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Memorandum of Law

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Memorandum of Law - Securities Law (Amendment No ____)(Designated Exchange) 5780-2020
General

- Amendment to Section 1
- Addition of Section 51A
- Amendment to the Companies Law

A. Title of the proposed law

Memorandum of Securities Law (Amendment No. ____)(Designated Exchange) 5780-2020.

B. The aim of and need for the proposed law, main regulations, and effect on existing law

The proposed law is designed to establish the foundation for the establishment of designated exchanges in Israel by, among other things, removing barriers and adjusting the regulation that will apply to companies whose securities will be registered in a designated exchange, without compromising on the protection of public investors or fair and proper conduct of trading.

The provisions of the Securities Law 5728-1968 (“the Securities Law”) concerning stock exchange licensing and supervision envisioned a major national stock exchange that is a central force in the Israeli capital market due to its trading volumes and impact on the economy. Consequently, several of the regulatory requirements that apply to a stock exchange under Chapter Eight of the Securities Law may impede the establishment of smaller trading platforms with unique trading features.

To promote Israel’s capital market by expanding the investment and trading options available to investors, the range of services offered on the capital market, and the technologies in use, the Ministry of Finance wishes to promote securities trading activities on trading platforms that do not operate on the same scale as the Tel Aviv Stock Exchange, and have unique features or designated purposes, such as trading platforms designated for sophisticated investors (such as insurance companies, pension funds, and banking corporations) or platforms that use novel technologies (such as blockchain technology).

The establishment of one or more designated exchanges with such unique features is designed to expand the investment options available to the public, and the financing options of companies that seek to finance their operations using outside sources. Creating new financing channels for a broad range of corporations is important for the economy, especially in view of the coronavirus crisis, which heightened the need for financing solutions to support businesses’ efforts to return to activity after the economy’s closure. Furthermore, the establishment of designated exchanges will also expand the exposure of Israel’s public investors to additional investment sectors such as high-growth companies in the high-tech sector, to which the major exchange offers limited access.

The proposed amendment will permit the Authority, subject to approval of the Minister of Finance, to exempt an entity that wishes to operate a designated exchange from the requirements that apply to stock exchanges, in entirety or in part, and stipulate conditions for such exemption. Public investors’ interests will be protected by restricting the scope of operations of designated exchanges and imposing full supervision on them, and by defining the appropriate conditions and requirements for designated exchanges and the companies trading on them. It is further proposed to amend the Companies Law 5759-1999 (“the Companies Law”) to authorize the Minister of Justice to exempt, after consulting with

the Authority, companies registered for trading on a designated exchange from the provisions of the Companies Law that apply to public companies or private companies that are Debenture Companies as defined in the Companies Law, where such provisions would apply as result of a company's registration on a designated exchange.

C. Main points of the proposed law

Point 1 - Establishment of a designated exchange

It is proposed to lay the legislative foundation for the establishment and operation of a designated exchange in Israel.

Point 2 - Relaxation of requirements applicable to stock exchanges and corporations whose securities are traded on them

It is proposed to authorize the Authority to exempt, subject to approval of the Minister of Finance, designated exchanges or companies that apply for a stock exchange license in order to establish and manage a designated exchange, from the provisions of Chapter Eight of the Securities Law, either in entirety or in part, and to stipulate conditions for such exemptions. In granting such exemptions, the Authority will consider, among other factors, the fair and proper conduct of the designated exchange, the type of investors who have access to it, and the impact of the exemption on capital market activity. It is further proposed to authorize the Authority, subject to approval of the Minister of Finance, to issue exemptions from the provisions of the Securities Law, either in entirety or in part, to corporations whose securities are listed on a designated exchange.

Point 3 - Relaxation of corporate governance rules

It is proposed to authorize the Minister of Justice to determine, after consulting with the Authority, that the provisions of the Companies Law applicable to public companies or private companies that are Debenture Companies as defined in the Companies Law, will not apply, either in entirety or in part, to companies whose issued securities are registered for trading on a designated exchange, if these provisions would apply to them as a result of their registration for trading on the designated exchange.

D. The effects of the Proposed Memorandum of Law on the budget and the staffing needs of the initiating office, other government ministries, and other authorities

The proposed amendments are not expected to have an effect on the State budget, or on the staffing needs of the Ministry of Finance or the Authority.

