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I. INTRODUCTION

In the wake of the rapid development of the Israeli economy, Israeli securities markets have been particularly active recently. There have been numerous public offerings, both initial and subsequent, of a wide variety of companies, including the increasing use of public offerings as a mode of privatizating major government companies. Foreign investment activity, both international and private, has also increased, coupled with sometimes frenetic stock exchange trading. Consequently, there is increasing importance in the regulation of the securities markets. These regulations are contained in the Securities Law of 1968 (the "Law"), securities regulations promulgated under the Law (the "Regulations"), and the internal rules of the country's only public market for the trading of securities, the Tel Aviv Stock Exchange (the "TASE"). Related issues concerning the regulation of publicly traded companies are dealt with in the Companies Ordinance [New Version] 1983, an amended version of the 1929 English Companies Act.

Israeli securities regulation, as reflected in the Law, is in turn based in major respects on the pattern established by the U.S. Securities Act of 1933 and Securities Exchange Act of 1934. The study that led to an enactment of the Law was conducted by a committee headed by Dr. A. Yadin, then serving in the Ministry of Justice. The committee, appointed in 1962, rendered its report in 1963. Among the distinguished witnesses who testified before the committee were Professor

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Louis Loss of the Harvard Law School and Emanuel Cohen, then a member of the Securities Exchange Commission and subsequently its chairman. Mr. Cohen's testimony before the Yadin committee, the only testimony quoted in detail in the committee report, included the following suggestions:

> [W]hile there are no serious abuses as yet, it is better to have the law and anticipate the abuses than to wait for abuses and then adopt a law. You should provide against such abuses in the future by making appropriate laws in advance.... To the extent that you are in a position to tell the public that you have erected a structure and adopted a law designed for their protection, you will have a better chance of encouraging local investment. Finally, Israel is interested in encouraging portfolio investment from abroad. In the U.S. and England you will instill confidence if people know that you have erected a structure of control which provides a real measure of protection. Consideration should be given to a law rather more sophisticated than present conditions alone would warrant but one which will serve the above purposes.[1]

In response to the committee report, and closely following Commissioner Cohen's suggestions, the Israeli Knesset (Parliament) adopted a broad scheme of regulation, far more sophisticated than was called for in the early 1960s when the Israeli securities markets were in their infancy, only fifteen years after the establishment of the State. Although there have been some major changes in the Law since its adoption, the initial Law has remained the basic structure of securities regulation and has certainly fulfilled Commissioner Cohen's vision.

II. THE SECURITIES AUTHORITY

The Law established a statutory Securities Authority (the "Authority"), modeled generally after the U.S. Securities and Exchange Commission. The responsibilities and powers of the Authority are broad and include the approval of prospectuses for public offerings, the supervision of the TASE, and the review of periodic reports submitted by all companies that have issued securities that are publicly traded.

The purpose of the Authority, as expressed in the Law, is to protect the interests of the general public who invest in securities.[2] The Authority is today composed of no more than thirteen members (an increase from the original limit), appointed by the Minister of Finance (the "Minister"). The only stipulations regarding the appointment of the members of the Authority is that some should be members of the public, some should be employees of the State, and one should be an employee of the Bank of Israel. In addition, the Minister is charged with appointing a chairman and deputy chairman from among the

1. YADIN COMM. REP. 4 (1963) [hereinafter YADIN].
2. Securities Law 5728-1968 § 2 (1968) (Isr.) [hereinafter Securities Law].

members of the Authority.[3] In contrast with the SEC's employment of full time commissioners, the Law does not require that any member of the Authority be a full-time employee. In practice, the chairman is the only full-time employee of the Authority.

There are a number of disqualifications for service as a member of the Authority, such as (1) individuals who are members of the TASE, (2) persons who engage in the business of the trading securities for their own or others' accounts, and (3) employees of those who do one of the above.[4] Further, individuals who are not employees of the State or the Bank of Israel and who, in the opinion of the Minister, carry on business activities that may lead to conflicts of interest with the position on the Authority are similarly disqualified.[5]

A member is initially appointed for a period of three years and may thereafter be reappointed for additional terms of similar length.[6] The chairman serves for a term of five years, with the possible renewal of his appointment for further terms of three years each.[7] The Minister is empowered, however, to cancel the appointment of any member who exceeds certain boundaries of reasonable absences from meetings without cause.[8]

For the obvious reason of avoiding conflicts of interest, members of the Authority must report all securities held by them or their spouses to the Minister and the Authority within seven days of their appointment. Subsequently, members must notify the Minister and the Authority within seven days of the relevant transaction of any acquisition or sale of shares by them of their spouses.[9] Furthermore, a member of the Authority is forbidden to acquire any securities except as authorized under a special permit (whose form may be specific to a certain category of securities or general) from the Minister.[10] The Law also includes a provision regarding notice to the Minister and required permits for the acquisition of securities by any employee of the Ministry of Finance who undertakes administrative or professional tasks regarding securities.[11]

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3. *Id.* § 3(a)-(b).
4. *Id.* § 3(c)(1)-(3).
5. *Id.* § 3(c)(4).
6. *Id.* § 4(a), (c).
7. *Id.* § 4(b).
8. *Id.* § 4(d). The Minister is authorized to act in this manner if a member of the Authority, without a reason satisfactory to the Ministry, misses four consecutive meetings or six meetings in a year. A parallel provision for removal of a director of a government company who misses board meetings of that company appears in the Government Companies Law § 22(a)(2) (1975) (Isr.). In that instance, however, the removal is automatic unless the Ministers responsible for that company excuse the absence after consultation with the Government Companies Authority.
9. Securities Law, *supra* note 2, § 5(b).
10. *Id.* § 5(a).
11. *Id.* § 5(c).

The Minister is required to remove a member of the Authority if he becomes a member of the TASE, violates one of the holding or acquisition of securities provisions mentioned above, is convicted of a crime that involves ignominy, is declared bankrupt, or has a receiver appointed for him by the court.[12] Similarly, members of the Authority who are employees of the State or of the Bank of Israel are automatically removed from their positions as members of the Authority upon the termination of their employment in any such position.[13] Upon resignation, removal from office, death, or determination of a lack of fitness to perform a member's functions, the Minister is charged with appointing a successor for the remainder of the term of the member who has been so removed.[14]

Despite its statutory nature, the Authority is treated as a corporate entity, competent with regard to any right, legal action, or duty.[15] However, concomitantly, the Authority is deemed subject to government audit under Section 9(2) of the State Comptroller Law [Consolidated Version] 1958.[16]

The Authority is granted a free hand in determining the procedures to be followed in its meetings and discussions, so far as they are not established by the Law. Notably, the Authority is charged with preparing rules for the consideration of permit applications for the issuance of prospectuses, but the Authority does not adopt such rules. The rules are instead adopted by the Minister and must be published in Reshumot, the official register.[17]

A number of significant changes were made in the Law in 1988 (Amendment No. 9 to the Law). Among them was a provision granting the absolute right to any party injured by a decision of the Authority to appeal such a decision directly to the District Court.[18] Previously, injured parties could petition to the Supreme Court sitting as the High Court of Justice (the so called "Bagatz" action), a very familiar Israeli judicial technique, patterned on that of the English court system, for challenges to administrative and other government actions. The Knesset wisely chose to amend this procedure since the District Court, Israel's senior trial court of general jurisdiction, can effectively take testimony and rule on matters of fact and law and is better equipped to deal with testimony than the Supreme Court. Moreover, the District Court considers significant business transactions and has the greatest

12. *Id.* § 6(a).
13. *Id.* § 6(b).
14. *Id.* § 6(c).
15. *Id.* § 8(a).
16. *Id.* § 9.
17. *Id.* § 12 (providing that the Minister can take the initiative with respect to the rules, needing only to consult with the Authority).
18. *Id.* § 14A.

background for dealing with securities law matters in the first instance.

A similar right of appeal may be granted under Section 47 of the Law (discussed below). The District Court recently considered the fundamental difference between the two possible paths of appeal. While recognizing the Supreme Court's time limitations, the District Court judge also noted that the lower courts possessed the requisite ability and authority to carry out a review of the facts of a case concerning administrative decisions of governmental authorities. The Court quoted Professor Yitzhak Zamir's[19] book, *Judgment of Administrative Issues,* as stating that the investigation of the District Court will very often be more thorough than that available in a corresponding appeal to the Supreme Court.[20]

III. PUBLIC OFFERINGS AND PRIVATE PLACEMENTS; PROSPECTUS DISCLOSURE

A. *In General*

The cornerstone of the Law is the requirement, parallel to that of the Securities Act of 1933, that any offer of securities to the public must be in accordance with a prospectus that has been published pursuant to a permit granted by the Authority.[21] The term "securities" is broadly defined to include any serial certificates issued by a company,[22] a cooperative entity, or any other corporate body that grants participatory or membership rights in, or a basis of claim against, such an entity, including certificates of participation in a trust fund for joint investments and any certificate that carries the right for the bearer to acquire any such securities.[23] In all of these cases, the fact that the securities are registered or in bearer form is immaterial.

However, the definition of securities, for purposes of the prospectus requirement, significantly excludes any securities issued by the Government or under the authority of any special law.[24] The Knesset considered prospectus disclosure unnecessary when the Government issues securities, as it has regularly done over the years. If, however, the sale of securities are those of a government company, as is the case in privatization by public offering, then the Law requires prospectus

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19. Israel's former Attorney General who was appointed to the Supreme Court in December 1993.

20. Katz v. Securities Exchange Ltd., (2) P.M. 296 (Dist. Ct., Tel Aviv/Jaffa 1991) (Isr.).

21. Securities Law, *supra* note 2, § 15(a).

22. Israeli corporate law, following the lead of the English Companies Act, which was its source, describes a corporation as a "company." In general, the same terminology is used herein.

23. Securities Law, *supra* note 2, § 1.

24. *Id.*

disclosure, since such a sale is *not* of securities issued by the Government. The Law focuses on the *offer* of securities rather than on their actual *sale*. Finally, it is clear that the only prospectus that counts for purposes of a public offering is one that has been reviewed by the Authority and for which an Authority permit has been issued; the most complete and accurate offering memorandum, cast in the form of a prospectus, will not suffice for these purposes.

The distinction between private placements and public offerings has been an interesting one. The first case to interpret the Law, in 1977, dealt with an offer of securities by an Israeli real estate company to private investors in Turkey and Iran.[25] Evron and two companies under his control had sought financing for the construction of a hotel in the Metropolitan Tel-Aviv area. Agents acting for Evron and the companies travelled to Turkey and Iran and met with investors in those countries who were interested in investments in Israel. A criminal proceeding was brought in Israel with respect to the alleged offering of securities to the public without a prospectus approved by the Authority as required by the Law and, at the same time, claiming that the offering material used was fraudulent. Prior to the hearing, the two companies, which by then had been acquired by other shareholders, pleaded guilty and Evron was the only defendant left in the case. The District Court held that there had been a violation of the Law on both issues and discussed at length and in detail the history of the Law and its underlying purposes. The Court, reviewing the legislative history of the Law, concluded that the definition of a public offering was based on the U.S. Securities Act of 1933 pattern and was designed to prohibit a public offering where offers were made to those who did not have access to the kind of information that registration would disclose. Citing the leading Supreme Court case of *SEC v. Ralston Purina*,[26] the Court concluded that in the case at hand the investors should have been provided with a prospectus approved by the Authority and held that there had been a violation of the Law. Interestingly, the Court specifically referred to the development by the SEC of similar rules, citing Professor Louis Loss' treatise and the early opinion of the SEC General Counsel that an offer to not more than twenty five investors would not require a prospectus. The District Court, however, rejected the position that any rigid standard should be adopted. The Evron case was subsequently appealed and affirmed in this respect by the Israeli Supreme Court. Evron's appeal from the portion of the District Court decision holding the offering material to be deceptive was accepted, and he withdrew his appeal from the conviction of affecting an offering without a prospectus. No real conclusion can be reached from the withdrawal of the appeal. Since the penalty imposed on

25. State v. Evron, (1) P.M. 329 (Dist. Ct., Tel Aviv/Jaffa 1977) (Isr.).
26. S.E.C. v. Ralston Purina Co., 346 U.S. 119 (1953).

Evron with respect to the prospectus violation was a modest one, it was clear that the Supreme Court was not interested in hearing argument on that issue. Once Evron's counsel saw that the Supreme Court was inclined to rule in Evron's favor on the more serious count, with respect to the quality of the offering materials, he withdrew the appeal.[27]

Very recently, again following the lead of U.S. securities regulation and the safe harbor of Rules 502-506 under the Securities Act of 1933, the Securities Authority has informally adopted a similar approach, without all of the protections offered by the U.S. Rules, and today the Authority will, in effect, take no action with respect to a private placement to not more than thirty five investors.[28] Regulations have recently been adopted providing for certain procedures and public notifications to be followed for a private placement by a company whose shares are publicly traded.[29]

The Law also provides for certain instances where the Authority may waive the requirement of offer by prospectus for reasons of convenience or sensible business practice. Thus, offers for sale of securities that are registered on the TASE in the course of trading on the market merit a statutory exemption.[30] Consequently, transactions by a controlling person, no matter what the extent of his holdings, do not require an Israeli prospectus so long as the transactions are effected on the TASE, a significant change from the U.S. pattern. Similarly, the Authority is authorized to exempt offers by receivers, trustees in bankruptcy, or other cases where the offeror is not the issuer, in accordance with regulations made by the Minister and approved by the Knesset Finance Committee (the "Finance Committee").[31] In addition, the Authority may exempt from the obligation to offer by prospectus securities that will not be traded on the TASE and will only be offered to insurers, benefit funds, or banking corporations.[32]

B. *Disclosure Requirements*

The Law establishes two guiding principles that govern the content of materials that are to be included in the prospectus to be pub-

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27. *Evron*, 32(2) P.D. at 189 (1978).

28. This is true although there is no "formal no action letter" procedure in effect in Israel.

29. Securities Regulations, Private Placement of Securities by a Registered Company (1992).

30. Securities Law, *supra* note 2, § 15(b). The Minister and the Knesset Finance Committee have very important roles under the Law, in contrast to the provisions of the Securities Act of 1933, Securities Exchange Act of 1934, and other U.S. securities legislation. As a result, the SEC is much more independent in issuing regulations and performing other functions than the Authority.

31. *Id.* § 15(c).

32. *Id.* § 15(d).

lished under the permit from the Authority. First, the prospectus must include every particular that a reasonable investor would regard as material when considering investment in the securities described in the prospectus.[33] A non-exhaustive list of particulars that are deemed to fall into this category is to be provided by the Minister in regulations to be approved by the Finance Committee. Second, no misleading particular may be included in the prospectus.[34] With these two governing principles as a background, it is possible to commence an examination of the sections of the Law, including regulations promulgated thereunder, governing the particulars that should be included in the prospectus.

Section 17 of the Law provides the basic framework for the regulations that the Minister, after consultation with and recommendation of the Authority, may present to the Finance Committee for approval. This task was discharged almost immediately with the adoption of the Securities Regulations, Particulars of a Prospectus, Its Structure and Form (1969) (the "Prospectus Regulations"). Amendments 9 and 11 to the Law, passed in 1988 and 1990 respectively, greatly increased the type and nature of particulars accompanying professional opinions that the Minister could require, by regulations, to be included in the prospectus.

Regulations, according to Section 17(b) of the Law, may, among other things, refer to the following particulars: (1) financial reports of the issuer, its subsidiaries, and affiliated companies and the opinions of the accountants on such reports;[35] (2) an opinion from an attorney referring to certain specified legal matters as prescribed by the regulations;[36] (3) confirmation from an attorney that all necessary permits for the offering have been obtained;[37] and (4) details as to interested parties of the issuer and the nature of such interests, particulars of which the interested party is obligated to deliver in order to enable the issuer to meet this requirement.[38]

1. Regulations Regarding Prospectuses

The prospectus must be in a printed form that is easily readable.[39] The cover must include the word "prospectus," the name of the issuer (and the offeror, if he is a different person), the date of the prospectus, and a description of certain details regarding the securities

33. *Id.* § 16.
34. *Id.*
35. *Id.* § 17(b)(1)-(2).
36. *Id.* § 17(b)(3).
37. *Id.* § 17(b)(4).
38. *Id.* § 17(b)(5), (c).
39. Securities Regulations, Particulars of a Prospectus, Its Structure and Form, 5729-1969, § 2 (1969) (Isr.) [hereinafter Prospectus Regulations].

offered.[40] The prospectus must include all details required under these regulations, as well as any particular of which the issuer notified the Authority as being potentially of interest to a reasonable investor and that the Authority requested be included in the prospectus.[41] Finally, unlike the U.S. prospectus, which must meet certain requirements but does not need to follow a specific order, the structure of the prospectus must follow the order established under the regulations.[42] The discussion set forth below follows the order required by the regulation, which prescribes the structure and content of the various sections of the prospectus.

2. Introduction to Prospectus

The introduction must include a notice that all relevant permits for the offering have been obtained, a statement regarding the status of an application (or lack thereof) for the registration of the offered securities for trading on the TASE, a description of the issuer that includes details of its outstanding share capital and existing reserves, and a list of any outstanding debenture series previously issued.[43] From this starting point, the regulations move into a prescription of the details that must be included within the body of the prospectus itself.

3. Particulars on the Offering of Securities

The rules first require inclusion of details regarding the securities to be offered under the prospectus.[44] In addition to the expected requirements to disclose information regarding the price and payment terms, the manner of ordering the securities, the date of allocation, the manner of refunding refused orders, and the details of any underwriting agreement, the regulations also include a number of prescribed disclosures that are rooted in concern for the protection of the unwary investor.[45] Examples of such rules include the disclosure of the undertaking by any party to acquire securities of the same category as those being offered which have not as yet been issued and the specification of any rights to acquire the offered securities that have been extended to any specific category of persons (e.g. the previous shareholders).[46]

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40. *Id.* § 3.
41. *Id.* § 6.
42. *Id.* § 5.
43. *Id.* §§ 7, 9, 11-15.
44. *Id.* § 16.
45. *Id.* §§ 21-23, 25.
46. *Id.* §§ 19-20; *see also* State v. Rubinstein, (1) P.M. 89 (1992) (Isr.) (providing a judicial application of these regulations).

4. Issuer's Securities and Capital

The regulations continue by enumerating various rules surrounding particulars regarding the issuer's securities and capital. The first such requirement regards the disclosure of certain rights and restrictions that are attached to the offered securities and any other categories of outstanding securities.[47] The prospectus must also disclose various details, depending on whether the offered securities are shares or debentures, regarding the capital of the issuer. These include particulars of changes in the capital of the issuer in the three years prior to the date of the prospectus, the terms of any underwriting agreement during that period, and the general details of any offering by prospectus in the relevant years.[48] Further facts that also require disclosure include the nature of the holdings of any interested parties in the issuer, any undertaking by the issuer to issue or to abstain from issuing securities or to abstain from taking loans under certain conditions for a specified period, and the particulars of any exemptions or reductions from the provisions of tax or foreign currency control regulations available to holders of the offered securities.[49] Additionally, the prospectus must contain the highest and lowest quotation prices in trading on the TASE for the two years preceding the prospectus for all categories, if any, of the issuer's shares that are registered for trading thereon.[50] Lastly, in connection with the offering of debentures, the prospectus must disclose various material facts regarding the parties to and the terms of the trust indenture that is used in accordance with Section 35B of the Law (discussed below).[51]

5. Use of Proceeds

The regulations require that the issuer clearly state the anticipated use of the proceeds of the offering. More specifically, the company must disclose all of the intended objectives to be achieved with the funds, the amount necessary for each objective, the timetable under which the issuer intends to operate with the funds, and how any additional money required for the achievement of these objectives will be raised.[52]

An insurer, a banking corporation, or a company whose main purpose is the investment in other companies may give notice that the consideration of the offering is not intended for any specific objective

47. *See* Prospectus Regulations, *supra* note 39, § 26 (providing details of the types of restrictions and rights that require disclosure).

48. *Id.* § 27.

49. *Id.* §§ 28, 30-31. Israel has broad foreign currency control rules under the Currency Control Law of 1978.

50. Prospectus Regulations, *supra* note 39, § 29.

51. *Id.* §§ 32-33.

52. *Id.* § 39(a)-(b).

but rather is earmarked for use in the expansion of the business. Nevertheless, even in these exceptional cases, if twenty-five percent or more of the funds are intended for a specified objective, the nature of such an intended use must be disclosed.[53] Similarly, the regulations set rules governing disclosure of certain essential particulars and details of any asset or enterprise that is to be acquired, of any contemplated expansion or building in relation to the concern of the issuer, or of any company in which the issuer plans to invest, all with the proceeds of the offering.[54]

Along the same lines, if the issuer reserves the right to alter the stated objectives or any details related thereto, it must disclose the conditions under which such a right of adjustment might be exercised, the type of decision that must be taken on the part of the company to authorize such changes, and the means by which notice of such a decision will be publicized.[55] Finally, if no minimum amount that the issuer expects to raise through the public offering is set, then this fact must be included in the prospectus.[56]

6. Particulars of the Issuer

The prospectus must include a detailed description of the issuer for a period of at least five years prior to the prospectus, focusing in greater detail on the last two years prior to the offering.[57] In the same section, the prospectus must include disclosure of certain vital details of its directors. These include personal details, such as age, address, and citizenship, as well as business facts, such as the director's position in the company, his service on board of directors' committees, and his being a relative of any interested party in the issuer.[58] Further, the prospectus should include the provisions of the Memorandum and Articles of Association, the Israeli statutory names for charter documents, of the issuer as they relate to the appointment, service, and powers of the directors.[59]

In addition, the issuer must list personal details and certain professional facts regarding the remaining senior officers in the issuer for whom details were not included in the section regarding directors.[60]

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53. *Id.* § 39(c).

54. *Id.* §§ 41-43 (providing details of the required disclosure in each of these cases).

55. *Id.* § 39A.

56. *Id.* § 40; *see also* Securities Law, *supra* note 2, § 27(a) (providing the background rules regarding minimum amounts and refunds).

57. Prospectus Regulations, *supra* note 39, §§ 44-44A.

58. *Id.* § 45(a).

59. *Id.* § 45(b).

60. *Id.* § 45A; Section 1 of the Prospectus Regulations defines "ranking officers" of a company to include the directors, the general manager, the deputy general manager, the vice general manager, the accountant, the internal auditor, and any

Furthermore, the prospectus must contain a list of the number of employees, by profession, who work for the issuer at the date of the prospectus.[61] Lastly, the issuer is required to disclose the nature of any undertaking, agreement, or practice under which the company is liable to make payments, calculated as a percentage of its profits, income, assets, or turnover, to anyone.[62]

7. Subsidiaries and Associated Companies

For obvious reasons, the prospectus must include a list of all the subsidiaries and affiliated companies of the issuer, including details of the nature of the issuer's holdings in the companies and the essential terms of any loans or other transactions between them.[63] A description of the main business of each such company and basic financial information must be disclosed.[64] In addition, following the line of disclosure regarding interested parties in the issuer that is discussed below, the prospectus must specify the names and the holdings of any persons who, to the best knowledge of the issuer and its directors, hold twenty-five or more percent of the outstanding share capital, of the voting rights, or of the power to appoint directors in any of the subsidiaries or affiliate companies.[65]

The regulations contain even stricter disclosure requirements if the issuer has invested, or is about to invest, at least fifty percent of its total assets, including the proceeds of the current offering, in another company, whether by way of shares, loans, or other means. In such a case, the issuer must include particulars of the entity as if it were the issuer, with all the attendant requirements discussed above.[66] However, the regulations do provide an exemption from such a disclosure in the case of an issuer that offers debentures, all the consideration of which is intended for deposit in a "bank" that undertakes to fulfill all of the payment terms under the debentures qualifying as a "recognized investment" according to the Income Tax Regulations (Rules for the Approval and Management of Benefit Funds) 1964.[67]

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other individual who performs those functions regardless of title. In addition, any employee of the issuer who holds at least five percent of the outstanding nominal share capital or of the voting power in the issuer is, for the purposes of these regulations, considered a "ranking officer."

61. *Id.* § 46.

62. *Id.* § 47.

63. *Id.* §§ 48, 50.

64. *Id.* § 50.

65. *Id.* § 49.

66. *Id.* § 51(a).

67. *Id.* § 51(b)-(c). In this context the regulation defines a "bank" as a company that deals with the receipt of money on current account from which, by check, payments can be made on demand.

