

Banking Corporation Business with Related Parties

Introduction (07/14)

1. In order to minimize risks arising from transactions by a banking corporation with related parties, banking corporations shall act in accordance with the provisions of this Directive.
The objective of this Directive is to limit the extent of indebtedness of related parties to the banking corporation and to ensure that transactions between a banking corporation and related parties are undertaken on an arm's-length basis, in accordance with commercial terms that are not preferential to similar transactions with unrelated parties.
- 1a. To eliminate doubt, it is stated for clarity that these provisions supplement the Companies Law, 5759-1999 (hereinafter, "the Companies Law").

Application (07/14)

2. (a) This Directive shall apply to a banking corporation as this term is defined in the Banking (Licensing) Law, 5741-1981 (hereinafter, the Banking (Licensing) Law), excluding a joint services company.
(b) The Directive shall also apply to a corporation as specified below as if it were a banking corporation—a corporation as stated in Sections 11(a)(3a) to (3b) and 11(b) of the Banking (Licensing) Law that is incorporated in Israel and controlled by a banking corporation.
(d) This Directive shall not apply to a contractual arrangement of a banking corporation relating to terms of service or employment that were set forth under the provisions of Directive 301A.

Definitions (07/16)

3. A "**related party**" vis-à-vis a banking corporation is—
 - (a) anyone who has a controlling interest in the banking corporation, a candidate, and a relative of either of these;
 - (b) a corporation in which those listed in Paragraph (a) control or hold more than 10 percent of any means of control, and a corporation in which the foregoing corporation holds more than 50 percent of any means of control.

- (c) the holder of more than 5 percent of any means of control in the banking corporation or in a banking corporation that controls said banking corporation, and his/her relative; With regard to this subsection only—excluding one who received a holding permit subject to the terms established in the Banking Supervision Department letter dated June 16, 2016 on the issue of “Bank-holding permits for institutions managing customers’ money—policy update”.
- (c1) a person who has nominated (on his own or as a member of a group of holders) a candidate to serve as a director in a banking corporation without a controlling core, and his/her relatives. The classification as a related party shall remain in effect as long as the director nominated by him/her holds the position.
- (d) an officer of the banking corporation, or of one of the following: a corporation that holds the means of control of the banking corporation’s controlling group, as defined in Section 5, or of a corporation as set forth in Subsection (c), and his/her relative;
- (e) a corporation controlled by those listed in paragraphs (c)–(d);
- (f) a corporation that the banking corporation controls or in which it holds more than 10 percent of any means of control, and a corporation controlled by a corporation noted in the beginning section;
- (g) a party that holds 10 percent or more of any type of means of control in a corporation controlled by the banking corporation, and his/her relative;
- (h) any party whom the Supervisor of Banks defines as a related party, generally or in a specific case.

“Credit” - As defined in Proper Conduct of Banking Business Directive 313, “Limitations on the Indebtedness of a Borrower and Group of Borrowers” (henceforth—Directive 313);

“Housing loan” As defined in Directive 451, provided that said loan is not issued for investment purposes;

“Capital” - Tier 1 capital after regulatory adjustments and deductions as defined in Proper Conduct of Banking Business Directive 202;

“Indebtedness”- As defined in Directive 313, including credit from deposits in which payment to depositor is contingent upon the collection of the credit; however, for the purpose of a guarantee given by a related party on behalf of the banking

corporation to secure credit extended to a third party by the banking corporation, the following provisions shall apply to the definition of indebtedness:

- (a) If the guarantee was given to secure credit extended to an unrelated party, the entire guarantee shall be viewed as part of the indebtedness;
- (b) If the guarantee was given to a secure credit extended to a related party, the guarantee shall not be included in the indebtedness;

“Group of holders” As defined in Section 11d of the Banking Ordinance, 1941;

“Candidate” - A person who has applied to the Governor for a permit to control a banking corporation, either individually or in conjunction with others, where the Supervisor has served the relevant banking corporation with notice thereof;

“Officer” - As defined in the Companies Law;

“Transaction” - As defined in Section 1 of the Companies Law;

“Relative” - As defined in the Banking (Licensing) Law except for the purposes of sections 3(c), 3(c1), 3(d), 3(g), and 5(b)(4). For the purposes of sections 3(c), 3(c1), 3(d), 3(g), and 5(b)(4): spouse, offspring, and dependent.

