

## **Banking Corporation Business with Related Parties**

### **Introduction**

1. In order to minimize risks arising from transactions by a banking corporation with related parties, banking corporations shall act in accordance with the provisions of this Directive. The objective of this Directive is to limit the extent of indebtedness of related parties to the banking corporation and to ensure that transactions between a banking corporation and related parties are undertaken on an arm's-length basis, in accordance with commercial terms that are not preferential to similar transactions with unrelated parties.
  - 1a. To eliminate doubt, it is stated for clarity that these provisions supplement the Companies Law, 5759-1999 (hereinafter, "the Companies Law").

### **Application**

2. (a) This Directive shall apply to the following corporations (hereinafter, banking corporation):
  - (1) a banking corporation, excluding a joint services company, although regarding a foreign bank, provided it does not fulfill the terms established in Appendix A;
  - (2) a corporation as noted in Sections 11(a)(3a) and (3b) and 11(b) of the Banking (Licensing) Law, which incorporated in Israel and is controlled by a banking corporation;
  - (3) An acquirer;
- (b) This Directive shall not apply to a contractual arrangement of a banking corporation relating to terms of service or employment that were set forth under the provisions of Proper Conduct of Banking Business Directive 301A.

### **Definitions**

3. A "related party" to a banking corporation is—
  - (a) anyone who has a controlling interest in the banking corporation, and a Candidate;
  - (b) a corporation in which those listed in Paragraph (a) control or hold more than 10 percent of any means of control, and a corporation in which the foregoing corporation holds more than 50 percent of any means of control.

- (c) the holder of more than 5 percent of any means of control in the banking corporation or in a banking corporation that controls said banking corporation;

With regard to this subsection only—excluding one who received a holding permit subject to the terms established in the Banking Supervision Department’s updated policy document published on the Bank of Israel website on the topic of “Permits for holdings in banking corporations, acquirers, and in corporations holding them for institutions managing customers’ money—policy update”.

- (c1) a person who has nominated (on his own or as a member of a group of holders) a candidate to serve as a director in a banking corporation without a controlling core. The classification as a related party shall go into effect from the moment the actual tenure as director begins and shall remain valid as long as the director nominated by him/her holds the position.
- (d) an officer of the banking corporation, or of a corporation that controls the banking corporation, including corporations through which the controlling group’s means of control in the banking corporation are held;
- (d1) the CEO and the Chairperson of the board of directors in a main subsidiary of the banking corporation; in this regard, “main subsidiary” is as it is defined in Section 32(i) of the Banking Supervision Department’s Reporting to the Public Directives no. 632–45. However, the banking corporation may opt not to include the corporations complying with the terms of Section 4(b) in this definition);
- (e) a corporation controlled by those listed in paragraphs (c)–(d1);
- (f) a corporation that the banking corporation controls or in which it holds more than 10 percent of any means of control, and a corporation controlled by a corporation noted in the beginning section; However, a holding of more than 10 percent of any type of means of control in a corporation, without control, shall only be considered a “related party” if the value of the holding in the banking corporation’s records exceeds 0.5 percent of the banking corporation’s capital;
- (g) an entity that holds 20 percent or more of any type of means of control in a corporation controlled by the banking corporation;
- (h) any entity whom the Supervisor of Banks defines as a related party, generally or in a specific case;

Regarding a “related party” that is an individual—including his relative.

**“Credit”** - As defined in Proper Conduct of Banking Business Directive no. 313 (henceforth—Directive 313);

**“Controlling core”** – The minimum share of means of control in a banking corporation that the controlling group must hold as noted in the group’s control permit, and if not noted, said share shall be as established by the Supervisor;

**“Capital”** - Tier 1 capital after regulatory adjustments and deductions as defined in Proper Conduct of Banking Business Directive 202;

**“Indebtedness”** - As defined in Proper Conduct of Banking Business Directive no. 313, including credit from deposits in which repayment to depositor is contingent upon the collection of the credit; however, for the purpose of a guarantee given by a related party on behalf of the banking corporation to secure credit extended to a third party by the banking corporation, the following provisions shall apply to the definition of indebtedness:

- (a) If the guarantee was given to secure credit extended to an unrelated party, the entire guarantee shall be viewed as part of the indebtedness;
- (b) If the guarantee was given to secure credit extended to a related party, the guarantee shall not be included in the indebtedness;

**“Group of holders”** As defined in Section 11d of the Banking Ordinance, 1941;

**“Candidate”** - A person who has applied to the Governor for a permit to control a banking corporation, either individually or in conjunction with others, where the Supervisor has served the relevant banking corporation with notice thereof;

**“Officer”** - As defined in the Companies Law;

**“Transaction”** - As defined in Section 1 of the Companies Law;

**“Controlling group”** – A group of people with a permit to control and hold means of control in the banking corporation;

**“Relative”** - A spouse, offspring, and dependent; however, regarding Section 3(a) – as defined in the Banking (Licensing) Law.

