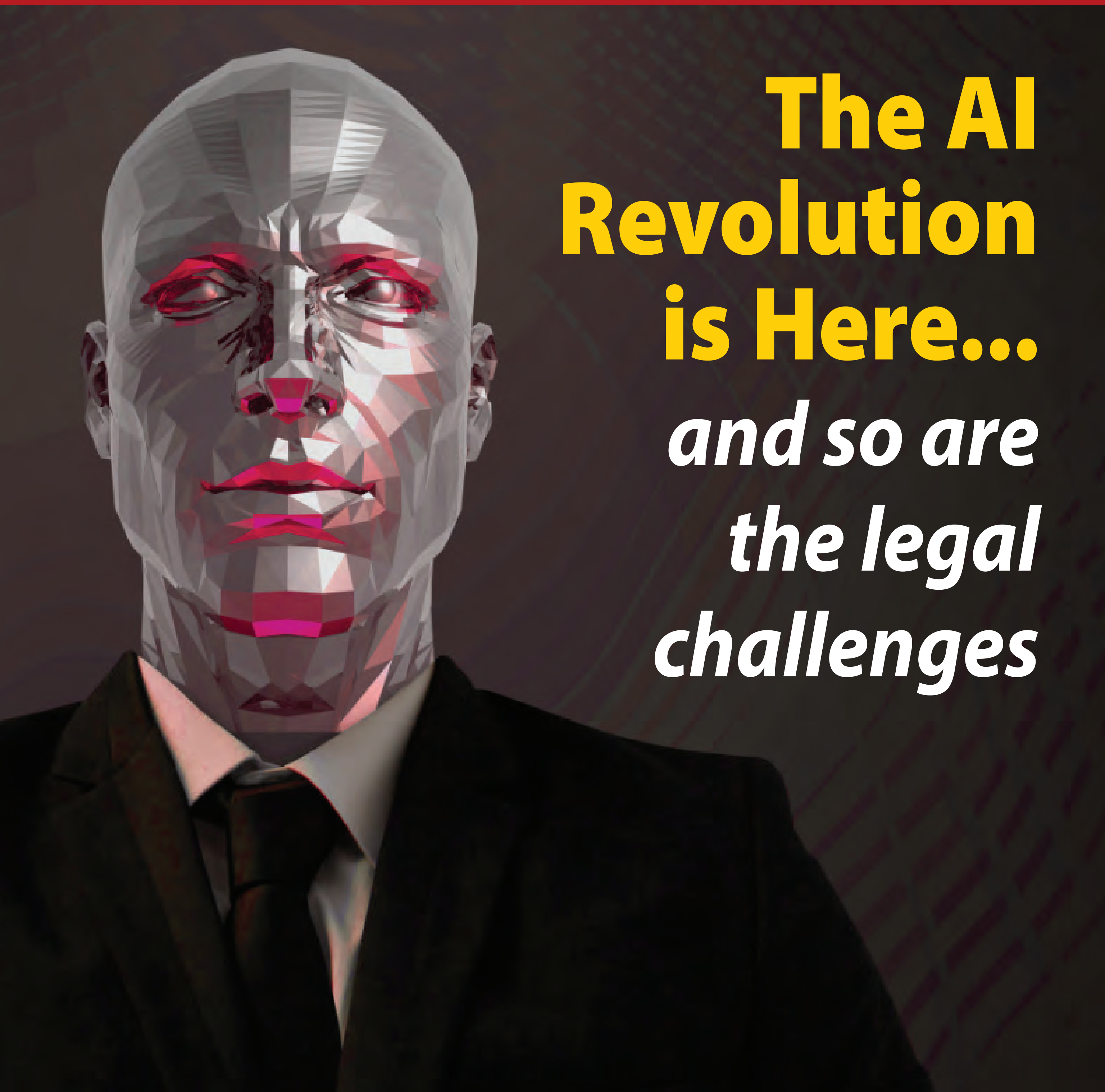
THE US-ISRAEL LEGAL REVIEW 2024/25



The AI Revolution is Here... *and so are the legal challenges*

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IN ASSOCIATION WITH:
ACC Association of Corporate Counsel
ISRAEL

Lowenstein Sandler

Navigating the U.S. Capital Markets for Israeli Companies

The U.S. capital markets continue to offer compelling opportunities for Israeli companies seeking to raise capital and achieve global reach.