3a. Policies and procedures (07/14)

- (a) The board of directors shall set out policies and processes for the approval of transactions with related parties, as well as procedures for monitoring, control, reporting, and follow-up of material transactions with related parties after receiving a recommendation from the Audit Committee or the Committee for Transactions with Related Parties in the relevant matters. Without derogating from the foregoing, the provision of credit to a related party in an amount exceeding 0.5 percent of the capital of the banking corporation, or a transaction of a different type in an amount that the board of directors shall determine, shall be reported to the full board of directors in its next meeting.
- (b) The board of directors shall establish guidelines for cases in which an officer in a banking corporation has a personal conflict of interest concerning a transaction of the kind noted in Section 56(c) of Proper Conduct of Banking Business Directive number 301 (hereinafter: “Directive 301”).

Transactions with related parties (7/14)

4. (a) A banking corporation shall not enter into a transaction with a related party on terms that are preferential to those it offers others in similar transactions.
- (a1) A banking corporation shall not accept securities issued by itself as collateral for a related party's indebtedness, and if said related party has a controlling interest in the banking corporation, it shall also not accept securities issued by said possessor of controlling interest or by the corporation that he/she controls.
- (b) This Section shall not apply to a corporation in which the banking corporation holds 95 percent or more of means of control and that does not extend credit or any other service to persons outside the banking group. For this purpose, a "banking group" comprises the banking corporation and banking corporations under its control.

Restrictions on indebtedness of related parties (7/14)

5. (a) The aggregate indebtedness of all related parties to the banking corporation shall at no time exceed 10 percent of the banking corporation's capital.
- (b) (1) The indebtedness of a related party who is a member of a controlling group shall not exceed the product obtained by multiplying said member's share in the core holding by 10 percent of the banking corporation's capital.
- (2) The indebtedness of a related party (other than a member of a controlling group) that holds 5 percent or more of any means of control in the banking corporation, or in a banking corporation that controls said banking corporation, and also, in banking corporations that have no controlling core, the indebtedness of a party that has nominated (on his/her own or as a member of a group of holders) a candidate to serve as a director, where the director-nominee is serving in the position, shall not exceed 5 percent of capital at any time;
- (3) The indebtedness of any related party that holds 10 percent or more of any means of control in a corporation that the banking corporation controls shall not exceed 5 percent of capital at any time (except corporations controlled by the holder);
- (4) The indebtedness of a related party who is an officer of the banking corporation, with the exception of a housing loan, shall not exceed NIS 1 million at any time. This Subsection shall not apply to a holder of means of control who serves as a director of the banking corporation.

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For the purpose of this Section:

“Controlling Core” - The smallest share of means of control in the banking corporation that the group must hold as stated in the control permit issued to the members of the group and, if not stated, such a share as the Supervisor of Banks determines;

“Indebtedness” - Indebtedness, as defined in Section 3, of that member of the group, together with his/her relative and corporations controlled by him/her or by his/her relatives;

“Controlling Group” - A group of people that has a permit allowing it to control and possess means of control in a banking corporation.

- (c) In calculating the collective indebtedness of related parties to a banking corporation, the following shall not be included:
- (1) the State and any sovereignty that may be assigned a zero risk weight under sections 53–56 of Proper Conduct of Banking Business Directive 203;
 - (2) a candidate and a related party who is considered such only due to his/her proximity to the candidate (a relative of the candidate, corporations held by him/her, corporations holding him/her, etc.);
 - (3) a banking corporation;
 - (4) a corporation belonging to the same group of bank borrowers to which the banking corporation belongs in the sense of Directive 313;
 - (5) a “controlled group of borrowers” in the sense of Directive 313.

Deductions ^(7/14)

6. For the purpose of Section 5, the items specified in Section 5 of Directive 313 shall be deducted from the amount of indebtedness.

