

# Israel

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## IMMOVABLE PROPERTY

### 1. What are the most common forms of security that can be granted over immovable property?

The following security interests can be granted over immovable property:

- **Hypothec (*Mashkanta*)**. This type of security interest is suitable when the immovable property to be used as security is registered with the Land Registry. It applies to a defined asset. In event of a default, the lender can materialise the asset (under the terms of the Hypothec deed and subject to applicable laws) and use the proceeds to cover the financial debt.
- **Charge (*Mashkon* or *Shiabud*)**. This type of security interest is suitable when the immovable property to be used as security is not registered with the Land Registry (for example, registered with the Israeli Lands Administration or with a Housing company). It is also suitable when acquiring a security interest in rights that refer to immovable property, but which are contractual only without being registered. In event of a default the lender can materialise the asset (under the terms of the charge agreement and subject to applicable laws) and use the proceeds to cover the financial debt.
- **Floating charge (*Shiabud Zaf*)**. This type of security can apply to all or part of the assets of the company creating the charge. This charge does not immediately create a security interest. It hovers over the assets of the company and on the occurrence of a constituting event it materialises and applies to those assets that the company has at that time.

### 2. Can security over immovable property be granted to foreign lenders? If not, are there any ways to circumvent this?

Security over immovable property can be granted to foreign lenders.

## MOVABLE PROPERTY

### 3. What are the most common forms of security that can be granted over movable property?

The following security interests can be granted over movable property:

- **Charge**. A charge can also be applied to movable property (see *Question 1*). In this context movable property rights are broadly defined and include, for example, future income, intellectual property, intangible assets and rights.
- **Floating charge**. This type of security can also be applied to movable property (see *Question 1*).

### 4. Can security over movable property be granted to foreign lenders? If not, are there any ways to circumvent this?

Security over movable property can be granted to foreign lenders.

## PERFECTING SECURITY

### 5. What conditions must be satisfied to make the security valid and enforceable? Please answer for each form of security identified in *Questions 1* and *3* above and consider both:

- **Legal formalities (for example, in writing, by deed or notariation)**.
- **Perfection requirements (for example, the giving of notice or registration at a public office)**.

#### Legal formalities

All the securities mentioned in *Questions 1* and *3* must be created by an agreement (in respect of certain assets, such as real estate, there is a mandatory requirement for the agreement to be written) between the debtor (plus any third party providing the security for the debtor) and the creditor.

#### Perfection

The following perfection requirements apply:

- **Hypothec**. The hypothec deed must be registered with the Land Registry and the Companies Registry (*Israeli Lands Law 57 (1969)*, *The Companies Law 57 (1999)* (*Companies Law*), and corresponding case law).
- **Charge**. In order for a charge to become perfected (that is, binding on the liquidator and any of the company's creditors), it must be registered with the Companies Registry, unless it is a movable property that is in the possession of the creditor (*Companies Law*).

Certain forms of security require an additional registration including, for example:

- a charge on immovable property should also be registered with the Lands Registry;
- a charge on a vessel should be registered also with the Vessel Registry;
- a charge on a patent should be registered in the Patent Registry.
- **Floating charge.** In order for a floating charge to become perfected (that is, binding on the liquidator and any of the company's creditors) the charge must be registered with the Companies Registry (*Companies Law*).

The perfection of the above securities by registration has to be made within a certain period of time. (These time requirements are complex and should be consulted upon on an individual basis.)

To be duly authorised, a company granting a security must fulfil all its corporate obligations and pass any required resolutions relating to the execution of a security in favour of a lender.

A floating charge can include a limitation order on the creation of future charges, which prevents the creation of additional charges. However, charges imposed on a specific asset, in order to provide credit to allow the borrower to purchase that specific asset, are considered an exception and can be granted despite the existence of such limitation order at first priority.

For an overview of assets and related securities regulations, see table, *Taking security over assets in Israel*.

