



February 1, 2017

**Circular no. C-06-2527**

Attn:

**Banking corporations and credit-card companies**

**Re: Debt Collection Proceedings**

(Proper Conduct of Banking Business Directive no. 450)

**Introduction**

1. A customer who takes a loan from a banking corporation must repay it under the terms set forth in the agreement between the customer and said corporation. Insofar as a customer fails to honor his or her undertakings and repay the loan systematically, a banking corporation may launch legal proceedings against the customer to collect what it is owed. Before doing so, however, it is expected to try to exhaust, insofar as is possible, other methods of collection such as rescheduling, grace, and so on.

Accordingly, this Directive is meant to regulate the actions that should be taken to enhance fairness and transparency in collecting debts from customers who fail to honor the terms of their loans and to effect payback systematically. This is because fairness and transparency are needed not only when a loan is given but also when debt collection becomes necessary before and even after the onset of legal proceedings.

The promulgation of a directive specifically devoted to debt-collection proceedings reflects the importance that the Banking Supervision Department attributes to the fairness, respect, and transparency that banking corporations must display at all stages of debt-collection proceedings vis-à-vis customers who fail to honor the terms of their loans.

After consulting with the Advisory Committee on Banking Business Affairs and with the approval of the Governor, I hereby establish this Directive.

**Main provisions of the Directive**

2. Sections 7–9 of the Directive concern the requirement of establishing a function for the handling of debt collection, the duties and powers of said function, and the responsibility of the banking corporation's management and Board of Directors for its work.

**Explanation**

The Directive mandates the establishment of a dedicated function for the handling of debt collection and the appointment of an executive to manage it. The function shall be given various powers in order to ensure appropriate treatment by the banking corporation of debt-collection proceedings, carrying out the requisite actions for this purpose in accordance with the law and maintaining fairness in customer–banking corporation relations. The Directive also determines the duties of senior management and the Board of Directors in this regard, so that they are aware of and involved in the banking corporation's conduct in the debt-collection

process. It is stated for clarity that the Directive does not rule out the existence of several debt-collection functions, each dedicated to a different activity segment.

3. Sections 10–11 of the Directive determine the maximum penalty interest rate and the indexation mechanism of a loan. According to these sections, the penalty interest rate on a loan at the time the loan is taken shall not exceed the maximum interest rate that the banking corporation charges for exceeding the credit facility in a current/overdraft account, in accordance with the banking corporation’s notice about changes in credit cost under Addendum B of the Banking (Customer Service) (Proper Disclosure and Presentation of Documents), 5752-1992. Insofar as further law exists in this matter, the penalty interest rate shall be the lower of the two. It is also determined that a banking corporation shall have control neither over setting the base interest rate that is used to calculate the penalty interest formula nor over the indexation base; instead, both shall be based on a benchmark that is made known to the public under law or by custom.

#### **Explanation**

The interest cap is meant to prevent a state of uncertainty surrounding the interest rate that a banking corporation may charge. Said maximum interest rate must be transparent and accessible to the customer and shall be determined in accordance with the definition of the customer with the banking corporation as private or business. For credit-card companies, the maximum rate shall be set at the maximum interest rate charged by the parent corporation.

4. Sections 12–13 of the Directive concern requisite proper disclosure to the customer and determine that a banking corporation must note, in the loan agreement or in a complementary document (hereinafter: the loan agreement) the formula used to calculate the penalty interest rate on the loan and the indexation mechanism. Furthermore, the banking corporation must, to the best of its ability, advise the customer of the possible implications of delinquency for him or her, in ample time for him or her to be able to avoid this outcome. When a settlement between the parties is executed, a banking corporation shall note its possible implications for the customer and shall give him or her a copy of the settlement after he or she signs it.

#### **Explanation**

To ensure that when a customer takes a loan he or she is aware of the penalty interest rate and the possible financial implications for him or her of failure to make systematic payback, a banking corporation must disclose to the customer at the initial stage of the relationship, i.e., in the loan agreement, the formula that it used to calculate the penalty interest rate on the loan. In cases where the balance in a current account that lacks an approved and agreed-upon credit facility becomes negative for an unpreventable reason, said proper disclosure shall take place by means of a notice to the customer about the overrun.

Furthermore, given the possible future implications of delinquency, it is important to disclose said implications to the customer in good time so that he or she may consider what to do and take appropriate actions. At the time a settlement is drawn up, too, it is important to advise the customer of its possible implications for him or her, e.g., those concerning the possibility of renewing bank–customer relations in the future.