Since the 1980s, hundreds of Israeli companies have listed on the Nasdaq or NYSE and 99 are currently listed. Israel has led all other countries in foreign companies listed on these exchanges, apart from China and Canada. U.S.-listed Israeli companies span all industries, but fast-growing and innovative technology and life sciences companies are particularly well represented and have found great success in the U.S. capital markets.

The U.S. capital markets offer excellent opportunities for tech and life sciences startups to raise the necessary capital to achieve growth and scale. A listing on a U.S. exchange allows Israeli companies to access deep pools of capital from institutional and retail investors and attract investment from both U.S. and global investors. A NYSE or Nasdaq listing provides liquidity, visibility, and credibility to a company, often leading to further opportunities for strategic partnerships, acquisitions, and brand recognition.

Additionally, the U.S. market tends to offer higher valuations for innovative tech and life sciences companies, compared to many other regions of the world. As a result, Israeli companies may achieve better valuations, which can help them raise more capital at favorable terms. The advantages of a U.S. listing can help Israeli companies accelerate growth, benefit their founders and early investors and expand their global reach.

MARKET OVERVIEW AND OUTLOOK

The U.S. capital markets saw a solid increase in IPO activity in 2024. 150 IPOs raised over $29 billion in proceeds, more than was raised in 2022 and 2023 combined. While the increase was a positive sign, volumes and deal count were still below historical averages. Foreign issuers accounted for slightly more than half of the year's IPOs by deal count. In 2024, Gauzy was the only Israeli company to go public via a traditional IPO. By sector, industrials and healthcare deals led the way with many venture capital-backed technology companies staying on the sidelines. Although a traditional IPO is viewed favorably by the U.S. capital markets, many companies are unable to access such offering due to company stage and size and other metrics, as well as the overall public markets generally, and such companies need to rely on an alternative public offering to gain access to the U.S. capital markets. Such alternative public offerings include de-SPACs and traditional reverse mergers. During 2024, the SPAC market began to stabilize with 56 blank check companies raising $8.5 billion through IPOs. While the market continues to work its way through the backlog created by the 2020-2021 SPAC boom, there was a significant number of SPAC liquidations but also 71 companies listed through completed de-SPAC transactions.

Expectations are that the IPO market will continue to normalize through 2025 with increases in amounts raised and deal counts. There are hopes that technology companies, many of which will leverage investor interest in artificial intelligence, will return to drive the IPO market. We also expect to continue to see a challenging environment for de-SPAC transactions as the last SPACs of the prior boom reach their termination dates. Through 2025 there will likely be continuing high levels of SPAC investor redemptions, deal terminations and liquidations, but also a number of successful business combinations that could form the foundation for a stabilized and more healthy market environment in the back half of the year and into 2026.

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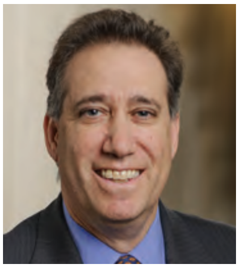

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PARTNER

Fueling expectations for improved market conditions is a relaxed U.S. regulatory environment that could lead to higher levels of growth, corporate profits and company valuations. Notwithstanding this, actions taken by the new administration and related developments in Washington, D.C. could lead to significant market volatility and increase deal execution risk. Continued global geopolitical unrest, including in the Middle East, and the impact of tariffs and global decoupling could also dampen the IPO market and capital markets overall.