E. The text of the Memorandum of Law and explanatory notes.

Proposed Law submitted by the Ministry of Finance

Memorandum of Securities Law (Amendment No. ____)(Designated Exchange) 5780-2020.

Amendment to Section 1 1. In the Securities Law 5728-1968¹ (“Main Law”), the following definition will be added after the definition of a “Stock Exchange Abroad”:

“‘Designated Exchange’ - A company that was issued a license to set up and manage a system for trading in securities pursuant to Sections 45 and 51A, and whose operations are limited to one of the following modes:

- (1) A stock exchange in which trading is restricted exclusively to investors listed in Schedule One;
- (2) A stock exchange with novel operating features, including trading technologies or trading infrastructure, which contribute to innovation and to the development of advanced infrastructure;
- (3) A stock exchange that should be considered a designated exchange due to the scale of its trading volumes, or the number or value of its traded corporations, or due to the type of securities traded on it, as determined by the Authority, subject to the approval of the Minister of Finance.”

Addition of Section 51A 2. The following will be added after Section 51 of the Main Law:

¹ Book of Laws 5728, p/ 234; 5779, p. 63.

- “Exemption for the operations of a designated exchange 51A (a) The Authority may, subject to approval of the Minister of Finance, exempt a designated exchange and a company that applies for a stock exchange license in order to set up and manage a designated exchange, from the provisions of this Chapter, either in entirety or in part, and may stipulate conditions for said exemption. In granting such exemption, the Authority will take into consideration, among other factors, the fair and proper conduct of the designated exchange, the types of investors, and the exemption’s impact on capital market activity.
- (b) The provisions of this Law will apply to corporations whose securities are traded on a designated exchange and to activities involving the securities of said corporations. The Authority may, subject to the approval of the Minister of Finance, exempt them from the provisions of this Law, either in entirety or in part, and may stipulate conditions for said exemption. Said conditions may be determined with respect to a specific corporation or to a class of corporations.
- (c) This section also applies to a stock exchange with respect to its activities as a designated exchange.”

Amendment
to the
Companies
Law

3. Companies Law 5759-1999,² the following will be added after Section 365A:
“Chapter 5B: Restrictions Applicable to Companies Traded on a Designated Exchange

² Book of Laws 5759, p. 189

Restricted Application	365B The Minister may determine, after consulting with the Authority, that the provisions of this Law that apply to public companies or to private companies that are Debenture Companies, will not apply, either in entirety or in part, to companies registered for trading on a designated exchange, as this term is defined in the Securities Law, whether in general or to specific classes of companies, under such terms as will be determined.”
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F. Explanatory notes

General

The provisions of the Securities Law 5728-1968 (“the Securities Law”) concerning stock exchange licensing and supervision envisioned a major national stock exchange that is a central force in the Israeli’s capital market due to its large trading volumes and impact on Israel’ economy. For example, in line with the exchange’s unique role and focal position in the capital market, these provisions impose on the stock exchange a set of detailed and significant obligations concerning its corporate governance and its officers. Consequently, several of regulatory requirements that apply to a stock exchange under Chapter Eight of the Securities Law may impede the establishment of smaller trading platforms that offer unique trading features.

One of the aims of the Authority is to advance the capital market in Israel by expanding the investment and trading options available to investors, and increasing the diversity of services and products offered and the technologies in use. To this end, the Authority wishes to promote securities trading activities on trading platforms that operate on a smaller scale than the Tel Aviv Stock Exchange and offer unique features or are designed to fulfill a designated purpose, such as a stock exchange exclusively for sophisticated investors (which may be insurance companies, pension funds, and banking corporations) or platforms that operate using novel technological infrastructure such as blockchain technology.

The establishment of such designated exchanges with unique features is designed to expand the capital market investment options available to the public, and the financing options of companies that seek to finance their operations through outside sources. Creating new financing channels for various corporations is important for the economy, especially in view of the coronavirus crisis and the need to devise financing solutions for businesses in support of their efforts to return to activity after the economy’s closure. Furthermore, the establishment of designated exchanges in Israel will also increase the public’s exposure to additional investment sectors such as high-growth companies in the high-tech sector, to which the main exchange offers limited access.

