

ISRAELI CONTRACT LAW: AN OVERVIEW

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The aim of this overview is to supply a succinct account, organized according to familiar categories, of the major doctrines, interpretative approaches and trends developed and applied within the “hybrid” framework of Israeli commercial law. The account is designated to be informative rather than exhaustive, an accessible reference point for the beginning of research rather than its conclusion.

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1. Introduction

The purpose of this review is to render a clear and as comprehensive as possible account of Israeli commercial law (with an emphasis on the law of international sales and other international business transactions) within a narrow span, mostly pertaining to transactural rather than corporate or strictly financial contexts. It is written for jurists, lawyers and students who are unfamiliar with Israeli law yet are versed in law

otherwise, and thus basic and general jurisprudential concepts are assumed rather than explained. The study seeks to present law-in-action as seen through the lens of practitioners and courts, and surveys legislative innovations and practical concerns beyond black letter law. However, due to its scope, this review is perforce limited. It indicates the major doctrines, trends and concepts used in Israeli commercial law and relates them to some constitutional, administrative, tort, corporate and quasi-contractual fields of civil law, but does not pretend to supply in-depth analysis beyond positive exposition. At the most it explores some judicial and legislative trends when discussing specific topics, and draws analogies to comparative law when such are deemed helpful. However, every account of complex legal regimes that goes beyond the most rudimentary black letter law involves some level of interpretation, and this study is no different.

2. Source and Nature of Israeli Law

The Israeli legal system is frequently typified as a mixed or “hybrid” system: its basic structures and several jurisprudential concepts stemming from common law, it nevertheless bases many of its doctrines and jurisprudential notions, especially in the areas of contract law and remedies law, on continental civil law and German civil law in particular. Although the essential legal fields of contract, quasi-contract, remedies, sales, etc. are covered by legislation, courts have been very active in further developing both doctrine and jurisprudence. Broadly, one may typify Israeli commercial law as being originally based on English law (a heritage of the British Mandate over Palestine, 1922-1948). Over the years, most of the civil law has been replaced by original Israeli legislation, which is influenced mainly by continental and English law. The 1970 saw a boom of original legislation as well as very active judicial creation, influenced more by continental, and especially German civil law. Even where common law remained the inspiration, the comparative tendency shifted towards US rather than English law. Contract and commercial law has also been influenced by Israel’s constitutional transition from a parliamentary democracy to a constitutional democracy in 1992; among other things, freedom of contract and freedom of enterprise are since recognized as having constitutional status. It should furthermore be noted that religious law (Jewish, Muslim, Canon law etc.) has some formal standing in Israel, but that is generally limited to some areas of family law only and is irrelevant to the topics discussed in this study. This review will attempt to render a coherent synchronic account of current Israeli commercial law, with only cursory transgressions into legal history when such are deemed necessary.

Israeli commercial legislation is fairly comprehensive. Around the central piece of legislation in contract law – the Contracts (General Part) Law, 5733 – 1973 (henceforth “Contract Law”) – are arranged several statutes that regulate specific

contracts such as sales, international sales, agency, suretyship, pledges, contracts of adhesion, and so forth, as well as remedies for breach of contract and quasi-contractual interactions (e.g. unjust enrichment and commercial torts). A comprehensive Civil Code is in course of preparation, and when applicable this review will invoke relevant clauses from it; except in the area of excused non-performance (*force majeure*, see below), the proposed Code does not alter significantly the current prevailing law. It should be noted that during the last decade or so, several substantive areas of commercial law have been considerably reformed, overhauled and/or developed both by statute and by an activist judiciary. Such is the case in the areas of taxation, international sales, unjust enrichment, contract interpretation, remedies and corporate law, among others. Some of these modifications reflect changes in constitutional law that since 1992 tends to emphasize personal autonomy and the freedom of economic enterprise.

Israel is a party to various international commercial treaties, such as the UN Convention on Contracts for the International Sale of Goods (1980) (henceforth CISG), and the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958). Israel is also a party to bilateral treaties for the avoidance of double taxation with several countries,¹ and maintains several Free Trade Area agreements.²

3. Governing Law and Arbitration

3.1 Choice of Law

Israeli case law has drawn upon the choice of law principles of English common law. Apart from certain specific subjects (such as inheritance, marriage and divorce), choice of law is regulated by judicial precedent. According to the common law's approach, the parties may choose the law to govern their transaction as part of their

¹ To date, Israel is party to treaties for the prevention of double taxation with Austria, Belarus, Belgium, Brazil, Bulgaria, Canada, China, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, India, Ireland, Italy, Jamaica, Japan, Latvia, Lithuania, Luxembourg, Mexico, the Netherlands, Norway, Philippines, Poland, Romania, Russia, Singapore, Slovakia, South Africa, South Korea, Spain, Sweden, Switzerland, Thailand, Turkey, the United Kingdom, the United States of America, and Uzbekistan. Treaties with Ukraine, Luxemburg, Latvia and Ethiopia have been signed but not yet ratified, and additional treaties are under negotiation. Under most treaties, residents of a treaty country are exempt from the Capital Gains Tax on capital gains (other than on immovable property) in the other treaty country. Certain treaties contain tax-sparing provisions, the effect of which is to enable a foreign taxpayer who obtains a tax concession in Israel to receive a tax credit in her own country.

² Israel maintains FTAs with Bulgaria, Canada, Egypt, EFTA (Iceland, Liechtenstein, Norway, Switzerland), the EU, Jordan, Mercosur (Argentina, Brazil, Paraguay, Uruguay), Mexico, Romania, Turkey and the USA.

general freedom of contract. If the parties fail to do so expressly or impliedly, the law with the closest relations and links to the transaction will govern. Israeli courts will not apply law which is contrary to Israeli public policy, such as discriminatory law. If foreign law needs to be applied in an Israeli court, the relevant details must be proven as any other factual matter.

3.2 International Sales

In international sales transactions, the CISG will apply by default unless excluded or derogated from by the parties. Israel has broadened the default application of Art. 1 of the CISG so that the Convention would apply also to transactions between parties whose place of business is in a non-contracting state (i.e. a country that has not joined the CISG), thus Israel does not require reciprocity in CISG application. Courts will apply the CISG to all international sales transactions formed after February 5, 2000.³ For previous ones, the Uniform Law on the International Sale of Goods (ULIS) and the Uniform Law on the Formation of Contracts for the International Sale of Goods (ULF) – the 1964 Hague Conventions – will apply. Israel has made no declarations or reservations to the CISG pursuant to CISG Arts. 92-96.

With some exceptions, the CISG “sits” well with Israeli domestic law, and several of the basic doctrines embedded in the CISG are similar to their corresponding domestic ones. These include: lack of a general requirement of form, no requirement of consideration, the availability of specific performance, a *Nachfrist* rule for rescission for non-fundamental breach of contract, incorporation of customs, courses of conducts and in some respects standards of reasonableness, and others. The major exception is the general requirement of conduct in good faith that prevails over Israeli contract and civil law yet is absent from the CISG, except as an interpretative principle under CISG Art. 7 (for discussion see “Good Faith,” below).

