entitled to deduct the cost of shares acquired during the period between January 1, 2011 and December 31, 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 cost of the acquisition. The Law specifies a number of conditions for applying the deduction, including a condition according to which the investment must 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 beneficial 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 paid during the acquisition year and in each

**In 2016, the Israeli legislator announced a new and more simplified route for tax deduction.**

acquisition years both by the acquiring as well as the entitling company. For the purpose of deduction, approval must be obtained from the tax authorities that the purpose of the investment is neither the avoidance of tax nor the reduction of the tax liability. The law stipulates additional conditions for the tax deduction.

## ENCOURAGEMENT OF CAPITAL INVESTMENTS IN THE TOURIST INDUSTRY

It should be noted that the previous law benefits (both in the tax benefit track and in the grant track) are applicable to hotels, accommodation facilities, and other tourist attractions. Since Amendment 60 to the Law (from 2005), only conditions for "foreign resident accommodation" are eligible to receive 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 by foreign residents. This condition does not apply to tourist attractions.
According to the Law, benefits may be claimed on the construction or expansion of a "tourist facility for overnight stays".

The legislator provided a distinction for the meaning of the term "tourist facility for overnight stays", stipulating that such a facility must be: "A structure comprised of 11 or more rooms, providing overnight services to guests passing by, as well as for fixed periods of time, together with accompanying services including catering, entertainment and leisure services".

As indicated above, a wide range of overnight accommodation services and other facilities are eligible to receive 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 comply with the condition of the number of rooms stipulated by Law.
It should also be noted that the map of priority zones applicable to tourist facilities is different from the map of priority zones applicable to the industrial sector. Thus, with regards to hotels, it was determined that, among others, Development Zone A includes the Western and Upper Galilee, around the Sea of Galilee, Nazareth, Haifa, along the Carmel Shore, Nethanya, Ramla, Jerusalem and Jerusalem Corridor, and the Southern Region, not including Eilath and the Dead Sea.

### Investment Grants

An entrepreneur wishing to establish an 'overnight tourist facility' is entitled to receive 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, minus land costs. The investment grant is not offered automatically; the entrepreneur must submit a detailed preliminary application to the Investment Center Administration at the Ministry of Tourism. Based on established criteria, the application must address 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 grants mentioned above, the regulations prescribe a number of tax benefits for approved tourist facilities, the main one, in our opinion, being accelerated depreciation on investments in a tourist facility structure.

#### Tax Benefit Track for Overnight Tourist Facilities

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

1. The facility must be owned by an Israeli company not fiscally "transparent" for tax purposes.

2. The capital financing the establishment or expansion of the hotel was invested there in a minimum amount prescribed by Law.

Under the tax benefit 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 a 10-year exemption in priority Zone A, a 6-years exemption in Priority Zone B, and a 2-year exemption in the rest of the country. Accelerated depreciation and reduced tax rates (tax on the shareholders' level for the receipt of dividends is

generally 15%). An alternative track is available In Priority Zone A, with a final 11.5% tax on undistributed profits on the company's level for increase in turnover and (no additiona taxation on the company's 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. For this reason, those who build and rent out apartments are eligible to receive 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 Encouragement of Capital Investments Law. The second and relatively new law is the Encouragement of Rental Housing Law, enacted in 2007. In effect, following its stipulation, two parallel legal systems were created to encourage the building of rental apartments, and an assessed may operate to apply one of them. According to Chapter Seven-1, tax incentives are granted in respect of a building in compliance with the terms of the "Rental Building" designation, or the "New Rental Building" designation. This is usually one whole or several buildings located in one complex, approved as such by the Investment Center Administration.

It should be noted that there are entitlement conditions for actual tax benefits, including, among others: the size of a minimum rental area, minimum rental terms, compliance with monthly rent limits, restrictions on the sale of part of a building for a specific term, etc. The Encouragement of Rental Housing Law, 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 granting them a full exemption from Appreciation Tax.

Unlike Chapter Seven-1, this track requires no prior government approval. It should be noted that this law, too, sets entitlement conditions for obtaining actual tax benefits, including among other things: minimum number of apartments in a building, minimum rental fee, minimum rental term, restrictions on the sale of a building etc.

Below is a review of the scope of tax benefits available between these two legislative systems. (This review will only address the provisions applying to a "New Rental Building" as per Chapter Seven-1).

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

**Dividend:** a 20% tax (since 2014) is applied to 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. It should be emphasized that these tax rates apply to betterment accumulated for the entire period, and not merely from the effective date (November 7, 2001). It should also be noted that Section 72A of the Property Tax 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%.

