Recent Israel Securities Authority Position Places New Restrictions on Investment Funds in Israel

The Israel Securities Authority recently published a staff position that has material implications on investment funds in Israel.

This ISA position was issued following a ruling by the Tel Aviv District Court in the Integral Fund case – a hedge fund that caused substantial losses to the hundreds of its investors. In this case, contrary to Integrals argument, the court ruled that the provisions of the Joint Investment Trust Law apply to the fund and therefore Integral Fund breached the regulatory obligations that apply to it.

The Integral Fund Ruling

In the framework of the Integral Ruling, Judge Dania Keret-Meir of the Economic Division of the Tel Aviv District Court ruled that the Joint Investment Law applied to Integral Fund, as the purpose of the fund (which was a hedge fund) was a joint investment in securities and for the purpose of making profit through investment in those securities. In determining whether the conditions for an exemption under the above Section 2(b) of the Joint Investment Law were satisfied, the judge held that in less than two years following the establishment of Integral Fund the number of investors considerably exceeded fifty investors (without distinguishing between accredited and non-accredited investors) and, furthermore, the principals of the Integral Fund engaged in active public marketing activities in order to solicit investors. Consequently, the court held that the exemption from the Joint Investment Law was not applicable to Integral Fund and, thus, concluded that such fund was subject to the regulatory regime of the Joint Investment Law.

The Integral Ruling prompted several applications submitted to the ISA by various hedge funds requesting clarification as to its seemingly far-reaching effect. Until the Integral Ruling, the issue of application of the Joint Investment Law was subject to ambiguous interpretation and was not directly addressed by either Israeli law nor by the ISA.

In its position, the ISA provided clarifications about some of the topics addressed in the court ruling, specifically clarifying its position regarding the correlation between the Israeli Securities Law and the Israeli Joint Investment Trust Law in the context of private investment funds. According to the ISA staff position, investment funds, (including hedge funds, venture capital, private equity and others) that meet particular criteria are subject to the Joint Investment Trust Law and to the stringent regulations that apply by virtue of this law.

1. Mode And Place Of Incorporation

Section 2(a) of the Joint Investment Trust Law exempts an investment arrangement if that arrangement is regulated under another law. Prior to the publication of the ISA position, the prevailing interpretation was that hedge funds incorporated as limited partnerships are regulated under the Partnership Ordinance, and therefore the Joint Investment Trust Law does not apply to them.

It was further clarified that the mode of incorporation (whether as limited corporation or partnership), and the place of incorporation (in Israel or abroad), do not constitute a comprehensive designated arrangement that suffices to exempt a fund from application of the Joint Investment Trust Law. This determination is also true if the fund's activities are regulated under foreign law.

2. Maximum Number Of Investors

Section 2(b) of the Joint Investment Trust Law stipulates two conditions in order for an investment arrangement to qualify for an exemption from the law. The law shall not apply to an investment arrangement (i) if the number of participating investors does not exceed fifty and (ii) was not made via an offer to the public. The ISA Circular definitively states that Accredited Investors shall not be taken into account, when determining the total number of participating investors. Accordingly, a private offer made by an investment fund solely to Accredited Investors will not be considered as an offer to the public. However, the number of non-Qualifying Investors may not exceed fifty at any point in time.

The ISA's stance as reflected in the ISA position provides long awaited guidance by supporting and acknowledging the view adopted by most legal practitioners in the private equity industry, whereby the number of Sophisticated Investors in a private equity fund should not be limited. However, accepting subscriptions from thirty-five non-accredited investors on a continuous basis during any given twelve month period is not permissible under the Joint Investment Law if it would cause the total number of non-accredited investors to be over fifty. This is contrary to the provisions of the Securities Law which allow the offering to up to thirty-five non-accredited investors each twelve month period.

With respect to private equity funds and venture capital funds, which are generally closed-end investment vehicles whose fundraising period is in any event limited the recent ISA position may not have a material effect on its ability to raise capital. Conversely, with respect to open-ended funds admitting investors on an ongoing and periodic basis, such as hedge funds, the recent ISA Circular may be viewed as having a detrimental effect by limiting the total number of investors and thus public access to hedge funds through the 50 non-accredited investors limitation at all times.

3. Name Of The Fundraising Entity

The name of the fundraising entity has no effect on which law or regulation applies to it. The applicable law will be determined according to the characteristics of the entity or the investment. In other words, the Joint Investment Trust Law will not apply solely to entities called a "mutual fund" and can also apply to entities called "hedge fund," "private equity fund", "investment fund," etc.

4. Artificial Splits

Various investment arrangements have tried to circumvent the limit of thirty-five offerees in a public offer pursuant to the Israel Securities Law, by artificially splitting the investment arrangement into a number of disparate investment arrangements and counting the offerees in each arrangement separately instead of aggregately. The ISA staff clarified in its position that artificially splitting funds into separate legal entities

cannot serve to circumvent the provisions of the Israel Securities Law or the Joint Investment Trust Law as they pertain to the maximum number of offerees and investors.

5. Contacting And Publicizing Offers To The Public

The Joint Investment Trust Law and the Israel Securities Law prohibit funds from contacting the public and publicizing any investment offer without an ISA approved prospectus. The ISA clarifies that contacting the public and publicizing offers to the public encompass an open list of the various ways potential investors may be contacted (telephone, email, written and oral advertisements, advertisements on social networks, presentations and brochures, word of mouth, etc.—all of which are prohibited.

This document provides a general summary and is for information purposes only. It is not intended to be comprehensive nor does it constitute legal advice. If you are interested in obtaining further information please contact our office at:

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