



Tel Aviv
November 23, 2016
16LM2440

To: The banking corporations and credit card companies

**Re: Preparedness for Compliance Risk Management In View of Setting Tax
Offenses as Predicate Offenses**

Introduction

1. The risks to the banking corporations concerning being exploited for tax evasion purposes have increased considerably in recent years, against the background of increased efforts by the tax authorities, including in Israel, in their struggle against illegal capital originating from tax offenses, to increase tax collection and reduce the phenomenon of tax evasion by tax offenders.
2. As part of this effort, the Ministry of Justice, the Israel Money Laundering and Terror Financing Prohibition Authority and the Israel Tax Authority advanced the Money Laundering Prohibition Law (Amendment 14), 5776–2016 (“the Amendment”). The amendment, which came into force on October 7, 2016, included the addition of a number of serious tax offenses, under certain conditions, to the list of offenses enumerated in the first addendum to the Money Laundering Prohibition Law, 5760–2000 (“the Law”) as predicate offenses.
3. Pursuant to the provisions of existing law, the banking corporations are required to detect and report on irregular activity, as defined in Section 9 of the Prohibition on Money Laundering (Banking Corporations’ Requirement regarding Identification, Reporting, and Record Keeping) Order, 5761–2001 (“the Order”).
4. Therefore, all the Anti-Money Laundering directives that apply to banking corporations (such as the Order and Directive 411, as defined below) shall hereafter also apply in connection with the commission of tax offenses by the customer, particularly the provisions concerning “Know the customer”; controls; monitoring and detecting unusual activity.
5. Following the publication of the amendment, the Banking Supervision Department has found it proper to publish this letter, which is intended to assist the banking corporations in managing risks, by emphasizing issues that may be more relevant to tax offenses.



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6. In the future, the Banking Supervision Department will examine integrating the contents of this letter in the framework of Proper Conduct of Banking Business Directive 411—“Prevention of Money Laundering and Terrorism Financing, and Customer Identification”.

Corporate Governance

7. Due to the Amendment, the banking corporation’s management must examine the necessary changes in the banking corporation’s policy, risk assessment, and procedures, and the Board of Directors must discuss and approve the policy and risk assessment, including:

7.1 An examination of the required changes in the anti-money laundering and combating the financing of terrorism policy, with an emphasis on the issue of “know the customer”, while taking into consideration all risk factors connected to the ownership structure of the account or activity in the account, with an emphasis on complex ownership structures where it is difficult to determine the controlling owner or the use of trustees that make it difficult to identify the beneficiary, particularly concerning the purchase of real estate.

7.2 Updating the banking corporation’s risk assessment.

7.3 Examining what typologies from the list of activities in the second addendum to the Order are relevant for detecting accounts or activities that may be connected to the customer’s avoidance of paying taxes or where the source of funds is from income unreported to the tax authorities as required, including typologies that appear in the list in the Appendix, and acting to find and determine additional typologies that match.

7.4 Making sure that the updated policy and risk assessment, as well as the typologies in Section 7.3 above, are included in the procedures set out pursuant to Directive 411 and the provisions of Proper Conduct of Banking Business Directive 308—“Compliance and the Compliance Function in a Banking Corporation”.

7.5 Updating the banking corporation’s controls and training programs, while emphasizing the changes and revisions that have been made in the banking corporation’s procedures as a result of the Amendment.

Unusual activity



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8. The amendment sets out a number of conditions under which serious tax offenses will be considered predicate offenses. These include minimum thresholds comprised of tax amount and period, regarding which tax offenses were committed. In this context, it is emphasized that there is no minimum for reporting on irregular activity pursuant to Section 9 of the Order. Therefore, the Banking Supervision Department's position is that in reporting on unusual activity, there is no relevance to the minimum thresholds set out in the Law, but they can be used to formulate a risk-based policy.
9. A banking corporation that, based on the information in its possession, identifies activity that fits within the typologies as stated in Section 7.3 above, or other unusual activity in the account of a customer or executed by someone who is not an account holder, must obtain an explanation from the customer as to the purposes of the activity or its business or economic rationale, including relevant documentation.
- Laconic explanations such as "tax planning" (or similar explanations), do not, in and of themselves, constitute a satisfactory explanation, and the banking corporation must, according to a risk-based approach, examine the need to demand a declaration from the customer that he has reported his income in accordance with the law, including a professional and substantiated opinion, and must examine its relevance to the circumstances of the case.

Reasonable refusal

10. To avoid doubt, Section 24 of Directive 411 shall also apply to the banking corporation's activity in implementing the contents of this circular.

Application

11. The provisions of this letter shall take effect no later than December 31, 2016.

Sincerely,

Dr. Hedva Ber
Supervisor of Banks

Cc: Head of the Israel Tax Authority
Head of the Israel Money Laundering and Terror Financing Prohibition Authority



Appendix “Red Flags”

Ownership structure

1. The establishment of an additional active company with a similar name in another country.

Actions

2. A large number of transfers of significant amounts to offshore countries and vice-versa.
3. Withdrawal or deposit of cash with amounts close to the reporting threshold in Section 8(a)(1) of the Order.
4. Circular transactions where money is reinvested in the source country after being deposited in a foreign country (frequently offshore).
5. The activity in the account is uncharacteristic of the customer’s profile, such as the conduct of business activity in an account not opened for this purpose, or a volume of activity that is not consistent with the information provided by the customer when opening the account.
6. Nonresidents’ accounts, where the Power of Attorney is held by an Israeli resident.
7. Numbered accounts or code name accounts (as defined in Section 18 of Directive 411).
8. Accounts in the name of a company incorporated offshore that is controlled by an Israeli or where an Israeli is an authorized signatory on the account.
9. Loans issued to Israelis (directly or indirectly, including in trust) in Israel, fully or partially backed by collateral or guarantees located in foreign branches.
10. Loans issued to Israelis (directly or indirectly, including in trust) against collateral provided by companies incorporated offshore.

Information on customer identity

11. Hiding dual citizenship or country of tax indebtedness.
12. Indicators of nondisclosure of a customer’s details that may imply different tax residency than what is declared, if there was a declaration, by the customer.

Hold mail



13. The use of Hold mail.

Interaction with the customer

- 14. The customer insists that the banking corporation shall not contact him directly, except where the customer is in a country where, due to the prevailing relations between that country and Israel, contact cannot be made with him.
- 15. Concern that an account was closed due to the tightening of tax legislation or due to the banking corporation's request to obtain additional information on tax matters.
- 16. The customer shows greater-than-normal interest in tax matters.

Source of funds or source of wealth

- 17. The customer is unable or refuses to disclose the source of his wealth or income.
- 18. The customer is unable to confirm or present confirmation that the source of his wealth or income was lawfully reported to the authorities.