



## Insight #5: Arrangements That May Apply to IP Rights of Israeli Companies

Israel is the “start-up nation”, with hundreds of new technology-oriented start-up companies founded each year. Many international purchasers of or investors in Israeli companies are accordingly interested in their intellectual property rights and in the possibility of transferring or utilizing these rights outside of Israel. When considering a strategic investment in, and even more so – an acquisition of, an Israeli high-tech company, limitations that might apply to its IP rights should be taken into consideration and carefully reviewed. The list below includes a typical, but certainly not exhaustive, list of such limitations.

**Innovation Authority Grants.** The Israeli Innovation Authority, formerly known as “The Office of the Chief Scientist”, provides grants to Israeli technology companies subject to certain conditions, one of which may be that the IP rights remain in Israel. These restrictions may be lifted through payment of certain amounts to the Innovation Authority, calculated based on the amount of the original grant.

- Note that the restrictions on transferring IP rights outside of Israel might be considered as breached if the company places its source code in escrow with a non-Israeli escrow agent, a condition sometimes required by significant customers. Make sure this matter is reviewed as part of your due diligence process.

**Tax Benefits.** Israeli companies may be eligible to significant tax benefits subject to certain conditions, including that the IP rights remain in Israel and that the manufacturing of products or licensing of IP rights originate in Israel. In such companies, removing the IP or the manufacturing from Israel might result in adverse tax consequences that should be considered.

**Encryption License.** Israeli law imposes restrictions on transfers outside of Israel of products that include encryption components, which may apply to standard encryption technology included in commercial products intended for civilian uses. Some companies will be required to receive an encryption license from the Israeli Ministry of Defense regulating the sale of their relevant products outside of Israel. While purchase of shares in and even control of an Israeli company that holds an encryption license may not require an approval by the Ministry of Defense, access to the technology might require a specific license.

- Note that this license may sometimes be obtained before the transaction documents are signed, as the Ministry of Defense requires a notice of the proposed sale and details of the purchaser but not an executed sale agreement.

**Academic and Other Institutions.** Many Israeli technologies originate in academic, health or security and defense related institutions. Many of these institutions hold companies devoted to commercializing the IP derived from their research and development activities and have specific rules governing these matters. In other cases, employees of academic and other institutions may be involved in commercial endeavors as founders, employees or advisors. If you are investing in or acquiring a company that has any relationships of this sort, make sure you understand the limitations that may apply to the company's IP rights or their commercialization.

**Rights of Employees, Advisors and Third Party Service Providers.** Founders, employees, advisors and third party service providers may all be involved in developing a company's IP. Make sure all relevant individuals have executed IP assignment forms assigning their rights to the company and have waived their rights to economic benefits derived from these IP rights. Note that employees must explicitly waive their right to receive compensation for a patent developed by them during their employment, otherwise their right to receive compensation will be determined by a committee established under law.

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