3.3 Court Jurisdiction and Enforcement of Foreign Judgments

As a rule, an Israeli court has jurisdiction over any dispute between parties who are both in Israel or who agree to its jurisdiction. In addition, the court may, in its discretion, assume jurisdiction over a dispute between parties one of whom is outside Israel if service outside Israel is permissible under the Civil Procedure Regulations (Regulation 500). This would apply, inter alia, in the following cases: 1. When relief

³ Some publications mistakenly state 1 February 2003 as the operative date for the CISG in Israel. While that is the correct date for Israel becoming a “member state” of the CISG (see CISG Art. 99(2)), the Sales (International Sale of Goods) Law, 5760-1999 applies internally as stated above.

is sought against a person whose regular place of residence is in Israel; 2. The subject of the action is real estate in Israel; 3. The case concerns a contract signed in Israel or subject to the laws of Israel; 3. The action is in respect of an act or omission in Israel; 4. The person abroad is a necessary party, or the proper party in an action duly submitted against another person on whom a summons was duly served in Israel. The Israeli court will exercise its jurisdiction subject to the principles of *forum non conveniens* and *lis alibi pendens*.

An Israeli court will enforce a judgment awarded by a foreign court in a civil matter under conditions of reciprocity and comity, as long as the following are fulfilled: 1. The judgment is no longer appealable; 2. The obligation imposed by the judgment is enforceable and not contrary to public policy; 3. The judgment is executable in the country where it was awarded; 4. The judgment was awarded by a court which was competent to give it according to the laws of the country in which it was awarded; 5. The judgment was awarded in a country under the laws of which judgments of Israeli courts are enforced.

3.4 Choice of Forum

As part of the general freedom of contract and constrained by limited considerations of public policy, contracting parties may agree that a foreign court or non-judicial tribunal will have jurisdiction over all or some disputes. Special provisions restricting unilateral determination of forum or unduly unfair choice of forum apply to contracts of adhesion (standard contracts); for details see below.

3.5 Arbitration

Israel participates in the global trend towards expansion of alternative dispute resolution mechanisms in various areas of legal disputes. In commercial matters, the use of arbitration is steadily increasing. The Arbitration Law 5728–1968 requires agreements to arbitrate, or arbitration clauses, whether they involve institutional or ad-hoc arbitration, to be in writing. Arbitrators may be released by the parties from applying substantive or procedural law; of course, any such release is ineffective against immutable statutory requirements or matters of public policy. Special provisions restricting unilateral determination of arbitration resulting in unfairness towards a weaker party apply to contracts of adhesion (standard contracts); for details see below.

Arbitral awards are subject to very limited judicial review based on a closed list of defenses listed in the Arbitration Law. These regard mostly questions of the arbitrator's competence over the dispute and the arbitration's propriety; the award is

not subject to appeal on the merits. Local business make use both of ad-hoc and institutional arbitration offered by various trade organizations; the first kind is still quite prevalent. Contracts of an international nature frequently refer disputes to arbitration under the rules of the International Chamber of Commerce.

Foreign arbitral awards are enforceable in Israel according to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958 (a.k.a. the NY Convention), to which Israel is party. Relevant clauses of the Arbitration Law were amended to accommodate the application of the convention, including those pertaining to stay of proceedings, recognition and enforcement of a foreign award, etc. Israel has not made any reservations to the Convention under Art. I(3) (reciprocity and commercial nature of the relations under dispute). An Israeli court will stay a legal action where arbitration has commenced elsewhere, if the international convention applied to such arbitration. Motions to recognize or enforce an award, stay proceedings, or order arbitration according to the Convention are filed according to special Civil Procedure Regulations governing the Convention's administration.

4. Contract Principles

4.1 Freedom of Contract

Freedom of contract is one of the two basic principles of Israeli contract law (the other, the principle of good faith, is discussed below) and is recognized as a constitutional principle. Freedom of contract extends both to the freedom to enter into a contract (or refrain) and to the freedom to design the contract's form and substance. There are several important limitations to this general principle. These include invalidity on grounds of public policy, good faith duties, protection of weaker parties and specific requirements of form.

The latter three categories are dealt with separately below. As for the first, the Contract Law states that a contract, the making, contents or object of which is or are illegal, immoral or contrary to public policy is void. Despite the nullity of such a contract, the court may order either party to make restitution or, if unilateral performance (in whole or in part) already took place, order a party to perform its obligation in part or in full under the contract. The courts exercise this equitable discretion flexibly and contextually.

Courts are allowed -- and when possible, tend to -- sever the void element from the rest of the contract and uphold the non-objectionable portions (a "blue pencil rule"). Courts may take into account the legitimate interests of third parties who relied on the void contract in good faith and issue orders accordingly.

Alongside the general contract laws, there is extensive legislation in Israel concerning consumer protection and the protection of the weaker party. Some of these provisions are discussed below.

4.2 Good Faith

Good faith is a basic tenet of Israeli contract law and courts apply the duty to act in good faith extensively. Courts repeatedly relate to the good faith principle more as a guardian of the freedom of contract than as a substantive limitation on it. Good faith obligations apply in three contexts: 1. In contractual negotiations (whether a contract was eventually formed or not); 2. In performance, including in exercising a right arising from a contract; 3. The duty of conduct in good faith may be extended *mutatis mutandis* to legal acts or obligations in non-contractual contexts. Note, that the obligation to negotiate in good faith is a personal as well as vicarious duty and as such applies to all participants in the negotiations, including agents and representatives who may be liable though not parties to the contract itself. Parties may not derogate from their duty to act in good faith.

No statutory definition of the nature and scope of good faith exists, and courts develop those casuistically; however, good faith is generally accepted as an objective matter regarding course of conduct rather than just a matter of fraudulent intent. Paradigmatic examples are: misleading or failing to disclose required information, retiring from advanced negotiations without justifiable cause, negotiating with no intention to enter into a contract, raising new demands at advanced stages, insistence on strict performance of the contract where the cost to the debtor far outweighs any benefit to the creditor, etc. In a contract that requires form (such as real estate transactions that require a document in writing, see below), the contract is enforceable, and the debtor is estopped from claiming lack of form, if the creditor has substantially performed and performance has been accepted by the debtor. A party that illegitimately retires from negotiations or effectively frustrates acceptance (*culpa in contrahendo*) risks that the court deny the defense of non-formation and treat the contract as formed. Since its legislative introduction in 1973, Israeli courts have made extensive use of the duty of good faith by way of application and interpretation. Albeit its wide array of applications, the requirement itself imposes only a minimal standard of performance. Thus, e.g., in private tenders, unless otherwise expressed or implied, the party inviting offers is not required to treat all offerors equally.