It is also determined that the customer must be given a copy of the debt settlement, insofar as the parties sign one, in order to ensure certainty and transparency in regard to its terms.

5. Sections 14–17 of the Directive concern notices and warning letters. Banking corporations must send delinquent customers a notice that includes relevant details. It is also determined that the frequency of sending notices and warning letters to a customer due to delinquency in repaying a loan shall be proportional and commensurate with the circumstances the case at hand.

**Explanation**

It is determined that a banking corporation must serve notice shortly after the debt is created. Said notice shall include information about the debt and the provisions of Section 16(a)(5) of the Credit Data Services Law, 5662-2002, or of its replacement, the Credit Data Law, 5676-2016, as well as information on how to approach the banking corporation in any matter relating to the debt in arrears.

Before the handling of a debt is passed on to the banking corporation’s agent or debt-collection function, whichever occurs earlier, the banking corporation shall advise the customer of this step, attaching the information specified in Section 15, with the contact details in the notice being those of the debt-collection function.

Further notices and, in turn, warning letters ahead of the onset of legal proceedings, if such become necessary, shall be proportional and commensurate with the circumstances of each case.

6. Sections 18–19 of the Directive concern customer access to information. Banking corporations must give customers access to information and notices received via the electronic means through which the customers generally received notices before the customer became indebted to the banking corporation and/or before the banking corporation transfers the handling of the debt to its agent and/or before it begins legal proceedings against a customer on account of his or her debt. The banking corporation must also allow the customer to contact it directly in regard to the debt and to receive information about his or her account at each stage of the debt-collection proceedings.

**Explanation**

The Directive determines the requirement of providing information to the customer so that she or he will have all data pertaining to her or his debt is. The fact that collection proceedings have been brought against a customer shall not deprive the customer of access to information formerly sent to him or her in electronic ways before the proceedings against him or her were launched, and shall not preclude her or him from receiving up-to-date information about the debt directly from the banking corporation at her or her request, like any customer, and under the accepted terms between them, even if the treatment of said debt has been handed over to the banking corporation’s agent. For the sake of clarity, it is explained that the information at issue concerns the customer’s activity in his or her account, to which he or she would be entitled even if the legal proceedings not been initiated.

Furthermore, customers may approach the banking corporation or the debt-collection function directly even if represented by an attorney.

7. Sections 20–21 relate to payments that are made in order to retire or reduce the customer’s debt.

### **Explanation**

It is determined that the date of a payment that is made for the purpose of retiring or reducing the customer's debt shall be the determining date in debt-collection proceedings. This is meant to prevent a situation in which a debtor who is paying off his or her debt is forced to pay an additional sum because of lack of update as aforesaid.

Additionally, the Directive mentions two events of special importance to a customer who is in the midst of a debt-collection proceeding: drawing up a settlement and repaying the debt in full. For the customer to be able to plan his or her steps optimally, she or he must be shown not only the balance of the debt as recorded in the bank's books but also information about said balance in accordance with the latest records at the Execution Office. The banking corporation shall present this information as well except in cases of technical mishaps that render said information inaccessible. The information shall be given to the customer at no charge because it is accessible to the banking corporation as the creditor and does not entail any payment whatsoever.

Furthermore, to allow the customer to check the way the debt was calculated, the banking corporation, on the aforementioned dates, shall present the customer, at his or her request, with a breakdown of the method used to calculate the debt.

8. Sections 22–24 of the Directive regulate banking corporations' conduct in Execution Office proceedings.

### **Explanation**

The penalty interest rate that the banking corporation reports to the Execution Office shall accord with the penalty interest rate that appears in the loan agreement or in a court order.

Additionally, when a banking corporation applies to the Execution Office to open a file, it shall attach to its application a copy of the loan agreement, the court order, or the document, as the case may be, with clear reference to the sections that specify the relevant penalty interest formula and indexation mechanism. If support documentation for the penalty interest formula or the indexation mechanism is lacking, the banking corporation may present an institutional record concerning these details in accordance with the terms established by law.

To eliminate doubt, it is explained that this provision also applies to loans taken before this Directive goes into effect and for which Bailiffs Office proceedings are launched after the Directive goes into effect, even if the loan agreement does not specify the penalty interest formula and the indexation mechanism. In these cases, the banking corporation shall specify in its application to open the Execution Office file the formula used to calculate the penalty interest and the indexation mechanism, and shall attach support literature in respect thereto.