BENEFITS OF BEING A FOREIGN PRIVATE ISSUER

Israeli companies that access the U.S. capital markets are subject to the U.S. federal securities laws. With the goal of making the U.S. capital markets more attractive to these issuers, the Securities and Exchange Commission (SEC) makes available certain accommodations to alleviate some of the burdens of being a public company in the United States. Generally, to take advantage of these accommodations, an Israeli company must qualify as a foreign private issuer (FPI). FPIs may benefit from more relaxed reporting requirements under SEC rules and regulations, including scaled disclosure requirements, not being subject to U.S. proxy rules, and exemptions for insiders from certain beneficial ownership reporting requirements and short-swing trading rules under the U.S. Exchange Act. In addition, the NYSE and Nasdaq also provide for more relaxed rules for FPIs, including certain rules related to stockholder approval for certain securities offerings, making access to capital potentially more streamlined for FPIs.

CORPORATE GOVERNANCE CONSIDERATIONS

Generally, FPIs are permitted to opt out of most NYSE and Nasdaq corporate governance requirements and may, instead, follow home-country practice. These companies must publicly disclose the ways in which their corporate governance practices differ from those followed by U.S. domestic issuers. Additionally, under the Israeli Companies Law, Israeli "public companies," which includes those with shares listed on the NYSE or Nasdaq, are required to appoint at least two external directors. If such companies do not have a controlling shareholder (as defined in the Companies Law), they may (but are not required to) elect to opt out of the requirement to maintain external directors and certain board committee composition requirements.

Board Independence

U.S. domestic companies are required to have a board composed of a majority of independent directors within 12 months of listing. Most issuers have a majority independent board at time of listing. FPIs may opt-out of this requirement and apply home-country practice. As noted above, Israeli companies are required to have at least two external directors, unless they are eligible and so elect to opt out of this requirement.

Audit Committees

FPIs are required, just as U.S. domestic companies, to have an independent audit committee that meets the requirements of Exchange Act Rule 10A-3. Audit committees under NYSE and Nasdaq rules must:

- Be composed of only independent directors; and
- Have at least one audit committee financial expert.

Both U.S. domestic companies and Israeli FPIs are required to have audit committees composed of at least three directors. If an Israeli company has not opted out of the audit committee composition requirements under the Companies Law, then it would also be required to include all external directors on the board and be chaired by an external director. The board chair should not serve, and directors or affiliates of any controlling shareholder(s) also should not serve on the audit committee. Under the Companies Law, the board of an Israeli public company must also appoint an internal auditor recommended by the audit committee.

Other Committees

U.S. domestic companies are required by both the NYSE and Nasdaq to have: (i) a compensation committee, and (ii) a nominating and corporate governance committee, each composed of independent directors. Generally, each of these committees consists of three directors. FPIs may opt out of these additional committee requirements and apply home-country practice.

If an Israeli company has not opted out of the compensation committee composition requirements under the Companies Law, then the compensation committee generally must be comprised of at least three directors, including all the external directors, who must constitute a majority of the members of the compensation committee. The chairperson of the committee must be an external director. In general, under the Companies Law, a public company must have a compensation policy approved by the board after receiving and considering the recommendations of the compensation committee.

Israeli companies are not required to have nominating and corporate governance committees; however, many companies that list on the NYSE or Nasdaq do establish them.

FINANCIAL STATEMENT REQUIREMENTS

FPIs may take advantage of several accommodations under the SEC's rules with respect to financial statement requirements and additional accommodations if they qualify as an emerging growth company (EGC) under the JOBS Act. Generally, an EGC is defined as a company with less than $1.235 billion in annual gross revenue.

In addition to including its own audited annual and interim financial statements in a registration statement, issuers may be required to provide acquired company financial statements and pro forma financial statements of recently acquired businesses, depending upon the significance of the acquisition.

