Re: Transitioning from the LIBOR Rate

Introduction

1. Reference interest rates (such as IBOR rates, based on interbank finance around the world) play an important role in money and financial markets and provide a basis on which funding costs of loans and bonds floating interest rates in derivatives markets may be set. The most common base rate around the world today is LIBOR (London Inter-Bank Offered Rate).
2. Serious failures, manipulations, and false reports in the processes of setting benchmark rates, coupled with a steep downscaling of transactions in the interbank financial market after the global crisis and a decrease in the number of interest-quoting banks, caused confidence in LIBOR rates to plummet and led to decision to replace them. Consequently, in a notice sent out on March 3, 2021, the FCA (Financial Conduct Authority) in the UK announced the cessation of publication of LIBOR rates in sterling, Euros, Swiss francs, Japanese yen, and U.S. dollars to one-week and two-month terms on December 31, 2021; and the cessation of publishing USD LIBOR rates to all other terms on June 30, 2023.
3. The termination of LIBOR rate publication around the world is expected to affect many aspects of banking corporations' business and requires banking corporations to examine the impact of the cessation and the transition to an alternative benchmark rate, and to manage the risks that flow from the transition, including legal, operating, behavioral, and reputational risks.
4. Accordingly, the banks were instructed on February 13, 2020, as part of their reporting to the public, to disclose their preparations for terminating their use of LIBOR rates. Furthermore, lenient measures were allowed in dealing with the effect of the transition on the handling of derivatives, securities, and interest income in accordance with Topic 848 in the United States Codification concerning "Reference Rate Reform."
5. In accordance with the foregoing, I find it correct to spell out principles for the implementation of the transition in order to make sure the banking corporations will be adequately prepared and will relate to the potential risks and aspects of fairness toward customers, as specified in this Directive.

Incidence

6. This Directive shall apply to the following entities (hereinafter, singly: "banking corporation")
   (a) a banking corporation with the exception of a Joint Services Company, as these are defined in the Banking (Licensing) Law, 5741-1981;
   (b) a settlement institution as defined in Section 36i of the Law.

Definitions

7. Base rate	A benchmark interest rate in foreign currency as defined in Proper Conduct of Banking Business Directive 421, “Interest rate reduction or increase.”
Alternative base rate	A benchmark rate that replaces LIBOR
LIBOR	A daily benchmark rate for interbank loans to terms of up to one year among banks in London (London Inter-Bank Offered Rate), published for the public’s knowledge.
Working groups and committees	**USA**—Alternative Reference Rates Committee (ARRC) **Europe**—Working Group on Euro Risk-Free Rates **UK**- Working Group on Sterling Risk-Free Reference Rates **Swiss**—The National Working Group on Swiss Franc Reference Rates **Japan**—Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks
New contract	Including the renewal or recycling of a contract that creates a credit facility (including current or overdraft), loan, deposit, or derivative financial instrument
Micro or small business	A business with activity turnover smaller than NIS 50 million, as set forth in Section 79 of the Reporting to the Public Directives.

Definitions

8. A banking corporation that offers products indexed to or denominated in foreign currency that are based on LIBOR rates shall make adequate preparations for the transition to alternative base rates.
9. Subject to the provisions of any law, including Section 4a of the Fair Credit Law, 5753-1993, a banking corporation shall cease to execute new contracts based on LIBOR as the base rate at the earliest possible opportunity and, in any case, no later than December 31, 2021, in order to help transition from the LIBOR rate systematically and safely.
10. Notwithstanding the foregoing, a banking corporation may, under limited circumstances, execute new contracts based on the USD LIBOR rate even after December 31, 2021, for example, for the purpose of transactions that mitigate or hedge an exposure to the USD LIBOR rate of the banking corporation or of its customer, originating in contracts executed before January 1, 2022.
11. A banking corporation shall have in place a systematic action plan for the choice of an alternative base rate and shall document the considerations that guided it in this matter.

12. In choosing the alternative base rate, a banking corporation shall bear in mind the recommendations of the relevant committees and working groups in the various currencies, the recommendations of the Financial Stability Board (FSB), and the recommendations of the International Swaps and Derivatives Association (ISDA), all of which subject to the provisions of Section 13 below.
13. In choosing the method of calculating an alternative base rate, a banking corporation shall act fairly and shall also take account, *inter alia*, of considerations pertaining to customers' well-being. Within this construct, a banking corporation shall, *inter alia*, use a method of computation in regard to housing loans that will make it possible to present the customer, at the beginning of the term, with the interest rate that he or she will be charged in the next installment.
14. In new contracts based on a base rate, including those using LIBOR as the base rate, where such contracts will end after December 31, 2021, a banking corporation shall include an adequate mechanism for the transition to another base rate where necessary (a fallback mechanism). Said mechanism shall be adequate and fair and shall include, *inter alia*, reference to disclosure and compulsory notices to the customer in the event of a change in rate, including the timing of said notice.

