

Banking Supervision Department

Jerusalem, October 31, 2022

Circular No. C-06-2727

Attn: The Banking Corporations and Merchant Acquirers

Re: The Liquidity Coverage Ratio and Net Stable Funding Ratio

(Proper Conduct of Banking Business Directive No. 221 and 222)

Introduction

1. In view of the experience accumulated since the implementation of the Liquidity Coverage Ratio in Israel and in view of the scope of activity in operational deposits at banks in selected countries vis-à-vis the activity in Israel, the Banking Supervision Department has decided to update the policy regarding the recognition of operational deposits in the Liquidity Coverage Ratio.
2. In Proper Conduct of Banking Business Directive no. 222, a technical change was made, due to the change in Proper Conduct of Banking Business Directive no. 203, which included shifting the coverage of counterparty credit risk to Proper Conduct of Banking Business Directive no. 203A.
3. After consulting with the Advisory Committee on Banking Business Affairs, and with the approval of the Governor, I have amended Proper Conduct of Banking Business Directive no. 221 and Proper Conduct of Banking Business Directive no. 222 as follows.

Update of Proper Conduct of Banking Business Directive no. 221

4. The following details, regarding the process of approval by the Supervisor, were added to the latter part of Section 93 of the Directive:
 1. In its application to the Supervisor of Banks regarding operational deposits, the banking corporation shall attach, among other things, the following details:
 - (a) The banking corporation's policy on the issue, and the methodology it formulated;
 - (b) Information on the manner of implementing the conditions and limitations in Sections 93 and 93a, including the controls over it;
 - (c) Notice by the Chief Risk Officer that the issue has been examined and approved by him; and
 - (d) Notice by the senior management that the issue has been approved by it.
 2. The Banking Supervision Department shall examine the reasonability of the request and the completeness of the details that the banking corporation is required to submit as noted above. The Supervisor may request information, documents, or clarifications from the banking corporation. The Supervisor of Banks shall provide the banking corporation his decision no later than 60 days from the date of receiving all the information required from the banking corporation for the purpose of the examination. If the Supervisor of Banks decides not to allow the

banking corporation to recognize operational deposits, he shall provide a reasoned decision.

5. Section 93a—regarding limitations on recognizing operational deposits—was added:

- (a) Ceiling on operational deposits from a single entity.
- (b) Ceiling on aggregate operational deposits.
- (c) Operational deposits shall not be recognized for entities whose activity is sensitive to market changes and for which it cannot be assumed that their deposits will remain at the banking corporation in a stress scenario.

6. Section 93b, which deals with coverage of the issue by the banking corporation's Internal Audit function, was added.

7. Section 93c, which deals with a specific arrangement regarding a banking corporation that received the Supervisor's approval to recognize operational deposits prior to the publication of this circular, was added.

Explanatory remarks

The Banking Supervision Department reexamined the issue of recognizing operational deposits in the Liquidity Coverage Ratio and found it suitable to update the policy on the issue, in view of comparison of the actual implementation in selected countries abroad. The process will include transferring preliminary information to the Supervisor of Banks, as detailed in the Directive, and the establishing of limitations on the scope of the recognition of operational deposits and the types of entities from which operational deposits will be recognized. The limitations regarding the scope of recognition of operational deposits are intended to reduce concentration, both from the perspective of reliance on a single source of liquidity and from the perspective of the total recognition of operational deposits. In regard to a single institutional source of liquidity ("the same entity"), see the definition of "institutional investor" in the Banking (Licensing) Law, 5741-1981.

Update of Proper Conduct of Banking Business Directive no. 222

8. The referrals in Sections 3.8 and 3.23 to the relevant sections in Appendix C of Proper Conduct of Banking Business Directive no. 203 were cancelled, and added in their place were referrals to the relevant sections in Proper Conduct of Banking Business Directive no. 203A.

Explanatory remarks

A technical correction due to the cancellation of Appendix C in Proper Conduct of Banking Business Directive no. 203.

Commencement

9. The updates to the Directive, pursuant to this Circular, shall go into effect on January 1, 2023 (hereinafter, the start date).

10. A banking corporation that is prepared to implement the revision to Section 93 and to implement Sections 93a—93c, may notify the Supervisor of such, as required by Section 93 of the Directive, before the start date, but the Supervisor’s approval of the banking corporation’s activity shall not go into effect before the start date.

5. Following are the updates to the Proper Conduct of Banking Business file:

Remove pages	Insert pages
221-1-48 [3] (5/22)	221-1-49 [4] (10/22)
222-1-21 [2] (5/22)	222-1-21 [3] (10/22)

Respectfully,

Yair Avidan
Supervisor of Banks