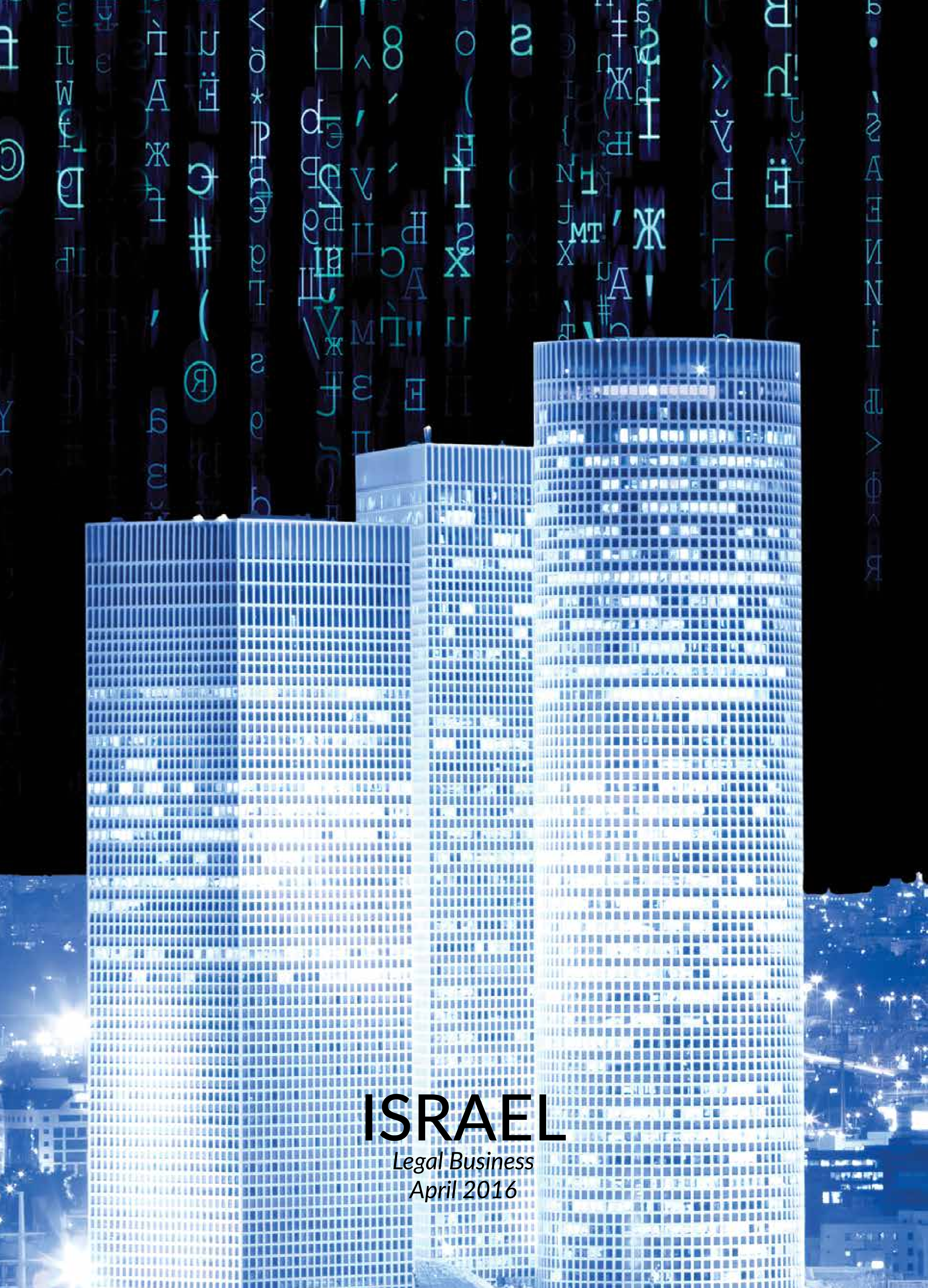

ISRAEL

Legal Business

April 2016

Value range

Investment is pouring into Israel's technology sector. Can increased capital take Tel Aviv's high-growth stars global?