**VAT Benefit on the Sale of a Building:** Section 31(a) of the Value Added Tax Law sets 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.

**VAT on Apartment Rental:** The exemption specified in Section 31(1) of the Value Added Tax Law applies with regards to rental housing for a period of no more than 25 years.

### Encouragement of Rental Housing Law

**Rental Income:** at the corporate tax rate, which is currently 25%.

**Dividend:** Tax rate as stipulated in Section 125-b of the Ordinance or 126(b) of the Ordinance.

**Income from the Sale of a Building (Appreciation Tax):** Tax exemption on a sale will only apply if the rental building has been fully sold. No exemption will apply on the sale of individual apartments or on parts of a building, or upon the sale to a relative. The full exemption will apply only following a rental term of 25 years. If the building is sold earlier (provided this is not before the termination of such rental term of 10 years), it must be sold only to a company that undertakes to continue renting it for an additional term, such that the total of rental terms would reach 25 consecutive years.

**Accelerated Depreciation:** at the rate of 20%. The term "depreciation" refers to the structure component without the land. In regions where the land component is high, the benefit pertaining to depreciation will only amount to the cost of the structure - a fact likely to impact the feasibility of a project. To take the fullest advantage of accelerated depreciation, the company must show positive income in the amount of losses from the rental of structures throughout the first five years of rental at least.

**VAT Benefit on the Sale of a Building:** Non-existent.

**VAT on Apartment Rental:** The exemption specified in Section 31(1) of the Value Added Tax Law will apply with regards to the rental of residential apartments for a term of up to 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. Each loan extended to a single business is for approximately ILS 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 ILS 100,000,000.
- The loan must be used solely for new activities: establishing a new business or expanding an existing one. The funds should not be used for the purchase of real estate, construction activities, or an existing business.
- Paid-in capital should not be 10-25% of the amount 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 sale turnover of ILS 22-100 million. The scope of collateral security required is 25%, while the government extends a guarantee of up to 70% of the loan amount. In addition, the owners' personal guarantee is required. The loan is for a term of up to five years, with an extended grace period of one year for repayment of the principal. Interest is at the customary rate used by the banking system on such loans. The fund is operated by commercial banks.

### Assistance to Industrial Enterprises in Financial Difficulties

In accordance with a government resolution, a committee of Ministry director-generals was formed to review industrial enterprises and submit recommendations to a ministerial team. Government assistance is conditional on an independent investment in the enterprise, or a recovery plan including additional funding from the owners. An external examiner appointed by the committee reviews applicant enterprises and their compliance with specific criteria, including:

- A recovery plan, its economic feasibility, the financial justification of the enterprise's long term existence, and its ability to introduce recovery measures within a specific period of time.
- The lateral implications.
- The number of employees and a 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 ILS 10 million, and may disqualify the enterprise's eligibility for further government assistance. However, should the enterprise apply for other financial assistance from a government entity, then it would be obliged to repay the loan.
- The salaries of managers and employees must not exceed ILS 50,000.

If the applicant enterprise 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 provide guarantees for 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 receive up to 150 hours of tutorship; small businesses (5-10 employees) are entitled to receive up to 100 hours. Very small businesses (up to 4 employees) are entitled to receive 20 hours only.
In addition, the managers of very small businesses may participate in special courses at Small Business Development Centers, designed to develop their managerial skills. The Ministry of Agriculture allocates funds for “tutelage” of agricultural businesses.

### Employment Grant Program

In order to complement the revised Encouragement of Capital Investments Law, the government has decided to establish an additional program to increase employment in remote areas of Israel, as well as specific centers with high rates of 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 this program, these enterprises are 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 are 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 ILS 120,000 per employee for the entire period. Minority and Ultra-Orthodox towns - as above.
Enterprises paying wages below ILS 6,750 are entitled to receive more than ILS 60,000. Notwithstanding the above, the total average support granted to each enterprise will not exceed ILS 100,000 per employee. The eligible areas are:

Priority Development Zones A and B, and designated towns for minority populations (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 - ILS 6,750 ILS monthly wage.

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

### Intra-Plant Training

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

### Quality Management Project

This 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

This fund is designed to help industrial enterprises gear up for competition following exposure, and assists them in increasing imports and reducing customs and import duties.

> Support will be provided for the establishment or expansion of industrial plants, telephone call centers, computer service support centers or logistic centers.

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 pay Israeli income tax at a rate of up to 25% during the first three years of employment. This period may be extended by one 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 Encouragement of Capital Investments Law, Israeli and foreign entities fully-owned by foreign investors, whose paid-in capital exceeds US $30 million, at least 75% of which is applied for "qualifying activities", are entitled to receive a special status as 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.