As regarding remedies for breach of good faith duties in negotiations: initially, the relief available to a party injured by conduct which was not in good faith was limited to compensation for the damage caused by the faulty negotiations (a.k.a. “reliance” damages). This rule, based on language in the Contract Law, was significantly

amended by the courts, to the effect that currently all the remedies available for breach of contract are available, *mutatis mutandis* and under fitting circumstances, for breach of good faith duties either in negotiations or in performance. Thus courts award relief equivalent to expectation damages or specific performance in cases of *culpa in contrahendo*. That said, declaring the contract avoided on grounds of fundamental breach of good faith obligations alone (i.e. when no other cause, such as mistake or undue influence can be sustained) is a rarity, yet in principle available as well.

The duty to act in good faith applies, naturally, also to performance. The main dispute here is whether the duty is broad enough to impose on parties extra-contractual performances, or merely perform the contractual performances in good faith. Here, too, courts have mostly taken the broader view and required parties to act in ways that, while not expressed in the contract, were deemed necessary in order to allow or facilitate performance in good faith of their contractual obligation. However, courts in such cases are weary from intervening in the contractual allocation of risks between the parties and thus proceed cautiously and on a case by case basis.

An interesting question regards the status of good faith duties in cases governed by the CISG. The CISG contains no general provision requiring parties to act in good faith, other than in interpreting the treaty itself, c.f. CISG Art. 7(1). As no direct cases have been decided on this question, one need resort to indirect ones and to analogies. If the CISG governs the case as part of Israeli law (i.e., directly or through a choice of law clause), it is the opinion of the authors that Israeli courts would then apply the general duty to negotiate and deal in good faith; the CISG, as part of Israeli law, would be applied as *lex specialis* that does not derogate from the immutable good faith requirement of domestic general contract law. The answer may be different if the CISG is applied as the governing law through a choice of law determination of a legal system that does not impose such extensive good faith duties. E.g., the CISG may become the governing law in an Israeli court if the effective choice of law is US law and no derogation from the application of the CISG was made by the parties (CISG Art. 6). As US sales law does not contain a general requirement of behavior in good faith in negotiations, and nor does the CISG, an Israeli court may refrain from such imposition, in contrast to its own immutable jurisprudence.

4.3 Contract Formation

Contract formation is governed by the Contract (General Part) Law as well as by some peripheral statutes and a wealth of precedent. While the Contract Law invokes the familiar model of formation through offer and acceptance, Israeli courts—as well

as authoritative scholarship—have applied a liberal, in some senses relational approach to contract formation, focusing of the parties’ mutual intent to enter into a bonding relationship as manifested by their language and/or conduct, rather than insisting on discrete acts discernable as “offer” or “acceptance”. Thus a contract under Israeli law typically entails the fulfillment of four basic elements, broadly construed: offer, acceptance, definiteness and the intention to create a legal relationship. There are no general formal requirements for contract formation (such as a document in writing), although such are required in specific areas and agreements (see below). Likewise, Israeli law requires no consideration for the completion of a contract, nor must *causa* be evident, although a separate statute—the Gift Law—applies to the gratuitous transfer of goods, money, rights etc.

4.3.1 Offer

A person’s proposal to another constitutes an offer if it attests to the offeror’s intention to enter into a contract with the offeree and is sufficiently definite to enable the contract to be concluded by acceptance of the offer. The offeror’s intention to enter into contract is adduced from the objective communicative facts: statements (contextually interpreted), conduct, etc. Under Israeli contract law, language does not enjoy, as a general rule, a precedence over conduct: inasmuch as both may be communicative, both may bind the relevant agent according to the reliance-sensitive principle of reasonable interpretation of her language or conduct. This principle would apply generally in contract formation, i.e. to acceptance as well.

An offer may be made to the public. Tenders, although addressing the public, are normally classified as an invitation to make offers rather than as offers; in any event, this is a question of interpretation and must be circumstantially determined. Prudent offerors make this matter clear in the language of the tender.

An offer expires when rejected by the offeree, when a reasonable time has elapsed since its tender, or when the offeror or offeree passes away or becomes incompetent (in the case of corporations, once a corporation enters receivership or liquidation). Firm offers -- offers that set a time for acceptance and/or indicate their time of expiration -- may not be withdrawn and the offeree may accept or reject them until that time, whereupon they automatically expire.

4.3.2 Acceptance

Acceptance is tendered either by notice delivered by the offeree to the offeror or by conduct, as long as it attests to the offeree’s intention to form a legal contractual

relationship (such as sending money or goods, or else beginning performance), or otherwise indicating the offeree's assent. The offeror may restrict the methods of acceptance available to the offeree. A stipulation by an offeror to the effect that the absence of any response on the part of the offeree would count as acceptance is generally invalid, unless the parties made a prior agreement to the contrary; an exception to this rule is a purely beneficial offer, where the contract in question would require no performance from the offeree and puts her to no disadvantage, cost or inconvenience.

Israeli law does not apply a "mailbox rule" for acceptance and thus acceptance is binding once it reaches the offeror or her place of business. However, once a notice of acceptance has been discharged, even before it reached the offeror, a revocation of the offer by the offeror is no longer effective. Except in international sales (where the CISG applies), Israeli law applies a "mirror image rule" to offer and acceptance, whereby a purported acceptance that alters in any way the terms of the offer is considered a counter-offer (compare with the more flexible rule of CISG Art. 19(2)). No distinction is made on this issue between merchants and non-merchants, as made in UCC §2-207. However, this doctrine, like all others, is subject to the principle of good faith (as well as normal course of conduct) and thus trivial alterations would not invalidate the acceptance or give rise to a counter-offer.

4.3.3 Definiteness

An offer should be sufficiently definite to enable acceptance. While this requirement applies to all the essential components of the offer, courts would normally not consider an offer to have failed for lack of definiteness were it may be supplemented and completed by internal or external mechanisms. These include an array of supplemental default rules, the legal recognition of external sources such as custom and *lex mercatoria*. Courts normally tend to uphold offers rather than ascribe to them failure for lack of definiteness as long as the matter of mutual assent has been settled. Sources for supplementing a wanting offer may be: (1) the offer itself and the presumed intention of the parties; (2) the circumstances in which the offer was made; (3) existing practices between the parties or, in the absence of such practices, practices customary in contracts of that kind; and (4) statutory supplementation, namely the importation of default provisions into the deficient offer. Two main sources for such provisions are the Sales Law 5728 – 1968 and the Contract (General Part) Law 1973. Such supplementary details may include matters of place for performance (default: creditor's place of business, but in sales—the seller's); time (default: reasonable time after the contract was made or came into effect), quality

(default: average), terms of payment, price (market price where such can be determined), conformity, documents of title, etc.

4.3.4 Intention

Mutual assent is really the essence of contract. Israeli law follows the so-called “objective” model of contract formation whereby intent is inferred from conduct as well as entailed by appropriate language. The main point is not whether a certain party had or did not have a subjective intention to contract, but whether by her language and conduct communicated such an intention to a reasonable party under the circumstances. Courts follow a pragmatic approach and would in fact scrutinize the communicative interactions between the parties—verbal, conduct, etc.—in cases of disputes regarding intention to contract.