CHRIS CROWE

Israel's regional tensions contrast with optimistic hopes for foreign investment and a burgeoning economy. While war still rages over the border in nearby Syria, Israel's start-up and hi-tech sector is flourishing. In addition, its nascent natural gas industry finally looks primed for substantial development.

Life is good in Israel's commercial capital Tel Aviv, says Barry Levenfeld, a partner at Yigal Arnon & Co: 'Economically and politically, Israel remains stable, while our neighbours are more dangerous by the minute. Sitting here on the 47th floor in Tel Aviv, looking across the Mediterranean and with all the restaurants and coffee houses below, you just wouldn't know that any of this was going on.'

Israeli start-up companies raised a record \$4.43bn in 2015, according to Israel Venture Capital (IVC) Research Center, the figure contrasting with a slowdown in venture funding in the US and other start-up hotspots. IVC says hi-tech exits increased by 16% in 2015 to \$9.02bn.

Israel continues to ride high in the investment stakes thanks to its dynamic start-up community, but also because Israeli growth stars are often seen as better value to many international investors tired of over-sold tech firms.

Simon Jaffa, a founding partner at Barnea & Co, has just returned from an extended visit to the west coast of the US, where he argues he saw an unprecedented eagerness for the Israel growth story. Jaffa says that the large number of prominent Israelis that have entered Silicon Valley and other growth company centres in recent years are helping to fuel this enthusiasm for Tel Aviv as a global tech hub. 'There is a dynamic flow of information and transactions between the US and Israel, and this is significant because many perceive a slowdown in the US market,' he remarks. Jaffa maintains that valuations remain relatively subdued because foreigners are naturally wary of the geopolitical situation and feel that prices should be lower on account of regional volatility.

That said, any residual concerns have hardly dampened investment flow, not least because Asian investors are following suit.

It means the Israeli legal community has become alive to the Start-up Nation moniker and is now taking a lead from Silicon Valley.

Jaffa says his firm looks to west-coast legal icons such as Cooley, Fenwick & West, Gunderson Dettmer and Wilson Sonsini Goodrich & Rosati for inspiration, particularly in their willingness to take risks in offering discounted or free legal advice for companies they see as prospects to be the next big thing. Jaffa says that start-ups tend to stick with their traditional legal counsel throughout their lifecycle and sees potential parallels for Israel's legal community. '[US law firms] are waiting for the next Steve Jobs or Mark Zuckerberg to come through the door. We need to make that assessment of the start-up and there is a degree of risk in that. If you want to be working in the technology sector, you have to be prepared to take that risk.'

TECH CRAZY

A willingness to 'invest' in your growth clients doesn't always come easy to legal professionals, but it is a strategy that is becoming increasingly dominant in the entrepreneurial Tel Aviv market. So much of the domestic ▶

economy and cross-border investment is driven by hi-tech and start-ups. Amazon.com launched a research and development (R&D) centre in Israel last year, following the example of other tech leaders, such as Cisco, Apple, Google and Facebook. Cisco has spent more than $1.5bn in acquiring ten Israeli start-ups, according to the Israeli newspaper *Haaretz*, and has invested in around 25 others.

Nitzan Hirsch-Falk, a partner at Israeli law firm H-F & Co, says that US tech companies often struggle to find the right legal talent to develop an R&D centre, and can take advantage of a globally-cheap and highly-educated workforce in Israel.

Israel's start-up community is constantly expanding. MassChallenge, the Boston-based start-up accelerator, launched a Jerusalem branch in January this year. Doron Stern, a founding partner of Tulchinsky Stern Marciano Cohen Levitski & Co, says that MassChallenge accelerator is a venture intended to transform the lives of lower-income orthodox Jews and Arabs that populate the vicinity.

Until recently, the vast majority of the start-up community has existed in Tel Aviv and the surrounding region. But growth is pushing the industry into other areas, such as Jerusalem and Beersheba in southern Israel, the latter being a flourishing sector for cyber security firms. Many of the nation's military and former military personnel, having been intensively trained in cyber defence, are now part of the growing tech scene in Beersheba.

