

LIMITATIONS ON FINANCING CAPITAL TRANSACTIONS

Introduction

1. (a) Financing capital transactions (for example, financing the purchase of control or means of control in corporations) is characterized in many cases by large sums or high proportions of financing, where the ability to repay the credit is often based on the purchased corporation and sometimes without recourse to the borrower.
- (b) Because of the complexity and level of risk inherent in financing capital transactions, such activity was regulated within the framework of Proper Conduct of Banking Business Directive 327, titled “Leveraged Lending Management” (hereinafter, **Directive 327**).
- (c) Without detracting from the requirements of Directive 327, this directive is established, dealing with quantitative limitations on financing capital transactions.

Definitions

2. **“Capital”** - Tier 1 Capital after regulatory adjustments and deductions, as per the provisions of Proper Conduct of Banking Business Directive 202 regarding Regulatory Capital.

- “Capital transaction”** - A transaction with one of the following goals:
 - (a) Buyout—purchase or buyback, by the borrower, of the borrower’s issued capital (including an employee stock ownership plan);
 - (b) Acquisition of another corporation—the purchase of any capital rights in another corporation, or the purchase of all, or a significant share, of the assets of another corporation;

(c) Capital distribution—the payment of a dividend or other transaction whose goal is to increase shareholder value;

“Credit for a capital transaction” -

Credit for a capital transaction, provided that the balance of said credit is greater than 0.5 percent of the capital of the financing banking corporation, or than NIS 35 million, whichever is higher. With that, regarding credit for purchasing capital rights in another banking corporation or bank holding corporation, the threshold shall be NIS 35 million.

“Credit for a capital transaction” is also to include additional credit extended to the borrower at a date later than the date of financing the capital transaction, if the repayment of the credit is based mainly on cash flows deriving from the capital rights whose purchase was financed by the banking corporation;

Credit for the purchase of capital rights in a corporation and in a corporation under its control will be considered as a single credit.

“Proportion of Financing” -

The ratio, as a percentage, of the balance of credit extended for a capital transaction to the cost of the transaction. Similarly:

(1) If the capital rights were purchased in installments, or if some of the capital rights were sold, the proportion of financing shall be calculated as follows: the ratio of the balance of credit extended for the purchase of the capital rights to the value of the rights

as derived from the cost of the last transaction.

- (2) Collateral which is deductible under Section 5 of Proper Conduct of Banking Business Directive 313 on "Limitations on the Indebtedness of a Borrower and of a Group of Borrowers" may be deducted from the balance of credit in accordance with the regulations set there.

3. Revoked.

Quantitative limitations

4. (a)(1) The total balance of credit for capital transactions, in cases where the proportion of financing exceeds 50 percent, shall not exceed 70 percent of the capital of the banking corporation extending the credit.

- (2) Without detracting from the provisions of paragraph (1), the balance of credit extended by a banking corporation for the purchase of capital rights in another banking corporation, or in a bank holding corporation, in cases where the proportion of financing exceeds 30 percent, shall not exceed the lower of the following:

- (a) 5 percent of the capital of the banking corporation extending the credit;
- (b) 5 percent of the capital of the banking corporation purchased or of a bank holding corporation (accordance to its last published financial statements), or another rate determined by the Supervisor of Banks for a banking corporation whose capital is lower than NIS 500 million.

- (b) (1) At the end of every quarter the banking corporation shall adjust the amounts and rates for the purpose stated in subsection (a);

- (2) The adjustment as stated in paragraph (1) shall be undertaken for each transaction in accordance with the following calculation:

The ratio of the actual credit balance to the cost of the transaction.
Dividends received by the borrower from accumulated profits in the

purchased corporation prior to the date of purchase shall be deducted from the transaction cost.

- (c) There is no need to continue including partially repaid credit in the computation of the limitation, so that the current balance is below the minimum set in the definition of “credit for a capital transaction” in Section 2 above, or so that the proportion of financing is below the threshold set in Sections 4(a)(1)–(2) above.

Credit to several borrowers

- 4a. (a) Credit extended separately to several borrowers for the purchase of capital rights in the same corporation or in a corporation controlled by it shall be considered as a single credit for the purposes of this limitation.
- (b) For the purposes of subsection (a) above, a banking corporation may disregard credit extended for the purchase of capital rights to borrowers for whom the amount of credit extended to them is lower than half the amount specified in the definition of “Credit for a capital transaction”.

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Revisions

Circular 06 number	Version	Details	Date
1939	1	Original directive	30/7/1998
1965	2	Revision	14/3/1999
2097	3	Revision	22/12/2002
2151	4	Revision	13/12/2004
2323	5	Revision	27/12/2011
2461	6	Revision	28/4/2015