Memoranda, letters of intent, agreements to contract and other interim documents frequently pose the problem of intention—has it matured, or whether the parties merely used those to facilitate future negotiations and “freeze” preliminary stages of agreement. The courts have departed from the English approach and not given decisive weight to using the format of a preliminary agreement in order to negate its binding force. The present approach is pragmatic, whereby the court will seek to infer the parties’ intention from both language and conduct—before, during, and after the preliminary agreement. The performance of obligations pursuant to a memorandum of agreement is strong evidence of intention to enter into the contract.

It should be emphasized that even where there is a document which is clearly not binding, like a duly drafted comfort letter or letter of intent, the party giving it still labors under good faith duties (liability for breach of good faith obligations is indifferent to the question whether a contract was eventually formed or not; see above).

4.3.5 Form

No general requirement of form, such as writing, seal or registration exists in Israeli contract law. However, specific regulation requires that some contracts be in a certain form, and in particular a written document. The most important of these are an undertaking to make a transaction in land; arbitration agreements; consumer banking agreements; and an undertaking to make a gratuitous transfer (gift). The requirement of writing in these cases is substantive and is a material condition for the making of a binding contract. In some cases, substantive performance was allowed to compensate for lack of writing.

A written document may be required as evidence of common contracts, as well as when contesting another written document in court. This requirement is not substantive but merely evidential and the courts apply it pragmatically. Electronic transmissions may generally satisfy the evidentiary requirement, although both courts and the legislature still require a “tangible form” for the fulfillment of the requirement (such as a computer printout or retrievable, stored digital data). For the time being, electronic documents do not fulfill the substantive requirement. This is expected to change.

4.4 Interpretation of Contract

Israeli courts apply a model of “purposive interpretation” to all legal interactions and texts. The role of contract interpretation is to reconstruct the agreement in light of the manifested common purpose of the parties at the time of formation. Thus, Israeli courts do not apply the parol evidence rule, and allow interpretative evidence regarding context, circumstances, and parties’ behavior before, during, and sometimes even after formation. Nor do courts, in general, use other exclusionary devices that may frustrate true understanding of the agreement between the parties. Courts may resort to the “rational of the deal” as an interpretative yardstick. Customs, courses of conduct, prior agreements and *lex mercatoria* may be brought in evidence of the parties’ purported agreement and sometimes form interpretative presumptions. Good faith is applied as an interpretative principle as well; thus when reconstructing the parties’ purposes, a party may not benefit from having failed to disclose information that under the good faith requirement it should have disclosed.

Israeli law enforces third party beneficiary contracts. Whether a contract empowers a third party to enforce an obligation or not is determined by analysis according to the standard rules of contract interpretation.

(On the interpretation of contracts of adhesion see below).

4.5 Estoppel and Reliance

The doctrine of estoppel has been absorbed into Israeli law, originally in its English form, and the courts have shown great readiness to apply it. It is nowadays seen both as a corollary of good faith requirement as well as an independent source of obligation. Israeli law tends to blur the traditional demarcation between promissory estoppel (where the claim is based on a promise, and is the crux of the field of quasi-contract) and equitable estoppel or “reliance” (where the claim is based on a representation, and is in the domain of torts). According to the latter, when a party

makes a representation and the other reasonably relies on it, altering her position to her detriment, the first party is estopped from denying this representation; according to the former, the promissory is estopped from reneging on the promise.

Since the enactment of the Contracts (General Part) Law in 1973, the courts have begun to rely more on the duty of good faith in order to achieve similar results, and the two doctrines presently coexist. While estoppel was traditionally seen as a defense rather than a form of action, a “shield” rather than “sword”, this is not the case under contemporary Israeli law, especially when the doctrine is combined with that of good faith in negotiation or with negligence. For example, when an insurance company made a representation to the policy holder that the policy covered him, although according to the language of the policy it did not, the company was made liable to act as though the policy did provide cover.

4.6 Delay, Justifiable Postponement and Force Majeure

The time for the performance of contractual obligations does not enjoy special standing as a cause for rescission of the contract or for other relief; whether delay is considered a fundamental breach or not is given to the parties’ antecedent agreement and, barring that, to analysis by the court. Nor does delay in delivery enjoy a special *Nachfrist* protection in comparison with other performances (see below, rescission of contract; compare CISG Art. 49(1)(b) as well as the Principles of European Contract Law (2003) Arts. 9:301(2) and 8:106(3)). If the parties do not fix a time for tender, it should be made in reasonable time after the making of the contract. A seller should give the buyer reasonable advance notice of the date of delivery. Generally, an obligation may be fulfilled prior to the due date, provided that the debtor gives the creditor reasonable notice in advance and the creditor is not adversely affected.

Israeli law allows a debtor to postpone the performance of a contractual obligation in one of the following circumstances:

(1) If its fulfillment on the due date is prevented by a circumstance depending on the creditor – until the obstacle has been removed.

(2) If its fulfillment is conditional upon the prior fulfillment of an obligation by the creditor – until such obligation has been fulfilled.

(3) If the parties must fulfill their obligations *pari passu* – as long as the creditor is unable or unwilling to fulfill the correlative obligation.

Postponement of performance under (3) is especially important as it may occur in conditions of anticipatory breach and thus serve as a preventive measure whereby the postponing party avoids further risk of loss without committing breach or driven to rescind the contract. As a preventive measure two conditions must be met: 1. The

creditor has reasonable grounds to suspect that debtor is about to default, and 2. The respective performances are deemed “mutual” rather than merely reciprocal and thus independent of each other. This determination is a matter of interpretation, and several helpful presumptions and auxiliary rules exist. Thus, in a sales contract, the seller’s obligation to deliver the goods and the buyer’s obligation to pay are considered *pari passu* or mutual; in contrast, a landlord’s obligation to keep a property in good repair is independent of the tenant’s obligation to pay the lease. In addition, the principle of good faith may act as an interpretative guideline in determining whether performances are independent of each other or not.

4.7 Force Majeure

The crux of the current Israeli doctrine of frustration is a combination of material impossibility (alternately, the actual performance would be fundamentally different than the contractual performance), unforeseeability of the frustrating event and its unavailability. Only when all apply, is a non-performance excused on grounds of frustration.

The doctrine has been narrowly applied and defenses of frustration are seldom successful in Israeli courts. A main restriction—in addition to material impossibility—is foreseeability: Israeli courts are very reluctant to allow that frustrating events are unforeseeable; in the past, substantial increases in market prices due to geopolitical outbursts such as the 1973 war were not deemed unforeseeable.

This, however, is about to change. As noted above, Israeli civil law is in the process of codification. The single most important reform in the area of contract law is in the doctrine of frustration. The new code will scrap the present doctrine based on foreseeability and impossibility in favor of a more flexible doctrine that focuses on impracticability and the objective occurrence of a frustrating event. The question then will be, which party assumed or was allocated—contractually or by default—the risk for the occurrence of the frustrating event. If the risk was distributed between the parties, so must their liabilities be. In addition, frustration may be deemed temporary, resulting in *suspension* of performance. The legal effect of suspension would be a permissible delay in performance rather than wholesale excused non-performance.