Ram Toren, a partner at Gideon Fisher & Co, says that Tel Aviv has become too expensive for some businesses that are now seeking cheaper real estate and labour costs. 'There is a big shift towards the south. The mayor of Beersheba is helping to build it into a hi-tech area and there are government incentives for people to move there.'

'Economically and politically, Israel remains stable, while our neighbours are more dangerous by the minute.'

Barry Levenfeld, Yigal Arnon & Co

A more dispersed economy may represent additional challenges to the legal sector, but Levenfeld is comfortable with it, saying that Jerusalem is only a 40-minute drive from Tel Aviv without traffic, similar to travelling from Palo Alto to San Francisco on the west coast of the US.

'I never thought there would be a hi-tech future for Jerusalem, but now I am a believer,' he says. 'There seems to be a buzz that wasn't there before.'

FOREIGN ENTHUSIASM

Israel's buzzing economy continues to capture attention across the world, including China and the far East, in hi-tech industries and beyond. Last year, China's Bright Food acquired a 77% stake in Tnuva, the largest food manufacturer and distributor in Israel, from Apax Partners for $1.07bn. Herzog Fox & Neeman advised Apax with FBC&Co representing Bright Food.

Jonathan Morris, head of corporate at Berwin Leighton Paisner, says that the Chinese and other Asian jurisdictions are also enthused by Israel's dynamic business culture, but also the ability to find relative bargains in acquisitions: 'Investments are both direct and indirect. We see companies coming in and acquiring entire companies, taking a majority stake or even establishing an incubator. Israel is developing cutting-edge technology, whether it is cyber, fintech or medtech. Israel is not somewhere that you can ignore and the valuations are more sensible than in other jurisdictions.'

Morris is seeing a growing interest from other Asian jurisdictions such as Singapore, Japan and Korea. Elie Sprung, a partner at Tadmor & Co Yuval Levy & Co, believes that Asian investment so far is only the 'tip of the iceberg'.

Israel is in investment mode itself. Last year, Teva Pharmaceutical Industries, the world's largest generic drug maker, launched an

‘US firms are waiting for the next Steve Jobs or Mark Zuckerberg. We need to make that assessment of the start-up and there is a degree of risk in that.’
Simon Jaffa, Barnea & Co

▶ audacious $40.5bn bid for Ireland-based Allergan. Tulchinsky and Sullivan & Cromwell advised Teva, with Latham & Watkins representing Allergan.

Despite the cooling of the capital markets in 2015, international investors still have an appetite for Israeli companies. In March, ZAG-S&W, a joint venture between Zysman, Aharoni, Gayer & Co and US-based law firm Sullivan & Worcester, advised two Israeli-based companies, Nano Dimension and LabStyle Innovations Corp, on their Nasdaq listings.

The regularity and size of cross-border deals is forcing Israel’s legal community to ‘learn new perspectives’ says Tulchinsky’s Doron Stern: ‘We are learning how to cope with the different expectations of China, South Korea and other jurisdictions.’

Internationalisation has also intensified the emphasis on English language skills. Even the smallest Israeli start-ups have their corporate documents drafted in English to make them more attractive targets. Guy Ne’eman at Ne’eman, Keynan & Co says that he ‘hardly engages in Hebrew anymore’ as clients want ‘everything set up in English to welcome foreign investors’.

Clifford Davis, a partner at S Horowitz & Co and a former London associate at Jones Day, has worked on a series of recent export credit financings, including Bank Hapoalim’s $200m financing to the Ethiopian Sugar Corporation for a large-scale sugar-cane irrigation project to be developed by Netafim, the Israeli drip and micro-irrigation leader. Davis says that the firm needs to recruit more international lawyers to enable it to work on the growing number of cross-border transactions involving Israeli investors, acquirers and lenders. ‘These loan documents are not subject to Israeli law. They are subject to English law,’ he remarks, indicating that there is a growing demand for people that can ‘write perfect English’ particularly for ‘off-piste drafting’. He believes that Israeli clients still prefer to work with a local adviser, even on English and US law transactions, because charge out rates are less than a third of equivalent lawyers in New York and London. Gil White, a partner at Herzog Fox & Neeman, agrees: ‘The Israeli market is cosmopolitan by its very essence. The majority of transactions have an international element. This makes lawyers with international experience and training a valuable commodity.’