8. Interested Parties in the Issuer

The definition of "an interested party" in a company includes the following: (1) a person who holds five percent or more of the outstanding share capital or voting power of the company;[68] (2) a person who can appoint one or more of the directors, or the general manager of the company or an individual who serves in such a position; (3) a company in which a person meeting the requirements of (1) or (2) holds twenty five percent or more of the outstanding share capital or of the voting power or in which such a person is entitled to appoint one quarter or more of its directors; and (4) a subsidiary of the company, except for a bank registration company.[69]

For the purposes of this definition, the director of a trust fund for joint investments is to be considered as the individual who holds the securities included among the fund's assets. Similarly, a trustee, as opposed to a registration company, who holds securities in trust for another is to be considered as the holder of those securities.[70]

With these definitions in mind, the regulations provide that the issuer must disclose the holdings of shares and options of any interested party or of any ranking officer in the issuer, its subsidiaries, and its affiliated companies, at a date as near as possible to the prospectus and at a date twelve months prior to such a date.[71] Additionally, the nature of any benefits that any interested party has received or is due to receive, directly or indirectly, from the issuer, its subsidiaries, or its affiliated companies in the two years prior to the offering, must be detailed. However, the salaries and related expenses paid to the directors and the general manager, as long as they do not deviate from expected norms, do not need to be individually specified; rather, they are to be included in a total sum figure for all the employees.[72] The interest that any such interested party had in any transaction not executed in the ordinary course of business, involving the same compa-

68. Amendment 11 to the Law, enacted in December 1990, reduced the previous figure of 10% of the outstanding shares in the corporate entity to the current figure of 5%. This change brings the Israeli law into line with the corresponding United States law on the issue of interested parties. *See* Section 13(d) of the U.S. Securities Exchange Act of 1934. A special set of regulations has just been adopted to exempt the Government from certain regulatory provisions, in connection with privatization of the banks in order to avoid the nightmarish disclosures of all affiliations of Government companies with the bank. *See* Securities Law, Interested Persons Emergency Order (1993).

69. Share certificates of securities traded on the TASE are generally held by banks for their customers through subsidiaries of the banks called registration (or nominee) companies. Such companies are defined by the Law as "registration companies." *See* Securities Law, *supra* note 2, § 1(f).

70. Securities Law, *supra* note 2, § 1(m).

71. Prospectus Regulations, *supra* note 39, § 55.

72. *Id.* § 53.

nies in the two years prior to the date of the prospectus, must be detailed in this section, to the best of the knowledge of the issuer and of its directors.[73]

9. Financial Information

Audited annual financial reports of the issuer, dated no more than fourteen months prior to the date of the prospectus, must be presented as part of the prospectus. The regulations also provide for a presentation of interim reports (including the profit/loss report, the change in financial status report, and the change in capital report), to be included for the interim period.[74] In addition, there are specific provisions for the disclosure of comparative reports; in general, this incorporates the comparison of figures in the latest profit/loss report with the corresponding figures for the prior three annual reports.[75]

Lastly, the regulations establish that all financial reports required under this heading in the prospectus must be drawn up in accordance with the provisions of Securities Regulations (Preparation of Financial Reports) 1969.[76] However, with the recent publication of the new Securities Regulations (Preparation of Annual Financial Reports) 1993 ("1993 Regulations"), which repeal the 1969 regulations on financial reports, changes were made in this regard.[77] Except for certain interim provisions regarding applications to publish a prospectus that were made before March 31, 1993, allowing in certain circumstances the inclusion of reports based on the now-repealed format, the financial reports to be included in a prospectus must be modeled on the format provided in the new Annual Report Regulations.[78]

10. Miscellaneous Particulars

The regulations require the inclusion of an opinion of an attorney certifying the following: (1) the accuracy of the description of the rights related to the offered securities and of the rights related to the other shares of the issuer if the offered securities are shares; (2) the authori-

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73. *Id.* § 54.

74. *Id.* § 56. The system works as follows: (i) if the date of the annual report predates the prospectus by more than five months, then the interim reports must be presented up to a date three months after the annual report; (ii) if it predates by more than eight months, then the interim reports must cover up to a date six months after the annual report; and (iii) if it predates by more than eleven months, then the interim reports must cover up to a date nine months after the annual report. All of the interim reports must conform to the format of the annual report.

75. *See Id.* § 59 (providing further details on the presentation of such information).

76. *Id.* § 60.

77. Securities Regulations, Preparation of Annual Financial Reports, 5753-1993, § 65 (1993) (Isr.) [hereinafter 1993 Regulations].

78. *See Id.* § 67 (providing details of these interim provisions).

ty of the issuer to offer the securities in the form in which they are offered; (3) the lawful appointment of and the full disclosure of the directors of the issuer; and (4) the agreement of the attorney to the inclusion of the opinion in the prospectus.[79]

Similarly, the regulations stipulate that the issuer must include the opinion of its accountants regarding the audited financial reports that are included in the prospectus. The opinion must include certification that the reports were prepared in accordance with Securities Regulations (Preparation of Financial Reports) 1969 and that the accountant has agreed to the inclusion of his opinion in the prospectus.[80]

In addition to the opinions described above, this section of the prospectus must describe the rate of the underwriting commissions that the issuer has agreed to pay in connection with the offering of the securities, as well as an estimate of the total expenses connected with the offering.[81] Further, the issuer must detail any commissions that it undertook to pay in connection with the subscription of the various categories of securities offered by the issuer in the two years leading up to the date of the prospectus.[82] The issuer must also include the names of the parties to, and a short description of the substance of, every material agreement signed by the issuer in the two years prior to the offering and of every material agreement that still obligates the issuer, unless in either case the agreement was made in the ordinary course of business.[83]

Similarly, this section must include a disclosure of all liens created by the issuer in respect of any of its obligations along with the outstanding balance of such underlying obligations.[84] Finally, the issuer must describe any guaranty, effective at the date of the prospectus,

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79. Prospectus Regulations, *supra* note 39, § 61. In the published adopted regulations, not all areas suggested in the corresponding list in the Securities Law, § 17(b)(3) (1968) (Isr.) (as amended), have been mentioned. These omissions include the references in the attorney's opinion to such issues as the certification of the accuracy of the descriptions, if any, mentioned in the prospectus of the agreements to which the issuer is party, and of the details of any liens or sureties that are still effective and that were created by the issuer, and the particulars of any legal proceedings to which the issuer is party at the date of the prospectus. Even though updated regulations have not yet been published, in practice the Authority has required the attorney's opinion to conform to the revised provision in the Law. An argument could be made that this should not be required until the regulations are amended.

80. Prospectus Regulations, *supra* note 39, § 62; *see also* Securities Law, *supra* note 2, § 17(b)(2) (containing the background provision regarding this opinion). Presumably, with the repeal of the 1969 regulations on financial reports and the introduction of the 1993 Annual Reports Regulations, this section is amended *mutatis mutandis* to reflect this change.

81. Prospectus Regulations, *supra* note 39, § 63.

82. *Id.* § 64.

83. *Id.* § 66.

84. *Id.* § 67.

that it has given to any company other than a subsidiary in which it holds more than fifty percent of the voting power, if such a guaranty is not limited in amount or represents a sum larger than one-quarter of its adjusted equity; further, any guaranty in any amount that is given to any company otherwise than in the ordinary course of business must be described.[85]

11. Prospectus for Commercial Securities

The regulations provide for a special form of prospectus in the case of an offering of "commercial securities," which are defined to include securities issued by a company that grant the right to claim monies from the company at a date that is not less than ninety days following the offering and not later than nine months after the offer date.[86] As a part of the cover which discloses the vital information regarding the offering, the description of the securities offered by the prospectus must include the following: (1) the total value of the series; (2) the nominal value of each commercial security; (3) the interest rate carried by the securities; (4) the maturity date of the securities; and (5) the name of the guarantor, if any.[87] Apart from this change, the content of the prospectus is governed by the regulations described above applying to any other prospectus.[88]

C. *Other Requirements*

After drafting a prospectus, the offeror must submit the draft to the Authority for review. If the offeror wishes to take advantage of certain exemptions that the Authority may grant concerning the inclusion of specified particulars in the prospectus, it should omit the relevant particular and attach an application to the Authority requesting that such an omission be authorized under the powers granted to the Authority to issue exemptions.[89] Furthermore, the Authority, at its discretion, is empowered to request further details or clarification regarding any information surrounding the offering and the prospectus.[90]

The Law then proceeds to explain the procedure and grounds under which an exemption from the publication of a certain particular may be obtained. Amendment 9, passed in 1988, was a major step forward in the clarification of these matters. Grounds under which an exemption may be granted include the protection of trade secrets of the offeror, provided that the excluded particular is not of a type that

85. *Id.* § 67A.
86. *Id.* § 70.
87. *Id.* §§ 71-72.
88. *Id.* § 73.
89. Securities Law, *supra* note 2, § 18(a)-(b).
90. *Id.* § 18(c).

would likely deter a reasonable investor from considering acquisition of the offered securities.[91] In addition, the Authority may grant an exemption on the grounds that publication is liable to cause damage to the State's economy, to the national security, or to an ongoing police or Authority investigation.[92] However, in the latter cases, if the Authority believes that the omitted particular would be important to the reasonable investor, then the Authority is not authorized to permit the publication of the prospectus.[93] In all cases where an exemption has been granted, notice of that fact must be disclosed in the prospectus.[94]

After specifying the particulars that are generally to be included in every prospectus pursuant to Section 17 of the Law and the related regulations, the Law proceeds to establish a wide-ranging residual power of the Authority to demand the inclusion of any particulars beyond those listed in the regulations that, in the Authority's opinion, would be important to the reasonable investor, regarding the issuer and its subsidiaries and affiliated companies.[95] In addition, the Authority may request the inclusion of further matters that in the opinion of the attorney should be attached to the prospectus; it may also request additional opinions or reports, especially in relation to financial matters.[96] Finally, presumably to protect the interests of an unwary or careless investor, the Authority may require that the offeror emphasize any detail to be included in the prospectus in a particular matter.[97]

Once the Authority has reviewed the prospectus and insured its compliance with the Law and regulations and the receipt of all necessary permits for the publication of the prospectus, the Authority is to grant a permit allowing the publication of the prospectus.[98] The Law stresses that such a permit does not constitute any opinion on the part of the Authority regarding the reliability or completeness of any particulars in the prospectus, and the permit is not meant as an expression of any belief regarding the quality of the offered securities.[99] That

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91. *Id.* § 19(a)(1).

92. *Id.* § 19(a)(2). In each case such a claim of potential damage must be confirmed by a signed document from the Minister of Finance, the Minister of Defense, the Minster of Police, or the Chairman of the Authority (or a person authorized to act in his stead) sanctioning the claim of the offeror.

93. *Id.* § 19(b). In the case of confidential trade secrets, which are governed by the test of being "likely to deter the reasonable investor," it would seem that the test is wider and less favorable to the offeror, than the proposed test. The opposite would be expected, with greater emphasis on encouraging offerors to apply for exemptions in the so-called "security" cases without fear of being refused permission to publish the prospectus.

94. *Id.* § 19(c).

95. *Id.* § 20(a)(1)-(2).

96. *Id.* § 20(a)(3)-(6).

97. *Id.* § 20(b).

98. *Id.* § 21(a).

99. *Id.* § 21(b); *see also id.* § 21(c) and the resulting regulation in Prospectus

statement is, of course, parallel to the one that SEC regulations require to be included on the cover page of a U.S. prospectus. There is, however, one major difference in prospectus procedure between the two countries. Whereas SEC regulations generally require that the preliminary prospectus (the so-called "red herring prospectus") be distributed widely prior to the distribution of the final prospectus, no such procedure exists in Israel; instead, the contents of the Israeli draft prospectus are deemed confidential prior to the granting of the permit in the actual public offering. The assumption that the public reads prospectuses in detail is not a very well founded one, however, despite the efforts of the Authority by requiring summary statements and cover emphases to highlight important points. One of the problems is that prospectuses are not distributed to every potential purchaser. Rather, they are made available at branches of banks, brokerage firms, and at the Authority and TASE. On the other hand, there is a very active and competitive financial press that generally provides summaries of prospectuses and general evaluations of companies going public.

Another difference between Israeli and U.S. procedures is that the Authority has not yet developed any rules with respect to so-called "gun-jumping." When a public offering is pending in Israel, articles frequently appear in the press that partake of obvious promotion by the company and its interested parties. It would not be surprising if this issue is dealt with by legislation or regulation in the years to come.

Both the draft submitted to the Authority and the final prospectus to be published by permit from the Authority must be approved by the board of directors of the issuer.[100] Once the final draft is approved, the prospectus must be signed by the issuer and by a majority of its directors, including at least one public director; in the case of an initial public offering, at which point public directors will not yet have been appointed, the majority of the directors must include at least one director who is only considered an interested party as a result of his serving as a director.[101]

The concept of a "public director" was provided for in 1987 by amendment to the Companies Ordinance. The concept is that any

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Regulations, *supra* note 39, § 8 (regarding the language used to emphasize the limits on the Authority's permit to be included in the "Introduction" section of the prospectus).

100. Securities Law, *supra* note 2, § 22(a). The requirement that the draft, as well as the final prospectus, be signed, was added by Amendment 9 in 1988 and was designed to overcome the problem created by companies filing inadequate and incomplete draft prospectuses, in periods of substantial prospectus activity, just to get on line at the Authority.

101. Securities Law, *supra* note 2, § 22(b); *see also* Companies Ordinance (New Version) 5724-1983, § 96B(c) (1983) (Isr.) [hereinafter Companies Ordinance] (providing the definition of "public director").

company that has effected a public offering is required by law to have two public directors appointed. These must be Israeli residents who have no economic connection or familial relationship with the company or its controlling shareholders and whose appointment has been approved by a special committee established under the Ordinance for that purpose.[102] In addition, if an underwriter has undertaken to acquire securities that are not purchased by the public, the underwriter must also sign the prospectus.[103] Further, if the securities are offered otherwise than by the issuer, the offeror must also sign.[104] It must be noted that as in U.S. and other securities laws, signatories to the prospectus are not merely for show; rather, the Law, as discussed below, attaches varying degrees of civil liability to those who have signed a prospectus that contains misleading particulars or omits material details.[105]

As a result of the potential liability even of directors who do not sign the prospectus, the Law adopted a procedure by which a dissenting director may cause the Authority to consider staying the publication of the prospectus for a period of twenty days (unless otherwise instructed by a court of law). This power may be exercised after a director brings to the notice of the Authority, in written form, any detail which, if brought before a court, would be considered sufficient grounds to warrant the court's intervention.[106] The Authority should receive notice of and may appear as a party to any proceedings in the courts that result from any action undertaken under this procedure.[107]

Assuming that all the preceding requirements have been fulfilled, the issuer may proceed to publish the prospectus and distribute it to the public. The prospectus is to be dated no more than seven days after the permit from the Authority has been granted, unless such a date has been extended by the Authority.[108] Within one business day of the date of the prospectus, the issuer must submit a copy thereof to the Registrar of Companies, a government office which deals with all matters affecting company charter documents and also keeps records

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102. Companies Ordinance, *supra* note 101, § 96B(a). It had been generally assumed that public directors need not be appointed for Israeli companies whose only shares are traded in the U.S. However, the District Court of Tel Aviv/Jaffa ruled otherwise in an unreported decision, Ido Ben-Yehuda, Adv. v. Interpharm Indus., decided on June 6, 1993. That case is on appeal to the Supreme Court, which entered a stay with respect to implementation of the District Court decision.

103. Securities Law, *supra* note 2, § 22(c).

104. *Id.* § 22(d).

105. *See Id.* § 31.

106. *Id.* § 22(e).

107. *Id.* § 22(f).

108. *Id.* § 23(a).

on all Israeli companies, along with a copy of the permit from the Authority.[109] Within the same time period, the issuer must publish, in two Israeli, widely-circulated, Hebrew language, daily newspapers, a notice that includes details of the submission of the documents to the Registrar, advice of the place where copies of the prospectus may be obtained and where orders for securities may be submitted, and of any other particulars that the Authority may require to be included in the notices.[110] Lastly, the Authority may require the distribution of prospectuses within a certain time period, in certain locations, and in certain numbers, all according to its discretion.[111]

The Tel Aviv-Jaffa District Court dealt with these prospectus related matters in the case of *Israel v. Rubinstein & Partners, Contracting Co. Ltd. et. al.* ("Rubinstein").[112] While this is a decision of the District Court, which therefore bears less precedental authority than a Supreme Court decision, it is one of the rare recent occasions in which any of the higher courts in Israel has undertaken an exploration of the issues involved in the criminal side of the securities law in a published opinion. Almost all of the criminal cases brought under the Law are heard in the Magistrates Court, and those decisions are almost never officially reported. The defendant company undertook a public offering of its securities in 1984. The pronounced intention was to sell a certain percentage of the shares in the company to the public; all of the shares were previously owned by two rival factions of the Rubinstein family. It was against a background of disagreements between the two groups that the offering was finally affected. Through a number of transactions, each involving participation by some or all of the ten named defendants, a significant majority of the shares which were offered eventually came back under the control of members of the family or parties close to them.

While the accused all claimed that their actions had been carried out in good faith and according to the Law and/or the prevailing practice in the securities markets, the Authority and the prosecution viewed these transactions differently. A number of different charges were brought against each defendant. The prosecution claimed that the accused, as a group, had been involved in a form of overall conspiracy with an intention to commit fraudulent or deceitful behavior. While some of the charges were brought under the Criminal Law of 1977, a portion of the charges were also brought under the Law, which provides for criminal sanctions in certain situations, as discussed below.

The Court began by making some general observations regarding

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109. *Id.* § 23(c)(1).
110. *Id.* § 23(c)(2).
111. *Id.* § 23(d).
112. *Rubinstein*, 192 (1) P.M. at 89 (1972). An appeal to the Supreme Court has been argued, but no decision has been rendered.

various sections of the Law and securities law in general. The judge stated that despite its suspicious appearance, the purchase of securities through strawmen and the splitting of purchases through various accounts or persons are not unlawful in and of themselves. Because such activity was accepted practice at the time of the alleged offenses, such actions would only run afoul of the law if they were connected to some form of unlawful activity. He then went on to establish Sections 16 and 18(a), the tests of the reasonable investor, as the sources for the requirements of disclosure in the prospectus. He added that oral, as well as written, contracts and agreements needed to be tested for disclosure. With this in mind, the judge moved on to describe certain fundamental points about the overall approach adopted by the Law.

The judge pointed out that the Law clearly provides a framework that focuses on civil obligations and remedies. The focus on civil remedies and the relegation of criminal sanctions to a position of secondary importance show that the lawmakers hoped that securities law questions would center around civil rather than criminal litigation.[113] He added that, except for the provisions of Section 25 that deal with amendments to the prospectus after its publication, all transgressions of the provisions of the Law relating to prospectus liability that are relevant in creating liability must occur before the date of the signing of the prospectus by the relevant parties. Any events that occur after that date are not to be relied upon in establishing prospectus related liability under the Law.[114] Before proceeding to an examination of the particular facts of the case, the judge explicitly noted the enormity of the task before him as he realized that he was entering an area of the law, namely the criminal penalties, that had been little touched in previous decisions of the higher courts.

With this background established, the judge began to attack the legal and factual issues raised in the charges against each of the defendants. The overall claim of the prosecution was that the so-called public offering was not meant to be for the public at all. Rather, it was alleged that, under a wide-ranging conspiracy, the defendants had colluded in a plan that would allow the family to purchase the offered shares in an attempt to tighten their control over the company. While the judge recognized that the imposition of control by a group of share-

113. The judge pointed to the continuing reluctance of the lawmakers to amend problematic areas of the criminal sections of the Law, for example, the difficulty of meeting the requirements of "fraud" in order to convict the defendants of manipulative actions with regard to the value of securities in Section 54(a)(2). At the same time they have amended civil areas of the Law on eleven separate occasions since it was enacted. This demonstrates the lack of importance attached to the criminal penalties offered therein. This theme is discussed further in the section dealing with the criminal provisions of the Law.

114. The judge did comment that, although this was the current state of the law, it could hardly be considered ideal.

holders was by itself a legal action, the transactions involved had to be tested in their circumstances and surroundings. While numerous technical issues were involved with the verdicts passed on the individual parties, often revolving around fine distinctions in questions of criminal law that are not particularly relevant for present purposes, the judge did enunciate certain principles regarding securities law that bear mention here.

First, the judge, on the available evidence, was unable to find a basis for claiming that the various parties were involved in some sort of overall criminal conspiracy to defraud the Authority and the public. Thus, the court was left to consider the charges against each accused independently. With regard to the family and the related investors, the judge found that they had tried to disguise the purchase of shares by current shareholders (members of the family) and thus, taking account of the wide definition of acquisition, violated provisions of the prospectus, which stated that no current shareholders would purchase shares in the offering.

The meaning of "holding" or "acquisition" in relation to securities and voting power and similar issues was amended in July 1988 as part of the wide-ranging Amendment 9 to the Law. It now includes holding or acquisition by an individual alone or in conjunction with others, directly or indirectly, through the medium of a trustee, a trust company, a registration company, or by any other means.[115] So, a subsidiary or an affiliated company may be held liable for holding or making acquisitions on behalf a company. Similarly, trading by an individual includes all trades made by the individual, family members who live with him or whose livelihoods depend on one another.[116] As a result, they could be found guilty of deceit under Section 415 of the Criminal Law in their false representations and actions that lacked good faith when they procured the permit from the Authority and the right to register the shares for trading on the TASE. Further, these defendants had run afoul of the disclosure requirements in Section 16 of the Law. Their plan to purchase shares, in addition to directly contradicting to explicit statements in the prospectus, also should have been disclosed to the public, perhaps in an emphasized form, for the parties to fulfill their legal requirements of disclosure.

The judge went on to consider the criminal liability of the company itself. The judge stressed that a company, through its agents, could be guilty of criminal activity. On examination of the facts, the judge held that Abraham Rubinstein, in view of his exercise of significant control over the affairs of the company, represented the alter-ego of the company for the purposes of liability. Thus, once charges were proved

115. *See Rubinstein*, (1) P.M. at 89 (providing an example of the application of the wide definition of acquisition).

116. Securities Law, *supra* note 2, § 1(G).

against this individual, the company, for the purposes of criminal law, could also be considered guilty.

With these issues settled, the judge proceeded to the question of criminal liability as to the underwriters of the offering. While he felt confident in stating that the underwriters had some form of responsibility in regard to proper disclosure in the prospectus, the extent of such responsibility was an issue that raised great doubts. While the United States securities law establishes a test for underwriters based on whether a reasonable investigation would reveal facts that would be of interest to a prudent investor,[117] the Israeli law in this matter was subject to great debate among legal scholars.[118] However, the judge did say that it is clear that no comparison or assumptions about the underwriters' criminal liability may be made from the extent of the underwriters' civil liability as regards issues of disclosure, clearly spelled out in the Law. It is only based on the words of the statute that criminal liability could be established; as a result of the prevailing uncertainty in this area, any doubts had to be decided in favor of the defendants, following a cardinal principle of the criminal law. The remaining issues decided by the judge regarding these defendants and the others tend to turn on technical issues of interpretation of certain criminal and securities offenses. As a result, they will, where relevant, be discussed elsewhere in this article.

IV. SALES BY PROSPECTUS: PROCEDURAL CONSIDERATIONS

A separate chapter of the Law sets out the rules and procedures that must be followed in the placement and filling of orders for securities offered by prospectus. Amendment 9 changed a number of these provisions in a significant fashion. First and foremost, the Law was amended to provide for a shorter maximum duration in which orders may be received for an offering under a particular prospectus.

The lawmakers were obviously concerned to ensure that the information provided to potential investors by a prospectus remain as current as possible. As a result, the Law, as it stands today, provides that the period for receiving orders must not commence less than seven days, and must not terminate more than one month, after the date of the prospectus.[119] Further, the Authority is empowered to shorten the seven day period or to extend the one month deadline (provided that the date does not extend past six months, or twelve months in the case

117. *See* Section 11 of the U.S. Securities Act of 1933; Escott v. Bar Chris Constr., 283 F. Supp. 643 (S.D.N.Y. 1968); Feit v. Leasco Data Processing Equip., 332 F. Supp. 544 (E.D.N.Y. 1971).

118. *See, e.g.*, MEIR CHET, THE UNDERWRITING OF SECURITIES IN ISRAEL-THE CURRENT STATUS AND SUGGESTIONS FOR AMENDMENTS (Hamishpat A, 1993) (arguing in favor of expanding the Israeli law in this area); *see also Rubinstein*, (1) P.M. at 122.

119. Securities Law, *supra* note 2, § 24(a).

of a mutual fund, described as a "joint trust investment fund" in the Law), under such conditions as they might establish.[120]

The Law does not require circulation of preliminary prospectuses. Therefore, the Law requires that there be a specified waiting period between the date of publication of the prospectus and the actual completion of sales under that prospectus, thereby at least theoretically providing investors with an opportunity to study the prospectus and to make their investment decisions.

In addition, the Law provides for a broad area of discretion and responsibility for the Authority with respect to the post-publication amendment of the prospectus. Thus, the offeror, issuer, or any person who gave a report, permit, or opinion in the prospectus must inform the Authority of any material facts that have arisen or come to light and that are omitted from the prospectus as soon as they become aware of those facts.[121] If through this obligation of reporting, or by other means, between the time that the publication permit was granted and the expiration of the period for the placing of orders, the Authority learns of a fact that would have prevented the granting of the permit or caused the Authority to require that the draft prospectus be amended in a material fashion, then the Authority may demand, in a form or manner that it sees fit, that the offeror, after being granted an opportunity to present its case, print and distribute an amendment to the prospectus or an amended prospectus including the relevant changes or additions.[122]

The Law provides for the postponement of the period for the placement of orders if such an amendment is ordered. As a result of these postponement provisions, unless the Authority sets alternative dates, the offeror is precluded from accepting orders for securities from the date on which the Authority issues an order to amend the prospectus until the end of seven days following the publication of the required amendment.[123]

One of the other Amendment 9 changes was in the improved mechanism providing for the amendment of the prospectus, after its publication, on the initiative of the offeror. The new provision allows the offeror, before the expiration of the offer period, to apply to the Authority for permission to amend any particular in the prospectus; if that permission is granted, the prospectus is to be amended in accordance with the request.

