

Top 10 Legal Issues Affecting (or Which May Affect) Israeli Investment in the US

Peter J. Tucci, Esq.
Fox Rothschild LLP
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Overview

- Between 2000 and 2010, Israeli companies invested over \$57.0 billion in US companies and created over 200,000 jobs in the US.
- There are no general restrictions imposed by the US government on Israeli investment in the US.
- There are a handful of industries that are subject to restrictions: natural resources, communications, shipping, nuclear and other power-generating facilities, and aviation.
- The US government does impose certain reporting requirements through the Commerce and Agriculture Departments for Israeli and other non-US investment in the US (e.g., BEA's Surveys on Foreign Direct Investment in the US).

1) Choice of Legal Entity

- In the US, Sub-S corporations are taxed similar to partnerships (i.e., profits and losses flow through to their shareholders).
- However, Israeli companies can neither establish nor acquire Sub-S corps. since Sub-S corps. cannot have corporate shareholders and cannot have non-resident US shareholders.
- In the US, a limited liability company (LLC) is a hybrid legal structure that provides the limited liability features of a corporation, the operational flexibility of a partnership, and may be taxed as a partnership.
- If an Israeli investor establishes or acquires an LLC (which has elected to be taxed as a partnership), then the Israeli investor will have to file income tax returns in the US.

2) Choice of Law/Choice of Forum

- The choice of law clause (or governing law clause) allows the contract parties to choose the substantive law of the appropriate country or state to apply to the contract (e.g., NY law or Israeli law).
- The choice of forum clause provides for where the contract parties adjudicate disputes under the contract and whether through litigation or arbitration (Tip – always use arbitration for the reasons cited below).
- Convention on the Recognition and Enforcement of Foreign Arbitral Awards (NY Convention). Since both Israel and the US are parties to this Convention, an arbitral award in either country will be recognized and enforced in the other country.

3) State and Local Laws and Regulations

- Local sales and use taxes
- State and local estate taxes
- Some US states tax LLCs
- State and local employment laws
- Some states have stringent environmental laws (e.g., NJ and CA)
- Some states restrict certain types of foreign investments; an example would be agricultural land and other real estate.

4) FIRPTA

- The Foreign Investment in Real Property Tax Act (FIRPTA) is a US tax law that imposes withholding tax on foreign persons disposing of US real property interests.
- Withholding may be reduced from the standard 10% to an amount that will cover tax liability, upon application in advance of sale to the IRS.

5) Foreign Corrupt Practices Act

- The FCPA was passed into law in the US in 1977 to decrease unscrupulous business practices involving bribes paid to foreign officials with the intention of “obtaining or retaining business.”
- Foreign companies are also subject to the FCPA if a corrupt payment is made within the US.
- Companies are barred from paying, or offering to pay, anything of financial value.
- No payments may be made through intermediaries.
- These restrictions apply to payments made to any public official, regardless of rank or position.

6) USA PATRIOT Act of 2001

- The USA PATRIOT Act of 2001 was designed to prevent and detect international money laundering and terrorism financing.
- To do this it requires financial institutions to monitor their client's accounts and balances, then report any suspicious actions regarding foreign transfers of funds.
- The practical impact has been to make many financial transactions between the US and other countries more cumbersome and time consuming.

7) Sarbanes-Oxley Act of 2002

- Starting in the 1990s, federal regulators increased the scrutiny of how a publicly owned business operates. Scandals cost investors billions of dollars when share prices of effected companies collapsed, and shook public confidence in the US securities markets.
- SOX requires publicly-owned companies registered with the SEC to document their financial-reporting controls, which has resulted in heightened compliance standards and increased cost of compliance.

8) Exon-Florio/CFIUS

- The Exon-Florio Amendment was promulgated in 1988, and gives the President of the US broad powers to block certain types of foreign investment in the US.
- The Committee on Foreign Investment in the US (CFIUS) is an inter-agency committee authorized to review the national security implications of foreign investments in US companies.
- Pre-approval of a foreign investment is not required, but the President can block the investment if “there is credible evidence that leads the President to believe that the foreign interest exercising control might take action that threatens to impair the national security.”

9) Office of the Chief Scientist (OCS)

- The OCS of the Israeli Ministry of the Economy is the support arm of the Israeli government charged with fostering the development of industrial R&D within Israel. It does so by making loans and investments in Israeli technology companies.
- If a Israeli high-tech company acquires a US company and licenses and/or transfers some of its technology to the US company, it may need to deal with the OCS.

10) Bankruptcy

- Bankruptcy issues to be discussed in detail next by Audrey Noll.

Peter J. Tucci, Esq.

215.918.3562

ptucci@foxrothschild.com