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Israeli Lending Licensing Requirements – a Step Towards Certainty for International Lenders

Background

The Financial Services Supervision Law (Regulated Financial Services) 5776 – 2016 (the “Law”) came into force on 1 June 2017. Prior to the introduction of this regime, the provision of credit in Israel was regulated in relation to banks and institutional lenders but not when it came to other lenders. The Law introduced a new regulatory regime with respect to several financial services and market participants that were not previously regulated. Notably, it includes a broadly drafted prohibition on the provision of credit without holding a license as well as requirements for a control permit of such entities.

Although most likely not intended, the broad manner in which the new Law was drafted and its potential application caused significant uncertainty in the market, in particular in relation to the extent to which the licensing requirement applies to a foreign lender conducting business in Israel or lending into Israel on a sporadic basis or otherwise, and to large scale corporate loans to sophisticated borrowers.

On 28 May 2017, just a few days before the entry into force of the Law, the Capital Market, Insurance, and Savings Authority in the Ministry of Finance (the “Authority”) published two important draft documents for public consultation, namely the Draft Financial Services Supervision Regulations (Regulated Financial Services) 5777 – 2017 (the “Draft Regulations”) and a draft legal position outlining the Authority’s position on the applicability of the licensing regime to lenders that operate outside of Israel. The Draft Regulations carve out certain types of lenders and the draft position paper discusses when a lender’s activity will be deemed to be outside of Israel and therefore fall outside the scope of the Law.

On 1 October 2017, the Authority published an updated version of the Draft Regulations, which provides additional carve-outs and further clarity on several open questions.

The Draft Regulations

The Law authorizes the Minister of Finance, with the approval of the Finance Committee of the Knesset, to exempt a specific lender or types of lenders from the licensing requirement. By virtue of this authority, the new version published earlier this month (which was likely shaped at least in part following feedback from the public), provides for relatively broad exemptions from the licensing requirement for several categories of lenders. Importantly, the explanatory notes accompanying the Draft Regulations state that in order to guarantee the proper course of business during the period pending the regulations coming into effect, the regulator does not intend to carry out

enforcement actions during this period against the bodies set out in the Draft Regulations. Notable exemptions include:

- Foreign banks - a bank incorporated in and holding a banking license issued by an OECD member state as well as companies under direct control of such banks.
- Business Lenders - a corporation whose business is granting credit to business corporations, only if the following two criteria are satisfied: (a) the amount lent in a single transaction is no less than NIS 10 million, and (b) the borrower is not a purchase group¹. The explanatory notes to the Draft Regulations elaborate that the rationale for this exemption is that sophisticated business borrowers, that borrow large amount, have improved capabilities to choose the credit they take and their credit providers and therefore will not require licensing.
- Loans to Technology Start-ups – this exemption applies to one who deals with granting credit to high tech startup companies, the investment in which carries a heightened degree of risk.

It is worth noting that the Draft Regulations contain a provision whereby the regulations would be in effect until 31 December 2019. The explanatory notes explain that this is in order to allow the regulator an interim period in which it could/would monitor and check that the desired effect and objectives of the law/regulations are being achieved.

The draft legal position paper

The draft legal position paper issued in May 2017, exists alongside the Draft Regulations, and has the primary focus of addressing the question of the applicability of the Law to lenders who are incorporated in Israel or abroad and whose lending activities take place entirely outside of Israel. The draft position notes that the objective of the Law, other than enhancing competition in the retail and SME credit market, is to protect Israeli borrowers. The draft opinion expresses the view that a lender will be exempt from the licensing requirement, if all of the following conditions are met:

- the credit documents (except for security) are written in a foreign language, signed outside of Israel and governed by foreign law;
- the accounts to which the loan is disbursed are outside of Israel;
- the lender does not solicit new clients in Israel;
- the lender does not hold meetings with customers in Israel.

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¹ A structure for real estate development projects common in Israel typically involving individuals.

* This publication provides general information and does not constitute or substitute legal advice. As these issues are complex and of a circumstantial nature, which involve different legal aspects, each case should be examined according to its specific circumstances.