The criteria established by the Law for the Authority to consider in the case of such an application are two-fold. The Authority may

120. *Id.* § 24(b).
121. *Id.* § 25(d).
122. *Id.* § 25(a).
123. *Id.* § 25(c).

certify such a request if, in its opinion, such a change is "necessary" or if the granting of such permission will in no way adversely affect the rights of any party who submitted an order for or acquired the securities before the amendment is published.[124] Similarly, the Authority is required to order the publication of an amended prospectus or an amendment to the prospectus if the financial reports of the offeror, issuer, or any other corporate entity whose reports are included in the prospectus are submitted to the Authority, presumably, although not specifically mentioned, pursuant to the periodic reporting requirements of the Law (Sections 36 through 38B) before the order period terminates.[125]

The Law also provides for an amending procedure in cases of technical, linguistic, printing, or similar errors. The offeror is to report on such an error to the Authority, publish notification of such in at least two wide-circulation, Hebrew language, daily newspapers in Israel, and include a copy of such a correction in each copy of the prospectus.[126]

The Law also provides a mechanism to protect investors who may have placed orders for securities before the publication of any of the amendments described above. Thus, any such investor may, without penalty, cancel his order within ten days of the publication of those amendments.[127] Hence, no unwitting investor is left to the discretion of the offeror, or the Authority for that matter, in deciding whether the amended prospectus contains provisions that may have caused him not to place his order. Upon receipt of a cancellation notice, the offeror must, within seven days, refund all funds paid by such an investor.[128] If the Authority orders the publication of an amendment, and the offeror decides not to undertake such a publication, then the offeror must, within seven days of the date set by the Authority as a deadline for the publication of the amendment, refund all monies paid by any investors for the securities.[129]

Attention is also paid to cases where refunds must be made for other reasons. For example, the offeror is obligated, within seven days of the termination date for orders to be placed, to refund to investors all payments if the total amount of orders placed does not reach the

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124. *Id.* § 25A(a).

125. *Id.* § 25A(b); note that Section 25A(c) of the Securities Law provides that the same postponement provisions, described above as applying in the case of Authority-initiated amendments, also apply in the case of these procedures.

126. *Id.* § 25C; the public notification by way of newspaper advertisement is similar to that required in Section 23(c)(2) of the Securities Law with respect to announcing the submission of the documents to the Registrar and the locations where copies of the prospectus may be obtained.

127. *Id.* § 26(a).

128. *Id.* § 26(b).

129. *Id.* § 26(c).

minimum amount, if any, stated in the prospectus as being the expected minimum consideration to be obtained through the offering.[130] In the converse case, where orders received exceed the total offered, presently a fairly common although not inevitable occurrence, the 1988 amendment to the Law established that the available securities be distributed in the manner provided in the prospectus rather than on a purely discretionary basis.[131] The allocation of securities under such a plan specified in the prospectus must be announced, within seven days of the end of the order period, in at least two Hebrew daily newspapers of general broad circulation appearing in Israel.[132] In this case, however, the offeror must refund the monies within two business days of the distribution of the securities to any investors whose orders were wholly or partly rejected.[133]

A further provision of the 1988 amendments to the Law, intended to protect and enhance the position of those who have placed orders for securities, mandates the steps to be taken by the offeror with the monies paid in consideration of offers. The Law establishes, notwithstanding a power granted to the Minister and the Finance Committee to provide otherwise by regulation, that the subscription payments be maintained in a separate trust account in a banking institution, until the status of the offeror's obligation to refund payments to investors under the above provisions is clarified.[134] Thereafter, the offeror, if required, must refund the funds and the accrued interest to the date of repayment to any investors whose orders were not filled.[135]

In addition to providing such mechanisms for the protection of investors, the Law also establishes an enforcement clause to give teeth to these provisions. If the offeror fails to fulfill any of its obligations regarding the refund of canceled orders or the maintenance of a separate trust account and repayments, and the offeror is a company, then the directors are to be jointly and severally liable, except for any director who has taken the appropriate steps to ensure the repayment of funds

130. *Id.* § 27(a).

131. *Id.* § 27(b)(1). In the recent Bank Hapoalim partial privatization public offering, the Finance Committee insisted that there be no maximum price fixed; the offering was, as a result, almost a total failure, so much so that a subsequently scheduled offering for Bank Leumi has been postponed indefinitely. The secret seems to have been that the institutional investors were not prepared to invest on an uncertain basis.

132. Id. § 27(b)(2). The various publication requirements of the Law have led recently to a proliferation of notices in the Israeli Hebrew language economic press. As a result of the substantial volume of public offerings, much more material appears than in a typical U.S. "tombstone" notice.

133. *Id.* § 27(b)(3).

134. *Id.* § 28(a), (c).

135. *Id.* § 28(b). This provision obviously secures the investors from the dangers of the arbitrary use of their funds while they await the results of the offering.

to any investors who do not receive the proper payments.[136]

The final area covered in this section concerns the notification of the results of a public offering. The Law provides that the offeror must inform the Authority of the results of the offering within seven days after the end of the order period or the date of allocation in cases of over-subscription.[137] Further, the Law provides authority for regulations to be issued with respect to these issues; that authority was exercised almost immediately with the passing of the Securities Regulations (Announcement of the Results of an Offer by Prospectus) in 1969. These regulations, adopted by the Minister after consultations with the Authority, provide the framework and content required in the report to the Authority on the results of an offering. First, the report must include the nominal value, by category, of the securities ordered, of orders that were canceled under Section 26(a) of the Law (described above), and of orders rejected, as well as the details of the provisions made for the refunding of payments for orders that were not filled.[138] Further, the report must detail the total consideration received for orders that were filled and the total nominal value of the securities, if any, acquired by underwriters.[139] In addition, in cases of over-subscription, the manner of allocating the securities among those who have ordered them must be included.[140] Lastly, all of the above details must be arranged according to the categories of the investors if all or part of the offering consisted of securities offered to specific categories of investors.[141]

A recent amendment to the Law created special arrangements for the processing by the Authority of public offerings by government companies being privatized or by the sale of controlling shares by the government in its banks.[142] The commentary to the proposal of the new law states that

> [b]ringing a government company to the position where it is feasible to privatize it [by a public offering] involves considerable preparation, including structural changes in the company and in the business branch in which it operates. In order to prevent a situation in which after the investment of great efforts in these subjects the privatization would be delayed, it is proposed that special procedures be adopted as to companies being so privatized.

The commentary points out the possibility that prospectuses

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136. *Id.* § 29.
137. *Id.* § 30.
138. Prospectus Regulations, *supra* note 39, §§ 1-4.
139. *Id.* §§ 5-6.
140. *Id.* § 7.
141. *Id.* § 8.
142. Government Proposed Law, No. 2226 (1993), adopted as Amendment 13 to the Law on Feb. 13, 1994.

might be used in such a situation with financial statements which would otherwise be stale under current regulations. The commentary continues by stating that, "sale of controlling share interests in banks is also a very important challenge" and should be subject to these special proposed rules. In adopting the amendment, the Knesset extended its scope to public offerings of substantial companies and conglomerates based on criteria to be established administratively.

V. PROSPECTUS LIABILITY

The 1988 amendments had a sweeping effect on the civil liability of various parties connected to the offering. Prior to the amendments, a number of limitations on the extent and scope of the liability severely hampered potential plaintiffs. First, the liability extended only to those individuals who purchased the securities as part of the original offering by prospectus. In a market where securities rapidly and frequently change hands, such a provision was unsatisfactory. In addition, the scope of the liability of experts whose opinions or reports were included in the prospectus was not sufficiently defined. Further, the provisions regarding the signing of the prospectus by the directors of the company and the resulting liability were viewed as unsatisfactory.

The amendments strengthened the system of civil liability for defective prospectuses. As a starting point, the amended Law extends liability to any party who signed the prospectus as required under Section 22 (described above). These parties are liable to any party who acquired the securities from the offeror, and to any party who purchased or sold such securities in trading on or off the TASE, for any damages caused to that party as a result of the inclusion of any misleading particular in the prospectus.[143]

The signatories under Section 22 must include the company, a majority of its directors, any underwriter, and the offeror, when the offeror is not also the issuer. The change in requirements under Section 22 for signatures is noteworthy. Previously, this section required that all directors of a company sign the prospectus. A case arose in which a distinct minority group within a board of directors refused to sign. Although the majority of the directors had approved a public offering, that public offering never took place due to the objection of the minority and their ability to frustrate the offering by a failure to

143. Securities Law, *supra* note 2, § 31(a). Section one of the Securities Law defines "misleading particular" as including a fact, matter, or omission that would be likely to mislead a reasonable investor. Although there is some theoretical, academic debate as to whether there is an implied requirement of materiality, it would appear that since a reasonable investor would only be likely to be affected by material matters, materiality is implied. *See, e.g.*, E. KINDERMAN, LIABILITY OF ACCOUNTANTS, LAWYERS AND DIRECTORS AS TO A PROSPECTUS, ROEH HESHBON 402 (1972/1973) (in Hebrew) (supporting the notion of implied materiality).

sign. A request for exemptive relief from the Authority was rejected on the grounds that there was no available statutory authority for the granting of an exemption in such a case. The amendment to Section 22 was the Knesset's response to this dilemma. However, to negate any view that a non-signing director could escape liability arising out of the prospectus, the Law was also amended to provide that all directors of the company serving on the date that the final prospectus received approval by the board are deemed, for purposes of liability, to have signed the prospectus unless they can prove that they either (1) did not know about the prospectus and ought not to have known about it or (2) that they submitted a written statement to the Authority immediately upon becoming aware of the presence of a misleading particular in the prospectus.[144] The statute of limitations on such claims is the earlier of two years from the date of purchase by the plaintiff or seven years from the date of the prospectus.[145]

The Law, as amended in both 1988 and 1990, also overhauled the provisions surrounding the liability of experts whose opinions, permits, or reports were included in the prospectus. Despite initial confusion as to the scope of liability, it now is clear that the liability of such experts is limited to the information included in the prospectus, permission for the inclusion of which was received by the offeror prior to their publication.[146] The extent of the liability, the available defenses, and the limitation period on such claims is identical to those that are established for the other signatories.

The Law provides for a number of defenses to potentially liable parties for including misleading particulars. First, liability will not be incurred by any party who can prove that he took all necessary steps to insure that no misleading particulars were included in the area covered by his liability, that he believed in good faith that no such particulars were present, and that he fulfilled his obligation to immediately report any particular that might lead the Authority to require the amendment of the prospectus.[147] A similar complete defense is available against any plaintiff who knew or ought to have known about the presence of the misleading particular at the date of his purchase of the securities.[148] Third, a defense is available in any case where the issuer has submitted an immediate report to the Authority correcting any misleading particular, notification of such correction was publicized in a fashion similar to the publicity requirement deriving from the original offering, and the purchaser bought the securities

144. Securities Law, *supra* note 2, § 31(b)-(c); *see also id.* § 22 (regarding provisions concerning board approval and signature by the directors).

145. *Id.* § 31(b).

146. *Id.* § 32.

147. *Id.* § 33(1); *see also Id.* § 25(d) (concerning the report obligation discussed above).

148. *Id.* § 33(2).

after the date of the publication of that notice.[149] Finally, any individual who incurs liability as a result of being a signatory, of being viewed as a signatory for the purposes of liability, or due to his opinion or report being included in the prospectus, can escape liability if he submits to the issuer, in writing, notice regarding the correction of any misleading particular in the document; such a defense is only effective against a purchaser who acquired the securities more than twenty-four hours after the submission of such a notice.[150] If more than one party is liable to a purchaser under these provisions, the responsible parties are jointly and severally liable to each injured party. The distribution of liability among the defendants is governed by the same principles that control contributions between tortfeasors under the laws of tort.[151]

Even in cases where damages may not have been incurred, the purchaser from the issuer may cancel any purchase made in reliance on any misleading particular in the prospectus. However, to receive full refund of the consideration paid, the purchaser must cancel within a reasonable time after becoming aware of the misleading particular or after publication of an immediate report regarding the correction of that misleading particular. The Law limits the right to cancel to two years following the acquisition.[152] The right to cancel the purchase is available against an issuer even if the issuer is in the midst of liquidation proceedings.[153]

Two other areas of civil liability bear mention in this context. The first concerns the liability of interested parties. In certain circumstances described below, an interested party, the company, or other entity in which he holds an interest may be required to submit to the Authority, the Registrar, the TASE, or to include in the prospectus, certain reports or notices.[154] In such a case, the provisions regarding liability of signatories and experts for misleading particulars in notices or reports will also apply to interested parties .[155]

The second area is the surprisingly wide liability of the issuer to holders of its securities for any damages suffered as result of the issuer's violation of any provision of the Law or any regulations made thereunder, of the Joint Investments Trust Law 1961 or regulations made thereunder, or of the trust indenture under which the issuer incurs an obligation towards the trustee in favor of holders of obliga-

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149. *Id.* § 33(3) (1968); *see also id.* § 23(c)(2) (describing the notice procedures discussed above).

150. *Id.* § 33(4).

151. *Id.* § 34(5).

152. *Id.* § 35(a) (providing for this specially short limitation period).

153. *Id.* § 35(b).

154. *See* Id. §§ 36-37 (describing the conditions regarding such reports or notices).

155. Id. § 38B; *see also id.* § 1 (defining an "interested party," as described above).

tion certificates issued by him.[156] This liability applies to directors of the issuer, its general manager,[157] and its controlling parties.[158] It is not clear how the latter liability will combine with or augment the other liabilities of the parties in cases where they happen to intersect. For instance, where a prospectus contains misleading particulars, it is unclear whether liability would extend to the general manager and controlling persons. It would be anomalous if the Knesset intended this result, considering its detailed description of the signing requirements under Section 22 and the cross-reference in the prospectus liability sections to those requirements. Yet, the result is hard to avoid under ordinary rules of statutory interpretation.

It should be noted at this point that the Israeli securities markets were founded and have for years been controlled by Israel's commercial banks. Despite major problems involving the banking system and a government appointed investigatory commission that suggested reform, Israeli securities markets continue to be dominated by commercial banks, which have various functions (commercial banking, brokerage, investment companies and the like). Israel has never had the equivalent of the U.S. Glass-Steagall Act,[159] although interestingly enough just as Glass-Steagall is being liberalized and relaxed in the United States, Israel is considering ways of separating the banking and brokerage functions.

Another important question is the degree of liability extending to an underwriter that signs a prospectus, and the level of diligence required by underwriters examining the prospectus. The 1985 case of *Kaufmann v. First Int'l Bank of Israel*, decided in the District Court of Jerusalem, raised some pertinent questions concerning the role of the underwriter in the case as a secondary issue.[160] The case dealt with a claim for damages against the defendant bank, which had originally planned to serve as underwriter of the plaintiff company's public offering. After making numerous demands and receiving subsequent partial concessions regarding the contents of the prospectus, the bank, at the last moment, decided not to proceed with the underwriting. The bank claimed that the company and its principals had withheld vital facts and misrepresented certain circumstances throughout the relevant period. The bank's withdrawal gave the defendants short notice before the deadline set by the TASE for the offering expired. As a result, the public offering was abandoned. The plaintiffs demanded damages for

156. *Id.* § 52K(a).

157. In other words, using the terminology prevalent in English companies law, a senior executive officer of the company who is not a director.

158. *Id.* § 52K(b).

159. This was formally known as the Banking Act of 1933. It forced commercial banks out of the investment banking business.

160. Kaufmann v. First Int'l Bank of Israel, (1) P.M. 265 (Dist. Ct., Jerusalem 1988).

losses incurred by the company and its principals in the abortive public offering.

The court ruled that the bank had acted in good faith in its negotiations with the company and in its sudden last-minute withdrawal, despite suspicions that were obviously aroused by the timing of its actions. The court based its decision on a wide understanding of the underwriter's civil (Section 31 of the Law) and criminal (Section 53 of the Law) liability for the contents of the prospectus. Since the underwriter accepts this wide liability, it must undertake a continuing, diligent examination of the company that encompasses, among other things, the contents of the prospectus itself, the company's financial situation, and the suitability of its officers.

Further, the court decided that the general understanding between an underwriter and a company prior to the offering is just that and no more. Only upon the signing of the underwriting agreement, immediately prior to the offering, does the general understanding convert into a legal contractual obligation. As a result, the underwriter reserves the right to withdraw from the process at any point that it feels it lacks the requisite confidence of the veracity and accuracy of the information in the prospectus. The question of good faith in these situations is of a subjective nature. Due to the suspicious circumstances encountered throughout the process, the court felt that the underwriter in this case was justified in its withdrawal, even at a late stage. Thus, the extent of the underwriter's potential liability required its due diligence in investigating the company and the prospectus, and it could subsequently justify its withdrawal if unsatisfied with the results of such inquiries.[161]

VI. TRUST INDENTURES

The 1988 Amendment added a new chapter providing for the appointment of a trustee, including the execution of a trust indenture, before any corporate entity may offer any ordinary or convertible debentures to the investing public.[162] While certain of these provisions

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161. For an interesting comparison of the issues regarding the extent of the underwriter's civil and criminal liability, see *Rubinstein*, (1) P.M. at 89, where the District Court of Tel Aviv-Jaffa, a few short years later, was much less settled and much less clear on the extent of the underwriter's liability, both civil and criminal, for contents of the prospectus. The *Rubinstein* court did not refer to the *Kaufmann* case in its proceedings. It did decide, however, that regardless of the extent of the civil liability of the underwriter -- thus requiring underwriters to undertake a wide investigation -- no such conclusions could be reached regarding the scope of its criminal liability.

162. Securities Law, *supra* note 2, § 35A (establishing that the trust indenture provisions apply to "certificates of obligation"). This term, in turn, is defined as serial certificates issued by any company or other similar entity that grant to the holders the right to claim cash payments from the company or entity at a given

have proved controversial, overall they have been viewed as a positive step towards increasing the protection of the rights of the investors with respect to this type of security, where the absence of voting rights and participation in the affairs of the corporate entity often render the investors vulnerable.

The Law establishes as an absolute precondition the appointment of a trustee by a trust indenture in accordance with the terms of the Trust Law 1979 (the "Trust Law").[163] The Law also provides that the trustee must be a company registered in Israel and whose main occupation is trusteeship.[164] In addition, the trustee must have certain minimum levels of paid-in capital before it can engage in its business. It must hold equity in an amount at least equal to the total amount, or a proportion thereof, of the value of the debentures for which it acts as trustee, according to such regulations as the Minister, with the approval of the Finance Committee, shall determine.[165] Requiring a measure of paid-in capital, rather than possible alternatives such as the trustee's total capital or net worth, has proved less than satisfactory. Establishing one of the suggested alternatives as a minimum standard could more effectively serve the primary purpose of this particular provision, insuring the financial stability of the trustee company. Further, the Minster, after consulting the Authority and on the approval of the Finance Committee, is empowered to enact additional regulations regarding the permitted manner of investment of the equity of the trustee company and the submission of reports to the Authority regarding such investments and changes thereto.[166]

The chapter proceeds to detail certain circumstances that serve to disqualify a company from serving as a trustee; a company is deemed ineligible if any of the following hold true: (1) a director or officer of the company is also a director or officer of the issuer, its parent company, or of an affiliated company; (2) circumstances exist that suggest the possibility that conflicts between the interests of the trust company, its parent company, or of an affiliated company, and those of the owners of the debentures may arise; (3) the company has begun winding-up proceedings or receivership; or (4) the company or a director or officer thereof have been convicted of an offense that would call their

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date or on the occurrence of a specified condition but do not grant a right of membership or participation in the company or other entity. In addition, the definition includes certificates that are convertible into shares or other securities that grant the right to purchase such certificates, to the exclusion of certificates that are issued by the State or issued under the provisions of a special law. An interesting parallel to these new provisions is the U.S. Trust Indenture Act of 1939.

163. Securities Law, *supra* note 2, § 35B(a).

164. *Id.* § 35C.

165. *Id.* § 35D(a).

166. *Id.* § 35D(b).

credibility into question.[167]

The trust indenture signed by the issuer and the trustee is one of the central features of the trust mechanism. For the benefit and protection of the holders, the Law requires the trust indenture to contain certain terms regarding the activity of the trustee: (1) the total amount of liability assumed by the issuer in relation to the debentures, including a description of and the enforcement capability attached to any guarantees, liens, or other undertakings that are meant to secure the liability; (2) the means for the release or exchange of any such guarantees or similar undertakings; (3) the conditions and circumstances under which the trustee company will be able to demand the immediate redemption of the debentures or the realization of any guarantees or similar undertakings which the issuer used to secure its liability; (4) the obligation of the trustee to call meetings of the debenture holders and the procedures to be followed in those meetings; (5) the fees to be paid to the trustee, either as a set sum or as a percentage of the total of the obligation under the debentures; and (6) any other matter required in regulations that the Minister may enact, after consultation with the Authority and with the approval of the Finance Committee.[168] The Law further protects holders by stating that changes to the trust indenture may only be made if either the trustee is convinced that the change does not adversely affect the interests of the holders, or the holders, at a general meeting, approve of the proposed change by special resolution.[169]

The Law provides a detailed description of the obligations of the trustee with respect to the debenture holders. As a general principle, the trustee must act in the best interests of all of the holders.[170] Further, the trustee is assigned wide responsibility with regard to taking all necessary steps to insure, before the payment of any monies in consideration of the debentures, the validity of any guarantees or similar undertakings from the issuer or any third party in favor of the holders; in addition, the trustee must ascertain and is responsible to the holders for the accuracy of the description of these matters in the prospectus by which the debentures are offered to the public.[171] If the trustee becomes aware of any material violation of the terms of the trust indenture on the part of the issuer, it must notify the holders of the violation and of the steps taken by it to prevent such violation or

167. *Id.* § 35E.

168. *Id.* § 35F.

169. *Id.* § 35G. The meeting must be attended by holders representing at least fifty percent of the outstanding balance of face value of the relevant series of debentures. Alternatively, an adjourned meeting must include the representation of at least ten percent of that balance.

170. *Id.* § 35H(a).

171. *Id.* § 35H(b).

to insure that the issuer fulfills its obligations.[172] Although not granted the right to vote, the trustee must attend and participate in the general meetings of the issuer in order to assure the representation of the interests of the holders.[173] Also, specific provisions are made for the preparation of the annual trusteeship report and the availability for inspection thereof by the holders of the debentures.[174] Lastly, the trustee company is obligated to represent the holders in any matters arising from the obligations that the issuer has assumed towards them.[175]

The trustee is granted the legal right to receive such reports as the issuer may be required to submit to the Authority, in addition to receiving copies of any documents that the issuer may send to its share or debenture holders. Further, the issuer is obligated to turn over any information reasonably requested by the trustee.[176] In addition, the Minister is authorized to adopt regulations regarding special reports that the issuer may be required to submit to the trustee regarding the guarantees and similar undertakings that the issuer has given to secure its liability to the holders.[177] As is clear, the lawmakers have required the issuer to cooperate with the trustee, in a number of respects, in order to insure that the protection of the investors is not sacrificed due to a scarcity of information flowing between the two parties to the trust indenture.

In order to avoid the possibility of conflicts of interest, the Law provides that the trustee is not permitted to acquire or hold, for its own account, any of the debentures of the series for which it is acting as trustee. In addition, the trustee is disqualified from holding for its own account any securities of the issuer, its parent company, its subsidiary, or of an affiliated company.[178] For similar reasons, the trustee is excluded from executing any transactions on behalf of another party, by way of a power of attorney that grants freedom of discretion, in relation to any securities for which it is serving as trustee.[179]

In order to insure that the interests of the holders are not compromised, the Law provides that the actions of the trustee are valid regardless of any defects discovered in regard to its appointment or qualifications.[180] In addition, the Law sets specific conditions regarding the termination of the service or the resignation of the trustee. A trustee may resign by written notification to the party who appointed him;

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172. *Id.* § 35H(c).
173. *Id.* § 35H(d).
174. *Id.* § 35H(e).
175. *Id.* § 35I.
176. *Id.* § 35J(a).
177. *Id.* § 35J(b).
178. *Id.* § 35K.
179. *Id.* § 35L.
180. *Id.* § 35M.

however, the resignation is only effective if approved by the court and only from the date of such approval.[181] Further, the term of the trustee is automatically concluded if the trustee fails to continue to meet any of the qualifications set out above, including those related to minimum equity.[182] The Law also grants power to the court to dismiss a trustee if it fails to fulfill its duties properly, or if the court sees fit to do so for other reasons.[183] Finally, the holders of ten percent of the outstanding balance of the face value of a particular series of debentures may call a general meeting to initiate an action to dismiss the trustee. At the general meeting, the holders may remove a trustee by a vote of fifty-percent of the outstanding balance.[184] On the expiration of the term of the trustee, the court may appoint a replacement for a term and under such conditions as it sees fit; in the interim period, the trustee whose term has expired continues to serve as trustee.[185]

The Authority is also granted a role as to these matters. The Authority is authorized to apply to the court with regard to any of the provisions described in the preceding paragraph.[186] However, the Authority's role, as protector of the holders in court proceedings, is not limited to the period surrounding the expiration of the trustee's term. The Authority and the TASE must be informed, in writing, of the commencement of any court proceedings to which the trustee is a party.[187] When the chairman of the Authority believes that the interests of the holders are liable to be affected or involved in such civil proceedings before the court, he may appear in those proceedings and have his say regarding the matter.[188] This is a rare instance, but not the only one, in which the Law specifically assigns a responsibility to the chairman of the Authority and not to the Authority as such.