In contrast to Israel, regulation in the United States and in the European Union refers to two types of multilateral trading systems that differ mainly in their branding and degree of regulatory supervision. One class of multilateral trading systems includes large exchanges with extensive trading volumes, which are fully regulated by the authorities and subject to strict regulation. The second class of multilateral trading systems includes alternative trading platforms that are smaller enterprises, with typically more modest trading volumes. Separate regulation and supervision exists for these platforms, and the transparency and regulatory requirements that apply to them are more lenient.

For these reasons, it is proposed to lay the foundation for the establishment of designated exchanges in Israel by removing the barriers and adjusting existing regulation to companies whose securities will be registered for trading on these platforms, among other measures, without compromising on the protection of public investors and proper conduct of trading.

The proposed amendment will permit the Authority, subject to approval of the Minister of Finance, to exempt an entity that wishes to operate a designated exchange from the requirements that apply to stock exchanges, in entirety or in part, and to stipulate conditions for such exemption. Public investors' interests will be protected by restricting the scope of operations of designated exchanges and imposing full supervision on them, and by defining the appropriate conditions and requirements for designated exchanges and the companies trading on them. It is further proposed to amend the Securities Law to authorize the Minister of Justice, after consulting with the Authority, to exempt companies listed for trading on a designated exchange from the provisions of law that apply to public companies or private companies that are Debenture Companies as defined in Section 1 of the Companies Law, where such provisions would apply to such companies as result of their registration on a designated exchange.

Section 1

It is proposed to define a “designated exchange” as a company that was issued a stock exchange license under Sections 45 and 51A, and operates in one of three modes listed in the definition. In the first type of designated exchange, investors are limited to accredited investors only. In this type of exchange, investors may only be those entities listed in Schedule One of the Securities Law (e.g., insurers, pension funds, and banking corporations). The second type of designated exchange is an exchange that offers novel operating features, such as novel trading technology or trading infrastructure, which contribute to innovation and development of advanced infrastructure. This definition implements the recommendation of the Authority's Committee for Promoting and Institutionalizing Digital Markets in Israel. According to the Committee's January 2020 report,³ which focused on distributed ledger technology (DLT), the adoption of this technology potentially reduces trading costs to end-customers, reduces systemic risks for the economy, and cultivates a technological environment that encourages financial innovation, and increases the capital market's access to companies such as SMEs that

³ See http://www.isa.gov.il/הודעות2019/פרסומים/Reports/177/Documents/digital_markets.pdf

previously refrained from using the public capital market for their financing needs. The report stated that measures should be taken to remove regulatory barriers to the use of technologies that hold a promise of significant added value and support the development of a digital market in Israel. The third type of designated exchange is an exchange that is so designated exchange by the Authority, subject to the approval of the Minister of Finance, due to its trading volumes, number or value of its trading corporations, or type of securities traded on it. This definition corresponds to the situation in the United States and the European Union, where regulation distinguishes between two types of multiparty trading systems that differ mainly in their branding and degree of regulation.

Section 2

Chapter Eight “B” of the Securities Law defines rules for licensing and ongoing operations (including corporate governance) of stock exchanges. These rules, which were mainly enacted in Amendment no. 63 to the Securities Law 5777-2017, envisioned a major national stock exchange. Therefore, several of these rules are not appropriate for designated exchanges, whether the designated exchange is established as an independent entity or in linkage to the Main Exchange. It is therefore proposed to add Section 51A to the Securities Laws, and authorize the Authority to exempt, subject to the approval of the Minister of Finance, a designated stock exchange or company that applies for a license to operate a designated exchange from the provisions of the Law that apply to exchanges, either in entirety or in part, and to stipulate the conditions of said exemption. In granting such exemptions, the Authority will consider, among other factors, the fair and proper conduct of the designated exchange, the type of investors it, and the impact of the exemption on capital market activity. It is further proposed to authorize the Authority to issue, subject to approval of the Minister of Finance, exemptions from the provisions of the Securities Law, either in entirety or in part, to corporations whose securities are traded on a designated exchange.

Section 3

In an indirect amendment to the Companies Law it is proposed to authorize the Minister of Justice, after consulting with the Authority, to determine reliefs from the provisions of the Companies Law that apply to companies registered for trading on a designated exchange, according to the definition proposed for inclusion in Section 1 of the Securities Law. For example, in designated exchanges limited to small enterprises, certain requirements that apply to public companies may be relaxed. Notably, the Companies Law grants similar authority in other contexts.