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#### 6. For each type of security considered in *Question 5*:

- If all the required formalities have been complied with, where will the secured lender rank on a subsequent insolvency, in terms of priority over other creditors?
  - If all the required formalities have not been complied with, where will the lender rank on a subsequent insolvency, in terms of priority over other creditors?
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#### Compliance

The following priority rankings apply to a company's creditors and debts in the event of liquidation:

- Liquidation and receivership costs (including the liquidator's and receiver's fees).
- Secured creditors, which are defined as:
  - tax debts which are automatically secured by a statutory charge under the Taxes Ordinance Collection;

- contractual liens (although these are not seen as a practical option for lenders);
- debts secured by a specific charge, hypothec or a floating charge that has materialised before the liquidation proceedings.
- Preferred creditors, which are defined as:
  - salary and credit extended for the payment of salary;
  - amounts deducted from salary at source;
  - mandatory taxes and rent that date back one year or more.
- Creditors secured by a floating charge that materialised after the liquidation.
- Ordinary creditors (that is, suppliers).
- Deferred creditors (that is, shareholders).

#### Non-compliance

In general, failure to comply with the formalities required to execute a hypothec, charge or floating charge can lead to an annulment of the security and put the lender at the same rank as ordinary creditors. The validity of a security is usually examined by the liquidator or receiver in the course of the liquidation or receivership proceedings. The determination of the liquidator or receiver may be challenged before the District Court which has jurisdiction over liquidation matters.

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#### COMMERCIAL SECURITY

#### 7. What types of "commercial security" or "quasi-security" (that is, legal structures that are used as an alternative to taking security) are common in your jurisdiction? In particular, consider:

- Sale and leaseback.
  - Factoring.
  - Hire purchase.
  - Retention of title.
  - Other structures.
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- **Commercial security in general.** A transaction is considered as a charge (and is governed by the Charge Law's regulations) if it is meant to secure a debt with an asset, regardless of the transaction title (*Charge Law 5727-1967 (Charge Law)*).

In the guiding Supreme Court ruling from 2003 (*CAP 1690/00 M S Kiduchey Hazafon and others v A Avgal Technology*

*Ltd (in temporary liquidation)*), and in other court rulings, it has been established that "commercial securities" (such as retention of title, consignment and conditional sale) are to be upheld as such (rather than as providing a security under the Charge Law) if this was the intention of the parties.

However, if the parties intended to transfer title but merely postponed the actual transfer to secure an obligation, then the requirements pursuant to the Charge Law would still need to be fulfilled in order for such a "commercial security" to be binding on third parties in liquidation.

In practice, despite this ruling, several District Courts have continued to consider retention of title and conditional sale transactions as transactions providing for a security and apply the requirements of the Charge Law. In this situation the debt ranks as an ordinary creditor (*see Question 7*).

- **Sale and leaseback.** This sort of transaction is a normal financial deal common in real estate but is not used in practice for "commercial security" purposes.
- **Factoring.** This is a "commercial security" that has been recently introduced into the Israeli market. However, this method may be treated as a security, subject to the requirements of the Charge Law, if the receivables are not paid directly to the lender.
- **Hire purchase.** This sort of transaction is a normal financial deal common in real estate but is not used in practice for "commercial security" purposes.

## RISK AREAS WHEN GRANTING SECURITY

### 8. Are there any types of assets over which security cannot be granted or is difficult to grant, in particular:

- Future assets.
- Intangible assets.
- Fungible assets (that is, a pool of assets the constituents of which change over time).
- Other assets.

Future assets, intangible assets and fungible assets can all be granted as security.

Practical issues concerning the need for consent of other secured creditors arise when there is a secondary charge to be imposed on an asset or where there is a floating charge limiting the borrower's ability to grant additional securities.

### 9. Are there any company law rules which impact on the granting of security? In particular:

- Would the granting of security by a company to secure debt used to purchase its own shares (or the shares of a subsidiary) constitute the giving of unlawful financial assistance?
- Would a parent company granting security in respect of a loan to its subsidiary breach any "corporate benefit" rules?
- Other rules?