In short, the Law requires an effective mechanism by which the trustee arrangements are implemented in order to protect the interests of the investing public. Through the provisions outlining the obligations of the various parties, including the provision of information to the trustee by the issuer and the trustee's participation in the issuer's general meetings, the holder of a debenture is offered a level of protection heretofore unavailable under Israeli law.

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181. *Id.* § 35N(b).

182. *Id.* § 35N(a). The disqualifications are enumerated in Sections 35C, 35D(a), & 35E of the Securities Law.

183. *Id.* § 35N(c).

184. *Id.* § 35N(d).

185. *Id.* § 35N(e).

186. *Id.* § 35N(g).

187. *Id.* § 35O(a).

188. *Id.* § 35O(b).

VII. CONTINUOUS DISCLOSURE

A. *In General*

The Authority's responsibilities do not end after a public offering is effected. Instead, the Authority has a continuing responsibility to insure fair practice on the part of companies whose securities are held by the public. As a result, the Law and the related regulations provide for a system of reports to the Authority and the TASE on a periodic basis and on the occurrence of certain events, in order to facilitate continuing supervision by the Authority and the TASE and to furnish vital information to the investing public. These reports in a broad sense follow the pattern of periodic reporting called for by the U.S. Securities Exchange Act of 1934.

Any entity whose securities have been offered to the public by prospectus and are still held by public investors must submit reports to the Authority and to the Registrar of Companies. If the securities concerned are also traded or registered to be traded on the Stock Exchange, such documentation must also be sent to the TASE.[189] Because of the special structure of Israeli tax law, which provides for total exemption from capital gains tax where securities are listed on the TASE, essentially all publicly traded securities are listed and, as a practical matter, essentially all reports are rendered to the TASE as well.[190]

The underlying purpose of these provisions is to facilitate a regular flow of information about public companies to investors and potential investors, based on the overriding doctrine of disclosure of any information that the reasonable investor who is considering the purchase or sale of securities would consider important.[191] This doctrine, like the principle behind disclosure of information in the prospectus, reflects the Law's goal to protect the interests of the investing public by furnishing it with a continuous flow of information about companies extending beyond the issuance of a prospectus. As a result, the Law adopts the same general guidelines for the regulations concerning current reports as for those concerning prospectuses.[192] The Authority is also empowered to demand further particulars from the company regarding information contained in the reports or to require additions or amendments to the reports where the Authority deems it necessary.[193]

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189. *Id.* § 36(a).

190. In August 1994, the Government announced its intention to tax TASE gains as of January 1995; that action will require legislation.

191. *Id.* § 36(b)-(c).

192. *Id.* § 36(c); *see also id.* § 17(b) (providing the guidelines concerning the prospectus regulations, as discussed above).

193. *Id.* § 36(d)-(g).

The 1988 Amendments to the Law established a framework enabling the Authority to issue temporary directives to specific companies whose shares are traded publicly. The Authority may also issue directives of general application regarding the inclusion of certain particulars in the reports. The Authority may, if necessary to protect the investing public, issue a directive to a company specifying the manner of presentation of a certain particular in the company's annual financial, current, or immediate reports, as long as instructions regarding this issue are not already in force by power of regulations made under Sections 17 and 36 or by accepted reporting or accounting principles.[194] If the Authority believes that the interests of the public thus require, it may issue such instructions as temporary directives for all reporting bodies, made public in accordance with a method established by the Authority's Chairman.[195]

Directives issued by the Authority are effective for one year and may be renewed, on the approval of the Minister, for another year.[196] Presumably to ensure the fair and uniform application of these provisions, the Authority is required, within sixty days, to issue such a general directive if it has issued individual instructions with respect to a specific matter to more than one company.[197] Finally, as representative of an interested party in these directives, the President of the Israeli Chamber of Accountants is granted a statutory right to state his opinion to the Authority on the relevant provisions, both before the general directives are issued and before they can be extended. In return, the Chamber of Accountants may publicize an opinion regarding the directives while they are in effect only with the permission of the Authority.[198]

B. *Regulations Regarding Reports*

The principal regulations that have been promulgated under the authority of Sections 17 and 36 of the Law are the Securities Regulations (Periodic and Immediate Reports) 1970 (the "1970 Regulations) and the newly issued Securities Regulations (Preparation of Annual Financial Reports) 1993 (the "Annual Report Regulations"). While each of these sets of regulations will be examined in turn, it is clearly beyond the scope of this article to engage in a discussion of the minute technical details of the regulations. A discussion of general principles, with a focus on legal, as opposed to technical, aspects, follows.

The 1970 Regulations establish the timing, manner, and content of the various periodic and immediate reports that are required to be

194. *Id.* § 36A(a).
195. *Id.* § 36A(b).
196. *Id.* § 36A(c).
197. *Id.* § 36A(d).
198. *Id.* § 36A(e).

submitted to the authorities. In general, the reports must be legible and constructed in a manner prescribed in these regulations and must be signed by the company before their submission to the Authority and the Registrar.[199]

C. *Periodic Reports*

Chapter two of the 1970 Regulations establishes the framework for the submission of annual reports on the part of companies whose securities have been offered to the public by prospectus or are traded on the TASE.[200] The date for the submission of the annual reports is fixed as within four months of the end of the company's accounting year, provided that the report is presented by the date of the earlier of at least fourteen days before the date set for the general meeting at which the financial report of the company will be presented or within fourteen days of the date of signing of the accountant's opinion and of the audited reports of the company.[201] The particulars that are detailed below as requiring inclusion in these reports should be divided into separate statements regarding the accounting year which they cover and regarding the remainder of the report period.[202]

The first area covered by the regulations is the inclusion of financial reports of the company.[203] The regulations require the presentation of properly audited annual financial reports as of the date when the accounting year of the company ended, drawn up in accordance with the 1993 Regulations.[204] In addition, the company must include

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199. Securities Regulations (Periodic and Immediate Reports) 5730-1970, §§ 2, 3, 5 (1970) (Isr.) [hereinafter 1970 Regulations].

200. *Id.* § 2.

201. *Id.* § 7.

202. *Id.* § 8. Section 6 of the 1970 Regulations defines "report period" as the period beginning and ending with the respective start and final dates of the company's fiscal year, as long as the report is submitted within three months of the end of that year. If, however, the report is not submitted until after that three month period, then the report period includes the time period until the date of the report. This is, in turn, defined as the date of the signing of the periodic report, provided that it is within fourteen days of its being sent to the Registrar and the Authority.

203. Section one of the 1970 Regulations defines "financial reports" as including the balance sheet, profit/loss statement, report on changes in the company's equity, report on changes to its financial situation, and explanatory notes.

204. 1970 Regulations, *supra* note 199, § 9(a). Section 65 of the 1993 Regulations repealed previous Securities Regulations, Preparation of Financial Reports (1969). As a result, Section 67 of the 1993 Regulations provided an interim measure by which corporate entities could submit annual financial reports drawn in accordance with the repealed regulations as part of their periodic reports. These reports are submitted before February 28, 1993, and contain financial reports for the accounting year ending December 31, 1992. Obviously, the interim measures are no longer effective and all references to annual financial reports made in the Law and the Regulations now refer to the 1993 Regulations, discussed below.

a dated and signed opinion of the accountant for the company regarding the audited financial statements of the company and its consolidated financial statements, including confirmation of their conformance with the provisions of the 1993 Regulations.[205] A similar opinion of an accountant must be included regarding the financial report of any subsidiaries whose reports were attached to the reports of the company.[206]

Another area that must be covered by the periodic report is the use made of the funds raised by the sale of the securities offered by the last prospectus published before the date of the report. In general, the report must provide a breakdown of the various objectives specified in the prospectus and the status of progress made towards achieving these objectives.[207] Such a breakdown must be included in the periodic report of the company until all of the funds received pursuant to the offering have been expended and until a report that specifies the final breakdown of the application of the consideration has been submitted.[208]

Furthermore, the report must include an itemized description of the investments of the company in any of its subsidiaries or affiliated companies, with particular attention paid to the changes in these investments over the report period and the essential terms of the transactions that brought about such changes.[209] In addition, the report must include the profit/loss statement of each of the relevant subsidiaries and affiliated companies, adjusted as to the date of the company's annual financial statement, particularly specifying the dividend payments, management fees, and interest payments that the company has received or is due to receive from these other companies.[210]

If the granting of loans is one of the main business pursuits of the company, then the report must include a detailed list outlining the categories of loans and the outstanding balances owed to the company.[211] Also, details surrounding the occurrence of any special event that occurred during the report period that, in the opinion of the directors of the company, has had or is likely to have a material effect on the profits, assets, or liabilities of the company, must be divulged.[212]

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205. 1970 Regulations, *supra* note 199, § 9(b).
206. *Id.* § 9(c).
207. *Id.* § 10A(a)-(c).
208. *Id.* § 10A(d).
209. *Id.* §§ 11-12.
210. *Id.* § 13. Section 1 of the 1970 Regulations defines the term "adjusted" as referring to a multiplication to give effect to changes in the Consumer Price Index (including fruits and vegetables) as published by the Central Bureau of Statistics or to changes in the foreign currency exchange rate.
211. *Id.* § 14.
212. *Id.* § 15.

Along the same lines, the company must report on any changes in its registered, issued, or paid-up capital during the report period.[213] Further details that must be included regarding the outstanding capital of the company include the terms of any issues of shares for which full consideration in cash was not received and the particulars of any options for the purchase of securities of the company which were granted.[214] Lastly, details of the registration of the company's securities for trading on the TASE or the termination of such trading during the report period must be explained.[215]

The report must also include certain information regarding some of the internal transactions of the company. The report must detail any salaries and benefits, received or due to be received, by any interested party in the company, either directly or indirectly, from the company, any subsidiary, or any affiliated company. However, the overall payments made to the directors and to the general manager, as long as they do not deviate from accepted standards, can be reported as a total sum rather than in an itemized form for each individual.[216] The nature of any interest that an interested party in the company has or had in any transaction during the report period in which the company, its subsidiary, or affiliated company was a party thereto, unless such transaction was undertaken in the ordinary course of business of the company, must also be included.[217] Similarly, the report must describe the parties and substantive content of any material agreement made during the report period, unless the agreement can be described as being in the company's ordinary course of business. This includes, but is not limited to, any agreement under which a party consents to serve as underwriter to a public offering or as a trustee for an offering of corporate debentures.[218]

The last general area covered by the regulations regards the disclosure of information regarding various individuals who are involved

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213. *Id.* § 16.

214. *Id.* §§ 17-18.

215. *Id.* § 20.

216. *Id.* § 22. Section one of the 1970 Regulations establishes that the definition of "interested party" is the same as that given in Section one of the Securities Law. The Companies Ordinance, Amendment 6 (1983) (New Version), however, made a change by expanding the reporting of payments made to the five officers with the highest salaries in the company. The amended provision requires that the company includes in its periodic reports the total payments and benefits, including any cash or cash equivalent, loans, securities or any credit or benefits, made to these five individuals during the report period, that are not a result of the officer's capacity as a shareholder alone. The report must specify all payments made during that period, including any termination benefits. These details must be included regardless of whether the payment was made by the company itself or by one of its subsidiaries, affiliated companies or parent, and whether the payment was made to the officer himself or to another person on his behalf.

217. *Id.* § 23.

218. *Id.* § 25.

as shareholders or officers of the company. The required list of shareholders must include only the nature and quantity of the holdings of interested parties in the reporting entity and in its subsidiaries and affiliated companies.[219] For the purposes of this section, the regulations establish that the manager of any investment fund be considered as the holder of the securities in the fund's assets and that a subsidiary be automatically considered an interested party.[220] In addition, the report must list the directors of the company along with a variety of personal and professional information regarding each of them. Perhaps the most significant item, from the investor's viewpoint, is the disclosure, to the best of the company's and its directors' knowledge, of any familial relation between the listed directors and any interested party in the company.[221] A slightly less detailed description of the remaining ranking officers in the company must also be included along with a disclosure of the accountants of the company and any interest or office of rank held by the auditor or his partner or by a relative of one of those in the company.[222]

Interest has been expressed in regulating the benefits granted to interested parties. On January 13, 1994, Dan Tichon, a senior member of the Knesset, advised the press that he is preparing a proposed private law that would restrict the attractiveness of options that could be granted by a company to interested parties in a public offering context by requiring that the exercise price of such options be at least at a price equal to 95% of the public offering price of the underlying shares.[223]

The regulations concerning periodic reports conclude with the listing of certain miscellaneous information that must be included. Examples include the address and telephone number of the relevant entity and description of any changes made to the Memorandum or Articles of Association of the company during the report period.[224] Lastly, both the recommendations of the board of directors before the general meeting and decisions of the directors that do not require the

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219. *Id.* § 24(a)-(b).

220. *Id.* § 24(c).

221. *Id.* § 26. Section one of the 1970 Regulations defines the term "Relative" in the same way as does Section 52A of the Securities Law. However, no definition of the term is given there. It is likely that the regulations intend to refer to Section one of the Securities Law, which defines "relative" as "a spouse or a sibling, parent, grandparent, offspring, or spouse's offspring or a spouse of any of these."

222. Id. §§ 26A, 27. The term "ranking officer" is defined in Section one of the 1970 Regulations as including "the directors, general manager, vice- and deputy-general manager, accountant, internal auditor, and any person who fulfills such duties under a different title; also, any other employee of the entity who holds five percent or more of either the outstanding nominal share value or of the voting power of the body."

223. HA'ARETZ, Jan. 14, 1994, at 1C.

224. 1970 Regulations, *supra* note 199, §§ 25A, 28.

approval of the general meeting regarding the following matters must be included in the report: (i) the distribution of any dividends or bonus shares; (ii) changes in the registered or issued capital of the entity; (iii) changes in the Memorandum or Articles of Association of the company; (iv) the redemption of shares; (v) the early redemption of debentures; and (vi) any transaction between the company and an interested party in it if the transaction does not conform to market conditions.[225] In addition, decisions of the general meeting that do not accord with the recommendations of the directors about the above-listed matters must be stated, along with a disclosure of any decisions taken at extraordinary general meetings and any decisions, copies of which must, under law, be sent to the Registrar.[226]

D. *Immediate Reports*

In addition to the regular periodic reports, companies are required to submit immediate reports to the Authority and to the Registrar under certain circumstances. Generally, the report must be furnished to the relevant authorities as near as possible to the date of the pertinent event occurring or the company's becoming aware of such an occurrence; in all cases, the report must be made within seven days of the occurrence of the event and must be submitted before the germane information is made public by the company or its directors.[227] For the sake of clarification, the regulations state that publicizing the information on the TASE does not exempt the company from its obligations under this Law.[228] The regulations continue by establishing a residual discretion for the Authority to request that an immediate report be submitted regarding any event that the Authority considers to be important to the reasonable investor, despite the absence of a particular provision in these regulations requiring a report on such an occasion.[229]

The regulations proceed to identify a long list of events that trigger an obligation under this section. The first such event is a change in the issued share capital of the company, otherwise than by a public offering pursuant to a prospectus. When a change occurs, the company must describe it and identify the consideration paid or to be paid for such an issue of securities.[230] Similar information must be reported in cases where the company grants options or rights to purchase any of

225. *Id.* § 29(a).

226. *Id.* § 29(b)-(c).

227. *Id.* § 30(a)-(b). Section 30(c) of the 1970 Regulations creates an exception for reports under Section 37(a), which refers to decisions or recommendations of the board of directors to the general meeting, that must be submitted within two days of the decision or recommendation being adopted.

228. *Id.* § 30(b).

229. *Id.* § 30A.

230. *Id.* § 31.

its securities.[231]

The next group of regulations covers the holdings of and transactions involving interested parties in the company. The first such requirement arises in situations where a change has occurred in the holdings of an interested party in any of the categories of securities issued by the company, its subsidiaries, or an affiliated company. When such a change occurs, the company must file a detailed report that includes the following: (1) the name of the interested party; (2) the identity of the relevant security; (3) the date of the change; (4) the manner of the change occurring (e.g. by sale, purchase, bonus shares, etc.); (5) if the change was through acquisition or sale, then whether it was by way of trading on the TASE or outside of that framework, and if the change was by way of acquisition from an issue, whether such issue was to the public or by way of rights; (6) the number of securities held by the interested party both before and after the relevant change; (7) the price at which the change was executed and the total consideration received, including details of any arrangements for deferred payment; (8) the date, where relevant, for the delayed transfer of the securities; (9) the total proportion of the outstanding share capital of the company held by the interested party after the change; and (10) the total proportion of the voting power in the company held by such a party after the change.[232] Similar details must be provided, in addition to a description of the person's address and itemized holdings in the company, its subsidiaries, and affiliated companies, when such a person first becomes an interested party in the company.[233]

Various stages of reporting also surround the execution of a transaction between a company and a party interested in it. When negotiations between parties begin, the company must inform the Authority immediately regarding the contemplated transaction (the sides involved, its nature, size, and other details), if the proposed bargain is not pursuant to market conditions.[234] The Authority has the discretion to require the company, within a specified period, to submit a full, immediate report to the Authority and to the Registrar regarding the progress of the negotiations.[235] Finally, upon completion of the contemplated transaction, the company is obligated to file a further report

231. *Id.* § 32.

232. *Id.* § 33(a). Note that an additional immediate report, including reasons for such, must be submitted if the conditions regarding deferred payment or delayed transfer of title are not fulfilled in accordance with the conditions described in the initial report.

233. *Id.* § 33(b). Section 33(c) of the 1970 Regulations provides that for the purposes of this section, a subsidiary of a company is deemed to be a party interested in it. *See, e.g.*, Israel v. Elman, (1) P.M. 343 (1990) (dealing with a violation of the provisions of this section).

234. 1970 Regulations, *supra* note 197, § 33A(a).

235. *Id.* § 33A(b).

to the authorities.[236]

The next area covered by the regulations concerns changes in certain personnel of the company. If a ranking officer or alternate director ceases to be employed, then the name of such an individual, the vacated position, and the date of his departure must be reported; further, the report must indicate either that the circumstances surrounding the departure are not of a type that need to be brought to the attention of the shareholders or that the circumstances, which must then be specified, are in fact of such a variety.[237] Conversely, if an individual is appointed to a position of a ranking officer or alternate director, an immediate report must be filed, including, as the case may be, the same personal and professional details concerning that individual that must accompany the list of directors or the list of ranking officers submitted as part of the periodic report.[238]

The same dual scheme exists for immediate reports upon the termination of the employment of and the appointment of accountants of the entity. On the one hand, if an accountant ceases to be employed by the company, the name and the date of his departure must be included. In addition, the report must include a statement either that the circumstances surrounding the departure are not of the type that need to be brought to the attention of the shareholders or that the circumstances, which then must be detailed, are of that nature.[239] On the other hand, if an accountant is appointed, a report must be filed that includes the name and address of the new accountant, the date of the appointment, and the fact, if relevant, that the accountant, one of his partners, or a relative of either is an interested party or ranking officer in the company.[240]

The regulations then list a variety of miscellaneous situations that also require the submission of an immediate report. One such example is a report on the failure or the delay in the implementation of one or more of the objectives of the use of the consideration listed in a prospectus.[241] Further, a company must report on the date, place, and planned agenda for the calling of a general meeting, including special meetings called under Companies Ordinance (New Version) 1983.[242] In addition, a company must file an immediate report outlining the recommendations of the directors before the general meeting and decisions of the directors not requiring further approval regarding the fol-

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236. *Id.* § 33A(c).

237. *Id.* § 34(a).

238. *Id.* § 34(b); *see also id.* §§ 26, 26A (providing the required details regarding directors and other ranking officers).

239. *Id.* § 35(a).

240. *Id.* § 35(b); *see also supra* note 221 (discussing the definition of "Relative").

241. *Id.* § 36A.

242. *Id.* § 36B (referring to Companies Ordinance §§ 109-110 (1983) (New Version).

lowing matters: (i) any distributions of dividend payments or bonus shares; (ii) changes in the issued or registered capital of the capital; (iii) amendments to the Memorandum or Articles of Association of the company; (iv) the redemption of shares; (v) the early redemption of debentures; (vi) the exercise of any right that the company reserved in the prospectus to make changes to the objectives of the consideration of an issue of securities; and (vii) any transaction between the company and an interested party, other than in accordance with market conditions.[243] A report must also be filed describing any decisions of the general meeting regarding the foregoing matters if the meeting has not acted in accordance with the recommendations of the board.[244] Lastly, a company must submit an immediate report concerning recommendations of the board of directors to an extraordinary general meeting, in addition to any recommendations of the board concerning the adoption of any decision, a copy of which must be sent, by law, to the Registrar.[245]

The final, and perhaps most significant, situation that demands the submission of an immediate report is described in a broadly cast provision covering the reporting of "special occurrences." Any extraordinary event that has occurred otherwise than in the ordinary course of business of the company must be reported if the event has had or is likely to have material effect on the profits, assets, or liabilities of the company.[246] Similarly, the company must immediately inform the Authority of the conduct of negotiations outside the ordinary course of business that will likely lead to the occurrence of such an extraordinary event; the Authority is empowered to request a full report on those negotiations if it feels that such is necessary for the protection of the investors.[247] Further, the company is obligated to file an immediate report upon signing any contract or memorandum of understanding regarding a material matter if it is executed outside the ordinary course of business.[248] However, the regulations add a proviso that the requirements of this section regarding the report of special occurrences do not apply if the relevant event has been well-publicized, unless the event has extraordinary effect on the business of the company, in which case a report is still required.[249]

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243. 1970 Regulations, *supra* note 199, § 37(a). Note the similarities between the Section 37 of the 1970 Regulations and the provisions, described above, regarding periodic reports.

244. *Id.* § 37(b).

245. *Id.* § 37(c).

246. *Id.* § 36(a).

247. *Id.* § 36(b).

248. *Id.* § 36(c).

249. *Id.* § 36(d). The vague tests established by this section have the obvious potential to create difficulties in interpretation. It is hoped that the combined application of common sense by the Authority, the courts, and the companies involved in these matters will prevent these difficulties from giving rise to litigation.

E. *Interim Financial Reports*

The final topic covered by the 1970 Regulations is interim financial reports. "Interim reports" are defined as interim consolidated financial reports of the company that must be prepared on a calendar quarterly basis. With regard to a company that is not obligated to draw up consolidated reports under accepted bookkeeping principles, the term "interim report" refers to the interim reports of the company alone.[250] The relevant interim reports must be submitted to the Authority and the Registrar, as well as the TASE if the securities of the entity are traded there, within two months of the date of the report and no more than ten days after it was signed by the company.[251]

The interim reports must be prepared in accordance with generally accepted accounting principles governing such reports and should follow the detailed format provided in the first three schedules attached to the regulations.[252] The notes to the reports must include the following: (i) the seasonal effect on the reported results; (ii) the description of any changes in accounting methods adopted since the last annual reports and the resultant financial effect of such changes; (iii) deferred expenses in the interim report, indicating any similar expenses from the last accounting year which were not deferred in the last annual report; and (iv) any new presentation or recategorization in the interim reports as opposed to the last annual reports and any resulting financial effects of the changes.[253] If the last annual report of a company included the financial reports of a non-consolidated subsidiary or of an affiliate, then the interim reports of such a subsidiary or affiliate for the same period must also be attached to the company's interim reports unless the Authority, in its discretion, excuses the company from fulfilling this obligation due to the apparent inability of the company to comply with this regulation.[254]

If the company presents its interim reports in an abridged form, then the notes must include a detailed profit/loss report in nominal terms.[255] Further, if the company acquired or amalgamated with another company during the report period, then the effect, if it is material, of such an event on the interim report should be indicated.[256] Similarly, the report must disclose any material transactions entered

250. Id. § 38; *see also* Section 5 of the 1993 Regulations regarding consolidated reports.

251. *Id.* § 39.

252. *Id.* § 40(a) and Schedules 1-3. The format provided in the schedules includes sample reports for the three, six, and nine month periods covered by the respective interim reports.

253. *Id.* § 40(b).

254. *Id.* § 42.

255. *Id.* § 43.

256. *Id.* § 44.

into with an associated party, as defined by generally accepted accounting principles, during the period between the last annual report and the date of the signing of the interim report.[257]

The completed report must be approved by the board of directors of the company or by a committee of the board authorized to act. Before submission, the report must be signed, in the name of the company, by the chairman of the board of directors or by the managing director and by the chief financial officer.[258] Finally, the company's accountant must approve the interim report and certify the completion of a review of the report. The review should be filed with the Registrar, the Authority, and the TASE; if the review included any reservations on the part of the accountant, then those must be specified.[259]

F. *Annual Financial Reports*

The 1993 Regulations, adopted pursuant to Sections 17(b)(1) and 36 of the Law, represent a significant effort to tighten accounting practices of Israeli public companies.[260] The 1993 regulations, some interim transitional provisions notwithstanding, repeal the previous regulations that covered this topic, Securities Regulations (Preparation of Financial Reports) 1969.[261]

The general goal in instituting the new regulations was to update the accounting regulations and fully to adopt, as a rule, the principles that govern modern accounting practices in industrialized countries. While the extensive 1993 Regulations contain this important framework for the overhaul of the current system, a detailed study of the minute details is well beyond the scope of this article. The following examination is confined to a review of some of the guiding principles behind the enactment and a more detailed study of a few of the provisions that carry special significance for legal practitioners.