Auditing Standards

U.S. domestic issuers must file financial statements with the SEC in accordance with U.S. GAAP. Financial statements of FPIs may be prepared in accordance with U.S. GAAP, IASB IFRS or local GAAP. Where FPIs utilize IASB IFRS, no reconciliation to U.S. GAAP is required. Where FPIs utilize local GAAP, financial statements must include appropriate reconciliations to U.S. GAAP. Many Israeli companies that are listed in the United States elect to use U.S. GAAP. While the Tel Aviv Stock Exchange generally requires listed companies to follow IFRS, if a company is dual listed in the United States, it may choose to report in U.S. GAAP.

PROCESS FOR IPOs AND ALTERNATIVES

An initial public offering (IPO) is a company's first underwritten sale of stock to public market investors. Prior to an IPO, a company may be owned by its founders, its employees and by private investors, such as venture capital firms. Companies may pursue an IPO to raise growth capital, provide liquidity to its investors and for reputational reasons. Preparations usually commence up to two years in advance of an IPO but begin in earnest with an organizational

Financial Statement Requirements for Registration Statements

	EGC	Non-EGC
Annual Financial Statements*	Two years of audited annual financial statements	Three years of audited annual financial statements
Interim Financial Statements**	Interim financial statements covering the most recently completed quarterly period	Same

** For FPIs, date of the last audit cannot be more than 12 months prior to filing of a registration statement, subject to limited exceptions.*

*** For FPIs, interim financials covering at least the first six months of the year are required nine months after the fiscal year end. In the offering context, however, auditor comfort letters may require the issuer to include more current interim financial statements.*

meeting with the company's selected underwriters. An IPO can be completed in as few as four to six months following this kick-off. Key milestones for an IPO include confidential and public SEC filings, testing-the-waters meetings with investors, the launch of the roadshow, pricing of the offering, the first day of trading and the closing of the offering.

Alternatives to a traditional IPO include direct listings, reverse mergers and de-SPAC transactions. A "direct listing" is a process where a company goes public by allowing existing shareholders to sell their shares directly to the public on a stock exchange, without the need for an underwriter or issuing new shares, essentially bypassing the traditional IPO process and associated costs with investment banks. Many foreign issuers that are already listed on a non-U.S. exchange utilize direct listings to achieve a second listing on the NYSE or Nasdaq. Reverse mergers involve a private company merging with a publicly listed company and acquiring control of such public company, making the private company public. De-SPACs are a more structured version of the reverse merger whereby publicly listed shell companies are formed for the sole purpose of completing a business combination with a promising private company to bring it public. An Israeli company considering a U.S. public listing should carefully consider each path and alternative to determine which is most well matched to its goals and objectives.

CONSIDERING THE DE-SPAC

There are several factors to consider in evaluating whether a de-SPAC is right for your company. Successful IPOs may be more difficult to execute for small- and mid-cap companies, companies with limited public company peers or those that have a more complicated story to tell the market. SPACs provide an alternative for these types of companies and potentially allow them to communicate in a more direct way with the market and potential investors.

Negotiations over company valuation in the de-SPAC process occur in advance of an initial filing with the SEC and public disclosure of the deal, while IPO pricing is subject to market uncertainty and volatility after an issuer has already gone on the road. A de-SPAC process can provide more flexibility in structuring deal economics, potentially including future earnouts for company investors after achieving specified milestones.

Both IPOs and de-SPACs present market risk. An IPO is subject to market risk because valuation is based on shareholder demand. A de-SPAC is subject to market risk because closing is contingent on market receptivity to a deal and avoiding redemptions or raising additional capital sufficient to fund future growth.

Both de-SPACs and IPOs can offer liquidity to a company's current shareholders, but a de-SPAC may afford more flexibility. IPOs typically require that all current company shareholders sign 180-day lock-up agreements, while de-SPACs typically only require these lock-ups from company insiders and affiliates.

KEY CHALLENGES OF A DE-SPAC

While a de-SPAC can provide certain advantages, there are certain challenges inherent in their structure and the accompanying processes. Since 2021, SPACs have seen significantly higher rates of shareholder redemptions leaving less money available to fund the business combination with the company target. Redemptions and certainty of capital are continuously pressing issues that come up in negotiations and the execution of the transaction. As a result, de-SPACs are sometimes recut post-announcement and target companies should anticipate the need to revisit negotiations post-signing to keep redemptions in check and ensure favorable post-closing trading.