It is also determined that a banking corporation must monitor the opening of Execution Office files against customers and ensure that the data in the files are correct.

9. Sections 25–26 of the Directive determine compulsory reporting by a banking corporation to the Execution Office about sums received by the banking corporation on account of debts by means other than the Execution Office, and the execution of an arrangement with a customer concerning the receipt of sums by means other than the Execution Office and sums received within the framework of the arrangement.

**Explanation**

The requirements in reporting to the Execution Office as established in this Directive resemble those set forth in this matter under the Execution Office Law, 5727-1967. In this Directive, however, compulsory reporting is extended to receipts obtained under an arrangement concluded between a banking corporation and a customer within seven days of the day of receipt. Also, banking corporations are required to advise the Execution Office of an arrangement concluded with a customer within a reasonable time of its being signed, in order to ensure that sanctions are not brought against the debtor within the framework of the Execution Office file as long as he or she honors the arrangement. To eliminate doubt, it is explain that said compulsory reporting in these sections applies to receipts obtained both by the banking corporation and by means of its agent. Insofar as the banking corporation avails itself of an agent to carry out the reportage, its responsibility to ensure that said reportage is in compliance with the Directive is even greater.

10. Sections 27–31 of the Directive define the supervision and control measures that a banking corporation must take vis-à-vis its agents.

**Explanation**

In these sections, it is determined that a banking corporation must impose supervision and control over agents whom it appoints to begin collection proceedings against a client. It shall do so, *inter alia*, by documenting instructions that it presents to its agents and by staying abreast of actions taken against customers. It is also determined that a banking corporation must take appropriate actions to keep itself apprised of all material information that the customer gives its agent, including a request by the customer to settle a debt in arrears, so that it may examine the customer's request on its merits.

A banking corporation shall produce an annual report about customer debts that it has handed over to its agents for treatment, in order to allow said debts to be monitored and to ensure that their collection has been handled appropriately.

At least once every three years, a banking corporation shall audit each agent that it has appointed to deal with debt collection by means of an external CPA or an internal auditor, and shall present said audit report to the debt-collection function. A condensed presentation of the findings of the annual reports, audit reports, and actions taken shall be inserted into the function's periodic report to the management of the banking corporation.

11. Sections 32–34 of the Directive regulate the fee that a banking corporation's agent may charge for legal proceedings and other legal expenses, and refer to compulsory disclosure of the fee in the event of the conclusion of a compromise settlement.

**Explanation**

The matter of the fee that a banking corporation's agent may charge when it launches legal proceedings found expression in Proper Conduct of Banking Business Directive no. 409 and is inserted into the Directive presented herewith.

It is also determined that a banking corporation must specify the fee of its agent and/or that of a receiver within the framework of a compromise settlement, which must be presented to the customer before she or he signs it.

12. Section 35 of the Directive specifies the periodic notices that a banking corporation must send to a customer who is in the midst of legal proceedings and against whom a file with the Execution Office has been opened.

**Explanation**

To enable a customer to keep track of his or her payments on account of a debt and to receive periodic information about the balance, a banking corporation must send him or her an annual notice with data on the debt and ways of contacting the relevant player at the corporation's debt-collection function. This information is especially significant when the Execution Office instigates the debt-collection proceeding and invokes the enforcement tools available to it. To eliminate doubt, it is explained that this periodic notice is not a service included in the Banking (Customer Service) (Fees) Rules, 5768-2008, and that, therefore the customer shall not be charged a fee for it.

**Effective date**

13. This Directive shall go into effect on the day of its promulgation.

**Incidence**

14. This Directive also applies to loans given before it goes into effect. It is stated for clarity that the relevant provisions of the Directive shall apply to actions taken after the Directive goes into effect.

In reference to Section 10 of the Directive, if the interest rate on arrears determined in said Section is lower than the contractual interest rate on arrears, it shall apply only to the portion of the loan that is delinquent from the date on which this Directive goes into effect and onward. Furthermore, the interest rate on arrears established in this Section shall not apply in cases where an interest rate is set by court order before the Directive goes into effect.

**Indirect amendments**

15. Proper Conduct of Banking Business Directive no. 409 (Charging Customers for Legal Fees) shall be void from the effective date of the Directive presented herewith. (Its content is integrated into the Directive presented herewith.)

**Update of file**

16. Update pages for the Proper Conduct of Banking Business Directive file are attached. The provisions of the update follow.

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Respectfully,

Dr. Hedva Ber  
Supervisor of Banks