Under both doctrines, if frustration (or suspension) is indeed acknowledged, the court has the power to award an order of restitution, in whole or in part, of value exchanged prior to the occurrence of the frustrating event.

4.8 Warranties

This section will not discuss warranties under the CISG, which by default governs international sales under Israeli law (see above). However, the statute governing

domestic sales—The Sales Law 5728 – 1968, like the CISG, does not apply a UCC-like “perfect tender” rule nor an opportunity to reject the goods for non-conformity (other than by rescission of the contract, see below).

The Sales Law provides that the seller has not fulfilled her obligation if she has delivered goods (or other property) that differ from the contractual agreement in one or more of these respects: 1. quantity (including surplus); 2. kind; 3. quality or characteristics allowing for commercial usage or a specific usage if such is entailed by the contract; 4. non-conformity with a previously agreed sample; 5. other non-conformities in respect to the agreement.

All claims pertaining to non-conformity must be made in good faith. The buyer’s right to rely on non-conformity as cause to claim contractual remedies is conditional upon a double burden: 1. The buyer must inspect the goods immediately after receipt (and where carriage of the goods has been agreed upon – immediately after their arrival at the designated destination); and 2. The buyer must give the seller notice of any non-conformity immediately after the time of the inspection or immediately after discovering the non-conformity, whichever comes first. If the non-conformity was latent, i.e., could not have been discovered upon reasonable inspection, the time for giving notice is postponed and the buyer must give notice immediately upon discovering it. Finality, however, requires that there be a limit to how long this postponement period may run: two years as to the buyer’s right to rescind the contract for latent non-conformity, and four years for any and all other remedies for breach of contract due to non-conformity. The finality clause does not apply if the latent non-conformity was known (or should have been known) to the seller at the time of finalizing the contract, and she did not disclose this to the buyer (this situation is akin, in essence, to fraud).

It should be noted that the relatively high burden imposed on the buyer as regards inspection is lifted in the Civil Code draft (see above), and other provisions regarding conformity are changed as well (*inter alia*, a buyer who knew of the non-conformity at the time of the finalizing if the contract is estopped from making any claims thereof).

5. Remedies for Breach of Contract

Remedies for breach of contractual obligation are enumerated in the Contract (Remedies for Breach of Contract) Law, 1970. Courts have powers to award remedies beyond the Remedies Law provisions (generally seen as default rather than immutable provisions, with few notable exceptions) when such are necessary.

The main remedies for breach of contract available to the aggrieved party are specific performance, rescission (avoidance, termination) of the contract, and damages. All

remedies are available *mutatis mutandis* in cases of anticipatory repudiation, as long as an order for specific performance does not compel performance before the contractual stipulation (market-based damages are another exception).

A brief description of each category of remedies, as well as the conditions for combining them, follows.

5.1 Specific Performance

Specific Performance (often simply called “enforcement” in Israeli legal vernacular) is a matter of the aggrieved party’s right in Israeli contract law rather than a prerogative remedy given to the court’s discretion. Thus an aggrieved party may expect an order of specific performance as a matter of course. Courts therefore do not apply the doctrine of efficient breach—according to which a defaulting party may avoid performance by paying expectation damages (see below section 6, “Unlawful Enrichment”)—although this may be allowed in special categories of cases, as following.

There are four classes of exceptions in which the court has discretionary powers *not* to grant specific performance: 1. When the performance has become impossible; 2. Performance would entail compelling a tender or acceptance of personal work or a personal service; 3. Performance would require an excessive level of supervision by the court; 4. Enforcing performance would be unjust under the circumstances. The last exception is limited to considerations relating to the relations between the parties themselves (i.e. not to third parties or to general public policy) and the exception is exercised sparingly. The court, however, may make an order for specific performance conditional upon some reciprocal performance.

5.2 Damages

An aggrieved party may choose to substitute consequential damages for specific performance. These would normally amount to expectation damages, namely a compensation for the harm, including loss of profits or other benefits, caused to the aggrieved party by the breach and its effects, as long as those were foreseeable at the time of the contract’s formation as a probable consequence of the breach. The plaintiff must prove all the components of the claim, including causation and definiteness, just as she would in any monetary lawsuit. However, if the foreseeable expectation is impossible to prove, courts have occasionally allowed the plaintiff to recover reliance expenses instead.

A claim for damages is subject to the defense of mitigation of harm, which the aggrieved party must undertake in terms of reasonable measures.

Israeli courts are gradually developing and applying an approach of contributory fault to breach of contract, borrowed from the torts doctrine of contributory (or relative) negligence. This may apply to both the breach itself and to the subsequent accrual of compensable harm or loss, resulting in a defense, partial or complete, against a claim for damages (thus courts have occasionally divided the loss resulting from breach between parties according to an assessment of their respective relative contribution to the occurrence of the breach).

Alternately, an aggrieved party may sue for price or market-based damages. In such cases, proving causation and foreseeability is redundant: the plaintiff must prove breach and the relevant price or market fluctuation. Market-based damages are not subject to the duty to mitigate damages.

An aggrieved party may collect damages for non-pecuniary harm. This remedy cannot be used as a substitute for expectation damages when such a suit would fail for evidentiary or other reasons (e.g., definiteness of amount); courts use it sparingly to compensate, mostly, for emotional distress caused by the breach.

Damages may be combined with other remedies (e.g. specific performance or rescission of the contract) providing there is no over-compensation. E.g., an order of specific performance may result in late performance, and the ensuing delay may be compensated by appropriate damages.

An award for damages will not be reduced due to insurance payments collected by the aggrieved party for loss due to the breach.

5.3 Termination of the Contract

The aggrieved party may choose to forgo specific performance and rescind the contract ("terminate", "declare the contract avoided", etc.) with or without suing for damages. Rescission is a self-help remedy, performed by notice to the defaulting party in reasonable time after the breach has been known to occur (or, in anticipatory breach, at such time as allowed before the actual breach) and no court order is necessary.

A contract may be rescinded in two cases: 1. In the case of material breach; 2. In the case of non-material breach, as long as a reasonably long curative period has been set by the aggrieved party, and the party in breach failed to perform during that period. In this manner a non-material breach is "upgraded" to the status of material breach (this *Nachfrist* mechanism is akin, if not quite identical, to the one in German, Swiss, and Austrian law; compare with the more limited power to rescind in the CISG Art. 49(1)(b), limited to cases of non-delivery.) When a material breach is involved no grace period prior to the rescission is necessary.

The party in breach has no general right to cure the breach after the time for performance has past, although an aggrieved party's refusal to accept curative performance may amount to breach of the good faith obligations that the parties are continuously bound by, even at the post-rescission stage.