Oftentimes, the SPAC public shareholder base must be replaced in connection with the de-SPAC, requiring extensive marketing activities and efforts on behalf of both the SPAC and target company. De-SPAC companies also need to make extra efforts to secure research analyst coverage, a function that is ordinarily facilitated by underwriters in an IPO.

Lastly, if a deal fails, recourse against the SPAC is limited. If the deal has been publicly announced before failing, the expected company valuation and significant company disclosures remain in the public domain, which may make it more difficult to go public or undertake a strategic alternative later.

PREPARING TO GO PUBLIC

An Israeli company should start preparations 18 – 24 months in advance of a potential NYSE or Nasdaq listing regardless of whether it elects to pursue an IPO or an alternative. Below are some actions that a company can take to ensure its public market readiness and success as a public company.

Financial Statements

As discussed above, at least two years of audited financial statements will be required for a company to go public and additional financial statements may be required. The company's auditor must be registered with the Public Company Accounting Oversight Board (PCAOB) and satisfy both the SEC's and PCAOB's independence requirements. Potential issuers should take note that public company accounting rules often differ from private company accounting rules, so certain changes may need to be made to historical financial reporting practices.

Internal Controls over Financial Reporting

After becoming a public company, Section 404 of the Sarbanes-Oxley Act (SOX 404) will require that management evaluate and report on the issuer's internal control over financial reporting. In connection with a public listing any material weaknesses will be disclosed in the issuer's registration statement. Once public, compliance with SOX 404 is a significant undertaking, and newly public companies often engage third parties to assist them in evaluating and/or remediating internal control issues.

Evaluate Capitalization and Existing Shareholder Rights

In advance of a public listing, it is important to review the existing capital structure to determine the impact of the transaction on outstanding securities. A review of shareholder rights should be undertaken to identify any necessary consents, waivers and amendments. Consider whether existing investors have registration rights, approval or veto rights over the proposed transaction and whether investors are required to sign a customary lock-up.

Composition of Board and Management Team

It is often necessary or desirable for an issuer to change the composition of its board by changing or adding directors to satisfy independence requirements and build out the board's diversity and skill set. The public company demands on an issuer's management team are significant, and often companies need to increase their accounting and finance staff and add investor relations capabilities. Companies should consider whether it will be necessary or advisable to retain additional senior management or make changes ahead of going public.

Prepare for the Diligence Process

In an IPO, the underwriters and counsel for both the underwriters and the issuer will conduct legal and business diligence on the issuer, including a review of corporate records, material contracts and other similar materials, and documentary support for statistical information and other statements included in the IPO prospectus. In a de-SPAC, the same will be true but the SPAC acquirer will conduct diligence on the company in place of the underwriters. In both an IPO and de-SPAC, the SEC will also require companies to provide materials to substantiate any claims made in the registration statement regarding market position, industry size, etc. The company should be prepared to provide substantially all such materials well ahead of the initial submission of the IPO registration statement.

HOW LOWENSTEIN CAN HELP

Navigating the U.S. capital markets presents unique challenges and opportunities for Israeli companies. Lowenstein is uniquely positioned to guide them through every stage of the process. With deep expertise in capital markets transactions, extensive experience in the tech, startup, life sciences and venture space, and a proven track record of successfully advising Israeli companies and investors, Lowenstein provides strategic, solutions-oriented counsel tailored to the needs of high-growth businesses.

Our longstanding relationships with key market players, coupled with our close collaboration with leading Israeli law firms, allow us to offer seamless, pragmatic advice that balances legal complexities with business realities. Whether it's preparing for an IPO, structuring a PIPE, SPAC or reverse merger transaction, or navigating corporate governance or ongoing reporting obligations, Lowenstein delivers the insight, execution and commitment that Israeli companies need to succeed in the U.S. market. ■

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