■ **Unlawful financial assistance.** A company, or its subsidiary, purchasing its own shares is considered as a distribution of dividend and therefore must:

- be limited in value to the company's profits; and
- not result in the company being unable to meet its financial obligations.

■ **Corporate benefit rules.** The directors of a company have a duty to act in, what should be reasonably considered as, the best interests of the company. The directors are under the duty to consider and balance between the risks and benefits associated with the granting of security for another company's debt.

For a parent company and its subsidiary, the granting of securities for credit obtained by one of the companies is a daily matter. Often the interests are such that the parent company indirectly conducts a particular business activity through its subsidiary and while it enjoys the benefits of having the activity within a separate entity, it bears the financial risks of its subsidiary to a certain extent.

### 10. Is the trust concept recognised under domestic law? If not:

- Would a trust created under the law of another country be recognised in your jurisdiction?
- Would the rights of a security trustee be enforced in the local courts?

■ **Recognition.** Trusts are recognised and are regulated by the Trust Law 5739-1979 and court decisions.

If, under the laws of the country where the trust was established, the trust is considered as a fully authorised legal entity, then it will be recognised by the Israeli courts.

■ **Enforcement.** In general, the rights of a security trustee can be enforced in the local courts.

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**11. After a new security has been granted, is it vulnerable to being set aside within certain time limits if the grantor subsequently becomes insolvent? If yes, what types of transactions are potentially reviewable?**

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In an insolvency proceeding, a security may be vulnerable to being set aside and not binding on the liquidator, if one of the following conditions takes place:

- The security was:
  - granted in the two years before the debtor became insolvent; and
  - not granted in good faith and for reasonable consideration.
- All of the following occur:
  - the security was granted between two to ten years before the debtor became insolvent;
  - the security was not given in good faith and for reasonable consideration;
  - the claimant does not prove that at the time of giving the security, the company was solvent without the need of the security.
- The grant of the security is considered as a fraudulent preference.
- If the security is a floating charge that has been granted in the six months before the company's insolvency, then the floating charge will only apply in respect of those amounts actually paid after the creation of the floating charge but cannot secure prior debts.

## ENFORCEMENT

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**12. In what circumstances can the secured creditor generally enforce its security?**

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A lender is entitled to several remedies in case of a contractual breach by the borrower.

The circumstances in which the lender is entitled to enforce its security is usually defined in the loan agreement, and typical default events include:

- Failure to make a payment or breach of the payment terms.
- Other material breaches or misrepresentations that adversely affect the financial ability of the borrower.
- Insolvency, change of control, change of business, and other materially adverse changes.

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**13. Is enforcement limited to a public sale of the secured asset through the courts? If not, what other types of enforcement action can be taken?**

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Charged assets can be realised by filing a court claim (*Charge Law*). In the claim, the lender would have to establish that the contract terms have been breached and the remedy of realisation is valid.

However, in most cases, the security of movable and immovable assets is registered with the relevant Official Registrar and can be realised by directly filing a petition to the Enforcement Chambers without court involvement. In general, the realisation procedures through the Enforcement Chambers are initiated by the lender that holds the warrant, who petitions the realisation of the security from the Head of the Enforcement Chambers. The Head of the Enforcement Chambers' discretion is limited to the realisation procedure. It does not question the existence of a security and requested procedures are only rejected if they are excessively harmful to the debtor or to other creditors.

Following the approval of the Head of the Enforcement Chambers, the secured asset is realised by a public sale that is administered by an appointed receiver. The result of the sale and its finalisation require the approval of the Head of the Enforcement Chambers.

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**14. How will the secured creditor's rights to enforce its security be affected by the commencement of:**

- Any company rescue procedures in place in your jurisdiction?
  - Any insolvency procedures in place in your jurisdiction?
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### Company rescue procedures

If a court is presented with a recovery plan under which it believes there is a reasonable possibility of the company recovering, it can implement a procedure known as a "stay of proceedings". Under this, all proceedings against the company (including the materialisation of securities) are stayed. To administer and supervise the process, the court usually appoints a trustee or special administrator.