The principle of modernization finds particular expression in the overall requirement for more detailed and more specific reporting of expenses and profits alike.[262] Furthermore, the Authority insisted on

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257. *Id.* § 45.

258. *Id.* § 46.

259. *Id.* § 47. Although the regulations do not state as such, it is assumed that the requirement to send the survey report to the TASE will only apply in such cases where the interim report itself must be sent to the TASE (i.e. where the securities of the entity are traded or registered for trading on the stock exchange).

260. The provisions of these regulations, as stated in Section 66(a) of the 1993 Regulations, generally went into effect with regard to the annual reports for the year that ended December 31, 1992. Section 66(b) of the 1993 Regulations allows for an exception for Section 64(2)-(3), dealing with income from and transactions with interested parties, which did not take effect until the reporting year that ended December 31, 1993.

261. 1993 Regulations, *supra* note 77, § 65-67.

262. *Id.* §§ 46-58.

the adoption of a uniform format for all annual reports, from which any deviations must be accompanied by an explanatory notice.[263] Previously, under the repealed 1969 regulations, it was often left to the company's accountants to decide on the format of the statements, making comparison and examination by non-professionals difficult, if not impossible. In addition, the 1993 Regulations attempt to provide a general mechanism for the uniform definition of the concept of "materiality" that governs much of the determination of what information is to be included in or excluded from the statements. Instead of the decision being left to each accountant on a case-by-case basis, the regulations were designed to remove the uncertainty of such a procedure by providing, wherever possible, detailed rules regarding this matter.[264]

Chapter 8 of the regulations deserves special attention due to its approach to the issue of interested parties. The term "interested party" is defined as (i) one who holds at least five percent of the outstanding share capital or voting rights of the company; (ii) one who may appoint a director or general-manager of the company or one who serves in such a capacity; or (iii) a corporate body in which a person described in (i) or (ii) holds twenty-five of the outstanding share capital or voting rights therein or may appoint twenty-five percent or more of its directors.[265] Previously, the reporting of dealings with such parties was governed by scattered provisions of the now-repealed 1969 regulations. Perhaps the realization that the detailed presentation of such transactions was essential to accomplish full and proper disclosure of company finances led to provision of specified and detailed rules for the reporting of such activities in the company's financial statements.[266]

Without becoming entangled in the intricate details that are best understood by the accountants, it is possible to take a quick glance at the general provisions in this area. The statements must, in detailed fashion, reflect both the company's obligations to such parties and its investments in them. While the obligations of the company and its consolidated companies must be divided into sections reflecting long-term and short-term liabilities, the investments of the company and its consolidated companies in the interested party are defined to include capital investments (such as investment in securities and loans) as well as the giving of guaranties for such party's debts.[267] Similarly, detailed procedures are set out for the report of benefits and payments paid to, and transactions with, such interested parties by the company

263. *Id.* § 8.

264. For examples of this trend in the 1993 Regulations, see §§ 37, 45, and 64, among others.

265. Section 1 of the 1993 Regulations refers to the definition of "interested party" contained in Section 1 of the Securities Law.

266. 1993 Regulations, *supra* note 77, §§ 62-64.

267. *Id.* §§ 62-63.

and its consolidated companies.[268]

One of the principles upon which the new regulations are based is clearly investor security and tighter corporate regulation. Both the uniform format and the detailed reporting required will allow for closer scrutiny of companies' actions. This trend is not unique to accounting regulations; similar interests have been the driving force behind much of the recent legislation in the area of company law.[269] As in these other areas, the lawmakers and the regulatory authorities have shown a willingness to modernize the sometimes outdated framework provided under previous enactments.

G. *Other Provisions*

After a digression concerning the regulations regarding the submission of certain reports to various authorities, the analysis returns to the Law itself. After establishing the framework for the enactment of the regulations and other forms of directives, the Law states that in a case where the prospectus for the offering of debentures to the public (covered by Section 35A of the Law) includes the financial statements of a company that gave guarantees for the fulfillment of the obligations under the debentures, then the provisions regarding reports to the various regulatory bodies will also apply to that company for as long as the guarantees are still effective.[270]

Further, the Law provides for a framework by which a company may be exempted from reporting certain particulars required under this chapter. The Authority is empowered to exempt the disclosure of a certain particular if, in its opinion, the exemption is justified for the protection of trade secrets of the company, as long as such a particular is not of the variety that would deter potential reasonable investors if it had been included in the report.[271] In addition, the District Court, on application, can grant an exemption from the disclosure in a report of a particular if such a disclosure is likely to harm national security, the State economy, or a continuing investigation of the police or the Authority, if, respectively, the Minister of Defense, Minister of Finance, Minister of Police, or the chairman of the Authority, or their designee, certifies the possibility of such harm being suffered. In such cases, the Attorney General is to act as respondent to the applications before the court.[272] If an exemption is granted under this section,

268. *Id.* § 64.

269. *See, e.g.*, Companies Ordinance, Amendments 4-7 (New Version) 1983.

270. Securities Law, *supra* note 2, § 36B.

271. *Id.* § 36C(a). The conditions in this provision are identical to those stated in § 19(a)(1) regarding exemptions from publication of particulars in a prospectus.

272. *Id.* § 36C(b). The conditions here are copied from § 19(a)(2) regarding exemptions from the prospectus disclosure.

then this fact must be noted in the relevant report.[273]

Because of the extensive responsibilities placed on the company to report particulars, some of which are outside of its control, the Law provides certain mechanisms, especially in regard to interested parties, by which the company is assisted in obtaining the necessary information to fulfill accurately its obligations. The Law places an obligation on any interested party to affect a timely submission to the company of such particulars as are necessary to allow the company to complete its duty under Section 36. If the securities of the interested party are held by a trustee, and the trustee has submitted such information, then the interested party is free from his obligation. Similarly, a report by the interested party exempts the trustee from any such obligation.[274]

The District Court is also given a role in insuring the proper submission of reports to the Authority. On application of the Authority, the court may issue an order requiring that the company and its directors, within a time set by the court, submit or amend a report or attached opinion, if the entity has failed to properly and fully fulfill any of its reporting obligations. When necessary, the court may also order that an interested party file his particulars with the company as provided in Section 37. Further, the company itself has the statutory right to apply to the District Court in order to force an interested party to submit or amend a report that he was obligated to submit under this chapter.[275] The Legal Procedure Regulations (Securities) 1991 clarified that the application of the Authority under this section is to be executed by summary proceedings in the Jerusalem District Court.[276]

In order to insure that investor security is not jeopardized by shortcomings of the company in the fulfillment of its reporting obligations, the Law provides that the Authority may, after consultation with the chairman of the TASE and after giving the company an op-

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273. *Id.* § 36C(c).

274. *Id.* § 37(a). *See also* State of Israel v. David Ben Abraham Blass, 1990 (1) P.M. 255 (Dist. Ct. Tel Aviv/Jaffa 1990) (considering the failure of an interested party to report as a peripheral issue in a criminal case that centered around the acquisition of the means of control in a banking corporation without the requisite permits). While the case report does not state which section of the Securities Law such a failure to report would violate, presumably the relevant provision is found in § 37 of the Law, violation of which is grounds for a fine being imposed on the offender. *See also* State of Israel v. Aviva Elman, et al, 1990 (1) P.M. 343 (Dist. Ct. Tel Aviv/Jaffa 1990) (considering the imposition of criminal penalties for the admitted violations of certain provisions of the Securities Law, including charges of violating § 37 of the Law and § 33 of the 1970 Regulations as a result of an interested party's failure to submit proper reports to the necessary bodies). However, again the issue is not discussed in any detail.

275. Securities Law, *supra* note 2, § 38(b).

276. Legal Procedure Regulations of 1991 § 1. It is presumed that the same procedure applies to applications by a corporate body under Section 38(b) of the Securities Law.

portunity to state its case, stop trading on the TASE of the securities of the company. Such shortcomings are failure either to submit a report required by the specific deadline or submission of a report that deviates, in a material and substantive fashion, from the stated requirements.[277] Once the relevant reports have been submitted or amended to the Authority's satisfaction, then the Authority should instruct the TASE to resume trading in the securities.[278]

The Law also provides that an interested party who has submitted a report under this chapter has the same civil liability towards holders of the company's securities as do signatories and experts who give opinions in a prospectus.[279]

In *Boronovitch Properties and Leasing Ltd. v. The Securities Authority,*[280] the Supreme Court, in a leading decision written by the President of the Court, Justice Meir Shamgar, unanimously upheld the earlier decision of the District Court. The Court stated that the Authority was correct in demanding the production of the financial reports of a private company that was affiliated with a public company. The appellant company, before commencing a public offering of its shares, had transferred part of its operations to a private company under the control of the same parties who maintained control of the public company. Before the offering, the appellant company had given bank guarantees for the general obligations of the private company, without any security being received in return from the private company. The public company pledged a fixed amount of its assets as a security for these guarantees, receiving a commission of six percent from the private company on the obligations for which the guarantees were needed.

The rental monies that the public company collected from the properties pledged as security on the guarantees equaled about ninety-five percent of its total income from rentals in 1987. The Authority, after a review of the appellant's financial statements, requested a copy of the financial statements of the private company. The Authority claimed that examination of the private company's statements was imperative to the Authority's determination of the appellant's potential liability due to the guarantees. The appellant company appealed against the decision of the Authority pursuant to the statutory right of appeal granted under Section 14A of the Law.

In a sweeping opinion, the Court ruled in favor of the Authority. Among the reasons given for its decision, the Court relied on some

277. Securities Law, *supra* note 2, § 38A(a).

278. *Id.* § 38A(b).

279. *Id.* § 38B. *See also id.* §§ 31-34 (concerning liability in connection with a prospectus).

280. Boronovitch Properties & Leasing Ltd. v. Securities Authority, 46 P.D.(2) 818 (1992).

issues of technical interpretation of the relevant clauses and their application to the case at hand. However, more importantly for present purposes, the Court made a number of general statements regarding the role of the Authority in the protection of the investing public. The Court viewed the role of the Authority as twofold. In addition to a one-time responsibility of insuring the proper disclosure in the prospectus of material facts at the time of an offering, the Authority also has a continuing responsibility to ensure full disclosure by the company when its shares are traded on the secondary markets, in other words the TASE. The guiding principle behind the operations of the Authority, expressed in Section 2 of the Law, is the protection of the interests of the investing public. The subsidiary principle under which the Authority operates, expressed in Section 16 of the Law, is to insure the full disclosure of any information that a reasonable investor would consider as relevant to his investment decisions.

Such disclosure serves two purposes: on the one hand, it allows investors to make rational decisions regarding their investments; on the other hand, disclosure serves to dissuade controlling individuals of a company from abusing their positions by fraudulent or manipulative behavior. As a result, the power to seek further information from a company concerning particulars, granted to the Authority by Section 36(f), must be viewed broadly, considering the breadth of the task assigned to the Authority. The section was added in 1988 by Amendment 9, which, according to the representative of the Finance Committee, MK Yoram Aridor, was primarily based on the principle of full material disclosure and the supervision of that disclosure by the Authority.[281] In short, the Court stated that the underlying principle of full disclosure for the protection of the investor outweighs the principle of the separate corporate personality, whereby a private company need not reveal details of its financial situation.

In applying these principles to the case at hand, the Court took a number of factors into account. First, the close, almost inseparable, relationship between the two companies served to increase the level of suspicion that any unusual transaction would raise among the Authority, and among investors as a whole. Second, the Court viewed the obvious accessibility to the public company of the private company's financial statements as a factor favoring their disclosure. Further, the level of liability incurred by the guarantors was such that the appellant could not claim that accounting statements and its own financial reports were sufficient to cover the requirement of disclosure. Lastly, because the Authority's request for disclosure fell within the bounds of the test of "materiality," the Court had no place in curbing or limiting the power of the Authority to request further particulars under Section 36 of the Law. It bears mention that the Court declined to rule defin-

281. Divrei Knesset 109-111, Session of July 20, 1988, at 3871.

itively on the question of disclosure where it was not within the public company's legal or practical ability to reveal the documents requested by the Authority.

With this background, it is possible to give short consideration of the more general principles that the Boronovitch decision represents. The Court clearly established the supremacy of the interests of the Authority, representing the principles of full disclosure and the protection of the investor. As part of a general trend in all facets of Israeli securities law, involving the Knesset and the courts, the decision reflects a recognition that the courts should take an active role in insuring that the fast-maturing securities markets in Israel provide a level playing ground for all of the participants.[282] At the same time, the Law should attempt to avoid overburdening companies with excessive bureaucratic regulations, and the overriding principle must remain the protection of the investing public.

VIII. ANCILLARY PROVISIONS

A. *Transnational Considerations*

The Law contains a collection of miscellaneous provisions relating to issues and offers of securities to the public and to current reports. The Law establishes that the issue of securities and their subsequent offer to the public require a permit from the Minister of Finance or a person appointed by him for this purpose, without which authorization the Authority may not grant approval for the publication of the prospectus.[283] However, the discretion of the Minister is limited so that the only grounds upon which he can refuse to grant a permit are that the timing or conditions of the offer are contrary to the economic policy of the Government.[284] For many years, this rule was implemented by a special department of the Ministry of Finance responsible for capital markets and insurance regulation. More recently, however, a general permit has been issued by the Minister permitting the issuance of securities by Israeli companies in Israel, without any special statutory permission.[285]

The Law provides that the prospectus requirements, the current report requirements, and the criminal penalties apply in the case of a

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282. *See* Companies Ordinance, Amendments 4-7 (1983) (New Version) (providing examples of this trend in the Knesset lawmaking); *see also* Ido Ben-Yehuda, Adv. v. Interpharm Industries Ltd., (unreported) (Dist. Ct. Tel Aviv-Jaffa June 6, 1993) (following the same trend in the courts).

283. Securities Law, *supra* note 2, § 39(a), (c), (d).

284. *Id.* § 39(b).

285. However, Israeli companies must gain approval of the Ministry to issue securities abroad even though, in practice, this is dealt with as part of the exemptive proceedings available to foreign companies issuing their securities outside of Israel pursuant to Section 40(c) of the Securities Law of 1968, which for the most part has meant issuance of securities in the United States.

public offering by an Israeli company to the public abroad. This provision is coupled with authorization to the Authority to provide a complete or partial exemption from any of these provisions, whether such offering is undertaken by the company itself, by another on its behalf, or by its consent.[286] The Authority has discretion to exempt a company from the provisions of these sections if the circumstances so justify.[287] In proposing adoption of a securities law, the Yadin Committee had suggested this supervisory authority, stating that "[w]e believe that this arrangement will to a substantial extent prevent distribution of Israeli securities [abroad] which carry the country's name and are not worthy of doing so."[288]

This exemptive authority has been frequently exercised in recent years, although in the past there were periods during which all public offerings in the United States had to pass a thorough Authority review before being approved. There are today over 50 Israeli companies that have successfully effected one or more public offerings in the U.S. and other companies presently involved in the registration process. Shares of those companies are traded over the counter and on the New York and American Stock Exchanges. The number and volume of those public offerings has led to considerable familiarity at the SEC about the special problems that exist in Israeli companies, and that in turn has led the Authority to be much more willing to exempt Israeli companies from the dual registration process.[289]

Conversely, if a foreign-registered corporate entity desires to offer securities to the Israeli public, then the Authority, in its discretion, may exempt the offeror from some or all of the provisions of the Law if the corresponding legislation in the country of registration sufficiently serves to protect the interests of the investing public in Israel.[290] As of late 1993, there have been a few efforts by foreign companies to raise money in Israel, but none has succeeded. The main barrier has been Israel's Foreign Currency Law and related regulations, and the need to obtain a special permit from the Bank of Israel for the financing in Israel of activities abroad. Two efforts that ultimately failed included a proposed application of some portion of the proceeds to Israeli related activities. As a result of the increasing openness of Israel to international securities markets, in August 1994 the Bank of Israel advised that these foreign currency restrictions will be substan-

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286. Securities Law, *supra* note 2, § 40(a)-(c).

287. *Id.* § 40(c).

288. YADIN, *supra* note 1, at 22.

289. In a March 1993 circular, the Securities Authority advised that it was now willing to provide that exemption on a regular basis to companies that affect public offerings in the U.S. Those companies now have to submit a copy of their U.S. prospectus to the Securities Authority with a one page summary in Hebrew of the terms of the offering and are then automatically granted the exemption.

290. Securities Law, *supra* note 2, § 41.

tially relaxed, effective October 1994. Foreign companies may then begin to raise capital in Israel for their international activities.

When the State offers securities for acquisition by the public, unless the securities were issued by the State itself, the offer must be effected by way of prospectus.[291] The definition of "securities" excludes securities of the State of Israel itself or those issued pursuant to special law.[292] The State holds substantial securities in commercial enterprises, however, and where the State holds more than 50% of the control of such companies, then the activities of those companies are regulated by a separate law.[293] The Government has embarked on a program of privatization of at least some of these government companies.

A popular mode of privatization in Israel, and to some extent in the U.S., has been by public offering. In addition, as a result of certain problems in the banking system, the government has acquired control of the major Israeli banks, on a temporary basis, with an articulated goal of selling such control. Privatization of those banks is also being effected to some extent by public offering. In each of these instances, the Law requires that a prospectus be filed pursuant to which the State is the offeror, and the company provides the prospectus. This procedure is analogous to the situation in the U.S. when a so-called secondary offering takes place in which controlling shareholders or others who have registration rights effect an offering pursuant to a prospectus of the company itself.[294]

Distribution of bonus shares is not considered a public offering and therefore is exempt from the prospectus provisions under the Law, so long as the bonus shares are the equivalent of a stock dividend (using U.S. nomenclature), where there is no choice given to the shareholders.[295] As a further step adopted by the Law to insure that the public has access to all relevant documents that are likely to be of interest to the reasonable investor, an issuer is required to provide copies of any prospectus or current report, along with all relevant

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291. *Id.* § 42.

292. *Id.* § 1. When it comes to trading securities on the exchange, however, Government securities are regarded as securities for all purposes. *See id.* § 52.

293. The Government Companies Law of 1975, as amended.

294. This approach is envisioned by Section 22(d) of the Securities Law, which provides that in the case of a public offering of securities for the benefit of a party other than the company, that other party will also sign the prospectus. Sections 31 and 35 of the Law apply then to such offers as well and create civil liability in the event of a misleading particular in the prospectus. Recent statutory relief was given to the Government in connection with privatization of the banks, by a technical amendment to simplify the definition of interested parties for these purposes and thereby exclude the disclosure of complex, multifaceted relationships of Government companies and the banks.

295. Securities Law, *supra* note 2, § 43.

attachments, for inspection or duplication at the Registry and at the main office of the issuer.[296] A final measure, designed to insure that conflicts of interest do not adversely affect the interests of the investing public, provides that any person who gives a professional opinion required under any section of the Law may not be an interested party in the issuer for which the opinion is granted.[297]

B. *The Stock Exchange*

A separate chapter of the Law is dedicated to the provisions that govern the activities and make-up of the stock exchange. Currently the TASE is the only licensed market in Israel; as a result, all references to the current stock market herein refer to the TASE. The TASE is located in Tel Aviv, the commercial and business center of the country. There have been suggestions made from time to time that a second stock exchange should be established in Jerusalem, the capital of Israel, to provide access to public capital for high-tech and other companies that do not meet the rules for listing on the TASE. Such a development is contemplated by the Law — another example of the implementation of Commissioner Cohen's prescient proposal that the Law be broad enough to deal with future developments of the securities markets.[298]

The rules affecting the TASE were very significantly altered by amendments to the Law in 1988 and 1990. However, before examining the affected provisions of the Law and the defects of the previous clauses that the draftsmen hoped to remedy, it is necessary to examine the underlying framework established by the Law, much of which has not been significantly altered since being enacted. Further, there have been a number of significant court decisions in this area, as are discussed below.

The Law begins by establishing the general principle that no person may open or administer a stock exchange without a license from the Minister, to be granted only after consultation with the Authority.[299] Further, the Minister is given guidelines to govern his discretion in granting a license. The license is only to be granted to a company if the Minister satisfies himself that the company, and the proposed exchange to be established by it, comply with the following requirements: (i) it does not limit the number of members; (ii) its Memorandum of Association limits its function to the operation of a stock market; (iii) its Articles of Association ("Articles") state that

296. *Id.* § 44.

297. *Id.* § 44A.

298. In early 1994, the Ministry of Finance published a preliminary tender with respect to the establishment of a second stock exchange. Groups promoting Jerusalem and Haifa as alternative sites have responded.

299. *Id.* § 45(a). The TASE was established long before the Law was enacted.

profits will only be used to further the company's objectives and will not be distributed among its members, and upon liquidation, the remaining assets will be used for objectives designated by the Minister; (iv) its charter has complied with the requirements of Section 46 (described below) and such charter has been approved by the Minister, after consultation with the Authority, and by the Finance Committee; and (v) the exchange will operate in a city where no other exchange is already operating.[300]

In addition to these general licensing requirements, the Law also prescribes various specific rules concerning the operation of the market and its employees. The first area considered is that of the board of directors of the exchange. Here, the 1988 Amendments took a significant step to tighten the controls of the Government (through the Authority) and the investing public over the Exchange. Overturning previous provisions, the Law now requires that a majority of the directors of the exchange be "outsiders". The present statutory composition of the board creates a balance between the interests of the exchange, of the public and traded companies, and of the governmental authorities. Currently, the total board of fifteen must consist of seven directors elected by the members of the exchange, five "external directors" appointed by the appointment committee with the agreement of the chairman of the Authority, one director each appointed by the Minister of Finance and the Governor of the Bank of Israel, and one director who meets the qualifications of an "external director" who is elected to serve as chairman by the board with the approval of the chairman of the Authority, provided that he is not an interested party in any company whose securities are registered for trading on the exchange.[301] The board of the exchange is also mandated to select a non-voting general manager who must meet the qualifications of an "external director" and must not be an interested party in any entity whose securities are registered for trading on the exchange.[302] The Law proceeds to define the specially established appointment committee and the "external directors" that they must appoint. The committee has four members, including the chairman of the Authority, the chairman of the board of the exchange, the dean of the Law faculty at the university located in the city where the exchange is established (presently Tel Aviv University) or a member of the academic staff appointed by such a dean to serve in his place provided that he meets the criteria of an "external director," and a judge appointed by the Minister of Justice with the approval of the president of the Supreme Court who is to

300. *Id.* § 45(b). This limit of one exchange for a given city is the basis for the suggestion that any second exchange be located in Jerusalem or Haifa.

301. *Id.* § 45A(a)(1)-(5). *See also id.* § 45A(d) (providing that the definition of "interested party" in this context means the person himself or in conjunction with any relative).

302. *Id.* § 45A(6).

serve as the chairman of the committee and cast the deciding vote in case of a tie.[303] The "external directors," appointed to represent the interests of the public, may not be any of the following: (i) a member of the exchange or an employee or interested party in such an entity; (ii) an interested party or employee of a company that controls a member of the exchange; (iii) a person who regularly provides paid services to any of the above; (iv) an interested party due to holdings of shares of any entity whose securities are registered for trading on the exchange; or (v) any other person meeting any other criteria established by the Minister.[304]

The Law continues by establishing regulations concerning the terms of office of the various directors and the termination of such a position. An external director is appointed for a period of two years, after which he may be reappointed for two further terms of two years each.[305] The chairman of the board, on the other hand, is appointed for a term of five years and may be reappointed for one additional term of five years.[306] However, the service of an external director may terminate prematurely if he resigns, is deemed incapable of performing his functions by the appointment committee, is regarded by the appointment committee as fitting one of the disqualifications with respect to external directors, or is inexcusably absent from a fixed number of meetings of the board over a period of time.[307]

To prevent the obviously unacceptable position of potential conflicts of interest involving staff of the exchange, the board members and other exchange employees are forbidden, as are employees of the Authority, from acquiring securities other than under a permit from the Minister. Such a permit may be general in nature or refer to specific categories of securities. Similarly, each employee must notify the chairman of the board of the exchange, and the Authority, of all holdings of securities by himself or his spouse and of any acquisitions of shares by himself or his spouse, within seven days of his appointment or the relevant transaction, respectively.[308]

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303. *Id.* § 45A(d). This is an interesting example of the statutory assignment to a judge of a role with respect to a quasi-public institution, and one which is itself subject to judicial review.

304. *Id.* § 45A(f).

305. *Id.* § 45A(b).

306. *Id.* § 45A(c).

307. *Id.* § 45B. A director absent from four consecutive board meetings or a total of six board meetings in a calendar year is removed, unless the appointment committee concludes that the absences are reasonably justified. A similar provision appears in Section 22(a)(2) of the Government Companies Law of 1975.

308. Securities Law, *supra* note 2, § 45C. The provisions were directly lifted from § 5(a)-(b) of the Law regarding similar restrictions on employees of the Authority. However, the one slight change is that while the required notices there are to the chairman of the Authority and the Minister, here the notice is to the chairman of the Authority and to the chairman of the board of the exchange.

One of the major areas improved under the 1988 and 1990 amendments was the charter of the exchange. "Charter," for these purposes ("takanon" is the term used in the Hebrew original), is the set of rules that govern the conduct by the exchange of its listing and other responsibilities, and is to be contrasted with the corporate governing documents, in Israel (as in England) called the Memorandum of Association and the Articles of Association. The charter of the exchange, which must be published for public scrutiny, has to include rules that will generally provide for the proper and fair management of the exchange.[309] The Law proceeds to provide a non-exhaustive list of various topics that may be covered by these charter rules, only some of which are considered herein.