OPEN FOR BUSINESS

Further cross-border activity is poised to develop with greater regulatory clarity. The development of Israel’s nascent natural gas industry had slowed with uncertainty over the regulatory framework for market access. This had followed antitrust concerns about the dominance of Noble Energy and the Delek Group, and their control of all the gas reservoirs off Israel’s coast. Uncertainty stalling investment of offshore exploration and the commercialisation of the major Tamar, Leviathan, Karish and Tanin fields.

The new framework will help ensure that the recent gas discoveries will be developed, but will require significant divestitures by the incumbent owners and see new players coming into the market.

Under a new regulatory framework that is still subject to court approval, Noble and Delek are expected to sell their stakes in Karish and Tanin, with the buyer of these assets expected to develop them for the Israeli domestic market. In addition, Delek is required to sell all of its interest in Tamar within six years and Noble is to reduce its stake in the field

CONSOLIDATING MARKET SHARE

A desire for expansion has created a frenetic legal market, with a series of mergers and headline team moves in recent months. The volatile nature of the market also provided a major casualty in February when the well-regarded Zellermayer, Pelossof, Rosovsky, Tsafrir & Co shut its doors. Seasoned dealmaker Michael Zellermayer joined FBC&Co, after leading litigator and fellow name partner Eyal Rosovsky and his team moved to Meitar Liquornik Geva Leshem Tal Law Offices in January. Earlier, high-profile M&A partner Doni Toledano had switched to Erdinast Ben Nathan & Co. The demise of the firm sent a jolt through the local profession but is symptomatic of the unpredictable character of the market.

In recent years, a spate of mergers created relative legal giants Goldfarb Seligman & Co, Herzog Fox & Neeman and Meitar Liquornik, all with in excess of 250 fee-earners.

Anxieties over losing national and international status due to lack of size have become increasingly apparent. One partner in a leading smaller firm admits to worrying about the largest firms ‘pulling away’ and his practice ‘being left behind’.

In 2015, the merger trend continued with the union of Tadmor & Co and Yuval Levy & Co, creating 85-lawyer practice Tadmor & Co Yuval Levy & Co.

Opher Levy, co-chairman and co-managing partner of the new firm, says the merger created a larger firm that could offer a much broader suite of services and this was crucial to its ongoing credibility: ‘Foreign clients expect the law firms that they work with locally to have a one-stop shop and offer various practice areas that operate at the highest level.’

from 36% to 25%. This is intended to further incentivise the development of the Leviathan gas field.

Dan Hacohen, a partner at Agmon & Co Rosenberg Hacohen & Co, represents both Tamar and Leviathan consortiums, and expects a fervent movement in the gas sector, including further exploration, once the new framework is approved. 'There has been little new exploration activity recently. It has all been frozen until the regulatory environment is cleared up,' he says.

If further foreign investment in the energy sector is expected, the same is true for the wider economy. The long-debated anti-concentration law, that seeks to increase competition in Israel, is beginning to bite. Under the law, Israeli owners of financial sector businesses are restricted from holding industrial businesses. It is an attempt to dismantle the dominance of Israel's conglomerates.

'Israel is not somewhere that you can ignore and the valuations are more sensible than in other jurisdictions.'

Jonathan Morris, Berwin Leighton Paisner

According to Adir Waldman, Freshfields Bruckhaus Deringer's representative in Tel Aviv, this is encouraging Israeli businesses to expand overseas in place of domestic exposure. Major asset sales are also attracting foreign investors. 'Sentiment has changed and people have started to address the anti-concentration law, conform to it and bring it into their thinking. More Israeli business people are looking to invest abroad as they are conscious of not holding assets across sectors,' Waldman comments. 'If a business in the non-financial sector goes on sale today, you are likely to have fewer local bidders than you would have before the law. If you are in the FIG [Financial Institutions Groups] sector, you will be thinking about not buying a business today that you will not be able to hold in three years.'