### Insolvency procedures

In Israel, insolvency proceedings against a company are called liquidation proceedings. The court appoints a company liquidator who must liquidate the company's assets and other rights, and examine the debts of the company. Once the liquidation of assets is accomplished, the liquidator distributes a dividend to the creditors in accordance with the ranking of their debts (*see Question 6*).

Any actions taken by creditors against the company are suspended and no new actions can be brought without the court's approval. The materialisation of a charge or other security can be

ordered by the court in parallel to the liquidation proceedings, but in practice if there is a liquidator or a temporary liquidator then he usually realises all the securities.

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**15. Are there any laws that restrict the recovery of costs or interest under the security document or loan agreement, in particular, default interest?**

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Costs and interest can be recovered if they are provided for in the loan agreement. The parties can agree on a fixed or variable rate of interest above the usual interest rate payable, which is valid as long as it:

- Does not exceed a certain statutory limitation (more than twice the average interest rate for similar credits in the Israeli banking system).
- Is not punitive in its nature.

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**16. Will the enforcement (or holding) of the security attract any liability under environmental laws?**

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No liability is imposed on creditors until the debtor is in default and the lender enforces its security by taking over the debtor's business or assets. Following this, if the lender breaches any environmental laws regarding the enforced security it may become subject to liabilities.

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**17. Will a foreign choice of law clause in a security document be recognised and applied by the courts in your jurisdiction?**

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The Israeli courts respect an express choice of law and jurisdiction in a security document, unless the choice of law was made deliberately to avoid provisions of national laws or contradicts public order.

However, in a liquidation (except where it is a conflict limited to the borrower and lender only) the Israeli courts do not usually consider a security interest under a foreign choice of law to be binding on third parties unless all the requirements of form and registration under Israeli law have been met.

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**18. Are there any exchange controls in force that could prevent any repatriation of realisation proceeds or other payments to a foreign lender under the security document or loan agreement?**

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Except for money laundering regulations, there are no exchange controls in force that would prevent the repatriation of proceeds realised in Israel through the enforcement of security or other payments to a foreign lender under a security document or loan agreement.

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**19. Will a judgment obtained in a foreign court (for example, ordering that a lender can sell the secured asset and retain the proceeds of sale) be enforceable in your jurisdiction without the need for a retrial of the case?**

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A foreign judgment cannot be automatically enforced as a local one. Judgments obtained by foreign courts are only enforceable in Israel if the foreign judgment is in accordance with the terms of the Israeli Foreign Judgments Enforcement Law 5718-1958 and other conventions (if applicable). Under this Law, an Israeli court can declare a foreign judgment as enforceable in Israel if all the following conditions are fulfilled (*Enforcement Law*):

- The foreign court was properly authorised to obtain that judgment.
- The foreign judgment is final and cannot be appealed or reversed.
- The enforcement of the foreign judgment does not contradict Israeli laws or public order.
- The foreign judgment is enforceable in the jurisdiction in which it was issued.

To get an Israeli court to declare a foreign judgment enforceable, a petition must be served to the Israeli court. The subject matter of the foreign judgment is not re-examined; instead the examination of the petition and permissible arguments of objection are usually limited to the above-mentioned conditions.

If the judgment is enforced then it can be executed as a local judgment. However, in liquidation proceedings a foreign judgment ordering the sale of a specific security would probably not be enforced and rank just as an ordinary debt unless all requirements of form and perfection under Israeli law were made as well.

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## TAX

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**20. Are any documentary taxes (for example, stamp duty), registration fees or notaries' fees payable in connection with the granting or taking of security, or its enforcement?**

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### Taking security

Stamp duty (previously 0.4%) was abolished on 1 January 2006. The registration fees of the various registries are usually fixed and are not particularly high. In some registries the amount of the fee may correspond to the period of the charge, but the amounts are not material.