Existing contracts

15. A banking corporation shall examine the effect of ceasing to publish LIBOR rates and switching to an alternative base rate on its customers and on its existing contracts, and shall act to minimize uncertainty in the possible effects of this measure on customers. Within this construct, a banking corporation shall apply fairness, caution, good faith, and transparency, and shall refrain from changes that the cessation of publishing LIBOR rates does not make necessary.
16. A banking corporation shall have in place policies and procedures that govern its transition from the LIBOR rate to an alternative base rate in existing contracts, in accordance with the terms of said contracts and the types of customers and products, all of which subject to the provisions of law and in accordance with the contents of the following sections. Within this framework, a banking corporation shall also set clear parameters for the way it will apply the requirements in Sections 17–20 below, script scenarios, and provisions for updating, referencing, and obtaining customer consent, to the extent necessary.
17. Without derogating from the provisions of any law, a banking corporation shall, with all possible celerity, approach all customers who are directly affected by the cessation of publishing LIBOR rates and shall explain, in clear language, the need for the transition to an alternative base rate, the background of the transition, the implications of the change, and its impact on the customer's various products and possibilities. Said approach shall be made in writing and in appropriate language. Without derogating from the provisions of any law, when it approaches the customer the banking corporation shall present, *inter alia*, the new method of calculation, the frequency of updating the interest rate, and data for quantitative comparison. Said quantitative data shall include, at the very least, the rate of the alternative base rate that would have been set for the same payment had the new calculation method been applied, the alternative interest rate that would have been charged to the customer in this case, and the interest sums that were paid or

would have been paid in accordance with them, adjusted to the same payment date. The approach may be communicated online, as the case may be and in accordance with the terms of the contract that determine how information and notices between the bank and the customer is to be presented. Notwithstanding the foregoing, ahead of the transition on December 31, 2021, and for practical reasons, a banking corporation may present the customer, in lieu of the aforementioned quantitative comparison data, a general numerical example that will reflect the effect of the transition from LIBOR to the alternative base rate that the bank has chosen for each type of product, and that shall include the quantitative data specified above.

18. In cases where, after it ceases to publish LIBOR rates, the banking corporation will need the customer's consent to update the rate or the rate-calculation mechanism, or to revise other terms in an existing contract, the approach to the customer shall also include an explanation of the requisite revisions in the contract and the reasons for them. To abet the customer's decision, the banking corporation shall present the customer with the options available to him or her and their implications. The banking corporation shall enable the customer to put this stage of examining available possibilities to full use and shall give him or her ample time to make the decision in order to avert harm to the customer insofar as consent is not given. The contract shall be updated in accordance with the terms of the existing contract and the provisions of any law, and the fact that the revision does not originate in a request by the customer (including aspects of its cost) shall be borne in mind.
19. If a customer who is an individual, a micro business, or a small business decides not to accept the banking corporation's offer to switch the base rate, this shall not be construed as a request for early repayment by him or her.
20. In addition to the foregoing, a banking corporation shall directly approach any customer who is likely to be materially affected by the cessation of publishing LIBOR rates in order to explain the change and its implications. Said direct approach shall be made in appropriate language and may be carried out by telephone, face-to-face with a banker at the branch, or on any other platform where a dialogue between the banking corporation and the customer may take place, all in accordance with the terms of the contract and the means and channels of communication that are specified in the agreement between the bank at the customer. The banking corporation shall document said approaches.

Information for customers

21. A banking corporation shall publish on its website general information about the cessation of publishing LIBOR rates, including a clear explanation of the requisite change, its background, its possible implications for various products and customers, and a numerical example for each type of product as set forth in Section 17 *supra*.
22. From the day of the rate change onward, a banking corporation shall publish on its website, on a regular basis, the alternative base rates that it offers its customers and how they are calculated.
23. A banking corporation shall allow its customers, at the various service centers and on its website, the possibility of obtaining information, support, and assistance in inquiries about the transition from LIBOR rates. The corporation shall allocate the requisite resources and give its staff

appropriate training to ensure an adequate and rapid response to customers' inquiries, including the assignment of staff members who speak the relevant languages.

Management of risks

24. Within the framework its preparations for the transition, the banking corporation's management and Board of Directors shall hold periodic discussions about progress in the transition project and shall continue taking action to mitigate exposures occasioned by the changeover in base rates that are contingent upon each banking corporation's specific circumstances. The potential risks may include:
    - 24.1 practical hardships occasioned by difficulty in quantifying the exposure, a large number of customers, keeping the information up-to-date and complete, and adapting technological infrastructures to the change;
    - 24.2 financial risk, including risk originating in revaluation, management of interest-risk and currency-risk positions, and model risk associated with switching benchmark rates;
    - 24.3 business risk, including pricing of transactions and margins;
    - 24.4 behavioral risks, including those originating in consumer-protection directives;
    - 24.5 regulation and accounting risks including effects of valuation, value adjustments (XVA), accounting and taxation effects, and estimation of risks to regulatory requirements;
    - 24.6 risk stemming from the effect of the switch on third-party service providers (outsourcing) and these suppliers' limited ability to support operational changes;
    - 24.7 inadequate risk-management processes and inadequate controls for support of the changeover;
    - 24.8 potential litigation and reputational risk originating in the changeover and in delay of operational readiness or deviation from accepted market standards.

Beginning date and effect

25. This ad hoc directive shall go into effect two weeks from the day on which it is promulgated, with the exception of the provisions of Section 26 below.
26. The provisions of Section 17 shall go into effect for customers who are individuals, micro businesses, or small businesses, no later than two months before the date of the change in interest and, for customers in other sectors, no later than a month before the date of the interest change. The provisions of Section 20 shall go into effect no later than two weeks before the date of the interest change, and the beginning of the provisions of Section 21 no later than a month after promulgation.
27. This Directive shall remain in effect until December 31, 2023.

Updates

Circular no. 06	**Version**	**Details**	**Date**
2673	1	Original circular	September 30, 2021

Respectfully,

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