Jerusalem, 25 Adar 5775
March 16, 2015
15LM2017

To:
The Banking Corporations
Attn: Chief Executive Officer

**Re: Managing risks deriving from customers' cross-border activity**

**Introduction**

1. In recent years we have seen more determined and intensive activity by various countries to locate their residents' funds that are held outside the country of residence. The US has taken steps against banks that managed accounts for US customers and that were suspected of collaborating with those customers to conceal the funds from US tax authorities, and in addition adopted the FATCA legislation in order to receive reports on bank accounts and other financial accounts of Americans outside the US. Said legislation came into effect on July 1, 2014. Other countries such as the UK, Germany, and France also act to receive data on their residents' bank accounts held outside the countries of residence.
2. In July 2014, the OECD published a standard for exchanging data between countries for tax purposes. The goal of the publication was to create a uniform language to the extent possible that will enable countries to exchange information between them for tax purposes, with an emphasis on information on nonresidents' cross activity (that is, information on accounts at financial institutions of a resident of Country A that are managed in Country B, and vice-versa), similar to the arrangement set up by FATCA, which is inherently limited to bilateral relations with the US.
3. The standard may be viewed as an additional pillar in the OECD's Model Tax Convention to avoid double taxation, as it is intended to serve countries interested in regulating bilaterally the priorities in taxation and create a uniform language. The OECD's Model Tax Convention already includes a section on exchange of data, but the innovation is in the level of detail, the due diligence checks, and automation of the reporting, similar to the FATCA regime.
4. On October 27, 2014, the Ministry of Finance notified the OECD that Israel will adopt the said standard by the end of 2018. The announcement also noted that the adoption will be via signing agreements with relevant authorities in various countries. In order to carry out the obligations that Israel will take upon itself, changes in legislation are required.
5. The trend of international collaboration in the battle against tax evasion is liable to increase the exposure of Israeli banking corporations to the compliance risks deriving from cross border activity as well as reputation risk, and obligates them

to prepare suitably both in terms of activity vis-à-vis existing customers as well as in accepting new customers, in particular until the international reports are arranged.

6. Proper Conduct of Banking Business Directive 411—"Prevention of Money Laundering and Financing of Terrorism, and Customer Identification" ("**Directive 411**") and the Prohibition on Money Laundering (the Banking Corporations' Requirements regarding Identification, Reporting, and Record-keeping for the Prevention of Money Laundering and the Financing of Terrorism) Order, 5761-2001, establish guidelines and relevant tools related to "Know Your Customer", which enable Israeli banking corporations to reduce the risks involved in activity as detailed in Section 5 above. This letter is intended for implementing what is mentioned there, related to certain activities, with an emphasis on tax liabilities outside the country in which the account was opened, and in the future the requirements will be integrated as part of Directive 411.
7. After consulting with the Advisory Committee on Banking Business, and with the approval of the Governor of the Bank of Israel, I have decided to establish the following requirements:

**Application**

8. The provisions of Section 9 below are also effective in relation to the banking corporation's activity outside of Israel, with the necessary changes, in accordance with what is listed in Section 3a(b) of Directive 411.

**Establishing policy and procedures**

9. In light of the increased risks detailed above, and in accordance with the provisions of Section 4–6 of Directive 411, the board of directors of a banking corporation is to examine and update its policy, as well as to verify that management is suitably updating its procedures and controls with regard to the risks inherent in cross-border activity of the banking corporation's customers, with an emphasis on tax liabilities outside the country in which the account was opened, whether the customer is a resident of said country or not, in a risk-based approach, while referring to the following points:

   Customer classification

   9.1 Classification of a customer as high risk due to cross border activity shall be based on, among other things, the following parameters: the source of the customer's wealth and income and the source of funds that are to be deposited in the account, including receiving appropriate documentation; the extent and type of activity in the account; the customer's manner of organization; private banking; the customer's link to the country in which the banking services are provided; the customer's country of residence;

   9.2 Countries in which customer activity therein or fund transfers from them are considered as countries at risk for this matter, such as countries known as off-shore tax shelters;

9.3 A change in identification particulars that may effect the customer's tax obligation.

Required steps

9.4 Receive a declaration from the customer regarding the country or countries in which the customer is a resident for tax purposes, and a declaration that the customer reported income in accordance with the law applicable to said customer, and his or her obligation to notify of any change in tax liability. If necessary, certification should also be requested that that the customer has acted as declared, or alternatively certification that the customer has begun a voluntary disclosure process in the country in which the customer is a resident for tax purposes;

9.5 Receive a waiver on customer confidentiality vis-à-vis authorities abroad;

9.6 Set procedures as well as a scale of authorities for approval of an account's opening, management, and execution of transactions defined as potentially bearing cross-border risk.

In providing banking services to customers subject to FATCA directives, banking corporations are to act to implement them pursuant to the provisions of my letter dated April 6, 2014.

**Reasonable refusal**

10. Refusal to provide banking services, as detailed below, shall be considered reasonable refusal with regard to the Banking (Service to Customer) Law, 5741-1981:

10.1 Opening an account for a customer who does not cooperate with the banking corporation in a manner necessary to implement the banking corporation's policy and its procedures regarding cross border risk.

10.2 Continued provision of banking services in an existing account, including withdrawal of funds and changing account owner or beneficiaries, in a manner that exposes the banking corporation to the risk of being viewed as collaborating with the customer in order to bypass foreign legislation that applies to the customer.

**Start**

11. The provisions of this letter begin on the date of its publication.

**Provisional directives**

12. A banking corporation shall complete the activities noted in Section 9 above, regarding funds of customers in existing accounts, as detailed below:

12.1 Accounts of customers classified by it as high risk customers by December 31, 2015.

12.2 Other accounts by December 31, 2016.

13. The provisions of this circular shall not apply to an account whose owners cannot be contacted due to the relations between the country they are in and the State of Israel.

Sincerely,

David Zaken
Supervisor of Banks