### **3a. Policies and procedures**

(a) The Committee for Transactions with Related Parties, and if such a committee has not been

appointed per Directive 301, the Audit Committee, shall recommend to the board of directors before setting policies and procedures for approving transactions with related parties, and among other things shall refer to determining the amount of a related party's indebtedness that requires the Audit Committee's approval, and setting criteria for imposing limitations that apply to a related party even on one that is not defined as such, if it was of the view that there is a need for that, as well as procedures for monitoring, controlling, reporting and following up material transactions with related parties; Without derogating from the foregoing, the providing of credit to a related party in an amount exceeding 0.5 percent of the banking corporation's capital, or a transaction of a different type in an amount that the board of directors shall determine, shall be reported to the full board of directors in its next meeting.

- (a1) The Audit Committee or the Committee for Transactions with Related Parties, as relevant, shall establish procedures for monitoring, controlling, and reporting transactions with related parties that do not require documented approval of the Audit Committee or the Committee for Transactions with Related Parties in accordance with Section 7(a). This includes reporting transactions with related parties that are exempt from the provisions of Section 4(a), as per the directives of Section 4(b).
- (b) Cancelled.

#### **Transactions with related parties**

- 4. (a) A banking corporation shall not enter into a transaction with a related party on terms that are preferential to those it offers others in similar transactions.
  - (a1) A banking corporation shall not accept securities issued by itself as collateral for a related party's indebtedness, and if said related party has a controlling interest in the banking corporation, it shall also not accept securities issued by said possessor of controlling interest or by the corporation that he/she controls.
  - (b) Subsection (a) and Section 7(a)(1) shall not apply to transactions of corporations in the banking group with a corporation in which the banking corporation holds 95 percent or more of means of control and fulfills one of the following 2 conditions:
    - (1) It does not extend credit or any other service to persons outside the banking group.
    - (2) Its entire occupation is issuing bonds for corporations in the banking group.

For this purpose, a “banking group” comprises the banking corporation, a banking corporation that controls it, and banking corporations controlled by one of them.

**Limitations on indebtedness of related parties**

5. (a) The aggregate indebtedness of all related parties to the banking corporation shall at no time exceed 10 percent of the banking corporation’s capital.
- (b) The total indebtedness of a related party, including his relative and banking corporations controlled by one of them, shall at no time exceed the following amounts:
  - (1) The indebtedness of a related party who is a member of a controlling group shall not exceed the product obtained by multiplying said member’s share in the controlling core by 10 percent of the banking corporation’s capital.
  - (2) The indebtedness of a related party (other than a member of a controlling group) that holds 5 percent or more of any means of control in the banking corporation, or in a banking corporation that controls said banking corporation, and also, in banking corporations that have no controlling core, the indebtedness of an entity that has nominated (on his/her own or as a member of a group of holders) a candidate to serve as a director, where the director-nominee is serving in the position, shall not exceed 5 percent of capital at any time;
  - (3) The indebtedness of any related party that holds 20 percent or more of any means of control in a corporation that the banking corporation controls shall not exceed 5 percent of capital at any time (except corporations controlled by the holder);
  - (4) The indebtedness of a related party who is an officer of the banking corporation, with the exception of a holder of means of control who serves as a director of the banking corporation, shall not exceed NIS 3 million at any time, except for a housing loan;

For the purpose of this Section:

**“Housing loan”** – as the term is understood in Section 1 of Proper Conduct of Banking Business Directive no. 329 and except an investment home as defined there;

- (c) In calculating the collective indebtedness of related parties to a banking corporation, the following shall not be included:
  - (1) the State and any sovereignty that may be assigned a zero risk weight under Sections 53–56 of Proper Conduct of Banking Business Directive 203;

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- (2) a candidate;
- (3) a banking corporation;
- (4) a corporation belonging to the same group of bank borrowers to which the banking corporation belongs, as it is understood in Proper Conduct of Banking Business Directive no. 313;
- (5) a “controlled group of borrowers” as understood in Proper Conduct of Banking Business Directive no. 313.

### **Deductions**

6. For the purpose of Section 5, the items specified in Section 5 of Directive 313 shall be deducted from the amount of indebtedness.