While the 1988 Amendment made significant progress towards defining the rules to be covered in the charter of the exchange, the lawmakers, when considering the enactment of the 1990 Amendment, still clearly felt further clarification regarding the authority of the exchange to establish rules in certain areas was needed. As the explanatory notes to the proposed legislation state,

> with respect to a portion of these matters, it was argued that the exchange did not have the authority to regulate them and this argument was even accepted in the Tel Aviv-Jaffa District Court . . . .It is proposed to detail the subjects which may be set forth in the charter of the exchange, and to determine the authority to add details, terms, and exceptions with directives of the board of directors of the exchange, which will require the approval of the Authority.

The first issue, in this regard, relates to rules governing membership on the exchange. The exchange may, in its charter, adopt rules concerning, among other things, eligibility requirements for membership, types of activities that members may undertake, and obligations of the members towards clients and towards the exchange and other members. However, in order to allow for a smooth and fair transition to the new provisions of the Law and the regulations, the Law does state that any person who was a member of the TASE on the eve of the adoption of the Law is permitted to continue operating in that capacity, notwithstanding his failure to meet any new qualifications stated therein.[310] In addition, the rules may encompass procedures for disciplinary offenses and the resulting proceedings.[311]

More significantly, this section covers the rules the exchange may adopt regarding listing requirements for companies that will register their shares for trade on the exchange. These requirements may in-

309. *Id.* §§ 46(a), 49.
310. *Id.* § 55.
311. *Id.* § 46(a)(1), (c), (g).

clude the following: (i) the types of companies that may register their securities for trading, regarding the length of time since the company was established, the scope of and the results of its activities, the value of its assets and extent of its liabilities, its relationship to other corporate bodies, and categorization for registration purposes (the exchange may prescribe different requirements for the various categories of economic activity undertaken by companies); (ii) the types of securities that may be registered; (iii) the manner in which the securities will be issued and offered, and the relationship between the initial offering price of the securities and the trading price of the securities on the exchange; (iv) an undertaking by the company that the offering will be made on terms, at a price, and by a manner that is equal for all prospective investors, or the conditions, where necessary to encourage investment in the particular circumstances, under which a company may deviate from such an undertaking; (v) the manner by which securities that were not issued by way of public offering may be registered for trading; and (vi) an undertaking on the part of the company that all of its outstanding issued capital be registered for trading, with certain exceptions for industrial companies and special Government issued shares.[312]

In 1990, Amendment 11 provided a similar list regarding the third subject as to which the exchange may enact rules. In the area of rules regarding trading activity on the exchange, the regulations included in the charter may encompass (i) times and methods of trading; (ii) supervision and orderly conduct of trading on the exchange; (iii) circumstances and procedure under which trading may be suspended or limited with regard to one share or a group of shares; (iv) release of trading results; and (v) terms and manner of obtaining permits by members of the exchange and the conditions under which such permitted members may execute trades involving registered securities outside of the exchange.[313] The Law also provides for the enactment of rules regarding the continuing obligations of companies whose shares are registered for trading, the procedures and conditions for organization and cancellation of trading in a given security, the method of publication of information by the exchange, the fees for the services of the exchange, and the applicability and the adjustment of all of these rules for entities that are not companies.[314]

The last major subject covered by this section relates to the exchange's refusal to register certain securities. The Law provides that the charter of the exchange may state that the board of directors of the exchange may refuse to register a security for trading if the board considers that a material conflict of interest exists between the compa-

312. For the complete list, *see id.* § 46(a)(2).
313. *Id.* § 46(b).
314. *Id.* § 46(a)(4)-(8).

ny making the application and a controlling party in that company or between the company and a company under the control of a controlling party in the first company.[315] However, the Law establishes that such a decision may only be made by a majority of the board of directors of the exchange who represent at least two-thirds of the participants in the relevant meeting; the company must also be given a reasonable opportunity to present its case at that board meeting.[316]

The scope of the rules to be adopted by the TASE was explored in the 1984 District Court of Tel Aviv-Jaffa case of *Tzvi Shaul v. United Mizrahi Bank*.[317] In the context of a decision that focused on the agency responsibilities of a bank towards a customer who places an order for the purchase of securities, the court made several interesting remarks regarding the TASE and its rules. The court stated that the discretion granted to the exchange under Section 46 to enact rules regarding a wide range of topics showed that the TASE was a self-managing body. As a result, there exists an implied agreement between the investor and his agent (a member of the exchange) that the relations of the two sides involved in the complex and fast-changing business of trading in securities will be governed by the rules established by the TASE. Therefore, the rights of the member against his client will be secured as long as the former remains within the bounds of the rules adopted by the exchange, while at the same time the client can be assured of his rights as long as the member of the exchange does not stray beyond those bounds. Thus, the court was recognizing that the wide discretion granted to the exchange in enacting its charter made the charter the source of legitimate expectations, and perhaps even rights, as between parties who transact business within that framework.

Amendment 9 in 1988 also made a significant contribution to the provisions under which the TASE is authorized to issue temporary directives, in addition to the permanent rules contained in its charter. While prior to the amendment the exchange often issued temporary guidelines subject to little or no public or governmental scrutiny, now these temporary directives must, as is the case with the permanent guidelines, gain the approval of the Authority.[318] The Law states that

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315. Section 1 of the Law defines "control" as the ability to guide the activity of the corporate entity, to the exclusion of such powers that derive solely from an individual's filling the position of director or other position in the entity. Additionally, it is assumed that a person "controls" a corporate entity if he holds one half or more or a certain "means of control" in that entity. "Means of control" in a corporate entity are defined as one of the following: (i) the right of voting in the General Meeting of the company, or in the corresponding body of another corporate entity; or (ii) the right to appoint directors or the general manager of that entity.

316. *Id.* § 46(b), as amended on Feb. 21, 1994.

317. Tzvi Shaul v United Mizrahi Bank, 1983 P.M. 177 (Dist. Ct. Tel Aviv/Jaffa 1984) (Isr.).

318. Securities Law, *supra* note 2, § 46A(b). *See also id.* § 45(b)(3) (establishing

the exchange is authorized to issue trial directives regarding any of the matters on which they may pass permanent guidelines, for the purpose of testing their possible inclusion in the charter itself.[319] However, the Authority is obligated to inform the Minister of Finance and the Knesset Finance Committee of the proposed temporary directives, which will then only take effect fourteen days after the committee was notified. If a member of the committee objects to the enactment of the temporary directives, they will only take effect after thirty days following the demand that they be considered by the committee, unless during that period the committee votes to cancel the proposed directives completely.[320] In order to curb the all-too-common abuses by the TASE of the temporary directive provisions, Amendment 9 also limited the term of any temporary directives to a period of one year, subject to the possibility of the Authority approving a further one year extension.[321] Lastly, the Authority, for supervisory purposes, is also empowered to demand reports regarding the manner and results of the enactment of these temporary directives.[322] These provisions as to temporary directives have certainly not ended all controversy. In late 1993, the TASE substantially tightened the rules as to new listing requirements, pulling the rug out from under quite a few companies who were about to file their prospectuses. An outcry resulted that has led to discussions in the Finance Committee as well as an action against the TASE and the Authority. In this action, the District Court required the Board of Directors of the TASE to reconsider its decision at a future meeting.[323]

Similar improvements under Amendment 9 have tightened the regulations surrounding the adoption of changes to the charter of the exchange. The exchange itself, through action of its Board of Directors, may initiate the process of amending the charter. Such a change, like the provisions of the original charter, requires the approval of the Minister in consultation with the Authority and of the Finance Committee.[324] However, more significantly, the Law now provides a mechanism by which the Authority itself can initiate the process of adopting such a change. If the Authority believes that a change is required to facilitate the fair and proper functioning of the exchange, then it may inform the exchange of that belief. If the exchange refuses to change its charter in accordance with the suggestion, then the Authority may apply to the Minister who, with the consent of the Finance Committee,

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that the permanent charter of the exchange must be approved by the Minister in consultation with the Authority, and by the Finance Committee).

319. *Id.* § 46A(a).

320. *Id.* § 46A(c).

321. *Id.* § 46A(d).

322. *Id.* § 46A(e).

323. Association of Public Companies Registered on the Exchange v. TASE and the Securities Authority (Dist.Ct. Tel Aviv/Jaffa, Misc. Appeals 1672/93, unreported).

324. *Id.* § 48(a).

may by executive order force such a change into the charter.[325] Understandably, a change effected by order of the Minister may in the future only be amended or removed by the exchange if it has the permission of the Minister.[326]

One of the most radical changes under Amendment 11 (1990) was the adoption by Israeli law of provisions regarding what is commonly referred to as the "one share, one vote" rule. Generally, this rule requires that the exchange ensure the existence of certain conditions of equal voting rights in both initial and subsequent offerings of securities that are to be registered on the exchange. The prior situation, under which no such rule existed, was considered unsatisfactory for the needs of the maturing capital markets in Israel. As the explanatory note to the amendment stated,

> [t]he situation whereby founding shares or shares with preferred voting rights allow their holders to exert control over the company in disproportion to the amount of capital that they invested in the company, while the rest of the public provides most of the operating capital of the said company, is inappropriate.

The amended Law provides that the exchange is not allowed to register shares or securities convertible into shares for trading on the exchange unless the following conditions are met: (i) in the case of a company first registering its shares on the exchange, the capital of the company may include only one class of shares that grant equal voting rights in proportion to their nominal value; or (ii) in the case of a company whose shares were already registered on the exchange prior to the amendment, any future offerings of shares must be of the class that grants the greatest level of voting power.

The Law adds that the provisions for equal voting rights for companies first registering their shares on the exchange do not apply to "special State shares." These are shares that the government decides it needs to hold in the interest of protecting a vital matter and that grant special rights, defined by the Government prior to the registration of the shares for trading. Such shares, sometimes referred to as "golden shares," have been created or contemplated as part of the Government's program of privatization. Israel Chemicals Limited, Israel's leading natural resources Government company, is the classic case in which such a special State share was created prior to an Israeli public offering, as the first phase of privatization. Furthermore, notwithstanding the other provisions applicable to companies registering for the first time, a company is authorized, after the expiration of at least one year subsequent to the date that the shares were registered on the exchange, to issue non-voting preferred shares. A similar excep-

325. *Id.* § 48(b).
326. *Id.* § 48(c).

tion exists for companies whose shares have been previously registered and whose capital only includes classes of shares permitted under provision (i). They, too, may issue non-voting preferred shares, provided that more than one year has passed subsequent to the date that the capital of the company met the qualifications of provision (i).[327]

In addition to these requirements, a further provision governs the holders of founders' shares in the company. These are shares that have been quite popular in Israel historically, particularly in banking, by which private and public companies have been controlled by founders or their successors. The 1990 Amendment 11 changed the Law to provide that anyone who holds founders shares and capital shares in a publicly traded company as of August 1, 1990, or any person who acquires the said shares, must continue to hold capital shares in a proportion that does not fall below the proportion held on that date, unless that proportion falls below the limit by virtue of the exercise of rights to acquire or convert shares that were granted to the other holders of securities in the company prior to the said date.[328]

The Supreme Court had the opportunity to examine the question of equal voting rights in the period prior to the enactment of Amendment 11. In the 1984 case of *Abramson v. Tel Aviv Stock Exchange,* the appellant, in his status as an owner of securities traded on the TASE, sought a court order to force the relevant authorities to effectively adopt the "one share, one vote" rule before it was finally adopted into the Law.[329] As discussed below in the section regarding appeals to the courts against decisions of the exchange, the Supreme Court restated its traditional stance that it would not take sides in an argument where there were reasonable positions on both sides. The guiding principle behind the rules that the exchange might or might not enact is the standard of "fairness" and "propriety." The Court proceeded to review decisions of the courts, reports of various committees (including the Yadin Committee) on this topic, and the solutions adopted in other countries that have a developed securities law. On the basis of this review, the court concluded that the principles of democratic management, proper scrutiny, and unfettered fluidity of markets all stood in favor of adopting a rule dictating equality of voting power. However, the court also recognized that the principles of freedom of contract and other economic interests, such as encouraging private and family controlled companies to seek expansion by using the proceeds of a public offering without fearing the loss of control in the company to outside interests, stood equally firm against such a proposal. In the absence of overwhelming evidence pointing in either direction, the Court concluded that it could not say that one alternative was "less proper" than

327. *Id.* § 46B(a)(1).
328. *Id.* § 46C.
329. Abramson v. Tel Aviv Stock Exchange, 38 (2) P.D. (1984).

another. In the case at hand, the appellant was unable to convince the Court that the result of the decision of the authorities not to adopt the proposed rule caused such manifest unfairness that the decision could be said to be outside of the realm of propriety. Thus, it was left to the Knesset, a few years later, to adopt the rule that the appellant had hoped to force upon the TASE by way of the courts.

The Law provides for a special right of appeal against decisions of the stock exchange. Any person who feels injured by virtue of a decision of the exchange regarding an application for membership, the suspension or cancellation of membership, or the effects of any disciplinary proceedings may appeal such a decision to the District Court.[330] Similarly, any person who feels wronged by any other decision of the exchange that is not taken in the course of trading may also appeal to the District Court. However, in the case of this latter appeal, notice of the commencement of proceedings must be given to the Authority. The Authority may appear in such proceedings and present its position if it wishes.[331]

The Law Procedure Regulations (Securities) 1991, mentioned above in the context of applications to the Jerusalem District Court for an order concerning the submission of reports (Section 38 of the Law), also established procedural regulations regarding the right of appeal under Section 47(a). The appeal must be submitted to the District Court in whose jurisdiction the company that controls the exchange is located — in other words, in Tel Aviv.[332] The writ of appeal, stating certain particulars including the nature of the decision appealed against and the grounds for an appeal, must be filed within sixty days of the decision of the exchange.[333] Next, the company that controls the exchange, the respondent in those proceedings, must file its response to the appeal within fifteen days of the service of the writ upon the company unless a special exemption has been granted.[334] Beyond the limited special procedural provisions in these regulations, the proceedings are to follow the standard practices established by the Civil Law Procedures Regulations 1963.[335]

An interesting case involving this statutory right of appeal against decisions of the exchange made its way through the Israeli courts, culminating in a Supreme Court decision in 1992. At first instance, the District Court of Tel Aviv-Jaffa decided in favor of the appellant in the case of *Marcus David Katz v. Tel Aviv Stock Exchange*.[336] The facts of the case can be summarized as follows. The

330. Securities Law, *supra* note 2, § 47(a).
331. *Id.* § 47(b).
332. Legal Procedure Regulations of 1991, § 2.
333. Legal Procedures Regulations of 1991, § 3.
334. Legal Procedure Regulations of 1991, §§ 4, 6, 7, 8.
335. Legal Procedure Regulations of 1991, § 9.
336. Marcus David Katz v. Tel Aviv Stock Exchange, 1991 (2) P.M. 296 (Dist. Ct.

TASE, upon receiving notice from the controlling party in a company that he wished to purchase all of the outstanding shares of the company and to delist the shares from trading on the exchange, decided to begin delisting proceedings upon being informed that this shareholder had reached the level of holding nearly 99.8% of the outstanding shares as a result of a tender offer, which was required by TASE procedures. The appellant, upon receiving notice of the TASE's intention to delist, advised the TASE that he had an outstanding legal claim against the controlling party with respect to a block of 60% of the outstanding shares that the appellant claimed to have acquired. As a potential major shareholder in the company if his claim succeeded, the appellant stated his opposition to delisting the shares of the company, a view rejected by the TASE, which decided nevertheless to delist the shares. As a party allegedly aggrieved by a decision of the exchange, the appellant appealed to the District Court under Section 47(b) of the Law to reverse or stay the decision of the board of the TASE.

The District Court ruled partially in favor of the appellant. The Court stated that in the circumstances the TASE had two avenues open to it: it could have either ordered a suspension of trading of the shares, or it could have adopted the more severe step of delisting. The Court felt that the TASE had wrongly failed to take account of all the relevant considerations by refusing to take notice of the interests of the appellant; in addition, the TASE could have better fulfilled its mandate, insuring the fair and proper management of the exchange, by adopting the less severe interim measure of suspension. Further, the TASE, in its function of facilitating trading rather than stifling it, should always adopt the alternative that holds out the greatest possibility of the resumption of trading in a security at some point in the future. Finally, the Court did not doubt that the appellant had standing to appeal to the District Court under the Section 47(b) test of an "aggrieved party." Contrary to the claims of the TASE, there was no need that the applicant to the court be a registered shareholder in the company. The District Court suspended the decision of the TASE for a two month period, during which time it said that it hoped that a decision would be reached in the litigation between the parties.

The TASE appealed to the Supreme Court, which was asked to consider two questions: What is the scope of the review of the District Court of TASE decisions under Section 47, and is the exchange obligated to take the interests of a non-shareholder into consideration when making decisions? The Supreme Court began by stating that Amendment 9 had clearly intended that the previous path of appeal against decisions of the exchange to the Supreme Court sitting as a High Court of Justice be replaced by the new route via the District Court.[337] The Court proceeded to define the scope of the review that

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Tel Aviv/Jaffa 1991), *rev'd*, 46 (2) P.D. 441 (Supreme Ct. 1992) (Isr.).

337. While some commentators saw this as an unfortunate move away from tight-

was available under the old system. The Court, quoting from the decision in *Abramson*, stated that it would not substitute its discretion for that of the exchange.[338] Where two possible approaches to a problem could both objectively meet the test of being "proper," the Court would not force the TASE to reverse its original ruling. Further, as explained in the Supreme Court decision in *Babchuk v. Tel Aviv Stock Exchange*, the Supreme Court would only interfere and reverse a ruling where the decision was void for legal reasons; the Court would not interfere with the professional judgment of the administrative body.[339] The question before the Supreme Court in the *Katz* case was whether under the new regime of appeals to the District Court the extent and scope of the review was to be expanded.

After a detailed discussion of the arguments and authorities cited by the parties, the Court decided in favor of an expanded scope of review. The Court stated that the expanded review by the District Court, allowing the judge to order adoption of a decision that the exchange could have adopted in the first place, would not constitute the substitution of the discretion of the District Court for that of the TASE. Of course, the District Court would take notice of and give weight to the professional expertise of the TASE and hesitate to interfere with their decisions, especially where those decisions related to technical, rather than legal, questions. However, the Court was quick to comment that the substantial measure of professional knowledge possessed by the TASE would not render it immune from the review of the court.

Applying these principles to the case at hand, the Court decided that the TASE procedure supported by the District Court at first instance varied from the approach expected under the Law. The District Court should move far beyond the tests of "irrelevant considerations" and "unreasonableness" available under judicial review and undertake a fundamental review of the TASE decision being appealed. The Court addressed whether the exchange, when deciding whether to delist a

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er scrutiny, others felt the lower costs and increased efficiency of the lower courts, coupled with the limits on the time of the Supreme Court, pointed in favor of the switch under the amendment.

338. Abramson v. Tel Aviv Stock Exchange, 38 (2) P.D. 1 (Supreme Ct. 1984) (Isr.). In that case, the limitations on the Supreme Court's willingness to interfere and the resulting negligible scrutiny were evident. The Court in that case stated that the TASE and the Authority were permitted to take many varied considerations into account when making decisions. A decision is not nullified, and there is no violation of the principles of "fairness" or "propriety," if the body takes a decision where the authorities and the experts are divided in their support. It is not the role of the Supreme Court to exercise discretion statutorily granted to a legal body; rather, the court will only review the decision's compliance with standards of administrative law and judicial review.

339. Babchuk v. Tel Aviv Stock Exchange, 32 (2) P.D. 377 (Supreme Ct. 1978) (Isr.).

particular security, should consider the interests of a potential shareholder whose claim to be recognized as a shareholder is still pending in separate litigation. It is clear that this is not an issue upon which the District Court should be overly respectful of the expertise of the TASE. Rather, this question, at its heart, was a quasi-legal question, as to which the courts of law are more qualified than the exchange to decide the proper approach.

Despite the expanded review process supported by the Supreme Court, it still proceeded to reverse the lower court ruling by stating that, in a specific case, the proper interests to be taken into consideration were limited to those of the current registered shareholders of the company. The exchange was in no position to begin measuring the probability of success of the appellant in his legal claim that could potentially enable him to attain the status of shareholder at some future point. The exchange could not predict future events and could only effectively give credence to the concerns of the present shareholders. Thus, the TASE had acted appropriately by acceding to the wishes of the controlling party that the shares be delisted. The Court concluded by stating that the door remained open for the appellant to seek civil damages from the current controlling shareholder, if the appellant were to succeed in his legal battle and the appellant could prove that the decision to delist the securities had caused him financial damages.

Returning to the Law, provision is also made to protect the interests of the investing public by insuring the continuity of operation of the stock exchange. The exchange is generally not allowed to close, unless in its opinion or in the opinion of the Minister such an action is necessary to protect the interests of the investing public.[340] Moreover, the exchange is not authorized to close on its own initiative for more than one business day, except with the approval of the Minister of Finance.[341] If a decision is made to close the exchange for even one day, notice of that decision must immediately be given to the Minister, who may order that the exchange not close or, if it has closed, that it reopen.[342] In short, the Law states that there is a public interest in an ongoing, regular course of exchange activity, an interest which is to be protected by the Minister rather than by the Authority. This example of the dual role played by the Minister and the Authority under the Law stands in contrast to the pattern of SEC dominance established by U.S. securities laws, to the complete exclusion of the executive branch.

Finally in this respect, the Law, in effect reasserting the role of the Authority, deals with the supervision of the exchange by the Authority. Amendment 9 made significant changes, dramatically increas-

340. Securities Law, *supra* note 2, § 50(a).
341. *Id.* § 50(b).
342. *Id.* § 50(c).

ing the scope and manner of supervision and conferring a broad discretion in this regard on the Authority, in lieu of the previous supervisory role of the Minister. The general principle governing the exercise of this control is that the Authority is responsible for the fair and proper functioning of the exchange.[343] As a result, the Authority is empowered, after allowing the chairman of the exchange to state his case, to direct the exchange to take corrective action if, in the Authority's opinion, the exchange is operating in a manner contrary to its charter, its directives, or the general principles of fair and proper management.[344] In order to enable the Authority to properly exercise these functions, the Law provides that the exchange must submit all reports to the Authority and turn over any information on the affairs of the stock exchange that the Authority may request.[345] Furthermore, a representative of the Authority is entitled to be present at all general meetings and board and committee meetings of the exchange in order to ensure that the Authority is aware of all decisions and proposals of the exchange.[346]

In the period since the adoption of Amendment 9 in 1988, the Authority has shown a willingness to pursue the supervisory responsibilities assigned to it. In order to cope with these responsibilities, the Authority has established a new committee whose sole task is to pursue the functions of the Authority in relation to the TASE. The committee focuses in particular on examining the proposed directives of the TASE and submitting suggestions to the Authority, the Minister, and the Finance Committee. As a result, the TASE has found that its heretofore relatively unfettered discretion on various issues concerned with its operations is increasingly being narrowed by the supervision of the Authority.

A number of pertinent issues were raised in the case of *Nimrodi Land Development Ltd. v. Tel Aviv Stock Exchange* in the District Court of Tel Aviv-Jaffa.[347] While certain technical aspects of the case were considered in a further 1991 proceeding in the Supreme Court sitting as the High Court of Justice,[348] the decision of the lower court is a more relevant one for present purposes. The case dealt with an appeal by a company from a decision of the TASE to impose certain conditions regarding the capital of any company, especially in relation to founder's shares, that must be met before a registered company may undertake a public offering.[349] The TASE was attempting to move in

343. *Id.* § 51(a).
344. *Id.* § 51(b).
345. *Id.* § 51(c).
346. *Id.* § 51(d).
347. Nimrodi Land Development Ltd. v. Tel Aviv Stock Exchange, 1990 (2) P.M. 89 (Dist. Ct. Tel Aviv/Jaffa 1990).
348. Nimrodi Land Development Ltd. v. Tel Aviv Stock Exchange, 45 (3) P.D. 154 (Supreme Ct. 1991) (Isr.).
349. See the discussion above of the changes caused to the Law by Amendment

the direction of the "one share, one vote" rule reflected in Section 46C, as discussed above, by requiring that holders of founder's shares maintain a certain ratio of regular shares to founders shares. It is not so much the particular facts of the case, but rather the Court's review of several important principles regarding the TASE and the Authority and their respective powers under the Law, that is important for purposes of this section.

The District Court confirmed that appealing a TASE decision is not limited by the usual framework of review. Rather, the District Court is mandated to undertake a fundamental review of the decision appealed from and to rule accordingly.[350] The District Court moved on to consider the nature of the exchange's powers. It stated that the exchange acts under the authority of the Law, and, although it is organized as a corporate entity, it is in fact an administrative body subject to the general legal principles that govern such entities. Before taking any action, the TASE had to point to the source, whether in the Law, its corporate charter or any other source, that authorized it to exercise such powers. Hence, the exchange was prohibited from limiting or canceling the rights of shareholders who had acquired their securities legally and in good faith without appropriate compensation. This especially held true in the case at hand, where the decision affected holders of founders' shares that were not even registered for trading on the exchange. While the Law revolved around the principle of full material disclosure, it in no way authorized the exchange to set conditions on an offering or the securities issued therein based on extraneous matters.