Though businesses affected by toughened competition laws have until the end of 2019 to comply with the new regulations, there is already movement in the market with the major conglomerates hoping to avoid ▶

FOR A FEW SHEKELS LESS – FLEXI-LAWYERING HITS ISRAEL

Israeli lawyers are not shy of highlighting the quality of professional expertise that exists within the nation. It is common to hear claims that Israel's legal elite is on a par with the best that London and New York has to offer.

And just as sophisticated alternative service models are springing up in the UK, Israel's own LawFlex launched last year. Its pool of freelance lawyers is hired out to plug gaps at firms operating above capacity or where specific expertise is required.

While the same sort of model is well established in other jurisdictions and many international firms are attempting to formalise their use of alumni networks for similar resourcing, LawFlex's co-founder Jackie Donner Stocki says that the business has sated a latent demand. LawFlex has already grown to over 70 lawyers and Donner Stocki says it gives Israeli firms another option rather than joining the popular merger-and-rapid-growth trend.

The former London associate at Freshfields Bruckhaus Deringer began working in Israel at Epstein Rosenblum Maoz before leaving to become a freelance lawyer after having three children. Having launched LawFlex with Zohar Fisher, the head of Robus – Legal Marketing and Consulting Services, Donner Stocki says that the business is already working with 20 mid-sized firms and is now targeting the larger practices.

So far the business is more oriented towards the complex and higher-value work with the average LawFlex lawyer being seven-years qualified. Lower-value volume work is not the priority. LawFlex usually takes between 10% and 15% of the lawyer's hourly rate.

Donner Stocki argues that LawFlex can further eat into foreign markets, as its lawyers are largely internationally-trained and would charge 'a quarter of the price that they would be paid in England'. She adds: 'We have seven years-plus-qualified lawyers with impressive CVs that are charging 300 sheckels ($77) per hour.'

'I hardly engage in Hebrew anymore. Clients want everything in English to welcome foreign investors.'

Guy Ne'eman, Ne'eman, Keynan & Co

▶ a last-minute fire sale. Even so, recent transactions that have been linked to the new law have not all gone to plan. China's Fosun International abandoned its $462m acquisition of a controlling stake in Phoenix Group Holdings from Delek Group in February, blaming market turmoil. Fosun's chair Guo Guangchang was recently detained in connection with a corruption investigation and many in Israel are suggesting that the deal was blocked by Israeli regulators.

In January, Chinese investment house Macrolink Group also backed out of a deal to buy a controlling interest in Israel's Clal Insurance Enterprise, citing regulatory obstacles. IDB Group, the financially distressed Israeli conglomerate, had agreed a deal with the Finance Ministry to sell its 55% stake in Clal Insurance over a three-and-a-half-year period.

The deals are not thought to have damaged Israel's strengthening relations with China. 'I don't see this denting the enthusiasm for China-Israeli collaboration,' Morris argues.

Enthusiasm for Israel continues to outweigh its small population and economy, and largely withstood widely-broadcasted geopolitical tensions. 'Relative prosperity is around, but a lot of it comes from the way that business has matured,' Stern concludes. 'People tend to forget that this was a huge refugee camp only 30 or 40 years ago, and now it has transformed into a healthy and vibrant business arena.' **LB**

Litigation funding: Levelling the playing field

Kobre & Kim's Robert Henoch and Michael Ng discuss third-party financing

Outward-facing Israeli companies often find themselves facing off against larger, deep-pocketed adversaries, such as joint venture partners, investors, distributors, customers, licensees, or those who have infringed on their intellectual property (IP) rights. When this happens, well-financed opponents can leverage the threatened expenses of the legal process in their home countries to destroy the rights of smaller Israeli companies. Third-party litigation funding offers a potential solution for Israeli companies to vindicate their legal rights under such circumstances.

IN CROSS-BORDER DISPUTES – DAVID v GOLIATH

As most well-seasoned executives know, the costs of foreign litigation and potential recoveries can reach stratospheric heights. Even a small US patent litigation dispute can cost $2m to litigate and disputes with over $25m at stake can costs well over $5m. As such, despite their success, innovators from the 'Start-up Nation' remain vulnerable when cross-border legal disputes arise.