Effects of rescission: 1. Severability: parties are excused from all further contractual performances, except those set to apply under conditions of breach, such as an arbitration or other dispute resolution clause, or liquidated damages. 2. Restitution: once a contract has been rescinded, parties are required to mutually return all goods or substitute value exchanged between them as part of the contract.

5.4 Penal Provisions and Liquidated Damages

Israeli courts have no power to award punitive damages, nor nominal compensation for non-proven loss. The yardstick for compensation is either actual consequential damages or the equivalent market-based damages (see above).

However, courts would normally enforce clauses stipulating contractual damages agreed upon by parties ("liquidated damages") in lieu of the other available categories of damages. In principle, awarding liquidated damages requires no proof of loss. However, courts have the power to reduce liquidated damages if they find that those were fixed with unreasonable proportion to the consequential damage as foreseeable at the time of formation of the contract. The point of intervention and the amount of reduction depend upon the circumstances of the case and are by no means standard. Courts would balance the freedom of contract and the allocation of risks undertaken by the parties, as expressed by the liquidated damages clause, with the basic bias against punitive damages, generally seen as an abuse of the freedom of contract.

Barring agreement to the contrary, an aggrieved party may choose between exercising the liquidated damages clause or resorting to other remedies.

5.5 Special Remedies: Sale of Goods

Domestic sale of goods transactions are governed by the Sale Law that makes available to the aggrieved buyer, in addition to the general remedies for breach of contract, another remedial or quasi-remedial measure. This, applicable in cases of non-conformity, is unilateral price reduction, conditional upon the seller's failure to cure the breach after a reasonable period has elapsed since the buyer has provided a notice to the effect of non-conformity. Price reduction is performed pro-rata in relation to the contractual performance. A buyer choosing to reduce the price will thereby waive both a claim for specific performance and her right to rescind the

contract, if such exists (the logic of this provision is that the buyer may, if she so chooses, treat the seller's breach as an offer for partial revision of the contract, as long as pro-rata price is governed by the "original" contract). However, the buyer does not by reducing the price forfeit the right to damages for any loss generated by the breach. Price reduction is available whether the buyer has already made payment or not, and extra payment may be claimed in restitution or, with some restrictions, be subject to set-off (see below).

6. Unjust Enrichment, Quasi-Contract, and other Remedies for Breach of Contract

In Israeli law, the contractual obligation is protected not only by the contract but also by related fields of law, particularly tort law and the law of unjust enrichment.

6.1 Unjust Enrichment

Unjust enrichment (a.k.a restitution) is an especially powerful construct in Israeli civil law. The basic rule requires any person (including the state) to make good on gains that she has illegitimately made at another's expense. Albeit some statutory language to the contrary, the Supreme Court has time and again asserted that the law of unjust enrichment applies also to contractual relations. Thus, in cases of so-called "efficient" breach—where value generated by breach is higher than that generated by performance, and thus payment of expectation damages would still keep the defaulting party in profit—unjust enrichment would allocate to the aggrieved party restitution of all revenues generated by the breach (in one seminal case, plaintiff was awarded on an unjust enrichment claim as much as six times the purported expectation damages). Thus Israeli contract law does not abide by the efficient breach model. In addition, an unjust enrichment claim may apply where a claim for breach of intellectual property rights would fail on technical grounds and possibly on substantive ones as well (e.g., for lack of some constitutive requirement such as registration, which does not effect unjust enrichment). It may likewise retain a property owner's rights in goods or entitlements which were obtained or tendered illegitimately, unless the further transfer or negotiation was made in good faith, for value, and in due course of business, thus overcoming the property defense.

Claims of unjust enrichment are subject to equitable defenses, primarily that the plaintiff has suffered no loss due to the defendant's enrichment or that other circumstances justify withholding restitution, in whole or in part.

Several unjust enrichment principles are embodied into the Commercial Torts Law, 5759-1999; see below.

6.2 Tort Law

The general protection of the contractual obligation in tort law is the tort of instigating a breach of contract, whereby any person who knowingly and without sufficient justification causes another to break a legally binding contract with a third party is liable to compensate the aggrieved party. Apart from that protection, whose roots are in English common law, general tort law serves to make good economic damage primarily through the doctrine of negligence. Israeli courts award compensation for economic loss on the ground of negligence. This is most apparent in claims for negligent misrepresentation, in precontractual negotiations as well as in other contexts involving reliance. The typical remedy in such events is compensation for the foreseeable consequential loss caused to the plaintiff by reasonable reliance on the negligent misrepresentation. To some extent, this overlaps with the cause of lack of good faith in negotiations, although negligence need not amount to a lack of good faith and vice versa.

6.3 Commercial Torts

The Commercial Torts Law, 5759-1999, is a relatively new, innovative legislation combining the elements of unjust enrichment and unfair competition in a tort framework. The Law lists a number of objectionable business practices such as intervention with a competitor's affairs, misleading customers, assuming false identity etc., making those actionable torts and allowing the plaintiff to collect statutory damages without proof of actual loss. Likewise, the Law restricts the improper acquiring or misappropriation of trade secrets—any information conveying commercial advantage that is not in the public domain—by competitors who have gained access to them illegitimately (such as by commercial espionage, breach of trust relations, etc.), even when those are not protected by intellectual property law. However, skills gained by an employee or other person in the course of employment, even when a trade secret of the employer, are no longer protected once they become incorporated into the employee's general set of skills and professional know-how.

The use of reverse engineering, in and by itself, is excluded from the scope of the statute and thus not actionable, as long as it does not involve other actions, covered by the statute. Good faith and public policy are defenses in some instances. Typical remedies are damages (with or without proof of damage), injunction, and restitution, including all or part of gains generated by the tort. A receiver, wielding wide powers including entry, searches and seizures of evidence may be appointed by the court to verify tortious behavior as long as a *prima facie* case has been proven; the court would

usually require the plaintiff in such cases to deposit a sum in security in order to compensate the defendant for any loss incurred by bogus complaints. Application of the statute does not exclude unjust enrichment causes nor defenses.

6.4 Product Liability

The sphere of product liability is regulated by the Defective Products (Liability) Law, 5740-1980. The statute provides that a manufacturer is strictly liable to a person who suffered personal injury as a result of a defect in the product manufactured. If the damage is caused by a defective component, both the manufacturer of the product and the manufacturer of the component are liable. Liability is strict, and whether the manufacturer was at fault or not is immaterial. The statute provides manufacturers with a closed list of defenses, e.g. that the defect in the product arose in circumstances over which the manufacturer had no control or that the injured party voluntarily exposed himself to the risk. A manufacturer may not contractually exclude liability under the statute.

The Law also specifies certain mitigating provisions pertaining to liability: 1. There is a ceiling to the compensation recoverable under the law; 2. There is an abbreviated prescription period of three years, and, in any event, an action may only be brought within ten years from the end of the year in which the product left the manufacturer's control; 3. The statute does not apply to property damage, livestock or unprocessed agricultural produce. The Law does not apply to harm caused outside Israel, which, like other matters not covered by the statute, is subject to general tort law and the principle of negligence.