The Court continued by distinguishing the respective roles assigned to the exchange and the Authority under the Law. The Authority's function centered around the protection of the interests of the investing public. The exchange, on the other hand, is, as its name implies, a market for trading securities; the exchange's sole mandate is the management of that market in a manner that guarantees fair and proper transactions. As a result of this clear distinction, the TASE had to be careful not to interfere in the realm of functions assigned to the Authority by the Law.

The Court concluded by considering the principles that must lie behind decisions of the exchange. A legal entity such as the exchange could only make decisions in areas authorized by its founding corporate documents, or alternatively, by the Law or other regulations. Any decision regarding an issue not expressly within such boundaries was void as *ultra vires*. Thus, in the absence of clear authority to enact a decision such as the one taken by the TASE in the case at hand, the

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11 regarding this subject after the *Nimrodi* decision.

350. For a concurring view, see *supra* note 336.

Court concluded that it had no choice but to nullify such a decision. The appeal of the company was upheld and the decision of the exchange reversed.

One other feature of TASE function, not directly related to the Law, should be discussed. Due to the exemption from capital gains taxation for listed securities, a strong motivating factor for listing on the exchange, the TASE review process with respect to new prospectuses has assumed a major role. A company affecting a public offering, therefore, must overcome the hurdles of both Authority and TASE review. The TASE, in addition, has adopted substantive rules with respect to the size and track records of companies offering securities, including special rules for particular classes of securities, such as those in more speculative fields like oil and gas exploration. Consequently, to some extent the TASE has assumed the role of a demanding blue-sky commissioner in the U.S.

C. *Insider Trading*

Although the Law in its original format was largely based upon the U.S. Securities Act of 1933 and Securities Exchange Act of 1934, insider trading regulation was added by amendment in 1981. In contrast to the extraordinary interpretive structure based upon Rule 10b-5 under the Securities Exchange Act of 1934, the Israeli approach to insider trading regulation is much more detailed, to a substantial extent drawn from English and other sources. Furthermore, in contrast to the vague U.S. approach to insider trading, the Israeli approach was designed to achieve maximum clarity through detailed rules and explicit definitions.

The Law defines a company for these purposes to be one whose shares have been issued to the public by a prospectus or are traded on the TASE and, in both cases, remain in the hands of the public. The definition also includes subsidiaries and affiliated companies. The term "insider information" is specifically defined to mean any knowledge of a development or expected development in a company, a change or expected change in its standing, or other information regarding the company that is not known to the public and that if known would cause a material change in the price of the securities of the company.

An "insider" in a company is (i) a director, general manager, "principal shareholder,"[351] or another individual whose standing, position in, or ties to the company grant him access to insider information on the "determining day," defined as the day when use is made of the insider information, or within six months prior to such a date; (ii) a

351. Defined as an individual who holds five percent or more of the nominal value of the outstanding capital of the company, or of the voting rights in the company, or who has the power to appoint one or more directors.

relative of any individual listed above; and (iii) a company or other entity under the control of any person named in (i) or (ii). Finally, a "transaction" is defined as the exchange, sale, purchase, or subscription of a security, or an undertaking to affect the same, whether the individual is acting for his own account or on behalf of others and regardless of whether he acts through an agent or trustee.[352]

The Law establishes a variety of scenarios that, by statute, are considered the use of insider information. These include the execution of a transaction in securities of the company while insider information is in the individual's possession. Another example is passing insider information or an opinion based thereon to a person where there is reasonable basis to assume (or it is actually known) that the person will make use of the information or the opinion to affect a transaction or pass it to someone else. This is generally called the "tipper" liability in the "tipper-tippee" relationship in legal scholarship.[353] Similarly, a company will be deemed to have access to or possess insider information if a director or employee of the company has access to or is in the possession of the insider information, unless the company has enacted clearly drawn and properly published directives that strictly prohibit the use and dissemination of such information by those individuals for the purpose of undertaking transactions in the relevant securities and has ensured that arrangements are made for internal supervision to guarantee compliance with such directives.[354]

The Law provides that a presumption of the use of insider information will arise in certain circumstances. For these purposes, the Law created a new category, that of a "principal insider," a more tightly defined group than the general class of insiders. A principal insider is defined as (i) a director, general manager, deputy or assistant general manager, controller, internal auditor, and any individual who fulfills those duties under a different title, in addition to a principal shareholder; (ii) a relative of any of the above; and (iii) a corporate entity under the control of any individual listed in (i) or (ii). The approach is somewhat similar to the short swing profit provisions of Section 16(b) of the Securities Exchange Act of 1934 but with significant differences. Whereas Section 16(b) provides for an absolute, irrefutable presumption of use of inside information for transactions made within a six month period, the Law provides that when a principal insider profits from a purchase and sale, or a sale and purchase, of securities within a

352. Securities Law, *supra* note 2, § 52A.

353. *Id.* § 52B(a). *See also* LOUIS LOSS, FUNDAMENTALS OF SECURITIES REGULATION 83-84 (1983).

354. Securities Law, *supra* note 2, § 52B(b) (prescribing the exact nature of the directives that must be enacted). The legislative message to companies is clear: companies should institute internal programs to police the access to insider information and to prevent misuse of that information; otherwise they will be liable for employee misconduct.

three month period, that will be viewed as *prima facie* evidence that he utilized insider information, unless the principal insider can prove that he did not have any insider information at the time of the transactions, or under the circumstances it is reasonable to assume that he did not have such insider information.[355]

The Law provides that certain information is not considered insider information. For instance, any data concerning a report submitted to the Authority or to the TASE published or publicized in some accepted manner is not considered to be insider information once one exchange trading day passes subsequent to the publication. In the alternative, the facts cease to be insider information upon the passing of four days after the report is submitted to the TASE or the Authority, if they decide not to publish the report.[356] However, the Law establishes that the burden of proof is on the defendant to prove that the material was submitted and/or published in accordance with these provisions.[357]

If an insider in a company makes use of insider information, the Law makes him liable to one year in prison or a fine of NIS 6,000.[358] Similarly, a person (the "tippee") who makes use of insider information that he has received, directly or indirectly, from a person whom he knows is an insider in the company, is liable to a prison sentence of six months or a fine of NIS 3,000.[359] In addition to the criminal penalties, the Law makes a person who profits from the use of insider information liable in a civil action to pay the profits to the company whose securities were involved in the transaction.[360] The calculation of the profit from the transaction is computed by figuring the difference between the price at which the transaction (presumably the transaction in which the profit was realized) was executed and the price of the relevant security immediately after the information is made public.[361]

After establishing the scope and extent of the criminal and civil liability, the Law continues by listing a wide range of defenses that may be raised by a defendant to escape liability. Thus, the defendant is free of liability if he can prove one of the following: (i) the sole purpose of the transaction was the acquisition of "qualifying shares" that, according to the Articles of Association of the company, a director must

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355. *Id.* § 52E.
356. *Id.* § 52F(a).
357. *Id.* § 52F(b).
358. *Id.* § 52C. To appreciate the size of fines, it is worth noting that the current exchange rate is about NIS 3 to U.S. $1. Thus, the maximum fine under § 52C is equivalent to approximately U.S. $2,500. Clearly, the prison sentence is the much more serious deterrent. Note, however, that some of the fines provided for other offenses, discussed below, are much more substantial.
359. Securities Law, *supra* note 2, § 52D.
360. *Id.* § 52H(a).
361. *Id.* § 52H(b).

acquire as a condition of his service;[362] (ii) the transaction was executed in good faith in fulfillment of the defendant's responsibilities as receiver, trustee in bankruptcy or liquidator, or in the realization of a pledged security; (iii) the transaction was part of the good faith implementation of an underwriting agreement; (iv) the reason for the use of the insider information was not, or was not significantly, for the purpose of obtaining profits or preventing losses to the defendant or another; (v) the transaction was concluded by the defendant in his role as agent of another, and he did not exercise his discretion and did not give his opinion or information in a manner that brought about the execution of the transaction; (vi) the transaction was effected outside of the framework of the TASE and the other party also had the relevant insider information in his possession; (vii) the transaction was affected on behalf of an insider by a "blind trust," defined as a trust that operates at the sole discretion of the trustee without any input from the insider; (viii) the purpose of the transaction was the stabilization of the price of the security, as to which the company had established guidelines and advised the Authority of these guidelines before the transaction was affected;[363] or (ix) in the circumstances of the case, the relevant transaction was justified.[364] A special defense is available to a company in response to either civil or criminal charges in a case brought under the provision concerning the vicarious possession of insider information by the company.[365] Although a director or employee had access to or was in the possession of the insider information about the company whose securities were involved in the transaction, the company will be excused from liability if it can prove that the director or employee in question was not the individual who made the decision to effect the transaction and that there is a reasonable expla-

362. Whereas qualifying shares were once reasonably common in Israeli companies, especially private ones, they are almost non-existent today in Israeli public companies or substantial private ones.

363. The existence of the stabilization defense was used by the major Israeli banks as one of a series of arguments in legitimization for very substantial market support of their shares. Those arguments were submitted before a special government commission, the Beisky Commission, which was established to review these matters, and more recently in a criminal proceeding against those banks, their chief officers and some bank accountants. Most of the defendants were convicted on February 16, 1994 and sentenced on April 14, 1994. Israel v. Bank Leumi Le-Israel B.M., (Dist. Ct. Jerusalem, unreported decision). The case has been appealed to the Supreme Court. The background to the indictments was discussed in Uri. Ganor v. Attorney General, 44 (2) P.D. 485 (1990), a case brought in the Supreme Court, acting as the High Court of Justice, as a result of which the Attorney General was required to reconsider his earlier determination not to prosecute the banks and related parties.

364. Securities Law, *supra* note 2, § 52G(a). The last defense constitutes a fully justified grant of broad authority to the courts, in this complex area, to create additional defenses where justified on a case by case basis.

365. *Id.* § 52B(b).

nation for the execution of the transaction.[366] The Law establishes that no transaction will be voided only by virtue of the violation of any provision as to insider trading.[367]

The Law adopts rules governing securities transactions by employees of the members of the exchange.[368] For purposes of this section, an "employee of a stock exchange member" includes a director or employee of the member, his spouse, his family members whose sustenance depends on him, and companies under the control of any of those. Similarly, "security" is taken to include shares, or securities convertible or realizable into such shares, that are registered for trading on the TASE.[369] The Law provides that an employee of a member may not affect a purchase or sale of securities, otherwise than in the course of trading on the TASE by written instructions given at least one day prior to the date of the transaction.[370] Further, such an employee must hold all of his securities in an account under his own name with a member of the exchange.[371] Similar provisions apply to limit the manner in which an employee of a member may effect a transaction on behalf of someone else.[372] The Minister is empowered to enact regulations, after consultation with the Authority and with the approval of the Finance Committee, that place a ban on trading for various categories of employees of members and in relation to various categories of securities.[373]

Some other insider trading issues were examined by the Jerusalem District Court in the 1988 case of *Establissement Mollet de Dupont Freres, Vadus v. United Mizrahi Bank Ltd. and Aaron Meir*.[374] The individual defendant, managing director of United Mizrahi Bank Ltd., acquired shares from the plaintiff in an Israeli company for the bank a short time before the company was to make a public offering and register its shares for trading on the TASE. Although the public offering

366. *Id.* § 52G(b).

367. *Id.* § 52J.

368. *See id.* § 45C (concerning acquisition of securities by board members and employees of the TASE).

369. *Id.* § 52I(a); *see also supra* note 111 (discussing a case in which this limited definition of "securities" resulted in the acquittal of one of the defendants on a charge under Section 52 of the Law). Because the change dealt with the purchase of the shares in an initial public offering, the shares did not yet fit the definition of "being registered for trade on the TASE."

370. Securities Law, *supra* note 2, § 52I(b); *see also supra* note 233, where one of the charges in the case included offenses against § 52I(b), (c) by an employee of an exchange member.

371. Securities Law, *supra* note 2, § 52I(c).

372. *Id.* § 52I(d); *see also supra* note 112 where the judge conducted an examination of some of the technical aspects of the interpretation of this section in convicting one of the defendants of offenses under its provisions.

373. Securities Law, *supra* note 2, § 52I(e).

374. Establissement Mollet de Dupont Freres, Vadus v. United Mizrahi Bank Ltd., 1989 (2) P.M. 268 (Dist. Ct. Jerusalem 1989).

and the act of registration for trading was likely to result in a rise in the value of the shares, the defendant, who was also a member of the board of directors of the company, decided that it was not necessary to reveal the fact of the intended public offering and registration to the plaintiff. Based on this background, the plaintiffs applied to the court for a declaratory judgment that the defendants had not acted in good faith in the negotiations for the purchase of the shares.[375]

One of the defenses offered by the individual defendant centered around the question of insider information under the Law. Because the plans of the company were not known to the public, the defendant claimed that under Section 52C of the Law he was prohibited from revealing this information to the other party, information to which only the defendant had access in his capacity as director of the company. The judge rejected this claim and instead stated that the terms of the Law regarding insider information in fact further served as a basis to criticize the defendant's actions. She stated that the defendant himself had run afoul of that section of the Law by making use of insider knowledge in effecting the questioned transaction.[376] Finally, the judge on her findings of fact rejected outright the defendant's claim of falling under a number of the defenses listed in Section 52G.[377]

The judge continued by stating that the provisions of the Law regarding insider information were meant not only for the protection of the company but also for the protection of parties who deal with an individual with inside information. While the Law does state in Section 52G(a)(6) that a defense is available where the transaction was affected with another party outside of the exchange and where both parties have access to the inside information, the judge stated that where, as in a case like the one before the court, an individual was prohibited under the Law from disclosing the information to the other party, the party with the information was not allowed to execute the transaction by virtue of his possession of an unfair advantage.

However, as stated above, the Law also provides (in Section 52J) that a transaction is not voided solely by virtue of a violation of any of the offenses. Further, the Law does not make any provision regarding the obligation of good faith in the framework of transactions that it outlaws. Thus, the judge felt that the ordinary principles of good faith that apply in Israeli civil law must apply to these cases. As a result, the judge undertook to apply some of those principles, as articulated in the Contracts Law 1973, to the facts of the case. She pointed out that

375. Contracts Law of 1973, § 12 (requiring good faith in contract negotiations, just as § 39 of that law requires good faith in contract implementation). These sections, based mainly upon Continental civil law precedents, have spawned case law extending the good faith requirement to other fields as well.

376. The judge especially pointed to § 52B(a)(1) of the Law.

377. The claimed defenses are found in § 52G(a)(4), (5), (9) of the Law.

the failure to disclose a material fact to the other party in a transaction, when that party could not himself have discovered that information, was enough in itself to constitute bad faith. She also noted that such obligations could apply in the pre-contractual stages of negotiations and that, in certain circumstances, the obligation to disclose may require the party to reveal the facts of his own initiative, and not necessarily in response to a question of the other party. Therefore, in the court's opinion the defendant had acted contrary to good faith and the plaintiff merited the requested declaration.

While there are not many reported cases of litigation in Israel regarding the insider information provisions, there have been an increasing number of criminal indictments brought in the Magistrate's Court, with convictions obtained in most of the cases (in non-reported decisions).[378] These indictments and convictions have resulted in a flurry of news articles that will probably have a material deterrent effect in this area.

IX. SPECIAL CIVIL AND CRIMINAL LIABILITIES

Two chapters of the Law consider the extent and scope of the civil and criminal liabilities incurred by parties who violate provisions of the Law and regulations. Liability connected with the publication of a defective prospectus was reviewed above. Other securities law liabilities are discussed herein.

The Law establishes a general civil liability of an issuer of securities for all damages caused to a holder of the securities caused by the issuer's violation of the Law or regulations, of the Joint Investments Trust Law of 1961 or regulations, or the terms of the trust indenture under which debentures of the company are held.[379] The liability of the issuer extends to the directors, the general manager, and any controlling party in that company.[380]

This section may have the unintended effect of adding to the number of parties potentially liable for misleading particulars in a prospectus. For instance, controlling shareholders and general managers who are not directors are not obligated to sign the prospectus and, therefore, are not liable under Section 31 for misleading particulars in a prospectus. Similarly, a trustee who holds certificates of obligation in trust for the holders of the issuer's debentures is liable to those holders for any damages caused to them by the trustee's violation of the trust

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378. *See e.g.* Israel v. Gibor Sabrina, Crim. Action 5322/90 (Tel Aviv-Jaffa Magistrates Court); Israel v. Joseph Peleg, Crim. Action 6206/89 (Tel Aviv-Jaffa Magistrates Court). The judge in both of these cases, Judge Bracha Ofir, has been particularly active in dealing with securities law cases.

379. Securities Law, *supra* note 2, § 52K(a); *see* §§ 35A-35O for the provisions regarding trust indentures.

380. *Id.* § 52K(b).

indenture or of the provisions of the relevant sections of the Law and regulations.[381]

The liability may be avoided if a defendant can meet the requirements of one of the listed statutory defenses. A party will not be liable if he can prove that (i) he took all the appropriate steps to prevent the breach; (ii) he did not, could not have known, or ought not to have known of the violation; (iii) the injured party acquired the securities at a time when he did know or ought to have known of the existence of the violation.[382] In any case where more than one party is liable to the plaintiff, a common occurrence in securities cases, the defendants are liable, jointly and severally, for all damages. Among the defendants themselves, the rules governing the contributions of tortfeasors will apply.[383]

The Law establishes a broad range of criminal sanctions available against various parties for violations of different sections of the securities law.[384] The first portion of the chapter consists of different groupings of uniform penalties for sets of violations.

The first category of these offenses renders the party liable to three years imprisonment or a fine that is calculated as four times a standard rate set in Section 61(a)(3) of the general Penal Law of 1977 (the "Penal Law").[385] The offenses include (i) the issuance of a prospectus without a permit from the Authority, as required under Section 15(a) of the Law, with the intention of misleading the reasonable investor, the burden of proof being on the defendant to prove that he did not so intend to mislead; (ii) the violation of Section 16(a) of the Law, which provides that a prospectus must contain all information likely to be important to the reasonable investor, if the defendant is unable to prove that the failure to do so was not calculated to mislead the investing public; (iii) the giving of an opinion, report, or confirmation containing misleading particulars, that was included or mentioned in the prospectus with the prior knowledge of the defendant; and (iv) a variety of violations of the terms of Sections 36-37 regarding current reports to the Authority or the TASE, including the provision of a

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381. *Id.* § 52L.

382. *Id.* § 52M.

383. *Id.* § 52N.

384. *See Rubinstein, supra* note 112, where the judge stated that the securities law has focused its attention on civil remedies. The lawmakers have continued to ignore criminal sanctions at the same time that they have amended numerous provisions relating to civil remedies over the year. The judge especially pointed to the Knesset's unwillingness to ease the difficult burden placed on the prosecution of proving fraudulent influence in order to constitute an offense under § 54(a)(2) of the Law.

385. Section 61(a)(3) of the Penal Law provides for a fine equal to NIS 36,000, so that the fine provided for by the Securities Law would be NIS 144,000, roughly equal to U.S. $48,500 (based on mid-December 1993 exchange rates).

report under those sections to the Authority or TASE that includes a misleading particular that is intended to deceive a reasonable investor.[386]

The second, less severe, grouping renders the offender liable to one year in prison or a fine equal to three times the standard set in Section 61(a)(2) of the Penal Law.[387] These offenses include (i) violation of Section 13 of the Law, which provides for the confidentiality of the proceedings of the Authority and the materials submitted to it; (ii) violation of Section 16(a) or Section 18(a), regarding the inclusion of all relevant information in the draft or final prospectus;[388] (iii) failure to comply with the provisions of Section 25(d), which outlines the responsibilities of various parties to furnish a report to the Authority immediately upon learning of the inclusion or omission of a particular from a prospectus that the Authority might consider warrants amendment of the prospectus; (iv) failure to follow instructions of the Authority under Section 25(a) or Section 25A(b) regarding the amendment of a prospectus; (v) neglecting to perform responsibilities under Section 35B(a) regarding the appointment of a trustee by deed before the issuance of certificates of obligation or under Section 35J concerning reports of the issuer to the trustee in such cases; (vi) the offering of securities to the public without the permit of the Minister, contrary to Section 39(a); (vii) the operation of a stock exchange without a license, in violation of Section 45(a); (viii) violation of Section 52I(b), which prohibits an employee of an exchange member from engaging in a transaction in securities other than in the course of trading on the TASE via written instructions given at least one day before the transaction is effected; (ix) breach of Section 52I (c or d), which governs the holding of securities and transactions involving them by an employee of an exchange member on his behalf or on behalf of others; (x) failure to fulfill the provisions of Section 56A(a) or Section 56C(a), which provide authority to subpoena information or documents and to interrogate involved parties when there exists a suspicion that a provision of the Law may have been violated; and (xi) breach of Section 56E, which

386. Securities Law, *supra* note 2, § 53(a) (providing also that certain evidentiary rules construe delays and improper reports as *prima facie* proof that the intention to mislead lay behind the hesitation to submit the proper reports within the time set by the regulations).

387. Section 61(a)(2) of the Penal Law provides for a fine of NIS 14,000. Accordingly, the fine provided for in this section of the Law would be NIS 42,000, equal to approximately US$14,150 (based upon mid-December 1993 exchange rates).

388. The lack of a distinction between a violation of the prospectus rules in the draft or final prospectus should be noted. As indicated previously the 1988 amendments added the requirement for director signatures on draft prospectuses. Civil liability under Sections 31, 32, and 35 of the Securities Law of 1968 only applies to the final prospectus. Therefore, in order to raise the level of draft prospectus preparation, stiff criminal sanctions were imposed, an approach that is too harsh and therefore impractical.

guards the confidentiality of the information obtained under the powers of investigation granted to the Authority under the Law.[389]

The last major grouping subjects offenders to a fine of three times the standard level established in Section 61(a)(1) of the Penal Law[390] but does not refer to a prison term. The relevant offenses include (i) violation of the terms of Section 5 or Section 10(b) regarding the acquisition and notification of holdings of securities by members or employees of the Authority; (ii) the failure of an interested party to deliver particulars to the issuer under Section 17(c), which the latter needs in order to fulfill its disclosure requirements in the prospectus; (iii) publication of a prospectus where the provisions of Sections 22 and 23 regarding the approval and signature of the prospectus by the relevant parties and the proper manner of dating and publishing the prospectus have not been fulfilled; (iv) failure to comply with the terms of Section 23(c) regarding submission of the prospectus to the Registry and public notice of its publication, or with the instructions of the Authority under Section 23(d) regarding the distribution of copies; (v) the acceptance of orders for securities offered by prospectus outside of the periods allowed under Sections 24(c) and 25(c); (vi) failure to fulfill obligations under Section 26(b) or (c) or Section 27(a) or (b)(3) regarding the refund of payments to those whose orders for securities under the prospectus were canceled or not filled for other reasons; (vii) violation of the terms of Section 28(a, b) concerning the investment of monies received on account of orders for securities and the refund of such funds, or of the terms of Section 30 regarding the notification to the Authority of the results of an offering by prospectus; (viii) non-compliance with regulations made under the authority of Section 35D(b) regarding the nature and obligations of a trust company holding certificates of obligation on trust for the holders; (ix) violation of the provisions of Sections 36, 36B, or 37 regarding current reports to be submitted by various parties to the authorities or failure to comply with regulations or directives regarding such reports that the Authority is empowered to enact under Section 36A; (x) an offeror or other corporate entity that fails to fulfill its obligation to provide for the inspection of documents by the public under Section 44; (xi) failure to publish the charter of the exchange under Section 49; and (xii) violation of Section 51(c), which states that the exchange must submit reports and information as requested by the Authority.[391]

The Law addresses a number of special provisions regarding particular offenses. If a continuing offense is committed under the pro-

389. Securities Law, *supra* note 2, § 53(b).

390. The fine provided for by Section 61(a)(1) of the Penal Law is NIS 7,000. Thus, the fine called for by the Law is NIS 21,000, equal to approximately U.S. $7,100 at mid-December 1993 exchange rates.

391. Securities Law, *supra* note 2, § 53(c).

visions of Sections 36, 36B, or 37, regarding the submission of current reports to the authorities by various involved parties, or under the regulations established by the Authority by virtue of Section 36A regarding such reports, the Court may impose an additional fine equal to one-fiftieth of the total fine for each day that the offense continues.[392] Further, if any of the offenses detailed in this section were committed by a company, the directors and general manager are also criminally liable, unless they can prove either that the violation occurred without their knowledge (and that they did not need to or could not have known of them) or that they took all reasonable steps to prevent the commission of the offense.[393] In one case, a company was convicted of failing to render periodic reports. The court, however, excused a senior officer of the company from any responsibility on the assumption that he had indeed taken all reasonable steps to prevent the commission of the offense. It took fifteen detailed pages to get to that result.[394]

The final area of criminal liability covered in this chapter regards the more serious offense of committing fraud in connection with securities transactions. A person violating one of these rules is liable to five years imprisonment or a fine equal to five times the standard stated in Section 61(a)(4) of the Penal Law: (i) the inducement or attempted inducement of a person to acquire or sell securities by way of a forecast or promise, written, verbal, or otherwise, when he knows or ought to know that such are false or misleading, or by way of withholding of material information; or (ii) the fraudulent or manipulative influence on the movement of the price of securities.[395]

An important case arose under this Section in the State's appeal to the District Court of Tel Aviv-Jaffa from an acquittal of the defendants by the Magistrates Court in the 1989 case of *State of Israel v. Yaakov Rosenbach*.[396] The case concerned the execution of "matched orders" by the defendant in order to arouse a dormant market for trading in the securities of a certain company. The operation accomplished its goal of driving the price of the shares to a level that the defendant

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392. *Id.* § 53(d).