While foreign companies in the tech and life sciences industries are multinational conglomerates, with significant resources and experience with litigation, Israeli companies in those industries tend to be smaller start-ups with no litigation budget, limited legal sophistication and no understanding of how to enforce their rights.

THE SOLUTION: THIRD-PARTY LITIGATION FINANCING

Third-party litigation financing can help level the playing field. After tremendous growth in recent years, small companies now enjoy enhanced access to investment designed to help them through critical legal battles. Typically provided on a non-recourse basis in exchange for a share of the proceeds, litigation finance can be used to pay legal fees, other litigation costs and, in some instances, ongoing business expenses.

Litigation funding can mean the difference between a company folding due to the expense of litigation and that company preserving its legal rights. This is true in a broad array of disputes, including IP, contract, joint venture and trade secret matters going to the very heart of the company. For example, the benefits could be realised by an Israeli enterprise software producer facing off against an intransigent foreign licensee or a digital camera product start-up whose patents have been infringed in the US.

SECURING THIRD-PARTY FINANCING

Third-party funding is available for both court cases and international arbitrations involving a wide variety of legal issues.

> **'Despite their success, innovators from the "Start-up Nation" remain vulnerable when cross-border legal disputes arise.'**

Companies seeking funding should first develop a deep understanding of the potential return, the strength of their claims, the time until pay-off and the possible avenues to recovery. Some cases are more resource-intensive, while others are amenable to resolution through lower-cost mechanisms for dispute resolution. Some cases can drag on for many expensive years, while others can be resolved following early rulings on key issues. Parties seeking funding are therefore wise to secure cross-border litigation counsel with experience in third-party funding to assist them in assessing cases and negating appropriate terms.

The funding process typically begins with the identification and vetting of potential legal claims, including the development of a strategy for enforcement in a venue with jurisdiction over the matter. To comply with legal restrictions, funders generally cannot exercise control over the litigation. Instead, their rights are constrained to receiving updates about progress in the case. Next, discussions with potential funders are held under a non-disclosure agreement, with a presentation of the legal background and proposed enforcement campaign. Many funders will engage in extensive due diligence, often requiring a period of exclusivity. To protect against harm from the delay that may result, it is important to identify the right funder in advance and ensure that the case aligns with the funder's profile.

After due diligence, the parties will negotiate the terms of funding, taking care to adopt a structure suitable for the particular case. Funding is typically structured as debt that is secured by the proceeds of the litigation. In some disputes, the traditional contingency model is followed, with payment of all fees and costs in exchange for a percentage of the recovery. In other cases a line-of-credit model is used, with the funder entitled to a multiplier on amounts drawn down. In other models, the funder will stage its investment, with later funding rounds dependent on certain milestones being met. In most cases, the funders will require reimbursement of their investment from the first portion of the recovery, with subsequent portions of the recovery shared between the funder and funded party according to a formula or schedule.

There are pitfalls. Failure to match the funding structure to the litigation risks can diminish returns to the funded party. A company that seeks but fails to obtain funding can unwittingly and unwisely create a harmful record that serves as an obstacle to other opportunities. But when deployed wisely and on appropriate terms, litigation funding can be a powerful tool to leverage the otherwise inaccessible value of legal claims, and can result in substantial returns to small companies in Israel and elsewhere facing cross-border litigation with larger opponents.

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Does populism have a price?

HFN's Alan Sacks highlights the economic inequality issue

Despite the obvious successes of the Israeli business sector – driven by Israel's extraordinary achievements in the technology arena – there are clearly systemic problems in the economy. There are few who begrudge the sudden wealth of hi-tech entrepreneurs who secure an 'exit' for their technology and knowhow. The situation changes though when the disparity between rich and poor is highlighted, and when large sections of the public feel that a limited group of individuals is growing rich at their expense.

In 2011, many members of the public boycotted certain basic food items in protest against the high cost of living. The focus of the protest then turned to the small group of business 'tycoons' who had effectively acquired control over huge portions of the Israeli economy, largely on borrowed money. The result of this protest was the Anti-Business Concentration Law, which aims to break up multi-level corporate conglomerates, and ensure that significant financial and non-financial assets are not under common ownership. In parallel, to the undisguised joy of the financial press, a number of the tycoons have seen their empires collapse under the burden of debt.