### Enforcement

Securities are enforced through the Enforcement Chambers or, in certain cases, through court (*see Question 13*). There are mandatory official fees paid to the state for these proceedings and while they may be fixed in certain cases, they are usually calculated in proportion to the debt in receivership and may therefore be significant.

TAKING SECURITY OVER ASSETS IN ISRAEL			
Asset type	What form(s) of security can be granted?	Can security be granted to a foreign lender?	What conditions must be satisfied to make the security valid and enforceable?
Real estate (rights serving as security is registered with the Land Registry)	Hypothec.	Yes.	Agreement in writing. Registration with the Land Registry and the Companies Registry.
Real estate (rights serving as security are not registered with the Land Registry)	Charge.	Yes.	Agreement in writing. Companies Registry and Registry* where the right serving as security is registered.
Registered intellectual property rights	Charge.	Yes.	Patents: agreement in writing and registration with the Companies Registry and the Patent Registry. Trademarks: registration with the Companies Registry.
Unregistered intellectual property rights	Charge.	Yes.	Registration with the Companies Registry.
Plant and machinery	Charge.	Yes.	Registration with the Companies Registry (it can also be perfected without registration if the creditor receives possession**).
Trading stock	Floating charge.	Yes.	Registration with the Companies Registry.
Other movable property	Charge.	Yes.	Registration with the Companies Registry (it can also be perfected without registration if the creditor receives possession**). Vehicles: additional registration with the Ministry of Transportation*. Vessel: additional registration with the Vessel Registry at the port of registration.
Financial instruments	Charge.	Yes.	Registration with the Companies Registry.
Choses in action (such as debts or rights under contracts)	Charge.	Yes.	Important to provide notice to third party to prevent payment directly to the debtor. Registration with the Companies Registry.

The following professional fees may also have to be paid:

- Mandatory professional fees if the enforcement is done through the Enforcement Chambers.
- Discretionary professional fees determined by the court (*The Companies Regulations (Rules concerning the Appointment of Asset Receivers and Liquidators and their fees) 1981*).

Both of the above-mentioned professional fees are usually in proportion to the debt and the amounts materialised.

Fees due to the receiver or liquidator rank before other creditors. However, where there is a surplus from the security materialisation beyond the amount of the debt, then the professional fees are normally imposed on the debtor's part.

## 21. Where such taxes and fees make the granting or taking of security prohibitively expensive, are any strategies available to minimise costs?

There is no stamp duty and registration fees are minimal (see Question 20). Therefore, the mitigation of taxes and fees is not normally an issue.

## 22. Is any withholding tax or other tax due in relation to any payments made under the loan to a foreign lender?

Any interest paid by an Israeli resident is considered as income generated in Israel. However, as an exception, interest payments made by an Israeli resident, due to credits extended to his permanent establishment outside of Israel, are considered as generated outside of Israel (*section 4A, The Income Tax Ordinance (New Version)*).

If the interest is considered as being generated in Israel it is subject to local taxation and withholding tax should be expected.

In addition, Israeli tax treaties with other jurisdictions may affect the situation.

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**23. Will a foreign lender be deemed to be resident or domiciled in your jurisdiction for tax purposes by reason of the security document or loan agreement?**

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In principle, a foreign lender is not considered to be a resident for tax purposes by sole reason of a security document or loan agreement.

However, there may be taxes that apply to the asset granted as security, duties of deduction at source, or similar regulations, that must be taken into account in specific cases.

## REFORM

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**24. Please summarise any proposals for major reform in the area of taking security.**

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There are currently no plans to reform the law in this area.

*\*The necessity of registering the security with the marked registry may be questionable.*

*\*\* In spite of the alternative of perfecting a charge by receipt of possession with the creditor, in practice the charges are registered with the Companies Registry as a precaution.*



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