393. *Id.* § 53(e). For similar provisions regarding the civil liability of the issuer and its employees, but without the defenses specified as to criminal liability, see *id.* § 52K(a), (b).

394. Israel v. Rassco Ltd., Crim. Claim 1298/90 (Magistrates Court Tel Aviv-Jaffa 1991) (unreported).

395. Securities Law, *supra* note 2, § 54(a); *see* Sassoon H'ugi v. The Int'l Bank, 1985 (1) P.M. 256, (Dist. Ct. Tel Aviv/Jaffa 1985) (concluding that once the judge had decided that the investment advice given by the defendant to the plaintiff was not negligent, there could be no finding of violation of the terms of § 54(a)(1) of the Law).

396. Israel v. Yaakov Rosenbach, 1989 (2) P.M. 309 (Dist. Ct. Tel Aviv/Jaffa). Under Israeli jurisprudence, the State can appeal from an acquittal in a criminal case, and the higher court may convict. Such an appeal is a fairly common occurrence in Israel.

felt was appropriate, considering the circumstances of the company, a level at which investors would have been willing to sell their shares to allow the defendant to increase his holdings. The question before the court was whether the execution of matched orders transgressed Section 54(a)(2) of the Law, which prohibits the fraudulent manipulation of the price of securities. The three judges arrived at the same verdict, overturning the acquittal. However, one judge, Michael Ben-Yair, who in late 1993 began to serve as Israel's Attorney General, arrived at his decision by applying different principles than those considered by the other two.

The other two judges, Judges Ben-Ito and Even-Ari, followed the standard established by Judge Ben-Ito in her judgment in the 1980 District Court case of *State of Israel v. Yaakov Levinkoff*.[397] There, as part of a 2-1 majority, she stated that speculation is an acceptable form of trading in securities — in a sense, as a form of betting on the market based on evaluations of market conditions, economic knowledge, and an analysis of the available information. Manipulation, on the other hand, is a direct action that seeks to influence the fluctuations in the value of the securities beyond that which the market itself justifies. However, in order to constitute a crime, the manipulation has to be in a deceitful manner.

In *Levinkoff*, Judges Ben-Ito and Even-Ari held that even a legitimate action could become manipulative in the legal sense if the action is utilized, in a deceitful manner, to create a false impression regarding the value of the shares and to influence that value. In their opinion, the execution of matched orders was a classic example of such a manipulative action. Manipulation is not established by the fact that the action was simply intended to adjust the price of the security to a suitable level, even if the action did create a false impression regarding the market for the securities. However, Judge Even-Ari added, creating a false impression of activity in the market for a security when in fact no such activity existed was enough, in itself, to constitute a violation of the Law, if the purpose was to influence the value of the security. He rejected as groundless the distinction between the proper motive and the criminal intention, pointed to as integral by Judge Ben-Yair. Judge Even-Ari concluded by stating that it is possible that a situation may arise where there is no legal way to accomplish a desired goal. However, the absence of such a legal route does not in any way validate a violation of the law by a citizen in the pursuit of that goal. The prosecution was not required, contrary to *dicta* of Judge Ben-Yair, to offer proof of an alternative method of achieving the goals before it can be said that it had proved criminal intention.

Judge Ben-Yair, on the other hand, showed greater concern for

397. Israel v. Yaakov Levinkoff, 1980 (2) P.M. 221 (Dist. Ct. Tel Aviv/Jaffa 1980).

the motives behind the defendant's activities. He stated that the nature of the activities causing fluctuations in the value of the shares could not be properly established without paying attention to the motives of the individual who undertakes those actions. He established, as a principle, that if the motivation for the activity is legitimate and proper, then the activities will not be illegal regardless of the influence they may have on the price of the securities. This holds true whether or not these fluctuations were a principal or concurrent result of the actions. Thus, transactions in securities, including matched orders that contain a measure of pretense, may be legal if they are accompanied by a legitimate motive. The underlying motive of the defendant in this case, in the end, was to increase his holdings in the securities of the company; both sides conceded that this was a legitimate motive.

However, contrary to Judge Even-Ari, Judge Ben-Yair felt that there was an important distinction between a legitimate motive and criminal intention. He stated that the issue at hand was whether such a distinction could be drawn, thus allowing the prosecution to prove the requisite criminal intention. He decided that it was necessary to prove that the defendant had an alternative method of fulfilling his desire without influencing the price of the shares, in order for the court to distinguish between the possibly legitimate motive and a criminal intention. Judge Ben-Yair felt that the possibility of accomplishing the stated goals by continually entering buy orders on the market, in conjunction with a willingness to purchase any offered shares until the price of the shares reached the desired level at which the public would be willing to sell its shares, showed that there was such a legitimate alternative. This option, albeit slower than the one selected, was the proper route that the defendant should have adopted, rather than attempting to reach his goal by creating a false picture of activity that constitutes an offense. Once this alternative had been provided, the prosecution had relieved itself of the burden of proving criminal intention despite the legitimate motives behind the defendant's activity.

In a 1993 case, the District Court held that a money manager who acted also as a financial reporter had used his newspaper column to affect the market price of securities, using false information and forecasts, while benefitting personally from transactions in those securities. He was held to have committed fraud in connection with these transactions, a violation of Sections 54(a)(1) and 54(a)(2) of the Securities Law. The Court acquitted him other such claims.[398]

The difficulties in defining the offense and the circumstances of its commission, reflected in the varied approaches of the judges in the Levinkoff and Rosenbach cases, shows the need for legislation to pro-

398. State of Israel v. Aharon Zilberman, Crim. Action 97/91 (Dist. Ct. Tel Aviv/Jaffa, 1993) (unreported).

vide a more accurate definition of the elements of the offense.[399] In light of the severity of the violations involved and the potential financial effects on the investing public, lawmakers should overcome their reluctance to reconsider the criminal sanctions under the Law and clarify these essential sections in the interests of fairness and certainty.

A. *Representative Class Actions*

One of the most significant additions to the Law under Amendment 9 was the creation of representative class actions in securities cases. The explanatory notes to the draft of the Amendment explained that the goal was to provide a mechanism by which an investor, whose personal damages are small but are part of a significant potential sum of collective damages, could seek restitution in the courts without having to contend with the large expenditures of money and time required to prove a claim. This form of action has recently begun to be a significant weapon in combating violations of the Law. Israeli securities law procedures have thus been revolutionized, bringing them much closer to U.S. procedures.

The Law defines a number of the general principles underlying the representative class action. Any holder of securities is authorized to bring a suit in the name of a group of holders on any legal grounds and against any defendant against whom an individual could have brought suit in his own right.[400] If the requested remedy under the claim is damages, the only prerequisite to establishing the action is proof that he has suffered such damages.[401] In addition, a decision of the court in the class action is considered to be a verdict for all members of the class, subject of course to the definition of "class" provided by the Law as described below.[402]

Before the class can be defined, the court must sanction the proposed representative action. A court will permit an action if it is convinced of the following facts: (i) the action is brought in good faith; (ii) there is a reasonable chance that material questions of fact and law, common to the members of the class, will be decided in their favor in

399. *See supra* note 25. The Supreme Court reversed the conviction of a defendant under § 54(c) of the Securities Law of 1968 for use of misleading offering materials.

400. Securities Law, *supra* note 2, § 54A(a). Thus, the action may lie against, among others, an offeror, issuer, underwriter, or interested party, or directors or senior management, in addition to professionals who rendered opinions to be included in a prospectus or report. Interestingly, the Section speaks of a suit "on any legal ground", suggesting that the Israeli representative class actions may be available for claims arising from legal theories outside of securities law. The Section has not yet been tested in this respect.

401. Securities Law, *supra* note 2, § 54A(b).

402. *Id.* § 54A(c).

the course of the proceedings; (iii) the size of the class justifies the claims being brought as a representative class action; (iv) under the circumstances, the representative class action is the most effective and fairest manner to decide the relevant issues; and (v) there is a reasonable basis to believe that the plaintiff represents the interests of the entire group in a proper fashion.[403] One very important factor in the Law's approach is the need to have court approval of the legitimacy of the class action, an extremely important safeguard against abuses of judicial process. This safeguard is even more important inasmuch as the class action was added to an already busy, competitive judicial legal system.[404]

Once the court has certified the class action, it must define the class on whose behalf the action will be conducted and give directives for the publication of its decision in that respect. The Law does not require a potential claimant to opt in to a group action. Rather, it considers any person falling within the court-defined class as consenting to be included in the group claim. That person may, however, notify the court within forty-five days of publication of the decision that he desires to opt out of the class. This period may be extended in special circumstances for certain persons upon application to the court.[405]

Because the interests of the group are being put forward by a single representative plaintiff, that individual is prohibited from dropping the action or arriving at a compromise settlement with the defendants without court approval. Thus, the court has an active role to ensure that group interests are not sacrificed in favor of a collusive settlement.[406]

The Legislature authorizes the Minister of Justice to adopt regulations concerning procedural issues regarding the submission of group claims and of their conduct by the courts. In particular, the Minister may establish guidelines for proving damages by each member of the class. Such regulations were published soon after the Amendment was adopted, under the title Securities Regulations (Procedure in Class Actions) 1991. Whereas the Law provides that all other regulations are to be promulgated by the Minister of Finance, the regulations concerning court procedural matters are to be issued by the Minister of Justice.[407]

The regulations state that a plaintiff seeking certification for a

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403. *Id.* § 54B.

404. There were over 12,000 licensed lawyers in Israel in late 1993, and the number promises to increase very rapidly in the years ahead. Over 2,000 new lawyers are expected by the end of 1995.

405. *Id.* § 54C.

406. *Id.* § 54D. This protection seems fair since many of the plaintiffs will usually be forced into the class action in default of opting out of the group.

407. *Id.* § 54E.

class action should attach a request to the statement of claim, submitted under summary proceedings.[408] The request should include details such as the estimated maximum number of claimants in the class, the material issues of law and fact common to the group, the bases upon which the request for class certification are grounded, and the proposed method of remuneration of the lawyer who represents the claimant.[409]

The court may accept the application and sanction the class, or it may amend the application regarding any of the particulars of the action where necessary to ensure the effective and fair pursuit of the claim. If the court accepts the application after amending it, the applicant is authorized to amend his statement of claim accordingly or to drop his claim altogether.[410] If the plaintiff elects not to pursue the action, or if the court decides not to certify the claim because of its failure to meet any of the conditions listed in Section 54B of the Law, then the "failure" of the class action does not prevent either the representative plaintiff from pursuing a claim in his own name or another claimant from applying for the certification of a class action in the name of the same or a similar group.[411]

The regulations then deal with cases where the court certifies the class. They detail the approval that the court must give and the notice that must be publicized. These requirements include (i) the definition of the class that will be covered by the action; (ii) the basis of the claim and the desired remedies; (iii) the material questions of law and fact which are common to the whole group; (iv) any instructions regarding the proceedings in the court, as the court deems appropriate; and (v) instructions regarding the manner and content of the notice of the decision of the court and who will bear the costs of publication of the notice.[412]

The notice must contain the following information: (i) the name and address of the representative plaintiff; (ii) the definition of the class and the grounds of the claim and the desired remedies; (iii) the name and address of the lawyer who will represent the group; (iv) advice of the fact that the decision of the court in the action will be considered a verdict binding on all members of the class; and (v) notice that all people included in the group will be deemed to have agreed to the class action unless they indicate to the court their desire to opt-out of the group, within forty-five days of the notice or within an extended period that the court may set, on application, for a particular individu-

408. *Id.* § 2-5752.
409. *Id.* § 3.
410. *Id.* § 5.
411. *Id.* § 5 & 6.
412. *Id.* § 7.

al.[413]

Once these procedural outlines have been established, the regulations deal with the verdict in the action. If the court decides that the grounds of the claim have been proven in favor of the plaintiff, it is authorized to instruct each member of the group to prove his entitlement to the requested remedy by way of an affidavit.[414] If the requested remedy is damages, the affidavit should at least include information regarding the type, amount, and value of the securities held by the claimant at the date relevant to the claim.[415] However, the court is authorized to waive or amend this requirement for an affidavit if convinced, in the circumstances of the case, that such a requirement would place an unwarranted burden on the members of the group.[416] The court may also, as it deems appropriate, direct the manner in which its decision will be brought to the notice of the members of the class.[417]

The regulations state that the withdrawal of one plaintiff from the representation of an authorized class, with the permission of the court, does not impair the substitution of another plaintiff as representative of the class. However, withdrawal of all potential plaintiffs from representation of the group will result in the cancellation of the action.[418] The regulations conclude by stating that any issue regarding representative class actions not covered by the Law or the regulations will be dealt with under the general regulations on civil procedure.[419]

A plaintiff who submits a class claim is required to notify the Authority, the exchange upon which the relevant securities are traded — the TASE — and the Attorney General.[420] Since it is unfair to ask the representative plaintiff to bear the full cost of the application and a claim that is in the public interest, the Authority may accede to a request to pay the costs, on terms and in an amount set by it, if the Authority is convinced that the claim is in the public interest and that there is a reasonable chance that the court will certify the class.[421] If

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413. *Id.* § 8.
414. *Id.* § 9(a).
415. *Id.* § 9(b).
416. *Id.* § 9(d).
417. *Id.* § 9(c).
418. *Id.* § 10.
419. *Id.* § 11.
420. *Id.* § 54F. In Israel, the Attorney General is the senior legal official in the Government. His role, a strictly non-political and professional one based on the English pattern, is to provide legal advice on matters of importance and to serve as the final arbiter of questions whether an indictment should be pursued in a controversial case.
421. *Id.* § 54G. It should be considered whether the decision on financing claims that are in the public interest would be better left to an independent (possibly judicial) figure, better qualified to identify deserving claims and free from possible accusations of conflicts of interest.

the final verdict includes an award of damages, the court is instructed to order that the Authority be compensated, on terms and conditions set by the court, for any expenditures undertaken in the financing of the representative action.[422]

Further, the court is directed to set the remuneration of the lawyer who represents the class in the action, notwithstanding any agreement between the lawyer and the representative plaintiff. In addition, the total fees of the lawyer may not exceed the sum set by the court for these purposes.[423] In order to encourage claimants who are often reluctant to serve as the representatives of the class, the court is authorized, in its verdict of damages, to order that a specified share of the total award, after expenses and lawyers fees have been deducted, be paid to the representatives in recognition of their efforts, with the remaining amount being divided between the other claimants in proportion to their damages.[424]

The Law concludes with this topic by stating that its provisions do not in any fashion affect the ability of any holder of securities to seek an alternative form of remedies against the defendant.[425] The provisions regarding the class actions only apply to cases where the claim arose after October 31, 1988.[426]

The Supreme Court first considered the issue of representative class actions in October, 1993.[427] The Court, led by its president, Justice Meir Shamgar, considered a request for permission to appeal brought by the Teva Corporation against a decision of the District Court of Tel Aviv-Jaffa to certify a representative action brought by a group of investors against the company. The action concerns a claim that the company delayed the release of the news of an approval of one of its generic drugs by the U.S. Food and Drug Administration until after the expiration of a group of options held by the investing public. The plaintiffs claimed that the company wanted to prevent the inevitable rise in the price of Teva's shares on the TASE from occurring before the options expired in order to ensure that the investors would not exercise their options. When the plaintiffs applied to the District Court for certification of the case as a representative action, the company objected on two grounds. First, the company claimed that the representative plaintiffs did not fall within the scope of potential claimants considered by the Law, which includes only holders of securities. Since the

422. *Id.* § 54I(1).
423. *Id.* § 54H.
424. *Id.* § 54I(2).
425. *Id.* § 54J.
426. *Id.* § 54K.
427. Teva Pharmaceuticals Industries Ltd. v. Zat Economic Advisors Co. Ltd., Civil Request for Permission to Appeal 1701/93 (not yet reported). The decision was rendered on October 14, 1993.

claimants had only held options that had now expired, some even selling them before the expiration, they could only be described as former holders of securities. Second, the options upon which the claims were based could not, according to the company, be described as securities for the purpose of class actions. The District Court rejected both of these arguments.

In response to the request for leave to appeal, the Supreme Court upheld the decision of the District Court rejecting the claims of the company. The Supreme Court held that the only relevant date for the establishment of a claim was the date on which the grounds for the claim were established. Thus, the plaintiffs only needed to prove that they were holders of securities on that date for the purposes of bringing an action. This ruling significantly increases the scope of potential claims as representative actions. Despite Teva's claims that such a decision would widen the scope of an action beyond manageable bounds, it is now clear that the Court was prepared to allow even those investors who sold their securities to participate in the claim. Thus, the Court held, it is possible that a defendant will be required to compensate more than one investor with regard to damages for the holding of the same security, so long as the class members were damaged.

On the second claim of Teva, the Court held that it went against the spirit of the Law to claim that options fall outside the definition of security for the purposes of these actions. As a possible alternative, the Court suggested that the company should have explicitly stated in the prospectus the fact that the options are not to be considered as securities, if the company so desired. Justice Shamgar noted, in all fairness, that after the Court had reached its decision, but before it was announced, Teva's lawyers withdrew their argument as to the definition of "security."

Once a class has been certified, it remains for the courts to consider the claims for damages themselves. It seems that this case, as well as other cases involving various large Israeli companies that the press has reported as forthcoming,[428] will provide the courts with ample opportunity to make various judicial pronouncements and rulings as to important mechanism for investor protection. Perhaps, courts in the future will follow the Supreme Court in the Teva case and maintain a broad approach to the representative action. In the present market, such a mechanism is an indispensable tool in the arsenal available to the courts for policing the conduct of companies towards their shareholders.

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428. For example, a class action was filed in December 1993 against the Isramco group of oil and gas exploration companies for NIS 96 million.

B. *General Provisions*

The final chapter of the Law is a collection of miscellaneous provisions regarding a wide range of issues that were not otherwise covered. The most important of these provisions are discussed below; a few provisions in this chapter of the Law have been considered elsewhere herein.

The Law outlines a number of powers granted to the Minister of Finance. The Minister is authorized, after consulting the Authority and gaining the approval of the Finance Committee, to adopt regulations concerning payment and collection of fees to the Authority.[429] Further, in a broad statement, the Minister is charged with supervising the implementation of the Law. After consultation with the Authority, the Minister may also enact regulations in connection with any aspect of that responsibility, as long as the Law does not contain provisions to the contrary. Similarly, the Minister of Justice is authorized to enact procedural regulations regarding various legal issues raised in different parts of the Law.[430] In addition, the Minister of Finance, upon the proposal of the Authority, consultation with the Minister of Justice, and the approval of the Finance Committee, is instructed to issue regulations concerning an underwriter who undertakes to acquire all of the securities offered under a prospectus and which are not acquired by the public. These regulations should include provisions regarding the following: (i) qualifying conditions; (ii) professional liability insurance and minimum equity; (iii) reports that the underwriter must submit; (iv) limitations in relation to conflicts of interest between the underwriter and any individual who acquires securities offered by the relevant prospectus through his services or at his behest; and (v) any other issues related to the underwriter's business.[431] Under the same mechanism, the Minister should also make regulations concerning the acquisition of control of and an offer for the purchase of securities of a company registered for trading on the TASE. Further, the regulations should cover the issue of securities in the registered company that are not offered to the public and restrictions regarding conflicts of interest between the registered company and a controlling party in it or a company under the control of such a party.[432]

The last major area covered in this chapter, widely expanded under Amendment 9, is a delegation of various investigative powers to

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429. Securities Law, *supra* note 2, § 55A.

430. *Id.* § 56(a), (b).

431. *Id.* § 56(c). *See also* Section 25 of the Prospectus Regulations of 1969 for provisions regarding the inclusion of details of the underwriter in the prospectus.

432. Securities Law, *supra* note 2, § 56(d). Sections 56(c)-(d) became effective on March 1, 1992. Subsection (d) applies for only one year after its commencement with the possibility of extension for another year by the Minister, with the approval of the Finance Committee.

the Authority to assist in the enforcement of the various provisions of the Law and the Joint Investments Trust Law 1961. Prior to Amendment 9, the Law was subject to considerable criticism for failing to provide for broad investigative powers in these areas. Amendment 9 was designed to grant powers to the Authority similar to those exercised by the SEC. Under the Law, if the suspicion of a violation arises, or if assistance is needed to administer the rules, the chairman of the Authority, or any person authorized in writing to act in his stead, may demand from any person access to any information or document regarding the business of any company to which the provisions of the relevant laws apply. After inspecting the documents, the Authority must return them to their respective owners within six months of obtaining them, unless an indictment has been submitted in a case in which the document is likely to serve as evidence. A judge of the Magistrates Court may, on the application of the Authority or a representative of the Attorney General, conditionally extend the six month period after allowing the owner of the document a reasonable opportunity to state his case.[433]

When suspicion arises concerning a possible violation of the statutes, a person authorized by the chairman of the Authority may apply to the Magistrates Court for a warrant that allows entry to any premises to conduct a search and to seize any relevant document. The Criminal Procedure Ordinance (Stop and Search) [New Version] 1969[434] provides the conditions for such a search. Similarly wide powers are granted for interrogation. An individual authorized by the chairman of the Authority may interrogate any person who, in his opinion, is connected to the matter and to order any individual to appear before him and turn over any detail or information related to the suspected offense.[435] The chairman of the Authority may apply to the Magistrates Court for a temporary or permanent injunction against the commission or the continued commission of certain acts, if the chairman has reasonable grounds to assume that a violation of the statutes or regulations thereunder is occurring or is about to occur.[436] Further, the Authority may, if necessary to protect the interests of the investing public, to appoint an independent party to investigate, audit, and demand the production of documents from a company to which the Law applies. However, the powers to appoint a third party investigator do not apply in cases where the investigated body is a stock exchange,

433. Securities Law, *supra* note 2, § 56A.

434. *Id.* § 56B(b).

435. *Id.* § 56C. For the purposes of the investigation, the authorized individual is granted the powers of a police officer of the rank of Inspector, as defined in § 2 of the Criminal Procedure Ordinance (Evidence) 1969, and the evidence collected by that individual is covered by the rules in § 3 of that Ordinance.

436. *Id.* § 56D. It is interesting again to note that the chairman himself, and not the Authority as a whole, may take certain action.

banking corporation, or insurer.[437]

Finally, in order to protect the confidentiality of the material or persons investigated under this chapter, the Law prohibits the revelation of any information or document that came into the possession of any individual pursuant to these provisions, other than in the pursuit of the investigation, or to the chairman, or to other authorized employees of the Authority. However, this prohibition obviously does not in any way prevent the disclosure of this information at the request of the Attorney General for the purposes of a criminal trial or on the demand of a court of law.[438]

The inclusion of these broad powers under Amendment 9 was an important step forward in the protection of those who invest in securities. The Authority, charged with the task of supervising most of the provisions of the securities law in Israel, now possesses the requisite investigative powers properly and actively to pursue this responsibility. The extent and nature of the powers granted to the Authority are modeled on the powers granted to the SEC in the United States. Experience in the U.S. convinced the Israeli lawmakers that the absence of such wide powers makes it very difficult to collect sufficient evidence to secure convictions in securities cases, which typically involve complex issues and, usually, intelligent and ably represented defendants.[439]

X. CONCLUSION

The rapid growth in securities markets in Israel since the mid-1980's has forced the Government and the courts to wrestle with increasingly complex issues. As shown throughout the course of this paper, the Government and courts have taken significant steps in the right direction. The positive effects of Amendments 9 and 11 and the increased willingness of the courts to delve into the complex questions raised in cases like *Boronovitch* and *Rubinstein* augur well for the future development of securities law and markets. There are areas, however, that have not yet been adequately addressed, such as proxy solicitations, which in the United States are heavily regulated under the U.S. Securities Exchange Act of 1934. Proxy regulation is not dealt with by the Yadin Report, presumably because of the view that this area of corporate governance is not strictly a part of securities laws. Nonetheless, proper disclosure in proxy solicitations would generally seem to be no less important than disclosure in prospectices or interim reports. Although beyond the immediate scope of this article, increased regulation of mutual fund activity, now covered by the outmoded Joint

437. *Id.* § 56F.

438. *Id.* § 56E.

439. It should be noted that similarly wide powers are granted to the Income Tax Authority in Israel, presumably for the same reasons mentioned above.

Investments Trust Law 1961, and regulation of investment advisers are sorely needed. Proposed legislation for both matters is now being considered by the Government.

The lawmakers and courts must boldly face the task of balancing the often conflicting interests of the involved parties, including the public, the investors, business, and the Government. An overly zealous approach to regulation could stifle the growth of Israeli companies and markets; on the other hand, allowing unfettered discretion to the involved parties would be a recipe for disaster, as illustrated at the outset by SEC Commissioner Emanuel Cohen. The experience of the Israeli public in the wake of the 1983 crisis involving the collapse in the prices of bank shares has taught both the Government and investors a bitter lesson in the dangers of insufficient control over these sensitive areas. The bad memories of that crisis lie behind much of the movement today in favor of greater investor protection and increased supervision of the markets and companies. The continued modernization of the securities law is essential to the proper maintenance of Israeli securities markets, which are rapidly attracting world-wide attention and investment.