The saga of Israel's natural gas monopoly rumbles on. Israel's huge offshore natural gas discoveries were heralded as a game-changer for the Israeli economy. Five years on, however, the public protest against the monopoly in the offshore gas reserves (the major discoveries are all held by the same exploration groups) continues. The government has shown unprecedented hesitancy and inconsistency in dealing with the situation, encouraging the suspicion that the government has some ulterior motive in supporting the monopoly. The final arrangement for exploiting and marketing the gas reserves was pushed through the Knesset (Israel's parliament) by the Prime Minister, virtually single handed. The High Court of Justice has now determined that the Prime Minister's action was unconstitutional and that the details of the 'Gas Arrangement' required the approval of the Knesset. Whatever the final arrangement, the uncertainty over the future of the exploration rights has delayed the exploitation of the natural gas reserves. Perhaps more significant will be the question of whether the government's behaviour, and its lack of clarity on issues such as royalty levels, rates of taxation, export quotas and so on, will deter foreign players from entering the Israeli natural gas market.

Next in line for criticism were the Israeli banks and, in particular, the two major banks that dominate Israel's highly concentrated financial sector. Finance Minister Moshe Kahlon (who made his political name by introducing competition into the mobile telephone sector) came into office promising to open up the finance sector to competition. At the time of writing, a committee established by the Minister is yet to publish its final recommendations for increasing competition in the finance sector. However, the interim recommendations of the committee (for example, forcing the banks out of the profitable credit card sector, and encouraging new sources of credit for the domestic and small business markets) were provocative enough to invite immediate criticism both from Kahlon and from the Governor of the Bank of Israel.

Early in March, the Ministry of Justice published its proposed Law for Insolvency and Financial Recovery. The declared goals of the proposed law include facilitating the financial rehabilitation of an insolvent obliger (whether individual or corporate), and ensuring a 'fairer' distribution of the assets of a debtor among secured and unsecured creditors. It is unclear whether the promoters of the draft law have considered the full economic and regulatory consequences of their proposals. The threshold question is though, whether this 'fairer' distribution of assets (for example, only 75% of assets covered by a security interest will be available to the secured creditor, with the remaining 25% being available for the general body of unsecured creditors), as well as the lengthier process that will be involved in realising any security interest, will result in banks being less willing to lend or raise the cost of borrowing, or both.

The latest episode in 'populist' economic legislation occurred at the end of March, when the Knesset approved legislation imposing a limit on salaries in the financial sector – as a multiple of the lowest-paid employee in the organisation, with a cap of NIS2.5m (approximately $640,000) per annum. Any salary above this limit will require special corporate approvals and will result in additional tax obligations on the employer. The chair of the Finance Committee of the Knesset announced the decision as 'a historic move that will reduce the economic disparity in society'. Even if (as the legislators propose) the idea of a salary cap is extended to public companies in Israel, this will leave open the possibility of uncapped salaries for private companies and will inevitably encourage publicly-listed companies to de-list. Successful managers in the finance sector (and later on in public companies) will no doubt look for more profitable opportunities in private companies, hedge funds and in other unregulated areas.

The growing disparity between rich and poor in Israel is certainly a source of concern. The question is whether the recent measures introduced by the legislators will improve the lot of the weaker elements in society and reduce economic disparity, or whether the measures are merely popular measures aimed at punishing the financially strong, without furthering the true goals of fair wages and honest prices.

'Will the government's behaviour deter foreign players from entering the Israeli natural gas market?' Alan Sacks, HFN

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Israel: 'Early exit' controversy

Yigal Arnon's Barry Levenfeld discusses tech sector exits

Do Israeli companies exit too early?

Some, primarily government officials, but also esteemed academics, think so. Israeli technology companies should resist being sold, they say. Instead, the companies should develop into global giants, employ thousands of Israelis – including those without advanced computer science degrees – and thereby enhance their contribution to the Israeli economy. The most recent salvo came from Manuel Trajtenberg, a Knesset member and respected economist, who warned at a conference: 'The exits we applaud today are a disaster for the state of Israel.' And then, twisting the knife further, he added: 'A handful of people grow rich by selling the future of the nation.'