The Ministry of Finance's 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 are declared as a free trade zone. The major benefits are as follows:

- Companies which provide services and/or are residents of 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 located (only) in the free port zones are eligible for benefits, granted in addition to other benefits 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 ports zones has not been enacted.

### Free Processing Zones

In June 1994, the Free Processing Zone Law was enacted. However, it's almost certainly expected to be amended in the near future. The first zone under this law is currently in its planning stages, and is planned to 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 concessionaires and enterprises operating in these zones are as follows:

- Companies are fully exempt from any direct tax for up to 20 years. Other entities are subject to a 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 Israel government provides cash grants of usually up to 50% of approved R&D expenses. The approval of R&D programs and actual expenses is under the responsibility of the Chief Scientist's Office at the Ministry of Economy. The research committee may approve a participation grant of 20%, 30%, 40%, or 50% of total R&D expenses. Enterprises located in National Priority Zones are entitled to receive a 10% grant.

Startup companies may receive certain alleviations.

There are several incentive plans under the sponsorship of the Chief Scientist's Office. These include:

- 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, for the purpose of developing key technological infrastructure. Magnet also supports the integration of advanced technologies into the industry through user associations. Grants of 66% of the total approved R&D costs for industrial entities, and up to 80% of the approved costs for academic institutions are available, with no royalty requirements.

- Magneton: This program is similar to Magnet; however, it encourages cooperation between a single academic institution and one industrial enterprise. The available grant is up to 66% of the approved research budget office, including the following:

- **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 designed to support applied academic research which is not yet ready for business involvement. Activity is performed at 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 receive grants.
If the R&D program is successful, royalties are paid 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 until the grant is fully repaid, linked to the LIBOR+1%. If production is relocated overseas, the Chief

> Technological incubators provide a supportive framework, enabling innovative entrepreneurs to develop their ideas into a commercial product.

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 the event of projects, sponsored by the Chief Scientist, selling technology, know-how, or any other right derived from such technology, to enterprises outside Israel, then 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 must not be higher than the amount of the grants given 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 the sale of the supported technology or know-how, and up to 600% of the grant received if R&D discontinue is 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 ILS 200,000 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

Technological incubators provide a supportive framework, enabling innovative entrepreneurs - Israeli nationals 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 receive grants of up to 85% of the approved program or 100% in peripheral incubators. The grant is limited to ILS 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 first year, up to 80% in the second year and up to 75% in the third year. The approved budget for up to 3 years cannot exceed ILS 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 business with adequate infrastructure for biotechnological R&D, administrative staff and accessibility to consultation 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, as well as the European Union. These agreements were signed for the purpose of fostering ties between Israeli and foreign companies, designed to facilitate joint ventures in the R&D, manufacturing, and marketing fields. Agreements of this kind were signed with the United States, Canada, European Union member countries, and Asia.

### The Seventh Framework Program of the European Union's Commission on Science and Technology

The European Union's Seventh Framework Program for Research and Technological Development (FP7) was a 7-year program, active from 2007 to 2013. Its budget was Euro 50 billion. Priorities covered by FP7 include life sciences, genomics, and biotechnology for health, information society technologies, nanotechnologies, and nanosciences, "intelligent" materials, new production processes and devices, aeronautics and space, food quality and safety, sustainable development, global change and ecosystems, citizens and governance, and other promising research areas.

Research institutes and companies in associated EU countries are eligible to receive fundinging for joint projects, in partnership with EU countries. The projects must be trans-national, i.e., only consortia of partners from different member and associated countries can apply. The coordinating office is ISERD.

### 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-US 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% of the amount of the grant.

CIIRDF: The Canada-Israel Industry and Research Development Foundation was founded in late 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. In its initial stage, each country deposited an annual amount of US $2 million to a grant fund, with the aim of increasing 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). This fund is a Korean non-profit organization run by representatives from both countries. Each country deposited an annual amount of US $1 million into the fund for the first three years of activity, for the purpose of financing bi-national R&D projects. The fund finances 3-year R&D 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

US: Israel Science and Technology Commission - the Commission was a joint initiative of the late Prime Minister Itzhak Rabin and United States President Bill Clinton. Its purpose was to further collaboration between Israel and the United States, and to add a new dimension to scientific and technological cooperation between Israeli and US 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-US Bi-national Science Foundation provides assistance to scientists and startup 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.

> **The Israeli government has entered into a number of R&D cooperation agreements, to foster ties between Israeli and foreign companies designed to facilitate joint ventures in the R&D, manufacturing, and marketing fields.**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