7. Unlawful Limitation of Liability and Protection of the Weak Party

The Contracts (General Part) Law recognizes two causes for rescission of contract by the party who held an inferior bargaining position in the negotiations. One is *duress*, whereby a person who has entered into a contract as a result of duress applied to him by the other party or by a person acting on her behalf may rescind the contract. Courts have applied the doctrine to purely economic duress as well, if the party claiming duress can show it was placed by the other party in a position where no available and practical alternatives to consenting to the contract existed. In one leading case, a large diamond merchant who defaulted and fled abroad offered his creditors meager settlements under threat that no other means of recovery would be available to them; the court accepted the claim that this was premeditated conduct and as such constituted a breach of good faith duties as well as duress. While some see the

defense of duress as a limitation on the freedom of contract, courts stress that the role of the doctrine in defending genuine assent.

Israeli courts do not have a general power to police unconscionable contracts (except contracts of adhesion, see below). However, the Contract Law did adopt the equitable relief of Undue Influence to allow a party to rescind an unconscionable contract under two conditions: 1. Abuse, namely that the contract was achieved through undue influence owing to the rescinding party's physical or mental distress or inexperience; 2. That the terms of the contract are unreasonably unfavorable. Courts have ruled that the weakened condition—which obviously need not be so extreme as to amount to legal incompetence—does not, as a rule, cover momentary or transitory weakness. However, unlike in traditional equity, the doctrine is not limited to abuse of trust or confidence relations between the parties. The provision is thus intended to supply relief to persons who are either systematically weak bargaining parties or at least subject to serious incapacitating circumstances, of which the other party takes advantage. In relation to duress, undue influence is a fairly narrow category and it is very unusual to see it applied in ordinary commercial contexts.

An obvious source for attacking liability limitation or exclusion clauses is public policy. As noted above, a contract or a clause that is contrary to public policy is invalid. Israeli courts have used the doctrine, among other things, to invalidate contractual clauses that prevented access to courts altogether. In one case, it was held that an exemption clause by a marine carrier releasing it from liability for personal injuries is contrary to public policy and thus void.

7.1 Contracts of Adhesion (Standard contracts)

Alongside general contract law, Israeli law contains innovative legislation pertaining to contracts of adhesion or “standard contracts” as well as other forms of consumer protection legislation.

The Standard Contracts Law, 5743-1982 applies to any contract the terms of which are laid down by one party in order to be used in standard contracting with numerous, non-specified parties. The Law is not restricted to consumer transactions, but would apply in most such contexts. The dominant party is termed the “supplier”, the other party the “customer”; these definitions apply whether the supplier delivers or receives goods or services and are indifferent to the question which party was offeror and which was offeree. The statute's purpose is to protect customers from unfair or unconscionable provisions that give suppliers undue advantages in standard contracts over whose drafting the customer had no influence. The statute enumerates a long,

and yet open list of presumptions of unfairness. These include waiver or extreme limitation of liability; unilateral powers to significantly alter, determine performance, or cancel the contract; limitation on the customer's freedom of contract or right to compete; stringent limitations on making lawful claims in courts or other tribunals (except for arbitration and ADR agreements, as long as the supplier does not have undue influence on the place and determination of the arbitration); unreasonable or unilateral choice of forum; etc. These presumptions are not irrefutable, but the onus shifts to the supplier to prove that the clause in question is not unduly unfair. In addition, a provision in a standard contract prohibiting or significantly restricting the customer's right to take legal action in courts is irrefutably void.

Courts have broad powers to uphold, strike out, or amend unfair clauses in standard contracts ("blue pencil rule"). The amendment may be performed only to lift the undue disadvantage or its effects, and may not otherwise intervene in the allocation of risks between the parties. The petition to do so may arise in the course of usual litigation.

While contesting unfair clauses may be done in any court civil as part of usual contract litigation, the statute has also set up a special tribunal, the Court for Standard contracts (sitting within the framework of the Tel Aviv District Court). This Court doubles as a judicial body and an administrative one. It may uphold, strike out, or amend unfair clauses in standard contracts *ex ante* and *in rem*, outside the context of a particular litigation. Petitions to the Court may come from various sources, depending on the remedy sought. Suppliers, wishing to avoid the risk of having clauses later stricken out or amended, may approach the Court in order to uphold *ex-ante* a certain clause. This would amount to a license to use the clause in standard contracts; the license's terms is five years (the respondent will be the Attorney General and any other party approved by the court, such as a consumer organization). Contrariwise, consumer organizations, the Attorney General or other governmental bodies may appeal to the Court in order to invalidate a certain clause *in rem*; the respondent would then be any relevant supplier or a representative organization of suppliers.

On top of the Standard Contract Law, The Consumer Protection Law 5741–1981, the Sales (Apartments) Law 5733-1973, charge card laws and other statutes as well as corollary regulations provide extensive consumer protection. While consumers are defined as persons who buy goods or commodities or receive a service for personal, domestic or family use, some protections (e.g. relating to misuse of credit or debit cards) may apply also in commercial contexts.

In consumer contexts, The Law prohibits a dealer (who sells a commodity or performs a service by way of business) to mislead a consumer in any material matter expressly or impliedly. The Law enumerates matters defined as material, but the list

is not exclusive. The dealer must also disclose to the consumer any defect or special feature or material particular with regard to the commodity or good, and must not take advantage of the consumer's weakness, distress, ignorance, etc., in order to achieve abnormal or unreasonably favorable terms. Contravention of the Law constitutes a tort, actionable not only by the injured consumer but also by consumer organizations.

While there is a certain overlap between consumer protection law and general contract law, the former is a specialized and highly developed area of law that goes beyond civil law to administrative enforcement and criminal sanctions; these cannot be dealt with in this study

8. Prescription Law

Prescription in Israel is a procedural barrier to litigation (as well as to arbitration) and does not effect the substantive entitlement itself. The default period of prescription in civil matters (except for land) is seven years. The period in land is twenty five years, except for the relatively small category of non-registered land, in which case it is fifteen years. Executory judgments left unenforced are also subject to a twenty-five year prescription period. In civil matters, the period of prescription begins on the day on which the cause of action accrued, except where the cause of action is fraud, in which case the period begins on the day on which the plaintiff learned of it. When the plaintiff does not know and could not by reasonable means know of the cause, the prescription period begins on the day on which the facts constituting the cause of action become known.

The prescription period may be reduced or extended contractually, although extremely shortened periods in contracts of adhesion (see above) may be suspect as creating an undue advantage and thus subject to change or cancellation by the court (prescription cannot be shortened for real estate transactions). By statute, the minimal permissible prescription period for any civil matter is six months. Agreements varying the default prescription period must be in writing. In addition to the general rule, shorter prescription periods exist in some legal areas, notably a three year period for claims involving defective product liability (see above)..