Approval of transactions with related parties ^(7/14)

7. (a) Transactions with a related party as specified below require documented approval of the Audit Committee or of the Committee for Transactions with Related Parties, appointed in accordance with Directive 301, as the case may be:
- (1) Any transaction undertaken with a related party in which one of the following conditions is present:

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- (a) The related party's total indebtedness exceeds NIS 100,000 or 0.1 percent of the banking corporation's capital, whichever is greater (henceforth—the "minimum amount");
 - (b) As a result of the transaction, the related party's total indebtedness exceeds the minimum amount.
- (2) Any indebtedness transaction undertaken with an individual related party in a sum that exceeds NIS 500,000; with an officer of the banking corporation, or of a corporation controlled by such or by his/her relative, in a sum that exceeds NIS 250,000;
 - (3) Any sale or lease transaction with a related party in a sum that exceeds the minimum amount;
 - (4) Any other transaction with a related party, if no amount has been set in respect thereto, or if the amount exceeds an amount fixed by the board of directors, provided the amount does not exceed the minimum amount; in respect of deposits and account management terms, no specific approval is required if the conditions were set forth under a long-term framework agreement;
 - (5) A provision for, or the writing-off of, a debt of a related party.
- (b) The Committee for Transactions with Related Parties or the Audit Committee shall discuss transactions undertaken by a related party with the banking corporation before the person became a related party if the outstanding amount at the time he/she became a related party exceeds the amounts requiring approval under sections (1)–(4).
If the Committee reaches the conclusion that the transaction size exceeds the permitted amount for a related party, or that its terms deviate from market terms, and for reasons of legal liability it is unable to annul or alter its terms, the chair of the committee shall inform the Supervisor of Banks via the secretary of the banking corporation.
- (c) The approval specified in Subsection (a) shall also include certification that the transaction does not contravene the terms of Section 4 of this Directive; the minutes of the discussion shall include the explanations given to the committee to verify the foregoing.

Personal conflict of interest (7/14)

7a. An officer who has a direct or indirect personal interest in an existing or proposed transaction of the banking corporation that is taken up for discussion, or in a decision that is about to be made, shall act as set forth in sections 56(a) and 56(b) of Directive 301, *mutatis mutandis*, no later than at the board meeting where the transaction is first discussed.

A related party who is an employee (4/97)

8. These provisions shall not apply to a transaction with a related party undertaken by a banking corporation, if said related party is an employee of the banking corporation and the transaction is implemented in the ordinary course of business and does not exceed the proportion specified for this purpose in a collective labor agreement or collective arrangement that applies to the employees of the banking corporation.

Reporting to the Banking Supervision Department (7/14)

9. (a) A banking corporation shall present the Banking Supervision Department with a list of all related parties and the indebtedness of each, using the reporting format specified in the Reporting to Banking Supervision Directives. The banking corporation shall also keep such a list in its offices and update it whenever necessary.
- (b) A banking corporation shall submit an immediate report to the Banking Supervision Department in the event of a deviation that occurs in accordance with Section 7(b).

General provisions (7/14)

10. The Supervisor of Banks, when there are special reasons to do so and it is seen as correct, may take the following actions:
- (a) Authorize an “exception” of a related party from the definition or excuse him/her from having to comply with certain sections of the Directive, for such a period or under such conditions as shall be determined;
- (b) Determine that a transaction with a related party was carried out under conditions that deviate from market conditions and have the indebtedness on its account deducted from regulatory capital.

Deviation due to classification as a related party

11. Indebtedness of a related party that was created before he/she became a related party and exceeds the limit established in Section 5(b) shall be settled gradually over a two-year period. This shall also apply due to circumstances beyond the bank's control, such as corporate mergers and acquisitions.

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Updates

Circular 06 no.	Version	Details	Date
1508		Original circular	March 10, 1991
—	1	Placement among Proper Conduct of Banking Business Directives	Aug. 1991
1528	2	Update	Nov. 4, 1991
1616	3	Update	Jan. 3, 1993
1701	4	Update	April 4, 1994
—	5	Revised version of Proper Banking Conduct file	Dec. 1995
1868	6	Update	April 30, 1997
1882	7	Update	Aug. 3, 1997
1933	8	Update	June 30, 1998
2277	9	Update	Oct. 19, 2010
2425	10	Update	July 10, 2014
2516	11	Update	Sept. 29, 2016