### **Approval by the board of directors of transactions with related parties**

7. (a) Transactions with a related party as specified below require documented approval of the Audit Committee or of the Committee for Transactions with Related Parties, appointed in accordance with Directive 301, as the case may be:
  - (1) Any transaction undertaken with a related party in which one of the following conditions is present:
    - (a) The related party’s total indebtedness exceeds NIS 1,000,000 or 0.1 percent of the banking corporation’s capital, whichever is greater (henceforth—the “minimum amount”);
    - (b) As a result of the transaction, the related party’s total indebtedness exceeds the minimum amount.
    - (c) The limitations established in this paragraph shall not apply to the renewal of an agreement with a controlled corporation, at a scope and under conditions that are not materially different from those approved by it in the past, unless the Committee decided otherwise;
  - (2) Any indebtedness transaction undertaken with an individual related party in a sum that exceeds NIS 500,000;
  - (3) Any other transaction with an individual related party at an amount that exceeds NIS 500,000, or with a related party that is not an individual in which the amount exceeds the minimum amount;

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- (4) Any other transaction with a related party, if no amount has been set in respect thereto, or if the amount exceeds an amount fixed by the board of directors, provided the amount does not exceed the minimum amount; in respect of deposits and account management terms, no specific approval is required if the conditions were set forth under a long-term framework agreement;
- (5) A provision for, or a debt restructuring of, a debt of a related party.
- (b) The Committee for Transactions with Related Parties or the Audit Committee shall discuss transactions as detailed in Subsection (a) undertaken by a related party with the banking corporation before the person became a related party.  
If the Committee reaches the conclusion that the terms of said transaction deviate from market terms, and for reasons of legal liability, it is unable to annul or alter its terms, the chair of the committee shall inform the Supervisor of Banks via the secretary of the banking corporation.
- (c) The approval specified in Subsection (a) shall also include certification that the transaction does not contravene the terms of Section 4 of this Directive; the minutes of the discussion shall include the explanations given to the committee to verify the foregoing.

7a. Cancelled.

**A related party who is an employee**

- 8. These provisions, except for Section 5(b)(4) shall not apply to:
  - (a) A transaction with a related party undertaken by a banking corporation, if said related party is an employee of the banking corporation and the transaction is implemented in the ordinary course of business and under conditions specified for this purpose in a collective labor agreement or collective arrangement that applies to the employees of the banking corporation.
  - (b) Any other agreement that is signed in the presence of the an organized Workers Committee or via a personal employment contract, the terms of which are similar to the collective labor agreement or other arrangement, as noted above, in the same banking corporation or under service or employment terms that were established as such in Proper Conduct of Banking Business Directive no. 301A.

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### **Reporting to the Banking Supervision Department**

9. (a) A banking corporation shall present the Banking Supervision Department with a list of all related parties and the indebtedness of each, using the reporting format specified in the Reporting to Banking Supervision Directives. The banking corporation shall also keep such a list in its offices and update it whenever necessary.
- (b) A banking corporation shall submit an immediate report to the Banking Supervision Department in the event of a deviation that occurs in accordance with the provisions of the Directive, when created.

### **General provisions**

10. The Supervisor of Banks, when there are special reasons to do so and it is seen as correct, may take the following actions:
  - (a) Authorize an exception of a “related party” from the definition or excuse him/her from having to comply with certain sections of the Directive, for such a period or under such conditions as shall be determined;
  - (b) Determine that a transaction with a related party was carried out under conditions that deviate from market conditions and have the indebtedness on its account deducted from regulatory capital.

### **Deviation due to classification as a related party**

11. Indebtedness of a related party that was created before he/she became a related party and exceeds the limit established in Section 5(b) shall be settled gradually over a two-year period. This shall also apply due to circumstances beyond the bank’s control, such as corporate mergers and acquisitions.



## Appendix A

### Section 2(a)(1)

#### A foreign bank's business with related parties in its branches in Israel

#### Conditions for an exemption from the Directive's requirements regarding a foreign bank

A foreign bank with regard to its activity in its branch in Israel shall be exempt from this Directive given the existence of all the following terms:

- (a) Authorization by the foreign bank's senior management, according to which the bank implements the regulatory requirements imposed on it regarding the bank's business with related parties and that it is subject to supervision on the issue by the regulator in the home country, including with regard to a branch of the bank outside of Israel.
- (b) Approval by the foreign bank's senior management that there is ongoing management and monitoring of transactions carried out between the branch in Israel and its officers and that there is reporting of such transactions, once a year, to the internal auditor of the branch in Israel.

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#### Updates

<b>Circular 06 no.</b>	<b>Version</b>	<b>Details</b>	<b>Date</b>
1508		Original circular	March 10, 1991
—	1	Placement among Proper Conduct of Banking Business Directives	Aug. 1991
1528	2	Update	Nov. 4, 1991
1616	3	Update	Jan. 3, 1993
1701	4	Update	April 4, 1994
—	5	Revised version of Proper Banking Conduct file	Dec. 1995
1868	6	Update	April 30, 1997
1882	7	Update	Aug. 3, 1997
1933	8	Update	June 30, 1998
2277	9	Update	Oct. 19, 2010
2425	10	Update	July 10, 2014
2516	11	Update	Sept. 29, 2016
2688	12	Update	January 31, 2022

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