9. Set-off

Whether payments or mutual debts may be subject to set-off depends upon their origin and other characteristics. Generally speaking – and in sales in particular – all monetary debts originating from the same contractual transaction may be set-off against each other. If the debts do not originate from the same transaction, parties may still perform set-off as long as the debts are “fixed”, that is there is no reasonable

dispute regarding either their validity or the sum involved (e.g. documented sums, judicial awards, etc.). Debts and all monetary obligations originating from remedies for breach of contract, including restitution (e.g. following the contract's rescission) are subject to set-off.

10. Government Contracts

Contracts to which a state organ, including government agencies and municipal authorities, is party are subject to a dual system of law: general contract law and administrative law. Government agencies are therefore held to higher standards of practice than private parties in contracting and performing. While good faith duties apply to all contractual relations, administrative bodies are held to the basic principle of reasonableness as well. Public tenders are subject to special legislation and more stringent contract regulation that does not apply to private tenders.

However, government contracting is exposed to the special risk of the "release" doctrine by which the state, under certain conditions, is allowed to release itself from its contractual obligations without being liable for the ordinary remedies for breach of contract. A governmental body or agency may be released from a legally binding contract if a significant, adverse and unforeseen change in circumstances has occurred. Release must be exercised for public interests only, and financial gain alone is normally not a permissible excuse. The state organ must balance the public interest in release from the contract against the other party's reliance on it. Even when the court allows release, the aggrieved party is entitled to restitution and compensation for its justifiable reliance. While civil courts will not normally grant specific performance against the state (a remedy available in the High Court of Justice), substitute expectation relief in terms of monetary damages may, in excessive cases, be available to the plaintiff, especially if the court does not grant the justifiability of the release or the manner in which it was performed.

11. Business Organization

11.1 Forms of Business Organization

Several forms of business organization are available to foreign entities wishing to maintain a business presence in Israel. A presentation of some of the more common ones follows.

Note, that a relatively new statute, the Companies Law of 1999 has made several significant changes to Israeli corporate law, described below.

11.1.1 Branch or Subsidiary

A foreign corporation (a term which includes most forms of business entities) may establish a place of business in Israel as a local extension of its own business entity. Such a branch requires registration as a “foreign company.” The procedure for registration is simple and inexpensive (the company must file notarized copies of its statutes, memoranda and by-laws, a list of its directors, the name and address of a person resident in Israel authorized to accept service on its behalf and a power of attorney nominating a person ordinarily resident in Israel.) Unless the company’s control and management are exercised within Israel, a branch is only taxable on income generated locally.

Alternately, the foreign corporation may set up a local subsidiary, i.e., an Israeli corporation held by the foreign parent. Such are subject to simple and inexpensive registration. Capital may be nominal and there are no requirements that shareholders or directors reside in Israel.

A subsidiary, being an Israeli resident, would be taxed on overseas income and capital gains. A branch, will not normally be regarded as resident in Israel unless it elects to be so treated in order to take advantage of certain tax benefits available to resident companies. However, a subsidiary may remit income in a number of forms, e.g. dividends, amendment fees, royalties or interest. These are subject to withholding tax but a credit is normally available on such tax withheld. Reasonable management fees are deductible from the Israeli tax.

Companies limited by shares may be public or private (“closely-held” companies.) Only a public company may, upon publication of a prospectus approved by the Securities Authority, offer securities to the public. A private company may have a single shareholder and is required to have at least one director. The management and discharging of official requirements are normally simpler, quicker and less costly in a private company than in a public one.

11.1.2 Partnership

A partnership is an independent legal entity, and must be registered with the Registrar of Partnerships. Partnerships are either general, in which case the partners are jointly and severally liable for partnership debts, or limited. A limited partnership must have at least one general partner who is liable for all partnership debts. A foreign partnership, limited or not, may register as a foreign partnership with the Registrar, and it must do so in order to open any place of business in Israel; however, a foreign limited partnership must be approved by the Justice Ministry prior to its registration.

Technically, a partnership is limited to twenty members (in some cases, such as a legal or auditing partnership, fifty). However, as corporate bodies may be members of a partnership as well, partnership made of sub-partnerships are permissible.

Partnership is a common form of incorporation for foreign business involvement, inter alia for taking advantage of several tax benefits and other forms of government aid in some areas such as research and development, construction, infrastructure, petroleum exploration, etc.

11.1.3 Distributorships

A distributorship is a contractual rather than a corporate relation with a local entity that undertakes the distribution of goods or services (and in some areas, the required ensuing servicing of goods, networks, etc.) Subject to antitrust policies, a local distributorship may be exclusive or non-exclusive. The Israeli economy is characterized by a slow but steady increase in competition in areas that were traditionally restricted, such as energy, communication, transportation, automobile distributorship etc.

Some areas of practice require the distributor to be licensed by the state. Such is generally the case with sales to the defense establishment (permits are issued by the Ministry of Defense), which may also regulate the distributor or agent's remuneration.

11.1.4 Sales Representation

Empowering a local agent normally does not require registration, unless the agent's activities are deemed "swallowed" by the foreign corporation to such an extent that the relation will no longer be considered one of agency but of direct business activity, requiring registration as noted above. If the agent's activities become wholly integrated with those of the foreign corporation, considerations of immutable labor law may arise (a contractor or agent may inadvertently become an employee). Maintaining the agency relation, however, is a simple matter of structuring the business relation and should normally pose no serious problem.

11.2 Franchise

As a form of doing business in Israel, the franchise model has boomed in the last decade, both responding to and participating in the extensive expansion of shopping malls of various types and sizes in both urban and rural areas, to the profit of some

and the lament of others (this socio-economic trend has somewhat saturated). Many of the successful franchises are local, but some are international brands, especially in consumer areas such as fast food, apparel, retail and car rental. In the services, many Israeli providers have formed strategic alliances that do not amount to franchise with foreign and global firms, including in the areas of communication, financial services, insurance, information technology and some areas of manufacturing. As no special regulatory framework applies to franchise—whether locally or internationally centered—detailed contractual frameworks are indispensable. These must take into account particular Israeli legal regimes in such areas as labor law, antitrust law, consumer protection and the regulation of contracts of adhesion (see above).

11.3 Foreign Investment

This capsule cannot, of course, supply any in-depth information regarding foreign investment in Israel. The Israeli government encourages both foreign and local investment, especially in technology and information technology and manufacturing. This would include not just tax relieves but may include direct government grants. Government policies may require that supported enterprises be based in provincial centers rather than in the greater Tel-Aviv area. Israel is party to the Washington Convention on the Settlement of Investment Disputes Between States and Nationals of other States, 1965. For Free Trade Area agreements see below.

11.4 Currency Control

Israeli currency became gradually convertible during the 1990's and since December 31, 2002 all foreign currency control measures and restrictions—once a staple of Israeli governmental involvement in business—were abolished; the New Israel Shekel is now fully convertible. Israel has an open currency market and an active community of financial players involved in currency transactions, both locally and globally. Since 1992, Israeli banks also operate as currency clearinghouses for the Palestinian Authority and other Palestinian bodies.