The accusation stung and there were a number of high-profile responses from the industry, arguing that exits were actually good for the economy and that Trajtenberg had misdiagnosed the problem. 'No Manuel, the government is the problem – not the exits,' countered Michael Eisenberg, a well-known venture capitalist, in his blog, arguing that government incompetence, particularly in the field of education, is the true culprit. Moreover, regulations hamstring some Israeli start-ups, forcing them to beta-test their products abroad, or to outsource development activities to workers in other countries.

This controversy is not new in Israel. Some blame the founders, others blame the venture capitalists, but the refrain has remained remarkably similar throughout the years. However, it used to be phrased differently and that difference is telling: 'We want to establish an Israeli Nokia in the not too distant future' was just one of many manifestations of 'Nokia envy' that characterised the critique of the 'early exit' syndrome in the not too distant past. Needless to say, when Nokia was sold, so ignominiously, to Microsoft for a 'mere' $5.4bn, the Israeli economic establishment stopped using Nokia as its poster child. However, today, the critics of the early exit seem to have forgotten the risks presented where an economy depends on one or even a few large companies.

I make my living providing legal representation to the buyers and sellers of Israeli tech companies, and our firm made its contribution (on the legal side) to the slightly-over-$9bn in hi-tech exits that Israel witnessed in 2015. We have seen up close the consequences of early exits and I must say that I unequivocally side with those who see no disaster whatsoever resulting from the Israeli exit scene. Moreover, any attempt to fix something that isn't broken could itself dampen the success of the thriving hi-tech sector in Israel. And here's why:

- In many, if not most exits, the buyer – typically a global technology giant – retains and expands Israeli research and development (R&D) activity, dramatically increasing headcount and assimilating key Israeli employees into company-wide management activities. So, not only are more people hired for R&D activities in Israel, but some Israelis obtain invaluable experience in the management techniques, discipline and global outlook of the tech buyer. In fact, although statistics are a bit murky, reliable sources report that multinationals currently finance almost 50% of all corporate R&D in Israel. Some say that multinationals are also responsible for over 50% of the R&D headcount. Contrary to what the critics say, these exits result in a 'brain gain', not a brain drain.
- Founders with successful exits often go on to establish new start-ups and start the process all over again. Some Israeli serial entrepreneurs have founded and sold several companies, thus creating more jobs and opportunities than would have been possible in any one company. Again, no brain drain, but rather a source of experienced repeat entrepreneurs.
- Israeli start-ups, like their Silicon Valley counterparts, rely on multiple financing rounds to reach maturity. Decrease the chance of exit and you decrease the attractiveness of Israeli companies to potential investors. The result of the delayed exit may be less investment capital.
- Consider the issue from the point of view of the founders, who have worked tirelessly, often at the expense of their relationships with families and friends. When presented with an opportunity to sell their company at tremendous profit, can we really expect them to say, 'Sorry, not selling because Israel needs more Nokias'? Keep in mind that any determination that the exit price was too low will only be made in hindsight. It is just as possible that a delay in the sale of the company will enable a better-financed competitor to move in and reduce the company to a fractional market share. Fewer exits mean fewer entrepreneurs willing to sacrifice everything to create their companies.

All this serves to explain why the Israeli tech ecosystem is the envy of other countries. At Yigal Arnon & Co, we host government and industry delegations from countries far and wide, from Brazil to China, Australia to Russia and many others, visiting Israel in order to learn about the 'secret sauce' that enables the start-up nation to flourish. Not one of them is concerned about the early-exit syndrome; they only wish that they could recreate the bubbling, innovative, Israeli tech scene in their own countries.

Rather than wringing their hands about the 'disaster' of too many tech exits, Israeli policy-makers should focus on increasing the competitiveness of the economy: invest in education; bring under-employed sectors of the population into the workforce; allow Israeli companies to import skilled labour; and reduce regulations hampering the development of new technologies. The exits will take care of themselves.

'Fewer exits mean fewer entrepreneurs sacrificing everything to create companies.'

Barry Levenfeld, Yigal Arnon & Co

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